July 28, 2015

Matt Galloway
CBC Radio One
Metro Morning
PO Box 500 Stn. "A"
Toronto, ON M5W 1E6

Dear Mr. Galloway:

Re: Shadow Banking

I am responding to your broadcast on the subject of "shadow banking" with guest, Armine Yalnizyan, which aired last Friday, July 24, 2015.

By way of background, the Canadian Mortgage Brokers Association represents mortgage brokers and many alternate mortgage lenders across the country.

Admittedly, shadow banking is quite the term – it connotes a sense of mysterious, perhaps even nefarious individuals lurking in a dark background, lending money to hapless victims in a clandestine, illegal fashion, akin to (as you have suggested) "loan sharking". However, the term lacks clarity and does not do justice to the various "alternate mortgage lenders" in the Canadian marketplace. I shall explain this.

First off, alternate lenders do not do "banking" and should not in way be characterized as "bankers". Banks are deposit taking institutions, which take deposits from the public, and then highly leverage those deposits for lending purposes. Of course, in some ways alternate lenders do resemble banks. For instance, both make money off of the spread between funds paid to investors, or in the bank's case, interest paid to depositors on their deposit funds, and the interest income earned from loans, which for obvious reasons, needs to be higher than the investor or depositor costs. However, banks are much more highly leveraged than your traditional alternate lender, resulting in a dramatic asymmetry in the liquidity structure of a bank.

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In addition, there are many kinds of alternatives to non-bank lenders. These include credit unions, trust companies, and monoline or wholesale lenders. Some of these lenders make equity loans and all follow lending guidelines not too far from those of the banks. They make a massive contribution to the economy by providing mortgage funds, which are generally brokered through mortgage brokers. Are these lenders captured in the term "shadow banking"? This is far from clear. Who is caught in the shadow banking net, and the value of the mortgage loans they fund needs clarification and quantification in order for there to be any meaningful dialogue on this subject.

Also, did you know that up until the 1960's, mortgage brokers who sourced mortgages from alternate lenders, and NOT banks, were the primary source of mortgage funds for most Canadians? A 6 per cent cap on interest rates which could be charged on residential mortgages by banks was eliminated in legislative amendments in the late '60's. Non-bank mortgage lenders were the primary mortgage lenders for the majority of Canadian households in the 1960's as the interests rate rose above 6%, pushing banks out almost completely out of the mortgage market.

The implication that Canadians who use alternate mortgage lenders in today's environment of low interest rate, might experience the same fate and catastrophic economic collapse as the US sub-prime mortgage crises of 2008, has no foundation. Alternate lenders existed long before 2008 and there is no reason to think that having alternate lenders in today's financial environment will put the Canadian economy at any greater risk of collapse than it did in 2008.

To the contrary, there is no question that alternate lenders are an essential component of the Canadian economy. Alternate lenders play a pivotal role in the financial lives of Canadians by providing:

- financing for new buyers, who have not yet established credit;
- debt consolidation loans, which result in affordable debt payments for borrowers;
- solutions to borrowers with impaired credit, so that they can eventually repair their credit;
- financing to homeowners who are in the midst of foreclosure or creditor protection proceedings, so they can continue with homeownership;
- bridge financing for buyers who need temporary financing pending the sale of another property;
- equity take out mortgages for needed repair and maintenance projects;
- start-up capital for new developments which banks are not prepared to fund; and
- funds for business development and expansion.

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If alternative lenders did not exit, the effects would reverberate throughout the country, with the loss of many jobs, more foreclosures and bankruptcies, drastically reduced business and construction development, and a devastating impact on Canada's economy.

Please know that we are prepared to discuss this subject with you and your listeners, if you should wish to present a competing perspective from that of Ms. Yalnizyan. You can contact me at samanthagale@mbabc.ca

Yours truly,

Samantha Gale, LLB
CMBA Executive Director