3. Additional reserves contributed in the first six months by new banks based on one-half of the notes payable of Canadian financial institutions affiliated with foreign banks have been estimated.

4. Phasing-in of the reduction of reserve ratios commencing with January 1, 1981

	Deposits (Billions)	Reserve Rate Demand	Reserve Rate Notice	Estimated Primary Reserves
October 29/80	\$129	12%	4%	\$6.6
December 31/80	130	12	4	6.7
June 30/81	138	11¾	3⅞	6.9
December 31/81	147	11½	3¾	7.1
June 30/82	157	11½	3⅝	7.3
December 31/82	167	11	3¼	7.5
June 30/83	178	10¾	3⅜	7.7
December 31/83	190	10½	3¼	7.9
June 30/84	203	10¼	3⅛	8.1
December 31/84	216	10	3	8.3

The above schedule indicates that even with an extremely conservative estimate in the growth of deposits, the primary reserves at the Bank of Canada would always increase even in spite of the gradual decrease in the statutory reserve ratios and without including reserves on foreign currency deposits. If foreign currency deposits were included in the above schedule, the reserves would be increased by an additional \$90 million based on October 31, 1980 statistics. After December 31, 1984 the reserve ratios would remain constant and based on a rate of growth proportionate to the growth of deposits in the banking system, the reserves would continue to grow at a faster rate than shown in the schedule.

The above projections indicate for example that, after the first full year of the phasing-in of the reduction in reserve ratios, it is estimated that the primary reserves will have grown from \$6.6 billion at October 29, 1980 to \$7.1 billion at December 31, 1981, without including any reserves on foreign currency deposits. That is to say, the effect of the phased-in reduction of the reserve ratios is more than offset by the effect of the projected growth in the deposit base.

Therefore your Committee estimates that there should be no net loss of reserves nor decrease in revenue to the Bank of Canada if foreign currency deposits were exempted from the primary reserve requirement. Indeed, as indicated, on a conservative basis it is estimated that there would be a steady growth in the reserves and in the revenue earned by the Bank of Canada from the investment of these cash reserves.

It appears, therefore, to your Committee that the proposed reserves are in excess of requirements and that the elimination of the proposed 3% reserve on foreign currency deposits of Canadian residents would not result in a net decrease in revenue to the Bank of Canada and the Consolidated Revenue Fund.

The proposed reserve introduces inefficiencies in the Canadian foreign currency market which eventually results in higher rates on foreign currency loans to Canadian residents booked in Canada.

Your Committee notes that the demand for foreign currency funding by Canadian residents is related largely to specific, legitimate financing needs. Export of large transactions in lumber, pulp and paper, wheat or fish are often denominated in foreign currency, and most exporters try to hedge their foreign currency position in the currency in which the payment is to be made. Your Committee believes that the reserve on foreign currency deposits by Canadians will thus increase the cost to Canadian exporters and that this is not in the public interest.

SUMMARY

1. The proposed reserve will probably increase the cost of foreign loans to Canadian exporters who hedge their foreign currency position, to the Canadian and Provincial Governments and other Canadian foreign currency borrowers as well as increase the costs of importers who maintain foreign currency deposits. This is not in the public interest.

2. It would discriminate against the smaller depositors who do not have the facilities to move their deposits offshore like other larger depositors.

3. It would discriminate against Canadian resident depositors of foreign currency in favour of non-resident depositors.

4. It would discriminate against Canadian banks in competition with trust companies and other near-banks.

5. The annual growth of deposits and the addition of reserves from new banks would result in an increase in the aggregate reserves even if the proposed reserve on foreign currency deposits was eliminated, with no decrease in revenue to the Consolidated Revenue Fund.

Your Committee is of the opinion that the Government has greatly underestimated the amount of foreign currency deposits which will flow out of Canada.

As noted earlier in this report, representatives of the Canadian Bankers' Association in their testimony before your Committee have indicated considerable concern about the potential loss to the Canadian banks in Canada and to the general Canadian economy at large if most of these foreign currency deposits are booked off-shore.

Your Committee has received evidence that the 12% and 4% reserves were in excess of requirements of the Bank of Canada for monetary control and for purposes of liquidity. The reserve on foreign currency deposits of Canadian residents as proposed