



December 17, 2010

HIGHLIGHTS OF THE WEEK

United States

- Signs of improved economic growth continue to spring forth. This week, retail sales, industrial production and housing starts all surprised on the upside.
- The bi-partisan tax plan passed the Senate and the House this week and will soon become law, providing an additional boost to economic growth in 2011.
- Beyond the next few quarters, a further improvement in economic activity will require resolution of the outstanding issues holding back growth: clearing foreclosures, reducing uncertainty in the housing market, and repairing household balance sheets.

Canada

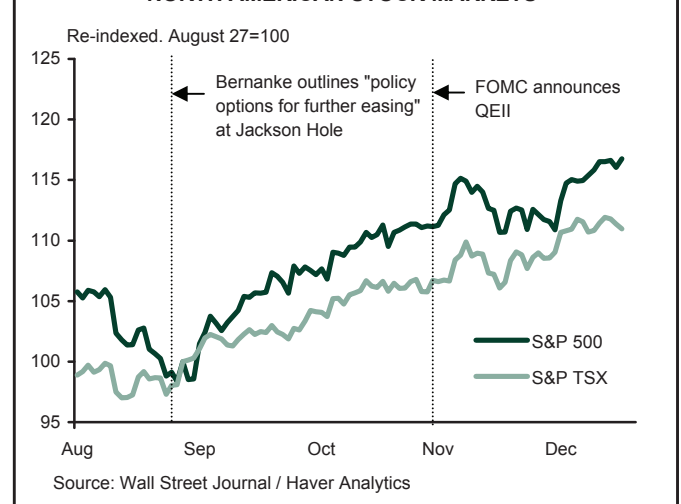
- The economic data this week were mostly good news. Manufacturing sales up 1.7% in October, and forward looking indicators point to continued strength in the coming months. Meanwhile, more good news came from the existing home market with sales up 5.4% - a fourth consecutive monthly gain. Sales are still down 16% from year ago levels.
- In other news, we learned the Canadian household debt-to-income ratio surpassed that in the U.S., rising to 148%. Both Bank of Canada Governor Mark Carney and Minister of Finance Jim Flaherty expressed concern over the level of household indebtedness. In the event that household debt became a larger concern, both argued that regulation would be the most appropriate tool to curb household borrowing.

THIS WEEK IN THE MARKETS

	Current*	Week Ago	52-Week High	52-Week Low
Stock Market Indexes				
S&P 500	1243	1240	1243	1023
S&P/TSX Comp.	13181	13239	13296	11093
DAX	6999	7006	7029	5434
FTSE 100	5870	5813	5891	4806
Nikkei	10304	10212	11339	8824
Fixed Income Yields				
U.S. 10-yr Treasury	3.38	3.32	3.99	2.38
Canada 10-yr Bond	3.23	3.30	3.72	2.69
Germany 10-yr Bund	3.01	2.95	3.39	2.12
UK 10-yr Gilt	3.51	3.52	4.23	2.83
Japan 10-yr Bond	1.20	1.21	1.41	0.85
Foreign Exchange Cross Rates				
C\$ (USD per CAD)	0.99	0.99	1.00	0.93
Euro (USD per EUR)	1.33	1.32	1.45	1.19
Pound (USD per GBP)	1.55	1.58	1.64	1.43
Yen (JPY per USD)	84.0	84.0	94.6	80.4
Commodity Spot Prices**				
Crude Oil (\$US/bbl)	87.7	87.8	89.4	66.0
Natural Gas (\$US/MMBtu)	4.19	4.34	7.51	3.18
Copper (\$US/met. tonne)	9030.5	9033.0	9295.0	6067.8
Gold (\$US/troy oz.)	1374.4	1386.0	1423.8	1062.9

*as of 9 am on Friday, **Oil-WTI, Cushing, Nat. Gas-Henry Hub, LA (Thursday close price), Copper-LME Grade A, Gold-London Gold Bullion; Source: Bloomberg

NORTH AMERICAN STOCK MARKETS



GLOBAL OFFICIAL POLICY RATE TARGETS

	Current Target
Federal Reserve (Fed Funds Rate)	0 - 0.25%
Bank of Canada (Overnight Rate)	1.00%
European Central Bank (Refi Rate)	1.00%
Bank of England (Repo Rate)	0.50%
Bank of Japan (Overnight Rate)	0.10%

Source: Central Banks, Haver Analytics

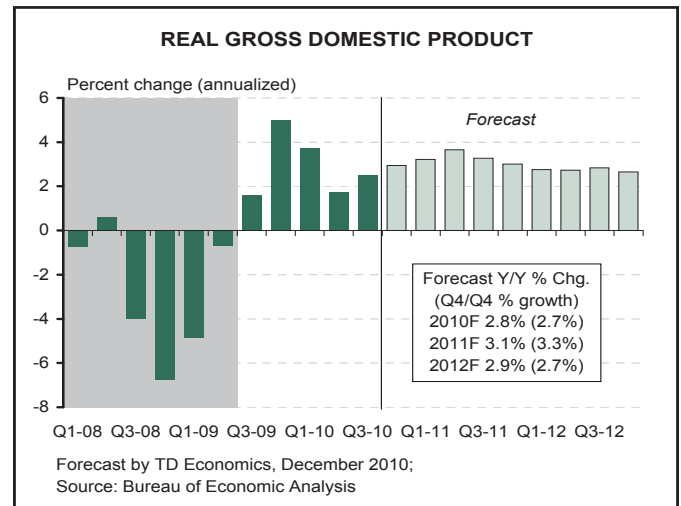
UNITED STATES - IT'S GETTING BETTER ALL THE TIME

The prospects for U.S. economic growth over the next year have brightened in recent weeks. Retail sales, industrial production, and housing starts all surprised on the upside this week, suggesting that economic growth in the fourth quarter of this year has accelerated from the previous two quarters. Just as important, and in the spirit of the season, policymakers in Washington were able to put aside partisan differences and agree to an over \$800 billion tax package that should likely provide a significant boost to economic activity over the next several quarters.

Amidst all this action, it is useful to step back and consider the forces that will shape the pace of economic recovery not just over the next few months, but over the next several years. As we argue in our recently released [Quarterly Economic Forecast](#), economic growth is likely to improve in 2011, but a move to a sustained robust economic recovery will require much more than near-term stimulus.

The aftermath of financial crises typically leave long-standing issues that continue to constrain growth years after they have taken place. Recovery in this environment requires resolving the issues that have been holding back growth in the first place. The long standing issues in the case of the U.S. are clearing foreclosures, reducing uncertainty in the housing market, and repairing household and financial sector balance sheets. The housing and wealth issues are related and progress on the housing front would likely precipitate improvement in the other.

So, the key question becomes where are we in this clearing process? At best, mid-way through the process, and at worst closer to the beginning than to the end. Consider the arithmetic: in a normal housing market, the average home

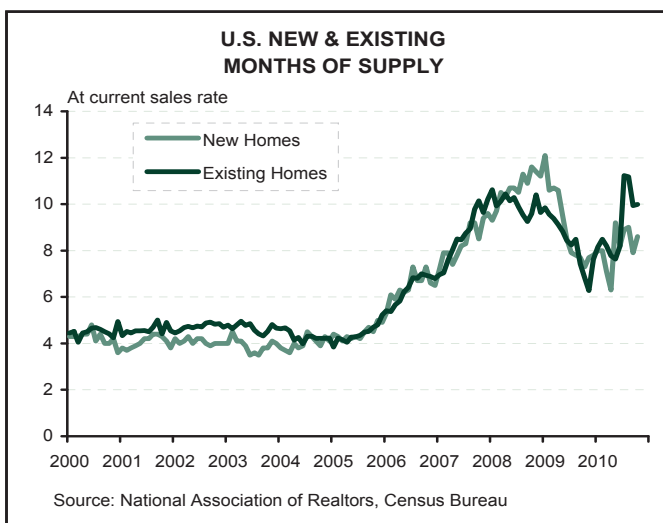


put up for sale will take between 5 and 6 months to find a buyer. Currently with close to 4 million homes on the market, this has moved up to just over 10 months. However, with over 4 million mortgages that are either 90 days past due on their payments or in some stage of foreclosure, the potential months' supply including this "shadow inventory" could be as high as 21 months.

This is a useful starting point because it is an upper bound to the malaise in housing, as not all of the seriously delinquent mortgages will end up in sales liquidation. Just as important, the number of home sales in the aftermath of the tax credit has likely reached a nadir and as job and income growth pick up steam, home sales should show continued improvement. Nonetheless, the sheer magnitude of foreclosure inventory means that even as home sales rise, the increase is unlikely to be sufficient to clear through the stock of homes available for sale. And, with the balance of supply and demand deeply in buyers' market territory, home prices are likely to fall over the next year. Given that real-estate makes up roughly 25% of the assets of U.S. households, this outturn will also impede improvement in household balance sheets.

All told, events over the last few months have increased our confidence that the U.S. economy will continue to move in the direction of recovery rather than slip into another economic recession. However, while economic growth is likely to improve over the next few quarters and average 3.1% in 2011, a faster pace of growth – necessary to make a material dent in the housing market and the unemployment rate, is likely still two to three years off.

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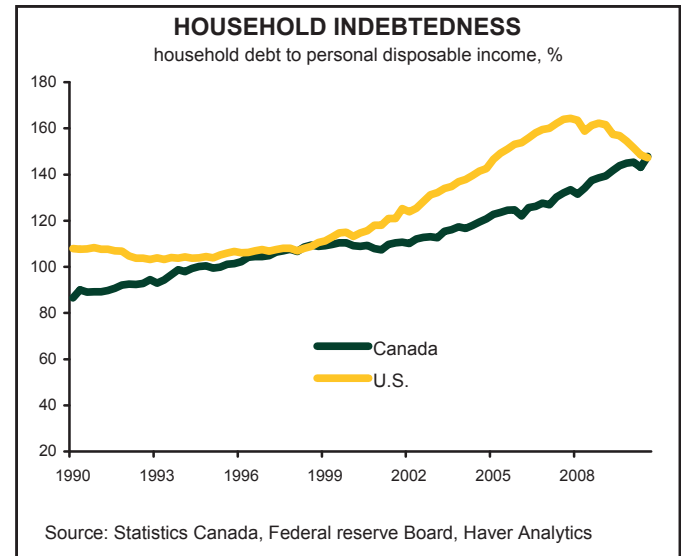
CANADA - HOUSEHOLD DEBT A CHALLENGE

This last week brought with it some holiday cheer. The economic data were mostly good news – with Canadian manufacturing sales up in October, and the existing housing market remaining remarkably resilient through November. Better still, U.S. officials passed the U.S. tax reform bill which is expected to be a boon to Canadian economic growth in the near term through stronger exports and commodity prices. But, along side the good news came reminders that Canadian policy makers have a number of challenges to face in the years ahead.

Challenge number one – household indebtedness. It's official, Canadian households are just as indebted as their U.S. counterparts. The Canadian household debt-to-personal disposable income ratio climbed to 148% in the third quarter of 2010, slightly surpassing the U.S. ratio. While this is a cause for concern, it is not as scary as it sounds.

U.S. households got into financial trouble when the debt-to-income ratio reached a much more dangerous level of 164% in 2007. Since the recession began, U.S. households have been deleveraging, which is a major reason the two ratios have converged.

That being said, Bank of Canada Governor Mark Carney and Minister of Finance Jim Flaherty continued to publicly express concern over household debt this week. Rising household indebtedness is a peril of extraordinarily low interest rates. But, as signaled in a speech by Governor Mark Carney in Toronto on Monday, the global economic backdrop is not one in which the Bank of Canada would want to navigate through while increasing interest rate in the coming months. Rather, the Central Bank Governor would prefer to restrain household debt through regulation changes. On that front, the federal government has shown a willing-

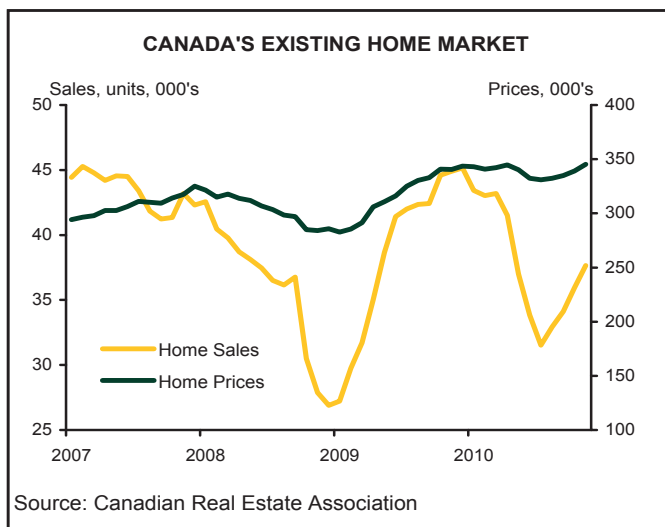


ness to tighten mortgage insurance rules should things start to get out of hand. Such measures can include shortening the allowed amortization period on mortgages from 35 to 25 years, increasing the required down payment on house purchases, stricter income testing rules, or a combination of all three. Each measure is expected to have differing degrees of impacts on economic growth.

For now, the federal government has taken a “wait and see” approach, given that there are factors in place that should work to slow the pace of household borrowing going forward. First, employment gains have cooled significantly over the last three months, and income growth is expected to be modest. Second, the Federal Government’s move to tighten mortgage insurance rules in late 2009 is still likely working its way through the housing market.

Nonetheless, these natural breaks may not be enough. As long as rates remain low, households are likely to continue to wrack up debt at a pace that outstrips income growth, driving the debt-to-income ratio higher. Ultimately, what the government does depends on what happens in the Canadian housing market – the root of the household debt problem. This week’s housing data showed that existing home sales rose 5.4% in November, a fourth consecutive monthly gain. While home sales remain 16% below year ago levels, the Canadian housing market appears to be picking up steam. Should sales accelerate further in the coming months, pressures may mount for governments to take further action. For now, our bet is that reducing debt levels is going to be a popular new year’s resolution in 2011.

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U.S.: UPCOMING KEY ECONOMIC RELEASES

U.S. Existing Home Sales - November*

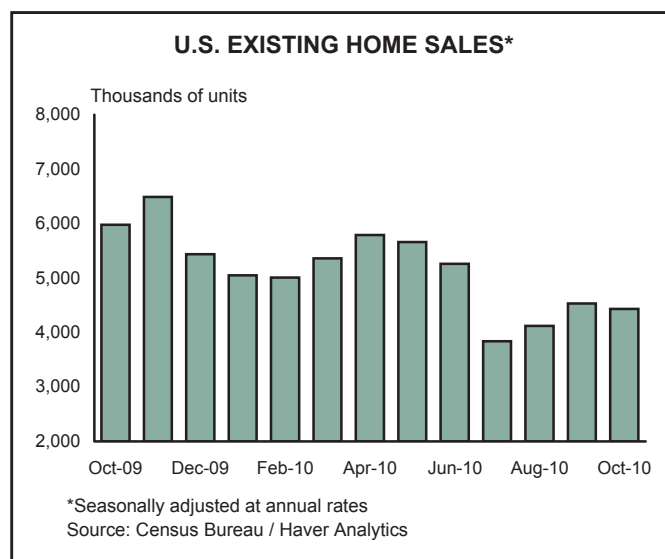
Release Date: December 22/10

October Result: 4.43 Million

TD Forecast: 4.80 Million

Consensus: 4.71 Million

U.S. existing home sales are expected to rise in November after the surprising decline the month before. During the month, we expect sales to move well above the 4.75 million mark for the first time since June with a print of 4.80 million units. The number of single-family and condo homes changing hands are expected to rise on the month as sales activity regain some of the ground surrendered during the summer slump. Pending home sales were quite strong in October, posting its first double-digit advance in many years, and we expect this strong bounce-back in pending sales to be reflected in actual home sales in November. Notwithstanding this positive momentum, given the very stiff headwinds that U.S. households continue to face, we



expect the pace of existing home sales to remain at very depressed levels, despite the very favorable buying conditions and low mortgage rates.

U.S. Personal Income - November*

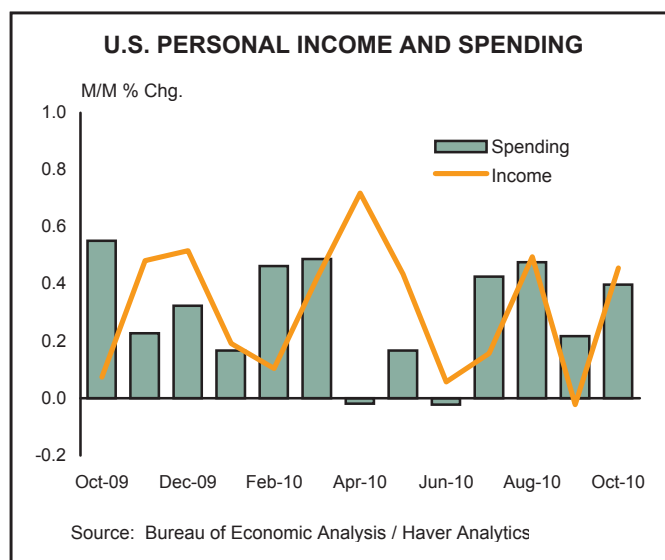
Release Date: December 23/10

October Result: Personal Income 0.5% M/M, Personal Spending 0.4% M/M

TD Forecast: Personal Income 0.3% M/M, Personal Spending 0.4% M/M

Consensus: Personal Income 0.3% M/M, Personal Spending 0.5% M/M

With the labour market recovery beginning to show signs of life, personal spending (the lynchpin of US economic activity) is itself also appearing to be shifting into a self-sustaining mode. This has been reflected in personal consumption expenditures, which have risen in 11 of the last 13 months. In November, we expect the pace of personal income growth to remain very tepid, advancing by only 0.3% M/M, following the slightly better 0.5% M/M gain the month before. However, personal spending is expected to grow at a more respectable 0.5% M/M pace, which will be consistent with the gains in retail sales during the month. On the inflation front, core PCE is expected to remain quite soft, rising by only 0.1% M/M after two consecutive flat



prints, reflecting the very soft backdrop for consumer price inflation. In the months ahead, with the economic recovery likely to remain subpar, we expect core consumer prices will remain well below the 2.0% Y/Y mark, given the significant amount of slack that continues to exist in the economy.

CANADA: UPCOMING KEY ECONOMIC RELEASES

Canadian CPI - November*

Release Date: December 21/10

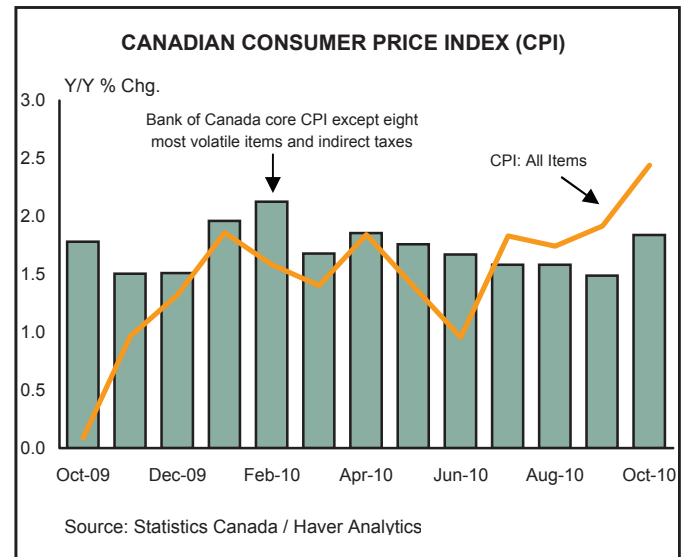
October Result: core 0.4% M/M; all-items 0.4% M/M

TD Forecast: core 0.0% M/M; all-items 0.4% M/M

Consensus: core 0.2% M/M; all-items 0.3% M/M

Following the unexpected increase in core inflation in October, this inflation report warrants close attention. In digging into the details of the October report, we attributed much of the increase in core inflation to several temporary factors. As such, we do not anticipate that the upwards pressure can be sustained, and instead expect core prices to be flat on the month (both on a seasonally unadjusted and adjusted basis). On a year-ago basis, core inflation is expected to retreat to 1.4%, which is consistent with the rate observed between July and September. In assessing the risk around this forecast, we concede that past jumps in core prices have been followed by a month where core prices decline outright. We are somewhat more conservative in our forecast, but if we allow for a -0.2% (M/M) fall in core prices, year-ago core inflation could fall to 1.2%.

At the other end of the spectrum, higher food and energy prices are expected to contribute to a 0.4% (M/M) increase in the non-seasonally all-items price index. Seasonal factors will provide headline prices with an additional kick, with prices forecast to rise by 0.5%. On a year-ago basis, headline inflation is expected to retreat modestly to 2.3%, due in large part to a stronger base year effect (recall that



headline inflation accelerated from 0.1% to 1.0% between October and November 2009).

From a monetary policy perspective, the Bank of Canada appears to be looking through the October jump in core CPI. In their most recent communiqué (released after the CPI data), the Bank noted that the inflation outlook was unfolding largely as they had expected in the October Monetary Policy Report (MPR). We share this view. With our forecast for November CPI, our Q4 tracking for core CPI stands at 1.6% – exactly in line with what the Bank expects.

Canadian Retail Sales - October*

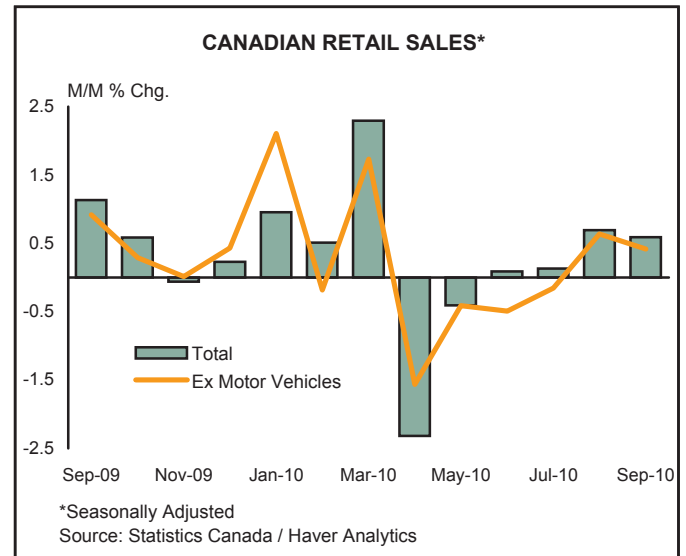
Release Date: December 21/10

September Result: total 0.6% M/M; ex-autos 0.4% M/M

TD Forecast: total 0.7% M/M ; ex-autos 0.7% M/M

Consensus: total 0.5% M/M; ex-autos 0.7% M/M

Retail sales are forecast to have grown by 0.7% in October, which is consistent with the pace set in recent months. What will be unique, however, is the composition of sales. After doing much of the heavy lifting, auto sales were flat on the month, which will shift the burden of growth to other retail sectors. Fortunately, higher gasoline prices and continued momentum in existing home sales are expected to provide a considerable offset (ex-autos sales are also forecast to have increased by 0.7%). The impact of higher gasoline prices, however, will have a less favourable impact on real retail sales, which is expected to show a more moderate advance. Nevertheless, the strength in this report will help underpin a 0.2% M/M growth rate in industry-level real GDP growth in October.



Canadian GDP - October*

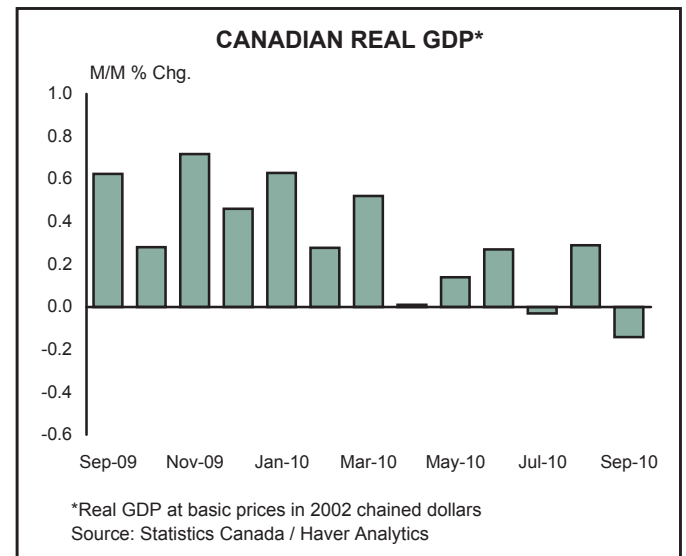
Release Date: December 23/10

September Result: -0.1% M/M

TD Forecast: 0.2% M/M

Consensus: 0.3% M/M

With the arrival of the holiday season, this is a difficult release to forecast. Unfortunately, we only have a third of the input data that is typically available. Nevertheless, on the back of a robust 1.1% increase in real manufacturing sales and based on a reasonably strong forecast for real wholesale and retail sales, we are comfortable in expecting industry-level real GDP to advance by 0.2% (M/M) in October. A portion of this strength can be traced to a rebound from the weakness observed in the previous month (recall that September real GDP fell by 0.1% due in large part to weakness in the mining, oil, and gas sector). Looking out to the quarter as a whole, the strength in the recent dataflow provides us with sufficient confidence that the soft patch observed in Q3 will be short lived. Our recently released forecast for Q4 annualized real GDP growth is for a re-



bound to 2.3%. Although this estimate does fall short of the Bank of Canada's 2.6% forecast, it is consistent with their expectation that growth in the second half of the year will likely remain subdued before activity improves into 2011.



RECENT KEY ECONOMIC INDICATORS: DECEMBER 13-17, 2010

Release Date	Economic Indicators		Data for Period	Units	Current	Prior	
United States							
Dec 14	NFIB Small Business Optimism		Nov	Index	93.2	91.7	
Dec 14	Producer Price Index		Nov	M/M % Chg.	0.8	0.4	
Dec 14	PPI Ex Food & Energy		Nov	M/M % Chg.	0.3	-0.6	
Dec 14	Advance Retail Sales		Nov	M/M % Chg.	0.8	1.7	R▼
Dec 14	Retail Sales Less Autos		Nov	M/M % Chg.	1.2	0.8	R▲
Dec 14	Retail Sales Ex Auto & Gas		Nov	M/M % Chg.	0.8	0.8	R▲
Dec 14	Business Inventories		Oct	M/M % Chg.	0.7	1.3	R▲
Dec 14	FOMC Rate Decision		14-Dec	%	0.25	0.25	
Dec 14	ABC Consumer Confidence		12-Dec	Index	-43	-45	
Dec 15	Consumer Price Index		Nov	M/M % Chg.	0.1	0.2	
Dec 15	CPI Ex Food & Energy		Nov	M/M % Chg.	0.1	0.0	
Dec 15	CPI Core Index SA		Nov	Index	221.982	221.765	
Dec 15	Empire Manufacturing		Dec	Index	10.57	-11.14	
Dec 15	Total Net TIC Flows		Oct	USD, Blns	7.5	80.1	R▼
Dec 15	Net Long-term TIC Flows		Oct	USD, Blns	27.6	77.2	R▼
Dec 15	Industrial Production		Nov	M/M % Chg.	0.4	-0.2	R▼
Dec 15	Capacity Utilization		Nov	%	75.2	74.9	R▼
Dec 15	NAHB Housing Market Index		Dec	Index	16	16	
Dec 16	Housing Starts		Nov	Thousands	555	534	R▲
Dec 16	Building Permits		Nov	Thousands	530	552	R▲
Dec 16	Current Account Balance		3Q	USD, Blns	-127.2	-123.2	R▲
Dec 16	Initial Jobless Claims		11-Dec	Thousands	420	423	R▲
Dec 16	Continuing Claims		4-Dec	Thousands	4135	4113	R▲
Dec 16	Philadelphia Fed.		Dec	Index	24.3	22.5	
Dec 17	Leading Indicators		Nov	M/M % Chg.	1.1	0.4	R▼
Canada							
Dec 13	Capacity Utilization		3Q	%	78.1	76.9	R▲
Dec 14	Leading Indicators		Nov	M/M % Chg.	0.3	0.3	R▲
Dec 14	Labour Productivity		3Q	Q/Q % Chg.	0.1	-0.6	R▲
Dec 15	Manufacturing Sales		Oct	M/M % Chg.	1.7	-0.5	R▲
Dec 16	Int'l Securities Transactions		Oct	CAD, Blns	9.507	13.362	R▲
International							
Dec 13	FR	Current Account	Oct	Euro, Blns	-2.5	-4.4	
Dec 13	NZ	REINZ Housing Price Index	Nov	M/M % Chg.	1.9	-0.9	
Dec 13	AU	NAB Business Confidence	Nov	Index	6	8	
Dec 14	FR	CPI - EU Harmonised	Nov	Y/Y % Chg.	1.8	1.8	
Dec 14	UK	CPI	Nov	Y/Y % Chg.	3.3	3.2	
Dec 14	UK	Retail Price Index	Nov	Y/Y % Chg.	4.7	4.5	
Dec 14	EU	Eurozone Industrial Production WDA	Oct	Y/Y % Chg.	6.9	5.4	R▲
Dec 14	GE	ZEW Survey (Current Situation)	Dec	Index	82.6	81.5	
Dec 14	GE	ZEW Survey (Econ. Sentiment)	Dec	Index	4.3	1.8	
Dec 14	AU	Westpac Consumer Confidence Index	Dec	Index	111.0	110.7	
Dec 15	UK	ILO Unemployment Rate (3mths)	Oct	%	7.9	7.7	
Dec 15	EU	Eurozone Employment	3Q	Y/Y % Chg.	-0.2	-0.6	
Dec 15	AU	Consumer Inflation Expectation	Dec	%	2.8	3.1	
Dec 15	NZ	NBNZ Business Confidence	Dec	Index	29.5	33.2	
Dec 16	GE	PMI Manufacturing	Dec	Index	60.9	58.1	
Dec 16	GE	PMI Services	Dec	Index	58.3	59.2	
Dec 16	UK	Retail Sales Ex Auto Fuel	Nov	Y/Y % Chg.	1.8	1.7	R▲
Dec 16	EU	Eurozone CPI - Core	Nov	Y/Y % Chg.	1.1	1.1	
Dec 16	EU	Eurozone Labour Costs	3Q	Y/Y % Chg.	0.8	1.6	
Dec 17	GE	IFO - Business Climate	Dec	Index	109.9	109.3	
Dec 17	EU	Construction Output WDA	Oct	Y/Y % Chg.	-6.8	-7.7	R▲
Dec 17	EU	Eurozone Trade Balance SA	Oct	Euro, Blns	3.6	2.0	R▼

Source: Bloomberg, TD Economics



UPCOMING ECONOMIC RELEASES AND EVENTS: DECEMBER 20-24, 2010

Release Date	Time*	Economic Indicator/Event	Data for Period	Units	Consensus Forecast	Last Period
United States						
Dec 20	8:30	Chicago Fed Nat Activity Index	Nov	Index	--	-0.28
Dec 21	17:00	ABC Consumer Confidence	19-Dec	Index	--	-43
Dec 22	7:00	MBA Mortgage Applications	17-Dec	W/W % Chg.	--	-2.3
Dec 22	8:30	GDP (Annualized)	3Q T	Q/Q % Chg.	2.8	2.5
Dec 22	10:00	Existing Home Sales	Nov	Millions	4.71	4.43
Dec 22	10:00	House Price Index	Oct	M/M % Chg.	-0.1	-0.7
Dec 23	8:30	Durable Goods Orders	Nov	M/M % Chg.	-0.6	-3.3
Dec 23	8:30	Durables Ex Transportation	Nov	M/M % Chg.	1.6	-2.7
Dec 23	8:30	Cap Goods Orders Nondef Ex Air	Nov	M/M % Chg.	0.8	-4.5
Dec 23	8:30	Cap Goods Ship Nondef Ex Air	Nov	M/M % Chg.	--	-1.5
Dec 23	8:30	Personal Income	Nov	M/M % Chg.	0.3	0.5
Dec 23	8:30	Personal Spending	Nov	M/M % Chg.	0.5	0.4
Dec 23	8:30	PCE Deflator	Nov	Y/Y % Chg.	--	1.3
Dec 23	8:30	PCE Core	Nov	M/M % Chg.	0.1	0.0
Dec 23	8:30	Initial Jobless Claims	18-Dec	Thousands	420	420
Dec 23	8:30	Continuing Claims	11-Dec	Thousands	--	4135
Dec 23	10:00	New Home Sales	Nov	Thousands	300	283
Canada						
Dec 20	8:30	Wholesale Sales	Oct	M/M % Chg.	0.7	0.4
Dec 21	7:00	Consumer Price Index	Nov	M/M % Chg.	0.3	0.4
Dec 21	7:00	Bank of Canada CPI Core	Nov	M/M % Chg.	0.2	0.4
Dec 21	8:30	Retail Sales	Oct	M/M % Chg.	0.5	0.6
Dec 21	8:30	Retail Sales Less Autos	Oct	M/M % Chg.	0.7	0.4
Dec 23	8:30	Gross Domestic Product	Oct	M/M % Chg.	0.3	-0.1
International						
Dec 19	16:30	NZ Performance Services Index	Nov	Index	--	52.0
Dec 20	2:00	GE Producer Prices	Nov	Y/Y % Chg.	4.5	4.3
Dec 20	4:00	EU Eurozone Current Account SA	Oct	Euro, Blns	--	-13.1
Dec 20	10:00	EU Eurozone Consumer Confidence	Dec	Index	-9.0	-9.4
Dec 20	18:00	AU Conference Board Leading Index	Oct	M/M % Chg.	--	-0.1
Dec 20	19:01	UK GfK Consumer Confidence Survey	Dec	Index	-22.0	-21
Dec 20	19:30	AU Reserve Bank's Board December Minutes				
Dec 21	2:00	GE GfK Consumer Confidence Survey	Jan	Index	5.7	5.5
Dec 21	4:30	UK Public Finances (PSNCR)	Nov	GBP, Blns	13.2	2.4
Dec 21	--	JP BoJ Target Rate	21-Dec	%	0.10	0.10
Dec 21	16:45	NZ Current Account Balance	3Q	NZD, Blns	-2.304	-0.880
Dec 21	18:30	AU Westpac Leading Index	Oct	M/M % Chg.	--	0.0
Dec 21	18:50	JP Adjusted Merchnds Trade Bal.	Nov	JPY, Blns	626.3	578.5
Dec 22	--	JP BoJ Monthly Economic Report				
Dec 22	4:30	UK Bank of England Minutes				
Dec 22	4:30	UK Current Account (BP)	3Q	GBP, Blns	-8.5	-7.4
Dec 22	--	JP Cabinet Office Monthly Economic Report				
Dec 22	16:45	NZ GDP	3Q	Y/Y % Chg.	1.8	1.9
Dec 23	2:45	FR Consumer Spending	Nov	Y/Y % Chg.	-0.4	-0.3
Dec 23	4:30	UK Index of Services (3mth/3mth)	Oct	M/M % Chg.	0.8	0.6

* Eastern Standard Time; Source: Bloomberg, TD Economics



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