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Canada drawing foreign investors

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Capitalizing on 'world's love affair' with country, Ottawa plans first euro-denominated bond issue in more than a decade

Foreign investors are hungry for a piece of Canada.

A stable banking system, a recovering economy, an abundance of commodities and a fiscal policy deemed to be sound are enticing investors, and in turn boosting Ottawa's access to foreign financing and strengthening the dollar.

Playing into what Scotia Capital has labelled "the world's love affair with Canada," the Finance Department announced plans Tuesday for its first euro-denominated bond issue in more than a decade. The government is seeking at least €1-billion ($1.49-billion) from the 10-year bonds, and bankers said there is enough interest to sell twice that amount. Ottawa's move came as the dollar rose for the fourth consecutive day, closing at 96.25 cents (U.S.), its highest since mid-October.

"The world wants what Canada has: natural resources, stable currency and responsible fiscal policy," said Andy Busch, Chicago-based currency and public policy strategist for BMO's U.S. investment unit.

Canada's financial system is stable, the country's economy is relatively strong and the national debt load is forecast to be much lower than that of many other developed nations as they spend their way out of recession. On top of that, commodity prices are resurgent, boosting sales for exporters of raw materials and drawing foreign investment in Canadian companies in areas such as mining and the oil sands.

Oil prices are near a 14-month high and metals such as gold and aluminum are jumping. The Reuters/Jefferies CRB Index, which tracks 19 raw materials, rose on Tuesday to its highest level since October, 2008, amid signs factories are revving back to life.

"There has been renewed interest in commodity currencies generally and the Canadian dollar is benefiting," said Ian Stannard, foreign-exchange strategist at BNP Paribas SA in London. "We see some further potential for the Canadian dollar to appreciate."

The rising dollar is good for the country's psyche, and for shoppers heading to the U.S., whether they be consumers or companies looking for acquisitions. However, it's likely to concern the Bank of Canada and slow the pace of recovery because it can hurt exporters by making their goods more expensive.

Central banks, meanwhile, are looking at currencies such as Canada's to diversify their holdings amid a long-term decline in the U.S. dollar. Russia said late last year that it would add Canadian dollars to its holdings, and Finance

Minister Jim Flaherty has said he suspects China may do the same.

Global investors, including central banks, "are beginning to look at countries like Canada as a place to not only buy commodities from, and buy companies from, but also buy currencies from," said Rob Wittmann, chief executive officer of Toronto-based Knightsbridge Foreign Exchange.

The Canadian government is hoping to benefit from that positive sentiment. The Finance Department said it will issue the euro-denominated bonds in the "near future." The new bonds, the first in more than a decade to be floated in euros, will be used to bolster its foreign exchange reserves.

Credit markets in Europe are booming and the sale will likely go well, said Suki Mann, a credit strategist at Société Générale in London.

The federal government raised $3-billion (U.S.) in September in its first sale of U.S.-dollar denominated bonds in more than a decade. That deal was met with massive demand, bankers said, which bodes well for the new offering in euros.

"Canada's standing in the world is currently very high, which should mean relatively easy access to ample foreign financing," said Eric Lascelles, chief economics and rates strategist at TD Securities. "This is especially true in Europe, where various European states have recently fallen upon hard times, providing an especially sharp contrast with Canada."

The Canadian currency, meantime, could trade at parity with the greenback on a sustainable basis by the middle of the year, said Bank of Nova Scotia strategists.

The dollar reached parity against its U.S. counterpart in late 2007, rising as high as $1.087, before dropping below 80 cents in late 2008 as the financial crisis deepened. The Canadian dollar rebounded and rose 15.8 per cent against the greenback last year. It also strengthened against the yen, euro and Mexican peso.

Not everyone thinks the currency will continue to climb. Canada remains vulnerable to a still-weak United States, its main trading partner, and the auto sector continues to flail, said Carl Weinberg, chief economist of Valhalla, N.Y.-based High Frequency Economics. He thinks both oil prices and the loonie will decline from current levels.

For now, the appreciating currency and the challenges it poses to exporters diminish the odds of a Bank of Canada interest rate hike any time soon.

"The Canadian dollar's rise means the Bank of Canada needs a really, really, really strong case for tightening monetary conditions in the spring," Mr. Weinberg said. "We cannot see it happening."

The central bank will make its next interest rate announcement on Jan. 19. Officials have said they plan to keep the key lending rate at a record low of 0.25 per cent until the middle of the year, unless the outlook for inflation changes.