Weekly Updates Issue # 727

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1. Weekly Markets Changes

[August 16, 2019]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
16,149.79 -191.55 -1.17%	2,888.68 -29.97 -1.03%	25,886.01 -401.43 -1.53%	7,895.99 -63.15 -0.79%	$0.7527 -0.37c -0.49%	$1,513.52 +16.55 +1.11%	$54.87 +0.37 +0.68%

2. $10.6B in securities flowed out of Canada in June

[August 16, 2019] Canadian investors padded their foreign securities holdings in June, whereas foreign investors dumped Canadian stocks and bonds.

Statistics Canada reports that foreign investors pulled $5.1 billion from Canadian bonds, and another $1.1 billion from domestic equities, during the month. This was somewhat offset by investors buying $2.3 billion in Canadian money market instruments.

Overall, foreign holdings of Canadian securities dropped by $4.0 billion in June, which represents the third divestment in four months.

At the same time, Canadian investors added $6.6 billion worth of foreign securities in June.

On balance, the Canadian economy recorded a net outflow of $10.6 billion due to cross-border securities flows. And, for the second quarter, net portfolio outflows totalled $17.0 billion.

For the first half of 2019, foreign investors bought $32.5 billion in Canadian securities, down from $49.4 billion for the same period in 2018.

Canadian investors added $8.4 billion in foreign securities through the first half, compared with $29.4 billion in 2018.

3. Edibles could draw 3 million new cannabis users: study

[August 16, 2019] Three million new consumers could enter the Canadian cannabis market when edibles and other products become available for sale at licensed stores, according to a study by EY and Lift & Co.

Regulations for edibles, extracts and topicals—products that weren't available for sale when cannabis was legalized last October—come into force on Oct. 17. The products could become available for sale in December, the report said, but those interested in buying them likely won't see "robust product portfolios" until the spring.

The report found that 12% of all current non-consumers of cannabis may buy new types of products when they become available. Edibles could draw 1.5 million consumers, while topicals such as creams could bring in 2.25 million people and extracts could add 750,000 consumers.

More than half (51%) of respondents who don't currently use cannabis said they would either be very or somewhat likely to try cannabis-infused beverages. The report noted that beverages will be sold only online and at licensed retail stores, rather than at bars and restaurants, which could limit sales.

Statistics Canada's National Cannabis Survey for Q2 2019, released on Thursday, found that smoking was by far the most common method of consuming cannabis (for 68% of men and 62% of women).

From mid-May to mid-June this year, about 4.9 million Canadians aged 15 and older (16%) reported using cannabis, StatsCan said, unchanged from the same period last year when cannabis hadn't yet been legalized.

4. Needless comma sinks Bell Canada retirees' pension claim

[August 15, 2019] In a case that turned on a dispute over number rounding and comma placement, an Ontario court has dismissed a class action brought against Bell Canada by the company's retired employees.

On Aug. 12, Ontario Superior Court of Justice certified a proposed class action brought on behalf of 35,000 retired Bell employees that claimed the company had miscalculated their pension cost of living increases. The suit sought $150 million in damages.

In the same judgment, the court ultimately ruled in favour of the company, saying, "For those who loved law school, it does not get any better than this."

The claim concerned how the pensioners' indexing increase was to be calculated. In 2017, the company calculated a 1% increase, whereas the plaintiff group argued it should have been 2%.

While the two sides agreed on the mechanics of the calculation, they disagreed about how to round off numbers.

For 2017, both sides agreed that the percentage increase over the previous year was 1.49371%.

The plaintiffs said that figure should have been rounded to one decimal place, or 1.5%; the company said it should have been two places, or 1.49%. The rounding mattered because the figure was then rounded to the nearest whole number, which would have been 1% using the company's approach, but 2% using the pensioners.

"That 1% difference is, of course, crucial to the 2017 payment calculation for retirees. But it will also reverberate through time, since each year's calculation is premised on an increase from the previous year," the court said.

In deciding which approach was correct, the court noted that the issue rested on the interpretation of a pension provision stating that the increase is to be determined by "the Consumer Price Index, as determined by Statistics Canada."

The question was whether Bell, as manager of the pension plan, was to determine the increase, or whether it should have applied the cost of living increase calculated as Statistics Canada does—by rounding to one decimal place.

"As both sets of counsel point out, the proper interpretation of this provision depends on the importance one ascribes to the comma after the words 'Consumer Price Index,'" the court noted, adding that interpreting the provision "raises a classic comma question."

Ultimately, the court concluded the offending comma was placed needlessly and did not imply that StatsCan's approach to rounding must be used.

"I do not know why [the provision] is phrased in the awkward way that it is. I certainly do not know why a comma had to be inserted," the court said. "It was likely punctuated that way unconsciously; I do not believe it was a legally induced comma."

As a result, the court found that the company was correct in using its own approach to rounding, and that it did not breach its duties to its pensioners. The court dismissed the class action.

5. Insolvencies continue to push higher year over year

[August 15, 2019] Insolvencies, both consumer and business, continue to grow on an annual basis.

In June, consumer insolvencies rose 4.6% year over year, said a Scotiabank report released Wednesday. Insolvencies comprise bankruptcies and proposals, the latter of which are offers to creditors to settle debts under new terms. June's increase in consumer insolvencies was driven by an acceleration in proposals, the report said.

Year over year, **proposals climbed at a growth rate of 14% in June**, marking the ninth consecutive month of double-digit expansion, the report said. **Proposals exhibited an increase in their growth rate shortly after the Bank of Canada started increasing its key interest rate in 2017, it said.** Despite that rate holding steady since last October, proposals have continued to climb.

Ontario leads the way, with a growth rate in proposals that's almost two times larger than that of Canada overall. The province's three-month moving average of year-over-year growth in proposals **is about 23%,** the report said.

In contrast to proposals, consumer bankruptcies fell. Bankruptcies decreased by 7.4% year over year in June, the largest contraction in a year, likely due to the Bank of Canada holding its key interest rate since last fall, the report said. Overall, the growth rate of consumer bankruptcies in Canada has been contracting since January 2014, it said.

Alberta is an exception. After a period of recovery from the oil crisis in 2014, Alberta's insolvency rates fell in 2017 and began accelerating again in mid-2018. (Rates in the province are now falling.)

For businesses, insolvencies reached a new level in June, in part due to a struggling manufacturing sector. The three-month moving average of year-on-year growth in business insolvencies was 11.4%—an 11-year high, the report said. The increase was driven by insolvencies in manufacturing, which comprises more than one-third of the goods-producing sector of GDP, it said.

6. Home sales up in July: CREA

[August 15, 2019] The Canadian Real Estate Association says home sales in July rose 12.6% compared with the same month last year.

The increase came as sales were up in most of the country's largest markets, including the B.C.'s Lower Mainland, Calgary, Edmonton, the Greater Toronto Area and Hamilton-Burlington, Ottawa and Montreal.

On a month-over-month basis, sales were up 3.5% compared with June.

The increase in sales came as the number of newly listed homes edged back by 0.4% in July.

The national sales-to-new listings ratio tightened to 59.8% last month from 57.6% recorded in June.
The national average price of a home sold in July was just under $499,000, up 3.9% from the same month last year.

7. What is the yield curve -- and why it matters

[August 15, 2019] The bond market is flashing a big neon caution sign.
Yields on 10-year US Treasury bonds dipped below the yield on the US 2-year bond Wednesday. It was the first time the 10-year yield was below the 2-year yield since 2007 — just before the Great Recession. Both were hovering around 1.58% as of late Wednesday afternoon.
In another worrisome sign, the yield on the 30-Year US Treasury fell to a record low Wednesday of about 2.01%.
This is significant. **When shorter-term rates are higher than longer-term bond yields, that is known as an inverted yield curve.** The 3-month US Treasury already inverted versus the 10-year this spring. Yield curve inversions have often preceded recessions and are a sign of just how nervous investors are about the immediate outlook for the economy. They are demanding higher rates for short-term loans, which is not normal.
Typically, investors expect to get paid a higher rate of return when they are lending money for a longer period of time, because the risks are higher.
"Historically speaking, the inversion of that benchmark yield curve measure means that we now must expect a recession anywhere from six-to-18 months from today," said Tom Essaye, founder of The Sevens Report, an investment research firm, in a note to clients Wednesday.
The plunge in longer-term yields like the 30-Year are also a symptom of investor anxiety. Bond yields fall in the opposite direction of prices. In other words, they tumble when investors are buying bonds.
So, investors have continued to plow into bonds even though they are being promised a miniscule rate of return — or in the case of certain bonds in other big developed markets, no return at all. Long-term yields are negative in Japan and Germany. Worries about the global economy's slowdown have stoked renewed fears of a downturn in the United States, particularly in light of the trade war with China.
The US stock market plunged Wednesday following the yield curve inversion, more than erasing all the gains in stocks from Tuesday after a truce in the trade skirmish led to a massive market rally.
President Trump said Tuesday that he was delaying tariffs on certain consumer goods — such as electronics, toys and sneakers — so that US

consumers would not be hurt by higher prices during the holiday shopping season.

That's a sign that the US consumer may be on edge — and it's clear that investors are nervous about the outlook for the US economy as well.

"The business cycle has entered its final stages and recession risks are elevated," said Joseph Brusuelas, chief economist with RSM, in a report Wednesday.

"In our estimation, there would need to be a clear signal of a permanent cessation of trade hostilities between Washington and Beijing to turn around risk and business sentiment," he added.

Although some were quick to point out that an inverted yield curve doesn't necessarily cause a downturn itself, turmoil in the bond market can wind up becoming a self-fulfilling prophecy.

"While much debate is on the curve's ongoing predictive economic power, market participants also need to remember that an inversion can also bring about a downturn in economic activity," said Joseph LaVorgna, chief economist for the Americas at Natixis.

But some dismissed the inverted yield curve fears.

"We have to be careful about not over-interpreting signals about the US economy," said Mohamed El-Erian, chief economic adviser at Allianz, on the CNN Business Markets Now show Wednesday. "This yield curve is distorted by what central banks are doing and worries about Europe."

Aaron Anderson, senior vice president of Fisher Investments, said in an interview with CNN Business that rates have been falling for some time now. So, the inversion shouldn't be a huge surprise.

He said investors also need some perspective. Overall rates are relatively low, which could eventually boost lending demand. Anderson added that the current negative market sentiment will eventually subside, and that confidence will grow. He thinks this may be more like a market correction, a brief pullback like in 2011 and 2015, and not a full-blown bear market like 2008.

8. FSRA introduces new disclosure rules for syndicated mortgages

[August 13, 2019] Ontario's new financial sector regulator, the Financial Services Regulatory Authority of Ontario (FSRA), is proposing new disclosure requirements for syndicated mortgage investments (SMIs) designed to enhance investor protection by highlighting red flags.

The FSRA is proposing to enhance the disclosure that mortgage brokers are required to provide when dealing in SMIs that may be higher risk due to an inherent conflict of interest, high loan-to-value ratio, or the inclusion of a subordination clause.

"For the first time, we will require investors and FSRA to be made aware of whether syndicated mortgage investments bear the red flags associated with a high-risk transaction," the FSRA said in a notice outlining the proposals.

"This will ensure that retail investors are more informed of the potential risks associated with the investment they are considering," it said.

Additionally, firms will be required to report these sorts of higher risk instruments to the FSRA, which will enable the FSRA to "identify when high-risk transactions are being marketed to retail investors."

At the same time, the FSRA is also introducing a new $200 fee for certain syndicated mortgages to offset the cost of the regulator's enhanced oversight efforts.

For mortgages brokered between the launch of the FSRA on June 8 and Aug. 13, firms have until Aug. 23 to pay their fee. Starting on Aug. 13, however, the fee must be paid within five days of a transaction.

The FSRA said that it will also be contacting mortgage brokerages that have sold high-risk syndicated mortgages in the past to ensure they are providing the required disclosures and paying their regulatory fees.

"Where they are not, FSRA will take appropriate action," it said.

While the FSRA is seeking to beef up investor protection in the SMI market, policymakers have also indicated that the regulation of high-risk syndicated mortgages is ultimately to be handed over to the Ontario Securities Commission (OSC).

To that end, the OSC is working with the rest of the Canadian Securities Administrators (CSA) to finalize proposed rule changes that would created a more harmonized regulatory framework for SMIs across the country. It's also working with both the FSRA and Ontario's Ministry of Finance to facilitate the oversight transfer, which is expected to take place by the end of 2019.

In the meantime, the changes being proposed by the FSRA are out for comment until Sept. 6.

9. Brookfield to acquire 57% stake in Genworth Canada

[August 13, 2019] Brookfield Business Partners has signed a deal to buy a controlling interest in Genworth MI Canada Inc. for $2.4 billion.

Under the deal, Brookfield has agreed acquire 48.9 million shares, or a roughly 57% interest, in the business from the Virginia- based parent company Genworth Financial Inc. at a price of $48.86 per share.

Genworth Canada is a private provider of mortgage default insurance for Canadian residential mortgage lenders. Shares in the company closed at $51.46 on the Toronto Stock Exchange on Monday.

"Genworth is an industry-leading business that generates strong, consistent earnings and operates in a sector with high barriers to entry," David Nowak, managing partner at Brookfield Business Partners, said in a statement.

"We look forward to partnering with management to support its ongoing success, drawing on our expertise in insurance and residential real estate."

Genworth Financial launched a strategic review of its Canadian business earlier this summer after what it said was a "lack of transparent feedback or guidance" from regulators regarding Ottawa's review of the U.S. company's pending takeover by China Oceanwide Holdings Group Co. Ltd. announced in 2016.

Genworth's discussion with Canadian regulators centred around national security matters, including data protection. Genworth and Oceanwide agreed to extend their merger agreement to Nov. 30, 2019 from a previous deadline of June 30.

"We are pleased to find such a high-calibre buyer for our interest in Genworth Canada," Tom McInerney, president and CEO of Genworth Financial, said in a statement.

"We look forward to working with Brookfield Business Partners through the sale process and required regulatory approvals and, ultimately, moving forward with our long-awaited closing of our merger with Oceanwide."

The Brookfield deal which is subject to customary approvals, including approval by Ottawa, is expected to close by the end of the year.

Brookfield Business Partners said it has no current intention to make an offer for the balance of the outstanding shares given the short time frame available to complete the deal.

However, it said that it may in the future consider the appropriateness of such an offer after discussion with Genworth Canada's shareholders and other stakeholders.

10. CPA Canada calls for action on climate change

[August 12, 2019] Accounting industry trade group the Chartered Professional Accountants of Canada (CPA Canada) is calling on the federal government to pursue sustainable finance, overhaul the tax system and beef up its anti-money laundering efforts as part of its recommendations for the next federal budget.

In a submission to the House of Commons Standing Committee on Finance, CPA Canada called on the government to accelerate the transition to a "low-carbon, climate-resilient and globally competitive" economy.

CPA Canada said it views climate change as a "key business issue" and suggested that "Canadians are looking to leaders in the public and private sector to confront climate change and the other drivers of change with solutions that protect their economic prosperity and quality of life."

The trade group said, "Failure to adequately transition to a low-carbon, climate-resilient economy — by either political or business leaders — will further erode public trust in the institutions that underpin our society. That is why climate change must be addressed by both government and business, in partnership."

In particular, the group said that the government should implement the recommendations of the Expert Panel on Sustainable Finance that are under federal jurisdiction — chiefly its call for a plan setting out Canada's long-term path to a low-emission economy.

"Not only is this long-term path necessary to ensure Canada remain committed to its climate objectives, but it is needed to instill business confidence," CPA Canada said.

"As proposed by the expert panel, Canada needs to map — and commit to — a long-term path in order to maintain forward momentum in addressing climate policy objectives and to entrench the policy certainty that business and investors require."

CPA Canada said that the government should also spearhead the collection of reliable climate data, and provide businesses and investors with analytics to help decipher the implications of that data.

"By facilitating more informed business decisions, a Canadian centre for climate information and analytics would accelerate private sector transition to a low-carbon, climate-resilient economy," it said.

The group also recommended that the government initiate a comprehensive review of the tax system, led by an independent expert panel, with a view to supporting the transition to a more sustainable economy.

"We have allowed our tax system to grow untended to the point that it is inefficient for today's economy, much less tomorrow's," it said in calling for an overarching review.

"The process should be led by an independent expert panel and guided by the principles of fairness, simplicity, efficiency and competitiveness to ensure that Canada's tax system meets the needs of the future economy," it said.

Among other things, CPA Canada’s submission also calls on the government to work with the provinces to combat money laundering and facilitate whistleblowing.

“More action to strengthen Canada’s anti-money laundering regime is required to counter this criminal conduct and to ensure our economy and society is protected for the benefit of all Canadians,” it said.

“We believe our recommendations will help the next government set a course for a sustainable future,” Gordon Beal, vice-president, research, guidance and support at CPA Canada, said in a statement.

Have a nice and fruitful week!

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