

# Business Weekly

## Businesses feeling the pinch

### This Week

The latest NZIER Quarterly Survey of Business Opinion confirmed that businesses continued to feel the blues in the September quarter, with both headline confidence and businesses' assessment of their own conditions again declining. In isolation, the results point to another quarter of subdued economic activity in Q3, which is concerning in light of the much weaker than expected Q2 GDP result released recently.

This pessimism amongst businesses appears to be fuelled by weak profitability, as businesses find it increasingly difficult to pass on rising costs. A smaller proportion of businesses have indicated they intend to raise prices, despite an increase in the proportion of businesses expecting higher costs in the months ahead. With GST increased from 12.5% to 15% on the 1 October, this suggests businesses were feeling less confident they could pass on this tax increase in the form of higher prices.

Despite weak profitability, businesses' intentions to hire and invest in plant and machinery are holding up at average levels. The fact that the level of both intentions measures point to a continued recovery in both employment and business investment over the coming year is encouraging as it indicates businesses still believe demand will recover enough to warrant investing in an expansion of operations. The risk lies in further declines in profitability derailing these expansion plans in the coming months.

In contrast, Australia once again showed why it is called "the lucky country", with another robust increase in employment. The 49,500 increase in September was much higher than market expectations of a 20,000 increase. All the more positive for the Australian economy was the fact that the result was driven entirely by a surge in full-time jobs. The Australian unemployment rate remained at a low 5.1%, which many believe to be close to the natural rate of unemployment. Overall, the results point to inflation risks ahead in Australia.

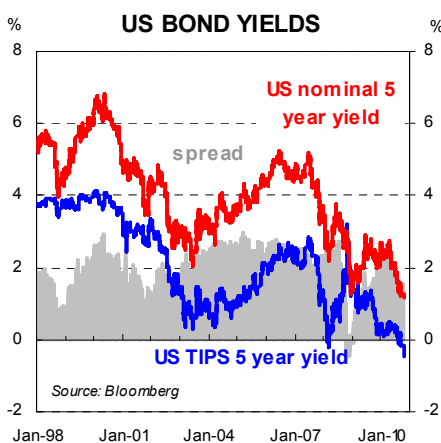
The continued strength in the Australian economy is continuing to underpin the currency's ascent, with the Australian dollar inching closer to parity with the US dollar. The surge in the currency is likely to have been one reason behind the RBA's shock decision last Tuesday to leave its cash rate on hold. Nonetheless, the RBA clearly indicated the tightening cycle was not over yet: "it is likely that higher interest rates will be required, at some point, to ensure that inflation remains consistent with the medium-term target." However, the shock of the on-hold decision have seen markets reluctant to price in a substantial probability of a rate increase from the RBA over the remainder of 2010, despite the strength in the data.

Meanwhile, speculation over the potential for further quantitative easing from the US Federal Reserve continues. Markets will be poring over the FOMC minutes on Wednesday morning for clues as to the likelihood of the Fed increasing stimulus to the US economy.

### Click here for:

- [Foreign Exchange](#) • NZD/USD continues to appreciated on USD weakness; AUD closer to parity.
- [Interest Rates](#) • Domestic interest rates dragged higher by strong Australian activity.
- [Week Ahead](#) • REINZ House Sales and Retail Sales.
- [Week in Review](#) • NZIER Quarterly Survey of Business Opinion shows increased pessimism.
- [Global Calendars](#) • FOMC minutes, US CPI, Retail Sales and Empire Manufacturing.

### Chart of the week



- The spread between the nominal bond yield and the yield on Treasury Inflation Protected Securities (TIPS) can often provide an indication of inflation expectations in the market.
- Over the past few weeks, the yield on the 5-year US TIPS has turned negative.
- This negative yield is partly a reflection of weak activity currently in the US economy, which puts downward pressure on bond yields in general.
- However, the negative TIPS yield also suggests that markets expect inflation to be positive over the coming years despite current weak activity. Underpinning this result is likely to be continued expectations that the US Fed will expand its quantitative easing programme soon.

### 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 <sup>^</sup>	Resistance <sup>^</sup>
NZD/USD	0.7566	0.7423	0.7247	0.7163	0.7393	UP	0.7450	0.7650
NZD/AUD	0.7654	0.7656	0.7855	0.7668	0.8176	DOWN	0.7550	0.7700
NZD/JPY	61.99	61.99	60.84	66.66	65.93	FLAT	61.00	63.00
NZD/EUR	0.5411	0.5393	0.5713	0.5235	0.5019	FLAT	0.5350	0.5450
NZD/GBP	0.4746	0.4695	0.4702	0.4626	0.4613	FLAT	0.4680	0.4780
TWI	67.0	66.6	67.4	66.0	66.6	FLAT	66.00	68.00

<sup>^</sup>Weekly support and resistance levels \* Current is as at 10.20 am Monday; week ago as at Monday 5pm

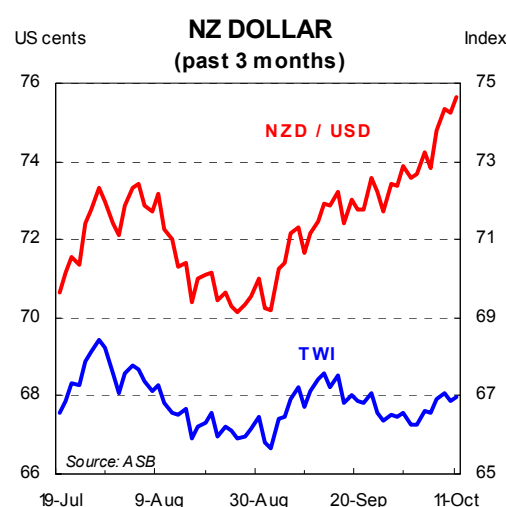
- The NZD ended the past week over a cent higher against the USD at around USD0.756, though it was roughly flat against the other major currencies. Weak NZ data pulled the NZD down slightly but offshore events have propelled it higher.
- The weak details of the NZIER business survey on Tuesday nudged the NZD down around 40 points to USD0.7380. However, the RBA's surprise on-hold decision knocked the AUD down sharply and saw the NZD/AUD back up above AUD0.77. Thursday's strong Australian employment figures put a rocket under the AUD and it briefly touched above USD0.99, contributing to further strength in the NZD. AUD parity with the USD is a realistic possibility, and our forecasts expect it by the end of March.
- In the background, Fed officials' comments and weak employment data have fuelled speculation that further quantitative easing will occur, prompting additional USD weakness.
- It will be worthwhile keeping an eye on the yen this week. With USD/JPY now trading below 82, the implicit line in the sand for the Bank of Japan, a further attempt to weaken the yen (push USD/JPY up) is entirely possible. The added strength in the yen in the past day's trading comes despite the added asset purchases the BoJ announced last week to combat deflation.

### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
REINZ housing – Sept	14/10	10.00am	-
Retail Sales, Aug, mom ex-auto	14/10	10.45am	0.2%

**Potential currency movers from the offshore this week:** UK CPI (12<sup>th</sup>); FOMC minutes, AU consumer confidence, Japan machine orders, China trade balance, UK industrial production, unemployment rate, US import price index, monthly Budget statement (13<sup>th</sup>); AU consumer inflation expectations, US initial jobless claims, import price index, trade balance (14<sup>th</sup>); Japan industrial production, EU CPI, trade balance, US CPI, retail sales, University of Michigan Confidence, Empire manufacturing, business inventories (15<sup>th</sup>).

**Fed speeches:** Yellen (11<sup>th</sup>); Bernanke (15<sup>th</sup>)



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

- We updated our currency forecasts in late September: the NZD forecasts have been lifted slightly. The near-term lift is driven by rising New Zealand Terms of Trade and USD weakness, rather than the New Zealand economy's domestic strength.
- Currency volatility remains low and is trending lower. Reflecting this lower volatility, episodes of risk aversion are likely to be smaller and less frequent in the future. When volatility is low, relative economic health becomes a major driver of exchange rates. With this in mind, we have revised up our forecasts for the AUD and CAD as well as the NZD forecasts. These economies continue to benefit from strong Terms of Trade and upward pressure on local interest rate settings. AUD in particular is likely to out-perform over the coming months.
- We anticipate that the USD will decline further over the next six months, as the Fed continues with its commitment to keep rates at extremely low levels for an extended period of time. If the Fed implements more quantitative easing before year-end, the USD will further decline.
- GBP is forecast to out-perform EUR, reflecting a more rapidly improving UK economy and a healthier banking system. We are holding to our medium-term view that the EUR is likely to exhibit a mild bias to depreciate as selected Eurozone sovereign states continue to experience funding pressures and the European Central Bank (ECB) extends "unlimited liquidity" to Eurozone banks.
- JPY, CHF and SGD are likely to continue to appreciate in the coming months as market participants gravitate toward the "safety" of current account surplus country's currencies.

## Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	3.00	3.00	3.00	2.50	2.50	FLAT
90-day bank bill	3.18	3.17	3.19	2.67	2.77	FLAT
2-year swap	3.80	3.76	3.92	4.32	4.37	FLAT
5-year swap	4.37	4.32	4.53	5.28	5.44	FLAT/UP
5-year benchmark gov't stock	4.39	4.34	4.72	5.24	4.93	FLAT/UP
NZSX 50	3233	3229	3161	3314	3164	FLAT

\* Current is as at 11.00 am Monday; week ago as at Monday 5pm. Please note that we have recently changed the NZ gov't 5-year benchmark bond to April 2015 maturity (from April 2013). This does cause some distortion in the comparison against the previous levels (i.e.6 months ago).

- The NZ curve finished roughly 5bp higher over the week despite the weak detail in the NZIER survey, the only domestic release of last week.
- The Australian market got whipsawed over the week. The RBA kept rates on hold at its Tuesday policy announcement, against the majority expectation for a rate hike, triggering a sharp drop in the Australian curve. On Thursday, however, the large lift in September employment (+49.5k vs. 20k expected) gave a sharp reminder of the underlying strength of the Australian economy. Australian rates partly reversed Tuesday's drop.
- US interest rates have ground down further as weak data fuelled speculation of additional quantitative easing measures from the Fed. Friday night's Non-farm Payrolls drop of 95k was substantially weaker than expected, even though the drop was driven by public, rather than private, sector jobs.

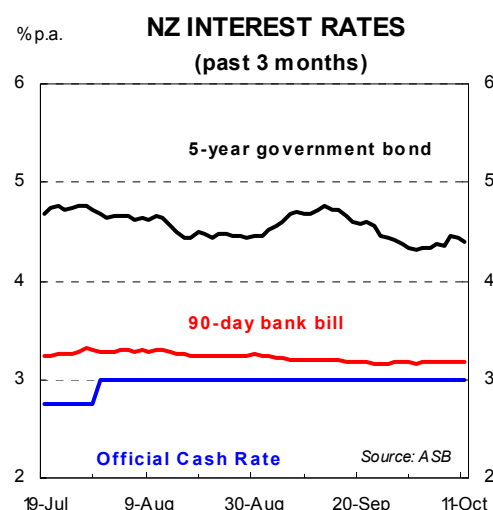
### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
REINZ housing – Sept	14/10	10.00am	-
Retail Sales, Aug, mom ex-auto	14/10	10.45am	0.2%

**Comment:** September REINZ House Sales and August Retail Sales data on Thursday are the focus for domestic markets this week. We expect housing market activity to remain subdued in the September month. Meanwhile, retail sales should show continued improvement, albeit at a gradual pace.

Food prices for the September month will be the final result for the food group for Q3 CPI.

FOMC minutes on Wednesday will be of much interest given the continued speculation surrounding the Fed's likely expansion of its quantitative easing programme. A slew of US data is released towards the end of the week, including CPI, retail sales, University of Michigan Confidence, Empire Manufacturing and Inventories.



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

- The RBNZ kept the OCR unchanged at 3% at the September Monetary Policy Statement. The RBNZ had lifted the OCR in June and July. However, with recent data proving weaker than expected, fears the global economy may be losing some momentum and added uncertainty created by the Canterbury Earthquake, we expect the RBNZ to remain on hold until early next year.
- The RBNZ slashed its growth forecasts in its September Monetary Policy Statement. The RBNZ undertook a major rethink on the household sector outlook. Noting the weakening fundamentals for the housing market and weak appetite for credit, the RBNZ substantially scaled back forecasts for household spending and investment.
- The RBNZ also slashed its projection for the 90-day interest rate, reflecting its weaker outlook for the domestic economy as well as placing more emphasis on higher bank funding costs. The RBNZ now has an implicit assessment of neutral closer to our own, although we expect that the RBNZ will get there more quickly than the 2.5 years implied by its MPS forecasts.
- The RBNZ has also revised its inflation forecast lower. However, we believe the RBNZ is being optimistic in assuming medium-term inflation expectations will remain subdued in face of a spike in headline CPI over the coming year.
- We now expect the RBNZ will wait until March to resume lifting the OCR. That gives another 6 months to allow the economy to strengthen and better assess the earthquake disruption. Between now and then two CPI and two inflation expectations results will be released. On both fronts we expect the RBNZ to become less sanguine about its low medium-term inflation outlook. Market pricing of a 3.8% OCR peak by mid-2012 still looks too light, but in the immediate future there appears no catalyst to change that expectation.

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

Data	Date	Time (NZT)	Previous	Market expects	ASB expects
REINZ House Sales – Sept (year-on-year turnover)	14/10	10.00am	-27%	-	-
Retail Sales, Aug, mom ex-auto	14/10	10.45am	-0.1%	0.2%	0.3%

### Thursday 14 October

#### REINZ House Sales, Sep, y%ch, (-27% prev)

We expect house prices nationwide to soften, and post small year-on-year declines of around 2%. However, behind the nationwide decline we expect a range of experiences, from modest price gains in cities where the market remains tight, through to annual declines in areas where the property fundamentals remain weak. Recent QVNZ regional price data are consistent with this view. QV residential property indices for September show values are gradually declining, and are 5.3% below the 2007 market peak. Between September 2009 and March 2010 values lifted, but have subsequently eased back again, dropping 1.4%.

Data from agent Barfoot & Thompson showed Auckland turnover was down a seasonally-adjusted 2.8% in September. This would typically imply another low level of turnover in the nationwide REINZ figures. Our indicator suggests seasonally-adjusted REINZ turnover of around 4700 properties. However, September REINZ sales figures will likely be significantly impacted by the Canterbury earthquake, and we expect an even lower level of turnover in the REINZ nationwide figures.

### Thursday 14 October

#### Retail Sales, Aug, m%ch, (f) 0.4 total, 0.3 ex-auto

Retail sales have generally been recovering in recent months, albeit at a gradual pace. We expect this to continue in August. Anecdotes suggest the bringing forward of major household purchases in the months leading up to the GST increase on 1 October was muted.

Consumer confidence has weakened in recent months, and this is likely to be weighing on retail spending. We expect an improvement in the labour market and thus wage growth would boost consumer confidence over the coming year and this is expected to underpin a pick up in retail sales.

Recent business surveys indicate this optimism amongst retailers. Despite continued weakness in experienced sales and profitability, retailers remain hopeful that sales will improve in the coming months.

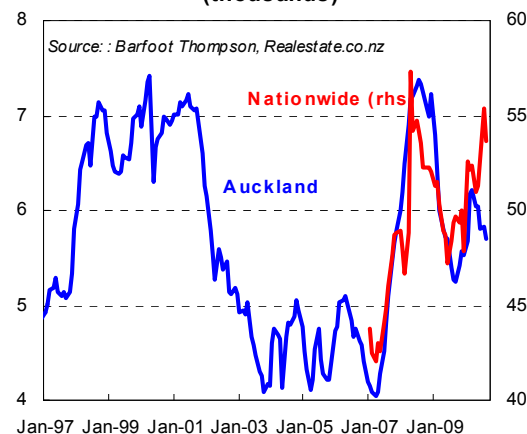
### Monday 18 October

#### Q3 Consumer Price Index, q%ch (f) +1.2%, y%ch (f) +1.7%

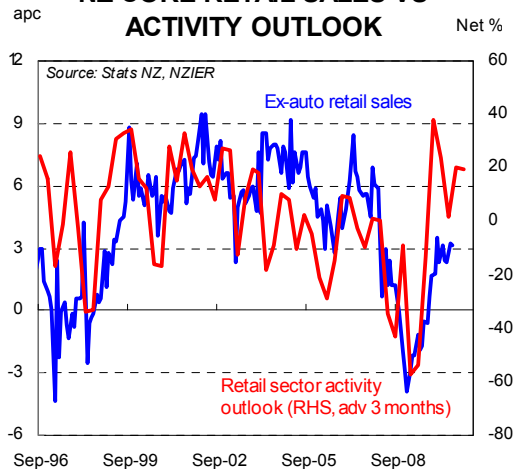
We expect a 1.2% increase in the CPI in the September quarter, thus bringing annual inflation to 1.7%. Behind the modestly high increase for the quarter will be a host of government charges. We estimate the effects of ACC levies, tobacco excise taxes and Emissions Trading Scheme will boost CPI by around 0.3%.

Further Government charges, including the increase in GST to 15% at the beginning of October, means that annual headline CPI is expected to peak at over 5% by mid-2011. While the Policy Targets Agreement allows the RBNZ to look through the first round effects of major Government policy changes, such a high headline CPI runs the risk of the effects spilling over to generalised inflation. We expect the RBNZ will become less sanguine about inflation pressures in the NZ economy over the coming year.

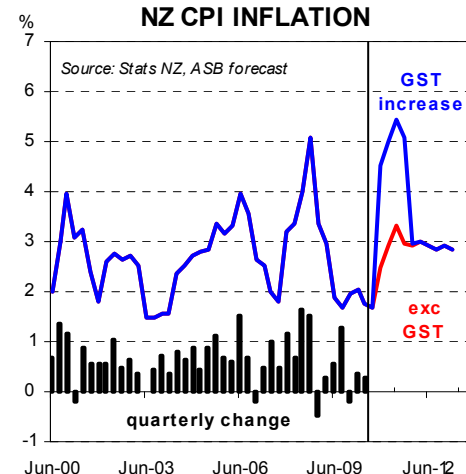
#### TOTAL HOUSING INVENTORY (thousands)



#### NZ CORE RETAIL SALES VS ACTIVITY OUTLOOK



#### NZ CPI INFLATION



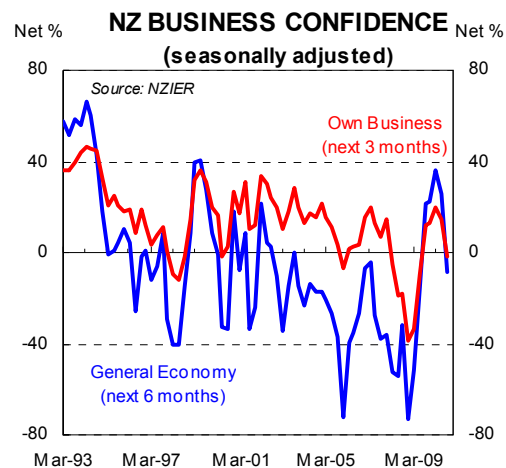
## NZ Data Review: weekly recap

### NZ NZIER Business Opinion Survey, QIII

- Headline business confidence: -8.9, prev 26.2
- Own trading activity: -2.0, prev 14.7

Business confidence fell once again, as weak profitability fuelled pessimism amongst firms. It appears firms are finding it difficult to pass on rising costs, with a smaller proportion of businesses indicating they intend to raise prices despite the increasing proportion of businesses facing higher costs.

Despite weak profitability, businesses' intentions to hire and invest in plant and machinery are holding up. This is encouraging as it indicates businesses still generally feel confident enough about the recovery in demand to invest in expansion of operations. While the decline in headline business confidence was broad-based, the pessimism was particularly acute in the building and retail sectors. We expect reconstruction activity following the Canterbury earthquake will boost the building sector over the coming year.



## Global Data Calendars

Note: Calendar 2 is in UK times. Add 12 hours for NZ times.

### Calendar - Australasia, Japan and China

Date	Time		Event	Period	Unit	Last	Forecast	
	NZT	Econ					Market	ASB/CBA
Mon 11 Oct	13.30	AU	Housing Finance – value of new loan approvals	Sep	m%ch	2.3	1.0	1.0
	13.30	AU	Housing Finance – no. of own-occ loan approvals	Sep	m%ch	1.7	~	2.0
Tue 12 Oct	13.30	AU	NAB business conditions	Sep	Index	5.0	~	~
	13.30	AU	NAB business confidence	Sep	Index	11.0	~	~
	18.00	JP	Consumer confidence	Sep	Index	42.5	~	~
Wed 13 Oct	~	CH	Trade balance	Sep	USD bn	20.0	17.8	~
	~	CH	Exports	Sep	y%ch	34.4	26.8	~
	~	CH	Imports	Sep	y%ch	26.8	25.0	~
	10.45	NZ	Food prices	Sep	m%ch	-0.1	~	~
	12.50	JP	Machine orders	Aug	m%ch	8.8	-3.8	~
					y%ch	15.9	8.5	~
	13.30	AU	MI consumer confidence	Oct	m%ch	-5.0	~	~
	13.30	AU	MI consumer confidence index	Oct	Index	113.2	~	~
	15.00	CH	Business climate index	QIII	Index	135.9	~	~
	15.00	CH	Entrepreneur confidence index	QIII	Index	133.0	~	~
Thu 14 Oct	10.00	NZ	REINZ housing price index	Sep	Index	3,202	~	~
					m%ch	0.3	~	~
	10.00	NZ	REINZ house sales	Sep	y%ch	-27.1	~	~
	10.45	NZ	Retail sales	Sep	m%ch	-0.4	~	0.4
	10.45	NZ	Retail sales ex-auto	Sep	m%ch	-0.1	~	0.3
	11.30	NZ	Business NZ PMI	Sep	Index	49.3	~	~
	12.50	JP	Domestic CGPI	Sep	m%ch	0.0	0.0	~
					y%ch	0.0	0.0	~
	13.30	AU	MI consumer inflationary expectation	Oct	y%ch	3.1	~	~
	13.30	AU	MI consumer unemployment expectation	Oct	Index	102.0	~	~
17.00	JP	Tokyo condominium sales	Sep	y%ch	18.5	~	~	
Fri 15 Oct	15.00	CH	Conference Board China August leading economic index					
	17.30	JP	Industrial production	Aug	m%ch	-0.3	~	~
					y%ch	15.4	~	~
17.30	JP	Capacity utilization	Aug	m%ch	-0.3	~	~	



## 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	
Tue 12 Oct	00.01	UK	RICS house price balance	Sep	%	-32.0	~	~	
	07.00	GE	CPI	Sep	y%ch	1.3	~	~	
	09.30	UK	DCLG UK house prices	Aug	y%ch	8.4	~	~	
	09.30	UK	CPI	Sep	y%ch	3.1	~	~	
	09.30	UK	Retail price index	Sep	y%ch	4.7	~	~	
	09.30	UK	Total trade balance	Aug	£mn	4,916	~	~	
	12.30	US	NFIB small business optimism	Sep	Index	88.8	~	~	
	19.00	US	Minutes of FOMC meeting	Oct	~	~	~	~	
Wed 13 Oct	09.30	UK	Jobless claims change	Sep	'000	2.3	~	~	
	09.30	UK	ILO unemployment rate	Aug	%	7.8	~	~	
	10.00	EZ	Industrial production	Aug	m%ch	0.1	~	~	
					y%ch	7.3	~	~	
	13.30	CA	New housing price index	Aug	m%ch	-0.1	-0.1	~	
Thu 14 Oct	09.00	EC	ECB Monthly Report	Oct	~	~	~	~	
	13.30	CA	International merchandise trade	Aug	C\$bn	-2.7	-2.2	~	
	13.30	US	Trade balance	Sep	\$bn	-42.8	-44.5	~	
	13.30	US	Producer price index	Sep	m%ch	0.4	0.1	~	
					y%ch	3.1	3.7	~	
	13.30	US	Initial jobless and continuing claims	Oct	~	~	~	~	
	Fri 15 Oct	07.00	EZ	EU 25 new car registrations	Sep	y%ch	-12.9	~	~
		10.00	EZ	CPI	Sep	m%ch	0.2	~	~
10.00		EZ	Trade balance	Sep	€bn	-0.2	~	~	
3.30		CA	Manufacturing sales	Aug	mch	-0.9	~	~	
13.30		CA	New motor vehicle sales	Aug	m%ch	2.4	~	~	
13.30		US	CPI	Sep	m%ch	0.3	0.2	~	
					y%ch	1.1	1.2	~	
13.30		US	Advance retail sales	Sep	m%ch	0.4	0.4	~	
13.30		S	Empire manufacturing	Oct	Index	4.1	7.0	~	
13.30		US	Uni. of Michigan confidence	Oct	Index	69.2	68.2	~	
13.30	US	Business inventories	Aug	m%ch	1.0	0.5	~		

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