CANADIAN FORECAST EXECUTIVE SUMMARY

AUGUST 2010

Update of the Canadian Short-Term Outlook

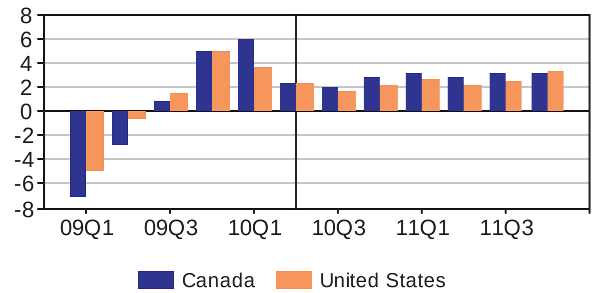
Slowing Growth in Canada

Evidence is growing that real economic output in both the United States and Canada is slowing significantly. Second-quarter real GDP growth in the United States was weak at 2.4%. The outlook for the third quarter is the worst yet of this year, as real GDP growth is expected to decelerate to a dismal 1.7%. The forecast calls for a marked slowdown in fixed non-residential investment and government sectors. The biggest drag on the U.S. outlook is the retrenchment of residential construction investment, plunging at a double-digit pace in the third quarter. The U.S. economy is forecasted to grow by 2.8% this year and a slightly milder 2.4% in 2011.

The euphoric feeling of Canada's strong growth prospects expected earlier this year has diminished now to a tiny hope. The weakness experie nced south of the border and in Europe is spreading to Canada. As well, slowing demand is spreading throughout most sectors, particularly consumer spending, residential investment, and trade. We have downgraded our economic outlook for both second- and third-quarter growth. Real GDP will grow around 2.4% in the second quarter and closer to 2.0% in the third quarter as these headwinds weigh on domestic and foreign demand. We are still expecting Canadian real GDP growth to outperform that of the United States this year and next, with output growing 3.2% and 2.9%, respectively.

Canada and U.S. — Slowing Growth

(Real GDP, percent change, annualized)



Canada's domestic demand is already wavering and we judge that the consumer will probably not be a significant contributor to growth over the next few quarters. A deteriorating trade balance is evidence that economic woes in the United States and Europe are affecting Canada, and that weakening foreign demand will weigh on Canada's economic output as well. Some commodity prices have bounced back since June, particularly oil. Rising commodity prices will prop up Canada's nominal trade balance, but the ongoing deceleration in the growth of real exports will act as a fairly major drag on overall real GDP growth in the second half of 2010.

Canadian real GDP by industry edged up by 0.1% in May. This was a welcome advance after the flat reading in the prior month. There were mixed results as the advances and

In This Issue

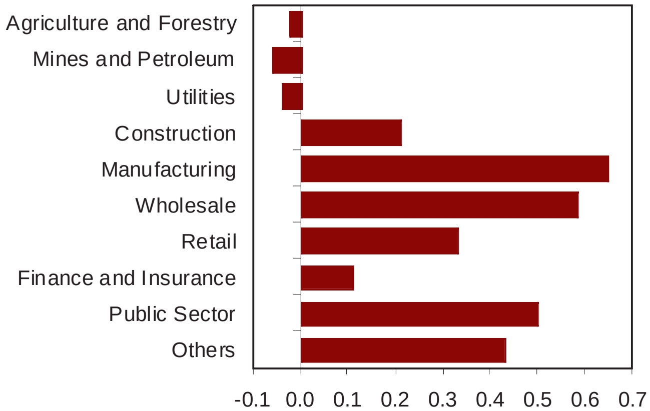
Update of the Canadian Short-Term Outlook
Special Topic: Canadian Dollar Report—Keeping an Eye on the Loonie
Special Topic: Canada's Job Recovery—Swift, But Not Solid
U.S. August Forecast Highlights and Summary Table
Canadian August Forecast Summary Table

Recent and Upcoming Special Reports/Presentations

Canadian Economic Outlook Seminar: "Charting the North American Economic Recovery: Key Drivers of the Economic Expansion Beyond 2010" (September 22, 2010). Please visit the website, http://www.ihsglobalinsight.com/Events/EventDetail104825.htm

IHS GLOBAL INSIGHT

Major Industrial Sectors' Contribution to Total Growth
(Year to date, percentage points)

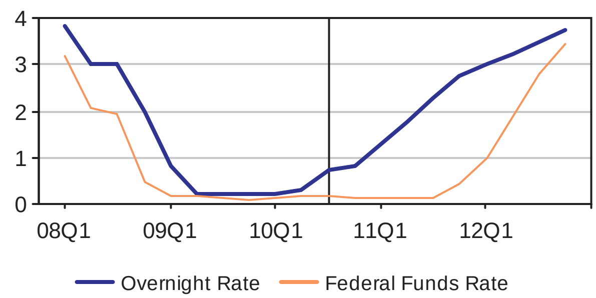


declines in output varied across industries. The overall increase in economic output was led by the 0.6% jump in the goods-producing industries. Three of the five sectors advanced handily. Among the gainers, output in mining and oil and gas extraction led the way with a 3.4% leap. All areas within this sector gained, reflecting a healthy increase in commodity demand, which is a vital boon to the Canadian economy.

Leading the overall decline in output in the services-producing industry was the 1.8% drop in wholesale trade activity. There was also a 0.1% fall in finance, insurance, and real estate activity. The slowing existing-homes market resulted in an 11.3% nose dive in real estate agents' and brokers' output.

Canadian housing start fell by 1.6% in July to 189,200 units (annualized). Housing starts are on a downward trend; this was the third consecutive decline. We were forecasting housing starts to fall to 190,000 units from June's final reading of 192,300 units. The likelihood of starts hitting the 200,000 mark is very small, especially as mortgage rates climb. The housing starts forecast is unchanged at 189,000 units this year and 177,000 units in 2011.

Monetary Policy Trends
(Percent)



The Bank of Canada announced another technical upward adjustment to short-term interest rates, bumping the overnight and bank rates up by a quarter of a point each to 0.75% and 1.00%, respectively. The move was widely expected as the Bank has sent signals that it intends to "normalize" the level of short-term interest rates.

The Bank of Canada has made a couple of upward technical adjustments to short-term borrowing rates in the past two months, but market rates and mortgage rates have jumped considerably higher as markets extrapolated further tightening moves by the Bank. This effective tightening in monetary conditions is expected to propagate through the economy and, in conjunction with a major slowdown in the U.S. economy, will lead to considerably slower growth in the second half of 2010 and in 2011. Thus, it is no surprise that the Bank of Canada has downgraded its outlook for growth in 2010 and 2011, and there is a strong likelihood that the outlook will have to be reduced yet again in the fall 2010 update.

by Arlene Kish and Brian Bethune

High-Frequency Indicators
(As of August 8)

	May-10	Jun-10	Jul-10	Aug-10	Sep-10	Oct-10	Dec-10
Real GDP by Industry (M/M, percent)	**0.1**	0.2	0.2	0.3	0.3	0.3	0.3
Employment (Thous.)	**25**	**93**	**-9**	15	13	20	25
Unemployment Rate (Percent)	**8.1**	**7.9**	**8.0**	7.9	7.8	7.8	7.7
Consumer Price Index (Y/Y, percent)	**1.4**	**1.0**	2.0	1.9	2.1	2.3	2.2
Exchange Rate, Month-End (U.S. cents)	**95.83**	**93.93**	**97.25**	96.55	96.57	96.76	98.06
Exchange Rate, Average (U.S. cents)	**96.16**	**96.35**	**95.90**	96.59	96.52	96.62	97.57
3-Month T-Bill Rate, Month-End	**0.50**	**0.50**	**0.66**	0.70	0.73	0.76	1.15
Overnight Rate, Month-End	**0.25**	**0.50**	**0.75**	0.75	0.75	0.75	1.00

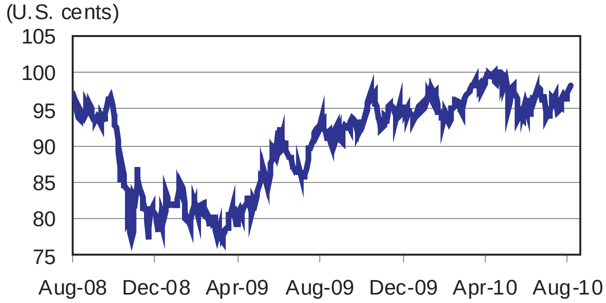
Note: Bolded numbers indicate historical data.

Special Topic: Canadian Dollar Report—Keeping an Eye on the Loonie

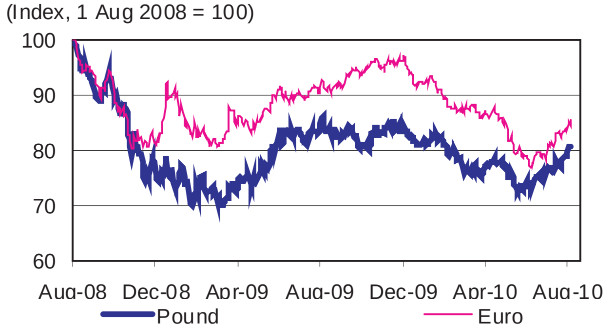
After stalling out around 96 U.S. cents since the start of the summer months, the Canadian dollar is heating up and making another run for parity. Typically, energy prices—especially oil—have heavily influenced the direction of the dollar. This time around, however, there is a general uptick in the currency because all of the drivers are supporting the lift. The loonie is very close to hitting parity with the U.S. dollar, but the question remains whether it will hit it and hold it throughout 2010. We examine the three major drivers that influence the movement of the Canadian dollar: other exchange rates, interest-rate spreads, and commodity prices. We will try to answer the question, where will the loonie float this year?

There have been plenty of heavy hitters swaying financial markets since the start of the year. If it wasn't questions regarding the economic recovery in global markets, especially in the United States, there were issues surrounding the sovereign debt crisis that are still playing out (to a lesser degree) today. Through it all, though, the Canadian dollar has remained resilient. The general weakness of the U.S. dollar has helped the Canadian dollar's upward drift. Plus, the steady appreciation of both the euro and the U.K. pound for most of this time was another source of strength. Indeed, with the swift upward movement of these two currencies, the outlook for the loonie is positive.

The Lofty Loonie
(U.S. cents)

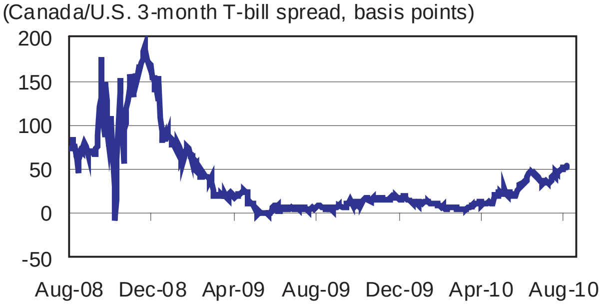


The U.K. Pound and Euro Also Rise
(Index, 1 Aug 2008 = 100)

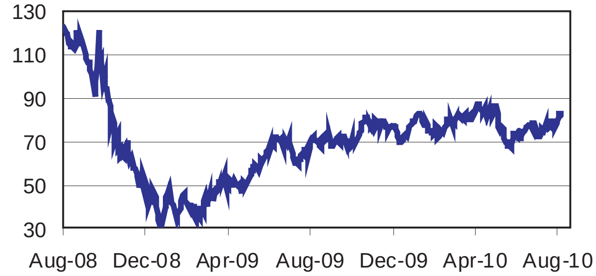


The period of increased monetary policy easing by both the Federal Reserve and the Bank of Canada is well over. The Fed is likely to keep the federal funds target rate at the historical low level well into next year. The U.S. recovery is still on shaky ground, with a still-weak labour market and a troublesome housing market. On the flip side, Canada's economic recovery is stronger, but it is beginning to lose momentum. Employment is close to pre-recession levels and job gains have been concentrated in the public sector. The upward momentum in Canada's housing market since late last year has slowed significantly. Nevertheless, the Bank of Canada has raised the overnight rate twice already this year, by 25 basis points in both June and July. With the increase in this policy rate, Canadian/U.S. interest rate spreads have widened. Canada's three-month Treasury bill yield is around 0.7% while the U.S. Treasury three-month bill yield sits around 0.16%. Currently, the Canada/U.S. three-month Treasury bill spread is at an 18-month high. We are forecasting the Bank of Canada to continue on the monetary tightening path, but not until late this year. As such, interest rate spreads will widen even further, at least until mid-2011. Therefore, spreads will likely heavily influence the upward movement of the Canadian dollar in the near term.

Spreads Widen
(Canada/U.S. 3-month T-bill spread, basis points)



Oil Prices Grease the Canadian Dollar Wheel
(U.S. dollars per barrel)



The rise in oil prices has been the main driver behind the Canadian dollar's recent ascent. Oil prices have again edged above US$80/barrel. IHS Global Insight is forecasting oil prices to hover just below this level for the remainder of 2010, with only a slight increase expected in 2011. Therefore, barring any shock to the market, oil prices are likely to steady this year and next—a neutral for the Canadian dollar.

There are still risks to the outlook for the Canadian dollar. IHS Global Insight believes that market fundamentals do not support a quick advance in oil prices, therefore, some downward adjustment to prices is likely in the near term—posing highly probable downside risks for the loonie. Uneven or deteriorating economic activity in Europe would likely put the U.S. dollar in a favourable position, with an uptick in safe-haven buying. Our outlook for the Canadian dollar has not changed too much from last month: it should end the year around 98 U.S. cents, and then head towards parity over the subsequent six months. Theeafter, the Canadian dollar will remain in the low-to-mid-90 U.S. cent range, close to purchasing power parity values.

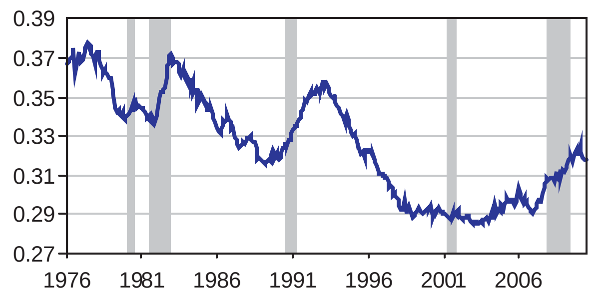
by Arlene Kish

Special Topic: Canada's Job Recovery—Swift, But Not Solid

Canadian employment, hit hard by the global recession, reached a cycle low just under 16.8 million workers in July 2009. A year later, almost all jobs lost have been recovered, but is that enough? We find that although job creation in Canada has been swift, the types of employment gains are not solid and therefore the recovery is still somewhat shaky, implying that the outlook for the Canadian economy is sluggish in the near term.

Since the employment cycle troughed last year, jobs gains have mostly been concentrated in the public sector. Here we are defining public-sector jobs to include those in educational services, healthcare, and public administration. The ratio of public to private sector workers is just slightly down from the recent high of 33%. In four of the past five recessions, this ratio has climbed sharply, reflecting the government's stimulus job creation. And, according to the latest employment data, the total share of public employees relative to all employees is at 24.4%, a 2.6% increase in the share from the total employment peak back in October 2008.

Public Sector Recovery
(Ratio, public/private sector employees)



Note: Shaded area indicates recession

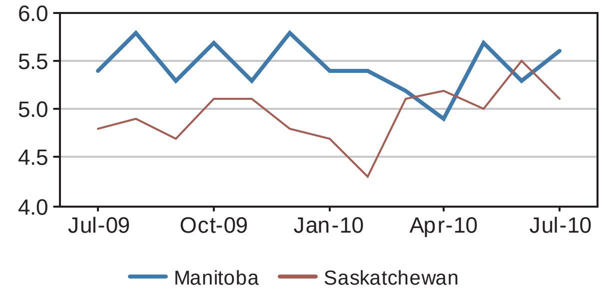
Based on year-earlier data, healthcare employment is up a very strong 6.2% and public administration increased by 4.0%. Education jobs are down 1.1% from a year earlier, but the sector took a massive hit and suffered severe job losses (down 65,000) last month. Overall, education jobs are up 2.5% in the first seven months of the year, relative to all of 2009. As is typical with recession-based recovery, the government sector generates jobs to stimulate the economy. However, this cannot and should not last. As stimulus projects come to an end and government fiscal policy calls for balanced budgets, there will likely be job losses in the public sector, requiring the employment market to rely more heavily on the private sector to keep the job creation engines running.

Not only has there been an increase in public sector workers, but many of the overall jobs recouped have been in part-time employment. The share of part-time workers relative to all employees is at an all-time high of 20% (with data going back to 1976). Part-time workers have increased more than 5% from a year earlier. In addition, average weekly hours, which was already on a downward trend, have hit a record low of 36.4 hours. Obviously the pickup in part-time employment is not favourable to sustainable economic growth, but businesses remain cautious. However, in the July Bank of Canada Business Outlook Survey, businesses expressed a strong positive sentiment regarding increasing payrolls over the coming year. Therefore, we believe that the heavy reliance on part-time workers is only temporary and will eventually be replaced by a stronger full-time employment workforce.

The unemployment rate increased from 7.9% to 8.0% in July, which was not too much of a surprise. Regionally, there have been large swings in provincial unemployment rates, especially in Atlantic Canada, where the jobless rates are among the highest in Canada. Moreover, employment growth in Manitoba is catching up to the strong performance by Saskatchewan last year, as the two provinces have changed pole position over the last few months for the lowest unemployment rate in Canada. In terms of annual employment growth among the provinces, however, Prince Edward Island leads the pack with 3.6% gains, followed by British Columbia (3.0%), Ontario (2.6%), and Quebec (2.5%).

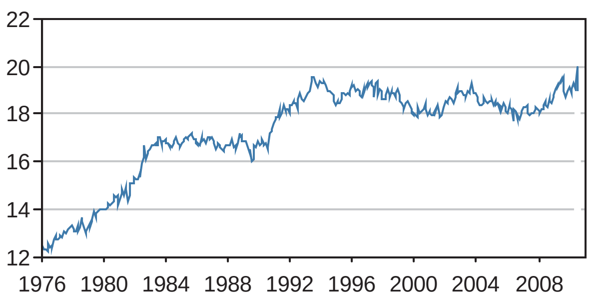
Race to the Bottom

(Unemployment rate, percent)



Part-Time Worker Boost

(Percent, part-time/total employment)



In the near term, without solid full-time employment growth, the consumer outlook is weakening. We have already seen a dip in consumer confidence for June, and the outlook for Canada's housing market is gearing down and purchases of new motor vehicles are cooling. With July's uninspiring and dismal Labour Force Survey results, the evidence of slowing growth in the second and third quarter is mounting. Yet, productivity gains will likely remain robust in the near term as investment in machinery and equipment trickle through to increased output. Ultimately a brighter Canadian and U.S. economic recovery, stronger corporate demand, and increased activity in private sector hiring will lead to a more confident consumer, which is a positive for Canadian economic growth. We have lowered our third-quarter employment growth outlook from 1.9% to 1.6% for this year, as the bulk of job gains already occurred in the second quarter. For all of 2010, employment will grow around 1.7%.

by Arlene Kish

TABLE 2
Canadian Short-Term Forecast Update

	09Q4	10Q1	10Q2	10Q3	10Q4	11Q1	2010	2011	2012	2013	2014	2015
Real GDP (Bil. chained 2002 $)	1296.4	1315.6	1323.3	1330.1	1339.5	1350.1	1327.1	1365.4	1405.6	1444.2	1481.3	1518.1
Annual % Ch.	4.9	6.1	2.4	2.1	2.8	3.2	3.2	2.9	2.9	2.7	2.6	2.5
Consumer	825.2	834.1	839.2	844.0	848.7	853.2	841.5	860.4	880.0	900.8	921.3	941.3
Annual % Ch.	3.9	4.4	2.5	2.3	2.2	2.2	3.3	2.2	2.3	2.4	2.3	2.2
Government	331.3	333.1	333.8	338.3	341.1	341.3	336.6	344.3	350.2	353.0	358.7	366.7
Annual % Ch.	9.1	2.3	0.7	5.5	3.4	0.2	4.7	2.3	1.7	0.8	1.6	2.2
Bus. Res. Investment	75.4	79.5	82.6	83.0	83.5	84.0	82.2	84.8	87.2	89.0	90.2	91.5
Annual % Ch.	26.3	23.6	16.6	1.9	2.2	2.5	15.4	3.3	2.8	2.1	1.3	1.5
Bus. Non-Res. Inv.	154.7	155.1	158.6	160.8	162.6	164.1	159.3	166.4	172.2	177.3	181.2	184.7
Annual % Ch.	-9.8	0.9	9.5	5.6	4.5	3.9	-0.5	4.5	3.5	3.0	2.2	1.9
Exports	428.0	440.3	449.9	456.8	463.4	470.4	452.6	481.0	511.4	541.1	571.6	605.2
Annual % Ch.	13.8	12.0	9.0	6.2	5.9	6.1	8.4	6.3	6.3	5.8	5.6	5.9
Imports	525.3	542.9	553.0	560.1	566.4	573.0	555.6	582.5	609.3	636.7	664.6	694.6
Annual % Ch.	12.4	14.1	7.6	5.3	4.6	4.7	11.2	4.8	4.6	4.5	4.4	4.5
Business Inventory Ch.	-1.2	8.2	11.1	6.3	5.5	8.9	7.8	9.7	12.3	18.0	20.6	20.4
Statistical error	0.0	-1.4	0.0	0.0	0.0	0.0	-0.3	0.0	0.0	0.0	0.0	0.0
Nominal GDP (Billion $)	1561.2	1600.5	1624.2	1643.5	1663.7	1685.1	1633.0	1719.8	1816.4	1911.3	2002.2	2090.0
Annual % Ch.	9.9	10.4	6.1	4.8	5.0	5.2	6.9	5.3	5.6	5.2	4.8	4.4
Raw Mat. Price Index	163.0	168.7	162.8	162.8	161.7	160.5	164.0	159.7	159.5	161.6	163.9	167.1
% Ch. Year Ago	7.6	23.7	6.8	3.8	-0.8	-4.9	7.8	-2.6	-0.1	1.3	1.4	2.0
Industry Price Index	115.9	116.9	117.1	117.8	117.8	118.8	117.4	120.3	122.7	124.9	126.9	128.5
% Ch. Year Ago	-3.4	-0.6	0.5	1.7	1.6	1.6	0.8	2.5	2.0	1.8	1.6	1.3
GDP Deflator	120.4	121.7	122.7	123.6	124.2	124.8	123.1	125.9	129.2	132.3	135.2	137.7
Annual % Ch.	4.4	4.4	3.5	2.7	2.1	2.0	3.6	2.4	2.6	2.4	2.1	1.9
CPI	114.9	115.4	116.2	117.0	117.4	117.7	116.5	118.6	120.9	123.3	125.8	128.3
% Ch. Year Ago	0.8	1.6	1.4	2.0	2.2	2.0	1.8	1.8	1.9	2.0	2.0	2.0
Employment (Thousands)	16876	16944	17119	17188	17280	17355	17133	17461	17700	17957	18235	18484
Annual % Ch.	1.3	1.6	4.2	1.6	2.1	1.8	1.7	1.9	1.4	1.5	1.5	1.4
Unemployment Rate (%)	8.4	8.2	8.0	7.9	7.7	7.6	8.0	7.5	7.3	7.1	6.8	6.5
Productivity (Annual % Ch.)	3.7	4.4	-1.8	0.5	0.7	1.5	1.5	1.0	1.6	1.3	1.0	1.1
Average Hourly Earnings	20.52	20.58	20.75	20.87	20.99	21.12	20.80	21.34	22.06	22.96	23.87	24.78
Annual % Ch.	1.0	1.2	3.3	2.4	2.4	2.5	1.7	2.6	3.4	4.1	4.0	3.8
3-Month T-Bill Rate (%)	0.22	0.21	0.47	0.82	1.00	1.44	0.63	2.18	3.38	4.31	4.75	4.75
US 3-Month T-Bill Rate (%)	0.06	0.11	0.15	0.18	0.22	0.23	0.16	0.38	2.38	3.45	4.07	4.60
Canada-U.S. Differential (% pts.)	0.16	0.11	0.32	0.65	0.79	1.20	0.47	1.80	1.00	0.86	0.67	0.15
Prime Rate (%)	2.25	2.25	2.33	2.75	2.82	3.28	2.54	4.03	5.38	6.31	6.75	6.75
Overnight Rate (%)	0.24	0.25	0.33	0.75	0.82	1.28	0.53	2.03	3.38	4.31	4.75	4.75
Bank Rate (%)	0.50	0.50	0.58	1.00	1.07	1.53	0.79	2.28	3.63	4.56	5.00	5.00
GOC Bond Rate (1-3 yrs.) (%)	1.26	1.34	1.59	1.75	1.86	2.13	1.64	2.62	3.74	4.52	4.99	5.18
GOC Bond Rate (3-5 yrs.) (%)	2.34	2.35	2.43	2.42	2.47	2.63	2.42	2.93	3.99	4.67	5.16	5.49
GOC Ten-Year Bond Rate (%)	3.43	3.45	3.33	3.15	3.14	3.18	3.27	3.28	4.28	4.83	5.35	5.83
U.S. Ten-Year T-Note Rate (%)	3.46	3.72	3.49	3.00	2.99	3.03	3.30	3.13	4.13	4.68	5.20	5.68
U.S. Real GDP (Bil. 2000 US$)	13019.0	13138.8	13216.5	13271.8	13345.1	13432.9	13243.0	13555.5	13952.8	14353.7	14816.4	15262.5
Annual % Ch.	5.0	3.7	2.4	1.7	2.2	2.7	2.8	2.4	2.9	2.9	3.2	3.0
Household Credit (Billion $)	1395.7	1422.2	1449.7	1477.8	1506.5	1535.6	1464.0	1578.7	1685.0	1779.1	1865.9	1949.6
Annual % Ch.	8.3	7.8	7.9	8.0	8.0	8.0	7.9	7.8	6.7	5.6	4.9	4.5
Standard of Living Canada/U.S. (Nominal GDP per Capita at PPP Can/U.S.)							0.831	0.836	0.838	0.837	0.832	0.826
Exchange Rate (U.S.-Can.)	94.7	96.1	97.3	96.3	97.0	99.0	96.7	98.4	94.9	93.7	92.1	89.0
Curr. Acct. Bal. (Billion $)	-40.8	-31.3	-36.9	-37.1	-30.0	-23.2	-33.8	-15.4	-0.2	7.7	13.9	16.2
Fed. Gov't. NA Bal.(Billion $)	-37.5	-24.0	-21.4	-20.5	-19.2	-17.5	-21.3	-15.7	-11.6	-8.8	-2.2	3.5
% GNP	-2.4	-1.5	-1.3	-1.3	-1.2	-1.0	-1.3	-0.9	-0.6	-0.5	-0.1	0.2
Before-Tax Profit (Billion $)	158.9	172.6	192.0	196.5	200.4	201.3	190.4	209.0	225.6	234.7	246.3	248.5
Annual % Ch.	36.8	39.1	53.4	9.7	8.2	1.7	29.6	9.8	8.0	4.0	5.0	0.9
Housing Starts (Thousands)	178	193	199	186	179	174	189	177	180	185	185	183
Auto Sales (Thous. SAAR)	1550.9	1591.5	1543.7	1557.0	1534.4	1578.3	1556.6	1635.7	1687.6	1735.7	1757.4	1718.7
Nominal Exports (Billion $)	450.9	470.7	481.6	491.5	501.1	511.0	486.2	525.9	569.7	612.0	655.0	700.2
Nominal Imports (Billion $)	471.3	484.2	496.6	505.5	513.6	521.9	500.0	533.2	566.9	602.3	639.6	682.8
Nominal Trade Balance (Billion $)	-20.5	-13.6	-15.0	-14.0	-12.5	-10.9	-13.8	-7.3	2.8	9.6	15.4	17.4
Personal Saving Rate (%)	3.5	2.8	3.0	3.2	3.4	3.4	3.1	3.7	4.5	5.3	5.5	5.8
Real Disp. Inc. - Annual % Ch.	0.1	1.1	2.8	2.6	2.7	2.1	1.5	2.5	3.0	3.2	2.5	2.5
Industrial Production - Annual % Ch.	9.4	11.4	1.3	7.3	10.8	8.7	4.6	8.2	6.3	4.2	4.1	3.7