

## **North American Economic Outlook: “Climbing Out of Recession”**

**Presentation to the Canadian Association of  
Movers**

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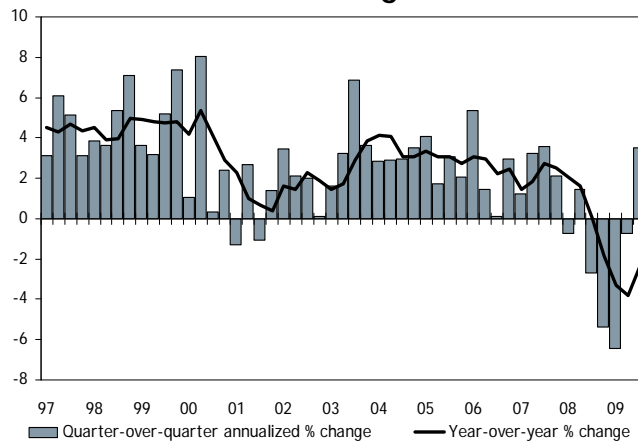
## **U.S. Economic Outlook:**

**Return of Positive Growth  
Expected to be Sustained**



**The U.S. economy is starting to recover from a severe shock that boosted the cost-of-capital**

**U.S real GDP growth**

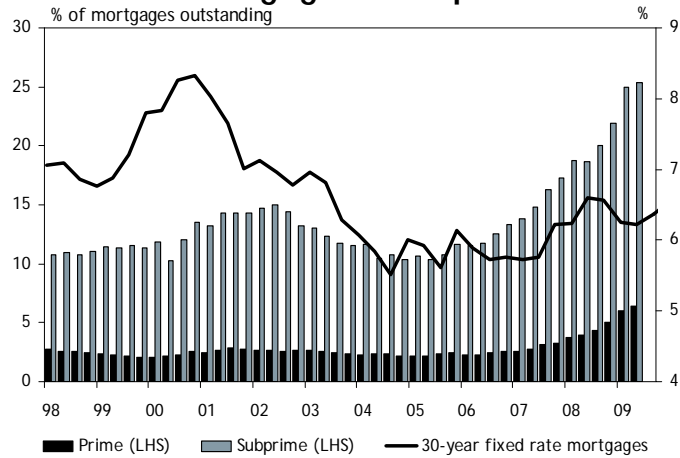


Source: Bureau of Economic Analysis, RBC Economics Research



**The rise in defaults on subprime mortgages was the catalyst for this pressure in financial markets**

**U.S. mortgage delinquencies**



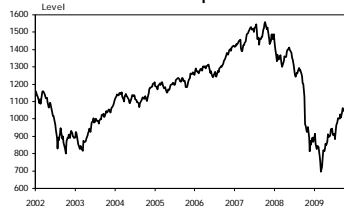
Source: MBA, RBC Economics Research



**The uncertainty as to who holds U.S. subprime assets had weighed on financial markets though greater stability is starting to emerge**

**Weekly observation**

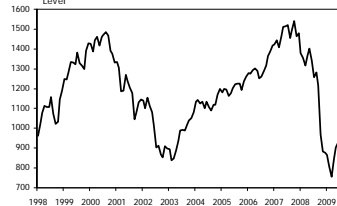
S&P 500 composite index



Source: Bloomberg, RBC Economics Research

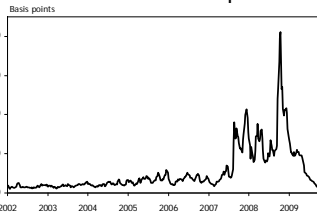
**Monthly observation**

S&P 500 composite index



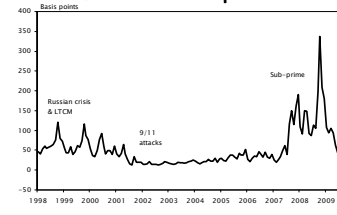
Source: Bloomberg, RBC Economics Research

**Three-month TED spread\***



\*Three-month LIBOR rate minus three-month T-bill  
Source: Federal Reserve Board, RBC Economics Research

**3-month TED spread\***

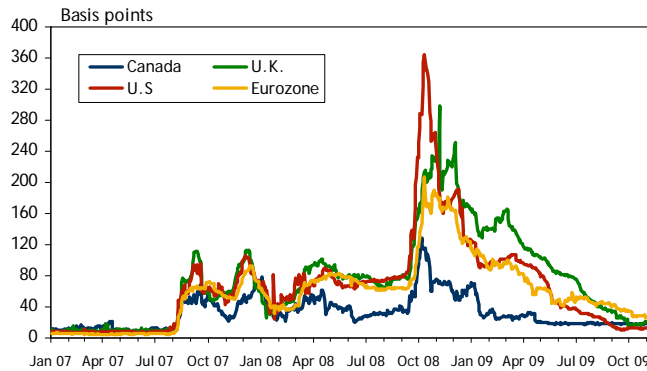


\*3-month LIBOR rate - 3-month T-bill  
Source: Federal Reserve Board, RBC Economics Research



**The rise in lending cost was more muted in Canada**

**Short-term funding spreads  
3 month LIBOR vs. OIS**



Source: Bloomberg, RBC Economics Research



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## **What prompted the improvement in financial markets?**



## **Aggressive policy actions by the Administration and Congress:**

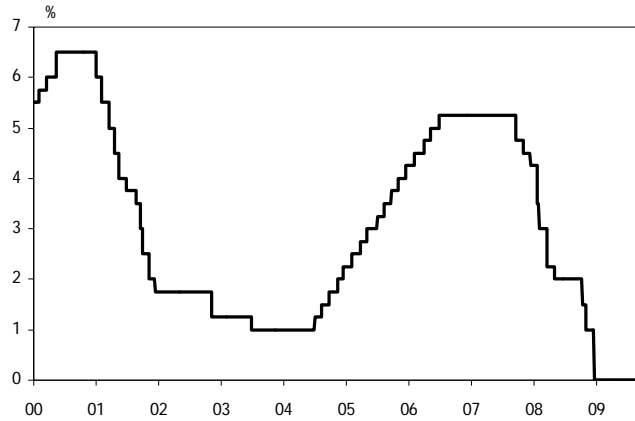
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- **undertook credible stress tests of the banking system**
- **committed over a trillion dollars to “rid the system of toxic assets”**
- **the Obama Administration introduced a \$787 billion fiscal stimulus package**
- **undertook initiatives to stem mortgage delinquencies**



**The Fed has been forcefully cutting interest rates though with rates bordering on 0%. . .**

### U.S. Fed funds rate

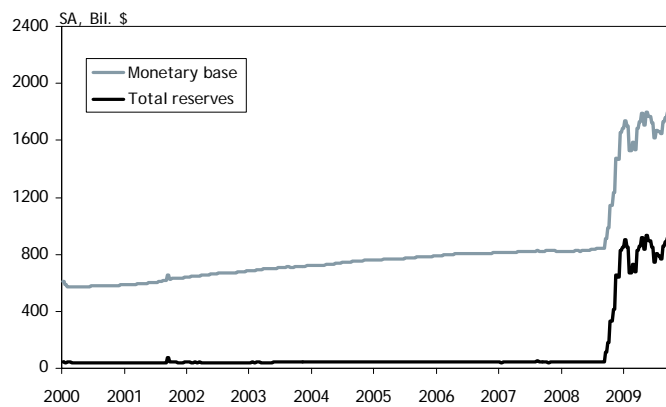


Source: Federal Reserve Board, RBC Economics Research



**... the central bank turned increasingly to “using its balance sheet”**

### Reserves held by the Fed

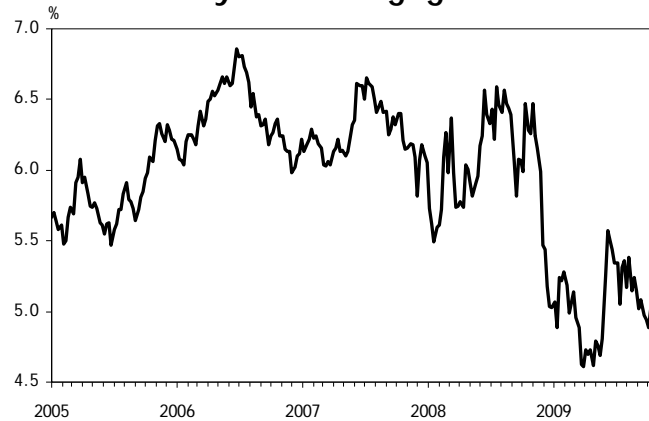


Source: Federal Reserve Board, RBC



## Fed actions were successful in pushing mortgage rates lower

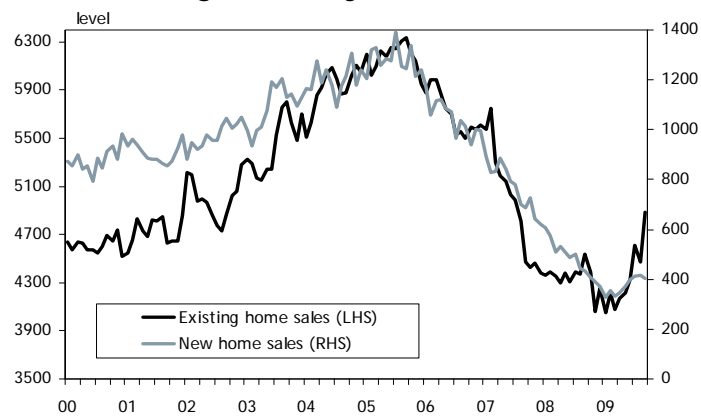
### 30-year mortgage rate



Source: Mortgage Bankers Association, RBC Economics Research

## Hints of a stabilization in home sales does provide a hopeful sign that housing has troughed

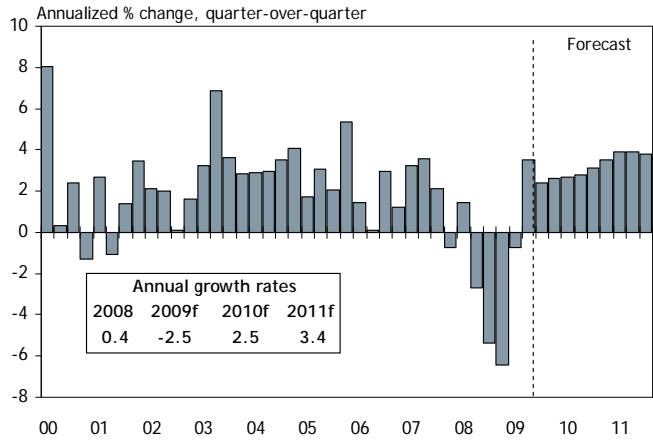
### Single family homes sold



Source: National Association of Realtors, Bureau of Census, RBC Economics Research

**A steady easing in credit tightening and stimulative policy are expected to allow positive growth to be sustained**

### U.S. real GDP



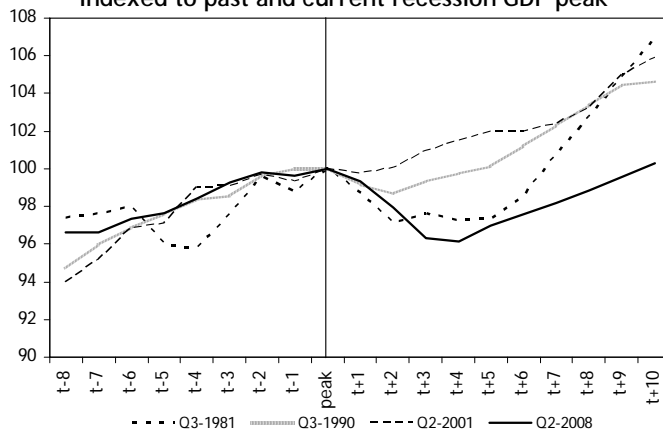
Source: Bureau of Economic Analysis, RBC Economics Research



**However, the recovery is expected to be the weakest relative to past three cycles...**

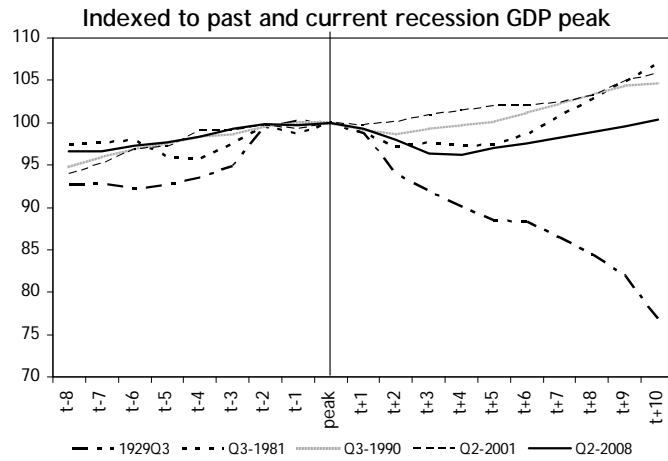
### U.S. GDP

Indexed to past and current recession GDP peak



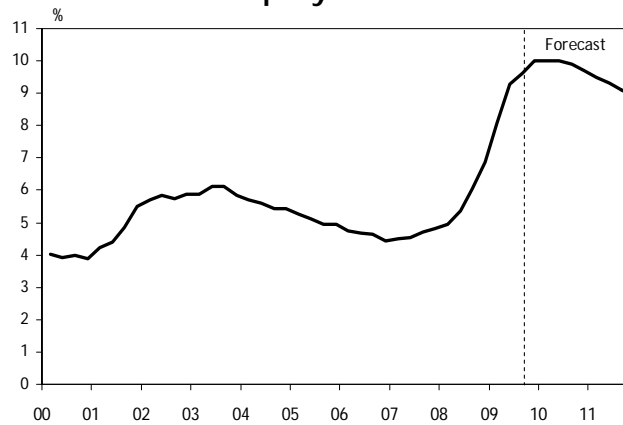
...though it will be markedly less weak compared to the Depression of the 1930s

### U.S. GDP



The modest recovery will keep unemployment historically high...

### Unemployment rate



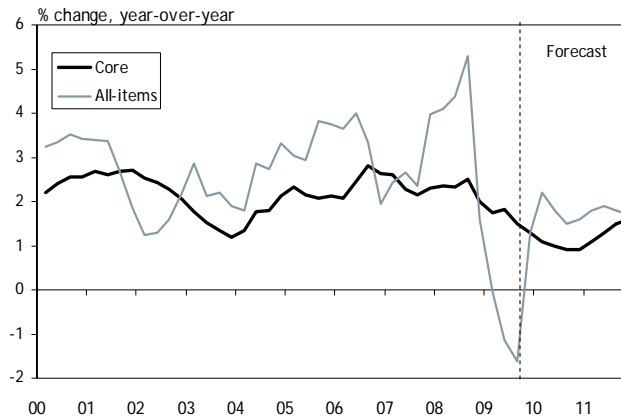
Source: Bureau of Labor Statistics, RBC Economics Research





**...and inflation low...**

### U.S. inflation

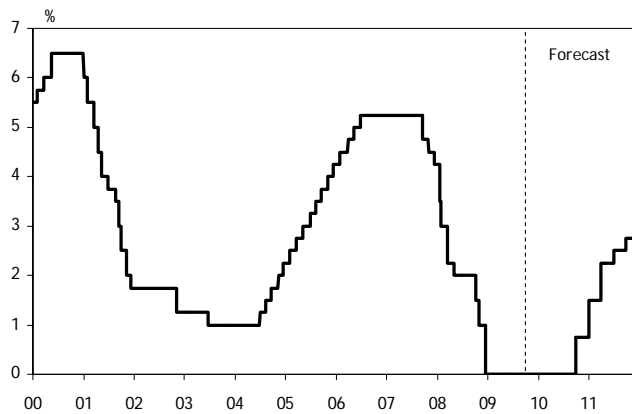


Source: Bureau of Labor Statistics, RBC Economics Research



**...that will delay the tightening in monetary policy until late next year**

### U.S. Fed funds rate



Source: Federal Reserve Board, RBC Economics Research

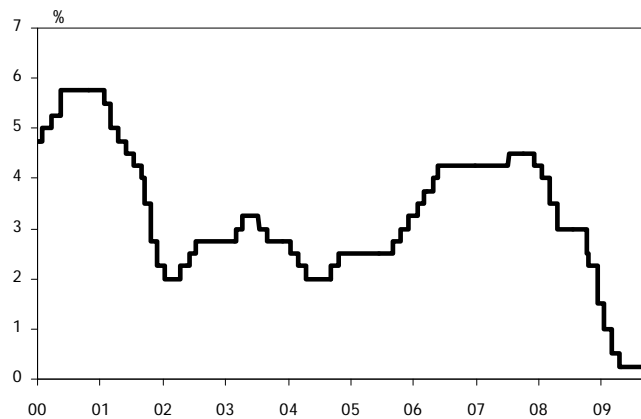


## Canadian Economic Outlook: Pulling Out of Recession



**Canada has weathered the U.S. downturn helped by  
an aggressive easing in policy...**

### Bank of Canada overnight rate



Source: Bank of Canada, RBC Economics Research



**...though the impact of the U.S. recession has been tempered by three additional factors:**

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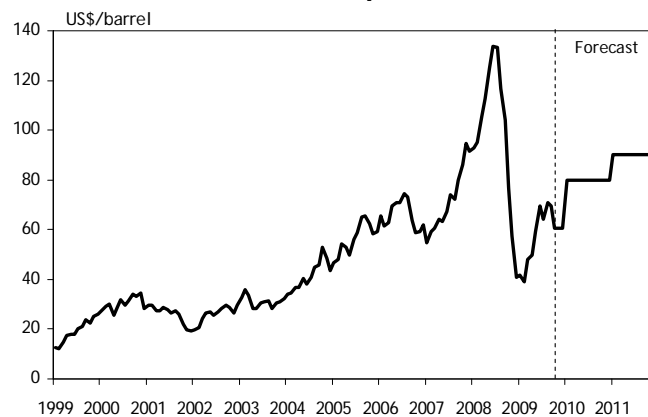
- **less upward pressure on the cost of capital**
- **commodity prices, though trading lower, remained at historically high levels which helped boost export revenues**
- **the Canadian housing market avoided the free-fall in activity evident in the U.S.**



**Oil prices remained historically high ...**

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### Crude oil price WTI

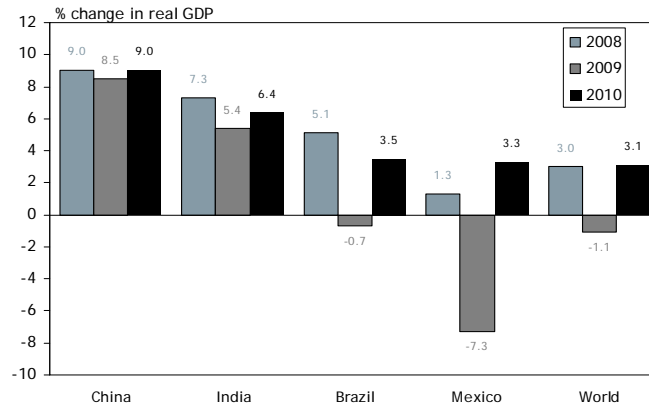


Source: Wall Street Journal, Bloomberg, RBC Economics Research



**...as demand from emerging markets, though slowing, did not collapse**

### Major emerging economies

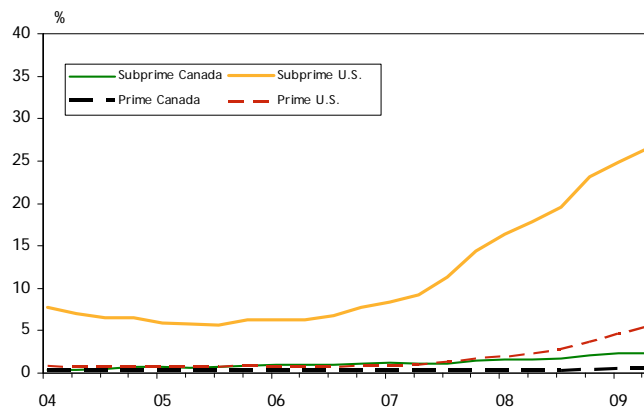


Source: IMF, RBC Economics Research



**More prudent mortgage lending in Canada with less involvement in subprime mortgages...**

### Percentage of mortgage in arrears

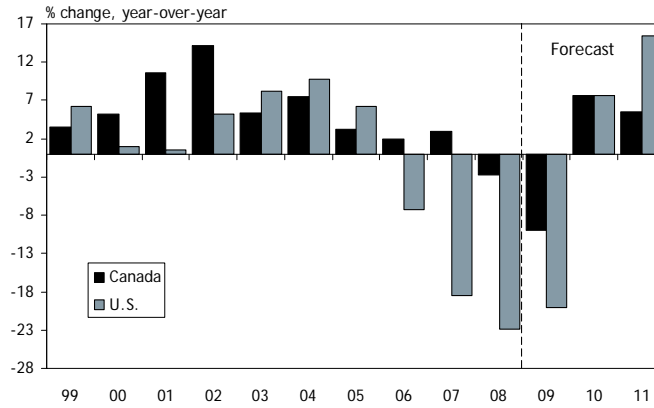


Source: Bank of Canada, Mortgage Bankers Association, RBC Economics Research



**...has limited the extent of declines in residential investment in Canada relative to the U.S.**

**Residential investments**

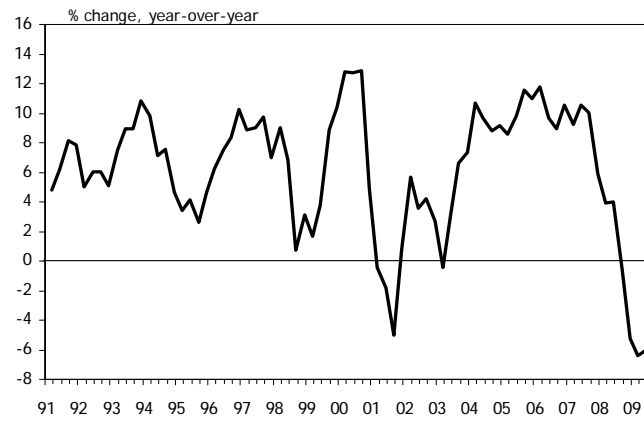


Source: Statistics Canada, Bureau of Economic Analysis, RBC Economics Research



**However, financial market turmoil has hit household net worth...**

**Household net worth**

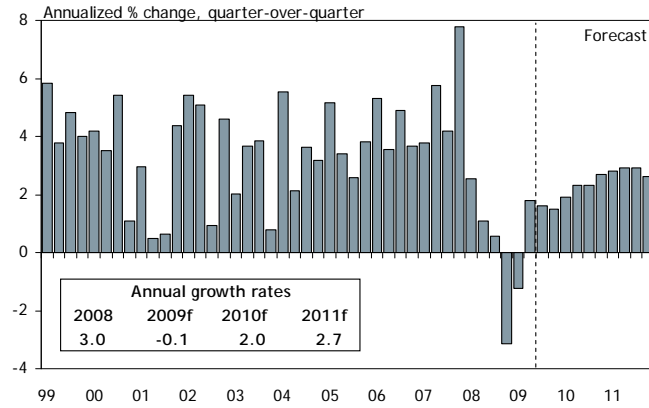


Source: Statistics Canada, RBC Economics Research



**...which will keep the recovery in consumer spending subdued despite low interest rates**

**Consumer spending**

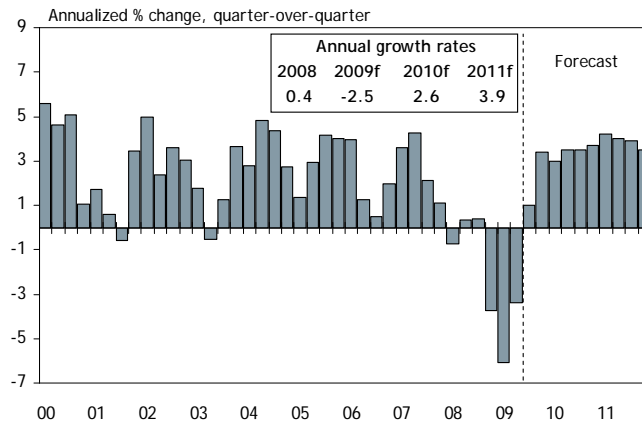


Source: Statistics Canada, RBC Economics Research



**Stimulative policy and U.S. recovery should allow Canada to return to positive growth by 2009Q3**

**Canada's real GDP**

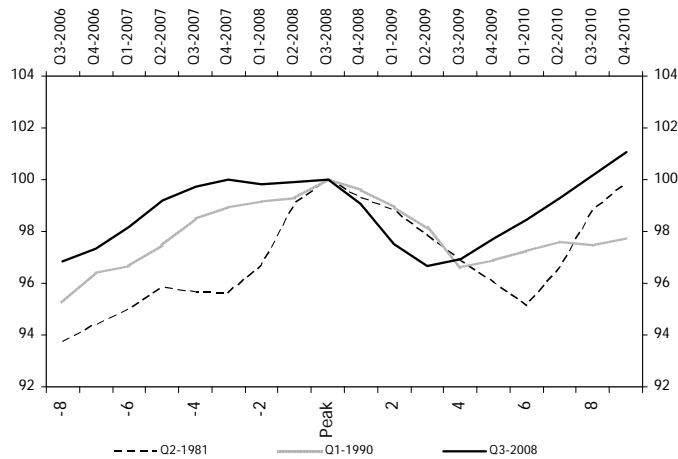


Source: Statistics Canada, RBC Economics Research



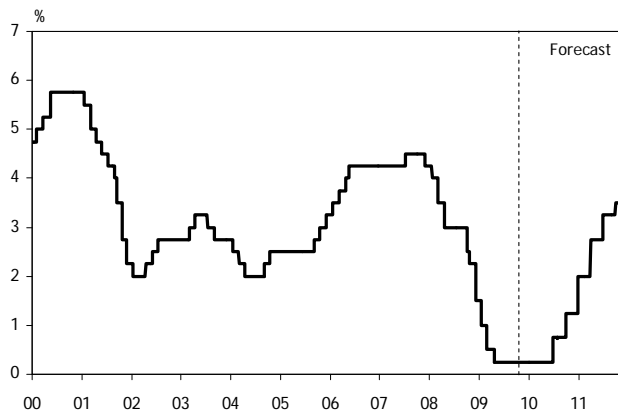
## The recession in Canada will likely be the mildest of the past three downturns

### Canada GDP (Indexed to peak)



## To help sustain the recovery, interest rates will be held low though start to be raised by the second half of 2010

### Bank of Canada overnight rate

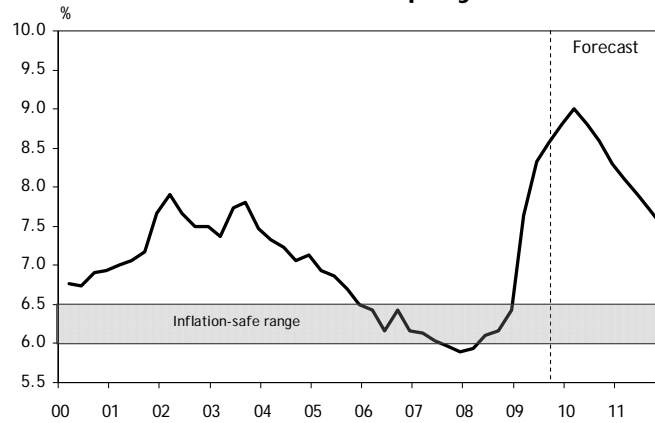


Source: Bank of Canada, RBC Economics Research



## The modest rebound will keep the unemployment rate high

### Canadian unemployment

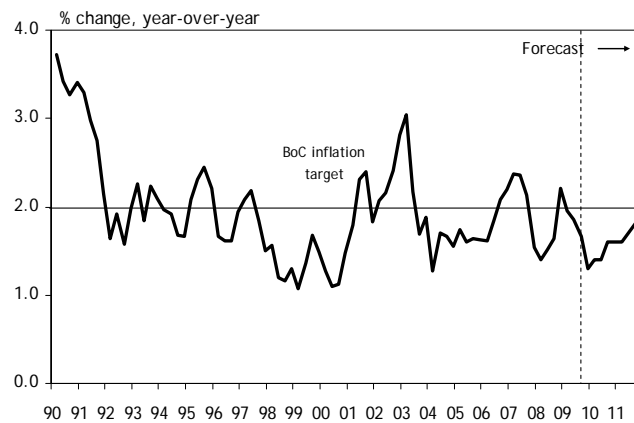


Source: Statistics Canada, RBC Economics Research



## This slack in the economy will also keep inflation below target near term

### Canadian core inflation



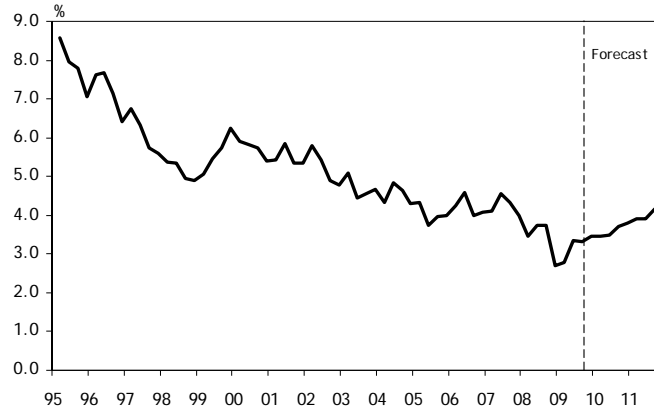
Source: Statistics Canada, RBC Economics Research





**Bond yields eventually rise as markets anticipate that the central bank easing will start to be reversed**

**Canadian 10-year bond yield**

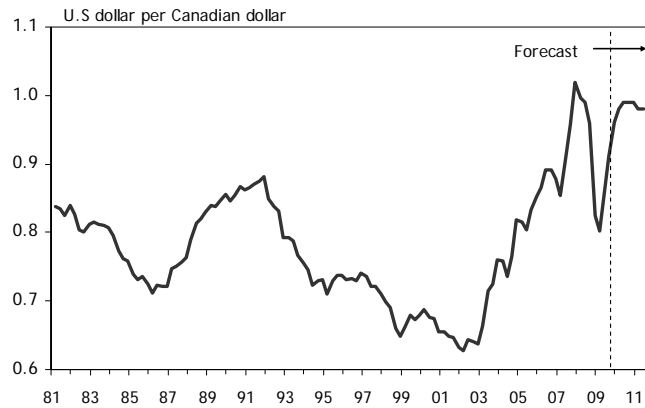


Source: Bank of Canada, RBC Economics Research



**The Canadian dollar to mirror growing optimism about the global recovery and attendant rise in commodity prices**

**Canadian dollar forecast**

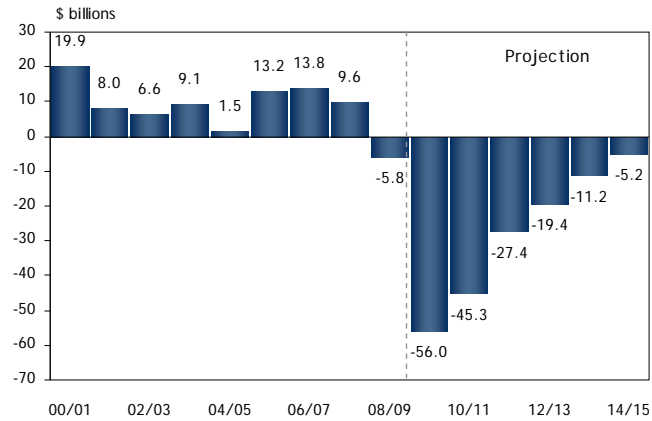


Source: Bank of Canada, RBC Economics Research



## Just as monetary policy will need to tighten so will fiscal policy over the medium term

### Canadian federal government fiscal balance

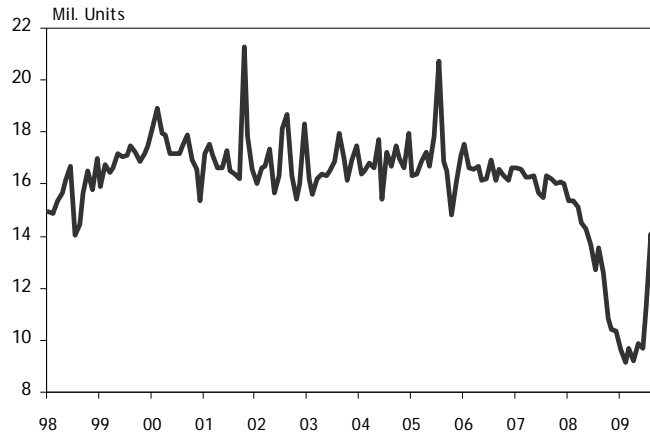


Source: Ministry of Finance, RBC Economics Research

## Regional Outlook: Ontario feeling the full brunt of the U.S. recession

The Ontario economy is currently feeling the full brunt of weak U.S. demand, particularly for autos...

### U.S. auto sales



Source: BEA, RBC Economics Research



...with high commodity prices representing high input costs

### Provincial real GDP growth

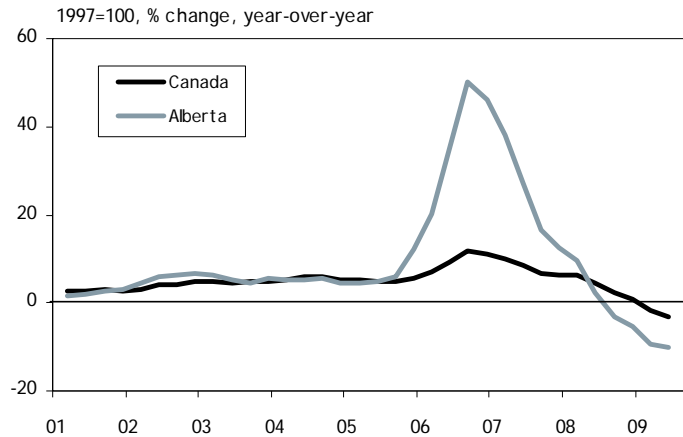


Sources: Statistics Canada, RBC Economics Research



## Alberta is paying the price for the earlier housing market surge...

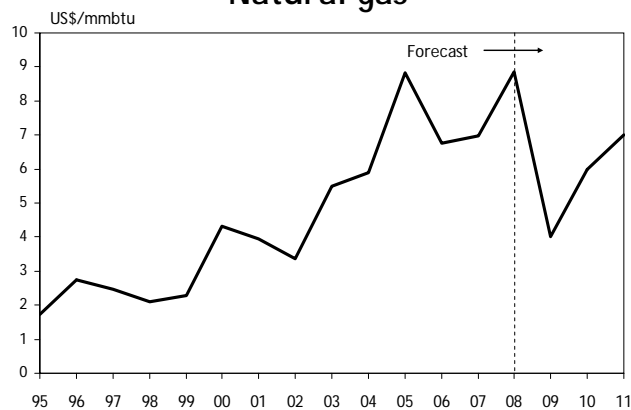
### New housing price index



Source: Statistics Canada, RBC Economics Research

## ...and weakness in natural gas prices

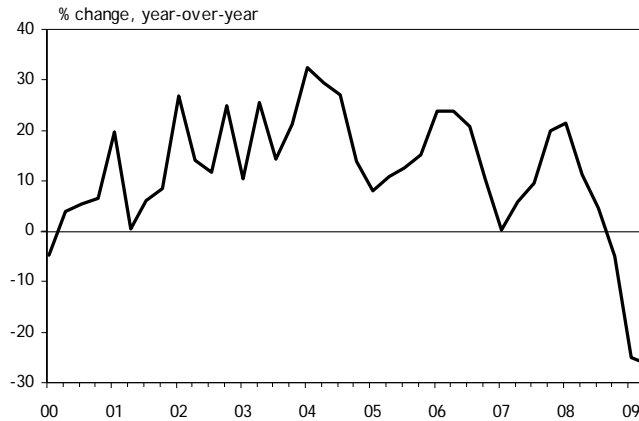
### Natural gas



Source: RBC Economics Research

**Similarly, British Columbia is being hurt by weak residential investment as well**

**B.C. residential investment**

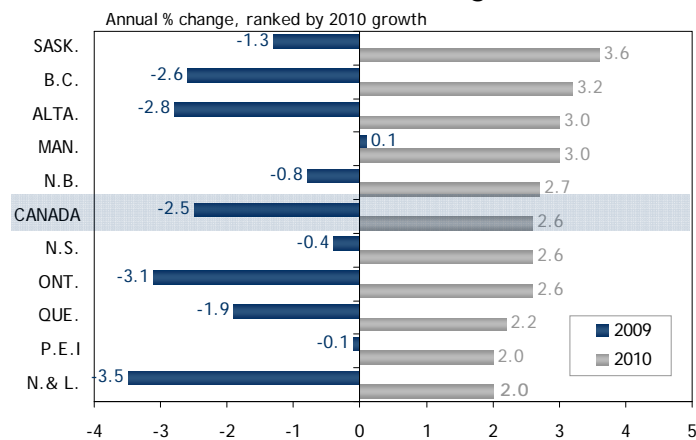


Source: Statistics Canada, RBC Economics Research



**The impact of high commodity prices on provincial growth will be more apparent in 2010**

**Provincial real GDP growth**

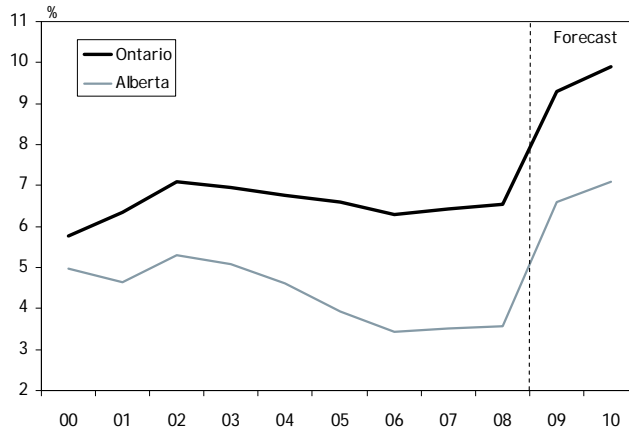


Sources: Statistics Canada, RBC Economics Research



**However, job growth across the country will be modest keeping the unemployment rate high east and west**

### Unemployment rate

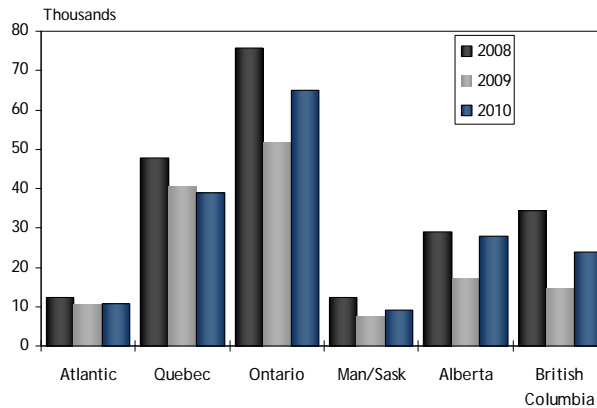


Source: Statistics Canada, RBC Economics Research



**Provincial housing starts outside of Quebec will recover in 2010 but remain below 2008 levels**

### Provincial housing starts

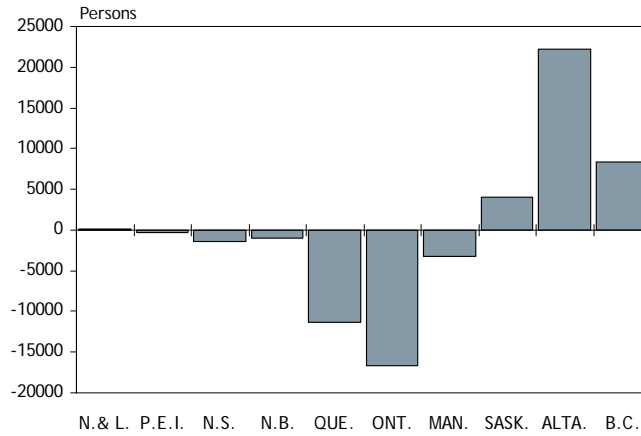


Source: Statistics Canada, RBC Economics Research



## Intra-provincial migration will likely revert closer to the 2008 pattern with gains largely out West

### Intra-provincial migration



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