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Market View – Canada's NIIP is showing (and growing)

By Warren Lovely

As the holiday lull settles over markets, why not reflect on a seemingly arcane set of data offered up by Statistics Canada this morning: Canada's net international investment position (or NIIP for short). Why bother? Well, ask yourself this: does the Canadian dollar outlook interest you? Or what about Canada's sovereign rating… any cares there? If so, then these data are informative. At its root, Canada's NIIP is synonymous with the country's net foreign asset position. Take the total value of Canada's international assets (i.e., money put to work outside the country in direct investments, foreign equities and other portfolio assets, loans, etc.), then subtract the current value of foreign investment in Canada and, voilà, you have a net international investment position. As of Q3, it looked like this:

Canada's international assets	–	Canada's international liabilities	=	Canada's net international investment position
C$6,087 billion	–	C$4,917 billion	=	C$1,170 billion
[Record]		[Record]		[Record]

As market valuations for many financial assets are trending variables, there are records all over the place. Canada has never had such a valuable stockpile of international assets. We've also never owed as much to international investors, but I digress. Objectively, Canada's NIIP is reasonably solid. At C$1.17 trillion, it has reached record heights too, rising C$94 billion vs. the prior quarter and up a nifty C$344 billion compared to a year ago—more than recovering an early 2020 setback as virus onset saw equities briefly tank. Again, as a market value measure, this international investment position is subject to FX and asset price valuation adjustments. These revaluation effects were the real story in Q3, since Canada remained a net borrower on a flow basis (consistent with an ongoing current account deficit). During Q3, the revaluation boost from rising market prices (read resurgent equities) dwarfed the translational hit from a stronger C$ by roughly 4½:1.

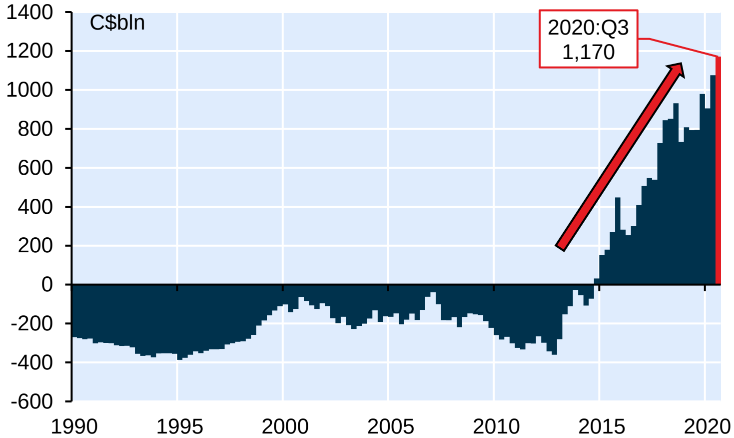
Canada's positive NIIP tally for Q3 works out to C$31,000 for every single Canadian. (Not enough for a shiny new Tesla Model 3, but just imagine all those dollar bills stuffed in your holiday stocking.) Put another way, Canada's NIIP is now around 50% of annual nominal GDP—hardly chump change. Of course, Canada hasn't always been so handsomely endowed when it comes to our external balance sheet. The country was a net external debtor all through the 1990s, which made a loss of investor confidence particularly problematic a generation ago. Canada was still a net debtor through the 2000s, before starting to turn things around in 2013 or thereabouts (Chart 1).

Turning to the sectoral breakdown, it's no surprise that Canadian governments are running up the credit card with international investors. As of Q3, Canada's general government sector owed C$576 billion to non-resident investors (>25% of GDP). This gross external debt has surged more than C$100 billion since the start of the year. Judging from the deficits being run (and the borrowing being done) in Ottawa and across the provinces, Canadian governments will be running an even larger international tab in the coming quarters. As StatCan appropriately highlighted, about one quarter (~C$140 billion) of our government gross external debt needs to be repaid (or refinanced) in the next year. So maintaining the confidence of international investors is presumably a key priority for treasurers at all levels of government, even if the Bank of Canada is currently doing its utmost to swallow net government bond supply.

To be sure, today's pandemic-driven budgetary erosion and rapid debt accumulation (a sizeable chunk of it financed externally) is not lost on rating agencies. Fitch, who was quick(er) to crack the sovereign with a downgrade back in June, just offered a fresh warning: "Canada's Federal Fiscal Plans Could Renew Rating Pressure" (7-Dec). But coming full circle, don't lose sight of the support Canada's positive net international investment position lends to the sovereign rating at some other credit rating agencies, including at S&P. Having a positive NIIP is a non-trivial mitigant to a persistent current account deficit. It gives Canada a better external risk assessment that what you might see in some other small, open economies… Australia being a particularly relevant example. We're not apologizing for the red ink our governments are running, but this is hardly the only factor influencing our nation's sovereign credit rating or currency valuation. So while this data release might have escaped your attention, consider tucking Canada's positive NIIP somewhere in the recesses of your investor brain during the holiday season and beyond.

Chart 1: Canada's positive external balance sheet

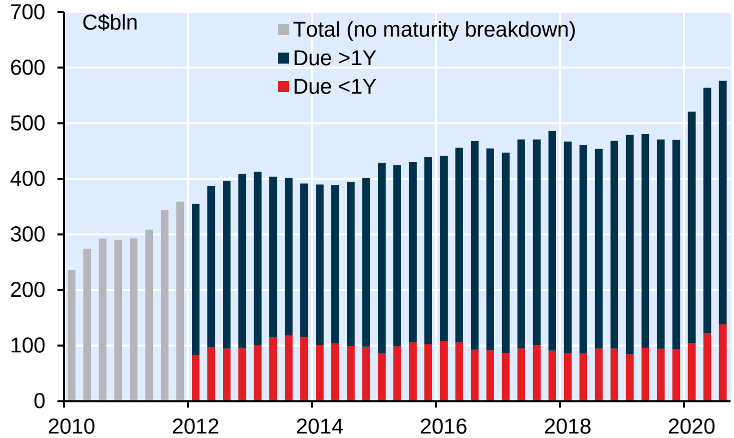
Canada net international investment position (market value)



Source: NBF, StatCan | Note: Canada's international assets less international liabilities

Chart 2: But more external debt for governments

Canada government gross external debt (market value)



Source: NBF, StatCan | Note: Maturity breakdown available from 2012 onwards

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