Weekly Updates Issue # 623

1. Weekly Markets Changes
2. Lower growth for 5 provinces: DBRS
3. Pace of inflation slows in June
4. Five issues to consider during NAFTA negotiations
5. When Canada's rebound will lose steam
6. Home sales drop, but effect of foreign buyers' tax unclear
7. Millennials forgo travel insurance at their peril
8. Feds may have questions for OAS recipients

1. Weekly Markets Changes

[July 21, 2017]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
15,183.13 +8.32 +0.05%	2,472.54 +13.27 +0.54%	21,580.07 -57.67 -0.27%	6,387.75 +75.29 +1.19%	$0.7974 +0.69c +0.87%	$1,255.00 +28.00 +2.20%	$45.60 -1.21 -2.58%

2. Lower growth for 5 provinces: DBRS

[July 21, 2017] Five provinces are expected to see lower real GDP growth in 2017 than 2016, according to DBRS private sector consensus data.

Those provinces are B.C., Manitoba, New Brunswick, P.E.I. and Newfoundland, with Newfoundland seeing the largest dip from 1.9% in 2016 to -2% in 2017 — that compares to nominal GDP growth of 2.4% in 2017, which is still set to be the lowest out of the provinces. Statistics Canada data indicates the province had the highest unemployment rate, at 13.4%, in 2016. As a result, Newfoundland and P.E.I. are the lowest-rated provinces, at R-1 (low) for short-term debt and A (low) for long-term debt. B.C. and Alberta are the highest-rated, with both boasting R-1 (high) short-term ratings and AA (high) long-term ratings.

B.C. is one of the provinces set to lead real GDP growth in 2017 at 3% annual growth. DBRS predicts Alberta will come out on top at 3.1%, while Ontario and Quebec will trail at 2.8% and 2.3%. In terms of unemployment rates for 2016, these four provinces' rates range between 6% (B.C.) and 8.1% (Alberta).

3. Pace of inflation slows in June

[July 21, 2017] The annual pace of inflation slowed once again last month as lower gasoline and electricity prices helped offset higher costs in most other categories, Statistics Canada said Friday.

Overall, the agency’s latest inflation report found that prices were 1% higher in June compared to a year earlier.
The June number followed inflation readings of 1.3% in May and 1.6% in April.
Last month’s inflation figure matched expectations from a consensus of economists that had predicted a reading of 1%, according to Thomson Reuters.
In a research note, TD Economics says, “Two of the Bank of Canada’s three core measures edged up on the month. CPI-median accelerated to 1.6% from 1.5%, while CPI-common was up to 1.4% from 1.3%. CPI-trim was unchanged at 1.2%.”
But, the Bank of Canada did say that it expects “the weakness in the core measures to firm, and the June data suggests a break from the several month downward trend. This may provide confidence that as slack diminishes, inflation should begin moving toward the 2% target,” the bank adds.
In its commentary, RBC sends a similar message. “Modest price growth continues to contrast sharply with what increasingly would otherwise look to be an economy that is operating very close to its long-run capacity.”
It adds, “More recent comments from the Bank of Canada — including in justifying July’s interest rate hike — have argued that sub-trend price growth is more a reflection of a number of transitory factors and the lagged impact of past weakness in the economy.”
Statistics Canada said lower gasoline prices last month were a primary contributor behind inflation’s deceleration as pump prices contracted 1.4% compared to a year earlier.
Electricity prices dropped 5.3% over the same period, while other energy costs rose, including 10% growth in natural gas and a 7.8% increase in the price of fuel oil and other fuels.
Upward pressure on prices also came from a 7.1% rise in traveller accommodation, seven% for travel tours and 2.5% for restaurants.
Food prices were up 0.6% in June — the first increase after eight consecutive months of contractions, the report said.
The latest inflation numbers show that the headline rate once again slipped further away from the Bank of Canada’s target of 2%.
Canadian inflation has been dropping since February — the last monthly reading of 2%.
Some experts had pointed to weak inflation data in recent months as a reason for the central to bank to hold off on hiking its benchmark interest rate, despite signs the economy was building momentum

Earlier this month, however, the bank raised its trendsetting rate for the first time in nearly seven years.
The data also showed that two of the Bank of Canada's three measures for core inflation, which omit volatile consumer items like gas, accelerated slightly last month to 1.6 and 1.4%. The other one was unchanged at 1.2%.
The inflation-targeting bank also scrutinizes these core measures ahead of its rate decisions.
The agency also released retail trade figures Friday for May that show total sales increased 0.6%, its third straight month of growth. Total retail trade for May rose above $48.9 billion.
The expansion in retail trade was propelled in part by stronger auto sales as well as grocery and alcohol purchases, Statistics Canada said.

4. Five issues to consider during NAFTA negotiations

[July 21, 2017] U.S.-initiated negotiations to overhaul NAFTA are bound to be long and difficult.
Canadian officials maintain Mexico is the real target of President Donald Trump's determination to renegotiate what he considers to be a bad deal for America.
Nevertheless, there are a number of issues bound to spark friction between Canada and the United States. Below is a primer on five of the them.

Dispute resolution mechanism

When Canada was negotiating a bilateral free trade agreement (FTA) with the U.S. in 1988, it sought to eliminate the use of countervailing duty and anti-dumping laws, measures designed to neutralize the effect of imports deemed unfairly priced or subsidized.
Canada believed such laws were over-zealously employed by the U.S. and upheld by their courts to protect American products from competition, including from Canadian softwood lumber.
For Canada, the issue was a deal breaker. The U.S.'s refusal to consider the matter almost scuppered the deal but the two countries eventually struck a last-minute compromise to establish a temporary, binational dispute resolution mechanism, known as Chapter 19.
The FTA was superseded in 1994 by NAFTA, which made the dispute resolution process permanent.
Each of the three countries retains the right to impose countervailing duty and anti-dumping measures. But, under Chapter 19, a country may request that those penalties be reviewed by an ad hoc panel composed of members from

the two countries involved in the dispute. Once a panel review is initiated, the matter can no longer be subject to judicial review.

Studies suggest Chapter 19 has resulted in far fewer countervailing duties or anti-dumping measures being imposed against Canadian or Mexican imports than the U.S. has imposed against other countries.

Some American industries — in particular the U.S. Lumber Coalition — argue that Chapter 19 robs them of their constitutional right to a fair and impartial judicial hearing and strips the president of his power to enforce U.S. trade laws. Trump is now seeking to eliminate Chapter 19.

Canada's ambassador to the U.S., David MacNaugton, has said this country is open to improving Chapter 19 but it's "critical" that some kind of external dispute resolution mechanism remain embedded in NAFTA.

Dairy products

The supply management system that limits the amount of dairy that can be imported into Canada before sky-high tariffs kick in is a long-standing trade irritant, but the bigger dairy-related issue expected to come up under NAFTA involves something much newer: milk protein ingredients known as diafiltered milk, or ultra-filtered milk, which are used to make cheese, yogurt and other products.

Since these newly invented products are not subject to tariffs, U.S. dairy producers began exporting them at a low cost to Canadian processors, a loophole that dairy farmers here argued was costing them some $200 million in lost revenue per year.

That changed when the Canadian dairy industry reached a deal to begin selling milk ingredients at a discount, and Canada created a new class of milk to allow it, undercutting the U.S. efforts.

The U.S. dairy lobby has cried foul. It also caught the attention of Trump, who blamed Canada earlier this year for the fact that a small number of dairy farms in Wisconsin — the heart of the American dairy industry — were in crisis.

The Canadian dairy lobby, meanwhile, has said the pricing strategy applies only to the domestic market in Canada, is legal under international trade law and sees no evidence that dairy, which was excluded from the original NAFTA deal, should be revisited in this one.

Wine

An ongoing Canada-U.S. feud over wine found its way into the U.S. Trade Representative's news release on its NAFTA objectives, even though the issue was not specifically outlined in the accompanying list of negotiating goals.

The battle began before Trump took office. The U.S. government has argued that American wine producers are at a disadvantage because the province of British Columbia only permits the sale of B.C. wine on grocery store shelves.

Washington has launched a trade enforcement action based on its allegations that B.C. appears to have breached Canada's commitments with the World Trade Organization.

Mark Warner, a Canada-U.S. trade lawyer, said U.S. and European producers have had long-standing issues with how Canada sells wine in its stores.

The dispute found some peace a few years back, he added, but re-emerged as B.C. and Ontario started testing the limits of the agreement.

It's tricky for the federal government because alcohol falls into a provincial jurisdiction, he said.

"It would be inconceivable to think that the wine issue would not factor in — indirectly or directly — into NAFTA negotiations," Warner said.

Trade expert Laura Dawson isn't convinced wine will be a major sticking point during NAFTA talks, unless a very strong coalition emerges out of the U.S. or Mexican wine industries.

"There are so many issues competing for floor space in the NAFTA," said Dawson, director of the Wilson Center's Canada Institute in Washington.

Investment

The USTR's negotiating objectives called for rules to reduce or eliminate barriers to U.S. investment in all sectors, although it did not specify which industries the Americans might try to put on the table.

Trade lawyer Lawrence Herman said it could mean the U.S. will seek to pry open investment access to exempt sectors that some Canadians might consider "sacrosanct."

"They didn't spell it out, but I can guess that they will have an interest in assaulting the Canadian exemptions for, for example, cultural industries, maybe health care, maybe public education," said Herman.

"We can expect a tough round of negotiations and the targeting by the Americans, at least initially, of some of the areas that were protected under the FTA and the NAFTA."

Dawson said as the easier-to-resolve trade barriers are dealt with in the NAFTA talks, areas, such as investment, covered by more-entrenched protections often become greater targets.

She added that if there's an area "ripe" for reform, it's probably Canada's telecommunications sector. But in return for doing so, Canada would have to show some kind of gain, she said.

"Canada can reduce any barrier that it chooses to, but there has to be a good, domestic public policy reason," Dawson said.

Duty-free cross-border shopping

The U.S. wants Canada to allow a whopping increase in the value of goods American companies can send into Canada without paying an import tax.

At the moment, Canada's limit — what's known as the de Minimis threshold — is just $20, among the lowest in the world. It was set decades ago, long before the explosion in online shopping.

The U.S. wants that limit raised to $800, matching the American threshold.

The proposal is bound to be popular with consumers. But Canadian retailers are apoplectic, maintaining such a move would be catastrophic for them.

They warn that it would mean providing a more favourable tax regime to foreign retailers than applies to homegrown retailers who actually create jobs and invest in Canada. Moreover, they argue it would encourage Canadians to do all their shopping online from American retailers and result in domestic retailers moving some or all of their operations south of the border.

5. When Canada's rebound will lose steam

[July 18, 2017] The Canadian economy improved during the first half of 2017, thanks to higher oil prices and a stronger Canadian dollar.

But that likely won't continue, says Luc de la Durantaye, head of asset allocation and currency management at CIBC Asset Management.

"We've been surprised by the strength of the Canadian economy of late but we think, going forward, it'll be difficult to maintain," he explains. "We have to think the energy rebound is almost over and, with oil prices remaining around $45 to $50 [a barrel], Canada will not get as much momentum in the second half of the year." (Just think of oil's dip in June and how that has affected commodity indexes.)

Another challenge for Canada is the amount of debt held by Canadian consumers, says de la Durantaye, who manages the Renaissance Optimal Inflation Opportunities Portfolio. This is especially concerning following the Bank of Canada's key rate increase on July 12 to 0.75%, and the subsequent hike in mortgage rates by Canada's big banks.

What's more, says de la Durantaye, "We're not as optimistic in the U.S. economy, so exports to the U.S. are not necessarily expected to be strong in the second half of the year. We're a bit more prudent in terms of momentum to the Canadian economy and monetary policy in the second half [of 2017]."

Other factors influencing his less optimistic outlook are "the recent backup in Canadian bond yields combined with the rapid appreciation of the Canadian dollar. That, essentially, is an important component of financial conditions in Canada; they've tightened quite rapidly in a short period of time," says de la Durantaye.

He expects the BoC won't like that trend, meaning it could moderate its enthusiasm about growth prospects for Canada as 2018 approaches.

Otherwise, yields will continue to backup and the Canadian dollar will continue to strengthen, "which will by default nip the recovery in the bud. We expect a bit more prudence and less momentum."

Any opportunities?

De la Durantaye isn't giving up, despite his modest outlook.

He says, "We think Canadian bonds could be a decent investment in the short term. We're starting to see better value in Canadian bonds because they've backed up so much and because we don't think the economic recovery will be as strong."

However, he recommends against investing in Canadian currency. "We don't think the Canadian dollar could continue the speed of its appreciation that we've seen in the early months of the summer, and so we would be a bit more careful about [it]," de la Durantaye explains.

Instead, he's looking at opportunities overseas. "Europe looks brighter and a number of emerging markets also look brighter than the Canadian economy at the moment."

6. Home sales drop, but effect of foreign buyers' tax unclear

[July 17, 2017] If your client is looking to buy a home, the fear of a bidding war may be a thing of the past, thanks to Canada's cooling real estate market.

Home sales activity in June posted its largest monthly drop in seven years, driven by a plunge in the Greater Toronto market, the Canadian Real Estate Association (CREA) said Monday.

Transactions last month were down 6.7% compared with May on a national basis, the third consecutive monthly decline, with the Greater Toronto Area (GTA) registering a 15.1% drop.

"Changes to Ontario housing policy made in late April have clearly prompted many homebuyers in the Greater Golden Horseshoe region to take a step back and assess how the housing market absorbs the changes," CREA chief economist Gregory Klump said in a statement.

"The recent increase in interest rates could reinforce a lack of urgency to purchase or, alternatively, move some buyers off the sidelines before their pre-approved mortgage rate expires. In the meantime, some move-up buyers who previously purchased a home before first selling may become more motivated to reduce their asking price rather than carry two mortgages."

The number of sales fell from the previous month in 70% of all local markets measured by CREA, including the Lower Mainland in B.C., Montreal and Quebec City.

Compared with a year ago, national home sales in June were down 11.4%.

Effect of foreign buyers' tax

The Ontario government moved earlier this year to cool the Toronto real estate market, bringing in more than a dozen measures including a 15% tax on foreign buyers. Since then, sales in Canada's largest city have slowed.

But recent data suggest that foreign buyers aren't the driving force behind runaway home prices in Ontario's Greater Golden Horseshoe, though it's still too early to settle the matter, says RBC senior economist Robert Hogue in an industry note.

A new dataset from the Ontario government shows that foreign buyers accounted for 6.2% of all transactions in the GTA from April 24 to May 26, 2017.

During the same period, in two areas — York and the city of Toronto — foreign buyers were responsible for a greater percentage of home sales: 9.1% and 7.2%, respectively. But those areas haven't appreciated at faster rates than elsewhere in the Golden Horseshoe region.

"The contrary has occurred, in fact," says Hogue. "Price increases have had a tendency to be stronger in areas where the intensity of foreign buyer involvement was lower. Furthermore, we find no evidence that York region and the City of Toronto led price gains. Rather, the price surge was remarkably synchronized."

Referring to CREA data, Zoocasa notes in an email to Advisor.ca that the notable hot city for the month is Hamilton-Burlington, where prices increased 9.9% year over year. In that area — Halton region — non-residents accounted for 3.7% of home transactions from April 24 to May 26.

Mortgage rates rise, prices moderate

Separately, mortgage interest rates have started to rise in recent days. That came after the Bank of Canada raised its key interest rate last week, a move that prompted the big banks to increase their prime rates. Rates for new fixed-rate mortgages ticked up in anticipation of the central bank rate hike.

The national average price for a home sold in June was $504,458, up 0.4% from a year ago. Excluding Greater Vancouver and Greater Toronto, the national average price was $394,660.

The aggregate composite Multiple Listing Service home price index for June was up 15.8% compared with a year ago.

However, June saw the first month-over-month decline in Toronto's benchmark price in almost three years (-0.7%).

And on a year-over-year basis, the rate of increase in the Toronto benchmark moderated for the second-straight month to 25.3% from a high of 31.3% in April.

"Average home prices declined month over month in the majority of [Ontario] markets in June, including Hamilton, Kitchener-Waterloo and Guelph," says Hogue, in a housing market update. "We expect prices to ease further in the near-term in southern Ontario."
Overall, Hogue forecasts a soft landing for the housing market, driven by policy changes, poor affordability in some markets and rising rates.
"We project home resales in Canada to ease by 3.7% to 515,300 units this year from a record 535,300 units in 2016, and price increases to moderate from 9.6% in 2016 to 7.8% in 2017," he says.

7. Millennials forgo travel insurance at their peril

[July 17, 2017] About 43% of Canadian travellers who report not acquiring travel insurance when they leave the country are younger Canadians aged 18 to 34, reveals data from Allianz Global Assistance.
For those millennials surveyed who weren't otherwise protected, almost 16% felt travel insurance was unnecessary, while about 15% thought insurance was too expensive and another 15% felt their trip was too short to warrant insurance.
Internal claims data reviewed by Allianz show that, from 2014 to 2016, people under the age of 30 made nearly 32% of all claims submitted — the highest demographic bracket — while buying only 21% of all Allianz policies.
Of the Canadians surveyed, about 79% had travelled outside Canada in the past five years (2013 to 2017).
"Millennials and other young Canadians make up the majority of […] travellers looking for adventure and more authentic experiences," says Dan Keon, senior director of market management at Allianz Global Assistance, in a release. "But the off-the-beaten-path travel experiences can also result in increased risks regardless of age."
Of those who had recently travelled outside Canada, 81.5% report being covered by a travel insurance policy in addition to their provincial health care plan. Canadians heading overseas were somewhat more likely to have insurance coverage.
About the survey: Data was collected from 2,159 Canadians and weighted to the population by age, gender and province of residence.

8. Feds may have questions for OAS recipients

[July 17, 2017] The federal government aims to eliminate fraud or mistakes from Old Age Security through a massive review of payments and recipients.

In May, the government started testing a new, simplified application form for Old Age Security benefits to prevent misunderstandings about eligibility — specifically questions about residency, where concerns have been raised about potential fraud.

The findings from the review and the application pilot project will feed into a larger strategy to modernize Old Age Security and improve payment accuracy.

The department overseeing the program, Employment and Social Development Canada, says payments are accurate almost 99% of the time. But mistakes even 1% of the time can mean hundreds of millions of dollars in mistaken payments.

Old Age Security benefits are expected to cost the federal treasury about $51.1 billion this fiscal year.

Have a nice and fruitful week!