Market Focus

New Zealand

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THE MARKET AND THE RBNZ

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Page 2: Economic overview

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Page 5: Economic comment – financial conditions update

> Credit markets continue to show signs of improvement and equity markets have largely held on to recent gains. This has translated into further improvements in our Financial Conditions Indices (FCI), which suggest the trough in real economic activity is at hand. However, the speed of recovery is still uncertain at this stage.

Page 7: Economic comment – monthly inflation gauge

> Our experimental monthly inflation gauge was essentially flat in May. Barring a surprise spike in June, we are potentially looking at the softest quarterly non-tradable CPI print for Q2 in some time time. This will certainly tie in with the RBNZ's view of lower inflationary pressure, and keeping rates lower for longer.

Page 8: Economic comment – global watch

> The data was reasonably mixed last week. Better than expected Australian employment data shows that that economy continues to hold up better than most other developed nations. US retail sales posted their first monthly increase in three months, while the number of jobless continues to rise. Chinese trade data was weak and while industrial production improved, it shows that green shoots remain fragile.

Page 10: Interest rate strategy

> There is a massive disconnect between market pricing and the RBNZ's stated policy view. While we expect a "gap" to remain based on historical trends, we nonetheless expect the magnitude to close towards the RBNZ view. But the market will remain wary of positioning and mortgage paying flows.

Page 11: Currency strategy

> The G8 talks of the withdrawal of stimulus and a return to normality, and markets are responding. US 10 year bonds continue their rally from the 4 percent level seen last week. The question to be asked is what is normal for a currency that has seen above 80 cents and below 50 cents in the past 15 months. The market will go back to focusing on yield differentials, growth differentials, commodity prices and potentially swine flu. External imbalances do not appear to feature heavily as yet.

ECONOMIC OVERVIEW

We now expect 2.5 percent to be the trough in the OCR, absent a major systemic event offshore or the market pushing too far against the RBNZ's "lower for longer" message resulting in overtly tighter financial conditions. De-leveraging remains a major theme for the economy and within our forecasts. Activity across deposit rates continues to bear this out. With a significant downward correction in NZD/USD somewhat constrained by a weak USD (although we still expect weakness), we now expect the NZD/AUD to act as more of a release valve.

What's ahead?

> **NZ March quarter Economic Survey of Manufacturing** (Monday 1045 NZST). Manufacturing production is expected to have contracted given sector trends in the National Bank *Business Outlook* and also the Business NZ PMI survey.

Addendum: Manufacturing sales volumes rose 0.2 percent in the quarter, driven by meat and dairy product manufacturing. Excluding dairy and meat, sales fell 6.5 percent. Adjusting for inventory changes, we estimate that non-primary food manufacturing production fell around 5.5 percent and will act as a considerable drag on GDP growth in the quarter.

What's the view?

The RBNZ's decision to leave the OCR unchanged at 2.50 percent, and the subsequent market reaction, was obviously the big talking point last week. The RBNZ now appear comfortable with the current policy setting and barring any major deterioration in economic prospects or systemic risks emerging in the financial system, we now feel the easing cycle is over. But while the Bank did not cut, the spirit of what they were trying to do was ram home their message they have delivered previously: this adjustment will take some time to play out and that *"it is likely to be some time before the recovery becomes self-sustaining and monetary policy support can be withdrawn."* We totally agree, and are not expecting interest rate hikes until late 2010.

You could argue from the reaction to the *Statement* that the market was not really listening or misread the message or both. We suspect this is the case in some instances and a relatively dovish statement was taken the other way. The swaps market sold off aggressively, with the curve closing 12 to 24 basis points higher on the day, and interest rate hikes being priced in from early next year – in stark contrast to what the RBNZ have explicitly stated. However, when there is a belief in some quarters that the RBNZ has stopped cutting, the natural reaction for the market is to begin pricing in the reverse and a lot of the reaction on the day was not much more than position unwinding and noise. Hence, looking forward, it will be critical to keep maintaining those lower for longer nuances. If the market does not correct over the coming days we would not at all be surprised to see some explicit communication from the RBNZ to "clarify" its June *Statement*. Likewise, the Bank may feel it necessary to tweak the OCR further in July as a reminder, if financial conditions continue to tighten. This is not our core view, but something we are mindful of at present.

When it comes to interest rates, most attention focuses on the OCR, wholesale rates, and lending rates. These are all important – up to a point, and higher wholesale interest rates (for now anyway) make it difficult to see borrowing rates falling. But probably the most important interest rates to monitor at present are deposit rates.

A key theme underpinning our macroeconomic view is one of rebalancing. That is, the reallocation of resources and the focus of growth away from a model of debt fuelled consumption and towards export and earnings centric growth – a view that underpins the RBNZ's assessment as well. Rising deposit rates – as a relative price mechanism encouraging saving for tomorrow as opposed to spending for today – are merely reflective of that process. When there is a limited pool of something such as savings, Economics 101 tells us that the price has to go up, which is precisely what is happening. Of course investors "win" under this scenario but borrowers "lose".

The fact credit markets are freeing up offshore is certainly encouraging, and gives greater capacity to fund offshore, which on the face of it should ease pressure in the deposit space and also potentially on borrowing rates. But this also misses the point and is a rather narrow interpretation.

> NZ is already overly reliant on offshore capital, so we cannot continue to borrow offshore willy-nilly, even if it is getting cheaper relative to recent extremes seen. The prudent thing to do is in fact to fund domestically. As the RBNZ noted in their May *Financial Stability Report* *"…debt levels are high in New Zealand, and there is significant reliance on offshore financing. Following an extended period of large current account deficits, net international liabilities had increased to more than 90 percent of GDP by the end of 2008. …the scale of New Zealand's external debt liabilities implies significant exposure to developments in international capital markets."*

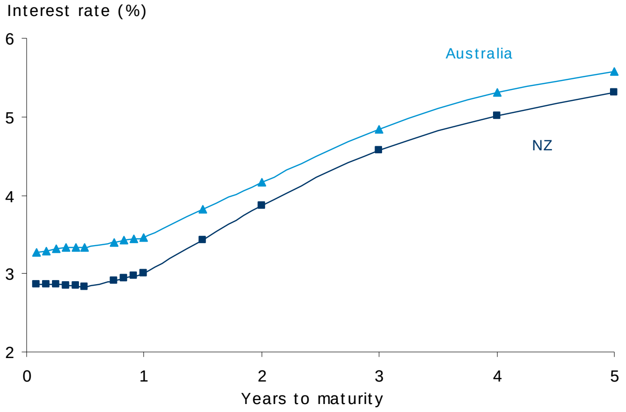
> There is intense competition for cash domestically from other areas including corporate issuance.

> Retail investors are targeting nominal as opposed to real returns. A year ago 90-day, 1 and 2 year deposit rates sat around 6½ to 8 percent. Annual inflation was 5 percent. Now, 90-day, 1 and 2 year rates sit at 4 to 5.5 percent, and the RBNZ's latest projections had headline inflation falling to 1 percent in 2009. Investors are actually better off in a real sense under the latter scenario, but this is certainly not the perception with yield expectations nominal as opposed to real driven. Hence, the same frustration the RBNZ had when it needed to raise nominal interest rates further to cool the housing market, are now playing out in the deposit space.

Collectively, it's all part of getting the current account deficit down, and reducing NZ's debt burden, which is amongst the highest in the OECD. As far as interest rates go, the most important benchmark we check each day in terms of testing our macroeconomic assessment is deposit rates. The more intense we see pressure across deposits, then the more we become convinced that a de-leveraging dynamic – a critical part of improving NZ's poor current account position and increasing national savings – is taking hold.

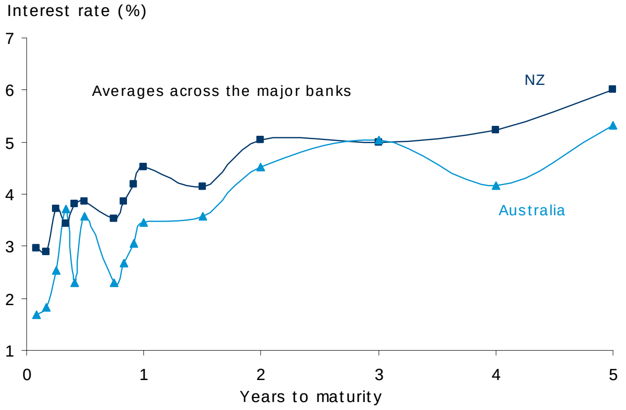
This theme can easily be shown by comparing NZ and Australia's wholesale interest rates and retail deposit rates. While Australia runs a current account deficit as well, there is no where near the same intense pressure to undergo a correction given the current position (-4.2 percent of GDP versus -8.9 in NZ and the same applies for the stock of debt). Despite NZ's wholesale interest rates sitting below those of Australia, due in part to a weaker economy and a lower central bank policy rate, NZ's retail deposit rates are higher. In fact, on average NZ's wholesale interest rate curve sits around 40bps below Australia's, while the retail deposit curve is around 82bps higher. Once again, it's a simple story of the price having to adjust to reflect a limited pool of savings and so long as we see this dynamic at work, de-leveraging will remain a key focal point within our economic assessment for NZ.

NZ and Australia wholesale curves



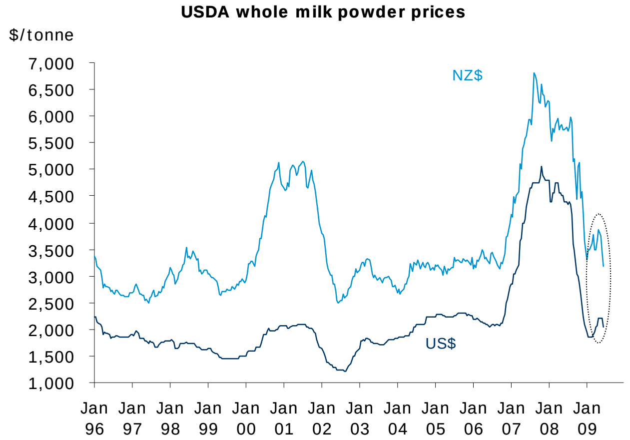
Sources: ANZ National, Bloomberg

NZ and Australia deposit curves



Sources: ANZ National, www.interest.co.nz, www.interest.com.au

Going forward we continue to see the NZD as a key part of this de-leveraging and rebalancing process. You only have to look at the challenges at present for NZ's two largest export earners (tourism and dairy) to know that the NZ economy cannot sustain a currency around current levels. Despite global commodity prices jumping on the "green shoots" bandwagon of late, with the CRB index up around 32 percent from its trough, these are not the commodities that NZ generally exports. USDA dairy prices for the past fortnight actually fell 6.8 in USD terms, and 7.3 percent in NZD terms. The recent decision by the World Health Organisation to officially declare a flu pandemic is also not great news for our tourism industry if the uncertainty sees travellers decide to remain at home. In addition to these developments, the latest Business NZ PMI survey for May (where the index fell to 42.7) shows that the manufacturing sector remains well entrenched in contraction mode.



Sources: ANZ National, USDA, Bloomberg

This leaves us with little doubt that the currency will eventually adjust lower. However, there are a couple of uncertainties we are pondering. First is the timing. Ironically, the path to a lower currency may be to crush the economy first. As the RBNZ noted in the *Statement*: *"The recent rise in the New Zealand dollar creates an unhelpful tension with our projections. A stronger dollar at a time of weak global growth risks delaying or even reversing the projected increase in exports, putting the sustainability of recovery at risk."* The second is who the adjustment takes place against. The US economy is facing structural issues of its own, which is weighing on the USD. While we have our reservations against how low the USD can go given risks we feel are emerging in the likes of Europe (and a bounce looks imminent), the world seems happy for the US economy to go through an adjustment first.

Our Australian counterparts have put through some pretty significant revisions for the AUD/USD in light of recent trends, which we obviously need to be mindful of for the NZD. Where possible we've heavily tempered it to keep the spirit of a weaker NZD/USD intact (we still see 54 cents in 2010 and are mindful of another run down the elevator with the EUR/USD looking very extended), but it does mean a more protracted correction in the NZD/AUD. We now expect the NZD/AUD to head to a low of 0.73 by the middle of next year and near the lows recorded in the early 1990s. While this seems a major call, and most tend to anchor a weaker NZD/AUD off the respective economic outlooks and wholesale interest rate assessments, we are taking more comfort from what the respective deposit curves are telling us about the rebalancing dynamics required, and what is in fact taking place across the two economies. (Note: we are releasing a new FX Quantitative product this week. If you would like to receive it please email one of the authors on the front page).

Turning to the events this week, there is not a lot to discuss in terms of local data. Internationally, the main releases will be the meeting minutes from the RBA, BoE and BoJ. All these central banks left their respective policy rates unchanged, and so the focus will be on how close those decisions were, and some of the themes the policy makers are noticing. In terms of data, inflation is the underlying theme, with CPI data released in the US, UK and Euro-zone. The Philadelphia Fed survey, which is a good leading gauge for the US economy, will also be of interest to see if the recent improvement is sustained.

Recent local data…

> **Value of Building Work Put in Place (March quarter):** The volume of residential construction fell 0.4 percent, while non-residential building work fell 1.0 percent.

> **Overseas Trade Indexes (March quarter):** The merchandise terms of trade fell 3.0 percent driven by an 8.2 percent fall in export prices. Export volumes rose 2.0 percent, while import volumes contracted 9.8 percent.

> **Electronic Card Transaction (May):** Total retail spending rose 0.7 percent, while core spending rose 1.6 percent.

> **RBNZ *Monetary Policy Statement*:** The RBNZ left the OCR unchanged at 2.50 percent.

> **BNZ Capital Business NZ PMI (May):** The index fell to 42.7, from 43.7 in April.

> **REINZ House Sales (May):** In seasonally adjusted terms, house sales fell 13.3 percent, following a 22.6 percent surge in April. Days to sell continues to fall, with the median at 41 days.

> **Retail Trade Survey (April):** Total retail spending rose 0.5 percent, while core spending fell 0.1 percent.

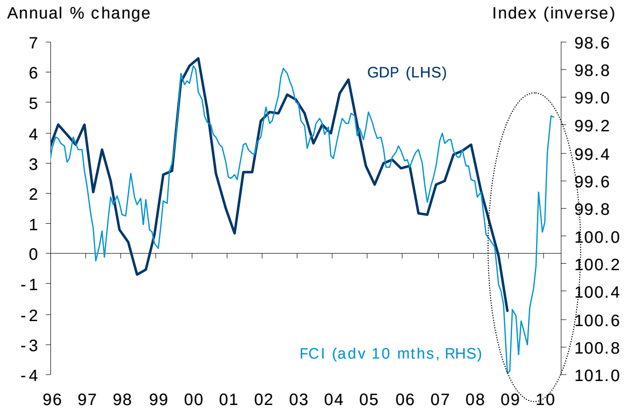
FINANCIAL CONDITIONS UPDATE

Credit markets continue to show signs of improvement and equity markets have largely held on to recent gains. This has translated into further improvements in our Financial Conditions Indices (FCI), which suggest the trough in real economic activity is at hand. However, the speed of recovery is still uncertain at this stage.

"Some clear upside opportunities"

In last week's *Monetary Policy Statement*, the RBNZ expressed concern that *"a premature tightening in financial conditions could undermine the recovery."* Certainly, swap yields and the NZD have moved higher throughout May and into the early part of June. But despite that, our NZ FCI indicates a further easing in conditions. A rally in NZ equities, slight easing in lending standards from the US Federal Reserve Senior Loan Officer Survey (which we use as a proxy for the supply of credit), and further narrowing in the credit default swap spreads for the big four Australian banks (a proxy for the cost of funds) have more than offset the impact of higher yields and the currency.

NZ GDP vs Financial Conditions Index



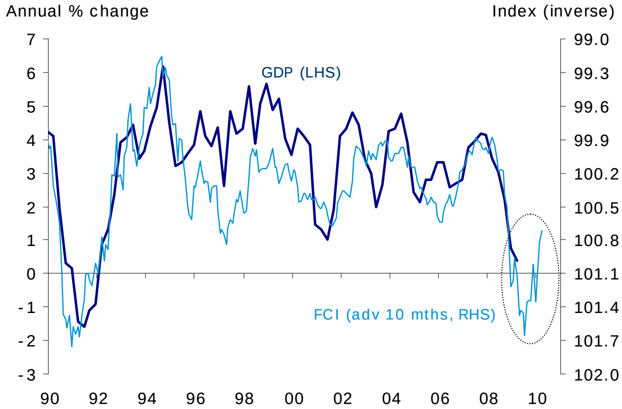
Sources: ANZ National, Statistics NZ

At current levels, our FCI is flagging a rebound in activity from early 2010 with annual GDP growth potentially heading past 4 percent by late 2010. Such a profile is a reflection of the deep trough the economy is recovering from, but does hint of the upside that the RBNZ sees. But we remain mindful that our FCI may not be fully capturing certain structural aspects to this economic cycle, such as the mitigating effects that deposit rates are having on the monetary policy channel. With a lower dairy payout and downside risks to tourism from the influenza pandemic alert weighing on the economic outlook, the eventual recovery may indeed prove to be *"slow and fragile"* just like the RBNZ said.

Avoiding the dreaded R but for how long?

The Australian economy avoided the technical definition of a recession by expanding in Q1. But it is not out of the woods yet, with our Australian FCI pointing to further weakness in activity ahead. Despite a higher AUD and swap yields, this was offset by a rally in equities and narrowing in banks' credit default swap spreads. Even then, our FCI continues to point to negative year-on-year growth, though it will be of the "lite" variety compared to the recessions that other developed economies are going through. The Australian economy then looks set to head back into positive annual growth by the end of this year or early next year, with a somewhat modest rebound – a reflection of the fairly shallow dip the economy is expected to go through.

AU GDP vs Financial Conditions Index

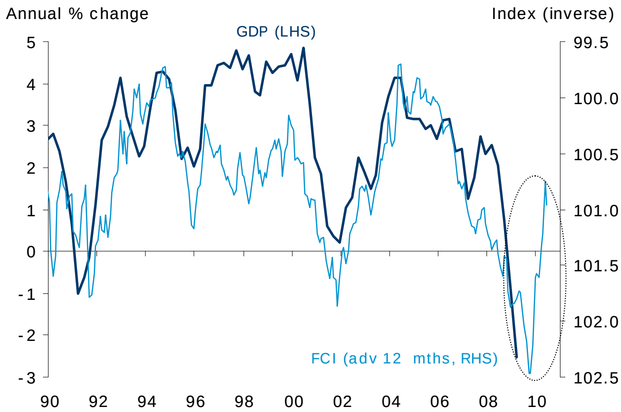


Sources: ANZ National, Bloomberg

Watch out for frost

The light at the end of the tunnel is starting to shine through in the US. The green shoots could yet grow taller, which is what our US FCI is suggesting. A weak USD, recovering equities and a financial system that is slowly healing bodes well for the outlook and has kept financial conditions on the easy side. But recent increases in bond yields, not to mention higher gasoline prices, could yet threaten the fragile recovery.

US GDP vs Financial Conditions Index



Sources: ANZ National, Bloomberg

The upshot

Our FCI points to a return to positive growth by the end of this year or early next year. Signs of improvement in global credit markets, as shown by narrowing swap spreads, are welcome. Increased investor confidence, which have seen equities rise and largely holding on to recent gains, have also helped ease financial conditions. Overall, it suggests a trough in real economic activity may be at hand. But while our FCI suggests a turnaround soon, higher longer term yields and potential structural changes to the traditional financial conditions linkages to the real economy as a result of the financial crisis, mean the extent of any recovery is uncertain at this stage. Specifically, coefficient estimates will not be constant over time, and of course the credit channel of monetary policy is having a more significant impact on the economy than the traditional monetary policy channel (i.e. wholesale versus deposit curve). These are aspects we continue to assess and research how to integrate into our specifications.

MONTHLY INFLATION GAUGE[1]

Our experimental monthly inflation gauge was essentially flat in May. Barring a surprise spike in June, we are potentially looking at the softest quarterly non-tradable CPI print for Q2 in some time time. This will certainly tie in with the RBNZ's view of lower inflationary pressure, and keeping rates lower for longer.

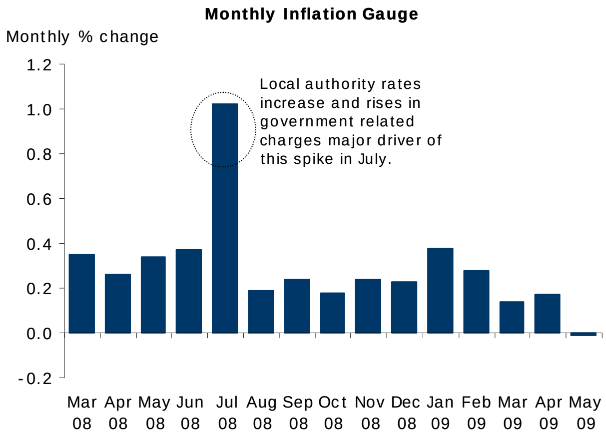
Following a 0.2 percent increase in April, our monthly inflation gauge was flat in May. In fact, based on the second decimal point, the gauge actually recorded a very small decline. This is the softest reading since we began collecting data for our gauge in March last year.

Over May, price rises for alcohol as well as for miscellaneous goods and services were recorded. Prices increases were also put through in medical services. These were offset by lower housing related costs (specifically construction costs) and the transport group. The latter likely reflects ongoing soft construction activity, which is at its lowest level in decades. Rents remain flat, and we are yet to see any signs of upward pressure stemming from the recent strong pick-up in net migration.

While our monthly inflation gauge has not been running very long, there has been a discernable trend emerging which shows easing domestic inflation pressure. In the early part of last year, our gauge was recording monthly increases of 0.3 to 0.4 percent. In the second half of last year, this eased towards 0.2 percent (abstracting from the 1 percent spike in July 2008 which was driven by local authority rate increases and government related charges). It will be some months yet before we can be certain whether the May reading was an anomaly, or an indication of further easing pricing momentum. Even if June was another soft month, July is likely to see a spike due to local authority rates and other government related price increases.

Barring an unexpected spike in June, Q2 non-tradable CPI is looking on the soft side, which would not exactly be a surprise given the amount of spare capacity being freed up in the economy (falling capacity utilisation, rising unemployment rate, large negative output gap etc). Looking at the RBNZ's latest non-tradable CPI projections, they are expecting a 0.5 percent increase for Q2. But the Bank then expects a few quarters of very soft prints of around 0.1 percent from Q3. This implies quite an extended period where our monthly inflation gauge will print flat to 0.1 percent, implying no pricing power at all for firms.

	Monthly Inflation Gauge (m/m%)	Implied Inflation Gauge (q/q%)	Actual non-tradable CPI (q/q%)
Mar-08	0.4		1.1
Apr-08	0.3		
May-08	0.3		
Jun-08	0.4	1.0	0.9
Jul-08	1.0		
Aug-08	0.2		
Sep-08	0.2	1.4	1.3
Oct-08	0.2		
Nov-08	0.2		
Dec-08	0.2	0.7	0.8
Jan-09	0.4		
Feb-09	0.3		
Mar-09	0.1	0.8	0.7
Apr-09	0.2		
May-09	0.0		



Source: ANZ National

The next steps

Our gauge has managed to track the actual Statistics NZ non-tradable CPI print so far, which gives us confidence that we are on the right track. We are in the process of making further refinements to our methodology, and the Q2 outturn will give us another benchmark to compare how our gauge is tracking. After that, we will look to drop the "experimental" tag and formally launch the monthly inflation gauge, joining our other suite of survey publications.

[1] Our monthly inflation gauge is intended to provide a timely indication of domestic inflation trends. For simplicity, we have limited ourselves to a domestic or non-tradable inflation measure. It should be noted that our monthly inflation gauge will not exactly mirror the official non-tradable CPI due to coverage and methodological issues. Our main priority is to come up with a gauge that is timely and able to provide an indication of domestic inflation trends. This will allow us to assess whether inflation pressures remain, or whether they are starting to ease. Our gauge, however, is designed to be as comparable as possible to the official Statistics NZ series. Note that our gauge is still in the experimental stages, and is subject to further refinements.

GLOBAL DATA WATCH

The data around the globe was reasonably mixed last week. Better than expected Australian employment data shows that that economy continues to hold up better than most other developed nations. US retail sales posted their first monthly increase in three months, while the number of jobless continues to rise. Chinese trade data was weak and while industrial production improved, it shows that green shoots remain fragile.

Country / Area	Indicator	Market	Actual	Last	Outturn vs market
Australia	Westpac Consumer Confidence (Jun) - mom	-	12.7%	-4.3%	-
	Home Loans (Apr) – mom	1.5%	0.9%	4.8%	Weaker
	Employment Change (May)	-30.0K	-1.7K	25.4K	Stronger
	Unemployment Rate (May)	5.7%	5.7%	5.5%	In-line
US	Wholesale Inventories (Apr)	-1.2%	-1.4%	-1.8%	Weaker
	Trade Balance (Apr)	-$29.0B	-$29.2B	-$28.5B	In-line
	Monthly Budget Statement (May)	-$181.0B	-$189.7B	-$165.9B	Weaker
	Advance Retail Sales (May)	0.5%	0.5%	-0.2%	In-line
	Continuing Jobless Claims (w/e May 31)	6,780K	6,816K	6,757K	Weaker
	Business Inventories (Apr)	-1.0%	-1.1%	-1.3%	In-line
	Import Price Index (May) – mom	1.4%	1.3%	1.1%	In-line
	University of Michigan Confidence (Jun P)	69.5	69.0	68.7	In-line
Euro-zone	Sentix Investor Confidence (Jun)	-31.0	-27.0	-34.3	Stronger
	Industrial Production (Apr) - mom	-0.4%	-1.9%	-1.4%	Weaker
UK	RICS House Price Balance (May)	-52.0%	-44.1%	-58.7%	Stronger
	DCLG House Prices (Apr) – yoy	-13.3%	-13.0%	-13.6%	In-line
	Total Trade Balance (Apr)	-£2400M	-£3014M	-£2716M	Weaker
	Industrial Production (Apr) – mom	-0.1%	0.3%	-0.3%	Stronger
Japan	Money Stock M3 (May) – yoy	1.7%	1.8%	1.7%	In-line
	Adjusted Current Account (Apr)	¥960.0B	¥966.3B	¥902.3B	In-line
	Eco Watchers Survey: Current (May)	34.0	36.7	34.2	Stronger
	Leading Index CI (Apr P)	77.2	76.5	75.5	Weaker
	Machine Orders (Apr) – mom	-0.6%	-5.4%	-1.3%	Weaker
	Domestic CGPI (May) – mom	-0.3%	-0.4%	-0.6%	In-line
	GDP (1Q F) – qoq	-4.0%	-3.8%	-4.0%	Stronger
	Industrial Production (Apr F) – mom	-	5.9%	5.2%	-
	Consumer Confidence (May)	34.0	36.3	33.2	Stronger
Asia Ex-Japan					
China	PPI (May) – yoy	-6.9%	-7.2%	-6.6%	Weaker
	CPI (May) – yoy	-1.3%	-1.4%	-1.5%	In-line
	Exports (May) – yoy	-23.0%	-26.4%	-22.6%	Weaker
	Imports (May) – yoy	-22.0%	-25.2%	-23.0%	Weaker
	Money Supply M2 (May) – yoy	25.9%	25.7%	26.0%	In-line
	Retail Sales (May) – yoy	15.0%	15.2%	14.8%	In-line
	Industiral Production (May) – yoy	7.7%	8.9%	7.3%	Stronger
South Korea	PPI (May) – yoy	-	-1.3%	1.5%	-
	Unemployment Rate (May)	3.8%	3.9%	3.7%	Weaker
	BoK 7-Day Repo Rate (Jun)	2.0%	2.00%	2.00%	In-line
Hong Kong	Industrial Production (1Q) – yoy	-	-10.2%	-10.6%	-

Continued over page

Country / Area	Indicator	Market	Actual	Last	Outturn vs market
Hong Kong cont.	Producer Prices (1Q) - yoy	-	-1.4%	3.9%	-
Taiwan	Exports (May) – yoy	-34.0%	-31.4%	-34.3%	Stronger
	Imports (May) – yoy	-39.0%	-39.1%	-41.2%	In-line
India	Industrial Production (Apr) - yoy	-0.1%	1.4%	-0.8%	Stronger
Indonesia	Money Supply (Apr) – yoy	-	18.4%	20.3%	-
Philippines	Total Exports (Apr P) - yoy	-34.4%	-35.2%	-30.8%	Weaker
Malaysia	Industrial Production (Apr) – yoy	-15.2%	-11.4%	-12.7%	Stronger
Thailand	Consumer Confidence (May)	-	64.3	65.1	-

INTEREST RATE STRATEGY

There is a massive disconnect between market pricing and the RBNZ's stated policy view. While we expect a "gap" to remain based on historical trends, we nonetheless expect the magnitude to close towards the RBNZ view. But the market will remain wary of positioning and mortgage paying flows.

Market themes…

- RBNZ pauses and reiterates "lower for longer" message.
- NZ rates market starts to price in hikes from early next year (prematurely in our view).
- US 10-year bond yields close in on 4% – a key technical level.
- G8 Communiqué talking about exit strategies for unwinding stimulus ultimately positive for bonds as it reduces inflation risks.

Review and outlook

With the RBNZ pausing and signalling that, barring any unforeseen deterioration in economic prospects or a rise in systemic risks, the easing cycle is over, the rates market has moved swiftly to start pricing in the tightening cycle. A full rate hike has been priced in by March next year, and the June 2010 bank bill futures is implying a 90-day rate of 3.84 percent, despite the RBNZ projecting it staying at 2.8% until late 2010. There is clearly a disconnect between market pricing and RBNZ policy. Indeed, the RBNZ's message seems to have gotten lost in the midst of the reaction following the pause decision. It is worth recounting that the RBNZ said *"it is likely to be some time before the recovery becomes self-sustaining and monetary policy support can be withdrawn"*, *"The OCR could still move modestly lower over the coming quarters"*, *"we expect to keep the OCR at or below the current level through until the latter part of 2010"*, and the Bank's 90-day projections had it staying below 3% until the end of 2010, and rising gradually towards 4% by the end of 2011.

It is quite clear that the rates market remains dictated by flow and payside pressure, and we can expect some choppy trading in the near term as this washes through as a result of the easing cycle coming to an end. But we expect the disconnect to close. While we believe it to be unrealistic for the market to fully converge to the Bank's view (the market will remain mindful of history and the narrow window between previous ends to easing cycles and hikes), we still see the magnitude of the gap closing as the message sinks in, and data remains skittish. We must also note that the more the RBNZ's message sinks in, and the more borrowing switches to floating or short-rates, the more bang for the buck the Bank will get on the eventual tightening cycle, and hence less need to hike as far. For the RBNZ, it's the "win-win" scenario all round, so we expect them to remain strong in their lower for longer mantra.

Borrowing strategies we favour at present

The RBNZ has reinforced its lower for longer message for rates. In the current environment, you have to pay for certainty, which is being reflected in a steep yield curve. But with the economy still fragile, the RBNZ is providing certainty for borrowers who choose to float by signalling a commitment *"to keep the OCR at or below the current level through until the latter part of 2010."* Staying floating remains our favoured theme.

Gauges for NZ interest rates

Gauge	Direction	Comment
RBNZ / OCR	↔	RBNZ seem comfortable with policy where it is. Risk still to downside, but OCR staying put for a while.
NZ data	↔/↑	Q1 GDP may not be as bad as initially feared.
Fed Funds/ front end	↔/↑	Market still running with end of year hikes.
RBA	↔	Easing bias but no urgency to move given still resilient employment numbers.
US 10 year	↔	4% yield tested and rejected. Look to range trade for now.
NZ swap curve	↓	With easing cycle over, pressure is on curve to flatten in the near-term.
Flow	↔/↑	Market still wary of mortgage paying pressure.
Technicals	↔	Long-term yields may have topped for now.

Market expectations for RBNZ OCR (bps)

OCR dates	Last week	This week
Thu 30-Jul-09	-4	-4
Thu 10-Sep-09	-3	-3
Thu 29-Oct-09	-2	-5
Thu 10-Dec-09	+5	+4
Thu 21-Jan-10	+7	+5
Thu 11-Mar-10	+28	+27
Thu 29 Apr-10	-	+33

Trading themes we favour at present

The easing cycle looks to be over, and the market is quick to start looking ahead at the next tightening cycle. We think the market is getting ahead of itself in pricing in hikes, hence we see value in going long outright in the March and June bank bill futures. As a hedge, we favour 2s10s flatteners looking for a near-term moved towards 200bps.

CURRENCY STRATEGY

The G8 talks of the withdrawal of stimulus and a return to normality, and markets are responding. US 10 year bonds continue their rally from the 4 percent level seen last week. The question to be asked is what is normal for a currency that has seen above 80 cents and below 50 cents in the past 15 months. The market will go back to focusing on yield differentials, growth differentials, commodity prices and potentially swine flu. External imbalances do not appear to feature heavily as yet.

Market themes…

> G8 talk upbeat.

> Iran election result moved our currency on Friday! Surely it's time to get back to focusing on basics.

> RBNZ perceived to be finished as growth to return later this year.

Review and outlook…

Last week, the market oscillated between 0.6150 and 0.6350 prior to the RBNZ decision. A no change decision and an accompanying statement that was perceived as less dovish (or even hawkish by some) gave the NZD a boost, with stop-loss buying after the announcement forcing the NZD as high as 0.6470. The USD found some friends late in the week as the US bond auctions attracted good bidding interest. The offshore market continues to sit happily long NZD while the local players have now squared many of their shorts.

The yield differential has widened over the past week with the RBNZ easing cycle perceived to be over, causing a spike higher and a flattening of the NZ curve. The US curve fell as global investor demand for its bonds were seen. The NZD is not massively out of line based purely on yield differentials. As a rule of thumb, a 1 year forward of around -150 equates to the currency at around 0.6500 cents. The current 1 year forward is -130 so the NZD going as low as 0.6000 should not be a surprise.

Growth prospects domestically, though, are not as favourable as many offshore investors believe based on the recent climb in the CRB index. The fact that the Australian economy missed a technical recession and S&P upgraded NZ's credit rating outlook from negative to stable has given offshore investors a rosy view of NZ growth prospects. The global uplift in sentiment has been reflected in a boost to consumer confidence here, but recent currency gains have wiped the smile off exporters' faces. Global commodity prices may not be out of line with a currency of 0.6500 cents at present, but any forward looking analysis suggests further downside risk to dairy payouts. Swine flu cannot help our tourism sector, which earns as much in foreign revenue as the much touted dairy sector. Still, we believe the NZD rise is based on unfounded optimism and a herd mentality effect coming from high correlations with Australia and Canada.

Technically we will sell the NZD/AUD on a rise to 0.7940 looking for a good move lower and we will look to sub 0.7500 for profit some time in late July. The NZD/USD gap fill up to 0.6600 is complete. We target the 200 day moving average currently just below 0.5800 to turn long.

NZD vs AUD: monthly directional gauges

Gauge	Direction	Comment
Fair value	↔	Within the range.
Yield	↓	Yield advantage Australia.
Commodities	↓	Dairy lower.
Partial indicators	↔/↓	NZ going forward looks worse.
Technicals	↔/↓	0.8000 the top, sell as close as you can.
Sentiment	↔	RBNZ perceived to be done.
Other	↓	Break of 0.7725 very bearish. 0.72 potential.
On balance	↓	**Negatives here but not the focus.**

NZD vs USD: monthly directional gauges

Gauge	Direction	Comment
Fair value – long-term	↔/↓	Above long term average.
Fair value – short-term	↔/↓	Slightly above cyclical fair value estimates.
Yield	↔	Stabilised.
Commodities	↓	Dairy prices down again.
Risk aversion	↔	Stabilised.
Partial indicators	↔	Both stabilising.
Technicals	↓	Top seen last week. 0.6420 to cap from now.
AUD	↔/↓	AUD disappointing after strong GDP outturn.
Sentiment	↔	Loved offshore hated onshore.
Other	↓	Bearish on debt, growth and yield factors.
On balance	↓	**Target 0.58 cents.**

DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
15-Jun	**NZ**	**April Performance of Services Index**	**-**	**-**	**10:30**
		Economic Survey of Manufacturing (1Q) – qoq	**-**	**0.0%**	**10:45**
	EC	ECB's Tumpel-Gugerell Speaks at Conference in Rome	-	-	19:15
		Employment (1Q) – qoq	-	-0.3%	21:00
16-Jun	US	Empire Manufacturing (Jun)	-4.60	-4.55	00:30
		Net Long-term TIC Flows (Apr)	$57.5B	$55.8B	01:00
		Fed's Evans Speaks on Financial Crisis in Chicago	-	-	01:30
		NAHB Housing Market Index (Jun)	17	16	05:00
	EC	ECB's Tumpel-Gugerell, Nowotny Speak at Vienna Event	-	-	05:00
		CPI (May) – mom	0.0%	0.4%	21:00
		CPI (May) – yoy	0.0%	0.6%	21:00
		CPI – Core (May) – yoy	1.6%	1.8%	21:00
		Labour Costs (1Q) – yoy	3.0%	3.8%	21:00
		ZEW Survey (Econ. Sentiment) (Jun)	34.0	28.5	21:00
	AU	RBA's Board June Minutes	-	-	13:30
	NZ	**Non Resident Bond Holdings (May)**	**-**	**71.3%**	**15:00**
	JN	BoJ Target Rate	0.10%	0.10%	-
	UK	CPI (May) – mom	0.3%	0.2%	20:30
		CPI (May) – yoy	2.0%	2.3%	20:30
		Core CPI (May) – yoy	1.5%	1.5%	20:30
		RPI (May) – mom	0.2%	0.1%	20:30
	GE	ZEW Survey (Econ. Sentiment) (Jun)	35.0	31.1	21:00
		ZEW Survey (Current Situation) (Jun)	-92.6	-92.8	21:00
17-Jun	US	Producer Price Index (May) – mom	0.6%	0.3%	00:30
		PPI Ex Food & Energy (May) – mom	0.1%	0.1%	00:30
		Housing Starts (May)	485K	458K	00:30
		Building Permits (May)	509K	498K	00:30
		Industrial Production (May)	-1.0%	-0.5%	01:15
		Capacity Utilization (May)	68.4%	69.1%	01:15
	AU	Westpac Leading Index (Apr) – mom	-	0.3%	13:00
		Dwelling Starts (1Q)	-	-9.9%	13:30
	JN	BoJ Monthly Report	-	-	17:00
	EC	ECB's Constancio Speaks at Conference on Banking, Markets	-	-	20:00
		Trade Balance s.a. (Apr)	-1.5B	-2.1B	21:00
		Construction Output (Apr)	-	-1.0%	21:00
	UK	BoE Minutes	-	-	20:30
		Claimant Count Rate (May)	4.9%	4.7%	20:30

Continued over page

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
17-Jun cont.	UK	Jobless Claims Change (May)	60.0K	57.1K	20:30
		Average Earnings inc bonus (Apr) – 3m/yoy	0.2%	-0.4%	20:30
		ILO Unemployment Rate (3mths) (Apr)	7.3%	7.1%	20:30
18-Jun	US	Consumer Price Index (May) – mom	0.3%	0.0%	00:30
		CPI Ex Food & Energy (May) – mom	0.1%	0.3%	00:30
		Consumer Price Index (May) – yoy	-0.9%	-0.7%	00:30
		CPI Ex Food & Energy (May) – yoy	1.8%	1.9%	00:30
		Current Account Balance (1Q)	-$84.8B	-$132.8B	00:30
		Fed's Bernanke Speaks at Financial Literacy Summit in D.C.	-	-	04:00
	UK	Retail Sales (May) – mom	0.3%	0.9%	20:30
		Public Sector Net Borrowing (May)	19.3B	8.5B	20:30
		Public Finances (PSNCR) (May)	16.0B	5.2B	20:30
		M4 Money Supply (May P) – mom	0.7%	0.2%	20:30
19-Jun	US	Initial Jobless Claims (w/e Jun-14)	605K	601K	00:30
		Continuing Claims (w/e Jun-7)	6839K	6816K	00:30
		Leading Indicators (May)	1.0%	1.0%	02:00
		Philadelphia Fed (Jun)	-17.4	-22.6	02:00
	JN	BoJ to Release Board Meeting Minutes	-	-	11:50
	GE	Producer Prices (May) – mom	0.0%	-1.4%	18:00
	EC	ECB's Bini Smaghi Speaks at Milan Conference on Supervision	-	-	19:00
		ECB's Gonzalez-Paramo Speaks in Oviedo, Spain	-	-	21:30

Key: AU: Australia, EC: Euro-zone, GE: Germany, JN: Japan, NZ: New Zealand, UK: United Kingdom, US: United States. Sources: Dow Jones, Reuters, Bloomberg, ANZ National Bank. All $ values in local currency. (Note: all surveys are preliminary and subject to change).

NEW ZEALAND DATA WATCH

Key focus over the next four weeks: March quarter GDP is now in the spotlight to determine how deep a hole the economy was in at the start of the year. More timely or forward looking gauges should continue to point to stabilisation and base-finding.

Date	Data/Event	Economic Signal	Comment
Mon 22 Jun (10.45)	International Travel and Migration (May)	More of the same	Less New Zealanders departing will ensure that solid monthly net inflows continue to be recorded.
Wed 24 Jun (14.00)	Westpac McDermott-Miller Consumer Confidence (Q2)	Slight increase	Tax cuts in the pocket, a recovering housing market and better news from offshore should see an improvement in confidence. A weaker labour market will continue to weigh on sentiment though.
Thu 25 Jun (10.45)	Balance of Payments (Mar qtr)	Rebalancing	Recent improvement in the trade balance should help drive the current account deficit to an improved deficit of 8.5 percent of GDP.
Fri 25 Jun (10.45)	GDP (Mar qtr)	Another contraction	While recent partial indicators have not been as bad as initially feared, the economy is still expected to contract in the vicinity of 1 percent in the quarter.
Mon 29 Jun (10.45)	Overseas Merchandise Trade (May)	Rebalancing continues	The trade balance typically records a surplus in May. However, we are expecting this to be larger than normal given a further capitulation in imports.
Mon 29 Jun (10.45)	Building Consents Issued (May)	The bounce	A further pick-up is expected considering the near record low levels and a natural response to an improvement in housing market activity.
Mon 29 Jun (15.00)	Credit Growth (May)	De-leveraging continues	Household credit growth will remain subdued. However, top on the watch list is now business and rural lending growth, which are also showing signs of substantial slowing.
Tue 30 Jun (15.00)	NBNZ *Business Outlook* (Jun)	-	-
Thu 2 Jul (15.00)	ANZ Commodity Price Index (Jun)	-	-
Tue 7 Jul (10.00)	NZIER Quarterly Survey of Business Opinion (Jun qtr)	An improvement in sentiment?	The survey is likely to mirror the latest National Bank *Business Outlook* and show an improvement in sentiment. However, gauges will remain consistent with an economy that continues to contract.
circa 11 Jul	REINZ House Sales (Jun)	A winter turn?	We are on the lookout for signs of waning momentum as we head into winter. Higher longer-term mortgage rates and a weak labour market remain key headwinds.
On Balance		**Base forming?**	**There is a strong base effect appearing in some data, which suggests Q2 is the nadir in the cycle. But the jury is out on the speed of recovery and in H2 2009 we expect the economy to be moving along the bottom of the bath tub.**

SUMMARY OF KEY ECONOMIC FORECASTS

	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
GDP (% qoq)	-0.3	-0.2	-0.5	-0.9	**-1.5**	**-0.5**	**0.0**	**0.1**	**0.5**	**1.2**
GDP (% yoy)	2.1	1.0	-0.1	-1.9	**-3.1**	**-3.3**	**-2.9**	**-1.9**	**0.1**	**1.8**
CPI (% qoq)	0.7	1.6	1.5	-0.5	0.3	**0.7**	**0.6**	**0.6**	**0.5**	**0.5**
CPI (% yoy)	3.4	4.0	5.1	3.4	3.0	**2.1**	**1.1**	**2.2**	**2.4**	**2.2**
Employment (% qoq)	-1.0	1.2	0.2	0.6	-1.1	**-1.0**	**-0.9**	**-0.4**	**-0.2**	**0.0**
Employment (% yoy)	-0.2	0.8	1.1	0.9	0.8	**-1.3**	**-2.4**	**-3.4**	**-2.5**	**-1.5**
Unemployment Rate (% sa)	3.8	4.0	4.3	4.7	5.0	**5.6**	**6.4**	**7.0**	**7.5**	**7.7**
Current Account (% GDP)	-8.0	-8.4	-8.7	-9.0	**-8.5**	**-7.1**	**-6.1**	**-5.2**	**-5.0**	**-4.9**
Terms of Trade (% qoq)	4.2	-0.4	-1.0	-1.0	-3.0	**-2.0**	**-2.0**	**-1.4**	**-1.1**	**-0.9**
Terms of Trade (% yoy)	11.6	10.7	5.8	1.8	-5.2	**-6.8**	**-7.7**	**-8.1**	**-6.3**	**-5.3**

KEY ECONOMIC INDICATORS

	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-09
Retail Sales (% mom)	0.3	0.4	-1.3	0.0	-0.5	-1.2	0.2	-0.2	0.5	..
Retail Sales (% yoy)	-0.9	2.2	0.7	-4.1	-0.9	-3.7	-6.9	-1.9	-1.7	..
Credit Card Billings (% mom)	-0.3	1.3	-1.8	-0.8	-2.2	1.5	0.8	-2.8	2.3	..
Credit Card Billings (% yoy)	2.6	2.5	0.9	-0.9	-3.8	-2.4	-1.9	-4.8	-1.6	..
Car Registrations (% mom)	-3.7	11.6	-1.4	-20.3	14.0	-14.4	-15.2	7.3	-2.4	-3.2
Car Registrations (% yoy)	-30.5	-15.6	-19.9	-34.4	-23.7	-36.5	-44.6	-32.9	-41.0	-33.3
Building Consents (% mom)	-6.0	8.0	-19.9	4.2	-7.2	-12.6	12.0	-1.7	11.2	..
Building Consents (% yoy)	-42.9	-28.4	-43.1	-39.5	-41.6	-51.3	-40.1	-34.5	-56.6	..
REINZ House Price (% yoy)	-5.7	-6.1	-4.3	-4.1	-4.8	-4.4	-2.2	-4.0	-1.4	-2.2
Household Lending Growth (% mom)	0.4	0.2	0.1	-0.1	0.2	0.2	0.2	0.1	0.2	..
Household Lending Growth (% yoy)	7.2	6.6	5.8	4.8	4.2	3.8	3.1	2.8	2.6	..
Roy Morgan Consumer Confidence	91.4	108.6	99.7	99.0	102.9	103.7	98.8	94.7	101.1	104.9
NBNZ Business Confidence	-20.5	1.6	-42.3	-43.0	-35.0	..	-41.2	-39.3	-14.5	1.9
NBNZ Own Activity Outlook	4.7	16.7	-11.4	-14.1	-21.5	..	-20.1	-21.2	-3.8	3.8
Trade Balance ($m)	-848	-1252	-994	-594	-341	-102	481	447	276	..
Trade Balance ($m annual)	-4369	-5048	-5269	-5234	-5614	-5405	-5166	-4676	-4108	..
ANZ World Commodity Price Index (% mom)	-3.4	-5.1	-7.6	-7.4	-7.4	-4.3	-4.6	1.0	2.6	2.7
ANZ World Commodity Price Index (% yoy)	3.5	-2.1	-11.1	-18.3	-24.3	-26.5	-30.7	-31.4	-29.4	-28.1
Net Migration (sa)	340	-20	40	-290	320	820	1620	1730	2160	..
Net Migration (annual)	4938	4403	4329	3569	3814	4538	6160	7482	9176	..

Figures in bold are forecasts. mom: Month-on-Month qoq: Quarter-on-Quarter yoy: Year-on-Year

SUMMARY OF KEY MARKET FORECASTS

	Actual		Current	Forecast (end month)						
NZ FX rates	Apr-09	May-09	15-Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
NZD/USD	0.572	0.598	0.639	0.580	0.550	0.540	0.540	0.550	0.560	0.580
NZD/AUD	0.801	0.785	0.787	0.763	0.753	0.735	0.730	0.733	0.737	0.734
NZD/EUR	0.433	0.439	0.456	0.460	0.444	0.443	0.450	0.458	0.467	0.475
NZD/JPY	56.6	57.8	62.9	56.8	52.3	52.4	54.0	56.7	58.8	62.1
NZD/GBP	0.389	0.389	0.389	0.367	0.355	0.355	0.360	0.372	0.378	0.387
NZ$ TWI	57.0	57.9	60.5	57.4	54.9	54.3	54.8	56.0	57.0	58.4
NZ interest rates	Apr-09	May-09	15-Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
OCR	3.24	2.76	2.50	2.50	2.50	2.50	2.50	2.50	2.75	3.25
90 day bill	3.12	2.82	2.84	2.80	2.80	2.80	2.80	2.80	3.20	3.70
10 year bond	5.24	5.74	6.04	5.70	5.50	5.50	5.40	6.20	6.10	6.40
International	Apr-09	May-09	15-Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
US Fed funds	0.25	0.25	0.25	0.25	0.25	0.50	1.00	1.50	2.00	2.75
US 3-mth	1.02	0.66	0.62	0.70	0.50	0.70	1.25	1.75	2.25	3.00
AU cash	3.00	3.00	3.00	2.50	2.00	2.00	2.00	2.00	2.75	3.25
AU 3-mth	3.08	3.19	3.32	2.30	2.30	2.30	2.40	2.60	3.30	4.40

KEY RATES

	12 May	7 Jun	9 Jun	10 Jun	11 Jun	12 Jun
Official Cash Rate	2.50	2.50	2.50	2.50	2.50	2.50
90 day bank bill	2.90	2.70	2.71	2.72	2.84	2.86
NZGB 07/09	2.79	2.63	2.63	2.63	2.65	2.65
NZGB 11/11	3.60	3.75	3.72	3.73	3.85	3.80
NZGB 04/13	4.47	4.78	4.77	4.77	4.89	4.85
NZGB 12/17	5.57	6.00	5.95	5.95	6.04	6.01
2 year swap	3.53	3.68	3.67	3.64	3.87	3.86
5 year swap	4.83	5.22	5.17	5.14	5.36	5.31
RBNZ TWI	58.3	59.8	59.1	59.6	60.2	60.7
NZD/USD	0.6004	0.6278	0.6178	0.6296	0.6366	0.6433
NZD/AUD	0.7915	0.7867	0.7849	0.7824	0.7851	0.7903
NZD/JPY	58.40	61.76	60.56	61.44	62.29	62.95
NZD/GBP	0.3975	0.3939	0.3861	0.3859	0.3878	0.3891
NZD/EUR	0.4418	0.4488	0.4456	0.4472	0.4533	0.4570
AUD/USD	0.7586	0.7980	0.7871	0.8047	0.8109	0.8140
EUR/USD	1.3590	1.3988	1.3864	1.4078	1.4043	1.4078
USD/JPY	97.27	98.38	98.03	97.59	97.85	97.85
GBP/USD	1.5103	1.5940	1.6002	1.6317	1.6414	1.6532
Oil	57.79	68.43	68.05	70.02	71.38	72.69
Gold	912.25	958.85	949.25	959.80	957.20	953.85
Electricity (Haywards)	7.93	6.44	7.20	4.28	3.47	n/a
Milk futures (US$/contract)	85	86	86	86	86	86
Baltic Dry Freight Index	2253	3646	3518	3452	3483	3583

NEW ZEALAND DISCLOSURE INFORMATION

The Bank (in respect of itself and its principal officers) makes the following investment adviser disclosure to you pursuant to section 41A of the Securities Markets Act 1988.

The Bank (in respect of itself and its principal officers) makes the following investment broker disclosure to you pursuant to section 41G of the Securities Markets Act 1988.

Qualifications, experience and professional standing

Experience

The Bank is a registered bank and, through its staff, is experienced in providing investment advice about its own securities and, where applicable, the securities of other issuers. The Bank has been selling securities, and providing investment advice on those securities, to customers as a core part of its business for many years, drawing on the extensive research undertaken by the Bank and its related companies and the skills of specialised staff employed by the Bank. The Bank is represented on many bank, finance and investment related organisations and keeps abreast of relevant issues by running seminars and workshops for relevant staff and having its investment adviser staff attend external seminars where appropriate. The Bank subscribes to relevant industry publications and, where appropriate, its investment advisers will monitor the financial markets.

Relevant professional body

The Bank is a member of the following professional bodies relevant to the provision of investment advice:

- New Zealand Bankers Association;
- Associate Member of Investment Savings & Insurance Association of NZ;
- Financial Markets Operations Association; and
- Institute of Finance Professionals.

Professional indemnity insurance

The Bank (and its subsidiaries), through its ultimate parent company Australia and New Zealand Banking Group Limited, has professional indemnity insurance which covers its activities including those of investment advisers it employs.

This insurance covers issues (including 'prior acts') arising from staff fraud, electronic crime, documentary fraud and physical loss of property. The scope of the insurance also extends to third party civil claims, including those for negligence. The level of cover is of an amount commensurate with the size and scale of the Bank.

The insurer is ANZcover Insurance Pty Limited.

Dispute resolution facilities

The Bank has a process in place for resolving disputes. Should a problem arise, you can contact any branch of the Bank for more information on the Bank's procedures or refer to any of the Bank's websites.

Unresolved complaints may ultimately be referred to the Banking Ombudsman, whose contact address is PO Box 10-573, Wellington.

Criminal convictions

In the five years before the relevant investment advice is given none of the Bank (in its capacity as an investment adviser and where applicable an investment broker) or any principal officer of the Bank has been:

- Convicted of an offence under the Securities Markets Act 1988, or the Securities Act 1978 or of a crime involving dishonesty (as defined in section 2(1) of the Crimes Act 1961);
- A principal officer of a body corporate when that body corporate committed any of the offences or crimes involving dishonesty as described above;
- Adjudicated bankrupt;
- Prohibited by an Act or by a court from taking part in the management of a company or a business;
- Subject of an adverse finding by a court in any proceeding that has been taken against them in their professional capacity;
- Expelled from or has been prohibited from being a member of a professional body; or
- Placed in statutory management or receivership.

Fees

At the time of providing this disclosure statement it is not practicable to provide accurate disclosure of the fees payable for all securities that may be advised on. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

Other interests and relationships

When a security is sold by the Bank, the Bank may receive a commission, either from the issuer of a security or from an associated person of the Bank. Whether that commission is received and, if received, its value depends on the security sold. At the time of providing this disclosure statement it is not practicable to provide a detailed list of each security that may be advised on, the name of the issuer of that security and the rate of the commission received by the Bank. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

In addition to the interest that the Bank has in products of which it is the issuer, the Bank, or an associated person of the Bank, has the following interests or relationships that a reasonable person would find reasonably likely to influence the Bank in providing the investment advice on the securities listed below:

- ANZ Investment Services (New Zealand) Limited (ANZIS), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. ANZIS may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- UDC Finance Limited (UDC), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. UDC may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- The Bank has a joint venture relationship with ING (NZ) Holdings Limited (ING). ING and its related companies may receive remuneration from a third party relating to a security sold by the Investment Adviser.

Securities about which investment advice is given

The Bank provides investment advice on the following types of securities:

- Debt securities including term and call deposits, government stock, local authority stock, State-Owned Enterprise bonds, Kiwi bonds and corporate bonds and notes;
- Equity securities such as listed and unlisted shares;
- New Zealand and overseas unit trusts;
- Share in a limited partnership;
- Superannuation schemes and bonds;
- Group investment funds;
- Life insurance products;
- Derivative products including interest rate and currency forward rate contracts and options; and
- Other forms of security, such as participatory securities.

PROCEDURES FOR DEALING WITH INVESTMENT MONEY OR INVESTMENT PROPERTY

If you wish to pay investment money to the Bank you can do this in several ways such as by:

- Providing cash;
- Providing a cheque payable to the relevant product or service provider and crossed 'not transferable'; or
- Making an automatic payment or payment through another electronic delivery mechanism operated by the Bank.

Investment property (other than money) may be delivered to the Bank by lodging the relevant property (for example, share certificates) with any branch of the Bank offering a safe custody service, or by posting (using registered post) the documents or other property to a branch of the Bank, identifying your name, account number and investment purpose.

Any investment money lodged with the Bank for the purchase of securities offered by the Bank, its subsidiaries or any third parties will be deposited in accordance with your instructions, to your nominated account or investment. Such money will be held by the Bank according to usual banking terms and conditions applying to that account or the particular terms and conditions relating to the investment and will not be held by the Bank on trust unless explicitly accepted by the Bank on those terms. Any investment money or property accepted by the Bank on trust will be so held until disbursed in accordance with your instructions. Any investment property lodged with the Bank will be held by the Bank as bailee according to the Bank's standard terms and conditions for holding your property.

Record Keeping

The Bank will keep adequate records of the deposit of investment moneys or property and all withdrawals and dealings with such money or property, using the account/investment number allocated to your investment. You may have access to those records upon request.

Auditing

The Bank's systems and operations are internally audited on a regular basis. The financial statements of the Bank and its subsidiaries are audited annually by KPMG. However, this does not involve an external audit of the receipt, holding and disbursement of the money and other property.

Use of Money and Property

Money or property held by the Bank for a specific purpose communicated to the Bank (e.g. the purchase of an interest in a security) may not be used by the Bank for its own purposes and will be applied for your stated purpose. No member of the Bank's staff may use any money or property deposited with the Bank, for their own purposes or for the benefit of any other person. In the absence of such instructions, money deposited with the Bank may be used by the Bank for its own purposes, provided it repays the money to you upon demand (or where applicable, on maturity), together with interest, where payable.

NEW ZEALAND DISCLAIMER

The Bank does not provide investment advice tailored to an investor's personal circumstances. It is the investor's responsibility to understand the nature of the security subscribed for, and the risks associated with that security. To the maximum extent permitted by law, the Bank excludes liability for, and shall not be responsible for, any loss suffered by the investor resulting from the Bank's investment advice.

Each security (including the principal, interest or other returns of any security) the subject of investment advice given to the investor by the Bank or otherwise, is not guaranteed, secured or underwritten in any way by the Bank or any associated or related party except to the extent expressly agreed in the terms of the relevant security.

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