

## **FINANCE MINISTER JIM FLAHERTY'S SPEECH AT CANADA-U.K. CHAMBER OF COMMERCE**

It is good to be here for the third time since I became finance minister more than three years ago. And it is a pleasure to be here.

This is a momentous time, as you know, as we go through the synchronized global recession. And I will speak a bit this morning about where we are in Canada, of course, where we are globally. A bit about the last day and a half here in the United Kingdom and our discussions with our G20 partners...

I'll talk a bit about the meetings of the past day and a half. I can tell you that the results exceeded our expectations. The spirit of partnership in the G20 and the determination around the table looks well globally and I think will augur well in the weeks and months ahead.

The G20 leaders and the Finance Ministers, all of us together, we're firmly focused on tackling the global crisis and the decisions that were taken reflect that focus. This focus I might add began at our meetings in October in Washington. The G7, G8 ministers meet semi-annually. So in the autumn, we meet in Washington in October. And I can tell you that the October meeting in mid October, the Friday afternoon in the Treasury Department was not the ordinary meeting of G7 Finance ministers.

This was the meeting at which there was incredible focus, as I guess crises focus the mind. There was incredible focus.

That was a meeting at which the usual communiqué was done away with and which we agreed on five basic principles upon which we would proceed. That was also that Friday afternoon where we agreed that we would take that to the IMF, to the World Bank, to the G20, which we did, that evening and the next morning to the then President of the United States, George Bush, George W. Bush. And then to the IMF, to the Council of the Americas, the Finance ministers from North America, Central America and South America, and we all agreed then on those five principles.

I say all of that because the five principles upon which we agreed in October 2008 are the principles that continue to guide us in our discussions globally. In the G7, the G8, the G20, the IMF, the World Bank, APEC. I'm going to tell you, if global meetings could solve this crisis, it would have been solved some months ago. We have lots of meetings.

But this meeting in particular this week built on those principles. We've made strides towards renewing global economic growth and toward preventing further

crisis. But I also need to say this: that the focus is on the current situation. There are those who are advancing more grand schemes, if I may put it that way. But we are focused. We are focused on what we are facing now.

That is we need to fix the banks, we need the financial markets to function properly. We used to talk about last year about, what was it, liquid assets and then they became toxic assets. Now, I'm told we're to call them legacy assets. It doesn't matter. They're bad debts. And we need to cleanse the banking system. That's number one.

Number two, we need to ensure that we together as governments, including the government of Canada, provide adequate stimulus in our economies. Why is that important globally? It's important globally because stimulus builds on stimulus. We're a trading country. We're all trading countries who believe in free trade. We're against protectionism. Therefore, it's important that we all emulate ourselves and have stimulus in our economies. The World Bank, the IMF talked to us about having more than two per cent stimulus by the end of 2010. In Canada with our partners in the provinces we will have a stimulus of in excess of three per cent of our GDP by the end of 2010.

Thirdly, stand firmly against protectionism. And this is vitally important. If the 1930s teach us anything, it is to stand against protectionism. Protectionism does not protect us. In fact, it exposes us to a great deal of economic harm. So we stand firmly against that. Not only do we say that. We act that in Canada. In my budget this year, in January, we are in fact taking away some tariffs that exist now on manufacturing. So this is important that we actually act in a way that is consistent in that in which we believe. And that is, we believe in free trade and we are against protectionism.

Fourthly, and this is important also, this crisis in credit, this financial crisis that began or became evident, I suppose, in August 2007 in the United States with the sub-prime mortgage crisis, as it has moved from being a financial-sector issue into being an issue in the real economies, in the industrialized world, in the developed world and then into the emerging economies and then, into the lowest income countries in the world.

So we made important strides in the last day and a half in terms of ensuring that there's adequate financing available, credit available through the International Monetary Fund, for emerging economies that need that access to credit, some of which is caused by repatriation of credit. And secondly then, moving to the lowest income countries, particularly through the World Bank, to ensure that those countries have the support they need from the stronger economies.

So Canada has done its part. We are in fact the lead contributor with respect to the lowest income countries. This is important because this crisis has moved throughout our economies into all of the countries in the world.

Now, let me talk a bit about Canada, which is a happier note, I must say, in the global situation. I have a reputation now with my colleagues, Finance ministers, with the Chancellor and so on of talking about our boring banking system. So I'm going to talk to you about our boring banking system for a while and our life insurers will tell me that I shouldn't talk about our boring banking system. I should also talk about our boring financial system. So I include our life insurers in all of this.

We're fortunate in Canada in several ways. Our banking system has now all of our top five banks in the top 50 banks in the world. I don't know if you saw in the Financial Times last week when they did the list, from 1999 on one side of the page and the list in 2009, on the other side of the page, in 1999, none of the Canadian banks were in the top 50. In 2009, all five of the top Canadian banks are in the top 50; one of which is number 10 globally; four of the top 10 in North America.

And our life insurers are doing well as well.

Why is this? And if we look back in recent Canadian history, we can see I think three clear factors. One is a relatively conservative economic philosophy, investment philosophy by our banks. One other reason is that our governments in Canada permitted the commercial banks, the top banks to acquire the investment banks, which they did acquire the investment firms back in the late 80s, early 90s.

Why is that important? It's important because then they came under the regulatory umbrella of the Office of the Superintendent of Financial Institutions in Canada. Why is that important? That's important because we are relatively strict regulators with relatively high capitalization requirements.

So this followed over several years. We do have a relatively strict regulatory environment. I speak, I can tell you especially in recent months, regularly with the Superintendent of Financial Institutions, of course, the Governor of the Bank of Canada, we interact in a coordinated, collaborative way to ensure that our financial system does not have difficulties that we do not anticipate.

This is important for our economic potential as well. Our challenges are not over, of course. We've done a great deal to mitigate the effects of these difficult times.

If I go back to September of last year, there was no suggestion then by any economist that our economy would go into recession. It did go into recession in the last quarter of last year. When we see the numbers for the first quarter of this year, they will confirm that we are in a recession.

How does one describe this? Something like one of my colleagues, a Finance minister, said the other day, "In November, the ball rolled off the table and it hasn't hit the floor yet."

It's not a bad description. And then where are we in this recession? Well, the most accurate description I've heard is that we are closer to the bottom and I think that is fairly descriptive of how I see things.

So what did we do in Canada? Well, in October, we were in an election campaign and so it's unusual for a government to do this, but we did move forward because we had to, to guarantee the international debt of our banks, which we did, and also to provide capital to our banks by purchasing CMHC mortgages, which are ensured mortgages by the government of Canada.

That provided some capital to our banks and we did that precipitously during the election campaign which is unusual for any government. But we also did it so that our banks would not be at a competitive disadvantage internationally because of the intervention of other governments with respect to their banking systems.

Having said that, we have not had to put any taxpayers' money into our financial system in Canada, nor do I anticipate that we'll be obliged to do so. We did this year in our budget bill after the January 27th budget provide me, the Minister of Finance, with the authority to do that if we have to do that. But that was done in a prophylactic way because I had sense over the course of the past 18 months or so what the Americans have had to do. And to some extent, what the U.K. has had to do, and other countries, in terms of their financial system.

So we want to ensure in Canada that we have all the tools at our disposal that we might need to use, were things to get dramatically worse. Which we do not anticipate.

Our economy did contract in the last quarter of last year. But the contractions in other places have been substantially more significant. As you know, the GDP in France contracted by five per cent in the last quarter; the GDP in Japan contracted by 12 per cent; our economy contracted by 3.4 per cent in the last quarter.

So what do we do as we move forward? We did a very broad consultation in Canada in the months of December and January. We listened to the Canadian people. This is not a time, my friends, for ideology. This is a time for ensuring that we do what countries need and what we need to do globally. And that's why we did the steps, we took the steps we took in the January 27th budget in Canada.

We did several key things. One is reduce taxes again to provide a stimulus to the Canadian economy. I am very pleased that the provinces in Canada have followed our exhortation since 2006 to reduce their corporate taxes, especially in the budget of the province of Ontario last Thursday.

We will have overall in Canada and in 80 per cent of the Canadian economy now by 2013 the corporate tax rate combined, the federal-provincial of 25 per cent. This is a great step forward in terms of branding Canada as a low-tax jurisdiction. Fifteen per cent federal tax, brought it down by more than 22 per cent when we took office in 2006, and get the provinces down to about 10 per cent. This is a great opportunity globally to brand Canada as a low-tax jurisdiction.

We're harmonizing our federal goods and services tax, GST, with provincial taxes. Again, a major step forward last week in the Ontario budget when the Ontario government announced a recent agreement with us to reduce their tax and to harmonize it overall. What does it mean? It's a stimulus of five billion dollars in the Ontario economy this year.

I'm from Ontario, I was the Finance minister of Ontario, so it's a bit of a cause for me. So forgive me for talking about this. But this is very important in the middle and longer term for the Canadian economy. Lower corporate taxes, harmonized sales taxes across the country.

Because of the leadership of the government of Ontario, what we'll see coming is that those provinces, the remaining four provinces that are not harmonized in terms of a VAT will seek to do so.

So that's important in the longer term for our country and for a rational system. It also means that for businesses, just carrying on business in the province of Ontario their savings administratively will be about half a billion dollars, 500 million dollars each year.

So this is a remarkable time. It shows that there's some good that comes out of crises and focusing the mind and making sure that we take actions that are well placed during a difficult time.

How does the world view Canada? The IMF says Canada is better placed than many countries to weather the global financial turbulence and world-wide

recession, thanks to sound policy management and proactive steps to maintain economic and financial stability.

Critics used to call us boring. As I said, boring has its benefits these days. I was pleased to see the BBC economist, the website the other day, Stephanie Flanders says, she says... She gave Canada best prepared award. She said nowhere, but by most key measures, the Canadians are coming out of this crisis in a league of their own. She compliments our financial system's strength and soundness. She also compliments our fiscal position and the fact that it has allowed us to contribute significant stimulus to the economy.

And I quote: "The most impressive thing of all about Canada's position is that you are probably reading about it for the first time. Canadians are so sensible they even have the sense not to brag in case things turn out badly for them after all."

So I perhaps should stop bragging.

The truth is, of course, we have a lot to brag about. In many parts of the world, governments have been forced to intervene and bail out banks and other financial institutions. As I said a moment ago, we have not been obliged to do that in Canada. We have not seen any bank failures or anything close to that.

We have not had to inject equity in our banks. In fact, our top five banks have been able to raise equity this year and in the last quarter of last year. Over a year and a half into the global liquidity crisis, Canada's banks and other financial institutions remain sound, well capitalized and less leveraged than their international peers. And as I say, this is a tangible result of a rigorous regulatory regime.

We have substantial capital requirements for our financial institutions. They are above minimum international standards and they are higher than in other jurisdictions. In fact, heading into this crisis, Canadian banks maintain healthy capital buffers above what was required by our regulator. Canada also has a cap on leverage.

And as I said a moment ago, you know, the number-one issue is fixing the banks internationally and making sure that we have a flow of credit. This is imperative in order for the real economies to begin to recover.

Capital to asset ratios in Canadian banks are in the high teens compared to ratios in the 30s for U.S. investment banks and the 40s and 50s for many European banks. In the aftermath of the financial crisis, we are now witnessing global

banks trying to reach those Canadian capitalization levels. So it's a global race, I'd say, to get boring like the Canadian banking system.

Past practice is paying off for us. I thank the people who are in this room, many of whom are involved with Canadian banks or work with the Canadian banks. We have a close working relationship with the Canadian banks and I certainly do with the CEOs in Canada. This is important in terms of ensuring that we do not engage in practices collaboratively that are negative for the Canadian people and that we're fully aware of what is transpiring.

The positive state of the Canadian banking system was highlighted by the, just before his visit to Canada, by President Obama on February 19th when he pointed to Canada as a model for the way forward.

So has the World Economic Forum, which has described the Canadian financial system as the most sound in the world. The IMF describes it as a system displaying remarkable stability amidst global turbulence.

But we're not an island. We are a trading country. We are a relatively small trading country. So how do we deal with this crisis?

First of all, in the budget, as I said, we'd lower taxes. We also created an extraordinary financing framework of up to 200 billion dollars to make sure that there is adequate credit available for small business, medium size business and big business. In Canada, as some of you know, we have a particular problem relating to the North American auto sector, the Detroit Three that we are working on in tandem with the government of the United States and the government of the province of Ontario.

But the number-one issue that I heard when I consulted across Canada through the month of December, the Christmas period and into January with small business people, with Canadians from every walk of life and my economic advisory council which represents some of the larger businesses in Canada, the number-one issue was access to credit, access to financing. We're not over that hurdle yet. But we ensured in the budget that we created the extraordinary financing framework to make sure that we can address these issues.

I'll announce next week the advisory group that's going to keep me informed about gaps in our financing network. We're employing our Crown corporations, Export Development Corporation, EDC, the Bank, BDC as well for the smaller businesses. We're employing the power we have to put equity into those Crown organizations to ensure that we have adequate credit across the country.

This is being done collaboratively with the Canadian banking system. I'm meeting with the CEOs sequentially now to ensure that they understand exactly what we're trying to accomplish here, which is to make sure that we do not have

gaps in our system, that creditworthy entities in Canada will be able to obtain credit. And as I say, we will use our Crown organizations, our Crown corporations to accomplish that, in cooperation, I trust, with our banks to ensure access to credit.

The other thing of course we did, and this is further to the agreement that all of us reached at the G20 leaders meeting in Washington in November, is to ensure adequate stimulus in our economy. So our stimulus in the Canadian economy by the end of 2010 in cooperation with the provinces will be in excess of three per cent, what the IMF had mandated, we agreed to this, was at least two per cent. This is important. It's important in Europe as well. There's some debate, as you know, about the amount of stimulus in Europe.

We understand in Canada, the inclusion of the automatic stimulators that happen in the economies in Europe and they happen in our economy as well in terms of employment insurance. And these are substantial when they kick in because of increasing unemployment.

And I have to say this, that there is agreement among the G20 countries that we are all taking adequate stimulus steps. This is very important, as I said earlier, because stimulus builds on stimulus as we deal with trading economies.

In our economic action plan as well, which was our budget this year, as I say, we provided permanent tax relief, substantial stimulus. Some calls now, and they were in the last day and a half, for more stimulus spending. I respectfully would suggest that we let the stimulus spending that we're doing enter our economies. Our fiscal year started two days ago in Canada, April 1st, and I look forward to a very substantial stimulus entering our economy in the next 90 days. Our Parliament was cooperative in terms of getting our stimulus package through Parliament and our public servants have been quite responsive, if I put it that way, to the sense of urgency that we face.

There is no point in spending 10, 20 billion dollars in 2010. We need to spend it now. The stimulus is needed in our economy now, as it is in the other economies. The unemployment pressure is now. So we need to act now. That's not that easy to do with a large bureaucracy, so one has to impress upon them the need to act now.

I know you're all thinking, yes, Minister, and so on, but it is important to do that and we have, I can say, and I'm confident in the Canadian government that we have that, that support that we need in terms of getting the money out the door in the next 90 days.

We have the authority now through Parliament to spend 90 per cent of our stimulus dollars in the next six months, most of which we can spend in the next 90 days. It's not glamorous. It's things like repairing bridges, repairing roads, repairing university and college buildings, that kind of thing. It's not glamorous. It doesn't require environmental assessments, thank goodness, because that would delay things substantially. But it is employing people, it is providing stimulus to the economy, and that's precisely what I heard from Canadians that we need to do.

Another challenge then, and this is a challenge for many of us in the G20, what do we do about running deficits and how do we exit from deficits? What's the exit strategy for governments? This is important, obviously, you know because running large deficits is inflationary eventually and has currency consequences as well.

What we did in our budget this year, in our economic plan and our plan for the next five years is we anticipated deficits going forward three, four years, mainly this year, this fiscal year and the next fiscal year. But the spending will end. It is a use-it-or-lose-it proposition for the provinces, the municipalities and the private sector. This is essential.

I mean, I got into politics because I was so upset in the 1970s and the 1980s at the spending habits of Canadian governments, of deficit upon deficit upon deficit, creating large public debt to the point where more than a third of Canadian tax dollars that were sent to Ottawa each year were being used to pay interest on the public debt. And we do not want to go back to that place.

So the rule that I put in the budget this year is this: that as we come out of this recession, every dollar that we have in surplus will be used first of all to pay off the deficits that we will incur in this year, next year and probably into the next fiscal year. We have to do that in order to ensure that we do not go back into deficit after deficit spending. And the other rule we need to do, of course, is when we get through the two years of stimulus spending, this fiscal year and the next fiscal year, that we stop and that we do not continue it as any part of program spending.

All of this is in recognition of the extraordinary times that we are in, requiring extraordinary steps which we took in this year's budget and which we will continue with over the course of this year and next year in Canada.

It is extraordinary. I mean, the events of the last six months, as I say, are extraordinary. The importance of coordinated stimulus internationally is very important. The importance of staying away from protectionist actions, very important, big lesson from the 1930s. In terms of regulation of our financial

institutions, Canada I'm proud to say was the co-chair of Working Group One for the Financial Stability Forum. The report was delivered to the G20 ministers and was accepted and was published yesterday. This is important in terms of financial regulation, of all systemically important institutions, and of all systematically important activities.

This is a system-wide approach to financial regulations, strengthening international regulatory standards, increasing transparency, ensuring that all financial markets, products and players are appropriately regulated and subject to the oversight needed to prevent future financial calamities.

So we've done the regulatory side. We'll have to persist in that, the G20 leaders are going to meet again in the autumn. The Financial Stability Forum, which will now be called the Financial Stability Board, will be doing the international financial standards setting. The IMF will be doing its financial assessments of governments and financial systems as they've done in the past throughout the world with the support of the G20.

This is important in order to restore confidence in the banking systems internationally. We will get through this. We have been through recessions before. For those of you who are Canadian, I look around the room and see how old people are, not as old as I am, I guess, but at least the 1980s, the early 80s, some of you will remember in Canada in September 1981, the prime rate was 22.5 per cent. You don't remember, you're too young.

And then we had the recession in the early 90s as well. But I say it to those of you who are Canadian here. Most people in Canada came from other places, including the United Kingdom. Most of them came on boats. Most of them came with nothing. Many of whom died because of disease while they were travelling to Canada. We commemorate that in various places in Canada.

Relatively speaking, this is a mild economic recession. These are relatively mild challenges for us. We will come out of this strongly. Fiscally, Canada and the Canadian governments, and I include the provinces, are in strong fiscal positions, having run surpluses for a time.

We are able to withstand this. We are taking the necessary steps so that Canada, in a monetary and fiscal policy sense, will accelerate out of this recession as we move forward. So I say to you with a degree of confidence that I think is warranted that the Canadian situation is strong, that our fiscal and monetary situations are both strong and that we're taking the necessary steps to move out of this recession. As we do so, we'll see the Canadian economy accelerate and I look forward to coming back, oh, next year or so, and being

able to talk in a very, very happy way about the recovery of the Canadian economy and I hope the economy throughout the G20.

Thank you very much.