

Q. Evidence of Ms. McShane Page 42

- (a) Please update Ms McShane's long Canada forecast for 2009 and 2010 and provide the referenced pages from the Consensus forecast.
- (b) Is it Ms. McShane's judgment that the Consensus Economics forecast has been and is an accurate forecast of the future long Canada yield if so please provide the evidentiary basis for this.
- (c) Please indicate why the best forecast for next year's 30 year yield cannot be obtained from the current yield curve?

A. (a) The average yield on long-term Canada bonds for the first six months of 2009 has been 3.8%. The three-month forward Consensus Forecast 10-year Government of Canada forecast as of June 2009 is 3.3% and the recent spread between 10-year and 30-year Canada bond yields has been approximately 0.50% indicating a long-term Canada forecast of approximately 3.8%. Based on the actual yields and the 3.8% forecast three months forward, the average yield for 2009 would be 3.8%.

For 2010, the 12 month forward forecast of 10-year Canada bonds is 3.8%. With an unchanged spread of 0.50%, the forecast 30-year Canada for 2010 is approximately 4.3%. The relevant pages from the June 2009 consensus forecast are attached as Attachment A.

- (b) As utilized to estimate the following year's actual average yield, the consensus forecasts have produced estimates of the 30-year Government of Canada bond yield which have been approximately 0.40% higher than the actual 30-year yields from 1995-2008. Since movements in interest rates are a function of multiple underlying variables, including the state of the domestic and global economies, monetary and fiscal policy, and not inconsequentially, human behaviour, forecasts of interest rates (as with any other variable) are subject to forecast error. Given the decline in long-term Canada bond yields from close to 9.5% in 1995 to less than 3.5% in 2008, an average difference between the actuals and forecasts of less than 0.50% suggests that the forecasts have been reasonably accurate on average.
- (c) While estimating forward yields from the spot yield curve is an alternative to relying on a consensus forecast, there is no a priori reason that that approach will turn out to have been a better forecast than the consensus. Further, the construction of a forward yield from a 'spot' yield curve is not practicable because (1) the yield curve between 10 and 30 years is an interpolation and (2) there are no Government of Canada bonds longer term than 30 years from which to estimate the 30-year forward yield. Any risk premium analysis, which is forward looking, should reflect investors' outlook for interest rates. The consensus forecast is a transparent means of representing investors' expectations for the long-term Canada bond yield.

Consensus Forecasts
June 8, 2009

CONSENSUS FORECASTS

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**Survey Date
June 8, 2009**

Every month, Consensus Economics surveys over 240 prominent financial and economic forecasters for their estimates of a range of variables including future growth, inflation, interest rates and exchange rates. More than 20 countries are covered and the reference data, together with analysis and polls on topical issues, is rushed to subscribers by express mail and e-mail.

Survey Highlights

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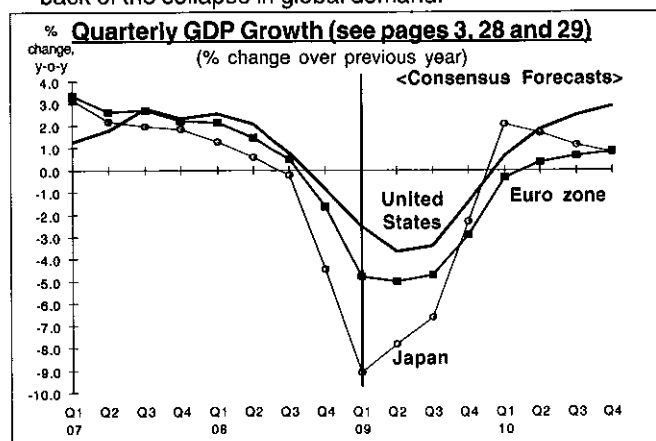
United States – Quarterly Real GDP Consensus Forecasts in December 2008 and March and June 2009

% change, y-o-y	2009				2010			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
June 8, 2009*	-2.5	-3.6	-3.4	-1.4	0.6	1.8	2.5	2.9
% change, q-o-q	-1.5	-0.5	0.1	0.4	0.6	0.7	0.7	0.8
March 9, 2009*	-2.5	-3.7	-3.5	-1.6	0.4	1.6	2.3	2.6
Dec. 8, 2008*	-1.3	-2.2	-1.8	-0.1	1.2	2.2	-	-

◆ Our regular special survey of **Quarterly Forecasts** (pages 3, 28 and 29) shows projections up to the final quarter of 2010. We have also extended this quarterly theme to page 2, where we examine **significant changes in our quarterly forecasts** from December 2008, March 2009 and June (see box, above).

◆ In the **US**, many observers are optimistic that the worst of the recession has passed. As the chart (below) illustrates, the **US** recession is being outpaced by the **Euro zone** and, especially, **Japan**. On the employment front, May saw a smaller number of non-farm payroll losses, compared with previous months. However, the jobless rate soared to 9.4%, suggesting that the labour market retrenchment is not over.

◆ **Japanese** and **German** GDP forecasts continue to drop on the back of the collapse in global demand.



	Average % Change on Previous Calendar Year														Annual Total	
	Gross Domestic Product		Personal Expenditure		Machinery & Equipment Investment		Pre - Tax Corporate Profits		Industrial Production		Consumer Prices		Industrial Product Prices		Average Hourly Earnings	Housing Starts (thousand units)
	Produit Intérieur Brut	Dépenses de Consommation des Ménages	Investissement Productif	Bénéfices des Sociétés avant Impôts	Production Industrielle	Prix à la Consommation	Prix des Produits Industriels	Rémunération Horaire Moyenne	Construction de Logements mises en chantier, milliers							
Economic Forecasters	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010	2009 2010
National Bank Financial	-1.5 2.5	-1.0 1.9	-10.4 4.1	-14.1 2.9	na na	0.0 1.8	na na	na na	130 145							
Conf Board of Canada	-1.7 2.5	0.2 2.1	-17.0 1.9	-32.0 8.8	na na	0.5 2.6	-3.0 3.2	na na	145 167							
EDC Economics	-2.0 1.7	-1.4 1.3	-3.2 2.8	na na	na na	0.2 2.0	na na	na na	155 160							
Infometrica	-2.1 2.4	0.0 2.0	-20.0 1.4	-27.0 5.0	-13.0 1.8	0.1 1.8	-1.5 1.5	3.0 2.8	126 150							
Scotia Economics	-2.2 2.5	-0.6 1.8	-20.2 -0.9	-16.5 10.0	-7.7 2.2	0.4 1.9	na na	na na	135 150							
IHS Global Insight	-2.3 2.3	-0.9 1.3	-20.1 -1.6	-36.8 26.5	-7.1 2.7	0.5 1.6	-1.9 2.2	na na	138 166							
Royal Bank of Canada	-2.4 2.5	-0.5 1.6	-20.1 1.7	-36.9 7.1	na na	0.4 1.7	na na	na na	141 173							
Toronto Dominion Bank	-2.4 1.7	-1.5 0.7	-23.6 -4.9	-38.8 6.9	na na	0.2 1.5	na na	na na	125 130							
BMO Capital Markets	-2.5 1.8	-0.7 1.7	-21.7 -3.6	-35.0 5.0	-8.4 1.0	0.5 1.8	-2.0 1.5	2.8 2.5	135 145							
CIBC World Markets	-2.5 1.5	-0.4 1.9	-20.5 -2.2	-24.0 9.5	na na	0.1 1.2	na na	na na	135 160							
Desjardins	-2.6 1.6	-0.9 0.9	-17.4 2.6	-35.3 12.3	na na	0.0 1.7	-2.0 1.6	2.5 1.0	126 130							
Economap	-2.6 1.9	-0.7 1.8	-19.5 -2.0	-30.0 4.0	-9.0 1.0	0.5 1.8	-3.0 4.0	2.5 2.6	140 145							
University of Toronto	-2.6 3.0	-1.2 1.5	-19.2 2.1	-34.9 22.8	na na	0.3 2.3	na na	na na	136 162							
Caisse de Depot	-2.6 2.1	-0.7 2.0	-18.2 1.4	na na	na na	0.1 1.6	na na	na na	131 152							
Consensus (Mean)	-2.3 2.1	-0.7 1.6	-17.9 0.2	-30.1 10.1	-9.0 1.7	0.3 1.8	-2.2 2.3	2.7 2.2	136 153							
Last Month's Mean	-2.5 2.0	-0.9 1.6	-12.8 -0.3	-26.0 8.8	-9.0 1.5	0.3 1.7	-2.8 1.7	2.7 2.2	138 156							
3 Months Ago	-1.8 2.3	-0.5 1.8	-9.9 1.0	-21.7 8.2	-6.6 1.7	0.2 1.8	-3.4 1.4	2.6 2.4	154 161							
High	-1.5 3.0	0.2 2.1	-3.2 4.1	-14.1 26.5	-7.1 2.7	0.5 2.6	-1.5 4.0	3.0 2.8	155 173							
Low	-2.6 1.5	-1.5 0.7	-23.6 -4.9	-38.8 2.9	-13.0 1.0	0.0 1.2	-3.0 1.5	2.5 1.0	125 130							
Standard Deviation	0.4 0.4	0.5 0.4	5.2 2.7	8.2 7.4	2.3 0.7	0.2 0.3	0.6 1.0	0.2 0.8	8 13							
Comparison Forecasts																
IMF (Apr. '09)	-1.9 1.7	-2.3 0.7	-8.0 1.3			-0.2 0.9										
OECD (Mar. '09)	-3.0 0.3	-2.2 0.1				-0.6 0.5										

Government and Background Data

Prime Minister - Mr. Stephen Harper (Conservative). Government - The Conservatives lead a minority government, with 143 out of 308 seats in parliament (155 seats are needed for a clear majority). Next Election - By 2013 (general election). Nominal GDP - C\$1,536bn (2007). Population - 32.9mn (mid-year, 2007). C\$/US\$ Exchange Rate - 1.064 (average, 2007).

Quarterly Consensus Forecasts

Historical Data and Forecasts (bold italics) From Survey of June 8, 2009

	2008				2009				2010			
	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
Gross Domestic Product	0.3	-1.0	-2.1	-2.7	-2.5	-1.0	0.6	2.0	2.7	3.2		
Personal Expenditure	3.0	0.2	-0.8	-1.2	-0.9	0.3	1.0	1.5	1.9	2.1		
Consumer Prices	3.4	2.0	1.2	-0.2	-0.8	0.7	1.4	1.7	1.8	1.9		

Percentage Change (year-on-year).

Historical Data

* % change on previous year	2005	2006	2007	2008
Gross Domestic Product*	3.0	2.9	2.5	0.4
Personal Expenditure*	3.7	4.1	4.6	3.0
Machinery & Eqpt Investment*	14.1	10.5	4.4	0.5
Pre - Tax Corporate Profits*	10.9	5.1	4.1	5.7
Industrial Production*	1.6	0.2	0.2	-4.1
Consumer Prices*	2.2	2.0	2.1	2.4
Industrial Product Prices*	1.5	2.3	1.6	4.3
Average Hourly Earnings*	3.1	2.6	4.6	3.5
Housing Starts, '000 units	225	227	228	211
Unemployment Rate, %	6.8	6.3	6.0	6.2
Current Account, C\$ bn	25.9	20.3	15.6	8.1
Federal Govt Budget Balance, fiscal years, C\$ bn	13.2	13.8	9.6	-2.6 e
3 mth Trsy Bill, % (end yr)	3.4	4.2	3.8	0.9
10 Yr Govt Bond, % (end yr)	4.0	4.1	4.0	2.9

e = consensus estimate based on latest survey

Year Average	Annual Total	Fiscal Years (Apr-Mar)		Rates on Survey Date			
				0.2%		3.5%	
Unemployment Rate (%)	Current Account (C\$ bn)	Federal Govt Budget Balance (C\$ bn)		3 month Treasury Bill Rate (%)		10 Year Government Bond Yield (%)	
Taux de Chômage (%)	Balance Courante (C\$ md)	Balance Budgétaire (C\$ md)		Rendement sur les Bons du Trésor de 3 mois %		Rendement des Obligations d'État de 10 ans %	
2009 2010	2009 2010	FY 09-10	FY 10-11	End Sep'09	End Jun'10	End Sep'09	End Jun'10
8.0	8.0	-17.1	4.5	na	na	0.3	1.4
8.3	9.4	-62.0	-64.0	-23.0	-31.0	0.4	1.5
8.5	8.2	-8.4	-2.5	na	na	na	na
8.6	8.7	-55.0	-5.0	-45.0	-36.0	0.3	1.0
8.5	8.9	-39.5	-34.5	-54.0	-42.0	0.3	1.1
8.5	9.8	-21.3	-30.8	na	na	0.2	0.5
8.5	9.0	-23.0	0.4	na	na	0.3	0.8
8.8	10.6	-12.6	7.9	-51.0	-45.3	0.2	0.6
8.6	9.0	-32.0	-35.0	-52.0	-40.0	0.2	0.5
8.3	9.0	-41.5	-35.0	na	na	0.2	0.3
8.7	9.3	-29.8	-8.5	-55.0	-35.0	0.3	0.8
8.7	9.0	-35.0	-30.0	-60.0	-45.0	0.2	0.3
8.5	8.7	-39.4	-36.0	na	na	0.2	0.7
8.5	9.0	-37.0	-31.0	-52.0	-37.0	0.3	0.8
8.5	9.0	-32.4	-21.4	-49.0	-38.9	0.3	0.8
8.5	9.1	-38.0	-29.1	-35.6	-33.6		
8.1	8.4	-31.6	-20.6	-34.0	-30.1		
8.8	10.6	-8.4	7.9	-23.0	-31.0	0.4	1.5
8.0	8.0	-62.0	-64.0	-60.0	-45.3	0.2	0.3
0.2	0.6	15.2	20.8	11.3	5.1	0.1	0.4
8.8	10.5						

Manufacturing Leads the Decline

GDP fell by 1.4% (q-o-q) in Q1, down from -0.9% in the previous quarter, on the back of deteriorating external and domestic demand. Investment in machinery and equipment was especially hard-hit by the fall-off in US and Canadian spending, declining by 10.5% over the previous quarter which brought the y-o-y rate down from a 10% fall in Q4 to a massive 19.5% decline. The 2009 forecast for investment this year has consequently been sharply downgraded from -12.8% last month to -17.9%. By comparison, Q1 personal expenditure fell by a relatively muted 0.8% in y-o-y terms, but this contrasts sharply with the 3.0% growth rate two quarters previously. Despite a boost in auto trade in March – which helped to lift overall retail sales month-on-month – the indicator painted a weakening picture of spending, with real retail purchases falling by 1.0% (q-o-q) over the first quarter. Employment indicators are also suffering on the back of the economic downturn, leaving consumption fundamentals shaky, as evidenced by our panel's quarterly forecasts (page 28).

However, it is the manufacturing sector which continues to drive the recession, with goods production in Q1 dropping by 4% (q-o-q) on the back of a 26% collapse in auto and parts output. According to the monthly GDP-by-industry report, the 0.3% (m-o-m) dip in activity in March was driven by a 1.0% fall in manufacturing and 1.9% loss in energy output. Meanwhile, March's factory report showed sales falling by 2.7% (m-o-m) as payback for February's 2.2% surge, which suggests that industry's retrenchment still has some way to go. While the relative stabilisation in US industrial indicators provides some hope going forward, a marked turnaround in the Canadian sector has yet to be evidenced.

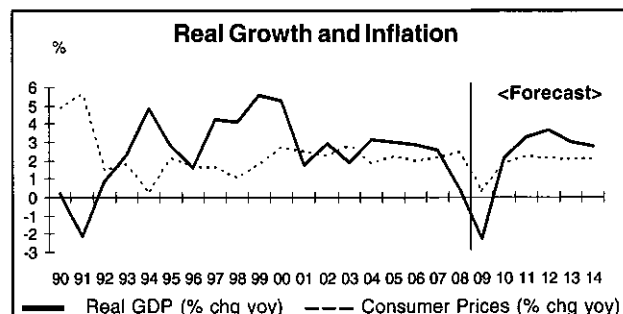
Likelihood of a Bank of Canada Interest Rate Change

Our panel's estimated average probability of a change in the overnight lending rate (0.25% on survey date) at or before the next key policy meeting (July 21, 2009) is:

INCREASE	NO CHANGE	DECREASE	
1.4	+ 97.8	+ 0.8	= 100 %
Most likely rate change mentioned: None			

Direction of Trade – First Half 2008

Major Export Markets (% of Total)		Major Import Suppliers (% of Total)	
United States	78.2	United States	53.6
United Kingdom	2.8	China	8.7
China	2.3	Mexico	3.9
Asia (ex. Japan)	5.5	Asia (ex. Japan)	13.9
Latin America	2.7	Latin America	7.0
Eastern Europe	1.1	Africa	3.0



GDP Growth and Inflation Forecasts

Consensus Forecasts from Survey of:

