

# ECONOMIC AND CAPITAL MARKETS MONTHLY UPDATE

## THE ECONOMY

### Canada

- ◆ The Canadian economy grew at a 0.4% annual rate in the third quarter and climbed further out of recession in October with real GDP estimated to have risen by 0.3%.
- ◆ Manufacturing sales volumes posted another strong gain in October and retail sales were also higher in the month.
- ◆ The real estate sector continues to be a major driver in the economic recovery as the value of building permits hit a 13-month high in October and housing starts hit their highest level this year in November.
- ◆ Holiday retail sales have outperformed expectations according to early reports. While the retail numbers are still preliminary, they indicate that consumer confidence is coming back, slowly.
- ◆ Canadian bankruptcies recorded their largest monthly drop on record in October but are still up significantly from last year's level.

### United States

- ◆ Third quarter U.S. GDP was revised lower to 2.2% but the economy has moved into positive territory for the first time since the second quarter of 2008.
- ◆ Manufacturing activity grew for the fifth straight month in December and at the fastest pace in more than three years. U.S. factories ended 2009 on an upswing with growing new orders indicating a durable recovery ahead.
- ◆ Existing home sales in November topped expectations, surging 7.4% to the highest level since February 2007. The increase was broadly-based across geographic regions.
- ◆ Consumer confidence moved higher for the second month in a row in December as expectations for the job market over the next six months reached their highest level in two years. However, there is less optimism about current job prospects.

### International

- ◆ The euro zone economy remains in recovery mode with manufacturing and the services sector continuing to expand in November. While German confidence business has risen for the ninth straight month, French sentiment weakened in November, the first setback since January.
- ◆ In Japan, business sentiment continues to improve, particularly in manufacturing. Manufacturers have become less negative about the profit outlook and business investment is expected to trend upward over the next year.
- ◆ The more advanced economies in Latin America remain well-positioned to continue to gain from increased exposure to the emerging markets in Asia which are leading the global economy out of recession.

### Canadian Economic Indicators

Annual % change <i>Unless otherwise indicated</i>	2008	2009 Estimate	2010 Forecast
G.D.P. (real)	0.6%	-2.5%	2.7%
Exports	-5.5	-14.1	4.2
Consumer spending	3.1	0.1	2.5
Business Investment	3.0	-13.9	1.9
Corporate Profits (pre-tax)	9.9	-34.2	12.7
Unemployment rate (%)	6.1	8.3	8.5
Inflation Rate (all items)	2.4	0.3	1.6

### Interest Rate Trends

	Dec. 2009	Dec. 2008	Dec. 2007
Canadian Bank Prime	2.25%	3.50%	6.00%
U.S. Bank Prime	3.25	3.25	7.25
30-Day Commercial Paper			
Canada	0.36	2.24	4.61
U.S.	0.20	0.38	4.78
5-Year Bonds			
Canada	2.77	1.69	3.87
U.S.	2.68	1.55	3.44
30-Year Bonds			
Canada	4.08	3.46	4.10
U.S.	4.64	2.68	4.45
Cdn./U.S. dollar	95.14¢	82.05¢	100.17¢

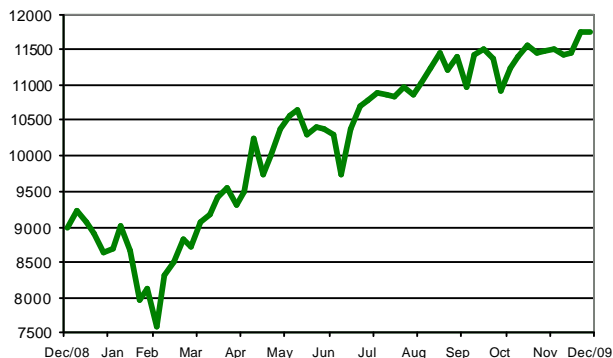
### Market Index Returns

	December	YTD	2008
S&P/TSX Composite Index	2.93%	35.05%	-33.00%
S&P 500 Composite	0.89	8.08	-21.92
MS EAFE (net)	0.40	12.62	-29.83
MS Japan	-0.26	-9.07	-12.15
MS Pacific (ex Japan)	1.19	47.89	-38.07
MS Europe	0.48	16.92	-33.18
MS Emerging Markets	2.90	53.00	-41.98
DEX Universe Bond	-1.42	5.41	6.41
GWL Real Estate Fund (Gross)	0.74	1.61	-0.49

All returns are in Canadian dollars and include income.  
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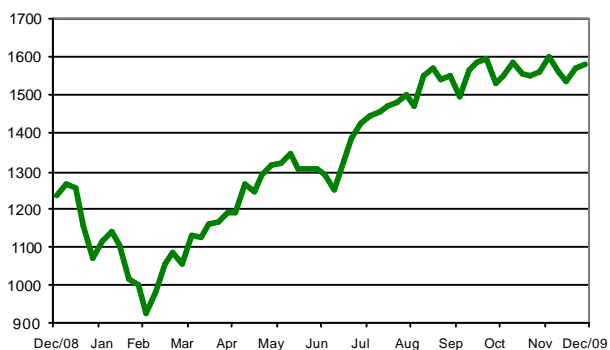
**S&P/TSX COMPOSITE INDEX**



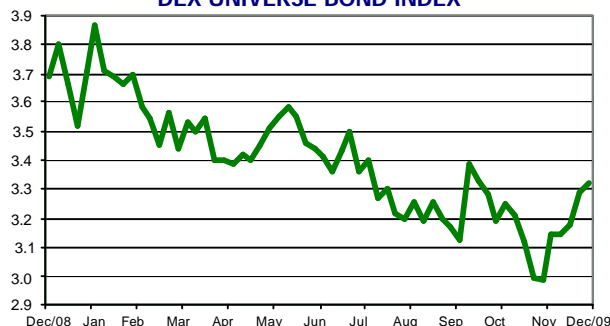
**STANDARD & POOR'S 500 INDEX**



**MS EAFE INDEX**



**DEX UNIVERSE BOND INDEX\***



\* Formerly the SC Universe Bond Index

## EQUITY MARKETS

December brought further gains for the S&P/TSX Composite Index, with the Index rallying 2.9% during the period. This performance puts the one year return for the Composite at 35.1% - a stunning recovery given the economic backdrop we faced at the beginning of the year. The market continued to be buoyed by further evidence of global economic recovery and ongoing strength in key commodity markets. Sectors that led the market higher during the month included the Technology, Industrials and Utilities sectors. Weakness was seen primarily in the Materials group as the strengthening US dollar caused the commodity trade to take a momentary break. Our outlook for Canadian equities remains very constructive. The market has essentially moved sideways for several months, allowing momentum indicators to positively reset. The global recovery thesis remains intact. Emerging economies look set to post sharply higher growth in 2010. Commodity markets should continue to firm and earnings momentum should improve significantly as we enter 2010. All this bodes very well for Canadian stocks.

The US equity markets rallied again in December, with the S&P 500 ending the month up by 1.9%, and putting it up 26.5% for the year. The strongest sectors in the Index were Technology and Utilities, up 5.6% and 5.2% respectively for the month. Technology stocks continued to perform well given their higher relative growth prospects and strong balance sheets. Utilities stocks began to perform better after having lagged the overall market since the March low. On the other hand, Financials and Energy lagged the market, which could suggest that the market is due for a correction or period of consolidation. The employment and housing pictures in the US remain weak, however there are concrete signs that both are improving. In addition, the ISM manufacturing data showed that the US manufacturing sector grew at the fastest pace in over three years in December. While these are very promising data points, ongoing improvement in the economy will likely be necessary for the market rally to continue through 2010.

## FIXED INCOME MARKETS

The DEX Universe Bond Index suffered its worst monthly performance of 2009 as interest rates backed up from the lower end of its seven month trading range to the upper end. For example, the 10 year Government of Canada bond yield increased from 3.22% on December 1 to 3.61% on December 31<sup>st</sup>. This resulted in the DEX Universe Bond Index losing 1.42% in December while gaining 5.41% for the 2009 year. Corporate bonds lost 0.99% in December but continued to outperform Government of Canada bonds which declined 1.50%. For the full year, corporate bonds returned a very healthy 16.26% compared to Government of Canada bonds which experienced a negative return of -0.21%. This huge outperformance from the corporate bond sector was driven by the virtual collapse of corporate credit spreads during 2009.

Government of Canada bond yields continue to trade in a narrow range because investors remain uncertain as to future economic growth prospects and the exact timing and extent of the Bank of Canada's removal of monetary stimulus in 2010. In this environment of low government bond yields and much tighter corporate credit spreads, 2010 bond returns will be lower than 2009.