

Market Focus

New Zealand

25 May 2009

A BIG WEEK

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Page 2: Economic overview

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Page 5: Budget 2009 preview

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Page 8: Economic comment – the regional gap

- > We are now seeing a universal easing in capacity pressures across the country. This reinforces that the 2008 "Auckland" housing recession has now gone economy-wide, along with the flow on from the global scene into the tradable sector and regions. The latter will remain an emerging trend as 2009 unfolds.

Page 9: Economic comment – global watch

- > A mixed week for data last week, with no real themes. European PMI surveys continue to improve, while weak housing construction in the US shows that challenges for that sector of the economy remains. March quarter GDP outturns have been poor around the globe.

Page 10: Interest rate strategy

- > Market sentiment remains skittish, and it is becoming clear that term premiums will have to rise. Worries about sovereign credit quality and rising inflation are weighing on long term rates. There is no safe harbour, but the RBNZ's commitment to keep the OCR low does offer some relief for borrowers. Investors should stick with yield curve steepeners.

Page 11: Currency strategy

- > There is no oxygen up here for the NZD. It is too early for the NZD to stage a meaningful recovery. USD weakness will continue but we argue the pieces are not in place for the NZD to survive above its long term average yet. Protectionism is another big headwind that has arrived on the horizon. We look for a correction this week as the LIBOR is expected to rise and struggling equity markets suggest the NZD is over-extended.

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ECONOMIC OVERVIEW

Signs of improvement in credit markets to levels prevailing before the collapse of Lehman Brothers is evidence of dissipating “systemic” risks. This is very encouraging, although there is still some way to go yet. And of course we must not lose sight of the fact that de-leveraging in the real economy will still follow on from the financial crisis. The *Budget* this week will show a deteriorating fiscal position, but all eyes will be on measures taken to reverse the upward trending debt track. Other data this week will be looked to for further signs of stabilisation.

What’s ahead?

- > **April Overseas Merchandise Trade** (Tuesday 1045 NZST). De-leveraging is expected to weigh on imports. A monthly trade surplus of \$350 million is expected.
- > **June quarter RBNZ Survey of Expectations** (Tuesday 1500 NZST). We expect the key 2-year ahead measure of inflation expectations to remain broadly similar to last quarter’s 2.3 percent.
- > **May NBNZ Business Outlook** (Wednesday 1500 NZST).
- > **Budget Economic and Fiscal Update** (Thursday 1400 NZST). Bigger deficits, more debt and larger bond tenders. For our full preview note, refer to page 5.
- > **April Credit Growth** (Thursday 1500 NZST). Household credit growth will remain subdued as de-leveraging continues. Business and rural lending is also likely to continue to show signs of moderation.
- > **April Building Consents Issued** (Friday 1045 NZST). The recent pick-up in house sales should see building consent issuance recover off its lows. Commercial consents though, will head lower.

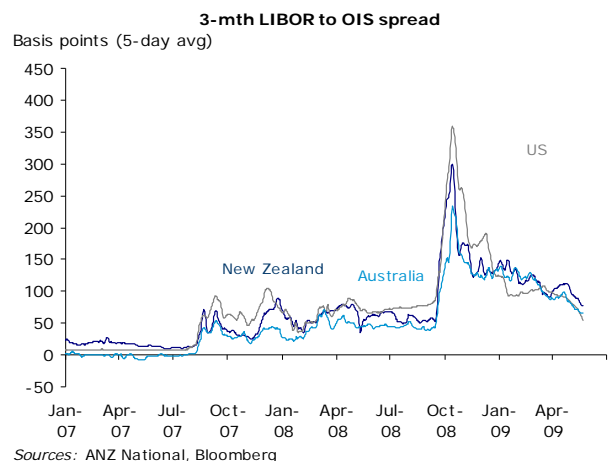
What’s the view?

This week is obviously a very important (and busy) one locally, with a number of pieces of data out, and of course the *Budget* on Thursday. The latter is viewed by many as one of the most important, but also challenging, budgets that will be delivered for some time. But before we get into the details and implications of these events, there is one theme that we feel is worthy of discussion. That is the encouraging signs of improvement seen in credit markets around the globe.

We don’t need to remind readers of the incredible events that have transpired in credit markets over the past 18 months. The real economic

consequences of those events are now only being felt, with the globe in the midst of its deepest and most synchronised recession since WWII. Restoring some semblance of functionality to credit markets is one of the key prerequisites that need to occur before the global economy can find a floor, let alone think about recovery. In this regard, recent nuances are encouraging.

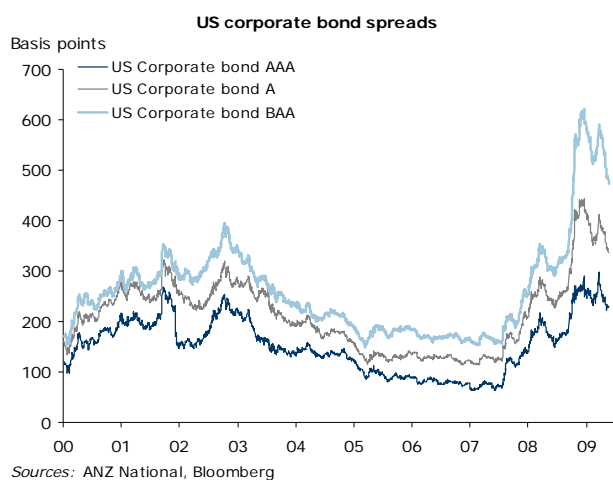
LIBOR rates continue to fall, with the US 3-month rate falling to 0.66 percent last week. More importantly though, is that the spread between LIBOR and OIS rates – a measure of stress in the interbank market – have continued to narrow, and are now below the levels prior to the Lehman’s collapse. The TED spread – or the difference between the rate at which the US government can borrow and the rate at which banks can borrow in the short-term (often known as the “panic barometer”) – has also narrowed. The Australian iTraxx index has fallen to 212bps, which is down 240bps from its March peak. Corporate bond spreads are also narrowing, and long-end CDS spreads for some large bellwether US institutions such as Goldman Sachs and JP Morgan are also below Lehman Brothers collapse levels.



Now, we must be wary of jumping on the all-clear bandwagon in so far as the financial crisis is concerned. Challenges remain, particularly in Europe. Spreads are now simply returning to levels prevailing before the collapse of Lehman Brothers, which effectively mean that markets are removing some of the systemic risk premium that had crept in. That is, stepping away from the dreaded ‘D’, but still being stuck with the “Great Recession”. We must not lose sight of the fact that real economic de-leveraging must flow on from the financial crisis, and we note that corporate bond spreads remain wide. Concerns over sovereign risk, inflation risk, and a swing in the balance of power towards investors still leaves the pendulum swinging against the borrowers. And that means continued de-leveraging and pressure on asset prices.

Nonetheless, we’ll take the improvements in credit markets as encouraging, and it certainly gives the

RBNZ some breathing space for June, despite a nasty by-product (in so far as economic rebalancing is concerned) being the strength of the NZ dollar. We'll be having a close look at our currency views this week. We continue to like the spirit of the TWI adjustment story, but the USD leg is now clearly challenged (although we are shaking our heads towards Europe and the euro). As alluded to a few weeks ago (4 May *Market Focus*), it may well be that we need to give the NZD/AUD a real rip lower if a weaker USD is going to constrain the NZD/USD leg. When we also look at stories on the protectionism front, and the news of the re-introduction of existing subsidies for the US dairy industry, we find it hard to justify a NZD up around current levels. But for now we are not inclined to panic. If there is a surprise to be had, it will be in Europe, and it won't be pleasant.

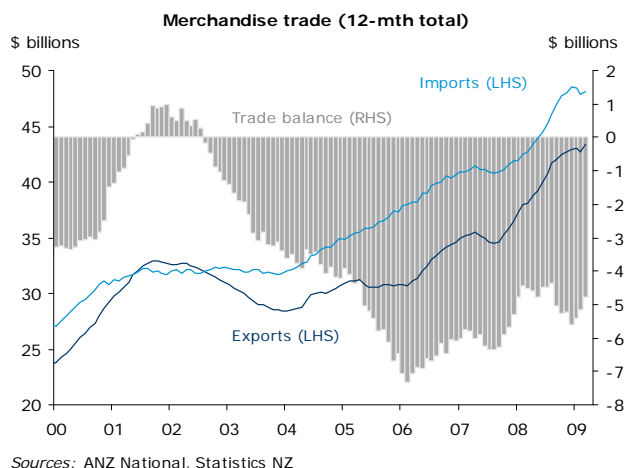


From a domestic perspective, we'll be watching to see whether improved offshore credit markets flow into domestic deposit rates – a key bellwether for borrowing rates. When offshore credit costs were high, everyone turned their attention towards the domestic base and competed aggressively, pushing deposit rates up. Now, *ceteris paribus*, falling offshore borrowing costs should dissipate pressure on the local deposit market. After all, why borrow locally if offshore is cheaper? However, the situation is complicated by three-dynamics. First, offshore markets remain "expensive" in level terms, despite recent improvements. Second, it is pretty clear that retail NZ investors have a nominal deposit rate in their heads below which they will simply not invest, particularly given competition from capital raisings and the like. Third, a desire to get a better mix of funding (i.e. more domestic, less offshore) may keep pressure in the market. And of course given NZ runs a savings shortfall, that would mean continued aggressive competition for deposits. For now we suspect it will remain a case of watching and waiting.

Now getting back to the events this week, as mentioned above, the *Budget* is the headline event. There is little doubt that it will show a considerable

deterioration in the Government's near-term fiscal position and over and above what was presented in the Treasury's *December Update* downside scenario. This has been well signalled by the Minister of Finance and Prime Minister. What will be of significant interest is the medium-term fiscal projections and in particular how the government goes about in achieving a declining debt track. As our recent research in the 11 May edition of the *Market Focus* showed, it is very difficult to reverse the trend. Our full preview is detailed on page 5.

Looking at the other data this week (in chronological order), overseas merchandise trade for April is expected to show that the economy is continuing to rebalance – again an encouraging sign. While the lagged effect of lower commodity prices is beginning to weigh on export values, last month's data shows that NZ has still been able to sell its product offshore – with exports hitting a record level in March. Imports, however, are being impacted by the de-leveraging domestic economy and a run-down in the considerable build up in inventories that had occurred. We are expecting a monthly trade surplus of \$350 million in April and for the annual deficit to fall to \$4,153 million – its smallest level since February 2005.



The RBNZ's *Survey of Expectations* for the June quarter is not as much of a focus as it was 12 months ago, with inflation pressures easing. However, the key 2-year ahead measure of inflation expectations is likely to remain around last quarter's level of 2.3 percent. With expectations well behaved, it will obviously provide the RBNZ with some comfort that their aggressive strategy to cut interest rates when inflation pressures were still high, was the correct one.

The NBNZ *Business Outlook* for May, released on Wednesday, should get plenty of attention. Considering the improvement seen in a number of gauges within the survey last month, which is another one of the green shoots many are talking about, the key question is whether this was just a flash in the pan or if further improvement in sentiment has been recorded.

Also out on Wednesday are credit growth numbers for April. On the whole they are likely to remain subdued, although housing related lending may show a small pick-up considering the improvement in housing market activity that was recorded in the month. Growth to the business and rural sectors is expected to continue to moderate, with most of the lending going to working capital rather than any new investment.

Finally, Friday's residential building consent issuance for April could potentially show a small recovery given the near-record lows at present. Similar to the credit growth numbers, the recent pick-up in housing volumes should lead to a recovery in building consents off its lows. However, looking at the incentives to build at present (downward pressure on prices, weak confidence and difficult credit conditions), it is likely that consent issuance will remain subdued for some time yet. As we have been saying for a number of months now, commercial consent issuance is likely to head lower. We have to admit that it has probably held in better than we would have expected given the economic backdrop. However, this is not something we expect to continue.

Internationally this week, there are a few releases that will get some attention. It is a quiet week in Australia. However in Europe, labour market data and the German IFO survey will be watched closely. The latter, like all sentiment surveys at present, will be looked at to see if the green shoots are sprouting further. In the US, durable goods data, house sales, the Chicago Fed survey and the provisional March quarter GDP numbers will be the main focal points.

Recent local data...

- > **Producer Price Indices (March quarter):**
Input prices fell 2.5 percent, while output prices fell 1.4 percent.
- > **International Travel and Migration (April):**
A seasonally adjusted net inflow of 2,160 people was recorded in the month, taking the annual total to 9,176.
- > **NBNZ Regional Trends (March quarter):**
Nationwide activity fell 1.2 percent in the quarter, with the Bay of Plenty recording the largest contraction.
- > **Credit Card Spending (April):** Spending on credit cards rose 2.3 percent in the month, following a 2.8 percent fall in March.

BUDGET 2009 PREVIEW

(due 1400 NZST on 28 May)

We expect the Government to walk the tightrope as it balances pressure on the fiscal position from the economic downturn with the usual pressure from baselines such as health, and the need to deliver a credible fiscal strategy to ensure large fiscal deficits (and rising debt) do not become endemic. The headline numbers themselves are expected to be poor, and this will include sizeable bond issuance. This will keep NZ's credit rating on a negative outlook, at a minimum.

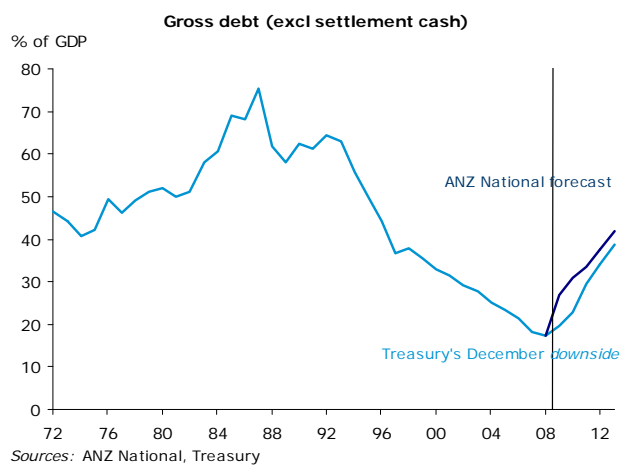
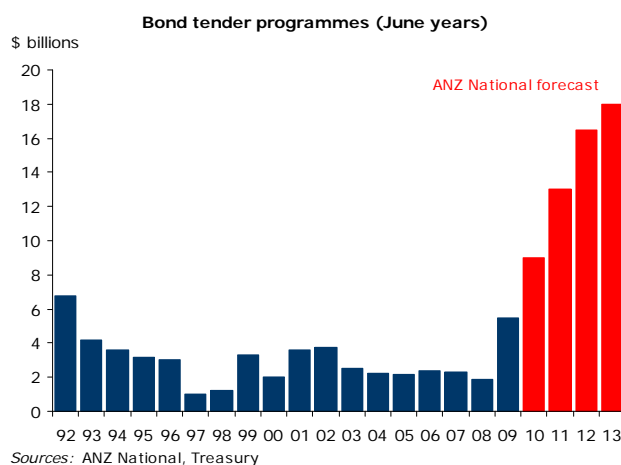
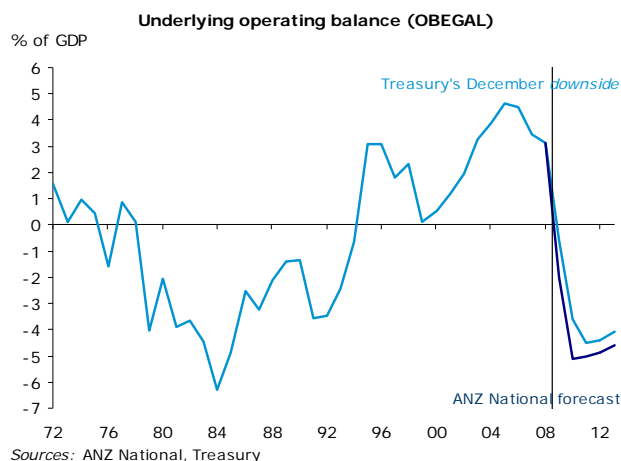
Bigger deficits, bigger bond tender programmes

We doubt this Thursday's *Budget*, the first under Finance Minister Bill English, will go down in history alongside Arnold Nordmeyer's infamous "*Black Budget*" of 1958 or Ruth Richardson's 1991 "*Mother of All Budgets*". There is no doubt that the NZ economy is facing its deepest and longest recession since the 1970s, and that the near-term underlying operating balance is set to deteriorate to its worst state since the 1980s. However, unlike the situation that previous Governments faced, the starting point for the fiscal position is far stronger. The Crown is in a net asset position, and gross debt is starting from a very low level. Indeed, NZ's starting position would be the envy of many overseas Finance Ministers at present. This means there is less need to embark on immediate contractionary fiscal policy, which risks further damaging an already fragile domestic economy.

However, there is very limited scope to embark on further stimulus spending to support the economy either, over and above what has already been put in place (i.e. the tax cuts that came into force on 1 October 2008 and 1 April 2009, bringing forward of infrastructure spending and the Small Business Relief Package). Hence, we see this year's *Budget* as really one of consolidation.

We expect the underlying operating balance (OBEGAL) to show deficits of over 5 percent of GDP, with cash deficits in excess of \$15 billion. This is a by-product of not only the recessionary environment which is seeing tax revenues coming under pressure (with more to come) and automatic stabilisers kicking in via increased benefit expenditure, but also a reflection of expenditure growth that had been rampant for the six years prior. These deficit figures will see the DMO announce bond tender programmes progressively rising towards \$18 billion. This is a far cry from the \$2.6 billion issued on average over the past decade. The plus side is additional liquidity in the bond market. But where the buyers are going to come from has us scratching our heads. And it's

hard to go past longer-dated yields continuing to rise. Gross debt is expected to rise from 17.4 percent of GDP in 2007/08 towards past 40 percent by 2012/13. Relative to our international peers, this is still low, although it is the pace of accumulation between years that is the real issue. Moreover, it's the combination of high external debt and rising government debt that is the real problem, and has Standard & Poor's concerned.

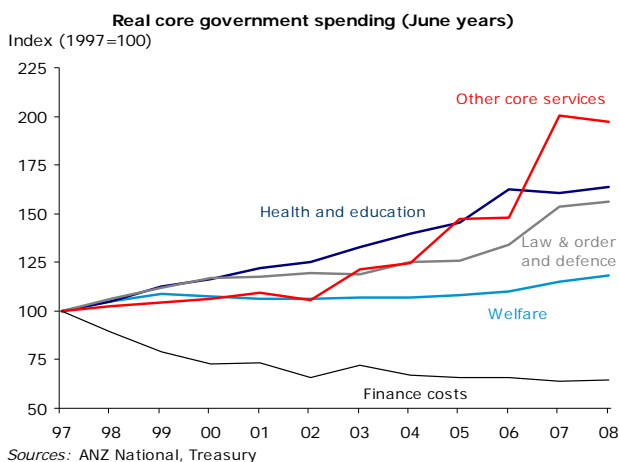


Cyclical support versus a structural problem

There is not a lot the Government can, or should do in response to the recessionary environment in so

far as the fiscal position is concerned. Given the size of the Government's balance sheet, it's more than common sense that the economy should leverage off it during downturns. But clearly, deficits cannot continue unabated, nor net debt rise unchecked, which is precisely what the Treasury was predicting in their downside scenario in December (sustained operating deficits of 4 percent of GDP and debt rising to 76 percent of GDP by 2023). Such projections would simply be the *coup-de-grâce* on a credit downgrade.

Communiqué coming out of the Beehive in various speeches has been pretty strong on the fiscal prudence rhetoric. It is clear the Government wants to show debt peaking and then tracking down, in effect moving from expansionary fiscal policy to a contractionary stance, and bringing the fiscal figures back into the black. The real issue is how this is achieved. Tax hikes are unlikely, which leaves spending. And we all know a lot of spending areas such as health are likely to be no go zones for cuts.



A large chunk of the \$57 billion core government spending is in welfare, health, education, law & order and defence, areas which are unlikely to see cuts in the near-term. All need additional money each year simply to keep ticking and turning over. And there will be upward pressure on welfare spending as a result of the recession. Finance costs will rise on the back of increased borrowing. This really only leaves what we call the "Other core services", at around \$11 billion. This has been the area that has seen the strongest growth in spending over recent years. But trying to generate even \$1 billion in savings from this area is a big ask, as this represents a 10 percent reduction. This leaves us coy about the ability to truly cut spending (few Ministers have actually done it and politically it's a tough ask), with the best most seem to do is actually constrain the growth going forward.

In a pre-Budget speech, the Prime Minister said, "So the Government will make some responsible decisions in this Budget. These will include delaying some steps in our economic plan that we

would have rather made sooner. They will also include reducing the amount of extra spending available for future Budgets and making some savings in less effective areas of government spending." We suspect that means:

- > The planned tax cuts over the next two years will be delayed (and we struggle to see them occurring unless some huge savings can be found in spending);
- > The \$1.8 billion allocated for future budgets will be cut, likely to around \$1 billion per annum;
- > A lot of new spending initiatives will be funded from within existing baselines via reprioritisation and savings; and
- > Contributions to the NZ Super Fund will be temporarily suspended.

The above decisions may just be enough to get the medium-term fiscal deficit projections to narrow and result in the debt track turning around. But as our modelling has shown (see our 11 May edition of *Market Focus*), it will not be until 2015/16 that the debt situation starts to get under control. However, from a credit rating agency point of view, it is all about presenting a credible medium-term strategy of arresting the deteriorating fiscal position that is ultimately the key to avoiding a rating downgrade. We suspect a strategy such as what we envisage above will be sufficient for now. Of course, the challenge will be to deliver on such a strategy.

No big bang policy announcements expected

Aside from the projections of the overall fiscal position, another area of interest is announcements of new policy initiatives. In the usual pre-Budget drip-feeds, the largest initiatives so far has been an extra \$104 million over 4-years to improve maternity services for parents, \$50 million for a proposed cycleway which was mooted at the Jobs Summit, and \$40 million for a Community Response Fund to support community and voluntary sector organisations. The Government also announced an extra \$1 billion to be invested in the state highway network over the next three years, but only \$258 million of that is new money, with the rest coming from a reallocation from other areas and increases in fuel taxes. Indeed, we suspect that while there will be a lot of noise about various initiatives, a substantial portion will be reallocations.

We do not expect any large major policy announcements, and a lot of the new initiatives will be largely funded from within existing baselines or through savings from lower priority areas. We will keep an eye out for any initiatives designed to improve NZ's dismal productivity performance. But on that basis we struggle to see any big-bang

winners, although a combination of policies, if delivered correctly, could start making incremental changes a few years out. Like the saying goes, never waste a good recession! It is an opportunity to knuckle down and focus on priorities.

Financial Market Implications

The NZ economy is rebalancing and consolidating. A by-product is a weaker fiscal position. Just like households, the Government will need to live within its means. This means evolving fiscal policy from an expansionary to a contractionary stance over the coming years. The inability of fiscal policy to ride out in perpetuity fits with the RBNZ's lower for longer view on interest rates.

We expect Standard & Poor's to leave NZ's AA+ rating on a negative outlook at a minimum. This will reflect a huge degree of uncertainty over the pace of debt accumulation, and reality than turning substantial deficits around typically proves to be very challenging. For sure, the government's opening position is strong, and medium-term fiscal projections are subject to a huge degree of

uncertainty. In this environment it seems more prudent than not to maintain the status quo of a "negative outlook" and continue to assess developments and in particular the impact of the downturn on the fiscal position, and also how credible the consolidation strategy is. Only time will tell in regard to the latter.

However the fiscal numbers are deteriorating rapidly, and must be read in conjunction with a poor external position. On this basis we would consider the credit rating decision to be very "tight", and it has not gone unnoticed by us that rating agencies now look to be taking a sterner line.

We expect the NZ bond market to remain heavy going forward. While the market has already, to a degree, factored in large future bond tender programmes, we see the risks as continuing to point higher, and we'll be closely watching tax receipt data over the coming months. With every nation around the globe now issuing bonds hell for leather, it's a simple case of the price having to adjust, and that's higher.

Fiscal Forecasts – Budget 2009* (DEFU 2008 downside forecasts in brackets)

June Years	2008/09	2009/10	2010/11	2011/12	2012/13
OBEGAL - \$ billion	-3.5 (-1.0)	-9.1 (-6.3)	-9.5 (-8.5)	-10.0 (-8.8)	-9.8 (-8.6)
- % GDP	-2.0 (-0.6)	-5.2 (-3.6)	-5.0 (-4.5)	-4.9 (-4.4)	-4.6 (-4.1)
Net Core Crown Debt - % GDP	3.0 (3.4)	9.2 (8.9)	18.0 (15.0)	23.0 (20.5)	28.5 (25.6)
Gross Sovereign-Issued Debt (% of GDP)	27.0 (19.5)	31.0 (22.7)	33.5 (29.4)	37.5 (34.0)	42.0 (38.6)
Bond tender - \$ billion [^]	5.5 (4.5)	9.0 (7.5)	13.0 (11.2)	16.5 (15.0)	18.0 (15.9)

* Budget 2009 numbers are ANZ National's forecasts.

[^] Bond tender numbers in brackets are as announced by DMO in the December Update.

THE REGIONAL GAP

We are now seeing a universal easing in capacity pressures across the country. This reinforces that the 2008 "Auckland" housing recession has now gone economy-wide, along with the flow on from the global scene into the tradable sector and regions. The latter will remain an emerging trend as 2009 unfolds.

We have updated our regional output gap measures. To refresh readers' memories, regional output gaps are estimated using data from the National Bank's *Regional Trends and Business Outlook* survey, and Statistics NZ's regional unemployment data.¹ While conventional output gap measures (while prone to huge degree of uncertainty) give us information about the aggregate economy, regional measures (additional standard errors aside that comes with disaggregation) give us a richer picture in terms of not just whether capacity pressure is rising, or falling, but its concentration and how broad it is.

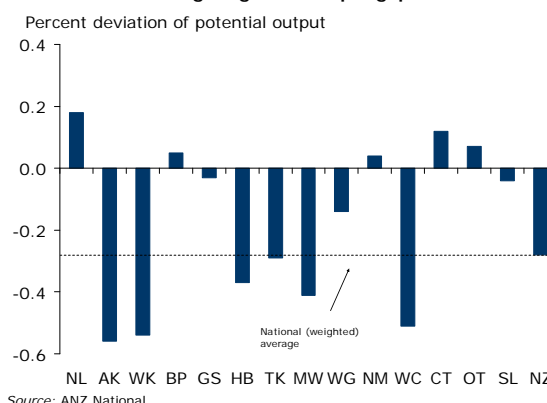
Here are some key messages from the analysis:

- > The economy-wide output gap has turned negative. This is the first time this has been the case since September 2001. Of the three gap measures we estimate, the activity gap is well in negative territory, the aggregate capacity gap is "neutral", while the unemployment gap remains positive. The latter is likely to be due to the natural business cycle lags.
- > Eight of the 14 regions reported negative output gaps in the March quarter. As was the case in the December quarter, the activity gap measure was negative across every single region. The capacity gap was slightly more mixed, with some regions still recording positive capacity pressures, while the unemployment gap was positive across all the regions, reflecting a still historically low unemployment rate.
- > The South Island is still experiencing the greater capacity pressures compared with the rest of the country. This is hardly surprising considering that the recession in 2008 was

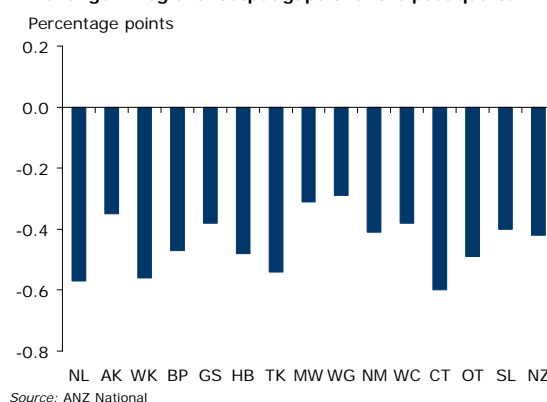
upper North Island centric. However, what is now clear is that the downstream implications are broadening, particularly as the flow-on from the global scene into the tradable sector unfolds. Indeed, we are now seeing a universal easing in capacity pressure across the entire country, and of broadly similar magnitudes.

- > For the third consecutive quarter, the Auckland region recorded the most negative (or least positive) output gap, once again a reflection of the reality that the recession effectively started in Auckland. But all, excluding two regions, showed a deterioration in the output gap greater than Auckland in the quarter.

Estimate average regional "output gap" in Mar 09



Change in regional output gaps over the past quarter



The upshot

Regional output gap calculations confirm that capacity pressure is easing, as would be expected given an economy in recession. Nonetheless, some capacity stickiness remains from the labour market although this will unfold rapidly. What our regional gap measures also tell us is that the easing in capacity pressure is now uniform across the country (the third consecutive quarter this has been the case) and moving south of the Bombay Hills.

Note: NL=Northland, AK=Auckland, WK=Waikato, BP=Bay of Plenty, GS=Gisborne, HB=Hawke's Bay, TK=Taranaki, MW=Manawatu-Wanganui, WG=Wellington, NM=Nelson-Marlborough, WC=West Coast, CT=Canterbury, OT=Otago, SL=Southland.

¹ The estimates are generated using estimates of the output gap, unemployment gap and a derived capacity utilisation gap from the NBNZ *Business Outlook* survey. We chose a broad approach for two reasons. First it minimises some of the error that may surround simple regional activity statistics (which are only partial indicators). Second, the Reserve Bank uses a similar combination to derive its multivariate filter measure of the output gap for the entire economy. For each input we use a band-pass filter to derive the business cycle – a standard statistical technique that is available on modern statistical software. The regional unemployment rates are advanced two quarters prior to filtering as this is a lagging indicator. Individual output gap measures across activity, unemployment and capacity utilisation for each region are then given an equal weighting.

GLOBAL DATA WATCH

A mixed week for data last week, with no real themes. European PMI surveys continue to improve, while weak housing construction in the US shows that challenges for that sector of the economy remains. March quarter GDP outturns have been poor around the globe.

Country/ Area	Indicator	Market	Actual	Last	Outturn vs market
Australia	Westpac Consumer Confidence (May)	-	-4.3%	8.3%	-
	Wage Cost Index (1Q) – qoq	0.8%	0.8%	1.3%	In-line
	Consumer Inflation Expectations (May)	-	2.3%	2.4%	-
US	NAHB Housing Market Index (May)	16	16	14	In-line
	House Starts (Apr)	520K	458K	525K	Weaker
	Continuing Jobless Claims (w/e May-10)	6650K	6662K	6587K	In-line
	Leading Indicators (Apr)	0.8%	1.0%	-0.2%	Stronger
	Philadelphia Fed (May)	-18.0	-22.6	-24.4	Weaker
	Euro-zone	Trade Balance (Mar) – s.a.	-3.8B	-2.1B	-2.9B	Stronger
PMI Manufacturing (May A)		38.3	40.5	36.8	Stronger
PMI Services (May A)		44.5	44.7	43.8	In-line
UK	CPI (Apr) – mom	0.4%	0.2%	0.2%	Weaker
	Total Business Investment (1Q P) – qoq	-4.0%	-5.5%	-1.5%	Weaker
	Retail Sales (Apr) – mom	0.5%	0.9%	1.2%	Stronger
	Public Finances (PSNCR) (Apr)	7.5B	8.5B	18.2B	Stronger
	GDP (1Q P) - qoq	-1.9%	-1.9%	-1.9%	In-line
Japan	Domestic CGPI (Apr) – mom	0.2%	-0.4%	-0.3%	Weaker
	Consumer Confidence (Apr)	31.0	33.2	29.6	Stronger
	GDP (1Q P) – qoq	-4.3%	-4.0%	-3.8%	Stronger
	Tertiary Industry Index (Mar) – mom	-1.5%	-4.0%	-1.3%	Weaker
	BoJ Target Rate	0.10%	0.10%	0.10%	In-line
Asia Ex-Japan					
<i>Singapore</i>	Non-Domestic Exports (Apr) – mom	1.5%	-1.3%	10.4%	Weaker
	GDP Annualised (1Q F) – qoq	-14.7%	-14.6%	-19.7%	In-line
<i>Hong Kong</i>	Unemployment Rate (Apr)	5.4%	5.3%	5.2%	In-line
	CPI – Composite Index (Apr) - yoy	1.0%	0.6%	1.2%	Weaker
<i>Taiwan</i>	GDP (1Q) – qoq	-9.3%	-10.2%	-8.6%	Weaker
	Unemployment Rate (Apr)	5.8%	5.8%	5.7%	In-line
<i>Thailand</i>	Customs Exports (Apr) – yoy	-28.0%	-26.1%	-23.1%	Stronger
	Customs Imports (Apr) – yoy	-41.5%	-36.3%	-35.1%	Stronger
	Benchmark Interest Rate	1.00%	1.25%	1.25%	Stronger
<i>Malaysia</i>	CPI (Apr) – yoy	3.2%	3.0%	3.5%	Weaker
<i>Philippines</i>	Balance of Payments (Apr)	-	\$466M	-\$472M	-

INTEREST RATE STRATEGY

Market sentiment remains skittish, and it is becoming clear that term premiums will have to rise. Worries about sovereign credit quality and rising inflation are weighing on long term rates. There is no safe harbour, but the RBNZ's commitment to keep the OCR low does offer some relief for borrowers. Investors should stick with yield curve steepeners.

Market themes...

- > Standard & Poor's decision to place UK's credit rating on negative outlook has rattled global bond markets, and has put the focus on Thursday's *Budget*, and the burden of issuance.
- > While we expect NZ to escape a downgrade, courtesy of a fiscally responsible *Budget*, the market seems to have an ear for bad news.
- > Governments across the globe appear to favour social considerations over economic discipline. This is most likely to result in the deliberate targeting of higher inflation, which is negative for bonds.
- > A responsible *Budget* puts more pressure on monetary policy to deliver. In a de-leveraging environment where global inflation is on the rise, this implies a much steeper yield curve.

Review and outlook

The outlook for long term interest rates isn't pretty. The market is not only reeling from the optimism surrounding the "green shoots" thesis, but the last week has seen the focus shift to two other factors – credit ratings and inflation. Both have been on the back burner for some time, and were always at risk of boiling over, but the fact that they have come together at the same time has been particularly damaging, and has seen Treasury yields soar.

So what's the fuss? Well, to start with, sovereign credit ratings of some erstwhile benchmarks now look under pressure. S&P's decision to place the UK's credit rating on negative outlook has not only taken the gilt-edge off Gilts, but it has put a question mark on the creditworthiness of other major sovereign borrowers like the US. Worse still for us, it has come at a time when the spotlight was already on New Zealand. Even if it seems futile downgrading the very essence of our fiat money system (i.e. USD), the point is simply this – Western governments have a ton of debt to issue and it's going to rattle the market to its foundations. Which leads us to the next point – what to do once the money is borrowed? Sadly, it's not just those peddling "noddy-nomics" that are calling for a deliberate policy of deflating this debt away – even the heavyweights of the economics fraternity seem to favour it. And that's not good news for bonds.

Borrowing strategies we favour at present

The radical steepening of the yield curve makes paying anything longer than about 3 years prohibitive. But at the same time, even the 1 year and 2 year part of the curve have ignored the RBNZ's message, and look expensive. As such, the only strategies we have confidence in are options. Better to spend some premium and stand to potentially benefit, than to tread out along the yield curve and guarantee a higher interest rate.

Gauges for NZ interest rates

Gauge	Direction	Comment
RBNZ / OCR	↓	RBNZ still has easing bias, but won't cut in June.
NZ data	↔/↑	Migration data supports our view of no cut in June.
Fed Funds/ front end	↔	US front end rallying. Are the "green shoots wilting"?
RBA	↔/↓	Not in focus now, but long term risk is for more cuts.
US 10 year	↑	Focus on credit ratings and temptation to deflate debt away not good for bonds.
NZ swap curve	↔/↑	Steepening set to continue as RBNZ talks down short end, global long end sells.
Flow	↔/↑	Receivers absent and running for the hills.
Technicals	↔/↑	US 10yr Treasuries made a new yield high. Not good.

Market expectations for RBNZ OCR (bps)

OCR dates	Last week	This week
Thu 11-Jun-09	-9	-9
Thu 30-Jul-09	-18	-11
Thu 10-Sep-09	-20	-10
Thu 29-Oct-09	-16	-9
Thu 10-Dec-09	-8	-8
Thu 21-Jan-10	-10	+1
Thu 11-Mar-10	-11	+18

Trading themes we favour at present

Notwithstanding our overall bearish economic view, and the market's misinterpretation of the RBNZ's message, it's difficult to get bullish on interest rates. Receivers are largely absent, especially given nervousness surrounding this week's Budget. As such it's hard to be long in this environment, despite the obvious roll and carry benefits. Hence, we continue to favour steepeners. Worries about the sustainability of AAA credit ratings in the US and UK will add to upward pressure to bond yields. This is further exacerbated by talk globally of deflating away the debt burden, which would have disastrous consequences for bond yields.

CURRENCY STRATEGY

There is no oxygen up here for the NZD. It is too early for the NZD to stage a meaningful recovery. USD weakness will continue but we argue the pieces are not in place for the NZD to survive above its long term average yet. Protectionism is another big headwind that has arrived on the horizon. We look for a correction this week as the LIBOR is expected to rise and struggling equity markets suggest the NZD is over-extended.

Market themes...

- > Dairy subsidies in the US in retaliation for European subsidies are a big negative.
- > S&P are in New Zealand reviewing our rating. Will Thursday's *Budget* be enough to prevent a downgrade?
- > USD is universally hated but do they care?

Review and outlook...

Another week, another high. The big question is on what? Only the migration data was better than expected, with most data suggesting the recession is lingering into Q2. The NZD's move higher was simply because the USD was despised, with most currencies gaining against the greenback as LIBOR continued to tumble, suggesting the world is a better place and people are again putting money to work. However, it is interesting to note that the LIBOR rate is now expected to rise and equities couldn't hold their gains from earlier in the week. The VIX index stabilised from its recent falls again, suggesting momentum is waning.

There is an argument that the world is awash with USD, particularly in foreign reserves. Over the medium-term, we agree and have no problems with a stronger NZD. But currently, weakness in the USD has driven commodity prices higher, though they have not benefited to the extent of the local currency. The argument for NZD strength comes from the QE and loose fiscal policy in the US; helping to reignite growth, causing inflation and accelerating commodity prices higher. The NZD, AUD, CAD and NOK all benefit greatly in this scenario, with the USD being the big loser. But clearly the NZD is getting ahead of itself. Especially given the reintroduction of US dairy subsidies announced over the weekend suggesting our basket of commodity prices are likely to be lower, not higher.

The NZD has to contend with the *Budget* this week and a very subdued picture of the local economy is expected to emerge. S&P and the other rating agencies will be very interested in what Finance Minister Bill English has to say. We see the NZD

struggling below 0.6220 this week and it could potentially target the 0.5810 level where the 200 day moving average currently resides. AUDUSD is diverging on most charts and suggests that rally is also over-extended. Talk of global trade subsidies will not benefit Australia either. The 0.7900 level is a major resistance for the AUD and we prefer both currencies to fall below last week's highs and move lower.

NZD vs AUD: monthly directional gauges		
Gauge	Direction	Comment
Fair value	↔/↑	Bottom of the range. No bad news priced into AUD.
Yield	↓	Yield advantage Australia.
Commodities	↔	Metals lower, Milk lower.
Partial indicators	↔/↓	NZ data not as bad as feared, AU's even better.
Technicals	↔	0.7700 to 0.8000 range.
Sentiment	↔/↑	Risk appetites wane.
Other	↓	S&P comments and US dairy subsidies are negative.
On balance	↔	Market happy playing current range.

NZD vs USD: monthly directional gauges		
Gauge	Direction	Comment
Fair value – long-term	↔/↓	Above long term average.
Fair value – short-term	↔	Slightly above cyclical fair value estimates.
Yield	↔/↓	Consolidating at narrow levels.
Commodities	↔/↓	Fonterra auction weak after recent good run.
Risk aversion	↔	Risk appetites wane.
Partial indicators	↔	Stabilisation occurring?
Technicals	↔/↑	Break of 200-day MA bullish sign.
AUD	↔/↑	AUD still holding up but tired.
Sentiment	↓	S&P comments and US dairy subsidies are negative.
Other	↔	Prefer to wait and see. 0.5800-6200 range.
On balance	↔/↓	0.58 cent key level.

DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
25-May	JN	All Industry Activity Index (Mar) - mom	-2.3%	-2.0%	11:50
		BoJ Governor Shirakawa to Speak in Kanazawa City	-	-	14:00
		BoJ Monthly Report	-	-	17:00
	GE	IFO - Business Climate (May)	85.0	83.7	20:00
		IFO - Current Assessment (May)	84.5	83.6	20:00
		IFO – Expectations (May)	85.5	83.9	20:00
	EC	ECB's Weber Holds Speech at Event in Helsinki	-	-	22:00
26-May	EC	ECB's Gonzalez-Paramo Speaks at Event in Madrid	-	-	06:00
	NZ	Trade Balance (Apr)	250.0M	324.0M	10:45
		Annual Balance (Apr)	-4153M	-4796M	10:45
		Imports (Apr)	3.35B	3.72B	10:45
		Exports (Apr)	3.68B	4.04B	10:45
		RBNZ 2yr Inflation Expectation	-	2.3%	15:00
	JN	Corp Service Price (Apr) - yoy	-2.2%	-2.1%	11:50
	GE	GDP (1Q F) - qoq	-3.8%	-3.8%	18:00
		GDP (1Q F) - yoy	-6.7%	-6.7%	18:00
		GfK Consumer Confidence Survey (Jun)	25	2.5	18:10
	EC	Current Account (Mar)	-	-8.1B	20:00
		Industrial New Orders (Mar) - mom	0.8%	-0.6%	21:00
27-May	US	S&P/CS Composite-20 (Mar) – yoy	-18.4%	-18.6%	01:00
		Consumer Confidence (May)	42.8	39.2	02:00
		Richmond Fed Manufacturing Index (May)	-6	-9	02:00
		Dallas Fed Manufacturing Activity (May)	-22.1%	-31.6%	02:30
	JN	BoJ Monetary Policy Meeting Minutes for April 28 Meeting	-	-	11:50
		Adjusted Merchandise Trade Balance (Apr)	-¥17.5B	-¥97.1B	11:50
		Merchandise Trade Exports (Apr) - yoy	-42.0%	-45.5%	11:50
		Merchandise Trade Imports (Apr) - yoy	-36.9%	-36.6%	11:50
	AU	Westpac Leading Index (Mar) - mom	-	-0.3%	12:30
		DEWR Skilled Vacancies (May) - mom	-	-8.9%	13:00
	NZ	NBNZ Business Confidence (May)	-	-14.5	15:00
	JN	Small Business Confidence (May)	-	30.8	17:00
	EC	ECB's Bini Smaghi Speaks at Rome Conference on Economic Crisis	-	-	20:00
28-May	US	House Price Index (Mar) - mom	0.2%	0.7%	02:00
		Existing Home Sales (Apr)	4.66M	4.57M	02:00
	JN	Retail Trade (Apr) - mom	0.5%	-1.1%	11:50
	AU	Conference Board Leading Index (Mar)	-	0.2%	12:00
		HIA New Home Sales (Apr)	-	4.2%	13:00

Continued over page

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
28-May cont.	AU	RBA Deputy Governor Battellino Speaks in Sydney	-	-	13:10
		Private Capital Expenditure (1Q)	-5.0%	6.0%	13:30
		Construction Work Done (1Q)	-3.0%	1.7%	13:30
	NZ	Annual Budget	-	-	14:00
		Money Supply M3 (Apr) - yoy	-	7.1%	15:00
	GE	ILO Unemployment Rate (Apr)	7.7%	7.6%	18:00
		Unemployment Change (000's) (May)	64K	58K	19:55
		Unemployment Rate (May)	8.4%	8.3%	19:55
	EC	Economic Confidence (May)	69.0	67.2	21:00
29-May	US	Durable Goods Orders (Apr) - mom	0.4%	-0.8%	00:30
		Durables Ex Transportation (Apr) - mom	-0.3%	-0.6%	00:30
		Initial Jobless Claims (w/e May-24)	630K	631K	00:30
		Continuing Claims (w/e May-17)	6740K	6662K	00:30
		New Home Sales (Apr)	360K	356K	02:00
	EC	ECB's Weber Holds Speech On Reichenau Island, Germany	-	-	02:15
		ECB's Tumpel-Gugerell Speaks at Event in Vienna	-	-	04:00
		M3 Money Supply (Apr) - 3-mth avg	5.1%	5.6%	20:00
		CPI Estimate (May) - yoy	0.2%	0.6%	21:00
		Unemployment Rate (Apr)	9.1%	8.9%	21:00
		ECB's Trichet Speaks at Event in Marrakech, Morocco	-	-	21:15
	NZ	Building Permits (Apr) - mom	-	-4.6%	10:45
	UK	GfK Consumer Confidence Survey (May)	-25	-27	11:01
	JN	Jobless Rate (Apr)	5.0%	4.8%	11:30
		Household Spending (Apr) - yoy	-0.7%	-0.4%	11:30
		National CPI (Apr) - yoy	-0.3%	-0.3%	11:30
		National CPI Ex-Fresh Food (Apr) - yoy	-0.1%	-	11:30
		National CPI Ex Food, Energy (Apr) - yoy	-0.4%	-0.3%	11:30
		Industrial Production (Apr P) - mom	3.3%	1.6%	11:50
		Vehicle Production (Apr) - yoy	-	-50.0%	16:00
		Housing Starts (Apr) - yoy	-22.0%	-20.7%	17:00
		Construction Orders (Apr) - yoy	-	-37.8%	17:00
	AU	Private Sector Credit (Apr)	0.2%	0.1%	13:30
30-May	US	GDP Annualised (1Q P)	-5.5%	-6.1%	00:30
		Personal Consumption (1Q)	2.0%	2.2%	00:30
		GDP Price Index (1Q)	2.9%	2.9%	00:30
		Chicago Purchasing Manager (May)	42.0	40.1	01:45
		University of Michigan Confidence (May F)	68.0	67.9	02:00

Key: AU: Australia, EC: Euro-zone, GE: Germany, JN: Japan, NZ: New Zealand, UK: United Kingdom, US: United States.
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: Further signs of stabilisation is likely to be the theme for upcoming data. While encouraging, stabilisation doesn't necessarily mean recovery, and conditions are likely to remain challenging for some time yet. The *Budget* this week looks likely to contain some tough choices.

Date	Data/Event	Economic Signal	Comment
Tue 26 May (10.45)	Overseas Merchandise Trade (Apr)	Rebalancing continues	Another monthly trade surplus is expected as the domestic economy continues to de-leverage, weighing on import growth.
Tue 26 May (15.00)	RBNZ <i>Survey of Expectations</i> (Jun qtr)	Not a concern for now	The key 2-year ahead measure of inflation expectations is expected to remain around the current level of 2.3 percent.
Wed 27 May (15.00)	NBNZ <i>Business Outlook</i> (May)	-	-
Thu 28 May (14.00)	<i>Budget Economic and Fiscal Update</i>	Ugly	The <i>Budget</i> should show a further sharp deterioration in the medium-term fiscal projections. Bigger deficits, more debt and larger bond tenders.
Thu 28 May (15.00)	Credit Growth (Apr)	De-leveraging	Household credit growth will remain subdued as de-leveraging continues. Business and rural lending is also likely to continue to show signs of moderation.
Fri 29 May (10.45)	Building Consents Issued (Apr)	Stabilising	The recent pick-up in house sales should see building consent issuance recover off its lows. Commercial consents though, will head lower.
Wed 3 Jun (10.00)	Financial Statements of the Government (10 months to April)	Further into the red	Lower tax revenue is expected to see the Government's underlying accounts head further into the red. Better returns in the month from Crown Financial Institutions will help stop the headline operating balance from deteriorating further.
Thu 4 Jun (15.00)	ANZ Commodity Price Index (May)	-	-
Tue 9 Jun (10.45)	Value of Building Work Put in Place (Mar qtr)	Still contracting	Residential building construction is likely to record another large quarterly contraction. Non-residential construction is expected to be largely unchanged.
Wed 10 Jun (10.45)	Overseas Trade Indexes (Mar qtr)	Terms of trade lower	Large falls in export commodity prices is expected to see the terms of trade fall in the quarter. Volume data is expected to confirm net exports will make a positive contribution to growth in the March quarter.
Thu 11 Jun (09.00)	RBNZ June <i>Monetary Policy Statement</i>	Temporary pause	While a case can be made for further immediate rate cuts, the green shoots need to be respected. However, we don't expect them to be sustained and hence rate cuts are likely to resume from H2 2009.
Fri 12 Jun (10.45)	Retail Trade Survey (Apr)	Finding a base	Second lot of tax cuts should give retail sales a bit of a kick.
Mon 15 Jun (10.45)	Economic Survey of Manufacturing (Mar qtr)	Weak	Manufacturing activity is likely to be weighed down by primary food, where less livestock slaughtering will impact.
Mon 22 Jun (10.45)	International Travel and Migration (May)	More of the same	Less New Zealanders departing will ensure that solid monthly net inflows continue to be recorded.
Thu 25 Jun (10.45)	Balance of Payments (Mar qtr)	Rebalancing	Recent improvement in the trade balance should help drive the current account deficit to an improved deficit of 8.5 percent of GDP.
Fri 25 Jun (10.45)	GDP (Mar qtr)	The worst yet?	We currently have a 1.5 percent contraction pencilled in for the quarter – the worst quarter of the recession yet.
On Balance		Base forming?	There is a strong base effect appearing in some data, which suggests Q2 is the nadir in the cycle. But the jury is out on the speed of recovery.

SUMMARY OF KEY ECONOMIC FORECASTS

	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
GDP (% qoq)	-0.3	-0.2	-0.5	-0.9	-1.5	-0.5	0.0	0.1	0.5	1.2
GDP (% yoy)	2.1	1.0	-0.1	-1.9	-3.1	-3.3	-2.9	-1.9	0.1	1.8
CPI (% qoq)	0.7	1.6	1.5	-0.5	0.3	0.7	0.6	0.6	0.5	0.5
CPI (% yoy)	3.4	4.0	5.1	3.4	3.0	2.1	1.1	2.2	2.4	2.2
Employment (% qoq)	-1.0	1.2	0.2	0.6	-1.1	-1.0	-0.9	-0.4	-0.2	0.0
Employment (% yoy)	-0.2	0.8	1.1	0.9	0.8	-1.3	-2.4	-3.4	-2.5	-1.5
Unemployment Rate (% sa)	3.8	4.0	4.3	4.7	5.0	5.6	6.4	7.0	7.5	7.7
Current Account (% GDP)	-8.0	-8.4	-8.7	-9.0	-8.5	-7.1	-6.1	-5.2	-5.0	-4.9
Terms of Trade (% qoq)	4.2	-0.4	-1.0	-0.9	-5.0	-2.1	-1.4	-1.1	-0.7	-0.4
Terms of Trade (% yoy)	11.6	10.7	5.8	1.8	-7.1	-8.7	-9.1	-9.3	-5.2	-3.5

KEY ECONOMIC INDICATORS

	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09	May-09
Retail Sales (% mom)	0.3	0.3	-1.2	-0.1	-0.6	-1.2	0.3	-0.4	..	..
Retail Sales (% yoy)	-0.9	2.2	0.7	-4.1	-0.9	-3.7	-6.9	-1.9	..	..
Credit Card Billings (% mom)	-0.3	1.3	-1.8	-0.8	-2.2	1.5	0.8	-2.8	2.3	..
Credit Card Billings (% yoy)	2.6	2.5	0.9	-0.9	-3.8	-2.4	-1.9	-4.8	-1.6	..
Car Registrations (% mom)	-3.7	11.1	-1.0	-19.7	12.7	-14.1	-15.1	7.3	-3.0	..
Car Registrations (% yoy)	-30.5	-15.6	-19.9	-34.4	-23.7	-36.5	-44.6	-32.9	-41.0	..
Building Consents (% mom)	-6.9	8.1	-19.4	3.8	-7.0	-12.9	11.6	-4.6	..	..
Building Consents (% yoy)	-43.2	-28.4	-42.8	-39.7	-41.4	-51.7	-40.0	-34.5	..	..
REINZ House Price (% yoy)	-5.7	-6.1	-4.3	-4.1	-4.8	-4.4	-2.2	-4.0	-1.4	..
Household Lending Growth (% mom)	0.4	0.2	0.2	-0.1	0.2	0.2	0.2	0.1	..	..
Household Lending Growth (% yoy)	7.2	6.6	5.8	4.8	4.2	3.8	3.1	2.8	..	..
Roy Morgan Consumer Confidence	91.4	108.6	99.7	99.0	102.9	103.7	98.8	94.7	101.1	104.0
NBNZ Business Confidence	-20.5	1.6	-42.3	-43.0	-35.0	..	-41.2	-39.3	-14.5	..
NBNZ Own Activity Outlook	4.7	16.7	-11.4	-14.1	-21.5	..	-20.1	-21.2	-3.8	..
Trade Balance (\$m)	-848	-1252	-994	-594	-341	-103	487	324	..	..
Trade Balance (\$m annual)	-4369	-5048	-5269	-5234	-5614	-5406	-5162	-4796	..	..
ANZ World Commodity Price Index (% mom)	-3.4	-5.1	-7.6	-7.4	-7.4	-4.3	-4.6	1.0	2.5	..
ANZ World Commodity Price Index (% yoy)	3.5	-2.1	-11.1	-18.3	-24.3	-26.5	-30.7	-31.4	-29.5	..
Net Migration (sa)	340	-20	40	-290	320	820	1620	1730	2160	..
Net Migration (annual)	4938	4403	4329	3569	3814	4538	6160	7482	9176	..

Figures in bold are forecasts. mom: Month-on-Month qoq: Quarter-on-Quarter yoy: Year-on-Year

SUMMARY OF KEY MARKET FORECASTS

NZ FX rates	Actual		Current	Forecast (end month)						
	Mar-09	Apr-09	25-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
NZD/USD	0.530	0.572	0.616	0.540	0.510	0.480	0.470	0.470	0.480	0.490
NZD/AUD	0.797	0.801	0.787	0.771	0.767	0.762	0.756	0.764	0.774	0.778
NZD/EUR	0.406	0.433	0.439	0.422	0.408	0.400	0.404	0.420	0.429	0.434
NZD/JPY	51.8	56.6	58.3	54.0	50.5	47.0	45.6	46.5	48.0	50.0
NZD/GBP	0.373	0.389	0.387	0.372	0.357	0.338	0.327	0.324	0.327	0.329
NZ\$ TWI	53.8	57.0	58.5	54.6	52.4	50.4	49.8	50.6	51.6	52.4
NZ interest rates	Mar-09	Apr-09	25-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
OCR	3.43	3.24	2.50	2.50	2.25	2.00	2.00	2.00	2.50	3.50
90 day bill	3.24	3.12	2.77	2.90	2.40	2.40	2.40	2.40	3.10	4.10
10 year bond	4.78	5.24	5.77	5.40	5.10	4.90	5.00	5.10	6.00	6.10
International	Mar-09	Apr-09	25-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
US Fed funds	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00	1.50	2.00
US 3-mth	1.19	1.02	0.66	0.90	0.70	0.50	0.70	1.25	1.75	2.25
AU cash	3.25	3.00	3.00	3.00	2.50	2.00	2.00	2.00	2.00	2.75
AU 3-mth	3.14	3.08	3.16	3.20	2.30	2.30	2.30	2.40	2.60	3.30

KEY RATES

	22 Apr	18 May	19 May	20 May	21 May	22 May
Official Cash Rate	3.00	2.50	2.50	2.50	2.50	2.50
90 day bank bill	3.04	2.77	2.79	2.78	2.79	2.78
NZGB 07/09	2.95	2.77	2.66	2.68	2.68	2.68
NZGB 11/11	3.50	3.51	3.57	3.63	3.62	3.66
NZGB 04/13	4.20	4.36	4.43	4.47	4.47	4.57
NZGB 12/17	5.10	5.39	5.47	5.53	5.52	5.72
2 year swap	3.59	3.37	3.43	3.46	3.49	3.55
5 year swap	4.70	4.65	4.71	4.77	4.81	4.92
RBNZ TWI	55.8	57.0	57.8	57.9	58.3	58.5
NZD/USD	0.5554	0.5857	0.5975	0.6012	0.6099	0.6141
NZD/AUD	0.7894	0.7832	0.7785	0.7781	0.7855	0.7884
NZD/JPY	54.52	55.55	57.61	57.56	57.65	57.79
NZD/GBP	0.3799	0.3867	0.3896	0.3880	0.3863	0.3874
NZD/EUR	0.4298	0.4359	0.4404	0.4414	0.4422	0.4412
AUD/USD	0.7036	0.7478	0.7675	0.7727	0.7764	0.7789
EUR/USD	1.2923	1.3438	1.3567	1.3620	1.3792	1.3920
USD/JPY	98.17	94.85	96.42	95.75	94.52	94.11
GBP/USD	1.4619	1.5145	1.5338	1.5493	1.5789	1.5853
Oil	46.65	58.99	58.99	59.52	61.45	60.49
Gold	883.65	921.60	921.90	927.25	941.90	952.60
Electricity (Haywards)	6.88	1.73	10.80	7.01	15.76	1.00
Milk futures (US\$/contract)	85	85	85	85	85	85
Baltic Dry Freight Index	1869	2605	2644	2665	2707	2786

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.
- The Bank has a joint venture relationship with ING (NZ) Holdings Limited (ING). ING and its related companies 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;
- 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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