

focus

A Weekly Financial Digest

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The Case for Corporates

- Dow, Loonie, Oil—All Hit 2009 Highs
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SHERRY COOPER

The U.S. Dollar's Decline Is Not Such a Bad Thing

Many have suggested that the fall in the U.S. dollar is reflective of the sad state of American economic affairs replete with surging budget deficits, profligate consumer spending, overleveraged banks, enormous current account deficits and an increasing reliance on foreign capital inflows to finance the overspending. I view this differently. The role the U.S. dollar plays as the world's sole reserve currency ensured that such imbalances developed, otherwise the growth in global reserves would have been impossible. Think of it this way: a growing global economy requires a growing global money supply to provide the liquidity necessary to finance rising activity. The U.S. provides that underlying liquidity to the world by spending more than it saves or, in essence, spending more than it can finance domestically. The U.S. became the consumer (importer) of last resort, providing currency to the rest of the world. This currency has been at least partially re-cycled back to the U.S. in the form of foreign purchases of private and U.S. government and agency debt. Without this recycling, the other currencies of the world would strengthen rapidly vis-à-vis the U.S. dollar, rendering these foreign exporters less competitive, returning the system to balance. The fall in the U.S. dollar is the equilibrating mechanism that reduces the net imports of the U.S., thereby reducing its current account deficit and, ultimately, its demand for foreign capital.

The broad trade-weighted U.S. dollar began falling in February 2002 and bottomed in July 2008 at under 95. With the onslaught of the credit crisis, the flight to quality (safe-haven flows) into Treasuries boosted the trade-weighted dollar to a peak of roughly 115 in March of this year when the stock markets bottomed. As the financial crisis dissipated and stocks rebounded sharply, the dollar resumed its decline, reflecting the success of the global authorities—especially the Fed and the U.S. Treasury—in averting disaster. The recovery in economic activity was beginning, as reflected in stocks and commodity prices. The reduction in the U.S. trade deficit has been an important contributor to GDP performance.

Even with the dramatic decline in the U.S. dollar since March, the trade-weighted dollar is still about 5% above its summer-'08 trough. Year-to-date, the Canadian dollar has risen almost 20%, but that is less than a number of other major currencies, particularly the Aussie dollar, which is up over 30%. These commodity-related currencies have benefited from the economic revival, especially in China. Even so, the Canadian dollar, at just over 96 cents, remains below the peak of \$1.10 hit in November 2007.

I expect the U.S. dollar to continue to decline—not because of American profligacy per se, but because under the current global monetary system, a fall in the dollar is the only way to reduce the global imbalances. The huge net inflow of foreign capital to the U.S., especially from China, facilitated America's over-leveraging and underpricing of risk.

Ever since the Asian crisis in the late 1990s, the emerging world (China) has been pursuing a policy of export-led growth by maintaining their currencies at undervalued levels. The U.S.'s consumption-led growth is the flipside of China's export-led growth, taking consumption to a record high 70% of U.S. GDP. Thanks to enormous foreign capital inflow, capital in the U.S. was cheap and plentiful and risk was woefully underpriced so consumers were incentivized to borrow. And borrow they did—extracting homeowner equity and running up huge credit card bills. Similarly, because

of the inordinately low interest rates and risk premia, investor demand for higher-yielding assets such as CDOs and CDSs surged, financing the subprime mortgage debt and housing bubble. The rest is history.

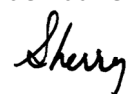
Being the sole reserve-currency country forced the U.S. into a current-account-deficit position, which by definition, ironically, weakens the currency over time. As long as the U.S. economy was strong, and the federal budget deficit was under control, no one worried much about the safety and soundness of the U.S. dollar. But with the explosion in U.S. government spending that was precipitated by the crisis and subsequent recession, the government deficit skyrocketed. Many began to worry about the ultimate inflation that might result if it were the only way to finance the deficit and so the currency weakened.

As the reserve-currency nation, the U.S. is the lender of last resort to the world. The Fed and the Treasury had to spend whatever it took to avert a global financial meltdown. Thus, in bad times, the dollar is necessarily vulnerable to inflation worries and ultimate devaluation. Right now, there are no other serious contenders to replace the U.S. dollar as the world's reserve currency—certainly not the renminbi or even the euro or yen.

It is essential that the Fed remain independent with no predilection or authority to conduct monetary policy in response to the dollar's fate; it is also required that the U.S. federal government remains solvent. That is certainly the case now, and will be for the foreseeable future. But the pessimists are very vocal and the media is increasingly espousing their views that the Fed will run the printing presses for too long, thereby devaluing the dollar and using inflation to reduce the cost of deficit financing. Never mind that inflation is nowhere to be seen.

The enormous excess capacity in the U.S. economy and the downward pressure on real wages suggest, as the Fed avers, that there is a greater likelihood of falling inflation than rising inflation in the U.S. The lower dollar helps to reverse these disinflationary pressures and improve the U.S. trade deficit, thereby boosting the U.S. economy. But sentiment is important, and the growing sense that the U.S. dollar is a "debauched" currency (similar to those in the 'Banana Republics' of the past) can become self-fulfilling if it triggers a dollar crisis. The unlikely, but possible, rout in the dollar could drive U.S. interest rates high enough to snuff out the recovery, debilitating the rest of the world's recovery. That is why it is so important to discredit the Chicken Littles.

Bottom Line: An orderly decline in the U.S. dollar is necessary to a sustained re-balancing of the global economy. This re-balancing is a necessary precursor to a sustained global economic and financial recovery. The only way the American economy can de-leverage gradually over time is for the overspending to cease, which also goes hand-in-hand with a weaker American dollar. The U.S. must encourage some export-led activity and China must encourage some consumer-led activity, which means a smaller U.S. trade deficit and a smaller trade surplus in the rest of the world. We see this in spades in Canada where our record trade surplus has now melted into a record trade deficit. Our exporters have been adjusting to this new reality since 2003 and further adjustment is necessary. Canadian business must continue to raise productivity growth and add value to the goods and services we export. We must also broaden our export horizons, especially to the rapidly growing emerging economies of Asia.





DOUGLAS PORTER

The flip side of the weak U.S. dollar is, of course, the astonishing comeback in the Canadian dollar. In a complete reversal from last fall's deep dive, the loonie has rocketed 25% from its low of just under 77 cents (or \$1.30/US\$), which not coincidentally was reached on March 9—the very day that global stocks bottomed. For all intents and purposes, the currency is right back to where it stood before it was so rudely interrupted by last year's financial market meltdown. And perhaps more importantly than the level, the underlying trend towards an even stronger Canadian dollar seems to be back in place as well. While the currency retreated a bit in the latter stages of the week, cooling to just over 96 cents, it still looks like a trip to par (and beyond) is all but inevitable.

Some have downplayed the surge in the loonie, since it has gone hand-in-hand with steep climbs in many other currencies. However, that hardly dulls the pain for domestic manufacturers. The simple fact is that the Canadian economy is much more sensitive to the US\$ than, say, Australia, because exports to the U.S account for a much bigger share of our economy than other industrialized countries. And, yes, we have been at parity before in recent years, but this episode is somewhat different. In contrast to the 2007 rush to par, this trip has not been accompanied by a commodity boom, and it also comes against the backdrop of still very weak U.S. demand. The Bank of Canada's commodity price index has risen by 20% from its February lows, but it's still more than 40% below the mid-2008 peaks and about 15% below the level when the C\$ first hit par in 2007. The main point is that the latest surge is indeed likely to put a heavy dampener on Canada's fledgling economic recovery, accentuating the lopsided nature of that rebound—solid domestic activity, very weak exports/manufacturing.




SAL GUATIERI

A couple of developments this week provided reassurance that, despite growing signs of recovery and more rumblings of dissent from some Fed hawks, policy will likely remain unchanged well into next year. First, Vice Chairman Kohn, probably the closest adherent to the mainstream Fed view, bluntly stated that lower inflation is still a bigger risk than higher inflation because of the massive output gap and fragile nature of the recovery. Second, the minutes of the September policy meeting noted that some members actually considered more credit easing, by expanding the mortgage-purchase program, while just one member thought that some pullback was in order. In the end, the members agreed to commit to buying the full \$1¼ trillion allotment, and extending the purchases by three months to the end of March to facilitate a smooth transition in mortgage markets. Of note, both Kohn and the meeting minutes cited inflation expectations as a critical barometer for future policy decisions, one that will likely determine how long the hawks can be kept at bay. So far, measures of inflation expectations from the TIPS market remain range-bound, though they turned up slightly this week in the wake of higher commodity prices, the lower greenback and the first increase in core CPI inflation (to 1.5%) in five months. Still, core inflation should continue to trend lower, as it has done after each of the last six recessions, with declining rents and real wages more than offsetting a recent upturn in medical care costs. As a result, we don't expect the Fed to begin raising rates until next September, about six months later than the market anticipates.



Jennifer Lee, Economist

CANADA

- CAD nears parity @ \$1.0253 (97.5 cents)

UNITED STATES

- Generally good earnings results boost Dow > 10,000
- FOMC minutes showed debate over whether or not to increase MBS purchases

EUROPE

- £ boosted on speculation APF won't be increased following comments from BoE's Fisher (QE is working)

JAPAN

- BoJ on hold, but upgrades view of economy to that of 'recovery'

CHINA

- Foreign institutional investment limit on domestic stocks raised to \$1 bln from \$800 mln

GOOD NEWS

New House Price Index +0.1% (Aug.)
Existing Home Sales +16.7% y/y (Sep.)—and
Average Prices +13.6% y/y
Consumer Prices unch (Sep.)
Manufacturing New Orders +0.2% (Aug.)

Core Retail Sales +0.5% (Sep.)—up 2 months in a row
Redbook +1.6% (Oct. 10 wk)
Initial Claims -10,000 to 514,000 (Oct. 10 wk)
Consumer Prices +0.2% (Sep.)
Import Prices +0.1% (Sep.)
Empire State Manufacturing Survey +15.7 pts to 34.6 (Oct.)
Industrial Production +0.7% (Sep.)
Capacity Utilization +0.6 ppts to 70.5% (Sep.)
Foreigners buy a net \$28.6 bln of U.S. Long-Term Securities

Eurozone—Industrial Production +0.9% (Aug.)
U.K.—Consumer Prices unch (Sep.)
U.K.—RICS House Price Balance +12 pts to +22 (Sep.)—highest since May 2007

Corporate Goods Prices +0.1% (Sep.)
Consumer Confidence +0.3 pts to 40.7 (Sep.)

Exports +6.3%, **Imports** +8.3% (Sep.)
Passenger Car Sales +83.6% y/y (Sep.)
M2 +29.3% y/y (Sep.)
New Yuan Loans +38.0% y/y to Y516.7 bln (Sep.)
Foreign Direct Investment +18.9% y/y (Sep.)
Home Prices +2.8% y/y (Sep.)

CANADA

U.S.

EUROPE

JAPAN

CHINA

BAD NEWS

New Motor Vehicle Sales -0.3% (Aug.)
Manufacturing Sales -2.1% (Aug.)

Business Inventories -1.5% (Aug.)
Philadelphia Fed Index -2.6 pts to 11.5 (Oct.)
U. of M. Consumer Sentiment Index -4.1 pts to 69.4 (Oct. P)

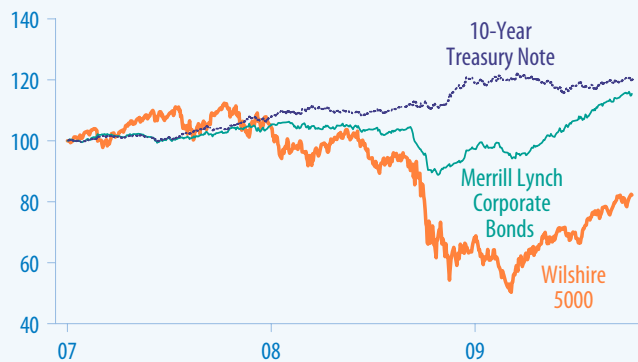
Eurozone—Trade Surplus shrank to €1.0 bln (Aug.)
Germany—ZEW Survey -1.7 pts to 56.0 (Oct.)
U.K.—Unemployment +20,800 (Sep.)

Bank Lending slowed to +1.7% y/y (Sep.)

Indications of stronger growth and a move toward price stability are good news for the economy.

CHART 1
CORPORATES BEAT STOCKS DURING CREDIT CRISIS

United States (January 1, 2007 = 100)

Total Returns

TABLE 1
STUCK IN THE MIDDLE AGAIN

United States

	Treasuries	Corporates	Stocks
Compound Annual Return (Jan '87-Sep '09)	7.0%	7.8%	8.9%
Standard Deviation	4.8	6.9	19.2

TABLE 2
POST-RECESSION: MANY HAPPY RETURNS

United States (y/y % chng)

Period	Corporates	Treasuries	Stocks
24 Months after Recession Ends:			
1991	15.4	12.2	15.4
2001	8.5	5.3	0.7
Average	12.0	8.7	8.1
12 Months after Recession Ends:			
1991	13.4	10.0	13.7
2001	6.2	7.0	-14.7
Average	9.8	8.5	-0.5

The Case for Corporates

Sal Guatieri, Senior Economist

A couple of weeks ago, our *Feature* article “Can Stocks Earn Their Keep?” argued persuasively that the equity rally still has legs, on the basis of reasonable valuations, aggressive cost cutting, profit margin expansion, low interest rates and (in Canada’s case) rising resource prices. However, a strong case can also still be made for corporate bonds, which stand a good chance of out-returning Treasuries and perhaps even stocks in the year ahead.

Although U.S. equities have racked up their best return since the 1930s (64% from March lows), corporate bonds haven’t exactly stood still, returning an impressive 22%. Growing signs that the financial crisis and recession are over have whetted risk appetites, and corporate defaults have been slowing since mid-year. With U.S. bank lending standards still restrictive, companies are offering juicy premiums to investors for funding. Corporates have actually outperformed equities in the credit crisis; and on a year-to-date basis, have almost stood toe-to-toe with stocks, returning 18% versus 24% (*Chart 1*). Both assets have trounced long Treasuries this year, which are slightly underwater after a 1¼-percentage-point leap in yields.

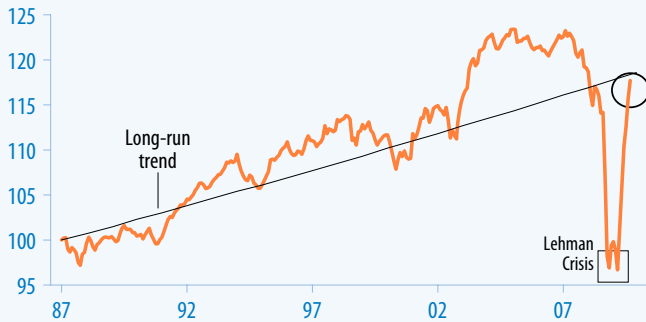
The “in-between” return for corporate bonds relative to equities and Treasuries this year adheres to the historical pattern. Since 1987, corporate bonds have returned an annual compound rate of 7.8%, topping 10-year Treasuries by 0.8 percentage points but lagging stocks by 1.1 percentage points (*Table 1*). However, the trade-off against higher-returning stocks is substantially less volatility (and a better night’s rest). The standard deviation for equity returns is three-times higher than that for corporates. Notably, corporate bonds usually perform well after recessions, topping their long-term return (*Table 2*). While corporates held their own against equities in the two years following the 1991 downturn, they swamped stocks in the post-2001 downturn, helped by an economic recovery that was too timid to stoke inflation and by the grinding correction in tech stocks.

Comparing asset returns with long-term trends suggests corporate bonds were grossly undervalued against Treasuries in the past year, after spending most of the prior decade in

CHART 2
CORPORATES RECENTLY UNDERVALUED VS. TREASURIES

United States (January 1987 = 100)

Corporates/Treasuries Return Ratio *

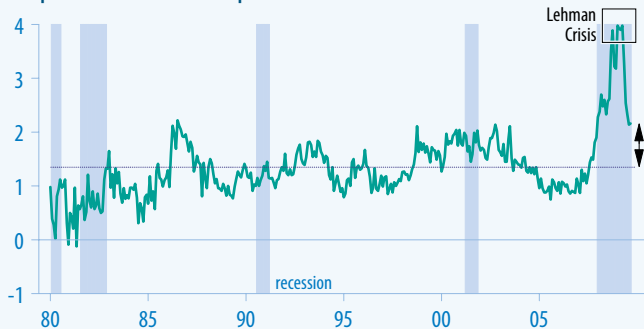


* Merrill Lynch Corp. Bonds / 10-Yr Treasury Total Returns

CHART 3
CLOSING THE GAP

United States (ppts)

Corporates-Treasuries Spread *

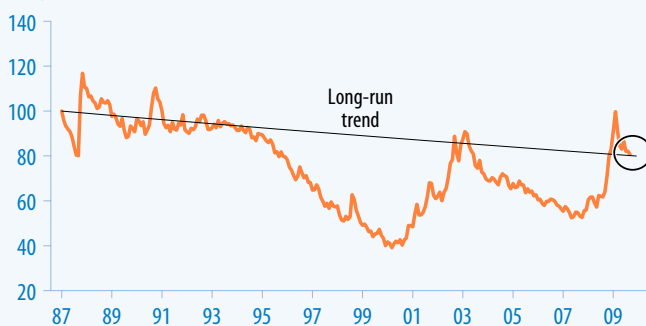


* Citigroup Corporate AAA/AA 10+ Year Yield less 10-Year Treasury Rate

CHART 4
CORPORATES FAIRLY VALUED AGAINST STOCKS

United States (January 1987 = 100)

Corporates/Stocks Return Ratio *



* Merrill Lynch Corporate Total Returns / Wilshire 5000 Total Returns

lofty territory because investors were under-pricing risk (Chart 2). Because credit risks haven't fully normalized from last year's blow-out, corporates could benefit from further spread compression (Chart 3). By contrast, corporate bonds were over-priced against stocks earlier this year due to the plunge in equity values to March, but the subsequent stock rally has largely rebalanced returns (Chart 4).

While a consideration of past performance and current valuation is important for assessing how well the three asset classes might perform in the future, it's the macroeconomic climate that will largely determine their fate. Given three plausible scenarios for the U.S. economy in 2010, corporate bonds would appear to offer the best risk-reward trade-off (Table 3)

- Under our base-case **modest growth** scenario (sub-3%), demand may be too weak to juice earnings, thus limiting stock price gains. Growth would also be too weak to sop up the massive spare capacity, pressuring inflation lower, and hence favouring bonds over stocks. At the same time, even a modestly growing economy should curb defaults, resulting in narrower credit spreads, a plus for corporates. This should provide some offset to an expected gradual tightening in monetary policy beginning in the fall of 2010 that will weigh on bonds.
- In the event of a **strong recovery** (plus-3%), stocks would likely outperform as earnings estimates get revised up, and Treasuries would get hammered as risk aversion beats a hasty retreat. Corporate bonds would weaken as interest rates climb, but the losses could be tempered by lessening default risk and narrowing credit spreads. The probability of a strong recovery next year, in our view, is low given still-severe headwinds—consumer deleveraging, rising foreclosures and strict lending standards, while the possibility of rising inflation is even lower given the massive output gap.
- Should the **economy reverse course**, Treasuries would win big and equities would plunge. Corporate bonds would also weaken amid rising default risk and widening credit spreads, though the losses could be limited by even lower inflation and further quantitative easing by the Fed.

TABLE 3
IMPLICATIONS OF THREE ECONOMIC
SCENARIOS FOR ASSET CLASSES

Growth in 2010	Stocks	Corporates	Treasuries
Strong	✓	✓	✗
Modest	✓	✓	✗
Negative	✗	✗	✓

This is not to say that corporate bonds are risk-free. The IMF expects U.S. business loan defaults to continue rising until late 2009 or early 2010. There is a small chance that a return of financial instability will cause risk appetites to evaporate and credit spreads to blow-out again. As well, investors need to be cautious of the wobbly commercial property market, where defaults and bankruptcies are still rising sharply. Longer term, the debt issued to finance the previous private-equity boom will come due, pressuring the market. An unexpected surge in inflation, leading to a faster renormalization of monetary policy, would slam bonds. A two-percentage-point increase in interest rates could reduce 10-year bond values by 17%. However, investors could seek to limit their losses (and potential returns) by purchasing shorter-term bonds.

The Bottom Line: In these unsettled economic times, corporate bonds look to offer higher risk-adjusted rates of return than Treasuries or even equities if the recovery and inflation stay subdued next year, as we expect.

CANADA	2009				2010				ANNUAL		
	I	II	III	IV	I	II	III	IV	2008	2009	2010
Real GDP (q/q % chng : a.r.)	-6.1	-3.4	1.3	3.4	2.9	3.3	3.5	2.9	0.4	-2.4	2.6
Consumer Price Index (y/y % chng)	1.2	0.1	-0.9	0.6	1.1	1.4	2.0	1.7	2.4	0.3	1.5
Unemployment Rate (%)	7.6	8.4	8.6	8.8	8.9	8.7	8.5	8.3	6.1	8.3	8.6
Housing Starts (000s : a.r.)	140	128	149	149	147	148	150	155	211	141	150
Current Account Balance (\$blns : a.r.)	-30.9	-44.8	-54.1	-50.2	-50.4	-51.7	-52.9	-53.1	8.1	-45.0	-52.0
Interest Rates (average for the quarter : %)											
Overnight Rate	0.83	0.25	0.25	0.25	0.25	0.25	0.58	1.08	2.96	0.40	0.54
3-month Treasury Bill	0.64	0.25	0.22	0.22	0.22	0.30	0.78	1.25	2.33	0.33	0.64
10-year Bond	2.89	3.20	3.42	3.30	3.43	3.54	3.65	3.76	3.61	3.20	3.60
Canada/U.S. Interest Rate Spreads (average for the quarter : bps)											
90-day	43	8	6	12	12	20	55	53	94	17	35
10-year	15	-11	-10	0	-7	-11	-15	-19	-6	-2	-13
UNITED STATES											
Real GDP (q/q % chng : a.r.)	-6.4	-0.7	3.8	3.0 ↑	2.3	2.5	2.7	2.9	0.4	-2.4	2.5
Consumer Price Index (y/y % chng)	-0.2	-0.9	-1.6	1.1 ↑	2.0	2.2 ↓	1.8 ↓	1.7 ↓	3.8	-0.4	1.9 ↓
Unemployment Rate (%)	8.1	9.2	9.6	10.0	10.2	10.0	9.9	9.8	5.8	9.2	10.0
Housing Starts (mlns : a.r.)	0.53	0.54	0.60	0.62	0.68	0.74	0.78	0.82	0.90	0.57	0.75
Current Account Balance (\$blns : a.r.)	-418	-395	-409	-379	-375	-373	-369	-361	-706	-400	-370
Interest Rates (average for the quarter : %)											
Fed Funds Target Rate	0.13	0.13	0.13	0.13	0.13	0.13	0.25	0.75	1.86	0.13	0.31
3-month Treasury Bill	0.21	0.17	0.16	0.10	0.10	0.10	0.23	0.73	1.39	0.16	0.29
10-year Note	2.74	3.31	3.52	3.31	3.50	3.65	3.80	3.95	3.67	3.22	3.73
EXCHANGE RATES (average for the quarter)											
US\$/C\$	80.3	85.6	91.1	96.6 ↑	98.7 ↑	99.7 ↑	100.7 ↑	100.3	94.3	88.4 ↑	99.8 ↑
C\$/US\$	1.245	1.168	1.097	1.035	1.013	1.003	0.993	0.997	1.067	1.136	1.002
¥/US\$	94	97	94	90 ↓	92 ↓	94 ↓	97 ↓	99 ↓	103	94 ↓	95 ↓
US\$/Euro	1.30	1.36	1.43	1.47	1.49	1.51	1.53	1.54	1.47	1.39	1.52
US\$/£	1.44	1.55	1.64	1.59 ↓	1.60 ↓	1.65 ↓	1.69 ↓	1.74 ↓	1.85	1.55 ↓	1.67 ↓

Note: Blocked areas represent BMO Capital Markets forecasts
Up and down arrows indicate changes to the forecast ↑↓

CANADA

Michael Gregory, CFA, Senior Economist

BoC Policy Announcement and Monetary Policy Report

Policy Announcement:

Tuesday, 9:00 am

Monetary Policy Report:

Thursday, 10:30 am

The Bank of Canada is expected to reiterate its commitment to keep the policy rate at 0.25% until the end of June 2010, conditional on the inflation outlook, after repeating it in nearly every public pronouncement during the inter-meeting period. As such, any potential alteration to the inflation outlook (mentioned in Tuesday's policy statement and detailed in Thursday's Monetary Policy Report) could be market moving. The previous MPR projected core CPI inflation to average 1.4% y/y in Q4 and Q1 (2010), before slowly grinding back to the 2% target by the spring of 2011. In September, core inflation was 1.5% and the short-term trend points to further deceleration: the three-month annualized change was just 0.7%.

More significantly, recent strength in the Canadian dollar argues for an inflation downgrade. The Bank employs the loonie's average level during the inter-meeting interval as a working assumption for their inflation projection, which was 87.2 US cents in the July MPR. But, the current period has averaged 92.7 cents with the loonie ending over 96 cents. Apart from the elevated average, the currency's parity approach also augments disinflation risks.

Although the massive downward pressure on core inflation displayed during late 2007, when the currency first pushed through parity, might not be repeated (the three-month trend plummeted to zero during the final two months of the year), re-ignited cross-border shopping should still have a powerful impact. Indeed, we judge that the Bank will signal heightened concern about the currency. The prior policy statement said: *"Persistent strength in the Canadian dollar remains a risk to growth and to the return of inflation to target. In its conduct of monetary policy at low interest rates, the Bank retains considerable flexibility."* The juxtaposition of these two sentences, also repeated in nearly every public pronouncement, is intentional, serving as a subtle warning that should "Type II" currency appreciation (the kind not driven by commodity prices) prove excessive, the Bank would take this into account in setting policy. Carney & Co. could conclude that a less subtle warning is warranted at this stage.

Perhaps tempering a potential inflation downgrade will likely be any upgrade to the Bank's near-term GDP outlook. In the September policy statement, it was already acknowledged that *"GDP growth in the second half of 2009 could be stronger than the Bank projected in July"*. The past projection was for annualized growth of 1.3% and 3.0% in Q3 and Q4, respectively (we match for Q3 but are at 3.4% for Q4). However, this is unlikely to fully offset the disinflation momentum on the ground and, particularly, the loonie's parity flight plan.

Retail Sales

Thursday, 8:30 am

		Ex. Autos
Aug. (e)	+0.4%	+0.6%
Consensus	+0.2%	+0.5%
July	-0.6%	-0.8%

With employment expanding in August, for the first time in 10 months, and consumer confidence spiking up, retail sales probably rose a respectable 0.4%. The figure was braked a bit by lower vehicle sales volumes but was flattered by higher gasoline prices. Ex-autos, retail sales likely increased 0.6%, and 0.4% ex-autos and gas. Importantly, with CPI goods prices inching up only 0.1% (nsa) in the month (-3.3% y/y), most of the retail sales rise is real. As such, real consumer spending appears on track to post another rise after Q2's 1.8% annualized advance.

UNITED STATES

Benjamin Reitzes, Economist

Producer Price Index

Tuesday, 8:30 am

Sep. (e)	+0.2%	-4.0% y/y
Consensus	+0.1%	-4.3% y/y
Aug.	+1.7%	-4.3% y/y
Ex. Food & Energy		
Sep. (e)	+0.1%	+2.0% y/y
Consensus	+0.1%	+2.0% y/y
Aug.	+0.2%	+2.3% y/y

Housing Data

NAHB Housing Index:

Monday, 1:00 pm

Oct. (e)	20
Consensus	20
Sep.	19

Housing Starts: Tuesday, 8:30 am

Sep. (e)	610,000 a.r. (+2.0%)
Consensus	610,000 a.r. (+2.0%)
Aug.	598,000 a.r. (+1.5%)

Building Permits: Tuesday, 8:30 am

Sep. (e)	590,000 a.r. (+1.9%)
Consensus	590,000 a.r. (+1.9%)
Aug.	579,000 a.r. (+1.5%)

FHFA House Price Index:

Thursday, 10:00 am

Aug. (e)	-3.1% y/y
July	-4.1% y/y

Existing Home Sales:

Friday, 10:00 am

Sep. (e)	5.50 mln a.r. (+7.8%)
Consensus	5.40 mln a.r. (+5.9%)
Aug.	5.10 mln a.r. (-2.7%)

Beige Book

Wednesday, 2:00 pm

Higher food and natural gas prices likely pushed producer prices slightly higher in September. However, lower gasoline and heating oil should temper the headline gain. The increase would slow the yearly rate of decline to 4.0%, a trend that should continue as big drops from a year ago fall out of the calculation. Look for a 0.1% gain in core PPI, slowing the annual rate of inflation to 2%, a more than two-year low and confirming that inflation concerns remain on the backburner.

The housing recovery likely continued in September and into October. The improving climate in the industry likely pushed homebuilder confidence up another point in October, with the NAHB index gunning for its sixth straight monthly advance. However, there is some downside risk to this report as the practical deadline for qualifying for the first-time homebuyer tax credit was the end of September (since it takes about 60 days to close).

Meantime, September housing starts and permits should also continue to improve, mirroring the positive trend in new home sales.

Existing home sales probably gained ground as well, after pending home sales were up 9.7% in July and August. Look for housing to start adding to growth in the near future for the first time in over four years. And importantly, FHFA home prices are expected to rise for the fourth straight month, another sign better times are ahead for housing.

The Fed's Beige Book prepared for the November 3-4 meeting will likely continue the cautiously optimistic tone from the previous release. Consumer spending (excluding autos, due to the cash-for-clunkers hangover), residential real estate and manufacturing should be more positive. In September, "*credit standards ranged from unchanged to tighter in most Districts.*" Improving financial market conditions could see some more encouraging developments on the credit front, which is essential for recovery. One trouble spot that isn't likely to fade any time soon is commercial real estate, which remains a significant concern for the Fed.

	OCT 16*	OCT 9	CHANGE FROM: (BASIS POINTS)		
			WEEK AGO	4 WEEKS AGO	DEC. 31/08
Canadian Money Market					
Call Money	0.25	0.25	0	0	-125
Prime Rate	2.25	2.25	0	0	-125
U.S. Money Market					
Fed Funds (effective)	0.25	0.25	0	0	0
Prime Rate	3.25	3.25	0	0	0
3-Month Rates					
Canada	0.24	0.21	3	2	-59
United States	0.06	0.06	-1	-2	-2
Japan	0.20	0.15	6	5	0
Eurozone	0.74	0.74	0	-2	-215
United Kingdom	0.57	0.56	2	-1	-220
Australia	3.67	3.51	16	38	-118
Bond Markets					
2-year Bond					
Canada	1.64	1.70	-6	36	55
United States	0.96	0.96	0	-3	20
10-year Bond					
Canada	3.53	3.51	1	13	84
United States	3.42	3.38	4	-4	121
Japan	1.33	1.29	3	-2	15
Germany	3.28	3.20	7	-10	32
United Kingdom	3.59	3.45	14	-15	57
Australia	5.58	5.22	36	30	159
Currencies					
				(% CHANGE)	
US\$/C\$	96.11	95.95	0.2	2.8	17.1
C\$/US\$	1.040	1.042	—	—	—
¥/US\$	91.01	89.78	1.4	-0.3	0.4
US\$/Euro	1.4870	1.4732	0.9	1.1	6.4
US\$/£	1.635	1.584	3.2	0.5	12.0
US\$/A\$	91.55	90.37	1.3	5.5	30.3
Commodities					
CRB Futures Index	272.41	262.55	3.8	4.8	18.7
Oil (generic contract)	77.29	71.77	7.7	7.3	73.3
Natural Gas (generic contract)	4.71	4.77	-1.4	24.5	-16.3
Gold (spot price)	1049.93	1049.25	0.1	4.2	19.0
Equities					
S&P/TSX Composite	11435	11437	0.0	-0.1	27.2
S&P 500	1082	1071	1.0	1.3	19.8
Nasdaq	2144	2139	0.2	0.5	35.9
Dow Jones Industrial	9947	9865	0.8	1.3	13.3
Nikkei	10258	10016	2.4	-1.1	15.8
Frankfurt DAX	5753	5712	0.7	0.9	19.6
London FT100	5190	5162	0.5	0.3	17.0
France CAC40	3830	3800	0.8	0.1	19.0
S&P ASX 200	4836	4753	1.8	3.1	29.9

* as of 10:30 am

JAPAN

U.K. EUROZONE

OTHER

MONDAY OCTOBER 19
Tertiary Index

Aug. (e) **+0.1%**
July +0.6%

Nationwide Dept. Store Sales

Sep.
Aug. **-8.8% y/y**

**Minutes from the September 16-17
BoJ Monetary Policy Meeting**

Rightmove House Prices

Oct.
Sep. **+0.6%** **-1.5% y/y**

TUESDAY OCTOBER 20
Leading Index

Aug. F (e) **83.3**
July 82.5

Machine Tool Orders

Sep. F (e) **-61.9% y/y**
Aug. **-71.5% y/y**

GERMANY
Producer Price Index

Sep. (e) **-0.1%** **-7.1% y/y**
Aug. **+0.5%** **-6.9% y/y**

ITALY
Industrial Orders

Aug. (e) **+1.0%** **-20.0% y/y**
July **+3.2%** **-23.2% y/y**

M4 Money Supply

Sep. P (e) **+11.4% y/y**
Aug. **+12.5% y/y**

AUSTRALIA

**Minutes from the Reserve Bank of
Australia Monetary Policy Meeting**

WEDNESDAY OCTOBER 21

**Minutes from the BoE Monetary Policy
Meeting**

AUSTRALIA
New Motor Vehicle Sales

Sep.
Aug. **+0.3%** **-6.2% y/y**

MEXICO
Jobless Rate

Sep. (e) **6.3%**
Aug. **6.3%**

THURSDAY OCTOBER 22
Merchandise Trade Surplus

Sep. '09 (e) **¥0.6 trln**
Sep. '08 **¥0.1 trln**

All-Industry Activity Index

Aug. (e) **+0.4%**
July **+0.5%**

ITALY
Retail Sales

Aug. (e) **+0.1%** **-1.7% y/y**
July **-0.4%** **-2.6% y/y**

Retail Sales

Sep. (e) **+0.5%** **+2.8% y/y**
Aug. **unch** **+2.1% y/y**

CHINA
Real GDP

Q3 (e) **+9.0% y/y**
Q2 **+7.9% y/y**

CPI **PPI**
Sep. (e) **-0.8% y/y** **-7.4% y/y**
Aug. **-1.2% y/y** **-7.9% y/y**

Retail Sales

Sep. (e) **+15.5% y/y**
Aug. **+15.4% y/y**

Industrial Production

Sep. (e) **+13.2% y/y**
Aug. **+12.3% y/y**

Fixed Asset Investment (ytd)

Sep. (e) **+33.1% y/y**
Aug. **+33.0% y/y**

MEXICO
Retail Sales

Aug. (e) **-3.6% y/y**
July **-4.8% y/y**

FRIDAY OCTOBER 23
EUROZONE
Manufacturing PMI

Oct. A (e) **50.0**
Sep. **49.3**

Services PMI

Oct. A (e) **51.3**
Sep. **50.9**

Industrial New Orders

Aug. (e) **+1.2%** **-22.5% y/y**
July **+2.6%** **-24.3% y/y**

GERMANY
Ifo Survey

Oct. (e) **92.0**
Sep. **91.3**

FRANCE
Consumer Spending

Sep. (e) **+0.6%** **-0.4% y/y**
Aug. **-1.0%** **-1.3% y/y**

Real GDP

Q3 A (e) **+0.2%** **-4.6% y/y**
Q2 **-0.6%** **-5.5% y/y**

MEXICO
Trade Deficit

Sep. P (e) **\$906 mln**
Aug. **\$835 mln**

CANADA

MONDAY OCTOBER 19

8:30 am	Int'l Securities Transactions	
	Inflows	Outflows
Aug.		
July	+\$0.4 bln	-\$0.5 bln
Ottawa's Budget Balance *		
Aug. '09		
Aug. '08	-\$1.7 bln	

TUESDAY OCTOBER 20

8:30 am	Wholesale Trade	
Aug. (e)	-0.5%	
<i>Consensus</i>	<i>+0.5%</i>	
July	+2.8%	
8:30 am	Leading Indicator	
Sep. (e)	+0.9%	
<i>Consensus</i>	<i>+0.7%</i>	
Aug.	+1.1%	

9:00 am BoC Policy Announcement
WEDNESDAY OCTOBER 21
10:30 am DoE's Petroleum Status Report (Oct. 16 week)
2:00 pm Beige Book
THURSDAY OCTOBER 22

8:30 am	Retail Sales	Ex. Autos
Aug. (e)	+0.4%	+0.6%
<i>Consensus</i>	<i>+0.2%</i>	<i>+0.5%</i>
July	-0.6%	-0.8%

10:30 am BoC Monetary Policy Report
FRIDAY OCTOBER 23
10:00 am Existing Home Sales
Sep. (e) **5.50 mln a.r. (+7.8%)**
Consensus *5.40 mln a.r. (+5.9%)*
 Aug. 5.10 mln a.r. (-2.7%)

8:30 am Fed Chairman Bernanke speaks in Boston

UNITED STATES

1:00 pm NAHB Housing Index
Oct. (e) **20**
Consensus *20*
 Sep. 19

11:00 am Fed Chairman Bernanke speaks in California
8:30 am PPI
Sep. (e) **+0.2%** **-4.0% y/y**
Consensus *+0.1%* *-4.3% y/y*
 Aug. +1.7% -4.3% y/y

8:30 am PPI Ex. Food & Energy
Sep. (e) **+0.1%** **+2.0% y/y**
Consensus *+0.1%* *+2.0% y/y*
 Aug. +0.2% +2.3% y/y

8:30 am Housing Starts
Sep. (e) **610,000 a.r. (+2.0%)**
Consensus *610,000 a.r. (+2.0%)*
 Aug. 598,000 a.r. (+1.5%)

8:30 am Building Permits
Sep. (e) **590,000 a.r. (+1.9%)**
Consensus *590,000 a.r. (+1.9%)*
 Aug. 579,000 a.r. (+1.5%)

8:55 am Redbook
Oct. 17
 Oct. 10 +0.4%

5:00 pm ABC News/Washington Post Consumer Comfort Index
Oct. 18
 Oct. 11 -45

1:00 pm 3 & 6-month T-bill auction \$60.0 bln
 (New cash -\$1.0 bln)

1:00 pm 1-year T-bill auction \$27.0 bln
 (New cash \$27.0 bln)

8:30 am Initial Claims
Oct. 17 (e) **515,000 (+1,000)**
 Oct. 10 514,000 (-10,000)

10:00 am FHFA House Price Index
Aug. (e) **-3.1% y/y**
 July -4.1% y/y

10:00 am Leading Indicator
Sep. (e) **+1.0%**
Consensus *+0.8%*
 Aug. +0.6%

10:30 am DoE's Natural Gas Status Report (Oct. 16 week)

 2, 5 & 7-year note auction announcement
 5-year TIPS auction announcement

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