



# Weekly Market Insight

June 11, 2010

## NORTH AMERICAN & INTERNATIONAL ECONOMIC HIGHLIGHTS

There are already early signs that point to the non-linear nature of the current recovery in both Canada and the US.

- Excluding the one-off impact of census related hiring, overall employment growth in the US during May was very weak.
- Retail sales fell by 1.2% in May. Sales tumbled at building supply stores, reversing more than half the surge of the prior two months. As well, auto sales show a notable softening.
- Overall mortgage application volume, which includes loans for purchases and refinancing, dropped by more than 12% during the week ending June 4, compared with the previous week. Refinance volume tumbled 14.3%. This is the lowest level in more than 13 years—a clear sign that the housing market is struggling without government incentives.

These observations are consistent with our call that overall US growth in the second half of the year and early 2011 will be on the soft side. This suggests that the Fed will not touch rates until probably the second quarter of 2011.

Note that the temporary lift from the government has led to a reversal of the deleveraging process by American households in recent months. For example, the saving rate is now at 3.4%—down from 5.4% in the second quarter of 2009. Even more interesting is the difference in savings among income groups. The savings rate of Americans with income of more than \$100,000 fell to the level seen before the recession. At the same time, those who earn less than \$100,000 managed to increase their saving to a 20-year high. As well, credit is starting to rise, but even here we have to take a closer look. Total revolving credit (credit cards) was down by \$8.5 billion while non-revolving loans (car and mobile homes) were up by \$9.5 billion. This suggests that banks are very selective in their lending practices which, in turn, lead to some improvement in the quality of credit.

In Canada there are clear signs that the housing market is softening. Housing starts are slowing, while supply of existing houses is outpacing demand. This raises the issue of the quality of mortgage credit in Canada, and how significant will higher rates will be impacting the market as a whole.

Note that the vast majority of home owners in Canada regardless of their age have not experienced any worsening in affordability despite the rapid increase in prices. The only sub-group of households that have seen some deterioration in their affordability position is older Canadians with average income of less than \$50,000. Zooming in on this group we find that on average they spend close to 60% of their gross income on mortgage payments, property taxes and electricity costs. This is three times the average ratio seen among households at the same age groups but with income of over \$50,000. Note, however, that as opposed to the situation in the US and to a common misconception, the share of this vulnerable group in total mortgage holders in Canada is on the decline—currently accounting for just over 13% of all mortgages in Canada, down from 19% five years ago. Also note that the share of the least vulnerable group (older/higher income) is on a clear upward

trajectory. The practical implication of this finding is that the composition of the mortgage market in Canada has, in fact, improved over the past few years.

Interestingly, there is no significant difference in affordability between households with fixed rate mortgages and those with variable rate mortgages. While variable mortgage holders enjoy lower interest rates, the average mortgage they carry is 7% larger.

While one cannot ignore the risk of an outright decline in home prices in the coming 12-18 months, nothing in the data supports a market crash. As opposed to the US, the share of mortgage holders in Canada has in fact declined in recent years, while the increase in the average size of mortgage has not coincided with a significant worsening in affordability. While higher interest rates will clearly erode affordability, our detailed look at the distribution of mortgage payments as a share of income does not reveal major pockets of vulnerability. Accordingly, the most likely scenario is that higher interest rates will lead to a modest decline in prices (probably in the magnitude of 5%-10%) in the coming year or two. But given relatively modest rate hikes and the current balanced affordability position, the more significant adjustment will be in housing market fundamentals that are likely to catch up with prices in the coming years—paving the way for a healthier housing market by mid decade.

**Benjamin Tal**

## Market Snapshot

US	Current*	yesterday*	a week ago*	a month ago*	a year ago
TED SPREAD (bps)	46	46	41	30	47
10Y / 2Y SPREAD (bps)	252	250	252	268	248
2Y SWAP SPREAD (bps)	38	38	45	36	42
3M T-Bill (%)	0.08	0.08	0.13	0.15	0.15
LIBOR 1 MONTH (%)	0.35	0.35	0.35	0.34	0.32
LIBOR 3 MONTH (%)	0.54	0.54	0.54	0.45	0.62
2-YR BOND (%)	0.75	0.76	0.73	0.77	1.30
5-YR BOND (%)	2.05	2.06	2.02	2.15	2.80
10-YR BOND (%)	3.27	3.26	3.25	3.44	3.77
A Rated / 10Y TREASURY (bps)	182	167	182	160	295
B Rated / 10Y TREASURY (bps)	596	574	562	494	838
BB Rated / 10Y TREASURY (bps)	435	421	423	384	656
<b>CANADA</b>					
PRIME / BA SPREAD (bps)	184	184	185	175	186
CDOR 3 MONTH (%)	0.79	0.79	0.76	0.54	0.65
CDOR 3 MONTH / 3M T-BILL SPREAD (bps)	25	25	26	15	41
10Y / 2Y SPREAD (bps)	159	163	164	159	212
2-YR BOND (%)	1.82	1.79	1.70	1.82	1.39
5-YR BOND (%)	2.74	2.74	2.62	2.75	2.71
10-YR BOND (%)	3.41	3.42	3.34	3.41	3.51
A Rated / 10Y TREASURY (bps)	129	117	128	117	217
BBB Rated / 10Y TREASURY (bps)	198	191	200	184	292
CAN Sovereign Agency / 10Y TREASURY (bps)	47	41	48	46	64
Provincial / 10Y TREASURY (bps)					
ALTA	79	69	75	77	102
BC	90	81	89	89	107
MAN	90	83	88	88	101
NB	94	84	93	93	103
PEI	105	96	104	113	143
NFLD	107	98	106	112	148
ONT	103	93	102	103	114
QUE	110	100	108	109	127
SASK	97	88	95	98	107
NS	101	93	98	100	122
<b>COMMODITIES</b>					
WTI CRUDE FUTURE (US\$ / bbl.)	74.2	75.8	73.4	73.2	71.6
NATURAL GAS (US\$ / MMBtu)	4.8	4.7	4.8	4.3	3.8
SILVER (US\$ / t oz.)	18.1	18.1	17.6	19.6	14.9
GOLD (US\$ / t oz.)	1228.9	1222.6	1205.4	1245.2	939.2
WHEAT (US¢ / bu.)	434.0	429.3	439.3	471.0	584.5
SOYBEANS (US¢ / bu.)	934.8	947.5	945.5	958.0	1265.0
SUGAR (US¢ / lb.)	15.5	15.5	14.6	14.3	15.2
CORN (US¢ / bu.)	344.8	336.0	345.5	366.5	438.3
<b>FX</b>					
C\$ / US\$	1.036	1.030	1.049	1.033	1.121
US\$ / EURO	1.210	1.212	1.205	1.244	1.398
C\$ / EURO	1.253	1.248	1.264	1.285	1.567
YEN / US\$	91.570	91.330	91.960	92.380	98.200
US\$ / BRITISH POUND	1.458	1.465	1.455	1.457	1.640
SWISS FRANCS / US\$	1.150	1.142	1.159	1.127	1.082

\* As of 11:00 a.m.

Note: Data is for reference only.

## International Stock Indexes

Thursday, June 10, 2010

Index (Region/Country)	DAILY					52 WEEK				
	High	Low	Close	Chg	% Chg -   +	YTD % chg	High	Low	% Chg	3-yr % chg
<b>Global</b>										
The Global Dow (World)	1760.16	1712.75	1757.3	39.97	2.33	-11.4	2087.12	1561.11	3.3	-10
The Global Dow (Euro) (World)	1367.06	1340.75	1366.82	25.66	1.91	4.9	1448.65	1054.36	20.1	-6.9
DJ Global Index (World)	210.44	205.04	210.12	4.63	2.25	-7.4	242.2	177.29	9.9	-11.1
DJ Global ex U.S. (World)	179.05	175.03	178.66	2.95	1.68	-11.2	210.96	156.94	5.6	-12.1
MSCI EAFE* (World)	n.a.	n.a.	1354.77	23.1	1.73	-14.3	1642.2	1251.65	0.2	-15.1
<b>Asia Pacific</b>										
DJ Asia-Pacific (Asia-Pacific)	114.64	113.11	114.46	1.29	1.14	-7	132.22	101.22	6.7	-10
All Ordinaries (Australia)	4459	4402.9	4448.4	45.76	1.04	-8.9	5024.1	3738	9.9	-10.8
S & P/ASX 200 (Australia)	4445.9	4385.6	4435.31	49.99	1.14	-8.9	5001.9	3737.5	9.6	-10.7
DJ CBN China 600 (China)	23485.46	23210.48	23264.04	-217.18	-0.92	-19.9	29890.92	22708.28	-2.6	-8.7
Dow Jones China 88 (China)	224.9	221.08	221.3	-3.69	-1.64	-26.6	327.69	217.8	-14.3	-11.8
Shanghai Composite (China)	2581.05	2554.79	2562.58	-21.29	-0.82	-21.8	3471.44	2511.73	-8.4	-13.2
Hang Seng (Hong Kong)	19729.15	19517.61	19632.7	11.46	0.06	-10.2	22943.98	17254.63	4.5	-1.5
Bombay Sensex (India)	16942.6	16668.91	16922.08	264.19	1.59	-3.1	17970.02	13400.32	9.8	6.4
Jakarta Composite (Indonesia)	2792.52	2758.16	2770.79	-15.01	-0.54	9.3	2971.25	1914.39	32.6	10.5
Nikkei 300 (Japan)	173.1	171.37	172.98	1.33	0.77	-6.5	202.75	164.24	-8.7	-21.1
Nikkei Stock Avg (Japan)	9544.04	9437.47	9542.65	103.52	1.1	-9.5	11339.3	9050.33	-4.4	-18.7
Topix Index (Japan)	857.26	848.87	856.79	6.42	0.75	-5.6	998.9	811.01	-8.9	-21.3
Kuala Lumpur Composite (Malaysia)	1293.27	1289.71	1291.31	1.23	0.1	1.5	1346.92	1044.48	18.6	-1.5
NZSX-50 (New Zealand)	3032.97	3000.11	3002.33	2.22	0.07	-7.1	3335.51	2736.89	7.4	-10.5
KSE 100 (Pakistan)	9692.33	9355.94	9379.78	-298.6	-3.09	-0.1	10677.47	6872.96	32.3	-10.9
Manila Composite (Philippines)	3252.81	3219.46	3224.49	-30.34	-0.93	5.6	3357.05	2370.06	24.1	-2.9
Straits Times (Singapore)	2779.58	2750.29	2779.58	33.78	1.23	-4.1	3019.74	2226.1	16.7	-6.6
Kospi (South Korea)	1662.32	1643.71	1651.7	4.48	0.27	-1.8	1752.2	1360.54	16.4	-1.5
Colombo Stock Exchange (Sri Lanka)	4512.39	4464.41	4496.24	31.83	0.71	32.8	4496.24	1797.85	102.5	20.7
Weighted (Taiwan)	7182.99	7085.34	7181.77	110.1	1.56	-12.3	8356.89	6144.53	9.4	-4.7
SET (Thailand)	768.25	763.66	768.16	3.95	0.52	4.6	812.63	562.55	22.5	0.7
<b>Europe</b>										
Stoxx Europe 600 (Europe)	249.03	242.29	248.46	3.86	1.58	-1.9	272.14	197.25	15.7	-13.6
Stoxx Europe 50 (Europe)	2408.45	2345.13	2400.51	27.45	1.16	-6.9	2711.84	2016.25	9.4	-14.6
Euro Stoxx 50 (Euro zone)	2623.05	2523.24	2608.74	52.06	2.04	-12.1	3017.85	2281.47	3.4	-15.8
Euro Stoxx (Euro zone)	251.95	243.13	250.94	5.07	2.06	-8.7	284.91	212.34	7.5	-16.1
ATX (Austria)	2338.71	2252.56	2338.71	68.98	3.04	-6.3	2795.32	1941.49	6.8	-21.1
Bel-20 (Belgium)	2465.1	2402.22	2463.32	37.64	1.55	-1.9	2716.7	1948.42	19.6	-18.2
PX 50 (Czech Republic)	1134.9	1106.5	1132.7	25.4	2.29	1.4	1314.6	875.9	17.4	-14.6
OMX Copenhagen (Denmark)	375.93	366.34	375.93	7.6	2.06	19.1	387.57	261.56	33.3	-6.5
OMX Helsinki (Finland)	6569.63	6384.73	6559.25	109.79	1.7	1.6	7452.62	5351.64	9.9	-16.4
CAC 40 (France)	3538.61	3405.26	3516.64	69.87	2.03	-10.7	4065.65	2983.1	5.4	-15.8
DAX (Germany)	6089.43	5925.06	6056.59	71.84	1.2	1.7	6332.1	4572.65	18.6	-7.3
BUX (Hungary)	21187.55	20564	21103.41	188.34	0.9	-0.6	25322.96	14325.71	29.2	-6.8
FTSE MIB (Italy)	19432.26	18658.6	19391.09	478.18	2.53	-16.6	24425.98	17836.99	-5.8	-22.5
AEX (Netherlands)	326.71	317.98	325.42	4.79	1.49	-3	357.43	243.2	21.4	-15.3
All-Shares (Norway)	406.29	397	406.28	4.52	1.13	-3.3	444.01	309.72	12.2	-9.7
WIG (Poland)	40705.4	39956	40666.63	474.18	1.18	1.7	44078.65	29611.48	27.4	-13.6
PSI 20 (Portugal)	7088.79	6841.69	7088.79	183.68	2.66	-16.2	8882.69	6624.29	-1.3	-17.8
DJ Russia Titans 10 (Russia)	5420.14	5219.7	5407.29	134.85	2.56	-3	6071.02	3573.62	14.1	-5.2
RTS Index (Russia)	1359.12	1319.79	1358.94	24.39	1.83	-4.8	1676.27	835.23	20.6	-8.8
IBEX 35 (Spain)	9242.6	8712.3	9198.2	329.5	3.72	-23	12222.5	8669.8	-5.3	-14.7
SX All Share (Sweden)	318.38	309.65	318.3	6.46	2.07	6.3	337.54	233.82	27.1	-7.8
Swiss Market (Switzerland)	6397.05	6290.72	6376.66	57.48	0.91	-2.6	6967.56	5237.81	16.3	-11.3
Istanbul National 100 (Turkey)	55066.53	53772.76	54861.83	556.91	1.03	3.9	59330.34	34537.04	58	7.4
FTSE 100 (U.K.)	5149.7	5030.9	5132.5	46.64	0.92	-5.2	5825	4127.2	15	-7.6
FTSE 250 (U.K.)	9609.68	9402.33	9609.68	122.5	1.29	3.3	10690.08	7174.84	23.9	-6
<b>Americas</b>										
DJ Americas (Americas)	290.34	281.52	289.98	8.27	2.94	-2.2	324.75	228.67	16.6	-8.7
Merval (Argentina)	2262.87	2218.9	2261.78	44.24	2	-2.5	2487.76	1477.84	35.5	1.4
Sao Paulo Bovespa (Brazil)	63146.32	61484.49	63048.8	1570.19	2.55	-8.1	71784.77	48872.58	18	6.4
S & P/TSX Comp (Canada)	11637.83	11450.64	11635.85	185.21	1.62	-0.9	12280.97	9653.45	8.6	-5.5
Santiago IPSA (Chile)	3945.68	3903.4	3944.33	40.93	1.05	10.1	3944.33	3020.17	21.1	6.3
IPC All-Share (Mexico)	31916.55	31231.96	31910.22	700.89	2.25	-0.7	34134.23	23314.68	25.8	0.5
Caracas General (Venezuela)	64703.55	64617.92	64625.51	-78.04	-0.12	17.3	64703.55	43166.44	49.7	18.4
<b>Other Countries</b>										
CASE 30 (Egypt)	6295.04	6230.99	6243.09	-105.07	-1.66	0.6	7603.04	5229.4	0.8	-6.8
Tel Aviv (Israel)	1092.7	1080.3	1090.8	0.87	0.08	-4.7	1237.85	832.74	23.9	-0.5
Johannesburg All Share (South Africa)	27133.87	26560.82	27133.87	483.01	1.81	-1.9	29565.1	21665.9	17.7	-1.2

\*Europe, Australia, Far East: U.S.-dollar terms.

Three year percent change is annualized.

Sources: Reuters; WSJ.com

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