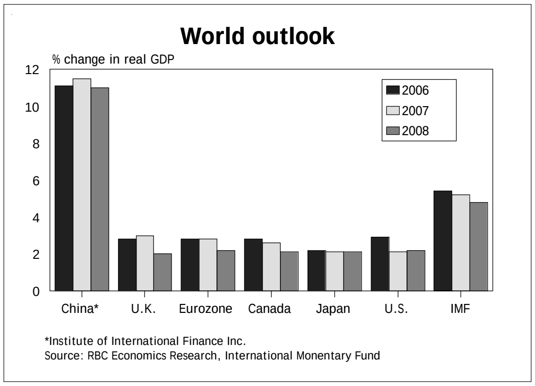


ECONOMIC & FINANCIAL MARKET OUTLOOK

January 2008

Financial market turmoil testing the global economy

▲ Financial market volatility is boosting the downside risks to the economic outlook.

▲ Central banks are acting to mitigate downside risks. Many of them have started to cut interest rates, with more easing expected in early 2008.

▲ We have revised our global growth forecast lower along with our Canadian and U.S. economic forecasts.

▲ The U.S. housing market is still contracting, but the pace of decline is expected to ease through 2008.

▲ U.S. economic growth is expected to slow in late 2007 and the first half of 2008 as tighter credit conditions dampen spending.

▲ The weak U.S. dollar is propping up exports. As a result, the trade sector is supporting the economy for the first time in 14 years.

▲ We expect the Fed to address economic risks by cutting rates a further 100 basis points early in 2008.

▲ Looser monetary policy should help prevent the economy from falling into recession. Stronger economic growth is expected in the second half of 2008.

▲ Canada's economy is forecast to slow as the drag from the trade sector becomes larger and domestic demand begins to soften.

▲ The elevated Canadian dollar and weak U.S. growth will dampen export growth.

▲ Canada's domestic economy will soften but will get a boost from the strong terms of trade.

▲ Upward inflation pressures are moderating, leaving room for the Bank of Canada to cut the policy rate.

▲ Our new forecast calls for lower market interest rates.

Ongoing turbulence in financial markets as investors reassess the creditworthiness of their own, and their counterparties' portfolios has dampened the outlook for the global economy in 2008. The strong performance in many countries in the first three quarters of 2007 will likely result in the global economy expanding by just above 5%, but we are now calling for a more moderate pace of GDP growth in 2008.

Craig Wright
Chief Economist (416) 974-7457
craig.wright@rbc.com

Paul Ferley
Assistant Chief Economist (416) 974-7231
paul.ferley@rbc.com

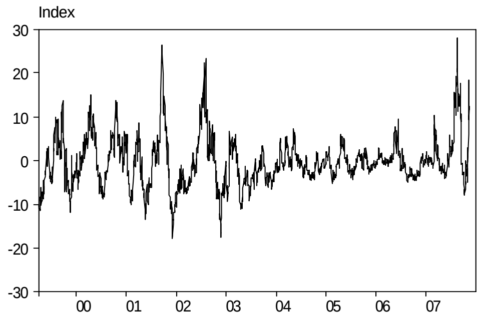
Dawn Desjardins
Senior Economist (416) 974-6919
dawn.desjardins@rbc.com

Rishi Sondhi
Economist (416) 974-8593
rishi.sondhi@rbc.com

No slowing in the global economy in the third quarter

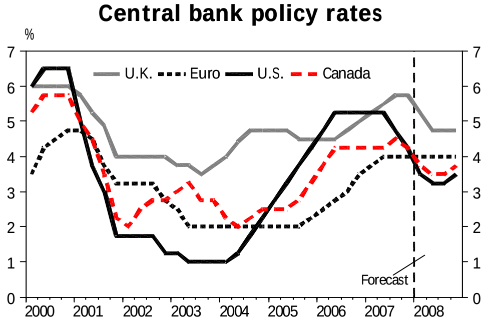
The world economy did not show signs of flagging in the third quarter even as financial markets became increasingly nervous about the impact of the U.S. housing recession and the unravelling of the sub-prime mortgage market. Third-quarter growth numbers surprised to the upside in many countries, with China growing at an 11.5% pace, the United Kingdom by 3.2%, Canada by 2.9% and the United States at an astounding 4.9% rate despite a huge decline in residential construction activity. Data for the fourth quarter are significantly less robust, although central banks are working aggressively to offset the negative impact of tighter credit conditions on their economies.

Risk aversion thermometer



Source: RBC Economics Research

Central bank policy rates



Source: Federal Reserve Board, Bank of Canada, Bank of England, European Central Bank, RBC Economics Research

Global markets still flush with cash, but markets remain nervous

The hesitancy to extend credit is occurring despite a high level of liquidity in the global financial system. In fact, central banks have been flooding funds into the system to keep financial markets functioning, which has kept global liquidity growing. However, uncertainty about what's lurking on balance sheets has investors largely sitting on this liquidity. This has pumped up market volatility, weighed on stock markets and produced a widening in credit spreads. The TED spread, which measures the difference between the three-month Eurodollar rate and the three-month Treasury bill rate, remains elevated and longer-dated credit spreads are wider, signalling investors' preference for safer government-backed paper.

Most important for the global economic outlook is whether or not the widening in credit spreads and commensurate tightening in lending conditions will persist and materially affect the pace of consumer and business spending in the quarters ahead. We expect global growth to ease in 2008 to 4.8% on the back of tighter credit conditions. The aggressive action by central banks to inject liquidity into financing markets to ensure that they continue to function combined with steady-to-lower official interest rates are expected to limit the impact of credit market tightening on the global economy.

Central banks ease monetary policy stance...

The financial market maelstrom in 2007 saw many major central banks shift their policy stance, with those who had been in tightening mode, like the Bank of Canada, the European Central Bank and the Bank of England, initially stepping onto the sidelines. The U.S. Federal Reserve was the only central bank that overtly moved to an easing stance soon after the credit problem hit. In December, the Bank of England and the Bank of Canada joined the U.S. Fed in cutting policy rates. Short-term interest rates, which were on a firm upward track until mid-August, drifted lower as the financial market volatility boosted downside risks to the economic outlook.

With rate cuts to continue into early 2008

We expect the Bank of England, the Fed and the Bank of Canada to ease interest rates again in early 2008 in an effort to offset the downside risks to their economies. The Federal Reserve is expected to ease the policy rate a further 100 basis points by mid-year following 100 basis points of cuts in 2007. Persistent financial market volatility means that investors and lenders will remain cautious and risk averse, leading to limited credit availability and slower borrowing activity. The Bank of England and the Bank of Canada are forecast to lower their policy rates a further 75 basis points through 2008.

U.S. economy powered along in the third quarter...

The U.S. economy powered along in the third quarter and GDP growth was much stronger than expected despite another 20% annualized decline in residential construction activity. Consumer spending growth came in at a 2.8% annualized rate, accounting for 2.0 percentage points of the total 4.9% advance in overall GDP activity. Business investment spending also increased at a strong clip and inventories were built up. A big boost to growth came from the trade sector where the combination of the currency's sharp decline and strong global demand resulted in exports growing at an 19.1% annual rate, the fastest since 2003. As a result, the trade sector added 1.4 percentage points to the quarterly growth rate, more than offsetting the drag from the housing market contraction.

...but is moving into a period of slower growth

We expect a sharp slowing in the pace of growth in the final quarter of 2007 and into 2008 as the tightening in credit conditions curbs consumer and business spending. The Fed's senior loans officer survey showed that banks tightened lending standards for both residential and commercial real estate loans as well as inching conditions tighter for some types of consumer loans. The softer spending rates combined with a continued contraction in the housing market will significantly slow the pace of GDP growth to about 1.5% during this period despite ongoing support from the net trade sector.

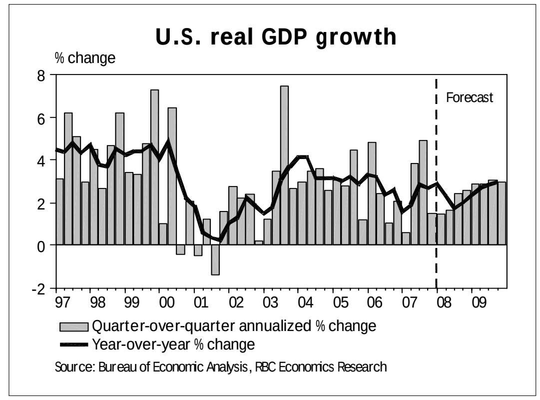
Stronger growth rates are expected in the second half of next year, however, as the Fed's rate cuts reduce the financial market turmoil and the decline in housing activity eases. As well, we are assuming that recently proposed Administration actions will help temper an expected jump in defaults this spring on sub-prime mortgages. Our forecast is for the economy to grow at an average 2.5% quarterly pace in the second half of 2008, much faster than the 1.5% average pace expected in the first six months of the year.

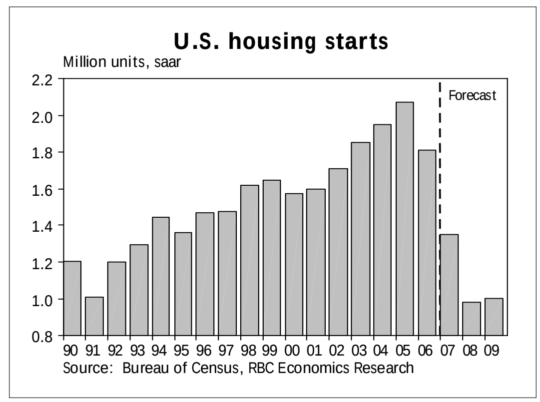
U.S. housing market correction continues

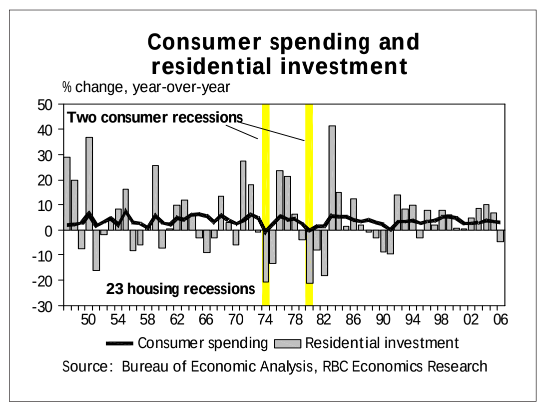
The U.S. housing market remains the Achilles' heel for the economy and financial markets. As yet, there have been limited signs that the correction is abating. The stock of unsold homes stands near record-high levels as home sales remain weak. In response, housing starts fell late 2007 to the lowest level since 1993 and were down 48% from their recent high. We are projecting another double-digit decline in residential investment in the fourth quarter. Declines will continue in 2008, although the magnitude will ease through the year.

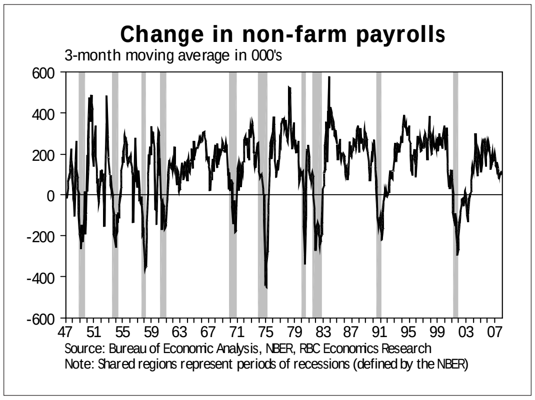
U.S. consumer expected to continue to spend

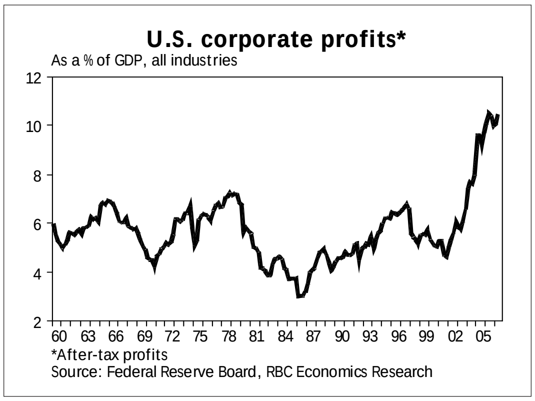
The ongoing recession in the U.S. housing market doesn't necessarily portend a contraction in consumer spending. During the past 60 years, there have been 23 annual housing market contractions, but only two times when consumer spending posted a negative annual growth rate. Housing price movements show a similar pattern. The U.S. consumer may be more at risk this cycle because of the relatively greater importance of the sub-prime mortgage market where foreclosures and delinquencies have been rising. However, the flow-through from the housing market correction into other parts of the economy has been limited so far, with real GDP excluding residential construction activity growing at a firm 4.1% rate during the first three quarters of 2007.

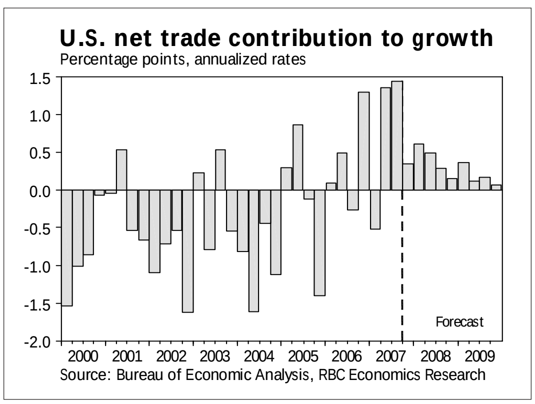


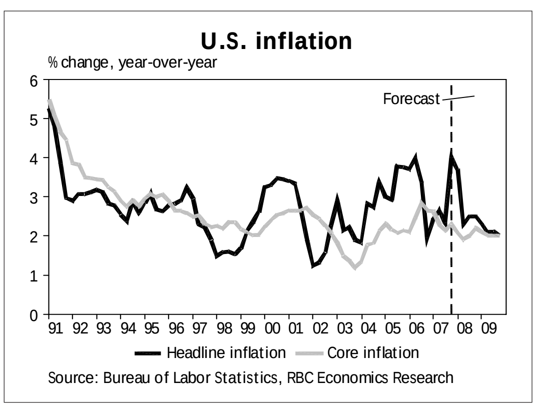












Income growth and job gains to offset pressure on consumer spending

The housing market correction is not the only threat to the outlook for consumer spending. The elevated level of energy prices and recent erosion in stock market net worth are also of concern. We summed up the total hit to the consumer from the deterioration in the housing market, weakening stock markets and rising energy prices and determined that, even with a fairly modest 4% increase in income, consumer spending likely would remain in positive territory (see RBC's Derek Holt, *Evaluating the Shocks Hitting the U.S. Consumer*, November 2007).

Labour market conditions deteriorated in 2007, with the unemployment rate rising to 5% currently from the recent low of 4.4% in March. The pace of job gains slowed to average 97,000 in the fourth quarter, slower than the 115,000 average in the first six months of the year and the 200,000 monthly average increase in 2005-06. Still, wage growth is not showing any serious signs of flagging and averaged 3.7% in the fourth quarter, just shy of the average pace of the previous 18-month period when consumer spending was running at a 3.1% pace. Our forecast calls for slower consumer expenditure in early 2008 on the back of tighter credit conditions and financial market uncertainty.

Business to pull back on spending but not retreat

Business investment was solid in 2007 mainly on the back of strong spending on non-residential structures, which we estimate increased by 13%. Purchases of equipment and software increased at a more tepid pace following three years of solid gains. We expect that businesses will continue to spend in 2008, although we are forecasting a significant slowing in structures investment and a modest rebound in spending on equipment and software.

Profit growth has been slowing, although the level of profits relative to the size of the economy remains near an all-time high. The downside risks to the profit outlook are increasing with the financial sector under pressure in the wake of the recent credit tightening. Still, corporate America has lots of cash to spend, which means that investment spending is likely to contribute to GDP growth next year even with higher corporate borrowing rates.

Weak U.S. dollar supporting export growth

The U.S. dollar continued its six-year downtrend last year, touching an all-time low on a trade-weighted basis and losing 18% against the Canadian dollar and 11% against the euro, the two largest-weighted currencies in the index. The weakening in the U.S. dollar boosted demand for U.S. exports and the net trade component of GDP added more than one percentage point to both the second- and third-quarter growth rates. Our forecast assumes that this will continue through the end of 2008, resulting in the trade sector acting as a meaningful addition to growth in 2007-08 for the first time since 1995.

Inflation worries lingering

The slowing in economic growth is likely to exert some modest downward pressure on inflation but is unlikely to completely offset the impact of higher energy prices and the weaker U.S. dollar on import prices. Import prices skyrocketed in November on the back of rising crude oil prices, but, even excluding petroleum, upward pressure is still evident. Rising imported goods prices will have only a limited impact on overall prices given that imports account for just 17% of the U.S. economy. However, when combined with higher energy prices, they are keeping the upside risks to inflation intact. The U.S. CPI rate jumped to 4.3% in November and is expected to remain elevated in the near-term in the face of rising energy prices. The core CPI rate, at 2.3%, is consistent with the core PCE deflator, the Fed's preferred inflation measure, holding to the upper-end of their estimated "comfort-zone" of 1%–2%. The high rate of increase in headline inflation will continue to fuel the Fed's worries that inflation expectations may become "unmoored."

Fed will put greater weight on mitigating downside risks to the economy

While the Fed may have niggling worries about inflation, the turbulence in financial markets will remain at the forefront in the months ahead. The continued erosion in credit markets and rising risk aversion on the part of investors are likely to prompt further rate cuts. Our view is that the Fed will lower the Fed funds rate by a further 100 basis points early in 2008, which, alongside a government-led program to limit future mortgage defaults, should be enough to stave off a recession and support stronger growth in the second half of 2008.

Bond yields to remain low as Fed shepherds the economy through financial market turmoil

We expect bond market yields to remain low early into 2008 as the Fed completes its round of interest rate reductions and works to stabilize financial markets. In the near-term, the combination of high volatility and risk aversion will see investors rush to the safety of government bonds, which will depress yields. We are forecasting that the 10-year Treasury bond yield will be 3.75% at the end of first quarter of 2008 with the two-year yield at 2.50%. Our forecast that the economy will reaccelerate in the second half of 2008 as the drag from the housing market wanes and financial markets stabilize sets the stage for interest rates to rise across the yield curve. We are forecasting that the Fed funds rate will close 2008 at 3.50%, two-year yields at 3.75% and 10-year yields at 4.50%.

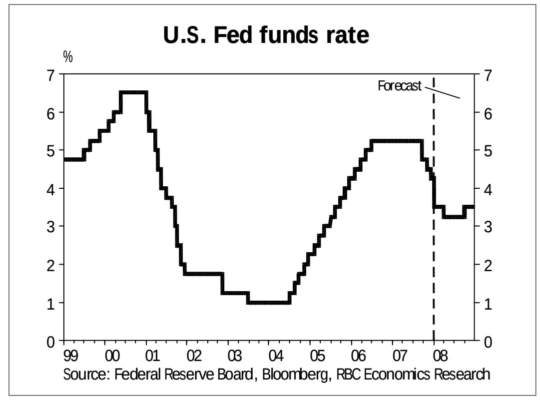
Canada's domestic economy powering along, but trade drag growing

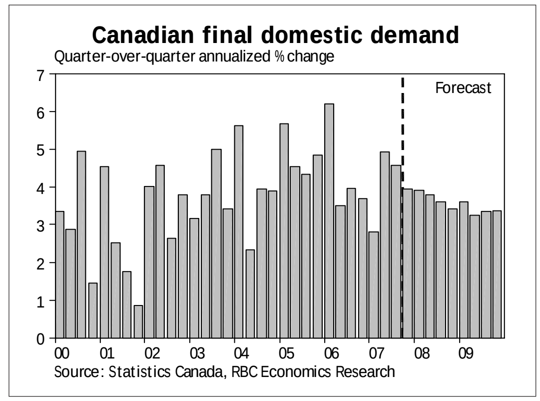
Canada's domestic economy has been growing at a solid clip and we expect that it will remain on relatively firm footing during this period of financial market turbulence. We are forecasting that domestic demand growth will continue to run at a 3.8% clip in 2008. One important factor supporting the domestic economy has been the improvement in Canada's terms of trade, with Canadian export prices rising more rapidly than import prices. This means that, for each dollar of export income earned, Canadian households and businesses have more money to spend on imported goods and services. Export prices have outpaced import prices by 20% during the past five years, boosting Canada's national income and improving overall net worth.

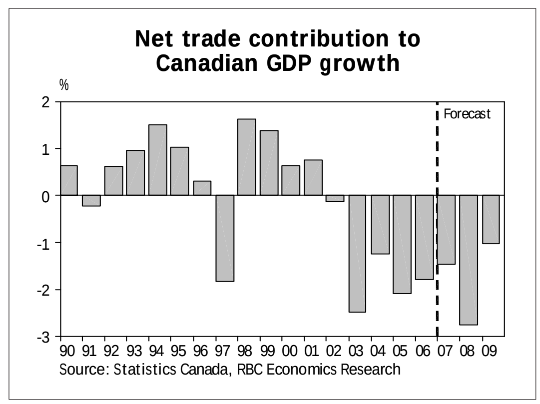
The terms-of-trade boost will support consumer spending on goods and services and housing and business investment flows, which we expect will more than offset the drag on the pace of GDP growth from the trade sector in 2008.

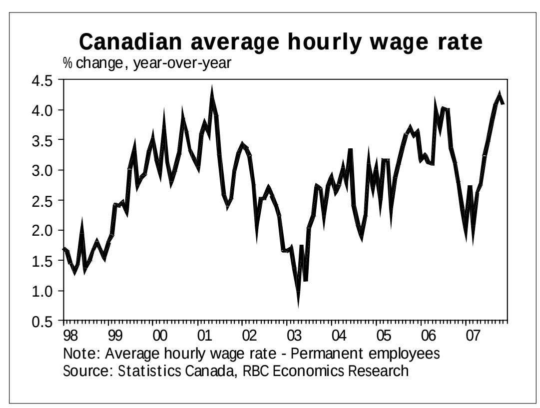
Trade sector to restrain GDP growth for seventh year running

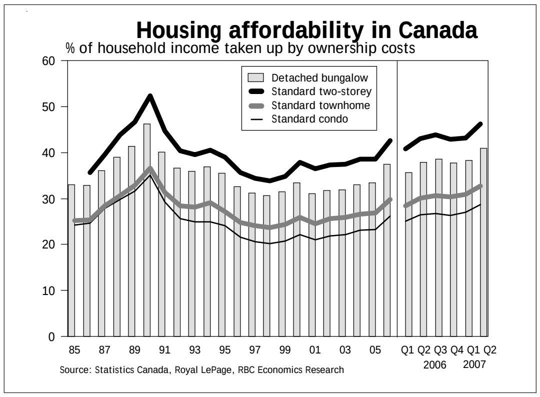
The stronger performance of export prices relative to import prices has led to the volume of exports growing more slowly than the volume of imports and has resulted in the overall trade sector working as a drag on GDP growth. In 2007, we

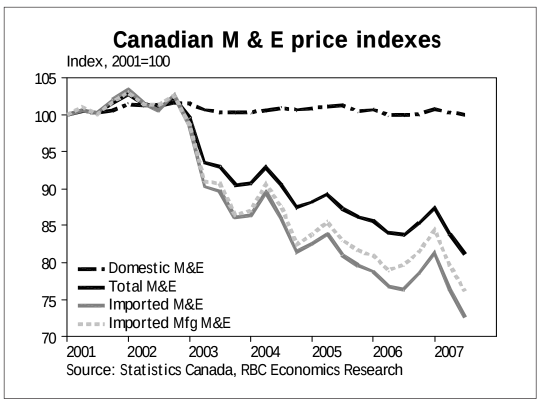












estimate that the trade sector subtracted about 1.5 percentage points from the economy's growth rate and, given the elevated Canadian dollar, will trim about another 2.7 percentage points from growth in 2008. This reflects the impact of both a strong Canadian dollar and the near-term weakening in U.S. growth.

Consumers to keep spending even with modestly tighter credit conditions

After growing at an average rate of 3.6% during the past six years, we expect consumer spending to moderate in 2008 but still record a solid 3.2% increase, backed by the strong labour market and rising wages. The moderation will also be tempered by the one percentage-point cut in the GST rate on January 1, 2008. The unemployment rate hit a fresh 33-year low in September and remained there through November. The economy generated 388,000 new jobs in the first 11 months of 2007 and more than two million jobs in the past six years, 82% of which were full-time and 86% in the services industries. Wage growth has also picked up pace, with average hourly earnings for permanent employees up 4.1% from a year earlier in the three months ending November 2007.

Canadian household balance sheets are also in good condition with the ratio of debt-to-assets improving because, even as households take on more debt, the value of their assets is rising even faster. The TSX gained 7.2% in 2007 despite the 2.6% drop in the fourth quarter, while house prices are rising at a double-digit rate that is likely to keep the debt-to-asset ratio within its recent range.

Canada-U.S. housing market performance diverge sharply

Canada's housing market is expanding at a strong clip in sharp contrast to the weakening trend in the United States. Housing starts surged last September to their highest level since 1978 and, even though the pace moderated in the fourth quarter, starts totalled 229,600 in 2007, the sixth year that starts exceeded 200,000 units. We expect another 210,000 units in 2008 — the reverse of the U.S. situation where starts for 2007 are projected to be close to their lowest level since 1993 and the outlook is that they will slow further in 2008.

The divergence in housing market performance is being mirrored in home prices with Canadian numbers rising at double-digit pace, while growth in U.S. home prices has been in negative territory for several months. The strong performance of Canada's housing market is beginning to stress affordability. RBC's housing affordability index is showing that conditions have eroded back to levels reported in 1990, which is likely to weigh on housing market demand going forward. The slowing is likely to be moderate, however, as longer amortization periods for mortgages – financial institutions now offer amortization periods as long as 40 years, up from the standard 25 years – will limit the increase in monthly payments and allow consumers to continue to be involved in the higher-priced housing markets.

Conditions for business will encourage investment in 2008

We expect that corporate Canada will continue to spend on capital goods and non-residential structures in 2008. Balance sheets have a high level of liquid assets and corporate profits are near their all-time high relative to the size of the economy, benefitting from the improvement in Canada's terms of trade. In addition, the strong Canadian dollar is giving firms the ability to import capital goods with the prices for imported machinery and equipment having fallen by almost

20% during the past five years. Canada imports about 75% of its capital goods, largely from the United States.

Strong domestic growth + growing trade drag = GDP growth near potential

The combination of slower domestic growth and greater restraint from trade will result in Canada's economy growing at a slower 2.1% in 2008 from an expected 2.6% in 2007 and 2.8% in 2006. The run of strong growth between 2004 and the first half of 2007 put the economy firmly into a state of excess demand, leading to upward pressure on prices that caused the core inflation rate to hold at or above the Bank of Canada's 2% target for 13 months.

As the economy slows in 2008, we expect some of the froth to come off prices and Canada's inflation rates to move back below the 2% target on a sustained basis.

The core inflation rate fell in October and November, moving below the 2% target for the first time since June 2006. The decline in the core inflation rate is occurring more rapidly than the Bank of Canada had expected as retailers aggressively trim prices to levels that are closer to their U.S. counterparts on the back of the surge in the loonie. While we expect that Canada's all-items inflation rate will remain above the 2% target in the near-term as the energy price-related declines in the index late last year fall out of the year-over-year calculation, the rapid price discounting by Canadian retailers will keep the core rate below the 2% target.

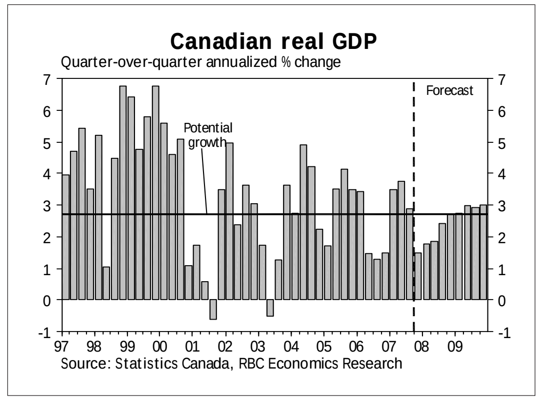
Burgeoning trade drag and lower core inflation will see Bank cut policy rate again

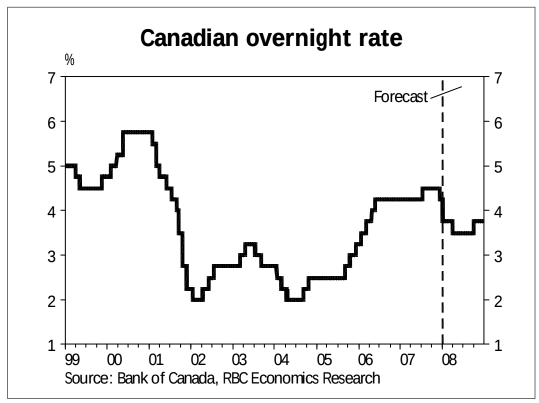
The Bank of Canada focuses on movements in the core rate as a guide to underlying price pressures and the sharp slowing in the three-month running rate is allaying some of their concerns about inflation. The lower core inflation rate combined with growing risks to the U.S. economic outlook and tightening in credit conditions were the catalysts for the Bank of Canada to lower the overnight rate in early December.

We expect the Bank to cut the overnight rate again in early 2008 as policymakers work to mitigate the negative impact of credit tightening and weakening U.S. demand on Canada's economy. Our assessment that the U.S. economy will rebound in the second half of 2008 will remove one of these downside risks, while more stable financial markets will dampen another, which will likely see the Bank start to reverse the rate cuts in the final quarter of 2008.

Interest rates to stay low in early 2008 but start to drift higher in second half of the year

We expect that interest rates will remain low in early 2008 with the overnight rate falling to 3.50% by the end of the second quarter, the two-year yield to 3.05% and 10-year rate to 3.75%. Similar to our U.S. forecast, we are projecting that the Bank of Canada will raise the overnight rate in the final quarter of 2008 by 25 basis points to 3.75 % and that market interest rates will finish 2008 at 3.80% in the two-year maturity and 4.35% in the 10-year maturity.





Economic forecast detail — Canada

Real growth in the economy

Period-over-period annualized % change unless otherwise indicated

	Actual							Forecast									Act.	Forecast		
	2006				2007				2008				2009				Annual average			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2006	2007	2008	2009
Consumer spending	5.5	3.8	5.1	3.7	3.4	5.9	3.0	2.9	3.1	3.1	3.0	2.6	3.5	3.4	3.8	3.4	4.2	4.1	3.2	3.3
Durables	12.8	7.9	11.1	4.7	6.6	14.9	-0.8	1.5	2.0	1.9	2.4	2.0	3.0	3.5	3.7	3.3	7.1	7.1	2.3	2.9
Non-durables	1.0	3.7	2.8	-0.7	2.6	5.1	-0.6	2.5	3.4	3.2	2.8	2.2	3.5	3.0	3.9	2.9	1.5	2.1	2.6	3.1
Services	4.7	2.4	4.4	5.8	2.0	4.6	4.7	3.3	3.3	3.3	3.4	3.0	3.9	3.8	4.0	3.7	4.3	3.9	3.5	3.6
Government spending	4.9	3.2	1.5	3.0	2.3	3.2	5.8	2.8	2.5	2.5	2.5	2.7	2.6	2.8	2.8	2.8	3.3	3.0	3.0	2.7
Business investment	9.0	2.8	3.8	4.3	2.3	4.4	7.6	6.8	7.0	6.3	6.1	6.1	3.5	3.1	2.6	3.9	7.1	4.2	6.6	4.3
Residential construction	9.5	-5.2	-6.2	-0.1	8.2	5.8	5.2	-1.5	2.0	1.8	2.0	1.7	0.1	0.2	0.1	0.5	2.1	2.4	1.9	0.8
Non-residential structures	14.3	10.5	12.6	11.8	1.6	1.4	2.9	3.0	8.0	5.8	5.6	5.3	2.9	2.9	4.4	5.5	12.9	5.5	5.1	4.2
Machinery & equipment	4.3	5.0	7.1	2.3	-3.2	5.8	15.4	11.0	9.8	9.5	9.0	9.4	6.0	5.0	3.0	5.0	7.4	4.4	10.3	6.6
Final domestic demand	6.2	3.5	4.0	3.7	2.8	4.9	4.6	4.0	3.6	3.6	3.5	3.3	3.6	3.2	3.4	3.4	4.7	3.9	3.8	3.4
Exports	-6.9	-1.8	2.6	2.7	0.8	3.1	2.3	1.0	0.6	0.8	2.0	1.3	4.0	3.5	3.8	4.0	0.7	1.8	1.3	2.9
Imports	-2.6	9.8	6.2	-0.9	0.1	7.7	18.6	4.2	6.6	6.3	6.4	5.5	4.0	4.0	4.0	4.2	5.0	5.1	7.5	4.7
Inventories (change in $b)	10.2	17.7	13.0	0.1	2.5	4.5	15.4	12.5	14.5	16.8	19.5	23.5	22.3	22.5	21.8	21.3	10.2	8.7	18.6	21.9
Real gross domestic product	**3.4**	**1.5**	**1.3**	**1.5**	**3.5**	**3.8**	**2.9**	**1.5**	**1.8**	**1.9**	**2.4**	**2.7**	**2.8**	**3.0**	**2.9**	**3.0**	**2.8**	**2.6**	**2.1**	**2.7**

Other indicators

	2006 Q1	2006 Q2	2006 Q3	2006 Q4	2007 Q1	2007 Q2	2007 Q3	2007 Q4	2008 Q1	2008 Q2	2008 Q3	2008 Q4	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2006	2007	2008	2009
Business and labour																				
Productivity (y/y %)*	1.8	0.9	0.5	0.0	-0.5	0.5	0.6	0.4	0.8	0.5	0.6	1.4	1.4	1.3	1.4	1.4	0.8	0.2	0.8	1.4
Pre-tax corporate profits (y/y %)	9.0	7.5	4.8	-0.6	5.8	5.6	5.9	6.2	2.5	3.5	3.3	2.0	4.5	3.6	4.2	3.8	5.0	5.9	2.8	4.0
Unemployment rate (%)	6.4	6.2	6.4	6.1	6.1	6.1	6.0	5.9	6.0	6.1	6.2	6.2	6.2	6.2	6.1	6.1	6.3	6.0	6.1	6.2
Inflation																				
Headline CPI (y/y %)	2.4	2.6	1.7	1.4	1.8	2.2	2.1	2.4	1.7	1.1	1.3	1.4	1.7	1.8	1.9	2.1	2.0	2.1	1.4	1.9
Core CPI (y/y %)	1.7	1.8	2.1	2.2	2.3	2.4	2.2	1.6	1.6	1.8	1.9	2.1	2.1	2.0	2.0	2.0	1.9	2.1	1.9	2.0
Personal savings rate	3.3	1.7	1.8	2.2	2.8	1.6	1.3	1.8	1.5	1.2	1.5	2.2	1.3	0.7	0.7	0.9	2.3	1.9	1.6	0.9
External trade																				
Current account balance ($b)	35.9	17.3	22.7	18.5	25.6	25.4	4.2	10.0	5.2	1.7	1.2	1.0	3.5	3.4	3.7	4.1	23.6	16.3	2.3	3.7
% of GDP	2.5	1.2	1.6	1.3	1.7	1.7	0.3	0.6	0.3	0.1	0.1	0.1	0.2	0.2	0.2	0.2	1.6	1.1	0.1	0.2
Housing starts (millions)	0.24	0.23	0.22	0.22	0.22	0.23	0.25	0.22	0.22	0.21	0.21	0.21	0.19	0.19	0.18	0.18	0.23	0.23	0.21	0.18
Motor vehicle sales (millions)	1.66	1.63	1.68	1.69	1.67	1.74	1.69	1.64	1.66	1.66	1.66	1.66	1.67	1.68	1.68	1.68	1.67	1.69	1.66	1.68

* Productivity is calculated as total real GDP divided by employment.

Source: Statistics Canada, RBC Economics Research forecasts

Economic forecast detail — United States

Real growth in the economy

Period-over-period annualized % change unless otherwise indicated

	Actual							Forecast									Act.	Forecast		
	2006				2007				2008				2009				Annual average			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2006	2007	2008	2009
Consumer spending	4.4	2.4	2.8	3.9	3.7	1.4	2.8	2.8	1.5	2.0	2.6	2.7	2.8	2.9	2.9	2.7	3.1	2.9	2.2	2.7
Durables	16.6	0.8	5.6	3.9	8.8	1.7	4.5	5.5	0.2	1.0	1.4	2.0	2.6	2.8	3.0	2.5	3.8	4.9	2.2	2.3
Non-durables	4.5	2.3	3.2	4.3	3.0	-0.5	2.2	3.0	2.0	2.2	2.9	2.8	2.5	2.4	2.7	2.7	3.6	2.5	2.3	2.6
Services	2.1	2.7	2.0	3.7	3.1	2.3	2.8	1.9	1.7	2.2	2.7	2.9	3.0	3.2	3.0	2.8	2.7	2.8	2.2	2.9
Government spending	4.9	1.0	0.8	3.5	-0.5	4.1	3.8	1.2	1.2	0.9	0.8	1.1	1.0	0.7	0.8	1.5	1.8	2.0	1.6	0.9
Business investment	7.9	-1.9	-4.7	-7.1	-4.4	3.2	-0.7	-2.3	-3.9	-2.4	0.9	2.1	2.3	3.8	4.5	4.3	2.4	-2.8	-1.5	2.5
Residential construction	-0.7	-11.7	-20.4	-17.2	-16.3	-11.8	-20.5	-20.0	-17.0	-12.0	-6.5	-3.5	0.5	2.0	3.0	1.5	-4.6	-16.7	-14.9	-1.4
Non-residential structures	15.0	16.4	10.8	7.4	6.4	26.2	16.4	10.0	1.0	1.0	4.3	4.6	3.5	3.5	3.0	3.5	8.4	12.8	6.5	3.6
Machinery & equipment	13.0	-0.1	2.9	-4.9	0.3	4.7	6.2	1.0	0.5	0.5	2.8	3.4	2.6	4.5	5.4	5.5	5.9	1.2	2.0	3.5
Final domestic demand	5.0	1.5	1.2	2.1	1.7	2.1	2.5	1.7	0.7	1.2	2.0	2.4	2.4	2.7	2.8	2.8	2.7	1.9	1.6	2.4
Exports	11.5	5.7	5.7	14.3	1.1	7.5	19.1	4.0	8.0	9.0	8.5	7.0	5.5	3.5	4.7	4.8	8.4	7.9	8.7	5.8
Imports	6.9	0.9	5.4	1.6	3.9	-2.7	4.4	2.8	1.9	3.4	4.6	4.3	2.8	2.0	2.6	3.0	5.9	2.2	2.8	3.2
Inventories (change in $b)	38.4	51.4	53.9	17.4	0.1	5.8	30.6	21.0	24.0	20.0	20.0	18.0	22.0	22.0	21.0	21.0	40.3	14.4	20.5	21.5
Real gross domestic product	**4.8**	**2.4**	**1.1**	**2.1**	**0.6**	**3.8**	**4.9**	**1.5**	**1.4**	**1.6**	**2.4**	**2.6**	**2.9**	**2.9**	**3.0**	**3.0**	**2.9**	**2.2**	**2.1**	**2.7**

Other indicators

Business and labour																				
Productivity (y/y %)*	1.2	1.3	0.6	0.9	0.0	0.4	1.6	1.5	1.8	1.4	0.9	1.2	1.5	1.7	1.6	1.6	1.0	0.9	1.3	1.6
Pre-tax corporate profits (y/y %)	11.7	16.7	21.1	8.2	4.3	4.8	1.5	2.0	2.0	1.5	2.0	2.5	3.5	5.0	5.7	4.9	14.3	3.2	2.0	4.8
Unemployment rate (%)	4.7	4.6	4.7	4.5	4.5	4.5	4.6	4.8	4.9	5.0	5.1	5.2	5.1	5.1	5.0	5.0	4.6	4.6	5.1	5.1
Inflation																				
Headline CPI (y/y %)	3.6	4.0	3.3	1.9	2.4	2.7	2.4	4.0	3.7	2.3	2.5	2.5	2.3	2.1	2.1	2.0	3.2	2.9	2.7	2.1
Core CPI (y/y %)	2.1	2.5	2.8	2.6	2.6	2.3	2.2	2.3	2.1	1.9	2.0	2.2	2.1	2.0	2.0	2.0	2.5	2.3	2.1	2.0
Personal savings rate	0.9	0.3	0.0	0.4	1.0	0.3	0.6	1.0	1.6	1.8	2.0	2.1	1.9	1.8	1.8	1.7	0.4	0.7	1.9	1.8
External trade																				
Current account balance ($b)	-802	-822	-869	-752	-788	-756	-714	-751	-740	-735	-741	-745	-740	-735	-740	-736	-811	-752	-740	-738
% of GDP	-6.2	-6.3	-6.6	-5.6	-5.8	-5.5	-5.1	-5.3	-5.2	-5.1	-5.1	-5.1	-5.0	-4.9	-4.8	-4.8	-6.2	-5.4	-5.1	-4.9
Housing starts (millions)	2.13	1.86	1.70	1.55	1.46	1.46	1.30	1.18	1.05	1.00	0.95	0.94	0.95	0.96	1.00	1.10	1.81	1.35	0.98	1.00
Motor vehicle sales (millions)	16.8	16.4	16.5	16.3	16.4	16.0	15.9	16.1	15.8	15.7	15.8	15.9	15.9	16.0	16.1	16.1	16.5	16.1	15.8	16.0

* Productivity is calculated as total real GDP divided by employment.

Source: Bureau of Economic Analysis, RBC Economics Research forecasts

Financial market forecast detail

Interest rates

%, end of period

	Actual							Forecast					Actual	Forecast	
	Q106	Q206	Q306	Q406	Q107	Q207	Q307	Q407	Q108	Q208	Q308	Q408	2006	2007	2008
Canada															
Overnight rate	3.75	4.25	4.25	4.25	4.25	4.25	4.50	4.25	3.75	3.50	3.50	3.75	4.25	4.25	3.75
3-month T-bills	3.86	4.30	4.15	4.15	4.17	4.43	3.97	3.84	3.35	3.10	3.25	3.50	4.15	3.84	3.50
2-Year GoC bonds	3.99	4.40	3.89	4.03	3.98	4.61	4.12	3.74	3.10	3.05	3.40	3.80	4.03	3.74	3.80
5-Year GoC bonds	4.16	4.49	3.88	4.00	4.02	4.58	4.24	3.87	3.50	3.35	3.70	4.00	4.00	3.87	4.00
10-Year GoC bonds	4.26	4.61	3.99	4.09	4.13	4.59	4.35	3.99	3.75	3.75	4.00	4.35	4.09	3.99	4.35
30-Year GoC bonds	4.27	4.66	4.08	4.14	4.21	4.51	4.44	4.08	3.85	3.85	4.15	4.50	4.14	4.08	4.50
Yield Curve (10's-2's)	27	21	10	6	15	-2	23	25	65	70	60	55	6	25	55
United States															
Fed Funds rate	4.75	5.25	5.25	5.25	5.25	5.25	4.75	4.25	3.50	3.25	3.25	3.50	5.25	4.25	3.50
3-month T-bills	4.53	4.89	4.77	4.90	4.92	4.69	3.64	3.10	2.50	2.55	3.00	3.75	4.90	3.10	3.75
2-Year bonds	4.82	5.21	4.67	4.82	4.60	4.93	3.94	3.08	2.50	2.45	3.00	3.75	4.82	3.08	3.75
5-Year bonds	4.81	5.18	4.56	4.71	4.55	4.97	4.19	3.46	3.00	3.00	3.45	4.10	4.71	3.46	4.10
10-Year bonds	4.85	5.22	4.62	4.72	4.65	5.06	4.53	4.03	3.75	3.75	3.95	4.50	4.72	4.03	4.50
30-Year bonds	4.90	5.28	4.76	4.83	4.83	5.16	4.79	4.46	4.30	4.30	4.40	4.75	4.83	4.46	4.75
Yield Curve (10's-2's)	3	1	-5	-11	4	14	60	95	125	130	95	75	-11	95	75
Yield spreads															
3-month T-bills	-0.67	-0.59	-0.62	-0.75	-0.75	-0.26	0.34	0.75	0.85	0.55	0.25	-0.25	-0.75	0.75	-0.25
2-Year	-0.83	-0.81	-0.78	-0.80	-0.62	-0.32	0.18	0.65	0.60	0.60	0.40	0.05	-0.80	0.65	0.05
5-Year	-0.65	-0.69	-0.68	-0.71	-0.53	-0.39	0.06	0.41	0.50	0.35	0.25	-0.10	-0.71	0.41	-0.10
10-Year	-0.59	-0.61	-0.63	-0.62	-0.52	-0.47	-0.18	-0.04	0.00	0.00	0.05	-0.15	-0.62	-0.04	-0.15
30-Year	-0.63	-0.62	-0.68	-0.69	-0.63	-0.65	-0.35	-0.39	-0.45	-0.45	-0.25	-0.25	-0.69	-0.39	-0.25

Exchange rates

%, end of period

	Actual							Forecast					Actual	Forecast	
	Q106	Q206	Q306	Q406	Q107	Q207	Q307	Q407	Q108	Q208	Q308	Q408	2006	2007	2008
Australian dollar	0.72	0.74	0.75	0.79	0.81	0.85	0.89	0.88	0.94	0.93	0.91	0.89	0.79	0.88	0.89
Canadian dollar	1.17	1.12	1.12	1.17	1.15	1.07	0.99	1.00	0.99	1.02	1.05	1.10	1.17	1.00	1.10
Chinese renminbi	8.02	7.99	7.90	7.81	7.73	7.61	7.51	7.30	7.30	7.25	7.15	7.10	7.81	7.30	7.10
Euro	1.21	1.28	1.27	1.32	1.34	1.35	1.43	1.46	1.50	1.45	1.40	1.38	1.32	1.46	1.38
Japanese yen	118	114	118	119	118	123	115	112	115	116	117	118	119	112	118
Mexican peso	10.87	11.34	10.98	10.82	11.04	10.81	10.94	10.91	10.85	10.95	11.00	11.10	10.82	10.91	11.10
New Zealand dollar	0.62	0.61	0.65	0.70	0.71	0.77	0.76	0.77	0.80	0.77	0.75	0.76	0.70	0.77	0.76
U.K. pound sterling	1.74	1.85	1.87	1.96	1.97	2.01	2.05	1.98	2.05	1.97	1.89	1.89	1.96	1.98	1.89

Source: Bank of Canada, Federal Reserve Board, Reuters, RBC Economics Research forecasts