

This Week

Last week's GDP figures were a huge surprise to all and sundry, registering growth of only 0.2% for the quarter. Market expectations were centred around 0.8%, with ourselves on 0.7% and the RBNZ on 0.9%. On the face of it, even a gradual economy recovery seems to be losing what steam it had. But, as they say, there are lies, da%ñ lies and statistics: - the underlying strength of the economy appears understated.

Weakness was isolated to a few key pockets. Most industries within the economy performed largely as expected, including solid growth in construction. Much of the weakness was in Manufacturing and Communications. The Northland drought hit dairy processing activity (recorded as manufacturing) by more than expected, though wider manufacturing activity was weaker than we anticipated.

But the real surprise has been in the Communications sector. Measured communications activity has fallen in the last 3 quarters and is at a lower level than during the recession. The main driver of the recent weakness seems to be more about measurement issues than an outright decline in communications usage.

The telecommunications measures rely on traditional activities such as phone call minutes. Yet components such as international calls are being displaced by Skype calls and Facebook postings to keep people up to date. The statistics also won't catch other completely new kinds of communications behaviour (if we can call it that), such as tweeting with Justin Bieber or, like, whoever. So the current measurements place a high weight on methods of communications that are declining in popularity whilst missing the replacement activity and other new types. Anyone who has observed the communication habits of teenage girls would find it hard to believe that activity in communications has been on the decline.

The 3 quarters of decline in Communications activity also suspiciously coincides with the start up of mobile network 2degrees. For confidentiality reasons StatsNZ is unable to divulge whether 2degrees is covered in the statistics. If it isn't covered, which would surprise us a little bit, then none of Rhys Darby's phone calls would be getting captured in the statistics.

The upshot is that one way or the other the Communications figures are under-reporting activity. Conservatively, assuming 'true' activity levels are just flat, GDP growth is being understated by up to 0.2 percentage points a quarter – and more if the sector is genuinely growing. Over a year that could add up to 0.6-0.8 percentage points. So the underlying pace of growth is slightly better than the reported figures, simply because the statistics aren't properly accounting for the rapid change in how we communicate with one another. And let's face it, it's not just statistics that struggle with that one!

Click here for:

[Foreign Exchange](#)

- NZD/USD lifts as USD weakness continues. NZD mixed on other cross rates.

[Interest Rates](#)

- Interest rates lower as RBNZ rate hike expectations pushed further out.

[Week Ahead](#)

- Trade balance, RBNZ Credit Aggregates, Building Consents, Business Outlook.

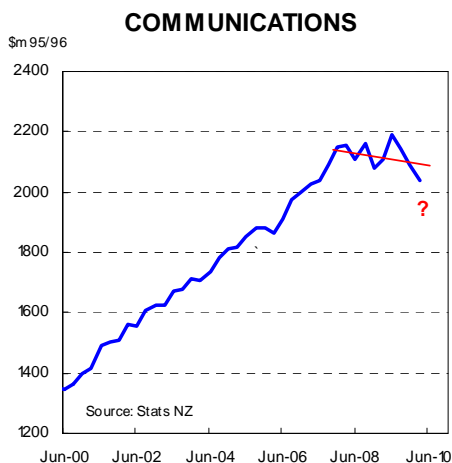
[Week in Review](#)

- Tourism and migration data, Current Account, GDP.

[Global Calendars](#)

- US & UK GDP, US house prices, US ISM Manufacturing & Confidence Surveys.

Chart of the week



- Trend Communications activity flat lined during the recession. However, it is very surprising that communications would now start to fall as the economy begins to recover.
- Part of the explanation may lie in measurement issues. With technology changing the way we communicate, the traditional methodology of measuring call minutes will be missing a big part of the picture yet still carries a relatively high weight.
- StatsNZ counts internet connections but currently does not directly capture data usage (though Telco revenues are incorporated). Consequently the statistics will understate the rise in popularity of smart phones (and the impact of their appetites for data) and increased usage of the internet to keep in touch with overseas friends and family (e.g. skypeing).
- The recent declines also coincide with 2degrees' start up.

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	0.7353	0.7277	0.7056	0.7071	0.7189	FLAT	0.7250	0.7400
NZD/AUD	0.7663	0.7709	0.7946	0.7783	0.8272	FLAT	0.7600	0.7750
NZD/JPY	62.05	62.34	59.76	65.55	65.26	FLAT	61.00	63.00
NZD/EUR	0.5456	0.5566	0.5544	0.5260	0.4896	FLAT/DOWN	0.5400	0.5500
NZD/GBP	0.4647	0.4643	0.4544	0.4741	0.4488	FLAT	0.4600	0.4700
TWI	66.6	66.9	66.1	66.0	65.6	FLAT	66.00	68.00

^Weekly support and resistance levels * Current is as at 10.20 am Monday; week ago as at Monday 5pm

- The NZD was mixed last week, posting gains against a weak USD, but slipping against the AUD. The NZD was also down on the euro, but little changed against the GBP and JPY.
- Volatility is relatively low in currency markets at present. The main themes at present are USD weakness and Japanese intervention.
- Late last week the USD index reached at its lowest level since February, although the Greenback did get some initial support on Friday night on talk the Bank of Japan had again been in the market trying to weaken the yen. However, gains were quickly reversed when the Japanese PM (speaking at the UN General Assembly) said he was unaware of any intervention.
- The AUD reached new 26-month high on Friday night. The EUR received a boost from the better than expected September Ifo index. The NZD started this week back above 0.73 against the USD – 0.80c down on the recent high of 0.742 against the USD, and 0.40c off its recent low of 0.762 against the AUD.
- A wildcard for the USD this week is a congressional vote on Wednesday. Congress may label China a currency manipulator and this could eventually lead to increased tariffs on some US imports from China. If Congress passes the bill, the USD will likely increase on safe-haven demand.

Short-term outlook:

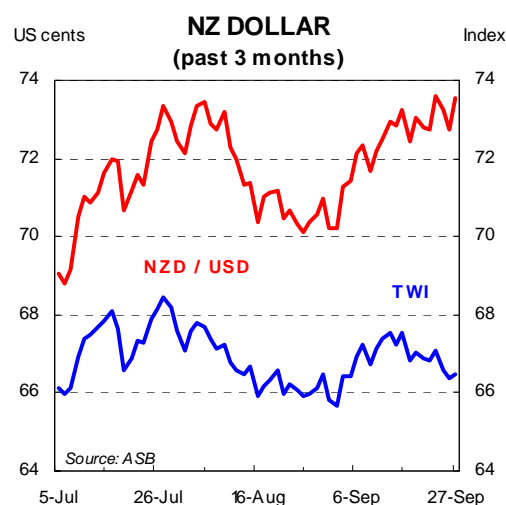
Key data	Date	Time (NZST)	Market expects
August Merchandise Trade Balance	29/9	10.45am	-
August Building Consents	30/9	10.45am	-
Sept. National Bank Business Outlook	30/9	10.45am	-

Potential currency movers from the offshore this week: Japan trade, Chicago Fed National Activity Index (27th); US Cash-Shiller house prices, US Richmond Fed manufacturing indices, US consumer confidence, Japan Tankan manufacturing indices (28th); China HSBC-Markit manufacturing PMI, EU consumer confidence (29th); South Korea & Japan industrial production (30th); EU manufacturing PMI, University of Michigan Consumer Confidence, ISM Manufacturing (1st).

Fed speeches: Lockhart (29th); Kocherlakota, Plosser, Rosengren (30th); Pianalto, Dudley, Fisher (1st).

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

- We have 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 rising 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.
- The 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	3.17	3.17	3.23	2.68	2.79	FLAT
2-year swap	3.77	3.84	3.79	4.35	4.27	FLAT/UP
5-year swap	4.37	4.45	4.27	5.31	5.49	FLAT/UP
5-year benchmark gov't stock	4.43	4.58	4.44	5.27	4.88	FLAT/UP
NZSX 50	3211	3217	3007	3251	3111	FLAT

* Current is as at 11.00 am Monday; week ago as at Monday 5pm. Please note that we have recently changed the NZ govt 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).

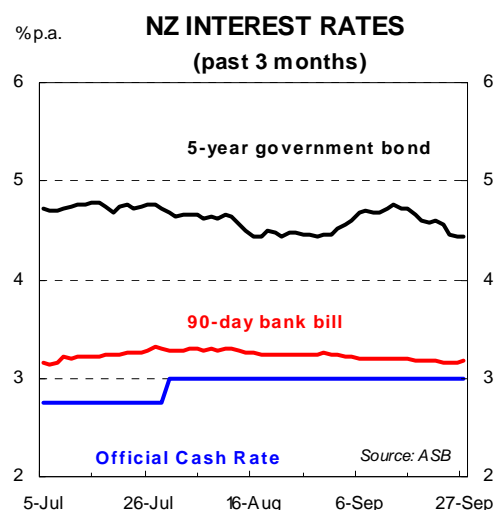
- Over the week NZ swap rates fell across the curve, with weak GDP data on Thursday providing the market with another reason to expect the RBNZ to remain on hold over the coming months.
- The GDP result was 0.7 percentage points below the RBNZ forecast in the previous week's September MPS. The GDP result reinforces the case for the RBNZ to remain on hold. Now we do not expect the RBNZ to resume the process of returning monetary conditions to normal levels until March 2011.
- Financial markets see a strong chance that the Fed will undertake another round of Quantitative Easing, which would keep US bond yields near their current lows. After a 3-week lull, the market is getting ready for a week of huge US supply, with US\$100billion going to auction this week with terms from 2 to 7 years. NZ Government bond yields eased lower last week, and are back trading around their 2010 low-point previously reached in August.

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Comment: The economic impact of the Earthquake was expected to overshadow the Q2 GDP release. However, the result was so weak it was hard to overlook, and already-low swap rates rallied lower. This week the market gets a forward-looking focus, and a look at the business mood after the Canterbury earthquake, with the September NBNZ Business Outlook Survey on Thursday. Building consent figures are for the August month, so we will have to wait until next month's release to see the early signs of an earthquake effect.

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



- The RBNZ kept the OCR unchanged at 3% at the September Monetary Policy Statement. The RBNZ has lifted the OCR 50 basis points since June. 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 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 (NZST)	Previous	Market expects	ASB expects
August Merchandise Trade Balance	29/9	10.45am	-186 mill	-	-650 mill
August Building Consents (Ex-apartment)	30/9	10.45am	-5.3% mom	-	-
September National Bank Business Outlook	30/9	10.45am	25.7	-	-

Wednesday 29 September

August Merchandise Trade Balance

Previous **-\$186 million, ASB(f) -\$650 million**

We expect a trade deficit of \$650 million in August, with the annual trade balance lifting to \$639 million (surplus) from \$573 million. The trade balance typically records deficits through the second half of the year, as agricultural exports decline while retailers begin to build stocks ahead of Christmas.

Exports receipts are up 12% on year-ago levels, largely supported by the recent strength in commodity prices. Meanwhile, volumes of exports from forestry, mining and manufacturing have also continued to grow due to strong demand from key trading partners.

Import demand has been slowly lifting, up 12% on year-ago levels. Volumes are stronger, in line with the improving economy. Meanwhile, prices have also been lifting (despite the strength in the NZD), as global commodity prices have pushed higher.

Thursday 30 September

August Building Consents

Previous Ex-Apartment consents **-5.3% mom**

Building consent data for July were soft, with weakness continuing in both residential and non-residential consents. We expect this weakness to continue in August.

July ex-apartment consents were down 5.3% in July compared with June. The number of residential consents issued each month appears to have started to trend down over recent months.

Non-residential consent issuance remains weak. The three month to July total value of non-residential consents is down 30% on the corresponding period in 2009. We expect the pattern of public spending offsetting some – but not all – of the weakness in private projects to continue in August.

From September onwards consent data will be significantly affected by the Canterbury earthquake which occurred on 4 September and caused widespread damage to buildings in the region.

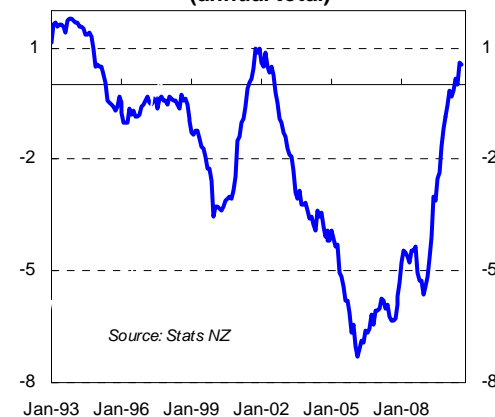
Thursday 30 September

National Bank Business Outlook Survey

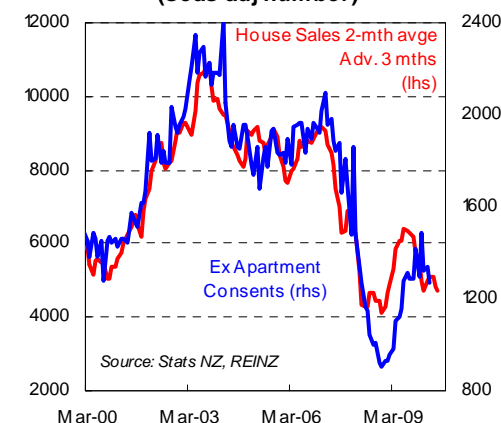
Previous: **Headline Confidence 16.4 (from 27.9 prev.)**

Business confidence has been softening in recent months, and the decline continued in the August month National Bank Business Outlook Survey. Headline business confidence fell to 16.4 (from 27.9 in the previous month) and businesses' assessment of own activity also eased to 25.7 (from 32.4). The declines are even starker given businesses typically become more confident in the months leading up to Christmas. It appears weak profitability is continuing to weigh on business confidence. For the past four surveys, a decreasing proportion of respondents have indicated improving profitability. The subdued nature of business sentiment is reflected in continued caution amongst businesses in regards to their expansion plans, with investment and hiring intentions falling in recent surveys. We expect the softness in headline and own activity expectations to continue in September.

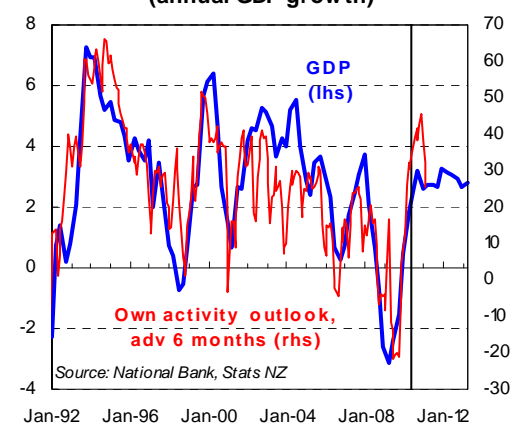
\$b **NZ GOODS TRADE BALANCE** (annual total) \$b



No. **NZ HOUSE SALES & CONSENTS** (seas adj number) No.



% **GDP & OWN ACTIVITY** (annual GDP growth) Index



NZ Data Review: weekly recap

NZ Migration - August

NZ net migration printed at +840 (Aug month, s.a.), to be +14,507 (year to Aug). Monthly net migration continued to show some recovery from the weak levels seen in recent months. Departures to Australia and UK show some signs of stabilising following some robust growth in recent months. Nonetheless, total departures looks to remain on an upward trend and departures to Australia will be one to keep an eye on given the continued strength in the Australian labour market.

Meanwhile, the decline in PLT arrivals in August was broad-based. This largely reflects a smaller number of people arriving here on work permits, given continued weakness in the NZ labour market.

Short-term visitor arrivals edged up slightly in August, reflecting a recovery in tourists from the US and Asia. Short-term visitor arrivals rose +0.8% mom, s.a. to be up +4.3% yoy.

NZ Q2 Balance of Payments

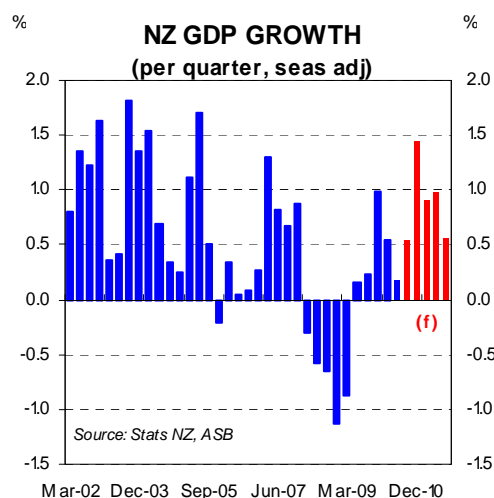
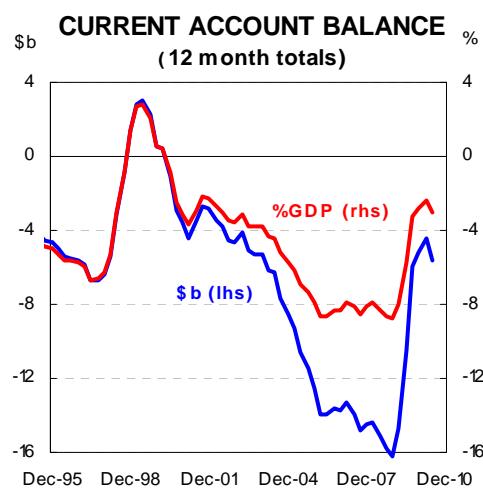
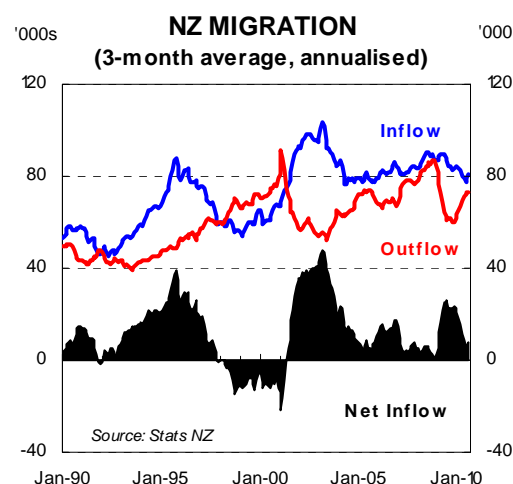
The current account started to widen in Q2, reaching 3% of GDP, after narrowing sharply over the past year. The wider deficit over Q2 largely reflects cyclical factors, with the recovering economy contributing to stronger profitability of foreign-owned NZ businesses. Also contributing to the wider deficit over Q2 was a deficit in the Transfers balance, due to a change in non-resident withholding tax policy, and a deficit in the services balance due to weak tourism exports. Providing some partial offset to these deficits was a strong trade surplus, owing to the recovery in global dairy prices since the start of the year.

Over the next year, we expect cyclical factors will continue to drive the current account deficit wider. However, this underlying dynamic is likely to be interrupted over the next few quarters as a result of the Canterbury earthquake. We expect the overall impact will be to narrow the current account deficit temporarily, due to the one-off transfers coming from insurance payouts. Meanwhile, the wealth impact of the earthquake will manifest in the international investment position.

NZ Q2 GDP

June quarter GDP was substantially weaker than expected, with just 0.2% growth recorded compared to market expectations of 0.8% growth. It appears that quarterly result was dragged down by a few sectors, rather than being symptomatic of underlying weakness in economic activity. In particular, the impact of the Northland drought had a greater than expected impact on agricultural production, which then fed through to extremely weak manufacturing activity. In addition, communications activity fell sharply for the 3rd consecutive quarter. Beyond the weakness in these industries was a respectable performance from many other areas. Providing large support to growth was recovery in retail volumes and construction activity. Growth in export volumes remained strong, but was met by a large run-down in inventories rather than by production. As a result, we expect that inventories will be rebuilt over the next few quarters which should add to growth.

Our early estimates suggest the Canterbury Earthquake in early September is likely to shave off around 0.3 percentage points off growth. Given we had 0.8% pencilled in prior, this takes our preliminary forecast down to 0.5%. However, the December quarter is likely to receive a substantial boost as the early stages of reconstruction kicks in.



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 27 Sep	12.50	JP	Corp service price index	Aug	y%ch	-1.2	~	~
	12.50	JP	Merchandise trade balance (Seas. Adj.)	Aug	¥bn	610.4	~	~
	15.00	CH	Industrial profits	Aug	ytd y%ch	81.6	~	~
Tue 28 Sep	18.00	JP	Small business confidence	Sep	Index	48.4	~	~
Wed 29 Sep	10.45	NZ	Trade balance	Aug	\$mn	-186.0	~	~
	11.50	JP	Tankan large manufacturers index	QIII	Index	1.0	7.0	~
	13.00	AU	Conference board leading index	Aug	m%ch	0.1	~	~
	15.30	CH	HSBC manufacturing PMI	Sep	Index	51.9	~	~
Thu 30 Sep	10.45	NZ	Building permits	Aug	m%ch	3.1	~	~
	12.15	JP	Nomura/JMMA manufacturing PMI	Sep	Index	50.1	~	~
	12.50	JP	Retail trade	Aug	m%ch	0.7	~	~
					y%ch	3.8	~	~
	12.50	JP	Industrial production	Aug	m%ch	-0.2	~	~
					y%ch	14.2	~	~
	14.00	AU	HIA new home sales	Aug	m%ch	-7.0	~	~
	14.30	AU	Building approvals	Aug	m%ch	2.3	0.0	3.0
					y%ch	11.0	10.0	12.8
	14.30	AU	Private sector credit	Aug	m%ch	0.1	0.3	0.2
					y%ch	2.8	2.9	2.9
	14.30	AU	RP data-rismark house price index	Aug	m%ch	0.1	~	~
	15.00	NZ	NBNZ activity outlook	Sep	Index	25.7	~	~
	15.00	NZ	NBNZ business confidence	Sep	Index	16.4	~	~
15.00	JP	Vehicle production	Aug	y%ch	16.8	~	~	
18.00	JP	Housing starts	Aug	y%ch	4.3	~	~	
18.00	JP	Construction orders	Aug	y%ch	-0.7	~	~	
Fri 1 Oct	12.30	AU	Ai-Group Performance of Manufacturing Index	Sep	Index	51.7	~	~
	12.30	JP	Job-to-applicant ratio	Aug	Ratio	0.5	~	~
	12.30	JP	Overall household spending	Aug	y%ch	1.1	~	~
	12.30	JP	Tokyo CPI	Sep	y%ch	-1.0	~	~
	12.30	JP	Jobless rate	Aug	%	5.2	~	~
	12.30	JP	National CPI	Aug	y%ch	-0.9	~	~
	14.00	CH	PMI Manufacturing	Sep	Index	51.7	~	~
	14.30	AU	Financial Stability Review	~	~	~	~	~
	18.00	JP	Vehicle Sales	Sep	y%ch	46.7	~	~

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 Sep	00.01	UK	Hometrack housing survey	Sep	m%ch	-0.3	~	~
					y%ch	1.5	~	~
	13.30	US	Chicago Fed national activity index	Aug	Index	0.0	~	~
Tue 28 Sep	15.30	US	Dallas Fed manufacturing activity	Sep	~	-13.5	~	~
	~	GE	CPI	Sep	y%ch	1.0	~	~
	09.30	UK	GDP	QII	q%ch	1.2	~	~
	09.30	UK	Current account	QII	£bn	-9.6	~	~
	14.00	US	S&P/CaseShiller composite-20 home price index	Jul	y%ch	4.2	3.2	~
	15.00	US	Consumer confidence	Sep	Index	53.5	53.5	~
	15.00	US	Richmond Fed manufacturing index	Sep	Index	11.0	~	~
	09.30	UK	Index of services (3mth/3mth)	Jul	%	0.7	~	~
Wed 29 Sep	10.00	EZ	Business climate indicator	Sep	Index	0.6	~	~
	00.01	UK	GfK consumer confidence survey	Sep	Index	-18.0	~	~
Thu 30 Sep	08.55	EZ	Unemployment rate	Sep	%	7.6	~	~
	13.30	CA	GDP	Jul	m%ch	0.2	~	~
	13.30	US	GDP (annualized)	QII	q%ch	1.6	1.6	~
	13.30	US	Initial jobless and continuing claims	Sep	'000	465	458	~
	14.45	US	Chicago purchasing manager	Sep	Index	56.7	56.0	~
	15.00	US	NAPM-Milwaukee	Sep	Index	59.0	~	~
	09.30	UK	PMI manufacturing	Sep	Index	54.3	~	~
Fri 1 Oct	10.00	EZ	Unemployment rate	Aug	%	10.0	~	~
	13.30	US	Personal income	Aug	m%ch	0.2	0.3	~
	13.30	US	Personal spending	Aug	m%ch	0.4	0.4	~
	13.30	US	PCE core	Aug	m%ch	0.1	0.1	~
					y%ch	1.4	1.4	~
	14.55	US	U. of Michigan confidence	Sep	Index	66.6	67.0	~
	15.00	US	ISM manufacturing	Sep	Index	56.3	55.0	~
	15.00	US	Construction spending	Aug	m%ch	-1.0	-0.4	~
	22.00	US	Motor vehicle sales	Sep	Mn	11.5	11.5	~

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