Economics

THE WEEK AHEAD

February 27-March 3, 2023

Unintended consequences require amending foreign home-buyer ban

by **Benjamin Tal** benjamin.tal@cibc.com

Late last year, the federal government enacted the "Prohibition on the Purchase of Residential Property by Non-Canadians Act". It came into effect on January 1st this year. The Act prohibits any direct or indirect purchase of residential property by non-Canadians for two years.

The motivation of course is to improve affordability by eliminating a source of housing demand that is often less price sensitive than local buyers. One of course might argue that the contribution of foreign buyers to Canada's housing affordability crisis is marginal at best. And that is a valid argument. Non-Canadians own a very small share of the housing stock — 2.2% in Ontario and 3.1% in British Columbia. And in both provinces, those rates have been on a downward trajectory since the introduction of the foreign buyers tax in 2017. But the counterargument is that whatever marginal role foreign buyers play, eliminating its impact on home prices is better than nothing. There is nothing to lose. And that's where the issue is. In fact, there is plenty to lose.

The language of the Act appears straightforward until you show it to a lawyer.[1] Let's start with the term "residential property". It turns out to be not only what you have in mind (detached, semi-detached, rows and condos), but also any developed or vacant land that does not contain any habitable dwelling and that is zoned for residential or mixed use and also is located within a census metropolitan area. It goes without saying that that definition includes many commercial real estate assets if they happened to be on land with zoning that permits a residential or mixed-use property. In fact, the entire area of downtown Toronto falls under that category. What about farmland within a census metropolitan area? Based on the Act's language, it cannot be touched by a non-Canadian.

That brings us to the second definition in question. What exactly is "non-Canadian"? The Act defines it as 3% or more foreign ownership. It of course excludes corporations whose shares are listed on a stock exchange in Canada, but importantly, it does not exclude REITs. Therefore, by definition, based on the language of the Act, the vast majority of publicly traded Canadian REITs are foreign entities.

And if that's not enough to confuse you, consider the language around the term "purchases". It refers to a direct or indirect purchase, which means that any acquisition of a lease or a mortgage tied to a residential property by a non-Canadian is prohibited. And what about share purchases? That also falls under "indirect", potentially working to ban acquisitions of units in a REIT that owned residential property.

While real estate lawyers are smiling, the rest of the industry is not. We have been in contact with many real estate players in recent weeks. The damage is real. Many commercial real estate deals have been cancelled or are on hold despite the fact that they have nothing to do with residential housing. Developers that are partly foreign owned or rely on foreign equity cannot proceed with purpose built developments that, in our view, are the most effective tool to tackle Canada's housing affordability crisis. As for REITs, by far the most capable and motivated potential builder of purpose built units, the Act is working to freeze their activity in the space. And the damage might be felt beyond the realm of real estate. Consider a private equity fund with a minority foreign investor trying to acquire shares in a manufacturing or pipeline business that sits on land zoned as residential or mixed use — only one example out of many.

Surely none of these shortcomings were the intention behind the Act. Policymakers should immediately take another look and amend the Act in a way that is consistent with what it was intended to achieve — focusing only on single units being purchased by foreigners while exempting development of new supply from the impact of the new legislation.

[1] Some information used here was obtained from Dentons Canada.

Week Ahead Calendar And Forecast—Canada

H, M, L = High, Medium or Low Priority
SAAR = Seasonally Adjusted Annual Rate
Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, February 27	8:30 AM	CURRENT ACCOUNT BAL.	(4Q)	(M)	-$11.0B	-	-$11.1B
Tuesday, February 28	-	AUCTION: 3-M BILLS $10.4B, 6-M BILLS $3.8B, 1-YR BILLS $3.8B	-	-	-	-	-
Tuesday, February 28	8:30 AM	GDP M/M	(Dec)	(H)	0.0%	-	0.1%
Tuesday, February 28	8:30 AM	GDP (annualized)	(4Q)	(H)	1.3%	-	2.9%
Tuesday, February 28	-	B.C. Budget 2023	-	-	-	-	-
Tuesday, February 28	-	Alberta Budget 2023	-	-	-	-	-
Wednesday, March 1	-	AUCTION: 2-YR CANADAS $3.5B	-	-	-	-	-
Thursday, March 2	-	-	-	-	-	-	-
Friday, March 3	8:30 AM	BUILDING PERMITS M/M	(Jan)	(M)	-	-	-7.3%
Friday, March 3	8:30 AM	LABOUR PRODUCTIVITY Q/Q	(4Q)	(M)	-	-	0.6%

Week Ahead Calendar And Forecast—United States

H, M, L = High, Medium or Low Priority
SAAR = Seasonally Adjusted Annual Rate
Consensus Source: Bloomberg

Date	Time	Economic Releases, Auctions and Speakers	Month	Priority	CIBC	Consensus	Prior
Monday, February 27	8:30 AM	DURABLE GOODS ORDERS M/M	(Jan P)	(H)	-4.0%	-3.9%	5.6%
Monday, February 27	8:30 AM	DURABLE GOODS ORDERS EX-TRANS M/M	(Jan P)	(H)	-0.1%	0.1%	-0.2%
Monday, February 27	10:00 AM	PENDING HOME SALES M/M	(Jan)	(M)	-	0.9%	2.5%
Monday, February 27	10:30 AM	Speaker: Philip N Jefferson (Governor) (Voter)	-	-	-	-	-
Tuesday, February 28	8:30 AM	WHOLESALE INVENTORIES M/M	(Jan P)	(L)	-	0.1%	0.1%
Tuesday, February 28	8:30 AM	ADVANCE GOODS TRADE BALANCE	(Jan)	(M)	-$91.4B	-$91.0B	-$89.7B
Tuesday, February 28	8:30 AM	RETAIL INVENTORIES M/M	(Jan)	(H)	-	-	0.5%
Tuesday, February 28	8:30 AM	HOUSE PRICE INDEX M/M	(Dec)	(M)	-	-0.2%	-0.1%
Tuesday, February 28	8:30 AM	S&P CORELOGIC CS Y/Y	(Dec)	(H)	-	-	6.8%
Tuesday, February 28	9:45 AM	CHICAGO PMI	(Feb)	(M)	-	45.0	44.3
Tuesday, February 28	10:00 AM	RICHMOND FED MANUF. INDEX	(Feb)	(M)	-	-	-11
Tuesday, February 28	10:00 AM	CONF.BOARD CONSUMER CONFIDENCE	(Feb)	(H)	108.1	108.4	107.1
Tuesday, February 28	2:30 PM	Speaker: Austan D. Goolsbee, Chicago (Voter)	-	-	-	-	-
Wednesday, March 1	7:00 AM	MBA-APPLICATIONS	(Feb 24)	(L)	-	-	-13.3%
Wednesday, March 1	10:00 AM	ISM - MANUFACTURING	(Feb)	(H)	47.6	47.8	47.4
Wednesday, March 1	10:00 AM	CONSTRUCTION SPENDING M/M	(Jan)	(M)	-	0.3%	-0.4%
Wednesday, March 1	-	NEW VEHICLE SALES	(Feb)	(M)	-	14.85M	15.74M
Thursday, March 2	8:30 AM	INITIAL CLAIMS	(Feb 24)	(M)	-	-	192K
Thursday, March 2	8:30 AM	CONTINUING CLAIMS	(Feb 18)	(L)	-	-	1654K
Thursday, March 2	8:30 AM	NON-FARM PRODUCTIVITY	(4Q F)	(M)	-	2.5%	3.0%
Thursday, March 2	2:00 PM	Speaker: Christopher J. Waller (Governor) (Voter)	-	-	-	-	-
Friday, March 3	8:30 AM	ISM - SERVICES	(Feb)	(M)	54.2	54.5	55.2
Friday, March 3	12:00 PM	Speaker: Raphael W. Bostic (Atlanta) (Non-Voter)	-	-	-	-	-
Friday, March 3	11:00 AM	Speaker: Lorie K. Logan (Dallas) (Voter)	-	-	-	-	-
Friday, March 3	12:00 PM	Speaker: Raphael W. Bostic (Atlanta) (Non-Voter)	-	-	-	-	-
Friday, March 3	3:00 PM	Speaker: Michelle W Bowman (Governor) (Voter)	-	-	-	-	-

Week Ahead's market call

by Katherine Judge and Andrew Grantham

In the **US**, a plethora of secondary indicators being released could provide more clarity on the direction of goods-producing sectors, with a likely increase in the ISM's manufacturing index reflecting an improvement in growth sentiment in the near term, but a drop in ex. transportation durable goods orders indicating looming uncertainty about demand in the second quarter, when interest rates will be higher. Any easing in the ISM services index in February could portend a welcome slowdown in hiring in that month.

In **Canada**, GDP data for the final quarter of 2022 will show the economy cooling, but not stalling, with consumer spending recovering from a modest dip in the prior quarter. However, perhaps most important will be the advance estimate of January activity. If that even partly reflects the strength in hiring, expect markets to further increase expectations for another rate hike later in the year. Budgets from BC and Alberta will give the first indications as to whether further stimulus money is on the way, which could add to inflationary pressures.

Week Ahead's key Canadian number: Gross domestic product—December and Q4

(Tuesday, 8:30 am)

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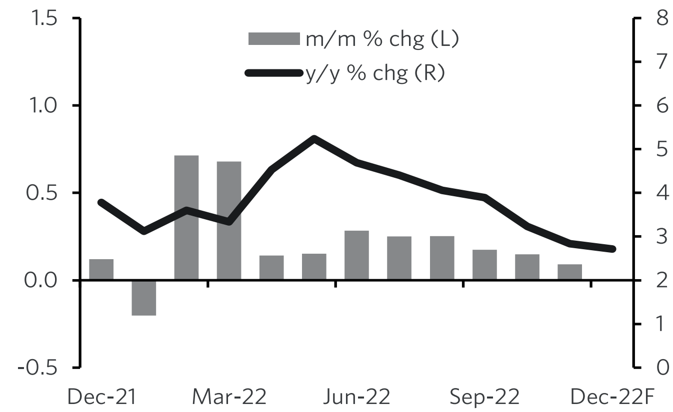
Variable (%)	CIBC	Mkt	Prior
GDP December (m/m)	0.0	-	0.1
GDP Q4 (q/q SAAR)	1.3	-	2.9

Chart: Canadian real GDP at basic prices



Source: Statistics Canada, Haver Analytics, CIBC

Growth in the Canadian economy continued to cool during the final quarter of 2022, likely clocking in at a pace below the economy's long-run potential and therefore helping ease inflationary pressures. Domestic demand appears to have rebounded modestly following an unexpected drop in Q3, with consumer spending rising and the drop in residential investment slowing. Opposing that, export volumes appear to have given back part of the jump seen in the prior quarter, and inventories should be a drag on growth following a strong stock build in Q3. Continued weakness in commodity prices likely brought a further drop in the overall price deflator and a second successive quarterly decline in GDP in nominal terms.

The monthly GDP print for December is expected to show little change in economic activity for that month, although the advance estimate for January should point to at least modest growth for the first month of 2023 if the surge in employment is a reliable guide.

Forecast implications — The economy continues to hold up better than expected following last year's rapid rise in interest rates. However, as household savings are drawn down, and more homeowners need to remortgage at higher interest rates, consumer spending is still expected to struggle as 2023 progresses. A stall in the economy, or even a modest recession, is likely more a question of when rather than if.

Other Canadian releases: Current account balance—Q4

(Monday, 8:30 am)

A weakening of commodity prices, combined with some softness in export volumes as well, saw the goods trade balance swing from surplus to broadly balanced in Q4. However, a narrowing in the deficit for services appears to have acted as an offset and left the current account deficit little changed at $11bn in the final quarter of 2022.

Week Ahead's key US number: Durable goods orders—January

(Monday, 8:30 am)

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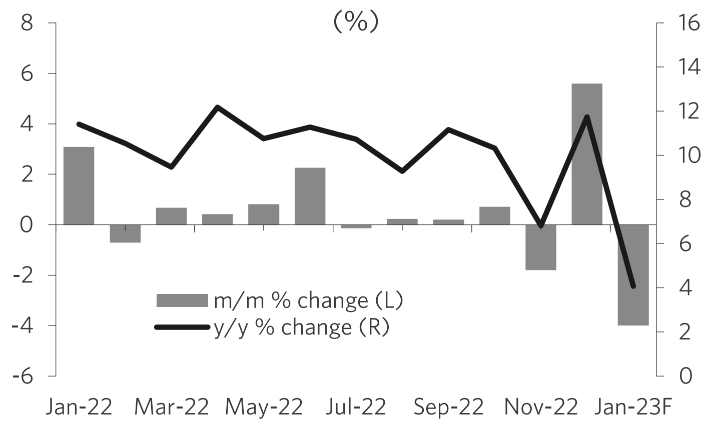
Variable (%)	CIBC	Mkt	Prior
Durable goods orders (m/m)	-4.0	-3.9	5.6
Ex-transportation (m/m)	-0.1	0.1	-0.2

Chart: US durable goods orders



Source: Census Bureau, Haver Analytics, CIBC

The boost to durable goods orders from the commercial aircraft component will be undone in January, likely resulting in a 4.0% decline in total orders. That could also include a modest 0.1% drop in the ex-transportation component, in line with the deteriorating trend seen in the ISM's new orders sub-index into January. While capacity utilization in the industrial sector increased in that month, it remained well below the peaks seen in 2022, suggesting that orders in the core capital goods group (ex. transportation and defense equipment) likely didn't receive much support.

Forecast implications — Goods sector indicators have been mixed so far in 2023, with consumer spending on goods stronger than expected, while the ISM manufacturing index has foundered. Any softening in orders in the core capital goods group could portend softness in business investment in equipment in the second quarter, with expectations for higher interest rates possibly weighing more on demand.

Other US Releases: Advance trade in goods—January

(Tuesday, 8:30 am)

Strong demand for consumer goods likely boosted US imports in January, facilitated by China's re-opening. That could have masked any progress in exports of industrial goods on signs of resilience in the global economy at the start of the year, causing the US goods trade deficit to widen to $91.4bn.

ISM Manufacturing—February

(Wednesday, 10:00 am)

Regional PMIs were mixed in February, suggesting that the ISM's index could have ticked up, but still remained in contractionary territory, at 47.6. A stronger start to the year than thought for domestic growth could have boosted sentiment, but uncertainty about future demand could have still left the new orders sub-index in negative territory.

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