



TD Economics

The Weekly Bottom Line

October 24, 2008

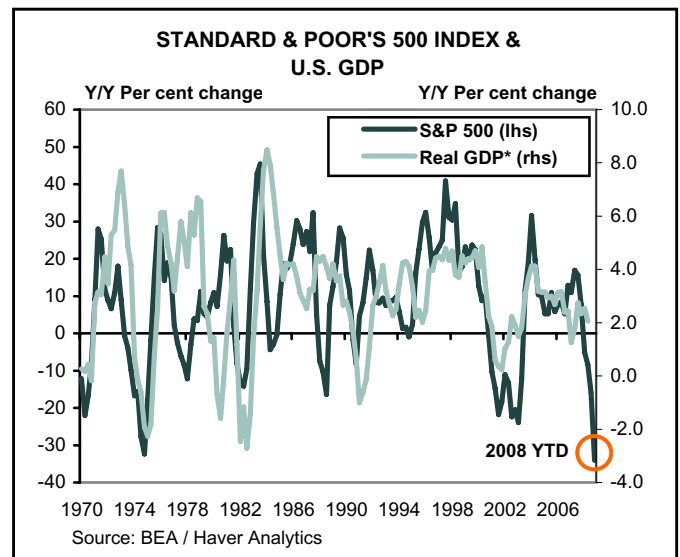
HIGHLIGHTS

- **Bank of Canada cuts rates 75bps in October, signals more to come**
- **Largest 4-week decline in the Canadian dollar ever**

Financial markets continue to be rocked by the ongoing elevated costs of bank funding, the uncertainty over the future economic landscape, and the need to reduce debt levels and leverage as a result of both of these factors. While the massive spike in the closely watched LIBOR-OIS spreads over late September and early October has receded, it remains unsustainably high. Moreover, contagion has led these problems to bleed into sectors and nations thought to be reasonably insulated from the subprime mess. Derivative products such as interest rate swaps widely used by corporations to hedge their interest rate risks – and tied to LIBOR rates – skyrocketed over the last month, making it that much more difficult for firms to manage risks. Corporations who raise money through commercial paper markets continue to have problems issuing any short-term debt with a maturity longer than a week. Emerging markets in Asia, Latin America, and Eastern Europe have seen the taps virtually turned off when it comes to investor inflows. Moreover, the massive volatility itself we are seeing in equity, currency, and commodity markets has costs for the global financial markets and economies.

Recent TD Economics Research

October 24, 2008 - Canadian Consumer Price Index
 October 23, 2008 - Ontario Fall Economic Outlook
 October 23, 2008 - Bank of Canada's MPR
 October 22, 2008 - Canadian Retail Sales
 October 21, 2008 - BoC Interest Rate Decision
 October 20, 2008 - Canadian Wholesale Sales
 October 20, 2008 - 2009 To Prove Testing Times For Small Businesses



The Canadian Context

The Canadian Ministry of Finance this week announced that it will begin a voluntary program whereby Canadian banks can pay a fee in return for a government guarantee of new bank debt issued over the next three years. Looking at a composite of various Canadian interest rates and spreads, TD Economics estimates that the level of financial stress for Canadian financial institutions right now is about twice what the peak level of stress was during the 2001 slowdown. This is a far cry from the U.S., where the level of financial stress is about four to five times larger than its worst point during the Tech Bust. However, the government guarantee was less about the current levels of stress for Canadian institutions – as a World Economic Forum report rated Canadian banks the soundest in the world this week – and more about keeping up with the Joneses. Since U.S. and European governments have announced guarantees of bank debt in recent weeks, it places Canadian banks at a relative disadvantage and the idea was to once again level the playing field.

This is not to say the Canadian economy and financial markets are immune from the global financial tensions.

Crude oil prices have fallen nearly 50% over the last three months and have been joined by a precipitous decline in the price of a number of metals, as well. Coupled with the growing risk that the U.S. may be in store for one of the worst recessions in 20 years, the concerns for the Canadian economy have grown in recent weeks. The Bank of Canada this week lowered interest rates by a quarter-point to 2.25%, but this came less than two weeks after they cut rates by half a percentage point as part of the global coordinated central bank easing on October 8th. In addition to this 75 basis points reduction in October, the biggest one-month move since they cut by 75 basis points following the 9/11 attacks, the Bank also signaled their intention to reduce rates further in the future, stating “further monetary stimulus will likely be required to achieve the 2 per cent inflation target over the medium term.”

Later in the week, the Bank fleshed out their current thinking in the Monetary Policy Report. The Canadian economy is expected to grow by only 0.6% in both 2008 and 2009, while the rapid decline in commodity prices and slack building into the economy is likely to pull headline inflation below 1% by mid-2009 and not rise to 2% until the very end of 2010. With how quickly economic conditions are rebalancing lower, the Bank of Canada is unlikely to bat an eyebrow at the Canadian inflation data released today that showed core inflation steady at 1.7% and headline inflation falling only a notch to 3.4%. Inflation pressures lag the economy and we believe the poor August retail sales figures also released this week and financial tensions omnipresent since then will be much more important for driving the BoC to cut interest rates by an additional half a percentage point when they meet again in December.

The Great Slump of 09

The global economic prospects continue to move from bad to worse. The year-over-year change in the S&P 500 is already the worst seen since the 1973-74 recession and is suggesting an imminent and sizeable contraction in the U.S. economy. This link to 35 years ago is telling as this is also the last truly global shock the world economy had when the oil embargo drove crude prices sky high. Now, the global credit shock may have started with U.S. subprime, but with financial markets more interlinked than ever before, these ructions are quickly spreading around the world.

SHARP FINANCIAL MARKET SHIFTS		
4-week per cent depreciation vis-à-vis U.S. dollar		
Currency	23-Oct	Largest since
Canadian dollar	21.6	Ever
Euro	12.1	Oct 1992 ERM Crisis
Pound	12.1	Sept 1992 ERM Crisis
Korean Won	22.6	Dec 1997 Crisis
Mexican Peso	26.4	Jan 1995 Crisis
Brazilian real	24.2	Jan 1999 Crisis
4-week per cent loss		
Market	23-Oct	Largest since
TSX	25.6	Oct 1987 Black Monday
SP500	24.9	Oct 1987 Black Monday
DJIA	21.1	Oct 1987 Black Monday
Crude Oil (WTI)	36.7	Feb 1986
Source: Bloomberg		

As the table here shows, going back to the early 1970s when currencies were not fixed to the price of gold, we have seen the largest monthly depreciation of the Canadian dollar ever. We have also seen the largest depreciations of the euro, the pound, the Korean won, the Mexican peso, and the Brazilian real since their respective crises in the 1990s. The declines in equity and commodity markets are some of the quickest since the 1980s.

In mid-September, we were already forecasting a global recession and the economic data and financial developments since that time have consistently surprised on the downside. As a result, we have downgraded our forecast for third quarter U.S. GDP to be released next week (details can be seen in the following pages). The U.K. economy contracted by over 2% in the third quarter, the worst result since 1990, while Eurozone manufacturing indicators suggest an economic contraction of 1-2% in Q4 is very possible. The financial landscape – and the world economy it is now holding hostage – is changing by the day. With the coordinated capitulation ongoing in global financial markets, we must now entertain the idea that we could be in store for one of the most coordinated slowdowns in the global economy since the early 1970s. Aggressive government and central bank actions will help to cap the downside, but the impacts of these aggressive moves are unlikely to find traction until early 2009.

Richard Kelly, Senior Economist
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UPCOMING KEY ECONOMIC RELEASES

U.S. Durable Goods Orders – September

Release Date: October 29/08

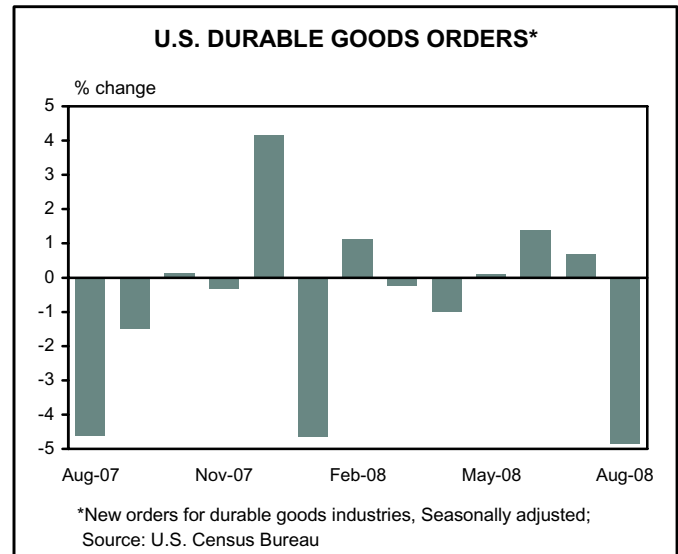
August Result: total -4.8% M/M;
ex-transportation -3.3% M/M

TD Forecast: total -1.5% M/M;
ex-transportation -0.5% M/M

Consensus: total -0.8% M/M;
ex-transportation -1.5% M/M

The weakening U.S. economic outlook, diminishing credit availability, and slumping consumer spending will continue to dampen capital expenditure by U.S. businesses, which should further depress durable goods orders. For September, we expect durable goods orders to decline by 1.5% M/M, following the dramatic 4.8% M/M plunge in August. However, with orders for Boeing aircraft down by a rather significant 9.8% M/M (on a seasonally-adjusted basis), orders excluding transportation equipment should fall by a more modest 0.5% M/M. In the coming months, we expect the sluggish domestic economy to further limit new durable goods orders.

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U.S. FOMC Interest Rate Decision

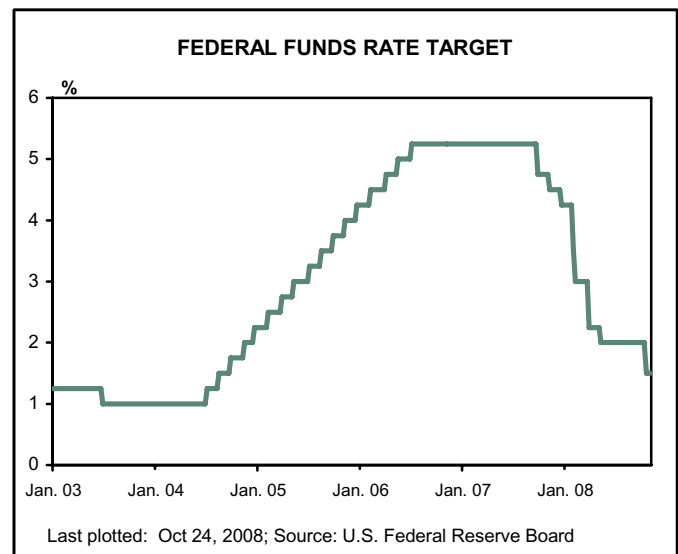
Release Date: October 29/08

Current Rate: 1.50%

TD Forecast: 1.00%

Consensus: 1.25%

The U.S. Federal Open Market Committee (FOMC) is set to meet on October 28-29. And with the U.S. economy appearing to have entered a recession, moderating inflation and inflationary expectations, and the intensifying banking crisis (with further adverse implications for the real economy) providing the backdrop, we expect the Fed to cut the fed funds rate by a further 50bps when they meet, taking the policy rate to a cyclical low of 1.00%. This reduction in the policy rate will come on the heels of the coordinated 50bps cut earlier this month, and should be the final instalment of monetary policy stimulus administered by the Fed for the time being. In the coming months, as the U.S. economy navigates against the headwinds of an intensifying financial crisis, retrenchment in credit, and



declining consumer spending activity, we expect the Fed to remain on the sidelines, but standing ready to take further action if warranted.

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U.S. Real GDP - Q3/08

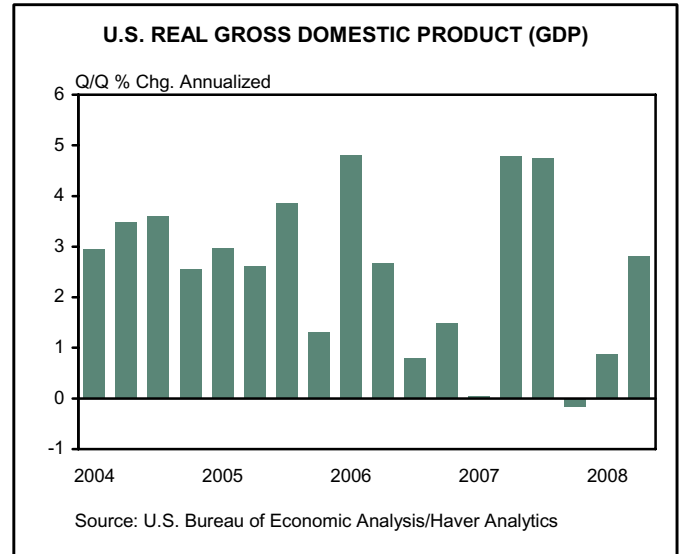
Release Date: October 30/08

Q2 Result: +2.8% Q/Q ann.

TD Forecast: -1.2% Q/Q

Consensus: -0.5% Q/Q

After surprisingly strong growth in the second quarter, the U.S. economy is expected to shrink in the third quarter by 1.2%. The fiscal stimulus package, which kept consumer spending alive in the second quarter, is fully behind us now. Retail sales reports show households have cut back significantly on all types of purchases from motor vehicles to eating out at restaurants. As a result, personal consumption expenditure is expected to pull back by over 3%, its worst decline since 1980. Businesses, struggling with falling demand and higher costs of funding are also expected to reduce their spending. Moreover, with housing starts falling to their lowest point in close to 30 years, residential construction will once again (for the eleventh straight quarter) subtract from economic growth. The only sector of the economy that will provide some relief is exports and this is due entirely to strength at the outset of the



quarter, in July. The re-emergence of the financial crisis in September dampens the outlook across the board for the third quarter but its full impact will not be felt until the final three months of 2008.

James Marple (416) 982-2557

U.S. Personal Income & Spending - September

Release Date: October 31/08

August Result: income 0.5% M/M, spending 0.0%

M/M; core PCE deflator 0.2% M/M, 2.6% Y/Y

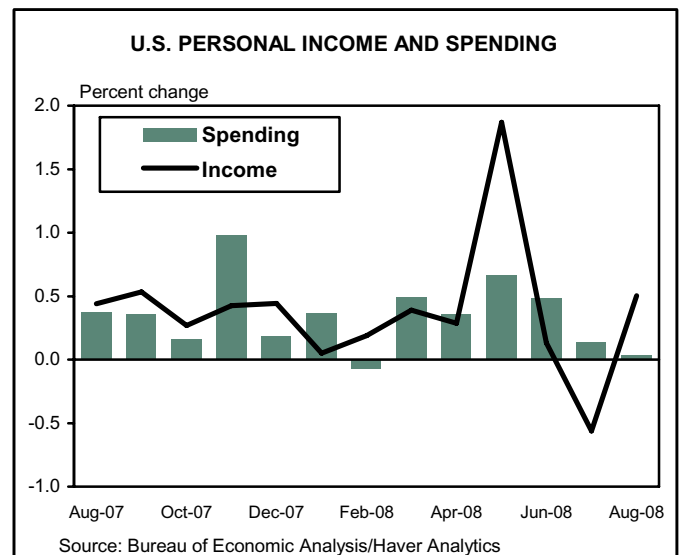
TD Forecast: income 0.1% M/M; spending -0.3%

M/M; core PCE deflator 0.2% M/M, 2.5% Y/Y

Consensus: income 0.1% M/M; spending -0.2%

M/M; core PCE deflator 0.1% M/M, 2.5% Y/Y

The outlook for U.S. consumers remains bleak. Moreover, with a weakening domestic economy, deteriorating labour market conditions, declining household wealth and tighter lending conditions, there is little to suggest an imminent turn around in the fortune of the average U.S. consumer in the near term. In September, we expect consumer income to rise by a meager 0.1% M/M, while spending should drop by a profound 0.3% M/M – which will be the first monthly drop in this indicator in two years. On the inflation front, the core PCE deflator is expected to rise by 0.2% M/M on account of the pass-through of the past run-up in energy prices. However, on an annual basis, the core PCE deflator should ease to 2.5% Y/Y, from the 13-



year peak reached last month. In the months ahead, we expect further core PCE disinflation as the growing economic slack dampens consumer price pressures.

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Canadian Real GDP - August

Release Date: October 31/08

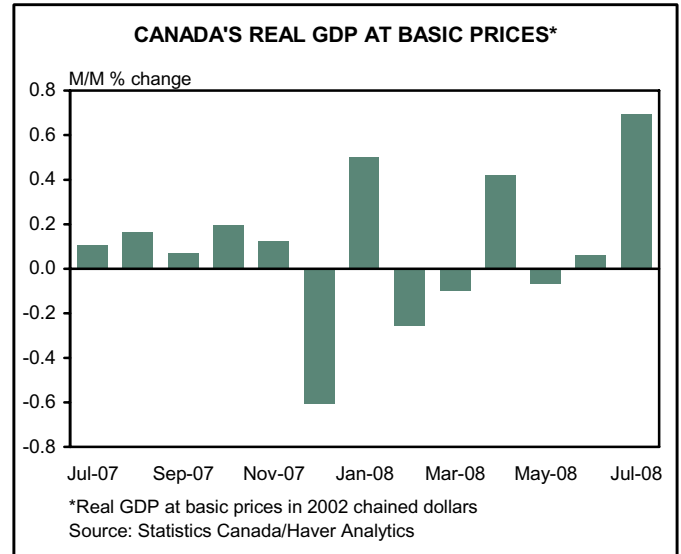
July Result: +0.7% M/M

TD Forecast: -0.4% M/M

Consensus: -0.3% M/M

Canadian economic activity is likely to be hit hard in August as the impact of a worsening U.S. economy, slumping commodity prices and weak manufacturing sector activity overwhelm the favorable support coming from the weakening domestic currency. In August, we expect Canadian GDP to fall by a sizeable 0.4% M/M, following the brisk +0.7% M/M pace in July. Much of the weakness during the month is expected to come from the dramatic slowdown in manufacturing sector production (which has declined by 3.7% M/M), with sluggish retail and wholesale activity, and declining real commodity exports providing additional drag on activity. If there are any risks to this forecast, they may even be to the downside. Looking ahead, we expect the Canadian economy to remain subdued, with little prospect of any meaningful economic growth in the coming months.

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RECENT KEY ECONOMIC INDICATORS
October 20 - October 24, 2008

		Data for	Units	Current	Prior	
Canada						
Oct 20	International Securities Transactions	Aug.	\$C, blns	-0.73	-5.48	R▲
Oct 20	Wholesale Sales	Aug.	M/M % chg.	-1.5	2.7	R▲
Oct 21	<i>Bank of Canada Rate</i>		%	2.25	2.50	
Oct 22	Leading Indicators	Sept.	M/M % chg.	-0.2	0.3	R▲
Oct 22	Retail Sales	Aug.	M/M % chg.	-0.3	0.1	
Oct 22	Retail Sales (Ex. Autos)	Aug.	M/M % chg.	-0.3	0.4	
Oct 23	<i>Bank of Canada Monetary Policy Report</i>					
Oct 24	Consumer Price Index	Sept.	Y/Y % chg.	3.4	3.5	
Oct 24	Bank of Canada CPI Core	Sept.	Y/Y % chg.	1.7	1.7	
United States						
Oct 20	Leading Indicators	Sept.	% change	0.3	-0.9	R▼
Oct 20	<i>Bernanke Testifies at House Budget Committee on Economy</i>					
Oct 20	<i>Atlanta Fed Governor Lockhart To Speak on U.S. Economic Outlook</i>					
Oct 20	<i>Fed Governor Kroszner Speaks on Risk Management in Baltimore</i>					
Oct 21	ABC Consumer Confidence	19-Oct	Index	-50	-48.0	
Oct 21	<i>Fed Governor Stern Speaks in Escanaba, Michigan</i>					
Oct 22	MBA Mortgage Applications	17-Oct	% change	-0.2	5.1	
Oct 23	Initial Jobless Claims	18-Oct	Thousands	478.0	463.0	R▲
Oct 23	Continuing Claims	11-Oct	Thousands	3720	3,726.0	R▲
Oct 23	House Price Index	Aug.	M/M % chg.	-0.6	-0.8	R▼
Oct 24	Existing Home Sales	Sept.	Millions	5.18	4.91	

Source: Bloomberg, TD Economics

UPCOMING NORTH AMERICAN ECONOMIC CALENDAR
October 27 - October 31, 2008

Release Date	Economic Indicators	Data for Period	Units	Consensus Forecast	Prior
Canada					
Oct 30	Industrial Product Price Index	Sept	M/M % chg.	-0.5	-0.2
Oct 30	Raw Materials Price Index	Sept	M/M % chg.	-4.3	-7.7
Oct 31	Gross Domestic Product	Aug	M/M % chg.	-0.30	0.70
United States					
Oct 27	New Home Sales	Sept	Thousands	455	460.0
Oct 28	<i>Former Fed's Volcker to Speak on Economy in Miami Beach</i>				
Oct 28	S&P/CaseShiller Home Price Index	Aug	Index	--	166.2
Oct 28	S&P/C-S Composite-20	Aug	Y/Y % chg.	-16.6	-16.4
Oct 28	Consumer Confidence	Oct	Index	52.3	59.8
Oct 28	Richmond Fed. Manufacturing Index	Oct	Index	-21.0	-18.0
Oct 28	<i>Treasury's Paulson Speaks At SIFMA Annual Meeting</i>				
Oct 28	<i>U.S. Federal Reserve Open Market Committee Meeting</i>				
Oct 28	ABC Consumer Confidence	26-Oct	Index	--	-50.0
Oct 29	MBA Mortgage Applications	24-Oct	% change	--	-16.6
Oct 29	Durable Goods Orders	Sept	% change	-1.0	-4.8
Oct 29	<i>Fed's Open Market Committee Meets on Interest Rates, Economy</i>				
Oct 29	<i>Former Fed's Volcker to Speak at IADI Conference in Washington</i>				
Oct 29	<i>FOMC Rate Decision</i>	29-Oct	%	1.00	1.50
Oct 30	Gross Domestic Product (GDP) (Annualized)	3Q A	Q/Q % change	-0.5	2.8
Oct 30	Personal Consumption	3Q A	% change	-1.9	1.2
Oct 30	Initial Jobless Claims	25-Oct	Thousands	470.0	478.0
Oct 30	Continuing Claims	18-Oct	Thousands	3,710.0	3,720.0
Oct 30	<i>Fed's Kroszner Speaks on Risk Management in New York</i>				
Oct 30	<i>Fed's Yellen Speaks in Berkeley, California</i>				
Oct 31	Personal Income	Sept	% change	0.1	0.5
Oct 31	PCE Deflator	Sept	Y/Y % chg.	4.2	4.5
Oct 31	Personal Spending	Sept	% change	-0.2	0.0
Oct 31	PCE Core	Sept	Y/Y % chg.	2.4	2.6
Oct 31	Employment Cost Index	3Q	%	0.7	0.7
Oct 31	Chicago Purchasing Managers Index	Oct	Index	48.3	56.7
Oct 31	U. of Michigan Confidence Index	Oct F	Index	58.0	57.5
Oct 31	<i>Fed's Bernanke Speaks at UC Berkeley</i>				

Source: Bloomberg, TD Economics

G-7 ECONOMIC RELEASES AND EVENTS

Date	Time*	Country	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
Oct 27	5:00	EU	Euro-Zone M3 s.a.	Sept	Y/Y % chg.	8.5	8.8
	10:00	U.S.	New Home Sales	Sept	Thousands	455	460
	19:50	Japan	Retail Trade	Sept	% Chg.	0.0	0.7
	20:30	AU	NAB Business Confidence	3Q	Index	--	-8.0
Oct 28	3:45	France	Consumer Confidence Indicator	Oct	Index	-46	-44
	8:00	U.S.	<i>Former Fed's Volcker to Speak on Economy in Miami Beach</i>				
	9:00	U.S.	S&P/CaseShiller Home Price Index	Aug	Index	--	166.2
	9:00	U.S.	S&P/C-S Composite-20	Aug	Y/Y % chg.	-16.6	-16.4
	10:00	U.S.	Consumer Confidence	Oct	Index	52.3	59.8
	10:00	U.S.	Richmond Fed. Manufacturing Index	Oct	Index	-21	-18
	10:00	U.S.	<i>Treasury's Paulson Speaks At SIFMA Annual Meeting</i>				
	--	U.S.	<i>U.S. Federal Reserve Open Market Committee Meeting</i>				
	17:00	U.S.	ABC Consumer Confidence	26-Oct	Index	--	-50.0
	17:45	NZ	Trade Balance	Sept	Millions	--	-750.0
	19:50	Japan	Industrial Production	Sept	Y/Y % chg.	-0.3	-6.9
Oct 29	--	Germany	Consumer Price Index	Oct	Y/Y % chg.	2.4	2.9
	5:30	U.K.	M4 Money Supply	Sept F	Y/Y % chg.	--	12.2
	5:30	U.K.	Mortgage Approvals	Sept	Thousands	32.0	32.0
	7:00	U.S.	MBA Mortgage Applications	24-Oct	% change	--	-16.6
	8:30	U.S.	Durable Goods Orders	Sept	% change	-1.0	-4.8
	9:00	U.S.	<i>Fed's Open Market Committee Meets on Interest Rates, Economy</i>				
	11:15	U.S.	<i>Former Fed Chair Volcker to Speak at IADI Conference in Washington</i>				
	14:15	U.S.	FOMC Rate Decision	29-Oct	%	1.00	1.50
	17:45	NZ	Building Permits	Sept	M/M % chg.	--	-7.9
	22:00	NZ	M3 Money Supply	Sept	Y/Y % chg.	--	7.2
	Oct 30	3:45	France	Producer Prices	Sept	Y/Y % chg.	6.5
4:55		Germany	Unemployment Rate s.a.	Oct	%	7.6	7.6
6:00		EU	Business Climate Indicator	Oct	Index	-0.9	-0.8
6:00		EU	Consumer Confidence	Oct	Index	-20.0	-19.0
6:00		EU	Economic Confidence	Oct	Index	86.0	87.7
8:30		Canada	Industrial Product Price Index	Sept	M/M % chg.	-0.5	-0.2
8:30		Canada	Raw Materials Price Index	Sept	M/M % chg.	-4.3	-7.7
8:30		U.S.	Gross Domestic Product (GDP) (Annualized)	3Q A	Q/Q % change	-0.5	2.8
8:30		U.S.	Personal Consumption	3Q A	% change	-1.9	1.2
8:30		U.S.	Initial Jobless Claims	25-Oct	Thousands	470	478
8:30		U.S.	Continuing Claims	18-Oct	Thousands	3710	3720.0
8:30		U.S.	<i>Fed Governor Kroszner Speaks on Risk Management in New York</i>				
15:15		U.S.	<i>Fed Governor Yellen Speaks in Berkeley, California</i>				
19:30		Japan	Jobless Rate	Sept	%	4.2	4.2
19:30		Japan	Household Spending	Sept	Y/Y % chg.	-4.0	-4.0
--		Japan	BoJ Target Rate Decision	30-Oct	%	0.5	0.5
Oct 31	1:00	Japan	Housing Starts	Sept	Y/Y % chg.	51.5	53.6
	3:00	Germany	Retail Sales	Sept	Y/Y % chg.	--	-3.0
	6:00	EU-12	CPI Estimate	Oct	Y/Y % chg.	3.2	3.6
	6:00	EU-12	Unemployment Rate	Sept	%	7.5	7.5
	8:30	Canada	Gross Domestic Product	Aug	M/M % chg.	-0.3	0.7
	8:30	U.S.	Personal Income	Sept	% change	0.1	0.5
	8:30	U.S.	PCE Deflator	Sept	Y/Y % chg.	4.2	4.5
	8:30	U.S.	Personal Spending	Sept	% change	-0.2	0.0
	8:30	U.S.	PCE Core	Sept	Y/Y % chg.	2.4	2.6
	8:30	U.S.	Employment Cost Index	3Q	%	0.7	0.7
	10:00	U.S.	Chicago Purchasing Managers Index	Oct	Index	48.3	56.7
	10:00	U.S.	U. of Michigan Confidence Index	Oct F	Index	58.0	57.5
	14:00	U.S.	<i>Fed Chair Bernanke Speaks at UC Berkeley</i>				

* Eastern Standard Time; Sources: Bloomberg, TD Economics

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