



Dawn Desjardins
Assistant Chief Economist
RBC Economics Research
dawn.desjardins@rbc.com

FINANCIAL MARKET UPDATE

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Global initiatives piling up

- ▲ Global central banks and governments have been active in putting policies into place to combat the weakening in economic growth, supplementing aggressive cuts to policy rates by central banks as global players worked to weigh against the burgeoning global recession.
- ▲ While these measures have been aggressive, the reaction in financial markets has been positive, but muted. Still, there are some encouraging signs that the policy actions are getting some traction with global LIBOR rates coming off recent highs. Corporate bond spreads, however, remain sticky and there has not been a discernible increase in loan supply or demand.
- ▲ Equity markets are nervous and, although there are tentative signs of stability, it is too early yet to tell if the bottom has been reached.
- ▲ Co-ordinated efforts to cut policy rates are being followed up, with individual countries easing further as data confirm many economies have fallen into recession, including the Eurozone and the United Kingdom.

U.S. economy slips in the third quarter; bigger declines ahead

- ▲ The Fed has pushed the funds rate back to 1% and, even though policymakers left the door open to additional cuts, early signs that funding costs are easing may give the Fed the leeway to hold rates steady and concentrate on other easing initiatives.
- ▲ But, with financial markets still under stress, aggressive Fed easing will do little to mitigate the downside risks to the U.S. economy in the near-term.
- ▲ The U.S. recession likely started in the third quarter. We now expect the economy to contract at a 2% annualized rate in the fourth quarter, with another substantial decline likely in the first quarter of next year of slightly more than 1% at an annual rate. The peak-to-trough decline in U.S. GDP will be greater than in any other three-quarter period during the 1970s, 1980s and 1990s.
- ▲ We still hold the view that the eventual narrowing in credit spreads, combined with accommodative monetary policy, will result in a modest recovery in late 2009.

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