NEW ZEALAND ECONOMICS
ANZ MARKET FOCUS

4 October 2010

INSIDE

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NEVER-NEVER LAND

ECONOMIC OVERVIEW

The recent global equity market recovery and improving tone of global leading indicators are encouraging signs for NZ.Inc. Of late, however, recent moves seem based on the expectation of further policy support, raising questions about their sustainability. Something has to give. The local dataflow provided something for everyone, highlighting an economy that is travelling along at low speed. This week sees the release of the QSBO for Q3 and commodity price data. The former will highlight the still tough economic environment that businesses are facing. But the latter should point to the possibility of a better 2011 eventuating.

FOREIGN OWNERSHIP OF RURAL LAND

Foreign ownership, particularly of rural land, is a controversial and emotive topic. In this article we look at the broader issues. A huge portion of New Zealand's comparative advantage resides in our land and the income generated from it. As such there is strong interest in maintaining local ownership. A firm but fair regulatory framework is key. Yet, New Zealand also needs to recognise the benefits that foreign ownership can bring. Foreign ownership in the rural sphere is currently very small and foreign direct investment brings substantial benefits in the form of linkages to international markets. Current angst over foreign ownership deflects attention from the heart of the issue which includes New Zealand's poor savings culture, reliance on foreign savings and poor relative investment returns. With the political breeze clearly favouring more restrictive foreign ownership rules, the onus is on the government to balance that with a more proactive stance towards saving.

INTEREST RATE STRATEGY

NZ interest rates continue to grind lower, and are approaching the year's lows again, spurred on by weak domestic data and global developments. Since the MPS, the rally in swap rates has been uniform across the curve. However, with no more rate hikes priced in for 2011, and just 1.5 hikes priced in by June 2011, scope for lower short end rates seems limited, especially with the RBA set to hike tomorrow. But the long end is a different story, with further quantitative easing (QE) in the US likely to see rates grind lower over the remainder of the quarter and remain somewhat anchored.

CURRENCY STRATEGY

The dominant feature last week was the sight of QE2 on the horizon and edging towards port. It should be noted that the result has been specific USD weakness rather than general "other currency" strength. The US is winning the "competitive devaluation" race at the moment. NZD/AUD near 10 year lows leaves little scope for further depreciation there. Tomorrow the RBA will provide the next clues.

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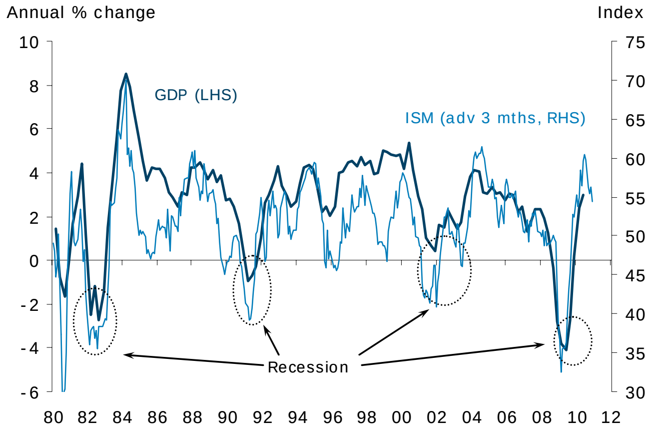
THIS WEEK'S EVENTS

- **ANZ Commodity Price Index** – September 2010 (Monday, October 4, 3:00pm).
- **NZIER Quarterly Survey of Business Opinion – Q3** (Tuesday, October 5, 10:00am). The general business situation is expected to continue tracking lower, with domestic trading activity stalling. The Canterbury earthquake may push up surveyed capacity utilisation.
- ***globalDairyTrade* online auction** (Wednesday, October 6, 6:00am). We expect the early October event to show some consolidation in whole milk powder prices following gains in the previous couple of months. Prices are expected to average US $3,600/tonne.

WHAT'S THE VIEW?

More questions than answers are appearing about the global economy, and one question at present is the rally in US equities, with the bellwether S&P 500 index up around 9 percent over September, the third largest monthly increase in a decade. It's hard to go past expectations of further quantitative easing (QE) by the FOMC next month pinning down long-term US interest rates as the catalyst, despite the sombre economic backdrop. Cash has to go somewhere after all. We're not equity specialists so will offer no comment on that. But the last few years has seen a strong correlation between equities and leading indicators including various confidence surveys and manufacturing indicators – something we refer to as a blind leading the blind dynamic. Last week saw a sizeable jump in the Chicago PMI, although the movement in the ISM survey was more muted. While still early days, if correlations over the past three years hold, we're set to see an improvement in the leading indicators over the coming months. Whether we see it in time to head off further QE remains to be seen. But with so much riding on QE, we suspect we're headed for a collision of sorts. Markets certainly can't sustain current pricing without the Fed doing something.

US GDP vs ISM Manufacturing



Sources: ANZ, National Bank, Bloomberg

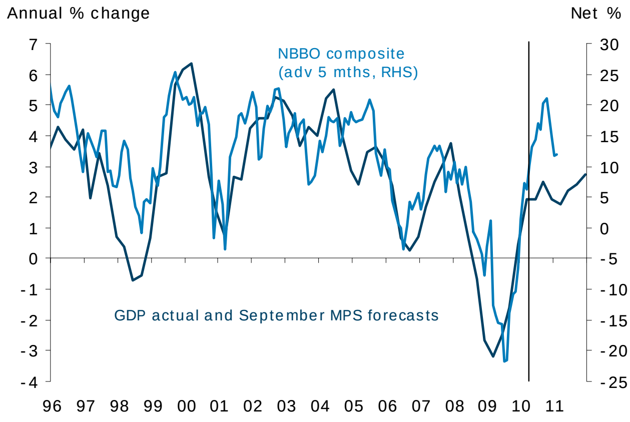
What the future holds is pretty much binary - we either see more QE or we don't. And with market pricing so heavily skewed in favour of it, it would be foolish to ignore the risk that it isn't forthcoming. But having opened the door to it, the Fed is hardly likely to move to a "no QE" stance. However they could leave the door open for a while, and let the improving outlook right itself, and that'd be the real risk. That said, comments by New York Fed President (and FOMC Vice Chairman) Dudley hint at more action. In his view, "both the current levels of unemployment and inflation and the timeframe over which they are likely to return to levels consistent with our mandate are unacceptable", adding that "we have tools that can provide additional stimulus at costs that do not appear to be prohibitive". How things play out from here remains to be seen, but Dudley's comments have certainly re-ignited the debate. What we do know is that the FOMC statement opened the door to it, Chairman Bernanke has said he is prepared to do it if necessary and now vice Chair Dudley appears to be outright in support of it. However, there is the small matter of Hoenig's dissent to deal with – which suggests that the earliest we can expect an announcement will be the November 3rd FOMC meeting. Indeed, even if that is the date, it will be some feat to "deal with" Hoenig's dissent and take additional steps all in the one meeting. Nonetheless, the level of scuttlebutt has gotten so loud that we feel QE is more likely than not, and we suspect it will be of the ongoing, measured targeted variety (i.e. adding at say US $200bn per meeting, upsizing as necessary) as opposed to the shock and awe tactics of March 2009.

ECONOMIC OVERVIEW

For NZ, the implications are non-trivial. First, we need to acknowledge the reasons for QE in the first place, and they are clear reminders of challenges that continue to abound the global economy. Second, lower US yields will continue to suppress long-dated NZ yields and support overall financial conditions. Financial conditions are forward looking in terms of their lead on GDP, and our Financial Conditions Index continues to ease. We'll be updating readers on this next week. Third, currency sentiment is being dominated by a weak USD, which is dragging up the NZD/USD. Technically, it's clearly extended - even allowing for commodity price movements and the yield differential. But currencies are strange beasts, even at the best of times, and a stronger NZD/USD will present some challenges for the continued wider rebalancing process required for the NZ economy.

In terms of local data, September's National Bank Business Outlook provided something for everyone. Historically, it has proven to be an accurate bellwether for the state of the economy, with the decline in sentiment since May suggesting a slowing in economic momentum over the last few months. Broadly unchanged readings for sentiment despite the September 4 Canterbury earthquake highlight the resilience of the region and the likelihood of respectable growth rates for 2011. Nevertheless, the September survey contained a soft underbelly, with further declines in employment and investment intentions.

RBNZ GDP forecasts vs NBBO composite

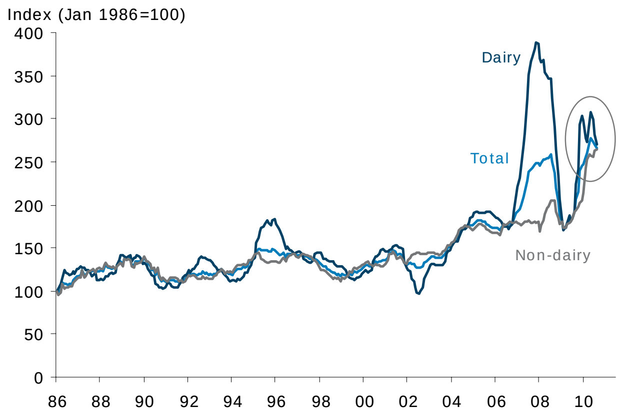


Sources: ANZ, National Bank, RBNZ, Statistics NZ

Last week's other data suggested that the economy remained stuck in low gear in Q3. The August merchandise trade data highlighted the importance of having a diversified export base. Weakness in commodity-based exports contributed to a large fall in exports to China, but this was partly offset by firming non-commodity exports, with exports to Australia and the US firming. The weakness in imports was consistent with an ongoing deleveraging environment confirmed by the soggy RBNZ credit aggregates. However, the lift in capital good imports to $617m was a clear positive, the first month this year they have cracked the $600m mark. Weak consent issuance for August was consistent with the spirit of the September MPS assessment. However, the real test for the RBNZ will be how the construction sector fares in 2011. By no means do we expect construction sector activity to be off to the races, but there are clear upside risks to the RBNZ forecasts for 2011.

This week's local calendar is relatively light. Today sees the September ANZ Commodity Price Index. As has been foreshadowed by the improving tone of recent *globalDairyTrade* auctions, we are likely to see improvement in dairy-related components. Other components will be closely watched as our view of a better 2011 is predicated on the broadening of export price strength.

NZ Commodity Price Indices (world currency terms)

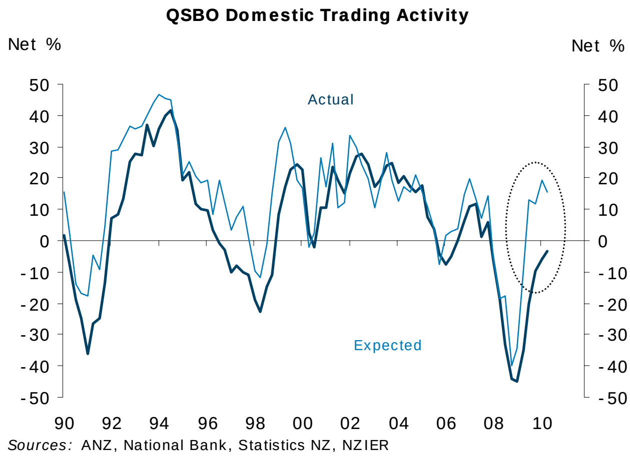


Sources: ANZ

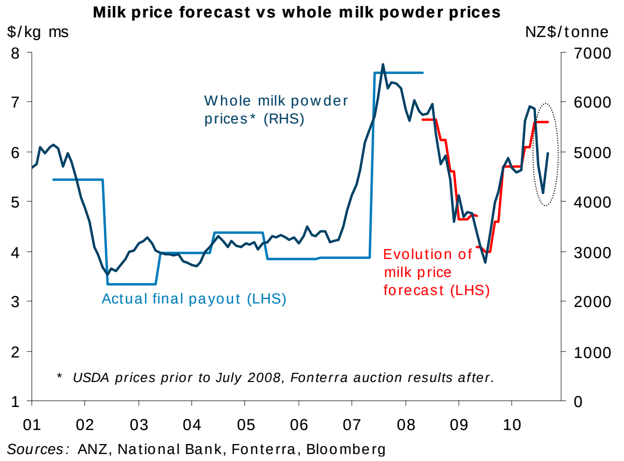
Tomorrow's QSBO is expected to mirror the spirit of recent readings of the National Bank Business Outlook. Of late we have seen an easing off in general business sector confidence in the National Bank survey, and we expect the QSBO to show a decline in the general business situation. In the QSBO a feature of late has been the widening gap between expected and experienced trading activity, with businesses proving over-optimistic regarding a return to business as usual. This gap is expected to narrow as the new reality of a softer than usual cyclical recovery starts to hit home. Pricing intentions are expected to firm on account of the October rise in GST, though the tough business climate will limit the extent of price increases. Profitability gauges are expected to continue worsening, which highlights the tough conditions being faced by corporate NZ. A feature of the last few QSBO outturns has been the difficulties being experienced by small and medium-sized enterprises.

ECONOMIC OVERVIEW

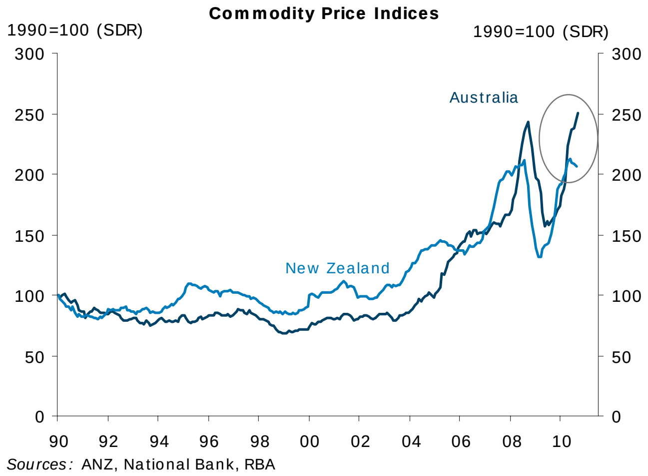
Nothing to date has suggested that things are starting to turn up for this sector.



Rounding off the week locally is the *globalDairyTrade* online auction. We expect the early October trading event to show some consolidation with whole milk powder averaging around the US $3,600 mark. This represents a 20 percent gain in two months but is still some way below the US $4,000+ readings in the June quarter.



We will also focus closely on offshore events, with tomorrow's RBA interest rate decision taking centre stage. Our Australian economists expect a 25 basis point hike, taking the cash rate to 4.75 percent, with the cash rate ending 2010 at 5 percent. Everyone now seems to have jumped on the October hike bandwagon. This effective tightening in Australian monetary conditions relative to New Zealand's largely reflects expectations of the Australian economy remaining in a sweet spot. The lucky country has been a major beneficiary of the structural shift to greater demand for commodities. But a by-product of a booming tradable sector is that growth needs to be sub-par somewhere else, especially when the economy is at full capacity. For now the growing interest rate divide will accentuate the tendency for the NZD/AUD to remain below 80 cents – and probably closer to 75 cents by year-end.



RECENT LOCAL DATA

- **Overseas Merchandise Trade – August 2010**. A monthly trade deficit of $437m was registered, with the annual trade surplus widening to $866m. Export values fell by a seasonally adjusted 2.8 percent (+15 percent y/y), with seasonally adjusted import values falling by 5.7 percent (+3.6 percent y/y).
- **RBNZ Credit Aggregates – August 2010.** Resident private sector credit ex repo was unchanged in August to be 0.4 percent higher than 12-months earlier. Household credit increased by a seasonally adjusted 0.1 percent in August (+ 2.2 percent y/y), with the annual growth in agricultural credit easing to 1.9 percent (2.3 percent y/y in July). Business credit declined by 6.6 percent compared to a year earlier.
- **SNZ Building Consents – August 2010**. The number of residential consents for new dwellings fell by 17.8 percent (-2.8 percent y/y), with the number of residential consents excluding apartments down by 8.9 percent (-2.4 percent y/y). The value of non-residential consents fell by 4.7 percent to $281m (-23 percent y/y).
- **National Bank Business Outlook – September 2010**. General business confidence fell 2 points, with a net 14 percent of respondents expecting improving general business conditions in 12 months time. Firms' own activity expectations rose by one point, to a net balance of 27 percent of firms expecting better times for their business. Employment and investment intentions for the coming year both eased to plus 1 and 2 percent respectively.

FOREIGN OWNERSHIP OF RURAL LAND

SUMMARY

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TAKING THE EMOTION OUT

In our travels around the country, we are constantly asked for our opinion on foreign ownership of New Zealand land. Like a lot of things, there are wider issues to think about when tackling the topic of foreign ownership. In this article, we outline the broader issues surrounding the debate and put it into perspective.

OBSERVATION 1: FOREIGN OWNERSHIP IS NOTHING NEW

There is always a fear that selling New Zealand assets to foreign investors will result in a ceding of control and a loss of sovereignty. Another common argument is that "selling the family jewels" will leave New Zealanders owning very little in their own country. A huge portion of New Zealand's comparative advantage resides in the land beneath our feet. The standard argument put forward is that the sale of it undermines the next generation's earning capacity, with the returns on the land accruing offshore as opposed to locally. You can see this easily through New Zealand's balance of payments figures showing net external debt rising from 70 percent of GDP in 1992 to 86 percent currently. Servicing that debt (either via interest payments or dividends that flow offshore) totals the princely sum of $9 billion in the latest 12-month period – a non-trivial sum that would of course be much better served if it was in our own pockets!

Foreign ownership in New Zealand is nothing new. As at 31 March 2010, the latest data available, total foreign investment stands at $289bn as compared to $75bn in 1992. Of that, $92bn is in direct investment – of which half is owned by Australians. The second largest foreign direct investors in New Zealand are the Americans, with the Dutch third on the list. At the same time New Zealand has $128bn of offshore investment.

Total foreign investment in New Zealand (as at 31 March 2010)

Country	Direct Investment		Portfolio and Other		Total Investment	
	$bn	%	$bn	%	$bn	%
Australia	47	51.2	53	26.8	100	34.6
UK	4	3.9	46	23.2	49	17.0
USA	11	11.5	38	19.2	48	16.7
Japan	2	2.3	4	2.1	6	2.2
Netherlands	4	4.2	0	0.1	4	1.4
Hong Kong	1	1.2	3	1.3	4	1.3
Singapore	2	1.7	2	1.1	4	1.3
Switzerland	0	0.2	2	0.9	2	0.7
Germany	1	0.8	1	0.4	2	0.5
Other	21	22.9	49	24.9	70	24.2
Total	**92**	**100**	**196**	**100**	**289**	**100**

Sources: ANZ, National Bank, Statistics New Zealand

By sector, foreign investment is most concentrated in the financial and insurance services sector, which account for around 58 percent of the total. Most of this is channelled by the banking system into housing. Or put another way, New Zealanders have an insufficient local savings pool to meet our borrowing demands and the balance is provided by offshore investors with banks acting as the intermediary. Foreign investment in the manufacturing sector is the second largest, accounting for almost 8 percent of the total. **The amount of foreign investment in New Zealand's agricultural sector is actually very small, at $5.0bn or around 1.6 percent of total foreign investment.**

Of course, most of the recent controversy has been about rural land sales, as opposed to other forms of asset sales. New Zealand's total arable and grazing land is currently estimated to be around 11.3 million hectares. How much rural land is in foreign hands is difficult to know. Data from the Overseas Investment Office (OIO) shows that since 2005, there have been 772 approvals for 1.2 million hectares of gross land (of which around a third actually went into foreign ownership). Over 80 percent of this was for forestry land. Actual freehold grazing and arable land approved for sale by the OIO since 2005 was 70,800 hectares, or around 0.6 percent of New Zealand's total grazing and arable land. A further 109,400ha of non-freehold land was

FOREIGN OWNERSHIP OF RURAL LAND

approved for sale by the OIO, taking the total to 1.6 percent of total grazing and arable land.

OIO Land Sale Consents			
Calendar Year	No. of Approvals	Net land area ('000 ha)	Gross land area ('000 ha)
2005	174	52.0	166.1
2006	145	270.5	397.0
2007	125	16.6	90.4
2008	126	38.7	70.6
2009	156	32.2	364.8
2010 YTD	46	18.0	112.4

Sources: ANZ, National Bank, Overseas Investment Office

Note: Net land area represents the total land area proposed to be transferred into foreign ownership, while gross land area is what has been consented. For example, a 50:50 joint venture between a New Zealand owned and foreign owned company that purchases 100 hectares mean that the gross land area approved is 100, while the net land area is only 50.

The bottom line is that the size of rural land sales to foreign investors is a very small proportion of both the total sales to date and New Zealand's total rural land area. This is not meant to trivialise the issue but rather to put it in perspective. **Of course, the real issue is that such effects accumulate over time,** so if you add up the hectares sold over a number of years you start getting into some chunky numbers. This in itself highlights a key issue. Discrete one-off purchases or intra-year movements are by-and-large irrelevant. **The real issue is the emergence of such sustained trends over time and when monitoring trends you need to fully understand what factors are driving them.**

OBSERVATION 2: DO WE NEED THEM MORE THAN THEY NEED US?

The current debate seems to be premised with the starting assumption that foreign owners are ultimately "bad" for New Zealand. This argument suffers from four misconceptions or inconsistencies.

- **Statistical and empirical evidence generally points to foreign direct investment bringing substantial economic benefits**. This can manifest itself in areas such as opening up markets and introducing capital and expertise, innovation and knowledge. Indeed, a Treasury paper noted that "without the capital inflow over past decades, the combined saving of the private and public sectors would have implied less investment and hence lower real output growth."[1] The Institute for International Economics note that foreign direct investment tends to be particularly beneficial if it is integrated into the global supply network, while those oriented towards protected domestic markets tend not to be beneficial[2]. While the World Bank has recently backed the practice of countries selling large tracts of agricultural land to overseas investors, this has a caveat, namely, host countries need to demand much more from investors to increase farming productivity and people's livelihoods.

- **New Zealand has hardly been a beacon of responsibility in regard to certain investment activities.** We have little time for some of the xenophobia that has emerged in certain pockets and the broad characterisations of foreign investors. Certainly New Zealand has a huge interest in ensuring foreign direct investment adds value to the country and the benefits are not simply directed offshore. But New Zealand must be wary of applying a double standard in regard to how offshore investors are viewed relative to what we've seen locally. Let's not forget that the 61 finance companies that have gone under or are under moratorium since 2006, affecting around $8.5 billion worth of deposits to 240,000 depositors, were all proudly New Zealand owned and operated. Just as we shouldn't tar all New Zealanders with the poor and irresponsible activities of a few, nor should we be making generalisations about all foreign investors being "bad".

- **It ignores the basic reality check, namely our poor savings culture.** The main reason New Zealand needs foreign capital is because as a country we do not save enough to fund all our investment needs. The last time we ran an annual current account surplus was in 1973. We have been in the red ever since! Hence, we have had to borrow or sell assets in order to balance the books. Financing our current account deficit can broadly take place via debt and / or equity (i.e. selling off assets). Up till the past year or so most of the financing of the current account deficit has taken place via borrowing. Of course in the aftermath of the global financial crisis, the implicit cost of debt has risen. For rural readers think about your margin! Realistically this is

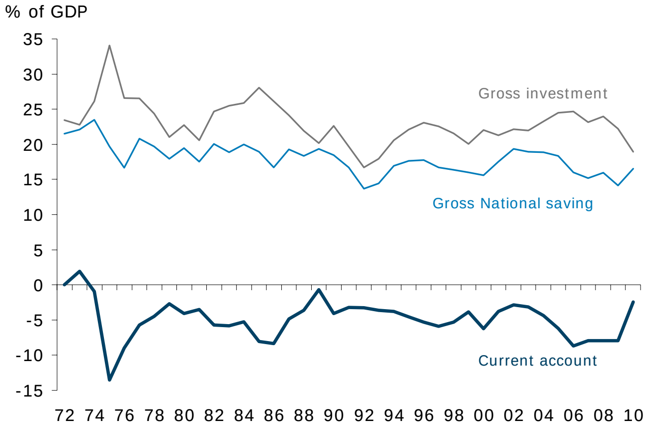
[1] Makin A, Zhang, W and Scobie G (July 2008) "The contribution of foreign borrowing to the New Zealand economy", Treasury Working Paper 08/03.

[2] Moran T, Graham E, Blomstrom, M (May 2005) "Does foreign direct investment promote development?", Institute for International Economics.

FOREIGN OWNERSHIP OF RURAL LAND

likely to make it even more attractive to start financing a bigger portion of our current account deficit via equity or selling off assets. But if we fix the current account deficit (i.e. save more) suddenly we become net accumulators of assets as opposed to liabilities.

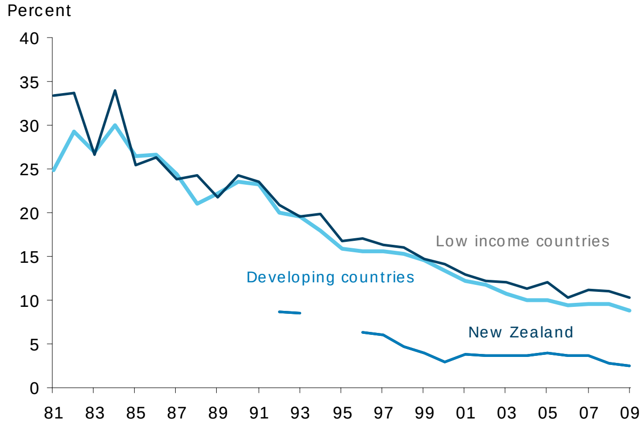
National saving-investment position (March years)



Sources: ANZ, National Bank, Statistics NZ

- **New Zealand is a huge beneficiary of trade liberalisation and the breaking down of trade barriers. Hence it would be somewhat ironic to be putting up non-tariff barriers in relation to restricting capital flows or taking an aggressive stance in spirit.** Of course the world is not a fair place in regard to trade. But over time things have moved in New Zealand's direction, with the signing of a number of free trade agreements that have brought tremendous economic benefit of late. We have been staunch supporters of free trade and the principles behind it, leading from the front. Some would say we're too far in front but we won't get into that debate. The real issue is one of consistency. If New Zealand is truly going to stand tall in its pursuit and arguments with other nations in regards to trade liberalisation, we can't really be seen to be breaking down barriers with one hand but erecting them with another. One of the key risks the global economy faces over the coming years stems from rising protectionism, and not necessarily in relation to traditional trade barriers such as tariffs. Non-tariff barriers have also become a frequently used tool.

Average tariff rates



Sources: ANZ, National Bank, World Bank

OBSERVATION 3: IT IS NOT A FREE-FOR-ALL FOR FOREIGN INVESTORS

New Zealand has rather liberal foreign investment rules, but that does not mean that it is a free for all. With respect to land sales, OIO approval is required before a foreign investor can purchase sensitive land, which is any non-urban land greater than 5 hectares, and where foreign ownership or control is greater than 25 percent. This applies to freehold purchases, leases and crown pastoral leases. The foreign purchaser will need to:

- demonstrate financial commitment, business experience and acumen relevant to the investment;
- be of good character and meet visa/permit criteria related to the Immigration Act (i.e. no criminal record etc);
- show that the investment benefits New Zealand - in particular, the creation and retention of New Zealand jobs, introduction of new technology or business skills, increased export revenue, greater productivity, more value-add to primary products and protect or enhance environmental/amenity values of the investment; and
- show that the relevant land has been offered for acquisition on the open market to persons who are not overseas persons.

Once consent has been granted, the OIO may require the purchaser of the land to provide information for compliance monitoring purposes. So it is not a case of foreign investors doing whatever they please.

This means that foreign investors have a much higher hurdle to climb over compared to local investors. Like most regulatory regimes there are of course limitations and "blind" spots. But as a general proposition the framework appears to work well.

FOREIGN OWNERSHIP OF RURAL LAND

On top of this we now have new rules which effectively tighten the criteria further. While the Overseas Investment Act will not be changed, government ministers will now have the power to veto overseas investment applications. The criteria for approval will be a new "economic interest" factor allowing ministers to consider whether economic interests are adequately safeguarded and whether the investment provides opportunity for New Zealand participation, oversight or involvement. These new rules effectively extend the existing regime but include a more direct political element. In many ways it's akin to having a single decision maker in regard to Monetary Policy (i.e. the Governor) as opposed to a full voting committee with published minutes. It works well while you have someone of high quality in place. But there are no guarantees forever. As the Svennson Report on the New Zealand monetary policy Framework noted in 2001: "Another Governor may not cope as well with the pressure, criticism and even abuse that seem to go with the territory, and may, in difficult times and under high pressure, lose confidence and let policy go awry in a number of different ways".

In regard to the changes, the political breeze is certainly blowing towards a more interventionist stance. The government have made the first move, and the opposition look set to take an even more stricter tone. **We won't go into the relative merits of the response but will restrict our attention to two comments.**

Firstly, a typical condition for government intervention is normally centred around what economists refer to as a market failure of some description. Although sales volumes are very low at present, with apparent tensions between buyers and sellers, this is not evidence of market failure but is typical of the market at this stage of the cycle.

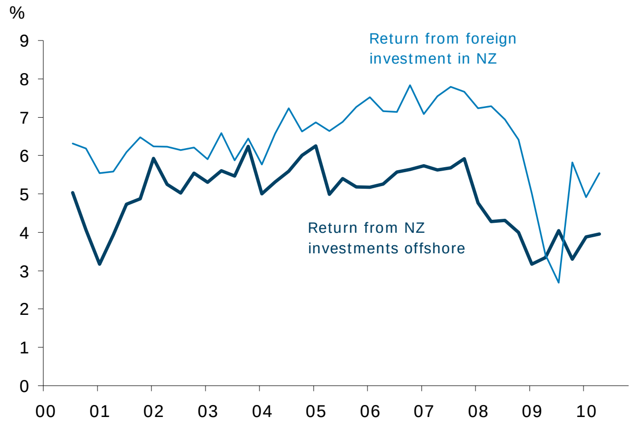
Second, any intervention needs to be counter-balanced by proactive steps on the savings and investment front. Indeed, the more restrictive any proposed foreign direct investment framework, the more imperative there is for a savings policy to fill the void. It is simply untenable to put up proposals that restrict foreign ownership and not have the appetite to address our national saving shortfall. Last time we looked there was limited political consensus or appetite for compulsory savings. If we restrict foreign ownership and don't address our savings shortfall, NZ's living standards will suffer.

OBSERVATION 4: WE ARE FOREIGN INVESTORS TOO

Too often, the debate around foreign ownership ignores the other side of the equation. We too are foreign investors, increasingly accumulating assets abroad. As at 31 March 2010, New Zealand investors have $128bn invested overseas, of which $21bn is in direct investment (mostly in Australia). This pales in comparison to the amount that foreign investors own in New Zealand, but the gap between the two largely reflects our poor savings rate.

In addition, we are not giving stuff away for free. A New Zealand resident receives the proceeds from any sale of assets or rural land to foreigners. It is what they decide to do with the proceeds that matters more. The "seller" can pay down debt, spend it, or re-invest in other areas (either domestically or offshore) that can generate a future income stream. Judging from our long running track record of running current account deficits, it seems that a decent portion of that gets spent.

Annualised rate of return from investment income



Sources: ANZ, National Bank, Statistics NZ

A bigger issue – and one that does not rate much of a mention – is how we are managing our foreign investments. The returns from our offshore investment have tended to be less than the rate that foreign investors have been able to generate from their investments in New Zealand. That is, not only do we not save enough, whatever savings we do have that are invested overseas tends to generate inferior returns. Whereas foreigners appear to get the cash cows, we've had a track record of picking up the dogs with fleas. If the returns on New Zealand assets overseas had been equal to those generated by foreign-owned New Zealand companies, the amount of income we got from offshore would have been higher by around $2bn a year and the current account deficit down by around 1 percent of GDP each year. When cumulated

FOREIGN OWNERSHIP OF RURAL LAND

over 20 years you are talking about a huge change in the stock of external debt, or the amount of assets we would hold relative to liabilities.

Indeed, if the rate of return on NZ-held offshore investments had matched local returns to foreigners, since 2000, New Zealand would find itself $14.7 billion better off. On top of this the additional income from this would have been cumulatively worth $3.9 billion (assuming the same return as foreigners get on NZ assets). To put this in perspective NZ.Inc could now hold offshore the equivalent of:

- Two to three of the major local banks; or
- The market capitalisation of the six largest listed companies in the New Zealand share market; or
- Fifty percent of the entire market capitalisation of the New Zealand share market; or
- Land equivalent to the entire Southland farming region.

Such simple calculations highlight the importance of relative returns but also how quickly low returns or poor investment decisions can spiral into significant sums. Moreover, these calculations only start from 2000.

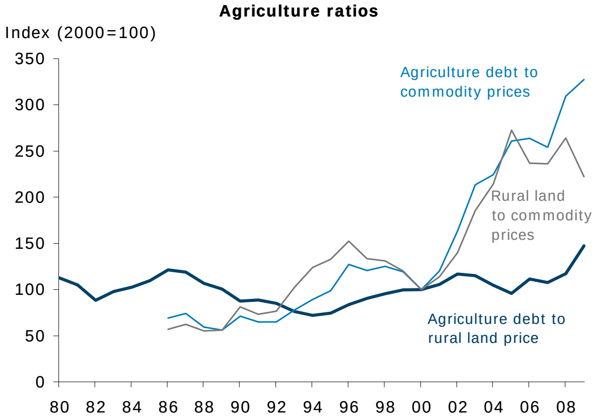
OBSERVATION 5: THERE ARE OTHER ISSUES TO THINK ABOUT

The issue of rural land sales to foreigners probably would not be controversial if there were locals with deep pockets willing to pay top dollar. However, unless we see a quick and immediate turnaround in New Zealand's savings behaviour, it is highly unlikely there is the domestically sourced pool of cash to fill this void. Moreover, the rural property market remains in a Mexican stand-off with values still looking at odds with underlying yields and this is keeping locally sourced cash on the sidelines – for the time being. That is not to say buyers are not around, rather that they're being selective.

Long-term prospects for agriculture look extremely promising. It has become clear that commodity prices have shifted to a higher structural plane. Global investor funds are naturally looking at agriculture as an emerging secular investment theme. We concur with this.

The trick will be unlocking agriculture's medium-term value. At this stage, valuations still look stretched. Rural land prices have risen strongly since 1990 by almost 400 percent in nominal terms. Over that time, growth in agriculture debt has been faster at 720 percent, while commodity prices have seen only an 80 percent increase. In effect, not only has the increase in commodity prices been capitalised into land prices, so has a lot of the expected future increases in commodity prices. The results are extended valuations.

Unlocking medium-term value requires a range of dynamics. These are issues such as reassessing the supply and production chain, getting greater linkages with the rapidly growing Asian market, re-examining ballooning cost structures (and central / local government is not helping here at all), consolidation in some instances, product transformation and further value-add, investment off-shore to service larger markets 365 days of the year, new on-farm productivity innovations and widespread adoption and sensible policy settings by local and central government for key areas such as the environment and infrastructure, and the list goes on. Foreign direct investment can help in a number of these areas, but it is not a magic bullet. There are many local challenges (and opportunities) to deal with.



Sources: ANZ, National Bank, RBNZ, QV

We would not underestimate the role that demographics will play going forward. The farming community is ageing. How does the seller extract maximum value, while at the same time potentially ensuring the likes of family interests continue? Over time we are going to have to see different ownership structures and transition models put in place. Such dynamics are going to complicate the picture further but are essential if the transition of knowledge and wealth creation from generation to generation is going to take place in a seamless fashion. The picture is further complicated when you consider the sectoral knowledge and skills that have been built up over decades. How this institutional skill-base is preserved will be a key challenge going forward.

FOREIGN OWNERSHIP OF RURAL LAND

THE UPSHOT

We have a natural parochial bias in supporting local ownership of New Zealand's comparative advantage, particularly given the long-term positive prospects for agriculture (subject to current valuation hiccups).

But such parochialism needs to be measured and read in conjunction with numerous reality checks. Foreign direct investment can bring huge economic benefits. The argument that foreign ownership is "bad" for New Zealand lacks robust evidence. At the heart of the issue is New Zealand's reliance on foreign savings, and our poor relative investment returns. Fix these and the issue of foreign ownership becomes secondary. New Zealand is making progress in this regard, but we are set for a long journey. New Zealanders apply a very high discount rate to saving, preferring the joys of consumption today over investing for tomorrow. The famous "evangelist" Freddie Mercury put it more succinctly: "I want it all, and I want it now". Changing this attitude is not going to happen overnight. But until we do, a portion of New Zealand's capital stock will steadily be accumulated by investors offshore who prefer the joys of investing over the immediate sugar fix of today's consumption.

With the political breeze clearly favouring more restrictive foreign ownership rules, the onus is on the government to balance that with a more proactive stance towards savings. In the absence of such countering forces, more direct restriction of foreign direct investment will only leave NZ poorer.

INTEREST RATE STRATEGY

SUMMARY

NZ interest rates continue to grind lower, and are approaching the year's lows again, spurred on by weak domestic data and global developments. Since the MPS, the rally in swap rates has been uniform across the curve. However, with no more rate hikes priced in for 2010, and just 1.5 hikes priced in by June 2011, scope for lower short end rates seems limited, especially with the RBA set to hike tomorrow. But the long end is a different story, with further quantitative easing (QE) in the US likely to see rates grind lower over the remainder of the quarter and remain somewhat anchored.

MARKET THEMES

- QE remains the major theme dominating global rates markets. New York Fed President (and FOMC Vice Chairman) Dudley upped the ante on Friday, saying he favours more action to rectify the "unacceptable" outlook.
- But the contrast with the RBA outlook couldn't be bigger, with a rate hike tomorrow on the cards, with another hike in November if the dataflow remains upbeat (with emphasis on Q3 CPI).
- Markets are likely to reconcile these cross-currents via a flattening of the curve. The more accommodative the Fed, the less accommodative the RBNZ needs to be.

REVIEW AND OUTLOOK

Last week's domestic data added to the long list of sub-par economic statistics, which continue to be heavily influenced by caution and deleveraging, and have gone a long way to validate the RBNZ's change of heart. Not surprisingly, interest rates continued to edge lower. But it wasn't just local news spurring the market along – **the market has also been heavily influence by US interest rates, which continue to grind lower. QE remains at the heart of the conversation** in the US bond market, and with the Fed doing little to dissuade the market that further QE is likely, attention has turned away from when, rather than if the Fed do it, and what form it will take. Until Friday, all we had was Bernanke's commitment to do more if the need arose, and a FOMC with the door open to possibly do more. Enter NY Fed President Dudley, noting that the outlook was "unacceptable", with further action "warranted". Strong words – and **if the Fed follows through, the impact will be felt in NZ** – that's why we keep talking about it.

But it's not all doom and gloom – in fact, Australia is humming, with **the RBA poised to hike tomorrow. In our view this will hone the focus on the NZ outlook**, especially now that the market is pricing a rate profile well below even the RBNZ's low rate profile. The upshot – **there is some upside risk to short end rates, in contrast to the long end**.

PREFERRED BORROWING STRATEGIES

Strategic calls at this juncture are extremely difficult, courtesy of the unusual interest rate environment we are in. Indeed, although we believe interest rates are too low relative to traditional fundamentals, there are good reasons for it. This offers potential opportunities for borrowers, but as always, hedging is about risk management. Although unusually low rates may appear to be attractive and potentially argues for higher hedge ratios; don't lose sight of other uncertainties and the value of flexibility. Indeed, the fact that the Fed is contemplating QE suggests there are grave concerns for the US economy, and this has implications for NZ. Our preferred strategy is to add progressively to hedges as rates ratchet lower, leaving a good amount of powder dry in anticipation of a formal announcement from the Fed. Although US rates have fallen substantially already in anticipation of further QE, confirmation will see them move even lower.

GAUGES FOR NZ INTEREST RATES

GAUGE	DIRECTION	COMMENT
RBNZ / OCR	↔	On hold till March 2010.
NZ data	↔	Last week's credit, building permits, confidence all soft.
Fed Funds / front end	↔/↓	NY Fed President Dudley hinting at further QE.
RBA	↔/↑	Rate hike tomorrow, but what about November?
US 10 year	↔/↓	Will remain pinned down by threat of further QE.
NZ swap curve	↔/↓	Biased to flatten as long end follows US rates.
Flow	↔/↓	Very light flow. No paying.
Technicals	↔/↓	Downward momentum.

MARKET EXPECTATIONS FOR RBNZ OCR (BPS)

OCR DATES	LAST WEEK	THIS WEEK
Thu 28-Oct-10	+0	+0
Thu 9-Dec-10	+6	+2
Thu 27-Jan-11	+7	+6
Thu 10-Mar-11	+19	+16
Thu 28-Apr-11	+31	24
Thu 9-Jun-11	+39	+37
Thu 28-Jul-11	+48	+44

TRADING THEMES WE FAVOUR AT PRESENT

This week's event risk looks set to be schizophrenic, with a likely RBA rate hike tomorrow set to skew rates higher, and Friday's US non-farm payrolls set to deepen arguments for further QE. Tactically, we favour adding duration on yield backups, looking for a move to new lows. Bond demand continues to improve, and should help swap spreads continue to normalise from recent negative extremes.

CURRENCY STRATEGY

SUMMARY

The dominant feature last week was the sight of QE2 on the horizon and edging towards port. It should be noted that the result has been *specific USD weakness* rather than *general "other currency" strength.* The US is winning the "competitive devaluation" race at the moment. NZD/AUD near 10 year lows leaves little scope for further depreciation there. The RBA on Tuesday will provide the next clues.

MARKET THEMES

- The increased prospect of QE2 from the US is driving the USD lower.
- The NZD/AUD had a look below 0.7600 but from a long term perspective it just looks too cheap down there.
- For EUR, USD weakness vs peripheral Europe problems, USD weakness wins.
- BoJ continues to fight a lonely fight and one that currently feels un-win-able.

REVIEW AND OUTLOOK

The NZD is being pushed around by external factors with little domestically to focus on. QE2 induced USD weakness is driving the NZD higher. However, technically, the NZD is at a critical juncture. Key resistance at 0.7440 has been tested over the last 24 trading hours. A convincing break sees the next resistance at 0.7525, then 0.7635. Coincidentally the break of 0.7440 brings into play a major head and shoulders bottom with a 1st target of 0.7832 and the 2nd target at 0.8224. One caveat – we need to give respect to the trading range we have been in for the last year. There have been a number of times during the past year where the NZD has looked set to break higher but failed. This time the prospect looks a little more certain, but "handle with care".

Despite more problems for peripheral Europe, the EUR is benefiting from the QE2 induced USD weakness. Bond spreads for the PIIGS continue to widen as the ratings agencies are busy downgrading. But USD weakness is winning out, driving the EUR higher.

NZD/AUD continues to be under some pressure as AUD gains more benefit than NZD from USD weakness. However some market chatter that the RBA may pause this month or next, together with the fact the NZD/AUD is near 10 year lows, suggests there is probably limited downside from here for the time being.

JPY has recovered all its losses since the BOJ intervened a couple of weeks ago. As we approach the previous intervention level, market nervousness will build and trading will become skittish. While we can expect to see the BoJ again at or (more likely) just below that previous level, any impact will only be temporary.

NZD VS AUD: MONTHLY DIRECTIONAL GAUGES

GAUGE	DIRECTION	COMMENT
Fair value	↔/↑	Under fair value now but not that far off.
Yield	↔/↓	RBA locked and loaded. RBNZ on hold till next year.
Commodities	↔	Soft commodities performing better, lending support to NZD.
Partial indicators	↓	Australian data outperforming NZ's.
Technicals	↔	Oversold. Looking for bounce to just above 0.78.
Sentiment	↔	Everyone bullish AUD.
Other	↑	At historically low levels.
On balance	↔	**Range trade 0.7650-0.7830.**

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 happy with weaker USD.
Commodities	↔/↑	Remain supportive overall.
Risk aversion	↔	Equities still relevant.
Partial indicators	↔/↓	NZ data still largely disappointing.
Technicals	↔/↑	Strong support above 0.7350, targeting break of 0.7450 resistance.
AUD	↑	Everyone bullish AUD.
Sentiment	↑	"New world/old world" theme shifting NZD sentiment toward Australia/Asia.
Other	↔	Domestic data weak but Fonterra news positive.
On balance	↔/↑	**Remains overall supported with rising base.**

DATA EVENT CALENDAR

DATE	COUNTRY	DATA / EVENT	MKT.	LAST	NZ TIME
4-Oct	JN	Monetary Base (YoY) - SEP	- -	- -	12:50
	AU	TD Securities Inflation MoM% - SEP	- -	- -	13:30
	AU	TD Securities Inflation YoY% - SEP	- -	- -	13:30
	JN	Labor Cash Earnings YoY - AUG	0.70%	0.70%	14:30
	NZ	ANZ Commodity Price - SEP	- -	- -	15:00
	EC	Sentix Investor Confidence - OCT	8	8	21:30
	UK	PMI Construction - SEP	51.4	51.4	21:30
	EC	Euro-Zone PPI (MoM) - AUG	0.20%	0.20%	22:00
	EC	Euro-Zone PPI (YoY) - AUG	3.60%	3.60%	22:00
5-Oct	US	Factory Orders - AUG	-0.40%	-0.40%	03:00
	US	Pending Home Sales MoM - AUG	2.80%	2.80%	03:00
	US	Pending Home Sales YoY - AUG	0.90%	0.90%	03:00
	NZ	NZIER Business Opinion Survey - 3Q	- -	- -	/2010
	AU	AiG Performance of Service Index - SEP	- -	- -	11:30
	AU	Trade Balance - AUG	2300M	2300M	13:30
	AU	ANZ Job Advertisements (MoM) - SEP	- -	- -	13:30
	AU	Retail Sales s.a. (MoM) - AUG	0.40%	0.40%	13:30
	CH	China HSBC Services PMI - SEP	- -	- -	15:30
	AU	RBA CASH TARGET - OCT	4.75%	4.75%	16:30
	JN	BOJ Target Rate - OCT	0.10%	0.10%	/2010
	GE	PMI Services - SEP F	54.6	54.6	20:55
	EC	PMI Composite - SEP F	53.8	53.8	21:00
	EC	PMI Services - SEP F	53.6	53.6	21:00
	UK	PMI Services - SEP	51	51	21:30
	EC	Euro-Zone Retail Sales (MoM) - AUG	0.20%	0.20%	22:00
	EC	Euro-Zone Retail Sales (YoY) - AUG	1.30%	1.30%	22:00
6-Oct	US	ISM Non-Manf. Composite - SEP	52	52	03:00
	UK	BRC September Shop Price Index			12:01
	EC	Euro-Zone GDP s.a. (QoQ) - 2Q F	1.00%	1.00%	22:00
	EC	Euro-Zone GDP s.a. (YoY) - 2Q F	1.90%	1.90%	22:00
	GE	Factory Orders YoY (nsa) - AUG	17.20%	17.20%	23:00
	GE	Factory Orders MoM (sa) - AUG	0.90%	0.90%	23:00
7-Oct	US	Challenger Job Cuts YoY - SEP	- -	- -	00:30
	US	ADP Employment Change - SEP	23K	23K	01:15
	AU	Employment Change - SEP	20.0K	20.0K	13:30
	AU	Unemployment Rate - SEP	5.10%	5.10%	13:30
	AU	Part Time Employment Change - SEP	- -	- -	13:30
	AU	Full Time Employment Change - SEP	- -	- -	13:30
	AU	Participation Rate - SEP	65.40%	65.40%	13:30
	UK	Industrial Production (MoM) - AUG	0.20%	0.20%	21:30
	UK	Industrial Production (YoY) - AUG	4.10%	4.10%	21:30
	GE	Industrial Prod. YoY (nsa wda) - AUG	9.80%	9.80%	23:00
	GE	Industrial Production MoM (sa) - AUG	0.50%	0.50%	23:00
8-Oct	UK	BOE Asset Purchase Target - OCT	200B	200B	00:00
	UK	BOE Announces Interest Rates - OCT	0.50%	0.50%	00:00
	EC	ECB Announces Interest Rates - OCT	1.00%	1.00%	00:45
	US	Initial Jobless Claims – Oct 2	450K	450K	01:30
	US	Continuing Claims – Sep 25	4450K	4450K	01:30

Continued on following page

DATA EVENT CALENDAR

DATE	COUNTRY	DATA / EVENT	MKT.	LAST	NZ TIME
	JN	Current Account Total - AUG	¥1023.0B	¥1023.0B	12:50
	AU	Foreign Reserves - SEP	- -	- -	18:30
	GE	Exports SA (MoM) - AUG	-0.30%	-0.30%	19:00
	GE	Imports SA (MoM) - AUG	0.40%	0.40%	19:00
	GE	Current Account (EURO) - AUG	0.40%	0.40%	19:00
	UK	PPI Input NSA (YoY) - SEP	0.40%	0.40%	21:30
	UK	PPI Output n.s.a. (YoY) - SEP	0.40%	0.40%	21:30
	UK	PPI Output Core NSA (YoY) - SEP	0.40%	0.40%	21:30
9-Oct	US	Change in Nonfarm Payrolls - SEP	0.40%	0.40%	01:30
	US	Change in Private Payrolls - SEP	0.40%	0.40%	01:30
	US	Unemployment Rate - SEP	0.40%	0.40%	01:30
	US	Avg Hourly Earning MOM All Emp - SEP	0.40%	0.40%	01:30
	US	Avg Hourly Earning YOY All Emp - SEP	0.40%	0.40%	01:30
	US	Avg Weekly Hours All Employees - SEP	0.40%	0.40%	01:30
	US	Wholesale Inventories - AUG	0.40%	0.40%	03:00

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: Last week's dataflow was light, with building consents and the trade data showing the economy is still in idle-mode. The National Bank *Business Outlook* for September did not show a perceptible impact of the Canterbury earthquake on business sentiment after broadly unchanged readings for overall consumer sentiment in September. The RBNZ credit aggregates also illustrated that the economy is still in deleveraging mode. This week's QSBO is expected to show the reality of sluggish growth dawning on businesses. New Zealand commodity price data will provide an update of a key support to economic activity. 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 near-term activity.

DATE	DATA/EVENT	ECONOMIC SIGNAL	COMMENT
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 Canterbury 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 consolidation of whole milk powder prices at around the $3,600 mark.
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 modest increase in August retail sales, though no signs of a pre-GST spend-up are likely to show up in the data. Households continue to focus on repairing balance sheets.
Mon 18 Oct (10:45am)	Consumers Price Index – Q3	High and low	Boosted by ETS related charges and large increases in motor vehicle registration and licensing fees, we expect a quarterly increase in the CPI of 1.1 percent. Annual CPI inflation should ease to 1.6 percent.
Thur 21 Oct (10:45am)	International Travel and Migration – Sep	Up and down	A small net monthly PLT inflow is expected, with a risk of a larger than expected pick-up in departures – especially to Australia. We will be on the lookout for any tourism disruption in the visitor arrivals number arising from the Canterbury earthquake.
Fri 29 Oct (10:45am)	Overseas Merchandise Trade - Sep	Still in the red	A monthly deficit in the region of $500m is expected, with the annual trade deficit expected to remain close to $900m.
Fri 29 Oct (10:45am)	Building Consents - Sep	Up	After the sharp fall in August issuance a pullback of sorts is expected. Earthquake related disruptions could be influential.
On Balance			**August data mixed but activity and confidence data for Q3 and Q4 may be subdued.**

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)	0.2	1.0	0.5	0.2	**0.4**	**0.5**	**1.2**	**1.4**	**1.6**	**0.5**
GDP (% yoy)	-1.6	0.5	1.9	1.9	**2.1**	**1.6**	**2.3**	**3.5**	**4.8**	**4.8**
CPI (% qoq)	1.3	-0.2	0.4	0.3	**1.1**	**2.8**	**0.6**	**1.0**	**0.8**	**0.5**
CPI (% yoy)	1.7	2.0	2.0	1.8	**1.6**	**4.6**	**4.8**	**5.6**	**5.3**	**3.0**
Employment (% qoq)	-0.8	0.0	1.0	-0.3	**0.5**	**0.4**	**0.6**	**0.7**	**0.6**	**0.4**
Employment (% yoy)	-1.8	-2.4	-0.1	0.0	**1.3**	**1.6**	**1.2**	**2.2**	**2.3**	**2.3**
Unemployment Rate (% sa)	6.5	7.1	6.0	6.8	**6.6**	**6.4**	**6.1**	**5.7**	**5.5**	**5.4**
Current Account (% GDP)	-3.2	-2.8	-2.4	-3.0	**-3.7**	**-3.0**	**-3.1**	**-3.0**	**-3.1**	**-3.1**
Terms of Trade (% qoq)	-1.6	5.8	6.1	2.0	**3.0**	**1.0**	**-0.5**	**-0.7**	**0.0**	**-1.0**
Terms of Trade (% yoy)	-14.1	-8.2	0.1	12.7	**17.9**	**12.5**	**5.6**	**2.7**	**-0.2**	**-2.1**

	Dec-09	Jan-10	Feb-10	Mar-10	Apr-10	May-10	Jun-10	Jul-10	Aug-10	Sep-10
Retail Sales (% mom)	-0.4	0.7	-0.6	0.5	-0.3	0.4	1.0	-0.4	..	..
Retail Sales (% yoy)	2.0	2.3	2.4	4.4	2.7	1.9	3.4	2.2	..	..
Credit Card Billings (% mom)	-1.2	1.7	-0.2	0.8	-1.7	1.9	1.0	-1.3	0.5	..
Credit Card Billings (% yoy)	1.9	2.6	1.1	5.2	0.8	3.4	4.5	2.6	2.0	..
Car Registrations (% mom)	6.8	-0.6	0.4	5.2	2.9	-3.8	5.6	-6.4	-0.2	..
Car Registrations (% yoy)	0.3	15.9	31.4	31.7	40.5	30.5	35.8	16.0	19.0	..
Building Consents (% mom)	-3.7	-2.7	6.1	-0.3	8.5	-9.2	3.3	3.2	-17.8	..
Building Consents (% yoy)	22.7	35.4	29.9	33.3	32.0	11.1	27.9	26.5	-3.0	..
REINZ House Price (% yoy)	9.6	7.7	6.1	7.6	4.7	3.7	3.7	2.6	0.9	..
Household Lending Growth (% mom)	0.2	0.2	0.1	0.1	0.2	0.2	0.2	0.2	0.1	..
Household Lending Growth (% yoy)	2.7	2.7	2.7	2.8	2.7	2.5	2.5	2.3	2.2	..
ANZ-Roy Morgan Consumer Confidence	118.6	131.4	123.6	121.8	121.9	126.0	122.0	115.6	116.3	116.4
NBNZ Business Confidence	38.5	..	50.1	42.5	49.5	48.2	40.2	27.9	16.4	13.5
NBNZ Own Activity Outlook	36.9	..	41.9	38.6	43.0	45.3	38.5	32.4	25.7	26.7
Trade Balance ($m)	-26	271	328	608	660	765	214	-186	-437	..
Trade Balance ($m annual)	-549	-176	-330	-160	178	37	581	573	866	..
ANZ World Commodity Price Index (% mom)	2.5	0.3	3.7	1.8	5.1	1.2	-1.6	-0.8	-1.4	..
ANZ World Commodity Price Index (% yoy)	30.4	36.7	48.6	49.5	53.2	51.8	50.1	47.3	38.6	..
Net Migration (sa)	1700	1850	1000	960	770	350	230	880	840	..
Net Migration (annual)	21253	22588	21618	20973	19954	17967	16504	15221	14507	..

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	0.744	0.710	0.720	0.734	0.730	0.720	0.710	0.700
NZD/AUD	0.802	0.785	0.765	0.755	0.750	0.753	0.760	0.766	0.755	0.795
NZD/EUR	0.556	0.551	0.540	0.568	0.600	0.612	0.608	0.610	0.602	0.583
NZD/JPY	62.78	58.86	61.98	60.35	62.64	65.33	67.16	67.68	69.58	70.00
NZD/GBP	0.463	0.455	0.471	0.461	0.465	0.474	0.471	0.462	0.449	0.432
NZ$ TWI	67.5	65.5	66.6	66.1	67.7	69.1	69.2	69.1	68.5	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	3.17	3.30	3.70	4.20	4.30	4.70	5.20	5.50
NZ 10-yr bond	5.33	5.13	5.04	5.20	5.30	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	4.88	5.30	5.60	6.00	6.00	6.20	6.10	6.10

	1 Sep	27 Sep	28 Sep	29 Sep	30 Sep	1 Oct
Official Cash Rate	3.00	3.00	3.00	3.00	3.00	3.00
90 day bank bill	3.23	3.17	3.18	3.18	3.16	3.17
NZGB 11/11	3.62	3.50	3.48	3.45	3.81	3.82
NZGB 04/13	4.03	3.88	3.85	3.81	4.29	4.30
NZGB 12/17	4.91	4.83	4.80	4.76	4.89	4.90
NZGB 05/21	5.22	5.11	5.07	5.03	5.01	5.02
2 year swap	3.73	3.71	3.69	3.68	3.67	3.71
5 year swap	4.30	4.32	4.29	4.26	4.23	4.28
RBNZ TWI	65.7	66.5	66.5	66.6	66.3	66.3
NZD/USD	0.7026	0.7342	0.7349	0.7393	0.7369	0.7373
NZD/AUD	0.7818	0.7668	0.7650	0.7640	0.7612	0.7606
NZD/JPY	59.31	61.85	61.91	61.98	61.59	61.55
NZD/GBP	0.4565	0.4643	0.4642	0.4673	0.4652	0.4687
NZD/EUR	0.5530	0.5455	0.5458	0.5440	0.5416	0.5397
AUD/USD	0.8987	0.9575	0.9607	0.9677	0.9681	0.9694
EUR/USD	1.2705	1.3460	1.3465	1.3589	1.3605	1.3661
USD/JPY	84.42	84.24	84.24	83.83	83.58	83.48
GBP/USD	1.5392	1.5814	1.5832	1.5822	1.5839	1.5731
Oil (US$/bbl)	71.93	74.63	76.51	76.15	77.85	79.95
Gold (US$/oz)	1247.90	1296.53	1292.80	1311.90	1308.08	1309.90
Electricity (Haywards)	3.71	0.22	0.35	0.13	0.69	1.07
Milk futures (US$/contract)	116	118	118	118	118	118
Baltic Dry Freight Index	2741	2451	2504	2468	2446	2452

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.

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