

Weekly Commentary

6 April 2010

Confidence, no trick

Last week's activity indicators underscored the level of confidence in those sectors that we expect to drive growth over the next year.

Residential building consents rose 5.9% in February, reasserting their upward trend after two months of declines. Apartment consents remained very weak, though with just 13 approved in February, it's fair to say that they have hit rock bottom (any fewer and they wouldn't be apartments, they'd be standalone houses). Excluding apartments, consents were 10% higher for the month, and are up 57% from the record lows seen a year ago.

The uncertainty around changes to the tax treatment of property in the May Budget has weighed on the housing market in the last few months – house sales have dropped sharply and listings have picked up, while building consents softened in December and January. But the rebound in consents in February suggests that builders and developers are prepared to push on despite this uncertainty.

A rebound in homebuilding activity is a key part of our (and the RBNZ's) above-consensus growth forecasts, especially for this year. The arithmetic of the housing market remains stark: current levels of building activity are not sufficient to meet population demand, which has been boosted in the last year by a drop in the number of New Zealanders heading overseas. There are three ways this can be resolved: either supply increases of its own accord, prices of existing houses

are squeezed higher (which in turn could induce more supply), or population pressures ease (Australia is once again becoming an attractive destination for jobseekers). In practice, we expect to see a mix of all three.

The value of non-residential consents rose from a weak January to \$317m, but was still down 17% on a year ago. Non-residential investment remains under pressure as a result of the lagged effects of the recession – hospitals and schools have accounted for much of the activity over the last year, as the government has played a role in offsetting the weakness in the private sector. We expect activity to start picking up in the second half of this year, although commercial property is likely to take longer to recover.

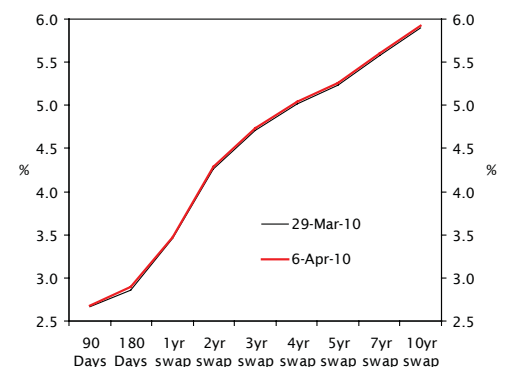
Meanwhile, monthly business confidence slipped to a net 43% in March, down from the ten-year high of 50% recorded in February. Own-activity expectations – a useful guide to current quarter GDP – fell by less, from 42% to 39%. Both measures remain comfortably within their recent ranges.

In fact the underlying picture may be even better than these figures suggest. There is an element of seasonality in this survey, although the pattern hasn't been consistent over time, so we tend to steer clear of quoting a precise 'adjusted' number. Nevertheless, it appears that the trend has been one of continued improvement in confidence in recent months.

The details of the survey were mixed, with a small pickup in investment intentions but a drop in employment intentions. Taking the absolute levels of these indicators can be misleading, especially for employment – only a net 9% of firms expect to hire more workers, but this is above its long-run average. Indeed, this measure never got higher than 16.4% during the jobs boom in the last decade. All that implies is that hiring tends not to be planned, but is reactive to rising demand.

Today's *Quarterly Survey of Business Opinion* for the March quarter echoed the findings of the monthly survey. In seasonally adjusted terms, general confidence rose to a net 36%, the strongest since June 1999, while own-activity expectations rose from 13% to 20%. Employment and investment intentions were modest in absolute terms, but were above their long-run average levels.

NZ Interest Rates



*Yield curve is yields on bank bills to 180 days, fixed interest rate swaps for 1 year onwards.

The quarterly survey generally provides more insight around the resource pressures that firms are facing. Capacity utilisation fell slightly from 91.1% to 90.5%, and has been above average for three of the last four quarters (note that this question reflects cost pressures more so than physical capacity constraints). The latest reading confirms that the surprisingly quick rebound is not an aberration that can be looked through. Skilled workers are still easy to find on balance, but less so in recent months.

The *QSBO* outturn supports our pick for 1% growth in March quarter GDP (and the RBNZ's forecast of 0.9%). To some degree, our forecasts reflect the much-vaunted rebalancing of the economy, although it seems to be driven more by circumstances than by 'good behaviour' on the part of households. Retail spending has been subdued in the early part of this year,

and housing – particularly investment properties – has been weighed down by higher long-term mortgage rates and uncertainty about tax changes. In contrast, export volumes have been boosted by good growing conditions (up to February) for the agricultural sector, while a booming Chinese economy has lifted commodity prices. In addition, a strong Australian economy and a low NZD/AUD exchange rate are a boon for sectors such as manufacturing and tourism. Homebuilding is rising out of necessity, and business investment in plant and machinery (much of which tends to be imported) has been aided by the strong NZD/USD rate, which has rebounded much earlier than in past recoveries. Given time, continued low interest rates would encourage a return to the borrow-and-spend behaviour of the last cycle, hence the need for the RBNZ to start returning the cash rate to more normal levels soon.

Fixed vs. floating: The prospect of OCR hikes through the second half of the year and beyond will eventually flow through to short-term fixed rates, which have only seen small increases to date and remain at historically low levels. As a result, we could see more borrowers moving to fix at the favourable rates still on offer – and the experience of March/April last year shows that these types of flows can put a great deal of upward pressure on mortgage rates. With floating and one-year fixed rates around similar levels, there may not seem to be much advantage in fixing right now, but those who wait until they see the whites of the RBNZ's eyes before fixing are likely to face much less attractive options. Repaying more than the minimum amount and spreading the loan over a mix of terms can help to reduce overall risk regarding uncertain future interest rate changes.

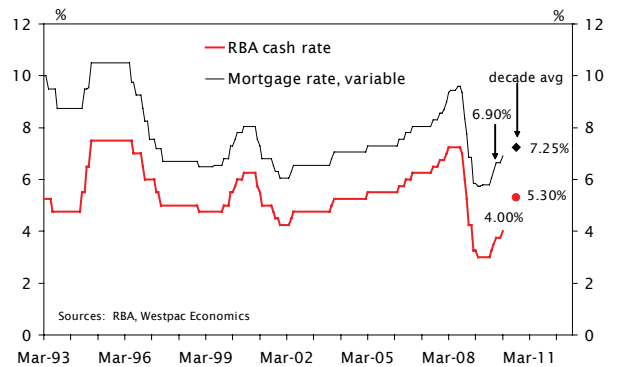
Key Data Previews

Aus RBA policy announcement

Apr 6, Last: 4.00%, WBC f/c: 4.00%, Mkt f/c: 4.25%, Range: 4.00% to 4.25%

- The RBA resumed its policy normalisation in March, raising the cash rate by another 25bps to 4.00%. It also retained a clear tightening bias noting that “rates to most borrowers ... remain lower than average” and that “... with growth likely to be close to trend and inflation close to target over the coming year it is appropriate for interest rates to be closer to average.” The March decision was seen as a step in that process.
- Data since the March meeting has been mixed. Although Q4 GDP was as expected and consumer sentiment continues to hold up well, housing finance, jobs, retail sales and dwelling approvals have all been on the soft side. Housing markets more generally have remained buoyant and are becoming more of a focus for the RBA. Overall we expect rates to remain on hold, but April will be another ‘finely balanced’ call.

RBA: lessening the monetary stimulus

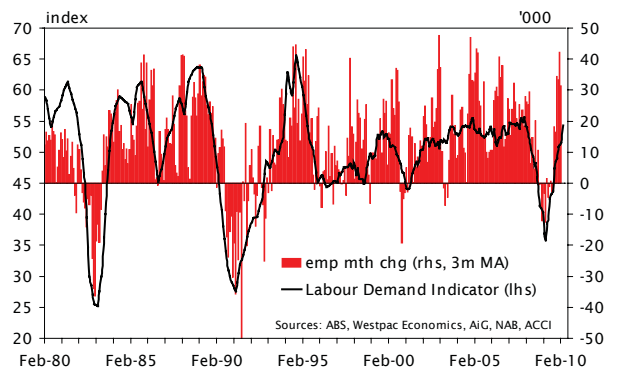


Aus Mar employment chg

Apr 8, Last: 0.4k, WBC f/c: 35k, Mkt f/c: 20k, Range: flat to 40k

- After five consecutive strong upside surprises in jobs growth, February saw a consolidation with a minor 0.4k rise. Still, 6mth annualised growth was a rapid 3.7% (highest since Sep-06). Trend growth also continued to accelerate to 1.7%yr (highest since Oct-08) from 1.4%yr previously, well up from the resilient low of -0.1%yr in July 2009.
- The continued uptrend in job ads implies an ongoing strong acceleration in annual trend jobs growth through 2010 to 3%yr. Also, our composite of business survey employment indices rose in its preliminary March reading to 54.3 from 51.5. Historically, this would be consistent with smoothed jobs growth around 19k mth, but with 3mMA jobs growth currently 31k, and the higher March composite, we expect a strong 35k employment rise in March. This would lift annual trend growth to 2.0%yr from 1.7%yr previously.

Westpac Australian Labour Demand Indicator

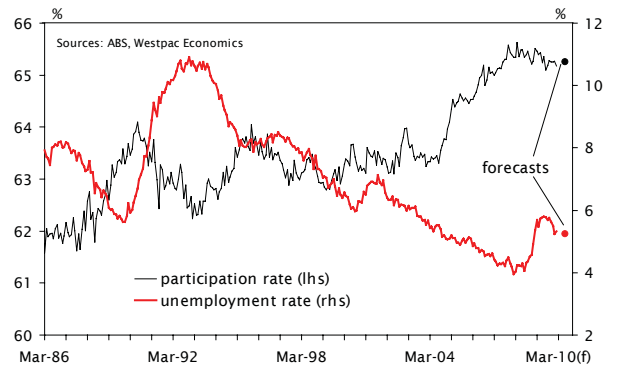


Aus Mar unemployment rate

Apr 8, Last: 5.3%, WBC f/c: 5.2%, Mkt f/c: 5.3%, Range: 5.1% to 5.4%

- With the weak jobs gain in February accompanied by a 0.1 ppt dip in the participation rate to 65.2%, the impact on the unemployment rate was tempered to a 0.1ppt rise to 5.3%, but its downtrend from a 5.8% peak continued, also to 5.3%. We expect the acceleration in jobs growth in 2010 to be accompanied by higher participation rates and population growth, slowing the downtrend in the unemployment rate.
- Months of jobs growth in line with what we expect for March, after a fall in the prior participation rate, have historically seen rebounds in the participation rate of 0.1ppts on average. We expect a 0.1ppt rise to 65.3%. Still, combined with a 35k jobs gain, this would allow the unemployment rate to fall back to 5.2%. With the trend participation rate stable since August, there is some downside risk to the unemployment rate forecast from the lack of any participation rate bounce.

Unemployment and participation rates



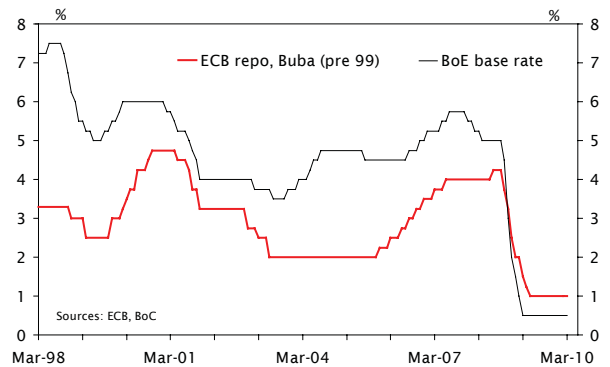
Bank of England and European Central Bank decisions

Apr 8, BoE Last: 0.50%, WBC f/c: 0.50%, Mkt f/c: 0.50%

Apr 8, ECB Last 1.00%, WBC f/c: 1.00%, Mkt f/c: 1.00%

- The BoE March meeting minutes showed another unanimous vote for no change in rates and no quantitative easing (QE) extension, although some members considered that upside inflation risks had increased "slightly". Q4 GDP growth was revised up further to 0.4% and recent business surveys suggest the economy may not have lost much momentum yet this year. These developments point to another unanimous on hold decision in April, and to some extent diminish prospects for a further QE extension as soon as May.
- Little has changed since the March ECB meeting: business surveys point to continued growth but hard activity data have been less robust and credit is still contracting. The ECB is so clearly on hold that we expect, once again, that the April press conference will be dominated by fiscal policy concerns.

ECB and BoE policy rates



Key Data and Events

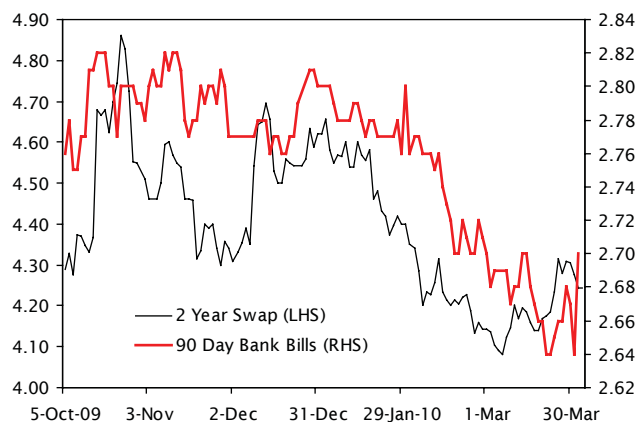
		Last	Market Median	Westpac Forecast	Comments
Tue 6 Apr					
NZ	Mar ANZ Commodity Price Index	3.8%	-	-	Dairy prices edged up over the month.
Aus	RBA Policy Announcement	4.00%	4.25%	4.00%	Will the weak run of partial data be enough for the RBA to pause?
	Mar ANZ Job Ads	19.1%	-	-	Feb an unwind of weak Jan from s.adj problems; strong 7mth uptrend.
US	Mar 16 FOMC Meeting Minutes	-	-	-	No big surprises were in the meeting statement.
	Fedspeak	-	-	-	Minneapolis Fed's Kocherlakota (new appointment so what's his bias?)
Eur	Apr Sentix Investor Confidence	-7.5	-5.2	-7.0	Further slight gain expected, despite sovereign concerns persisting.
UK	Mar PMI Construction	48.5	48.7	48.5	Still contracting but at a milder pace in early 2010 than last year.
	Q4 Mortgage Equity Withdrawal £bn	-4.9	-3.0	-3.5	For six qtrs (to Q2 09) MEW has been reversed. More of same in Q4.
Wed 7 Apr					
Aus	Mar AiG PSI	48.3	-	-	Slipped back below 50 in early 2010 indicating slight contraction.
US	Feb Consumer Credit \$bn	5.0	0.0	-	Jan saw first rise in a year.
	Fedspeak	-	-	-	Bernanke in Dallas. Also Dudley and Hoenig (the dissenter).
Jpn	Bank of Japan Meeting	0.10%	0.10%	0.10%	Prior meeting saw expansion of term facility. Status quo this time.
Eur	Mar PMI Services (F)	53.7a	53.7	53.7	Decent 1.9 pts rise in advance report.
	Q4 GDP (F)	0.1%a	0.1%	0.1%	Useful reminder that stronger PMIs don't always mean stronger GDP.
	Feb PPI %yr	-1.0%	-0.4%	-0.5%	Base effects drive %yr higher but Ger data suggest Feb mth subdued.
Ger	Feb Factory Orders	4.3%	-0.5%	-1.5%	Jan investment goods orders surge may not persist in Feb.
UK	Mar Nationwide Consumer Confidence	80	81	80	Sharp Feb rise but Mar unlikely to improve due budget/election issues.
	Mar BRC Shop Price Index %yr	1.7%	-	-	Guide to the high street part of the CPI basket.
	Mar PMI Services	58.4	58.0	56.5	Feb bounced from weather impacted Jan; not sustainable.
Can	Feb Building Permits	-4.9%	2.0%	-	Jan's decline weighed down by non-res volatility; residential rose 4.1%.
	Mar Ivey PMI nsa	51.9	55.0	55.0	Seasonality unclear but underlying economy doing OK so expect rise.
Thu 8 Apr					
Aus	Mar Employment chg	0.4k	20k	35k	Higher composite of business survey emp indices; lifts trend to 2%yr.
	Mar Unemployment Rate	5.3%	5.3%	5.2%	Jobs jump only partially offset by 0.1ppt PR rise; potential downside risk.
US	Initial Jobless Claims w/e 3/4	439k	435k	-	Modest claims downtrend re-emerging.
	Mar Chain Store Sales %yr	3.7%	-	-	Guide to retail activity but not always consistent with official data.
	Fedspeak	-	-	-	Minneapolis Fed's Kocherlakota again.
Jpn	Feb Machinery Orders	-3.7%	3.7%	-	Local capex still weak, but external demand has firmed of late.
	Feb Current Account s.a. ¥bn	1713	1249	-	Lagging domestic demand and slowly widening income surplus.
Eur	Feb Retail Sales	-0.5%	flat	-0.5%	French and German spending down in Feb.
	ECB Rate Decision & Press Conference	1.00%	1.00%	1.00%	Not exciting from policy perspective. Greece/fiscal issues to dominate.
Ger	Feb Industrial Production	0.6%	1.0%	0.6%	Recent orders bounce to drive back to back IP gains.
UK	Feb Industrial Production	-0.4%	0.5%	0.2%	Bounce from Jan but less utility output to constrain gain.
	BoE Rate Decision	0.50%	0.50%	0.50%	Firmly on hold and QE to be held at £200bn.
Fri 9 Apr					
US	Feb Wholesale Inventories	-0.2%	0.4%	0.2%	Further clue to less significant cont'n from restocking to Q1 GDP.
UK	Mar PPI %yr	2.9%	3.1%	-	Core output measure.
Can	Mar Employment ch'	21k	25k	25k	Date have been volatile but trend pace is around 25k per month.

New Zealand Economic and Financial Forecasts

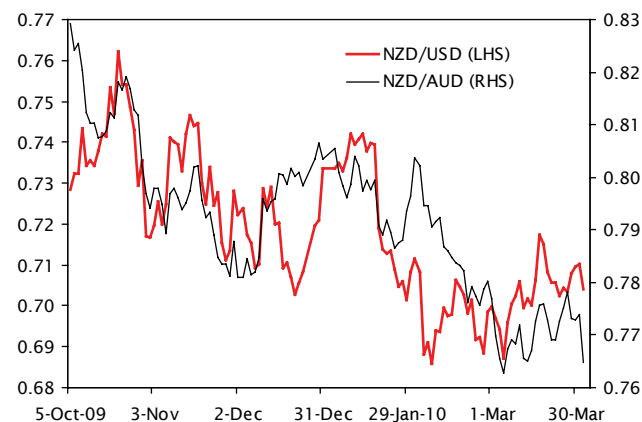
Economic Growth Forecasts	March years				Calendar years			
	2008	2009	2010f	2011f	2008	2009	2010f	2011f
% change								
GDP (Production) ann avg	2.9	-1.4	-0.2	4.1	-0.1	-1.6	3.4	4.4
Employment	-0.3	0.7	-1.3	1.8	0.9	-2.4	1.2	2.1
Unemployment Rate % s.a.	3.8	5.0	7.1	6.3	4.7	7.3	6.5	5.7
CPI	3.4	3.0	2.4	1.5	3.4	2.0	2.0	2.4
Current Account Balance % of GDP	-7.8	-7.9	-2.8	-4.9	-8.7	-2.9	-4.7	-5.2

Financial Forecasts	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11	Sep-11	Dec-11
Cash	2.75	3.25	3.75	4.25	4.75	5.25	5.75
90 Day bill	3.20	3.70	4.20	4.70	5.20	5.70	6.10
2 Year Swap	4.70	5.00	5.30	5.60	5.90	6.20	6.40
5 Year Swap	5.60	5.70	5.90	6.10	6.30	6.45	6.60
10 Year Bond	5.90	5.90	6.00	6.10	6.20	6.20	6.30
NZD/USD	0.67	0.72	0.77	0.76	0.74	0.72	0.71
NZD/AUD	0.79	0.80	0.81	0.82	0.82	0.84	0.84
NZD/JPY	61.0	67.0	73.9	77.5	78.4	78.5	79.5
NZD/EUR	0.50	0.53	0.56	0.56	0.56	0.56	0.57
NZD/GBP	0.46	0.48	0.50	0.48	0.47	0.46	0.46
TWI	63.3	67.1	70.8	71.1	70.7	70.4	70.5

2 Year Swap and 90 Day Bank Bills



NZD/USD and NZD/AUD



NZ interest rates as at market open on Tuesday 6 April 2010

Interest Rates	Current	Two Weeks Ago	One Month Ago
Cash	2.50%	2.50%	2.50%
30 Days	2.61%	2.58%	2.67%
60 Days	2.64%	2.63%	2.69%
90 Days	2.68%	2.64%	2.69%
2 Year Swap	4.29%	4.19%	4.08%
5 Year Swap	5.26%	5.12%	5.06%

NZ foreign currency midrates as at Tuesday 6 April 2010

Exchange Rates	Current	Two Weeks Ago	One Month Ago
NZD/USD	0.7035	0.7056	0.6958
NZD/EUR	0.5216	0.5226	0.5106
NZD/GBP	0.4599	0.4691	0.4596
NZD/JPY	66.380	63.810	62.900
NZD/AUD	0.7641	0.7692	0.7672
TWI	65.460	65.340	64.430

Economic and Financial Forecasts

Economic Forecasts (Calendar Years)	2005	2006	2007	2008	2009e	2010f	2011f
Australia							
Real GDP % yr	2.8	2.9	4.0	2.4	1.3	3.2	3.6
CPI inflation % annual	2.8	3.3	3.0	3.7	2.1	2.6	2.8
Unemployment %	5.1	4.8	4.4	4.2	5.6	5.2	4.9
Current Account % GDP	-5.8	-5.3	-6.3	-4.4	-4.1	-4.7	-4.1
United States							
Real GDP %yr	3.1	2.7	2.1	0.4	-2.4	2.4	3.0
Consumer Prices %yr	3.4	3.2	2.9	3.8	-0.4	1.3	2.4
Unemployment Rate %	5.1	4.6	5.8	5.8	9.3	9.6	9.1
Current Account %GDP	-6.1	-6.0	-5.3	-4.9	-3.1	-3.0	-2.3
Japan							
Real GDP %yr	1.9	2.8	2.2	-1.5	-5.8	2.3	1.8
Consumer Prices %yr	-0.3	0.2	0.1	1.4	-1.3	-1.1	-0.2
Unemployment Rate %	4.4	4.1	3.9	4.0	5.1	4.8	4.5
Current Account %GDP	3.6	3.9	4.8	3.2	2.8	4.1	4.3
Euroland							
Real GDP %yr	1.8	3.1	2.8	0.5	-4.0	0.6	1.1
Consumer Prices %yr	2.5	2.0	3.1	1.6	0.9	0.7	1.2
Unemployment Rate %	8.8	7.9	7.3	7.8	10.0	11.5	10.8
Current Account %GDP	-0.2	-0.1	0.1	-1.1	-1.0	-0.5	0.0
United Kingdom							
Real GDP %yr	2.2	2.9	2.6	0.5	-5.0	0.2	1.3
Consumer Prices %yr	2.1	3.0	2.1	3.5	2.9	2.0	1.5
Unemployment Rate %	2.8	3.0	2.5	3.1	5.5	7.0	7.3
Current Account %GDP	-2.6	-3.3	-2.7	-1.6	-2.4	-2.0	-1.5

Forecasts finalised 12 March 2010

Interest Rate Forecasts	Latest (Apr 6)	Jun-10	Sep-10	Dec-10	Mar-11	Jun-11
Australia						
Cash	4.00	4.25	4.50	4.50	4.50	5.00
90 Day Bill	4.48	4.50	4.60	4.75	4.75	5.25
10 Year Bond	5.84	5.90	6.00	6.00	6.10	6.75
International						
Fed Funds	0.125	0.125	0.125	0.125	0.125	0.50
US 10 Year Bond	3.99	3.40	3.75	4.00	4.50	5.25
ECB Repo Rate	1.00	1.00	1.00	1.00	1.25	1.50
Exchange Rate Forecasts						
AUD/USD	0.9207	0.85	0.90	0.95	0.93	0.90
USD/JPY	94.36	91	93	96	102	106
EUR/USD	1.3487	1.34	1.36	1.38	1.36	1.32
AUD/NZD	1.3087	1.27	1.25	1.23	1.22	1.20

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