

Market Focus

New Zealand

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THE HARD YARDS

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Page 2: Economic overview

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Page 4: Economic comment – putting in the hard yards

- > Improving productivity growth and getting a better resource mix are pre-conditions for a sustainable and durable recovery to take hold. Our "Hard Yards" indicator – derived from the National Bank Business Outlook survey, is pointing to such an improvement. However, history shows that it tends to take a number of years before the benefits are reaped.

Page 5: Interest rate strategy

- > The NZ rates market will be hostage to offshore moves this week, given the paucity of domestic data. Further upside surprises to US earnings should see global rates continue to selloff, pushing the NZ 2-year swap yield towards the top of its recent range.

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- > Rising risk appetites from a strong start to the US earnings season outweighed Fitch putting NZ on negative outlook. A light domestic data calendar means equity market correlations will be the key driver of NZD short-term direction. It seems unlikely that the NZD will have the impetus to break recent ranges.

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ECONOMIC OVERVIEW

New Zealand's imbalances were to the fore last week, being highlighted by both the RBNZ Governor and Fitch. Such nuances reinforce our bearish currency bent, despite near-term stickiness. This week's data calendar is light. Another solid migration print is expected, reinforcing the "many hands make light work" dynamic that is helping stabilise the economy.

What's ahead?

- > **June International Migration and Travel** (Tuesday 1045 NZST). Another solid net migration inflow is expected as New Zealanders cancel or delay their migration plans. Visitor arrivals should remain under pressure.
- > **June Credit Card Spending** (Tuesday 1500 NZST). Notoriously volatile on a monthly basis. The interest bearing component of outstanding balances is expected to continue heading higher.

What's the view?

New Zealand's external imbalances were to the fore last week, with timely reminders of the rebalancing process that needs to play out being expressed by both the RBNZ Governor in a speech, and the decision by credit rating agency Fitch to place NZ's sovereign credit rating on negative outlook.

While the RBNZ Governor's speech was taken by the markets as relatively upbeat, with the main focus on his comment that *"New Zealand looks likely to start recovering ahead of the pack"*, the more important debate surrounds the quality and durability of the recovery. On this front, the Governor's comments were relatively pointed, noting that *"Reliance on past experience of strong house price inflation and easy credit will be untenable"* and *"A clear risk beyond near-term recovery is that households resume their 'borrow and spend' habits before bringing their debt levels back to more prudent levels."*

This sort of recovery may be quicker, but ultimately of poorer quality and shorter duration. To imagine New Zealand borrowing and spending its way out of a debt-induced jam in the first place (and during the biggest credit crisis in 80 years) just doesn't pass the smell test.

Hence, the key going forward is about improving savings, and shifting resources into the economy's productive base. But there is no "free lunch". Saving and investing for tomorrow means growth being sacrificed today. These are themes that resonate closely with our core forecasts and bathtub shaped business cycle.

Our core view continues to centre on it being households who choose to adjust over an extended

time period as the message sinks in. They already look to have begun down this path, with discretionary spending reduced sharply (car sales are down 28 percent from their peak and the numbers embarking on overseas travel have fallen 9 percent). Credit growth has slowed rapidly and credit card billings are down on a year ago. A large portion of the tax cuts and benefit from lower mortgage payments look to have been saved (or used to pay down debt). The current account deficit has begun to ease from its peak and import volumes have fallen 15 percent. The developments in the retail deposit market are also highlighting this de-leveraging dynamic as retail deposit rates are shifting the relative benefit in favour of savers.

But the de-leveraging dynamic is now being tested. If house sales are anything to go by then credit growth is certainly picking up. The domestic spending juggernaut – Auckland – is firming, although the South Island is slowing rapidly. A lot of this is to be expected, and as we've written about before, will reflect the base effect and rebound off precipitous lows. But it is a fine line between support to the economy and rejuvenation, and our sense is that the domestic economy is now starting to flirt with the latter. In many ways we should not be surprised: having been addicted to a love of housing for decades, it is simply unrealistic to be weaned off overnight.

We should be under no illusions. A material period of de-leveraging is required, particularly when the net stock of foreign liabilities sits around 100 percent of GDP. Last week's placement by Fitch of NZ.Inc on negative outlook was a timely reminder that the adjustment is far from complete. A credit rating downgrade would almost certainly not be the elixir towards such rebalancing becoming *fait accompli* (AA+ versus AA are margins of excellence, and the NZD has frustratingly already taken the news in its stride). But equally, it's a stark reminder of where we could potentially be heading, with Fitch noting that *"New Zealand could fall into a low-growth trap as foreigners demand higher returns to incentivise them to continue to lend to New Zealand so it can consume more than it produces..."* So while we'll respect the "first wave" lift in housing, as we move along the bottom of the bathtub, we continue to be mindful of the bigger picture. Not only in terms of what needs to happen, but also what we think will happen when the reality of a rapidly deteriorating labour market and reduced rural incomes sinks in.

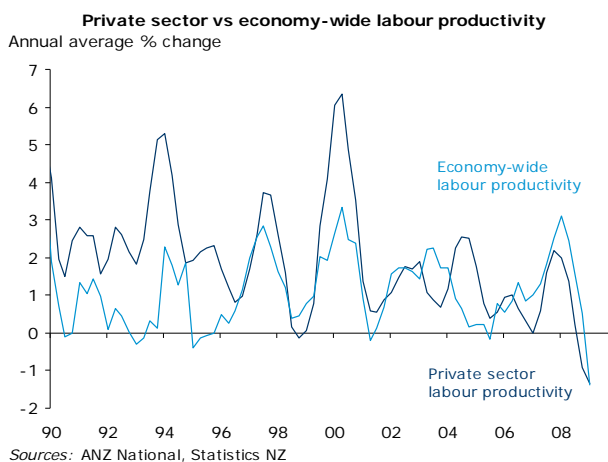
The RBNZ Governor was equally blunt, both in terms of the warning (*"This [a premature resumption in household spending] needs to be avoided"*) but also the preparedness to take active steps (*"prudential policy offers a more direct approach [our emphasis] to constraining excessive or misdirected borrowing and lending behaviour."*)

Indeed, we expect the adoption of financial regulatory measures both domestically and internationally to become increasingly apparent over the coming years (under the guise of reducing systemic risks or vulnerabilities). As noted previously, this should mean less need to pull the OCR lever as aggressively.

In an environment where both the central bank and a rating agency are expressing some wariness over the mix to growth (along with the Government), we're happy to maintain our bearish bent towards the currency. Indeed as noted by Fitch *"...adjustment is further complicated by the volatility of the New Zealand dollar that appears more responsive to global financial conditions than to domestic economic fundamentals."* But at some stage the domestic fundamentals will come back to the fore.

Of course these sorts of nuances may seem overpowering, but they are all part of generating not just a recovery, but a growth prognosis that is ultimately durable and long-lasting. This is opposed to a flash-in-the-pan affair.

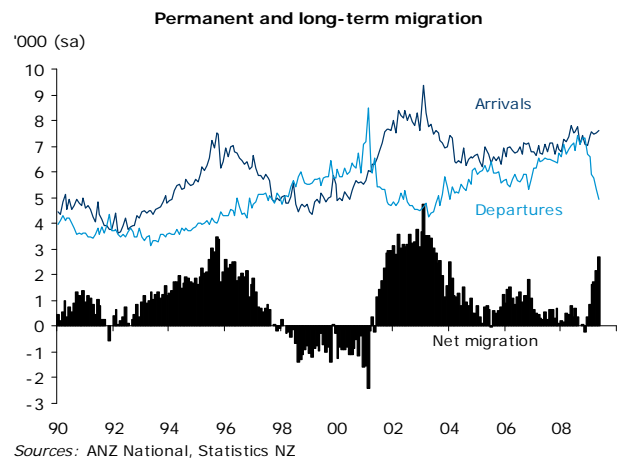
In terms of the adjustment itself, conventional structural indicators such as savings rates, the current account deficit and composition to imports are all barometers we are closely eyeing in regards to quality. But we are equally monitoring productivity aspects to this economic cycle. And in-so-far as statistics are concerned, there is probably no greater hole. But apart from conventional structural indicators, how can we tell whether the required resource adjustment is taking place? "Hard" data of course give us this information, but after the fact and with a considerable lag.



We spent a bit of time pondering over this last week, and page 4 details our "hard-yards" indicator. This is a composite measure from the National Bank *Business Outlook* survey, aimed at monitoring productivity aspects in regards to the cycle, but from more of a lead perspective.

For this week, there is not a lot in the way of domestic data released. The most important will be

net migration numbers for June, although we are expecting them to be relatively similar to May. That is, fewer numbers of New Zealanders choosing to leave will ensure another solid monthly net migration inflow. We will also be watching for signs of an increase in the number of ex-pats returning home. In terms of the visitor arrivals numbers, we expect the general trend to remain down. However, a compositional change is likely to be evident, with more arrivals from Australia, but less from other developed nations.



Internationally this week, there is also not a lot of data. A few leading indicators (the US Chicago Fed National Activity Index, the German IFO and Euro-zone PMIs) will be of interest, as will, June quarter Australian CPI data and the advanced UK Q2 GDP release. Minutes from recent RBA, BoE and BoJ meetings will also be perused. However, the big focus will likely again be the continuation of the US earnings reporting season, which has got off to a reasonably solid start compared with expectations to date.

Recent local data...

- > **Retail Trade Survey (May):** Total spending rose 0.8 percent in the month, while core spending rose 1.6 percent.
- > **CPI (June quarter):** Headline inflation rose 0.6 percent, taking annual CPI growth to 1.9 percent, from 3.0 percent in the March quarter.
- > **Business NZ-BNZ Manufacturing PMI (June):** The seasonally adjusted index rose 3.1 points in the month to 46.2.

PUTTING IN THE HARD YARDS

Improving productivity growth and getting a better resource mix are pre-conditions for a sustainable and durable recovery to take hold. Our “Hard Yards” indicator – derived from the National Bank *Business Outlook* survey – is pointing to such an improvement. However, history shows that it tends to take a number of years before the benefits are reaped.

During upswings or booms, imbalances manifest. The current account deficit widens, savings fall, and productivity languishes. The economy is like the energizer bunny on steroids. But ultimately these imbalances are the *coup de grâce* on a correction.

The economy is now emerging from recession with recovery seen in key cyclical gauges, albeit off lows. But it is equally clear that correcting imbalances, saving more, and investing in the productive base of the economy are the key to economic nirvana and a sustainable recovery (as noted by the RBNZ Governor last week).

This means we are closely watching various structural measures including the current account deficit and savings rates. But such indicators are notoriously slow moving. Moreover, we consider them as necessary as opposed to sufficient conditions for a sustainable recovery to take hold. Productivity must also play a role. Of course picking turning points in productivity is notoriously difficult given the quality of the data.

We’ve created a “Hard Yards” indicator to help gauge, in a timely fashion, whether resources are starting to reallocate and productivity trends are improving. The economic rationale is simple. In order for earnings and momentum to turn and a quality recovery to take place, you need to see the following dynamics: Labour productivity needs to improve; there needs to be changes in the mix of investment; and a different compositional mix to employment is required. These factors sow the seeds of the recovery. And of course, once we have done the work, the tendency is to sit back and reap the rewards.

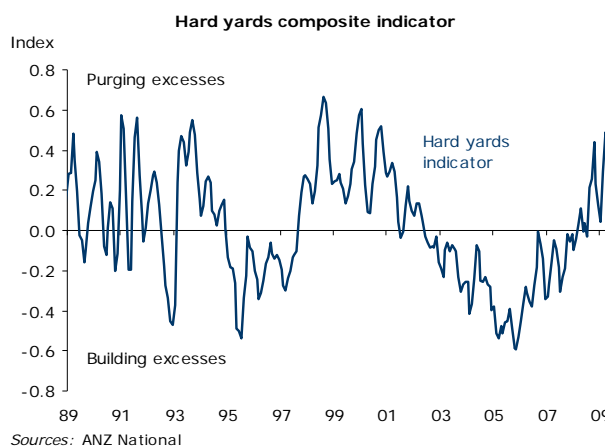
So what is in the indicator? It’s derived from the National Bank *Business Outlook* survey and comprises three measures:

- > Activity expectations relative to employment.
- > Investment relative to employment.
- > The composition of employment – productive versus non-productive areas.

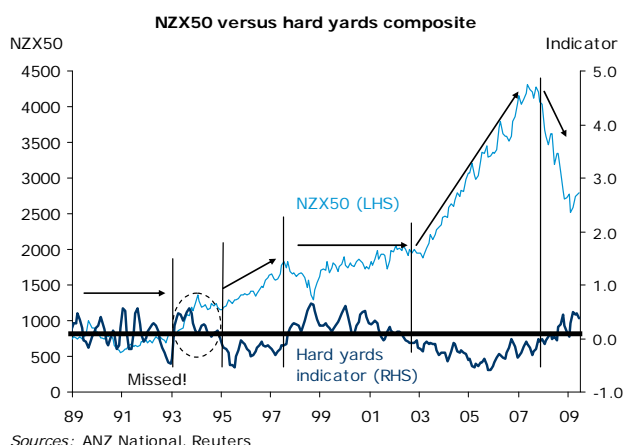
If activity expectations are correcting more rapidly than employment, we can say that firms are doing some hard yards by either working the existing workforce harder, or improving productivity. Both are key for turning the corner on investment. The

same applies for investment over employment to deliver capital deepening productivity growth. The mix to employment speaks for itself.

Our indicator turned positive in late 2008, with all three components contributing. This in itself tells us the business cycle has moved into a different stage. The first leg of the recession in early 2008 was met with natural conservatism and a desire to hold-on. As the recession lengthened, pressure to respond increased. Such responses tend to elongate the adjustment process (i.e. labour shedding), but also lay the groundwork for a stronger recovery.



On the chart below the Hard Yards indicator is overlaid on the NZX. When the indicator is negative, generally the equity market is rising, and the converse is also true. The cross over for the indicator broadly coincides with major turning points for NZ equities. Of course it is only partial – there have been huge global themes at play – but our indicator has performed relatively well across a 20-year time span (though it did miss in 1992).



The upshot

We are encouraged by the trends in our Hard Yards indicator. But the process of doing the hard yards tends to take time, and we are only six months into that process.

INTEREST RATE STRATEGY

The NZ rates market will be hostage to offshore moves this week, given the paucity of domestic data. Further upside surprises to US earnings should see global rates continue to selloff, pushing the NZ 2-year swap yield towards the top of its recent range.

Market themes...

- > RBNZ Governor's speech and Fitch putting NZ on negative outlook key events last week.
- > CPI stronger than expected, but brushed off by markets, as signs inflation will continue to ease.
- > Solid start to the US earnings reporting season led to selloff in global rates.

Review and outlook

A solid start to the US earnings reporting season, with major financials generally beating expectations, boosted investor sentiment and led to increased risk appetites, which were negative for rates. Even news that a major US lender may fail did not dent investor enthusiasm. In Australia, a recovery in business confidence led to a selloff as expectations of further rate cuts were taken out and the market started to contemplate hikes by the RBA early next year. The global selloff flowed through to the NZ market (yields up 5 to 14bps across the curve), though it outperformed offshore markets (US curve sold off 5 to 40bps, while the Australian curve sold off 14 to 35bps). The RBNZ Governor's speech earlier in the week saw rates bid as the market focused on comments that NZ is likely to start recovering ahead of the pack. However, the Governor's comments that prudential policy will potentially be playing a greater role in the future reinforces our view that the OCR lever will not need to be pulled as hard. The Fitch announcement putting NZ on negative outlook had a bigger impact on the currency than on rates. However, it does add pressure for the curve to steepen at the margin.

With a very light domestic data calendar this week, the NZ rates market finds itself hostage to offshore moves. A continuation of positive surprises in US earnings reports will see whatever receiving interest is left subside, with the payside dominating. This will be intensified should Australian Q2 core inflation measures remain stubbornly elevated. Indeed, with the NZ dataflow expected to show further signs of stabilisation, and the only "bad" news likely to be Q2 labour market data due in early August, the risk is that we see NZ swap yields move towards the top of recent ranges. This could see the 2-year swap yield push towards near 4 percent and the 5-year yield attempt a move to 5.5 percent. Of course, we remain mindful of the fickle nature of investor sentiment, which could

turn on a dime should a few disappointing earnings results emerge.

Borrowing strategies we favour at present

Floating rates remain the cheapest part of the curve, and rate hikes still look to be at least 12 months away. As such, our favoured strategy is still to go floating, or simply roll a series of short fixes rather than to fix for a longer period. Consideration can also be given to the use of options as a way to hedge further out. For example, Interest Rate Caps provides protection against rate rises but allows full participation in lower floating rates, for a premium.

Gauges for NZ interest rates

Gauge	Direction	Comment
RBNZ / OCR	↔	On hold. RBNZ unlikely to act on their easing bias. But hikes still a long way off.
NZ data	↔/↑	Further signs of stabilisation expected in the dataflow.
Fed Funds / front end	↔	FOMC statement makes clear that any exit strategy still some time away.
RBA	↔/↑	Recovery in confidence indicators suggest Australian economy may be starting to recover already.
US 10 year	↔	Expect more choppy moves as safe haven sentiment changes by the day.
NZ swap curve	↔	Fitch announcement adds pressure on the curve to steepen at the margin.
Flow	↔/↓	Maturities finding their way back to the market should help.
Technicals	↔	2-year swap yield in the middle of the range. Offshore moves will dictate in the week ahead.

Market expectations for RBNZ OCR (bps)

OCR dates	Last week	This week
Thu 30-Jul-09	-5	-4
Thu 10-Sep-09	-7	-4
Thu 29-Oct-09	-6	-1
Thu 10-Dec-09	-5	+1
Thu 21-Jan-10	+4	+14
Thu 11-Mar-10	+12	+18
Thu 29 Apr-10	+29	+33

Trading themes we favour at present

Last week's RBNZ Governor speech and Fitch placing NZ on negative outlook reinforce the challenges facing the economy still. We still favour being long outright in the March and June bank bill futures, though the 2s10s flatteners are under threat from the Fitch announcement. Expect 2-year swap yield to continue range trading.

CURRENCY STRATEGY

Rising risk appetites from a strong start to the US earnings season outweighed Fitch putting NZ on negative outlook. A light domestic data calendar means equity market correlations will be the key driver of NZD short-term direction. It seems unlikely that the NZD will have the impetus to break recent ranges.

Market themes...

- > Earning season – so far so good.
- > USD Index – testing support.
- > Data drought – range trade to persist.

Review and outlook...

Last week saw a number of different drivers fail to break the NZD out of its now well entrenched ranges. The currency market latched on to RBNZ Governor Bollard's speech, which said NZ was likely to recover ahead of the pack. Retail sales and CPI data both exceeded expectations and the NZD tested, but did not break, topside resistance at 0.6550. Offshore, the much discussed earnings season got underway in earnest last week. Results have by and large exceeded expectations amongst both financial stocks as well as non-financials such as IBM, Intel and Google. Negative news came in the form of Fitch placing NZ on negative outlook, citing concerns over a persistently large current account deficit. An initial knee-jerk sell off in the NZD was soon reversed as currency markets decided to leave this issue on the sidelines for now.

Looking ahead, it is clear that risk aversion has abated as a driver for currency markets. The much feared earnings season has failed to give the bears the ammunition they were looking for so far. The VIX index, a measure of volatility in the S&P 500, starts the week near the lowest level seen since August 2008. This more benign risk environment appears set to persist for now and lowers the probability of the NZD breaking support at 0.6200 in the short term.

The USD Index has been pushed down to key trend line support on the daily chart. For now it has lost its flight to safety support. As we start the week the market will be closely watching this, as a break may well signal a longer term resumption of risk appetite. Results this week from bellwethers such as Coca Cola, Caterpillar, Apple, Morgan Stanley and Microsoft will be important drivers for the fate of USD, and by implication where the NZD heads.

In terms of data, the local calendar remains light until August. A lack of information on this front is likely to see key ranges persist. Australia has the RBA Minutes and CPI, which seem likely to lend further support to the AUD.

Technically, the highs from late June of 0.6550 remain a key level of resistance – expect sellers here initially. A double base at 0.6200 will act as solid support on the week. For now, range trading seems the most likely scenario as the market respects offshore sentiment and has insufficient domestic news to deliver a strong trend lower. The latter is still pending, but needs a major catalyst. Until that occurs, the market seems happily fixated with recent trends.

NZD vs AUD: monthly directional gauges		
Gauge	Direction	Comment
Fair value	↔	Within the range.
Yield	↓	Yield favours Australia.
Commodities	↔/↓	A robust Chinese economy favours the Australians.
Partial indicators	↔	Both data looks ok.
Technicals	↔/↓	0.8080 to 0.8100 remains in place as important resistance.
Sentiment	↔/↑	Earning season sees improved risk appetite.
Other	↔	Positioning less extreme for the AUD.
On balance	↓	Respect the ranges.

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	↔	Not material at present.
Commodities	↔/↓	NZ's basket yet to improve.
Risk aversion	↔	Lowered for now.
Partial indicators	↔	A lack of local data this week.
Technicals	↔	Range trade.
AUD	↔	Sentiment improved towards the AUD. Watch equity markets.
Sentiment	↔	Improved with offshore developments driving markets.
Other	↑	USD can't break trend.
On balance	↔	Range trading with global developments the main driver.

DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
20-Jul	UK	Rightmove House Prices (Jul) - mom	-	-0.4%	11:01
		M4 Money Supply (Jun P) - mom	0.4%	0.2%	20:30
	AU	Producer Price Index (2Q) - qoq	-0.2%	-0.4%	13:30
	GE	Producer Prices (Jun) - mom	0.4%	0.0%	18:00
21-Jul	US	Leading Indicators (Jun)	0.5%	1.2%	02:00
		Fed's Lockhart Speaks on Economic Outlook in Nashville	-	-	05:30
	NZ	Visitor Arrivals (Jun) - mom	-	0.2%	10:45
		Credit Card Spending (Jun) - yoy	-	-2.4%	15:00
	JN	BoJ Monetary Policy Meeting Minutes for May	-	-	11:50
		Nationwide Dept. Sales (Jun) - yoy	-	-12.3%	17:30
	AU	RBA Board July Minutes	-	-	13:30
		New Motor Vehicle Sales (Jun) - mom	-	5.4%	13:30
	UK	Public Finances (PSNCR) (Jun)	20.2B	18.8B	20:30
		Public Sector Net Borrowing (Jun)	15.5B	19.9B	20:30
22-Jul	US	Chicago Fed National Activity Index (Jun)	-	-2.3	00:30
		Bernanke Gives Monetary Policy Report Before House Panel	-	-	02:00
	AU	DEWR Skilled Vacancies (Jul) - mom	-	-3.7%	13:00
		Consumer Prices (2Q) - qoq	0.5%	0.1%	13:30
		Consumer Prices (2Q) - yoy	1.5%	2.5%	13:30
		RBA's Debelle at Mortgage Industry Panel Discussion	-	-	14:00
	JN	BoJ Deputy Governor Yamaguchi to Speak in Hakodate City	-	-	13:30
	UK	BoE Minutes	-	-	20:30
	EC	Industrial New Orders SA (May) - mom	1.9%	-1.0%	21:00
23-Jul	NZ	Finance Minister Bill English Speaks on Economy	-	-	-
	US	House Price Index (May) - mom	-0.2%	-0.1%	02:00
	EC	ECB's Noyer Speaks in Philadelphia	-	-	08:00
		ECB Current Account SA (May)	-	-5.9B	20:00
	JN	Adjusted Merchandise Trade Balance (Jun)	¥513.9B	¥222.4B	11:50
		Merchandise Trade Exports (Jun) - yoy	-35.0	-40.9	11:50
		Merchandise Trade Imports (Jun) - yoy	-42.0	-42.4	11:50
	AU	RBA's Debelle Speaks at University Forum	-	-	19:00
	UK	Retail Sales (Jun) - mom	0.3%	-0.6%	20:30
24-Jul	US	Initial Jobless Claims (w/e Jul-19)	560K	522K	00:30
		Continuing Claims (w/e Jul-12)	6390K	6273K	00:30
		Existing Home Sales (Jun)	4.83M	4.77M	02:00
	JN	All Industry Activity Index (May) - mom	0.9%	2.6%	16:30
	GE	PMI Manufacturing (Jul A)	42.0	40.9	19:30

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Date	Country	Data/Event	Mkt.	Last	Time (NZST)
24-Jul cont.	GE	PMI Services (Jul A)	46.0	45.2	19:30
		IFO - Business Climate (Jul)	86.5	85.9	20:00
		IFO - Current Assessment (Jul)	82.8	82.4	20:00
		IFO – Expectations (Jul)	90.1	89.5	20:00
	EC	PMI Manufacturing (Jul A)	43.5	42.6	20:00
		PMI Services (Jul A)	45.2	44.7	20:00
		PMI Composite (Jul A)	45.3	44.6	20:00
		ECB's Gonzalez-Paramo Speaks in San Sebastian, Spain	-	-	22:00
	UK	GDP (2Q A) - qoq	-0.3%	-2.4%	20:30
		GDP (2Q A) - yoy	-5.2%	-4.9%	20:30
25-Jul	US	University of Michigan Confidence	65.0	64.6	02:00

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: Leading indicators continue to be the major focus over the coming weeks to help determine how quickly (if at all) the economy is bouncing back. In this regard, the July NBNZ *Business Outlook* next week will be important. The RBNZ's decision looms large at the end of the month, although we expect the OCR to be left unchanged. Labour market data next month is expected to be weak.

Date	Data/Event	Economic Signal	Comment
Tue 21 Jul (10.45)	International Travel and Migration (Jun)	Solid support	Net migration inflows are expected to remain solid as fewer New Zealanders choose to leave. Visitor arrivals should remain weak.
Tue 21 Jul (15.00)	Credit Card Spending (Jun)	Volatile	Notoriously volatile on a monthly basis. However, the interest bearing component of outstanding balances is expected to continue heading higher.
Tue 28 Jul (10.45)	Overseas Merchandise Trade (Jun)	Positive rebalancing signs	A monthly trade deficit is typically recorded in June months. However, we expect a small trade surplus as the weak domestic economy and inventory adjustment continues to weigh on import demand, and NZ exports to China continue to rise.
Wed 29 Jul (10.45)	Building Consents Issued (Jun)	Rebounding or record lows	While the level of consent issuance should remain very low, the recent pick-up in house sales activity should see consents begin to recover.
Wed 29 Jul (15.00)	NBNZ <i>Business Outlook</i> (Jul)	-	-
Thu 30 Jul (09.00)	RBNZ <i>OCR Review</i>	On hold	While the RBNZ will remain concerned about market prices and the elevated NZD, we expect them to hold the OCR at 2.50 percent. They will repeat their "low for an extended period" mantra.
Thu 30 Jul (15.00)	Credit Growth (Jun)	Housing improving, but overall credit still weak.	Housing credit growth may start to recover given the improvement in house sales activity. However, business and rural credit growth is likely to remain under pressure.
Tue 4 Aug (10.45)	LCI & QES (Jun qtr)	Softening quickly	While a lagging indicator, wage growth is easing as the economic backdrop and rising unemployment makes it difficult for workers to push for larger wage increases.
Tue 4 Aug (15.00)	ANZ Commodity Price Index (Jul)	-	-
Thu 6 Aug (10.45)	HLFS (Jun qtr)	Continuing to turn sharply	Trends in the number of people signing up for the unemployment benefit clearly shows that the unemployment rate is rising sharply. Another large contraction in employment is also expected.
Fri 14 Aug (10.45)	Retail Trade Survey (Jun)	Reversal	Following the surge in spending in May – partly driven by earlier spending on winter clothes, we expect a pull-back to have occurred in June, although high food prices will inflate the grocery bill. We expect a small contraction in volumes for the quarter.
On Balance		Base forming?	With Q1 data out of the way, attention now turns to how Q2 fared and on signs of green shoots. We expect any recovery to be subdued as we move along the bottom of the bath tub.

SUMMARY OF KEY ECONOMIC FORECASTS

	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10
GDP (% qoq)	-0.2	-0.5	-1.0	-1.0	-0.5	-0.3	0.0	0.3	0.8	1.2
GDP (% yoy)	1.0	-0.2	-2.1	-2.7	-3.0	-2.8	-1.8	-0.5	0.8	2.3
CPI (% qoq)	1.6	1.5	-0.5	0.3	0.6	0.6	0.5	0.3	0.7	0.7
CPI (% yoy)	4.0	5.1	3.4	3.0	1.9	0.9	1.9	1.9	2.0	2.2
Employment (% qoq)	1.2	0.2	0.6	-1.1	-1.0	-0.9	-0.4	-0.2	0.0	0.2
Employment (% yoy)	0.8	1.1	0.9	0.8	-1.3	-2.4	-3.4	-2.5	-1.5	-0.4
Unemployment Rate (% sa)	4.0	4.3	4.7	5.0	5.6	6.4	7.0	7.5	7.7	7.9
Current Account (% GDP)	-8.4	-8.7	-9.0	-8.5	-6.8	-5.8	-5.0	-4.8	-5.1	-5.1
Terms of Trade (% qoq)	-0.4	-1.0	-1.0	-3.0	-2.0	-2.0	-1.4	-1.1	-0.9	0.4
Terms of Trade (% yoy)	10.7	5.8	1.8	-5.2	-6.8	-7.7	-8.1	-6.3	-5.3	-3.0

KEY ECONOMIC INDICATORS

	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-09	Jun-09	Jul-09
Retail Sales (% mom)	-1.4	0.0	-0.5	-1.2	0.2	-0.1	0.5	0.8	..	..
Retail Sales (% yoy)	0.7	-4.1	-0.9	-3.7	-6.9	-1.9	-1.7	-2.4	..	..
Credit Card Billings (% mom)	-1.8	-0.8	-2.2	1.6	0.8	-2.8	2.4	-0.4	..	..
Credit Card Billings (% yoy)	0.9	-0.9	-3.8	-2.4	-1.9	-4.8	-1.6	-2.4	..	..
Car Registrations (% mom)	-0.9	-19.9	12.9	-14.1	-15.1	8.3	-2.4	-3.1	5.4	..
Car Registrations (% yoy)	-19.9	-34.4	-23.7	-36.5	-44.6	-32.9	-41.0	-33.3	-29.6	..
Building Consents (% mom)	-20.0	3.9	-6.8	-12.8	12.4	-0.9	11.9	3.5	..	..
Building Consents (% yoy)	-43.2	-39.6	-41.5	-51.4	-39.9	-34.3	-56.5	-22.9	..	..
REINZ House Price (% yoy)	-4.3	-4.1	-4.8	-4.4	-2.2	-4.0	-1.4	-2.2	0.0	..
Household Lending Growth (% mom)	0.1	-0.1	0.2	0.2	0.2	0.1	0.2	0.4	..	..
Household Lending Growth (% yoy)	5.8	4.8	4.2	3.8	3.1	2.8	2.6	2.6	..	..
Roy Morgan Consumer Confidence	99.7	99.0	102.9	103.7	98.8	94.7	101.1	104.9	105.3	106.1
NBNZ Business Confidence	-42.3	-43.0	-35.0	..	-41.2	-39.3	-14.5	1.9	5.5	..
NBNZ Own Activity Outlook	-11.4	-14.1	-21.5	..	-20.1	-21.2	-3.8	3.8	8.3	..
Trade Balance (\$m)	-994	-594	-341	-102	483	439	319	858	..	..
Trade Balance (\$m annual)	-5269	-5234	-5614	-5405	-5165	-4683	-4072	-3044	..	..
ANZ World Commodity Price Index (% mom)	-7.6	-7.4	-7.4	-4.3	-4.6	1.0	2.6	2.8	0.2	..
ANZ World Commodity Price Index (% yoy)	-11.1	-18.3	-24.3	-26.5	-30.7	-31.4	-29.4	-28.1	-27.9	..
Net Migration (sa)	80	-240	350	840	1630	1740	2170	2690	..	..
Net Migration (annual)	4329	3569	3814	4538	6160	7482	9176	11202	..	..

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

SUMMARY OF KEY MARKET FORECASTS

NZ FX rates	Actual		Current	Forecast (end month)						
	May-09	Jun-09	20-Jul-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
NZD/USD	0.598	0.637	0.645	0.580	0.550	0.540	0.540	0.550	0.560	0.580
NZD/AUD	0.785	0.795	0.805	0.763	0.753	0.735	0.730	0.733	0.737	0.734
NZD/EUR	0.439	0.455	0.457	0.460	0.444	0.443	0.450	0.458	0.467	0.475
NZD/JPY	57.8	61.6	60.8	56.8	52.3	52.4	54.0	56.7	58.8	62.1
NZD/GBP	0.389	0.389	0.395	0.367	0.355	0.355	0.360	0.372	0.378	0.387
NZ\$ TWI	57.9	60.3	60.64	57.4	54.9	54.3	54.8	56.0	57.0	58.4
NZ interest rates	May-09	Jun-09	20-Jul-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11
OCR	2.76	2.74	2.50	2.50	2.50	2.50	2.50	2.50	3.00	4.00
90 day bill	2.82	2.78	2.80	2.80	2.80	2.80	2.80	2.80	3.60	4.50
10 year bond	5.74	6.24	5.73	5.80	5.60	5.70	5.70	6.10	6.30	6.40
International	May-09	Jun-09	20-Jul-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	0.25	0.25	0.50	0.75	1.25
US 3-mth	0.66	0.60	0.50	0.70	0.50	0.70	0.80	1.25	1.50	2.00
AU cash	3.00	3.00	3.00	3.00	2.50	2.50	2.50	2.50	2.75	3.25
AU 3-mth	3.19	3.25	3.11	2.90	2.80	2.80	2.80	3.00	3.30	4.40

KEY RATES

	17 Jun	13 Jul	14 Jul	15 Jul	16 Jul	17 Jul
Official Cash Rate	2.50	2.50	2.50	2.50	2.50	2.50
90 day bank bill	2.81	2.80	2.81	2.81	2.80	2.80
NZGB 07/09	2.65	2.50	2.50	2.50	2.50	2.50
NZGB 11/11	3.76	3.68	3.72	3.76	3.78	3.74
NZGB 04/13	4.75	4.65	4.67	4.71	4.73	4.69
NZGB 12/17	5.92	5.66	5.66	5.73	5.76	5.71
2 year swap	3.76	3.68	3.72	3.79	3.81	3.80
5 year swap	5.19	5.15	5.19	5.27	5.28	5.28
RBNZ TWI	60.0	59.4	59.9	60.5	60.4	60.6
NZD/USD	0.6312	0.6258	0.6258	0.6405	0.6410	0.6441
NZD/AUD	0.7957	0.8058	0.7967	0.8071	0.8034	0.8057
NZD/JPY	60.99	57.90	57.90	59.94	60.23	60.27
NZD/GBP	0.3843	0.3882	0.3882	0.3924	0.3911	0.3932
NZD/EUR	0.4550	0.4493	0.4476	0.4580	0.4556	0.4564
AUD/USD	0.7933	0.7766	0.7855	0.7936	0.7979	0.7994
EUR/USD	1.3872	1.3929	1.3981	1.3985	1.4068	1.4114
USD/JPY	96.63	92.52	92.52	93.59	93.97	93.57
GBP/USD	1.6426	1.6122	1.6122	1.6323	1.6388	1.6381
Oil	70.47	59.93	59.69	59.62	62.07	62.07
Gold	934.80	912.00	919.85	926.00	937.85	937.25
Electricity (Haywards)	9.68	14.66	15.64	5.25	6.28	6.85
Milk futures (US\$/contract)	86	86	86	86	86	86
Baltic Dry Freight Index	4026	2975	3097	3324	3501	3542

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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