

Weekly Updates Issue # 578

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1. Weekly Markets Changes

[August 19, 2016]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
14,687.46 -59.99 -0.41%	2,183.87 -0.18 -0.01%	18,552.57 -23.90 -0.13%	5,238.38 +5.48 +0.10%	\$0.7768 +0.48¢ +0.62%	\$1,345.80 +4.10 +0.31%	\$48.57 +3.88 +8.68%

2. Stronger short-term outlook for Canada, says Conference Board

[August 19, 2016] Canada's in line for a slight acceleration in economic growth six months from now, says the Conference Board of Canada based on readings of its Composite Leading Index. That index increased by 0.9 points to 109.1 in June.

In June, there was a pickup in industrial and commercial building permits, says the Conference Board, which bodes well for building construction in the closing months of the year. “[That] could signal the long-awaited turnaround in business investment,” says Pedro Antunes, deputy chief economist of The Conference Board. “However, [this] good news was partially offset by more apprehensive credit lenders, and a modest decline in consumer confidence.”

Overall, four of the index's nine components improved, while two deteriorated and three saw little change. In addition to the increase in industrial and commercial building permits, employment insurance claims fell sharply in June—suggesting an improved labour market.

Meanwhile, the energy price index showed another improvement in the month as crude oil prices continued their slow and steady climb in June, from the sub-US\$30 levels seen earlier this year. New orders for durable manufactured goods also experienced decent gains.

On the other hand, the interest rate spread widened in June after narrowing in two consecutive months. This suggests apprehension in credit markets.

Additional data

The Conference Board's Index of Consumer Confidence saw a halt in its momentum in June, falling two points. That means consumers were more pessimistic regarding future financial conditions than they had been in May, which could hurt consumption spending in the coming months.

The S&P/TSX Composite Index was virtually unchanged in June, but is faring well, adds the Conference Board.

The average workweek also flattened in June, following its largest monthly decline in over two years. This component has remained below its 2014 average throughout much of the last year, a sign of the weak employment numbers seen since the collapse in oil prices.

3. Inflation rate 1.3% in July; June retail sales dip

[August 19, 2016] The country's annual inflation rate was 1.3% in July as Canadians paid more for shelter and food but less for fuel, Statistics Canada said Friday.

This overall inflation number in the federal agency's latest consumer price index came in a little weaker than the 1.5% year-over-year increase in June. Prices climbed in most major categories compared with 12 months earlier—with the cost of shelter and food items generating the biggest upward nudges on inflation, the report said.

For example, the index found that Canadians paid 9.8% more for potatoes last month compared with July 2015, 10.3 per cent more for fresh or frozen fish and 15.6 per cent more for apples. Under the shelter category, the price of electricity was 5.4% higher than the year before.

In contrast, gasoline prices fell last month by 14% compared to a year earlier, fuel oil dropped 13.4% and natural gas slid 10.3%.

The agency's core annual inflation rate, which omits some volatile items like gasoline, stayed at 2.1% last month.

By province, Statistics Canada found that Newfoundland and Labrador once again saw the highest inflation of any province last month at 3.4%, which followed a 2.4% rate in June.

In July, people in Newfoundland paid 14.1% more for telephone services and 26.3% more for home and mortgage insurance compared to 12 months earlier. Statistics Canada also noted that on July 1 the provincial portion of the harmonized sales tax increased in Newfoundland and New Brunswick, where consumer prices rose 2.5% last month.

Retail sales

On Friday, the agency also released its latest data for retail trade, which showed that total sales in June were 0.1% lower than the previous month. The overall number rang in at just over \$44.1 billion in June.

By comparison, revised numbers showed that total retail sales were essentially flat in May after rising 0.8% in April.

The agency found that weaker sales at food and beverage stores—down 1.5% compared to May—were a big contributor to the overall June decline in retail sales. At these stores, beer, wine and liquor sales dropped 4.7% the largest one-month drop in booze sales since June 2013, Statistics Canada said.

Sales at motor vehicle and parts dealers were up 2% in June. The category received a boost from a 2.5% increase in sales at new car dealers, which saw their numbers rise for the first time in five months, Statistics Canada says.

A CIBC research note says, “Retailing was a bright spot for the Canadian economy to start the year, so we can stomach a weak month in June, particularly with the Child Care Benefit cheques likely to boost spending in the second half of the year.

“Headline sales saw a modest 0.1% drop, but the notable weakness was beneath the surface, after stripping out a strong month for car-lot spending. Ex-autos sales slipped by 0.8%, with 7 out of 11 categories down on the month.”

4. Income of wealthy Americans climbed 7.7% in 2015

[August 19, 2016] Income inequality in the U.S. has surged near levels last seen before the Great Depression. The average income for the top 1% of households climbed 7.7% last year to \$1.36 million, according to tax data tracked by Emmanuel Saez, an economics professor at the University of California, Berkeley.

That sliver of the population saw pay climb at almost twice the rate of income growth for the other 99%, whose pay averaged a humble \$48,768.

This is a problem because most Americans are still recovering from the Great Recession, and wage disparity is adding to the problem. The average income for the 99% is still lower than it was back in 1998, after adjusting for inflation. Meanwhile, incomes for executives, bankers, hedge fund managers, entertainers and doctors have all steadily improved. This group accounts for roughly 22% of all personal income in the U.S.—more than double the post-World War II era level of roughly 10%.

This income disparity is thinning out the ranks of the middle class.

A defining economic challenge

President Barack Obama has called rising inequality “the defining challenge of our time,” and experts warn it may be slowing overall economic growth. Further, greater inequality has created a distrust of government and of corporate leaders.

The result has also been a backlash against globalization that many Americans feel has tilted the economy against them. For example, factory workers currently compete with employees in countries such as China, India and Eastern Europe who work for multinational corporations, while middle-class pay is being depressed.

Social factors have also amplified the income inequality trend. Single-parent families are more likely to be poor than other families, and are less likely to ascend the income ladder. Finally, men and women with college degrees and high pay are more likely to marry each other and amplify income gaps.

Clinton and Trump’s views

Hillary Clinton has highlighted inequality in multiple speeches, with her positions evolving somewhat over the past year. She says she hopes to redirect more money to the middle class and the impoverished.

Clinton would also raise taxes on the wealthy, increase the federal minimum wage, boost infrastructure spending and offer the prospect of tuition-free college.

Meanwhile, Donald Trump has offered a blunter message about a hollowed-out middle class and a system “rigged” against average Americans. He has yet to emphasize income inequality in his campaign, but has pledged to bring back factory jobs that are long associated with the rise of the middle class.

To achieve that, Trump has promised new trade deals and infrastructure spending. But Trump has also proposed a tax plan that focuses on dropping the corporate tax rate and simplifying the tax code—as a result, he’d bring the lowest marginal tax rate up to 12%, from 10%, and set the highest as 33%, compared to 39.6%.

5. CMHC approved Maple Bank before watchdog seized its assets

[August 18, 2016] Canada’s national housing agency gave Maple Bank GmbH’s Canadian branch the green light during a financial review, just one month before the federal banking watchdog seized the company’s assets amid a German tax investigation, documents show.

Documents obtained by The Canadian Press through an access-to-information request show that CMHC reviewed Maple Bank GmbH’s status as an issuer

of mortgage-backed securities and a seller of Canada Mortgage Bonds in January 2016.

At the time, CMHC's so-called operations support division said it was "comfortable" maintaining Maple Bank's status, the documents show.

The housing agency was aware of the German bank's dispute with authorities, which had been ongoing for about four years, according to the documents.

A month after the financial review, Canada's federal banking regulator announced it was taking temporary control of the Canadian branch's assets in light of the news that German banking regulator BaFin was shuttering the bank after a tax dispute threatened its financial stability.

Maple Bank is headquartered in Frankfurt but has a Toronto branch where its main business was securitization, securities financing and structured secured wholesale lending.

On Feb. 11, an insolvency administrator was appointed in Germany to handle the windup of the bank's operations.

The Office of the Superintendent of Financial Institutions, Canada's banking watchdog, announced on Feb. 15 that it was making its temporary control of Maple Bank's assets permanent.

The following day, the Ontario Superior Court granted a winding-up order with respect to Maple's Canadian branch and appointed KPMG as the liquidator. A winding-up order is a court order that forces an insolvent company into compulsory liquidation.

When asked why CMHC was comfortable with maintaining Maple Bank's status as an issuer of securities even though it was aware of the ongoing German tax probe, the federal agency says it does not disclose details of its internal assessments.

"CMHC has a rigorous process to assess participants in its securitization programs," the agency says in an emailed statement. "This includes the daily monitoring and evaluation of both public and non-public information to assess its risks, including the risk of loss due to the failure of any counterparty. CMHC's securitization programs are structured to minimize the risk of loss if a party were to fail."

A spokesperson adds CMHC does not expect to incur any losses stemming from Maple Bank's failure.

Maple Bank did not return requests for comment.

The insolvency of Maple Bank GmbH also prompted CMHC to undertake a review of another issuer, according to the documents, although the entity's name is redacted.

When asked for more details on that review, CMHC says it "regularly reviews all issuers and assesses any events that may impact them."

The federal agency declines to identify the entity under review or provide any further details.

6. Lenders may have to share mortgage risk

[August 17, 2016] The Department of Finance may soon require banks to share risk with mortgage insurers, reports the Globe and Mail.

“In a briefing note to Finance Minister Bill Morneau and released under Access to Information, department officials say they are studying an option to introduce ‘risk-sharing’ for lenders, a move that would likely mean a deductible payable by the banks on the mortgage insurance provided by Canada Mortgage and Housing Corp. (CMHC) and its private-sector competitors.”

A Finance Canada spokesperson cited OECD and IMF recommendations when explaining why the government was analyzing “housing-related vulnerabilities.”

Overheated housing markets have led to much hand-wringing. The briefing note’s release comes on the heels of Vancouver imposing a 15% tax on foreign property buyers.

7. Would more rental units make the GTA more affordable?

[August 16, 2016] Ontario regulators should do more to encourage rental construction in the Toronto area in response to the city’s housing affordability crisis, a CIBC economist says.

Benjamin Tal, lead author on a new CIBC Economics report about GTA housing, says provincial and municipal policies should encourage developers to build more family-friendly rental units to help reduce rental prices and cool demand for detached homes.

Provincial government policies have been encouraging new land for condo building over houses, but more renters are needed, the CIBC report says.

“The issue is that the condo market so far has been built for investors and designed mainly for young people, students, the one-person type unit,” Tal tells Advisor.ca, noting higher condo supply. “[T]he new supply should accommodate for the increased propensity to rent among older people and young families, and for this, you need larger units.”

Demand firm

Even as condo supply has surged, people continue to seek detached or semi-detached homes. Ryerson University’s Centre for Urban Research and Land

Development also released a study this week that found most home buyers in the GTA want a detached house or a low-rise home, as opposed to a condo.

“The GTA is in a twilight zone of home prices characterized by a homeownership mentality that is slow to change to the required higher propensity to rent,” the CIBC report says.

Tal says “purpose-built” rental units are projected to be 18% of total new supply this year in the GTA, but that number should be more like 25% or 30%. Regulators could use incentives like development charges to encourage more rental units, he says, with opportunities for pension funds to invest in the projects.

“Rent control was designed to help tenants, which is fine, but you also have to find a way to encourage supply. Otherwise it’s backfiring,” he says. People will also be nudged into renting because of affordability, he says, with higher supplies keeping rental prices affordable.

Rising house prices

CIBC says detached and semi-detached homes were less than 27% of GTA housing starts last year, falling from 40% in 2009, even as demand has increased. That has helped push up prices for the most sought-after housing.

“Evidently, a condo unit is not for everybody. Many priced-out millennials in search of a single-detached house simply take to the highway and start driving away from Toronto, not stopping until they find something that they can afford,” the CIBC report says.

The Ontario government has proposed higher-density requirements for the province’s municipalities, which would make less land available for detached homes.

CIBC also proposes that the federal government raise the minimum down payment above 10% for homes valued between \$500,000 and \$1 million. They also suggest hiking the qualification rate for those seeking popular five-year, fixed-rate loans, accounting for over 30% of originations.

Rising amortization periods, and increased borrowing to finance down payments, are supporting home ownership, CIBC says, adding: “Subprime lending is on the rise while the interest rate sensitivity of prime borrowers is elevated.”

8. Manufacturing gains 0.8% in June

[August 16, 2016] Statistics Canada says manufacturing sales gained 0.8% to \$50.2 billion in June after losing 1.0% in May.

Economists had expected a gain of 0.7%, according to Thomson Reuters.

Statistics Canada says the increase was due to higher sales of machinery and transportation equipment products. On a constant dollar basis, overall sales gained 0.5%, indicating a higher volume of goods sold.

The machinery industry gained 5.8% at \$2.7 billion, following five consecutive monthly declines, while the transportation equipment industry added 1.4% to total \$10.7 billion in June.

Manufacturing sales in June were up in four provinces, led by Ontario.

Ontario rose 1.4% to \$24.7 billion in June, while Alberta gained 1.8% to \$5.2 billion. New Brunswick fell 4.1% to \$1.3 billion.

9. Looking to precious metals? Watch these trends

[August 16, 2016] The depreciation of the Chinese renminbi and its impact on precious metals has gone largely unnoticed, says Scott Vali, vice-president of equity for CIBC Asset Management.

But, “[China] continues to depreciate that currency, and that’s a deflationary shock [to] the global system,” says Vali, who manages the Renaissance Global Resources Fund. However, “we’re still fairly constructive on gold. There are always gyrations in the near term but [gold’s] well supported as we look out.” The U.K. referendum and threat of Brexit has also affected the bullion market. “Brexit has increased the uncertainty around growth rates not only in the U.K., but has also now put question marks around the sustainability of the Eurozone and [its] growth,” says Vali.

This has meant the U.S. Federal Reserve is likely to pause in terms of its rate hike expectations, he adds, but that’s positive for bullion market. “In that environment, we think gold will continue to do well.”

He notes, “We’re also seeing interest rates on government bonds and 10-year bonds move into negative territory, both in Germany and in Japan. That’s creating an environment where constituents in those markets are now looking outside for yield, and they’re moving to the U.S. and other areas where [...] they’re driving up the value of bonds.”

Interest rates around the globe are likely to remain negative for a longer period, Vali says, and that, in turn, is also supportive for gold.

Silver, platinum and palladium

In some cases, “silver can be a higher-beta way of playing gold,” says Vali. “It tends to react with the economy. So if the economy looks like it’s becoming more robust, silver historically has done a little better than gold.”

The outlook for platinum and palladium is tied to the performance of the automotive and industrial industries. “[They’re] used as metals in exhaust manifolds and, as such, they’re impacted by industrial production,” he adds.

“And, more specifically, they’re impacted by automotive and trucking entities. We’re less certain about the value of those metals going forward.”

In addition, platinum and palladium markets are impacted by currencies and the cost of production. “We’ve seen the South African rand depreciate somewhat over the past few years, and that means the cost of producing platinum and palladium has also declined. In some cases, the supply and demand balance has [become] less favourable.”

Overall, says Vali, “There are more dynamics to look at when you’re looking at platinum and palladium, from [both] an industrial demand standpoint and a supply standpoint, than perhaps there is with gold.”

10. Canadian home sales drop for third straight month

[August 15, 2016] The number of homes being sold via Canadian MLS Systems fell by 1.3% month-over-month in July 2016. And, with similar monthly declines having been posted in May and June, national sales activity in July came in 3.9% below the record set in April 2016.

Overall, home sales activity was down from the previous month in slightly more than half of all markets in July, led by Greater Vancouver and the Fraser Valley. Transactions in these two markets peaked in February of this year and have since dropped by 21.5% and 28.8%, respectively—much of the national sales decline in recent months reflects slowing activity in B.C.’s Lower Mainland.

But, “national sales and price trends continue to be heavily influenced by a handful of places in Ontario and British Columbia, masking significant variations in local housing market trends and conditions across Canada,” says CREA President Cliff Iverson.

Gregory Klump, CREA’s Chief Economist, adds, “Home sales continued to trend lower, while price gains further accelerated in the lower mainland of British Columbia. This suggests sales are being reined in by a lack of inventory and a further deterioration in affordability.”

Plus, “the new 15% property transfer tax on Metro Vancouver home purchases by foreign buyers took effect on August 2nd, so it will take some time before the effect of the new tax on sales and prices can be observed. That said, the new tax will do little in the short term to increase the supply of homes.”

Home sales highlights:

- National home sales fell 1.3% from June to July.
- Actual (not seasonally adjusted) activity came in 2.9% below July 2015.

- The number of newly listed homes rose 1.2% from June to July.
- The MLS® Home Price Index (HPI) rose 14.3% year-over-year in July.
- The national average sale price climbed 9.9% in July from one year ago; net of the Greater Toronto Area (GTA) and Greater Vancouver, it advanced 7% year-over-year.

More details

Actual (not seasonally adjusted) sales activity was down 2.9% year-over-year (year-over-year) in July 2016, marking the first year-over-year decline since January 2015 and the largest since April 2013.

In line with softening activity in the Lower Mainland, year-over-year increases have been losing momentum since February 2016. Sales were down from levels one year earlier in about 60% of all Canadian markets, led by Greater Vancouver, the Fraser Valley, Calgary and Edmonton.

The number of newly listed homes rose by 1.2% in July 2016 compared to June. While new supply climbed in fewer than half of all local markets, increases in Greater Vancouver and the Fraser Valley, Greater Toronto, Calgary and Edmonton outweighed declines in smaller markets.

With sales down and new listings up, the national sales-to-new listings ratio eased to 61.6% in July 2016 – its second monthly decline following its peak of 65.3% in May (a sales-to-new listings ratio between 40% and 60% is generally consistent with balanced housing market conditions).

The ratio was above 60% in about half of all local housing markets in July, virtually all of which continue to be located in British Columbia, in and around the Greater Toronto Area and across Southwestern Ontario.

The number of months of inventory is another important measure of the balance between housing supply and demand—it represents the number of months it would take to completely liquidate current inventories at the current rate of sales activity.

For July, there were 4.6 months of inventory on a national basis at the end of July 2016. This is unchanged from readings in each of the previous two months and continues to indicate a tight balance between supply and demand for homes.

In fact, the number of months of inventory has trended lower since early 2015, reflecting increasingly tighter housing markets in B.C. and Ontario. It currently sits near or below two months in a number of local markets in British Columbia and in and around the GTA, with some regions in the GTA are down to just a couple of weeks of inventory.

Additional statistics

In July, the Aggregate Composite MLS Home Price Index rose by 14.3% year-over-year in July 2016, the biggest gain since November 2006. For the sixth

consecutive month, year-over-year price growth accelerated for all Benchmark property types tracked by the index.

Two-storey single family home prices continued to post the biggest year-over-year gain (+15.9%), followed by townhouse/row units (+15.3%), one-storey single family homes (+14.3%), and apartment units (+11.1%).

Overall, while prices in 9 of the 11 markets tracked by the MLS HPI posted year-over-year gains in July, increases continue to vary widely among housing markets. For example, Greater Vancouver (+32.6%) and the Fraser Valley (+37.6%) posted the largest year-over-year gains by a wide margin, followed by Greater Toronto (+16.7%), Victoria (+17.5%) and Vancouver Island (+11.6%).

By contrast, prices were down -4.2% and -1.5% year-over-year in Calgary and Saskatoon respectively.

Meanwhile, home prices rose modestly in Regina (+2.7% year-over-year), Greater Montreal (+1.8% year-over-year) and Ottawa (+1.1% year-over-year). Greater Moncton recorded its largest year-over-year home price increase (+8.4%) among an unbroken string of gains posted every month over the past year.

The national average price continues to be pulled upward by sales activity in Greater Vancouver and Greater Toronto, which remain two of Canada's tightest, most active and expensive housing markets. The actual (not seasonally adjusted) national average price for homes sold in July 2016 was \$480,743, up 9.9% year-over-year.

If these two housing markets are excluded from calculations, the average price is a more modest \$365,033 and the gain is trimmed to 7% year-over-year.

Even then, this reflects a tug of war between strong average price gains in housing markets around the GTA and in British Columbia versus flat or declining average prices elsewhere in Canada. The average price for Canada net of sales in British Columbia and Ontario in July 2016 edged down 0.2% year-over-year to \$310,905. The year-over-year percentage change in the national average price excluding B.C. and Ontario sales has now been in negative territory for 20 consecutive months.

Have a nice and fruitful week!