

NEW ZEALAND ECONOMICS ANZ MARKET FOCUS

20 December 2010

INSIDE

Economic Overview	2
Data Preview	5
December QEF Summary	6
Interest Rate Strategy	7
Currency Strategy	8
Data Event Calendar	9
Data Watch	11
Key Forecasts	12

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This will be the last *Market Focus* for the year. We would like to wish our readers a safe and enjoyable festive season. The first full edition of the New Year will be on 17 January.

THE FISCAL STRAJHTJACKET

ECONOMIC OVERVIEW

Two key structural measures released last week – the updated fiscal projections and institutional sector accounts - have highlighted the long journey the economy faces. Both will weigh on the recovery for some time: the former via a tighter fiscal stance, and the latter via continued restoration of the household savings buffer – or at least a return to a positive number! This week's GDP data for Q3 is expected to show the economy in stall-mode over the winter months, while favourable one-offs will contribute to the annual current account deficit falling below 3 percent of GDP.

DATA PREVIEW

A high investment income deficit and seasonal decline in the trade balance is expected to deliver a quarterly current account deficit of \$1.5b. It could have been much worse, were not for a one-off provided by insurance inflows from the Canterbury earthquakes, which is likely to restrict the deterioration of the annual deficit until mid 2011. Thursday's Q3 GDP release is expected to show a small decline in aggregate activity, but with wide sector divergences.

DECEMBER QEF SUMMARY

The spirit of our forecasts is hard graft and payback. We have spent more than we have earned for decades, and the events of 2008, 2009 and 2010 are the start of a long journey. The economic outlook is more positive for next year, particularly the second half. But overall, growth is going to be unspectacular yet again in 2011, stripping out one-offs, as we continue to get our house in order.

INTEREST RATE STRATEGY

The market has already gone into holiday mode, with NZ Q3 GDP data the main focus for the rates market this week. The prospect of a weak Q3 GDP print could leave the market biased to pushing out the timing of when the first hike has been priced in. However, the extent of any rally on a weak number will be limited by a market that is already very long. Further curve steepening pressure will be largely dependent on whether US Treasuries continue to sell off.

CURRENCY STRATEGY

The USD continues to benefit from higher bond yields and a better tone to US data. With the Euro looking suspect, the USD bid tone is expected to remain the default play, though we are mindful of the normal seasonal NZD buying. NZ data continues to look weak and the key data this week will likely be no exception. Heavy interest to sell NZD against AUD has been a feature and is expected to continue.

ECONOMIC OVERVIEW

SUMMARY

Two key structural measures released last week – the updated fiscal projections and institutional sector accounts - have highlighted the long journey the economy faces. Both will weigh on the recovery for some time: the former via a tighter fiscal stance, and the latter via continued restoration of the household savings buffer – or at least a return to a positive number! This week's GDP data for Q3 is expected to show the economy in stall-mode over the winter months, while favourable one-offs will contribute to the annual current account deficit falling below 3 percent of GDP.

THIS WEEK'S EVENTS

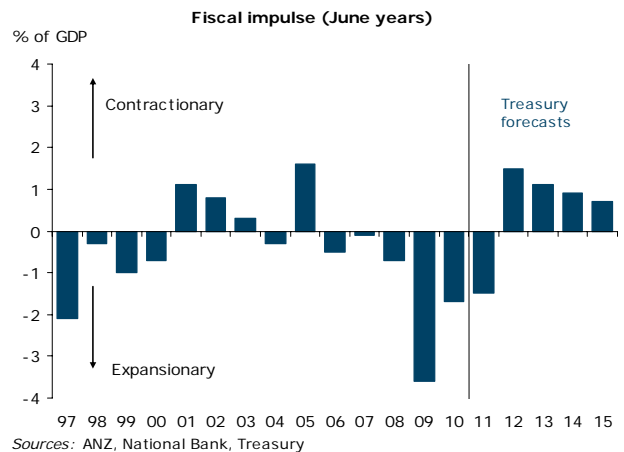
- **SNZ External Migration - November** (Tuesday, December 21, 10:45am). We expect a net monthly permanent and long-term inflow of around 700 persons. Overseas visitor arrivals are expected to rise 2 percent.
- **RBNZ Credit Card Billings - November** (Tuesday, December 21, 3:00pm). We expect a seasonally adjusted increase in billings of around 1.2 percent.
- **SNZ Current Account Balance - 2010Q3** (Wednesday, December 22, 10:45am). A quarterly deficit of \$1.5b is expected, with an annual deficit of 2.9 percent of GDP. See our preview on page 5.
- **SNZ Gross Domestic Product- 2010Q3** (Thursday, December 23, 10:45am). We expect a 0.1 percent quarterly decline in production-based GDP. Our preview is on page 5.

WHAT'S THE VIEW?

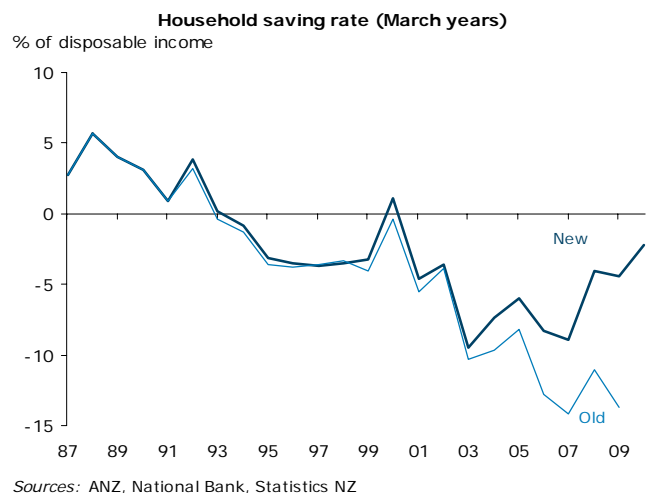
Two key structural measures released last week reinforced the long journey the economy faces.

- The Half Year Economic and Fiscal Update (HYEFU) projections showed the operating balance excluding gains and losses (OBEGAL) blowing out to a deficit of 5.5 percent of GDP in 2010/11. The accounts are projected to return to surplus by 2014/15 (though not in a cash sense). But the upshot is a tight fiscal rein. More money will be coming out of New Zealanders pockets than what is given back. The alternative is to keep borrowing \$300 million a week.
- Households continue to have a negative reported saving rate. However, the *level* of household "saving" has been revised up significantly, to the tune of \$8.6b in the March 2009 year. An improving *trend* in household spending is also evident from 2007, which accords more closely

with our readings of the economy. Little wonder that the retail environment was been weak as households concentrate on fixing their balance sheets. However, the job is not yet done. National savings remains too low and our growing external debt make us "highly vulnerable" according to the Savings Working Group interim report. With house prices continuing to trend lower, the "feel good" factor of homeownership is still conspicuously absent.



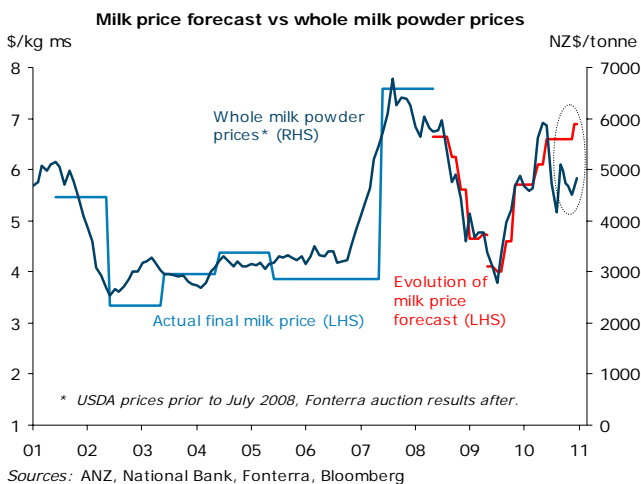
Belt-tightening by households and government will exert a strong contractionary impulse on the economy. We estimate a structural fiscal tightening or around 1 percent of GDP in 2011/12. Assuming the household savings rate improves by 1 percent per year over the next five years, that's another implicit contraction of about 0.6 of GDP. The economy will need economic support, with monetary policy, high commodity export prices and the low NZD/AUD all having a role to play.



ECONOMIC OVERVIEW

The Savings Working Group (SWG) report noted there is a need for government and households to lift productivity and national savings. **It summed up the structural side of the equation quite nicely: "The bottom line is that New Zealanders collectively have been spending too much and saving too little, using large amounts borrowed offshore to fund new investment. Its credit is about maxed out. It's time to get real".** The tenor of the entire report was blunt to say the least. There looks to be no holy cows and it was noted that doubling productivity growth in the government sector could make serious inroads into reducing government debt. The idea of compulsory saving was also raised as a means to improve our track record of very low and unbalanced savings (i.e. too much tied up in property). This will give the government plenty to think about over the summer break.

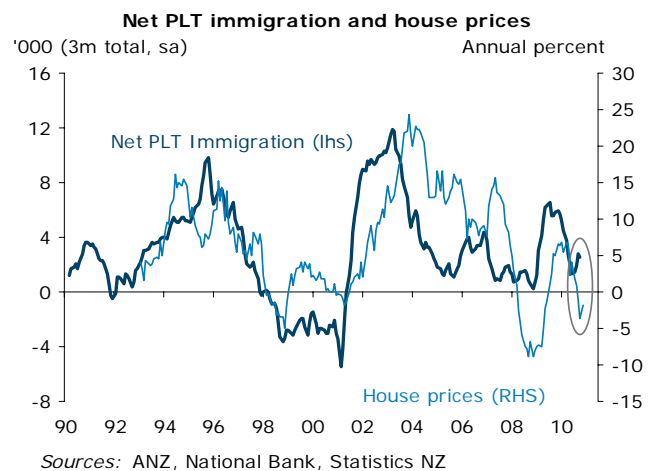
Thankfully, New Zealand is seeing some opportunity to improve our balance sheet from the income generation side. The improvement evident in milk powder prices from the globalDairyTrade online auction continued last week, with USD prices more than 20 percent above the August event. Improving manufacturing sector sentiment was also evident, no doubt helped by the low NZD/AUD. Both are positive for the rebalancing in economic activity for the NZ economy. **This does not reduce the scale of the challenges facing NZ.Inc (i.e. continued pressure on the spending side of the economy), but it certainly makes our situation an awful lot more palatable than what some other nations face.** In regard to the rural sector, we remain cautiously optimistic but are mindful of drought impacts, a key "niggle" factor at the moment.



The release of the current account and GDP data for Q3 dominates this week. Our preview is on page 5. **We expect the annual current account deficit to decline to 2.9 percent of GDP.** More favourable one-offs, this time reinsurance inflows from the Canterbury earthquakes, are expected to significantly narrow the invisibles deficit. With the HYEPU showing intent to improve national saving, this may buy us the time we need to get our own house in order.

Thursday sees the release of Q3 GDP. We are expecting a decline in activity of 0.1 percent. The key take out will be diverging sector performances, with weaker production in the goods-producing sectors of the economy weighing on aggregate economic activity. Such an outcome will naturally lead to speculation about recovery prospects and the potential double dip recession, but we need to remember we are talking about the September quarter: it is already mid December. Our December *Quarterly Economic Forecasts* will be out today and suffice to say the spirit of our economic assessment continues to be a long adjustment process for the economy, but with a bit of fun in H2 2011.

External migration for November is expected to remain a source of economic support. We are expecting a net permanent and long-term (PLT) inflow of approximately 700 persons, with an annual PLT inflow of around 11,000 persons. Tourist arrivals are expected to deliver a small monthly increase of around 2 percent, underpinned by higher arrivals from Asia.



RBNZ credit card billings data for November is expected to mimic the 1.2 percent increase in retail electronic card transactions. Our internal anecdotes suggest the mood of consumer caution has persisted into early December, with the shopping

ECONOMIC OVERVIEW

season starting later than usual and retailers having to discount to get the sale. The coming week is shaping as key for the retailing sector with momentum at present very skittish, patchy and promotional (read: specials) driven.

This is the last *Market Focus* for 2010. We would like to wish our readers a happy and responsible festive season. We have enjoyed bringing you our weekly commentary and trust you have found our insights useful. The “bathtub with waves” analogy that we used to characterise the economic outlook at the start of the year still appears to be an apt description. The economy continues to face challenges, and growth over the early part of 2011 is likely to remain of the “grumpy” variety. This year was a challenging one, with the NZ and global economies not really kicking on, after showing early promise. Many of the challenges facing the economy are likely to remain relevant in 2011. Borrowing our way to growth is no longer an option. However, there is light at the end of the tunnel and we remain positive over prospects for late 2011. **While difficult for many to fathom – and particularly those involved in retailing and housing, what we are seeing at present is precisely what is required to put the economy back on a firmer footing.**

RECENT LOCAL DATA

- **REINZ Housing Market Statistics - November**
Sales volumes rose a seasonally adjusted 19.2 percent (-15.2 percent y/y). The house price index rose 1.3 percent (s.a.), to be 1.9 percent lower than 12-months earlier. The median days to sell ticked down to 44 days (s.a.) from 45 in October.
- **SNZ Retail Trade Survey – October.** Retail sales values fell 2.5 percent (s.a.) following a 1.7 percent rise in October. Sizeable declines in durable spending were evident with furniture, motor vehicle parts and electrical goods. Core retail spending fell 1.7 percent (s.a.).
- **Treasury Half Year Economic and Fiscal Update.** The operating balance excluding gains and losses (OBEGAL) is expected to peak at \$11.1 billion in 2010/11, with a surplus of \$39m expected in 2014/15. Net core crown debt is expected to climb to 28.5 percent of GDP by 2014/15.
- **ANZ-Roy Morgan Consumer Confidence – December.** Overall consumer confidence eased 2 points to 112.2. The current conditions measure rose 5 points to 98.5, whereas the future expectations component eased 7 points to 121.4.
- **globalDairyTrade online auction.** Whole milk

powder prices averaged USD \$3,620 per tonne in the mid-December event, a 2.6 percent increase on the early December auction.

- **BNZ-Business NZ PMI – November.** The headline PMI index rose 2.7 points to 52.7. Four of the five subcomponents increased, with the largest gains for production and deliveries.
- **Westpac-McDermott Miller Consumer Confidence- 2010Q4.** Consumer confidence fell 6 points to 108.3. Perceptions of current and future conditions declined 6 points, to 97.3 and 115.6 respectively.
- **National Bank Business Outlook – December.** Headline business confidence eased 3 points to +30. Own activity and profit expectations were broadly unchanged at +35 and +15 respectively. Investment and employment intentions both climbed to +8 and +13.

DATA PREVIEW

SUMMARY

A high investment income deficit and seasonal decline in the trade balance is expected to deliver a quarterly current account deficit of \$1.5b. It could have been much worse, were not for a one-off provided by insurance inflows from the Canterbury earthquakes, which is likely to restrict the deterioration of the annual deficit until mid 2011. Thursday's Q3 GDP release is expected to show a small decline in aggregate activity, but with wide sector divergences.

Current account – September 2010 quarter
(due Wednesday 22 December, 10.45am)

Current Account	ANZ	RBNZ	Market
Quarter	-\$1.5b	- -	-\$2.3b
Annual	-\$5.6b	- -	-\$6.5b
% of GDP	-2.9%	-3.0%	-3.4%

We are expecting a quarterly current account deficit of approximately \$1.5b. Despite the higher terms of trade, we expect a small trade deficit as September is typically the low point for the trade balance. A worsening net trade balance would not have helped either. A large investment income deficit is expected for September, with profitability appearing to recovering from cyclical lows. Were it not for re-insurance inflows from the Canterbury earthquakes (which adds at least \$1.7b to the transfers surplus and also lowers external debt by this amount), the deficit would have been larger still. With the potential for more insurance inflows to arrive (which will increase the 2010Q3 transfers balance), the likelihood will be further improvement. We expect an annual current account deficit of 2.9 percent of GDP. With the positive one-offs from the structured tax transactions dropping out of the annual comparison, the reinsurance inflows will help cap the deterioration in the annual deficit until at least mid 2011.

Looking beyond seasonal influences we expect the trend nuances to remain simple: an improving trade balance courtesy of commodity prices yet a widening invisibles deficit, a consequence of borrow and spending habits of old and a rebound in corporate profitability. With the latter unlikely to improve, further progress remains trade dependent. Commodity prices look good but drought conditions will weigh on export incomes.

FINANCIAL MARKET IMPLICATIONS

We expect a better number than the market courtesy of reinsurance inflows. Such a dynamic has reduced

the risk of a shocker, which in the current environment could have led to an adverse reaction.

GDP – September 2010 quarter
(due Thursday 23 December, 10.45am)

GDP	ANZ	RBNZ	Market
QoQ	-0.1%	+0.3%	+0.2%
YoY	+1.6%	+1.9%	+1.8%
Ann. Ave.	+1.5%	+1.6%	+1.5%

Headline production GDP is expected to have declined by 0.1 percent in Q3. The GDP report is expected to highlight sector divergences. Primary sector output is expected to increase 0.5 percent as agriculture production recovers from drought related disruptions earlier this year. However, some pullback in fishing and forestry output is likely after the strength in Q2. Output in goods producing sectors is expected to fall by around 1.5 percent, largely as a consequence of lower construction and ex-primary food manufacturing. A decline in mining output is also possible, with lower electricity sector output on account of a decline in (higher value added) hydro generation. Activity in the services sector is forecast to manage a small increase, propped up by firmer retail and wholesale trade, with increasing paid hours in the non-market sector suggesting an increase in non-market sector activity. However, subdued housing turnover and declining paid hours for the market sector suggests there are likely to be pockets of weakness. With few indicators available in the "hard to measure" services sector, there are large margins of error around our picks for this area.

Sector divergences are also expected on the expenditure measure of GDP. The pre-GST spend-up is expected to boost private durables consumption, with higher plant and machinery volumes underpinning higher business investment. Government consumption and inventory rebuilding will add to growth. Offsetting this is a large quarterly decline in residential investment activity, and some likely falls in transport equipment and reduced mineral exploration. Net exports are also expected to make a large negative quarterly contribution.

FINANCIAL MARKET IMPLICATIONS

The market has become attuned to the possibility of a GDP number weaker than the 0.3 percent forecast by the RBNZ, due to softness in subsequent data for Q3. We agree this is where the risks reside. While attuned to this risk we're not inclined to overplay weakness. NZ data is notoriously noisy, and we are talking about the September quarter: we are now in December!

DECEMBER QUARTERLY ECONOMIC FORECASTS

SUMMARY

The spirit of our forecasts is hard graft and payback. We have spent more than we have earned for decades, and the events of 2008, 2009 and 2010 are the start of a long journey. The economic outlook *is* more positive for next year, particularly the second half. But overall, growth is going to be unspectacular yet again in 2011, stripping out one-offs, as we continue to get our house in order.

NEW ZEALAND ECONOMIC OUTLOOK

The New Zealand economy is undergoing a period of structural change from a spending-based model towards more balanced growth. This is necessary, but not fun. The trend rate of growth will be lower for years to come. There will be little easy money to be made for a while, as debt reduction continues to dominate the business cycle.

2011 will be a year of “grumpy growth”, focused in the second half of the year. The New Zealand economy continues to drag itself slowly out of the hole. Accommodative monetary policy and high commodity prices are helping, but the headwinds of a strong currency, contractionary fiscal policy, a dead housing market, falling rural land values, adverse weather and ongoing debt reduction will continue to have the upper hand in the short-term.

One-offs and loose financial conditions dominate a rebound in H2 2011, while we expect high commodity prices to boost 2012.

The latter requires stabilisation in rural land values and we are not there yet.

The process of balance sheet repair has further to run. The household debt to income ratio has fallen only slightly, as has New Zealand’s net external debt. The household sector still has a negative measured savings rate and rural sector debt remains massive compared to the sector’s size. Increased saving puts the brakes on the money merry-go-round, and **this necessary process will continue to dampen demand over the year ahead.**

The medium-term outlook remains positive, but not before we get our house in order.

Commodity prices sit at record highs. Growth in the Asia region is expected to remain strong. A much stronger “back to basics” culture is emerging across businesses, which is positive for productivity, though weak investment is a concern on that front at present. The current state of the economy is not friendly if you are involved in retailing or housing. But such weakness foretells better savings and will assist medium-term prospects.

GLOBAL OUTLOOK

The US economy is expected to grow more robustly next year, while the major Asian economies go through a policy-induced slowdown. The Eurozone will struggle as austerity measures weigh. Risks to the global outlook are to the downside, as Asian policymakers grapple with rising inflation and Western hemisphere policymakers try to rein in ballooning fiscal deficits. **Our numbers portray a robust backdrop but 2011 will be a bumpy ride.**

FISCAL POLICY

Our projections show the deficit approaching 6 percent of GDP in 2010/11, before moving closer to balance by 2014/15. **After providing support through the downturn, fiscal policy will move into a progressively tighter stance from 2011/12.** This will involve difficult choices. A key challenge facing the government is fostering an economic framework that encourages robust and sustainable growth, while at the same time focusing on expenditure restraint.

INFLATION

The lift in GST is expected to temporarily increase headline inflation, which is set to reach 5 percent by mid-2011. **In an underlying sense, our projections still have annual inflation within the 1 to 3 percent RBNZ target band, albeit at the top end.** Weak domestic demand and an elevated NZD may provide further downward near-term pressure on retail-related prices. However, upside inflation risks are prevalent in the medium term.

EXCHANGE RATE

The NZD continues to defy domestic economic weakness, staying elevated despite signs of easing momentum throughout most of the year. **A rampant AUD, which is set to trade through parity for most of next year, looks set to keep the NZD up, though still within a 0.70 to 0.74 range. A new decade low against the AUD is in prospect.** The key risk is of a resurgent USD if the US economy surprises to the upside next year and the Euro region fractures. **If the EUR/USD heads down, so too will the NZD/USD.**

INTEREST RATES

A more subdued recovery, well-anchored inflation expectations and a tighter fiscal stance provide the RBNZ with ample scope to leave monetary policy accommodative for longer. **We see a mid-year tightening cycle next year,** but one that goes in mini-cycles RBA-style. **There is a risk the RBNZ could be on hold the entire year.** We see a peak in the OCR at 4.75 percent.

INTEREST RATE STRATEGY

SUMMARY

The market has already gone into holiday mode, with NZ Q3 GDP data the main focus for the rates market this week. The prospect of a weak Q3 GDP print could leave the market biased to pushing out the timing of when the first hike has been priced in. However, the extent of any rally on a weak number will be limited by a market that is already very long. Further curve steepening pressure will be largely dependent on whether US Treasuries continue to sell off.

MARKET THEMES

- Weak retail sales and drought concerns play on the market.
- While the front end of NZ curve remains well anchored, the back end followed the sell-off in US Treasuries, causing further curve steepening.

REVIEW AND OUTLOOK

Pay-side interest remains low following the dovish December MPS, with media stories on the drought and soft domestic spending encouraging mortgage holders to stay floating. Offshore interest in the NZ market has been lower than usual and corporate activity has wound down for the year.

The NZ curve has continued to steepen, following US interest rates. US data of late has taken on an improving tone. This plus concerns over the size of US fiscal deficits has seen longer-dated US Treasury yields move higher.

The OIS market has all but erased the possibility of a March RBNZ hike. June is now preferred by market commentators as being the most likely date for the RBNZ to commence the policy tightening. However, there is the possibility of the RBNZ remaining on the sidelines for longer if events dictate.

We expect the NZ front-end to remain capped after the recent run of poor data but with a risk of a break to the downside on Thursday's GDP. If Q3 GDP registers a small decline (as our economists expect), the 2 year swap yield could break through the 3.80 percent level, with the carry looking attractive over the holiday break at around 6bpts per month.

The shape of the NZ curve will largely be dictated by the US with steadily improving US data continuing to steepen global curves.

PREFERRED BORROWING STRATEGIES

No change to what we said last week. The economic and monetary policy outlook strongly argues for remaining on floating, and maintaining exposure to what must be regarded as stimulatory interest rates. However, we have to remain mindful of how quickly things can evolve differently to forecasts, as we have seen over the past 12 months. As such, it remains prudent to have some interest rate protection in place. The slope of the curve makes paying fixed very expensive, so we prefer to use caps instead. For active risk managers, shortening the duration of existing hedges to reduce interest expense can be considered.

GAUGES FOR NZ INTEREST RATES

GAUGE	GAUGE	GAUGE
RBNZ / OCR	↔/↓	RBNZ looking at delayed start to next OCR hike.
NZ data	↔/↓	Apart from strong commodity prices, not much else is looking good.
Fed Funds / front end	↔	Improving US data not going to change the Fed's mind.
RBA	↔/↑	RBA look comfortable but could yet be in play earlier.
US 10 year	↑	Better US data could see the sell off continue.
NZ swap curve	↔/↑	Steepening continues on the back of higher US yields.
Flow	↔/↓	Mortgage paying non-existent.
Technicals	↔/↓	3.8% still a key level.

MARKET EXPECTATIONS FOR RBNZ OCR (BPS)

OCR DATES	LAST WEEK	THIS WEEK
Thu 27-Jan-11	+1	0
Thu 10-Mar-11	+2	+1
Thu 28-Apr-11	+6	+5
Thu 9-Jun-11	+19	+15
Thu 28-Jul-11	+27	+27
Thu 15-Sep-11	+41	+39
Thu 27-Oct-11	+48	+51

TRADING THEMES WE FAVOUR AT PRESENT

With the prospect of a weak Q3 GDP release this week and positive carry over the quiet holiday period, we favour being long outright in the 2-year. A further sell off in US Treasuries mean the curve could steepen further.

CURRENCY STRATEGY

SUMMARY

The USD continues to benefit from higher bond yields and a better tone to US data. With the Euro looking suspect, the USD bid tone is expected to remain the default play, though we are mindful of the normal seasonal NZD buying. NZ data continues to look weak and the key data this week will likely be no exception. Heavy interest to sell NZD against AUD has been a feature and is expected to continue.

MARKET THEMES

- More “randomness” expected with onslaught of holiday season. EURUSD directionally key.
- Will seasonal buying of NZD and AUD kick in?
- Interest to sell NZD vs. AUD is strong.

REVIEW AND OUTLOOK

NZD weakness continued given an extra kick by a weak retail sales print for October. In particular this spurred renewed interest to sell NZD vs AUD. This pair has now traded at its lowest level for 10 years. With the very real prospect that the September GDP announcement on Thursday could produce a negative print, there seems little hope for any real NZD strength this week. Technically speaking we broke some very important levels last week. The uptrend that has been in place since May this year was broken at .7465 and a key support at .7395 was also breached. This invokes a head and shoulders top formation with targets of .7106 and .6817 although expect support at the 200 day moving average at .7235.

The AUDUSD has set up some key technical levels also displaying a head and shoulders top. This however is in its very early stages so treat with some caution. A break of 1.0030 would negate this structure. If it bears fruit then targets are .9221 then .8935 so this is a big structure which will take weeks to unfold. With a general lack of data this week save for the RBA minutes on Tuesday weakness will have to come from external factors. We need to keep a close watch on further develops from the Chinese authorities as any action here to slow down the Chinese Juggernaut will have a material impact on the AUD.

The rise in US bond yields continued for the first half of the week but gave back some of the move towards the end. Bond yields have been a factor in recent USD strength with snippets and anecdotes suggesting the US economy is showing modest improvement are also having an impact. When you see the likes of Ireland receive a not one but five notch downgrade, there are firm reminders

the pockets of the eurozone face significant challenges. The US is not immune from such challenges, but the Euro looks more prone to near-term pressure. And where the EUR/USD goes, the NZD/USD follows.

There is evidence that the NZD and AUD experience “seasonal” support during the second half of December and the first half of January in most years. The current view for this week suggests seasonal factors may have a big battle against some very weak fundamentals. Perhaps this week will not be as quiet as perhaps hoped for. Merry Christmas and Happy New Year.

NZD VS AUD: MONTHLY DIRECTIONAL GAUGES

GAUGE	DIRECTION	COMMENT
Fair value	↑	Below fair value.
Yield	↔/↓	Yields less supportive as NZ growth prospects soften.
Commodities	↔	Holding up well.
Partial indicators	↓	Downside risk to NZ data this week.
Technicals	↓	Approaching 10 year lows at .7400. Momentum strong.
Sentiment	↓	Weak NZ data sends sentiment negative.
Other	↑	At historically low levels.
On balance	↑	0.7400 - 0.7600 range to play out.

NZD VS USD: MONTHLY DIRECTIONAL GAUGES

GAUGE	DIRECTION	COMMENT
Fair value – long-term	↔/↓	Above structural fair value of 0.67.
Fair value – short-term	↔/↓	Still above our cyclical fair value estimates.
Yield	↓	Higher US bond yields whereas NZ's turn lower.
Commodities	↔	Soft commodities higher.
Risk aversion	↔	End of year effect as market grabs carry.
Partial indicators	↔/↓	US data has been getting better apart from payrolls.
Technicals	↔/↓	Head and shoulders top in play. Expect weakness.
AUD	↓	AUD sentiment turned bearish.
Sentiment	↓	Weak data still at the fore.
Other	↓	USD strength resumes.
On balance	↓	Weak data, Euro and technicals could crowd out seasonal end of year effects sending NZDUSD lower.

DATA EVENT CALENDAR

DATE	COUNTRY	DATA/EVENT	MKT.	LAST	NZ TIME
20-Dec	NZ	Performance Services Index - NOV	--	52.0	10:30
	JN	Coincident Index CI - OCT F	--	100.7	18:00
	JN	Leading Index CI - OCT F	--	97.2	18:00
	JN	Nationwide Dept. Sales (YoY) - NOV	--	0.6%	18:30
	JN	Tokyo Dept. Store Sales (YoY) - NOV	--	2.7%	18:30
	GE	Producer Prices (MoM) - NOV	0.4%	0.4%	20:00
	JN	Convenience Store Sales YoY - NOV	--	-5.9%	20:00
	EC	Euro-Zone Current Account nsa - OCT	--	-9.2B	22:00
	EC	ECB Euro-Zone Current Account SA - OCT	--	-13.1B	22:00
21-Dec	US	Chicago Fed Nat Activity Index - NOV	--	-0.28	02:30
	EC	Euro-Zone Consumer Confidence - DEC A	--	-9.4	04:00
	NZ	New Zealand Net Migration SA - NOV	--	680.0	10:45
	AU	Conference Board Leading Index - OCT	--	-0.1%	12:00
	UK	GfK Consumer Confidence Survey - DEC	-21.0	-21.0	13:01
	AU	Reserve Bank's Board December Minutes - DEC	--	--	13:30
	NZ	Credit Card Spending SA (MoM) - NOV	--	0.6%	15:00
	JN	All Industry Activity Index (MoM) - OCT	-0.1%	-0.8%	17:30
	GE	GfK Consumer Confidence Survey - JAN	5.7	5.5	20:00
	UK	PSNB ex Interventions - NOV	--	10.3B	22:30
	UK	Public Finances (PSNCR) - NOV	--	2.4B	22:30
	UK	Public Sector Net Borrowing - NOV	16.8B	9.8B	22:30
22-Dec	JN	BOJ Target Rate - DEC	0.1%	0.1%	/2010
	NZ	Current Account Balance - 3Q	--	-0.880B	10:45
	NZ	Account Deficit-GDP Ratio - 3Q	--	-3.0%	10:45
	AU	Westpac Leading Index (MoM) - OCT	--	0.0%	12:30
	JN	Merchnds Trade Balance Total - NOV	¥480.1B	¥821.9B	12:50
	JN	Adjusted Merchnds Trade Bal. - NOV	¥626.3B	¥578.5B	12:50
	JN	Merchnds Trade Exports YoY - NOV	10.2%	7.8%	12:50
	JN	Merchnds Trade Imports YoY - NOV	9.0%	8.7%	12:50
	JN	Supermarket Sales (YoY) - NOV	--	-0.3%	18:00
	UK	Bank of England Minutes - DEC	--	--	22:30
	UK	Total Business Investment(QoQ) - 3Q F	--	-0.2%	22:30
	UK	GDP (QoQ) - 3Q F	0.8%	0.8%	22:30
	UK	Current Account (BP) - 3Q	--	-7.4B	22:30
23-Dec	US	GDP QoQ (Annualized) - 3Q T	2.8%	2.5%	02:30
	US	Personal Consumption - 3Q T	2.8%	2.8%	02:30
	US	GDP Price Index - 3Q T	2.3%	2.3%	02:30
	US	Core PCE QoQ - 3Q T	0.8%	0.8%	02:30
	US	Existing Home Sales - NOV	4.71M	4.43M	04:00
	US	House Price Index MoM - OCT	-0.1%	-0.7%	04:00
	US	Existing Home Sales MoM - NOV	6.8%	-2.2%	04:00
	NZ	GDP QoQ - 3Q	0.1%	0.2%	10:45
	UK	Index of Services (MoM) - OCT	--	0.6%	22:30
24-Dec	US	Durable Goods Orders - NOV	-0.6%	-3.3%	02:30
	US	Durables Ex Transportation - NOV	1.6%	-2.7%	02:30
	US	Cap Goods Orders Nondef Ex Air - NOV	0.8%	-4.5%	02:30
	US	Cap Goods Ship Nondef Ex Air - NOV	--	-1.5%	02:30
	US	Personal Income - NOV	0.3%	0.5%	02:30

Continued on following page

DATA EVENT CALENDAR

DATE	COUNTRY	DATA/EVENT	MKT.	LAST	NZ TIME
24-Dec	US	PCE Deflator (YoY) - NOV	- -	1.3%	02:30
	US	PCE Core (MoM) - NOV	0.1%	0.0%	02:30
	US	PCE Core (YoY) - NOV	0.9%	0.9%	02:30
	US	Initial Jobless Claims - w/e Dec 18	420K	420K	02:30
	US	Continuing Claims - w/e Dec 11	- -	4135K	02:30
	US	U. of Michigan Confidence - DEC F	74.5	74.2	03:55
	US	New Home Sales - NOV	300K	283K	04:00
	NZ	Money Supply M3 YoY - NOV	- -	1.8%	15:00

Key: AU: Australia, EC: Euro-zone, GE: Germany, JN: Japan, NZ: New Zealand, UK: United Kingdom, US: United States CH: China.

Sources: Dow Jones, Reuters, Bloomberg, ANZ, National Bank. All \$ values in local currency.

Note: All surveys are preliminary and subject to change.

LOCAL DATA WATCH

Key focus over the next few weeks: The December Half Year Economic and Fiscal Update signalled the Government's intention to move the public finances back into surplus by 2014/15, despite the weaker economy and various one-offs contributing to a larger deficit in 2010/11. Headline business confidence appears to be stabilising around mid-year levels after a September quarter lull, with firms appearing to be taking a wait and see approach. Encouragingly, employment, investment and profit expectations all increased. Household-centric data showed a cautious mood prevailing with a post-GST slump in consumer spending apparent, although housing market data showed some promise. The higher auction result for milk powder prices was a positive for the necessary rebalancing of the economy. This week the key focus will be the Q3 balance of payments and GDP. One-offs are expected to cap the annual deficit at 2.9 percent of GDP, whereas economic activity appears to have stalled in Q3. We continue to watch soft gauges for signs of direction, with forthcoming readings for business and consumer confidence providing insight into the pace of recovery in 2011.

DATE	DATA/EVENT	ECONOMIC SIGNAL	COMMENT
2010			
Tue 21 Dec (10:45am)	International travel and migration - Nov	Adding to the numbers	We expect a net permanent and long-term inflow of about 700 persons. Visitor arrival numbers should increase one to two percent.
Tue 21 Dec (3:00pm)	RBNZ Credit Card Statistics – Nov	Rising	We expect a 1.2 percent monthly increase in residential consent numbers. Firming consumer prices, particularly for petrol, appear to be partly responsible.
Wed 22 Dec (10:45am)	Balance of Payments – 2010Q3	Helpful one-offs	We expect a quarterly deficit of approximately \$1.5b, with re-insurance inflows boosting the transfers balance. The annual current account deficit is forecast to dip to 2.9 percent of GDP.
Thur 23 Dec (10:45am)	Gross Domestic Product – 2010Q3	Stalling	We expect a 0.1 percent quarterly fall in production GDP. There are large sector divergences, with weak construction and manufacturing activity partly offset by respectable retail and wholesale activity. Services sector output is likely to remain weak outside of the government sector.
2011			
Mon 10 Jan (10:45am)	Overseas Merchandise Trade - Nov	Improving annual surplus	A small monthly trade deficit of \$100m is expected. The annual trade surplus is projected to approach \$1.4b.
Tue 11 Jan (10:45am)	Building Consents- Nov	Up	We expect residential consent issuance to climb 2 percent. Consent issuance remains very weak.
Thur 13 Jan (10:45am)	Electronic Card Transactions - Dec	Last minute	A small monthly increase is expected as shoppers leave it till the last minute. Still, nothing too flash.
Thur 13 Jan (3:00pm)	ANZ Commodity Price Index – Dec	- -	- -
Mon 17 Jan (10:45am)	Food Price Index- Dec	Rising	We expect a 0.3 percent monthly increase.
Thur 20 Jan (10:45am)	Consumers Price Index- Q4	GST	We expect a 2.4 percent quarterly rise on account of the October increase in GST.
Thur 20 Jan (3:00pm)	ANZ-Roy Morgan Consumer Confidence	- -	- -
Fri 21 Jan (10:45am)	Retail Trade - Nov	Rising	Retail Indicators suggest a monthly increase of about 1.2 percent.
On Balance		An improving tone	GDP data will show the economy going backwards in Q3. Data for Q4 is likely to see a return to positive growth, but in fits and starts. We continue to look for forward-looking gauges to convey an improving tone.

KEY FORECASTS AND RATES

	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11
GDP (% qoq)	0.2	1.0	0.5	0.2	-0.1	0.5	0.8	1.0	1.7	1.5
GDP (% yoy)	-1.6	0.5	1.9	1.9	1.6	1.1	1.4	2.2	4.1	5.1
CPI (% qoq)	1.3	-0.2	0.4	0.2	1.1	2.4	0.6	1.0	0.8	0.5
CPI (% yoy)	1.7	2.0	2.0	1.7	1.5	4.1	4.4	5.2	4.9	2.9
Employment (% qoq)	-0.8	0.0	1.0	-0.2	1.0	0.3	0.5	0.7	0.6	0.4
Employment (% yoy)	-1.8	-2.4	-0.1	0.0	1.8	2.1	1.7	2.5	2.1	2.2
Unemployment Rate (% sa)	6.5	7.1	6.0	6.9	6.4	6.3	6.2	5.8	5.6	5.5
Current Account (% GDP)	-3.2	-2.8	-2.4	-3.0	-3.1	-2.4	-2.6	-2.4	-3.0	-2.7
Terms of Trade (% qoq)	-1.6	5.8	6.1	2.0	3.0	1.4	0.9	0.3	0.1	-0.9
Terms of Trade (% yoy)	-14.1	-8.2	0.1	12.7	17.9	13.1	7.5	5.7	2.7	0.3

	Feb-10	Mar-10	Apr-10	May-10	Jun-10	Jul-10	Aug-10	Sep-10	Oct-10	Nov-10
Retail sales (% mom)	-0.6	0.5	-0.4	0.4	1.0	-0.5	0.0	1.6
Retail sales (% yoy)	2.4	4.4	2.7	1.9	3.4	2.2	2.3	4.4
Credit Card Billings (% mom)	-0.2	0.9	-1.6	1.9	1.0	-1.1	0.8	0.9	0.6	..
Credit Card Billings (% yoy)	1.1	5.2	0.8	3.5	4.4	2.8	2.1	4.2	4.6	..
Car registrations (% mom)	0.9	5.0	2.7	-3.9	5.5	-6.4	-0.1	2.8	-3.7	11.9
Car registrations (% yoy)	31.4	31.7	40.5	30.5	35.8	16.0	19.0	19.2	9.4	23.5
Building consents (% mom)	6.4	-0.1	8.4	-10.1	2.1	3.0	-17.8	0.3	-2.0	..
Building consents (% yoy)	29.9	32.6	32.5	11.5	26.6	26.0	-3.1	-9.7	-17.7	-16.6
REINZ House Price (% yoy)	6.1	7.6	4.7	3.7	3.7	2.6	0.9	0.0	-1.4	1.4
Household Lending Growth (% mom)	0.2	0.0	0.2	0.2	0.2	0.2	0.1	0.2	0.0	..
Household Lending Growth (% yoy)	2.9	2.9	2.8	2.6	2.6	2.5	2.3	2.3	2.0	..
ANZ Roy Morgan Consumer Confidence	123.6	121.8	121.9	126.0	122.0	115.6	116.3	116.4	113.6	114.5
NBNZ Business Confidence	50.1	42.5	49.5	48.2	40.2	27.9	16.4	13.5	23.7	33
NBNZ Own Activity Outlook	41.9	38.6	43.0	45.3	38.5	32.4	25.7	26.7	30.5	35
Trade Balance (\$m)	328	608	660	770	221	-186	-413	-457	-319	..
Trade Balance (\$m ann)	-330	-160	178	41	593	585	889	993	1176	..
ANZ World Commodity Price Index (% mom)	3.7	1.8	5.1	1.2	-1.6	-0.8	-1.4	2.8	3.5	4
ANZ World Commodity Price Index (% yoy)	48.6	49.5	53.2	51.8	50.1	47.3	38.6	32.9	31.4	24
Net migration (sa)	1000	950	750	330	230	900	850	1040	680	..
Net migration (annual)	21618	20973	19954	17967	16504	15221	14507	13914	12610	..

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

KEY MARKET FORECASTS AND RATES

	ACTUAL			FORECAST (END MONTH)						
FX RATES	Oct-10	Nov-10	Today	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
NZD/USD	0.767	0.743	0.737	0.73	0.73	0.75	0.74	0.73	0.72	0.71
NZD/AUD	0.779	0.775	0.746	0.73	0.73	0.74	0.74	0.75	0.74	0.75
NZD/EUR	0.550	0.572	0.556	0.56	0.57	0.59	0.57	0.55	0.54	0.53
NZD/JPY	61.62	62.14	61.88	62.1	63.5	66.0	66.6	67.2	67.7	67.5
NZD/GBP	0.478	0.477	0.475	0.47	0.48	0.48	0.47	0.46	0.45	0.44
NZ\$ TWI	67.7	68.1	66.7	66.4	67.0	68.6	67.8	67.2	66.1	65.5
INTEREST RATES	Oct-10	Nov-10	Today	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12
NZ OCR	3.00	3.00	3.00	3.00	3.25	3.75	4.00	4.25	4.50	4.75
NZ 90 day bill	3.19	3.20	3.16	3.20	3.70	4.20	4.30	4.70	4.80	5.20
NZ 10-yr bond	5.24	5.66	5.71	5.60	5.90	5.90	5.90	5.80	5.80	5.80
US Fed funds	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.75	1.50
US 3-mth	0.29	0.30	0.39	0.35	0.35	0.35	0.35	0.35	0.85	1.60
AU Cash Rate	4.50	4.75	4.75	4.75	5.00	5.25	5.50	5.75	5.75	5.75
AU 3-mth	4.87	5.04	5.07	5.10	5.20	5.50	5.70	6.00	6.00	6.00

	17 Nov	13 Dec	14 Dec	15 Dec	16 Dec	17 Dec
Official Cash Rate	3.00	3.00	3.00	3.00	3.00	3.00
90 day bank bill	3.17	3.18	3.18	3.18	3.17	3.17
NZGB 11/11	4.21	4.09	4.07	4.10	4.10	4.09
NZGB 04/13	4.73	4.78	4.79	4.84	4.84	4.83
NZGB 12/17	5.42	5.63	5.66	5.73	5.74	5.72
NZGB 05/21	5.52	5.81	5.83	5.89	5.90	5.89
2 year swap	3.95	3.85	3.83	3.85	3.86	3.85
5 year swap	4.68	4.77	4.75	4.78	4.82	4.80
RBNZ TWI	69.1	67.8	67.4	67.5	67.0	67.0
NZD/USD	0.7680	0.7485	0.7501	0.7499	0.7391	0.7423
NZD/AUD	0.7855	0.7601	0.7530	0.7534	0.7492	0.7482
NZD/JPY	64.00	62.87	62.60	62.86	62.25	62.23
NZD/GBP	0.4836	0.4740	0.4728	0.4758	0.4753	0.4744
NZD/EUR	0.5683	0.5672	0.5601	0.5617	0.5593	0.5585
AUD/USD	0.9777	0.9847	0.9962	0.9953	0.9865	0.9921
EUR/USD	1.3513	1.3196	1.3393	1.3350	1.3215	1.3292
USD/JPY	83.33	84.00	83.46	83.82	84.23	83.83
GBP/USD	1.5881	1.5790	1.5864	1.5761	1.5549	1.5646
Oil (US\$/bbl)	80.43	87.81	88.62	88.33	88.66	88.02
Gold (US\$/oz)	1335.05	1386.91	1402.65	1397.10	1380.85	1375.00
Electricity (Haywards)	4.92	21.09	22.58	22.39	13.75	17.05
Baltic Dry Freight Index	2454	2076	2069	21004	2100	2100
Milk futures (US\$/contract)	117	120	121	122	122	122

IMPORTANT NOTICE

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.
- OnePath (NZ) Limited, as a wholly owned subsidiary of the Bank, is an associated person of the Bank. OnePath and its related companies may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- Direct Broking Limited (DBL), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. DBL 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;



IMPORTANT NOTICE

- 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.

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