TD Bank Financial Group

TD Economics

The Weekly Bottom Line

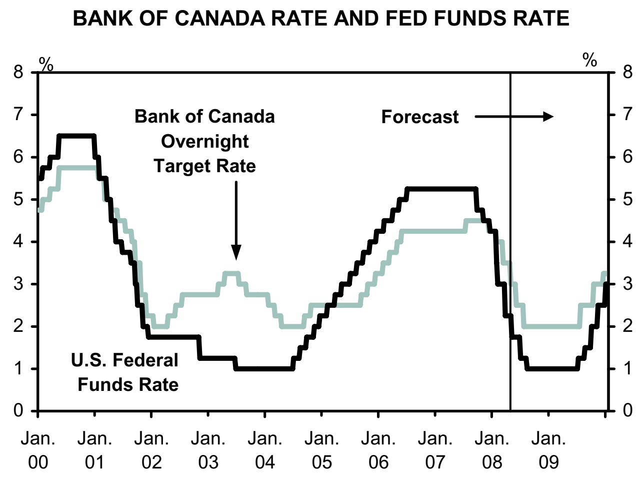
April 25, 2008

HIGHLIGHTS

- **Bank of Canada cuts rates by 50 basis points, more easing to come**
- **The Bank's Monetary Policy Report lays out a more dire outlook for the U.S. and Canada**
- **Signs of prolonged weakness in the U.S. economy continue with both new and existing home sales falling further this week**

The big news out this week was of course the Bank of Canada's interest rate announcement and accompanying Monetary Policy Report. On Tuesday, as expected, the Bank cut interest rates by 50 basis points for the second straight time, bringing the overnight rate to 3.0%. The Bank's accompanying statement maintained its bias towards further easing, saying, "some further monetary stimulus will likely be required to achieve the inflation target over the medium-term." As is usually the case, analysts were quick to jump on every change in wording and tone from previous statements for hints as to the timing and magnitude of further interest rate cuts. The Bank though is not new at this game and was as vague as any central bank should be. While some have questioned the intentional semi-opaqueness of central bank statements, they serve an important function in keeping analysts (such as this one) from running out of things to say about them in weekly commentaries. So without further ado, let's begin a brief discussion of the words "some" and "near" and the future direction of Canadian monetary policy:

Recent TD Economics Research
April 25, 2008 - Is the Credit Crunch Pushing the U.S. Federal Reserve to its Limit?
April 24, 2008 - Bank of Canada's Semi-Annual MPR
April 23, 2008 - The 2008 Alberta Budget
April 23, 2008 - Canadian Retail Sales
April 22, 2008 - Bank of Canada Interest Rate Decision



Actual data to Apr. 22, 2008; Forecast by TD Economics as at March 2008; Source: Bank of Canada, U.S. Federal Reserve Board

On "some" and "near"

One of the subtle changes to make its way into the Bank's April 22nd communiqué was the qualifying word "some" before the statement "further monetary stimulus is likely to be required…" The word "some" may be one of the most ambiguous words in the English language. By definition it is an "unknown, undetermined, or unspecified unit or thing."[1] Nonetheless, when qualifying *some* objects it does have considerable power. For example, the statement "give me freedom or give me death" would not be nearly as potent were it to read , "give me some freedom…." And to say, "or give me some death…" well, you get the point. In the view of this analyst, the part to focus on in the Bank's statement is the "further monetary stimulus" part. The "some" in this context simply means something more than nothing.

The other interesting wording change to make it into the Bank's statement was not an addition but a deletion. That is, where in their March communiqué the Bank said, "further monetary stimulus is likely to be required *in the near term*," this time they axed the "near term" part. Well, we must admit, *near* in this case, is much less ambiguous than *some* and the Bank seems to be trying to keep us guessing as to exactly when they will cut interest rates. In addition, if removing "near term" didn't make things clear as mud then the statement: "the timing of any further monetary stimulus will depend on the evolution of the global economy and domestic demand, and their impact on inflation in Canada," should have nailed the coffin shut. So where to from here? Well with that doosy, we seem to be close to drawing all the blood we can from the Bank's initial statement and we must now turn to the additional guidance provided by the Monetary Policy Report.

Of crystal balls and MPRs

The Bank's Monetary Policy Report (MPR) is key reading for anyone hoping to understand the Bank's outlook for the next three years. In it the Bank lays out their explicit forecasts for Canadian, U.S. and world economic growth and the future path of inflation. Once again in this edition of the MPR, the Bank lowered their forecasts for growth in nearly all areas. The Canadian economy is expected to grow by 1.4% this year and 2.4% in 2009, down from their January forecasts of 1.8% and 2.8% respectively. Net-exports will be the largest drag on economic growth, which follows from the Bank's downgraded view of U.S. and global economic prospects. This contrasts with our forecast of Canadian growth of 1.1% in 2008 and 1.8% in 2009. Admittedly, there is some upside risk to our 2008 view as the first quarter of this year appears to be on better standing than we had originally believed. However, this is likely only a postponement of the expected weakness and not a reprieve. A bigger difference between the Bank's view and our own is on our outlook for 2009. Furthermore, it is primarily in our longer term view of Canada's economic prospects where we believe the case for more monetary stimulus lies.

Digging a bit deeper for nuggets of truth in the MPR, we find the Bank's outlook for U.S. economic growth, upon which much of the outlook for both global and Canadian growth hinges. The U.S. economy, in the Bank's view, is now expected to contract through the first half of this year and to gradually recover over the second half of the year and into 2009, aided by the fiscal-stimulus. The Bank's explicit forecast for 2008 growth is for 1.0%, only a slight tick below our own forecast of 1.1%. The Bank then forecasts a recovery of growth to 1.7% in 2009. However, even with their expectation of improvement in 2009, the Bank is quite clear that conditions in housing and credit markets will remain an obstacle for U.S. prospects well into 2009. We believe that this analysis supports our more pessimistic view that the U.S. will grow by a more tepid 1.1% in 2009. Interestingly, the data to come out this week pointed to continued prolonged weakness in the one area of the U.S. economy that is a key harbinger for the future recovery of the broader economy: the housing market. Both existing home sales and new home sales came out this week and both underperformed market expectations. Worse still, the current inventories of unsold new and existing homes increased from the previous month, making further price declines a pretty sure bet. At current sales rates it will take 11 months to clear the inventory of unsold new homes and just under 10 months to clear existing homes.

All of this brings us back to what we can draw out of the Bank's statement and MPR as to the future path of monetary policy. In our opinion, looking at the substance of the Bank's arguments even more than their word choices, leads us to believe in an even weaker path for the Canadian economy over the medium-term. So while we take heed of the Bank's more cautious tone, our belief that the protracted weakness in the U.S. economy will result in an even weaker "evolution of the global economy and domestic demand" and hence explains the difference between our forecast for the Canadian economy of 1.8% in 2009 and the Bank's forecast of 2.4%.

Bottom line

The Bank of Canada ended their communiqué with a restatement of the guiding principles of the central bank, noting that the timing of future interest rate cuts will depend on the future path of global and domestic demand and its impact on inflation. In our view, things are going to get worse before they get any better and will necessitate continued aggressive action by the Bank of Canada in order to meet the Bank's objective of keeping inflation on a stable course over the medium-term.

James Marple, Economist
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Endnotes

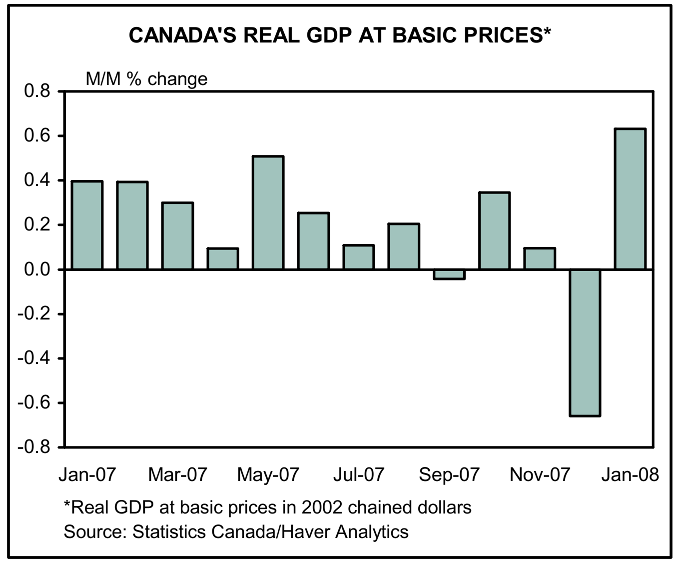
[1] "some." Merriam-Webster Online Dictionary. 2008. http://www.merriam-webster.com (25 Apr. 2008).

UPCOMING KEY ECONOMIC RELEASES

Canadian Real GDP - February

Release Date: April 30/08
January Result: +0.6%
TD Forecast: +0.2%
Consensus: +0.2%

We're expecting Canadian GDP to expand by 0.2% in February, returning to a more normal growth rate after a choppy December and January. For the second month in a row we expect to see some significant strength coming from the manufacturing sector, although it sill won't likely be enough to make up for the 3.4% M/M drop in activity that we saw in December. In fact, most export-intensive sectors should report healthy growth in February, as real exports expanded by 3.6%. On the other hand, we'll likely see weakness from both the wholesale and retail trade categories, as real wholesale sales fell by 2.0% and real retail sales fell by 0.7% in February. If anything, we'd guess that the risks to retail sales lie slightly to the downside, given the weak retail sales report for February. If Canadian consumers closed their wallets to retail goods, there is a chance that they held back spending in other sectors as well, potentially putting a damper on service-sector activity.



Jacqui Douglas 416-982-7784

U.S. Real GDP - Q1/08

Release Date: April 30/08
Q4 Result: 0.6%
TD Forecast: 0.5%
Consensus: 0.4%

First quarter GDP is expected to repeat the sluggish performance of the previous quarter and come in at an annualized pace of 0.5%. Final domestic demand will likely show an outright contraction led by considerable weakness in business fixed investment that will not be fully offset by an only slightly positive reading on consumer spending. Consumption of durables and non-durables likely contracted in the quarter offset only by continued growth in services. Weakness in residential construction seems to know no bounds and will once again subtract a full percentage point from overall GDP growth. Not wanting to be left out of the race to the bottom, non-residential construction looks to be joining its residential cousins and will also contract in the first quarter, leaving net exports and a rebound in inventory investment with the task of keeping overall growth out of negative territory.

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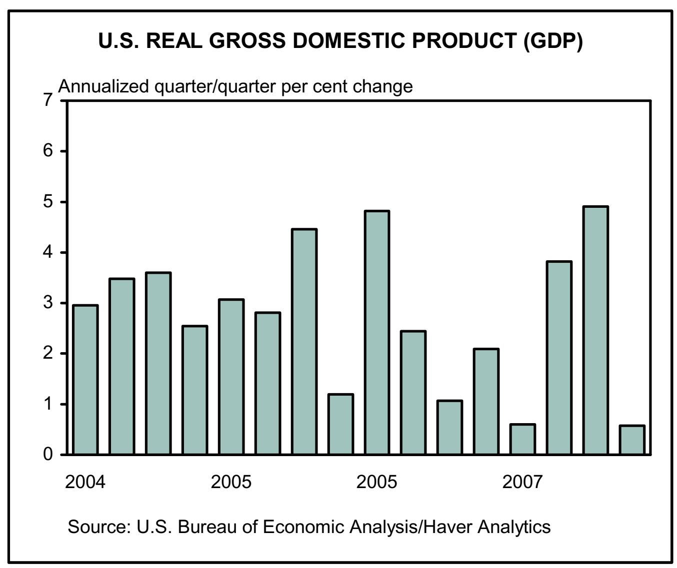
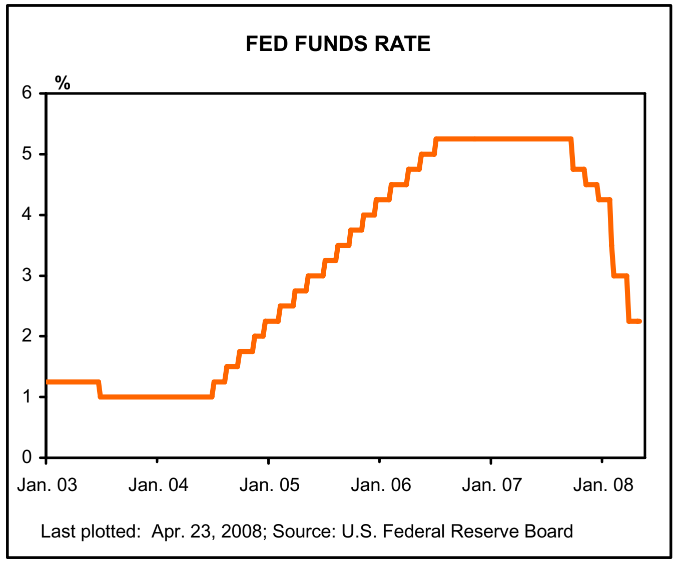


U.S. FOMC Interest Rate Decision

Release Date: April 30/08
Current Rate: 2.25%
TD Forecast: 1.75%
Consensus: 2.0%

Financial markets have calmed modestly since the March 18 FOMC decision to cut the federal funds rate by 75bps to 2.25%. However, since that meeting, the economic data continue to point to further deceleration in real economic activity. The housing market remains the nucleus of the downturn, and increasingly, consumers are growing more and more pessimistic as the labor market slack accelerates and food and energy prices remain on the boil thereby further eroding consumers' purchasing power. Anecdotal evidence contained in the Fed's last Beige Book indicated that the contraction in economic activity has hemorrhaged to even more districts than in March. The Beige Book released details that credit conditions remain generally tight and looking at credit spreads, there are only nascent signs that the credit market is responding to the resuscitation that the Fed has delivered via the many alternative liquidity measures. So against the background of continued signs that the economy is heading for recession, and a tight credit market, there is scope for the Fed to deliver additional stimulus. It is unlikely that inflation will hold the Fed back from what it needs to address on the economic growth side of the ledger. These factors underpin our view for another 50bps rate cut by the Fed, leaving the fed funds rate at 1.75%. The risk in this view tilts towards a 25bp cut. Ultimately, we think the Fed has further to go after the April meeting and look for a floor in the fed funds rate of 1.0% by the summer.

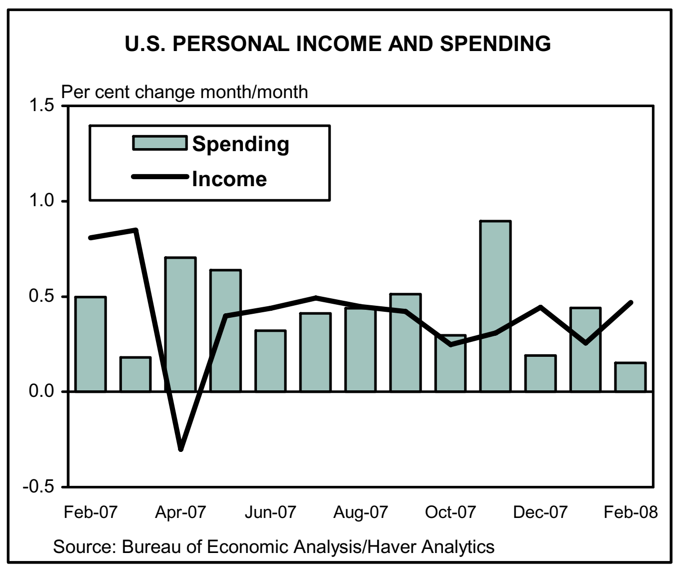


Charmaine Buskas 416 982 3297

U.S. Personal Income and Spending - March

Release Date: May 1/08
February Result: income +0.5%; spending +0.1%; core PCE deflator +0.1% M/M, 2.0% Y/Y
TD Forecast: income +0.4% ; spending +0.2%; core PCE deflator +0.1% M/M, 2.0% Y/Y
Consensus: income +0.4% ; spending +0.2%; core PCE deflator +0.1% M/M, 2.0% Y/Y

We're expecting to see U.S. income growth slow a little further in March, with a 0.4% M/M gain. While nonfarm payrolls have been falling for the last three months, both hours worked and wages recorded decent gains in March, which should support income. We'll be paying closer attention to real disposable personal income, as that's one of the series that the NBER uses to determine if/when a recession has started. On the spending side, we expect to see another month of moderate growth, with only a 0.2% increase. But, with gasoline prices up about 7% in March, the real number will once again be weaker, and will likely be flat or worse. As for the core PCE deflator, we expect to see another subdued 0.1% increase, given the weak gains that we saw in core CPI over February and March. However, due to base effects, the Y/Y rate for the core PCE deflator will likely remain unchanged at 2.0%.



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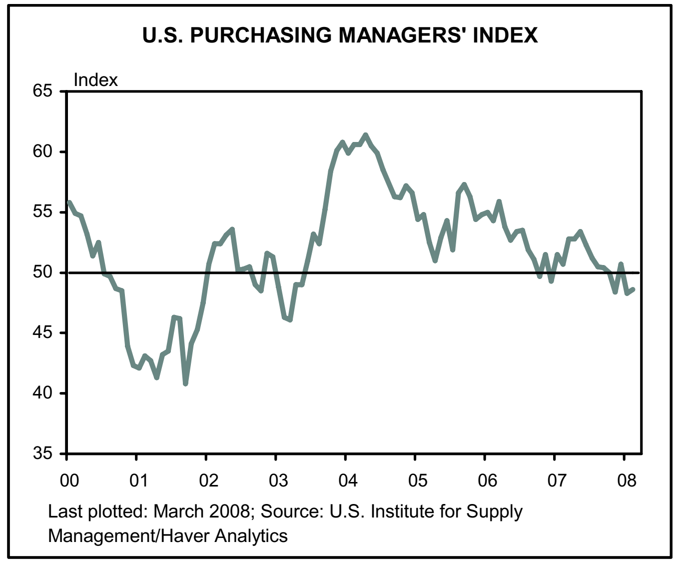
U.S. ISM Manufacturing Report - April

Release Date: May 1/08
March Result: 48.6
TD Forecast: 47.8
Consensus: 48.0

We're expecting to see the ISM manufacturing index drop to 47.8 in April from 48.6 in March, since the ISM index is somewhat stronger than other information on the manufacturing sector would suggest. For one, the new orders sub-index of the ISM has been sitting below 50 for four months now, suggesting that activity will decline going forward. In fact, at 46.5, the new orders sub-index for March was at its lowest level since October 2001. Furthermore, new orders of durable goods fell every single month in the first quarter of the year, indicating that demand for manufactured goods is waning. As for the regional Fed surveys, they seem to be pointing in opposite directions for April, with the Philly Fed weakening and the Empire Fed strengthening, so we can't glean much information there. Overall, we expect to see manufacturing conditions weaken going forward, but perhaps not quite as much as in past recessions, as a weak U.S. dollar will help to keep foreign demand for U.S. goods alive.



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U.S. Nonfarm Payrolls - April

Release Date: May 2/08
March Result: -80K; unemployment rate 5.1%
TD Forecast: -120K; unemployment rate 5.2%
Consensus: -78K; unemployment rate 5.2%

We're expecting to see the U.S. employment situation deteriorate further in April, with another 120K nonfarm payroll positions lost. We don't think that we've seen the worst of the job losses, by any means, and that the employment situation will get worse before it gets better. When the U.S. economy is in recession, which we believe is currently the case, we generally see much bigger job losses than the 80K per month or so that we've seen over the last few months. While the fact that jobless claims haven't accelerated too dramatically over the last month means that we probably won't yet see a -200K or -300K result in April, we think that the pace of job losses will pick up to some extent, and that it's just a matter of time until we see the bigger negative numbers. The unemployment rate in the U.S. is likely to rise another notch to 5.2% in April, since continuing jobless claims have continued to climb pretty steadily.

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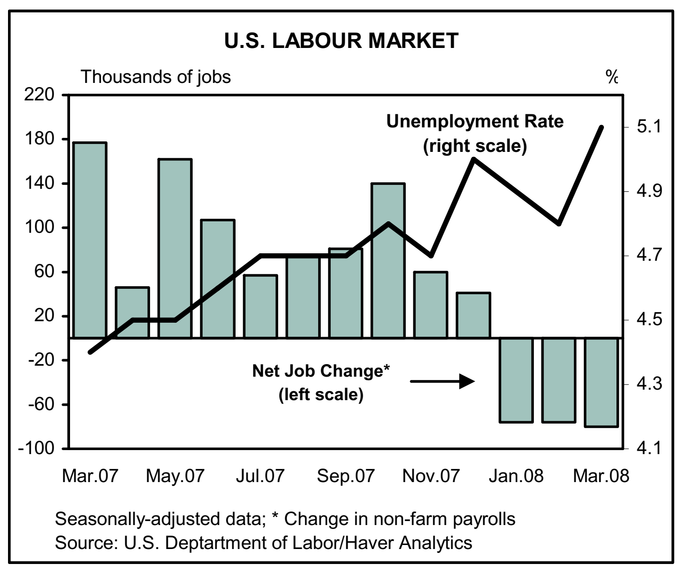

RECENT KEY ECONOMIC INDICATORS
April 21-25, 2008

Date	Economic Indicators	Data for	Units	Current	Prior	
	Canada					
Apr. 21	International Securities Transactions	Feb.	$C, blns	3.8	0.94	R▲
Apr. 22	*Bank of Canada interest rate announcement*	*22-Apr.*	*Overnight rate*	*3.00*	*3.50*	
Apr. 23	Retail Sales	Feb.	% change	-0.7	1.4	R▼
Apr. 23	Retail Sales - excl. autos	Feb.	% change	-0.3	1.1	R▼
Apr. 24	*BoC Monetary Policy Report Released*					
	United States					
Apr. 22	Richmond Fed Index	Apr.	Index	0.0	6.0	
Apr. 22	Existing Home Sales	Mar.	Millions	4.93	5.03	
Apr. 24	Durable Goods Orders	Mar.	% change	-0.3	-0.9	R▲
Apr. 24	Weekly Initial Jobless Claims	19-Apr.	Thousands	342.0	375.0	R▲
Apr. 24	New Home Sales	Mar.	Thousands	526.0	575.0	R▼

Source: Bloomberg, TD Economics

UPCOMING NORTH AMERICAN ECONOMIC CALENDAR
April 28-May 2, 2008

Release Date	Economic Indicators	Data for Period	Units	Consensus Forecast	Prior
	Canada				
Apr. 30	Industrial Product Price Index	Mar.	% change	1.0	0.1
Apr. 30	Raw Materials Price Index	Mar.	% change	2.0	0.5
Apr. 30	Real GDP at Basic Prices	Feb.	% change	0.2	0.6
Apr. 30	*BOC Governor Carney and Deputy Governor Jenkins appear before House of Commons Standing Committee on Finance*				
May 1	*BOC Governor Carney and Deputy Governor Jenkins appear before Senate Standing Committee on Banking, Trade and Commerce*				
	United States				
Apr. 28	*Richmond Fed officials to speak on Housing at University of Maryland*				
Apr. 29	S&P/CS Composite-20	Feb.	Y/Y % chg.	-12.0	-10.7
Apr. 29	Consumer Confidence	Apr.	Index	62.0	64.5
Apr. 30	ADP Employment Change	Apr.	Thousands	-60	8
Apr. 30	Real Gross Domestic Product (advance)	Q1-08	Ann. % chg.	0.4	0.6
Apr. 30	Chicago Purchasing Managers Index	Mar.	Index	48.0	48.2
Apr. 30	*FOMC Rate Decision*	*Apr. 30*	*Overnight Rate*	*2.00*	*2.25*
May 1	Personal Income	Mar.	% chg.	0.4	0.5
May 1	Personal Spending	Mar.	% chg.	0.2	0.1
May 1	PCE Deflator	Mar.	Y/Y % chg.	3.2	3.4
May 1	PCE Core	Mar.	Y/Y % chg.	2.0	2.0
May 1	Weekly Initial Jobless Claims	26-Apr.	Thousands	360.0	342.0
May 1	ISM Index (manufacturing)	Apr.	Index	48.0	48.6
May 1	Construction Spending	Mar.	% change	-0.6	-0.3
May 1	Total Vehicle Sales	Apr.	Millions	15.1	15.1
May 1	Domestic Vehicle Sales	Apr.	Millions	11.4	11.1
May 2	Change in Non-farm Payrolls	Mar.	Thousands	-78.0	-80.0
May 2	Unemployment Rate	Mar.	Per cent	5.2	5.1
May 2	Average Hourly Earnings	Mar.	% change	0.3	0.3
May 2	Factory Orders	Feb.	% change	0.2	-1.3

Source: Bloomberg, TD Economics

G-7 ECONOMIC RELEASES AND EVENTS

Date	Time*	Country	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
Apr. 27	19:50	Japan	Retail Trade	Mar.	% change	0.7	-0.9
Apr. 28	---	Germany	Consumer Price Index (prelim.)	Apr.	Y/Y % chg.	2.8	3.1
	17:45	*US*	*Richmond Fed officials to speak on Housing at University of Maryland*				
	18:45	NZ	Trade Balance	Mar.	NZ$, mlns	390.0	258.0
Apr. 29	3:40	France	Consumer Confidence Indicator	Apr.	Index	-37	-36
	4:00	EU-12	Purchasing Managers Index (Retail)	Apr.	Index	N/A	48.2
	4:00	Germany	Purchasing Managers Index (Retail)	Apr.	Index	N/A	51.5
	4:00	France	Purchasing Managers Index (Retail)	Apr.	Index	N/A	53.3
	9:00	U.S.	S&P/CS Composite-20	Feb.	Y/Y % chg.	-12.0	-10.7
	10:00	U.S.	Consumer Confidence	Apr.	Index	62.0	64.5
	19:30	Japan	Jobless Rate	Mar.	Per cent	3.9	3.9
	19:30	Japan	Workers' Household Spending	Mar.	Y/Y % chg.	0.5	0.0
	19:50	Japan	Industrial Production (prelim.)	Mar.	% change	-0.8	1.6
	---	*Japan*	*Bank of Japan Target Rate*		*Overnight rate*	*0.50*	*0.50*
	---	*Japan*	*Bank of Japan Monetary Policy meeting held*				
Apr. 30	0:00	Japan	Vehicle Production	Mar.	Y/Y % chg.	N/A	9.0
	1:00	Japan	Housing Starts	Mar.	Y/Y % chg.	-6.7	-5.0
	3:55	Germany	Unemployment Rate	Apr.	Per cent	7.8	7.8
	3:55	Germany	Unemployment Change	Apr.	Thousands	-30.0	-55.0
	5:00	EU	Consumer Price Index	Apr.	Y/Y % chg.	3.4	3.5
	5:00	EU	Unemployment Rate	Mar.	Per cent	7.1	7.1
	5:00	EU	Industrial Confidence Index	Apr.	Index	-1	0
	5:00	EU	Consumer Confidence Index	Apr.	Index	-13	-12
	5:00	EU	Business Climate Indicator	Apr.	Index	0.69	0.80
	5:00	EU	Economic Confidence Index	Apr.	Index	98.9	99.6
	5:00	EU	Services Confidence Index	Apr.	Index	9	9
	8:15	U.S.	ADP Employment Change	Apr.	Thousands	-60	8
	8:30	U.S.	Real Gross Domestic Product (advance)	Q1-08	Ann. % chg.	0.4	0.6
	8:30	Canada	Industrial Product Price Index	Mar.	% change	1.0	0.1
	8:30	Canada	Raw Materials Price Index	Mar.	% change	2.0	0.5
	8:30	Canada	Real GDP at Basic Prices	Feb.	% change	0.2	0.6
	9:45	U.S.	Chicago Purchasing Managers Index	Mar.	Index	48.0	48.2
	14:15	*U.S.*	*FOMC Rate Decision*	*Apr. 30*	*Overnight Rate*	*2.00*	*2.25*
	15:30	*Canada*	*BOC Governor Carney and Deputy Governor Jenkins appear before House of Commons Standing Committee on Finance*				
May 1	1:00	Japan	Vehicle Sales	Apr.	Y/Y % chg.	N/A	-3.3
	4:30	U.K.	Purchasing Managers Index (Man.)	Apr.	Index	50.8	51.3
	8:30	U.S.	Personal Income	Mar.	% chg.	0.4	0.5
	8:30	U.S.	Personal Spending	Mar.	% chg.	0.2	0.1
	8:30	U.S.	PCE Deflator	Mar.	Y/Y % chg.	3.2	3.4
	8:30	U.S.	PCE Core	Mar.	Y/Y % chg.	2.0	2.0
	8:30	U.S.	Weekly Initial Jobless Claims	26-Apr.	Thousands	360.0	342.0
	10:00	U.S.	ISM Index (manufacturing)	Apr.	Index	48.0	48.6
	10:00	U.S.	Construction Spending	Mar.	% change	-0.6	-0.3
	---	U.S.	Total Vehicle Sales	Apr.	Millions	15.1	15.1
	---	U.S.	Domestic Vehicle Sales	Apr.	Millions	11.4	11.1
	11:45	*Canada*	*BOC Governor Carney and Deputy Governor Jenkins appear before Senate Standing Committee on Banking, Trade and Commerce*				
	19:50	Japan	Monetary Base (YoY)	Apr.	Y/Y % chg.	n/a	0.0
	21:30	AU	Retail Sales	Mar.	% change	0.3	-0.1
May 2	2:00	Germany	Retail Sales	Mar.	% change	-2.3	-0.3
	8:30	U.S.	Change in Non-farm Payrolls	Mar.	Thousands	-78.0	-80.0
	8:30	U.S.	Unemployment Rate	Mar.	Per cent	5.2	5.1
	8:30	U.S.	Average Hourly Earnings	Mar.	% change	0.3	0.3
	10:00	U.S.	Factory Orders	Feb.	% change	0.2	-1.3