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The Elephant Rolls Over: Taxing Times for Canada?

by Avery Shenfeld

As Pierre Trudeau noted, Canada's relationship to the US is like sleeping next to an elephant, whose every twitch and grunt is felt. We're hearing a lot about how NAFTA changes might affect us, but what about the sweeping tax reform now wending its way through Congress?

If the US had delivered a big tax savings for average American consumers, Canadian exporters would have reaped collateral benefits. That's not the case here, particularly since the US growth rate will soon be capped by the constraints inherent in reaching full employment.

US high income earners, particularly shareholders or those earning pass-through income, will get a more material lift. But due to quirks in the bill, federal tax burdens aren't coming down for those in high tax states like California or New York—two states that compete with Canada for global talent in tech and financial services respectively.

At the corporate level, the American system will go from being much more punitive to closer in line with Canada's (likely a bit below for non-energy companies, higher for oil and gas producers). So Canada will lose an edge we offered earlier.

The US will also move to a system in which profits are generally taxed in the country they are earned. US-Canada cross-border multinationals could face rules that limit US tax benefits achieved through intra-company payments to an affiliate located abroad, as well as limits on the amount that can be shielded from US tax through interest deductions.

But if there's one major risk for Canada, it's in the American move to allow for immediate expensing of capital investments undertaken in the next five years. For companies that have existing income to write that off against, it could tilt a location decision to operations south of the border. This immediate depreciation is, in fact, a much more powerful tool to alter business investment decisions than lower tax rates, which reward companies with existing assets.

That new incentive could pile on to other developments that can lean towards a made-in-the-USA strategy. Those include bully-pulpit warnings from Trump to stay in America, lighter environmental restraints, tougher Buy-America provisions, a growing number of trade actions under antidumping or countervailing duty laws, and the uncertainty over what NAFTA might look like (if it exists at all).

Canada needn't match all of these measures. In trade, a floating currency is the great equalizer, since however painful it is to our personal buying power, the loonie will find a level at which the trade balance is sustainable. But if we want to avoid smacking ourselves with a weaker exchange rate, we could rise to the challenge on the business tax side without an expensive corporate rate cut. A matching five-year period for immediate expensing in the trade-exposed resource and factory sectors would level the playing field, at a time in which we face a lot of other headwinds in attracting business investment spending.

MARKET CALL

- Our call back in September was for a Bank of Canada hike that month, but then a pause until April. Early data for Q4 activity and employment are admittedly running firmer than our forecast, raising risks of a hike in Q1, but we're leaving our call in place for now. Troubled NAFTA negotiations could still tip the balance towards patience. Soft US core inflation will also keep the Fed on hold in Q1.
- The flat US yield curve reflects minimal inflation uncertainties and the hangover from years of central bank bond buying (see pages 3-5). Core inflation could very gradually creep higher over 2018, and markets will look ahead to greater Treasury funding needs and, by 2019, less aggressive ECB and BoJ policy that will allow upward pressure on global yields. Canadas should outperform in the latter half of 2018, given that there's no equivalent QE unwind, nor rising federal deficits to fund.
- The Canadian dollar didn't benefit from firmer global crude prices, in part because discounts on Canadian heavy oil increased. The loonie is pricing in greater odds of a Q1 rate hike than we see as likely, and is also not fully braced for an unsuccessful end to NAFTA talks.

INTEREST & FOREIGN EXCHANGE RATES

		2017	2018				2019	
END OF PERIOD:		**13-Dec**	**Mar**	**Jun**	**Sep**	**Dec**	**Mar**	**Jun**
CDA	Overnight target rate	1.00	1.00	1.25	1.25	1.50	1.50	1.75
	98-Day Treasury Bills	0.90	0.95	1.25	1.20	1.45	1.45	1.75
	2-Year Gov't Bond	1.53	1.55	1.60	1.65	1.75	1.85	1.95
	10-Year Gov't Bond	1.87	2.10	2.20	2.20	2.25	2.30	2.35
	30-Year Gov't Bond	2.17	2.40	2.60	2.70	2.70	2.65	2.70
U.S.	Federal Funds Rate	1.375	1.375	1.625	1.875	1.875	2.125	2.125
	91-Day Treasury Bills	1.31	1.40	1.65	1.70	1.70	1.85	1.95
	2-Year Gov't Note	1.80	1.80	1.90	2.05	2.15	2.25	2.30
	10-Year Gov't Note	2.36	2.55	2.65	2.80	2.90	2.85	2.90
	30-Year Gov't Bond	2.74	3.00	3.25	3.35	3.40	3.40	3.45
Canada - US T-Bill Spread		-0.41	-0.45	-0.40	-0.50	-0.25	-0.40	-0.20
Canada - US 10-Year Bond Spread		-0.50	-0.45	-0.45	-0.60	-0.65	-0.55	-0.55
Canada Yield Curve (30-Year — 2-Year)		0.63	0.85	1.00	1.05	0.95	0.80	0.75
US Yield Curve (30-Year — 2-Year)		0.94	1.20	1.35	1.30	1.25	1.15	1.15
EXCHANGE RATES	CADUSD	0.78	0.75	0.77	0.76	0.76	0.78	0.78
	USDCAD	1.28	1.33	1.30	1.32	1.31	1.28	1.29
	USDJPY	113	111	110	108	106	106	105
	EURUSD	1.18	1.21	1.22	1.23	1.25	1.23	1.23
	GBPUSD	1.34	1.31	1.31	1.34	1.38	1.38	1.40
	AUDUSD	0.76	0.80	0.84	0.85	0.85	0.86	0.86
	USDCHF	0.99	0.95	0.95	0.94	0.94	0.96	0.96
	USDBRL	3.32	3.35	3.30	3.45	3.51	3.60	3.45
	USDMXN	19.1	19.2	19.4	18.8	18.6	18.3	17.9

The Bound on Bonds: What's Keeping Treasuries So Flat?

Avery Shenfeld and Nick Exarhos

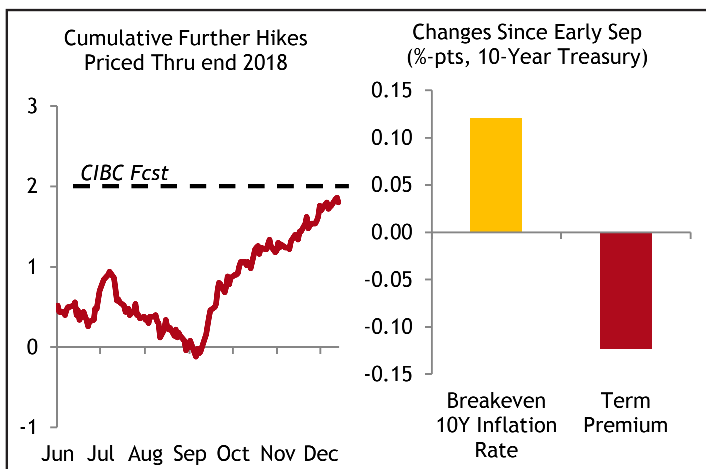
The "conundrum" is back. Alan Greenspan famously used that term years ago to describe a stubbornly sticky bond market, and today's puzzlingly tame US long-term yields are just as mysterious. Unlocking their secrets is key to understanding where the US bond market is headed, which is always a major driver for Canadian long rates.

It's relatively easy to reject some of the reasons one hears on trading room floors. This is not about a flat yield curve signaling a recession. For one, growth numbers have been rock solid. Moreover, the recession signal from a flat yield rests on market perceptions that short rates are approaching an unsustainable peak that the economy can't live with—a reason why investors would lock into longer term bonds with little or no pick-up. But investors have actually been building their expectations for rate hikes ahead (Chart 1, left).

Diminished inflation expectations can also lower longer-term yields. But that's not the story here, at least judged by the market for inflation-linked bonds, in which the implied 10-year "breakeven" rate of inflation has moved up by 0.1% since September, and sits at a reasonable 1.9% 10-year CPI pace (Chart 1, right).

Chart 1

More Expected from the Fed (L); Increases in Inflation Pricing Offset By Decrease in "Term" Premium (R)



Source: Bloomberg, CIBC

Instead, what's happened is that as short-rate expectations have risen, we've seen a decline in the premium that investors demand in long rates, over and above what they expect to obtain by continually rolling over bills for the coming decade. The recent drop in the term premium has again taken it into over 50 bps of negative territory. In theory, investors are now paying a half-percent to lock in money versus their median outlook for short rates over time.

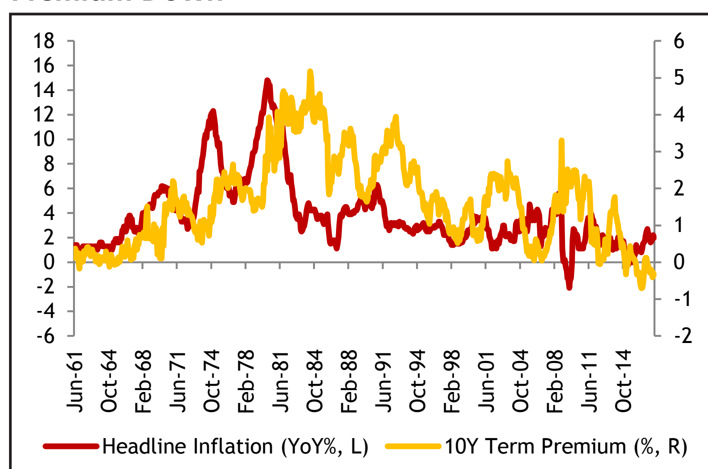
Why the Negative Term Premium?

It's atypical for investors to reduce their fear of upside surprises in inflation even as their medium-term inflation expectation is rising. Over the decades, it was high inflation that raised the term premium (with a lag), and then low inflation that gradually reduced these premiums (Chart 2). Perhaps we're not seeing enough inflation in monthly data to convince investors that the Fed is out of the woods in terms of being stuck in a sub-target inflation world.

The term premium can be thought of as a reflection of the uncertainty surrounding inflation forecasts, rather than just the level of inflation (since higher inflation also influences expected short rates). A measure of that uncertainty based on data from the Michigan Survey of Consumers has been tumbling (Chart 3).

Chart 2

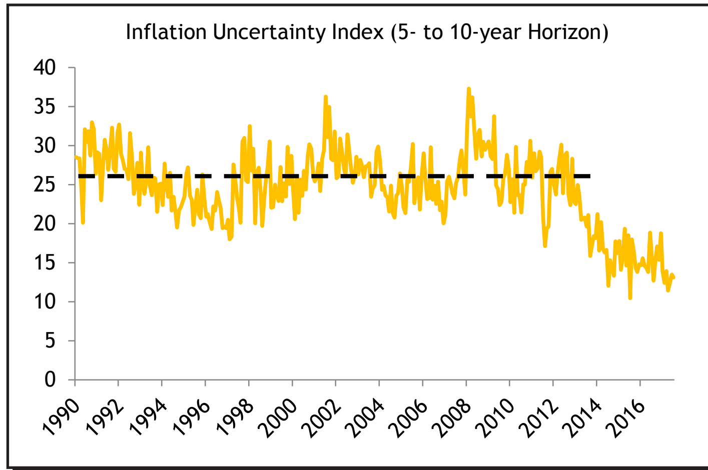
Low—and Stable—Inflation Has Driven Term Premium Down



Source: NY Fed, BLS, CIBC

Chart 3

Survey Data: Consumers Less Worried About Inflation Surprises



Source: Carola Binder (Haverford College), CIBC

If the same phenomenon is occurring amongst investors, they may simply be expressing confidence that a Fed prepared to hike before inflation has really emerged is one that will continue to keep it in a narrow range. These term premium factors could well keep Treasury yields below historical norms in the next few years.

Another demand side story bandied about is tied to the strong run we've seen for equities. That has pension funds catching up to liabilities, and now more able to take money off the stock market table and park it in less-generous bonds, paying in effect to reduce risk. We give that potential explanation less weight, since funds of that nature could simply roll 2-year notes for a while if 10s or 30s look too rich.

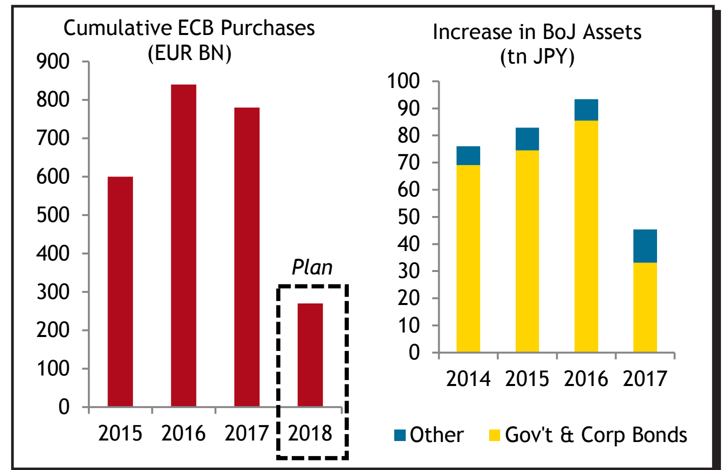
Buy America, From Abroad

There are in fact, easier explanations closer at hand—not on the demand side, but on the supply side. It's the legacy of years of QE from the Fed, and still-ongoing bond buying by the ECB and the Bank of Japan (Chart 4).

If you think that 2½% is too low on US 10s, don't look at German bunds which yield only 30 bps or so. While ECB buying has diminished in euro terms, so too has the remaining stock of bonds from which they are drawing their purchases.

Chart 4

ECB (L) and BoJ (L): Hoovering Up Assets

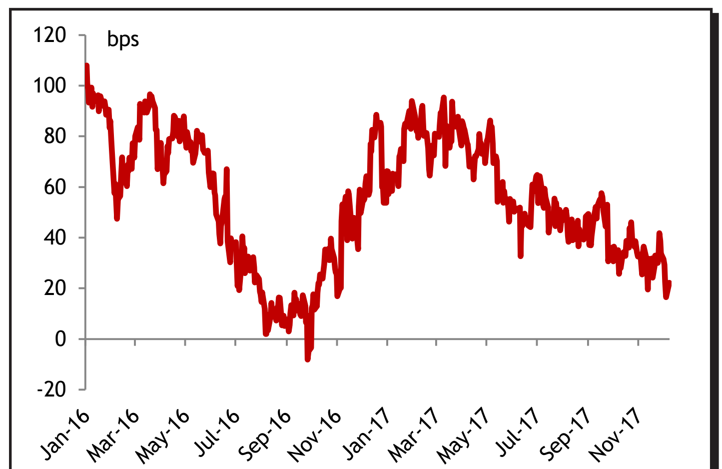


Source: ECB, BoJ, CIBC

Make sure to avert your eyes from Japan as well, where investors, incented by the Bank of Japan's policies, are willing to lock in money for a decade's worth of zero nominal returns. Even at current yields, that international comparison and pricing in the futures market for currencies, allows investors in the land of the rising sun to buy a US 10-year bond, lock in the exchange rate using FX forwards, and still earn a premium to the prevailing domestic rate in yen (Chart 5). That international bid helps explain why the longer end of the US curve hasn't moved, despite the market shifting its expectations higher for the likely path of overnight rates.

Chart 5

Excess Returns on Hedging Treasury Investment Into Yen vs JGBs (10-Year Tenor)



Source: Bloomberg, CIBC

US Supply Outlook Swells

Look for these global factors to fade as we move into 2018. Above-potential growth in Europe and Japan will see the ECB signal the end of its QE program, while the Bank of Japan is likely to act on recent musings about letting its 10-year rates attain a higher level.

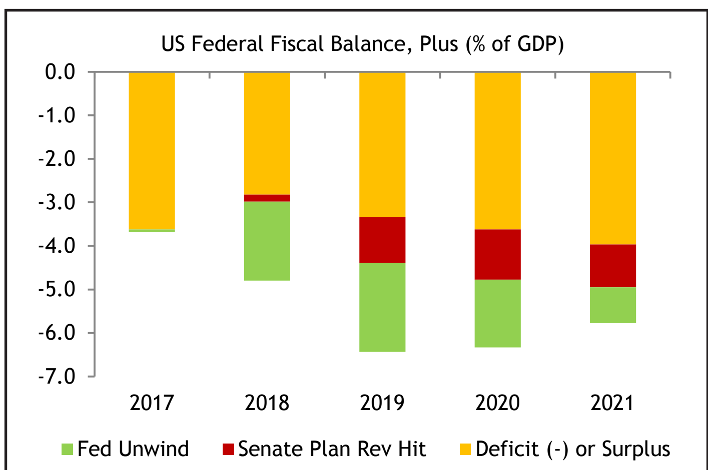
The net reduction in supply caused by aggressive central bank buying has already slowed from larger cumulative global purchases a few years ago. The further removal of a significant price-insensitive buyer from the market will have the *de facto* effect of increasing supply available to other investors.

Also on the supply side, Treasury issuance has been holding back long-end supply by favouring bills over longer-term securities in its funding mix. But higher grade corporate issuers will be tempted by a flat curve to fill in some of that supply gap at the long end.

Moreover, Treasury auctions won't be as light as we look ahead, given rising deficits under a likely passage of a tax cut bill, and the amortization of the Fed's balance sheet (Chart 6). The increase in bond supply that will have to be absorbed by the market will approach 7% of US GDP in 2019, nearly twice what we saw in 2017.

Chart 6

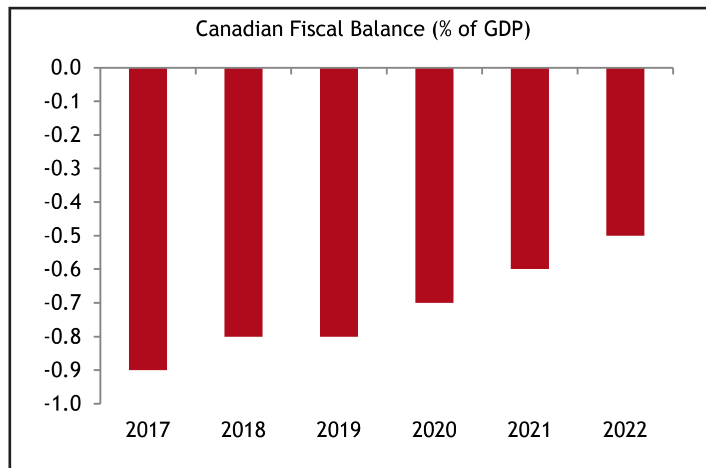
QE Unwind Adds to Wide US Deficits and Gap Created by Tax Cuts



Source: US CBO, Joint Committee on Taxation, Federal Reserve, CIBC

Chart 7

Canadian Fiscal Balance on the Mend



Source: Finance Department Canada, CIBC

Canada, by contrast, has an improving fiscal backdrop on deck, as the fiscal ease introduced in the wake of the oil shock is wound down (Chart 7). That's one reason we see rates north of the border climbing a bit less aggressively in the year ahead, with 10-year rates increasing 40 bps from here to the end of next year, compared to a 50-bps move expected stateside.

Policy, Inflation, and Yields Normalize in 2018

The "conundrum" binding the bond market to historically low yields doesn't have a single explanation, and therefore won't be fully loosened in a single tug. Confidence on moderate inflation ahead should hold long rates well below prior-cycle levels. But in the US, and to a lesser extent in Canada, some of the special factors impacting foreign demand and domestic supply will be easing off in the coming year, allowing yields to look a bit less puzzling.

Central Bank Guidance: Bad Directions?

Royce Mendes

If you don't know where you're going, you probably shouldn't be handing out directions. A couple of high-profile central banks seem to think otherwise. In an effort to limit market reaction to recent policy changes, both the ECB and BoE have fed investors healthy doses of forward guidance.

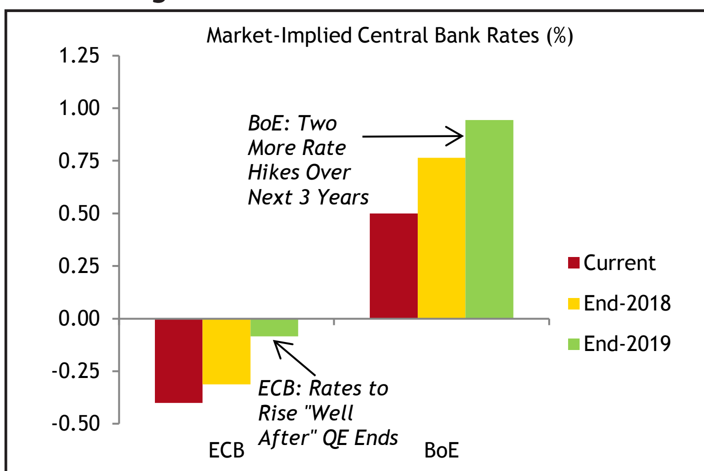
In President Draghi's words, his central bank will keep interest rates at their lower bound "well past" the end of its bond-buying program. Similarly, UK central bankers have added confidence to the market expectation of two rate hikes in three years from the Old Lady of Threadneedle Street.

Investors crave that kind of certainty. But policymakers are usually loath to prejudge meetings even just days into the future. Given the chance, markets are now running with the latest guidance, pricing in almost word for word the messages of European policymakers (Chart 1).

But those same central bankers will be the first to say that their statements are not some Odyssean pronouncement, tying them to one course of action no matter how the economic landscape unfolds. If the forecasts are wrong, the course will need to be adjusted. It's therefore crucial to figure out whether these forecasts pass the smell test.

Chart 1

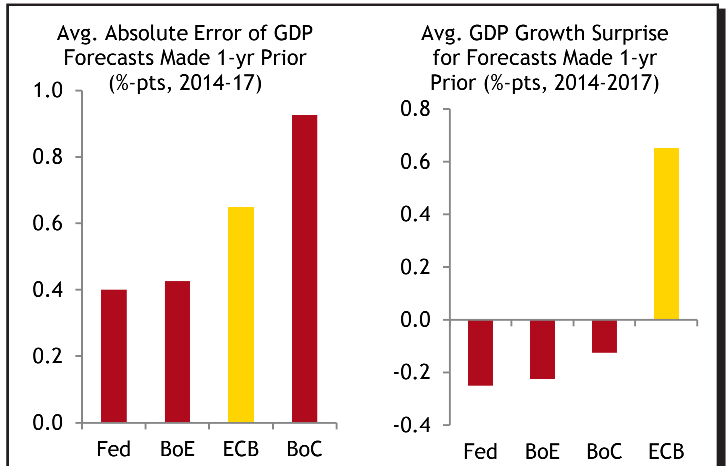
Markets Exactly Where Central Banks Are Guiding Them



Source: Bloomberg, CIBC

Chart 2

ECB Staff Avg Forecasters Compared to Other Central Bankers (L), But Underestimate Growth (R)



Source: Fed, BoE, ECB, BoC, CIBC

Aiming Too Low

The period of 2014-2017 shows that the Fed and BoE were slightly more accurate than the ECB in forecasting growth rates (Chart 2, left), with the Bank of Canada's projections suffering from the unexpected crash in oil prices.

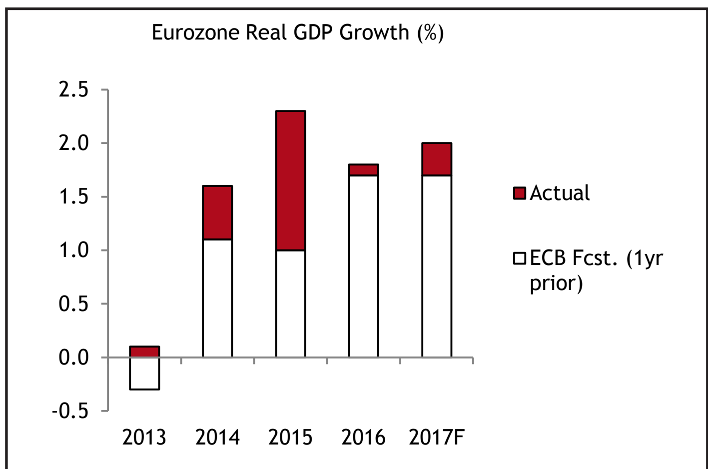
The direction of misses is, however, far more interesting than their size. Notably, the ECB has been the only one of that group to underestimate growth, and it's done so by a wide margin (Chart 2, right). In fact, staff at the institution have underestimated growth in each year since 2012 (Chart 3).

The headline inflation rate is also set to accelerate in the months ahead, potentially breaching 2% (Chart 4). When that happened earlier this year, President Draghi changed course and delivered a speech that was widely viewed as hawkish, causing the German 10-year rate to increase 35 bps in a matter of days.

This past year has been one of relative calm amongst Governing Council members with usually divergent views. A Eurozone economy any stronger than the ECB currently envisages combined with hotter inflation will, at the least, create a ripe environment for reigniting a more

Chart 3

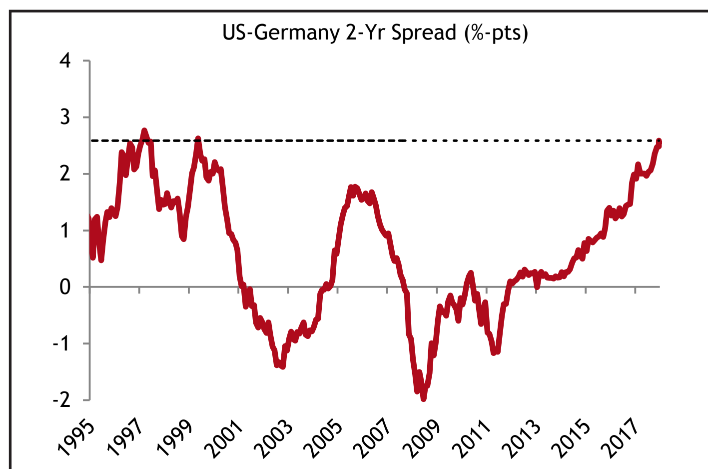
ECB Staff Have Underestimated Growth In Each of the Past Five Years



Source: ECB, FRED, CIBC

Chart 5

US-Germany Yield Spreads Stretched to the Limit



Source: Bloomberg, CIBC

vigorous public debate amongst policymakers. Such a development would undoubtedly jar those investors who have been following the testaments of central bankers too closely.

With the US 2-year spread to German bunds at its widest since the late 1990s (Chart 5), even a slight pulling forward of Eurozone interest rate expectations will have an important impact on rate differentials and the single currency.

Storm on the Horizon

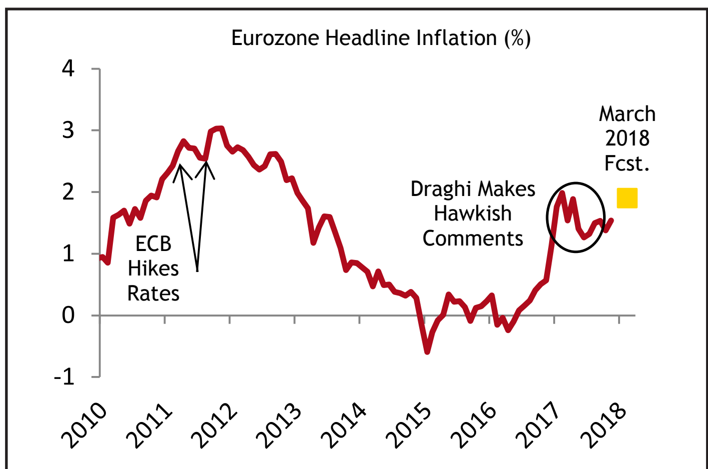
The Bank of England has even more reason to eschew the long-term guidance it has provided. For one, policymakers are split as to whether inflation will be at, below or above-target two years from now (Chart 6). Such uncertainty about the prospects for inflation should raise red flags on the worthiness of any rate guidance.

But growth uncertainties are even more of a factor that should be limiting BoE policymakers from lending their names to any specific rate projections. Brexit negotiations stand as a massive roadblock to providing forecasts with much conviction. The pending divorce has opened the economy to a very broad range of plausible outcomes.

Its starting point would augur for more tightening than is currently expected. The unemployment rate now stands at its lowest level since the 1970s, while the Office for

Chart 4

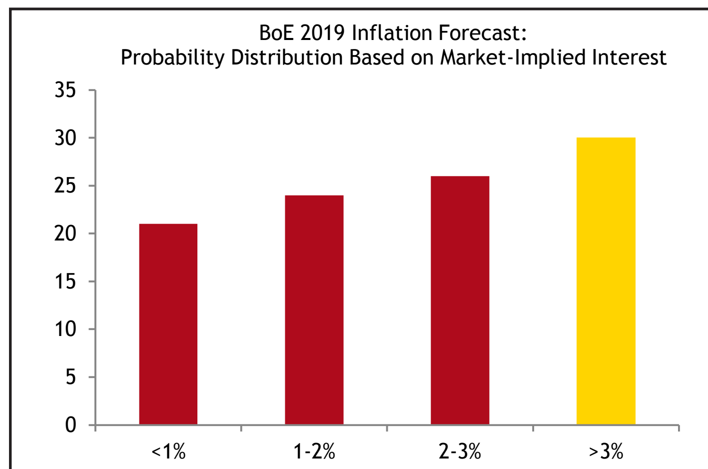
Eurozone Inflation Could Spur Hawks Back Into Action



Source: Bloomberg, CIBC

Chart 6

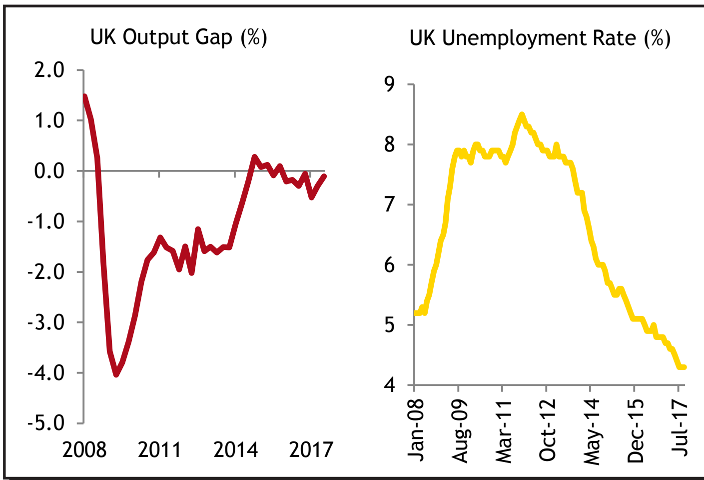
BoE Has Little Certainty About Where Inflation Will Be in 2019



Source: BoE, CIBC

Chart 7

If Brexit Goes Well, Fundamentals Suggest Much More Than Two BoE Hikes in the Next Three Years



Source: OBR, Bloomberg, CIBC

Budget Responsibility estimates that the output gap is virtually closed (Chart 7, left & right). An economy in such a position would normally require more than two rate hikes over the next few years if no other shocks occurred.

But an unfavourable turn in Brexit negotiations could see the UK's economic fortunes flipped upside down. A worst-case scenario, with a messy divorce and major trade barriers, is not our base case. But the BoE must at least recognize that outcome as a real possibility, reducing its ability to provide meaningful guidance.

Complacency about the economic environment is not confined to the BoE. The Economic Policy Index (produced by academics at Northwestern, Stanford and the University of Chicago) has completely reversed its post-Brexit spike (Chart 8). The measure uses newspaper references to assess public confidence in the economic environment, suggesting that it's no longer a hot topic in daily news cycles.

Investors also seem to be underpricing the risk that negotiations get rocky in the months to come. Option-implied volatility in sterling has come back to pre-Brexit levels (Chart 9), with the sheer length and complexity of negotiations seeing investors less interested in hedging. But is that really such a good idea?

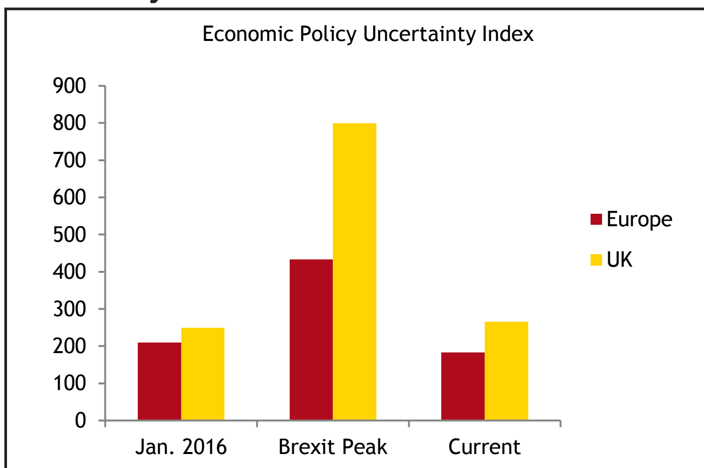
Major negotiations are set to occur on the trading relationship between the EU and UK. Political posturing, private sector lobbying and public outcry will almost assuredly see tensions heat up next year between the two, even if a favourable deal is eventually reached.

Silver Linings Playbook

The complacency surrounding risks and a trend toward following central bank guidance too closely has left a holiday gift for some market participants. Hedging the risk of a faster-than-expected sell-off in euro-area fixed income, or the possibility of Brexit-related volatility in sterling are on sale right now. Corporations and investors would be wise to think about whether they want to head into 2018 believing that central bank guidance has cleared up all the risks and obviated the need for hedging FX and rate risks.

Chart 8

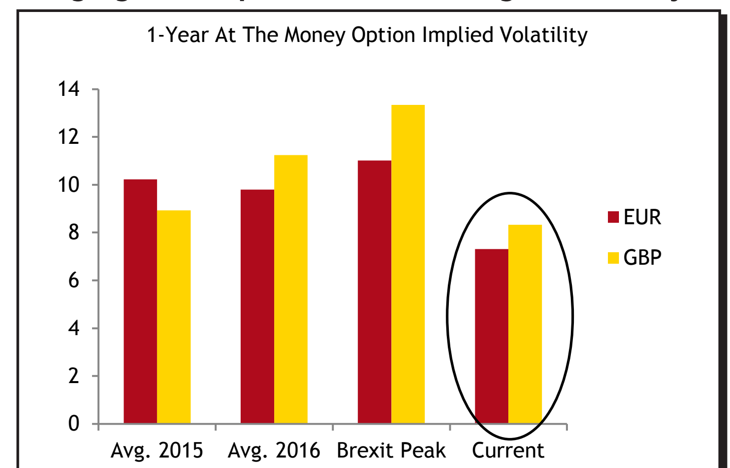
Given Brexit Risks, This Seems to Underestimate Uncertainty



Source: "Measuring Economic Policy Uncertainty" by Scott R. Baker, Nicholas Bloom and Steven J. Davis

Chart 9

Hedging is Cheaper Given Prevailing Uncertainty



Source: Bloomberg, CIBC

US Housing: Cracks in the Foundation

Andrew Grantham

The US housing market appears to be building momentum again, with starts and new home sales accelerating after treading water through much of 2016/17. While housing market activity will continue to be supported in the near term by re-building efforts following the late summer hurricanes, recent figures on household formation suggest that the longer-term outlook is on shakier foundations.

Recent annual figures suggested that, as of March this year, the number of households was only around 400K higher than the previous year (Chart 1). That's the second weak figure in the past three years, and as a result the five-year average of household formation is now only a little over 1,000K—below the current pace of housing starts. While we don't see it as a near-term problem, that trend, combined with the impact new immigration policy will have on one very important source of housing demand, has us lowering our forecast for housing starts in 2019.

No Need to Panic…Yet

For now, housing starts are benefitting from rebuilding efforts following this past year's hurricanes. Moreover, starts don't have to respond straightaway to a slowing in household formation because the US may have been underbuilding recently. After the excess of the pre-recession period, so far this decade housing starts have averaged well below the pace of household formation (Chart 2). Initially, that merely ran down excessive inventories, but months' supply of both new and existing homes are now near historical lows.

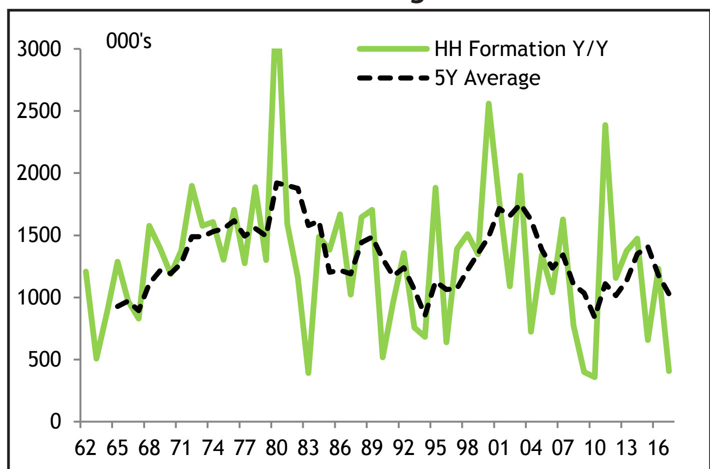
And there's always the chance that household formation has really been stronger than the recent data suggest. Even though recent monthly figures seem to confirm the slowdown, past revisions show a few instances where the number of households has been dramatically undercounted (Chart 3). Revisions don't occur every year, but upward shifts similar to those seen in 2010 or 2013 would certainly go a long way to changing the outlook.

Not Just a Young Person Story

Earlier in the US recovery from the financial crisis, much of the blame for continued sluggishness in housing was placed at the door of young people who decided to save money by living with their parents. That trend has continued well past the peak in the 16-34 year-old unemployment rate (Chart 4, left). The key issue here appears to not be whether those young people have a job, but whether they can afford a down-payment or qualify for a loan. With student debt high and savings/

Chart 1

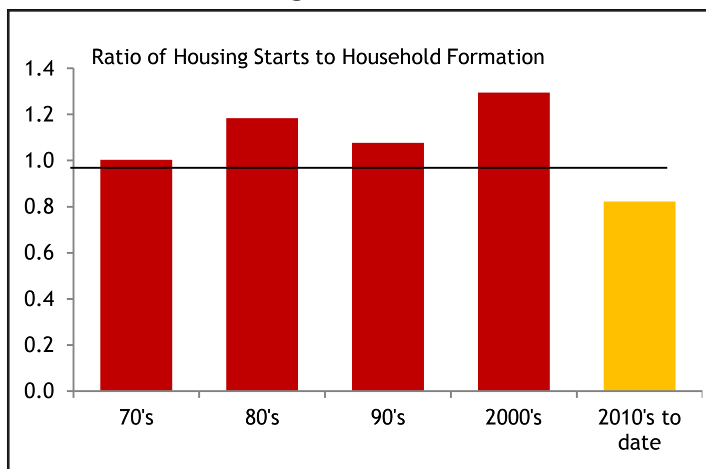
Household Formation Slowing



Source: US Census Bureau, CIBC

Chart 2

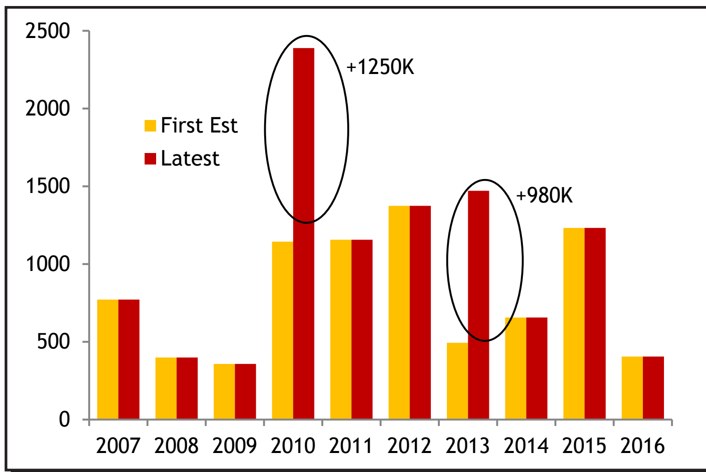
Ratio of Starts to Household Formation Suggests Recent Underbuilding



Source: BEA, US Census Bureau, CIBC

Chart 3

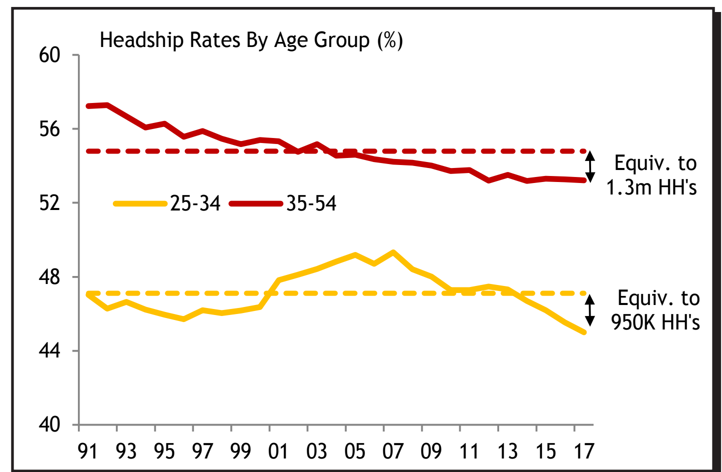
Household Formation Numbers Have Been Revised Up Significantly in the Past



Source: US Census Bureau, CIBC

Chart 5

Headship Rate Declines for 35-54 Year-olds as Well as 25-35



Source: US Census Bureau, BEA, CIBC

investments low, the leverage ratio for under-35 year-olds is already historically high, even though fewer people in that cohort have mortgage debt (Chart 4, right).

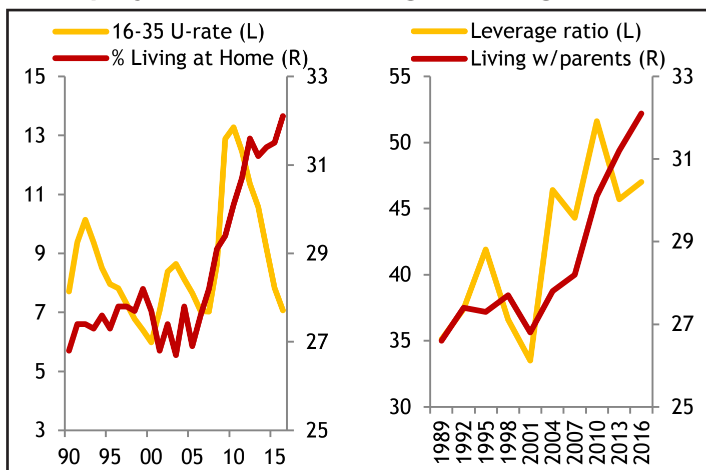
However, laying all of the blame for sluggish household formation at the door of younger Americans was, and still is, incorrect. Relative to the averages that prevailed before the financial crisis, headships rates for Americans aged 35-54 are also lower. And the number of households that undershoot represents is larger than that for 25-34 year-olds (Chart 5).

What's driving this decline, and whether we should expect it to recover, is unclear. Taking a longer-term view, the headship rate for the 35-54 cohort isn't as low as it was in the 60s and early 70s (Chart 6, left). However, the proportion of adults who are married and living together certainly hasn't been rising back to the levels seen during that period. A more likely reason for the drop in 35-54 headship rates is the ethnic change in US population.

Strong growth in the Hispanic (Chart 6, right) and Asian populations has increased the share of the population whose cultural backgrounds have a greater tendancy to share homes with elderly relatives. That trend in cohabitating can be shown in the wider spread between "five-person" households and "three-children" families for the Asian and Hispanic populations versus the White

Chart 4

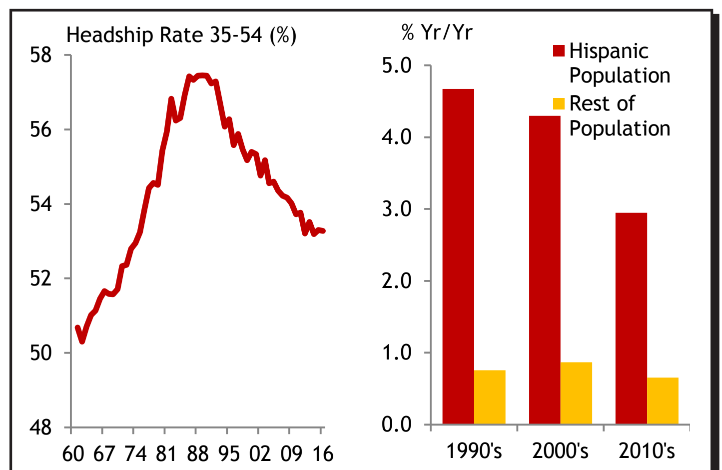
Young People Living at Home Well Past Peak in Unemployment (L) Due to High Leverage (R)



Source: BEA, US Census Bureau, CIBC

Chart 6

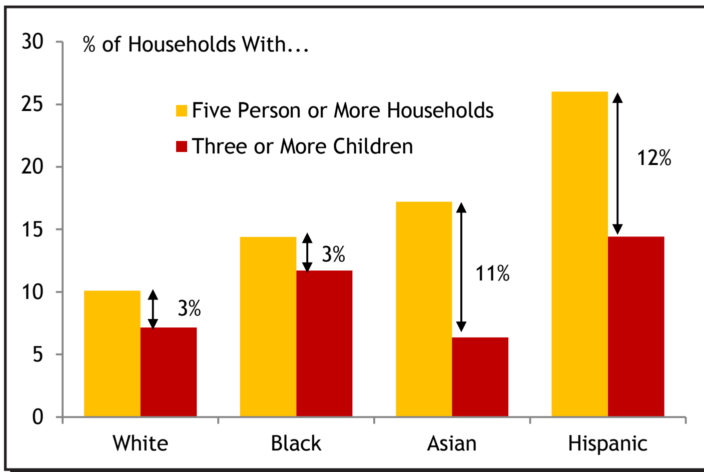
35-54 Headship Rate Not a Record Low (L), Hispanic Population Rising Faster (R)



Source: US Census Bureau, BLS, CIBC

Chart 7

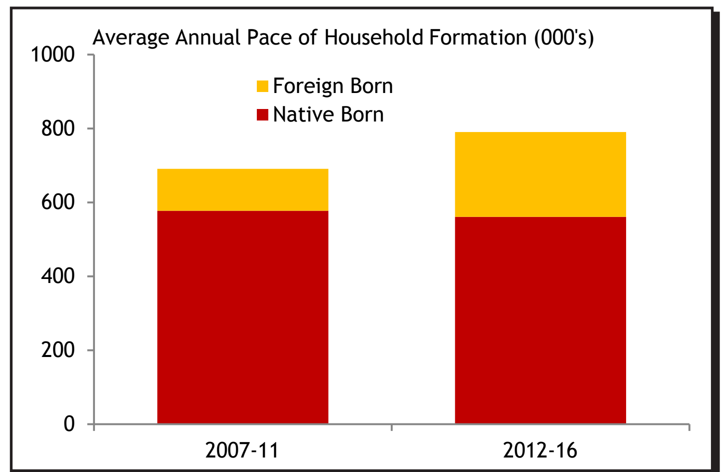
Larger Asian/Hispanic Households Not Due to More Children



Source: US Census Bureau, Pew Research Center, CIBC

Chart 8

Household Formation Becoming More Reliant on New Immigration



Source: US Census Bureau, CIBC

and Black populations (Chart 7) implying that there are "non-children" in more of these five-person Asian or Hispanic households. With demographic projections showing that these groups will continue rising as a proportion of the population, a big turnaround in the overall 35-54 headship rate appears unlikely.

Important Immigrants

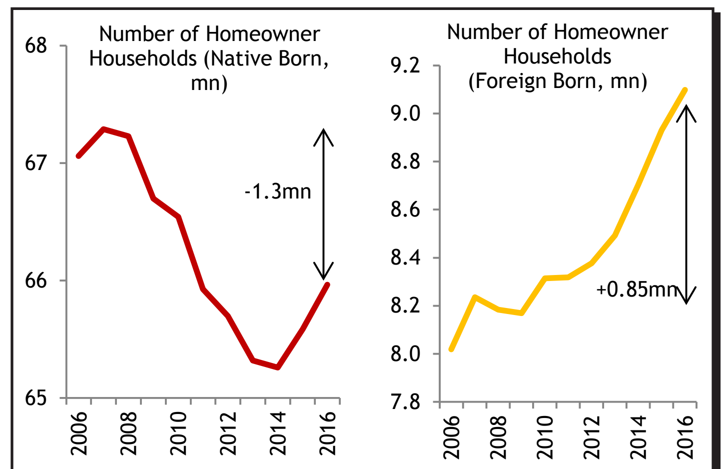
With headship rates still low and even falling further in some age groups, household formation in recent years has become increasingly reliant on immigration. Between 2007 and 2011 immigration was responsible for a little over 15% of new household formation. During the most recent five years, that's risen to 30%. And if it wasn't for the impact of immigration, household formation would have actually been slightly slower than during the previous five years (Chart 8).

That reliance on immigration is even larger when we focus on homeownership rather than simply the number of households. While the number of native-born homeowners in the US is still well below where it stood at the peak of the housing boom (Chart 9, left), that's almost been offset by the rise in foreign-born homeowners (Chart 9, right).

With household formation increasingly reliant on immigration, President Trump's proposal to halve the number of newcomers represents a potential threat to homebuilders. And even though new arrivals are still more likely to live in high-rise units, the recent pick-up in homeownership suggests they have been an important source of demand for single family homes as well. As a result, Canadian lumber producers should take note. After some continued strong months ahead, the shakier foundations suggest that housing construction likely won't be still rising come 2019.

Chart 9

Homeowner Numbers Down for Native Born (L), Up for Foreign Born (R)



Source: US Census Bureau, CIBC

ECONOMIC UPDATE

CANADA	**17Q3A**	**17Q4F**	**18Q1F**	**18Q2F**	**18Q3F**	**18Q4F**	**19Q1F**	**19Q2F**	**2017F**	**2018F**	**2019F**
Real GDP Growth (AR)	1.7	2.3	1.8	2.2	2.1	1.5	1.5	1.4	3.0	2.1	1.6
Real Final Domestic Demand (AR)	3.7	3.7	2.0	1.6	1.3	1.3	1.3	1.2	3.0	2.5	1.2
Household Consumption (AR)	4.0	3.1	1.6	1.6	1.3	1.3	1.3	1.3	3.7	2.3	1.3
All Items CPI Inflation (Y/Y)	1.4	1.7	1.5	1.8	2.2	2.3	2.4	2.2	1.6	2.0	2.1
Unemployment Rate (%)	6.2	6.0	5.8	5.8	5.8	5.7	5.7	5.7	6.4	5.8	5.7

U.S.	**17Q3A**	**17Q4F**	**18Q1F**	**18Q2F**	**18Q3F**	**18Q4F**	**19Q1F**	**19Q2F**	**2017F**	**2018F**	**2019F**
Real GDP Growth (AR)	3.3	2.7	1.2	2.3	2.1	2.1	1.6	2.0	2.3	2.2	1.9
Real Final Sales (AR)	2.5	3.1	1.3	2.1	2.1	2.1	1.7	1.8	2.4	2.2	1.9
All Items CPI Inflation (Y/Y)	2.0	2.1	2.0	2.3	2.5	2.4	2.4	2.5	2.1	2.3	2.4
Core CPI Inflation (Y/Y)	1.7	1.7	1.7	2.1	2.2	2.3	2.2	2.3	1.8	2.1	2.3
Unemployment Rate (%)	4.3	4.1	4.2	4.1	4.0	3.9	3.8	3.7	4.4	4.0	3.7

CANADA

Third quarter growth looks poised to be a bit firmer than we were expecting earlier, although a downwards revision to Q2's pace keeps 2017 GDP growth still tracking 3%. The labour market has put up another set of spectacular results, lowering the near-term profile for the unemployment rate. Applying some of the logic used in our recent paper on the US labour market, we're likely going to need a lower jobless rate in this cycle to see wages get into the range needed to sustain 2% inflation, something we've reflected in our forecasts.

UNITED STATES

We upgraded our 2017 growth forecast a tick to 2.3% on better-than-expected Q3 numbers. While the fourth quarter might show some deceleration, a 2.7% annualized advance in GDP still means the economy is set to finish the year on solid footing. That being said, our analysis shows inflation taking its sweet time to accelerate, with wages still needing further improvement in the labour market. Look for year-on-year growth in core consumer prices to average a mediocre 2.1% in 2018.

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