



# TD Economics

## The Weekly Bottom Line

February 8, 2008

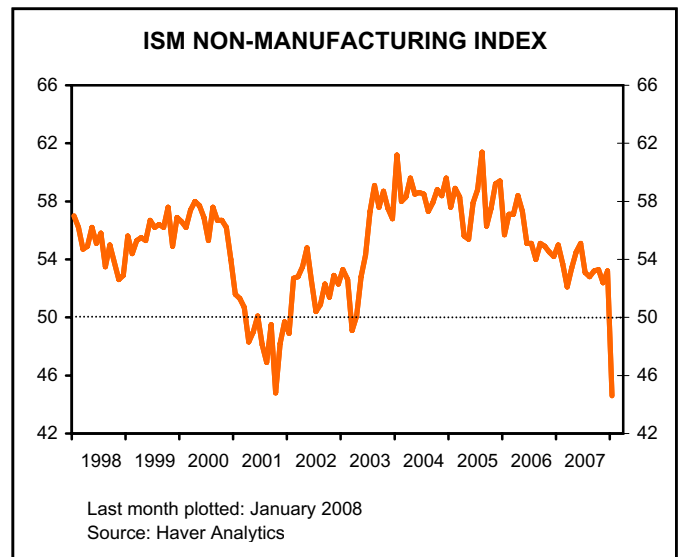
### HIGHLIGHTS

- **Non-manufacturing ISM spurs more recession talk in the U.S.**
- **TD Economics revises U.S. growth projections**
- **Canadian jobs data a shocker**

This week, investors continued to seek the relative safety of bonds at the expense of equities. Notably, U.S. 2-year government bond yields fell below 2% for the first time since April of 2004. Canadian 2-year government bond yields declined as well, though they still remain above 3%. Despite the 125 basis points in interest rate cuts by the Fed over the past 3 weeks, equity markets recorded losses across the board, led by the tech-heavy Nasdaq (-5%). Declines in the S&P 500 and Toronto's S&P/TSX were 4% and 3%, respectively.

### U.S. economic news disappoints

In addition to being served up with a number of disappointing fourth quarter earnings reports, investors continued to fret about the rising risks of a U.S. recession. Following poor January employment numbers last week, the ISM non-manufacturing reading for the same month was even worse, plummeting from 53.2 to 44.6. The sizable drop in January was not only the largest monthly decline on record, but also the lowest level since the series was created in 1997. The culprits behind the weak performance were substantial losses in the business activity, new orders and employment sub-indices. While these figures



certainly paint a dismal picture for the U.S. economy, they can be quite volatile on a month-to-month basis. Still, even if February records a moderate reversal, these data build the case that no growth was being recorded in the U.S. economy as the year kicked off.

Adding to concerns was Thursday's report on initial jobless claims, which came in above expectations at 356,000. On a 4-week moving average basis, jobless claims continued to edge higher. This report has proven to be a good leading indicator of recessions in the past. At this stage, the trend is not sounding off alarm bells, even though the January payrolls report increases the risks that the trend in claims could continue to worsen.

Worries about economic growth were also echoed in Fed speeches this week. Richmond Fed President Lacker acknowledged the possibility of a mild recession, similar to the last one experienced in 2001. He noted that business investment will likely slow this year, but still remain in positive territory, and that job growth will likely be lethargic for the better part of the year. Lacker also signaled upside risks to inflation, thereby making rate decisions even more difficult. Philadelphia Fed President Plosser also raised concerns about economic growth, but he too sounded a word

#### Recent TD Economics Research

February 8, 2008 - Canadian Employment  
 February 8, 2008 - Canadian Housing Starts  
 February 6, 2008 - Automakers Brace for a Difficult Year  
 February 5, 2008 - Economic Stimulus and the U.S. Outlook  
 February 5, 2008 - U.S. ISM Non-Manufacturing Index

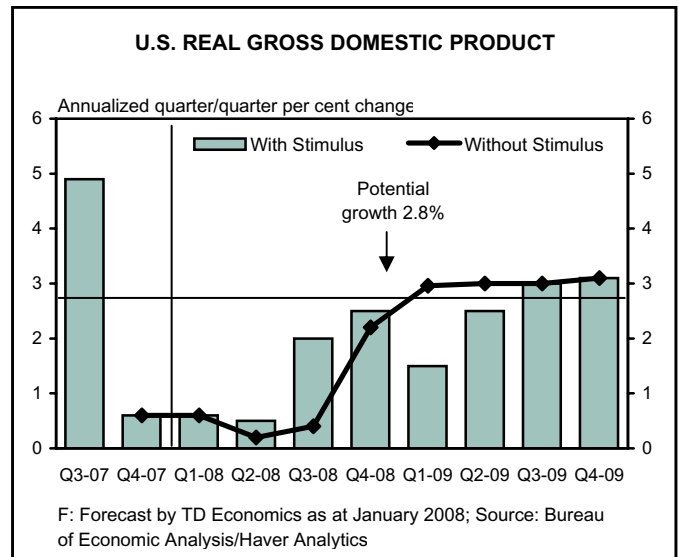
of caution about inflation, arguing that “ignoring price stability during times of economic weakness risks undermining our ability to achieve economic growth over the long run.”

In light of the latest signs as to the direction of the U.S. economy, we have downgraded our U.S. economic growth forecast. We are now projecting Q4/Q4 growth of 1.4% in 2008 (previously 1.9%) and 2.5% in 2009 (3.1%). For details, see TD Economics Special Report: *Economic Stimulus and the U.S. Outlook* available on our website. The volatility in equity markets, weakness in employment, and continued erosion of the housing market are likely to curb consumer spending during the first half of 2008, leading to virtually no growth during each of the first two quarters. The fiscal stimulus package expected to be implemented by the U.S. government will support growth during the second half of this year. However, this will provide only a temporary boost, and as such, a sub-par expansion is likely to carry into 2009 (see chart). The prominence of downside risks to growth has prompted us to revise our Fed rate call as well, from a cut of 25 bps to 50 bps in March. However, due to the inflationary pressures weighing on the economy, we expect the next cut to be the last.

### Canada's job market remarkable

As signs of U.S. weakness were further manifested, the Canadian economy continued to show remarkable resilience. Employment numbers released this morning showed that 46,000 jobs were created in January, bouncing back with a vengeance from December's revised 3,000 loss. The gain boosted the employment rate to a new record of 63.8%, and drove the unemployment rate back down to the 33-year low of 5.8% reached last October. January saw a reversal in recent trends, as growth in the private sector far outweighed declines in both the public sector and the self-employed, and the goods-producing sector outperformed the service-producing sector, which was relatively flat for the month. Perhaps the biggest surprise was the 18,000 jump in export-oriented manufacturing jobs. Still, employment in the sector over the past year is down 5.4%, dampened in part by the slowing U.S. economy. Elsewhere, job creation in other areas continued to be supported by domestic strength, with particularly large gains in professional, scientific and technical services as well as financial services.

Another key job generator in Canada was the construction sector. Today, we received news that Canadian housing starts also beat expectations in January, rising 21% from



December to 223,000. While single-unit housing starts recorded a modest decline, multi-unit housing starts rose by a whopping 64% month-over-month. The largest gains stemmed from Ontario (44%) and Quebec (22%), while the Atlantic region (-17%) was the only area to weigh down the total number of starts.

While this week's data are likely to spur further talk of decoupling between Canada and U.S., our view is that January's surge in Canadian economic activity represents more of a blip than a sign of renewed strength. Hence, look for both indicators to cool in the coming months. With the risks of knock-on effects from the deteriorating U.S. economy growing since the Bank of Canada's last fixed announcement data and Canadian core inflation remaining below trend, we expect that the central bank will remain forward looking and cut interest rates by 50 bps points in March and 25 bps in April.

### BOE cuts rates, ECB to follow

Similarly, the U.S. is not alone in its economic woes, as the Bank of England cut rates by 25 basis points this week, and the European central bank has signaled that it may cut rates going forward. The increasing recognition that central banks around the world will be required to jump on the rate-cutting bandwagon is likely to be instrumental in spurring a moderate recovery in the U.S. dollar later this year.

*Dina Cover, Economist*  
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## UPCOMING KEY ECONOMIC RELEASES

### U.S. Retail Sales - January

**Release Date:** February 13/08

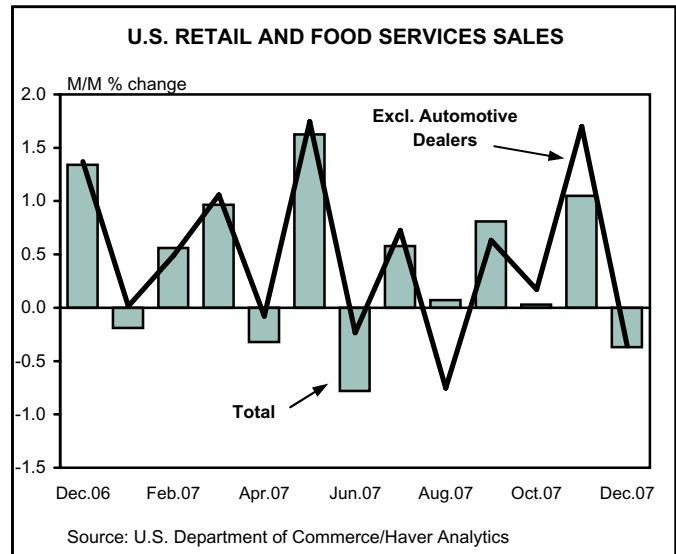
**December Result:** total -0.4%; ex-autos -0.4%

**TD Forecast:** total -0.6%; ex-autos 0.0%

**Consensus:** total 0.0%; ex-autos +0.2%

We're expecting to see U.S. retail sales fall further in January, with total sales down 0.6%. The big reason for the increase is the drag from the auto sector, as car and truck sales declined by more than 6% in January. However, we don't expect to see much strength in the rest of the report either, so ex-autos sales are likely to come in flat. Gasoline prices were up by 0.8% during the month, which will give a small boost to sales, but chain store sales were fairly weak, and the monthly sales results from major retailers were reported to be disappointing. The major drop in the ISM non-manufacturing index also does not bode well for retail sales, especially as the retail and wholesale sectors were reported to be among the weakest of all the sectors surveyed.

*Jacqui Douglas 416-982-7784*



### Canadian International Trade - December

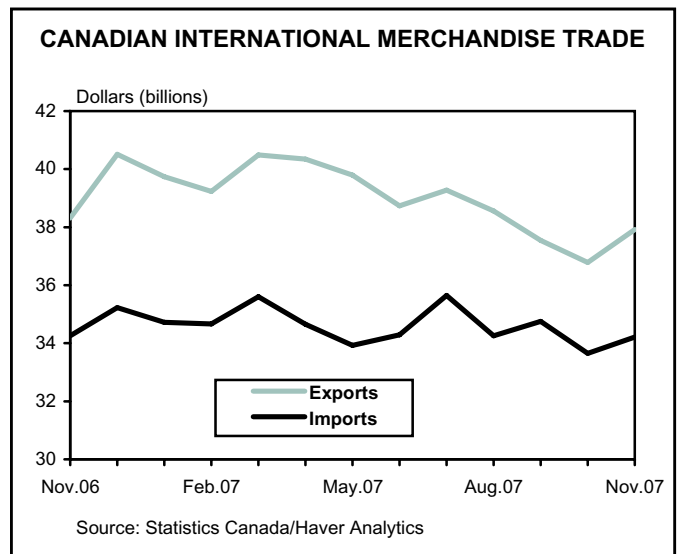
**Release Date:** February 14/08

**November Result:** \$3.7B

**TD Forecast:** \$3.2B

**Consensus:** \$3.6B

We're expecting to see Canada's international trade balance deteriorate in December, falling from \$3.7B to \$3.2B. And behind this forecast we see a 1.0% fall in imports, but an even bigger 2.2% fall in exports. There are several reasons why we expect to see such a weak export performance in December. One is that November's export performance was just too good to be true, with every single sector but consumer goods gaining on a M/M basis, so we're likely to see some pay-back in December. Other reasons include the declines in both Canada and U.S. motor vehicle assembly during the month, and the slowdown in the U.S. economy towards the end of 2007, leading to a decrease in the demand for Canadian exports. On the import side, we expect to see a fall in the automotive and industrial goods sectors, which will likely



be tempered to some extent by further investment by Canadian firms in machinery and equipment, and demand for imported U.S. consumer goods during the Christmas season.

*Jacqui Douglas 416-982-7784*

## Canadian Manufacturing Shipments - December

**Release Date:** February 15/08

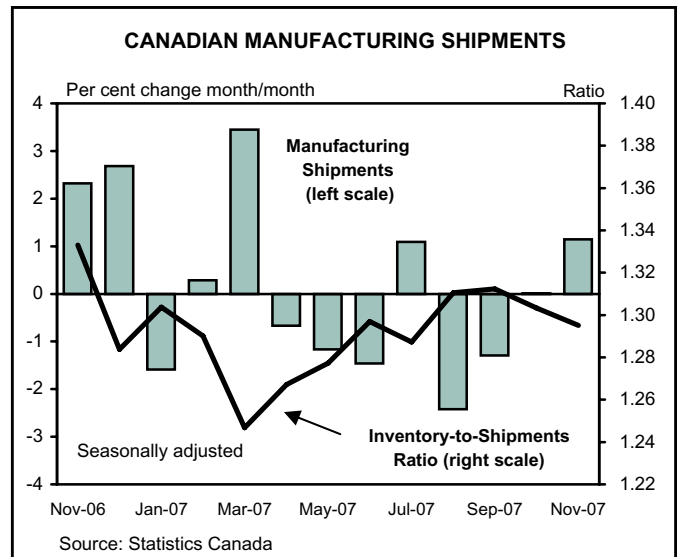
**November Result:** +1.1%

**TD Forecast:** -0.8%

**Consensus:** -0.1%

We're expecting to see Canadian manufacturing shipments fall by 0.8% in December after November's 1.1% gain. And since industrial prices were up 1.1% during the month, the real number is likely to be even weaker. Canadian motor vehicle production plummeted in December, and U.S. durable goods shipments fell by 0.2%, neither of which bodes well for Canadian manufacturing shipments. However, with the increase in new orders in both Canada in November and the U.S. in December, it looks like there's enough demand in the pipeline to keep North American manufacturing activity from falling off a cliff for the next couple of months.

*Jacqui Douglas 416-982-7784*



## UPCOMING NORTH AMERICAN ECONOMIC CALENDAR February 11-15, 2008

Release Date	Economic Indicators	Data for Period	Units	Consensus Forecast	Prior
<b>Canada</b>					
Feb. 11	New Housing Price Index	Dec.	% Chg.	0.3	0.5
Feb. 14	International Merchandise Trade Balance	Dec.	C\$, blns	3.6	3.7
Feb. 14	<i>Bank of Canada Review released</i>				
Feb. 15	New Motor Vehicle Sales	Dec.	% change	3.0	-2.9
Feb. 15	Manufacturing Shipments	Dec.	% change	-0.1	1.1
<b>United States</b>					
Feb. 11	<i>St. Louis Fed President Poole reflects on being head of the St. Louis Federal Reserve</i>				
Feb. 12	<i>San Francisco Fed President Yellen speaks on the economy in San Francisco, CA</i>				
Feb. 13	Retail Sales	Jan.	% change	0.0	-0.4
Feb. 13	Retail Sales ex. autos	Jan.	% change	0.2	-0.4
Feb. 13	Business Inventories	Dec.	% change	0.4	0.4
Feb. 14	Trade Balance	Dec.	US\$, blns	-61.0	-63.1
Feb. 14	Weekly Initial Jobless Claims	9-Feb	Thousands	340	356
Feb. 14	<i>Fed Chairman Bernanke testifies before the Senate Banking committee in Washington, D.C.</i>				
Feb. 14	<i>Chicago Fed President Evans speaks on the U.S. economic outlook in Chicago, IL</i>				
Feb. 14	<i>Former Fed Chairman Greenspan speaks on the economy in Houston, TX</i>				
Feb. 15	Empire Manufacturing Survey	Feb.	Index	7.8	9.0
Feb. 15	Industrial Production	Jan.	% change	0.1	0.0
Feb. 15	Capacity Utilization	Jan.	Per cent	81.4	81.4
Feb. 15	U. Michigan Consumer Confidence (prelim.)	Feb.	Index	78.0	78.4
Feb. 15	<i>Fed Governor Mishkin speaks at the Tuck Global Capital Markets conference in Hanover, NH</i>				

Source: Bloomberg, TD Economics

## RECENT KEY ECONOMIC INDICATORS February 4-8, 2008

Date	Economic Indicators	Data for	Units	Current	Prior	
<b>Canada</b>						
Feb. 6	Building Permits	Dec.	% change	0.4	-9.9	
Feb. 6	Ivey Purchasing Managers Index	Jan.	Index	56.2	45.9	
Feb. 8	Unemployment Rate	Jan.	Per cent	5.8	6.0	R▲
Feb. 8	Net Change in Employment	Jan.	Thousands	46.4	-2.9	R▲
Feb. 8	Housing Starts	Jan.	Thousands	222.7	184.7	R▼
<b>United States</b>						
Feb. 4	Factory Orders	Dec.	% change	2.3	1.7	R▲
Feb. 6	Non-farm Productivity (prelim.)	Q4-07	Ann. % chg.	1.8	6.0	R▼
Feb. 6	Unit Labour Costs (prelim.)	Q4-07	Ann. % chg.	2.1	-1.9	R▲
Feb. 7	Weekly Initial Jobless Claims	2-Feb	Thousands	356.0	378.0	R▲
Feb. 8	Wholesale Inventories	Dec.	% Chg.	1.1	0.8	R▲

Source: Bloomberg, TD Economics

## G-7 ECONOMIC RELEASES AND EVENTS

Date	Time*	Country	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
Feb. 10	19:30	AU	<i>Reserve Bank Quarterly Monetary Policy statement released</i>				
Feb. 11	2:45	France	Industrial Production	Dec.	% Chg.	0.7	-1.5
	2:45	France	Manufacturing Production	Dec.	% Chg.	0.7	2.5
	4:30	U.K.	Merchandise Trade Balance - Total	Dec.	£, blns	4,400	4,371
	4:30	U.K.	Merchandise Trade Balance - ex. EU	Dec.	£, blns	4,450.0	4,439.0
	8:30	Canada	New Housing Price Index	Dec.	% Chg.	0.3	0.5
	18:00	U.S.	<i>St. Louis Fed President Poole reflects on being head of the St. Louis Federal Reserve</i>				
Feb. 12	2:45	France	Trade Balance	Dec.	Eur\$, blns	NA	-3.6
	4:30	U.K.	Consumer Price Index	Jan.	Y/Y % chg.	2.3	2.1
	4:30	U.K.	Retail Price Index excl. Mortgages (RPIX)	Jan.	Y/Y % chg.	3.3	3.1
	5:00	EU-12	ZEW Survey - Economic Sentiment	Feb.	Index	NA	-41.6
	5:00	Germany	ZEW Survey - Economic Sentiment	Feb.	Index	-43.5	-41.6
	5:00	Germany	ZEW Survey - Current Situation	Feb.	Index	50.0	56.6
	11:05	U.S.	<i>San Francisco Fed President Yellen speaks on the economy in San Francisco, CA</i>				
	18:50	Japan	Current Account Balance	Dec.	¥, blns	1,713.8	1,782.5
	23:30	Japan	Bankruptcies	Jan.	Y/Y % chg.	NA	-1.0
Feb. 13	5:00	EU	Industrial Production	Dec.	% change	0.6	-0.5
	5:30	U.K.	<i>Bank of England Quarterly Inflation report released</i>				
	8:30	U.S.	Retail Sales	Jan.	% change	0.0	-0.4
	8:30	U.S.	Retail Sales ex. autos	Jan.	% change	0.2	-0.4
	10:00	U.S.	Business Inventories	Dec.	% change	0.4	0.4
	18:50	Japan	Gross Domestic Product (prelim.)	Q4-07	Q/Q % chg.	0.4	0.4
	21:30	AU	Unemployment Rate	Jan.	Per cent	4.3	4.3
	21:30	AU	Net Change in Employment	Jan.	Thousands	15.0	20.1
	23:00	Japan	<i>Bank of Japan Monetary policy meeting</i>				
Feb. 14	2:00	Germany	Gross Domestic Product (prelim.)	Q4-07	Q/Q % chg.	0.3	0.7
	2:45	France	Gross Domestic Product (prelim.)	Q4-07	Q/Q % chg.	0.3	0.8
	4:00	EU	<i>European Central Bank publishes February monthly report</i>				
	5:00	EU	Gross Domestic Product (advance)	Q4-07	Q/Q % chg.	0.4	0.8
	8:30	U.S.	Trade Balance	Dec.	US\$, blns	-61.0	-63.1
	8:30	Canada	International Merchandise Trade Balance	Dec.	C\$, blns	3.6	3.7
	8:30	U.S.	Weekly Initial Jobless Claims	9-Feb	Thousands	340.0	356.0
	10:30	Canada	<i>Bank of Canada Review released</i>				
	---	U.S.	<i>Fed Chairman Bernanke testifies before the Senate Banking committee in Washington, D.C.</i>				
	---	Japan	<i>Bank of Japan Target Rate</i>		<i>Overnight rate</i>	0.50	0.50
	13:30	U.S.	<i>Chicago Fed President Evans speaks on the U.S. economic outlook in Chicago, IL</i>				
16:45	NZ	Retail Sales	Dec.	% change	NA	2	
19:30	U.S.	<i>Former Fed Chairman Greenspan speaks on the economy in Houston, TX</i>					
Feb. 15	1:00	Japan	<i>Bank of Japan monthly report released</i>				
	5:00	EU	Trade Balance	Dec.	Eur, blns	NA	2.6
	8:30	Canada	New Motor Vehicle Sales	Dec.	% change	3.0	-2.9
	8:30	Canada	Manufacturing Shipments	Dec.	% change	-0.1	1.1
	8:30	U.S.	Empire Manufacturing Survey	Feb.	Index	7.8	9.0
	9:15	U.S.	Industrial Production	Jan.	% change	0.1	0.0
	9:15	U.S.	Capacity Utilization	Jan.	Per cent	81.4	81.4
	10:00	U.S.	U. Michigan Consumer Confidence (prelim.)	Feb.	Index	78.0	78.4
	12:45	U.S.	<i>Fed Governor Mishkin speaks at the Tuck Global Capital Markets conference in Hanover, NH</i>				

\* Eastern Standard Time; Sources: Bloomberg, TD Economics

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