



TD Economics

The Weekly Bottom Line

May 2, 2008

HIGHLIGHTS

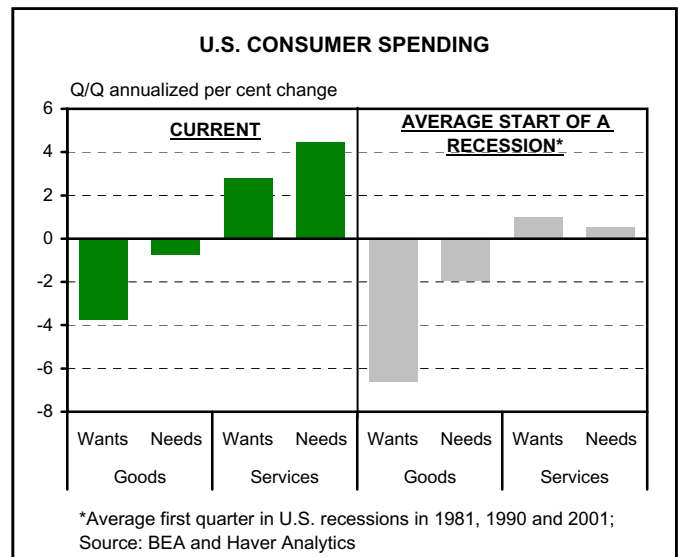
- U.S. economy grew 0.6% in the first quarter
- U.S. lost 20k jobs in April, less than expected
- Fed cuts a quarter-point; sees risks balanced

As the Oracle of Omaha prepares to meet with shareholders, we are left to sift through this week's plethora of data in order to prophesize what is to come for the U.S. economy. We have dispensed with the crystal balls, have left our dark robes at home, and require no secret handshakes or Gregorian chants in order to attend. Consuming the eye of newt and toe of frog is optional.

A touch of GDP

The U.S. economy maintained its 0.6% pace from the last quarter of 2007 through the first quarter of 2008. On face value, one may say the U.S. economy got no worse. The details, however, were less than convincing. The pace of decline in residential construction accelerated further, and was joined by new contractions in both non-residential construction and business investment. Were it not for an accumulation of inventories – businesses restocking shelves and producers resupplying inputs – the U.S. economy would have contracted by 0.2%. Increasing business capacity would be completely natural if there was an expectation the economy were about to turn a corner.

However, consumer spending growth slowed from 2.3% to just 1.0%, the slowest quarterly gain in over a decade. Perhaps consumers are waiting for their stimulus checks from the Treasury – the first of which were sent out this week and will continue through mid-July. Consumers are



losing about \$10bn per month in spending power just from the loss of mortgage wealth alone. The checks will add about \$10-12bn per month in spending power – but will only last for the next three to four months. So retailers could be gearing up for a short-term spending spree.

In our chart above, we have broken out U.S. consumer spending between goods and services, as well as between wants (cars, televisions, etc.) and needs (food, energy, bills, etc.). All four categories are outperforming the typical start of a U.S. recession. Goods purchases are falling across the board, but only at about half the pace typically seen at the start of a recession. Even more impressively, service growth is expanding at more than twice its usual pace for wants and eight times the usual pace for needs.

Since spending on consumer services constitutes 40 per cent of the U.S. economy, the question is whether this can be sustained. Well, one-quarter of consumer services (one-tenth of the U.S. economy) is rent (and its equivalent for homeowners). One result of increasing home foreclosures and retrenchment in construction has been falling vacancy rates among rental units. So the worsening housing market has actually provided some support for this component of GDP. However, in the last two recessions, there

Recent TD Economics Research

May 2, 2008 - U.S. Nonfarm Payrolls Commentary
 April 30, 2008 - Canadian Real GDP Commentary
 April 29, 2008 - Ontario Poised To Collect Equalization In 2010-11
 April 29, 2008 - Canadian Job Market To Be More Sedate In 2008

was a lag of about 12 months between the worst declines in residential construction and initial declines in this rental component. In the 1980s housing crash, the lag was even shorter. Adding to these risks, one-in-ten dollars of consumer services spending is household operations – gas, electric, sewage, phone, etc. – and the generally close relationship between this component and residential construction has never been more strained. Year-over-year declines of over 20% in home construction typically translate into 5% declines in household operations spending, which is now posting 5% y/y gains. With the potential for further foreclosures, and with hefty demands for utilities likely to ease after a bad winter across much of the U.S., the risks for this component lie squarely on the downside.

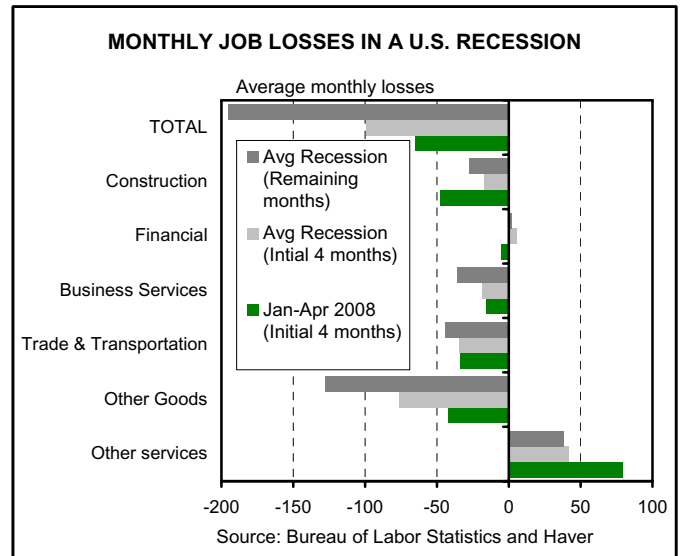
A dash of jobs

But ultimately, as goes the labour market, so goes the consumer. The U.S. economy shed just 20k jobs in April – one-quarter of the market's expectation – and the unemployment rate fell from 5.1% to 5.0%. The chart across compares the job losses over the last four months with the average in the last three U.S. recessions. At the aggregate, we have been averaging just 65k lost jobs per month, less than the 100k that would be typical. Losses in construction and financial services have been ugly – no surprise given they are at the heart of the current problems. But weaknesses have leaked into the business services, trade (retail and wholesale) and transportation sectors leaving them just as bad as in past recessions. Manufacturing and mining (Other Goods) have seen just half the recessionary level of average monthly job losses, while the pace of job gains in other services (health, education, IT, hospitality, etc.) has been twice the usual pace.

In a typical recession, the total monthly job losses tend to double from this point forward. Moreover, while every sector covered here tends to worsen in the remaining months of the recession, manufacturing and business services tend to be the hardest hit. The ISM manufacturing survey pointed to further weakness to come in this sector, but the weak dollar – by boosting exports – is likely to continue to help mitigate job losses here to some extent. For business services, the losses of temporary workers, which have constituted all of the job losses to date in this sector, tend to be followed by even larger losses in full-time staff as economic weakness continues and may offer a hint of the economy's health as we move forward.

The blind-worm's sting

The Federal Reserve this week cut interest rates an



additional quarter point, bringing the fed funds rate to 2.00%. Their statement generally left their descriptions unchanged for the economy (negative) and inflation (uncertain with a touch of hope). They did remove their mention of downside risks, which could imply they feel the level of interest rates is appropriate to balance the desire for moderate economic growth in the future with the risk of stoking inflation. In the near term, we may see the Fed pause to see how the economy reacts to 325bps of interest rate cuts over the last eight months – as well as \$100bn in tax rebate checks. However, 325bps in interest rate cuts have translated into less than 75bps in cuts to 30-year mortgage rates and less than 25bps in cuts to rates on new car loans. We fear further economic weakness will warrant more easing, bringing the target rate to 1.25% by year-end. The Fed on Friday announced an expansion of liquidity operations aimed at increasing the pass-through into lower consumer loan rates, but they have yet to find the right mix of ingredients in their cauldron to cure what ails the economy.

The economic environment in the U.S. is as clear as mud. There are no clear precedents for when the financial market problems will dissipate and exactly how they will continue to bleed into the U.S. and global economy. For instance, the Canadian economy contracted for the second time in three months in February, with growing weakness in the trade and transportation sectors. As a testament to the U.S. spill-over effect, the predominant areas of weakness in the Canadian economy remain goods sectors dependant on U.S. demand. The worst still remains contained within the U.S.

Richard Kelly, Senior Economist
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UPCOMING KEY ECONOMIC RELEASES

Canadian Housing Starts - April

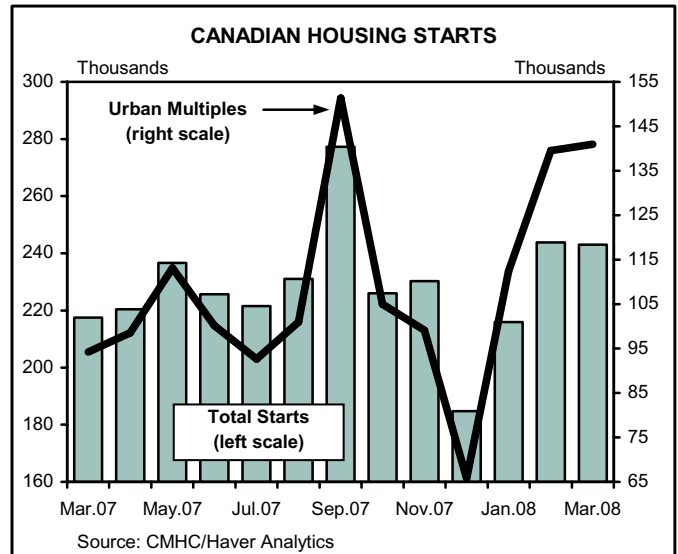
Release Date: May 8/08

March Result: 243K

TD Forecast: 210K

Consensus: 225K

We're expecting to see Canadian housing starts to soften rather significantly in April to only 210K. Housing starts have been incredibly strong for the last three months, but we think that they've been too strong, and that they're bound to come back to earth, particularly in the multi-unit segment. For instance, in January and February of this year, we saw the first back-to-back double-digit monthly increases in starts since the spring of 1991, when the housing sector was recovering from a housing crash. It's not normal to see that kind of strength towards the end of a housing boom. Furthermore, the quantity of building permits issued has declined since peaking last summer, which means that building activity should start slowing going forward. All in all, while we're almost certainly not going to see a housing downturn that's even comparable to what's



happening in the U.S., we do expect to see residential construction slow to a more sustainable pace.

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Canadian Employment - April

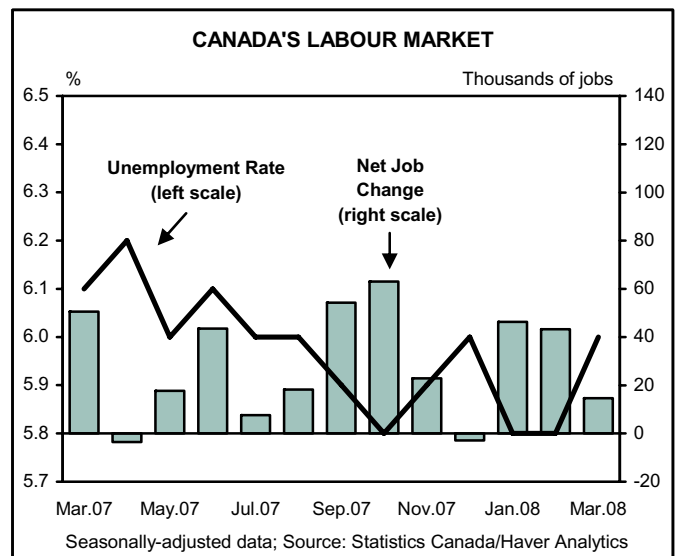
Release Date: May 9/08

March Result: +14.6K; unemployment rate 6.0%

TD Forecast: 8K; unemployment rate 6.0%

Consensus: 10K; unemployment rate 6.0%

We're expecting to see Canadian employment growth continue along its slower path in April, with only an 8K gain. With the Canadian economy having grown by less than 1.0% annualized in the fourth quarter of 2007, and likely in the first quarter of 2008 as well, we don't see a lot of need for Canadian companies to continue on their recent hiring spree. And given the uncertainty around the Canadian economy going forward, and just how badly it is going to get hurt by the U.S. recession, firms will likely want to scale back the pace of hiring and adopt a more cautious approach. The unemployment rate in Canada should remain unchanged at 6.0%.



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Canadian Int'l Merchandise Trade - March

Release Date: May 9/08

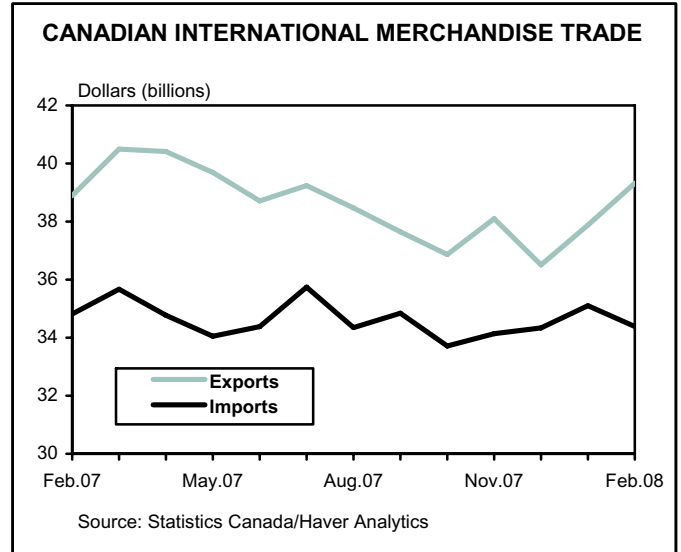
February Result: \$4.9B

TD Forecast: \$4.2B

Consensus: \$4.5B

We're expecting to see the Canadian trade balance fall from \$5.0B in February to \$4.2B in March. In February, the huge increase in the trade balance came partly from a big increase in exports, and a drop in imports, and we expect both those trends to reverse in March. On the export side, we're expecting to see a moderate 0.5% fall, but for real exports to fare much worse as rising commodity prices will be boosting the nominal figure. On the import side we're expecting to see a 1.5% rebound as the energy products category, which declined by nearly 20% in February, bounces back in March. Going forward, we expect to see further weakness in exports, although the headline figures may look better than they really are if commodity prices continue to increase.

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RECENT KEY ECONOMIC INDICATORS

April 28-May 2, 2008

Date	Economic Indicators	Data for	Units	Current	Prior	
Canada						
Apr. 30	Industrial Product Price Index	Mar.	% change	1.7	0.2	R ▲
Apr. 30	Raw Materials Price Index	Mar.	% change	6.6	0.6	R ▲
Apr. 30	Real GDP at Basic Prices	Feb.	% change	-0.2	0.6	
United States						
Apr. 29	S&P/CS Composite-20	Feb.	Y/Y % chg.	-12.7	-10.7	
Apr. 29	Consumer Confidence	Apr.	Index	62.3	65.9	R ▲
Apr. 30	ADP Employment Change	Apr.	Thousands	10	3	R ▼
Apr. 30	Real Gross Domestic Product (advance)	Q1-08	Ann. % chg.	0.6	0.6	
Apr. 30	Chicago Purchasing Managers Index	Mar.	Index	48.3	48.2	
Apr. 30	<i>FOMC Rate Decision</i>	<i>Apr. 30</i>	<i>Overnight Rate</i>	<i>2.00</i>	<i>2.25</i>	
May 1	Personal Income	Mar.	% chg.	0.3	0.5	
May 1	Personal Spending	Mar.	% chg.	0.4	0.1	
May 1	PCE Deflator	Mar.	Y/Y % chg.	3.2	3.4	
May 1	PCE Core	Mar.	Y/Y % chg.	2.1	2.0	
May 1	Weekly Initial Jobless Claims	26-Apr.	Thousands	380.0	345.0	R ▲
May 1	ISM Index (manufacturing)	Apr.	Index	48.6	48.6	
May 1	Construction Spending	Mar.	% change	-1.1	0.4	R ▲
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	-20.0	-81.0	R ▼
May 2	Unemployment Rate	Mar.	Per cent	5.0	5.1	
May 2	Average Hourly Earnings	Mar.	% change	0.1	0.3	
May 2	Factory Orders	Feb.	% change	0.2	-1.3	

Source: Bloomberg, TD Economics

UPCOMING NORTH AMERICAN ECONOMIC CALENDAR

May 5-May 9, 2008

Release Date	Economic Indicators	Data for Period	Units	Consensus Forecast	Prior
Canada					
May 5	<i>BOC Deputy Governor Murray speaks on exchange rate pass-through at StatsCan Socio-Economic Conference</i>				
May 6	Building Permits	Mar.	% change	1.2	-1.0
May 6	Ivey Purchasing Managers Index	Apr.	Index	55.0	59.0
May 8	Housing Starts	Apr.	Thousands	225.0	243.0
May 9	Unemployment Rate	Apr.	Per cent	6.0	6.0
May 9	Net Change in Employment	Apr.	Thousands	10.0	14.6
May 9	International Merchandise Trade Balance	Mar.	C\$, blns	4.5	4.9
United States					
May 5	ISM Non-Manufacturing	Apr.	Index	49.5	49.6
May 5	<i>Fed Chairman Bernanke speaks on mortgage foreclosures at Columbia's 32nd annual dinner</i>				
May 6	<i>Kansas City Fed President Hoenig speaks on market risk and policy to Economic Club of Colorado</i>				
May 7	Non-farm Productivity (prelim.)	Q1-08	Ann. % chg.	1.6	1.9
May 7	Unit Labour Costs (prelim.)	Q1-08	Ann. % chg.	2.5	2.6
May 7	<i>Fed Governor Kroszner speaks on foreclosures and neighbourhood stabilization at Neighborworks America Symposium</i>				
May 8	Weekly Initial Jobless Claims	3-May	Thousands	375.0	380.0
May 8	Wholesale Inventories	Mar.	% Chg.	0.5	1.1
May 8	<i>Former Fed Chairman Greenspan gives keynote address at the Alternative Public Strategies Conference in NY</i>				
May 9	Trade Balance	Mar.	US\$, blns	-61.4	-62.3

Source: Bloomberg, TD Economics

G-7 ECONOMIC RELEASES AND EVENTS

Date	Time*	Country	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period	
May 5	8:45	Canada	<i>BOC Deputy Governor Murray speaks on exchange rate pass-through at StatsCan Socio-Economic Conference</i>					
	10:00	U.S.	ISM Non-Manufacturing	Apr.	Index	49.5	49.6	
	20:30	U.S.	<i>Fed Chairman Bernanke speaks on mortgage foreclosures at Columbia's 32nd annual dinner</i>					
	20:30	AU	Trade Balance	Mar.	AU, blns	-2.9	-3.3	
May 6	4:00	EU	Purchasing Managers Index (Ser.)	Apr.	Index	51.8	51.8	
	4:00	France	Purchasing Managers Index (Ser.)	Apr.	Index	54.0	54.0	
	4:30	Germany	Purchasing Managers Index (Ser.)	Apr.	Index	54.6	54.6	
	4:30	U.K.	Purchasing Managers Index (Ser.)	Apr.	Index	51.7	52.1	
	5:00	EU	Euro-Zone PPI	Mar.	% change	0.7	0.6	
	8:30	Canada	Building Permits	Mar.	% change	1.2	-1.0	
	10:00	Canada	Ivey Purchasing Managers Index	Apr.	Index	55.0	59.0	
	21:30	U.S.	<i>Kansas City Fed President Hoenig speaks on market risk and policy to Economic Club of Colorado</i>					
22:30	AU	RBA Cash Target	7-May	Cash Rate	7.25	7.25		
May 7	2:45	France	Trade Balance	Mar.	Eur\$, blns	n/a	-2.8	
	4:30	U.K.	Industrial Production	Mar.	% Chg.	-0.1	0.3	
	4:30	U.K.	Manufacturing Production	Mar.	% Chg.	0.0	0.4	
	5:00	EU	Retail Sales	Mar.	% change	0.3	-0.5	
	6:00	Germany	Factory Orders	Mar.	% change	0.2	-0.5	
	8:30	U.S.	Non-farm Productivity (prelim.)	Q1-08	Ann. % chg.	1.6	1.9	
	8:30	U.S.	Unit Labour Costs (prelim.)	Q1-08	Ann. % chg.	2.5	2.6	
	8:45	U.S.	<i>Fed Governor Kroszner speaks on foreclosures and neighbourhood stabilization at Neighborworks America Symposium</i>					
	18:45	NZ	Unemployment Rate	Q1-08	Per cent	3.5	3.4	
	21:30	AU	Unemployment Rate	Apr.	Per cent	4.1	4.1	
21:30	AU	Net Change in Employment	Apr.	Thousands	10.0	14.8		
May 8	2:00	Germany	Trade Balance	Mar.	Eur, blns	17.0	16.9	
	2:00	Germany	Current Account Balance	Mar.	Eur, blns	n/a	15.4	
	6:00	Germany	Industrial Production	Mar.	% Chg.	-0.5	0.4	
	7:00	U.K.	<i>Bank of England rate announcement</i>	8-May	<i>Base rate</i>	5.00	5.00	
	7:45	EU	<i>European Central Bank rate announcement</i>	8-May	<i>Refin. rate</i>	4.00	4.00	
	8:15	Canada	Housing Starts	Apr.	Thousands	225.0	243.0	
	8:30	U.S.	Weekly Initial Jobless Claims	3-May	Thousands	375.0	380.0	
	10:00	U.S.	Wholesale Inventories	Mar.	% Chg.	0.5	1.1	
12:30	U.S.	<i>Former Fed Chairman Greenspan gives keynote address at the Alternative Public Strategies Conference in NY</i>						
May 9	1:00	Japan	Leading Economic Index (prelim.)	Mar.	Index	20.0	54.5	
	1:00	Japan	Coincident Index (prelim.)	Mar.	Index	33.3	70.0	
	2:45	France	Industrial Production	Mar.	% Chg.	n/a	0.3	
	2:45	France	Manufacturing Production	Mar.	% Chg.	n/a	0.3	
	7:00	Canada	Unemployment Rate	Apr.	Per cent	6.0	6.0	
	7:00	Canada	Net Change in Employment	Apr.	Thousands	10.0	14.6	
	8:30	U.S.	Trade Balance	Mar.	US\$, blns	-61.4	-62.3	
	8:30	Canada	International Merchandise Trade Balance	Mar.	C\$, blns	4.5	4.9	

* Eastern Standard Time; Sources: Bloomberg, TD Economics

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