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## Comments on Financial and Economic Developments



Comparing economic releases to forecasts, one is reminded of the quote by Steve Davidson that "Forecasting future events is often like searching for a black cat in an unlit room, that may not even be there." This is not to make fun of forecasters, but it

should be a wake-up call to those who put a lot of emphasis on the value of economic forecasts.

Nobody has a crystal ball — one need only look as far as the recent US August employment numbers, namely the reported loss of 4,000 jobs. The first Bloomberg article following the data release started with "The US economy unexpectedly lost jobs in August..." The article then commented on the surprise this created for economists, especially those surveyed by Bloomberg News, who had forecast that "payrolls rose 100,000 during the month, according to the median of 88 estimates, compared to the originally reported 92,000 gain in July. None of the analysts forecast a decline, as predictions ranged from 35,000 to 140,000."

What we found intriguing about this is that the impact of the collapse of the sub-prime loan market and the slump in housing seemed to have been completely misunderstood if not ignored by forecasters. It is not just the construction industry which is no longer generating jobs; the fallout is also severely hitting the mortgage and finance industries, with a number of firms either going bankrupt or curtailing activities. One need only open the newspaper to learn of layoffs and hiring freezes. Should this not be reflected in the forecast of employment data?

***"...downturns in housing construction have almost always been followed by a downturn in the economy, by a recession..."***

Harvard University economist Martin Feldstein had warned at the end of August of a significant risk of a recession. As he mentioned, downturns in housing construction have almost always been followed by a downturn in the economy, by a recession. Past experience leaves little doubt about the accuracy of this statement.

Today, of course, we also need to deal with the fallout from the sub-prime crisis. We read about the record numbers of foreclosures in the US and we know that coming upward adjustments in mortgage rates will result in even more people losing their homes. Unfortunate as this is, the exaggerations of the past need to be corrected. The way sub-prime mortgages were sold to hapless consumers was extraordinarily irresponsible. Those who should not have become homeowners in the first place are now the first to lose their homes. The ripple effect leads to declining consumer confidence and a slowdown. The logic is clear.

Common sense should always be part of forecasting. Unfortunately common sense is sometimes sorely missing! That does not say much for an industry awash with instant information, high intellect and sophisticated models. Indeed, the lack of common sense continues to be a source of constant fascination!

*By Rolf Spielmann, CFA*

## The price of a car in barrels of oil

On Tuesday July 17, 2007, an article written by William Robson, President and Chief Executive Officer of the C.D. Howe Institute, appeared in the Financial Post. It is worth commenting on. Much has been written about the impact of the Canadian dollar's appreciation and what, if necessary, the Bank of Canada can do about it. Mr. Robson's article clearly points out that the value of the Canadian dollar can be influenced only to a very small part by the Bank of Canada.

Mr. Robson asks how many barrels of oil it takes to buy a car, and he writes: "The exact prices compared are the cost of crude oil imported to North America and Statistics Canada's price index for passenger cars benchmarked to a 2007 Ford Fusion, but other oil and car prices would tell a very similar story. An automaker or car buyer might see in this the cost of a car versus the cost of filling its tank. An oil producer might see it as the number of barrels he or she must sell to buy a car. Either way, it neatly summarizes the huge ebbs and flows of the fortunes of Canada's resource and manufacturing sectors over more than three decades.

"The forces driving those changes were much larger than Canada, let alone its central bank. At the beginning of the 1970s, cars were expensive in terms of oil; it took more than 2,000 barrels to buy the then-equivalent of a Fusion. Then a booming world economy encountered the oil-supply squeeze that made OPEC a household word. By 1974, a car cost about 600 barrels of oil. Oil's purchasing power rose again in 1979, when another world boom ran into the Iranian revolution; by 1980-81, a car cost scarcely more than 300 barrels.

"Then came a recession and new oil supplies. From 1986 to 1996, a car averaged a little less than 1,000 barrels of oil, before the late-1990's oil-price collapse drove the price of a car briefly up to nearly 1,800 barrels. Since then, except for the blip after the tech bubble burst in 2000, the trend in the "oil price" of cars has been down. China's breakneck industrial development, along with robust growth elsewhere in Asia and around the world, has

pushed demand for energy — and its price — way up. Meanwhile, new manufacturers have come on line, driving prices of manufactures way down. In 2006, the price of a car in barrels again got close to 300, close to the record set more than 25 years earlier. Hence Canada's booming oilpatch — and the travails of its automakers.

"But here's a key point about the figure: The Canadian dollar doesn't appear in it at all. The price of a car in barrels of oil does not depend on the exchange rate. It is the same with a Canadian dollar at US65¢ as with a Canadian dollar at US95¢. It is the same in Canadian dollars as in U.S. dollars -- or Euros, Zambian kwachas, or any currency."

As Mr. Robson writes, the Bank of Canada's interest rate moves are a local side-show. What matters for Canadian prosperity is our speed and adeptness in transitioning out of sectors in decline and into the areas with the greatest promise for the future. That is a very wise recommendation indeed.

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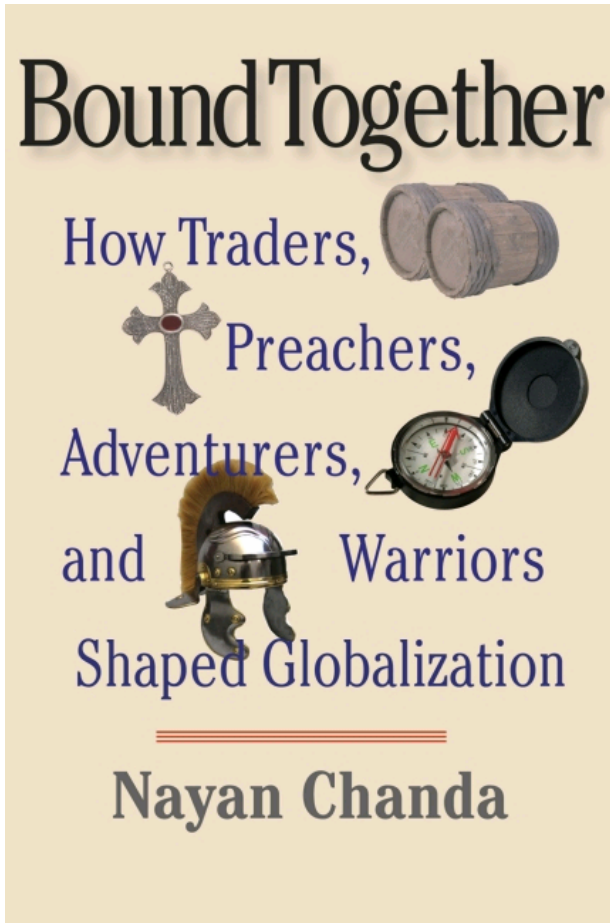
### ***European news***

#### **GERMANY**

The GfK Institute's barometer of German consumer confidence fell to an indexed 6.8 points in September from a revised level in August of 7.4, its second drop in as many months. Increases in food prices and fears about the "subprime crisis" were the main reasons for this decline, the institute's monthly survey found. Other factors sowing uneasiness in German households were soaring oil prices and fears about the impacts of the euro's current strength on the country's economy.

Source: lemonde.fr





***Bound Together: How Traders, Preachers, Adventurers, and Warriors Shaped Globalization***

By Nayan Chanda  
Yale University Press, 2007

Globalization is a much discussed phenomenon, and seemingly an invention of our time. But read the following statement: "*The extension and use of railroads, steamships and telegraphs break down nationalities and bring peoples geographically remote into close connection commercially and politically. They make the world one, and capital, like water, tends to a common level.*" It was made by David Livingstone, commenting on his experiences in Africa, in the 1850s.

Globalization did not start 20 or 30 years ago; it started maybe 60,000 years ago when people began to leave Africa. The process has not stopped since, and thus the term globalization refers to a very old development.

Nayan Chanda has written a very interesting book, concentrating on the four groups he considers instrumental in the advance of globalization, namely traders, preachers, adventurers and warriors. Each group had their own motives: traders to profit, preachers to convert, adventurers to learn and warriors to conquer. Those four groups still exist; preachers in particular are still going strong. And technological advances and cheap airfares allow even ordinary folks to become weekend or holiday adventurers, although Marco Polo would be amazed by today's ease of travel.

What is different today is the speed of communication. No longer does it take weeks for news to travel; everything is instant. This can be considered as great progress, but it has also increased the fragility of a globalized world. We need to look no further than the daily movements in stocks and commodities, etc. A decline in share prices in New York is almost instantly reflected in falling stocks around the globe. Or look back to the decline of the Shanghai stock exchange in February and the instant impact it had on all global markets, and you will understand that the world has become one, with all its advantages and disadvantages.

It is easy to see globalization as a villain that destroys jobs, livelihoods, maybe even societies, but when seen as an ongoing process, the picture changes somewhat. To see globalization and the emergence of large global conglomerates as automatically bad for the average citizen is to look at one side of the ledger only. It is true, and Mr. Chanda points this out in his book, that globalization has disadvantaged many people, namely those who stand no chance of ever benefiting because no matter how cheap the use of a phone, for example, they can never afford a phone in the first place.

We recommend this book because it puts many developments into an interesting perspective. Globalization has been around for a long time and is here to stay; why not learn about its origins and its possible ramifications.

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## Selection of Financial & Economic Indicators

Index	DJ Ind	DJ Transp.	Nasdaq	S&P500	S&P/TSX
September 28	13895.63	4836.32	2701.50	1526.75	14098.89
Monthly var.	+ 4.03%	- 0.87%	+ 4.05%	+ 3.58%	+ 3.21%
Year-to-date	+ 11.49%	+ 6.05%	+ 11.85%	+ 7.65%	+ 9.22%
Year-over-year	+ 18.98%	+ 8.60%	+ 19.62%	+ 14.29%	+ 19.88%



Index	FTSE	DAX	CAC40	SMI	Nikkei
September 28	6466.80	7861.51	5715.69	8933.48	16785.69
Monthly var.	+ 2.59%	+ 2.92%	+ 0.94%	+ 0.59%	+ 1.31%
Year-to-date	+ 3.95%	+ 19.17%	+ 3.14%	+ 1.68%	- 2.56%
Year-over-year	+ 8.49%	+ 30.93%	+ 8.87%	+ 6.02%	+ 4.08%

Commodities	Gold	Copper	Crude Oil	Lumber	CRB
September 28	750.00	363.30	82.54	248.50	335.12
Monthly var.	+ 9.99%	+ 6.95%	+ 11.66%	- 4.79%	+ 8.50%
Year-to-date	+ 17.46%	+ 27.47%	+ 35.20%	- 7.28%	+ 9.07%
Year-over-year	+ 24.13%	+ 4.85%	+ 31.64%	+ 2.69%	+ 9.69%



Currencies	\$CAN	¥	€	£	\$AU
September 28	0.9945	114.8500	1.4255	2.0470	0.8873
Monthly var.	+ 5.73%	+ 0.82%	+ 4.55%	+ 1.54%	+ 8.47%
Year-to-date	+ 14.71%	+ 3.53%	+ 7.95%	+ 4.55%	+ 12.39%
Year-over-year	+ 10.97%	+ 2.75%	+ 12.42%	+ 9.32%	+ 19.10%

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