

# Business Weekly

## Holding Steady

### This Week

All eyes will be upon the RBNZ on Thursday morning. Widely-held expectations are that the Official Cash Rate will remain at 2.5%. Market pricing also implies only a small chance of a cut this week. We are in with the consensus for this week, but do still see a chance the RBNZ cuts the OCR later on.

In keeping the OCR steady at this week's meeting the RBNZ will be taking into account some encouraging signs. The global outlook is stabilising and local business confidence recovering. The housing market is staging a recovery, aided by fewer people leaving the country. Retail spending is stabilising. Continued buoyancy in the housing market and consumer spending might be one source of upward revisions for the RBNZ's economic outlook.

But not every development is leaning towards economic recovery. While the household sector is comparatively buoyant, the export sector remains under considerable pressure. The manufacturing and tourism industries have already experienced a large contraction in activity, struggling to cope with weak international demand. Dairy also remains a key area of vulnerability.

The strength in the NZ dollar continues to undermine the economic outlook, and we continue to see the case for further stimulus. However, the RBNZ is likely to stick to its assumption that the NZ dollar will weaken substantially, meaning it is not yet prepared to deliver further OCR cuts. It will continue to hold, and hope the exchange rate will depreciate and provide a much-needed boost to a flagging export sector. From a structural perspective a lower NZD would also aid in rebalancing the economy to a more sustainable mix by increasing exports' share of the economy and contributing to slower domestic spending.

While we have sympathy for the RBNZ holding out for a more palatable mix of monetary conditions, we remain wary on the NZ dollar outlook. We continue to expect the NZD to hold up, particularly against the soft USD, hence see less chance of sustained NZD weakness in an environment of a global economic recovery. If the NZD remains stubbornly high eventually the RBNZ may need to deliver rate cuts, to try and mitigate the impact of the higher NZ dollar. With markets also implying OCR increases as soon as early 2010 a further OCR cut would also serve to reinforce that the RBNZ will keep interest rates low for an extended period.

Right now would be a good tactical time to cut the OCR. However, for that to happen requires the RBNZ to: 1) the RBNZ to judge further stimulus is needed; 2) to accept that it has lost its ability to push short-term rates down further; 3) being cognisant that, notwithstanding (2), an OCR cut may still have some wider effect.

### Click here for:

[Foreign Exchange](#)

- NZD lifts against a weak USD, focus remains on US reporting season.

[Interest Rates](#)

- Market continues to focus on offshore developments.

[Week Ahead](#)

- Big data week, RBNZ the focus. Business Outlook, Trade figures, Consents.

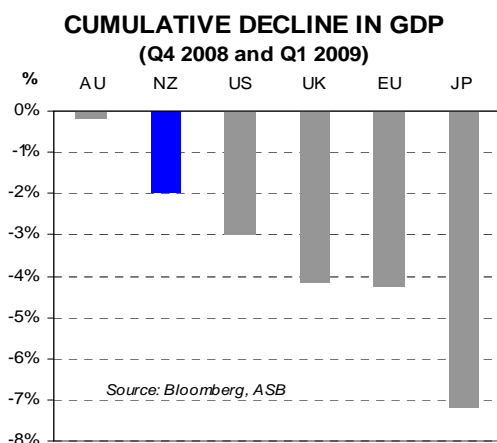
[Week in Review](#)

- Light data week. Annual net migration continues to pick up.

[Global Calendars](#)

- US company reports centre stage. US GDP due Friday. Beige Book Thursday.

### Chart of the week



- While New Zealand's external vulnerabilities remain a risk to the New Zealand dollar, risk appetites are improving and NZ's relative economic performance appears to have been a more influential driver of the NZD over recent months.
- NZ has performed comparatively well throughout the global economic recession. The 2% contraction in GDP over Q4 2008 and Q1 2009 is on the milder side compared to the UK and EU's 4% decline and Japan's 7% contraction.
- NZ's exports have remained reasonably resilient compared to our main trading partners: Japan's exports are down 35.7% on year-ago levels in June, and US exports down 21% on year-ago levels in May.
- Likewise, NZ's unemployment rate of 5% is low compared to the US rate of 9.5%, Eurozone's 9.5% and UK's 7.6%.

### General Advice Warning

As this report was prepared without taking into account your objectives, financial situation or particular needs, you should not take any action in reliance of this report without considering your particular circumstances and, if necessary, obtaining professional advice.

## Foreign Exchange Market

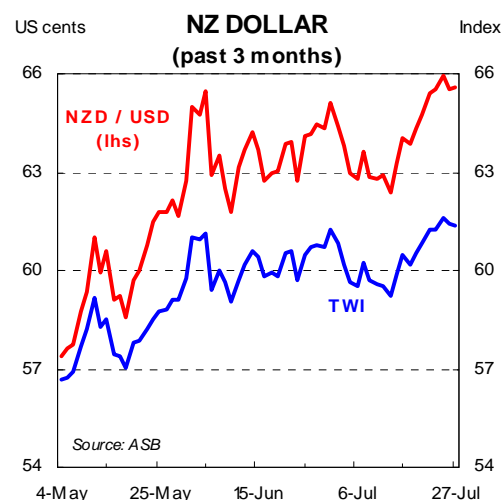
FX Rates	Current*	Week ago	Month ago	6 mths ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.6558	0.6474	0.6446	0.5281	0.7421	FLAT-UP	0.6450	0.6600
NZD/AUD	0.8030	0.8024	0.7986	0.8070	0.7740	FLAT	0.7950	0.8100
NZD/JPY	62.16	61.26	61.78	47.12	79.25	FLAT	60.00	63.00
NZD/EUR	0.4612	0.4573	0.4585	0.4081	0.4725	FLAT-UP	0.4550	0.4700
NZD/GBP	0.3991	0.3949	0.3927	0.3861	0.3736	FLAT-UP	0.3900	0.4050
TWI	61.4	60.9	60.8	53.4	66.2	FLAT-UP	59.50	62.00

^Weekly support and resistance levels \* Current is as at 12pm Monday; week ago as at Monday 5pm

- The NZD was flat against the AUD, but posted gains on the other crosses, including the USD last week. The main driver of the moves in FX is the ongoing improvement in risk appetite, and the USD and JPY have weakened with this backdrop.
- This week we find out whether the US economy continued to contract in the June quarter. Economists are expecting a small contraction in the economy though we think the rate of contraction risks being larger. Only 175 of the top 500 US companies have reported their earnings to date, so trends in US equity markets are likely to remain a major influence on currency markets. If the recent trend of earnings out-performing expectations continues this week the USD is likely to continue easing as US investors put money in offshore equity markets. A "left field" influence on the currency markets this week is a series of meetings between the Treasury & State Secretaries Geithner and Clinton with their counterparts from China. Comments of concern from the Chinese side about the large US budget deficit and/or the need to diversify away from US assets would push the USD lower across the board but the likelihood is more diplomatic dialogue.
- The NZD is sitting significantly above the much tested support level at 0.625. Further good news from the equity markets is a likely catalyst for the NZD to press higher. The US reporting season remains the focus for the FX market, and the RBNZ meeting this week is the significant local focus. Uridashi maturities are strong over the next month. Both AUD/JPY and NZD/JPY may come under intra-day pressure from net negative issuance.

### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
June Trade Balance	28/7	10.45 am	+\$260m
June Building Consents	29/7	10.45 am	-
NBNZ Business Outlook	29/7	3.00 pm	-
RBNZ OCR Review	30/7	9.00 am	2.5%
June Credit Aggregates	30/7	3.00 pm	-



**Potential currency movers from the US this week:** house sales (27th), house prices, consumer confidence (28th), Federal Reserve's Beige book, durable goods orders (29th), jobless claims (30th), economic growth (31st). Speakers: Geithner and Clinton meet Chinese officials (27th-28th), Bernanke (27th-29th), Yellen (27th), Dudley (29th).

### Medium term outlook: [\[Last Quarterly Economic Forecasts\]](#)

- As a consequence of the financial market turmoil centred in the United States, USD weakness was expected in early 2009. Although this weakness was initially offset in part by concerns about other regions, improved sentiment in financial markets has seen risk appetites improve and the USD weaken. Right now, the USD, which had shown countercyclical strength, is under pressure. The USD is weakening for the following reasons:
  - US residents increase their offshore investment, encouraged by improvement in the global economy.
  - USD liquidity demand and safe-haven buying of the USD reverses is easing.
  - Diversification out of USD is expected to occur due to concerns about US government debt.
- The arguments for buying EUR, GBP and JPY are strong enough to engineer a reasonable depreciation in the USD, but we do not expect to revisit fresh US TWI lows.
- We are also comfortable with our current forecast that the NZD and AUD have bottomed and will appreciate over the course of 2009, rather than revisit and break through the lows seen in early 2009. However, Fitch has put the threat of a credit rating downgrade back on the table. We expect the NZD to firm noticeably against the USD and yen as those currencies remain under sustained pressure. Against other key currencies the NZD is likely to appreciate but to a more modest extent: the NZD will leverage off the global recovery and NZ is in a relatively good position compared to a number of economies. The likelihood of the RBNZ intervening to try and weaken the NZD remains very low.

## Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	2.50	2.50	2.50	5.00	8.00	FLAT
90-day bank bill	2.74	2.79	2.81	4.14	8.29	FLAT
2-year swap	3.97	3.92	3.88	3.49	7.42	FLAT
5-year swap	5.39	5.40	5.42	3.98	7.22	FLAT
11/11 gov't stock	4.77	4.74	4.87	3.71	6.13	FLAT
NZSX 50	2973	2818	2768	2708	3257	FLAT

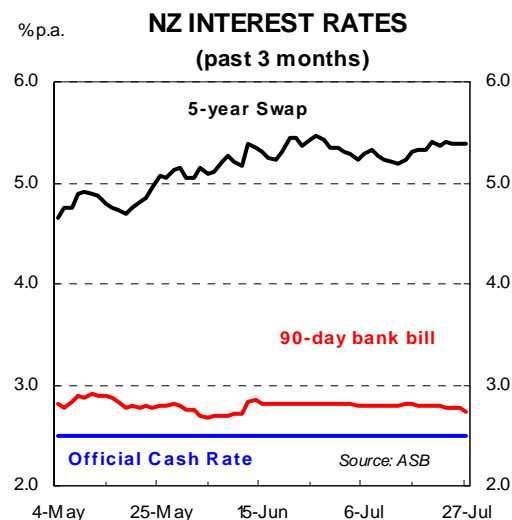
\* Current is as at 12pm Monday; week ago as at Monday 5pm

- The weekly NZ bond tender of \$400 (slightly larger than usual) received strong interest, partly supported by the recent maturity of the July 2009 bond. NZ markets continue to be mostly driven by offshore developments, with the rise in yields driven by the pick up in interest rates across the Tasman. US markets were more mixed with US bonds staging a strong rally (pushing yields lower) on the back of dovish comments by Bernanke.
- We expect the RBNZ to keep the OCR on hold at 2.5% at the July OCR review (Thursday 30<sup>th</sup> July). We expect no change in tone, with the RBNZ continuing to emphasise its easing bias and expectations to hold rates at or below current levels until the latter part of 2010. The RBNZ may be frustrated by the strength in the NZD and market pricing for rate hikes earlier than the RBNZ has signalled. With the economic outlook still fragile, we continue to see scope for further rate cuts, possibly in September and October.

### Short-term outlook:

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**Comment:** The RBNZ OCR Announcement is the focus of the week. The RBNZ is widely expected to keep rates on hold, with the devil in the detail as the one page statement is closely scrutinised. The expectation of a dovish tone will weigh on NZ interest rates, offsetting the upward influence coming from Australian markets.



### Medium term outlook: [\[Last Quarterly Economic Forecasts\]](#)

- The RBNZ left the cash rate unchanged at 2.5% at the June OCR announcement. The RBNZ has cut the cash rate 575 basis points in less than a year in response to the financial crisis offshore. The RBNZ has previously expressed reluctance to cut the OCR below 2%, which leaves just 50 bp of rate cuts up its sleeve.
- The RBNZ's June statement was dovish, playing down green shoots optimism and highlighting the downside risks to the economic outlook. The RBNZ maintained an explicit easing bias, mentioning the potential for the OCR to move lower and restated it continues to expect to hold the OCR at current levels until the latter part of 2010.
- The RBNZ revised down its growth outlook in June, and as a result inflation pressures are considerably weaker. The RBNZ forecasts CPI inflation to briefly fall through the bottom of the target band later this year, then recover to remain 'comfortably' in the middle of the target band.
- The RBNZ's export-led recovery is heavily dependent on the trade-weighted exchange rate remaining below average for an extended period. In our view, the RBNZ's exchange rate assumption is reasonably heroic, and differs from our own view of US dollar weakness remaining a dominant driver of the NZ dollar. The assumption leaves the RBNZ vulnerable to the risk inflation falls uncomfortably low. There remains downside risk to the RBNZ's economic outlook, and the RBNZ is likely to want to deliver further monetary policy stimulus.
- The market has underestimated the RBNZ's willingness to cut further, with market pricing implying the easing cycle is over – and that the OCR will increase as early as the start of 2010. The RBNZ is disappointed with this reaction. The longer that interest rates and the NZ dollar remain above the RBNZ's assumptions, the more pressure the RBNZ will feel for further cuts to remind the markets of its position. We have pencilled in two 25 basis point cuts for September and October, although the timing of these are partly dependent on the NZ dollar.
- The OCR remains the RBNZ's primary tool, although it has started to lose traction at very low levels. While the RBNZ has investigated other options, it remains very reluctant to use them while there is potential to cut the OCR further.

## NZ Data Preview: a look at the week ahead

Data	Date	Time (NZST)	Previous	Market expects	ASB expects
June Trade Balance	28/7	10.45 am	+\$858 m	+\$260	-\$50 m
June Building Consents	29/7	10.45 am	+3.5%	-	-6%
NBNZ Business Outlook	29/7	3.00 pm	+5.5	-	-
RBNZ OCR Announcement	30/7	9.00 am	2.5%	2.5%	2.5%
RBNZ Credit Aggregates	30/7	3 pm	+0.4%	-	-

### Tuesday 28<sup>th</sup> July

#### June Trade balance

**Previous: +\$858 Mn ASB -\$50 Mn**

We expect a trade deficit in June of \$50 million. May recorded the 4th consecutive surplus, but we expect the run to come to an end as imports stabilise and exports weaken.

Exports are likely to fall in June, reflecting the agricultural cycle. Exports have been tempered by falling dairy prices and lower slaughter volumes, and this will also be a feature in June figures. Meanwhile the underlying import trend remains weak, but may start to stabilise over the next few months. There is a risk that capital and intermediate goods imports are weaker than our forecasts. A weak expectation (relative to our forecast) on the import side of the equation is behind the market expectation of a trade surplus in June (compared with our deficit forecast). Weak domestic demand has seen import volumes fall dramatically compared to year-ago levels, compounded by falling oil prices. The recent pick up in the NZ dollar should help contain further price increases on imports. We are close to a turning point in monthly trade data, as exports slip into their seasonally weak months the extent of underlying weakness for export demand will become more apparent.

### Wednesday 29<sup>th</sup> July

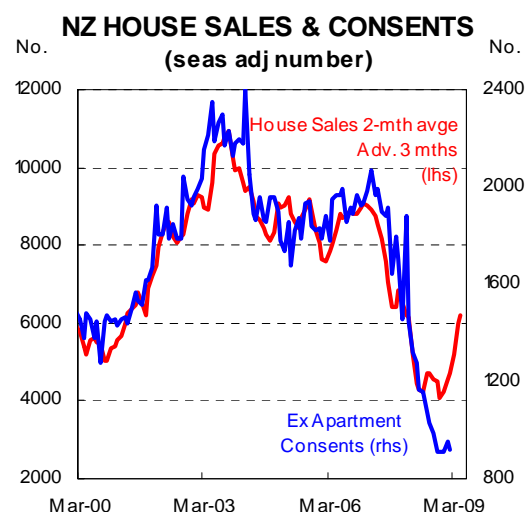
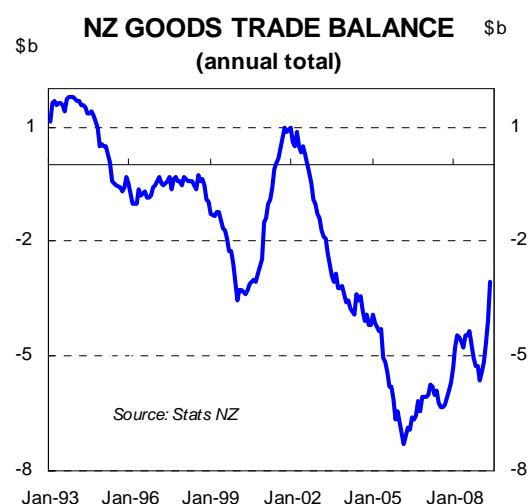
#### June Building Consents

**Previous: +3.5% mom ASB f/c -6%**

Residential building consents lifted over April and May, with a recovery in both apartment and core consents off the lows recorded earlier in 2009. Consent issuance is likely to have reached a bottom. Low interest rates and a turnaround in net migration have lifted underlying housing demand. The recent pick up in housing turnover also points to a recovery in construction demand, and consent issuance.

Apartment consent issuance tends to be lumpy, and following a surge in issuance over April and May some correction is possible during June. A fall in apartment consent issuance is likely to dampen the increase in overall consents.

Non-residential consent issuance surged in April due to the Christchurch International Airport development, and subsequently fell over May. Further falls are possible in June, but the value of Non-residential consent is expected to remain up on year-ago levels.



**Wednesday 29<sup>th</sup> July**

**July NBNZ Business Confidence**

Business optimists outnumbered pessimists for the first time since September 2008 over the past two National Bank Business Outlook Surveys. Both the overall outlook and own activity indicators within the survey have moved into positive territory. In June a net 6% expected general business conditions to improve over the next 12 months, and firms' expectations of their own activity is back in positive territory with a net 8% of firms expecting better times ahead. The improvement in own activity expectations signals a likely return to weak growth in the second half of 2009.

However, profit, investment and employment intentions all remain negative, and below Asian crisis levels. Pricing intentions remain weak, and point to lower inflation in the year ahead. This survey can be volatile from month to month, but overall we do not expect further lifts in confidence, given the pressure many businesses are under.

**Thursday 30 July**

**RBNZ OCR Announcement**

**ASB f/c: 2.5% - no change**

We expect the RBNZ will keep the cash rate on hold in July. Global markets have become more confident with signs of economic activity stabilising. There have also been positive signs at home, with a recovery in the housing market and business confidence returning to neutral levels.

The RBNZ is concerned by the lift in the NZ dollar and longer-term interest rates. However, the drivers for the movements have come from offshore and domestic monetary policy currently has little influence on these markets.

To date the RBNZ has cut 5.75 percentage points off the OCR in a relatively short period of time, and is not prepared to cut below 2%. Now, as was the case in June, is a good time to pause and assess the effectiveness of rate cuts to date, as right now further OCR cuts may achieve little.

Nonetheless, the risks to the inflation outlook remain to the downside and we expect the RBNZ will have to deliver some form of stimulus in the future. For that reason we still envisage an OCR of 2.0%. Ongoing NZD strength would be the main reason for future action.

**Thursday 30 July**

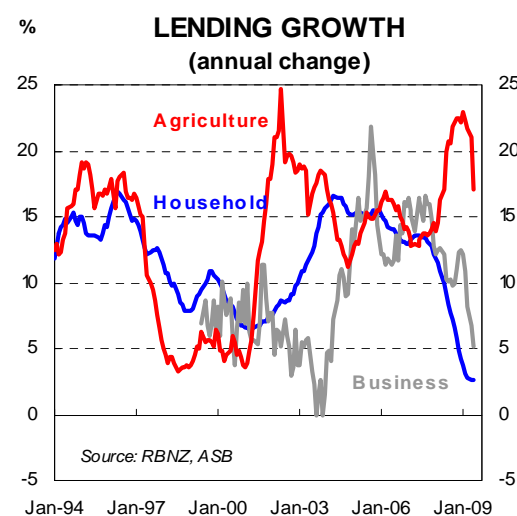
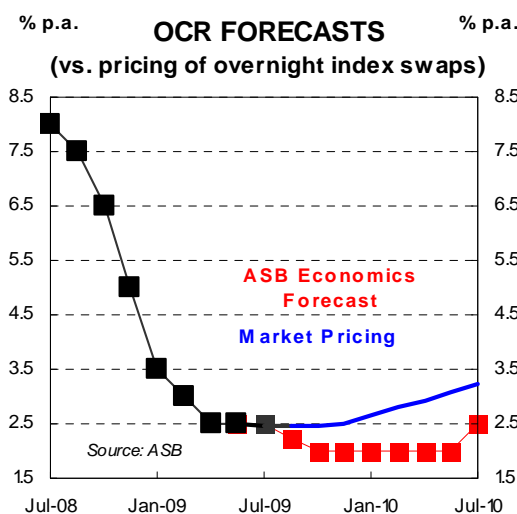
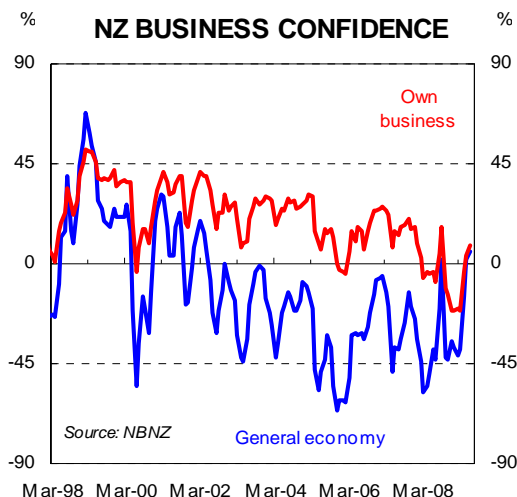
**June Credit Aggregates**

**Previous: Household Lending +0.4% s.a. mom**

Mortgage lending had another relatively robust month in May, with net lending up \$801mn. Ongoing strength in house sales over June suggests that lending growth is likely to remain firm. In contrast, consumer lending continued to contract slightly on an annual basis, and weakness in retail sales of durable goods suggests these declines are likely to continue. Growth in household lending is likely to remain muted as households focus more on saving.

Business lending growth has started to slow more noticeably in recent months and moderation in growth is likely to continue. Customer demand is weak, profits are under pressure, and capital investment is consequently being pared back.

Agricultural lending growth remains surprisingly resilient. However, growth is slowing sharply, and this is likely to continue. In particular, the low dairy payout for the upcoming season reinforces that on-farm investment is likely to be muted.



## NZ Data Review: weekly recap

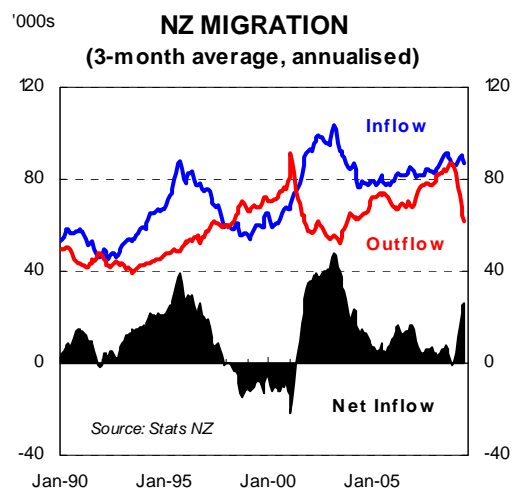
### June International Travel and Migration

Net migration posted another robust month, with 1,740 net new migrants recorded over June (although slightly weaker than the 2000 plus figures recorded in April and May). June's arrivals lifted annual net migration to 12,515 (from 11,200 previously).

Over the past few months the pick up in net migration has come on the back of fewer departures, in particular to Australia and the UK. The decline appears to have stabilised slightly in June, with the number of departures lifting slightly - up 2.4% from May.

Arrivals have remained fairly steady over the past few months. However arrivals fell sharply in June - down almost 10%. The fall appears to be relatively broad based across regions, with seasonally-adjusted arrivals falling from Europe, India, the Americas, Africa and United Arab Emirates.

Short-term overseas arrivals fell 3.8%, with the impact of swine flu starting to become more prevalent on travel plans. Arrivals from Asia (Japan and China in particular) fell sharply over June (on a seasonally-adjusted basis). Arrivals from Australia remain firm, offsetting the trend declines in tourist numbers from long-haul visitors.



## Global Data Calendars

Note: Calendar 2 is in UK times. Add 11 hours for NZ times.

### Calendar – Australasia, Japan and China

Date	Time		Econ Event	Period	Unit	Last	Forecast	
	NZT						Market	ASB/CBA
Mon 27 Jul	11.50	JP	Corp service price	Jun	%	-3.0	~	~
Tue 28 Jul	10.45	NZ	Trade balance	Jun	\$mn	858.0	207.5	-50
	10.45	NZ	Imports	Jun	\$bn	3.1	3.2	3.36
	10.45	NZ	Exports	Jun	\$bn	4.0	3.4	3.31
	10.45	NZ	Balance	Jun	YTD	-3,044	-2,621	-2,879
	12.00	AU	CB leading index	May	%	0.7	~	~
	13.30	AU	NAB business confidence	QII	Index	-24.0	~	~
	15.00	AU	Reserve Bank Governor Stevens Speech					
Wed 29 Jul	10.45	NZ	Building permits	Jun	m%ch	3.5	-5.0	-6.0
	11.50	JP	Large retailers' sales	Jun	%	-6.5	~	~
	11.50	JP	Retail trade	Jun	m%ch y%ch	0.1 -2.7	~ -2.4	~ ~
	15.00	NZ	NBNZ business confidence	Jul	Index	5.5	~	~
	17.00	JP	Small business confidence	Jul	Index	38.0	~	~
Thu 30 Jul	9.00	NZ	RBNZ official cash rate	Jul	%	2.5	2.5	2.5
	11.50	JP	Industrial production	Jun	m%ch y%ch	5.7 -29.5	2.3 -23.5	~ ~
	13.00	AU	HIA new home sales	Jun	m%ch	-5.7	~	~
	13.30	AU	Building approvals	Jul	m%ch y%ch	-12.5 -22.4	8.0 -18.2	11.5 -14.7
	16.00	JP	Vehicle production	Jun	y%ch	-41.4	~	~
	Fri 31 Jul	11.30	JP	Household spending	Jun	%	0.3	0.1
11.30		JP	Jobless rate	Jun	%	5.2	5.3	~
11.30		JP	National CPI	Jul	y%ch	-1.1	-1.8	~
11.30		JP	National CPI ex food, energy	Jul	y%ch	-0.5	~	~
17.00		JP	Housing starts	Jun	y%ch	-30.8	-30	~
17.00		JP	Annualised housing starts	Jun	¥mn	0.8	0.8	~
17.00		JP	Construction orders	Jun	y%ch	-41.9	~	~
12.30		AU	TD securities inflation	Jun	m%ch y%ch	0.4 1.4	~ ~	~ ~
13.30		AU	Private sector credit	Jun	m%ch y%ch	-0.1 3.9	0.1 3.4	0.1 3.3

## Calendar – North America & Europe

Please note all days and times are UK time, not local release day/times

Date	UK		Period	Unit	Last	Forecast	
	time	Econ Event				Market	CBA
Mon 27 Jul	07.10	GE GfK consumer confidence	Aug	Index	2.9	~	~
	15.00	US New home sales	Jun	%	-0.6	3.5	~
	15.30	US Dallas Fed manufacturing	Jun	%	-20.4	-12.0	~
Tue 28 Jul	11.00	UK CBI July distributive trades					
	14.00	US S&P/CS composite-20	May	y%ch	-18.1	-17.9	~
	15.00	US Consumer confidence	Jul	Index	49.3	48.0	~
	15.00	US Richmond Fed manufacturing	Jul	Index	6.0	8.0	~
Wed 29 Jul	~	GE CPI	Jul	m%ch	0.4	~	~
	09.30	UK Net consumer credit	Jun	£bn	0.3	~	~
	10.00	EZ Business climate indicator	Jul	-3.0	~	~	~
	13.30	US Durable goods orders	Jun	%	1.8	-0.5	~
	13.30	US Durable ex transportation	Jun	%	1.1	-0.1	~
	19.00	US Fed's Beige book					
Thu 30 Jul	08.05	GE Retail sales	Jun	m%ch	-1.3	~	~
	08.55	GE Unemployment rate	Jul	%	8.3	~	~
	10.00	EZ Consumer confidence	Jul	Index	-25.0	~	~
	10.00	EZ Industrial confidence	Jul	Index	-32.0	~	~
	10.00	EZ Services confidence	Jul	Index	-20.0	~	~
	13.30	CA Industrial product price	Jun	m%ch	-1.1	~	~
	13.30	CA GDP	May	m%ch	-0.1	~	~
	13.30	US Initial jobless and continuing claims					
Fri 31 Jul	00.01	UK GfK consumer confidence	Jul	Index	-25.0	~	~
	10.00	EZ CPI estimate	Jul	%	-0.1	~	~
	10.00	EZ Unemployment rate	Jun	%	9.5	~	~
	13.30	US GDP (annualised)	QII	%	-5.5	-1.5	~
	13.30	US Core PCE	QII	q%ch	1.6	2.4	~
	14.45	US Chicago purchasing manager	Jul	Index	39.9	42.0	~
	15.00	US NAPM-Milwaukee	Jul	Index	50.0	~	~

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