

### RBNZ Official Cash Rate Review

#### Key points

- > **The OCR was reduced by 100bps to 6.5 percent.**
- > **The decision was heavily influenced by global events.**
- > **The statement flagged more easings to come, though they are conditional on inflation pressures easing and the global scene.**
- > **RBNZ expressed discomfort over still elevated domestic inflation pressure, something which markets should not lose sight of, but is applying the medium-term framework.**
- > **We continue to look for a 50bp cut in December and for the OCR to fall below 5 percent.**

#### Assessment

**The Governor reduced the OCR by 100bps to 6.5 percent.** This decision was in line with our expectations, and the market's. Certainly, today's move was unprecedented but so too are the times we are navigating through. The biggest global financial shock in a generation was always going to require a significant policy response. The Governor made it clear that today's decision was largely influenced by the global situation, *"ongoing financial market turmoil and a deteriorating outlook for global growth have played a large role in shaping today's decision."* It is becoming clear that NZ is indeed seeing flow-on consequences via weaker demand, restricted credit, and consumer and business caution. To be fair, some avenues are encouraging, including lower oil prices, a weaker currency, and expansionary fiscal policy, which the Governor acknowledged. However, it is clear that NZ's terms of trade is falling (hence ignore the oil-impetus effect), the nation needs a lower currency to address the external imbalance, and fiscal policy is still somewhat constrained given the deterioration in the fiscal position (although the balance sheet is remarkably healthy). Monetary policy is hence playing a key role in trying to mitigate some of the "extreme" downside risks to the economy, which has already experienced six months of contraction.

**Inflation, while not a predominant policy concern for now, remains a background concern.** In a timely reminder that the RBNZ has not totally cast aside inflation concerns, the Governor reiterated the Bank's focus on medium-term inflation, and expressed discomfort at their stickiness. The Q3 CPI data out earlier this week, showing still broad-based inflation pressure, highlights the risk that the RBNZ is running in easing policy aggressively before inflation has actually eased. But given the domestic and

economic outlook, and the forward looking nature of the RBNZ, today's decision was wholly appropriate.

**Going forward, the RBNZ remains on a clear easing bias but this is conditional** on domestic inflation pressures easing and how the global scene plays out. The inflation conditionality was strengthened somewhat between September and October from *"signs of declining inflation pressures"* to *"evidence of actual reductions in domestic cost pressures"*. We note the choice of the term "pressures" as opposed to "outcomes", which means it is the inputs into the inflation generating process as opposed to the numbers themselves that matters; a further sign the RBNZ is focused on the medium-term picture.

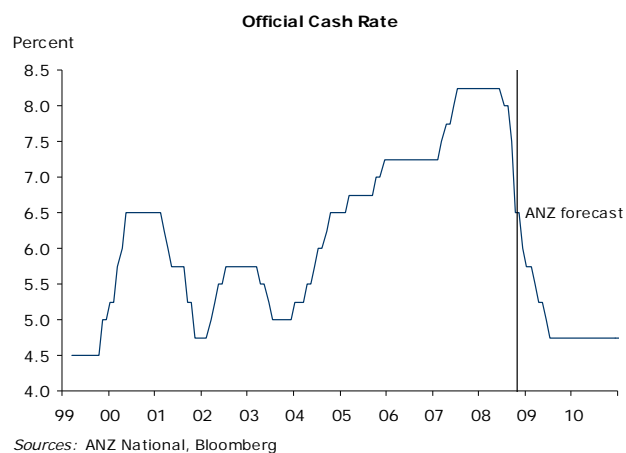
**The RBNZ has highlighted concerns over the stickiness of domestically generated inflation** (particularly from the labour market, construction costs, local body rates and electricity prices). We certainly concur with this view. A lot of the domestic inflation pressure is emanating from largely uncontestable pockets of the economy, which means a larger demand side adjustment is required to dampen the aggregate inflation picture. However, we would expect other areas of *"residual"* inflation pressure, such as the labour market and construction costs, to ease rapidly given the economic picture.

The September quarter employment report (due November 6) is shaping up as an important gauge of medium-term inflation pressure and "actual evidence", as are various pricing gauges from confidence surveys. Looking forward, the RBNZ will most certainly be taking a strong axe to their September economic projections when a full-forecast round is prepared for the December *Monetary Policy Statement* (due December 4). Indeed, given the global backdrop, we find it hard

to envisage economic growth in 2009 surpassing 2008's 0.5 percent likely final outturn.

**The media conference following the decision largely relayed the statement**, although with a couple of interesting aspects. Firstly, the Governor appeared to broadly endorse market pricing, which looks consistent with the Bank's easing bias. Second, in a similar fashion to the RBA, the Governor noted that today's move should not necessarily be taken as an indicator of moves to come. Net on net, the Governor once again has given himself and the Bank a huge degree of flexibility to respond going forward. With a cash rate remaining at the high "neutral" zone at present (compensating higher inflation expectations versus higher funding costs, with the latter arguing for a lower neutral rate), the RBNZ still has plenty of scope to ease.

**Going forward, we expect the pace of easing to slow, but the big picture is pointed to the OCR ending up sub 5 percent.** Recent developments make it clear that emerging markets are now also suffering heavily, and unlike previous cycles, the developed world has their own problems and cannot provide the usual lifeline. This points to global developments still having a key influence on policy deliberations going forward.



## Full text of the statement

OCR reduced to 6.5 percent

The Reserve Bank today reduced the Official Cash Rate (OCR) from 7.5 percent to 6.5 percent.

Reserve Bank Governor Alan Bollard commented that "ongoing financial market turmoil and a deteriorating outlook for global growth have played a large role in shaping today's decision.

"Economic activity in New Zealand will be further constrained, relative to the outlook presented in our September Monetary Policy Statement, by these international developments. New Zealand can expect to face lower demand for exports and credit is likely to be less readily available. In this environment consumers and businesses are likely to be more cautious and curtail spending.

"The reduction in domestic spending will be partly offset by the depreciation of the New Zealand dollar over the past few months, falling oil prices and the recent loosening of fiscal policy.

"With weaker short-term growth and sharply lower oil prices we now expect that annual CPI inflation will return to the target band of 1 to 3 percent around the middle of 2009. However, we still have concerns that domestically generated inflation (particularly in labour costs, local body rates, electricity prices and construction costs) is remaining stubbornly high.

"Consistent with the Policy Targets Agreement, the Bank's focus will remain on medium-term inflation. Should the outlook for inflation evolve as projected we would expect to lower the OCR further. However, the timing and extent of OCR reductions over the coming months will depend on evidence of actual reductions in domestic cost pressures as well as how the global financial developments play out."

## 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.

This document is provided for informational purposes only and does not constitute an offer to sell or solicitation to buy any security or other financial instrument. No part of this document can be reproduced, altered, transmitted to, copied to or distributed to any other person without the prior express permission of the Bank.

This document is a necessarily brief and general summary of the subjects covered and does not constitute advice. You should obtain professional advice before acting on the basis of

This document has been prepared by ANZ National Bank Limited.

ANZ (part of ANZ National Bank Limited), Level 7, 1 Victoria Street, Wellington 6011, New Zealand Phone 64-4-802 2000 Fax 64-4-496 8639 <http://www.anz.co.nz> e-mail [ecnmcs@anz.com](mailto:ecnmcs@anz.com)

any opinions or information contained in it. The information contained in this document is given in good faith, has been derived from sources perceived by it to be reliable and accurate and the Bank shall not be obliged to update any such information after the date of this document. Neither the Bank nor any other person involved in the preparation of this document accepts any liability for any opinions or information (including the accuracy or completeness thereof) contained in it, or for any consequences flowing from its use.

#### UNITED STATES DISCLAIMER

This document is being distributed in the United States by ANZ Securities, Inc. ("ANZ S") (an affiliated company of Australia and New Zealand Banking Group Limited ("ANZBG") and the Bank), which accepts responsibility for its content. Further information on any securities referred to herein may be obtained from ANZ S upon request. Any US person(s) receiving this document and wishing to effect transactions in any fixed income securities referred to herein should contact ANZ S 1177 Avenue of the Americas, New York, NY 10036 USA, Tel: 1-212-801-9160, Fax: 1-212-801-9163, not its affiliates.

This document is issued on the basis that it is only for the information of the particular person to whom it is provided. This document may not be reproduced, distributed or published by any recipient for any purpose. This document does not take into account your personal needs and financial circumstances. Under no circumstances is this document to be used or considered as an offer to sell, or a solicitation of an offer to buy.

In addition, from time to time ANZBG, the Bank, ANZ S, their affiliated companies, or their respective associates and employees may have an interest in any financial products (as defined by the Australian Corporations Act 2001), securities or other investments, directly or indirectly the subject of this document (and may receive commissions or other remuneration in relation to the sale of such financial products, securities or other investments), or may perform services for, or solicit business from, any company the subject of this document. If you have been referred to ANZBG, the Bank, ANZ S or their affiliated companies by any person, that person may receive a benefit in respect of any transactions effected on your behalf, details of which will be available upon request.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all of the securities and issuers referred to herein. The author however makes no representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. No part of the author's compensation was, is or will be directly or indirectly related to specific recommendations or views expressed in this document. ANZBG, the Bank, ANZ S, their affiliated companies, their respective directors, officers, and employees disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.