

BDC's MONTHLY ECONOMIC LETTER

June 2009



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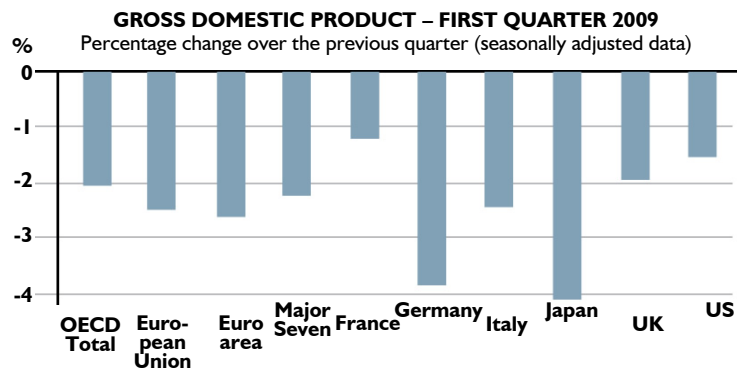
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OECD reports record GDP fall

- The world's largest economies are shrinking at a record rate. According to preliminary estimates, gross domestic product (GDP) in the top 30 countries fell by 2.1% in the first three months of the year, the largest drop since OECD records began in 1960.
- This followed a fall of 2.0% of GDP in the previous quarter, signalling a deep and synchronized global downturn.
- In the United States, GDP fell 1.6% in the first quarter of 2009, the same rate as in the previous quarter. Japan's GDP declined by 4.0%, following a 3.8% decrease in the previous quarter. GDP in the euro area was down 2.5%, following a 1.6% fall in the previous quarter.
- Compared with the same quarter a year earlier, all seven major economies recorded a fall in GDP, and a marked deterioration over the previous quarter's year-over-year figures.
- While it is still too early to assess whether it is a temporary or a more durable turning point, OECD composite leading indicators (CLIs) for April 2009 point to a reduced pace of deterioration in most of the OECD economies with stronger signals of a possible trough in Canada, France, Italy and the United Kingdom.



Source: OECD



Highlights

Canada

- Bank of Canada warns of loonie's rapid appreciation
- Unemployment rate hits an 11-year high
- Real GDP contracts 5.4% in Q1 2009
- Retail sales rise 0.3% in March
- Manufacturing shipments decline 2.7% in March

United States

- U.S. nonfarm payrolls drop by 345,000 in May
- ISM manufacturing index rises to 42.8
- Housing starts plunge to record low of 458,000 units in April
- Retail sales decline 0.4% in April

U.S.: Cautious optimism

Speaking to the U.S. House Committee on the Budget, Federal Reserve Chairman Ben Bernanke said that even though the U.S. economy has contracted sharply since last fall, the "pace of economic contraction is slowing" and activity in the housing market has shown "some signs of bottoming". But the Fed Chairman added that businesses remain cautious and continue to reduce their workforces and capital investments.

The same thoughts were echoed by the U.S. National Association of Business Economists (NABE) whose recent survey found that business economists look for the recession to end soon, but that the economic recovery is likely to be considerably more moderate than recoveries typically experienced following steep declines.

Moreover, despite encouraging signs seen in the last several weeks, the NABE panel downgraded the economic outlook for the next several quarters, compared with the previous survey. According to the survey, the key downside risks remain continued large job losses, no improvement in credit conditions, and further sharp declines in home values. These same forces are causing consumers to remain cautious, a feature that the NABE panel thinks is here to stay.

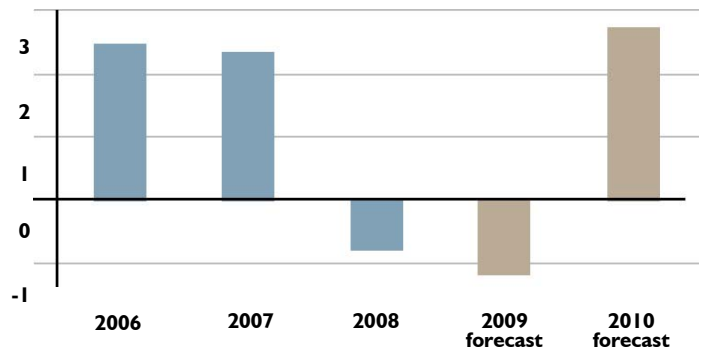
Following a sharp 6.1% (annual rate) contraction in the first quarter of this year and another 1.8% drop in the second quarter, NABE forecasters expect U.S. real GDP to rise at a subpar 1.2% rate in the second half. This would result in a 1.2% decline in 2009 (on a Q4-over-Q4 basis), on the heels of a 0.8% decline in 2008. The near-term weakness is largely due to a sharp retrenchment in business investment.

Consumer spending is considered key to economic recovery since it represents about two-thirds of U.S. output. The NABE panel predicted that labour market conditions would

deteriorate further, but the pace of job losses would decline through the rest of the year. The U.S. unemployment rate is forecast to rise to 9.8% by year-end and inflation is expected to moderate, as economic slack builds and as oil prices are forecast to remain relatively depressed. The panel projected modest job gains in 2010 that would trim the unemployment rate to 9.3% by the end of next year.

The NABE panel expects economic growth to turn positive in the second half of this year, with the pace of job losses narrowing sharply over the remainder of this year and employment turning up in early 2010. Growth in 2010 is slated for a return to near its historical trend, with real GDP rising 2.7% on a Q4-over-Q4 basis. The survey states that firms have started to address their inventory problems, with widespread shutdowns in the automotive sector in particular. Moreover, labour productivity remains impressive and is expected to improve.

NABE: U.S. REAL GDP FORECAST
Percent change, Q4/Q4



Any improvement in the U.S. economy will bode well for the global and Canadian economy. But not everyone is convinced that the U.S. contraction has ended. Robert Hall, head of the National Bureau of Economic Research's Business Cycle Dating Committee, says it's too early to call for the end of the U.S. recession. Mr. Hall notes that gross domestic product estimated on a monthly basis "had a trough earlier this year, but it is way too early to say that it is a true trough rather than a pause in a longer decline."

Canadian economy

Bank of Canada warns of loonie's rapid appreciation

- The Bank left its overnight target rate at the practical low of 0.25%, reiterating its conditional commitment to keep the rate low until the second quarter of 2010. But the Bank also warned that it is concerned about how far and how fast the Canadian loonie has risen since April and that it is prepared



to intervene if necessary. Noting that there had been clear signs of improvement in economic and financial conditions in Canada, it added: "If the unprecedentedly rapid rise in the Canadian dollar proves persistent, it could fully offset these positive factors." Moreover, on quantitative easing; "The Bank retains considerable flexibility in the conduct of monetary policy at low interest rates, consistent with the framework in the April monetary policy review." In April, the Bank of Canada predicted the economy would begin to grow again in the fourth quarter of this year and expand by 2.5% next year. But one of the assumptions it included in the projection was that the loonie would average about 80 cents US. Since then, the currency has soared past the 90-cent level and remains at a three-month high.

Unemployment rate hits an 11-year high

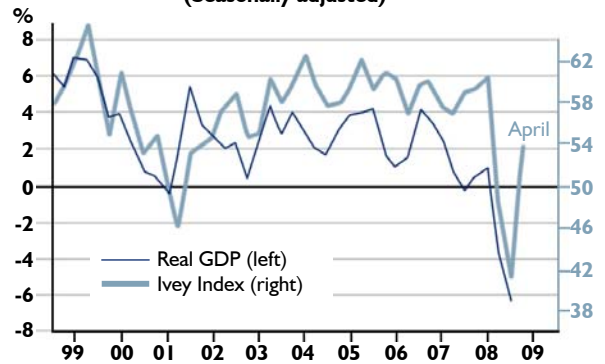
- The Canadian economy shed a further 42,000 jobs in May, more than retracing April's gains. The unemployment rate jumped 0.4% to 8.4%, an 11-year high. Manufacturing accounted for most of the job losses, shedding 58,000 jobs. Since the U.S. recession began in 2007, manufacturing has shed about 325,000 jobs, 15% of its workforce. After being the weakest sector in the prior six months, construction only clipped lightly in the month (-4,000). Significant gainers were mostly in public sector areas, with public administration up 19,000, and education adding 10,000, while trade also added 11,800 jobs. By region, the deep drop in manufacturing hit Ontario hard, as the province shed 59,700 jobs. Most of the other provinces added jobs but none of the increases were significant, with the largest being a 5,700 rise in Quebec. Accordingly, Ontario's jobless rate shot up 0.7% to 9.4%, fully a percentage point above the national average. Alberta's rate also rose 0.6% to 6.6%, as the labour force continues to grow rapidly there. With the latest report, the job loss tally for the current recession sits at a staggering 362,500, as the labour market has shed about 2% of jobs since the employment peak in October. However, one encouraging sign is that the rate of job destruction has cooled significantly since the end of 2008. The three-month moving average for job losses stands at 20,000, a sharp improvement from the 90,000 peak back in March. Going forward, employment will likely bottom in the coming quarter and start recovering slowly in the fall.

Real GDP contracts 5.4% in Q1 2009

- Canadian real GDP contracted 5.4% (annualized) in the first quarter of 2009, following a 3.7% decline in the last quarter of 2008. This is the worst contraction since 1991. Weakness in the export sector accelerated in the first quarter of 2009, with exports plunging 30%, annualized. The main source of weakness for exports has been lower demand for machinery

and equipment, as firms around the globe faced stringent lending conditions making these purchases harder, and more expensive. Residential investment and personal consumption also withdrew with a 20% and 1.6% drop respectively. The fall in U.S. and world demand, coupled with falling commodity prices in the first quarter also hit business investment, down 25.8% in the first quarter, the largest contraction since 1982. Falling commodity prices also hit corporate profits as they plunged 67% in the first quarter of 2009. Nevertheless, easing in credit conditions, a possible bottom in the U.S. downturn, a pick-up in commodity prices, and a nice rally in stock markets since March, suggest that the worst is behind us. Another encouraging reading was the 10-point jump in the Ivey Purchasing Manager Index in April. This index currently stands at 53.7, suggesting growth will expand in the second quarter.

**CANADA: REAL GDP (Q/Q, Annualized)
vs. IVEY PURCHASING MANAGERS INDEX
(Seasonally adjusted)**



Source: NBF Economy and Strategy (Ivey data via Global Insight)

Retail sales rise 0.3% in March

- Retail sales rose by 0.3% in March. Overall, the level of retail sales still remains quite depressed, down 4.8% from a year ago, and -6.3% from the peak in September of 2008. Sales in real terms were up a stronger 0.7%, signalling that retailers offered deep discounts to attract buyers. The increase in total sales was driven primarily by a 3.6% rise in new motor vehicle sales in March, but auto dealers had to offer large discounts to attract these buyers. Moreover, auto sales remain weak, down 17% from their peak in January of 2008. Excluding autos, retail sales were down 0.2% as Canadian consumers shy away from spending on other discretionary items. The more recession-proof sectors, food and beverage stores and pharmaceuticals, also helped shore up retail sales with increases of 0.9% and 0.5% respectively. The Canadian economy has lost a total of 321,000 jobs so far over the recession, dampening any sustained pick-up in spending until the recovery becomes more firmly entrenched.



Manufacturing shipments decline 2.7% in March

- Manufacturing shipments declined 2.7% in March. Ex-autos, shipments fell 3.7% for the month. The monthly decline was broad-based with 15 of 21 major sectors experiencing a monthly decline. The overall weakness was concentrated in the durable goods, with transportation equipment (-5.2%), primary metals (-7.6%) and machinery (-5.5%) together accounting for over 60% of the monthly fall. Shipments of completed vehicles advanced, after plant closures in January and February curbed production steeply, but these are still down 34% from their July 2008 peak. Moreover, auto parts shipments fell by a staggering 17.6%. Regionally, Quebec experienced a 6.1% decline in shipments and accounted for 60% of this month's national decline. A 29% drop in Quebec's shipments of motor vehicle parts and aerospace products created much of the weakness. Ontario's primary metals and machinery shipments fell sharply, resulting in a 1.5% plunge for the province. Although central Canada is bearing the brunt of the auto-sector turmoil, the decline in manufacturing is spread throughout the country. Going forward, the overall Inventories/Sales ratio edged up to 1.58, signaling that manufacturers will continue to cut production in order not to accumulate excess inventories.

Trade surplus rises to \$1.1 billion in March

- Canada's merchandise trade surplus rose to \$1.1 billion from an upwardly revised \$262 million in February. Unfortunately, the larger surplus was due to a greater fall in imports, not a resurgence in export. The value of imports fell 4.4%, while exports edged down 1.8%. On the import side, energy imports fell 18% to its lowest level since October 2004 and it wasn't driven by prices. The volume of energy imports declined 16.2%, while prices fell 2.7%. On the export side, the decline was fairly widespread. Machinery and equipment exports led the way at -3.4%, followed by automotive products at -3.3%. With so much of the Canadian economy dependent on trade, the March trade data paints a bleak picture of the state of the Canadian economy. However, the recent pick-up in commodity and oil prices augurs well for exports and a pick-up in growth will bolster imports as well.

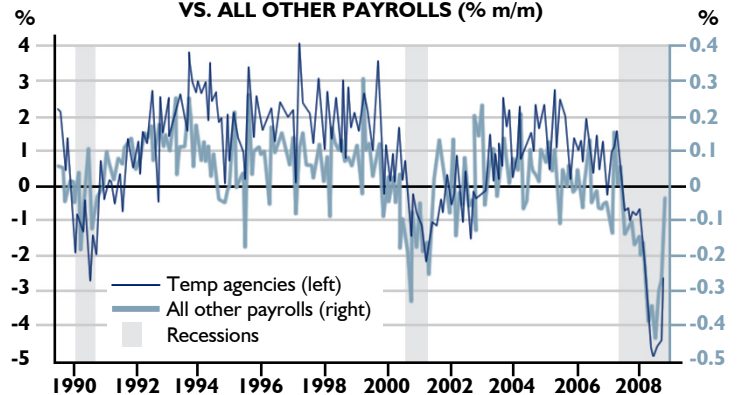
U.S. economy

U.S. nonfarm payrolls drop by 345,000 in May

- The pace of U.S. job losses eased dramatically in May, with nonfarm payrolls declining by 345,000, following the downwardly revised 504,000 jobs lost the month before. This is the fourth consecutive month in which the pace of

job losses has declined, and it is the slowest pace of job destruction since September last year. Despite the slowdown in the pace of job destruction in May, the total number of jobs lost so far this cycle climbed to 5.9 million. Moreover, as the entrance into the labour force continued to swell, the unemployment rate spiked to 9.4% from 8.9%. The main impetus for the improved print on the headline number was the slowdown in the pace of private sector layoffs. The job losses in the goods sector eased to 225,000 in May, while service sector job losses eased to 120,000. Overall, this was a favourable report. While the job losses are significant and the purchasing power of households continues to erode, there are encouraging signs. Apart from the pick-up in private sector employment, the temporary-help supply agencies are now very near the point where they could actually start hiring. Historically speaking, this typically heralds a favorable change in the overall trend in the U.S. labour market.

U.S.: EMPLOYMENT IN TEMPORARY-HELP SUPPLY AGENCIES VS. ALL OTHER PAYROLLS (% m/m)



Source: NBF Economy and Strategy (BLS data via Global Insight)

ISM manufacturing index rises to 42.8 in May

- The U.S. ISM manufacturing index rose to 42.8 in May, its highest level since September last year. The increase was the fifth consecutive monthly gain in the index. The strength was not widespread as only 5 of the 18 manufacturing industries surveyed reported growth in May. However, in terms of the individual sub-components, there were particularly strong gains in the new orders sub-index, which surged to 51.1 from 47.2, the first time since November 2007 that this component has breached the 50.0 barrier representing expansion. Another useful metric, the difference between new orders and inventories (a proxy for the future direction of production) also rose sharply, surging to 18.2, from 13.6 the month before. The key message of



this report is that the U.S. manufacturing sector has bottomed, and there are some indications that the sector will recover in the near term. Moreover, the weakening U.S. dollar will likely bolster U.S. exports and the rise in new orders will help spur production.

Housing starts plunge to record low of 458,000 units in April

U.S. housing starts plunged 12.8% in April to 458,000 units from the upwardly revised 525,000 (previously reported as 510,000) the month before. The declines were all in the volatile multi-units component, which dropped a further 46.1% to 90,000 units, while construction of the more stable single-family units rose 2.8% to 368,000 units. Permit approvals were also weaker during the month, falling by 3.3% to 511,000. Overall, the report was very weak and at odds with the other housing market indicators that have been pointing to an improved tone in U.S. housing market activity.

Retail sales decline 0.4% in April

U.S. retail sales declined for the second straight month in April, falling by 0.4%. Excluding autos, sales were down 0.5%. Core retail sales, which net out sales of autos and gasoline, declined by a more modest 0.3% during the month. On a year-ago basis, sales continue to be quite poor, as total retail sales have declined by a fairly big 10.1% since April last year. This is the eighth straight month in which sales have fallen below their year-ago level. The crux of this report appears to be that the positive momentum seen in U.S. consumer spending in the first few months of this year has stalled. Nevertheless, rising equity markets, improved consumer confidence and the massive fiscal stimulus package are likely to start kicking in this quarter, providing some much needed boost to U.S. economic activity.

Oil prices soar on speculation and weak U.S. currency

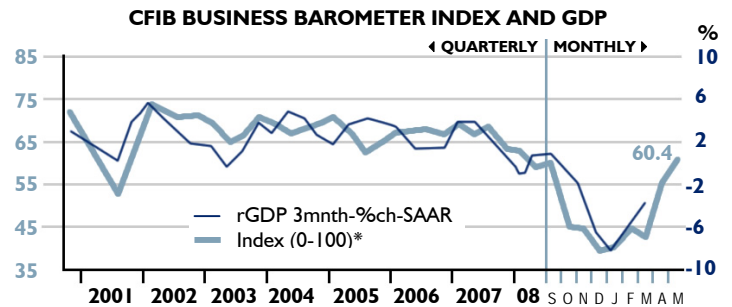
Oil prices are outpacing the economic recovery as speculative fervour and a weak U.S. currency sent the price of crude above \$70 a barrel for the first time this year.

Canadian dollar gains as commodities firm up

The petro-linked loonies has soared in the last month, and now stands close to 90 cents U.S. The surge in the Canadian currency has concerned the Bank of Canada as it may impede Canadian exports if it continues to rise.

SME sentiment continued to improve in May

There are growing signs the Canadian economy is turning the corner. CFIB's Business Barometer Index rose to 60.4 in May, from 54.9 in April, and a cyclical low of 39.4 in December 2008.* Despite the improvement, the index remains well below historical norms and suggests GDP growth has not yet entered positive territory. In terms of financing availability, 30% of business owners are saying a shortage of working capital is a constraint for them. Measured another way, only 23% of owners say they have access to only some of the financing they need – or none at all.



Source: Canadian Federation of Independent Business, May 2009.

* Index of 50 = equal balance of stronger and weaker business expectations. Note that CFIB's Business Barometer Index has been revised as of May 2009. The index is based on the same survey but is now a weighted average of response scores: 100 for stronger performance, 50 for same performance and 0 for weaker performance.

KEY INDICATORS - CANADA	Historical					2009					Forecast	
	2003	2004	2005	2006	2007	Q1	Q2	Q3	Q4	Latest	2009	2010
Real GDP (% growth)	1.9	3.1	2.9	3.1	2.7	-5.4					-2.5	2.0
Machinery & Equipment Expenditures (% growth)	7.7	9.3	10.8	7.4	5.1	-28.5					-12.8	-0.3
Pre-Tax Corporate Profits (% growth)	6.9	17.1	11.9	5.0	5.8	-34.7					-26.0	8.8
Industrial Production (% growth)	0.3	1.9	1.6	-0.2	0.3	-16.5					-9.0	1.5
Industrial Products Prices (% growth)	-1.4	3.2	1.5	2.3	2.1						-3.7	1.7
Non-Residential Construction (% growth)	5.7	0.8	6.8	7.5	6.9	-14.3						
Housing Starts ('000 units)	218	233	225	227	228	140				Apr. 117	138	156
Personal Expenditures (% growth)	3.0	3.4	3.8	4.2	4.7						-0.9	1.6
Consumer Price (% growth)	2.8	1.8	2.2	2.0	2.2	1.2				Apr. 0.4	0.3	1.7
Employment (% growth)	2.4	1.8	1.4	1.9	1.9	-5.5						
Unemployment Rate (%)	7.6	7.2	6.8	6.3	6.0	7.6				May 8.4	8.5	9.1
SMEs Confidence Index (CFIB)	107.8	107.8	106.6	107.5	108.2	42.4				May 60.4		
Manufacturers Confidence Index (CFIB)	109.8	109.0	107.4	107.5	105.7	41.3				May 57.5		

Sources: Statistics Canada, Consensus Economics and Canadian Federation of Independent Business