



**Bank
Financial
Group**

The Weekly Bottom Line

November 20, 2009

TD Economics
www.td.com/economics

HIGHLIGHTS OF THE WEEK

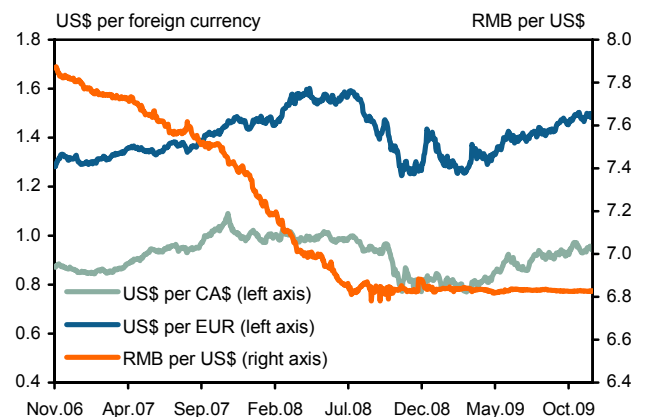
- U.S. industrial production falls by 0.1% in October M/M but still poised for strong growth in the fourth quarter.
- U.S. housing starts fall by 10.6% M/M in October, reversing somewhat the strong rebound seen through the third quarter.
- U.S. headline inflation rested at -0.2% Y/Y in October, poised to turn positive again next month, while core inflation has remained stickier than the spare capacity in the economy might suggest.
- Bernanke's speech makes rare comments about the U.S. dollar, saying that the Fed is watching it "closely" and speaking to the strong dollar that more typically is made by the U.S. Treasury.
- As base-year effects reverse, Canadian headline CPI inflation for October rises to 0.1% Y/Y from -0.9% Y/Y. Despite economic slack, core inflation jumps to 1.8% Y/Y from 1.5% Y/Y – though a slowdown in core prices is expected in coming months.
- Confirming expectations for output growth in September, Canadian manufacturing shipments rose 1.4% M/M in September, and the inventory-to-shipments ratio abated. However, Canada's inventory contraction continues.
- At odds with the broader economy, Canadian existing homes sales rose a further 5.1% M/M to 45.8k units in October, following the 3.0% M/M in September, now up 41.5% Y/Y.
- Growth in the average price of resale homes accelerated to 20.7% Y/Y in October from 13.7% Y/Y in September, and, controlling for the geography of sales, prices grew 14.0% Y/Y in October, up from 9.3% Y/Y in September.

THIS WEEK IN THE MARKETS

	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	1089	1093	1110	677
S&P/TSX Comp.	11513	11408	11653	7567
DAX	5678	5687	5854	3666
FTSE 100	5265	5296	5383	3512
Nikkei	9498	9770	10640	7055
Fixed Income Yields				
U.S. 10-yr Treasury	3.35	3.42	3.95	2.05
Canada 10-yr Bond	3.37	3.48	3.64	2.56
Germany 10-yr Bund	3.27	3.38	3.72	2.89
UK 10-yr Gilt	3.64	3.80	4.02	2.95
Japan 10-yr Bond	1.31	1.35	1.56	1.17
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.93	0.95	0.98	0.77
Euro (USD per EUR)	1.48	1.49	1.50	1.25
Pound (USD per GBP)	1.65	1.67	1.70	1.38
Yen (JPY per USD)	89.0	89.7	101.0	87.2
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	76.6	76.4	81.0	31.4
Natural Gas (\$US/MMBtu)	3.55	2.44	6.84	1.88
Copper (\$US/met. tonne)	6766.8	6500.8	6855.5	2809.5
Gold (\$US/roy oz.)	1138.2	1118.7	1145.5	745.1

*as of 11am Friday, **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price), Copper-LME Grade A, Gold-London Gold Bullion; Source: Bloomberg

CURRENCY MARKETS



Source: Federal Reserve Bank

GLOBAL OFFICIAL POLICY RATE TARGETS

	Current Target
Federal Reserve (Fed Funds Rate)	0 - 0.25%
Bank of Canada (Overnight Rate)	0.25%
European Central Bank (Refi Rate)	1.00%
Bank of England (Repo Rate)	0.50%
Bank of Japan (Overnight Rate)	0.10%

Source: Central Banks, Haver Analytics

UNITED STATES – INFLATION FAITH

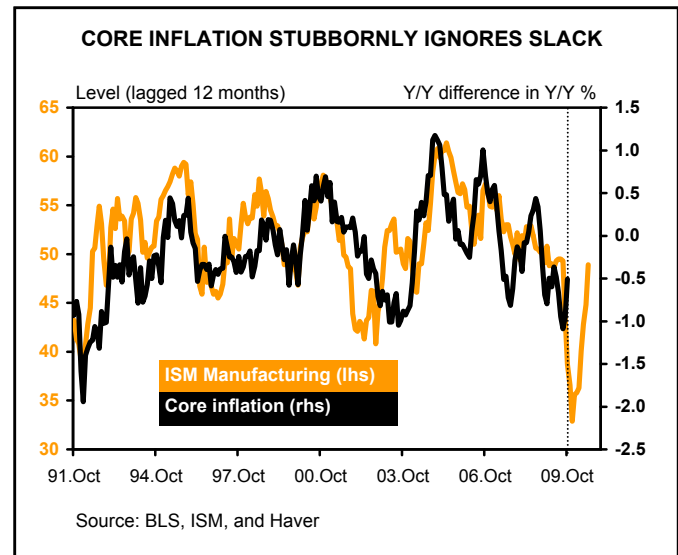
The fourth quarter has gotten off to a slow start for the economy. Industrial production for October fell by 0.1% from September while housing starts fell by 10.6% over the same period. Given the strong growth in the industrial sector in the third quarter, the level of production in October still remains well above the third quarter level so a healthy growth rate for the overall economy in the fourth quarter remains likely. The weakness in housing, on the other hand, would suggest some retrenchment in the construction sector after a phenomenal rebound in the third quarter, but a large part of the fall in October came from the volatile multifamily starts so it's likely too early to read too much into these numbers.

In spite of the weakness in some of this data, there did seem to be some fears of inflation creeping back into markets, as even though yields fell, the curve continued to steepen. Treasury yields fell across the curve this week, with 2- and 5-years down about 13bps while 10- and 30-years were down only 6-8bps. The data and speeches from Bernanke and several other Fed members made investors a bit more accepting of the fact that the Federal Reserve will be keeping rates low for a long time. And over the last 4 weeks, the short end has fallen by more than 30bps while 10-years have fallen only 16bps and 30-year Treasuries are completely unchanged.

With the short end of the curve falling further than the long end, this may be a symptom of strong buying of short-term securities by banks looking to boost their balance sheets as we near year-end. But, this could also be one sign that financial markets are a bit more concerned that this extended stay at the zero bound could come at the risk of higher inflation down the road. The expected inflation implied in inflation-protected Treasuries (TIPS) and the inflation swap market suggests this is a concern, as well.

So what are we to make of this? We still think that fiscal deficits and improvement in the economy over the next several years could eventually lead to inflation concerns in the U.S., but over the next year or two, it's hard to see inflation pressures in the U.S., given the unemployment rate is already sitting at 10.2% and the large amount of idle manufacturing capacity. These are not conditions that are ripe for inflation.

That said, there are some red flags for the forecast of extremely subdued inflation. We did see CPI inflation come in stronger than expected in October. Headline inflation grew by 0.3% M/M and the -0.2% pace of deflation Y/Y will likely turn back into positive territory in November. Core inflation, the one the Fed will keep a much closer eye



on as a better gauge of the inflation trend, also remained strong with a 0.2% M/M gain and an annual pace of 1.7%. This annual pace of core inflation is stronger than we would expect if the large amount of unemployed workers and idle capacity in the manufacturing sector were exerting as much influence on inflation as it has in the past.

Through the 1980s, the large amount of slack in the economy did exert a strong downward pressure on inflation, but the closer we move to the present, inflation expectations have increasingly anchored actual inflation close the 2% pace that the Fed likes to see. Through all this, we have generally seen the ISM index provide a decent guide as to how much influence the swings in manufacturing output – and thus the swings in idle capacity in the economy – would have on the change in the rate of inflation. According to this indicator, we should be seeing core inflation lag behind the real economy and slow much faster than it has.

This is an area of concern that we'll need to watch very closely over the next few months. Ben Bernanke reiterated this week the Fed's commitment to keep rates low for an "extended period" given "low levels of resource utilization, subdued inflation trends and stable inflation expectations." Most economists – us included – still take it on faith that spare capacity will mute inflationary pressures, but most also still worship at the altar of inflation expectations. Headline inflation will continue to move higher as the collapse in oil prices last year makes the Y/Y increase in oil prices appear strong. But if core inflation does not weaken further, then faith in the impact of resource utilization will have to succumb to the cold hard facts.

CANADA – SLOW REBOUND EMERGING BUT HOUSING OVERSHOOTING

Data from the past week confirmed our expectation that GDP advanced in the third quarter, although we now project a more modest annualized pace of quarterly growth in the 1.0% range. Canada turned the corner but growth will be “skinny” in this first quarter of rebound.

September’s manufacturing data point to stronger shipments rounding out the quarter, consistent with the improving trade balance. The value of Canadian shipments rose 1.4% in September, thanks to a 1.8% boost in volumes, but this didn’t fully retrace lost ground from August’s 2.2% retreat. Motor vehicles were the big push to the monthly gains, with vehicles shipments rising as U.S. auto retailers restocked depleted lots and parts up from heightened production. As well, some buoyancy can nonetheless be read from the new and unfilled orders data, with improvements in demand appearing sustainable. However, inventory contractions continue and, although real inventories are now at 1999 levels, inventory-to-shipments (I/S) remains high against history, pointing to continuing draw-downs through the coming quarter.

These ongoing inventory draw-downs in the manufacturing and wholesale sectors will also detract from third quarter growth. There is certainly a shift in composition of demand towards domestic sources and trade won’t be the prime propellant during recovery. Indeed, Canada’s export side is still battling major headwinds and it will be up to the domestic side to do much of the heavy lifting.

Canada’s pace of recovery will not be bursting from the gates, but the pace of recovery looks to pick up in the coming quarters on the strength of domestic demand – particularly durables purchases by households and heightened M&E investment by firms. With rallying stock markets and

blistering housing prices, household wealth is improving, which is supportive of consumer spending. However, facing weak job markets, consumers remain cautious.

The big surprise in recent months has been the strength in housing markets. Existing housing sales for October continued at a break-neck pace, up 41.5% Y/Y. Although distorted by geography and not accounting for quality of homes sold, the Canada-wide average price rose 20.7% Y/Y.

We do expect housing to moderate into November (www.td.com/economics/special/pg1009_rhousing.pdf), but we’re not certainly not seeing this yet. While strengthening borrowing by households and propelling housing-related purchases, this persisting pace of the housing market is obviously at odds with the general macroeconomic setting.

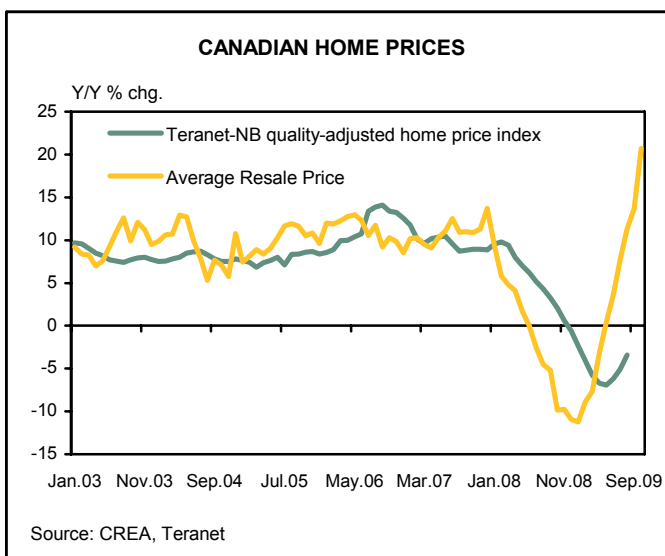
As we highlighted in a recent note (www.td.com/economics/special/ca1009_housing.pdf), the Bank of Canada will be paying increasing attention to a potential overpricing of housing if present housing strength fails to moderate into the late fall. Obviously, it’s a no-go to hike interest rates when unemployment is still rising, the loonie is still appreciating and excess capacity is still wide. While the Bank has signaled its unease about potential instability from emergent asset bubbles, it prefers the “scalpel” of targeted market-specific tools, rather than the “meat cleaver” of monetary policy.

Indeed, with the picture of a gradual recovery, excess capacity will remain wide and, though core inflation has remained sticky on firmly-anchored expectations, economic slack is sure to slow core price growth over the coming quarters, supporting a go-slow approach on rate hikes.

October inflation somewhat bucked the downward pressure on price growth. As was anticipated given the base-year effects in energy prices, headline inflation returned to positive year-over-year territory after drifting negative in past months. However, more surprisingly, October experienced an advance of core inflation from 1.5% Y/Y in September to 1.8% Y/Y, but base-year effects contributed (Core CPI in October 2008 abnormally weak, again advancing in November 2008).

Looking forward, a higher dollar will cheapen imports, with pass-through likely to be more elevated than in past loonie rallies. As well, higher food prices had previously propelled core inflation and this dynamic is now reversing. Despite well-anchored expectations, core inflation should soften in months ahead, supporting the Bank of Canada maintaining low interest rates for longer.

Grant Bishop, Economist, 416-982-8063





U.S.: UPCOMING KEY ECONOMIC RELEASES

U.S. Durable Goods Orders – October

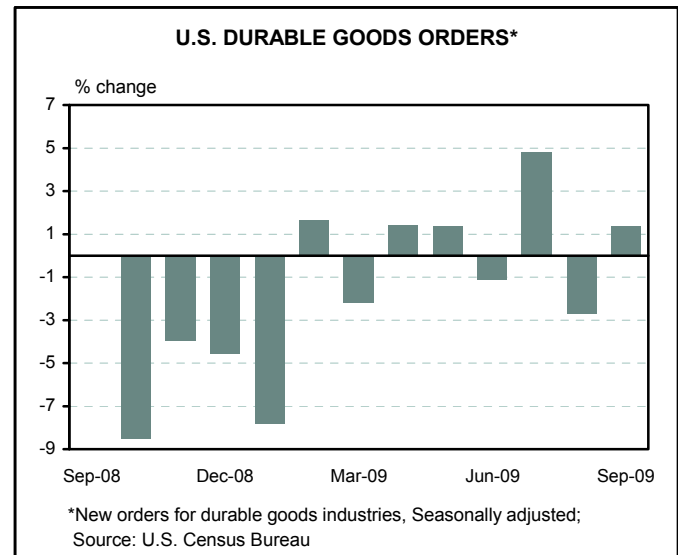
Release Date: November 25/09

September Result: total 1.4% M/M; ex-transportation 1.2% M/M

TD Forecast: total 0.5% M/M; ex-transportation 1.0% M/M

Consensus: total 0.5% M/M; ex-transportation 0.8% M/M

As the U.S. economy slowly pulls itself from the deep economic recession, favourable support is expected to come from business spending and export demand. And with durable goods orders rising in 4 of the last 6 months, the support from business capital expenditures has been quite evident. In October, we expect the positive momentum in durable goods orders to continue, with new orders rising a further 0.5% M/M. However, with the headline number likely to be depressed by weak transportation orders, excluding transportation, durable goods orders should rise by a more respectable 1.0% M/M. In the coming months, as the economic recovery gathers further traction, we ex-



pect orders to stay in positive territory as U.S. businesses replenish their depleted capital stock in anticipation of the pick-up in demand.

Millan Mulraine 416-308-2911

U.S. Personal Income & Spending - October

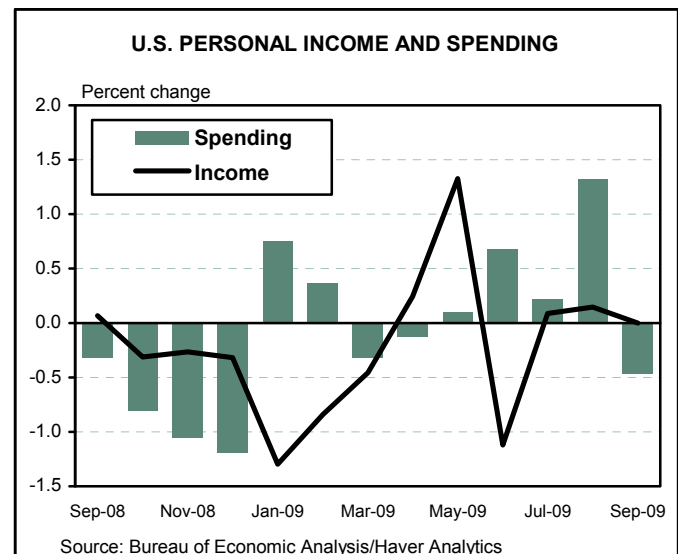
Release Date: November 25/09

September Result: income 0.0% M/M, spending -0.5% M/M; core PCE deflator 0.1% M/M, 1.3% Y/Y

TD Forecast: income 0.1% M/M; spending 0.6% M/M; core PCE deflator 0.1% M/M, 1.4% Y/Y

Consensus: income 0.2% M/M; spending 0.5% M/M; core PCE deflator 0.1% M/M, 1.3% Y/Y

Despite the distressed labour market conditions and weak economy, the positive momentum in the U.S. housing market (driven in large part by stimulative monetary and fiscal policies) and the dramatic recovery in financial markets over the past few months have contributed in large part to the stabilisation in consumer confidence, and consequently personal consumption expenditures. In October, personal income is expected to track modestly higher, rising by a meagre 0.1% M/M mostly on account of higher transfer payments by the government. Personal consumption expenditures are also expected to rise, posting its fifth monthly advance in six months, with a 0.6% M/M gain. Evidence of the strength in personal consumption has been seen in the corresponding retail sales report, thereby providing an upside risk to this call. On the inflation front, the core PCE



deflator is expected to rise by a modest 0.1% M/M, with the annual pace of core PCE inflation rising to 1.4% Y/Y, from 1.3% Y/Y in September. In the coming months, we expect the core PCE deflator to ease as the growing economic slack in the U.S. economy dampens core consumer price pressures.

Millan Mulraine 416-308-2911



CANADA: UPCOMING KEY ECONOMIC RELEASES

Canadian Retail Sales - September

Release Date: November 23/09

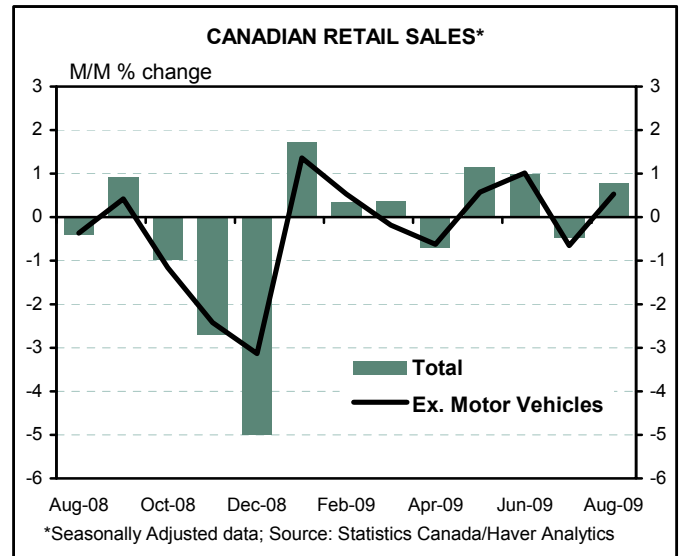
August Result: total 0.8% M/M; ex-autos 0.5% M/M

TD Forecast: total 1.0% M/M; ex-autos 0.5% M/M

Consensus: total 0.6% M/M; ex-autos 0.4% M/M

With the Canadian economy on the verge of emerging from the brief economic recession, we expect retail sales to post its fourth monthly advance in five months with a 1.0% M/M gain. Much of the upward momentum in spending should come from motor vehicle sales, which is poised to post its second consecutive month of strong gains. Additional support should come from expenditures on housing related items, on account of the buoyancy in Canadian housing market activity. Excluding autos, retail sales are expected to rise by a more modest 0.5% M/M. Real retail sales, should also advance on the month, though it is likely to rise at a more modest pace than the headline number. In the months ahead, with Canadian labour market conditions expected to remain soft, consumer spending should be tepid.

Millan Mulraine 416-308-2911





RECENT KEY ECONOMIC INDICATORS: NOVEMBER 16-20, 2009

Release Date	Economic Indicators	Data for Period	Units	Current	Prior		
United States							
Nov 16	Advance Retail Sales	Oct	M/M % Chg.	1.4	-2.3	R▼	
Nov 16	Retail Sales Less Autos	Oct	M/M % Chg.	0.2	0.4	R▼	
Nov 16	Empire Manufacturing	Nov	Index	23.51	34.57		
Nov 16	Business Inventories	Sep	M/M % Chg.	-0.4	-1.6	R▼	
Nov 17	Producer Price Index	Oct	Y/Y % Chg.	-1.9	-4.8		
Nov 17	PPI Ex. Food & Energy	Oct	M/M % Chg.	0.7	1.8		
Nov 17	Net Long-term TIC Flows	Sep	\$, Blns	40.7	34.2	R▲	
Nov 17	Total Net TIC Flows	Sep	\$, Blns	133.5	25.3	R▲	
Nov 17	Industrial Production	Oct	M/M % Chg.	0.1	0.6	R▼	
Nov 17	Capacity Utilization	Oct	%	70.7	70.5		
Nov 17	NAHB Housing Market Index	Nov	Index	17	17	R▼	
Nov 18	Consumer Price Index	Oct	Y/Y % Chg.	-0.2	-1.3		
Nov 18	CPI Ex Food & Energy	Oct	Y/Y % Chg.	1.7	1.5		
Nov 18	Housing Starts	Oct	Thousands	529	592	R▲	
Nov 18	Building Permits	Oct	Thousands	552	575	R▲	
Nov 19	Initial Jobless Claims	14-Nov.	Thousands	505	505	R▲	
Nov 19	Continuing Claims	7-Nov.	Thousands	5611	5650	R▲	
Nov 19	Leading Indicators	Oct	M/M % Chg.	0.3	1.0		
Nov 19	Philadelphia Fed	Nov	Index	16.7	11.5		
Canada							
Nov 16	Manufacturing Sales	Sep	M/M % Chg.	1.4	-1.8	R▲	
Nov 18	Consumer Price Index	Oct	Y/Y % Chg.	0.1	-0.9		
Nov 18	CPI Core	Oct	Y/Y % Chg.	1.8	1.5		
Nov 19	Int'l Securities Transactions	Sep	CND, Blns	13.590	5.067	R▼	
Nov 19	Wholesale Sales	Sep	M/M % Chg.	0.2	-1.5	R▼	
Nov 19	Leading Indicators	Oct	M/M % Chg.	0.7	1.2	R▲	
International							
Nov 15	NZ	3Q	Producer Prices - Inputs	Q/Q % Chg.	-1.1	0.0	
Nov 15	NZ	3Q	Producer Prices - Outputs	Q/Q % Chg.	-1.4	-0.7	
Nov 15	JN	3Q	Gross Domestic Product	Q/Q % Chg.	1.2	0.7	R▲
Nov 15	UK	Nov	Rightmove House Prices	Y/Y % Chg.	1.6	0.2	
Nov 16	EU	Oct	Euro-Zone CPI	Y/Y % Chg.	-0.1	-0.3	
Nov 16	EU	Oct	Euro-Zone Core CPI	Y/Y % Chg.	1.2	1.2	
Nov 17	UK	Oct	CPI	Y/Y % Chg.	1.5	1.1	
Nov 17	UK	Oct	Core CPI	Y/Y % Chg.	1.8	1.7	
Nov 17	EU	Sep	Euro-Zone Trade Balance	Eur, Blns	6.8	2.2	R▲
Nov 18	EU	Sep	ECB Euro-Zone Current Account	Eur, Blns	-5.4	0.6	R▲
Nov 18	EU	Sep	Construction Output	Y/Y % Chg.	-8.0	-10.0	R▲
Nov 18	AU	Oct	RBA Foreign Exchange Transactions	AUD Mlns	307	830	
Nov 18	JN	Sep	All Industry Activity Index	M/M % Chg.	-0.6	0.9	
Nov 19	UK	Oct	Major Banks Mortgage Approvals	Thousands	61	56	
Nov 19	UK	Oct	Retail Sales	Y/Y % Chg.	3.4	2.9	R▲
Nov 19	UK	Oct	Public Sector Net Borrowing	£, Blns	11.4	14.9	R▲
Nov 19	JN	20-Nov.	BOJ Target Rate	%	0.10	0.10	

Source: Bloomberg, TD Economics



UPCOMING ECONOMIC RELEASES AND EVENTS: NOVEMBER 23-27, 2009

Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Nov 23	8:30	Chicago Fed Nat Activity Index	Oct	Index	--	-0.81
Nov 23	10:00	Existing Home Sales	Oct	M/M % Chg.	2.3	9.4
Nov 24	9:00	S&P/CaseShiller Home Price Index	Sep	Index	--	146.00
Nov 24	10:00	Consumer Confidence	Nov	Index	47.5	47.7
Nov 24	10:00	Richmond Fed Manufacturing Index	Nov	Index	10	7
Nov 24	10:00	House Price Index	Sep	M/M % Chg.	0.1	-0.3
Nov 24	14:00	<i>Minutes of Nov. 4 FOMC Meeting is Released</i>				
Nov 24	17:00	ABC Consumer Confidence	22-Nov.	Index	--	-45
Nov 25	7:00	MBA Mortgage Applications	20-Nov.	M/M % Chg.	--	-2.5
Nov 25	8:30	Personal Income	Oct	M/M % Chg.	0.2	0.0
Nov 25	8:30	Personal Spending	Oct	M/M % Chg.	0.5	-0.5
Nov 25	8:30	PCE Core	Oct	Y/Y % Chg.	1.3	1.3
Nov 25	8:30	PCE Deflator	Oct	Y/Y % Chg.	0.1	-0.5
Nov 25	8:30	Durable Goods Orders	Oct	M/M % Chg.	0.5	1.4
Nov 25	8:30	Durables Ex Transportation	Oct	M/M % Chg.	0.7	1.2
Nov 25	8:30	Initial Jobless Claims	21-Nov.	Thousands	500	505
Nov 25	8:30	Continuing Claims	14-Nov.	Thousands	5550	5611
Nov 25	10:00	New Home Sales	Oct	Thousands	405	402
Nov 25	10:00	New Home Sales	Oct	M/M % Chg.	0.8	-3.6
Canada						
Nov 23	8:30	Retail Sales	Sep	M/M % Chg.	0.6	0.8
Nov 23	8:30	Retail Sales Less Autos	Sep	M/M % Chg.	0.4	0.5
Nov 27	8:30	Current Account (BOP)	Q3	\$, Blns	-13.2	-11.2
International						
Nov 22	19:30	AU New Motor Vehicle Sales	Oct	Y/Y % Chg.	--	-2.0
Nov 23	--	UK Nationwide House Prices	Nov	M/M % Chg.	0.3	0.4
Nov 23	3:00	FR PMI Manufacturing	Nov	Index	55.8	55.6
Nov 23	3:00	FR PMI Services	Nov	Index	57.4	57.7
Nov 23	18:00	AU Conference Board Leading Index	Sep	Index	--	1.8
Nov 24	2:45	FR Business Confidence Indicator	Nov	Index	91.0	89.0
Nov 24	2:45	FR Production Outlook Indicator	Nov	Index	-9	-11
Nov 24	2:50	FR Consumer Spending	Oct	Y/Y % Chg.	2.3	1.0
Nov 24	4:00	GE IFO Business Climate	Nov	Index	92.5	91.9
Nov 24	4:00	GE IFO Current Assessment	Nov	Index	88.0	87.3
Nov 24	4:00	GE IFO Business Expectations	Nov	Index	97.3	96.8
Nov 24	4:30	UK Total Business Investment	Q3	Y/Y % Chg.	-22.9	-21.8
Nov 24	5:00	EU Industrial New Orders	Sep	Y/Y % Chg.	-17.3	-23.1
Nov 24	17:20	AU <i>Australian Central Bank Deputy Governor Speaks in Melbourne</i>				
Nov 24	18:50	JP Adjusted Merchandise Trade Balance	Oct	¥, Blns	300.0	58.6
Nov 25	2:00	GE Gfk Consumer Confidence Survey	Dec	Index	4.0	4.0
Nov 25	4:30	UK GDP	Q3	Q/Q % Chg.	-0.3	-0.4
Nov 25	4:30	UK Private Consumption	Q3	Q/Q % Chg.	-0.3	-0.6
Nov 25	18:50	JP <i>Bank of Japan Monetary Policy Meeting Minutes is Released</i>				
Nov 25	21:00	NZ NBNZ Business Confidence	Nov	Index	--	48.2
Nov 26	4:00	EU Euro-Zone M3	Oct	Y/Y % Chg.	0.8	1.8
Nov 26	6:00	UK <i>UK CBI Quarterly Distributive Trades is Released</i>				
Nov 26	--	GE Consumer Price Index	Nov	Y/Y % Chg.	0.5	0.0
Nov 26	--	GE CPI - EU Harmonised	Nov	Y/Y % Chg.	0.5	-0.1
Nov 26	16:45	NZ Trade Balance	Oct	NZD\$, Mlns	-480	-424
Nov 26	18:30	JP Jobless Rate	Oct	%	5.4	5.3
Nov 26	18:30	JP Household Spending	Oct	Y/Y % Chg.	0.6	1.0
Nov 26	18:30	JP CPI	Oct	Y/Y % Chg.	-2.4	-2.2
Nov 26	18:30	JP CPI Ex-Fresh Food	Oct	Y/Y % Chg.	-2.2	-2.3
Nov 26	18:30	JP CPI Ex Food, Energy	Oct	Y/Y % Chg.	-1.1	-1.0
Nov 26	18:50	JP Large Retailers' Sales	Oct	M/M % Chg.	-5.8	-5.6
Nov 26	18:50	JP Retail Trade	Oct	M/M % Chg.	-0.9	0.9
Nov 26	21:00	NZ Money Supply M3	Oct	Y/Y % Chg.	--	2.7

* Eastern Standard Time; Sources: Bloomberg, TD Economics



CONTACTS AT TD ECONOMICS

**Don Drummond, Senior Vice President and
Chief Economist**

mailto:don.drummond@td.com

**Craig Alexander, Senior Vice President and
Deputy Chief Economist**

mailto:craig.alexander@td.com

ECONOMIC FORECASTING

Beata Caranci

Director of Economic Forecasting

mailto:beata.caranci@td.com

Richard Kelly,

Senior Economist, International

mailto:richard.kelly@td.com

James Marple

Economist, United States

mailto:james.marple@td.com

Diana Petramala

Economist, Canada

mailto:diana.petramala@td.com

Grant Bishop

Economist, Canada

mailto:grant.bishop@td.com

ECONOMIC STUDIES

**Derek Burleton, Associate Vice President and
Director of Economic Analysis**

mailto:derek.burleton@td.com

Pascal Gauthier

Economist, Regional & Fiscal Canada

mailto:pascal.gauthier@td.com

Dina Cover

Economist, Commodites & Industry

mailto:dina.cover@td.com

TO REACH US

Mailing Address

55 King Street West

21st Floor, TD Tower

Toronto, Ontario

M5K 1A2

Fax: (416) 944-5536

mailto:td.economics@td.com

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