

# NEW ZEALAND ECONOMICS ANZ MARKET FOCUS

20 September 2010

## INSIDE

|   |    |
|---|----|
| Economic Overview                         | 2  |
| Data Preview                              | 5  |
| Changes to New Zealand Trade<br>- Exports | 6  |
| Interest Rate Strategy                    | 8  |
| Currency Strategy                         | 9  |
| Data Event Calendar                       | 10 |
| Data Watch                                | 11 |
| Key Forecasts                             | 12 |

## NZ ECONOMICS TEAM

**Cameron Bagrie**  
Chief Economist  
Telephone: +64 4 802 2212  
E-mail: Cameron.Bagrie@anz.com

**Khoon Goh**  
Head of Market Economics and  
Strategy  
Telephone: +64 4 802 2357  
E-mail: Khoon.Goh@anz.com

**David Croy**  
Senior Interest Rate Strategist  
Telephone: +64 4 576 1022  
E-mail: David.Croy@anz.com

**Mark Smith**  
Economist  
Telephone: +64 4 802 2199  
E-mail: Mark.Smith2@anz.com

**Steve Edwards**  
Economist  
Telephone: +64 4 802 2217  
E-mail: Steve.Edwards@anz.com

**Con Williams**  
Rural Economist  
Telephone: +64 4 802 2361  
E-mail: Con.Williams@anz.com

## THE MIDDLE GROUND

### ECONOMIC OVERVIEW

We concur with a number of aspects presented in the RBNZ's September assessment. Notably, interest rates will need to move up over time and the path is likely to be intertwined with several on-hold decisions. But clearly monetary policy needs to remain more supportive for now. We likewise agree in spirit with the RBNZ that growth will be lower on average over a number of years – a dynamic we have referred to as the “transition” stage for the economy. However, abstracting from such dynamics (that will manifest over a number of years), we now find ourselves more upbeat than the RBNZ on prospects for 2011. As a result, we are now on the hawkish side relative to where markets (and the RBNZ's projections) believe interest rates will settle by the end of next year. This week sees the release of Q2 GDP and current account data, which we expect will highlight a respectable pace of expansion but with the current account deficit continuing its upward climb from cyclical lows.

### DATA PREVIEW

On account of a sizeable investment income deficit we expect a quarterly current account deficit of around \$1.8bn in the June 2010 quarter. The return to a quarterly goods and services deficit is also influential as imports recover from cyclical lows. June quarter GDP is expected to confirm the expansion is continuing, but with wide divergences in sectoral output.

### CHANGES TO NEW ZEALAND TRADE - EXPORTS

The much heralded lift in milk powder and log exports to China masks a wider trend in NZ's merchandise trade exports. This article looks at how the NZ merchandise export mix is evolving and how our export markets have changed over the past two decades. A greater share of our merchandise exports are heading to non-OCED economies, with commodity exports a key part to this.

### INTEREST RATE STRATEGY

The RBNZ's change of heart at last week's Monetary Policy Statement came as a bit of a surprise. But it was not so much their assessment, but the degree to which it had changed since June. Looking ahead, we wonder if the outlook is in fact brighter than the RBNZ is forecasting. Indeed, for the first time in a while we find ourselves at the optimistic end of the spectrum. But while we see limited scope for short end rates to fall, the back end should be supported.

### CURRENCY STRATEGY

The NZD continues to be rangebound against most currencies, despite a more dovish RBNZ. For this week, Q2 GDP and current account data is the key domestic focus, although given the historical nature of the releases, we do not anticipate much market reaction. Key for the NZD will be the RBA Governor's speech later today, and the FOMC meeting mid-week. Look for support at 0.7700 in NZD/AUD to be tested this week.

## ECONOMIC OVERVIEW

### SUMMARY

We concur with a number of aspects presented in the RBNZ's September assessment. Notably, interest rates will need to move up over time and the path is likely to be intertwined with several on-hold decisions. But clearly monetary policy needs to remain more supportive for now. We likewise agree in spirit with the RBNZ that growth will be lower on average over a number of years – a dynamic we have referred to as the “transition” stage for the economy. However, abstracting from such dynamics (that will manifest over a number of years), we now find ourselves more upbeat than the RBNZ on prospects for 2011. As a result, we are now on the hawkish side relative to where markets (and the RBNZ's projections) believe interest rates will settle by the end of next year. This week sees the release of Q2 GDP and current account data, which we expect will highlight a respectable pace of expansion but with the current account deficit continuing its upward climb from cyclical lows.

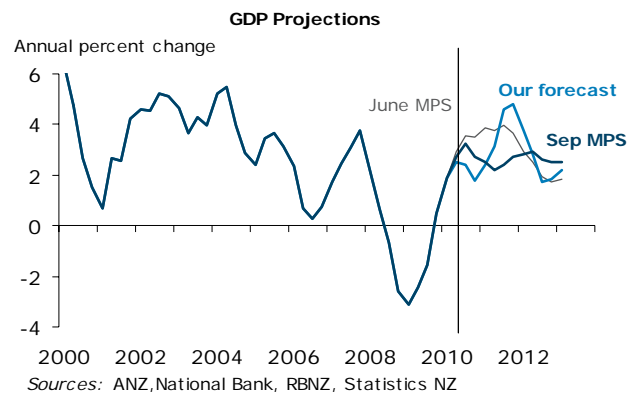
### THIS WEEK'S EVENTS

- **ANZ-Roy Morgan Consumer Confidence – September 2010** (Monday 20<sup>th</sup> September, 3:00pm).
- **SNZ External Migration – August 2010** (Tuesday 21<sup>st</sup> September, 10:45am). Last month's permanent and long-term (PLT) net inflow of 1,000 was a welcome development. We expect a similarly sized inflow but the risks of a pick-up in departures (after last month's fall) highlight the possibility of a smaller net inflow.
- **RBNZ Credit Card Billings – August 2010** (Tuesday 21<sup>st</sup> September, 3:00pm). We expect a broadly flat outturn for billings. The spirit remains one of consumer caution.
- **SNZ Balance of Payments – Q2 2010** (Wednesday 22<sup>nd</sup> September, 10:45am). We expect a quarterly deficit courtesy of a large investment income shortfall. The annual deficit is expected to climb to 3.5 percent of GDP. See our preview on page 5.
- **SNZ Gross Domestic Product – Q2 2010** (Thursday 23<sup>rd</sup> September, 10:45am). We expect a 0.7 percent increase. Lower primary and manufacturing sector production will be offset by firming services sector and construction sector activity. See our preview on page 5.

### WHAT'S THE VIEW?

We were looking for something cautious by the RBNZ last week, but were still taken by their

**assessment.** The tone of the Statement and policy assessment was considerably more circumspect than in June which on one hand is hardly surprising given the changing landscape. But when you see economic projections that have the level of GDP almost two percent lower by the end of next year, the change in view since the June MPS has been more than just a bit of tinkering. Examining the projections show a more subdued outlook for household and business spending. It seems the spirit of caution that is currently possessing domestic spending is now filtering through into the RBNZ's assessment of the economy and of the economic outlook.



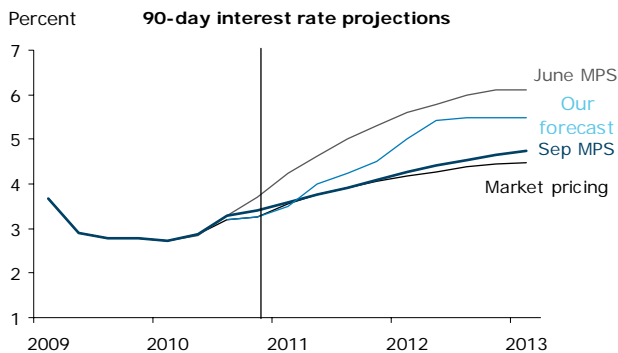
**The RBNZ's interest rate projections suggest only 150 basis points of tightening over the next two and a half years**, with several pauses implied by the forecasts. In part the more gradual tightening path also reflects the RBNZ now assuming a greater degree of permanence to bank funding costs and we concur with that! We did not believe speculation back in June that the cash rate was going to end up north of 6 percent.

**But we suddenly we find ourselves becoming cheerleaders for the economy relative to the RBNZ.** The economy is certainly in a flat patch and regular readers will be aware of the wariness we've expressed for 2010 and toward pockets of the global economy. But we'd caution against extrapolating that too far or too many years out, which is the inevitable temptation. The de-leveraging and balance sheet dynamic that is constraining growth at present is a huge positive for 2011. Sub 3 percent growth for the next 3 years as presented by the RBNZ just seems a little too plain to us. To be fair the RBNZ hasn't included the impact of the Canterbury earthquake yet, but neither did our projections a month ago and we still had something close to 4 percent for 2011.

**Why our different view? We're not only paying homage to the structural indicators that show an economy that is de-leveraging, but also to**

## ECONOMIC OVERVIEW

**human nature**, which tends not to stand idle and still indefinitely. Don't get us wrong, the economy faces challenges and has not de-leveraged anywhere near enough. But we simply suspect the degree of de-leveraging the economy has undergone will allow some scope for a bit of pent-up demand in 2011. Or put another way, it is not human nature to do everything (i.e. de-leverage) at once or in a linear fashion. At some stage people will want to have a bit of fun (i.e. have more growth) along the way.



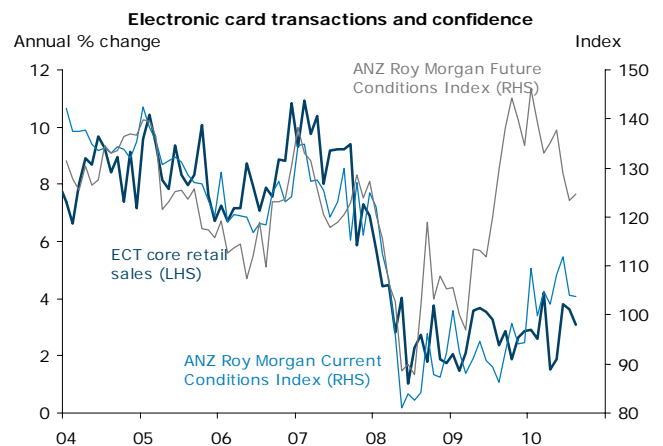
**With a more upbeat view on growth in 2011, we likewise find ourselves more hawkish vis-à-vis the market and RBNZ's interest rate projections.** In general we concur with a number of aspects presented in the RBNZ's September assessment. Notably, interest rates will need to move up over time, the path is likely to be intertwined with several on-hold decisions, but clearly monetary policy needs to remain more supportive for now. But just as we thought June's 90-day and growth projections were too high, September's seem too low and we now find our rate slate roughly half-way between the two.

**If there is a wake-up call in the RBNZ's economic projections, it resides in the underlying trends.** Potential growth is estimated to be around 2 percent. The economy plods along at 2.75 percent or so per year for the next three years. This is solid but hardly stellar given the downturn we have emerged from, and portends of an environment where it remains challenging to make a buck. Regular readers will be attuned to what we've referred to as the "transition" stage for the economy (refer to our *Market Focus* of 22 January), which is effectively a 5 year period where the economy simply cannot grow as fast owing to de-leveraging and physical changes that must occur across the economy (think capital and labour mobilisation for a start) in order for rebalancing from the non-tradable to the tradable sector to truly take hold. So we like the spirit of the RBNZ's view. **But policymakers should**

**be taking note here: the process of change and rebalancing requires more leadership and policy initiatives. Now is not the time to be pausing for a cup-of-tea.**

**This week sees the release of trade and activity data for Q2. Our preview is on page 5.** For the record we are expecting a 0.7 percent increase in Q2 GDP, with the annual current account deficit to widen to 3.5 percent of GDP. Given the lag at which this data is produced there is always a feeling that we are looking into the rear vision mirror when analysing the data. Given the events of late, the data is likely to take on an even more historical feel. However, knowing where you are heading depends in part on what has happened in the past, so we will still give the data some attention.

**Later this afternoon we have the release of the ANZ-Roy Morgan consumer confidence for September.** This is one of the first surveys to be released that covered the period leading up to and following the Canterbury earthquake, so it will be of interest, particularly as the survey records responses by regions.



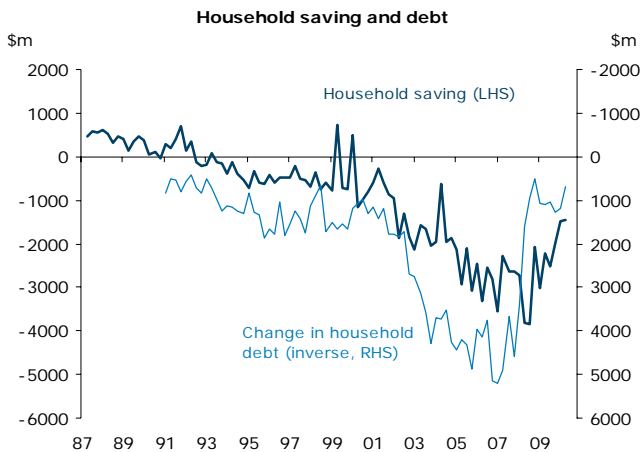
**RBNZ data on August credit card billings is expected to acknowledge that the month was not a particularly good one for retailers.** We expect a broadly flat result following the 1.2 percent fall in July. Last week's retail related data underlined the caution evident in the household sector. Evidence suggesting a pre-GST spend-up in durables was inconclusive but we are loath to rule this out at this stage given historical experience. When we look at early housing and retail reads for Q3, GDP prospects are looking pretty sombre, although once again we'd caution about reading too much into this. We are after all just about at the end of the quarter!

**If there is a positive spin to put on housing and retailing malaise, it is progress that is being**

## ECONOMIC OVERVIEW

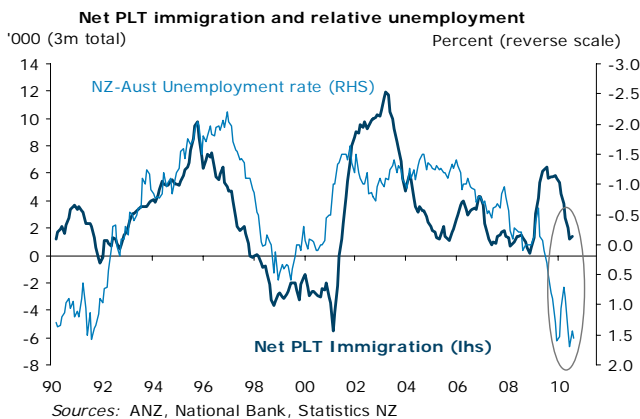
**made in terms of household saving.** Now NZ households remain dis-savers so the de-leveraging dynamic has not yet run its course. But according to our calculations, around two-thirds of the gap of consumption over household disposable income has closed over the last two years. This has occurred during a period where household debt accumulation has eased as the housing market slowdown has encouraged households to revisit borrow and spending habits and cut back spending on discretionary items.

**So while the household sector is not out of the woods, we can definitely see the light at the end of the tunnel.** It augurs well for a pick-up in household spending in 2011, after a subdued 2009 and 2010.



Sources: ANZ, National Bank, Statistics NZ, RBNZ

**External migration data for August is envisaged to show another large net inflow of around 1,000 persons.** This hinges on the assumption that departures do not trend higher. We have seen people put back their travel plans and there is always the risk that we could see a surge in departures.



Sources: ANZ, National Bank, Statistics NZ

Better employment conditions on offer across the Tasman are likely to remain tempting. Last week's

soggy housing market data suggested that this is the last thing that the sector needs at present. **Visitor arrivals are anticipated to continue trending higher in August.** An increase in Australian visitors is expected to boost the tally. However, as noted by the RBNZ, the composition of tourists matter for GDP, and the shift towards a greater proportion of high spending tourists would be more beneficial.

### RECENT LOCAL DATA

- REINZ Housing Market Statistics – August 2010.** Sales fell by a seasonally adjusted 3.3 percent to be 27.1 percent lower than 12-months earlier. The median days to sell inched down to 43 from 44 but is considerably above the mid 30s level that predominated over the second half of last year. In seasonally adjusted terms the REINZ housing price index eased by 0.1 percent in August and is 0.9 percent higher than in August 2009.
- SNZ Retail Trade Survey – July 2010.** Retail sales declined by 0.4 percent in July. Core retail values declined by 0.1 percent in July, to be 1.7 percent higher than a year earlier. Sales fell in 11 of the 20 core industries
- SNZ Electronic Card Transactions – August.** Total and core retail spending declined by a seasonally adjusted 0.2 percent (2.9 and 3.1 percent y/y respectively). The core retail components showed offsetting movements with durable spending declining by 1.1 percent.
- globalDairyTrade online auction – mid September.** Whole milk powder prices increased by an average of 1.4 percent in USD terms from the early September event. USD prices are nearly 10 percent below the April event but are around 20 percent higher than a year earlier in both USD and NZD terms.
- RBNZ Monetary Policy Statement – September 2010.** The OCR was held at 3 percent. Growth projections for the year to March 2011 were scaled back to 2.5 percent from 3.8 percent in the June MPS, with the 90-day interest rate climbing gradually to 4.7 percent by the March 2013 quarter (versus 6.1 percent in the June statement).
- Westpac-McDermott Miller Consumer Confidence –Q3.** Overall consumer sentiment eased 5.2 points to 114.1. Current conditions eased to 103.5, whereas future conditions fell to 121.3. Net balances in four out of the five questions fell, most notably for expectations of the economy over the next 12 months.

## DATA PREVIEW

## SUMMARY

On account of a sizeable investment income deficit we expect a quarterly current account deficit of around \$1.8bn in the June 2010 quarter. The return to a quarterly goods and services deficit is also influential as imports recover from cyclical lows. June quarter GDP is expected to confirm the expansion is continuing, but with wide divergences in sectoral output.

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

| Current Account | ANZ      | RBNZ  | Market   |
|-----------------|----------|-------|----------|
| Quarter         | -\$1800m | - -   | -\$700m  |
| Annual          | -\$6.6bn | - -   | -\$5.4bn |
| % of GDP        | -3.5%    | -3.1% | -2.9%    |

#### The June quarter is expected to herald business as usual with a quarterly deficit of \$1.8bn.

Improving domestic profitability is expected to deliver another large investment income deficit. This follows a period of much lower deficits over 2009 caused by lower profitability and debt servicing costs, and provisioning by the big four Australian banks over structured financial transactions. **Despite the improving terms of trade, we expect a small goods balance for Q2.** High export commodity prices will hold up export receipts but the key driver to the turnaround is a rebound in import volumes from cyclical lows. Declining tourism spending will contribute to the services deficit moving higher.

The annual current account deficit is expected to climb to 3.5 percent of GDP. The major factor in this is a return to large investment income deficits, with is partly offset by a narrowing trade balance. **The large investment income deficit is largely a consequence of borrow and spending habits of old.** Our high external debt is likely to restrict the ability of the spending side of the economy to fire without the support of the earning side. On the evidence of the September MPS it seems the RBNZ is also coming around to this conclusion.

**The Q2 release is when Statistics NZ introduce annual revisions** so this has the potential to affect the starting point. The new methodology for measuring investment income is expected to translate into higher historical estimates of investment income credits, but this will have a marginal impact on the size of deficits.

#### FINANCIAL MARKET IMPLICATIONS

The focus remains on the worsening trajectory of quarterly deficits. If the Q2 release suggests that a

larger than expected blow-out of the deficit is likely to occur, there could be some market reaction.

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

| GDP       | ANZ   | RBNZ  | Market |
|-----------|-------|-------|--------|
| QoQ       | +0.7% | +0.9% | +0.8%  |
| YoY       | +2.5% | +2.7% | +2.6%  |
| Ann. Ave. | +0.8% | +0.9% | +0.8%  |

**Headline production GDP is expected to expand by 0.7 percent in Q2.** Respectable, yes, but nonetheless a gradual recovery. By the end of June the economy will have recovered only about three quarters of the output lost in the recession.

**The Q2 GDP report is expected to highlight sectoral divergences.** Primary sector output is expected to ease by close to 1 percent in the quarter as a result of drought related disruptions, with production in the gas and mining sectors also lower. Output in the goods producing sector is expected to be weighed down with a sizeable fall in manufacturing sector output, offsetting a strong pick-up in construction output and an increase in value added from the electricity sector. **Driving growth in Q2 is a rebound in the services sector.** An increase in paid hours for real estate, business services and improving trade volumes is expected to underpin a pick-up in activity. Solid increases in wholesale and retail trade will also prove influential.

**On an expenditure basis, we expect growth in private consumption of consumer durables and residential investment to underpin a sizeable increase in gross national expenditure.** Stronger activity in these interest rate sensitive pockets would normally require interest rates to move higher, but data subsequent to Q2 suggests a stalling in activity in these sectors for Q3. Following a period of some weakness, we expect signs of recovering business investment to be evident, with non-residential construction activity rebounding from cyclical lows. Net trade is expected to make a more negative quarterly contribution with a solid increase in imports offsetting a small increase in export volumes.

#### FINANCIAL MARKET IMPLICATIONS

We expect limited market reaction as the focus will remain on the subsequent activity outlook in the quake aftermath. The RBNZ will be broadly comfortable with a GDP outturn slightly below its September MPS pick of 0.9 percent on account of weaker manufacturing data being publishing following the finalisation of their projections.

# CHANGES TO NEW ZEALAND'S TRADE - EXPORTS

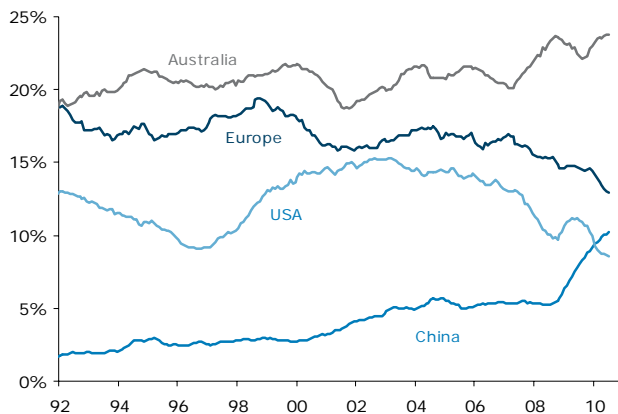
## SUMMARY

The much heralded lift in milk powder and log exports to China masks a wider trend in NZ's merchandise trade exports. This article looks at how the NZ merchandise export mix is evolving and how our export markets have changed over the past two decades. A greater share of our merchandise exports are heading to non-OECD economies, with commodity exports a key part to this.

## THE BIG PICTURE

**New Zealand's export mix is evolving.** Australia remains our largest trading partner, taking a larger share of our merchandise exports compared to two decades ago. By contrast, the share of merchandise exports to traditional trading partners in Europe and the US has eased considerably over the last decade. **The value of exports to emerging economies have increased fourfold since 1990, whereas those to OECD economies (excluding Australia) have only increased by a third.** Growing demand from China has been a factor, with this market now our second largest export destination. It is not just a China story, with exports to other destinations accounting for 80 percent of our exports to non-OECD countries.

Share of NZ's merchandise exports



Sources: ANZ, National Bank, Statistics NZ

To analyse what is going on in a little more depth we focus on New Zealand's 30 largest trading partners, which account for nearly 90 percent of the value of our merchandise exports. Within this subset we examine trends in exports by category and destination.

It showed that in 2010 exports to non-OECD countries accounted for 41 percent of total exports. Of commodity based exports, exports to non-OECD economies were slightly more than 50 percent. This represents a significant climb from the late 1980s

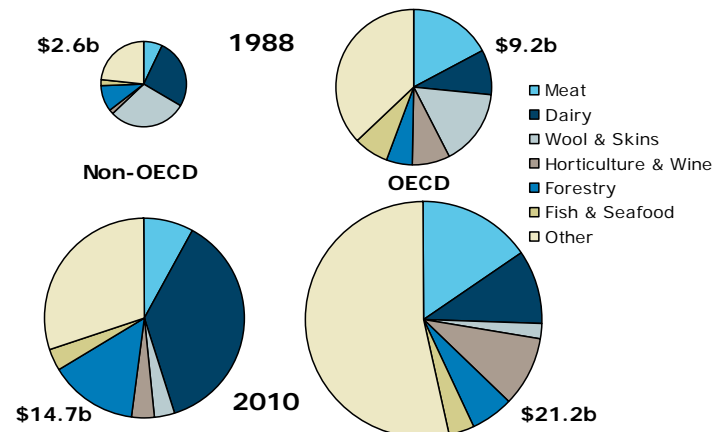
where emerging economies only accounted for 22 percent of commodity based exports.

**The mix of commodities has also changed with this transition.** Twenty two years ago wool and hides accounted for 30 percent of all the merchandise exports to the top 30 non-OECD nations, dairy accounted for 27 percent and forestry products 10 percent. In the latest data to July 2010, dairy's share of exports has risen to 37 percent, wool and hides has shrunk to just 4 percent and forestry products nudged up to 14 percent.

By comparison, in 1988 the share of wool and hides to the OECD nations within the top 30 nations we trade with was 16 percent, dairy accounted for 9 percent of exports and meat products recorded the largest share, at 17 percent. In 2010, wool and hides exports have evaporated to 2 percent, dairy was fairly stable on 10 percent, meat products have slipped a little to 16 percent and horticultural products (reflecting a surge in wine) has lifted from 8 percent to 10 percent.

The following pie charts summarise the trends in export markets in 1988 and 2010. The relative size of each pie reflects the total amount of exports for both periods.

NZ's Merchandise Exports to 30 Top Destinations



## THE RISING STARS

When looking across the commodity basket, there have been some large lifts in specific commodities.

- Dairy.** In pure monetary terms, dairy exports have posted the largest increase. In 1988 \$1.9b of dairy products was exported. In 2010 this figure had grown to \$9.6b. Over half of this increase has been in milk powder. Most of this went to emerging markets, with an increase of \$1.3bn in milk powder exports to China alone. Other growth markets included the Philippines

## CHANGES TO NEW ZEALAND'S TRADE - EXPORTS

(up \$218m), United Arab Emirates (\$217m) and Sri Lanka (\$214m).

- Forestry.** The value of forestry product exports has risen from \$800m in 1998, to \$3.3 b in 2010. Of the \$2.5b increase, \$1.8b was sent to emerging markets, with \$700m sent to developed nations. Once again China tops the table for individual countries taking our forestry exports. Total forestry products have increased \$930m between 1988 and 2010, with two-thirds of the increase being in the form of logs. The next largest increases have been forestry exports sent to Korea (up \$340m) and Japan (\$247m).
- Beef.** Over the past two decades the value of beef exports has increased by \$785m to \$1.8b in the 12-months to July 2010. The US remains our largest single market accounting for 40 percent of the value of exports. However, growth has been particularly noticeable in East Asian markets which tend to take the more valuable cuts. Major markets include Japan (nearly \$200m), South Korea (\$145m), Indonesia (\$136m) and Taiwan (\$115m). Nearly two-thirds of the growth in beef exports over the last 20 years has been to non-OECD markets.
- Seafood.** The value of exports in fish and seafood products has grown from \$700m in 1988 to \$1.3b in 2010. Exports to emerging nations have expanded by \$470m, with exports to China and Hong Kong accounting for \$363m.

### THE UPSHOT

New Zealand's main merchandise export markets are slowly but surely moving towards emerging Asia and Australia from the traditional markets of Europe and the United States. This shift has partly insulated the New Zealand export base from the worst effects of the global financial crisis. On the world stage, the Chinese, Indian and other emerging Asian economies are set to continue posting high rates of economic growth. Being more closely aligned to the wider Asian market bodes well for New Zealand's longer-term economic prospects but it also raises additional challenges.

Most of the export growth is still primary goods, which is not surprising given this is an area where NZ has strong comparative advantage. A secular upward trend in export commodity prices, on the basis of stronger demand from emerging markets, also played a role and will be beneficial for our prospects. However, the risk is that we become overly reliant on a few commodities, leaving ourselves vulnerable to large swings in commodity prices.

So while NZ has been successful in diversifying away from its traditional markets over the past two decades, the challenge is to diversify our export mix so that we do not become overly reliant on primary exports.

| NZ's top EXPORT markets for the 12mths ended July 2010 | Global Total  | Australia    | China        | USA          | Japan        | UK           | Korea        | Singapore    | Indonesia  | Hong Kong  | Taiwan     | Malaysia   | India      | Philippines | Germany    | Thailand   | Saudi Arabia | Canada     | Netherlands | France     | UAE        | Italy      | Belgium    | Vietnam    |   |
|--|---------------|--------------|--------------|--------------|--------------|--------------|--------------|--------------|------------|------------|------------|------------|------------|-------------|------------|------------|--------------|------------|-------------|------------|------------|------------|------------|------------|---|
|  | Sheepmeat     | 2,759        | 13           | 110          | 239          | 54           | 629          | 3            | 14         | 69         | 65         | 45         |            | 1           | 268        | 3          | 119          | 105        | 84          | 235        | 14         | 43         | 176        | 1          |   |
| Beef   | 1,839         | 11           | 8            | 730          | 197          | 29           | 145          | 42           | 136        | 37         | 115        | 12         | 35         | 15          | 6          | 5          | 99           | 23         | 1           | 17         | 19         | 7          | 1          |            |   |
| Other Meat   | 429           | 20           | 4            | 17           | 36           | 36           | 21           | 6            | 23         | 18         | 3          | 3          | 1          | 76          | 1          | 8          | 2            | 21         | 22          |            | 3          | 27         |            |            |   |
| Milk Powder  | 4,979         | 60           | 1,274        | 3            | 19           |              | 4            | 227          | 218        | 23         | 136        | 277        | 63         | 260         |            | 179        | 179          |            | 5           |            | 225        |            | 116        |            |   |
| Butter   | 1,786         | 77           | 92           | 107          | 2            |              | 17           | 38           | 54         | 16         | 49         | 37         | 70         | 79          | 1          | 24         | 72           | 10         |             |            | 26         |            | 53         | 58         |   |
| Cheese   | 1,382         | 288          | 62           | 16           | 273          | 53           | 94           | 11           | 42         | 20         | 37         | 26         |            | 59          |            | 10         | 44           |            | 28          |            | 17         |            | 28         | 3          |   |
| Whey/Casein  | 1,438         | 49           | 127          | 539          | 208          | 3            | 34           | 33           | 37         | 3          | 6          | 11         | 4          | 23          | 72         | 6          | 19           | 39         | 3           | 3          |            | 31         | 38         | 5          |   |
| Kiwifruit  | 1,051         | 49           | 80           | 33           | 295          |              | 73           | 9            | 4          | 23         | 64         | 12         | 2          | 1           |            | 4          |              | 4          |             |            | 3          | 34         |            | 1          |   |
| Apples   | 332           |              |              | 59           |              | 38           |              | 7            | 4          | 16         | 23         | 6          | 9          |             | 9          | 18         |              | 6          | 52          | 3          | 10         |            |            | 2          |   |
| other Fruit/Vege                                       | 561           | 248          | 3            | 31           | 132          | 5            | 19           | 12           | 1          | 9          | 13         | 20         | 1          | 1           | 5          | 8          |              | 1          | 2           | 2          |            | 1          |            |            |   |
| Wine   | 1,036         | 321          | 17           | 208          | 9            | 299          | 1            | 13           |            | 12         | 1          | 2          |            | 1           | 5          | 1          |              | 60         | 22          | 5          | 4          | 1          | 4          |            |   |
| Wool   | 672           | 89           | 133          |              | 118          |              | 87           | 1            | 121        |            | 32         | 23         | 10         | 12          |            | 31         |              |            |             |            |            |            | 4          | 2          |   |
| Skins/Hides  | 391           | 28           | 208          | 22           |              | 51           |              |              |            | 44         |            |            | 67         |             | 27         |            |              | 3          | 1           | 10         |            | 186        | 10         |            |   |
| Logs   | 1,254         |              | 677          |              | 146          |              | 284          |              | 1          |            | 10         |            | 121        |             |            | 3          |              |            | 2           |            |            | 7          |            | 2          |   |
| Sawn Timber  | 1,092         | 314          | 134          | 205          | 86           | 2            | 37           | 4            | 24         | 2          | 27         | 11         | 5          | 32          | 2          | 23         | 16           |            | 11          | 2          | 19         | 1          |            | 64         |   |
| Fibreboard/Plywood                                     | 341           | 65           | 35           | 16           | 149          |              | 2            |              | 18         |            | 5          | 5          | 3          | 4           |            | 1          | 4            | 2          |             |            | 2          |            |            | 22         |   |
| Wood Pulp  | 672           | 89           | 133          |              | 118          |              | 87           | 1            | 121        |            | 32         | 23         | 10         | 12          |            | 31         |              |            |             |            |            |            |            | 4          | 2 |
| Fish/Seafood   | 1,353         | 278          | 133          | 162          | 118          | 13           | 41           | 38           | 1          | 249        | 16         | 7          |            | 5           | 28         | 10         | 1            | 12         | 4           | 26         | 4          | 9          | 5          | 4          |   |
| Crude Oil  | 2,206         | 1,788        |              |              | 65           |              |              | 252          |            |            |            | 29         |            |             |            | 49         |              |            |             |            |            |            |            |            |   |
| Aluminium  | 1,091         | 126          | 28           | 34           | 588          | 36           | 105          | 1            | 4          | 12         | 14         | 5          | 11         |             | 9          | 12         |              | 3          | 43          | 7          | 1          |            | 2          | 5          |   |
| Remainder  | 13,983        | 5,832        | 939          | 1,151        | 589          | 354          | 386          | 409          | 205        | 283        | 189        | 223        | 356        | 170         | 139        | 159        | 43           | 135        | 169         | 125        | 64         | 80         | 48         | 93         |   |
| <b>TOTAL</b>   | <b>40,646</b> | <b>9,745</b> | <b>4,198</b> | <b>3,572</b> | <b>3,103</b> | <b>1,548</b> | <b>1,372</b> | <b>1,118</b> | <b>899</b> | <b>836</b> | <b>815</b> | <b>756</b> | <b>732</b> | <b>684</b>  | <b>655</b> | <b>566</b> | <b>509</b>   | <b>481</b> | <b>471</b>  | <b>441</b> | <b>412</b> | <b>408</b> | <b>407</b> | <b>383</b> |   |

# INTEREST RATE STRATEGY

## SUMMARY

The RBNZ's change of heart at last week's Monetary Policy Statement came as a bit of a surprise. But it was not so much their assessment, but the degree to which it had changed since June. Looking ahead, we wonder if the outlook is in fact brighter than the RBNZ is forecasting. Indeed, for the first time in a while we find ourselves at the optimistic end of the spectrum. But while we see limited scope for short end rates to fall, the back end should be supported.

## MARKET THEMES

- The RBNZ's endorsement of market pricing will keep a lid on interest rates for the time being. However, with such a flat profile, the market is vulnerable to positive data surprises.
- This week's US FOMC meeting takes centre stage offshore. Some expect the Fed signal QE, but most feel it's too soon. High unemployment and weak inflation has kept the market guessing.
- NZGS have finally found favour, after weeks out in the cold, with solid demand at last week's tender spurred on by negative swap spreads.

## REVIEW AND OUTLOOK

**It was not so much the RBNZ's projections themselves, but rather the degree to which they had changed that surprised us last week.**

Indeed, a downgrade was always on the cards, but we wonder whether the Bank is now too downbeat, mindful of what 2011 has in store. The Canterbury quake is a negative development for sure, but the associated re-building effort will take some slack out of the economy, as will the Rugby World Cup. The MPS certainly has a feeling of capitulation about it, and we're always mindful of not getting to bearish at the bottom (or bullish at the top). Indeed, for the first time in a while, we find ourselves more optimistic than the Reserve Bank!

Not surprisingly, **the market has gravitated to the RBNZ's 90-day bill rate projections.** But as we look ahead, with just 70bps of hikes priced in over the next year, **the market feels vulnerable to upside surprises.** In fact, given the degree of tightening that's been priced out (with 2yr swaps down from around 4.25 percent to 3.75 percent in the past 8 weeks), the market would need to move to expecting cuts for a move like that to be repeated, and that seems a tall order with the OCR at 3 percent. The point - most of the adjustment is done.

The long end is a different story, and this week's US FOMC meeting is the key event. Quantitative easing is still on the cards – but not yet. **This may**

**disappoint the market near-term, but the outlook for US rates remains benign,** keeping downward pressure on NZ rates.

## PREFERRED BORROWING STRATEGIES

We remain of the view that rates are at attractive levels to be gradually adding to cover. While the RBNZ's latest projections suggest there is no hurry to hedge, with the next rate hike not likely till March next year, if you wait till then the opportunity may have passed. We suspect the RBNZ has swung too far. As we head into 2011, with quake rebuilding and the RWC supporting activity, we think there could be upside surprises. But with the prospect of more QE keeping US rates down, rates may move lower yet. As such it pays to be picky. We favour progressively adding to cover as rates edge lower, mindful of conflicting domestic and global forces at play.

## GAUGES FOR NZ INTEREST RATES

| GAUGE                 | DIRECTION | COMMENT  |
|-----------------------|-----------|--|
| RBNZ / OCR            | ↔         | Very circumspect tone, and on hold until 2011.                           |
| NZ data               | ↔         | Stabilising. Q2 GDP data likely to be reasonable.                        |
| Fed Funds / front end | ↔         | All eyes on the FOMC on Wed morning (NZ time).                           |
| RBA                   | ↔/↑       | 2010 hikes still on the cards. RBA Minutes this week.                    |
| US 10 year            | ↔/↓       | Biased lower. Fed unlikely to want rates any higher.                     |
| NZ swap curve         | ↔/↓       | Biased to flatten. Short end rally complete, long end has downside risk. |
| Flow                  | ↔/↓       | Pay side has evaporated.   |
| Technicals            | ↔/↓       | Prior lows now in sight.   |

## MARKET EXPECTATIONS FOR RBNZ OCR (BPS)

| OCR DATES     | LAST WEEK    | THIS WEEK |
|---------------|--------------|-----------|
| Thu 28-Oct-10 | +10          | +2        |
| Thu 9-Dec-10  | +16          | +6        |
| Thu 27-Jan-11 | +24          | +15       |
| Thu 10-Mar-11 | +36          | +29       |
| Thu 28-Apr-11 | +43          | +40       |
| Thu 9-Jun-11  | +47          | +46       |
| Thu 28-Jul-11 | Not forecast | +54       |

## TRADING THEMES WE FAVOUR AT PRESENT

Swap spreads are finally crunching in (to less negative levels), spurred on by strong demand for NZGS. We think spreads are unsustainable here, but it was always going to take solid NZGS buying to expect some normalisation. That has now begun. We like curve flatteners here on the basis that you'd almost need to see cuts priced in for the short end to rally much further. However the long end should get supported by lower US rates.



# CURRENCY STRATEGY

## SUMMARY

The NZD continues to be rangebound against most currencies, despite a more dovish RBNZ. For this week, Q2 GDP and current account data is the key domestic focus, although given the historical nature of the releases, we do not anticipate much market reaction. Key for the NZD will be the RBA Governor's speech later today, and the FOMC meeting mid-week. Look for support at 0.7700 in NZD/AUD to be tested this week.

## MARKET THEMES

- NZD still rangebound. With a data-rich week ahead expect increased volatility.
- The support in NZD/AUD at 0.7800 broke on dovish RBNZ. Major support now 0.7700.
- EUR strength has been undermined by fresh fears about the solvency of Portugal and Ireland.
- BoJ has defined the high in yen for now.

## REVIEW AND OUTLOOK

**After a very strong start to the week, the dovish RBNZ undermined the NZD, again reconfirming its rangebound nature.** The myriad data both onshore and offshore this week will likely deliver volatility within the broad range but we see nothing significant to cause a break outside. We see the range this week at 0.7160 to 0.7360.

**The main offshore focus this week is on the FOMC meeting,** where the market is looking for some instant gratification in the form of language hinting at further QE. But we believe they will be disappointed again, as the hurdle for further Fed action is very high.

**NZD/AUD broke support at 0.7800 on the dovish RBNZ. Next support is at 0.7700, and RBA Governor Stevens' speech today could well bring that into play.** The weaker tone from the RBNZ, compared to the RBA's trademark upbeat assessments, is garnering support for a lower NZD/AUD. However, we need to be wary of how much of this difference is already priced in. Indeed the 0.7555 low we saw earlier this year was a 10 year low. From a medium to long term perspective, sub 0.7700 seems a good place to accumulate.

**The EUR shrugged off the negative side of Basel III and focussed instead on the extended timeframe to get the books in order.** After a strong week, the EUR suffered a setback from press articles questioning the solvency of Portugal and Ireland. As with other currencies the EUR remains

mired in a trading range and is capped by the 200 day moving average at 1.3235.

**BoJ surprised with unilateral intervention to weaken the yen.** The timing of the action immediately after a leadership contest in the ruling party also surprised. The action coincided exactly with the key support at 82.90 USDJPY. We can now be reasonably confident that a *short term* high in the yen is in place.

### NZD VS AUD: MONTHLY DIRECTIONAL GAUGES

| GAUGE              | DIRECTION | COMMENT  |
|--------------------|-----------|--|
| Fair value         | ↔         | Not that far off fair value.                                   |
| Yield              | ↔         | RBA on hold "for the time being". RBNZ on hold till next year. |
| Commodities        | ↔         | Soft commodities performing better, lending support to NZD.    |
| Partial indicators | ↓         | Australian data outperforming NZ's.                            |
| Technicals         | ↔         | Support at 0.7700, resistance at 0.8000.                       |
| Sentiment          | ↔         | Equities and China still influential.                          |
| Other              | ↑         | Earthquake insurance flows to support NZD.                     |
| <b>On balance</b>  | ↔         | <b>Range trade 0.77-0.80.</b>                                  |

### 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                   | ↑         | FOMC to hold long end down.   |
| Commodities             | ↔/↑       | Remain supportive overall.  |
| Risk aversion           | ↔         | Fresh sovereign debt concerns in Europe denting risk appetite.            |
| Partial indicators      | ↔/↓       | NZ data still largely disappointing.                                      |
| Technicals              | ↔         | Support at 0.7160. Resistance at 0.7350.                                  |
| AUD                     | ↑         | Australian economic data to lift.   |
| Sentiment               | ↑         | "New world/old world" theme shifting NZD sentiment toward Australia/Asia. |
| Other                   | ↔/↑       | Earthquake insurance flows to support NZD.                                |
| <b>On balance</b>       | ↔/↑       | <b>Remains overall supported sub 0.70.</b>                                |

## DATA EVENT CALENDAR

| DATE   | COUNTRY | DATA/EVENT                                   | MKT.   | LAST    | NZ TIME |
|--------|---------|--|--------|---------|---------|
| 20-Sep | NZ      | Performance Services Index - AUG             | --     | 50.5    | 10:30   |
|        | UK      | Rightmove House Prices (MoM) - SEP           | --     | -1.70%  | 11:01   |
|        | UK      | Rightmove House Prices (YoY) - SEP           | --     | 4.30%   | 11:01   |
|        | NZ      | ANZ Consumer Confidence Index - SEP          | --     | 116.3   | 15:00   |
|        | UK      | Major Banks Mortgage Approvals - AUG         | 46K    | 47K     | 20:30   |
|        | UK      | M4 Money Supply (YoY) - AUG P                | --     | 2.30%   | 20:30   |
| 21-Sep | US      | NAHB Housing Market Index - SEP              | 14     | 13      | 02:00   |
|        | NZ      | New Zealand Net Migration SA - AUG           | --     | 970     | 10:45   |
|        | AU      | Reserve Bank's Board September Minutes - SEP | --     | --      | 13:30   |
|        | NZ      | Credit Card Spending SA (MoM) - AUG          | --     | -1.20%  | 15:00   |
|        | NZ      | Credit Card Spending (YoY) - AUG             | --     | 2.70%   | 15:00   |
|        | UK      | Public Sector Net Borrowing - AUG            | 12.5B  | 3.2B    | 20:30   |
| 22-Sep | US      | Housing Starts - AUG                         | 550K   | 546K    | 00:30   |
|        | US      | Housing Starts MOM% - AUG                    | 0.70%  | 1.70%   | 00:30   |
|        | US      | Building Permits - AUG                       | 560K   | 565K    | 00:30   |
|        | US      | Building Permits MOM% - AUG                  | 0.20%  | -3.10%  | 00:30   |
|        | US      | FOMC Rate Decision - SEP                     | 0.25%  | 0.25%   | 06:15   |
|        | NZ      | Current Account Balance - 2Q                 | --     | 0.176B  | 10:45   |
|        | NZ      | Current Account-GDP Ratio - 2Q               | --     | -2.40%  | 10:45   |
|        | UK      | Bank of England Minutes - SEP                | --     | --      | 20:30   |
|        | EC      | Industrial New Orders SA (YoY) - JUL         | 16.20% | 22.60%  | 21:00   |
| 23-Sep | EC      | Euro-Zone Consumer Confidence - SEP A        | -10    | -11     | 02:00   |
|        | US      | House Price Index MoM - JUL                  | -0.10% | -0.30%  | 02:00   |
|        | NZ      | GDP QoQ - 2Q                                 | --     | 0.60%   | 10:45   |
|        | NZ      | GDP YoY - 2Q                                 | --     | 1.90%   | 10:45   |
|        | GE      | PMI Manufacturing - SEP A                    | 57.6   | 58.2    | 19:30   |
|        | GE      | PMI Services - SEP A                         | 57.2   | 57.2    | 19:30   |
|        | EC      | PMI Composite - SEP A                        | 55.7   | 56.2    | 20:00   |
|        | EC      | PMI Manufacturing - SEP A                    | 54.5   | 55.1    | 20:00   |
|        | EC      | PMI Services - SEP A                         | 55.5   | 55.9    | 20:00   |
|        | UK      | BBA Loans for House Purchase - AUG           | 34000  | 33698   | 20:30   |
| 24-Sep | US      | Initial Jobless Claims - 18 SEP              | 450K   | 450K    | 00:30   |
|        | US      | Continuing Claims - 11 SEP                   | 4483K  | 4485K   | 00:30   |
|        | US      | Existing Home Sales - AUG                    | 4.10M  | 3.83M   | 02:00   |
|        | US      | Leading Indicators - AUG                     | 0.10%  | 0.10%   | 02:00   |
|        | US      | Existing Home Sales MoM - AUG                | 7.10%  | -27.20% | 02:00   |
|        | CH      | MNI Business Condition Survey - SEP          | --     | 62.16   | 13:35   |
|        | GE      | Import Price Index (YoY) - AUG               | 8.70%  | 9.90%   | 18:00   |
|        | GE      | IFO - Business Climate - SEP                 | 106.4  | 106.7   | 20:00   |
|        | GE      | IFO - Current Assessment - SEP               | 108.7  | 108.2   | 20:00   |
|        | GE      | IFO - Expectations - SEP                     | 104    | 105.2   | 20:00   |
| 25-Sep | US      | Durable Goods Orders - AUG                   | -1.00% | 0.30%   | 00:30   |
|        | US      | Durables Ex Transportation - AUG             | 1.00%  | -3.80%  | 00:30   |
|        | US      | New Home Sales - AUG                         | 295K   | 276K    | 02:00   |
|        | US      | New Home Sales MoM - AUG                     | 6.90%  | -12.40% | 02:00   |

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.



## NEW ZEALAND DATA WATCH

**Key focus over the next four weeks:** As widely expected the RBNZ paused in the September MPS, but the tone of the statement was more circumspect, with the 90-day track only reaching 4.7 percent by the end of the projection period. This week's data should confirm a "respectable" increase in GDP for Q2, although the Q2 balance of payments will show further deterioration. Earthquake related reconstruction will provide a boost to 2011 but GDP for Q3 2010 will be weighed down by earthquake disruptions. We continue to closely watch the soft gauges for signs of direction but remain mindful of the earthquake impact on sentiment.

| DATE                  | DATA/EVENT                               | ECONOMIC SIGNAL        | COMMENT   |
|-----------------------|--|------------------------|---|
| Mon 20 Sep (3:00pm)   | ANZ Roy Morgan Consumer Confidence       | - -                    | - -   |
| Tue 21 Sep (10:45am)  | International Travel and Migration - Aug | Up                     | We expect a similarly sized net migration inflow to last month with risks of a larger than expected pick-up in departures.  |
| Tue 21 Sep (3:00pm)   | RBNZ Credit Card Billings - Aug          | Flat                   | A broadly flat outturn is expected, following the 1.2 percent decline in July. Consumers remain cautious.   |
| Wed 22 Sep (10:45am)  | Balance of Payments – Q2                 | Back to usual          | We expect a sizeable investment income deficit to deliver a large quarterly deficit. The annual deficit is expected to climb to 3.5 percent of GDP.                             |
| Fri 24 Sep (10:45am)  | Gross Domestic Product – Q2              | Respectable            | We expect a 0.7 percent increase. Firmer services sector output to be offset by weaker output from the primary and goods producing sectors.                                     |
| Wed 29 Sep (10:45am)  | Overseas Merchandise Trade - Aug         | In the red             | Seasonal factors, a higher NZD/USD, and lower commodity prices should contribute to a \$400m monthly deficit. The annual trade surplus should climb to \$900m.                  |
| Wed 29 Sep (3:00pm)   | RBNZ Credit Aggregates - Aug             | Subdued                | Deleveraging is ongoing with the subdued housing market likely to keep housing credit growth low.   |
| Thur 30 Sep (10:45am) | Building Consents - Aug                  | Rising                 | Some reversal of the July fall in ex-apartment consents is expected. Can non-residential consents maintain recent vigour?   |
| Thur 30 Sep (3:00pm)  | NBNZ Business Outlook - Sep              | - -                    | - -   |
| Mon 4 Oct (3:00pm)    | ANZ Commodity Price Index - Sep          | - -                    | - -   |
| Tue 5 Oct (10:00am)   | NZIER QSBO – Q3                          | Easing off             | The General business situation is expected to continue tracking lower, with domestic trading activity stalling. The earthquake may push up surveyed capacity utilisation.       |
| Wed 6 Oct (early am)  | globalDairyTrade online auction          | Inching higher         | We expect the early October event to show a small step up in whole milk powder prices. The smaller quantities on offer are likely to add to price volatility in trading events. |
| Mon 11 Oct (10:45am)  | Electronic Card Transactions - Sep       | Better late than never | We expect a monthly increase of more than 2 percent as households take the opportunity to beat the GST rise.  |
| Wed 13 Oct (10:45am)  | Food Price Index - Sep                   | Moving higher          | The unwinding of retail discounting and high commodity export prices should lift prices for groceries and meat.   |
| Thur 14 Oct (10:00am) | REINZ Housing Market Statistics - Sep    | Easing off             | As a consequence of the Canterbury earthquake we expect a 5 percent fall in sales. Downward pressures on prices remain.   |
| Thur 14 Oct (10:30am) | BNZ Business NZ PMI - Sep                | Disruption             | Christchurch is a major manufacturing hub so we expect some disruption. The spirit remains one of gradual expansion.  |
| Thur 14 Oct (10:45am) | SNZ Retail Trade Survey - Aug            | Cautious               | Retail indicators suggest a small fall in August retail sales. Households continue to focus on repairing balance sheets.  |
| <b>On Balance</b>     |  |                        | <b>August data mixed but activity and confidence data for Q3 and Q4 will be subdued.</b>  |

## ECONOMIC FORECASTS AND INDICATORS

|                          | Sep-09 | Dec-09 | Mar-10 | Jun-10      | Sep-10      | Dec-10      | Mar-11      | Jun-11      | Sep-11      | Dec-11      |
|--------------------------|--------|--------|--------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| GDP (% qoq)              | 0.3    | 0.9    | 0.6    | <b>0.7</b>  | <b>0.2</b>  | <b>0.3</b>  | <b>1.2</b>  | <b>1.4</b>  | <b>1.6</b>  | <b>0.5</b>  |
| GDP (% yoy)              | -1.5   | 0.5    | 1.9    | <b>2.5</b>  | <b>2.4</b>  | <b>1.8</b>  | <b>2.4</b>  | <b>3.1</b>  | <b>4.6</b>  | <b>4.8</b>  |
| CPI (% qoq)              | 1.3    | -0.2   | 0.4    | 0.3         | <b>1.1</b>  | <b>2.8</b>  | <b>0.6</b>  | <b>1.0</b>  | <b>0.8</b>  | <b>0.5</b>  |
| CPI (% yoy)              | 1.7    | 2.0    | 2.0    | 1.8         | <b>1.6</b>  | <b>4.6</b>  | <b>4.8</b>  | <b>5.6</b>  | <b>5.3</b>  | <b>3.0</b>  |
| Employment (% qoq)       | -0.8   | 0.0    | 1.0    | -0.3        | <b>0.5</b>  | <b>0.4</b>  | <b>0.6</b>  | <b>0.7</b>  | <b>0.6</b>  | <b>0.4</b>  |
| Employment (% yoy)       | -1.8   | -2.4   | -0.1   | 0.0         | <b>1.3</b>  | <b>1.6</b>  | <b>1.2</b>  | <b>2.2</b>  | <b>2.3</b>  | <b>2.3</b>  |
| Unemployment Rate (% sa) | 6.5    | 7.1    | 6.0    | 6.8         | <b>6.6</b>  | <b>6.4</b>  | <b>6.1</b>  | <b>5.7</b>  | <b>5.5</b>  | <b>5.4</b>  |
| Current Account (% GDP)  | -3.2   | -2.9   | -2.4   | <b>-3.5</b> | <b>-4.5</b> | <b>-3.7</b> | <b>-4.0</b> | <b>-3.8</b> | <b>-3.6</b> | <b>-3.6</b> |
| Terms of Trade (% qoq)   | -1.6   | 5.8    | 6.1    | 2.0         | <b>3.0</b>  | <b>1.0</b>  | <b>-0.5</b> | <b>-0.7</b> | <b>0.0</b>  | <b>-1.0</b> |
| Terms of Trade (% yoy)   | -14.1  | -8.2   | 0.1    | 12.7        | <b>17.9</b> | <b>12.5</b> | <b>5.6</b>  | <b>2.7</b>  | <b>-0.2</b> | <b>-2.1</b> |

|   | Nov-09 | Dec-09 | Jan-10 | Feb-10 | Mar-10 | Apr-10 | May-10 | Jun-10 | Jul-10 | Aug-10 |
|---|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Retail Sales (% mom)                    | 0.7    | -0.4   | 0.7    | -0.6   | 0.5    | -0.3   | 0.4    | 1.0    | -0.4   | ..     |
| Retail Sales (% yoy)                    | 2.4    | 2.0    | 2.3    | 2.4    | 4.4    | 2.7    | 1.9    | 3.4    | 2.2    | ..     |
| Credit Card Billings (% mom)            | 0.8    | -1.2   | 1.6    | -0.2   | 0.8    | -1.7   | 1.9    | 1.0    | -1.2   | ..     |
| Credit Card Billings (% yoy)            | 1.6    | 1.9    | 2.6    | 1.1    | 5.2    | 0.8    | 3.4    | 4.4    | 2.7    | ..     |
| Car Registrations (% mom)               | 2.3    | 6.8    | -0.6   | 0.4    | 5.2    | 2.9    | -3.8   | 5.6    | -6.4   | -0.2   |
| Car Registrations (% yoy)               | 2.4    | 0.3    | 15.9   | 31.4   | 31.7   | 40.5   | 30.5   | 35.8   | 16.0   | 19.0   |
| Building Consents (% mom)               | 0.8    | -3.7   | -2.7   | 6.1    | -0.3   | 8.5    | -9.2   | 3.3    | 3.2    | ..     |
| Building Consents (% yoy)               | 20.3   | 22.7   | 35.4   | 29.9   | 33.3   | 32.0   | 11.1   | 27.9   | 26.5   | ..     |
| REINZ House Price (% yoy)               | 5.2    | 9.6    | 7.7    | 6.1    | 7.6    | 4.7    | 3.7    | 3.7    | 2.6    | 0.9    |
| Household Lending Growth (% mom)        | 0.0    | 0.2    | 0.2    | 0.1    | 0.1    | 0.2    | 0.2    | 0.2    | 0.2    | ..     |
| Household Lending Growth (% yoy)        | 2.7    | 2.7    | 2.7    | 2.7    | 2.8    | 2.7    | 2.5    | 2.5    | 2.3    | ..     |
| ANZ-Roy Morgan Consumer Confidence      | 121.5  | 118.6  | 131.4  | 123.6  | 121.8  | 121.9  | 126.0  | 122.0  | 115.6  | 116.3  |
| NBNZ Business Confidence                | 43.4   | 38.5   | ..     | 50.1   | 42.5   | 49.5   | 48.2   | 40.2   | 27.9   | 16.4   |
| NBNZ Own Activity Outlook               | 33.7   | 36.9   | ..     | 41.9   | 38.6   | 43.0   | 45.3   | 38.5   | 32.4   | 25.7   |
| Trade Balance (\$m)                     | -280   | -26    | 271    | 328    | 608    | 660    | 765    | 214    | -186   | ..     |
| Trade Balance (\$m annual)              | -863   | -549   | -176   | -330   | -160   | 178    | 37     | 581    | 573    | ..     |
| ANZ World Commodity Price Index (% mom) | 11.0   | 2.5    | 0.3    | 3.7    | 1.8    | 5.1    | 1.2    | -1.6   | -0.8   | -1.4   |
| ANZ World Commodity Price Index (% yoy) | 17.8   | 30.4   | 36.7   | 48.6   | 49.5   | 53.2   | 51.8   | 50.1   | 47.3   | 38.6   |
| Net Migration (sa)                      | 1750   | 1690   | 1840   | 1000   | 950    | 760    | 300    | 140    | 970    | ..     |
| Net Migration (annual)                  | 20021  | 21253  | 22588  | 21618  | 20973  | 19954  | 17967  | 16504  | 15221  | ..     |

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       | Jul-10 | Aug-10 | Today | Dec-10               | Mar-11 | Jun-11 | Sep-11 | Dec-11 | Mar-12 | Jun-12 |
| NZD/USD        | 0.726  | 0.699  | 0.727 | 0.710                | 0.720  | 0.734  | 0.730  | 0.720  | 0.710  | 0.700  |
| NZD/AUD        | 0.802  | 0.785  | 0.775 | 0.755                | 0.750  | 0.753  | 0.760  | 0.766  | 0.789  | 0.795  |
| NZD/EUR        | 0.556  | 0.551  | 0.557 | 0.568                | 0.600  | 0.612  | 0.608  | 0.610  | 0.602  | 0.583  |
| NZD/JPY        | 62.78  | 58.86  | 62.34 | 60.35                | 62.64  | 65.33  | 67.16  | 67.68  | 69.58  | 70.00  |
| NZD/GBP        | 0.463  | 0.455  | 0.465 | 0.458                | 0.459  | 0.468  | 0.474  | 0.462  | 0.449  | 0.432  |
| NZ\$ TWI       | 67.5   | 65.5   | 67.0  | 66.1                 | 67.7   | 69.0   | 69.3   | 69.1   | 69.2   | 68.3   |
| INTEREST RATES | Jul-10 | Aug-10 | Today | Dec-10               | Mar-11 | Jun-11 | Sep-11 | Dec-11 | Mar-12 | Jun-12 |
| NZ OCR         | 3.00   | 3.00   | 3.00  | 3.00                 | 3.25   | 3.75   | 4.00   | 4.25   | 4.75   | 5.25   |
| NZ 90 day bill | 3.27   | 3.21   | 3.18  | 3.30                 | 3.70   | 4.20   | 4.30   | 4.70   | 5.20   | 5.50   |
| NZ 10-yr bond  | 5.33   | 5.13   | 5.31  | 5.50                 | 5.60   | 5.80   | 6.20   | 6.20   | 6.10   | 6.00   |
| US Fed funds   | 0.25   | 0.25   | 0.25  | 0.25                 | 0.25   | 0.25   | 0.50   | 0.75   | 1.25   | 1.75   |
| US 3-mth       | 0.45   | 0.30   | 0.29  | 0.35                 | 0.35   | 0.35   | 0.60   | 0.85   | 1.35   | 1.85   |
| AU Cash Rate   | 4.50   | 4.50   | 4.50  | 5.00                 | 5.25   | 5.50   | 5.75   | 6.00   | 6.00   | 6.00   |
| AU 3-mth       | 4.78   | 4.75   | 4.78  | 5.30                 | 5.60   | 6.00   | 6.00   | 6.20   | 6.10   | 6.10   |

|                              | 17 Aug  | 13 Sep  | 14 Sep  | 15 Sep  | 16 Sep  | 17 Sep  |
|------------------------------|---------|---------|---------|---------|---------|---------|
| Official Cash Rate           | 3.00    | 3.00    | 3.00    | 3.00    | 3.00    | 3.00    |
| 90 day bank bill             | 3.24    | 3.20    | 3.20    | 3.19    | 3.17    | 3.17    |
| NZGB 11/11                   | 3.52    | 3.82    | 3.77    | 3.74    | 3.68    | 3.63    |
| NZGB 04/13                   | 3.95    | 4.26    | 4.21    | 4.18    | 4.13    | 4.05    |
| NZGB 12/17                   | 4.85    | 5.17    | 5.13    | 5.12    | 5.07    | 5.01    |
| NZGB 05/21                   | 5.16    | 5.46    | 5.41    | 5.41    | 5.35    | 5.28    |
| 2 year swap                  | 3.82    | 3.91    | 3.87    | 3.85    | 3.75    | 3.80    |
| 5 year swap                  | 4.33    | 4.54    | 4.51    | 4.45    | 4.40    | 4.42    |
| RBNZ TWI                     | 66.0    | 67.6    | 67.2    | 67.5    | 66.8    | 67.0    |
| NZD/USD                      | 0.7081  | 0.7303  | 0.7290  | 0.7314  | 0.7249  | 0.7300  |
| NZD/AUD                      | 0.7866  | 0.7848  | 0.7809  | 0.7811  | 0.7748  | 0.7738  |
| NZD/JPY                      | 60.39   | 61.45   | 60.76   | 62.22   | 61.84   | 62.66   |
| NZD/GBP                      | 0.4520  | 0.4736  | 0.4732  | 0.4725  | 0.4645  | 0.4657  |
| NZD/EUR                      | 0.5514  | 0.5704  | 0.5658  | 0.5639  | 0.5580  | 0.5562  |
| AUD/USD                      | 0.9002  | 0.9306  | 0.9335  | 0.9364  | 0.9356  | 0.9434  |
| EUR/USD                      | 1.2842  | 1.2803  | 1.2885  | 1.2971  | 1.2992  | 1.3124  |
| USD/JPY                      | 85.29   | 84.15   | 83.35   | 85.07   | 85.31   | 85.84   |
| GBP/USD                      | 1.5666  | 1.5420  | 1.5407  | 1.5480  | 1.5607  | 1.5677  |
| Oil (US\$/bbl)               | 75.17   | 76.40   | 77.17   | 76.78   | 75.92   | 74.58   |
| Gold (US\$/oz)               | 1224.10 | 1245.58 | 1249.25 | 1268.95 | 1267.10 | 1279.35 |
| Electricity (Haywards)       | 3.36    | 0.27    | 0.56    | 0.90    | 2.08    | 0.97    |
| Milk futures (US\$/contract) | 116     | 120     | 120     | 119.5   | 119.5   | 119.5   |
| Baltic Dry Freight Index     | 2515    | 2976    | 2940    | 2840    | 2737    | 2676    |

# 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.
- ING (NZ) Holdings Limited (ING), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. ING and its related companies, including ING (NZ) Limited, 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.

### 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.

This document is provided for informational purposes only and does not constitute an offer to sell or solicitation to buy any security or other financial instrument. No part of this document can be reproduced, altered, transmitted to, copied to or

distributed to any other person without the prior express permission of the Bank.

This document is a necessarily brief and general summary of the subjects covered and does not constitute advice. You should obtain professional advice before acting on the basis of any opinions or information contained in it. The information contained in this document is given in good faith, has been derived from sources perceived by it to be reliable and accurate and the Bank shall not be obliged to update any such information after the date of this document. Neither the Bank nor any other person involved in the preparation of this document accepts any liability for any opinions or information (including the accuracy or completeness thereof) contained in it, or for any consequences flowing from its use.

### UNITED STATES DISCLAIMER

This document is being distributed in the United States by ANZ Securities, Inc. (Member of FINRA [www.finra.org] and registered with the SEC) ("ANZ S") (an affiliated company of Australia and New Zealand Banking Group Limited ("ANZBG") and the Bank), which accepts responsibility for its content. Further information on any securities referred to herein may be obtained from ANZ S upon request. Any US person(s) receiving this document and wishing to effect transactions in any fixed income securities referred to herein should contact ANZ S 277 Park Avenue, 31st Floor, New York, NY 10172 USA, Tel: 1-212-801-9160, Fax: 1-212-801-9163, not its affiliates.

This document is issued on the basis that it is only for the information of the particular person to whom it is provided. This document may not be reproduced, distributed or published by any recipient for any purpose. This document does not take into account your personal needs and financial circumstances. Under no circumstances is this document to be used or considered as an offer to sell, or a solicitation of an offer to buy.

In addition, from time to time ANZBG, the Bank, ANZ S, their affiliated companies, or their respective associates and employees may have an interest in any financial products (as defined by the Australian Corporations Act 2001), securities or other investments, directly or indirectly the subject of this document (and may receive commissions or other remuneration in relation to the sale of such financial products, securities or other investments), or may perform services for, or solicit business from, any company the subject of this document. If you have been referred to ANZBG, the Bank, ANZ S or their affiliated companies by any person, that person may receive a benefit in respect of any transactions effected on your behalf, details of which will be available upon request.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all of the securities and issuers referred to herein. The author however makes no representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. No part of the author's compensation was, is or will be directly or indirectly related to specific recommendations or views expressed in this document. ANZBG, the Bank, ANZ S, their affiliated companies, their respective directors, officers, and employees disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.