

Canada and the Commodity Super-Cycle

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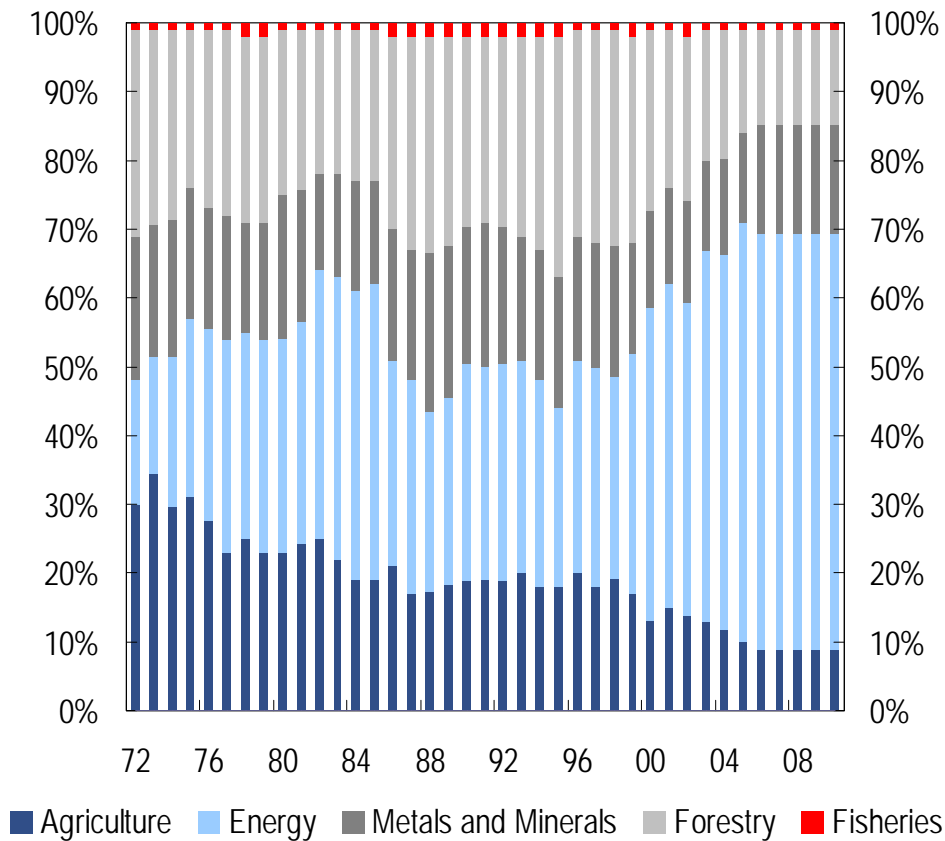
See the Disclosure Appendix for the Analyst
Certification and Other Disclosures

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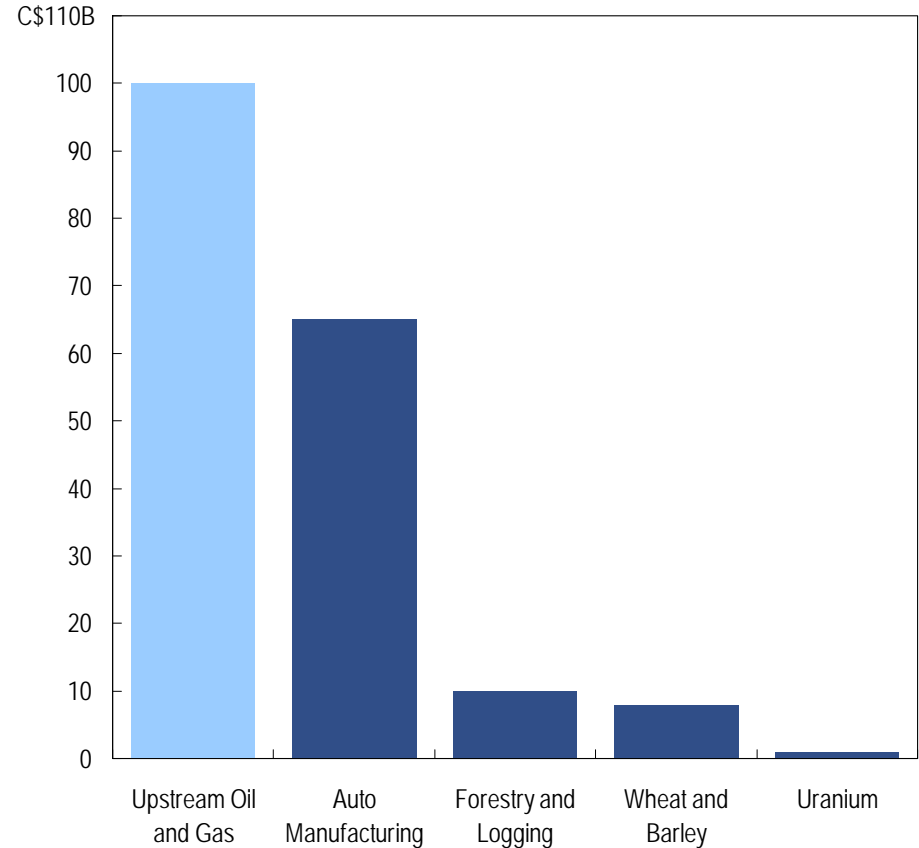
Extended Honeymoon

A Small, Open, Commodity Exporting Nation

Canada – Bank of Canada Chained Fisher Commodity Price Index: Nominal Commodity Shares (%), 1972 – 2010



Canada – Annual Revenue for Major Canadian Industries (Billions of C\$)

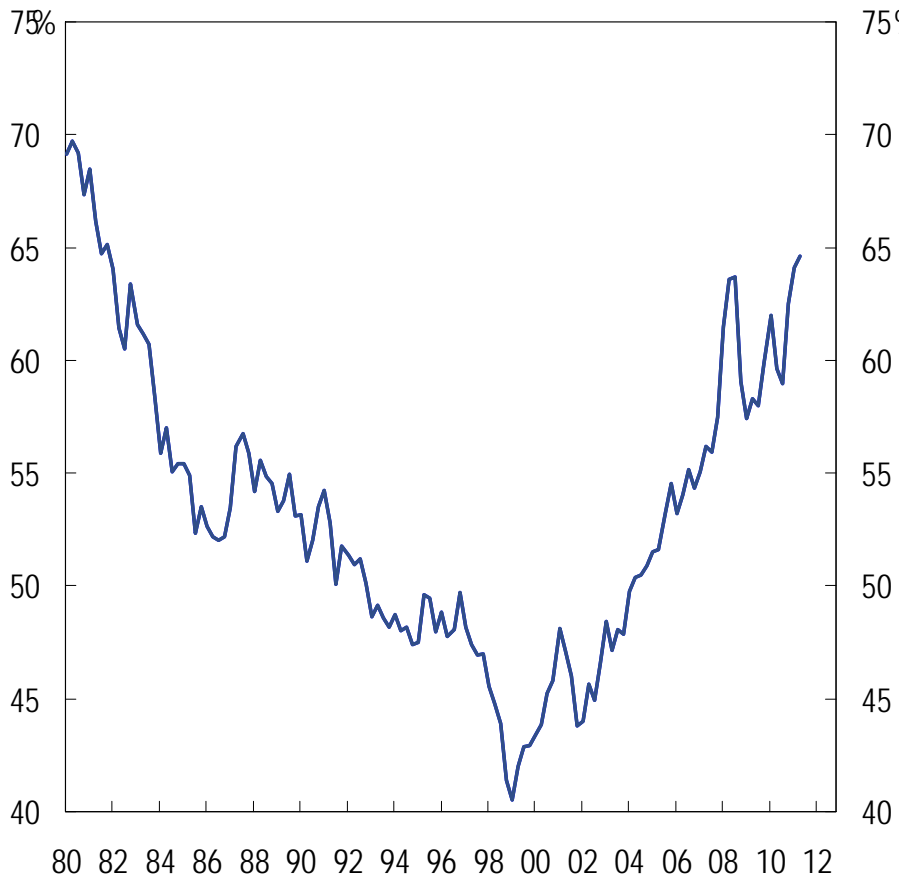


Source: Bank of Canada.

Source: Natural Resources Canada and ARC Financial (NRC May 2011 Report).

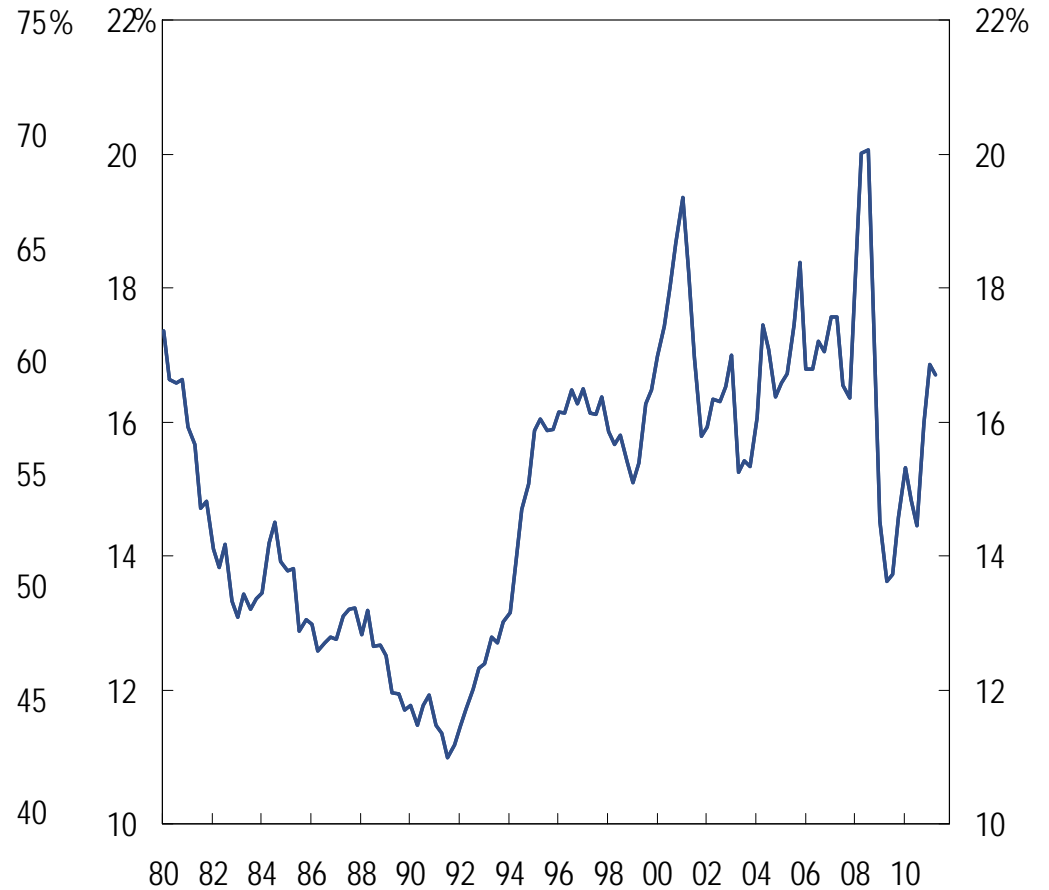
Commodities Are a Major Share Of Exports And Output

*Canada – Commodities as a Share of Nominal Exports (Percent),
1980 – 2Q 11*



Source: Statistics Canada.

*Canada – Commodity Exports as a Share of GDP (Percent),
1980 – 2Q 11*



Source: Statistics Canada.

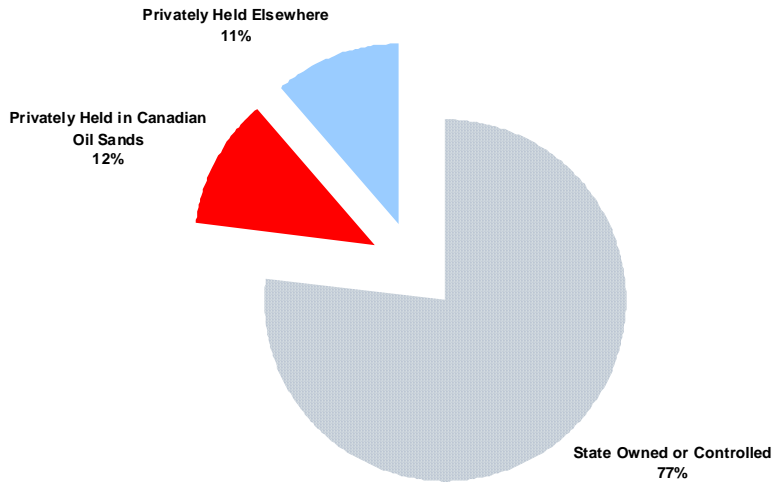
Canadian Commodities Exposure

Canada – Commodity Exports Detail, YTD 2011

Rank		% Total Commodity Exports	% Total Exports	2011 YTD Bil. C\$	Annualized C\$	% of GDP 2011	
	All Commodities		64.1	161.7	277.2	16.3	
	Crude Petroleum	1	23.1	14.8	38.3	65.68	3.9
	Forestry Products	2	8.0	5.1	13.2	22.71	1.3
	Petroleum and Coal Products	3	7.5	4.8	12.4	21.26	1.3
	Precious Metals	4	6.5	4.2	10.8	18.51	1.1
	Chemicals	5	5.9	3.8	9.7	16.65	1.0
	Natural Gas	6	5.1	3.3	8.4	14.46	0.9
	Iron and Steel	7	4.5	2.9	7.5	12.81	0.8
	Other Food, Feed, Beverages and Tobacco	8	4.1	2.7	6.9	11.76	0.7
	Synthetic Rubber, Plastics	9	4.0	2.5	6.6	11.26	0.7
	Aluminum	10	2.8	1.8	4.7	8.00	0.5
	Fertilizer	11	2.7	1.7	4.4	7.60	0.4
	Nickel	12	2.4	1.5	3.9	6.70	0.4
	Coal and Other Crude Bituminous Substances	13	2.3	1.5	3.8	6.54	0.4
	Copper	14	2.1	1.4	1.5	2.50	0.1
	Wheat, Wheat flower	15	1.9	1.2	3.1	5.27	0.3

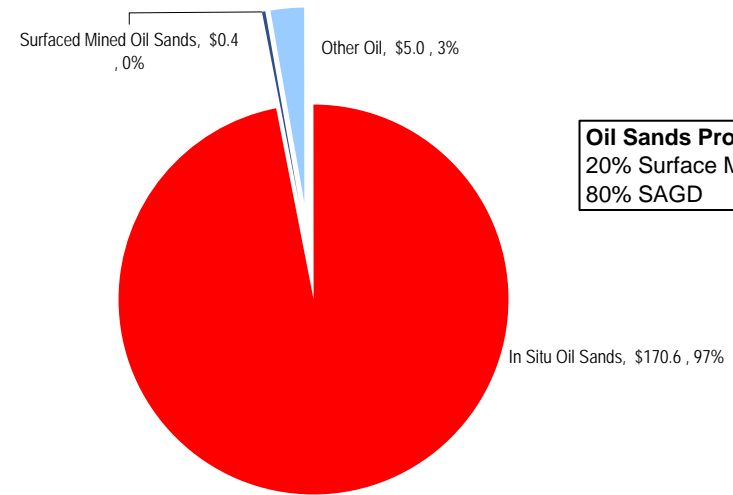
Comparative Advantage In Long-Term Energy Production

Global – Oil Reserve Ownership Percent of World



Country	Reserves (Billions of Barrels)	% Total
World	1,470	100
Saudi Arabia	260	18
Venezuela	211	14
Canada	175	12
Iran	137	9
Iraq	115	8
Kuwait	102	7
USSR	99	7
Abu Dhabi	92	6
Russia	60	4
Libya	46	3
Nigeria	37	3
Rest of World	135	9

Canada – Land Use in Oil Sands Extraction (\$Bil Barrels)



Oil Sands Production
20% Surface Mining
80% SAGD

TSX Market Value	2002	2011
Oil Gas & Consumable Fuels	12%	25%
Metals & Mining	12%	20%

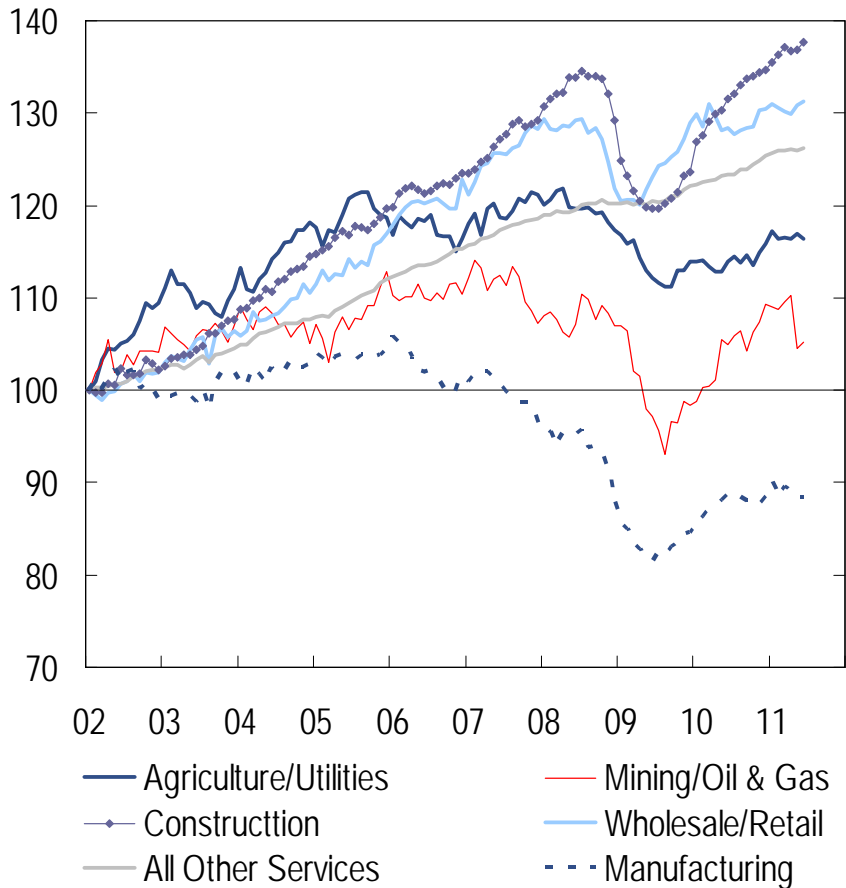
Stocks (Million Barrels)	2002	2011
Crude Oil	77.5	105.1
NGL + Feedstocks and other	17.5	15.6
Motor Gasoline	17.4	18.6
Middle Distillates	19.8	18.1
Residual Fuel Oil	3.8	3.6
Other Products	21.4	25.9
Total	157.3	186.9

Supply (Million Barrels/Day)	2002	2011
Crude Oil	1.7	2.0
Natural Gas Liquids	0.7	0.6
Nonconventional Oils	0.4	0.8
Total	2.9	3.4

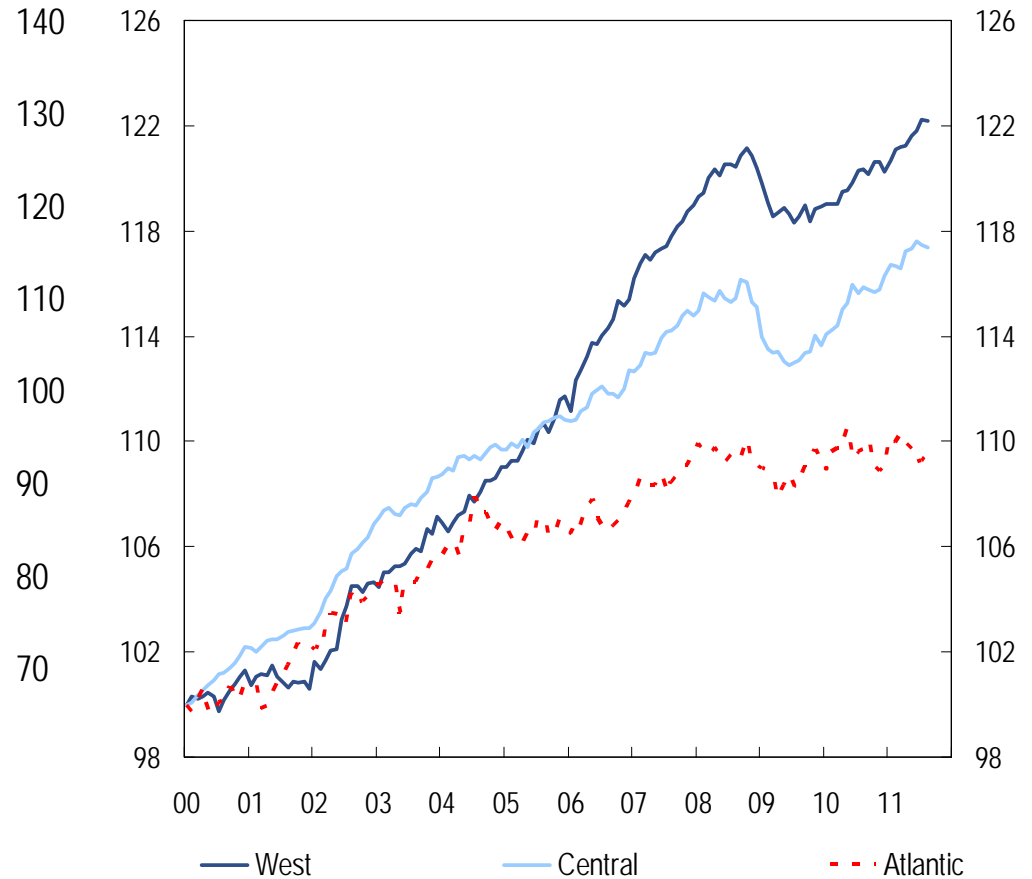
Source: Canadian Association of Petroleum Products, and Oil and Gas Journal 2011F.

Structural Adjustment: Output and Labor Stratification

Canada – Real Industry-Based Output (Jan 2002=100),
2002 – Jun 11



Canada – Regional Employment (Jan 2000=100),
2000 – Aug 11

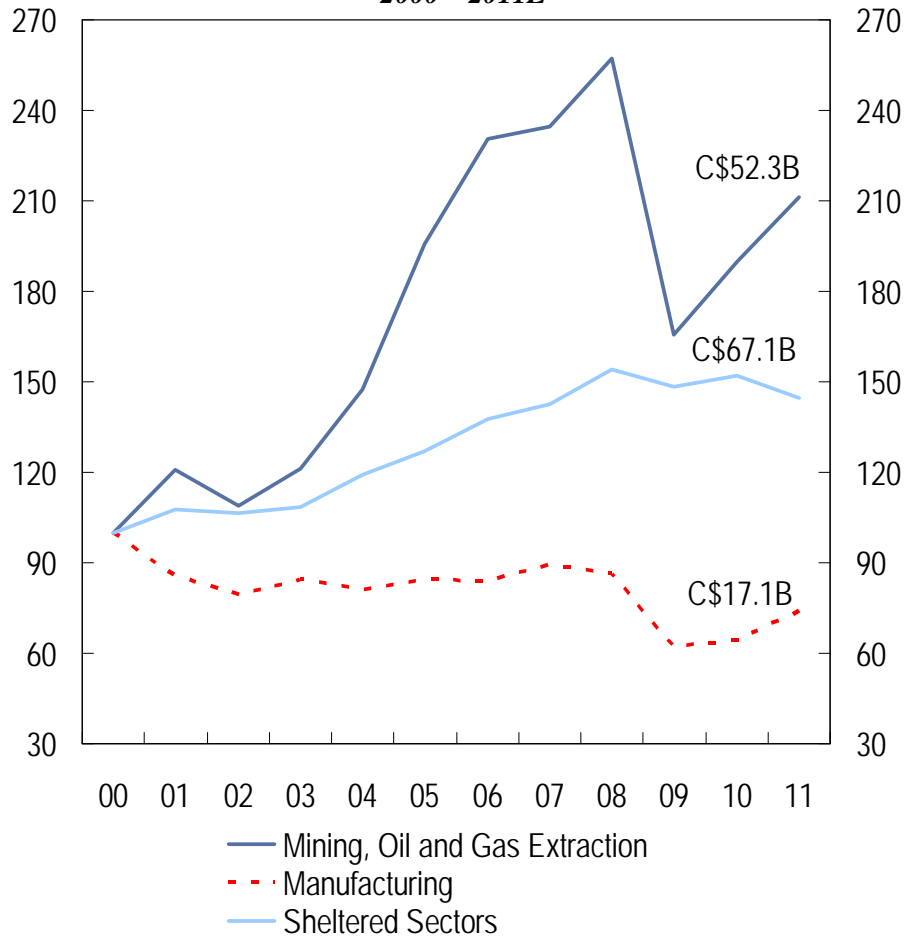


Note: West (Alberta, British Columbia, Saskatchewan and Manitoba), Central (Ontario and Quebec) and Atlantic (Labrador/Newfoundland, Prince Edward Island, Nova Scotia and New Brunswick). Source: Statistics Canada.

Source: Statistics Canada.

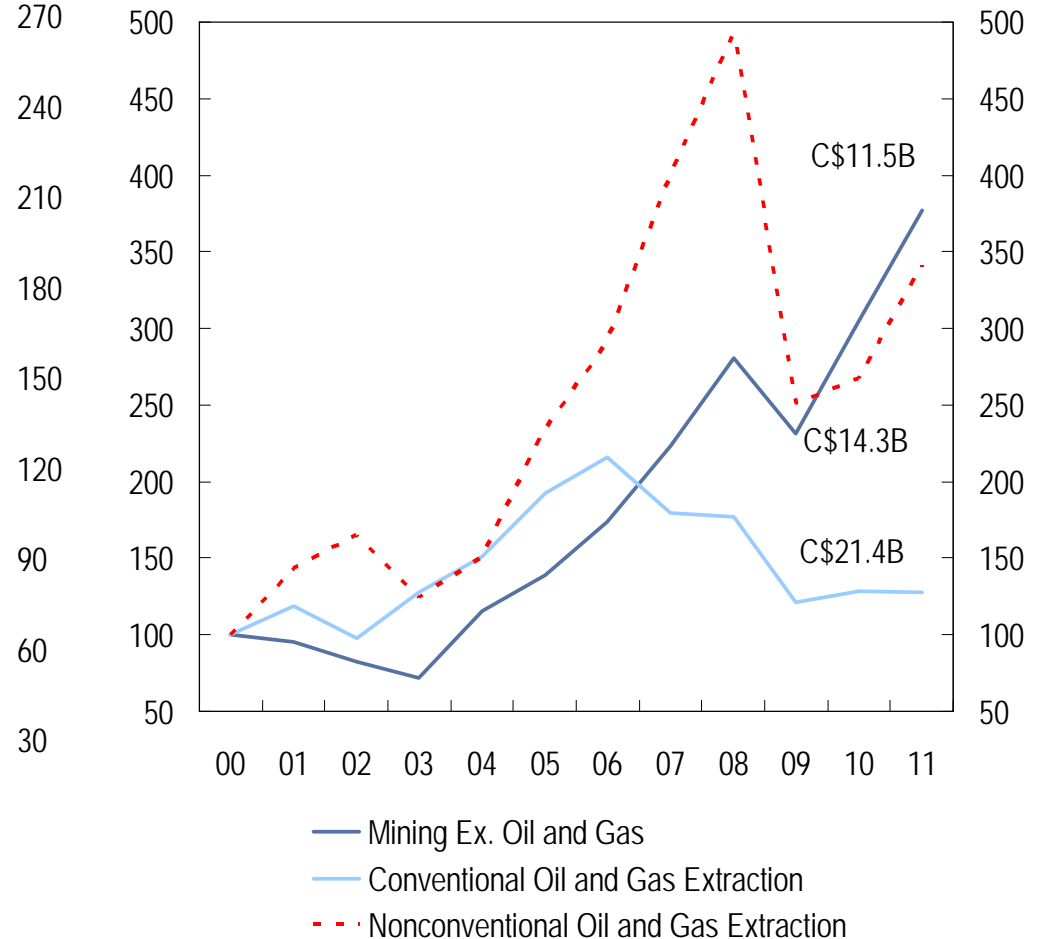
Capex Shifted Towards Natural Resources and Supporting Services

Canada – Capital Expenditures (2000=100),
2000 – 2011E



Source: Statistics Canada.

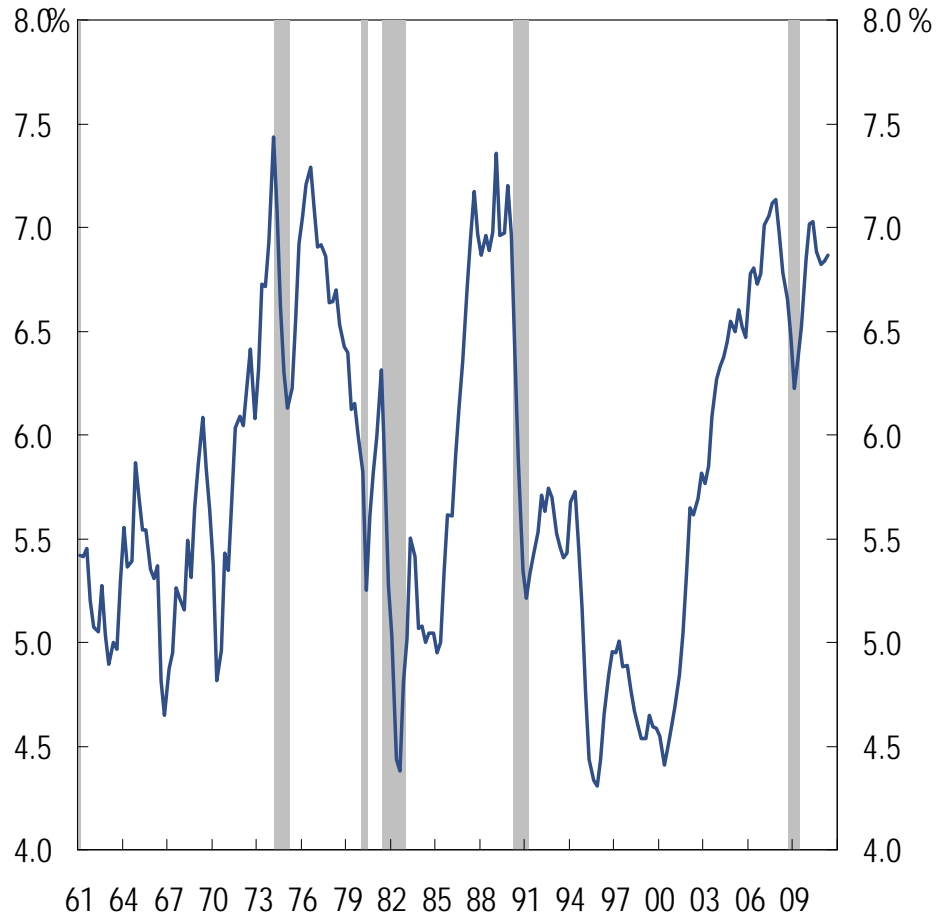
Canada – Mining & Energy Capital Expenditures (2000=100),
2000 – 2011E



Source: Statistics Canada.

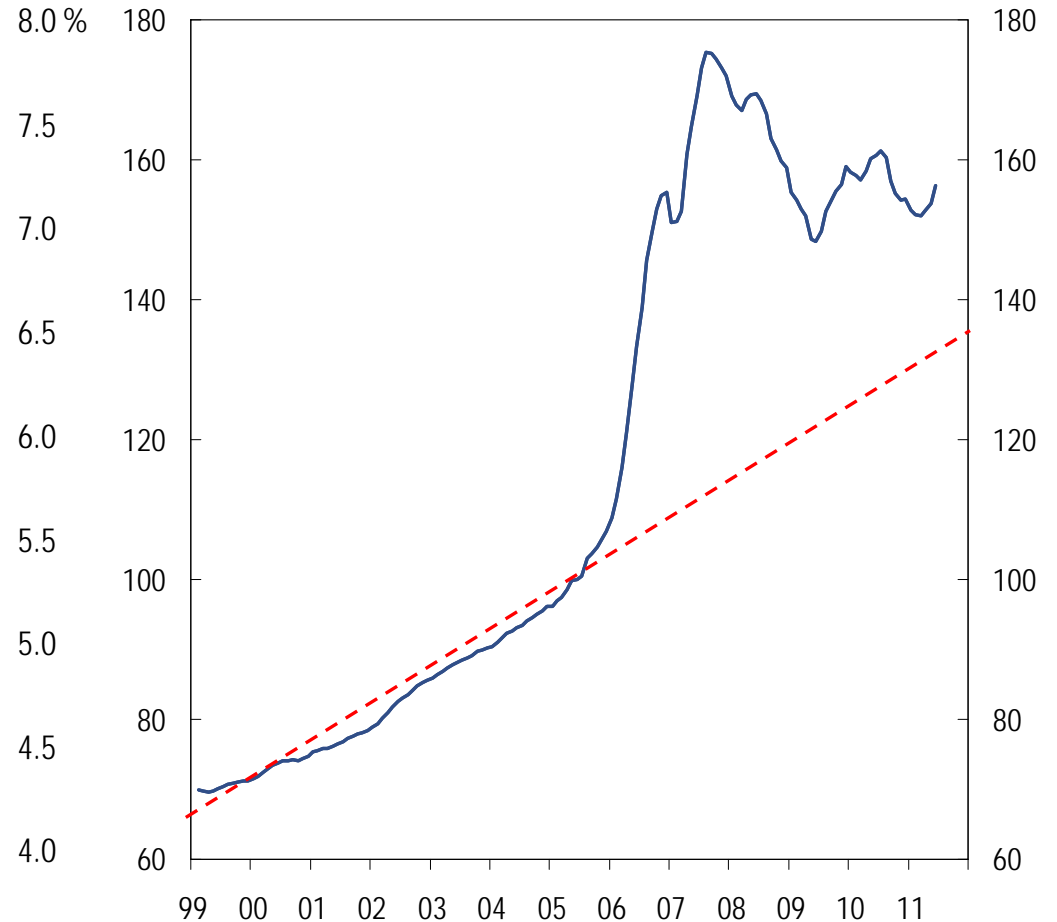
From Housing Lull To Boom, With Pockets of Excess

*Canada – Housing Investment as a Share of GDP,
1961 – 2Q 11*



Note: Shaded regions denote recessions. Source: Statistics Canada.

*Canada – Calgary, Alberta Existing Home Price Index
(Feb 99 =100), 1990 – Jun 11*

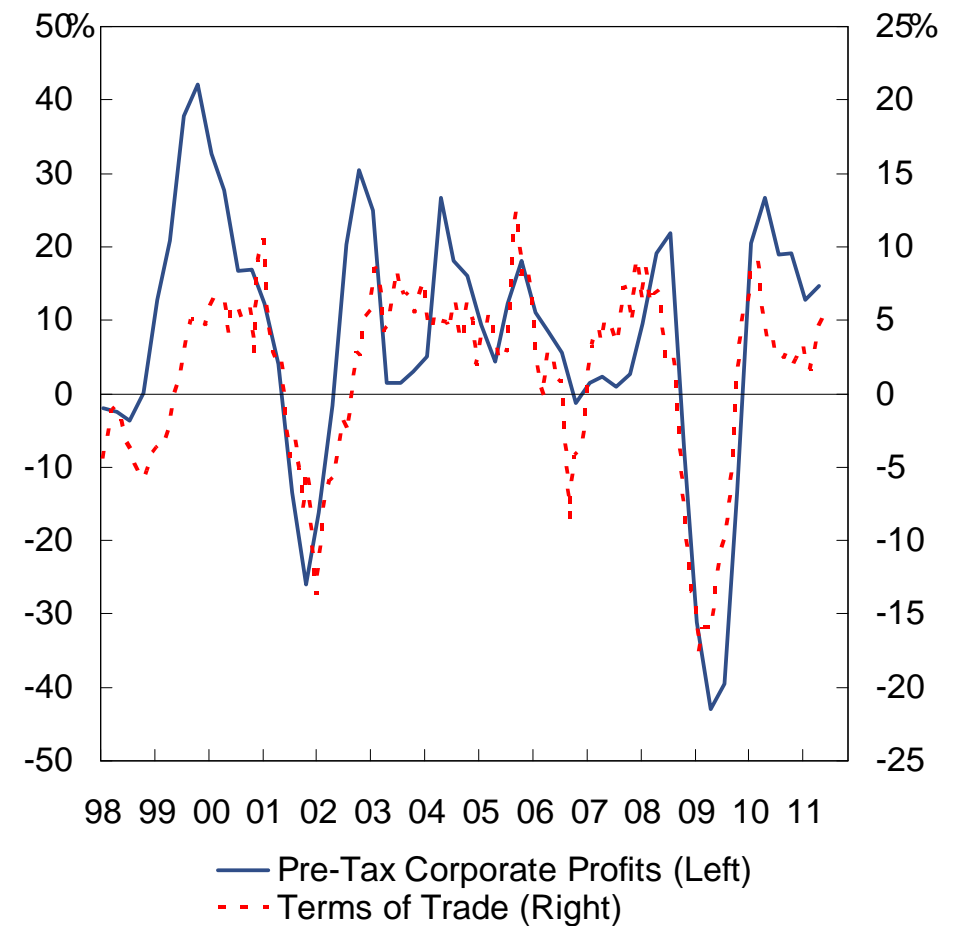
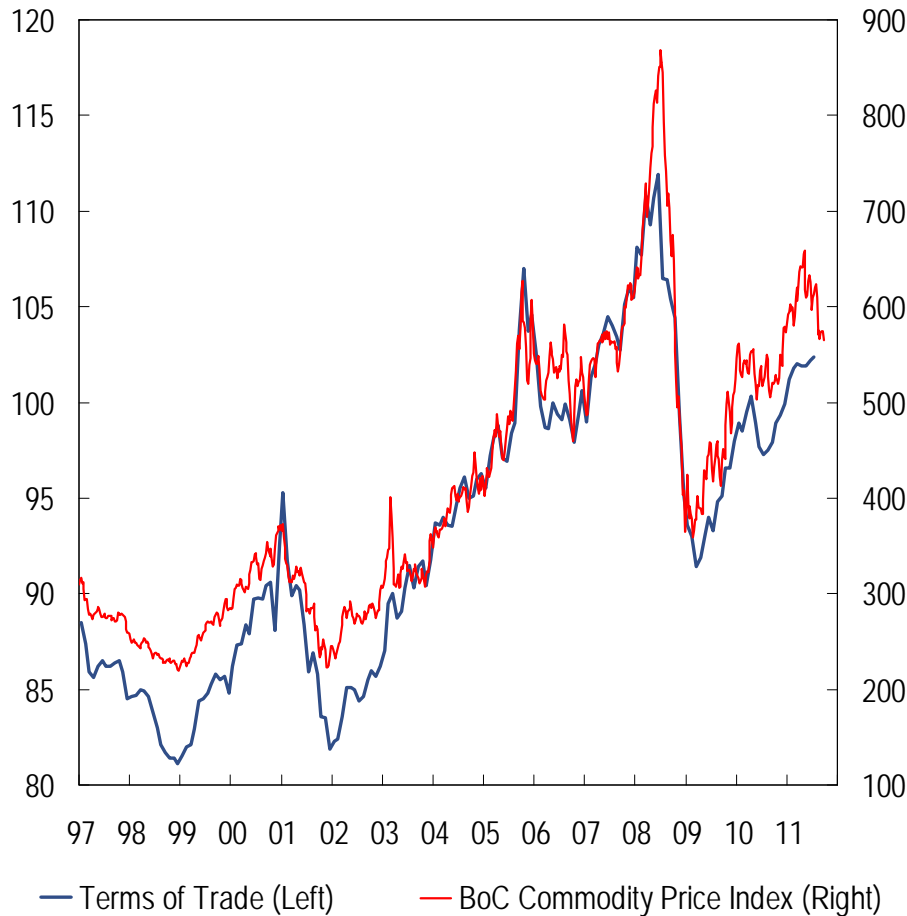


Source: Teranet-National Bank House Price Index™.

Terms of Trade Improvement Fueled Corporate Profits Growth

Canada – Terms of Trade (2005=100) vs. BoC Commodity Price Index (Jan 72=100), 1997 – 21 Sep 11

Canada – Pre-Tax Corporate Profits and Terms of Trade (Yr-to-Yr Percent Changes), 1998 – Jul 11

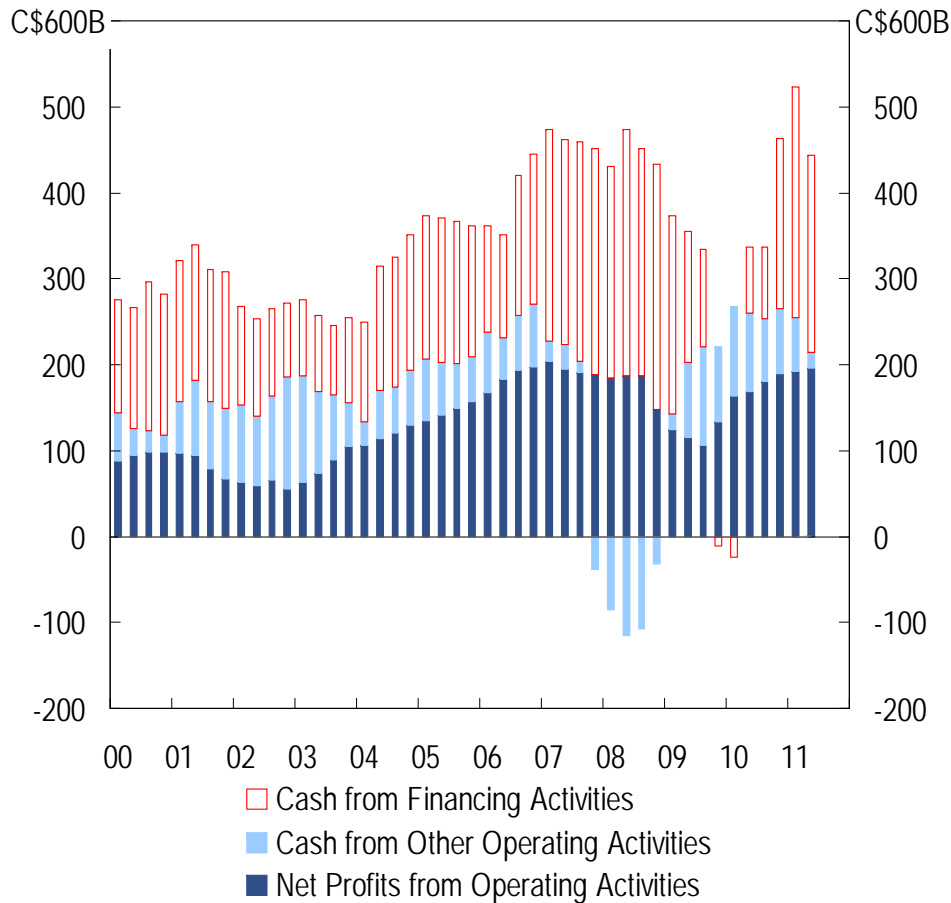


Sources: Bank of Canada and Statistics Canada.

Source: Statistics Canada.

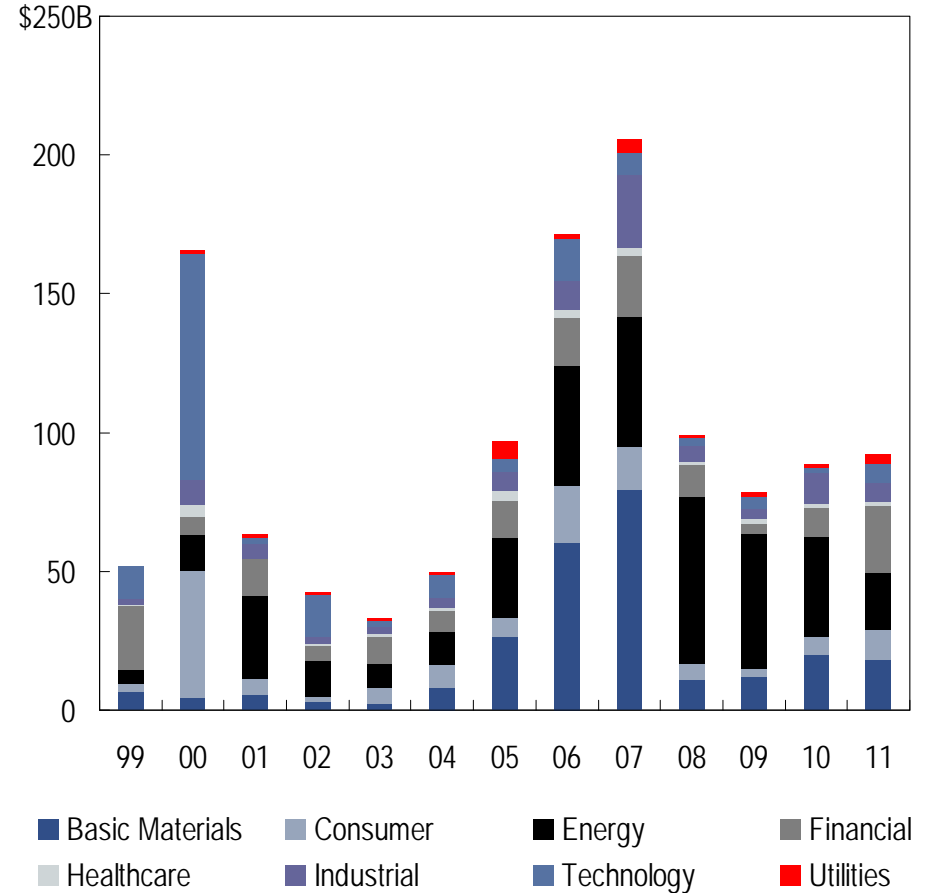
Awash in Cash From Profits, Financing And Foreign Investors

Canada – Total Cash Available of All Industries (Bil. C\$ EOP, 4-Qtr Moving Sum), 2000 – 2Q 11



Source: Statistics Canada.

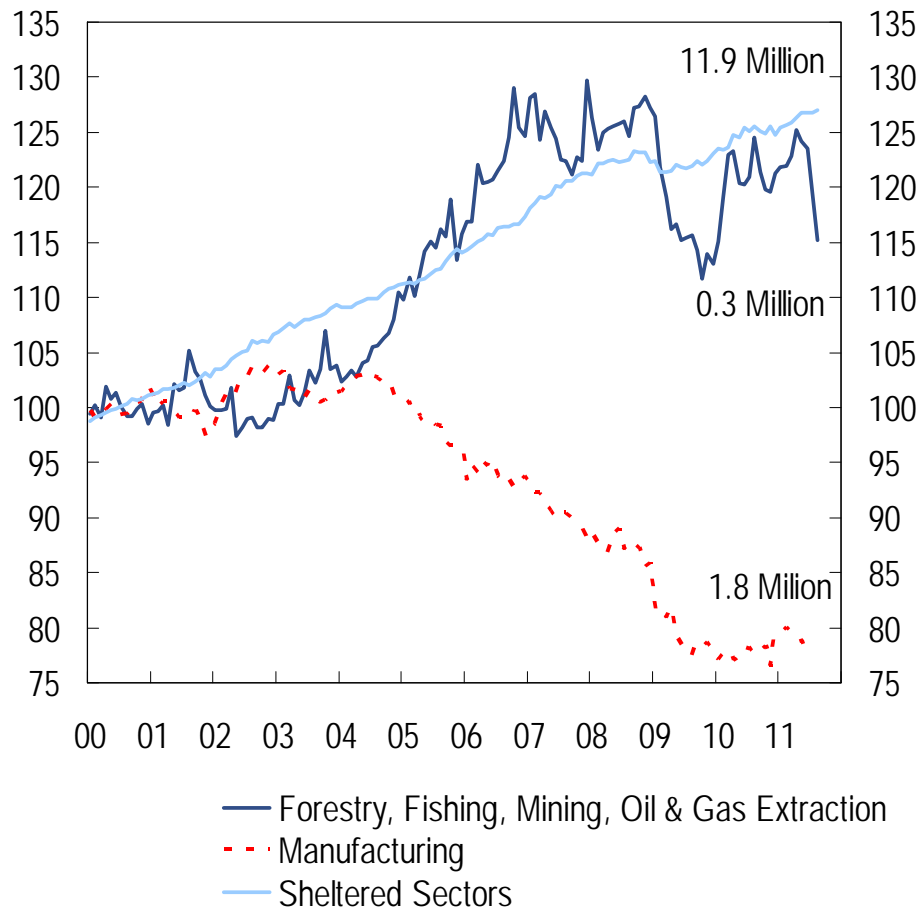
Canada – M&A of Canadian Companies by Foreign Entities (Bil US\$, 1999 – 11E)



Source: Bloomberg.

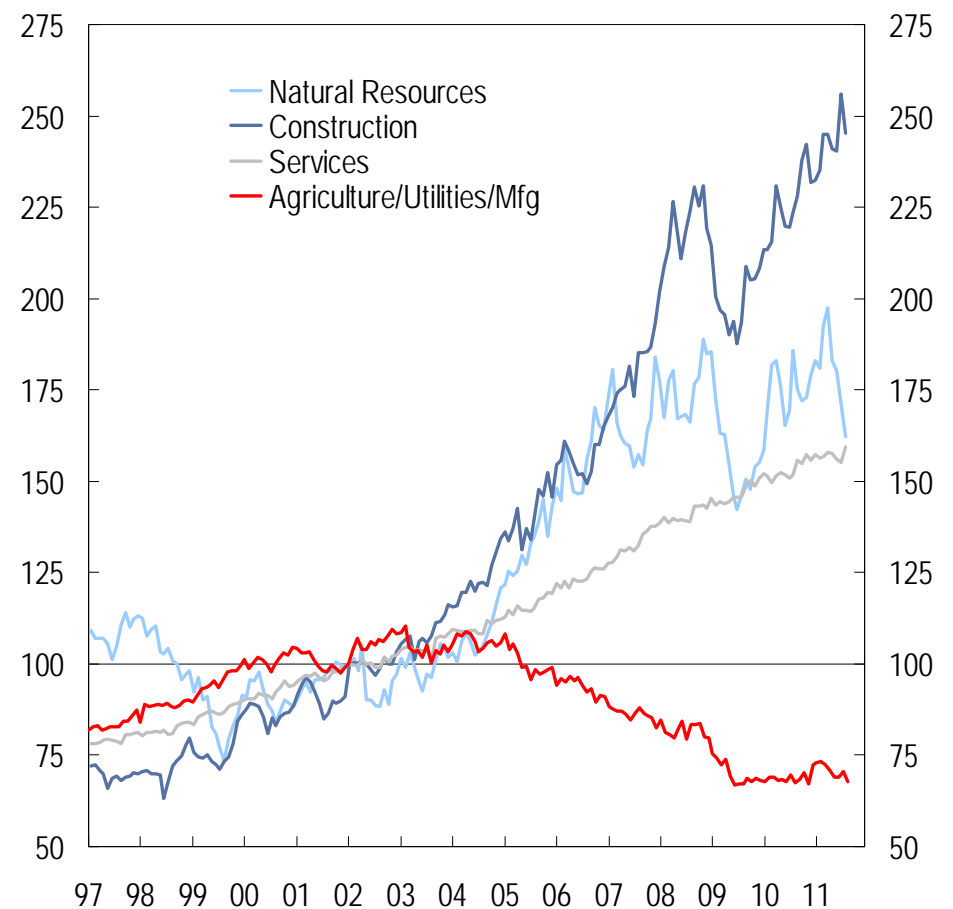
Canadian Consumers Reap Commodity Cycle Benefits

Canada – Employment By Industry (2000=100),
2000 – Aug 11



Source: Statistics Canada.

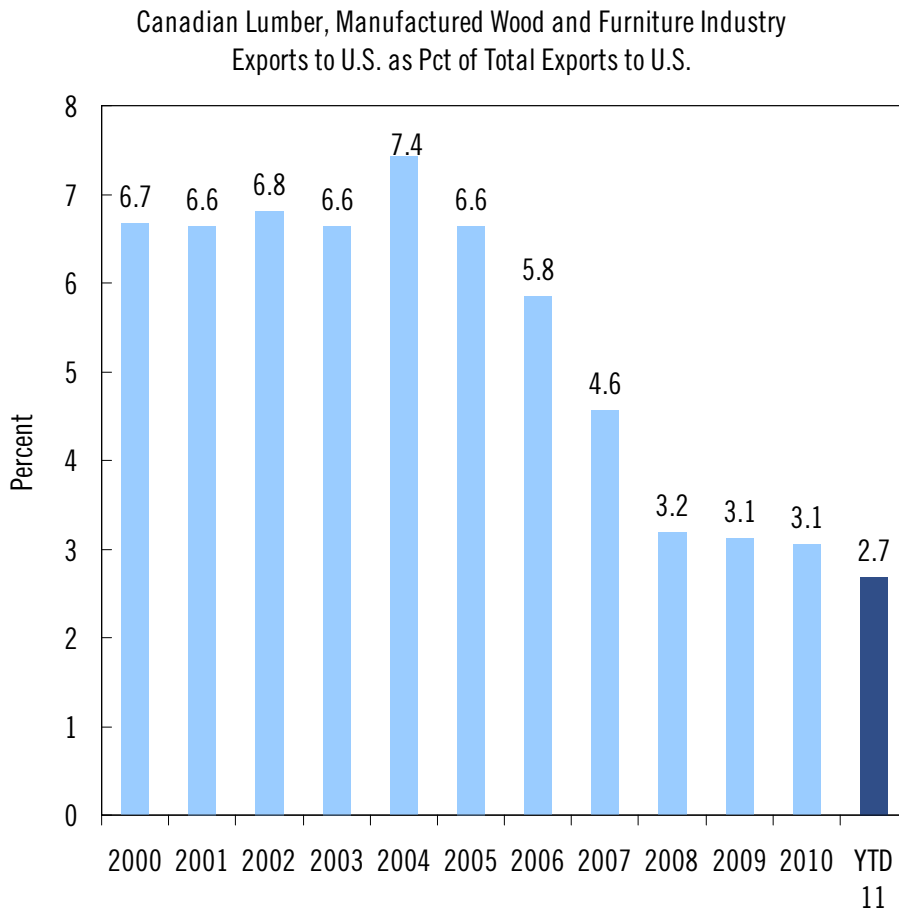
Canada – Wage Growth by Sector (Jan 2002=100) vs. CAD/USD,
1997 – Aug 11



Sources: Statistics Canada and Federal Reserve Board.

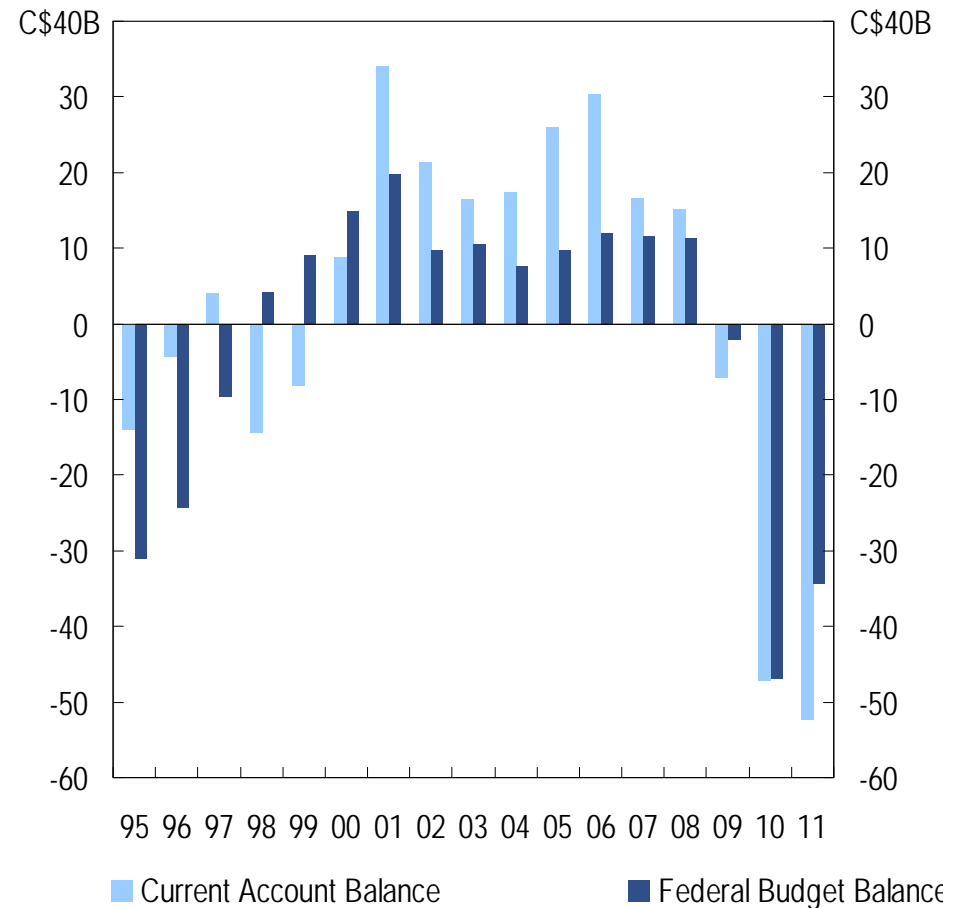
Global Recession's Impact

**Canada – Canadian Housing-Related Exports to the United States
(Percent of Total), 2000 – Jul 11**



Source: Industry Canada.

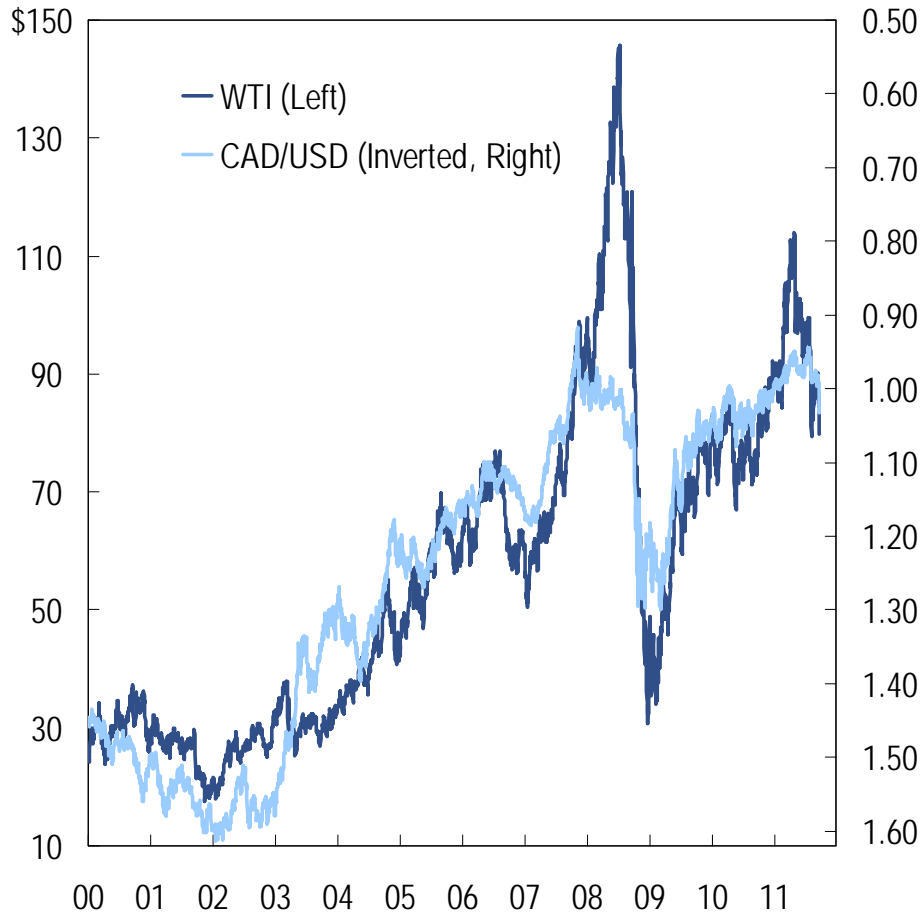
**Canada – External and Federal Budget Balances (C\$ Bil.),
FY94-95 to FY 11-12**



Sources: Statistics Canada and Canada Department of Finance.

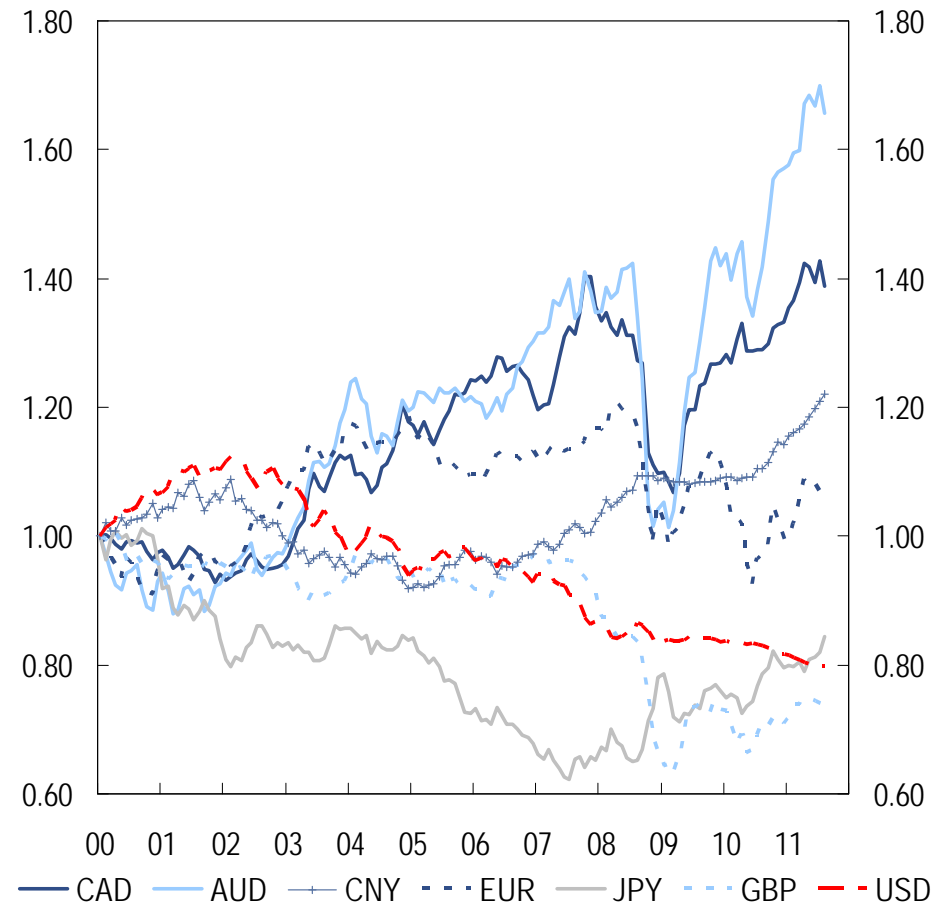
Blessings and Curses Of Commodity Currency Status

Canada and United States – CAD/USD and WTI Oil Price, 2003 – 23 Sep 11



Sources: Federal Reserve Board and Wall Street Journal.

Global – Various Real Trade-Weighted Currencies (Jan 2000 = 1.00), 2000 – Aug 11

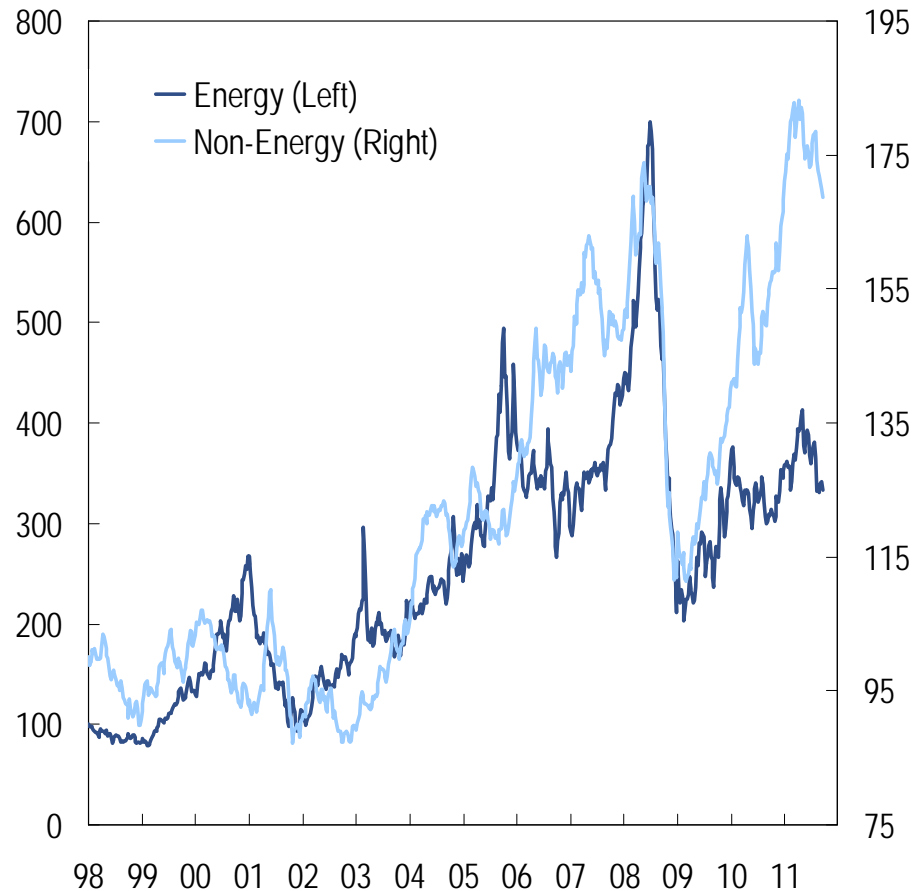


Source: Citi Investment Research and Analysis.

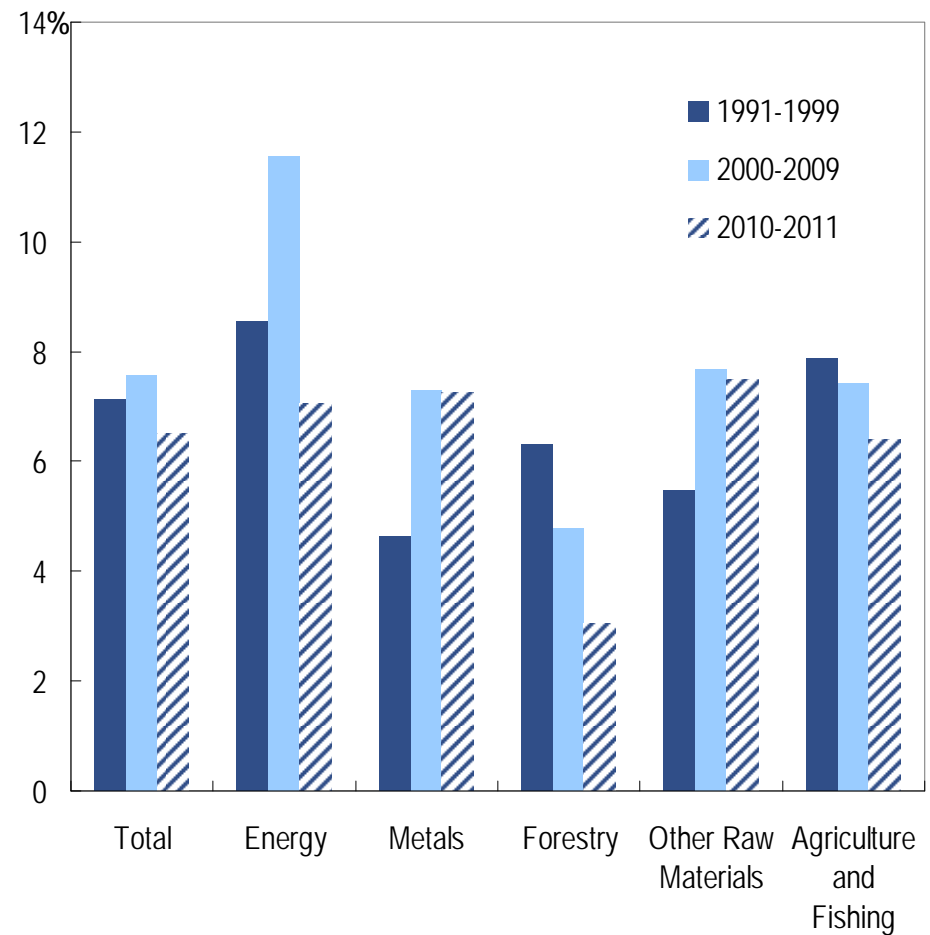
Troubled Marriage

Canada is More Vulnerable to Commodity Price Volatility

*Canada – Bank of Canada Commodity Price Indexes
(Jan 1998=100), 1998 – 21 Sep 11*



*Global – Commodity Real Price Volatility (Percent Change),
1991 – Jul 11*

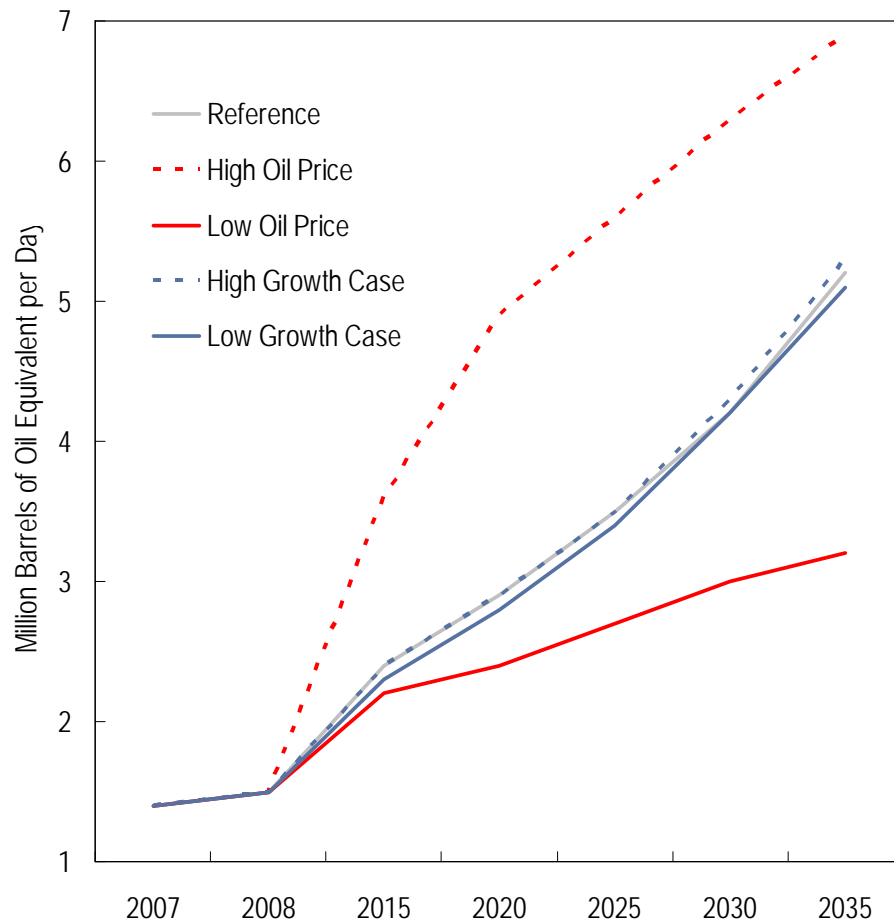


Sources: Bank of Canada and Citi Investment Research and Analysis.

Source: IMF and Citi Investment Research and Analysis.

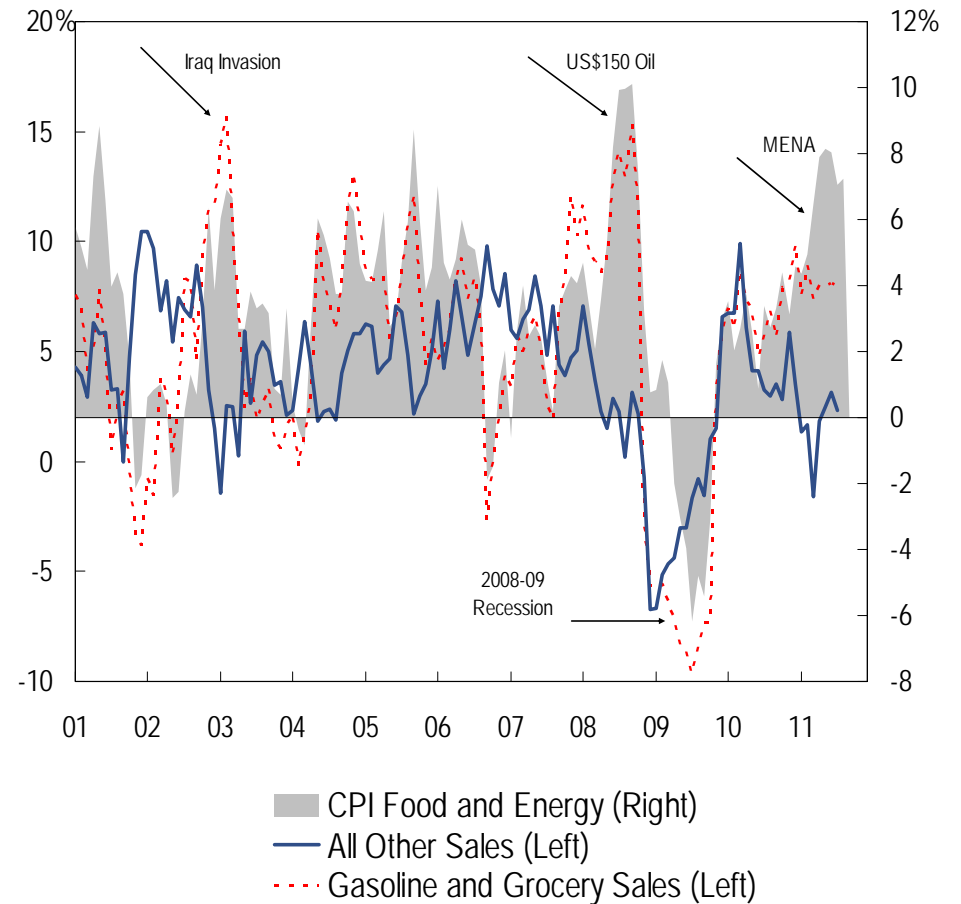
Energy Prices Influence Industry and Household Decisions

Canada – Oil Sands Production Outlook, 2005 – 2035E



Source: Energy Information Agency.

Canada – Nominal Retail Sales vs. CPI Food and Energy (Yr-to-Yr Percent Changes, 2001 – Aug 11)



Source: Statistics Canada.

Citi Commodity Price Forecasts

Global – Key Commodity Price Forecasts*

		0-3m	6-12m	2011E	2012E	2013E	2014E	2015E	5Y Cycle**
Energy									
WTI Crude	\$/bbl	82	72.5	89.9	71.8	92.5	88	90.2	81
Brent Crude	\$/bbl	95	91	105.9	86.3	102	87	89.1	85
Base Metals									
LME Aluminum	\$/mt	2,325	2,300	2,462	2,319	2,566	2,556	2,518	
LME Copper	\$/mt	8,500	8,000	9,099	8,375	8,534	8,051	7,077	
LME Lead	\$/mt	2,250	2,200	2,477	2,263	2,356	2,129	1,942	
LME Nickel	\$/mt	21,000	20,000	23,649	20,938	23,419	21,367	17,932	
LME Zinc	\$/mt	2,125	2,000	2,260	2,075	2,256	2,400	2,400	
Precious Metals									
Gold	\$/t. oz	2,000	1,650	1,591	1,650	1,500	1,350	1,250	
Silver	\$/t. oz	35	33	33.4	26	22.38	19.13	16	
Bulk Commodities									
Hard Coking Coal (benchmark Asia)	\$/t	305	280	289	275	248	240	230	
Thermal Coal (benchmark Asia)	\$/t	118	130	122	139	148	152	145	
Iron Ore Fines (Brockman, FOB)	\$/t	130	130	164	154	128	113	101	
Iron Ore Spot (TSI)	\$/t	165	175	173	160	135	125	115	
Agriculture									
Corn	\$/bu	675	700	688	671				700
Soybeans	\$/bu	1,247	1,343	1,289	1,369				1,350
Wheat	\$/bu	700	725	713	710				675
Rice	\$/cwt	15.6	15.6	15.3	15.5				14
Cotton	\$/lb	104	98	150	100				125
Sugar	\$/lb	27	26	28	25				25
Coffee	\$/lb	245	249	253	250				250
Cocoa	\$/mt	3,000	3,050	3,080	3,095				3,100

* Forecasts are Nominal, as of September 5, 2011. ** Real-adjusted. Source: Citi Investment Research and Analysis.

Canadian Breakeven Curves Can Be Higher For Energy

Global – Cash Costs for Assorted Metals by Percentile

	Global			Canada		
	10th	50th	90th	10th	50th	90th
Al \$/lb	\$0.71	\$0.93	\$1.12	\$0.70	\$0.83	\$0.96
Cu \$/lb	(\$0.69)	\$1.01	\$1.72	\$0.75	\$1.09	\$2.30
Ni \$/lb	(\$5.00)	\$4.81	\$7.25	(\$5.50)	\$1.00	\$4.75
Fe \$/tonne					\$120.00	
Steel \$/short ton					\$700.00	

Note: Prices can be negative due to byproduct credits from gold production.
Source: Citi Investment Research and Analysis and wood Mackenzie.

Canada – Crude Oil \$US WTI bbl: Breakeven Thresholds

Canada	High Investment	Low Price	High Price
Oil sands and conventional	\$ 35.00	\$ 65.00	\$ 95.00

Notes: The common range quoted for WTI is \$65 to \$80 per barrel. Canada oil production costs vary due to type of oil mined (Liquid, bitumen, synthetic), method (surface or in situ mining), technology deployed, price of Natural Gas used to extract in situ oil, past investment. Services cost inflation and discount of WTI to Brent are also factors in the cost of production, and can also determine whether projects are shelved. Source: CIRA.

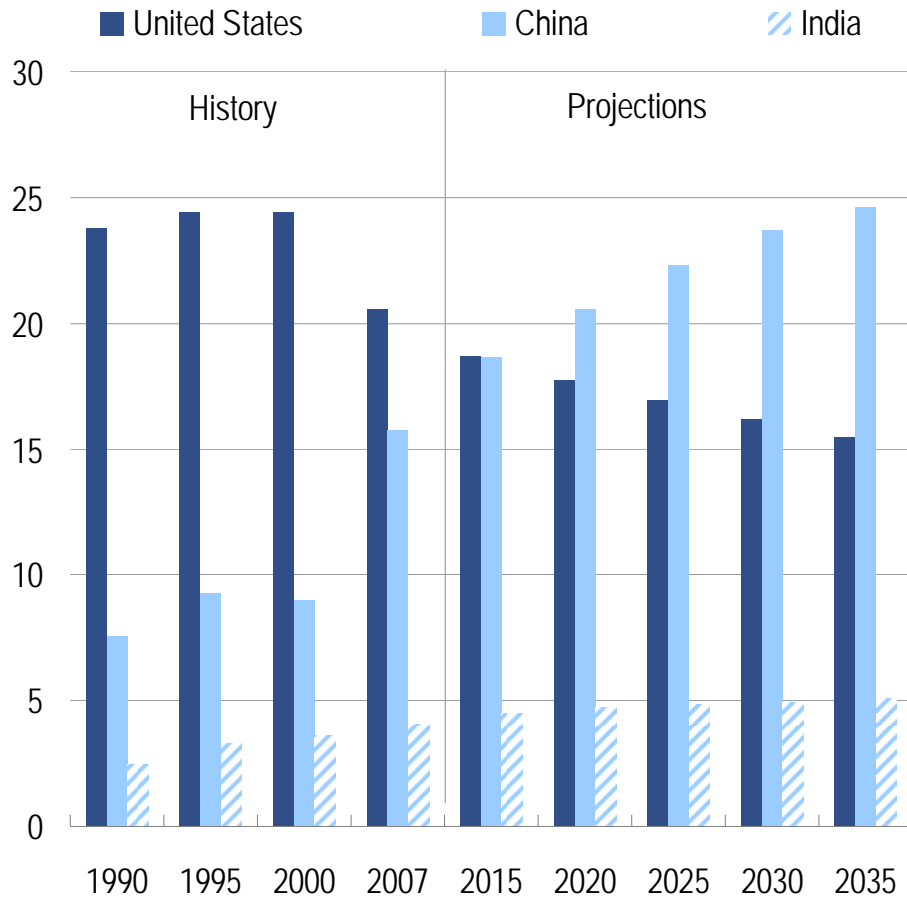
North America – Natural Gas \$US mbtu

Canada	Low	High	Usual
Shale Natural GAS	\$ 5.00	\$ 5.50	
US	Low	High	Usual
Marcellus Shale (PA, NY, WV)	\$ 2.50	\$ 4.00	
Conventional On-Shore			\$ 5.50
Haynesville Shale (LA, TX)	\$ 4.00	\$ 5.50	
Burnett & Fayetteville Shale			\$ 4.00
Liquids (from NG or oil production)			\$ -

Notes: Canadian natural gas production costs more due to higher transportation costs (far from target markets) and operating difficulty due to weather. US Liquids production is paid for by revenue from simultaneous natural gas and oil mining). Source: CIRA.

Canada III Positioned To Fully Capitalize On Future Of Trade

Global – Energy Consumption as Percent of World, 1990 – 35E



Source: Energy Information Agency.

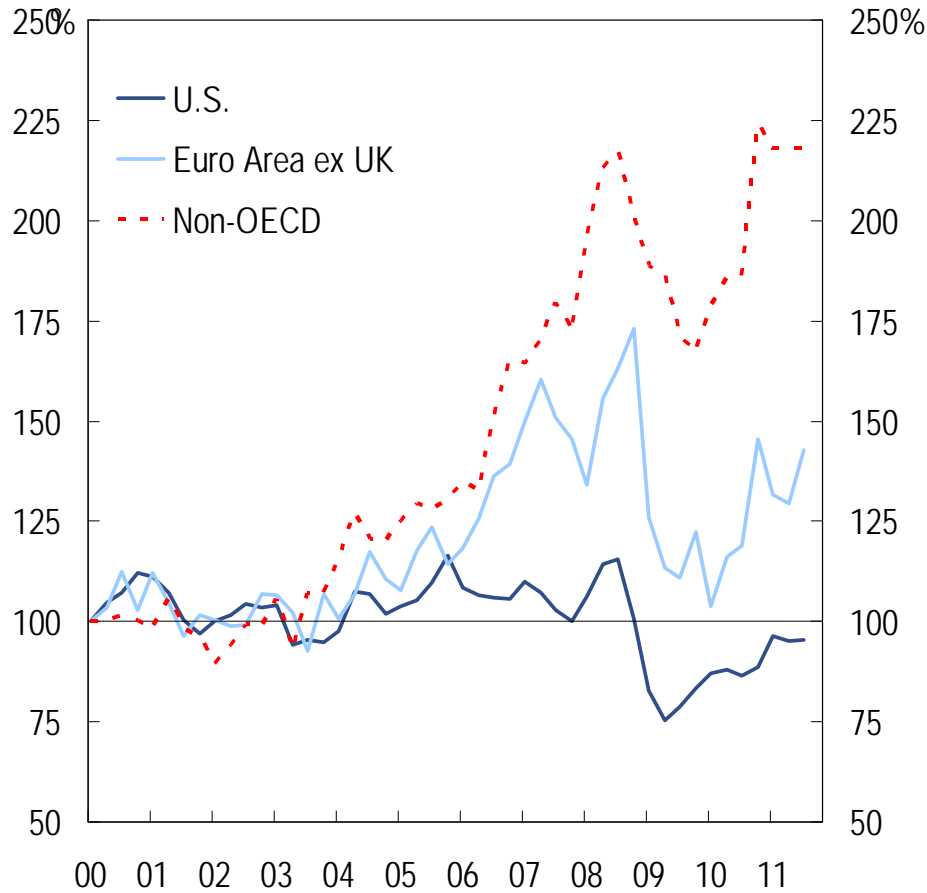
Canada – Top Exporting Markets (NSA), YTD 2011

	Bil. C\$	% of Total	Rank
Total	251	100.0	
United States	187	74.6	1
Other Asia	26	10.2	2
United Kingdom	10	4.0	3
China	9	3.4	4
Japan	6	2.4	5
South Korea	3	1.2	6
Mexico	3	1.2	7
Netherlands	3	1.1	8
Germany	2	0.8	9
Hong Kong	2	0.7	10
All Other Nations	1	0.5	

Statistics Canada.

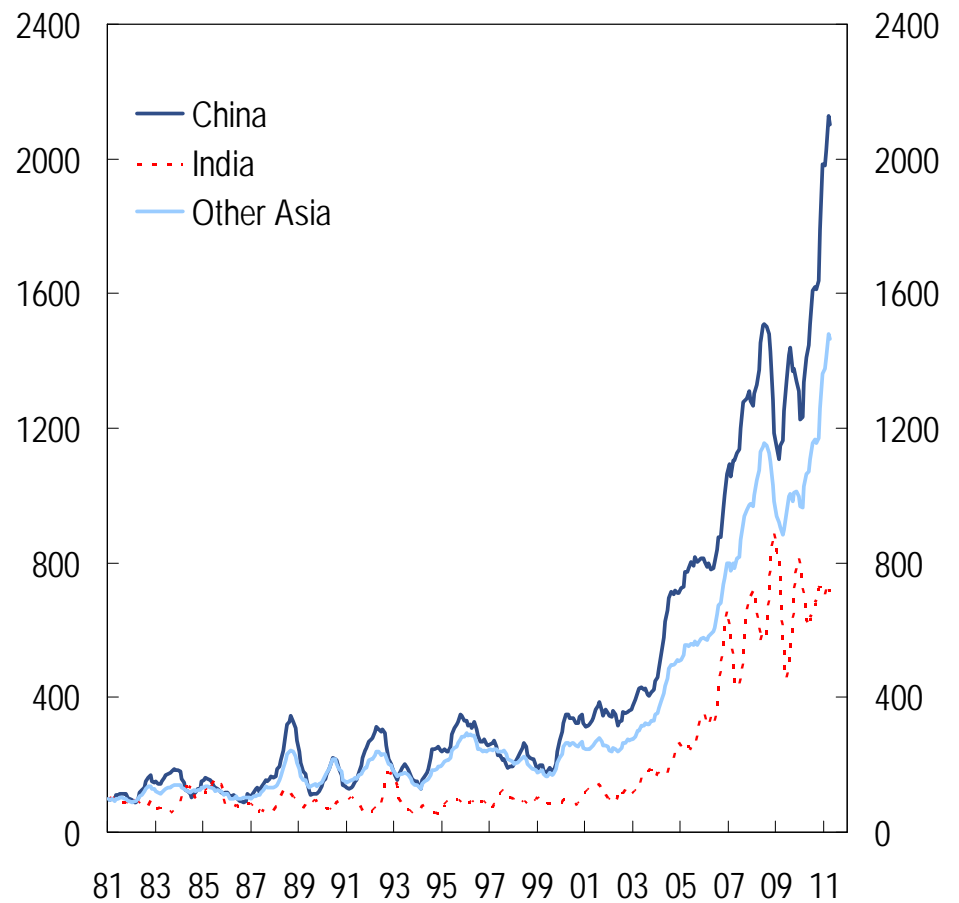
Emerging Market Trade Is The New Frontier

Global – Canadian World Exports (1Q 00 = 100), 2000 – 3Q 11E



Source: Statistics Canada.

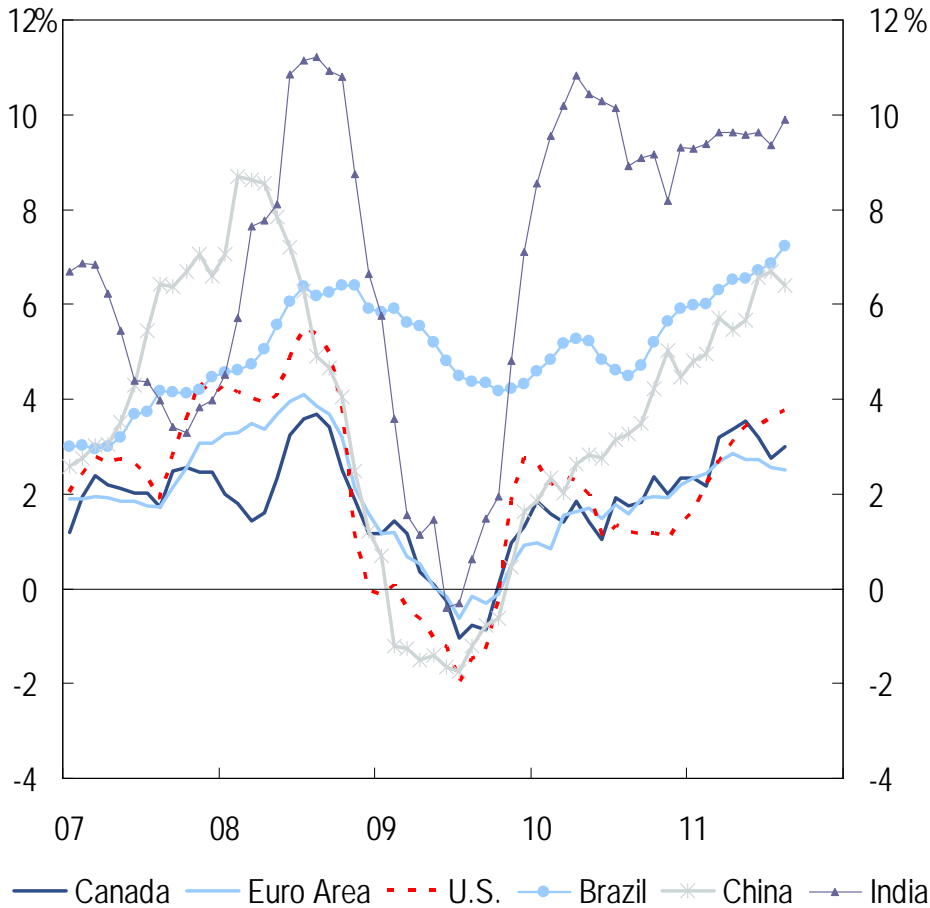
Canada – Canadian Asian Exports (Jan 81=100), 1981 – Apr 11



Source: International Monetary Fund.

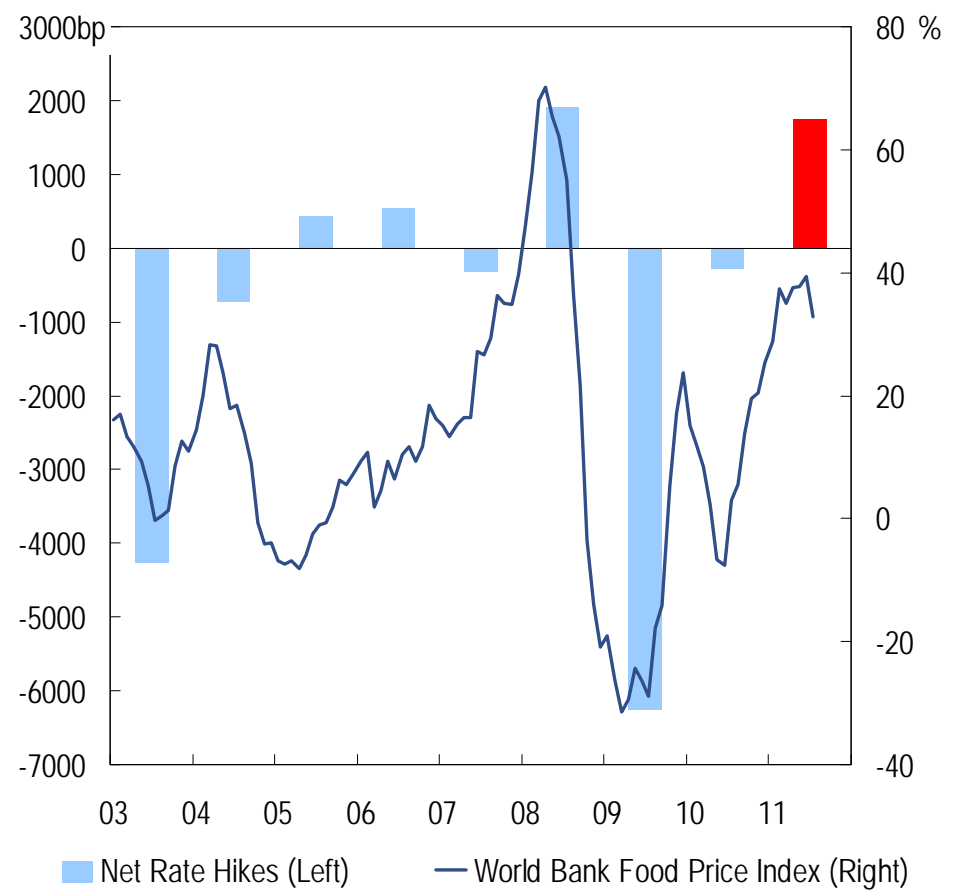
Emerging Market Risks Are Two-Sided

Global – Inflation Rates (Y/Y%), 2007 – Aug 11



Note: India inflation represented by wholesale price index. Source: CIRA.

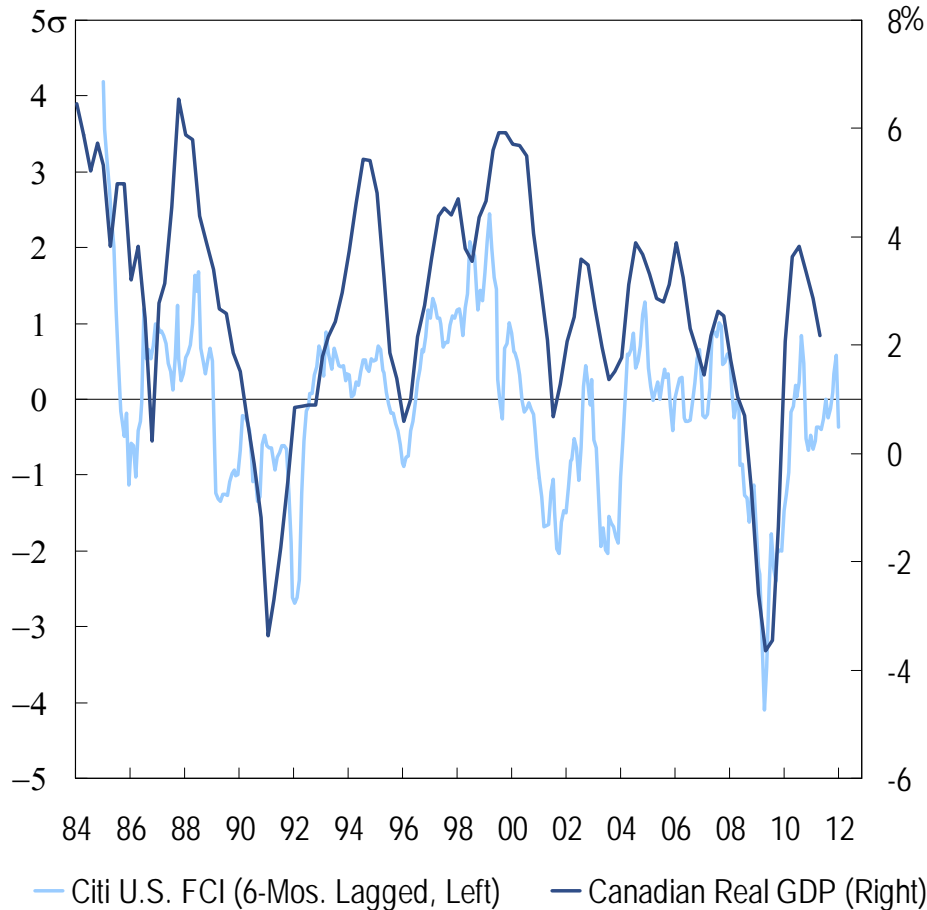
Aggregate Change in EM Monetary Policy vs. World Bank Food Price Inflation, 2003 – Aug 11



Source: Citi Investment Research and Analysis.

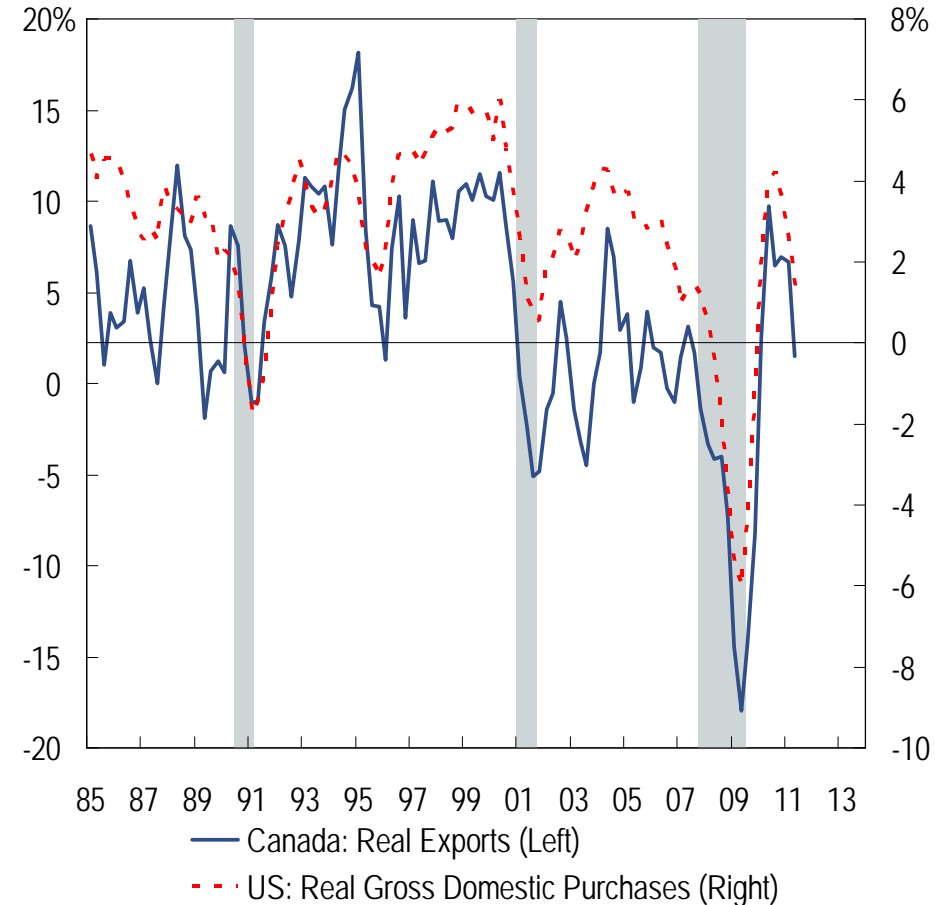
The Ties That Bind Can Be A Noose

United States and Canada – Citi US Financial Conditions Index (3-Mo. MAVE) vs. Real Canadian GDP (Yr-to-Yr Pct Chg), 1984 – Aug 11E



Sources: CIRA-Economics and Statistics Canada.

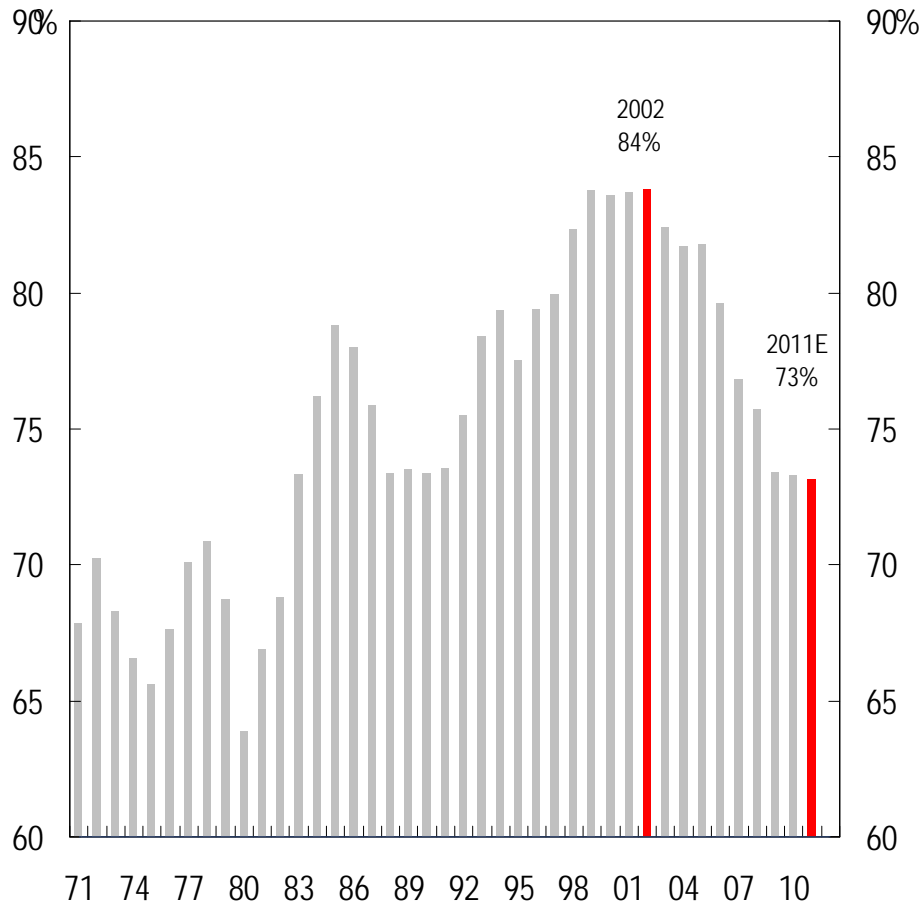
Canada and United States – Canadian Exports and U.S. Domestic Demand (Yr-to-Yr Percent Changes), 1985 – 2Q 11



Note: Shaded series denote U.S. recessions. Sources: Statistics Canada and Bureau of Economic Analysis.

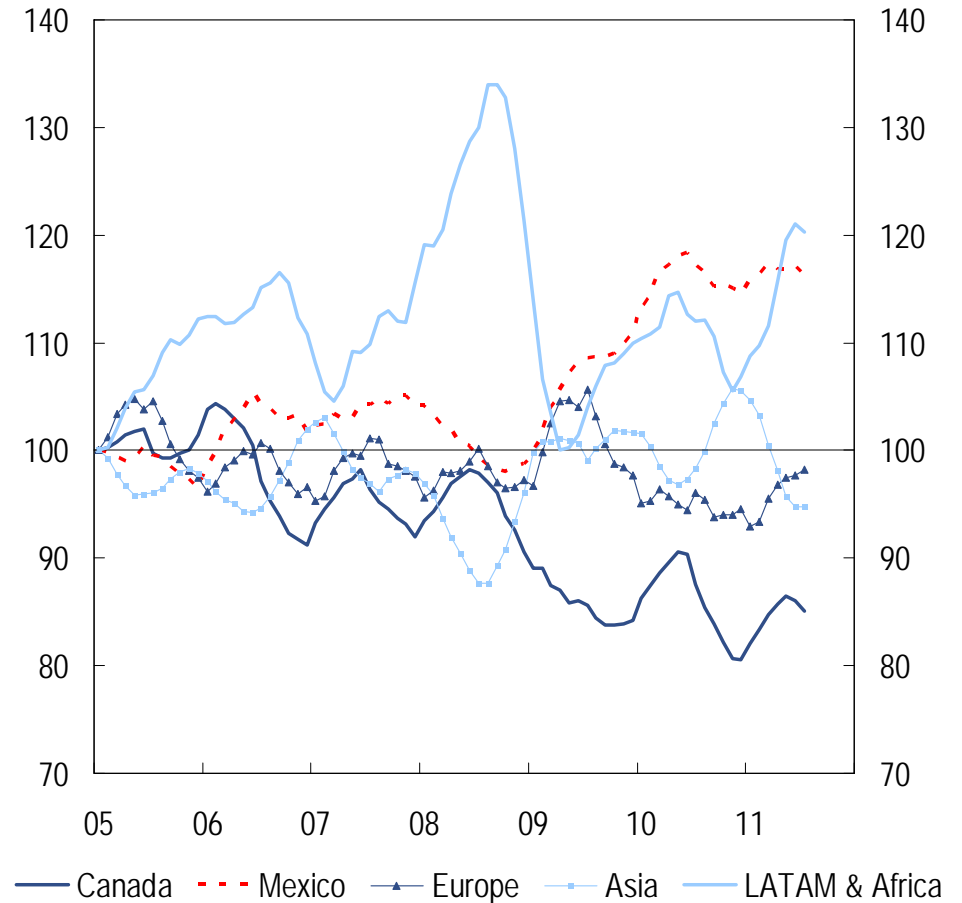
Canada Losing Market Share With the United States

Canada – Exports to U.S. as a Share of Total Canadian Exports (Percent), 1971 – 2011E



Source: Statistics Canada.

United States – Global Imports as a Share of Total (Jan 05 = 100), 2005 – Jul 11



Note: Series are computed by averaging over six months before indexing is applied. Source: Census Bureau.

Reconciliation and Growth

Impediments to Competitiveness: Persistent Currency Strength

Canada – Contributions to Real Exports Growth (Annualized Percent Changes)

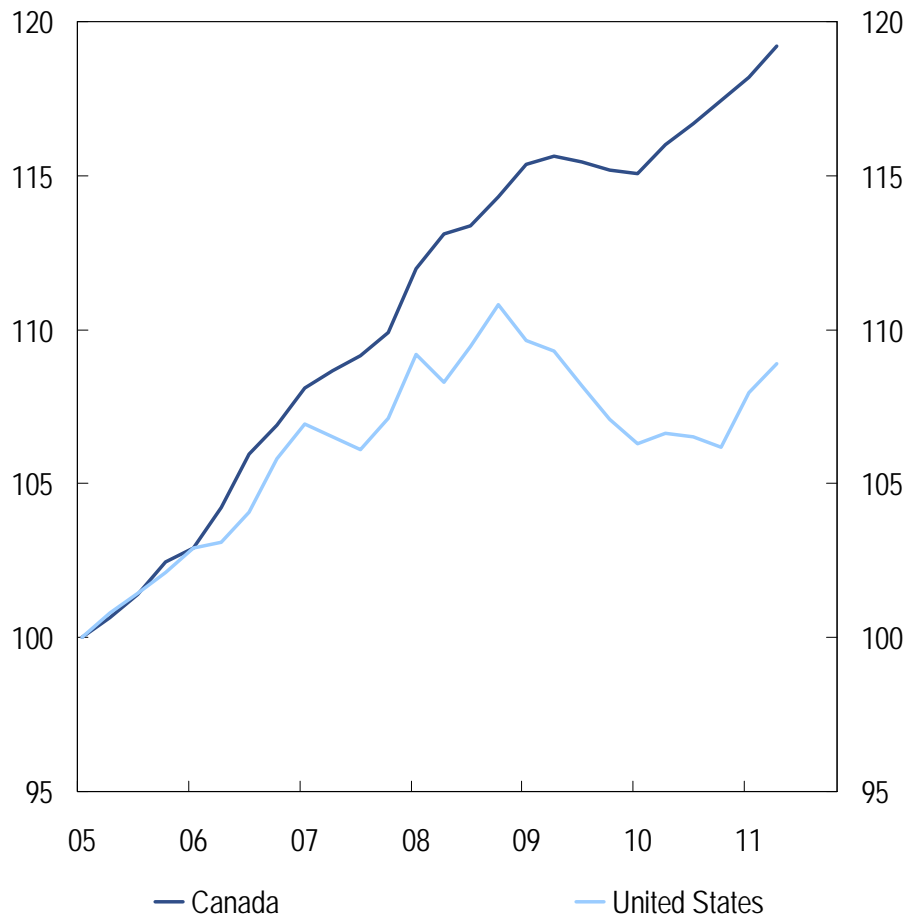
	1	2	3	4
	Pre-Commodity Boom	Extended Commodity Cycle	Recession	Recovery / Expansion
	1998 Q1 - 2002 Q4	2003 Q1 - 2008 Q1	2008 Q2 - 2009 Q2	2009 Q3 - 2011 Q2
Canadian Exports Growth *	4.6	0.6	-14.5	5.5
Growth Forecast by Cayen's Model	4.5	2.0	-3.9	2.2
Contribution of U.S. Demand (C + I + X)	3.6	6.3	-10.8	9.0
Contribution of Real Exchange Rate	0.9	-4.0	7.7	-6.2

* Annualized growth rates

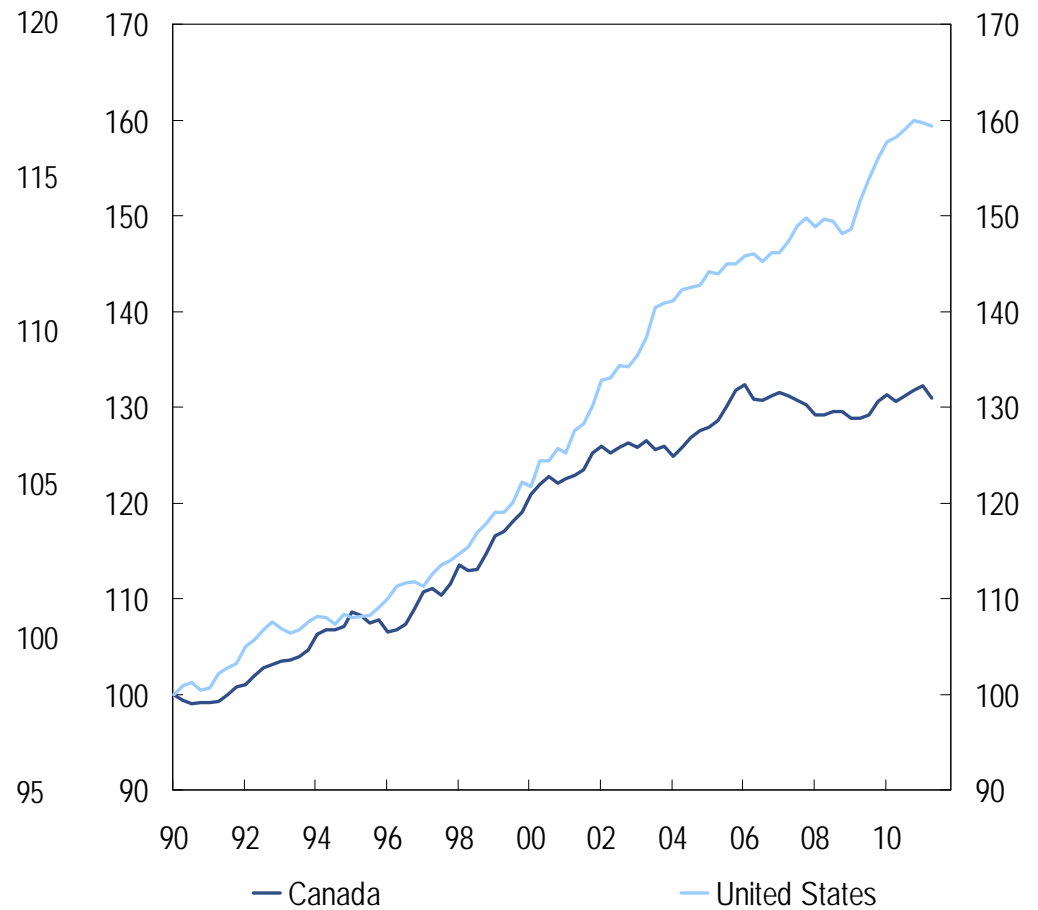
Cayen's error correction model re-estimates for 1973Q1 to 2008Q1 for LN(Real Canadian Exports)		
	Coefficient	t-value
LN(Real Exchange Rate (Citi Real CITERI))	-0.64	-8.86
LN(US Real Consumption)	0.39	3.71
LN(US Real Capex)	0.32	3.06
LN(Real US Exports)	0.41	5.33

Impediments to Competitiveness: Low Productivity; Higher Costs

*Canada and United States – Unit Labor Costs (1Q 05 =100),
2005 – 2Q 11*



*Canada and United States – Productivity Growth (1Q 90 =100),
1990 – 2Q 11*

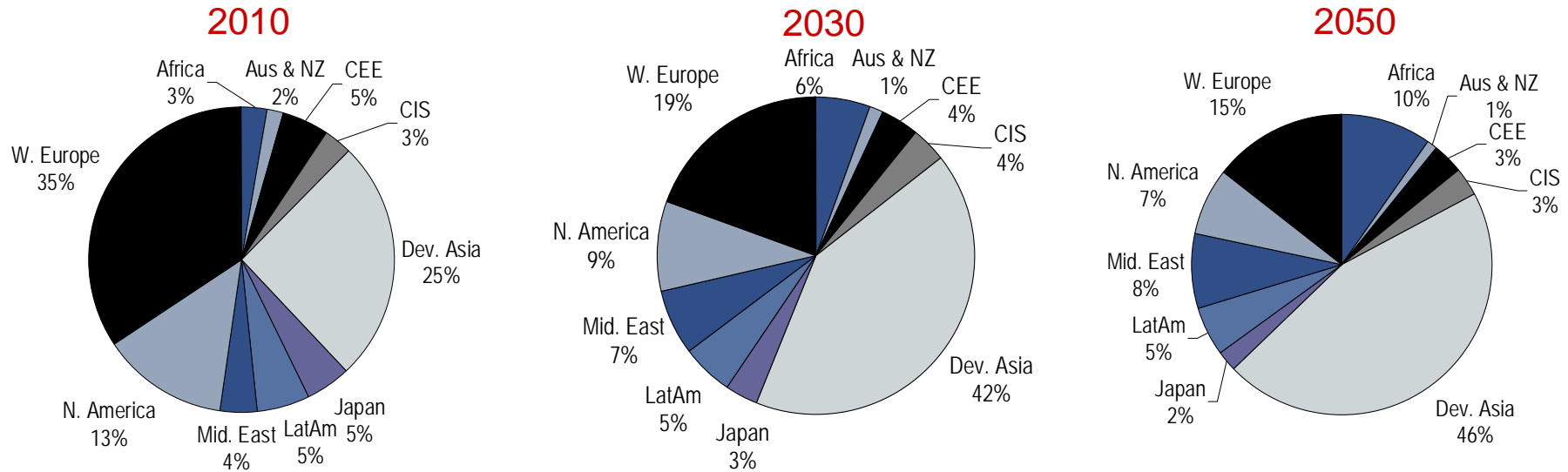


Sources: Statistics Canada and Bureau of Labor Statistics.

Sources: Statistics Canada and Bureau of Labor Statistics.

Shift In Global Trade On The Horizon

Global – Shares of World Trade, 2010, 2030 and 2050



Rank	Country	Trade in 2010	% of World Trade	Rank	Country	Trade in 2015	% of World Trade	Rank	Country	Trade in 2030	% of World Trade	Rank	Country	Trade in 2050	% of World Trade
1	US	4,024	10.7%	1	China	7,754	12.8%	1	China	24,879	16.7%	1	China	63,009	17.0%
2	China	3,579	9.5	2	US	5,794	9.6	2	US	11,290	7.6	2	India	31,074	8.4%
3	Germany	2,865	7.6	3	Germany	3,819	6.3	3	India	7,957	5.3	3	US	21,974	5.9%
4	Japan	1,783	4.8	4	Japan	2,508	4.2	4	Germany	6,367	4.3	4	Korea	11,523	3.1%
5	France	1,433	3.8	5	Korea	2,091	3.5	5	Korea	5,506	3.7	5	Germany	11,174	3.0%
6	UK	1,357	3.6	6	UK	1,861	3.1	6	Japan	4,850	3.3	6	Indonesia	10,581	2.9%
7	Neths	1,310	3.5	7	France	1,840	3.0	7	Singapore	4,121	2.8	7	Thailand	9,064	2.4%
8	Italy	1,146	3.1	8	Neths	1,765	2.9	8	HK	4,102	2.8	8	Japan	8,762	2.4%
9	Korea	1,047	2.8	9	India	1,651	2.7	9	Russia	3,558	2.4	9	Singapore	8,652	2.3%
10	Canada	976	2.6	10	Singapore	1,627	2.7	10	UK	3,439	2.3	10	HK	8,523	2.3%

Note: Trade is defined as sum of goods and services imports and exports. Sources: World Trade Organization and Citi Investment Research and Analysis Estimates from June 2011 Global Economic Outlook and Strategy <https://ir.citi.com/KOfmrHE7ghEVoVWKMmlVXyDBqAAqBEWf4%2Bf64VAGuSxLd0m8HRmw%3D%3D>.

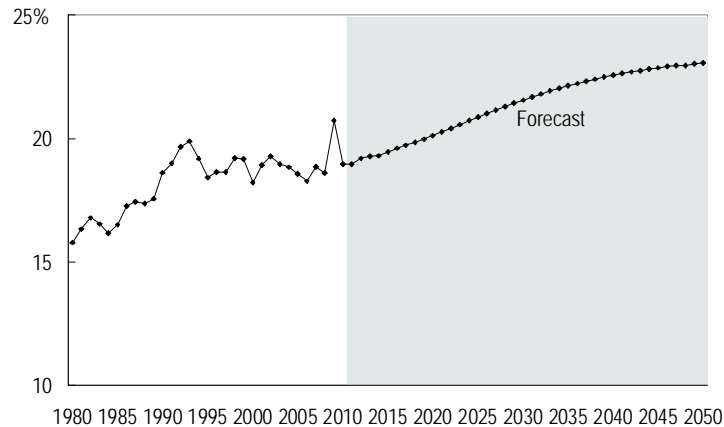
Demographics To Determine Future Trade Corridors

Global – Largest Trade Corridors (in Bil 2010 USD), 2010, 2015, 2020 and 2050

Rank	Trade Corridor	Trade, 2010	% of World Trade	Rank	Trade Corridor	Trade, 2015	% of World Trade	Rank	Trade Corridor	Trade, 2020	% of World Trade	Rank	Trade Corridor	Trade, 2050	% of World Trade
1	W. Europe - W. Europe	7,461	19.91%	1	Dev. Asia - Dev. Asia	9,087	15.05%	1	Dev. Asia - Dev. Asia	14,703	17.79%	1	Dev. Asia - Dev. Asia	88,364	23.82%
2	Dev. Asia - Dev. Asia	3,991	10.65%	2	W. Europe - W. Europe	8,846	14.65%	2	W. Europe - W. Europe	9,739	11.79%	2	Dev. Asia - Mid. East	31,383	8.46%
3	Dev. Asia - W. Europe	3,165	8.44%	3	Dev. Asia - W. Europe	5,667	9.38%	3	Dev. Asia - W. Europe	7,937	9.61%	3	Dev. Asia - W. Europe	30,971	8.35%
4	Dev. Asia - N. America	2,480	6.62%	4	Dev. Asia - N. America	4,331	7.17%	4	Dev. Asia - N. America	6,083	7.36%	4	Africa - Dev. Asia	30,055	8.10%
5	N. America - W. Europe	2,188	5.84%	5	Dev. Asia - Japan	2,767	4.58%	5	Dev. Asia - Mid. East	4,360	5.28%	5	Dev. Asia - N. America	21,519	5.80%
6	Dev. Asia - Japan	1,737	4.64%	6	N. America - W. Europe	2,714	4.49%	6	Dev. Asia - Japan	3,723	4.51%	6	W. Europe - W. Europe	18,457	4.98%
7	LatAm - N. America	1,552	4.14%	7	Dev. Asia - Mid. East	2,605	4.31%	7	N. America - W. Europe	3,122	3.78%	7	Dev. Asia - LatAm	14,035	3.78%
8	Dev. Asia - Mid. East	1,131	3.02%	8	LatAm - N. America	2,187	3.62%	8	LatAm - N. America	2,660	3.22%	8	Africa - W. Europe	12,048	3.25%
9	N. America - N. America	1,093	2.92%	9	Dev. Asia - LatAm	1,594	2.64%	9	Dev. Asia - LatAm	2,432	2.94%	9	Dev. Asia - Japan	11,276	3.04%
10	CEE - W. Europe	986	2.63%	10	N. America - N. America	1,408	2.33%	10	Africa - Dev. Asia	2,036	2.46%	10	CIS - Dev. Asia	9,124	2.46%

What Should Canada Trade and Why?

Global – Share of Services Trade in Total Trade (in %), 1980 – 2050F



Key Drivers of Future Global Trade

- EM GDP Growth, and Catch-up in Productivity and Incomes
- Demographics and EM Middle Class Demand
- Free and Open trade, FDI and Labor Mobility
- Increased/Decreased Protectionism, Taxation
- Commodity Supply/Demand and Prices
- Security and Geopolitical Risks
- Short to Long Term: Capital Goods and Commodities
- Very Long Term: Consumption Goods and Services

Global – Shares of Selected Product Categories in Total Exports and Imports (in %), 2009

	Exports										Imports	
	Agricultural products	Fuels and mining		Manufactures							Fuels	Manufactures
		Total	Fuels	Total	Iron and steel	Chemicals	Office and telecom equipment	Automotive products	Textiles	Clothing		
World	9.6	18.6	14.8	68.6	2.7	11.9	10.9	7.0	1.7	2.6	14.8	68.6
North America	11.2	13.6	9.8	70.5	1.3	12.3	10.8	8.9	0.8	0.6	15.1	73.0
Latin America	30.5	38.9	23.9	27.4	2.7	6.3	1.1	3.3	0.7	2.2	16.5	68.8
Europe	10.5	9.6	6.9	77.3	2.9	17.2	6.7	9.4	1.4	2.2	12.3	70.9
CIS	8.7	62.9	56.3	24.1	8.1	5.9	0.4	0.8	0.4	0.3	10.1	72.6
Africa	10.2	64.0	55.3	19.2	1.8	3.7	0.6	1.4	0.6	2.5	11.5	69.5
Middle East	2.6	68.0	66.8	27.3	0.7	6.3	2.9	2.7	1.1	0.8	7.2	77.0
Asia	6.3	10.8	7.4	79.7	2.7	7.7	22.0	5.3	3.1	4.7	19.6	62.8

Source: Citi Investment Research and Analysis Estimates from June 2011 Global Economic Outlook and Strategy

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Infrastructure And Trade Policies Present Major Hurdles

Canada – Potential Tax Receipts as a Result of Alberta Oil Sands Investments and Operations (Million C\$, Sum over 2010 – 2035)

	Existing Pipelines and Operations	+ TransCanada Keystone EX Pipeline	+ Northern Gateway Pipeline	+ Announced & Potential Capacity
Alberta	442,956	565,218	646,048	954,350
BC	7,660	9,944	11,297	16,972
Manitoba	1,208	1,582	1,796	2,715
New Brunswick	230	300	340	513
NFL & Labrador	77	101	114	172
NW Territories	29	38	43	65
Nov Scotia	270	351	398	599
Nunavut	4	6	6	10
Ontario	21,308	27,506	31,263	46,785
PEI	20	27	30	46
Quebec	5,219	6,759	7,680	11,518
Saskatchewan	1,412	1,883	2,135	3,266
Yukon Territory	7	9	11	16

Source: Canada Energy Research Institute: Economic Impacts of Staged Development of Oil Sands Projects in Alberta (2010-2035).

Canada – Free Trade Agreements and Negotiations

Nation/Organization	In Force Date/Status
World Trade Organization Membership	1/1/1995
North America Free Trade Agreement (U.S. and Mexico)	1/1/1994
Panama	Signed 5/14/2010
Jordan	Signed 6/28/2009
Columbia	Signed 11/21/2008
Peru	8/1/2009
European	7/1/2009
Costa Rica	11/1/2002
Chile	7/5/1997
Israel	1/1/1997
Possible Negotiations: Turkey	Pending
Ukraine	Pending
Launch of Negotiations: Morocco	Pending
EU: Comprehensive Economic and Trade Agreement	Pending
Korea	Pending
Andean Community Countries	Pending
Caribbean Community	Pending
Dominican Republic	Pending
Central America Four (CA4)	Pending
Launch of Negotiations: India	Pending (July 2011)
Singapore	Pending
Free Trade Area of the Americas (FTAA)	Pending
Modernize Agreement: Costa Rica	Pending
Honduras Free Trade Negotiations	Pending

Source: Foreign Affairs and International Trade Canada.



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Canada Economic Overview

Canada Economic Overview

- The outlook for the Canadian economy is now somewhat negative. Eroding confidence, dimming global economic prospects and financial market turmoil prompted further downgrading of the medium-term projection.
- The threat of a European recession, a tepid U.S. expansion, and a weaker profile for commodity prices all suggest sub-trend domestic growth through 2013.
- Near-term depreciation of the Canadian dollar will create some offset, but ongoing competitiveness woes will continue to weigh on exports.
- Narrower job gains, government layoffs and increased joblessness are likely given moderate growth prospects and downside risks. The unemployment rate probably will rise near-term amid tepid economic activity.
- Lackluster wage growth, cooling housing activity and outsized financial market losses probably will squeeze incomes and subsequently consumer spending. The capex revival could falter on flagging business sentiment.
- Food and energy costs, as well as residual effects of provincial tax amendments last year, probably will keep overall consumer inflation above 2% near term. This gauge should return to the central bank's 2% target by mid-2012.
- Underlying consumer costs will rise as Harmonized Sales Tax effects wane. However, higher costs for food may briefly push core inflation above 2% in the second half of this year before converging to 2% by mid-2012.
- Risks to the Canadian inflation outlook are two-sided, but tilted to the downside.
- The central bank is likely to keep interest rates at extraordinarily accommodative levels until early 2013.

Outlook Highlights

➤ **Upside risks** include higher commodity prices and global inflation fueled by EM demand; greater-than-projected momentum in the Canadian household sector due to faster earned income growth or persistent borrowing; and the possibility that the Canadian economy is operating closer to its production potential.

➤ **Downside risks** to the inflation outlook include the bank and sovereign debt crises in the Euro Area, Canada's reduced competitiveness caused by the strong CAD and low productivity; weaker-than-expected household expenditures due to rising debt, deleveraging, modest earned income growth, and reduced housing wealth.

➤ **Risks Balance:** U.S. political risks are likely to intensify in the months ahead. Our economists now anticipate a recession in the EA amid multiple defaults in the periphery. Canadian risks are tilted to the downside.

➤ **Policy Response:** The Bank of Canada softened its stance in order to apply additional monetary policy stimulus in reaction to deterioration in financial markets and threats to global growth. The central bank is likely to keep rates unchanged until early 2013. New fiscal policy is unlikely.

Canadian Economic Outlook Highlights (Annualized Percent Change Unless Noted), 2010-2012F

					2011				2012			
		2010	2011F	2012F	1Q	2Q	3QF	4QF	1QF	2QF	3QF	4QF
Real GDP	YoY	3.2	2.1	1.8	2.9	2.2	1.8	1.5	1.1	1.7	2.1	2.2
	SAAR				3.6	-0.4	1.0	2.0	1.9	2.0	2.5	2.3
Final Domestic Demand	YoY	4.5	2.9	1.8	3.7	3.5	2.6	1.8	1.8	1.5	1.9	2.1
	SAAR				1.8	3.0	0.9	1.5	1.8	1.9	2.4	2.4
Private Consumption	YoY	3.3	1.8	2.0	2.1	2.2	1.8	1.2	1.8	1.9	2.1	2.2
	SAAR				-0.1	1.6	1.5	1.8	2.2	2.1	2.4	2.2
Government Spending	YoY	4.7	0.9	-1.6	2.9	2.0	0.2	-1.4	-1.9	-2.5	-1.5	-0.6
	SAAR				0.2	1.5	-4.2	-3.1	-1.7	-0.8	-0.2	0.2
Private Fixed Investment	YoY	8.4	8.8	5.3	10.1	10.0	7.8	7.5	6.0	4.7	5.4	5.1
	SAAR				10.8	9.7	3.1	6.6	4.8	4.4	5.6	5.7
Exports	YoY	6.4	3.8	4.0	6.7	1.5	4.3	3.0	2.0	5.4	4.1	4.4
	SAAR				7.7	-8.3	10.1	3.5	3.8	4.4	4.8	4.7
Imports	YoY	13.1	6.5	3.3	9.5	6.8	4.6	5.2	3.6	2.2	3.4	4.0
	SAAR				9.5	10.0	-0.3	2.0	3.0	4.0	4.5	4.5
Consumer Price Index	YoY	1.8	2.8	2.0	2.6	3.4	2.8	2.5	2.3	1.8	2.0	2.0
Core CPI		1.7	1.7	2.0	1.3	1.6	1.7	2.0	2.2	2.0	2.0	1.9
Unemployment Rate	%	8.0	7.5	7.3	7.8	7.5	7.3	7.4	7.6	7.4	7.1	7.1
Current Account Balance (SAAR)	CAD bn	-50.9	-56.8	-61.2	-40.3	-61.3	-60.5	-65.2	-61.3	-65.4	-61.4	-56.6
	% of GDP	-3.1	-3.3	-3.5	-2.4	-3.6	-3.6	-3.8	-3.5	-3.7	-3.5	-3.2
Net Exports Contribution		-3.1	-1.5	-0.1	-0.6	-5.7	3.4	0.3	0.0	-0.3	-0.4	-0.4
Inventories Contribution		0.7	0.3	0.0	2.2	2.5	-2.0	0.0	0.0	0.2	0.2	0.1
Budget Balance (Fiscal Year)	% of GDP	-2.2	-1.9	-1.1								
Federal Budget Debt	% of GDP	33.6	34.2	34.0								

F Citi forecast. YoY Year-to-year percent change. SAAR Seasonally adjusted annual rate.
Source: Statistics Canada and Citi Investment Research and Analysis.

Long-Term Outlook

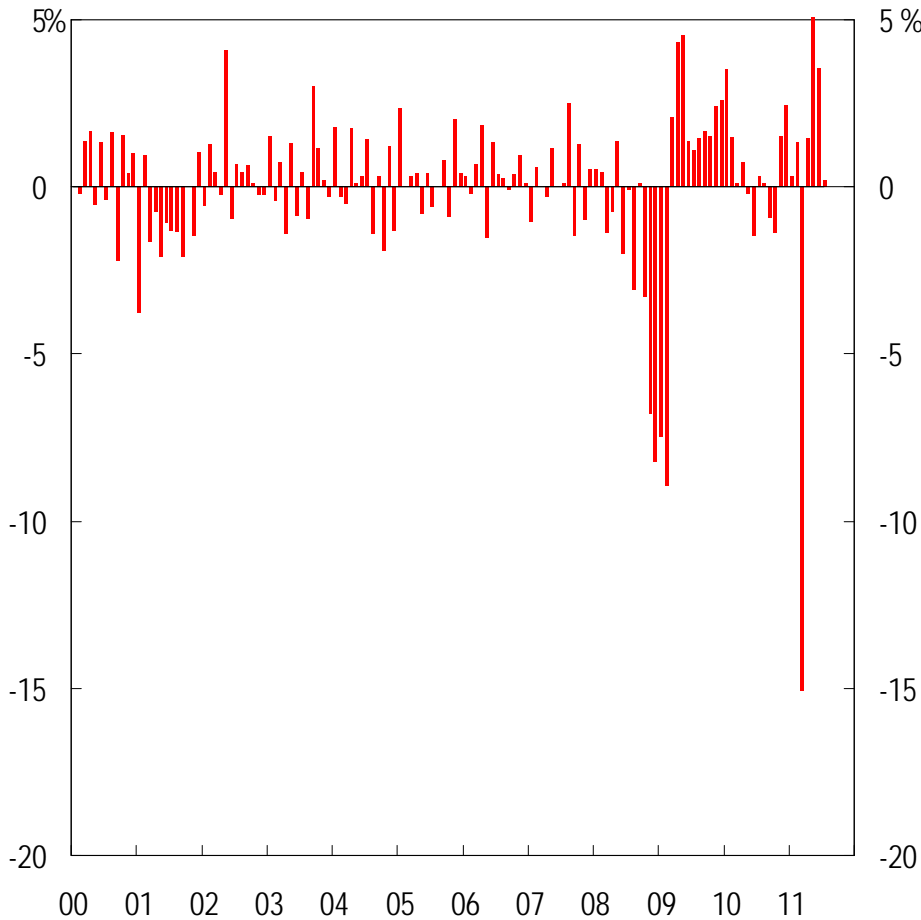
Citi Canadian Long-Term Forecast Projections

LONG TERM		2010	2011	2012	2013	2014	2015
Real GDP	YoY	3.2	2.1	1.8	2.3	2.5	2.8
Total CPI	YoY	1.8	2.8	2.0	2.0	2.0	2.0
Core CPI	YoY	1.7	1.7	2.0	2.0	2.0	2.0
Short-Term Interest Rates	%	0.69	1.00	1.00	1.63	2.19	2.50
Unemployment Rate	%	8.0	7.5	7.3	6.9	6.5	6.0
Industrial Production	YoY	4.6	0.8	-1.0	0.4	0.6	1.3
Budget Balance	% of GDP	-2.2	-1.9	-1.1	-0.5	0.0	0.2
CAD/USD	C\$	1.03	1.01	1.01	0.96	0.96	0.97

Source: Citi Investment Research and Analysis.

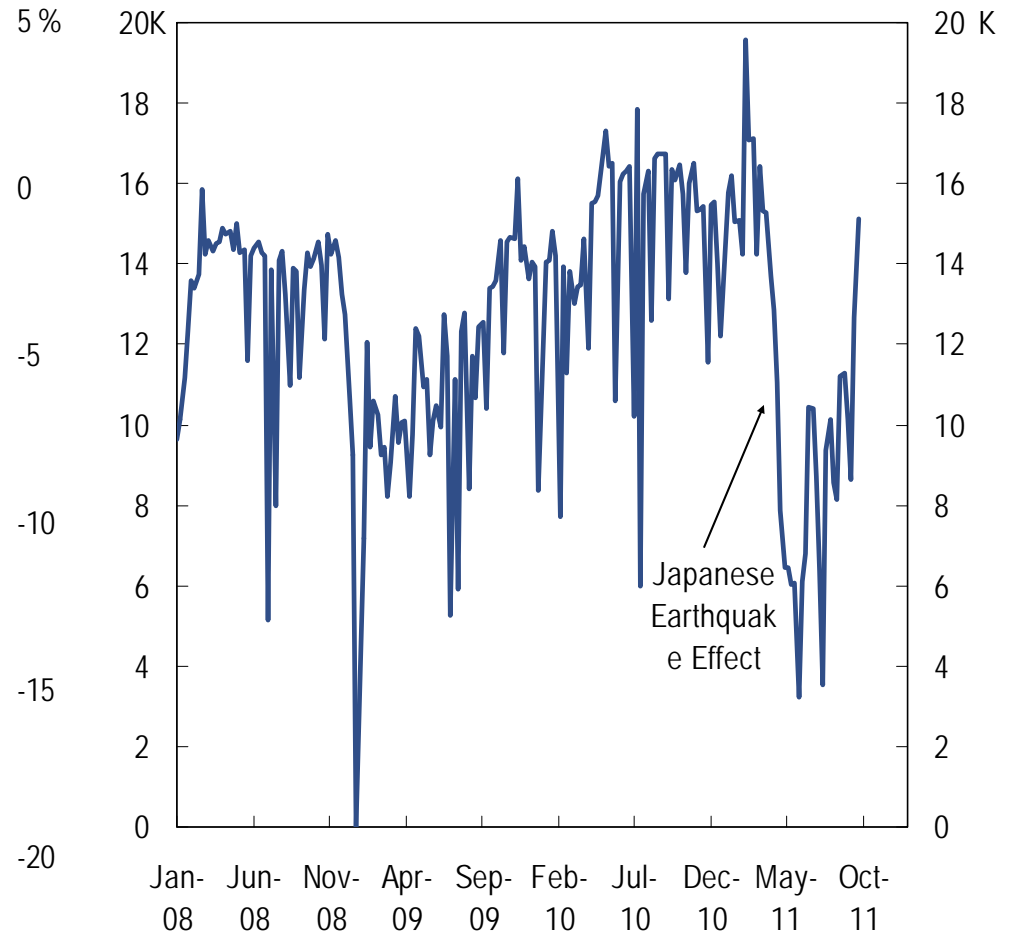
The Global Supply Chain Normalization Is Near Completion

Japanese Industrial Production (Percent Change), 2000 – Jul 11



Source: Japanese Ministry of Economy, Trade & Industry.

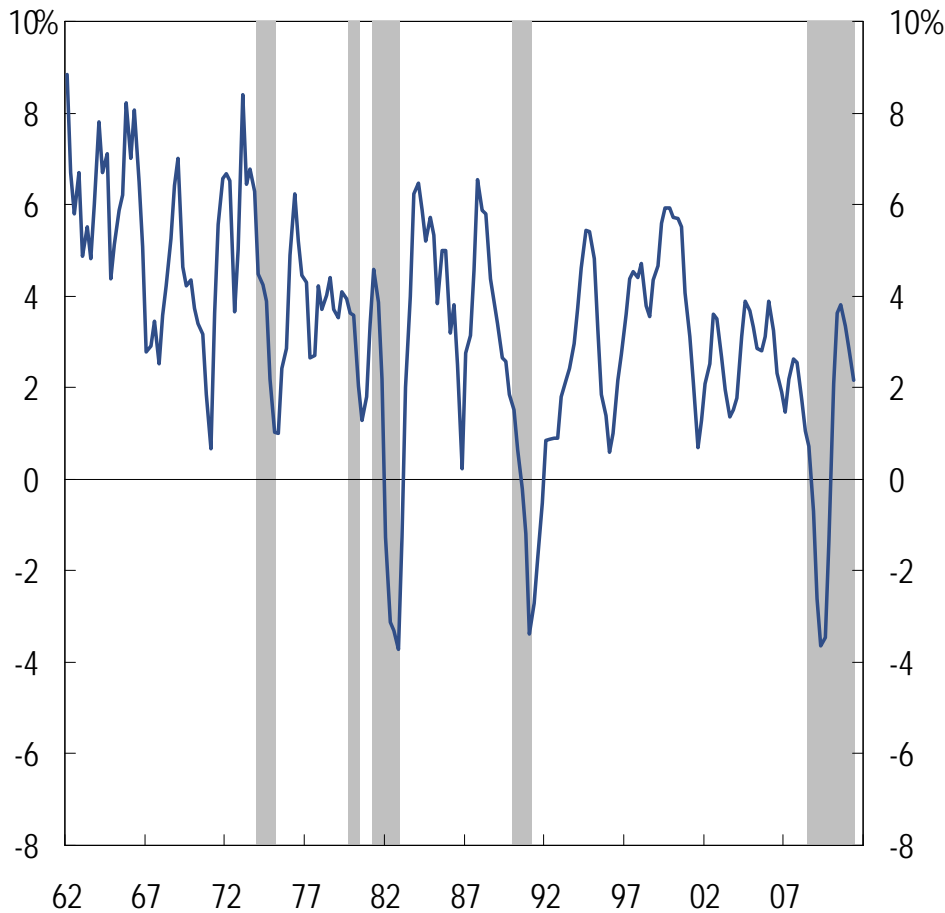
Canadian Production of Honda and Toyota Cars and Trucks (Thousands of Units), 2008 – 24 Sep 11



Source: *Automotive News*.

Canadian Fundamentals Relatively Sound

Real GDP (Yr-to-Yr Percent Change), 1962 – 2Q 11



Note: Shaded regions denote Canadian recessions. Source: Statistics Canada.

BoC Financial Conditions Index, 1999 – 9 Sep 11

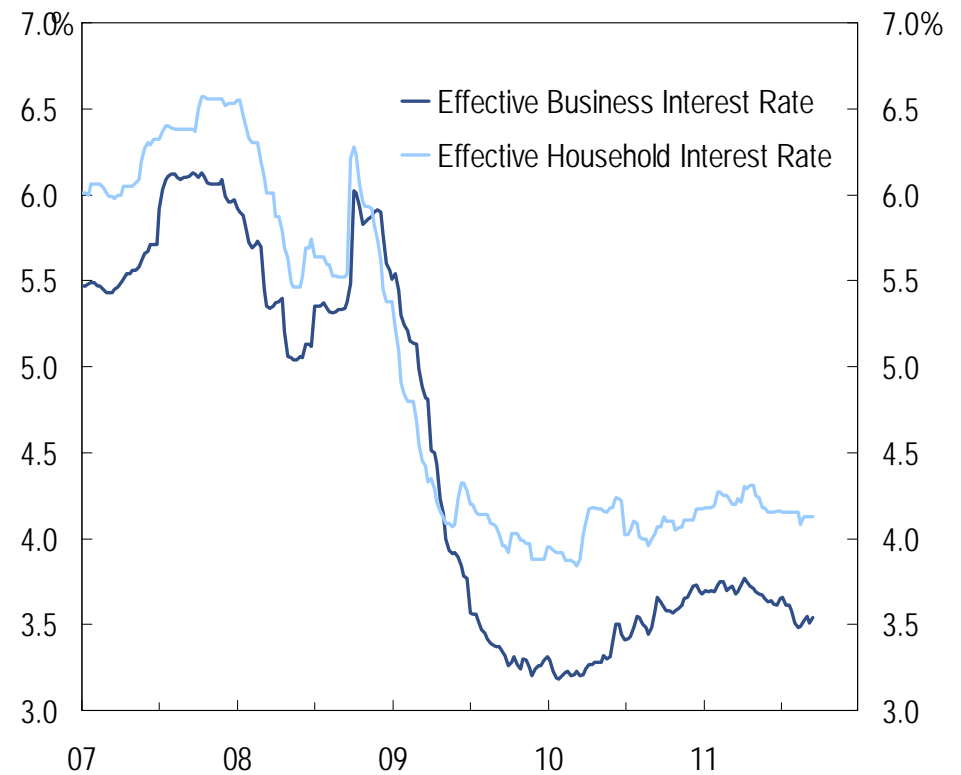
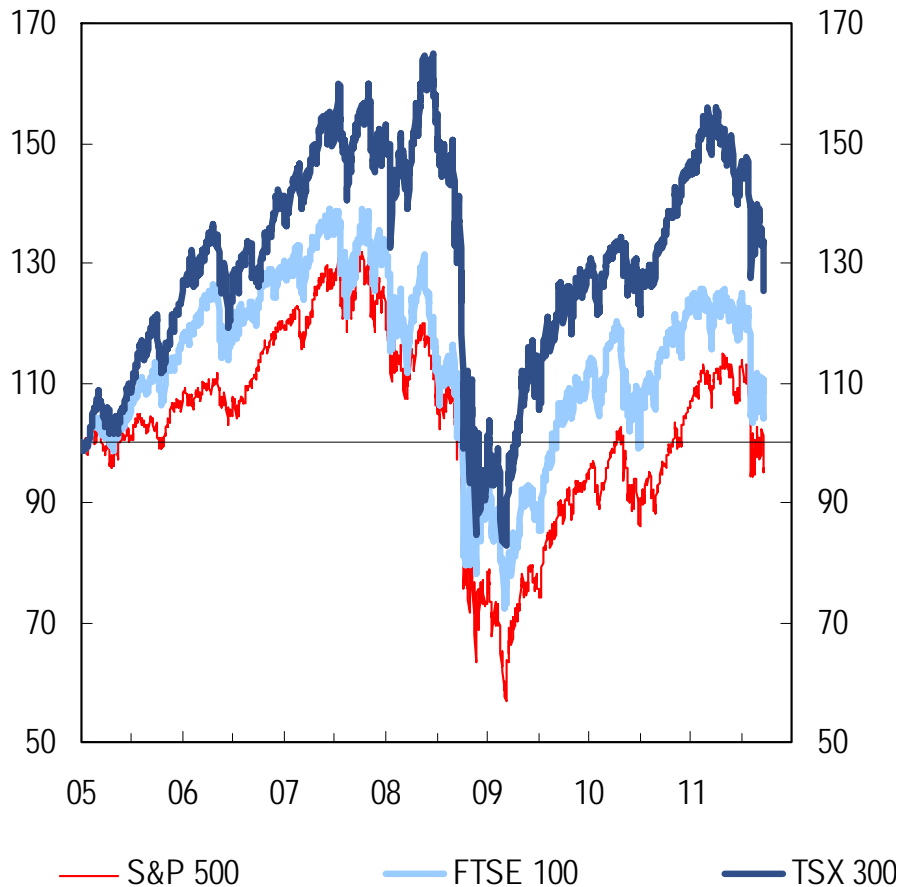


Note: The Bank of Canada FCI is a weighted average of credit conditions, corporate bond spread, short- and long-term interest rate, real exchange rate, equity, and housing prices variables. Sources: Statistics Canada and Bank of Canada. Source: Bank of Canada.

Financial Conditions Erosion In Equities Not Credit

*Global – Various Stock Exchanges (Rebase 15 Feb 05 = 100),
2005 – 23 Sep 11*

*Canada – BoC Effective Lending Rates (Percent),
2007 – 16 Sep 11*

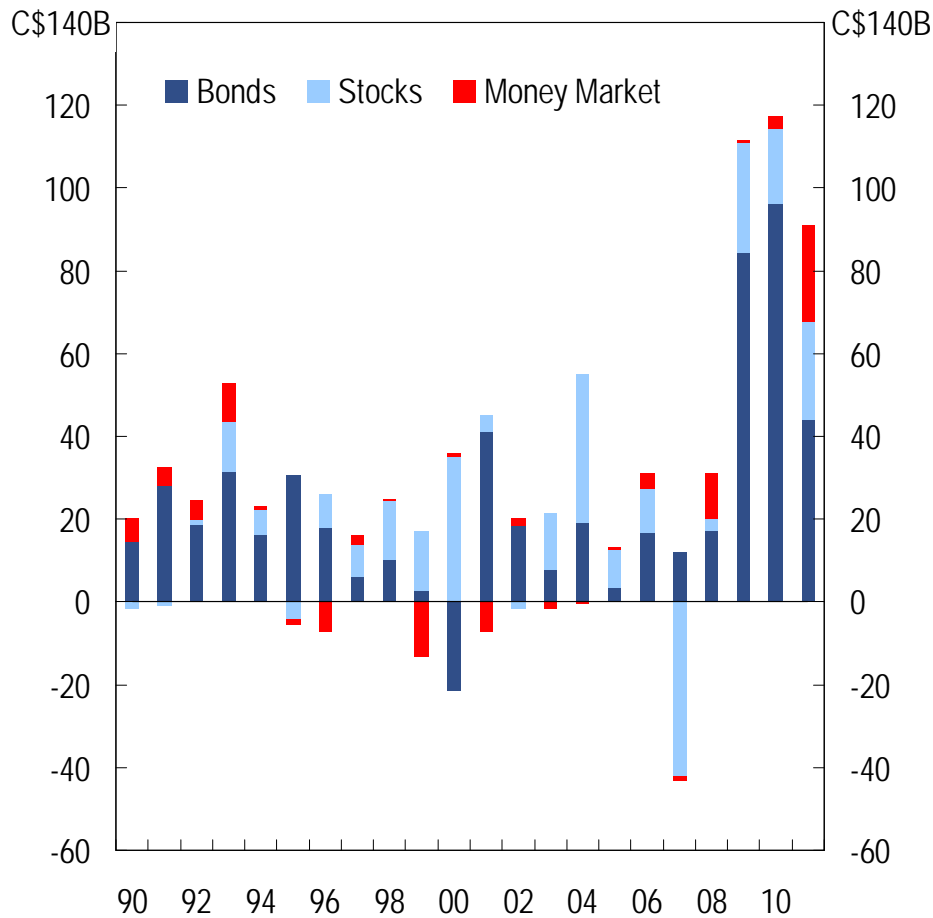


Sources: Financial Times, New York Times, and Wall Street Journal.

Note: The effective interest rate for households is a weighted-average of various mortgage and consumer credit interest rates. The weights are derived from residential mortgage and consumer credit data, adjusted for additional information provided by financial institutions. The effective interest rate for businesses is a weighted-average borrowing rate for new lending to non-financial businesses, estimated as a function of bank and market interest rates. The weights are derived from business credit data.
Source: Bank of Canada.

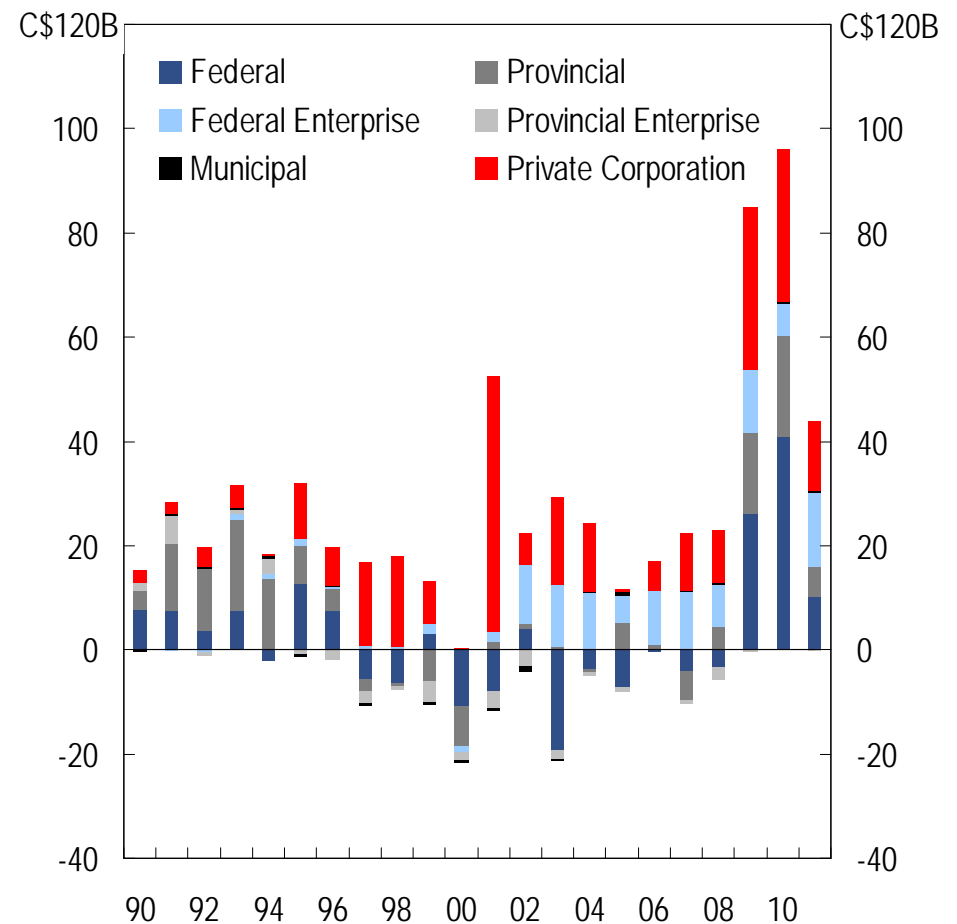
Canada Persists As An Investor's Safe Haven

Canada – Net Portfolio Securities Inflows by Type, 1990 – Jul 11



Source: Statistics Canada.

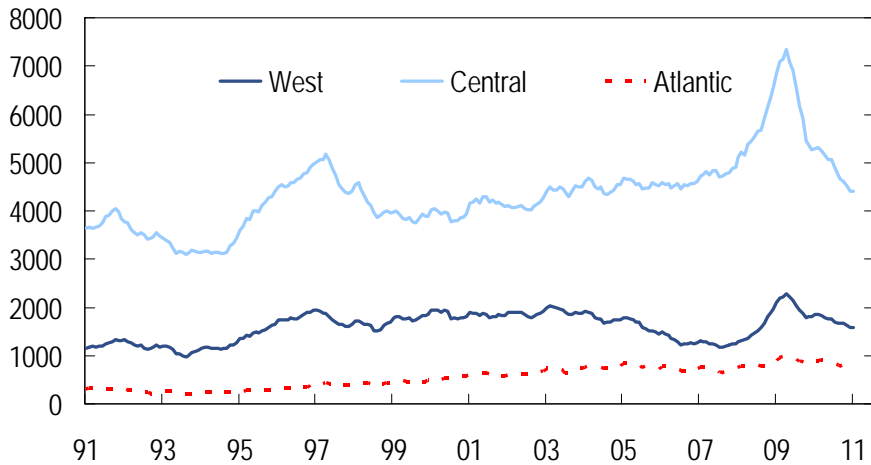
Canada – Net Portfolio Securities Inflows: Bonds, 1990 – Jul 11



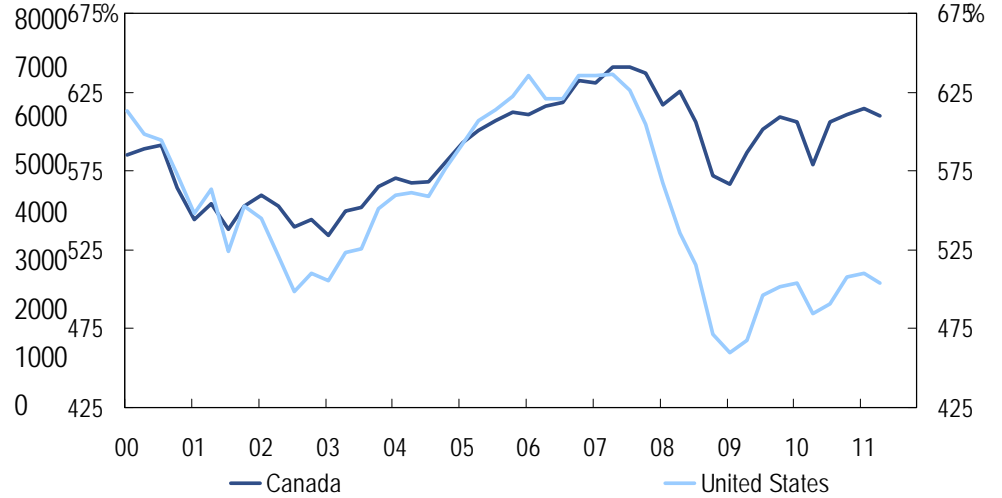
Source: Statistics Canada.

Favorable Financial Disposition; Modest Deleveraging

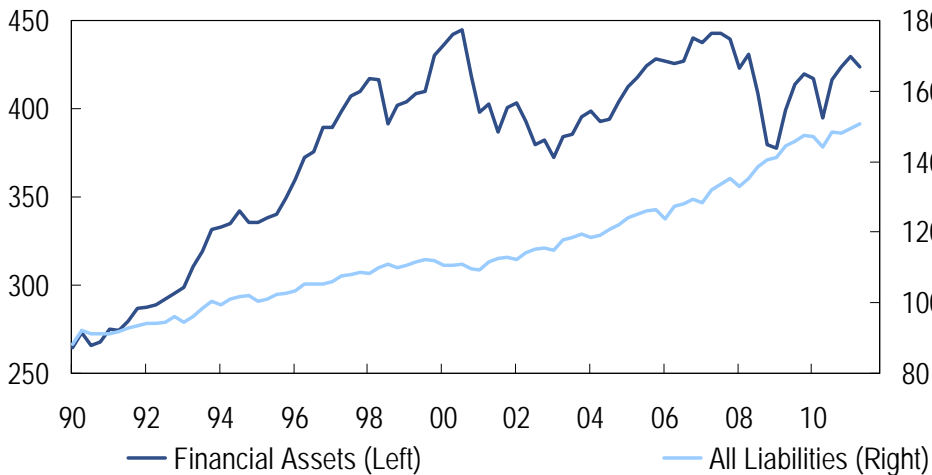
Consumer Bankruptcies: 6-Mo. Moving Avg (Number), 1991 – Jun 11



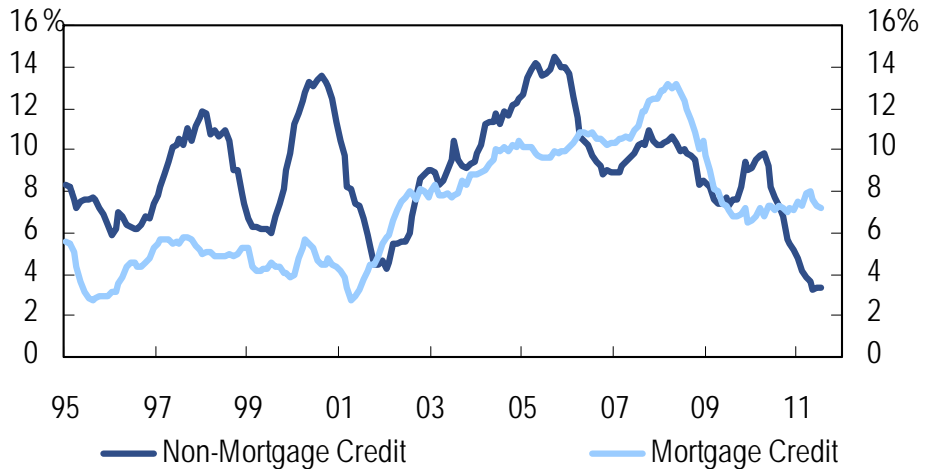
Household Net Worth as a % of Disposable Personal Income, 2000 – 2Q 11



Household Finances (Percent of Disposable Income), 1990 – 2Q 11



Consumer Credit (Y/Y%), 1995 – Jul 11



Sources: Statistics Canada and Federal Reserve Board.

Risks to the Outlook

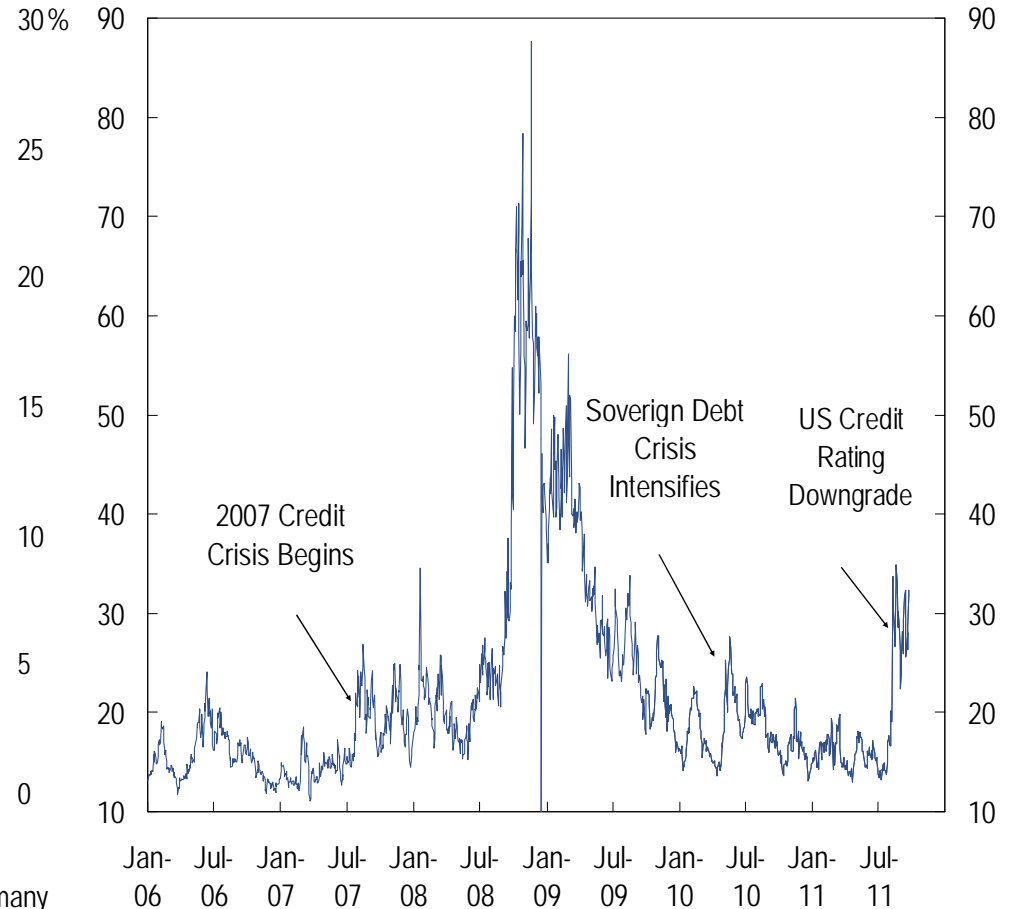
EA Sovereign and Bank Crises, US Politics Overshadow Outlook

Ten-Year Government Bond Yields, 2010 – 23 Sep 11



Source: Bloomberg.

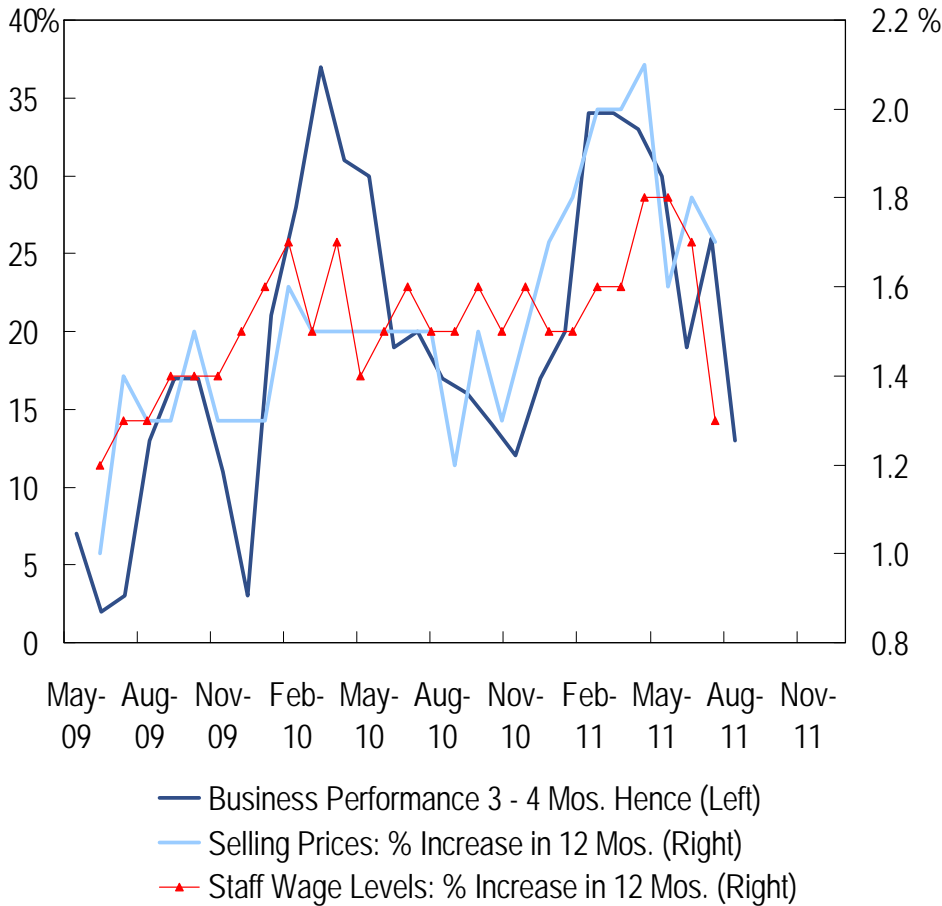
Canada – Implied Volatility Index, 2006 – 23 Sep 11



Sources: Statistics Canada, CIRA-Economics and IMF.

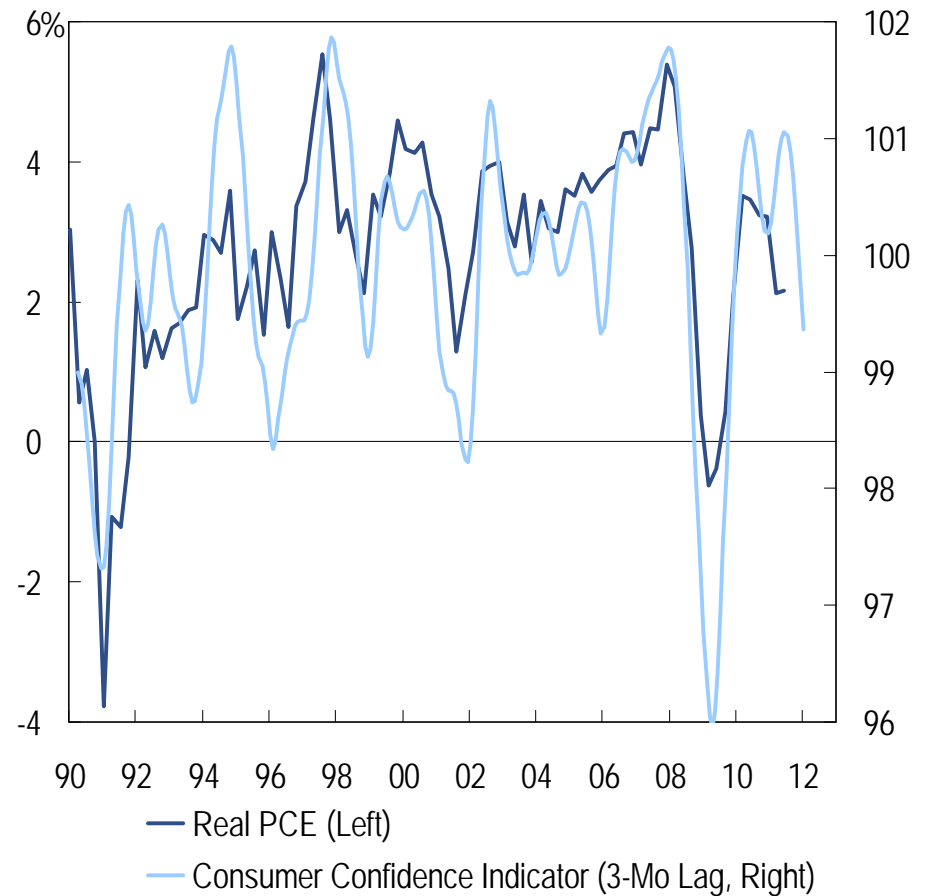
Flagging Confidence Threatens To Become Self-fulfilling

Canada – Small Business Performance (Balance of Opinion) and Inflation Expectations, 2009 – Aug 11



Source: Canadian Federation of Independent Business.

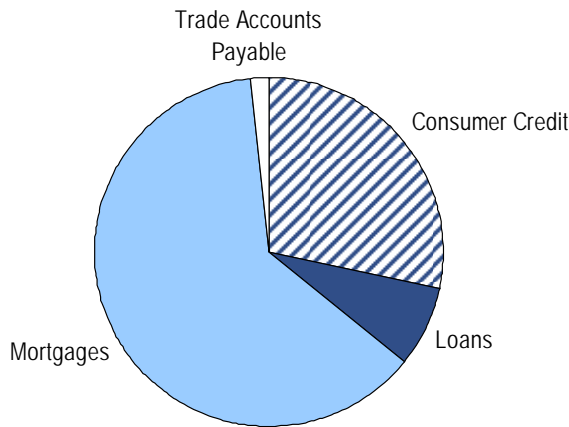
Real PCE (Y/Y%) and OCED Consumer Confidence Indicator (Normalized), 1990 – Oct 11



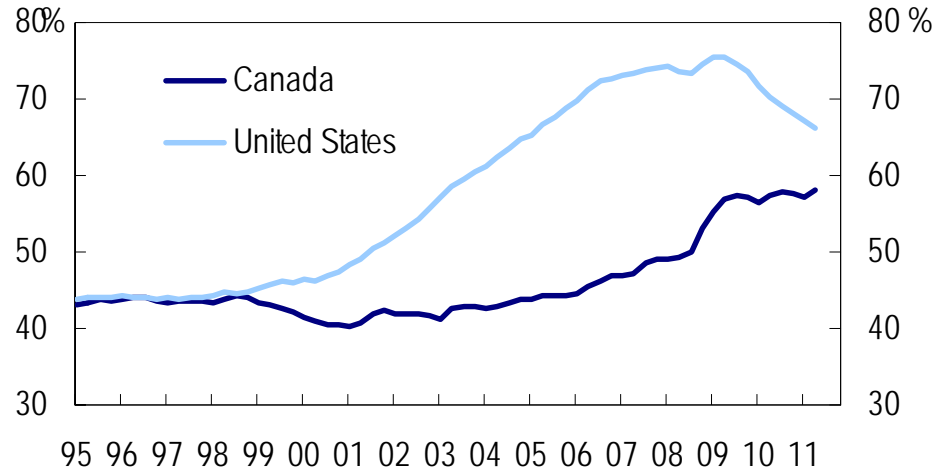
Source: Statistics Canada and Organization for Economic Cooperation & Development.

Domestic Household Debt Accumulation Strains Balance Sheets

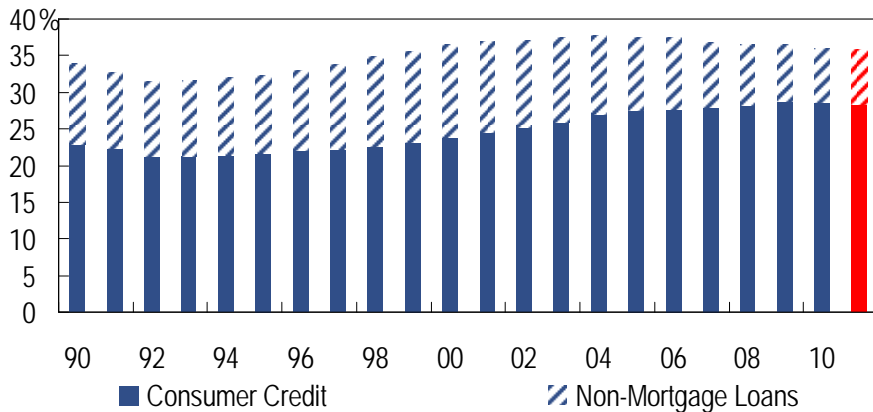
Household Liabilities as a % of Total Obligations, 2011E



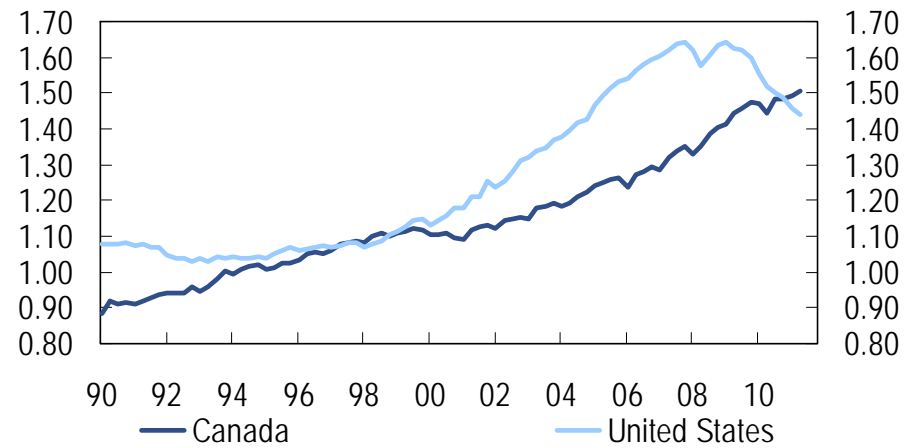
Mortgage Debt (Percent of GDP), 1995 – 2Q 11



Credit and Loans as a % of Total Obligations, 1990 – 1Q 11E



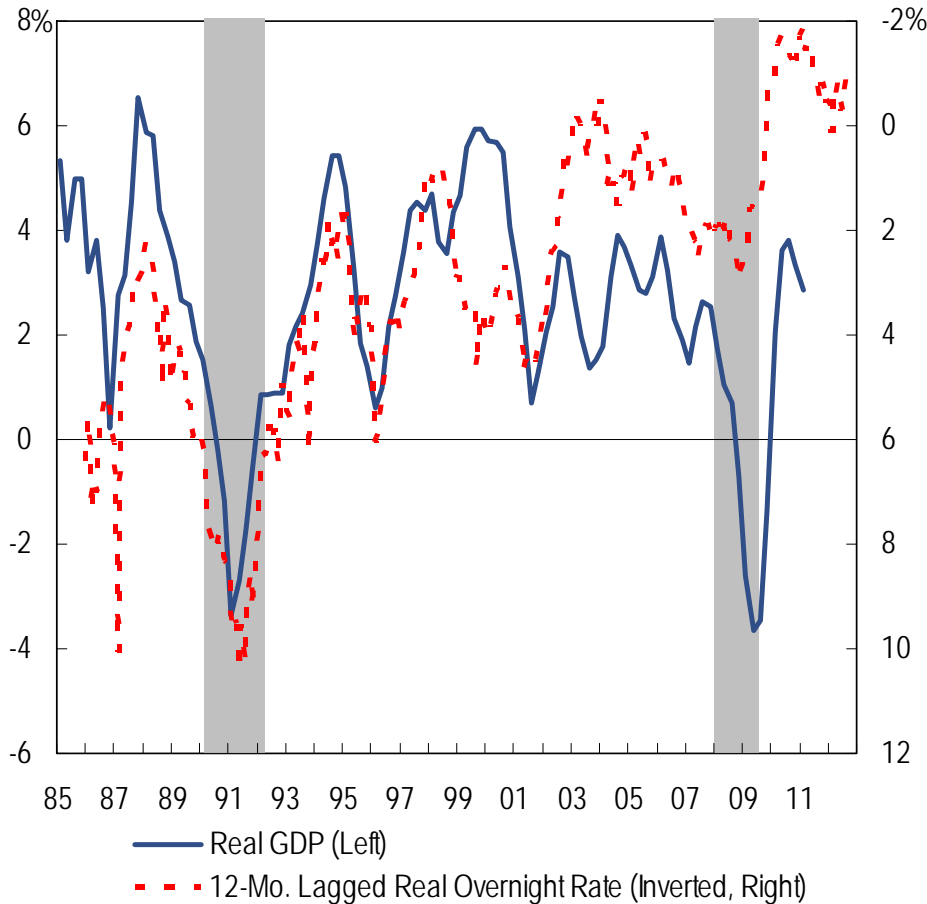
Household and Proprietor Debt to Disposable Income Ratio, 1990 – 2Q 11



Sources: Statistics Canada and Federal Reserve Board.

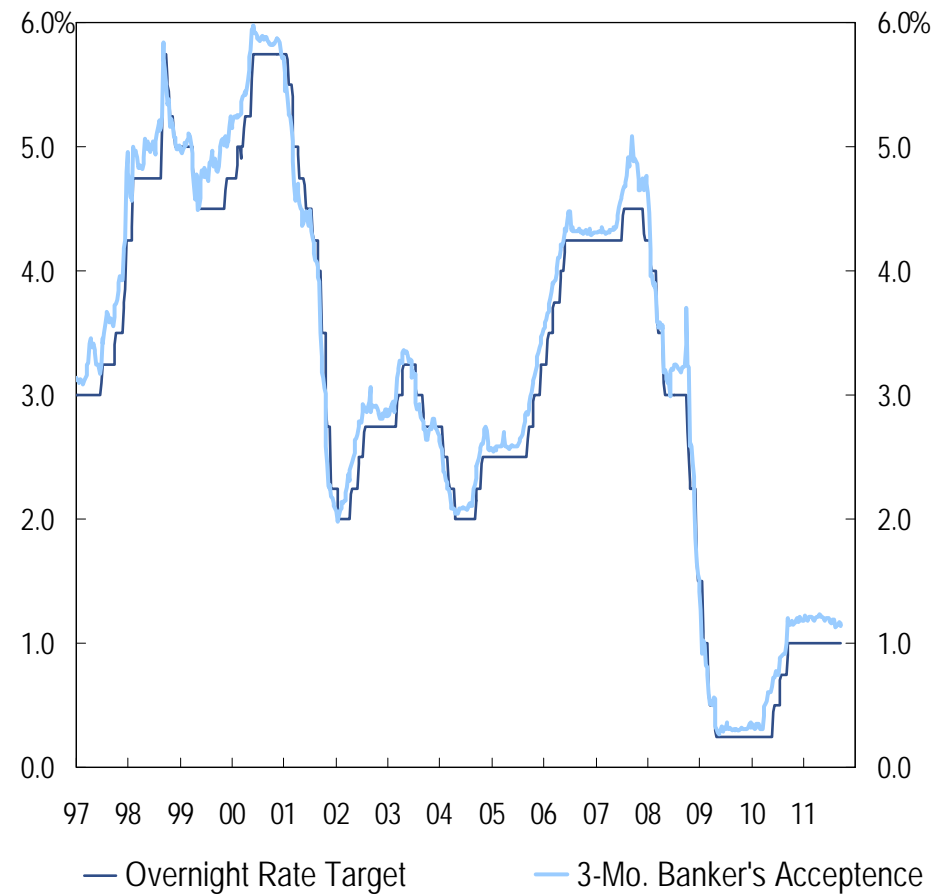
An Extraordinarily Accommodative Monetary Policy Stance

Real GDP (Y/Y Pct Change) vs. Real Overnight Rate (Percent), 1985 – Sep 11



Note: Shaded regions denote Canadian Recessions. Sources: Bank of Canada and Statistics Canada.

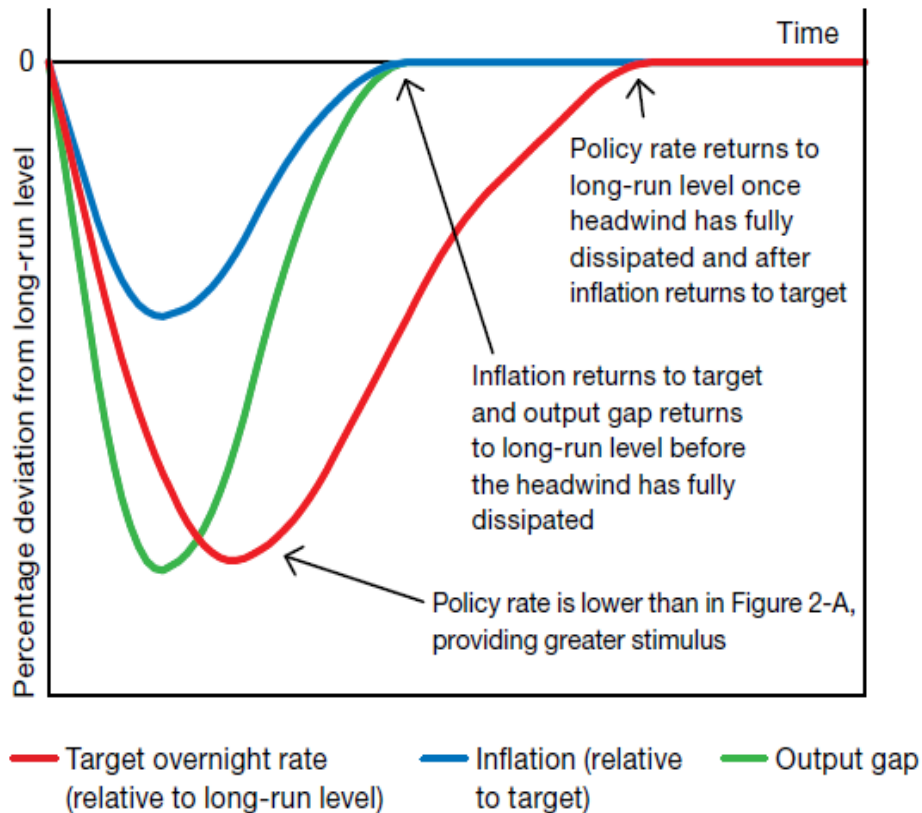
Policy Rate Target: History and BA Yields, 1997 – Sep 11



Sources: Bank of Canada and Bloomberg.

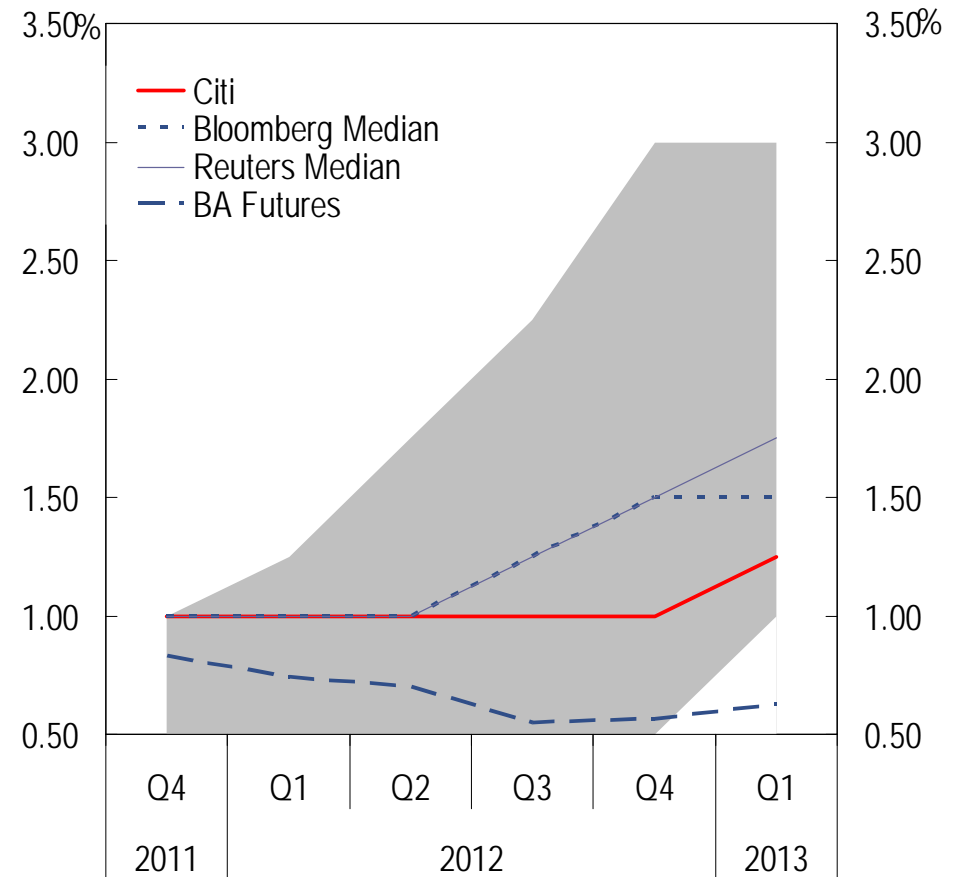
Policy Normalization Likely Protracted; BoC To Remain On Hold

Bank of Canada: "Impact of Foreign Demand Headwinds with a More Appropriate Policy Response"



Sources: Bank of Canada, July *Monetary Policy Report*.

BoC Policy Rate Target Expectations, as of 6 Oct 11



Note: Surveys pre-September meeting. BA yields as of 26 Sep 11.
Sources: Reuters, Bloomberg and CIRA-Economics.



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