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Foreigners Extending Canada Credit

Every time Bank of Canada Governor Marc Carney steps in front of a microphone he reminds Canadians how important it is to borrow prudently, and with good reason. Getting less attention to date is the fact that a good chunk of the borrowing (household & government) is only made possible thanks to foreigners extending us credit.

Transactions between Canadians and the rest of the world are tracked in the balance of payments (BOP). If Canada is consuming more from the rest of the world than it is selling, then it is able to do so because foreigners are effectively willing to extend Canadians credit. By definition, trade in goods and services (the current account) has to be offset by trade in financial assets (known as the capital account). It's actually pretty intuitive.

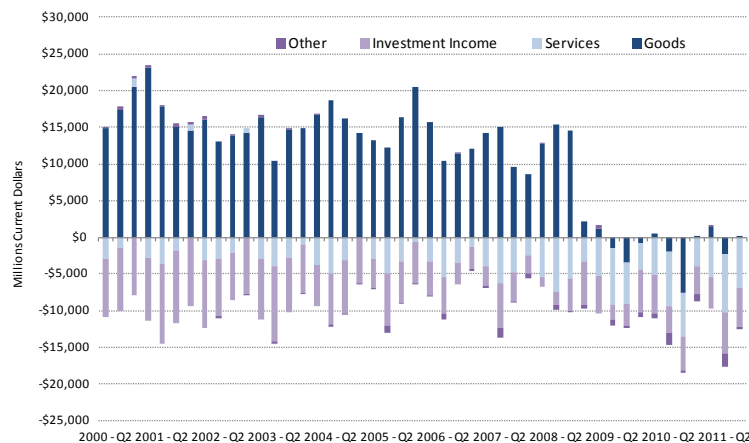
In the recent past Canada has had a large trade surplus in energy, forestry and even automotive vehicles/parts and this offset a rather large trade deficit in services (which

represents everything from business services to royalties and travel) and income due to foreigners for past investments.

Since the recession Canada's trade position has changed dramatically. Imports kept rising to the point where energy/mining exports no longer offset the imbalances elsewhere in the current account. To make the BOP balance, Canada has been importing over \$10 billion in foreign capital per quarter on average.

There's nothing inherently wrong with foreign borrowing - sometimes it's very useful - but it can't go on indefinitely (just ask Greece). Fortunately, Canada will have more time than others to correct the imbalance, thanks to its strong initial position; but the *status quo* is certainly not sustainable and we'll hear more about it going forward.

Canadian Current Account Balance, Quarterly



Source: Statistics Canada