



Economics

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THE WEEK AHEAD

October 15-19, 2018

Ottawa Should Accelerate the Path to Accelerated Depreciation

by Benjamin Tal

One should not underestimate the negative impact that NAFTA uncertainty had on capital expenditures in Canada. In numerous conversations we had with CEOs over the past year, the trade dispute emerged as the chief factor behind their inaction. With the birth of the USMCA, trade uncertainty may be still an issue for some sectors, but overall has markedly diminished. So we should see some improvement in capital spending soon. And we need it. The capacity utilization rate, at over 85%, is at an eleven-year high. There is an urgent need to raise our productive capacity.

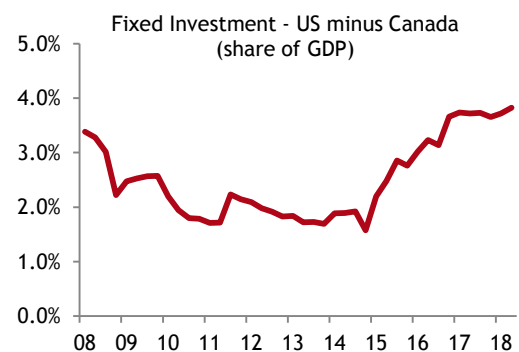
But those CEOs will be quick to tell you that the removal of trade uncertainty is a necessary, but not sufficient condition to generate a new wave of investment that is needed to close the investment gap with the US. And that gap is widening (Chart). As of the second quarter of the year, business fixed investment in Canada accounted for 9.8% of GDP — almost 4 percentage points below the equivalent share south of the border. In fact, that gap is currently at an eighteen-year high.

Leveling the playing field with the US requires much more than restoring trade certainty. Our corporate tax rate is now equivalent to that of the US — so we lost the advantage there. What's more, as we all know, the US magically doesn't suffer from global warming, but we do. So we will pay for carbon, they won't. But above all, the Trump Administration's new treatment of capital depreciation is a game-changer. The change replaces the 50% bonus depreciation with a 100% bonus depreciation schedule while expanding the eligibility to new and used equipment.

Now, how effective was the accelerated depreciation schedule in boosting US business investment? Well, with so many other things happening at the same time it's simply impossible to quantify. What we do know is that in the first half of the year, US business spending rose by an annual rate of close to 8% — notably stronger than the 3.5% pace seen in 2017. Moreover, empirical research conducted to assess the impact of the 50% bonus depreciation program found that the policy worked to accelerate investment in eligible capital by an average of more than 5% a year. Given that the current program is for full first-year deductibility and is more broadly based, it's fair to assume that the impact might be even larger.

So for Canada the course of action is clear. With an average depreciation schedule of 20% per year (10% in the first year) the cash flow implications relative to a US counterpart are significant. We believe that Ottawa has little choice but to act on that front and to match, or at least come close to the US policy. In fact, we expect it to happen as early as the upcoming fall economic update.

Widening US-Canada Investment Gap



Source: Statistics Canada, BEA, CIBC



Week Ahead Calendar And Forecast

		CANADA			UNITED STATES			
		CIBC	Consensus	Prior		CIBC	Consensus	Prior
Monday October 15	9:00 AM EXISTING HOME SALES M/M 10:30 AM BoC Business Outlook and Senior Loan Officer Surveys	(Sep) (M)		0.9% ▲				
Tuesday October 16	AUCTION: 3-M BILLS \$5.0B, 6-M BILLS \$2.0B, 1-YR BILLS \$2.0B CASH MANAGEMENT BUYBACK (Nov'18 - Mar'20) - \$0.5B 8:30 AM INT'L SEC. TRANSACTIONS	(Aug) (M)		\$12.7B				
Wednesday October 17	AUCTION: 10-YR CANADAS \$3B 8:30 AM MANUFACTURING SHIPMENTS M/M	(Aug) (M)		0.9%				
Thursday October 18	8:30 AM ADP EMPLOYMENT CHANGE							
Friday October 19	8:30 AM RETAIL TRADE TOTAL M/M RETAIL TRADE EX-AUTO M/M CPI M/M CPI Y/Y CPI Core- Common Y/Y% CPI Core- Median Y/Y% CPI Core- Trim Y/Y%	(Aug) (H) (Aug) (H) (Sep) (H) (Sep) (H) (Sep) (M) (Sep) (M)		0.3% 0.9% -0.1% 2.8% 2.0% 2.1% 2.2%				
		SAAR = Seasonally Adjusted Annual Rate			H, M, L = High, Medium or Low Significance			Consensus Source: Bloomberg

UNITED STATES

AUCTION: 3-M BILLS \$48B, 6-M BILLS \$42B								
8:30 AM	RETAIL SALES M/M RETAIL SALES (X-AUTOS) M/M RETAIL SALES CONTROL GROUP M/M NEW YORK FED (EMPIRE)	(Sep) (H) (Sep) (H) (Sep) (H) (Oct) (M)		0.7% 0.4% 0.3% 0.1%				0.1% 0.3% 0.4% 19.0
10:00 AM	BUSINESS INVENTORIES M/M	(Aug) (L)		0.5%				0.6%
AUCTION: 4-WEEK BILLS \$40B (prev) AUCTION: 8-WEEK BILLS \$xx								
9:15 AM	INDUSTRIAL PRODUCTION M/M CAPACITY UTILIZATION	(Sep) (H) (Sep) (M)		0.3% 78.2%				0.4% 78.1%
10:00 AM	NAHB HOUSING INDEX	(Oct) (L)		67				67
4:00 PM	NET CAPITAL INFLOWS (TICS)	(Aug) (L)		\$74.8B				
7:00 AM	MBA-APPLICATIONS	(Oct 12) (L)		-1.7%				
8:30 AM	HOUSING STARTS SAAR BUILDING PERMITS SAAR	(Sep) (M) (Sep) (H)		1218K 1280K				1282K 1249K
2:00 PM	Minutes of Sep 26th FOMC Meeting							
8:30 AM	INITIAL CLAIMS CONTINUING CLAIMS PHILADELPHIA FED	(Oct 13) (M) (Oct 6) (L) (Oct) (M)		21.0				214K 1660K 22.9
10:00 AM	LEADING INDICATORS M/M	(Sep) (M)		0.5%				0.4%
2:00 PM	TREASURY BUDGET	(Sep) (L)		\$75.0B				-\$214.1B
Speaker: 12:15 PM Randal K. Quarles (Governor) Speaker: 9:05 AM James Bullard (President, St. Louis)								
10:00 AM	EXISTING HOME SALES SAAR	(Sep) (M)		5.31M				5.34M
Speaker: 12:00 PM Raphael Bostic (President, Atlanta) and on October 20 at 12:00 PM Speaker: 9:00 AM Rob Kaplan (Dallas, President)								

Week Ahead's Market Call

by Royce Mendes

In the US, data look set to disappoint even only modest expectations heading into the week. Hurricane activity likely provided a drag on core retail sales in September. Ditto for housing starts. Hours worked data on the factory and mining sectors suggest that industrial production barely made any gains in September. That will leave it up to the FOMC minutes and slate of Fed speakers to keep signaling that the funds rate is headed north of 3%, a view we don't share.

In Canada, it's a packed week for economic releases. The Bank of Canada's Business Outlook Survey will get things going on Monday. Results from the questionnaire may need to be taken with a grain of salt, given that the survey was conducted before the USMCA deal. Manufacturing sales will erase the gains seen in the prior month, while retail sales will barely make any progress ex-autos, continuing the slowdown we've seen in that sector over the past year. Combined with inflation readings that won't look much different from the last release, there's scope for end-2019 BoC expectations to continue the pullback that began this week.

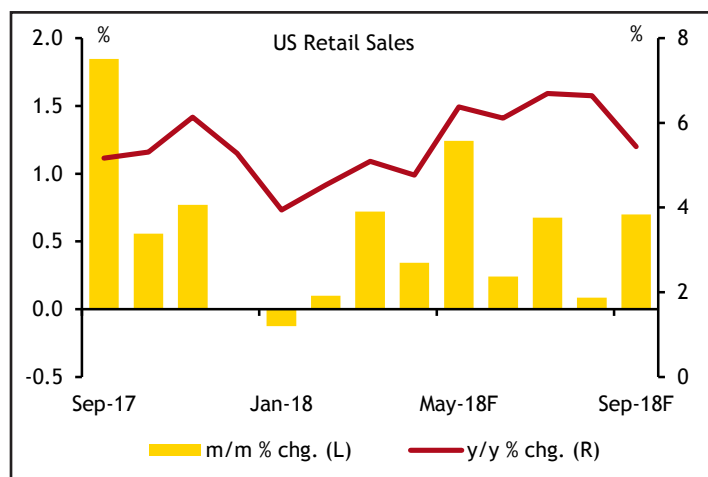
Week Ahead's Key Canadian Number:**Retail Trade—August**

(Friday, 8:30 a.m.)

Royce Mendes (416) 594-7354

	CIBC	Mkt	Prior
Retail Sales	0.3%	na	0.3%
Ex-Autos	0.2%	na	0.9%

After running at a torrid pace last year, growth in retail sales has moved into a lower gear. Early indications suggest that it was more of the same in August. According to unit auto sales data, dealerships will boost the headline number, but the overall retail sales reading still won't be anything to write home about. Ex-autos, a fall in gasoline prices likely weighed on receipts at filling stations, with other categories are expected to provide only a modest lift.



Forecast Implications—The days of heady household spending growth are fading into the past. Interest rate increases are working their way through the economy and suggest that only a couple more hikes will be needed to keep it from overheating.

Other Canadian Releases:**Consumer Price Index—September**

(Friday, 8:30 a.m.)

A slight decline in gasoline prices paired with an only trend-like increase in other categories will leave headline inflation tracking 2.7%, a tick below the prior month's print. While the Bank of Canada hasn't been much troubled by the above-target readings on headline inflation, given that they've largely been due to gasoline prices, rising core inflation could be a different story. The average of the Bank's three core measures are now a tick above 2% in August and likely remained marginally above target in the most recent month, highlighting the reason we expect rates to rise again later this month.

Manufacturing Shipments—August

(Wednesday, 8:30 a.m.)

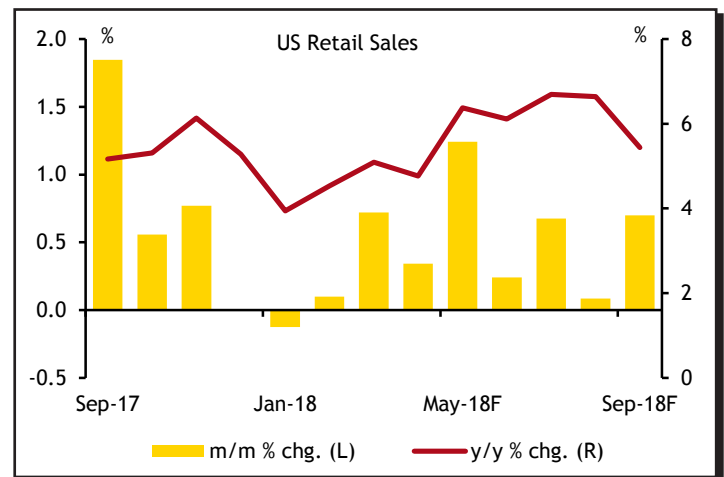
After taking a step forward in July, factory sales likely took a similar sized step back in August. Already-released export data combined with information on auto production and the currency all point to a decline of 1.0% in manufactured shipments. While Canadian factories still have a bit more room to run before bumping up against capacity constraints, already-high inventory levels could see production cool down, a negative for GDP.

Week Ahead's Key US Number:**Retail Sales—September**

(Monday, 8:30 a.m.)

Katherine Judge (416) 956-6527

	CIBC	Mkt	Prior
Retail Sales m/m	0.6%	0.7%	0.1%
Retail Sales – ex auto	0.3%	0.4%	0.3%
Retail Sales – control group	0.2%	0.4%	0.1%



Headline retail sales growth is tracking lower in Q3, in part due to price effects. However, a rebound in apparel prices in September following a soft prior month should support a rebound in nominal sales. With vehicle sales rising to their fastest pace this year, headline sales should advance by a robust 0.6%.

Excluding autos, a bump in building material sales in anticipation of hurricane Florence could have outweighed some of the decline in gas receipts resulting from a lower gasoline price. However, growth in core sales, which feeds more directly into GDP, could have been limited to 0.2% by Florence.

Forecast Implications—An acceleration in retail sales to end Q3 is consistent with solid consumption and provides a strong handoff for Q4. Indeed, the decline in core goods prices could help magnify gains in real terms, supporting above-3% growth in Q3. That said, soft spots in housing and autos indicate that higher rates are beginning to bite despite tighter labour markets and that should see consumption slow in the quarters ahead.

Market Impact—We are below consensus on the control group and that could be negative for the USD and positive for fixed income.

Other U.S. Releases:**Industrial Production & Cap. Utilization—September**

(Tuesday, 9:15 a.m.)

Industrial production likely advanced by a paltry 0.1% in September. Although unseasonably warm weather could have supported higher utilities output, production in the prior month was already elevated and should therefore limit gains in the index. At the same time, hours worked for production employees in both manufacturing and mining fell alongside an only marginal advance in rig counts. That should see capacity utilization creep ahead to 78.2%.

Housing Starts—September

(Thursday, 8:30 a.m.)

Housing activity has already showed signs of fatigue as higher interest rates hold back demand while labour and land shortages have challenged homebuilding. Indeed, building permits pulled back in the prior month and hurricane Florence should have added to the headwinds facing residential construction in September, sending the pace of housing starts down to 1187K. Building permits could have held up better if some of the softness in the Northeast and West subsided. However, housing data is likely to continue to reflect hurricane-induced volatility in the months ahead following the landfall of hurricane Michael this week.

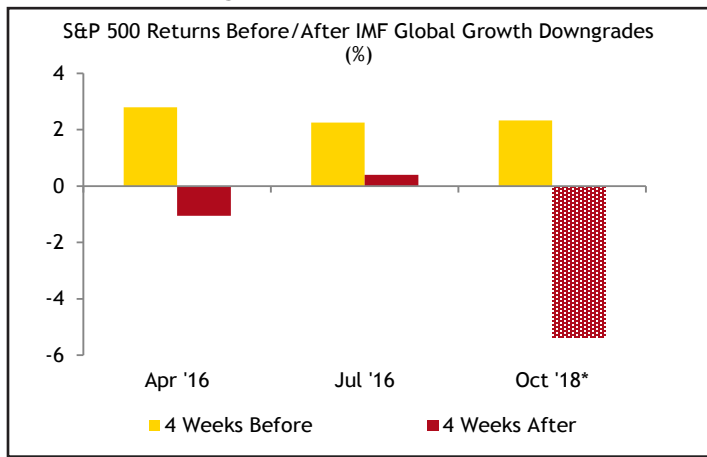
Equity Insights

Royce Mendes and Katherine Judge

A Real ‘Whodunit’

Equities are down and the hunt is on for who’s to blame. Many are pointing to the IMF’s recent downgrade of global growth, but the magnitude of stock losses this week is far more than after similar events in the past. So attention has turned elsewhere. President Trump has accused the Fed of raising interest rates too much, too fast. On the other hand, some investors say it’s Trump who has driven interest rates higher with fiscal stimulus and additional Treasury issuance. And then there’s the tit-for-tat trade war between the world’s two most important economies, China and the US. While a 5% decline is meaningful, the combination of slower global growth, rising rates and a budding trade war suggest that there could be more downside to equities if any is exacerbated.

IMF Forecast Downgrades Coincide with Market Softness



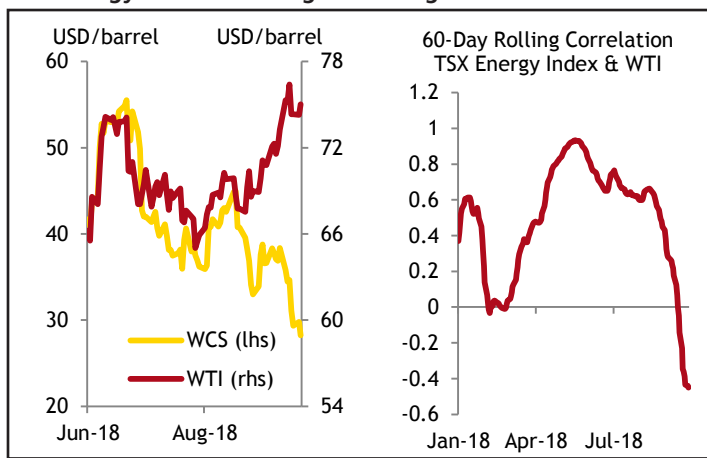
* only 1 week after available

Source: IMF, Bloomberg, CIBC

Breaking Up

Canadian oil prices have tumbled just as global benchmarks have been surpassing recent peaks, leaving the spread between WTI and WCS at its widest on record. Pipeline constraints are a well-known challenge for Canadian oil prices, but outages at US refineries designed for heavy oil have added to the headaches recently. As a result, the correlation between the TSX energy sub-index and the price of WTI is at its lowest point in years. While supply concerns are dominating the global discussion on oil prices, investors would be wise to be more attuned to local issues when determining when to jump back into Canadian energy stocks.

WCS Price Has Diverged from WTI (L), TSX Energy Stocks No Longer Tracking WTI

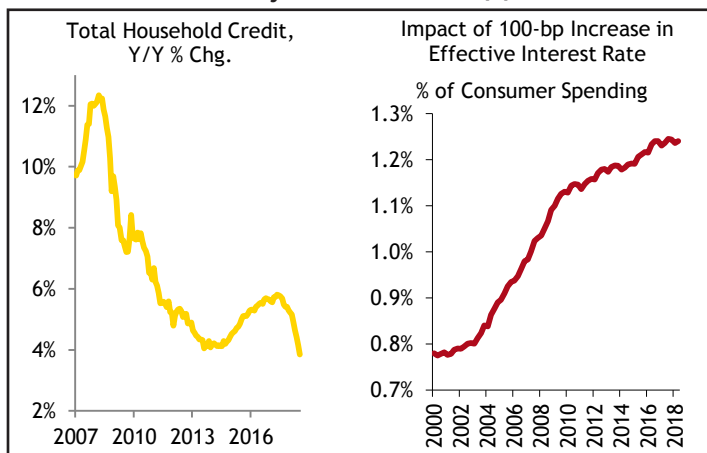


Source: Bloomberg, CIBC

Consumers Still Highly Exposed to Higher Rates

Tighter lending conditions and higher interest rates have done their part to limit the accumulation of credit by Canadian households. Indeed, credit growth is slower than it was during the recession. However, the previous run up in credit still has Canadians acutely sensitive to interest rate moves. Our updated analysis indicates that interest rate increases are still 50% more powerful in slowing consumption than they were at the beginning of the millennium. However, the effects could take time to show up as higher debt service costs gradually make their way through the economy. That could pose a headwind to consumer discretionary stocks next year despite the BoC taking an extended pause after January’s hike.

Slower Household Credit Growth (L), But Increased Sensitivity to Interest Rates (R)



Source: Statistics Canada, CIBC

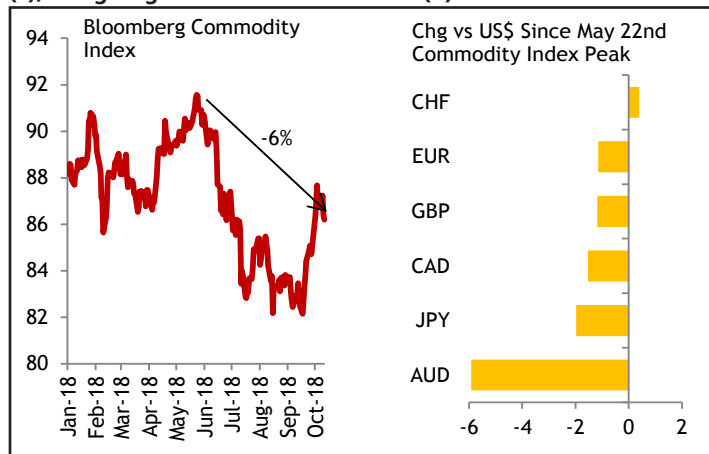
Currency Currents

Andrew Grantham

Global Growth Not a New Concern For FX

Equity markets have taken a beating this week thanks to concerns regarding global growth and rising interest rates. However, global growth concerns were playing out in commodity and FX markets earlier than that. Indeed, Bloomberg's commodity index peaked back in May, with the commodity-sensitive Aussie dollar underperforming by a wide margin. As such, this week's equity volatility hasn't resulted in the currency moves that may have been expected, but if it persists we could still see some further weakening of currencies such as the Aussie and loonie, and strength in safe havens such as JPY.

Commodity Prices Already Signaling Slower Global Growth (L), Weighing on Aussie in Particular (R)

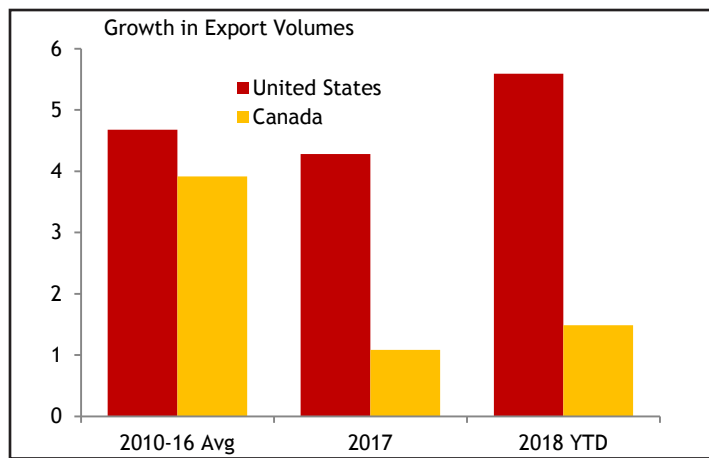


Source: Bloomberg, CIBC

Canada's Export Underperformance Continues

Although Canada's trade balance surprisingly turned to surplus last month, it wasn't because of good news on the export front. Indeed, in volume terms the year-to-date performance continues to look very sluggish particularly when compared to the US. In order to help exports become a bigger driver of growth, the C\$ will likely need to stay at or a little below current levels, otherwise overall economic growth could decelerate too much as consumer spending and housing cool.

Canada's Real Export Performance Still Underwhelming

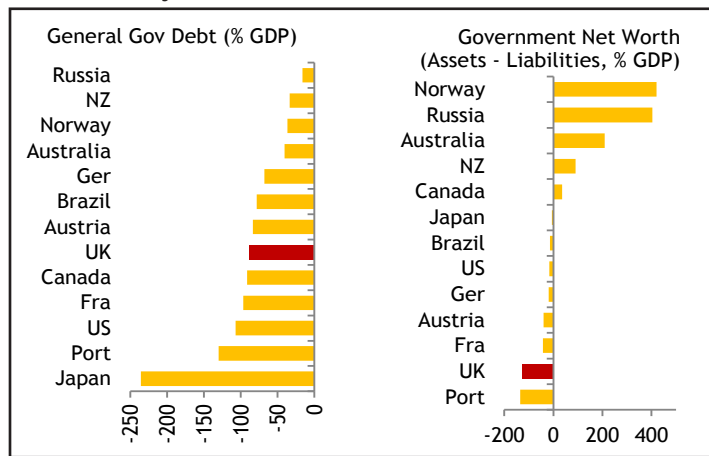


Source: Statistics Canada, BEA, CIBC

Maybe Not: Can UK Afford to Lighten Up on Fiscal Policy?

More accommodative fiscal policy, allowing interest rates to rise further from all-time lows, is a combination generally perceived as positive for currencies. In the midst of Brexit talks, UK PM Theresa May suggested that years of austerity could be coming to an end. However, while the UK's general government debt and deficit levels no longer stand out on an international basis, research by the IMF this week highlighted a concern for Britain's fiscal position. Because of privatizations and previous asset sales, the UK government no longer has assets that cover its liabilities. While not a near-term concern, that negative position could become a headwind to fiscal stimulus and GBP gains longer term.

UK Government Debt Doesn't Stand Out as High (L), But Asset Minus Liability Position Shows Weakness (R)



Source: IMF, CIBC

CANADIAN RELEASE AND EVENT DATES October/November 2018



MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
8	9	10	11	12
THANKSGIVING DAY (HOLIDAY) (MarketS Closed)	HOUSING STARTS 8:15 AM 000's (AR) TOTAL SINGLES JUL 202 54 AUG 199 52 SEP 189 53	BUILDING PERMITS (\$) 8:30 AM M M (RES) (NON-RES) JUN -4.5 5.9 JUL -2.0 -0.5 AUG -4.4 8.8	NEW HOUSING PRICE INDEX 8:30 AM	
15	16	17	18	19
Bank of Canada Business Outlook Survey	INT'L TRANSACTIONS IN SECURITIES C\$BN, NET 8:30 AM BONDS MONEY STOCKS TOT MARKET JUN 10.5 -1.7 1.4 10.3 JUL 11.1 -0.4 2.0 12.7 AUG	SURVEY OF MANUFACTURING 8:30 AM SHIPMENTS M Y JUN 1.3 6.9 JUL 0.9 10.5 AUG	ADP EMPLOYMENT SURVEY 8:30 AM	CPI 8:30 AM M Y JUL 0.5 3.0 AUG -0.1 2.8 SEP RETAIL TRADE 8:30 AM (Current\$) M Y JUN -0.1 4.0 JUL 0.3 3.7 AUG
22	23	24	25	26
WHOLESALE TRADE 8:30 AM		Bank of Canada Interest Rate Announcement Bank of Canada Monetary Policy Report Bank of Canada Governor Poloz & Sr. Dep. Gov. Wilkins speak at 11:15 AM ET	PAYROLL EMPLOYMENT, EARNINGS & HOURS 8:30 AM	
29	30	31	1	2
		GDP BY INDUSTRY 8:30 AM (2002\$) GDP IND.PROD. M M JUN 0.0 0.0 JUL 0.2 0.6 AUG INDUSTRIAL PRICES 8:30 AM M (NSA) Y JUL -0.2 6.7 AUG -0.5 5.8 SEP		LABOUR FORCE SURVEY 8:30 AM AVG EMPLOY UNEMP HRLY (HSHOLD) RATE EARN M Y % Y AUG -0.3 0.9 6.0 2.6 SEP 0.3 1.2 5.9 2.2 OCT MERCHANDISE TRADE 8:30 AM \$MN 12 MO. BALANCE JUL -189 -27,305 AUG 526 -23,907 SEP
5	6	7	8	9
INTERNATIONAL RESERVES 8:15 AM \$BN \$BN CHANGE LEVEL AUG -0.579 81.2 SEP -0.555 80.7 OCT	BUILDING PERMITS (\$) 8:30 AM M M (RES) (NON-RES) JUL -2.0 -0.5 AUG -4.4 8.8 SEP		HOUSING STARTS 8:15 AM 000's (AR) TOTAL SINGLES AUG 199 52 SEP 189 53 OCT NEW HOUSING PRICE INDEX 8:30 AM	

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U.S. RELEASE AND EVENT DATES October/November 2018



MONDAY	TUESDAY	WEDNESDAY	THURSDAY	FRIDAY
8 COLUMBUS DAY (HOLIDAY) (Treasury Markets Closed)	9 <i>BOT (9:00) REDBOOK (8:55)</i>	10 PPI 8:30 AM M (SA) Y (NSA) JUL 0.0 3.2 AUG -0.1 2.8 SEP 0.2 2.7 <i>3-, 10-Yr NOTE AUCTION</i>	11 CPI 8:30 AM M(SA) Y (NSA) JUL 0.2 2.9 AUG 0.2 2.7 SEP 0.1 2.3 TREASURY BUDGET 2:00 PM <i>30-Yr BOND AUCTION</i> <i>INITIAL JOBLESS CLAIMS (8:30)</i>	12 MICHIGAN SENTIMENT (P) 10:00 AM
15 RETAIL SALES 8:30 AM M Y JUL 0.7 6.7 AUG 0.1 6.6 SEP BUSINESS INVENTORIES 10:00 AM <i>30-Yr NOTE SETTLEMENT</i> <i>3, 10-Yr NOTE SETTLEMENT</i>	16 CAPACITY UTIL/IND. PROD. 9:15 AM LEV M Y JUL 77.9 0.4 4.1 AUG 78.1 0.4 4.8 SEP NET CAPITAL INFLOWS TICS 4:00 PM <i>BOT (9:00) REDBOOK (8:55)</i>	17 HOUSING STARTS 8:30 AM Mn. M/M JUL 1.174 -0.3 AUG 1.282 9.2 SEP FOMC Minutes	18 PHILADELPHIA FED INDEX 8:30 PM LEADING INDICATOR 10:00 AM <i>2, 5-, 7-Yr NOTE ANNOUNCE.</i> <i>INITIAL JOBLESS CLAIMS (8:30)</i>	19 EXISTING HOME SALES 10:00 AM
22	23 <i>2-Yr NOTE AUCTION</i> <i>BOT (9:00) REDBOOK (8:55)</i>	24 NEW HOME SALES 10:00 AM Beige Book <i>5-Yr NOTE AUCTION</i>	25 ADV. TRADE IN INTERNATIONAL GOODS 8:30 AM DURABLE GOODS ORDERS 8:30 AM M Y JUL -1.2 10.0 AUG 4.5 11.8 SEP <i>7-Yr NOTE AUCTION</i> <i>INITIAL JOBLESS CLAIMS (8:30)</i>	26 GDP 8:30 AM (AR) REAL IMPLICIT GDP DEFLECTOR 18:Q1(F) 2.2 2.2 18:Q2(P) 4.2 3.5 18:Q2(F) MICHIGAN SENTIMENT (F) 10:00 AM
29 PERS. INC & OUT. 8:30 AM SAVING INCOME CONS RATE M M AR JUL 0.3 0.5 6.6 AUG 0.3 0.3 6.6 SEP	30 S&P CORE LOGIC/CASE-SHILLERHOUSEPRICEINDEX 9:00 AM CONSUMER CONFIDENCE 10:00 AM <i>BOT (9:00) REDBOOK (8:55)</i>	31 ADP SURVEY 8:15 AM ECI 8:30 AM WAGES & TOTAL SALARY BEN. 18:Q1 0.8 0.9 0.7 18:Q2 0.6 0.5 0.9 18:Q3 CHICAGO PMI 9:45 AM <i>30-Yr BOND ANNOUNCEMENT</i> <i>3, 10-Yr NOTE ANNOUNCEMENT</i> <i>2, 5-, 7-Yr NOTE SETTLEMENT</i>	1 NON-FARM PRODUCTIVITY 8:30 AM Q/Q (AR) Y/Y 18:Q1 (F) 0.3 1.0 18:Q2 (F) 2.9 1.3 18:Q3 (A) ISM MFG SURVEY 10:00 AM COMP. PRICES INDEX INDEX AUG 61.3 72.1 SEP 59.8 66.9 OCT LIGHT VEHICLES SALES MIL (AR) Y AUG 16,620 1.0 SEP 17,364 -4.0 OCT <i>INITIAL JOBLESS CLAIMS (8:30)</i>	2 EMPLOY. SITUATION 8:30 AM NON- CIV AVG FARM UNEMP HRLY PAYROLL RATE EARN AUG 270 3.9 2.9 SEP 134 3.7 2.7 OCT GOODS & SERV. BALANCE (BOP) \$B 8:30 AM GDS SERV TOT JUL -73.2 23.1 -50.0 AUG -76.7 23.5 -53.2 SEP FACTORY ORDERS 10:00 AM M(SA) Y(NSA) JUL -0.5 9.2 AUG 2.3 10.0 SEP
5 ISM NON-MFG SURVEY 10:00 AM	6 <i>3-Yr NOTE AUCTION</i> <i>BOT (9:00) REDBOOK (8:55)</i>	7 CONSUMER CREDIT 3:00PM <i>10-Yr NOTE AUCTION</i>	8 FOMC Rate Decision <i>30-Yr BOND AUCTION</i> <i>INITIAL JOBLESS CLAIMS (8:30)</i>	9 PPI 8:30 AM M (SA) Y (NSA) AUG -0.1 2.8 SEP 0.2 2.7 OCT MICHIGAN SENTIMENT (P) 10:00 AM

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