Weekly Updates Issue # 681

1. Weekly Markets Changes

[September 14, 2018]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
16,013.49 -76.78 -0.48%	2,904.98 +33.3 +0.86%	26,154.67 +238.13 +0.92%	8,010.04 +107.5 +1.36%	$0.7673 +0.77c +1.01%	$1,194.85 -2.07 -0.17%	$68.99 +1.24 +1.83%

2. Household debt rose slightly in Q2

[September 14, 2018] The amount households owe relative to their income crept higher in the second quarter, even as mortgage borrowing continued to slow, Statistics Canada said.

The agency said Friday credit market debt as a proportion of household disposable income increased to 169.1% as growth in debt outpaced income.

In other words, Canadians owed $1.69 in credit market debt for every dollar of household disposable income.

The ratio was up from 168.3% in the first quarter, however it was down from 169.7% in the second quarter last year.

BMO Capital Markets economic analyst Priscilla Thiagamoorthy noted the increase was "well below seasonal norms" and one of the smallest second-quarter increases since 2000.

"Despite edging slightly higher in Q2, the closely watched household debt-to-income ratio appears to have finally turned the corner from all-time highs," Thiagamoorthy wrote in a brief report.

"The key takeaway here is that borrowing cooled with the housing market as households adjusted to a slew of policy changes including tighter mortgage rules and gradual rate hikes."

Household debt has been identified as a key vulnerability for the financial system by the Bank of Canada, however the central bank noted earlier this year that the risk has lessened.

On a seasonally adjusted basis, households borrowed $19.6 billion in the quarter, down from $22.2 billion in the previous quarter.

The decrease came as demand for consumer credit increased, but was more than offset by a decline in both mortgage and non-mortgage loans.

The decline in mortgages came as the housing market slowed amid tighter mortgage rules and rising mortgage rates.

Rates for five-year fixed mortgages have been rising as yields on the bond markets, where the banks raise money, have also climbed higher.

Meanwhile, rates charged for variable rate mortgages have also climbed as the Bank of Canada has raised its key interest rate target.

On an unadjusted basis, household credit market debt, which includes consumer credit, and mortgage and non-mortgage loans, totalled $2.16 trillion.

3. With Ontario out, what's next for the CSA's proposals?

[September 14, 2018] The Ontario government surprised the investment industry on Thursday when it came out against CSA's proposed amendments to mutual fund sales practices, which would ban deferred sales charges (DSC) and limit the use of trailing commissions.

The new Progressive Conservative government's move comes after six years of consultation on embedded fees for mutual funds. In a statement, Finance Minister Vic Fedeli said the CSA's proposals would "discontinue a payment option for purchasing mutual funds that has enabled Ontario families and investors to save towards retirement and other financial goals."

Rebecca Cowdery, a partner at BLG who formerly worked at the OSC, called the move "unprecedented" after two consultation papers and all the time and effort the industry has put in. "I'm not saying it was good or bad," she said.

Neil Gross, chair of OSC's Investor Advisory Panel, said it's doubtful the CSA will proceed without Ontario's support.

"That's quite unfortunate, and we'll see if the Ontario minister puts forward an alternative," he said.

Such a process would take time, however, and "Ontario residents and ordinary people across the country will pay a heavy price" in the meantime, he said.

"DSC is not inherently evil and [the charges] have uses, but they're open to abuse," he said, including "conflicts of interest and inappropriate recommendations."

Gross also said Ontario's move could give the impression that "the rules of the investment game may change with every different government." This could make investors "skittish" and make it harder to raise capital, he said.

"That's why it's important for the government to exercise its power through appointing commissioners and to then let those commissioners develop a policy."

Cowdery said it's unclear what will happen with the proposals.

"It's way too early to say but, at this stage, people could assume that it will go through the regular process and they should make comments if they have them," she said, adding that she plans to comment on the proposals eventually.

The other provinces could proceed without Ontario's participation, "but of course Ontario is a very important player," she said.

Fideli's office declined to comment further on the proposals.

In an emailed statement to Advisor.ca, the Ontario Securities Commission said the minister's support "is critically important to the OSC, and we are respectful of our government's authority to decide whether any rules published for comment ultimately come into effect."

Several industry groups support the government's position.

Advocis said in a release that the decision "stands up for the consumer's right to choice when it comes to financial advice." The association also cited studies from between 2011 and 2016 that found "restricting access to professional financial advice would make it harder for the public to save, invest and achieve their financial goals."

IFIC also supported the decision. "The DSC is a good payment option for some investors who would not otherwise have access to financial advice," the organization said in a statement. "We think the CSA concerns can be addressed by strict firm guidelines around the sale of funds with a DSC, and by continued compliance and enforcement."

Meanwhile, several industry participants tweeted their disappointment with the government's position.

4. Feds face calls for lower taxes to improve competitiveness

[September 13, 2018] Pressure is building on Finance Minister Bill Morneau ahead of the Liberal government's fall fiscal update to include tax breaks to boost Canada's competitiveness.

Reports from the C.D. Howe Institute and the Fraser Institute released Thursday recommend lowering and restructuring taxes to encourage capital investment and improve the country's competitiveness, while another from PwC warned about the effect of U.S. tax reforms.

The overall growth of capital investment in Canada has reached a 40-year low, the Fraser Institute report says, while business investment in Canada has fallen since 2014 compared to the U.S. and the outlook for 2018 is poor, the C.D. Howe Institute says in its study.

Both reports highlight diminishing investment in categories that improve productivity and future wages, such as machinery, equipment and intellectual property.

"More competitive tax rates, including quicker capital-equipment write-offs, regulatory measures that cut red tape, internal and international trade liberalization and removing frictions that impede the raising of capital can all help Canadian businesses better equip their workers," said William Robson, one of the authors of the C.D. Howe study, in a release.

A study released Wednesday by PwC warned the American tax reforms will have a major, negative impact on Canada. They will shift investment to the U.S. and hurt economic activity in Canada, it said.

Various business groups have called for tax changes to address the impact of the sweeping U.S. tax reform that passed Congress late last year.

The PwC analysis said the U.S. changes threaten 635,000 Canadian jobs, which represents about 3.4% of all workers, and could lower Canada's gross domestic product by 4.9%. The report said $20 billion worth of government revenue could also be at risk.

The study was commissioned by the Business Council of Canada, which has been pushing for lower corporate taxes.

"Canada's relatively favourable corporate tax environment was a major advantage in terms of attracting new investment," said the report, which recommends federal and provincial tax reductions among its policy options.

"Due to the U.S. tax reform, this advantage has now disappeared."

The assessment paints a far bleaker picture than estimates released last spring by the Bank of Canada.

The central bank figured the U.S. reforms could lower business investment by about 3% from 2017 to the end of 2020. The bank said this would shave the level of economic growth by about 0.2% by the end of 2020.

CIBC CEO Victor Dodig addressed foreign investment earlier this week in a speech to the Empire Club of Canada.

Canada could be more globally competitive if the government clarified foreign investment rules to match the U.S. policy that allows companies to immediately write off the full cost of capital investments, he said.

Dodig also called on the federal government to allow companies to expense capital investments within a one-year period, which is allowed in the U.S.

Government considering targeted measures

Sources say Morneau is looking at targeted measures rather than broad-based corporate tax cuts, the Canadian Press reported.

Morneau told reporters this week that he hadn't ruled anything out when specifically asked whether tax cuts would be part of his competitiveness plan.

Industry stakeholders have been calling for lower taxes—but a cut to the federal corporate rate would come at a cost. A tool on the parliamentary budget officer's website estimates that a one-percentage-point reduction to the business tax rate would trim about $1.7 billion per year from federal revenues.

There are, however, also recommendations that Morneau consider a cheaper option: allowing all companies to immediately write off new equipment purchases.

The finance minister has been analyzing the impacts of the U.S. changes and has spent the summer on a "listening tour" to get feedback from the Canadian business community.

Morneau faced criticism from the business community after his February budget lacked specific steps to address their competitiveness concerns.

The finance minister wanted more time to assess the situation and his office has insisted he would avoid any "knee-jerk reactions."

5. National Bank partners with fintech Thinking Capital to offer small business loans

[September 13, 2018] Small businesses across Canada can now apply online for a loan with National Bank through the bank's new partnership with fintech lender Thinking Capital.

Small businesses can apply online for a loan and receive an answer in minutes, a release said. National Bank is using Thinking Capital's fintech platform, which uses artificial intelligence and proprietary algorithms to process and evaluate loan applications from small- and medium-sized businesses more quickly.

"We believe fintech providers and banks can work together to close the gap between the financing small businesses need and what they have access to," said Jeff Mitelman, CEO at Thinking Capital, in a release.

Thinking Capital was acquired by Purpose Financial earlier this year.

6. Brexit deal with EU ‘doable’ in two months: UK Treasury chief

[September 11, 2018] Britain’s Treasury chief said Tuesday that striking a divorce deal with the European Union over the next two months is “doable,” while the boss of Jaguar Land Rover warned that tens of thousands of jobs could be lost if the country crashes out of the EU with no agreement.

With Brexit a little more than six months away, concerns have grown that the sides will not reach a deal because the British Parliament and the governing Conservative Party are divided on what Britain’s future relationship with the EU should be.

In that event, Jaguar Land Rover CEO Ralf Speth said a so-called “hard Brexit” could result in the “worst of times” for the U.K. He said the U.K. is the company’s “home” but that a hard Brexit would cost Jaguar Land Rover, which is owned by India’s Tata Motors, more than 1.2 billion pounds a year.

“It’s horrifying, wiping our profit, destroying investment in the autonomous, zero-emissions (technologies) we want to share,” he told a Zero Emission Vehicle Summit in Birmingham, England.

He said the loss of jobs would be “counted into tens of thousands if we do not get the right Brexit deal.”

Hopes are fading that Britain and the EU can strike a deal at an EU summit in October as originally planned, but there are growing expectations that the EU is planning another meeting for November.

Treasury chief Philip Hammond told a House of Lords committee that he agreed with the EU’s chief negotiator, Michel Barnier, that a deal was possible in six to eight weeks if both sides are realistic.

“I think it is doable,” Hammond said.

Business groups and civil servants say a “no-deal” Brexit could cause disruption to shipping, barriers to trade with the bloc, a fall in the value of the pound and even shortages of essential goods.

Hammond said that “if we leave the European Union without a deal … we could expect a period when there would be some turbulence.”

He said it was “very welcome” that Bank of England Governor Mark Carney had agreed to delay his departure date from June 2019 to January 2020 to help navigate any Brexit-related economic bumps.

Hammond spoke hours after leading bankers downplayed the immediate impact of Brexit on London’s role as the hub of the financial services industry in Europe and on jobs.

“There’s no question this has been an unsettling event, but our industry is in a state of constant flux,” Mark Garvin, vice chairman of JPMorgan’s corporate and investment bank divisions, told a parliamentary committee. “We have been involved in far more significant tumult than this.”
Garvin said the jobs of only “hundreds” of JPMorgan’s 16,000 staff in the U.K. would be immediately affected by Brexit, though that could rise to around 4,000 in the years to come depending on the settlement reached between Britain and the EU.
In the immediate aftermath of Britain’s vote to leave the EU in June 2016, many experts warned that Britain’s financial services industry—a huge tax source for the government—would see hefty job losses as businesses relocated to EU cities such as Dublin, Frankfurt and Paris, to retain benefits related to Europe’s single market.
However, the number of jobs lost has not matched the doomsday predictions, and with just six months to go until Britain officially leaves, there are few signs that banks are panicking.
A group of pro-Brexit politicians and economists, meanwhile, argued Tuesday that Britain will be better off, not worse, if it leaves the EU without a deal on future trade.
Economists for Free Trade held a news conference in Parliament Tuesday alongside several leading pro-Brexit lawmakers, including former Foreign Secretary Boris Johnson.
The group argued that reverting to World Trade Organization rules, which can lead to the imposition of tariffs on certain goods, “would boost the U.K.’s trade with the rest of the world including Europe, lower domestic prices and boost inward investment.”
Critics say that assessment relies on overly optimistic assumptions, particularly on the extent to which trade would be boosted if Britain unilaterally abolished tariffs.
Hammond said the model used by Economists for Free Trade “are wildly out of line with assumptions that are used by other economic modelers, and frankly, I believe, are not sustainable.”

7. Canada needs clearer foreign investment rules to boost competitiveness: CIBC CEO

[September 11, 2018] The CEO of the Canadian Imperial Bank of Commerce says Canada must boost its global competitiveness and prepare for a future downturn by offering clearer foreign investment rules, matching a U.S. policy

that allows companies to immediately write off the full cost of capital investments.
Victor Dodig says a lack of clarity on foreign investment rules is making business leaders and their clients hesitant to make significant investments in Canada.
He added that Ottawa should allow companies to expense capital investments within a one-year period, a measure which is now in place south of the border.
Dodig said during his speech to the Empire Club of Canada in Toronto that changing this rule in Canada would spur immediate capital investment, help level the playing field and attract investors—who have other global choices available.
Dodig also said that Canada should remove “embarrassing” interprovincial trade barriers to instill confidence.
He added that at a time when many countries around the world are saying no, Canada needs to do more to attract the best and brightest to have much needed human capital.

8. August housing starts fall below expectations

[September 11, 2018] Canada Mortgage and Housing Corp. says the pace of housing construction starts slowed in August compared with July.
The agency says the seasonally adjusted annual rate of housing starts was 200,986 units in August, down from 205,751 units in July.
Economists had expected an annual pace of 210,300 starts for August, according to Thomson Reuters Eikon.
The decrease came as the annual pace of urban starts fell 2.5% to 184,925 units. Starts of urban multiple-unit projects such as condos, apartments and townhouses fell 2.4% to 132,700 units in August while single-detached urban starts fell 2.6% to 52,225 units.
Rural starts were estimated at a seasonally adjusted annual rate of 16,061 units.
CMHC says the six-month trend for housing starts was 214,598 units in August, down from 219,656 in July.
“The national trend in housing starts continued to decline in August from the historical peak that was recorded in March 2018,” CMHC chief economist Bob Dugan said.
“This moderation brings total starts closer to historical averages, largely reflecting recent declines in the trend of multi-unit starts from historically elevated levels earlier in the year.”

The pace of housing starts is another sign that Q3 GDP growth will be slower than Q2, said Royce Mendes, chief economist at CIBC, in a research note. The slower pace also fits his expectations that higher interest rates and tighter mortgage rules "will turn this former stalwart of growth into a drag on the economy."

9. Commercial real estate investment hits record high in Q2

[September 10, 2018] Canadian commercial real estate (CRE) investment reached a record high in the second quarter, driven by two mergers-and-acquisitions transactions and large single-asset sales.

CBRE Canada reports in a release that $16.5 billion in transactions was recorded in Q2, up 38% from the previous record of about $12 billion in the first quarter of last year—and 105% above the five-year quarterly average.

Investment volume for the first half of the year was almost $27 million, an all-time high for a half-year period. Two major M&A transactions in the quarter—Choice Properties' acquisition of Canadian Real Estate Investment Trust and Blackstone's acquisition of Pure Industrial Real Estate Trust—represented 45% of the quarter's investment volume, says CBRE Canada.

Significant single-asset sales in the quarter included Hines and Oaktree Capital Management's $107-million purchase of Calgary's First Tower office building, and Tigra Vista Inc.'s $256-million acquisition of Toronto's Parkway Place.

Peter Senst, president of Canadian Capital Markets at CBRE Canada, says in the release that the quarter's record-breaking investment volume isn't surprising, given that the average deal size in Q2 was up 67% year over year to $9.4 million, "which is reflective of the size and significance of the investors in real estate today."

Assets of quality and income duration draw robust demand, he adds.

"If there is a downturn, investors want assets they can believe in, where the income profile is predictable in the longer term," he says in the release.

Toronto and Vancouver remain the primary locations for CRE investment, with the former accounting for more than one-third of all transactions in Q2 with $5.7 billion—a quarterly record in amount and volume—and Vancouver accounting for more than $3.2 billion in transactions.

"Toronto and Vancouver together have maintained the two tightest downtown office vacancies for four consecutive quarters and the two lowest industrial availability rates for six consecutive quarters in North America," says Senst in the release.

Calgary, Montreal and Edmonton were next with $2.5 billion, $1.7 billion and $1.5 billion in transactions, respectively.

By property type, industrial sales volumes outperformed all asset classes in Q2, due in large part to Blackstone's acquisition of PIRET. Industrial investment also had a record quarter in Q2.

For investments without M&A activity, multi-family transaction totals were comparable to industrial transactions totals.

"Investors want multi-family exposure because it is a good long-term investment strategy," says Senst in the release. "No matter the economic or political state, people are always going to need places to live, which translates to a consistent flow of income for investors."

To compare real estate investment by volume, city and property type since 2015, see CBRE Canada's website.

Have a nice and fruitful week!