



Weekly Market Insight

October 3, 2008

NORTH AMERICAN & INTERNATIONAL ECONOMIC HIGHLIGHTS

Where's The Trigger for a Canadian House Price Crash?

Every dollar drop in the value of Canadian real estate elevates the level of anxiety about a US-style housing meltdown in Canada. To be sure, house prices in Canada will continue to ease in the coming months. But the triggers that led to a freefall in Canadian real estate markets in the early 1990s and today in US markets are nowhere to be found.

Buyer's Market?

In six short months, the Canadian real estate market was transformed from a confident seller's market to a more muted balanced market. And at this rate of growth in unit sales and new listings, by early next year the Canadian housing market will turn, for the first time since 1995, to a buyer's market.

Direction is important, but so is magnitude. When measured against income, the Canadian real estate market has indeed overshot. But a mere 5-7% drop in prices from current levels should bring the national average back to equilibrium. That's a fraction of the 25% overshooting seen in the US by mid-2006.

Location, Location, Location

While the national housing market is still in a balanced position, the overall picture is far from uniform. Calgary and Edmonton, where until recently homeowners doubled the value of their real estate during the course of breakfast, are now seeing close to two and a half new house listings for every unit sold. Consequently, average home prices in these markets fell by 8.5% and 4.6%, respectively, during the year-ending July 2008.

The trigger for the current slowing in these markets is a sharp deterioration in affordability. With house prices in Alberta doubling since 2004, housing affordability has deteriorated to levels not seen since the early 1990s.

However, in other key markets such as Ontario and Québec did not worsen so rapidly. In fact, from a national perspective, it is now 20% more affordable to carry a house than it was after Governor Crow took interest rates to double-digit territory in 1990. Put differently, to bring national affordability back to the levels that triggered the real estate correction of 1990, current mortgage rates would have to double.

US Minus Subprime = Canada

US housing prices have been falling for two years with a cumulative decline of 18% to date—on their way to an eventual correction of 25%. Having started the housing boom roughly at the same time (around 1997), the Canadian housing market is now lagging the US market by roughly two years.

But that's where the similarity ends. By almost any measure, American households entered the current housing crisis from a more vulnerable position relative to their Canadian counterparts— carrying a heavier debt load and a much lighter net worth position. And when it comes to real estate speculation, Canada was not really a player.

But even more important than the absolute and relative level of debt is the distribution of debt. At the peak of the cycle, subprime and Alt-A mortgages accounted for no less than 33% of originations in the US market. In Canada we estimate that at the peak, non-conforming mortgages reached 5.4% of originations.

And at its core, the US meltdown is a subprime story. Average house prices in cities with above-average subprime exposure fell by more than 25% from the June 2006 peak—notably more than the 10% decline in cities with below average exposure. And in today's US market, below-average subprime exposure does not necessarily mean low exposure, as this category includes cities such as Dallas and San Diego with well over 20% in subprime exposure. In fact, house prices in cities with 10-19% subprime exposure fell by only 8% since the 2006 peak, and markets with single-digit exposure fell by an inconsequential 5%.

Eradicate subprime from the US housing market and, instead of the most severe house price meltdown since the great depression, you get a trivial moderate cyclical slowing—something along the line of what we are currently experiencing in Canada.

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International Stock Indexes

Thursday, October 02, 2008

Region/Country	Index	DAILY					52 WEEK				3-yr % chg
		High	Low	Close	Chg	% Chg - +	YTD % chg	High	Low	% Chg	
World											
World	DJ World Index	222.33	213.76	214.03	-8.25	-3.71	-28.9	320.33	214.03	-31.5	-1.9
World	DJ World ex U.S.	189.58	183.33	183.47	-6.03	-3.18	-32.5	291.11	183.47	-34.4	-1
World	MSCI EAFE*	n.a.	n.a.	1528.455	-39.745	-2.53	-32.2	2388.74	1528.46	-34.1	-1.9
Asia Pacific											
Asia-Pacific	DJ Asia-Pacific	112.6	110.01	110.28	-2.23	-1.98	-30.2	172.49	110.28	-33.9	-3
Australia	All Ordinaries	4843.5	4771.4	4774.1	-40.4	-0.84	-25.6	6853.6	4631.3	-27.4	1.3
Australia	S & P/ASX 200	4832.5	4757.3	4761.1	-33.5	-0.7	-24.9	6828.7	4600.5	-27.5	0.9
China	DJ CBN China 600	17889.67	17392.1	17780.97	...	Closed	-57.1	44631.83	15174.77	-58.6	26
China	Dow Jones China 88	206.29	200.49	205.16	...	Closed	-56.6	530.54	172.49	-58	27.7
China	Shanghai Composite	2310.445	2246.279	2293.784	...	Closed	-56.4	6092.057	1895.837	-58.7	n.a.
Hong Kong	Hang Seng	18285.68	17631.7	18211.11	194.9	1.08	-34.5	31638.22	17632.46	-32.5	5.7
India	Bombay Sensex	13203.86	12697.3	13055.67	...	Closed	-35.6	20873.33	12575.8	-26.6	14.8
Indonesia	Jakarta Composite	1856.07	1821.3	1832.51	...	Closed	-33.3	2830.26	1719.25	-25.9	19.3
Malaysia	Kuala Lumpur Composite	1023.24	993.6	1018.68	...	Closed	-29.5	1516.22	991.66	-25.6	3.2
New Zealand	NZSX-50	3232.66	3186.11	3232.64	44.68	1.4	-20	4325.09	3040.45	-24.8	-2.2
Pakistan	KSE 100	9182.71	9178.36	9179.68	...	Closed	-34.8	15676.34	9144.93	-34.9	3.7
Philippines	Manila Composite	2626.04	2574.5	2612.89	43.24	1.68	-27.9	3873.5	2339.84	-30.8	10.4
Singapore	Straits Times	2398.67	2313.63	2363.6	4.69	0.2	-31.8	3831.19	2358.91	-36.6	2
South Korea	Kospi	1458.68	1410.35	1419.65	-20.02	-1.39	-25.2	2064.85	1387.75	-29.1	5.2
Sri Lanka	Colombo Stock Exchange	2160.66	2142.26	2148.61	6.35	0.3	-15.4	2681.27	2142.26	-17	-4.1
Taiwan	Weighted	5840.09	5672.39	5703.72	-60.29	-1.05	-32.9	9809.88	5641.95	-40.8	-2.3
Thailand	SET	601.46	595.24	597.69	3.24	0.55	-30.3	915.03	594.45	-29.6	-6.2
Japan	Nikkei Stock Avg	11452.39	11143.79	11154.76	-213.5	-1.88	-27.1	17458.98	11154.76	-34.7	-6.3
Japan	Nikkei 300	226.38	219.91	220.62	-4.28	-1.9	-26.7	338.84	220.62	-34	-6.9
Europe											
Europe	DJ Stoxx 600	263.92	253.9	254.24	-3.51	-1.36	-30.3	390.63	251.43	-33.8	-5.1
Europe	DJ Stoxx 50	2710	2625.58	2629.17	-33.91	-1.27	-28.6	3932.44	2569.45	-32.1	-6.9
Euro zone	DJ Euro Stoxx 50	3113.87	3003.58	3007.51	-59.84	-1.95	-31.6	4489.79	3000.83	-32	-4.3
Euro zone	DJ Euro Stoxx	288.91	278.69	279.24	-4.97	-1.75	-32.7	432.27	279.2	-34.4	-3.9
Austria	ATX	2814.84	2638.49	2644.84	-122.54	-4.43	-41.4	4871.71	2644.84	-44.4	-8.5
Belgium	Bel-20	2837.29	2734.79	2741.08	24.6	0.91	-33.6	4534.91	2589.47	-38.2	-6.3
Czech Republic	PX 50	1251.9	1220.6	1223.7	-11.6	-0.94	-32.6	1936.9	1167.6	-34.3	-5.6
Denmark	OMX Copenhagen	329.28	312.91	316.77	-9.49	-2.91	-29.4	492.84	316.77	-34.3	-2.4
Finland	OMX Helsinki	7003.64	6743.11	6801.55	-152.13	-2.19	-41.4	12656.77	6801.55	-43.3	-4.8
France	CAC 40	4112.24	3962.74	3963.28	-91.26	-2.25	-29.4	5862.83	3953.48	-31.7	-4.8
Germany	DAX	5876.93	5630.46	5660.63	-145.7	-2.51	-29.8	8076.12	5660.63	-28.8	3.9
Hungary	BUX	19526.04	18893.01	19002.36	-172.15	-0.9	-27.6	28307.04	17464.02	-31.8	-6.1
Italy	S & P/MIB	26387	25155	25258	-423	-1.65	-34.5	41106	25258	-37.8	-10.1
Netherlands	AEX	342.98	330.83	330.83	-3.41	-1.02	-35.9	559.14	323.55	-38.9	-6.4
Norway	All-Shares	370.43	344.63	345.68	-19.72	-5.4	-39.4	603.98	345.68	-38.4	-2.5
Poland	WIG	38065.04	36812.11	37179.65	-603.43	-1.6	-33.2	64292.3	36431.54	-39.1	3.2
Portugal	PSI 20	8078.32	7826.39	7832.91	-166.8	-2.09	-39.8	13323.86	7698.53	-37.7	-1.1
Russia	DJ Russia Titans 10	4227.41	3985.3	3992.1	-190.78	-4.56	-47.9	7920.96	3452.34	-45.5	5.9
Russia	RTS Index	1194.07	1152.7	1152.7	-36.36	-3.06	-49.7	2487.92	1058.84	-44.8	4.6
Spain	IBEX 35	11364.4	10978.9	11002.3	-180.2	-1.61	-27.5	15945.7	10631.6	-25.2	0.6
Sweden	SX All Share	250.34	242	243.03	-2.4	-0.98	-30.9	407.81	243.03	-39	-4.7
Switzerland	Swiss Market	6825.14	6715.25	6730.94	3.31	0.05	-20.7	9218.28	6500.13	-25.7	-0.8
Turkey	Istanbul National 100	36541.32	35615.63	36051.3	...	Closed	-35.1	58231.9	32216.43	-34.4	2.7
U.K.	FTSE 100	5052	4862.1	4870.34	-89.25	-1.8	-24.6	6730.7	4818.77	-25.6	-3.8
U.K.	FTSE 250	8200.3	7904.2	7965.5	51.1	0.65	-25.3	11666	7792.9	-29.9	0.1
Americas											
Americas	DJ Americas	298.25	282.92	283.75	-14.45	-4.85	-24.7	399.86	283.75	-27.8	-2.1
Argentina	Merval	1605.68	1501.79	1520.92	-84.76	-5.28	-29.3	2351.44	1491.98	-32.5	-3.5
Brazil	Sao Paulo Bovespa	49805.26	45113.44	46145.1	-3653.55	-7.34	-27.8	73516.8	45908.51	-23.6	13.5
Canada	S & P/TSX Comp	11714.51	10900.54	10900.54	-813.97	-6.95	-21.2	15073.13	10900.54	-22.8	-0.3
Chile	Santiago IPSA	2776.51	2663.38	2668.88	-107.63	-3.88	-12.5	3496.18	2427.11	-19.1	7.4
Mexico	IPC All-Share	25117.48	23874.32	24027.35	-1089.97	-4.34	-18.7	32836.12	23456.84	-22.7	14.2
Venezuela	Caracas General	38197.52	37849.74	37878.29	-56.49	-0.15	-0.1	41450.77	34172.43	0.2	22.2
Other Countries											
Egypt	CASE 30	7066.67	6967.56	7059.16	...	Closed	-33.1	11935.67	6945.37	-19.5	n.a.
Israel	Tel Aviv	875.26	846.51	847.22	-39.62	-4.47	-30.4	1237.13	842.03	-26.8	3.7
South Africa	Johannesburg All Share	23786.46	22560.77	22560.77	-771.88	-3.31	-22.1	33232.89	22560.77	-27	10.2

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

Three year percent change is annualized.

Sources: Reuters; WSJ.com

MARKET INDICES	Oct 2	a month ago	a year ago
S&P/TSX Composite	10900.50	13299.5	14152.73
S&P 500	1114.28	1277.58	1546.63
Dow Jones Industrial Average	10482.8	11516.9	14047.3

INTEREST / FX RATES	Oct 3	a month ago	a year ago
Prime Can (%)	4.75	4.75	6.25
Prime US (%)	5.00	5.00	7.75
30 Day BA Can (%)	3.624	3.12286	4.87
3 month US T-Bill (%)	0.48	1.67	3.98
3 month Can T-Bill (%)	1.200	2.439	4.001
10yr US Bond (%)	3.715	3.591	4.610
10yr Can Bond (%)	3.68	3.44	4.41
10yr-2yr US Spread (bps)	194.10	144.3	52.70
10yr-2yr Spread Can (bps)	105.0	75.0	10.00
US\$/Cdn\$	0.9250	1.0663	0.9853
US\$/Euro	1.3807	1.4245	1.4099
Yen/US\$	105.850	106.3305	116.994

INTERNATIONAL INTEREST RATES	Oct 3		
	3 mo LIBOR (%)	Spread vs US (bps)	a wk ago (Spread—bps)
United States	4.33	NA	NA
Canada	4.20	-13	34
Euro-zone	5.33	99	138
Switzerland	3.02	-131.2	-90.7
Japan	1.03	-330	-282
Australia	7.76	343	395
	10 Year Bond (%)	Spread vs US (bps)	a wk ago (Spread—bps)
United States	3.72	NA	NA
Canada	3.68	-3.5	-15.4
Euro-zone	4.55	83.2	98.5
Switzerland	2.61	-110.9	-106.5
Japan	1.45	-227.0	-235.4
Australia	5.29	157.0	179.9

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