Deutsche Bank

4 March 2010

Data Flash (New Zealand)

Preview of RBNZ MPS & OCR Review, 11 March

Economics

Research Team

Darren Gibbs
Chief Economist
(+64) 9 351-1376
darren.gibbs@db.com

Summary

- As reflected in both analyst surveys and market pricing, once again we think it is virtually certain that the OCR will be maintained at 2.5%. As a result, the focus will be on how the Bank describes the outlook for the economy and monetary policy. We think that the Bank's activity outlook will be broadly similar to that seen in the December Monetary Policy Statement (MPS), with a slightly stronger outlook for the external sector of the economy balanced by a slightly weaker outlook for the domestic sector (a positive development).
- Nonetheless, we think that the tone of the MPS will read a little more dovishly than the Bank's January statement. This will largely reflect the weakness seen in the housing market in recent months (for the time being reducing the risk of stronger than expected domestic demand) and the higher than expected unemployment reading in Q4 (suggesting more downward pressure on wage growth than had been expected). However, as in January, we expect the Bank will conclude that contingent on the economy evolving as expected, it will likely begin removing stimulus "…around the middle of 2010".
- We think that such an outcome would reinforce market expectations that the first OCR hike will come no earlier than the June MPS meeting, with the risk of a slightly later start (especially if the first hike is to be larger than 25bps).

No change in the OCR next week, again the focus is on the RBNZ's words…

The key local event next week is the outcome of the RBNZ's OCR Review and the accompanying Monetary Policy Statement (MPS), which will be released at 9am on Thursday. With the RBNZ having indicated in its last policy review in late January that it did not expect to begin raising the OCR until around the middle of 2010, once again it should come as no surprise that neither the market nor analysts are anticipating any move in the OCR at this meeting. As a result, the focus for markets will be on the Bank's updated economic projections (updating those last published in the December MPS) and the Bank's characterization of what these imply for the likely stance of monetary policy this year and next.

In its January statement, the RBNZ indicated that the economy was evolving broadly in line with the projections underlying the December Monetary Policy Statement (those projections are summarized in a table at the end of this note). Since late January, the dataflow has been quite limited. Looking at international developments, whilst there has been much focus of late on potential sovereign debt problems in Europe, consensus growth forecasts for New Zealand's trading partners have in fact edged a little higher in recent months, reflecting a stronger assessment of the outlook for growth in Australia and Asia. New Zealand's export commodity prices, as captured by the ANZ commodity price index, have also increased further (despite a modest fall in prices in the dairy sector) to be just short of the mid 2008 highs, both in world price and NZ Dollar terms (see Figure 1).

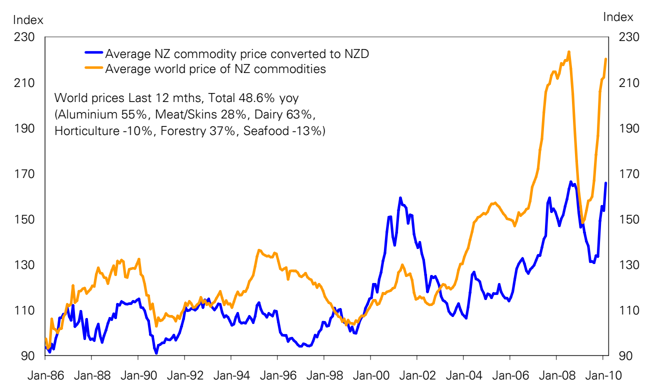
Domestically the dataflow has been mixed. Certainly last week's NBNZ business survey was stronger than we were expecting (and we suspect stronger than the RBNZ was expecting), with the headline and own-activity index rising to decade-long highs. On the face of it the very strong own activity index provides ample support for the RBNZ's quite bullish GDP growth forecasts, as it does our own (see Figure 2). The NBNZ survey also reported a further rise in the employment intentions index, which now sits a little above its historic average, consistent with solid employment growth later this year (see Figure 3). Against that, consumer confidence has moderated slightly over the past month. However, confidence remains stronger than at the end of last year and has encouraged the pick-up in overall retail spending seen late last year (see Figure 4). Still, whilst overall retail spending appears to be on a strengthening trend (see Figure 5), the pick-up in core retail sector activity remains much more muted at this stage (see Figure 6).

Of greater significance, activity in the housing market has fallen very sharply since late last year, which anecdotes suggesting that this weakness continued through most of February (the REINZ housing report for February will not be released until the day after the RBNZ's meeting although the RBNZ itself will see this data early next week). Whilst uncertainty about the tax regime facing property investors is likely part of the explanation, we think that the main reason is that activity (and prices) had earlier rebounded to levels that could not be supported given the broader weakness in the economy. The rise in term mortgage rates over the course of last year also likely discouraged some potential buyers (even though low floating and short-term fixed rates have remained). Whatever the reason, such low levels of activity are consistent with a downward pressure on house prices (see Figure 7), as in fact has been seen in the REINZ house price index over the past two months. This will comfort the RBNZ on two fronts. First, it reduces the risk of stronger that expected domestic demand (Figures 8 and 9 illustrate the link between housing activity and retail sales and dwelling consents respectively). Second, it alleviates concerns that historically low interest rates might inadvertently drive another housing market bubble.

The other key piece of local data in recent weeks was the Q4 Household Labour Force Survey. This report showed that employment had stabilised more-or-less in line with the RBNZ's expectations. However, in common with the market (indeed, even more so than the market) the Bank was surprised by the unexpectedly large jump in the unemployment rate, reflecting a higher level of labour force participation than had seemed likely considering the weakness that remains in the labour market (see Figure 10). Whilst this can be interpreted as a positive development – people felt encouraged to look for work despite the lack of net job creation – it still implies greater downward pressure on wage and salary growth than the RBNZ had hitherto been forecasting. We think that this should lead the RBNZ to modestly revised down its forecast of inflation in the non-tradeable sector of the economy, countering some greater than expected near-term strength coming through from the tradeables sector (largely due to rising commodity prices, including for food). Recent surprising rebounds in the NBNZ selling price intentions indicator (see Figure 11) and a further nudge higher in longer-term inflation expectations (see Figure 12) will likely prevent a larger revision, however.

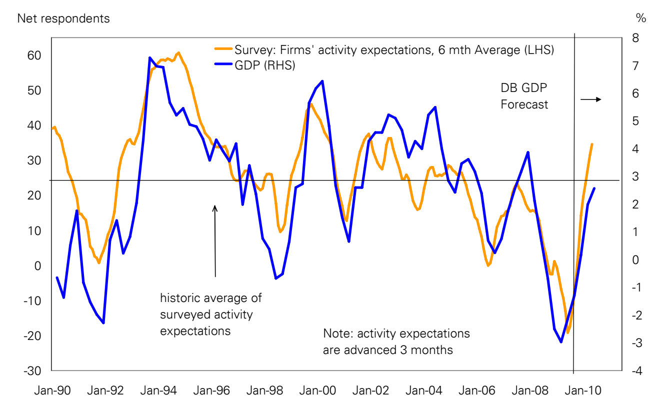
Given the developments above, on balance we think that the RBNZ's central view of the outlook for the real economy will have remained broadly as it was in January and December, with a slightly stronger outlook for the external sector balanced by a slightly weaker outlook for the domestic economy (a change in mix that the RBNZ will doubtless welcome). We should note that we are assuming that the Bank will make no formal allowance at this stage for the impact of a potential rise in GST later this year (as is being considered by the Government), which would likely tend to bring forward spending on big-ticket items in particular. However we think that recent developments in the housing and labour markets should have at least some impact on how the Bank judges the risks around the medium-term inflation outlook, if not the medium-term outlook itself. This will mean that the RBNZ probably sees slightly more scope for delaying the first hike in the OCR relative to what might have been assumed at the time of the January meeting, which may also be reflected in a slight pushing out of the tightening profile in the RBNZ's formal economic projections. This will impart a slightly more dovish tone to the Bank's statement, even though we think that the Bank will continue to conclude that "…we would expect to begin removing policy stimulus around the middle of 2010" (bearing in mind that the Bank is liberal in its interpretation of what constitutes the "middle"). Such a conclusion would leave the market and analysts with the belief that a first hike in the OCR will occur at the June MPS meeting at the earliest, with an increasing risk that this hike is delayed until the July or even September meetings, especially if (all else equal) the housing market continues to back peddle over the next couple of months. The risk of delay is even greater if the RBNZ's Governor opts to begin the tightening cycle with a more definitive 50bps move.

Figure 1: ANZ commodity price index



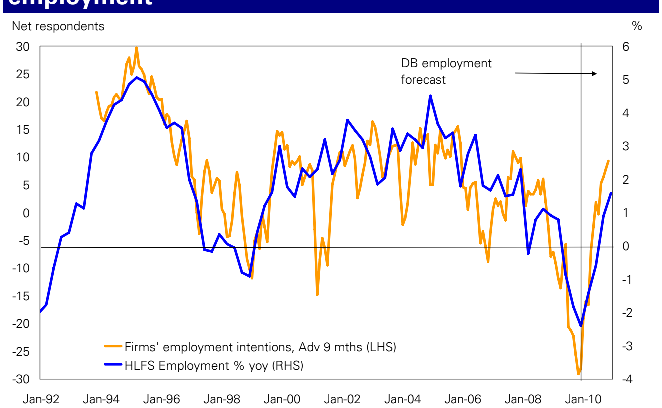
Source: Deutsche Bank, ANZ

Figure 2: NBNZ Own activity index & GDP



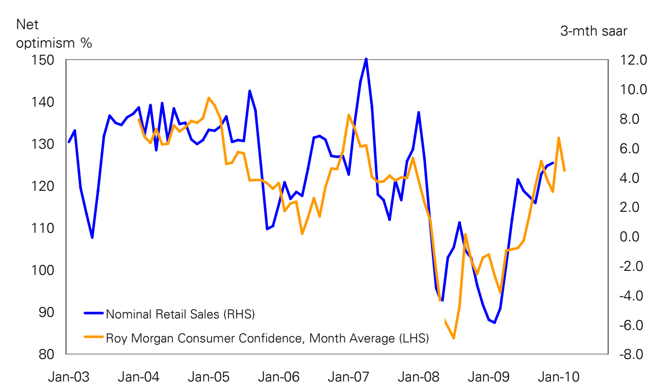
Source: Deutsche Bank, SNZ, NBNZ

Figure 3: NBNZ employment intentions index and employment



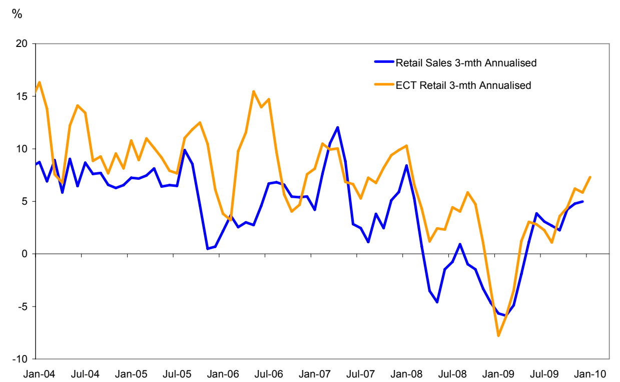
Source: Deutsche Bank, SNZ, NBNZ

Figure 4: Roy Morgan consumer confidence and retail sales



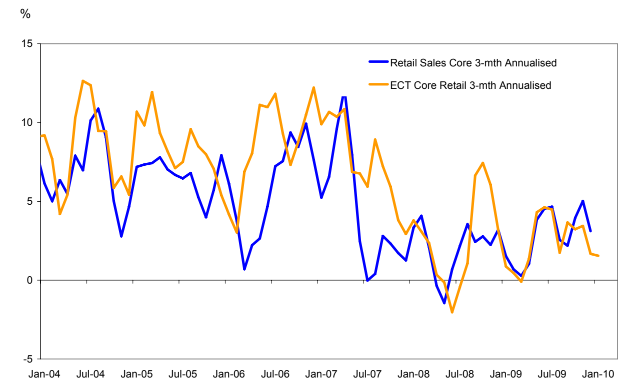
Source: Deutsche Bank, SNZ, Roy Morgan,

Figure 5: Headline official retail sales and electronic card transactions



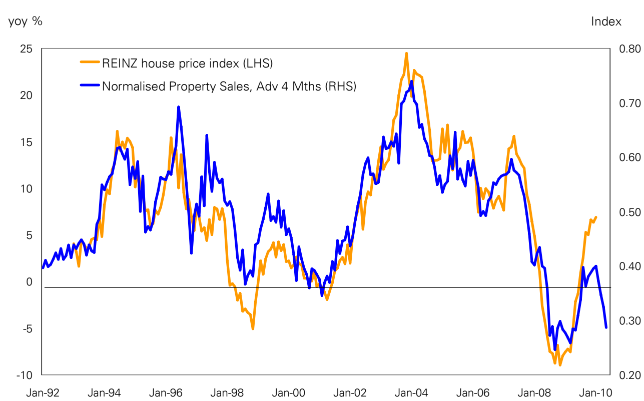
Source: Deutsche Bank, SNZ

Figure 6: Core official retail sales and electronic card transactions



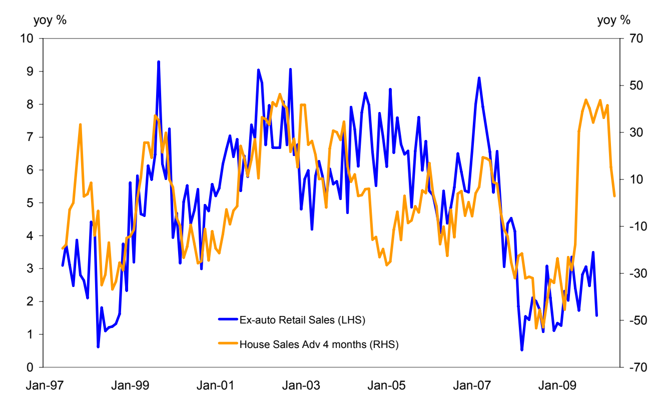
Source: Deutsche Bank, SNZ

Figure 7: House sales and prices



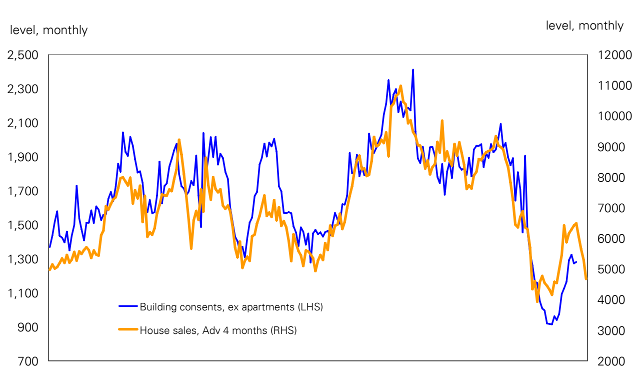
Source: Deutsche Bank, REINZ

Figure 8: House sales and core retail sales



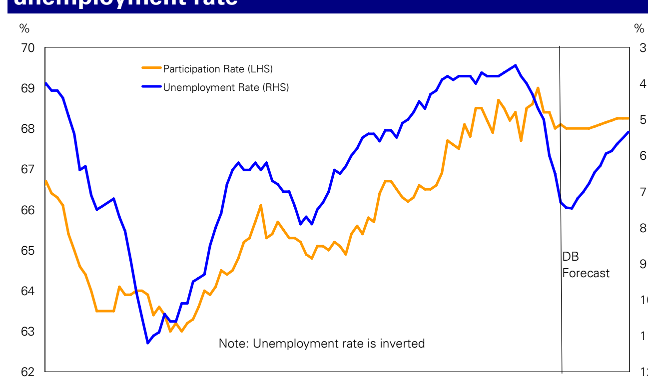
Source: Deutsche Bank, SNZ, REINZ

Figure 9: House sales and core dwelling consents



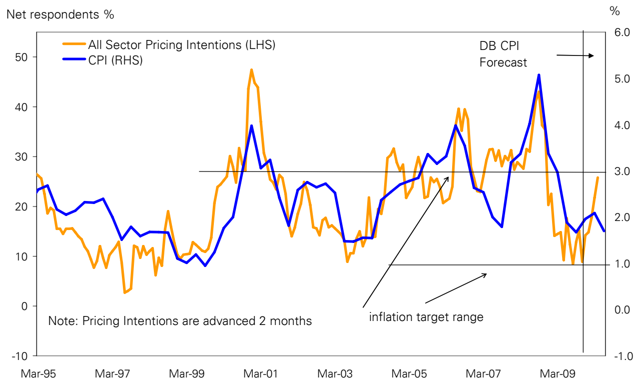
Source: Deutsche Bank, SNZ, REINZ

Figure 10: Labour force participation and the unemployment rate



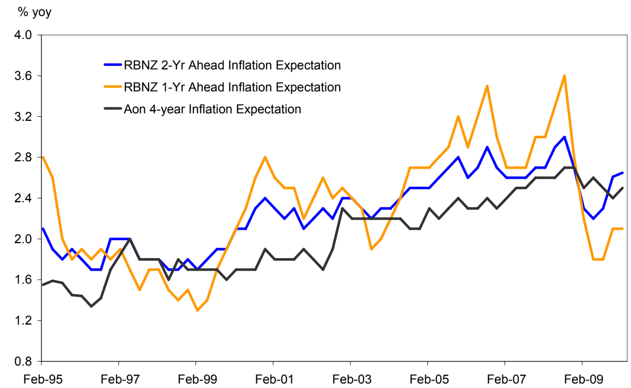
Source: Deutsche Bank, SNZ

Figure 11: NBNZ selling price intentions and CPI inflation



Source: Deutsche Bank, SNZ, NBNZ

Figure 12: Inflation expectations



Source: Deutsche Bank, RBNZ, AON

Table 1: RBNZ December MPS forecasts for growth and inflation

		Actual 2006/07	Actual 2007/08	Forecast 2008/09	Forecast 2009/10	Forecast 2010/11	Forecast 2011/12
March Qtr PRODUCTION GDP % yoy	RBNZ Dec	2.4	2.0	-2.6	1.9	4.2	3.4
CPI % yoy	RBNZ Dec	2.5	3.4	3.0	1.8	1.8	2.6

Source: RBNZ

Table 2: RBNZ December MPS 90 Day & TWI projections

	RBNZ Dec MPS	
	TWI	90-Day Bill Rate
Q1 09	53.7	3.7
Q2 09	58.4	2.9
Q3 09	62.6	2.8
Q4 09	66.0	2.8
Q1 10	66.5	2.8
Q2 10	66.6	2.9
Q3 10	66.2	3.3
Q4 10	65.5	3.5
Q1 11	64.5	3.9
Q2 11	63.4	4.4
Q3 11	62.2	4.7
Q4 11	61.2	5.1
Q1 12	60.5	5.6

The Bank's January Statement

The Reserve Bank today left the Official Cash Rate (OCR) unchanged at 2.5 percent.

Reserve Bank Governor Alan Bollard said: "The outlook for the New Zealand economy remains consistent with the projections underlying the December Monetary Policy Statement.

"Global activity continues to recover, helping push New Zealand's export commodity prices higher. Economic growth is most apparent in China, Australia, and emerging Asia. However, sustained growth throughout our trading partners is not assured, with many still facing impaired financial sectors and overall activity still reliant on policy support.

"Similarly, the New Zealand economy continues to recover. Policy stimulus and improving export earnings have seen a pickup in household spending. That said, households remain cautious, with credit growth subdued. Business spending remains weak.

"Annual CPI inflation is currently at the centre of the target band, and is expected to track comfortably within the band over the medium term.

"The economy is being assisted by both monetary and fiscal policy support. As growth becomes self sustaining, fiscal consolidation would help reduce the work that monetary policy might otherwise need to do.

"If the economy continues to recover in line with our December projections, we would expect to begin removing policy stimulus around the middle of 2010."

Appendix 1

Important Disclosures

Additional information available upon request

For disclosures pertaining to recommendations or estimates made on a security mentioned in this report, please see the most recently published company report or visit our global disclosure look-up page on our website at http://gm.db.com/ger/disclosure/DisclosureDirectory.eqsr**.**

Analyst Certification

The views expressed in this report accurately reflect the personal views of the undersigned lead analyst(s). In addition, the undersigned lead analyst(s) has not and will not receive any compensation for providing a specific recommendation or view in this report. Darren Gibbs

Regulatory Disclosures

1. Important Additional Conflict Disclosures

Aside from within this report, important conflict disclosures can also be found at https://gm.db.com/equities under the "Disclosures Lookup" and "Legal" tabs. Investors are strongly encouraged to review this information before investing.

2. Short-Term Trade Ideas

Deutsche Bank equity research analysts sometimes have shorter-term trade ideas (known as SOLAR ideas) that are consistent or inconsistent with Deutsche Bank's existing longer term ratings. These trade ideas can be found at the SOLAR link at http://gm.db.com.

3. Country-Specific Disclosures

Australia: This research, and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act.
EU countries: Disclosures relating to our obligations under MiFiD can be found at http://globalmarkets.db.com/riskdisclosures.
Japan: Disclosures under the Financial Instruments and Exchange Law: Company name – Deutsche Securities Inc. Registration number – Registered as a financial instruments dealer by the Head of the Kanto Local Finance Bureau (Kinsho) No. 117. Member of associations: JSDA, The Financial Futures Association of Japan. This report is not meant to solicit the purchase of specific financial instruments or related services. We may charge commissions and fees for certain categories of investment advice, products and services. Recommended investment strategies, products and services carry the risk of losses to principal and other losses as a result of changes in market and/or economic trends, and/or fluctuations in market value. Before deciding on the purchase of financial products and/or services, customers should carefully read the relevant disclosures, prospectuses and other documentation.
Malaysia: Deutsche Bank AG and/or its affiliate(s) may maintain positions in the securities referred to herein and may from time to time offer those securities for purchase or may have an interest to purchase such securities. Deutsche Bank may engage in transactions in a manner inconsistent with the views discussed herein.
New Zealand: This research is not intended for, and should not be given to, "members of the public" within the meaning of the New Zealand Securities Market Act 1988.
Russia: This information, interpretation and opinions submitted herein are not in the context of, and do not constitute, any appraisal or evaluation activity requiring a license in the Russian Federation.

Risks to Fixed Income Positions

Macroeconomic fluctuations often account for most of the risks associated with exposures to instruments that promise to pay fixed or variable interest rates. For an investor that is long fixed rate instruments (thus receiving these cash flows), increases in interest rates naturally lift the discount factors applied to the expected cash flows and thus cause a loss. The longer the maturity of a certain cash flow and the higher the move in the discount factor, the higher will be the loss. Upside surprises in inflation, fiscal funding needs, and FX depreciation rates are among the most common adverse macroeconomic shocks to receivers. But counterparty exposure, issuer creditworthiness, client segmentation, regulation (including changes in assets holding limits for different types of investors), changes in tax policies, currency convertibility (which may constrain currency conversion, repatriation of profits and/or the liquidation of positions), and settlement issues related to local clearing houses are also important risk factors to be considered. The sensitivity of fixed income instruments to macroeconomic shocks may be mitigated by indexing the contracted cash flows to inflation, to FX depreciation, or to specified interest rates – these are common in emerging markets. It is important to note that the index fixings may -- by construction -- lag or mis-measure the actual move in the underlying variables they are intended to track. The choice of the proper fixing (or metric) is particularly important in swaps markets, where floating coupon rates (i.e., coupons indexed to a typically short-dated interest rate reference index) are exchanged for fixed coupons. It is also important to acknowledge that funding in a currency that differs from the currency in which the coupons to be received are denominated carries FX risk. Naturally, options on swaps (swaptions) also bear the risks typical to options in addition to the risks related to rates movements.

David Folkerts-Landau
Managing Director
Global Head of Research

Stuart Parkinson	Guy Ashton	Marcel Cassard
Chief Operating Officer	Global Head Company Research	Global Head Fixed Income Strategies and Economics

Germany	Asia-Pacific	Americas
Andreas Neubauer Regional Head	Michael Spencer Regional Head	Steve Pollard Regional Head

Principal Locations

Deutsche Bank AG
London
1 Great Winchester Street
London EC2N 2EQ
Tel: (44) 20 7545 8000

Deutsche Bank AG
New York
60 Wall Street
New York, NY 10005
United States of America
Tel: (1) 212 250-2500

Deutsche Bank AG
Hong Kong
Cheung Kong Center,
2 Queen's Road Central
Hong Kong
Tel: (52) 2203 8888

Deutsche Bank AG
Japan
2-11-1 Nagatacho
Sanno Park Tower
Chiyoda-ku, Tokyo 100-6171
Tel: (81) 3 5156 6701

Deutsche Bank AG
Frankfurt
Große Gallusstraße 10-14
60272 Frankfurt am Main
Germany
Tel: (49) 69 910 00

Deutsche Bank AG
Aurora business park
82 bld.2 Sadovnicheskaya street
Moscow, 115035
Russia
Tel: (7) 495 797-5000

Deutsche Bank AG
Singapore
One Raffles Quay
South Tower
Singapore 048583
Tel: (65) 6423 8001

Deutsche Bank AG
Australia
Deutsche Bank Place, Level 16
Corner of Hunter & Phillip Streets
Sydney NSW 2000
Tel: (61) 2 8258 1234

Deutsche Bank Dubai
Dubai International Financial Centre
The Gate, West Wing, Level 3
P.O. Box 504 902
Dubai City
Tel: (971) 4 3611 700

Subscribers to research via email receive their electronic publication on average 1-2 working days earlier than the printed version.

If you would like to receive this or any other product via email please contact your usual Deutsche Bank representative.

Publication Address:
Deutsche Bank AG
Deutsche Bank Place
Level 16Corner of Hunter & Phillip Streets
Sydney, NSW 2000Australia
(61) 2 8258 1234

Internet:
http://gmr.db.com
Ask your usual contact for a username and password.

Global Disclaimer

The information and opinions in this report were prepared by Deutsche Bank AG or one of its affiliates (collectively "Deutsche Bank"). The information herein is believed to be reliable and has been obtained from public sources believed to be reliable. Deutsche Bank makes no representation as to the accuracy or completeness of such information.

Deutsche Bank may (1) engage in securities transactions in a manner inconsistent with this research report, (2) with respect to securities covered by this report, sell to or buy from customers on a principal basis, and (3) consider this report in deciding to trade on a proprietary basis.

Opinions, estimates and projections in this report constitute the current judgement of the author as of the date of this report. They do not necessarily reflect the opinions of Deutsche Bank and are subject to change without notice. Deutsche Bank has no obligation to update, modify or amend this report or to otherwise notify a recipient thereof in the event that any opinion, forecast or estimate set forth herein, changes or subsequently becomes inaccurate. Prices and availability of financial instruments are subject to change without notice. This report is provided for informational purposes only. It is not an offer or a solicitation of an offer to buy or sell any financial instruments or to participate in any particular trading strategy. Target prices are inherently imprecise and a product of the analyst judgement.

The financial instruments discussed in this report may not be suitable for all investors and investors must make their own informed investment decisions. Stock transactions can lead to losses as a result of price fluctuations and other factors. If a financial instrument is denominated in a currency other than an investor's currency, a change in exchange rates may adversely affect the investment. Past performance is not necessarily indicative of future results.

Unless governing law provides otherwise, all transactions should be executed through the Deutsche Bank entity in the investor's home jurisdiction. In the U.S. this report is approved and/or distributed by Deutsche Bank Securities Inc., a member of the NYSE, the NASD, NFA and SIPC. In Germany this report is approved and/or communicated by Deutsche Bank AG Frankfurt authorized by the BaFin. In the United Kingdom this report is approved and/or communicated by Deutsche Bank AG London, a member of the London Stock Exchange and regulated by the Financial Services Authority for the conduct of investment business in the UK and authorized by the BaFin. This report is distributed in Hong Kong by Deutsche Bank AG, Hong Kong Branch, in Korea by Deutsche Securities Korea Co. This report is distributed in Singapore by

Deutsche Bank AG, Singapore Branch, and recipients in Singapore of this report are to contact Deutsche Bank AG, Singapore Branch in respect of any matters arising from, or in connection with, this report. Where this report is issued or promulgated in Singapore to a person who is not an accredited investor, expert investor or institutional investor (as defined in the applicable Singapore laws and regulations), Deutsche Bank AG, Singapore Branch accepts legal responsibility to such person for the contents of this report. In Japan this report is approved and/or distributed by Deutsche Securities Inc. The information contained in this report does not constitute the provision of investment advice. In Australia, retail clients should obtain a copy of a Product Disclosure Statement (PDS) relating to any financial product referred to in this report and consider the PDS before making any decision about whether to acquire the product. Deutsche Bank AG Johannesburg is incorporated in the Federal Republic of Germany (Branch Register Number in South Africa: 1998/003298/10). Additional information relative to securities, other financial products or issuers discussed in this report is available upon request. This report may not be reproduced, distributed or published by any person for any purpose without Deutsche Bank's prior written consent. Please cite source when quoting.