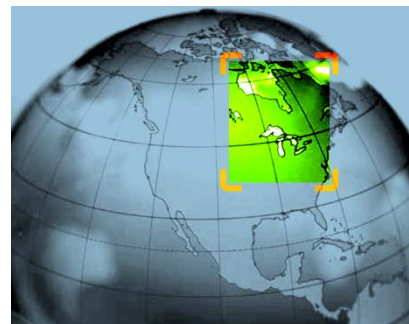


Great Lakes Region

North America's Economic Engine

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The Great Lakes region is a vital driver of North American economic output, employment and trade, accounting for nearly a third of combined Canadian and U.S. output, jobs and exports. While the region was hit hard during the Great Recession, economic activity has since turned around and is expected to shift into a higher gear in 2014. Still, some longer-term issues remain for the region's economy. Labor costs are in focus as the factory sector seeks to remain competitive on the global stage, while policymakers are encouragingly working to facilitate cross-border trade flows in this all-important region.



Weight of a Nation

The Great Lakes region boasts a massive geographic footprint, and is a major driver of the North American economy. With economic output of US\$4.9 trillion in 2012, the region accounts for 28% of combined Canadian and U.S. economic activity. By comparison, the region's output ranks ahead of Germany, France, Brazil and the U.K., and it would rank as the fourth largest economy in the world if it were a country, behind only the U.S., China and Japan. Quite simply, the economic importance of the region can't be overstated.

The region, however, suffered a relatively harsh downturn during the Great Recession, with nominal output falling nearly 2% between 2007 and 2009, versus a combined 1.0% decline for all of Canada and the U.S. In volume terms, all states in the region except Pennsylvania, New York and Minnesota saw real output fall more than the 3.9% U.S. decline, with contractions as deep as 14.5% in Michigan (auto sector woes). Real output in Ontario also fell 3.2% in these two years, underperforming the Canadian average as the manufacturing base was hit hard.

The good news is that economic activity in the region has bounced back, helped especially by a resurgent auto sector. North American car and truck production is back to pre-recession levels, the service sector remains sturdy and, while growth China is slowing, Europe and the U.K. are gaining momentum.

Employment Engine

The region also plays an extremely important role within the broad North American employment market, supplying 46 million jobs in 2013. That represents nearly 30% of the combined Canadian and U.S. workforce. The region's highly diverse economy supports employment across a wide range of manufacturing and service industries. While traditionally considered the manufacturing

Chart 1
Facts and Figures

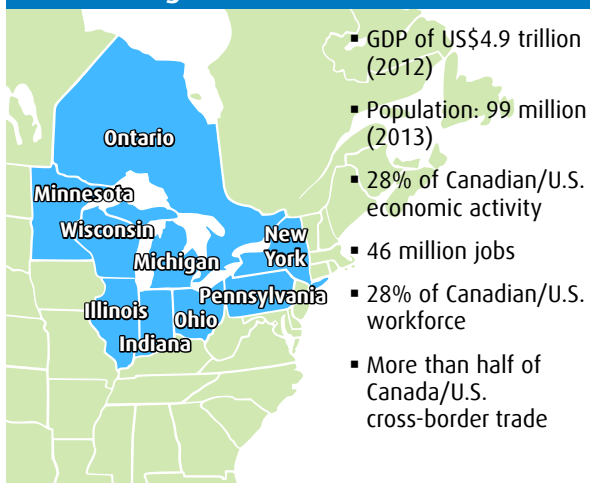
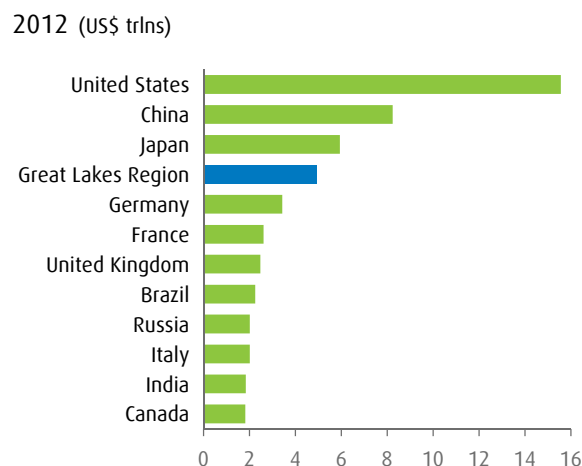


Chart 2
Gross Domestic Product



heartland, factory-sector employment now makes up just over 10% of the region's workforce, down from about 15% a decade ago.

True, part of that drop reflects the Great Recession's disproportionately hard hit on manufacturing, but it also reflects the gradual long-term diversification of the region's economy. While manufacturing employment is down about 20% from a decade ago, education & healthcare (+22%) and professional services (+16%) have helped make up the shortfall. In fact, education & healthcare now make up nearly 18% of employment, while retail & wholesale trade, government and professional services carry double-digit weights. While manufacturing still boasts a comparatively high employment share, education & health and finance & real estate also outweigh the North American average.

While union membership is in secular decline across the U.S., the Great Lakes region included, the region has well above-average membership (even with the recently enacted right-to-work laws in Indiana and Michigan). A combined 16.1% of the workforce were union members in 2013, compared to 11.3% nationally. In Southeastern states such as the Carolinas, Tennessee and Georgia, membership has dwindled to below 5%. The broader challenge facing the region's factory sector is to ensure that productivity remains in line with labor costs.

Integrated Trading Hub

The Great Lakes region is a critically important North American trading hub. The region's states were the origin of roughly a quarter of total U.S. merchandise exports in 2013, while Ontario accounted for 40% of Canadian shipments. Transportation equipment and machinery are the major drivers, but agricultural and food products, metals and chemicals are also important exports.

The region's cross-border trade linkages are also immensely important. For example, the Great Lakes states are Ontario's single largest trading partner, accounting for nearly \$170 billion of total trade in 2013. That represents a sizeable 36% of the province's total international imports and exports. The North American Free Trade Agreement has certainly helped to grease the trade relationship in the region, but more can be done to enable the efficient movement of goods, especially given how integrated the supply chain has become. The Beyond the Border Action Plan is one positive, carried out jointly by the U.S. and Canadian governments to improve trade flows. Among the measures are increased value thresholds for expedited customs clearance, preclearance initiatives for commercial cargo and a preclearance framework to expedite the movement of people. Improved border infrastructure is also a priority. For example, construction of an additional bridge between Windsor and Detroit continues to move closer to reality after

Chart 3
Service Sector Picks Up the Slack

Great Lakes Region (2002 = 100)

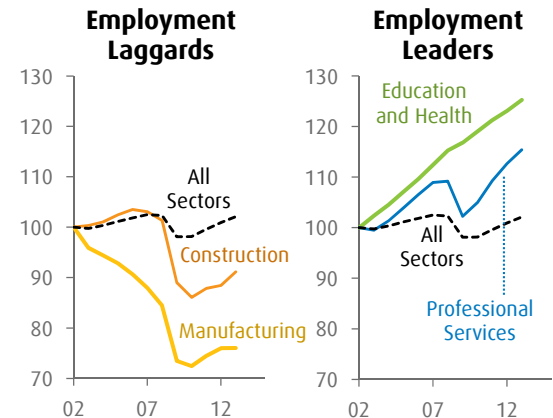


Chart 4
Diverse Labour Market

Great Lakes Region — 2013
(% of Great Lakes Region employment)

Employment by Industry

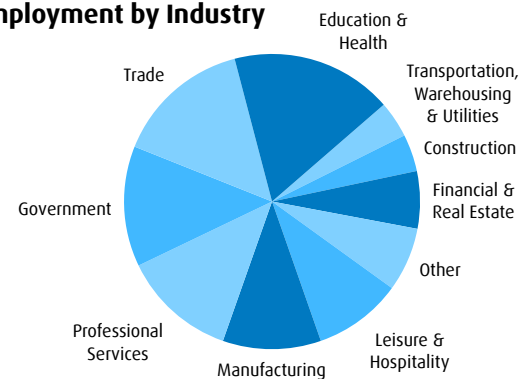
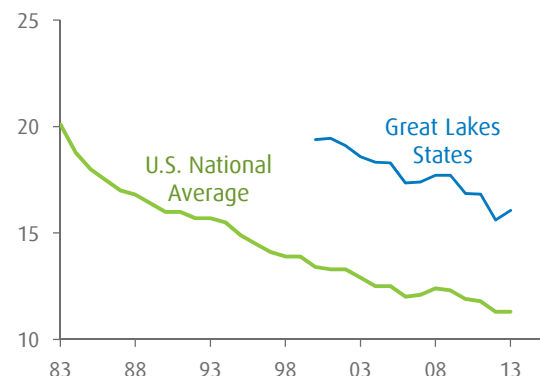


Chart 5
Union Membership Falling

(% of wage and salary workers)

Union Membership



Michigan voters defeated Proposal 6 in the 2012 election, but Federal funding (\$250 million) for a U.S. customs plaza is still pending. The Ambassador Bridge is among North America's busiest international crossings in terms of trade volume, carrying more than 25% of merchandise trade between Canada and the U.S.

The Bottom Line: There's little questioning the importance of that the Great Lakes region to North American economic output, employment and trade, and measures by policymakers to improve trade flows and to foster overall growth in the region are key for the long-term health of the broader economy.

Economic Update—Better Growth Ahead

The North American economy is expected to gain momentum in the year ahead. The U.S. economy is expected to lead, expanding at a roughly 3% clip beginning in the spring, as the housing recovery continues, consumer spending remains firm and business confidence improves. In Canada, firmer U.S. demand and a weaker Canadian dollar should help lift real GDP growth to around 2.5% through 2015, though a more balanced housing market and softer consumer spending will keep growth below that of its U.S. counterpart.

The U.S. housing recovery remains a key pillar supporting the outlook. While the jump in mortgage rates in mid-2013, harsh weather at the turn of the year and the Qualified Mortgage Rule have dampened activity, the soft patch should prove temporary. Affordability remains attractive enough to keep prices rising (albeit at a cooler rate). While the Great Lakes states overall were less-hard hit by the housing bust, pockets of extreme weakness such as Chicago are starting to recover. Toronto's housing market remains balanced overall, but construction activity is expected to follow a more subdued path with a large number of condo projects reaching completion in the year ahead.

Factory activity has levelled off in the past year amid fragile business confidence and harsh weather. Looking ahead, the dawn of spring should help activity, and a budget deal in Washington plus the lifting of the debt ceiling should help, even though gaining control of the country's finances remains a significant challenge for decision-makers on both sides of the aisle.

Finally, state finances have improved. Illinois' pension reform has been one problem area, but legislation passed late last year will address unsustainable benefits. In Ontario, a FY14/15 budget is still pending, and the Province continues to face challenging spending targets in order to balance the books by FY17/18 as planned.

The following pages are excerpts from BMO Capital Markets' *State Monitor* and *Provincial Monitor* reports—the full reports can be found on our website: <http://www.bmonesbittburns.com/economics/>

Chart 6
Cross-Border Linkages

2013 (C\$ blns)

Ontario's Trading Partners

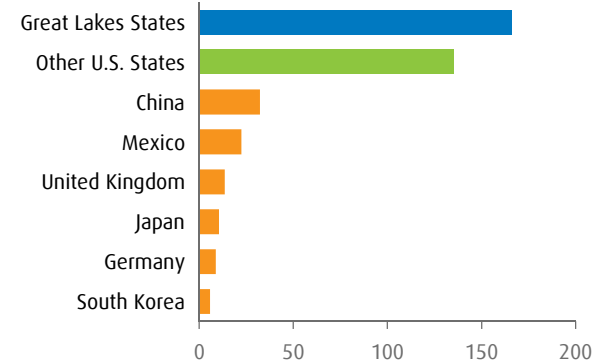


Chart 7
U.S. Expansion Strengthening

(y/y % chng)

Real GDP

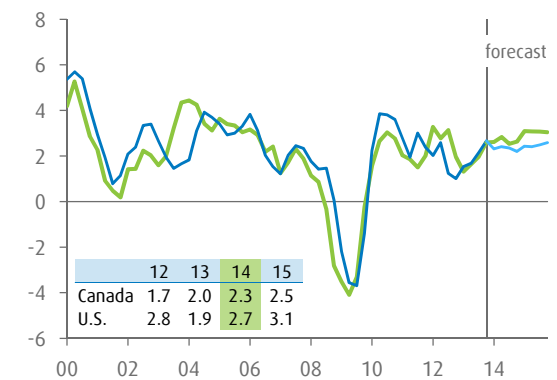
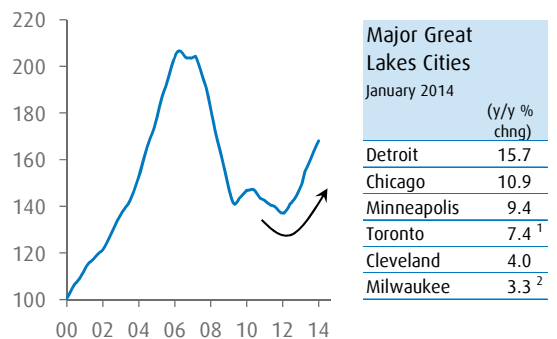


Chart 8
U.S. Housing Recovery Underway

United States (January 2000 = 100 : s.a.)

S&P/Case Shiller Home Price Index



¹ MLS HPI, Mar. 2014 ² Zillow Home Value Index, Feb. 2014

Ontario

- Weaker C\$/Stronger U.S. economy to support growth
- FY14/15 budget still pending

Economic growth is poised to pick up in Ontario, getting a boost from stronger U.S. demand and a weaker Canadian dollar. Real GDP is expected to expand 2.3% this year, improved from the subdued 1.4% average pace recorded over the prior two years, and pick up further to 2.5% in 2015—both years would fall in-line with the national average.

The stronger U.S. economy/weaker loonie combination is a clear positive one-two punch for Ontario **exports and manufacturing**. Estimates suggest that a 10% decline in the C\$ can lift real GDP growth by roughly a full percentage point over two years—while a declining manufacturing share and loss of capacity since the Great Recession could temper the response, it will still be positive. While the cyclical environment is improving, the longer-term story remains a cautious one for exports and manufacturing. Relatively high labour costs continue to pose challenges for the auto sector versus Mexico and the Southern U.S. High electricity rates are another challenge, with Hydro-Québec’s latest survey showing after-tax average prices paid by large consumers in Toronto well above those paid in competing cities such as Montreal, Winnipeg, Chicago and Detroit.

The **housing market** continues to hold up well, especially in Toronto, where the resale market remains balanced and valuations are within historical ranges—the typical mortgage payment on an average-priced home is just over 40% of estimated median family income, comfortably below the near-50% seen at the peak in 2007, and miles below the exorbitant valuations of the late-1980s. Housing starts also appear to be settling in to levels supported by demographic demand, though the condo market could be tested as the record 58,000 units currently under construction come to completion over the next two years. Ontario’s **labour market** performance has softened, with employment up a modest 0.7% y/y in Q1. While public-sector employment has fallen in the past year, the private sector has picked up the slack with gains in construction and trade. The jobless rate sat at 7.3% in March, matching the low of this cycle, but little-changed from two years ago.

The Province of Ontario’s fiscal plan remained on track in the Fall (2013) fiscal update, with the FY13/14 deficit pegged at \$11.7 billion (1.7% of GDP), unchanged from the budget estimate made in May and the first quarter update. The longer-term fiscal plan also remained unchanged, with the deficit falling to \$10.1 billion in FY14/15 and ultimately eliminated in FY17/18. The FY14/15 budget is still pending, but early indications suggest that there could be some deviation away (to the downside) from the fiscal plan in the near term, as well as some measures on the tax side to fund transit expansion, but the longer-term target of a balanced budget by FY17/18 is expected to remain in place. It remains to be determined if the budget will pass or if opposition parties will force an election.

Ontario

Population:	15,538,000		
Percent of Canada:	38.7		
Rank by Population:	1 st		
Area:	1,076,395 km ²		
GDP/Capita:	\$49,100	Legislative Seats:	
Capital:	Toronto	Liberals	49
Party in Power:	Liberals	PC	37
Premier:	NDP	NDP	20
	Hon. Kathleen Wynne	Vacant	1
Finance Minister:	Hon. Charles Sousa		

Minority government since October 2011

Economic Outlook

Ontario	13e	14f	15f
Real GDP (% chng)	1.4	2.3	2.5
Employment (% chng)	1.4	0.7	1.3
Jobless Rate (%)	7.5	7.3	7.0
Housing Starts (000s)	60.7	55.0	53.5
Cons. Prices (% chng)	1.1	1.7	1.8

e = estimate f = forecast

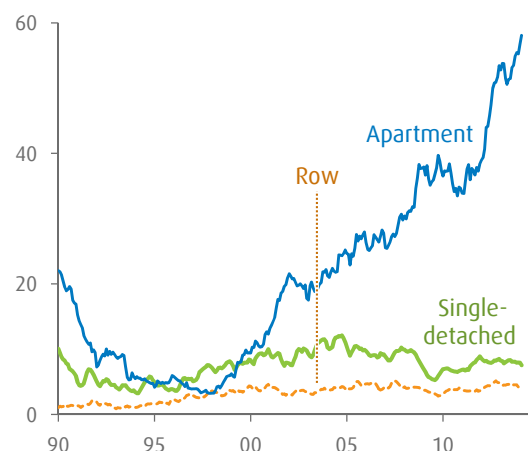
Ontario’s Fiscal Situation

(\$ mlns)	FY12/13	FY13/14 f
Revenues	113,369	116,834
Expenditures	122,589	127,575
Reserve Allowance	0	1,000
Budget Balance	(9,220)	(11,741)
(% of GDP)	-1.4	-1.7
Net Debt	252,088	272,106
(% of GDP)	37.4	39.4
Debt Service	10,341	10,605
(% of revenue)	9.1	9.1

() = deficit As of Q2 update

Homes Under Construction

Toronto (000s units)



Illinois



		Rank /50
Population	12,875,000	5
GDP/Capita	\$52,119	12
Jobless Rate	8.4%	3

Top Economic Concentration¹

Management Services	126
Transport & Warehouse	121
Finance & Insurance	121

Top Exports - 2012 (\$ blns)

Machinery	20.1
Chemicals	7.9
Transportation Equip.	7.4

¹ relative industry share (national average = 100)

- Fiscal challenge being addressed with pension reform
- Manufacturing and exports to pick up from soft patch
- Home prices poised to recover further
- Jobless rate still high

Economic growth remains challenged in Illinois, with factory activity and exports softening through much of 2013 and State finances in the spotlight. Real GDP likely grew a below-average 1.4% last year, but is poised to improve to a 2.5% pace in 2014 as business investment and housing gain momentum, and the severe drag from the public sector fades.

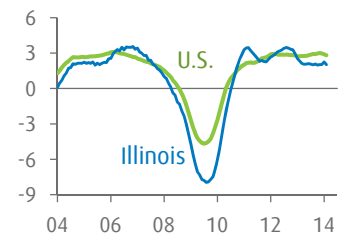
Labor market... Job growth remains muted, with nonfarm payrolls running at a 0.5% y/y pace in the three months through March. A few of the sectors that were stronger earlier in the recovery—such as manufacturing—have faded in the past year and are now seeing payrolls below year-ago levels. However, state and local government employment, which was a major drag in recent years, has finally levelled off and is no longer acting as a major drag on the labor market. Still, the unemployment rate remains among the highest in the country, ending 2013 at 8.6%, but is expected to drift down to 7.6% by 2015. Hours worked are down from a year ago and wage growth remains tame.

Housing market... While the market has clearly turned up, the housing recovery has yet to gain the same kind of traction in Illinois as in other hard-hit states—but the market appears to be gathering momentum. According to the S&P Case-Shiller Index, prices in Chicago were up a solid 11.1% y/y in January, near the fastest clip in 25 years. The months' supply of single-family homes for sale in the Chicago area has fallen to less than 6 from more than a year's worth as recently as early 2012, and the foreclosure rate, while still elevated, is on a downward track. With some improvement in economic growth and confidence in the state, that should set the stage for a more substantial recovery in home prices ahead.

Noteworthy... Business confidence remains subdued in the state, in part because of recent wrangling in Washington, but also due to Illinois' own **fiscal issues**. Moody's and S&P both cut the state's credit rating in 2013 amid concerns over unfunded pension liabilities. However, legislation passed late in the year will reduce cost-of-living increases, push back the retirement age and offer 401(k)-style plans in place of defined benefit plans. While challenges to implementation still remain, the development is a clear positive step. Meantime, **exports** backed off during the first three quarters of 2013 before a bounce in Q4, and growth should continue this year. Factory activity in the Chicagoland areas appears poised to recover from its soft patch as well, with the **Chicago PMI** surging to a 2½-year high recently.

Coincident Economic Index

(y/y % chng)



Economic Outlook

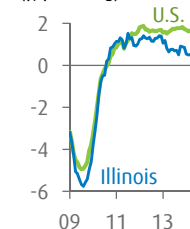
Illinois		13e	14f	15f
Real GDP	(% chg)	1.4	2.5	2.9
Pers. Income	(% chg)	2.4	3.5	4.5
Employment	(% chg)	-0.4	1.2	1.6
Jobless Rate	(%)	9.1	8.4	7.7
Housing Starts	(000s)	15.9	21.0	25.0

e = estimate f = forecast

Economic Indicators

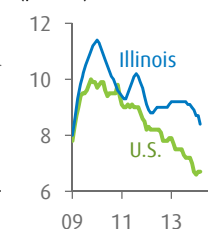
Employment

(y/y % chng)



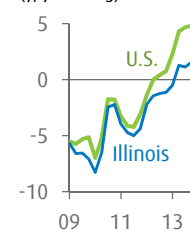
Jobless Rate

(percent)



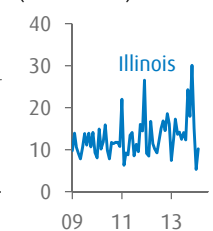
House Prices¹

(y/y % chng)



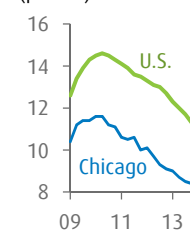
Housing Starts

(000s : s.a.a.r.)



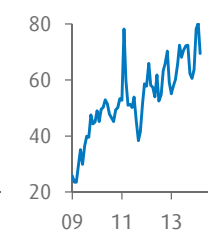
Industrial Availability

(percent)



Consumer Confidence

East North Central



¹ FHFA House Price Index

Wisconsin



		Rank /50
Population	5,726,000	20
GDP/Capita	\$40,613	29
Jobless Rate	5.9%	28

- **Moderate growth in 2013; pickup expected in 2014**
- **Manufacturing recovery lost steam in 2013 – better momentum this year**
- **Labor market improving amid solid payroll growth**
- **Fiscal backdrop favorable**

Top Economic Concentration ¹	Top Exports – 2012 (\$ blns)	Rank
Agriculture	Machinery	7.0
Manufacturing	Computer/Electronics	3.0
Management Services	Transportation Equip.	1.8
Health care	Food Products	1.7

¹ relative industry share (national average = 100)

Wisconsin's economy expanded at a moderate pace through much of 2013, but recent indicators point to a pickup in activity. Real GDP is expected to grow a solid 2.3% this year, up from an expected 1.2% pace in 2013, helped by firming factory activity and modest export growth. Still, growth is expected to trail the national average somewhat.

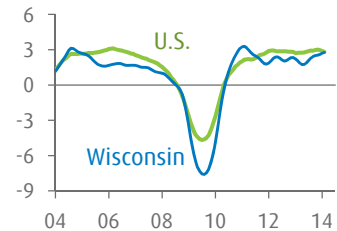
Labor market... Employment has improved markedly in recent months, with nonfarm payrolls up 1.4% y/y in the three months through March. Manufacturing employment has rebounded to the best level since early 2009 (though still about 7% below pre-recession levels), while leisure and hospitality jobs have jumped 5% in the past year. On the flip side, construction employment remains near recession lows, while financial-sector employment has slumped over the past year. With improved job growth, the unemployment rate has fallen to 5.9%, the lowest level since late-2008, and should stay below 6% in the year ahead. Average hours are still slightly below year-ago levels, but wage growth is firm at 2.8% y/y.

Housing market... Wisconsin's housing market was less severely hit than many other states, with prices falling 10% peak-to-trough as measured by the FHFA index, versus 18% nationally. As a result, while prices have begun to rise again, they haven't done so with the same vigor seen in other harder-hit markets. Because of a relatively mild downturn, the state's housing vacancy rate is near the low end of the spectrum at 1.6%, and the months' supply of homes for sale in Milwaukee now sits below 5, the lowest level since 2005.

Noteworthy... Exports have levelled off in the past year, largely due to a slowdown in machinery shipments. Improved growth in business investment this year should support modest gains in 2014. Meantime, factory activity has improved from last year's early-year soft patch, with the **Milwaukee PMI** rising steadily since mid-2013. **Personal income tax cuts** (compressed the number of brackets from 5 to 4 and lowered all rates) enacted last year will return an estimated \$328 million to the economy in fiscal 2014. Indeed, the financial backdrop is one of the main positives in the State—critically, unfunded pension liabilities are not an issue as in neighboring Illinois. Debate is ongoing over further income and property tax cuts this year.

Coincident Economic Index

(y/y % chng)



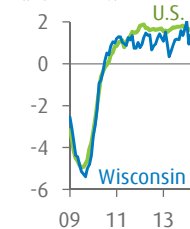
Economic Outlook

Wisconsin		13e	14f	15f
Real GDP	(% chg)	1.2	2.3	2.6
Pers. Income	(% chg)	3.1	3.3	3.8
Employment	(% chg)	0.6	1.1	1.2
Jobless Rate	(%)	6.7	5.9	5.5
Housing Starts	(000s)	13.3	16.5	18.5

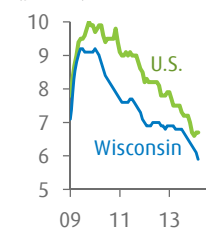
e = estimate f = forecast

Economic Indicators

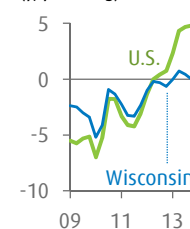
Employment
(y/y % chng)



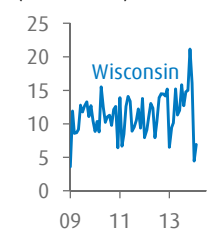
Jobless Rate
(percent)



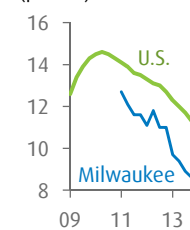
House Prices¹
(y/y % chng)



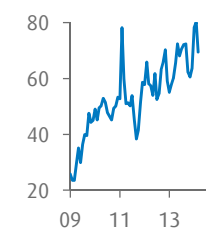
Housing Starts
(000s : s.a.a.r.)



Industrial Availability
(percent)



Consumer Confidence
East North Central



¹ FHFA House Price Index

Indiana



		Rank /50
Population	6,537,000	16
GDP/Capita	\$42,678	32
Jobless Rate	5.9%	30

- **Employment growth strong; payrolls back to pre-recession level**
- **Auto sector supporting broader economy**
- **State finances in relatively good shape; business tax cuts considered**

Top Economic Concentration ¹	Top Exports – 2012 (\$ blns)
Manufacturing 235	Transportation Equip. 9.7
Agriculture 123	Chemicals 8.9
Transport & Warehouse 115	Machinery 4.5
Utilities 115	Misc. Commodities 2.0

¹ relative industry share (national average = 100)

Economic growth remains solid in Indiana as the auto-sector continues to expand, job growth is impressive and government finances are in relatively good shape. Real GDP should expand a slightly above-average 2.8% this year, before picking up further to 2.9% in 2015.

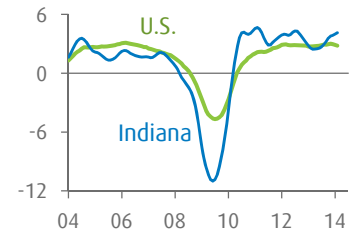
Labor market... Employment continues to recover at a solid clip in Indiana, up 1.6% y/y in March, a touch below the national average. In fact, nonfarm payrolls in the state are now near pre-recession levels, a rare feat in the manufacturing-heavy region of the country. A resurgent auto sector has clearly helped, with durable goods manufacturing employment rebounding by more than 60,000 positions since early 2009. The service sector, however, has been the main driver, with impressive gains in transportation & warehousing (also likely auto-related), retail trade and finance. With strong job growth, the unemployment rate has fallen sharply to 5.9%, down 2 percentage points from a year earlier. Notably, the State recently signed a ‘right-to-work’ measure into law, making it one of the first in the Great Lakes region to do so (subsequently followed by Michigan).

Housing market... Home prices are recovering, with the FHFA index up 1% y/y in 2013Q4, still well below peak levels but up 3% from the recession low. The foreclosure rate has fallen sharply in the past year, down a full percentage point, but remains close to the national average at 3.1%. The healthier backdrop has boosted construction activity, with housing starts totaling nearly 18,000 units in 2013, up 29% from the prior year—look for continued moderate growth this year.

Noteworthy... U.S. **auto sales** rose to the best level in nearly 6 years in 2013. This helped drive a solid 7.8% y/y gain in **auto production** in 2013Q4—growth has cooled, but the level of output is providing a strong support to Indiana’s industrial base. Recent moves by **Honda** and **Toyota** to boost output in the state (the latter recently announcing increased SUV production and 600 new jobs) are encouraging. The **fiscal situation** is favorable, with general fund spending slated to rise 2.8% in FY2014, a phase out of taxes on business equipment currently being considered and personal income tax rates set to fall modestly through 2017.

Coincident Economic Index

(y/y % chng)



Economic Outlook

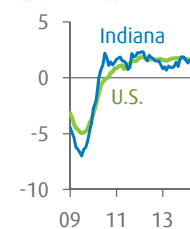
Indiana		13e	14f	15f
Real GDP	(% chg)	2.0	2.8	2.9
Pers. Income	(% chg)	2.6	3.7	4.7
Employment	(% chg)	1.0	1.4	1.7
Jobless Rate	(%)	7.5	6.5	5.7
Housing Starts	(000s)	17.8	22.0	26.0

e = estimate f = forecast

Economic Indicators

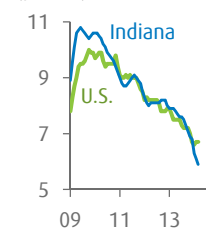
Employment

(y/y % chng)



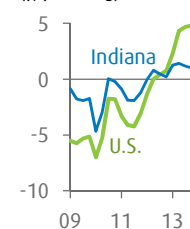
Jobless Rate

(percent)



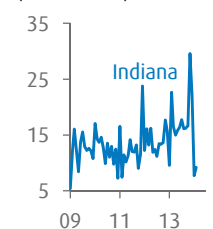
House Prices¹

(y/y % chng)



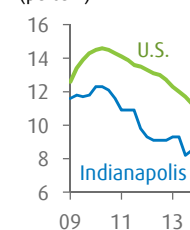
Housing Starts

(000s : s.a.a.r.)



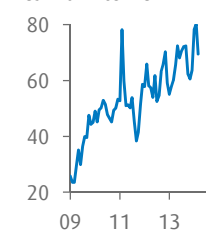
Industrial Availability

(percent)



Consumer Confidence

East North Central



¹ FHFA House Price Index

Minnesota



		Rank /50
Population	5,379,000	21
GDP/Capita	\$52,707	11
Jobless Rate	4.8%	40

- **Employment tops pre-recession levels; jobless rate falling fast**
- **Manufacturing and export growth moderating amid lower machinery shipments**
- **Tax increases in fiscal 2014**

Top Economic Concentration ¹	Top Exports – 2012 (\$ blns)
Agriculture 233	Computer/Electronics 4.0
Management Services 201	Machinery 3.4
Finance 122	Transportation Equip. 2.3
Wholesale Trade 117	Food Products 1.6

¹ relative industry share (national average = 100)

The Minnesota economy continues to grow at a modest pace as cooler export activity offsets a continued solid labor market performance. Real GDP likely grew 1.7% in 2013, close to the national average, but should pick up to a 2.9% pace this year.

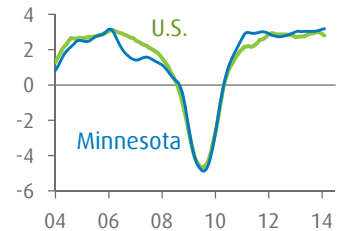
Labor market... Minnesota boasts a relatively healthy labor market, with payroll growth a firm 1.6% y/y in March and the jobless rate among the lowest in America at 4.8%. In fact, nonfarm payrolls have pushed to a record high in recent months, an impressive recovery from the Great Recession that has outperformed most of its Midwest peers. Recent gains have been seen across a wide range of service-sector industries, including transportation, finance, professional services and leisure & hospitality. Local governments have also resumed hiring, while the auto-sector expansion has lifted manufacturing payrolls.

Housing market... The housing recovery is taking root in Minnesota, with home prices across the state up a healthy 5.3% y/y in 2013Q4, according to the FHFA index. In Minneapolis, prices jumped 9.4% y/y in January, according to the Case-Shiller Index—not as robust as the gains seen in some other major cities, but the downturn was comparatively muted as well. The state-wide foreclosure rate sits at a well below-average 1.2%, and vacancies are low. With a healthy labor market and solid population growth (by Midwest standards), homebuilding is also on the rise. Housing starts totaled just under 15,000 units last year, marking a health recovery from the recession when building activity fell as low as 8,600 units in 2011.

Noteworthy... Enacted revenue increases in Minnesota are the highest among all states for FY2014, at \$1.4 billion according to the NASBO. That includes a higher tax bracket for the top 2% of earners, as well as increased corporate and tobacco taxes. Meantime, exports levelled off last year as machinery shipments softened, but momentum picked up to a 5.9% y/y pace by the fourth quarter.

Coincident Economic Index

(y/y % chng)



Economic Outlook

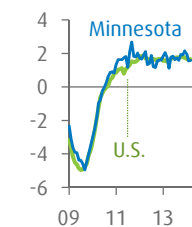
Minnesota		13e	14f	15f
Real GDP	(% chg)	1.7	2.9	3.0
Pers. Income	(% chg)	2.6	3.8	4.7
Employment	(% chg)	1.0	1.4	1.7
Jobless Rate	(%)	5.0	4.4	4.1
Housing Starts	(000s)	16.0	19.2	22.0

e = estimate f = forecast

Economic Indicators

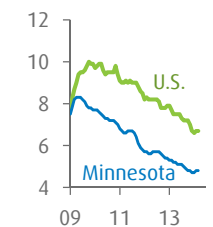
Employment

(y/y % chng)



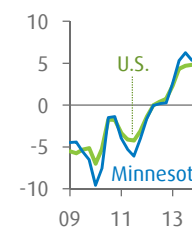
Jobless Rate

(percent)



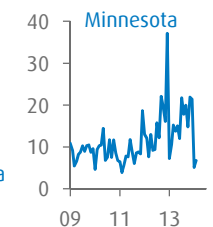
House Prices¹

(y/y % chng)



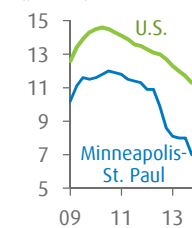
Housing Starts

(000s : s.a.a.r.)



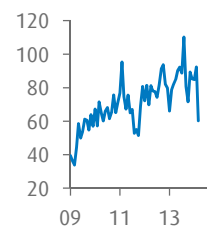
Industrial Availability

(percent)



Consumer Confidence

West North Central



¹ FHFA House Price Index

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