Weekly Updates Issue # 587

1. Weekly Markets Changes

[October 21, 2016]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
14,939.04 +354.1 +2.43%	2,141.16 +8.18 +0.38%	18,145.71 +7.33 +0.04%	5,257.40 +43.24 +0.83%	$0.7501 -1.10¢ -1.45%	$1,266.70 +15.00 +1.20%	$51.00 +0.68 +1.35%

2. Feds want to shift more mortgage risk to lenders

[October 21, 2016] The federal government formally launched consultations Friday to explore potential changes that would shift some of the financial risk tied to insured mortgages from the shoulders of taxpayers to lenders, such as the banks.

Under Canada's current system, lenders are able to transfer virtually all of the risk from insured mortgages to insurers, which are indirectly backstopped by taxpayers, the government said.

The Finance Department has been examining the possibility of making such a change for a couple of years and it's now seeking more input.

Finance Minister Bill Morneau announced the consultations into so-called "lender risk sharing" earlier this month as part of a package of changes related to Canada's housing market.

The consultations are designed to help Ottawa determine whether having lenders absorb a modest chunk of loan losses on insured- mortgage defaults would help shore up stability in the system.

"Lender risk sharing would aim to rebalance risk in the housing finance system," said a background document released Friday by Morneau's department.

The trade-off from such a shift in risk away from taxpayers would likely raise costs for lenders, and therefore, homebuyers _ but the government expects any impact to be “limited.”

The background document said a preliminary analysis suggests the average increase in lender costs over a five-year period could be 0.2 to 0.3 percentage points.

For several years, the International Monetary Fund has fired off warnings that Ottawa should consider scaling back its role in insuring home mortgages through the government’s Canada Mortgage and Housing Corp. The government-backed Canadian system is viewed as unique in the world.

Homebuyers with a down payment of less than 20 per cent of the sale price are required to acquire mortgage-default insurance from either CMHC or a private mortgage insurer.

Last week, CIBC CEO Victor Dodig said in an interview that he expected the talks on lender risk sharing to be “constructive.”

“I think the goal of the government is to make sure that the taxpayer is not on the hook to support financial institutions in a perceived or real way,” Dodig told The Canadian Press.

Dodig said it’s been a hallmark of the Canadian system for the regulator, the government, policy-makers and the financial services sector to work together towards ensuring stability access to credit for clients and strength in the banks.

He added that they also aim to manage the growth in asset values appropriately given the low-interest-rate environment.

For its part, the Canadian Bankers Association has shared some concerns about lender risk sharing.

In a statement earlier this month, the group said introducing the approach through a deductible on mortgage insurance would represent a “significant structural change” to the current housing finance system.

“We have concerns that it could have negative side effects on a housing finance system that has worked smoothly, simply and efficiently and served Canada’s economy well,” the association said.

“The CBA is looking forward to engaging with the government during the consultation process to explore in detail the implications of a possible move to lender risk sharing.”

3. Loonie takes a dive on Canada-EU trade deal setback

[October 21, 2016] The loonie took a dive this morning amid reports that Canada’s trade minister had walked out of talks aimed at salvaging a major agreement with the European Union.

The Canadian dollar was at 74.98 cents, down 0.65 cents from the previous close, about two hours after stock markets opened.

It had been above 75.5 cents US before the reports that Trade Minister Chrystia Freeland walked out Friday on talks aimed at convincing the holdout Belgian region of Wallonia to agree to the EU's wide-ranging free trade deal with Canada.

At the Toronto Stock Exchange, the S&P/TSX composite index was up 56.81 points at 14,904.73, with most sectors showing gains.

In New York, the Dow Jones industrial average lost 87.11 points to 18,075.24, while the S&P 500 index lost 5.43 points to 2,135.91. The Nasdaq composite rose 8.04 points to 5,249.87.

The December crude contract fell 13 cents to US$50.50 per barrel and November natural gas lost 11.5 cents to US$3.03 per mmBTU.

The December gold contract fell 50 cents to US$1,267.00 an ounce and December copper contracts fell nearly a cent to US$2.09 a pound.

4. CRA reports $240m in real estate tax fraud

[October 21, 2016] The CRA crackdown on real estate tax fraud is producing some big numbers in audit recoveries.

The CRA's website shows that, for the last year and a half, audit recoveries in B.C. and Ontario total more than $240 million. In B.C., $30.3 million (from 2,366 case files) was recovered; in Ontario, that figure jumps to $210.4 million (from 13,403 case files). The CRA applied an additional $12.5 million in penalties.

Taxes on real estate transactions in the Greater Toronto Area have been under greater scutiny for some years. In 2015, the CRA doubled its efforts in B.C. That was the same year the tax agency started a review of 500 high-dollar real estate transactions in B.C. to uncover tax issues not already identified.

On its website, the CRA lists its top areas of concerns for real estate tax compliance, including:

- questionable fund sources for buying property,
- property flipping,
- unreported GST/HST on the sale of new or renovated property, and
- unreported capital gains.

Taxpayers identified as high-risk are audited. The CRA applies penalties equal to 50% of the additional tax payable if a taxpayer knowingly makes a false statement when filing.

5. Three ways to lift Canada's growth

[October 21, 2016] The Trudeau government's team of economic advisers has presented growth-lifting recommendations; they focus on immigration, infrastructure and investment strategies.

The objective, the team says, is to double Canada's projected growth trajectory and add an eye-popping $15,000 to the annual incomes of Canadian households by 2030.

The suggestions comprise a first tranche of ideas from the group of external experts who have been enlisted by Finance Minister Bill Morneau to help Ottawa find ways to resuscitate Canada's lackluster economy.

The recommendations zero in on three items:

1. boosting infrastructure;
2. attracting more foreign investment; and
3. opening Canada's doors to a larger number of talented immigrants.

"Now is the time where we have to take very bold actions," council chair Dominic Barton, told a news conference in Ottawa. Barton is global managing director of McKinsey & Co.

"[The suggestions] may not be new—these have been talked about before—but they haven't been done. And so what we're keen to do is to jolt it," he added.

Breakdown of recommendations

The group calls on Ottawa to deliver more than $200 billion worth of infrastructure projects over the next decade using as few taxpayer dollars as possible.

To get there, the council suggests the government create an independent infrastructure bank designed to seek out private capital by offering investors steady returns through user fees from projects like toll highways, bridges and airports.

"Canada should leverage the trillions in institutional capital waiting on the sidelines and focus this investment productively," the council wrote in a report released Thursday.

The group also calls on Ottawa to create an agency with a mandate to increase foreign direct investment into Canada that it believes could triple investment and add $43 billion to the gross domestic product in only a few years.

"These actions would bring much-needed coherence to what is currently a disjointed approach to foreign investment," the report says.

The group also recommends that the federal government ramp up permanent immigration to 450,000 people a year over the next five years, with a focus on top business talent and international students.

"An increased immigrant population has positive implications for business and job creation for Canadians through entrepreneurship and innovation, international trade and if done right, can raise living standards for all Canadians," the document says.

But Immigration Minister John McCallum, who was briefed on the recommendation, has already described that kind of a spike in immigration levels as overly ambitious.

"There are many arguments for more immigrants—we have an aging population [and] labour shortages—but there are also constraints. It costs a lot of money," McCallum said Thursday. "We also have to consider the cost and the speed with which we can integrate them."

Morneau assembled the external, 14-member council earlier this year to help the government build a plan to help Canada break out of its slow-growth rut.

The finance minister said the ideas are recommendations only at this point, and that the government will decide whether elements of them will be implemented.

"I think they're all ideas that are going to be extremely helpful for us as we think through our policy options," said Morneau, who was asked why he sought outside advice. "I don't think we would have had nearly as good an understanding of the new challenges, nor as thoughtful a way of putting these ideas forward without the advice of this council."

The council's ideas come just days before Morneau is to deliver an economic and fiscal update on November 1.

The official Opposition Conservatives questioned the need for the recommendations when the government is already projecting large deficits: for 2016-17, the Liberals have predicted a budgetary shortfall of $29.4 billion, a number that some experts believe will be even deeper after Morneau tables his fall update.

Conservative finance critic Gerard Deltell said it's "useless to have good ideas if you live above your means and do not control public spending."

Deltell also referred to the Bank of Canada's recently downgraded growth projections for Canada. "A year of reckless Liberal spending has done nothing to improve our economy," he said in a statement.

Deltell added, "Instead of endless consultations, the government needs to take action to lower taxes, cut red tape and make it easier for businesses to compete."

6. Business owners aren't ready for retirement: Report

[October 20, 2016] Research shows that most Canadians aren't prepared for retirement, and a recent BMO report reveals business owners are no different.

In fact, they're considering increasing savings or selling their businesses to help reach their retirement goals.

The report's highlights include:

- Many business owners (72%) have saved less than $100,000 for retirement.
- About one third haven't considered which exit option to use to fund shortfalls in retirement savings.
- Withdrawing funds at a rate of $50,000 a year can cause a $500,000 pool of retirement savings to disappear in about 12 years.
- The amount needed for a sustainable retirement between the ages of 65 and 90 is approximately $1,100,000.

"Retirement dates can vary for business owners depending on their personal and business circumstances," says Chris Buttigieg, senior manager of wealth planning strategy at BMO Wealth Management, in a release. "By revealing the shortfalls in a business owner's retirement fund based on how much they're saving each year a financial plan will help them prepare for every circumstance."

ValidateIt Technologies conducted the survey for BMO between June 27 and July 1, polling 405 Canadian small business owners aged 25 to 64.

When it comes to exit options to fund retirement, more than one third of those surveyed said they would sell to buyers outside the family (36%).

Other exit options include transferring the business at no cost to family (15%), closing or winding down the business (12%), or selling the business to family (4%).

7. BoC opens door to rate cut

[October 19, 2016] The BoC has downgraded the country's growth outlook yet again as it released fresh projections on Wednesday that pointed to a dampened outlook for exports and real estate activity.

The central bank also held its trendsetting interest rate at its current low level of 0.5%, as widely expected.

The bank's latest monetary policy report blamed exports as a main contributor for the lower forecast, following a weaker-than-anticipated performance and somewhat gloomier prospects for the future.

CIBC economist Nick Exarhos said in a note on Wednesday that the BoC's cut to its economic outlook—with its projection for full economic capacity pushed to about mid-2018—was a warning to markets that a rate cut isn't out of the question.

“[T]he BoC is only operating with a thin margin of error when it comes to what might prompt another rate cut,” Exarhos said, noting the bank’s bearish view for exports and residential investment in the housing market. “All told, a dovish statement from the Bank of Canada that should keep odds priced for another cut despite the recent strength in Canadian indicators.”

The report also predicted growth to take a hit from an expected decline in real estate sales activity, which it said will follow the federal government’s recently announced measures intended to stabilize the housing market.

On Wednesday, the bank provided an analysis of those measures, predicting they will lower the country’s level of real GDP by 0.3% by the end of 2018.

The report also reiterated the bank’s position that it expects the changes, which seek to slightly limit borrowing and to cool hot markets, will help ease household vulnerabilities.

The bank is now projecting Canada’s real gross domestic product to expand by just 1.1% this year, down from its July projection of 1.3%. For next year, the bank is forecasting growth of 2%, down from its previous call of 2.2%.

“The outlook for exports remains subject to considerable uncertainty, which has significant implications for the economic projection,” the BoC. “The downward revision to exports, including spillovers to domestic demand and imports, lowers real GDP by 0.6 per cent by the end of 2018.”

The bank said its expectation that the economy would not return to full capacity until mid-2018 was “materially later” than the late-2017 time frame it had anticipated three months ago.

For a couple of years, the bank has been expecting a solid increase in non-commodity exports, helped along by a lower dollar, to offset the negative economic impact of low oil prices.

BoC governor Stephen Poloz has said the full adjustment should take three to five years, but the shift has been slower than expected — a process that has perplexed the bank.

“It’s our lack of understanding that causes us to say something like … there’s a level gap between where we thought the economy would be … and where it actually is,” Poloz said earlier this month.

Despite the downgrades, the bank also offered reassurances that it sees promise ahead.

Thanks to momentum in the global and U.S. economies, the bank still predicts the Canadian economy to rebound over the final half of this year from a second-quarter contraction.

The hoped-for bounce back, however, is expected to come at a slower pace, with an average real GDP growth of about 2.5% over the last two quarters of 2016.

The bank predicts Q3 growth of 3.2%, down from the July forecast of 3.5%, and fourth-quarter growth of just 1.5%, down from 2.8%.
“The bank expects solid household spending to continue to be the main contributor to growth, with additional support from government spending and exports in 2017,” said the report, which also noted that business investment is expected to provide some help.
The government’s enhanced child-benefit program, which started mailing cheques to families in the summer, is also expected to deliver a boost in the second half of 2016. In addition, Ottawa’s commitment to invest billions in infrastructure will begin having an impact moving forward, the bank said.

8. Belgian region rejects deadline to sign EU-Canada deal

[October 19, 2016] The head of Belgium’s small Wallonia region is rejecting a Friday deadline to sign up to a huge trade deal between Canada and the European Union, demanding a full renegotiation that could bring the whole transatlantic agreement down.
Wallonia President Paul Magnette said Wednesday that “we cannot sign by Friday,” when a two-day summit of EU government leaders is to end. It was set as a target day to get the last of the 28 EU nations on board.
Belgium can only back the deal if its regions, including Wallonia, approve it. Without unanimity among EU nations, the deal will collapse.
Magnette told TV network RTBF that despite progress over the past few days “it is insufficient. And you cannot say now: ‘you have three days to accept.’”
His statement further clouds the fate of the so-called Comprehensive Economic and Trade Agreement (CETA). Wallonia — a francophone southern region in Belgium — has expressed concerns the deal could erode labour, environmental and consumer regulations.
Canadian European trade envoy Pierre Pettigrew told the Montreal Board of Trade on Tuesday that he remains hopeful the agreement will be approved later this week, despite snags that have stalled a critical vote on the deal.
Pettigrew — who was dispatched to meet with Magnette last week — said Canada has done everything it could to address any concerns within the EU, and now the ball is in its court.
“We have worked very hard in the last few months to bring reassurances that we in Canada share those same progressive views,” Pettigrew said.
EU nations were scheduled to vote on the deal Tuesday, but that was delayed after Magnette raised objections, saying he needs a few more days.

Pettigrew said the vote could happen as early as Thursday, when EU leaders kick off a two-day summit.

Former prime minister Brian Mulroney, who is no stranger to trade deals given his role as one of the architects of NAFTA, appeared unfazed by the dispute.

"Every once in a while you run into a hiccup in these things," said Mulroney, who also spoke before the Montreal Board of Trade. "This is a hiccup, but I don't think it's going to derail such an important negotiation."

International Trade Minister Chrystia Freeland said Canada has made significant changes to the deal and remains "cautiously optimistic" that it will receive European approval. She met with the head of Wallonia on Wednesday.

"I am both hopeful and I also hope that Europe and Europeans can come together to make this decision, which is the right one for Canada and for Europe," she said in Ottawa.

Prime Minister Justin Trudeau is scheduled to fly to Brussels next week to sign the agreement should it be unanimously approved by the EU.

9. CMHC raises red flag over national housing concerns

[October 18, 2016] The head of the federal housing agency is raising a red flag about the state of Canada's real estate sector, saying affordability concerns have spilled over from the country's two most expensive cities to nearby markets.

In an opinion piece published Monday in *The Globe and Mail*, CMHC CEO Evan Siddall says the agency will raise its overall risk rating for the national housing market to "strong" from "moderate" for the first time when it issues its housing market assessment on Oct. 26.

"Affordability pressures hurt lower-income households the most and cause real socioeconomic consequences," Siddall wrote. "CMHC has recently observed spillover effects from Vancouver and Toronto into nearby markets. These factors […] will cause us to issue our first 'red' warning for the Canadian housing market as a whole."

Siddall said high levels of debt combined with rising house prices are often followed by contractions in the economy. "The conditions we now observe in Canada concern us," he wrote in the G&M piece.

Siddall's comments came the same day new mortgage rules introduced by Ottawa took effect. The rules require a stress test for all insured mortgage applications to ensure borrowers can still repay their loans in the event interest rates rise or their personal financial situations change.

Until now, stress tests were not required for fixed-rate mortgages longer than five years.

The federal government is making the change to try to stabilize the country's housing markets, particularly in Toronto and Vancouver where prices have soared.

Siddall said he supports the measure, even though it will cut into the purchasing power of some first-time buyers.

Have a nice and fruitful week!