

## Highlights

- The world's leading economic indicators have gained even more momentum. Their expansion signal is now stronger than at any point in the previous economic cycle, and we are upgrading our forecast accordingly. We now expect above-trend growth next year.
- Despite job losses, struggling consumer confidence and the end of cash for clunkers, U.S. consumer spending is likely to expand at about 2% annualized in the fourth quarter, reflecting considerable consumer resilience in the circumstances. We increased our forecast to 3.4% real GDP growth in 2010.
- In Canada, despite months of disappointing GDP growth, the news on domestic demand remains good. Growth is accelerating in both homebuilding and consumer spending. The latter will be buoyed by strength in the aggregate wage bill.

	Current Forecast			Change from Previous Forecast	
	2008	2009	2010	2009	2010
<b>United States</b>					
GDP	0.4%	-2.5%	3.4%	-0.2pp	+0.4pp
CPI inflation	3.8%	-0.4%	2.3%	unch	unch
Overnight rate*	0.25%	0.11%	1.50%	-9bp	-50bp
Ten-year bond yield*	2.21%	3.63%	4.28%	-22bp	-6bp
<b>Canada</b>					
GDP	0.5%	-2.4%	2.8%	-0.2pp	-0.1pp
CPI inflation	2.4%	0.3%	1.6%	unch	-0.1pp
Overnight rate*	1.50%	0.25%	1.50%	unch	-50bp
Ten-year bond yield*	2.68%	3.60%	4.24%	-16bp	-13bp
USD/CAD*	0.82	0.92	0.94	0.00	-0.01

\* end of period

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## World: Recovery at hand

The near-simultaneous recovery of the leading developed economies, together with a continuing rise of the leading economic indicators, prompts us to upgrade our forecast this month. We now see above-trend global growth next year.

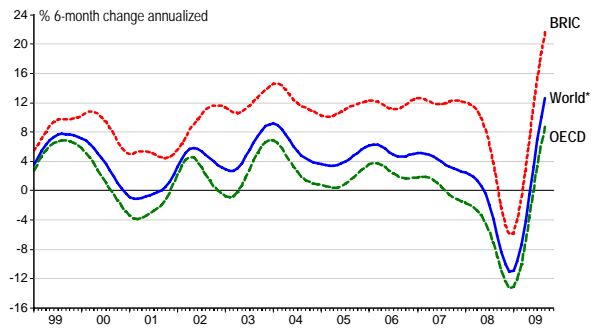
The world's leading economic indicators gained even more momentum in September. The six-month change in the global leading indicator now exceeds 12%, a steeper reading than at any time in the previous cycle. Though the composite leading indicator of the BRIC countries continues to outpace that of the developed countries, even the OECD indicator is now sending a stronger signal than at any time since the 1990s. The message is that global GDP growth is about to accelerate further.

The coordinated efforts of central banks and governments around the world bore fruit in the third quarter. Recovery is budding in most of the G-7 countries. Japan leads with real growth in the neighbourhood of 5%, though deflation persists. The euro-zone economy grew at 1.5% in Q3. The German economy – much more export-intensive and accordingly more exposed to global demand – grew at almost 3%. Only the U.K. has yet to turn the corner, and it is expected to do so in Q4.

Asia continues to forge ahead. Chinese exports, manufacturing output and retail sales continue to gain. The third-largest emerging Asian economy, South Korea's, posted a second consecutive quarter of spectacular real growth in Q3 – another double-digit annual rate driven by investment and exports. The latter rose at an annual rate of almost 20%. These reports confirm that global trade has revived in recent months.

### World: A signal stronger than after the last recession

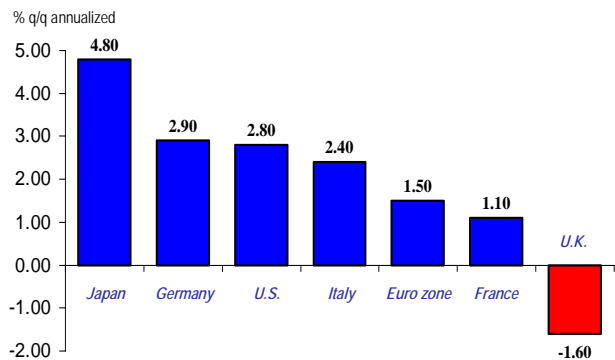
Leading economic indicators



\* 70% OECD, 30% BRIC (Brazil, Russia, India, China)  
NBF Economy & Strategy (OECD data via Datastream)

### World: A near-simultaneous recovery

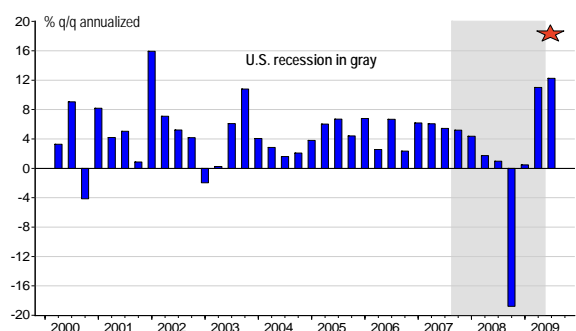
Q3 real GDP growth



NBF Economy & Strategy (data via Datastream and Global Insight)

### South Korea: Another spectacular quarter

Real GDP growth



★ Real growth of exports

NBF Economy & Strategy (data via Datastream)

**World Economic Outlook**

**Current Forecast**

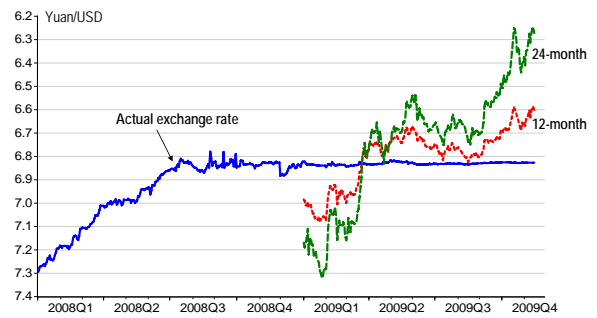
	2009	2010	2011
<b>Industrialized Countries</b>	<b>-3.0</b>	<b>2.5</b>	<b>1.9</b>
<i>(share of world GDP = 50%)</i>			
United States	-2.3	3.4	2.2
Euroland	-3.2	1.9	1.6
Japan	-5.0	1.7	1.5
UK	-4.0	1.6	1.8
Canada	-2.2	2.8	2.1
Australia	0.8	2.5	2.8
New Zealand	-1.3	2.0	2.2
<b>Asia (excluding Japan)</b>	<b>5.3</b>	<b>7.6</b>	<b>6.7</b>
<i>(share of world GDP = 25%)</i>			
China	8.5	9.8	8.2
Hong Kong	-2.8	3.5	3.3
India	6.2	7.5	7.2
Indonesia	4.4	4.6	4.2
Korea	-1.0	4.5	4.0
Malaysia	-2.5	4.0	3.8
Philippines	1.5	3.7	3.5
Thailand	-3.0	3.5	3.8
Taiwan	-3.5	4.0	4.2
Singapore	-2.5	4.0	4.3
<b>Latin America</b>	<b>-2.3</b>	<b>3.6</b>	<b>2.9</b>
<i>(share of world GDP = 6%)</i>			
Mexico	-6.0	3.5	2.5
Brazil	-0.2	4.4	3.5
Argentina	-2.5	2.3	2.0
Venezuela	-1.0	0.6	1.5
Chile	-0.8	4.0	3.5
Peru	1.5	4.2	3.8
<b>Eastern Europe</b>	<b>-4.6</b>	<b>3.0</b>	<b>3.1</b>
<i>(share of world GDP = 5%)</i>			
Russia	-6.0	3.5	3.3
Czech Rep.	-4.0	1.5	1.8
Hungary	-5.6	0.0	2.0
Poland	1.0	2.0	2.5
Turkey	-5.0	3.5	3.8
<b>World</b>	<b>-0.8</b>	<b>4.0</b>	<b>3.4</b>

Source: NBF Economic Research, Consensus Economic

However, the exports of all Asian economies benefit from China's peg of its currency to the U.S. dollar. Pressure is growing for Beijing to let its currency appreciate to allow a better adjustment of exchange rates to each country's current-account balance. In a drastic shift from the beginning of the year, financial markets have begun to anticipate a rise of the yuan over the next 12 to 24 months.

**Yuan: The market bets on revaluation**

Chinese currency futures (NDF)

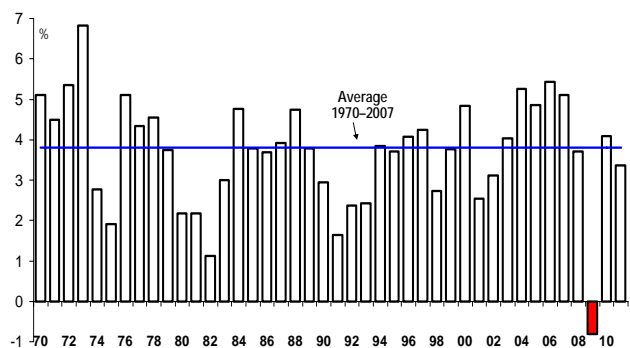


NBF Economy & Strategy (data via Global Insight and Bloomberg)

It is questionable whether China can keep its currency pegged to the greenback much longer without generating domestic inflationary pressures. Appreciation of the yuan would foster domestic demand growth via lower import prices, a development that would tend to correct global imbalances.

**World: Above-trend growth in 2010**

Global real GDP growth



NBF Economy & Strategy (historical data: IMF)

In sum, the key leading indicators herald a strong worldwide recovery in 2010. This alignment of the stars prompts us to upgrade our forecast this month. We now expect above-trend global growth next year.

## U.S.: Resilient consumer spending

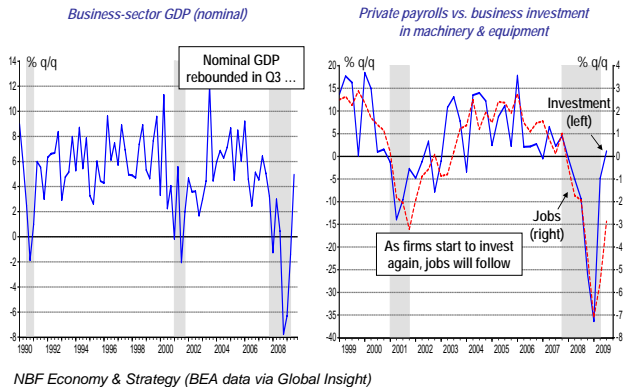
Despite job losses, struggling consumer confidence and the end of cash for clunkers, U.S. consumer spending is likely to expand at about 2% annualized in the fourth quarter. In other words, rising unemployment has not cut into consumer spending. We increased our forecast to 3.4% real GDP growth in 2010.

After some 20 months of recession, the U.S. economy is finally expanding again. The Bureau of Economic Analysis reports real growth of 2.8% annualized in the third quarter. We are especially encouraged by the growth rate of the business-sector GDP, because it suggests that corporate top lines are also in recovery. This development will likely end the aggressive cost-cutting that has led to sharp declines in employment and capital spending. Business investment rose at 2.3% in the third quarter, the first increase in almost two years.

Labour productivity jumped a spectacular 9.5% annualized in Q3, the strongest gain in six years. The corresponding peak in the ratio of nonfarm selling prices to unit labour costs has translated into a surge of profit margins. For now, the lion's share of recovery benefits is going to employers. The result will be strong earnings growth. Our forecast for the coming quarters is on track.

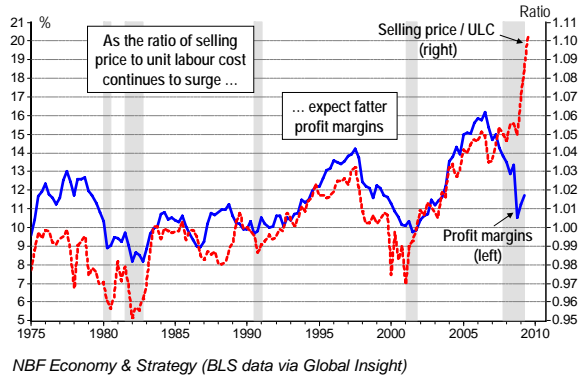
Payroll employment declined 190,000 in October and the unemployment rate rose to 10.2%. However, some labour market indicators suggest that job losses will soon end. First, the payroll numbers for prior months have been revised up a cumulative 91,000. This is often a sign of turnaround in employment. Second, the temporary-help supply industry, a bellwether of the labour market, added 34,000 jobs in October, the first substantial increase since the recession began. Third, the employment component of the ISM manufacturing index is now in positive territory, in contrast to its behaviour in the jobless recoveries of the early 1990s and early in this decade. And finally, initial unemployment claims have declined to the neighbourhood of 500,000, the lowest level since the beginning of the year, having fallen much faster than in the last two recoveries. The decline, amounting to 0.10% of the active population, exceeds that of several past recoveries. All in all, the threat of a jobless recovery has receded somewhat.

## U.S.: Business-sector GDP expands at 5% (nominal) in Q3

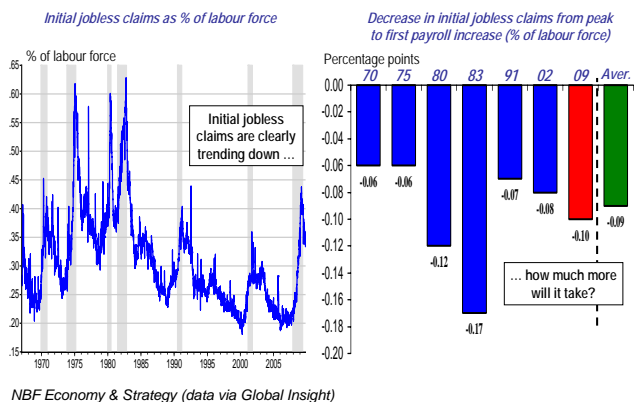


## U.S.: Efficiency gains point to strong profits

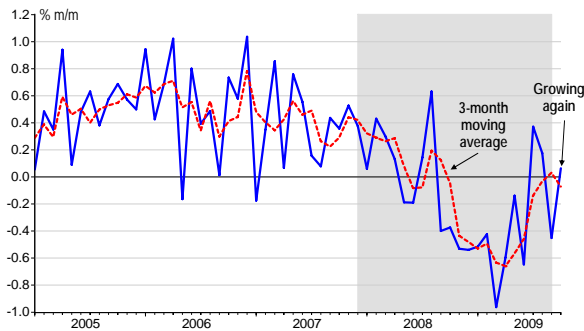
Ratio of selling price to unit labour cost, nonfarm business sector



## U.S. employment: Jobless claims vs. payroll growth



**U.S.: Aggregate wage bill on the rise in October**

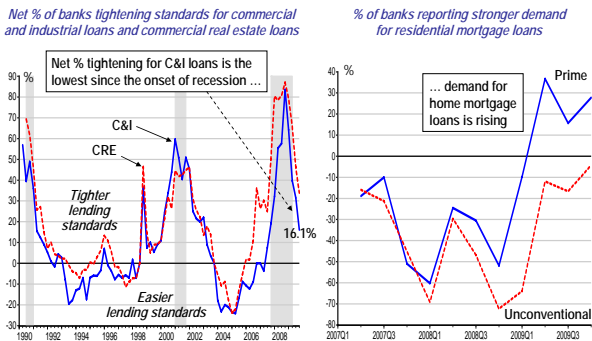


NBF Economy & Strategy (BLS data via Global Insight)

Despite struggling consumer confidence and the end of cash for clunkers, U.S. consumer spending is likely to expand at a respectable rate in the fourth quarter, close to 2% annualized. Retail sales were up 1.4% in October. In other words, consumer spending has been resilient despite deleveraging and a decline of aggregate consumer credit. This has been possible because household purchasing power has held out against job losses – the aggregate wage bill was flat in October. Going forward, a robust housing market, buoyed by stimulus including an extension to April of the \$8,000 tax credit for first-time homebuyers, can be expected to sustain consumer spending beyond the fourth quarter.

**U.S.: Least tightening of C&I lending since recession onset**

October 2009 survey of senior loan officers on bank lending practices

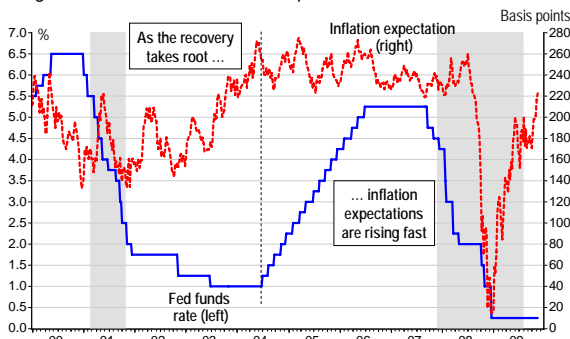


NBF Economy and Strategy (data via Federal Reserve)

The latest survey of senior loan officers shows another decline in the net percentage of banks tightening their commercial and industrial lending conditions. This reading is now the lowest since the onset of recession and its decline is consistent with the experience of other recoveries. We doubt that the revival of capital spending is threatened, especially since it is quite possible that bank lending conditions are only a reflection of reduced demand for credit.

**U.S. monetary policy: How long on the floor?**

Target fed funds rate and inflation expectation\*



\*Yield spread of 10-year Treasury over 10-year Treasury inflation-protected security  
NBF Economy & Strategy (data via Bloomberg)

Core inflation (i.e. excluding food and energy prices) came in at 1.7% in October, not far from the 2% generally taken to be the Fed's gauge of price stability. The rebound of energy prices will push all-items inflation up quite steeply in the months ahead. Since U.S. inflation expectations are up considerably after a single quarter of GDP expansion, the surge we expect in all-items inflation and inflation expectations will bear close watching. Considering that a long recession has left a yawning output gap, inflation has been fairly sticky.

This month we increased our 2010 forecast of U.S. real activity to 3.4%.

## Canada: Wage bill on the rise

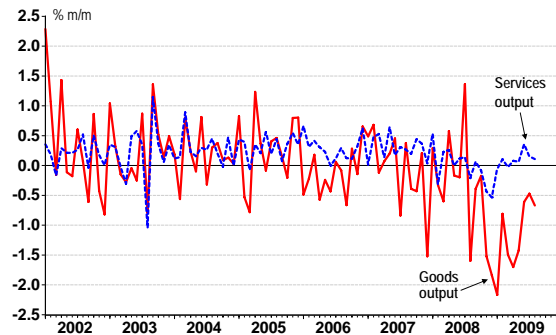
Despite months of disappointing GDP growth, the news on domestic demand remains good. Growth is accelerating in both homebuilding and consumer spending. The latter will be buoyed by strength in the aggregate wage bill.

The Canadian GDP report for August brought a second consecutive month of disappointment. The economy was once again held back by temporary factors. However, services output expanded for a fifth straight month. Though goods production declined, 13 of the 21 manufacturing industries produced more than in the previous month. If July and August were representative, GDP for the third quarter would be down 0.6% annualized from the second. However, a marked rise of hours worked in September suggests a gain in output.

The news on domestic demand remains good. September retail sales were up 1.2% in real terms from the previous month, for an acceleration of quarterly real growth to 5.2% annualized in Q3. This has set the stage for a strong increase in Q4 as well and supports our view that personal consumption expenditures will experience solid growth of at least 3% in Q3. Homebuilding is also gaining momentum. Housing starts, after jumping a spectacular 77% in Q3, surprised again in October with a rise to a 10-month high. An extrapolation of the October results to Q4 as whole implies a quarterly increase of 29% annualized.

Home prices have been rising vigorously. The cross-Canada index based on the repeat-sales method showed a fifth consecutive monthly increase in September. Prices in the three easternmost markets surveyed – Ottawa, Montreal and Halifax – are now above their pre-deflation peaks and the composite index is within 2.1% of its August 2008 peak. In short, home-price deflation is over. Homeowners are once again enjoying a significant wealth effect.

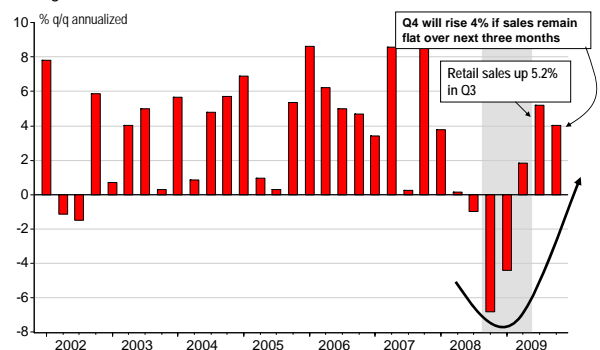
### Canada: Fifth straight month of rising services output



NBF Economy & Strategy (Statistics Canada data via Global Insight)

### Canada: Set for a second quarterly rise of retail sales

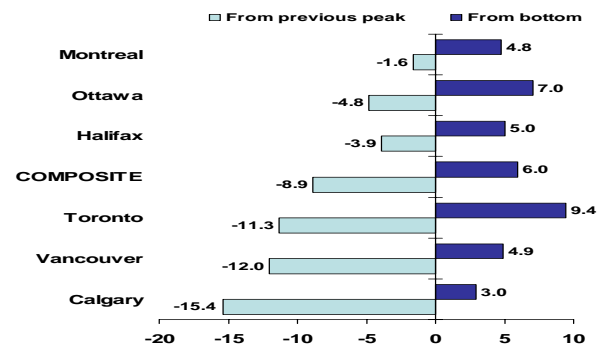
Real growth of retail sales



NBF Economy & Strategy (Statistics Canada data via Global Insight)

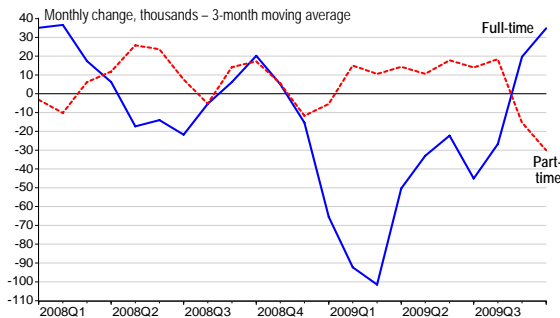
### Canada: Home prices climbing again

% change in home-price index (repeat-sales method)



NBF Economy & Strategy (Teranet-National Bank House Price Index)

**Canada: A shift from part-time to full-time jobs**

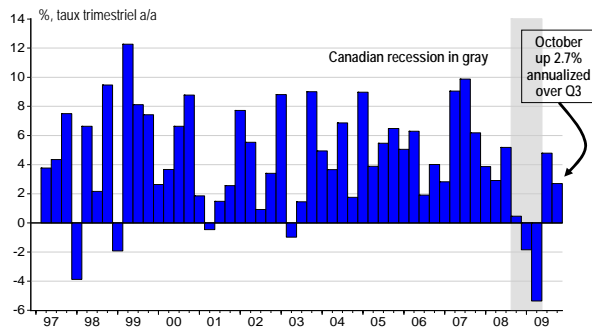


NBF Economy & Strategy (Statistics Canada data via Global Insight)

The Canadian labour market shrank in October for the first time in three months. The loss of 43,000 jobs reported by Statistics Canada seems discouraging at first sight, but there was good news in the details. All the losses were in part-time employment and 75% of them were among 15- to-24-year-old workers. Full-time employment was up 16,500, a very good showing on top of the startling September gain of 92,000. Over the last three months, 104,000 full-time jobs have been added and part-time employment equivalent to 90,000 jobs has been lost. A shift from part-time to full-time employment suggests an improving labour market.

**Canada: A strong start for the Q4 wage bill**

Total hours worked times average hourly earnings (seasonally adjusted)



NBF Economy & Strategy (Statistics Canada data via Global Insight)

Workers aged 15 to 24 are not the biggest contributors to the country's aggregate wage bill. For Canada's 16.8 million workers taken together, average hourly earnings jumped 0.7% in October after rising 0.2% in each of the previous two months. The three-month gain of 4.8% annualized brought the average hourly wage to \$22.35, a new high. Despite employment losses, the country's wage bill is up 3% in Q4 (extrapolating from October) and is now very close to the pre-recession peak. These indicators point to continued growth of consumer spending.

The Canadian trade deficit narrowed to \$0.9 billion in September from \$2.0 billion in August, mainly because of improvement in machinery and equipment exports and in automotive exports. Since the former now constitute the largest component of Canadian exports and will benefit from pent-up investment demand, Canadian exports may be spared severe collateral damage from the deleveraging of U.S. consumers. Canada is well-positioned to benefit from the U.S. recovery.

**Canada: Breakdown of merchandise exports**

	Current dollars		Constant dollars (2002)	
	2002	2009 ann.	2002	2009 ann.
Natural gas	4.4%	3.8%	4.4%	4.8%
Crude oil	4.5%	9.6%	4.5%	6.8%
Energy, other	3.0%	5.3%	3.0%	4.1%
Agriculture & fishing	7.5%	10.9%	7.5%	10.8%
Forest products	9.0%	5.6%	9.0%	7.1%
Industrial goods and materials	16.9%	21.6%	16.9%	17.5%
Machinery & equipment	23.4%	23.5%	23.4%	27.3%
Automotive products	23.3%	11.4%	23.3%	12.0%
Other consumption goods	4.3%	5.1%	4.3%	5.2%
Special transactions & adj.	3.6%	3.2%	3.6%	4.4%
<b>Total (\$billions)</b>	<b>414 038</b>	<b>409 548</b>	<b>414 038</b>	<b>341 447</b>

Source: Statistics Canada

**Yanick Desnoyers**  
Assistant Chief Economist

### Canada Economic Forecast

Annualized rate of change*	2006	2007	2008	2009	2010	Q4/Q4	
						2009	2010
Gross domestic product (2002 \$)	2.9	2.5	0.4	(2.4)	2.8	(1.1)	3.4
Consumption	4.1	4.6	3.0	0.1	2.5	1.5	2.3
Residential construction	2.0	2.9	(2.7)	(7.1)	4.2	2.4	0.6
Business investment	10.0	3.7	0.2	(13.1)	6.4	(8.4)	7.5
Government expenditures	3.3	3.7	4.8	3.5	3.0	4.0	2.4
Exports	0.8	1.1	(4.7)	(14.0)	4.3	(8.7)	4.2
Imports	4.7	5.8	0.8	(13.6)	7.4	(4.5)	4.0
Change in inventories (millions \$)	12,122	14,990	12,241	(4,230)	7,000	2,000.0	8,000.0
Domestic demand	4.5	4.1	2.6	(1.4)	3.2	0.8	2.9
Real disposable income	5.8	3.6	4.2	0.3	2.0	(0.0)	2.5
Employment	1.9	2.3	1.5	(1.6)	0.6	(1.8)	1.1
Unemployment rate	6.3	6.0	6.2	8.3	8.2	8.6	8.0
Inflation	2.0	2.2	2.4	0.3	1.6	0.8	2.0
Before-tax profits	5.1	4.1	5.7	(34.7)	13.6	(19.8)	15.0
Federal balance (Public Acc., bil. \$)	\$13.8	\$9.6	\$0.0	(\$45.0)	(\$30.0)	....	....
Current account (bil. \$)	\$20.3	\$15.6	\$8.1	(\$21.9)	\$4.5	\$0.0	\$5.0

\* or as noted

### Financial Forecast

	Current	Q4	Q1/10	Q2	Q3	2009*	2010*
	11/20/09						
Overnight rate	0.25	0.25	0.25	0.75	1.25	0.25	1.50
Prime rate	2.25	2.25	2.25	2.75	3.00	2.25	3.25
3 month T-Bills	0.29	0.23	0.45	0.93	1.33	0.23	1.43
Treasury yield curve							
2-Year	1.25	1.45	1.91	2.13	2.16	1.45	2.29
5-Year	2.56	2.79	3.22	3.40	3.44	2.79	3.57
10-Year	3.38	3.60	3.96	4.08	4.12	3.60	4.24
30-Year	3.93	4.03	4.23	4.29	4.33	4.03	4.43
Exchange rates*							
USD per CAD	0.93	0.92	0.88	0.89	0.92	0.92	0.94

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\* end of period

\*\* NBF forecast

### United States Economic Forecast

(Annual % change)*							Q4/Q4	
	2006	2007	2008	2009	2010	2009	2010	
Gross domestic product (2005 \$)	2.7	2.1	0.4	(2.5)	3.4	(0.3)	3.5	
Consumption	2.9	2.6	(0.2)	(0.6)	2.1	1.1	2.2	
Residential construction	(7.3)	(18.5)	(22.9)	(20.1)	8.7	(11.1)	9.5	
Business investment	7.9	6.2	1.6	(17.6)	3.7	(13.8)	7.3	
Government expenditures	1.4	1.7	3.1	2.2	2.6	2.0	2.0	
Exports	9.0	8.7	5.4	(10.4)	6.9	(3.6)	5.2	
Imports	6.1	2.0	(3.2)	(14.1)	8.6	(7.2)	7.7	
Change in inventories (bil. \$)	59.4	19.5	(25.9)	(119.4)	42.5	(70.0)	70.0	
Domestic demand	2.5	1.7	(0.4)	(2.6)	2.5	(0.6)	2.8	
Real disposable income	4.0	2.2	0.5	1.3	2.9	2.1	3.1	
Household employment	1.7	1.3	(0.5)	(3.7)	0.1	-3.9	2.0	
Unemployment rate	4.6	4.6	5.8	9.3	9.8	10.1	9.6	
Inflation	3.2	2.9	3.8	(0.4)	2.3	1.2	2.4	
Before-tax profits	10.5	(4.1)	(11.8)	(5.3)	13.1	23.6	8.0	
Federal balance (unified budget, bil)	(\$248.2)	(\$161.0)	(\$459.0)	(\$1,800.0)	(\$1,200.0)	...	...	
Current account (bil. \$)	(\$811.5)	(\$746.0)	(\$690.0)	(\$490.0)	(\$490.0)	(\$300.0)	(\$450.0)	

\* or as noted

### Financial Forecast

	Current						
	11/20/2009	Q4	Q1/10	Q2	Q3	2009*	2010*
Fed Fund Target Rate	0.19	0.11	0.25	0.75	1.25	0.11	1.50
3 month Treasury bills	0.02	0.07	0.42	0.93	1.33	0.07	1.43
Treasury yield curve							
2-Year	0.73	1.16	1.77	2.01	2.06	1.16	2.19
5-Year	2.18	2.54	3.06	3.26	3.30	2.54	3.43
10-Year	3.37	3.63	4.02	4.15	4.18	3.63	4.28
30-Year	4.30	4.44	4.67	4.73	4.75	4.44	4.81
Exchange rates*							
U.S.\$/Euro	1.49	1.45	1.40	1.35	1.30	1.45	1.25
YEN/U.S.\$	89	90	95	100	105	90	110

National Bank Financial

\* end of period

\*\* NBF forecast