Weekly Updates Issue # 635

1. Weekly Markets Changes

[October 13, 2017]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
15,807.17 +78.85 +0.50%	2,553.17 +3.84 +0.15%	22,871.72 +98.05 +0.43%	6,605.80 +15.62 +0.24%	$0.8008 +0.39c +0.49%	$1,303.82 +28.92 +2.27%	$51.45 +2.16 +4.38%

2. Year over year, September home sales down 11%: CREA

[October 13, 2017] The Canadian Real Estate Association says the number of homes sold in September edged up compared with August — as sales picked up in about half of all local markets.

The association says sales through its Multiple Listing Service in September were up 2.1% compared with the previous month.

The increase was led by gains in Greater Vancouver and Vancouver Island, the Greater Toronto Area, London and St. Thomas, Ont., and Barrie, Ont.

Compared with a year ago, sales in September were down 11% as the number of homes sold were down in close to three-quarters of all local markets.

The national average price for homes sold in September was just over $487,000, up 2.8% from a year ago.

Excluding Greater Vancouver and Greater Toronto, the average price was just over $374,500.

A look at home prices

Falling home prices in Toronto in September dragged down the Teranet National Bank national composite house price index — as it posted its first monthly decline since January 2016.

The national index, which includes 11 cities, fell 0.8% compared with the previous month, the largest monthly decline since September 2010.

The move lower came as the index for Toronto, Canada's largest housing market, fell 2.7% on a month-over-month basis.

David Madani, senior Canada economist at Capital Economics, said a sharper slowdown in price inflation in the coming months is unavoidable.

"And with interest rates on the rise and mortgage financing rules likely to be tightened significantly later this year, the worst is still to come," said Madani, who has been long-time bear on the housing market.

Home sales in Toronto have fallen since April when the Ontario government moved to cool the hot housing market with a package of changes including the introduction of a tax on foreign buyers.

The Bank of Canada has also raised its key interest rate target twice this year, prompting the big banks to raise their prime rates, pushing the cost of variable rate mortgages higher. The cost of new fixed rate mortgages have also climbed in recent months as yields on the bond market have risen.

In addition to Toronto, the price index for Quebec City lost 2.3%, while Hamilton slipped 1.9%, Halifax dropped 0.4% and Winnipeg lost 0.3%.

The index for Victoria was flat, while:

- Vancouver increased 1.3%;
- Calgary added 0.7%;
- Montreal climbed 0.3%;
- Ottawa-Gatineau gained 0.3%; and
- Edmonton edged up 0.2%.

Compared with a year ago, the national composite house price index was up 11.4%.

Toronto was up 18.0% compared with September 2016, while Hamilton gained 19.5% and Victoria added 14.7%. Vancouver climbed 10.5% compared with a year ago.

B.C. weighs in

Home sales and average prices rose in B.C. in September, according to the latest figures from the British Columbia Real Estate Association.

It says a total of 8,340 residential unit sales were recorded by the Multiple Listing Service during the month, an increase of 9.9% from the same period last year.

Total sales amounted to $5.8 billion, up 30.2% from September 2016, and the average MLS residential price was $693,774, up 18.5%.

Year-to-date, the dollar value of B.C. residential sales was down 12.8% to $57.6 billion, when compared to this time last year.

The BCREA also says residential unit sales declined 13% year-to-date to 81,608 units while the average price was down 0.2% to $705,501.

Cameron Muir, the association’s chief economist, says B.C. home sales rose nearly five% from August on a seasonally adjusted basis.
“Total active listings on the market continue to trend at 10-year lows in most B.C. regions, limiting unit sales and pushing home prices higher,” he said.
“While the economic fundamentals support elevated housing demand, rising home prices are eroding affordability, particularly for first-time buyers.”

3. More from Morneau next week on changes to tax proposals

[October 13, 2017] Finance Minister Bill Morneau will unveil changes Monday aimed at mollifying the many critics of his controversial small business tax reform proposals.
The damage control effort will begin with a special briefing early Monday morning for Liberal backbenchers, some of whom have been among the most vocal opponents of the measures.
Sources, speaking on condition of anonymity because they weren’t authorized to speak publicly, say Morneau wants to demonstrate to anxious Liberal MPs that he’s heard their concerns about his tax reform plan and is addressing them.
The proposed reforms were intended to put an end to measures which the government contends have allowed wealthy individuals to use incorporation as small businesses to unfairly reduce their income tax burden.
But they triggered an angry backlash from doctors, lawyers, accountants, shop owners, farmers, premiers and even some Liberal backbenchers, who maintained the reforms would hurt the very middle class Canadians that the Trudeau government claims to be trying to help.
The changes are expected to ensure the reforms are targeted more clearly at the wealthy.
They’re also expected to address concerns that the reforms will disproportionately impact women, inhibit the ability of small business owners to save for a rainy day and make it impossible for farmers, fishers and others to pass their businesses on to their children.
Morneau has acknowledged changes are required to address some of the concerns raised and to ensure there are no unintended consequences.
One source said that Morneau intends to emphasize to Liberal backbenchers that he will continue listening to any concerns about the proposed reforms, suggesting that Monday’s changes won’t necessarily be the end of the story.

As originally proposed, the plan would restrict income sprinkling, in which an incorporated business owner can transfer income to a child or spouse who is taxed at a lower rate, regardless of whether they actually do any work for the company.

It would also limit the use of private corporations to make passive investments that are unrelated to the company and curb the ability of business owners to convert regular income of a corporation into capital gains, which are taxed at a lower rate.

What's happened so far

The proposals were unveiled in mid-July but it took about a month for the backlash to materialize. Since then, the Liberals' popularity has taken a hit in some public opinion polls and the governing party's backbenchers have become increasingly anxious.

A number of Liberal MPs, including finance committee chair Wayne Easter, have complained about the messaging surrounding the proposals, which they say portrays small business owners as tax cheats.

The Conservatives have used the furor to accuse Morneau of hypocrisy, targeting small business owners while doing nothing to deal with legal tax avoidance strategies used by large corporations like Morneau Shepell, a human resources company headed by the minister until his appointment to cabinet in 2015.

That line of attack was bolstered Friday by news that for two years, Morneau failed to disclose to the federal ethics commissioner that he and his wife are partners in a private company that owns a family villa in southern France. CBC News reported that holding property through a private company is useful in avoiding inheritance taxes in France.

Morneau's ownership of the villa was disclosed but the involvement of the private company was not until last month, when CBC began to ask questions about it.

Dan Lauzon, a spokesman for Morneau, called the failure to disclose the company an "administrative error" and said the minister's office is working with federal ethics watchdog Mary Dawson to ensure he's "in full compliance with the spirit and letter of the rules."

Jocelyne Brisebois, a spokeswoman for Dawson, declined to say if the ethics commissioner is looking into the matter.

Under the Conflict of Interest Act, Dawson has limited power to do anything about it in any event, other than impose a fine of up to $500.

4. Global growth uptick not reducing income gap, says IMF's Lagarde

[October 13, 2017] World leaders should take advantage of the healthiest global growth in years to pursue policies that will spread prosperity to those being left behind, the head of the International Monetary Fund is arguing.

"It is not time to be complacent," IMF Managing Director Christine Lagarde said Thursday. "Policymakers can use this moment to provide more certainty and provide for the future risks."

Lagarde's warning came as global financial leaders gathered in Washington for the annual meetings of the 189-member IMF and its sister lending organization, the World Bank.

In addition, a meeting of finance officials from the world's 20 biggest economies, the Group of 20, is wrapping up Friday. Treasury Secretary Steven Mnuchin and Federal Reserve Chair Janet Yellen are representing the United States at these discussions.

IMF forecasters expect the global economy to expand 3.6% this year, the fastest pace since 2010. And Lagarde says three-fourths of the world economy is participating in the uptick, creating the broadest recovery in a decade.

But many workers have seen their wages stagnate and their jobs replaced or threatened by technology. And many countries are seeing a widening income gap between rich and poor. "The result is growing political tensions in many places and increased skepticism about the benefits of globalization," Lagarde said.

Discontent with globalization and inequality is stoking the populist politics that took Donald Trump to the White House and prompted British voters to opt out of the European Union. "We have to reduce the gap between those who have everything and those who have nothing," said French Finance Minister Bruno Le Maire.

While the IMF boosted its outlook for the 19-country Eurozone, Japan and China, it trimmed its estimates slightly for the United States compared with the projections it had made in April. It now sees U.S. growth at 2.2% this year and 2.3% next year, still up from the lacklustre 1.5% pace of last year.

IMF economists said the reduction of 0.1 percentage point for 2017 and 0.2 percentage point for 2018 reflected less certainty over when the Trump administration will be able to get its tax cut plan through Congress. Even before the reductions, the IMF's forecast was well below the 3% growth rates the administration says will be achieved with its policy changes to taxes and regulation and tougher trade enforcement.

A senior U.S. Treasury official, briefing reporters on this week's meetings, said the IMF has other concerns beyond getting involved in the U.S. tax debate. The official spoke on condition of anonymity to be able to discuss the U.S. agenda in advance of the meetings taking place.

An IMF report out Wednesday concluded that many countries could raise taxes on the wealthiest without sacrificing economic growth. But Lagarde suggested another way to cut income inequality: putting more women to work, improving their access to credit and narrowing their pay gap with men.

"A no-brainer," she said.

Lagarde said one thing the major economies will need to handle carefully is the movement away from massive economic support from their central banks. Such a move, if not well-telegraphed in advance, could disrupt global financial markets and reduce needed capital to developing countries.

The Federal Reserve has announced that it will start this month trimming its $4.5 trillion balance sheet, which was increased five-fold since 2008 as the Fed tried unconventional means to jump-start economic growth. The European Central Bank and the Bank of Japan have undertaken similar efforts.

On Thursday, European Central Bank chief Mario Draghi defended the ECB's aggressive easy-money campaign to revive the economy of the 19 countries that share the euro currency. He said the measures, which include a massive bond-buying program meant to push down interest rates, had helped create 7 million jobs over the last four years.

Speaking at a conference at the Peterson Institute for International Economics, Draghi conceded that unconventional monetary policy can have unintended economic fallout. But, he said, "the bottom line is, the distortions may be there, but sometimes the tradeoff is so powerful that you just ignore them and do the right thing."

5. Canada lags in business investment: Fraser Institute

[October 12, 2017] Canada is lagging far behind other developed countries when it comes to business investment, which is critical to grow the economy and increase living standards, finds a study released by the Fraser Institute.

"When businesses invest in the latest technologies and production techniques and expand their operations, it spurs economic growth and raises living standards for workers," says Philip Cross, former chief economic analyst for Statistics Canada and author of the study, in a release.

The study finds that Canada has suffered persistently weak levels of business investment — the money firms spend on buildings, machinery and equipment, and research and development — since at least 2000.

The last energy boom temporarily masked Canada's low levels of investment in other industries, but since the fall of energy prices in 2014, business investment in Canada is back to previously low levels. In fact, since the end of the third quarter of 2014, business investment in Canada has declined a staggering 18% (after accounting for inflation).

Crucially, Canada has one of the lowest levels of business investment among 17 developed countries in the OECD.

Business investment as a share of GDP (that is, business investment relative to the overall size of the economy) between 2015 and this year is projected to be just 10.9% in Canada — the second lowest among the 17 countries — compared to, for example, South Korea (21.3%), Australia (15.7%), Sweden (15%) and the U.S. (13.3%).

And Canada ranks 15 out of 17 in business investment per worker at just $9,290 compared to, for example, Switzerland ($17,423) and the U.S. ($14,889). Put differently, Canadian workers have just 62% of the capital available to them that American workers do.

"With low levels of business investment compared to other developed countries, Canadian workers do not have access to the tools and technology they need to be more productive and earn higher incomes," Cross says.

"The factors affecting business investment are complex, but governments across Canada have aggravated the problem in recent years with an onslaught of economically damaging policies such as higher taxes, costly regulations and increased uncertainty about future taxes by adding billions in debt."

6. Canadians face unfair income tax penalties: report

[October 12, 2017] Canadians are dealing with an unfair tax penalty on swings in their income from year to year, finds a report released by the C.D. Howe Institute. Further, the tax bite is the worst for lower-income Canadians and small business owners.

"Individuals whose incomes are irregular or fluctuate year-by-year face a greater tax burden than people with steady incomes," says Jean-François Wen, co-author of the report, in a release. "I call it the 'fluctuation penalty.' Reintroducing income-averaging provisions in the tax code would make the tax system fairer and encourage entrepreneurship."

The report tracks the individual incomes of Canadians for six consecutive years from 2005 to 2010 using Statistics Canada's database. Wen and co-author Daniel V. Gordon identify the characteristics of individuals with high penalties and assess the fairness of the outcomes.

To explain the penalty, they use the example of a person without dependents living in Ontario. Suppose she earns $50,000 in 2016 and $100,000 the following year, so her average income is $75,000 per year. However, her taxes for the two years are about $1,900 more than if she had earned $75,000 in both years. On an annual basis, her extra tax liability is almost $1,000, or 1.3% of her average annual income. A similar tax penalty on fluctuating income would occur in a case where her income had fallen from $100,000 in 2016 to $50,000 in 2017.

"The fluctuation penalty is a policy concern for reasons of fairness and the adverse incentives it may create for risk-taking activities, such as entrepreneurship," notes Wen. "Further, we find the fluctuation penalty is most acute for lower-income persons."

Prior to 1989, provisions in the tax code allowed taxpayers to smooth their taxable incomes by using an average of more than one year's income as the basis for calculating the tax liability, adds Wen. They were removed to simplify the tax code and because the number of federal tax brackets had lowered from 10 to three.

However, the federal and provincial governments have recently added new tax brackets. Taken together with the fact incomes have been less stable in Canada since the 1970s, particularly with the growth of part-time work in the so-called sharing economy, this points to the need for tax reform. "Reintroducing income-averaging provisions would help address the fluctuation penalty today," Wen concludes.

7. IMF warns Canada's high debt levels could weaken economy

[October 12, 2017] The IMF warns in a new report about Canada's high debt levels and higher-than-average pressure on Canadian households' ability to pay down that debt.

The IMF says in its Global Financial Stability report released yesterday that these dynamics in Canada's private non-financial sector leaves its economy more sensitive to tighter financial conditions and weaker economic activity.

Canada was named along with Australia, Brazil, China and Korea as countries where the debt-service ratio has risen to high levels.

The IMF also says there was a particularly strong need in these economies for financial sector policy to guard against letting these imbalances grow any further.

The IMF also notes that in Australia, China and Canada, where the ratio of household debt payments relative to disposable income is highest, it has been coupled with a steep increase in house prices.
It warns that past experience shows these two factors can create strain and, with a sharp fall in asset prices, can spill over to the economy.

8. Is Canada's housing market too hot?

[October 12, 2017] The price of a home in Canada increased 13.3% year-over-year in Q3 to $628,411, finds the Royal LePage House Price survey.
And home prices in the Greater Toronto Area (GTA), Greater Vancouver, the Greater Montreal Area, Calgary and Ottawa all rose at rates between 1.5% and 3.5%.
Despite the rise in prices, the "Canadian housing market is enjoying a Goldilocks moment – not too hot, and not too cold," says Phil Soper, president and CEO, Royal LePage in a release. "For the first time since 2011, we are seeing real estate in all five of our largest cities appreciate at a manageable, healthy clip."
Soper adds rising interest rates and a strong Canadian dollar should help to keep a lid on major market price appreciation. "Marginally higher borrowing costs should dampen domestic demand somewhat, and with less currency-adjusted purchasing power, foreign buyer activity is off peak levels and will likely stay that way in the near-term," he says.

Housing by city

Toronto and the GTA

During the third quarter, the GTA saw the largest year-over-year home price increase of any major Canadian market, surging 21.7% on the back of strong gains at the beginning of 2017. The aggregate price of a home in the GTA is $860,295, while the price of a home in the City of Toronto rose 21.8% to $861,397.
The market experienced a sharp drop in sales volumes beginning in April 2017, which continued through much of the third quarter. With underlying employment and economic growth on solid footing, the Toronto market began to grow again in August.
Potential buyers who were previously on the sidelines taking a wait-and-see approach have now jumped back into the market after realizing prices did not drop as certain market watchers had anticipated. On the supply side, some sellers who had attempted to capitalize on an uncharacteristically strong spring have taken their homes off the market. Together, these trends have

caused the region to revert to a more balanced market where supply and demand have stabilized in the majority of areas.

“A severe shortage of listings introduced unsustainable home price inflation into our two largest markets beginning in 2015,” says Soper. “Affordability eroded rapidly, concerned policy makers reacted with measures to slow demand, and sales volumes plummeted. Market corrections were triggered in Vancouver first, and some 10 months later, in Toronto.”

He adds, “Toronto home prices are much lower than those we see in Vancouver, and the overall size of the market is considerably larger. Waning foreign investment should impact the Toronto market less severely. We expect the correction to be shorter in comparison to what was experienced last year in B.C.’s Lower Mainland.”

Ottawa

Ottawa is turning out to be a major economic success story in 2017, given the heightened levels of hiring by the federal government. As of September, the city’s 5.8% unemployment rate sits below the national average, and it appears to be one of the few cities that has shrugged off the province’s new housing rules. Over the quarter, the aggregate price of a home in Ottawa increased by 7.9% year-over-year to $441,453.

Montreal

Quebec is now in the midst of what economists, and the province’s finance minister, refer to as a “virtuous circle.” The province’s economy has been improving over the last few years, and confidence among businesses and individuals is rising, with both choosing to spend and invest, creating jobs and further stimulating the economy. Further, the region is increasingly becoming a technology centre of excellence, attracting industry giants such as Google, Amazon and Facebook.

As a result of a stronger economy, the aggregate price of a home in the Greater Montreal Area rose 6.6% to $384,055. Montreal Centre saw the highest year-over year home price appreciation with an increase of 14.3% to $511,129, and home prices in Montreal West rose by 5.4% over the same period to $422,515.

Calgary and Edmonton

Alberta’s economy continues to rebound from its recession, and drilling activity has come back from last year’s levels. The price of West Texas Intermediate oil has averaged over US$49 per barrel this year, and the Alberta government is forecasting a price of US$55 per barrel in its 2017 to 2018 budget. Over the past year, Alberta has added 13,000 jobs, and full-time employment has grown by 31,500.

When looking to the housing market, many regions in the province have benefited from this recovery, with the aggregate price of a home in Calgary and Edmonton rising 5% and 4% year-over-year to $479,211 and $389,330, respectively.

Vancouver

Forecasters continue to raise their expectations for British Columbia's growth, with the province poised to lead or come close to leading all provinces in GDP this year, creating new jobs and stimulating growth within the province's residential real estate market.

During the third quarter of 2017, the aggregate price of a home in Greater Vancouver increased 2.5% year-over-year to $1,229,133. Over the same period, the City of Vancouver saw an increase of 2.2% to $1,439,652.

Housing by type

When broken down by housing type, the median price of a standard two-storey home in Canada rose 13.9% year-over-year to $748,049; and the median price of a bungalow grew 9.5% to $525,781.

Nationally, condominium prices increased 15.2% to $413,670 on a year-over-year basis, and have begun to appreciate faster than any other housing segment in large urban centres such as Toronto and Vancouver. This is likely to continue for the foreseeable future and begin a trend in other cities. The overall affordability of condominiums continues to attract first-time homebuyers and purchasers looking for attractively-priced real estate as new mortgage regulations, interest rate increases and higher home prices have effectively limited purchasing power.

"We expect single home buyers, couples or families with one child to favour condominium living," says Soper. "With the arrival of a second child, many young families will still follow their parents' footsteps and head to the suburbs."

He adds, "Regardless of where they live, the sheer number of peak millennials in Canada will shape our real estate markets over the next decade. Developers and planners will certainly respond with housing product that meets the needs of this influential cohort of real estate consumers."

9. Canadians pessimistic about their finances

[October 10, 2017] More than one-third (37%) of Canadians view themselves as working class, while 43% say they're middle class, finds an Ekos-Canadian Press survey.

It's the lowest sentiment recorded since 2002, Ekos says, when 70% of Canadians defined themselves as middle class.

At the same time, the incidence of those in the working class has nearly doubled.

Those self-identifications aren't just about people's bank balances, says Frank Graves, president of Ekos. It's about how they see their physical well-being, their emotional connections and general sense of their quality of lives.

"It's not just an economic debate," Graves says. "If we really see people falling out of the middle class, then we're going to have a less happy, less healthy society at some point in the future."

Ekos asked Canadians about their own short-term and medium-term financial outlooks, and only a minority of Canadians see things as getting better.

When asked about the quality of their own lives compared to those 25 years ago, 33% felt they were better off and 34% felt they were doing worse.

When asked how they think the next generation will do, 13% felt they'd be better, and 56% felt things would be worse.

But, perceptions of the economy do generally lag behind reality, Graves notes. The latest Statistics Canada numbers on job growth show there's been 10 months in a row of gains, the longest growth streak since 2008. Meanwhile, average hourly wages grew at the above-inflation pace of 2.2%, for the biggest increase since April 2016.

Canadians compared to Americans

The questions were asked as part of an ongoing effort to suss out whether the factors that have led to the overhaul of the political status quo in the U.S. and elsewhere in recent years exist in Canada.

The poll suggests they do. "It's not like people are moving out of the middle class and becoming upper class," Graves says. "They are falling backward, and I think the evidence is really quite clear is that that is probably the greatest source of the rise of populism and all of the unpleasant things that go along with that."

Anger from the working class in the U.S. was seen as a critical force behind U.S. President Donald Trump's march to victory. His promise to restore America's economy was embraced by people rallying around his slogan of making American great again.

Americans' outlook in turn shot up in the week after Trump was elected. A regular tracking survey done by the firm Gallup saw a 13-point jump in their confidence index, which looks at how Americans view current economic conditions and whether they think things are getting better or worse.

The jump came from a partisan shift — Republicans suddenly felt more optimistic about things than they had for a very long time, Gallup concludes.

About the survey: The telephone survey of 4,839 Canadians was conducted between September 15 and October 1. It has a margin of error of plus or minus 1.4%, 19 times out of 20.

Have a nice and fruitful week!

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