Weekly Updates Issue # 644

1. Weekly Markets Changes
2. Why millennials won’t be main boon for Canadian housing
3. Auto sector dragged on October manufacturing sales
4. After Fed hike, ECB and BoE hold rates
5. BoC warns of risks for people with mortgages
6. Canadians’ debt-to-income ratio rises in Q3
7. Mortgage stress test to temper home prices: report
8. Job vacancies reach new heights: CFIB
9. Childcare costs rising faster than inflation: report
10. Bubble speculation as bitcoin’s rise continues

1. Weekly Markets Changes

[December 15, 2017]

S&P TSX	S&P 500	Dow Jones	NASDAQ	CAD/USD	Gold	WTI Crude
16,041.98 -54.09 -0.34%	2,675.81 +24.31 +0.92%	24,651.74 +322.58 +1.33%	6,840.08 +96.50 +1.41%	$0.7792 +0.16c +0.21%	$1,256.44 -7.95 -0.64%	$57.30 -0.06 -0.01%

2. Why millennials won’t be main boon for Canadian housing

[December 15, 2017] In the medium to long term, Canada’s housing boom will be boosted by immigration more than by millennials looking to buy for the first time, says Adrienne Warren, senior economist at Scotiabank, in a new report on real estate trends.

“As millennials move past their prime household formation years beyond the middle of the next decade, immigration is emerging as a key driver […],” she says. As more new Canadians buy homes, the country will see “growing rental and homeownership demand, elevated new construction, and ongoing urban population densification,” she adds.

Warren highlights in the report that the number of new immigrants to Canada reached nearly 300,000 last year, “up from an average of 260,000 over the prior decade, and registering the highest level in almost a century.”

That number is set to increase, given the federal government’s Advisory Council on Economic Growth “last year recommended boosting Canada’s annual immigration target to 450,000 by 2021.”

Rental market demand is also set to rise over the medium to long term. Says Warren in the report: “Pressure on already drum-tight rental markets in many Canadian cities, primarily in British Columbia and Ontario, will continue.”

The solution is more rental supply, she adds, considering "the average vacancy rate for purpose-built rentals has dropped to 1% in Toronto and 0.9% in Vancouver," which is "well below the 3% level typically considered balanced."

The main driver of rental demand, says Warren, is millennials who are moving out of their parents' homes.

Millennials and homeownership

It shouldn't come as a surprise that some millennials are choosing renting over owning. Even the cost of renting is tough to deal with, given half of renters captured in the 2016 census spent more than 30% of their average monthly income on housing.

Plus, millennials are currently worried about challenges such as paying down debt, and finding good jobs and ways to save for retirement. Nonetheless, home ownership seems to be on their radar: a March 2017 HSBC study found more than 80% of Canadian millennial respondents planned to buy a home in the next five years, while 34% had already bought.

The challenge, however, is more than two-thirds (70%) of non-homeowners didn't have enough for a down payment. And, while 53% had only an approximate budget, 27% had no budget.

Many millennials who had bought a home in the last two years said they had overspent (42%).

3. Auto sector dragged on October manufacturing sales

[December 15, 2017] Statistics Canada says manufacturing sales in October declined 0.4% month-over-month, following two months of increases.

The Ottawa-based agency says manufacturing sales totalled $53.5 billion, down from a revised $53.7 billion in September.

Sales fell in eight of the 21 industries tracked by Statistics Canada, with most of the decline attributed to the transportation equipment sector that includes motor vehicles.

Sales in the motor vehicle industry fell 6.7% to $4.6 billion, reflecting lower volumes due to shutdowns at some assembly plants. Sales volumes in the motor vehicle industry fell 7.6%.

Ontario's manufacturing sales were down 2.2% to $24 billion, the biggest drop of any province, mainly due to declines in the motor vehicle and food industries, for example.

Four of 10 provinces showed advances, led by a 4.2% increase to $6 billion in Alberta and a 2.1% increase to $4.3 billion in British Columbia.

Derek Holt, vice-president and head of Capital Markets Economics at Scotiabank, said in a report that the numbers could be leading to flat GDP growth for the month.
"Little to no monthly GDP growth is being tracked in October pending next week's retail and wholesale reports," he wrote. "A 1.5% decline in shipment volumes, flat hours worked in October and a 1.8% rise in housing starts are among the ingredients to a flat GDP estimate thus far."

4. After Fed hike, ECB and BoE hold rates

[December 14, 2017] With the Eurozone economy showing strength, the European Central Bank left its interest rates and stimulus measures unchanged Thursday. It's looking ahead to the delicate matter of ending its bond-purchase program next year.
The Bank of England also kept its main interest rate unchanged at 0.50% on Thursday, a month after increasing borrowing costs for the first time in a decade to contain a rise in inflation stoked by last year's Brexit vote.
Together, Thursday's decisions show how the Eurozone and Britain are moving more slowly than the U.S. Federal Reserve as the world's leading central banks start to gingerly withdraw the massive stimulus measures they deployed against the 2007-2009 financial crisis and the subsequent Great Recession.
The Fed on Wednesday raised its benchmark federal funds rate by a quarter-point to 1.25-1.50% and signalled that three more hikes could come next year. The Fed is also withdrawing some of the stimulus from its years of bond purchases by letting some of its holdings run down.
Investors are now waiting for ECB President Mario Draghi's news conference for clues about when and how the bond stimulus might end. The bank decided in October to reduce the purchases to 30 billion euros ($35 billion) a month from 60 billion euros, and to extend them at least until September–or longer if necessary.
Growth has been robust in the U.S. and stronger than expected in Europe, but the stimulus withdrawal has moved slowly. That's because inflation in Europe and the U.S. remains lower than many would like and the central bankers are leery of startling financial markets that have been boosted for years by the introduction of newly printed money into the financial system through bond purchases, known as quantitative easing.
The ECB has tried to reassure markets that its stimulus efforts will be withdrawn slowly so as not to disrupt the economic recovery that saw

the economy in the 19 countries that use the euro expand 2.6% in the third quarter from the quarter before.
The bank's 25-member governing council left its key benchmark for lending to banks unchanged at zero. The rate on deposits it takes from commercial banks remained at minus 0.4%. That negative rate is a penalty imposed to push banks to lend the money, not let it pile up at the ECB.
The ECB will give an important clue about the future course of stimulus policy when it reveals its inflation estimate for 2020. That figure will suggest whether the bank expects to finally achieve its inflation goal of close to but below 2% annual inflation, the rate considered best for the economy. A projection of 1.8% would strengthen the likelihood that the stimulus would end in September, while anything less would support the view that the bank might have to continue it through the end of the year.
The bank is trying to reassure markets that the stimulus will only be withdrawn slowly. Its statements include a promise that interest rates will not rise until "well past" the end of the bond purchases. That would mean that the extraordinarily low benchmarks would remain in place until well into 2019.
Rock-bottom rates and bond purchases have meant unusually low market interest rates for government and corporate borrowers. A 10-year German government bond yields around 0.33 %, compared with 2.38% for the equivalent U.S. Treasurys. That has made it easier for companies to borrow affordably, and taken pressure off government finances.
On the other side of the ledger, the low rate environment has meant paltry or nonexistent returns for savers on conservative holdings such as bank deposits. Low rates have also squeezed bank profits by compressing the difference between their lending and borrowing rates.
The zero rate interest rate policy has also raised concerns that it may be driving unsustainable increases, or bubbles, in some asset classes, as investors take more risks to hunt for yield. So far, stock markets have shrugged off the stimulus withdrawal; major stock indexes such as Germanys' DAX and the U.S. Dow and Standard & Poor's 500 have hit record highs this year.
The ECB warned Nov. 29 that a key hazard for the economy in the months ahead remains the "risk of a rapid repricing in global markets."

BoE holds amid Brexit uncertainty

The Bank of England's decision was widely anticipated even though official figures this week showed annual inflation rising further above the bank's 2% target, to 3.1%. All nine members of the Monetary Policy Committee voted to keep rates unchanged.
Last month, while raising interest rates, the Bank of England published forecasts that showed inflation is likely to ease back next year, but not to the

target, as the inflation-boosting impact of the pound's fall following the vote to leave the European Union fades. The lower pound raised the price of imported goods like food and energy.

Policymakers have also voiced concerns over raising rates too much given the economic uncertainty surrounding Brexit, due to take place in March 2019. The Brexit vote has elevated uncertainty in the British economy and that's seen growth falter over the past year.

Brexit, according to the rate-setters in the minutes to the meeting, remains the "most significant influence on, and source of uncertainty about, the economic outlook."

The decision comes as British Prime Minister heads to Brussels for a summit of EU leaders where she hopes to win approval for the Brexit talks to move onto trade matters following an agreement last week on citizens' rights, the Irish border and Britain's divorce payment.

Despite that agreement between the British government and the EU representatives, there's still a welter of uncertainty related to Brexit, not least what it entails when Britain formally leaves the EU in March 2019. A parliamentary defeat for May on Wednesday over Parliament's role in authorizing the final deal is perceived to have chipped away at the boon offered by last week's deal.

"In such exceptional circumstances, the MPC's remit specifies that the Committee must balance any trade-off between the speed at which it intends to return inflation sustainably to the target and the support that monetary policy provides to jobs and activity," the rate-setting panel said, according to the minutes.

Overall, the Committee said it remained of the view that were the economy to follow the path anticipated in November's projections, then "further modest increases" in interest rates "would be warranted over the next few years, in order to return inflation sustainably to the target."

However, the committee stressed that any future increases are expected to be "gradual" and "limited."

The next meeting of the MPC is in February.

At the moment, the prevailing view is that there won't be any more rate increases in the months ahead given the Brexit uncertainty.

"Policymakers will naturally be keen to raise rates as fast as the economy allows, if only to provide some firepower when the next economic downturn arrives," said Ben Brettell, senior economist at stockbrokers Hargreaves Lansdown.

“But with domestic inflationary pressures thin on the ground and Brexit casting its customary shadow, there’s no real imperative to move for some time.”

5. BoC warns of risks for people with mortgages

[December 14, 2017] Bank of Canada governor Stephen Poloz is having trouble sleeping at night. But it’s not visions of sugarplums that are dancing in his head; it’s threats to Canada’s financial system.

In a speech Thursday, Poloz itemized these prime concerns:

- high house prices and household debt,
- cyber threats,
- cryptocurrencies and
- the labour market.

Housing concerns contain a message for clients

Though vulnerabilities in housing and household debt have shown signs of easing, “these vulnerabilities are elevated, and are likely to remain so for a long time,” said Poloz, according to prepared remarks of his address to the Canadian Club of Toronto.

Beyond the level of debt, he said its composition and distribution is concerning. “More than 80% of household debt is composed of mortgages and home equity lines of credit (HELOCs),” he said. “Increasingly, mortgages are being combined with HELOCs, to the point where about 40% of all housing-backed loans are blended with a HELOC component.”

Though HELOCs can be a convenient tool, the governor noted their risks, such as when clients make interest payments only, or use HELOCs to speculate (i.e., fund a down payment on a second house to flip the property).

“Given the potential for volatility in house prices and for higher interest rates, such activity may be adding to the overall vulnerability of the [financial] system,” he said.

He noted that macroprundential measures introduced last year aimed at high-ratio mortgages have resulted in “a sharp drop” in the number of highly indebted Canadians obtaining such mortgages. (He defined “highly indebted” as those Canadians with a debt-to-income ratio above 450%).

Guidelines for low-ratio mortgages that come into effect in 2018 should likewise limit the number of low-ratio mortgages going to highly indebted households, he said.

But the measures aren’t meant to control house prices. “Ultimately, the laws of supply and demand will determine the direction of house prices,” he said.

And in 2018, if clients are tempted to visit an unregulated lender for a mortgage—one not bound by the new lending guidelines—Poloz had this advice: "Testing yourself to make sure you could handle your mortgage payments if interest rates were higher at renewal is a very good idea, whether it is a rule or not."

Safeguarding against cyber threats

Poloz also noted that connectivity within the financial system creates vulnerability: "A problem in one institution may spread to others and be amplified. […] We need to be prepared to recover our systems should a cyber attack succeed."

He said the central bank is working with financial institutions and payment systems to ensure "robust joint recovery plans" are in place.

Where cyptocurrency is headed

The governor said cryptocurrencies aren't reliable stores of value, nor can they be easily spent. "What their true value is may be anyone's guess—perhaps the most one can say is that buying these things means buying risk, which makes it closer to gambling than investing."

Their elusive nature doesn't provide shelter from the taxman, however. Poloz reminded the audience that CRA considers cryptocurrencies as securities. "That means, if you buy and sell them at a profit, you have income that needs to be reported for tax purposes," he said.

He also said the central bank, like all central banks, is exploring the possibility of issuing its own digital currency, as demand for digital cash grows.

Remarks on monetary policy focus on labour market

Poloz also commented on the central bank's monetary policy, saying that, with the economy running at close to full tilt, a mechanical approach to setting interest rates would suggest higher borrowing rates should already be in place.

But he said the central bank is scrutinizing some unusual factors at play—including encouraging signs that companies are starting to expand their capacity by investing in equipment and by hiring more people.

Wages have been growing, and the workforce has seen a sudden jump in participation by young people, he said.

Poloz acknowledged the bank's current benchmark rate of 1% remains quite stimulative. However, there's still more room for the labour market to grow before it starts pushing inflation higher, he said.

The central bank introduced two rate hikes this year due to the strong economy: once in July and again in September. But since then, Poloz has kept the rate on hold, including at last week's announcement when he pointed to uncertainty over trade and a greater-than-expected weakness in exports.

Still, he continues to warn that higher interest rates will likely be required over time, even though the bank will proceed with caution by focusing on incoming data.

6. Canadians' debt-to-income ratio rises in Q3

[December 14, 2017] The amount Canadians owe relative to their incomes hit another new high in the third quarter.

Statistics Canada says household credit market debt as a proportion of household disposable income increased to 171.1%, up from 170.1% in the second quarter.

That means there was $1.71 in credit market debt, which includes consumer credit and mortgage and non-mortgage loans, for every dollar of household disposable income.

The household debt service ratio, measured as total obligated payments of principal and interest as a proportion of household disposable income, was relatively flat at 13.9%, while the interest-only debt service ratio was 6.3%, down from 6.4% in the previous quarter.

Meanwhile, the total net worth of the household sector edged down 0.1% to $10.61 trillion in the third quarter.

The move lower was due to a drop in home values as housing resale prices weakened.

However, the value of household financial assets edged up 0.1%, which means individual net worth is increasing.

7. Mortgage stress test to temper home prices: report

[December 13, 2017] Clients looking for new homes can expect price increases in 2018, but those increases are expected to be tempered.

New, stricter mortgage rules are expected to slow the housing market next year, but prices are still expected to rise about 5%, forecasts a report by Royal LePage.

In its market survey forecast, the real estate firm says its house price composite, which measures prices in 53 Canadian cities, is expected to increase 4.9% next year to $661,919.

A new stress test for homebuyers who don't need mortgage insurance will be required starting next year.

The new rules are expected to reduce the maximum amount buyers will be able to borrow, for those with a down payment of 20% or more.

The Royal LePage report suggests home prices in the Greater Toronto Area are expected to increase 6.8% in 2018, while the Greater Montreal Area is expected to see an increase of 5.5%.
Greater Vancouver is expected to increase 5.2% in 2018.
Royal LePage's forecasted home prices for various cities are shown below.

Region	2017 aggregate home price (estimate)	2018 aggregate home price (forecast)	Year-over-year (%)
Canadian House Price Composite (53 Cities)	$631,000	$661,919	4.9%
Greater Toronto Area	$844,000	$901,392	6.8%
Greater Montreal Area	$387,000	$408,285	5.5%
Greater Vancouver	$1,287,000	$1,353,924	5.2%
Ottawa	$444,000	$458,208	3.2%
Calgary	$483,000	$494,109	2.3%
Edmonton	$388,000	$382,180	-1.5%
Winnipeg	$303,000	$315,120	4.0%
Halifax	$319,000	$326,975	2.5%
Regina	$327,000	$329,289	0.7%

8. Job vacancies reach new heights: CFIB

[December 12, 2017] The combination of a growing economy and a dearth of skilled workers has created a labour shortage of approximately 361,700 jobs, notes a CFIB report, adding that's the highest number of unfilled private sector jobs ever recorded in Canada.
The corresponding vacancy rate—the proportion of unfilled jobs relative to all jobs available in the private sector—jumped up to 2.8%, its highest point since before the 2008 recession, says CFIB.
"Labour shortages are again becoming a major hindrance to businesses across the country, especially small firms," says Ted Mallett, chief economist at CFIB, in a release. "We need government to take action, to find solutions for chronic shortages that inhibit a small business's ability to take on new contracts, expand and innovate."

Regional vacancy rates

Businesses in Canada's three most populous provinces have the most difficult time finding suitable employees. B.C. has the highest vacancy rate (3.4%), followed by Quebec (3.1%) and Ontario (3%). All three provinces experienced rising vacancy rates in Q3 2017, as did Alberta and Saskatchewan.

	Vacancy rate	Unfilled jobs
British Columbia	3.4%	60,000
Quebec	3.1%	85,000
Ontario	3.0%	149,600
New Brunswick	2.5%	5,700
Saskatchewan	2.4%	8,200
Alberta	2.2%	33,900
Manitoba	2.1%	9,400
Nova Scotia	2.1%	6,100
Newfoundland and Labrador	1.9%	2,800
Prince Edward Island	1.9%	900

Industry groupings

Among broad industry groupings, eight of 12 sectors experienced rising vacancy rates in Q3. In terms of unfilled positions, the retail (50,000 jobs), hospitality (45,900 jobs) and construction (38,000 jobs) industries are experiencing the biggest labour shortages, notes CFIB.

9. Childcare costs rising faster than inflation: report

[December 12, 2017] A new report shows childcare costs are rising faster than inflation, straining pocketbooks and raising questions about whether billions in new federal spending will make daycare more affordable for those who want it.

Toronto remains the most expensive city for childcare, where median daycare costs families about $21,096 a year.

The cheapest spaces are in Quebec, where provincially regulated and subsidized daycare has a median cost of $183 a month, or $2,196 a year.

The annual report on childcare fees, released today from the Canadian Centre for Policy Alternatives, also finds for the first time that childcare costs in some rural parts of the country are not all that different from the high prices facing parents in many large cities.

“You can categorize your issues in childcare—there are not enough spaces, the quality is very variable—but affordability is a pervasive issue across the country,” says Martha Friendly, co-author of the study and executive director of the Toronto-based Childcare Resource and Research Unit. “It’s not getting better and we still have yet to see if any of the [federal] interventions are going to be enough to really address the issue.”

Feds promise help

The Liberals have vowed to make childcare affordable for those who need it and can’t afford it.

Federal coffers will dole out $7.5 billion over 11 years, beginning with $500 million this year and increasing to $870 million annually by 2026 in order to fund services in provinces and territories.

The money could potentially create 40,000 subsidized spaces by early 2020 at a cost of $1.3 billion. The government knows not all the money will be spent on subsidizing spaces, but could be used for professional development for childcare workers.

The government is also working on a separate childcare plan with Indigenous groups that would reflect the needs of First Nations, Inuit and Metis.

In some First Nations reserves in Ontario, the report found, parents didn’t pay anything for childcare, suggesting that direct operational funding from the government makes fees much more affordable.

David Macdonald, a senior economist at the policy centre who co-authored the study with Friendly, says it isn’t clear to him that the new federal spending will make a big dent in daycare costs. Making childcare more affordable requires governments to set fees and provide operating grants to defray costs, he says.

“That may not be what governments think is the case, but the data clearly shows a direct path between setting fees and affordability,” Macdonald says.

The House of Commons finance committee hints at the same issue in its budget wish list released last week. Among the recommendations for spending items in the 2018 budget was a request to provide the money needed to create an early learning and childcare system.

None of the money can flow without funding agreements with provinces. So far, three provinces and one territory have three-year spending deals in place.

A spokesman for Social Development Minister Jean-Yves Duclos says the Liberals may allow some provinces to carry over spending beyond 2020, but restrictions are tight to prod provinces into delivering services as soon as possible.

“We have an expectation that provinces and territories will deliver on the commitments they made,” says spokesman Mathieu Filion. “Delivering on the plans is how we’ll make child care better in Canada.”

10. Bubble speculation as bitcoin’s rise continues

[December 11, 2017] Is bitcoin in a bubble?

The price of bitcoin has been soaring this year, and last week alone it jumped from $11,000 to well over $17,000, according to Coindesk. It started the year below $1,000. (All prices are in U.S. dollars.)

That rocketing level of appreciation smells a lot like an irrational investor mania to many economists and financial pros, the kind that sent prices for unprofitable startup internet companies soaring in the dot-com boom. Those prices eventually came crashing down.

“We saw this in the 1990s,” says Barry Ritholtz, chairman and chief investment officer of Ritholtz Wealth Management. “Any of those things sound familiar? ‘This is unique; this will change everything?”’

Like many others in finance, Ritholtz expects the bitcoin bubble to pop. The only question is when. “Some people think it’s early days, some people think it’s late,” Ritholtz said. “We’ll find out in the not-too-distant-future who is right.”

Robert Shiller and Joseph Stiglitz, two Nobel-prize-winning economists who’ve seen their share of speculative manias, recently have called bitcoin a bubble. Stiglitz went so far as to tell Bloomberg TV that bitcoin should be “outlawed.”

Bitcoin was created in hopes it would become a new kind of currency that people could use outside of the traditional banking system, without backing from any country or central bank. It was also supposed to operate outside of government oversight, which has raised concerns that it will be a haven for criminals.

Unlike traditional currencies, bitcoin doesn’t have a country backing it, a central bank, interest rates, or a long history of exchange rates against other currencies, making it extremely difficult to place a value on. Its value is tied only to what people believe it’s worth at any given time.

Despite the growing interest, bitcoin still is not widely accepted in stores to buy merchandise, and you can’t deposit it at a bank. One of the problems with using it as a currency is that its value keeps bouncing around, sometimes very suddenly.

“We have seen bitcoin more as a speculative investment rather than an equivalent to cash,” says J. Craig Shearman, spokesman for the National

Retail Federation, the world's largest trade association of retailers. "Even if it were a foreign currency, you need to dependably know what the exchange rate is, and bitcoin doesn't meet any of those tests."

Backers of bitcoin say it's about time for a new kind of currency that can be exchanged in private and secure ways. Its promoters include internet entrepreneurs Cameron and Tyler Winklevoss.

This week mainstream financial markets are for the first time allowing investors to make future bets on the direction of bitcoin, but bitcoins themselves will continued to be traded only on private exchanges, which are mostly out of reach of regulators.

Mark Fratella, a teacher who lives in Elmhurst, Illinois, bought some bitcoin "for the novelty of it" back when it was worth $700 or $800.

Fratella is holding onto his bitcoin, and buying a little more from time to time. He's also buying other cryptocurrencies, such as Ethereum and Litecoin. He's heard the talk of a bitcoin bubble.

"But I have also seen a few analysts talk about how, in the grand scheme of things, there are a relatively low amount of people into bitcoin and there is a huge potential for growth," he said. With the futures trade starting, Fratella thinks people who have been leery of its decentralized, deregulated nature will start buying into it too.

The futures also give investors the opportunity to "short" bitcoin—that is bet that its price will go down—which presently is very difficult to near impossible to do.

While the value of bitcoin itself may be inflated, even some of its biggest critics say that the technology that's behind bitcoin has promise. That technology is called blockchain. It's a kind of digital ledger that securely records transactions and prevents the same bitcoin from being spent twice.

Jamie Dimon, the head of JPMorgan Chase, has called bitcoin "a fraud" that will eventually "blow up." Dimon also said he thought the blockchain technology was "good" and could be used to make transactions faster and easier.

For now, people keep buying bitcoin, even with all the talk of a bubble. To Ritholtz, the enthusiasm is a combination of the novelty of bitcoin, the built-in scarcity of it—only 21 million of them will ever be created—and the psychology of people being attracted to assets whose prices appear to keep going up.

"One of the first rules of investing is, only invest in things you understand," Ritholtz said. "If you want to speculate in a cryptocurrency and you don't understand it, you might get lucky for a while but those sorts of speculations don't work out well."

Have a nice and fruitful week!

To Unsubscribe Click Here