

# THE MOMENT OF TRUTH

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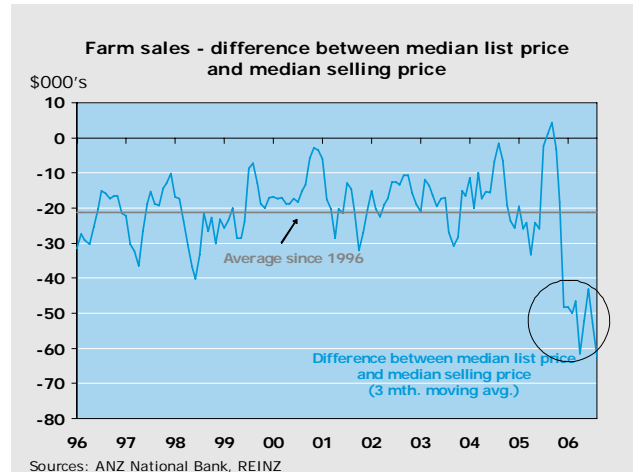
- The NZD surprised with its resilience this week given data that shifted the risk profile for monetary policy to no-change from the RBNZ. We expect ratification of the no-change view next week to see the NZD/AUD and NZD/USD test 0.8760 and 0.6880.

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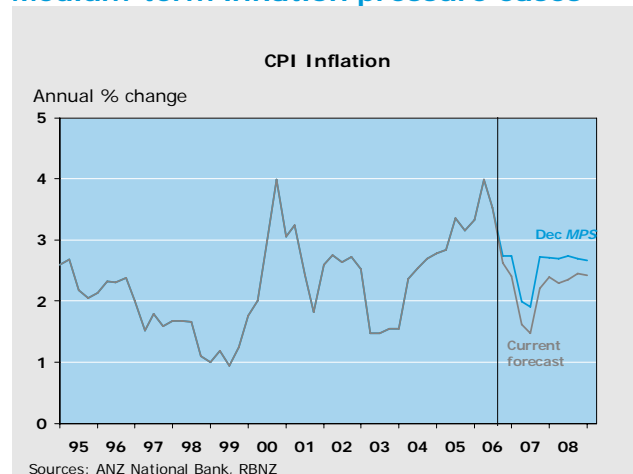
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## ECONOMIC OVERVIEW

**The Reserve Bank takes centre stage next week. We expect no change to the OCR. Strength in the Quarterly Survey of Business Opinion has the market biased towards economic momentum continuing to accelerate. While we acknowledge the trend, it is significant that the survey does not fully capture rural sentiment, where there is considerable unease towards the currency and where the property market is starting to turn.**

### What's ahead...

- RBNZ's *OCR Review* (0900NZDT Thursday 25 January). No change but hawkish tenor to remain. Our preview is detailed on page 6.
- NZ Dec credit card billings (due 1500NZDT Wednesday 24 January). Credit cards expected to have been given a good workout over the holiday shopping season. Strong monthly increase expected, especially after the 0.9 percent decline in November.
- Australian Q4 CPI (1330NZDT Wednesday 24 January). We expect headline CPI to be flat, and core inflation to be up 0.7 percent for the quarter.

### What's the view

This week's weaker headline CPI, and easing trajectory in non-tradable inflation and other core measures, was the final nail in the coffin for the Reserve Bank not to hike OCR next week.

With two major pieces of data (GDP and CPI) coming in weaker than the Reserve Bank expected, it is difficult to envisage the Bank raising interest rates next week. Further falls in pump prices and aggressive petrol price voucher discounting add further downside risks to the Reserve Bank's 0.6 percent forecast for Q1 CPI.

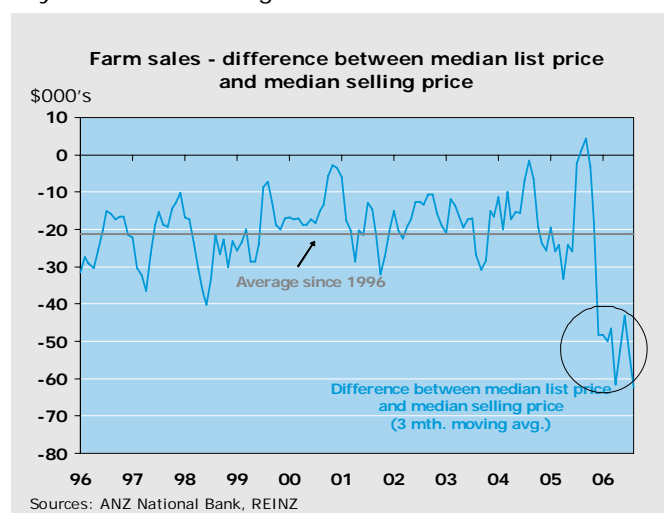
It is interesting to see the market reaction to the CPI release with the NZD holding up (after an initial fall) and the interest rate market still looking for a hike at some stage. This is obviously partly an overhang from Tuesday's QSBO survey showing a pick up in headline confidence, and an improvement in activity indicators and employment and investment intentions. While the QSBO showed the same broad trends as the *National Bank Business Outlook*, the overall level of gains in the QSBO looked healthier, notably on the employment front.

Based on historical correlations, the QSBO is forecasting Q4 GDP growth of around  $\frac{3}{4}$  percent, and the strength in employment presents a direct challenge to the idea that pressure on corporate earnings would eventually filter through to the household sector.

However, the divergence between the *National Bank Business Outlook* and QSBO can easily be explained by sampling, with one directly capturing the rural sector (farmers), and one not. Agriculture sector confidence is amongst the most bearish in the *National Bank Business Outlook* across business

confidence, profits and significantly employment. The late December run-up in the currency will have a marked impact on the sector. The lamb price schedule has fallen sharply in the new year. The rural sector was a key driver of the last leg of the housing market cycle. Anecdotally there have never been so many rural properties on the market.

Buyer resistance is emerging with the gap between the median farm list price and the median sale price increasing significantly in recent months, from a typical average of \$20k to close to \$60k. This suggests that prices could come under downward pressure in the near-term and going by previous cycles we would expect this to filter through to the residential market. As noted in our *Market Focus* of 20 November 2006, excess housing demand is greatest in the rural aligned regions, and looking forward, a turn in the rural property cycle will be a key factor eliminating that.



### Data this week...

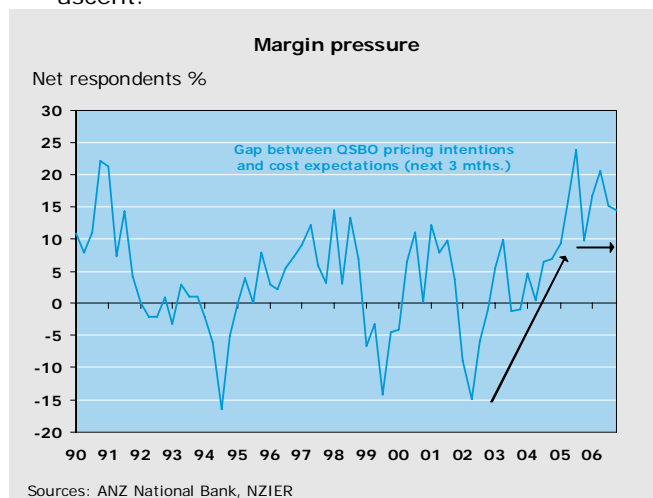
- **NZ NZIER Quarterly Survey of Business Opinion.** Business confidence rose to +3. Capacity utilisation eased to 91.7 while employment and investment intentions rose.
- **NZ CPI.** Q4 CPI fell 0.2 percent, taking the annual rate to 2.6 percent. Annual non-tradable inflation eased to 3.8 percent.
- **NZ Retail Sales.** Total sales for November fell 0.2 percent while core sales fell 0.1 percent.
- **NZ REINZ housing market data.** The average number of days to sell a house was unchanged in December as was the median selling price. The number of house sales was 19.4 percent above last year.
- **US.** Q4 CPI increased 0.5 percent while core CPI increased 0.2 percent (2.6 percent apc). The Fed's Beige Book described the economy as growing at a modest pace.
- **Global official interest rates.** The BoJ and the BoC both left rates unchanged at 0.25 percent and 4.25 percent respectively.

## ECONOMIC SPANNER

**A key assumption underlying our economic view is that declining corporate profitability will eventually see a fall in labour demand and this in turn will transfer the slowdown to households. However, recent data strongly challenges this view, particularly the labour market indicators from the QSBO. Although we are cautious, we are sticking to our guns.**

The pick up in labour market indicators such as employment intentions, overtime worked, difficulty in finding labour, and labour as a constraint to business all surprised us with their strength in the December QSBO. This was particularly significant because we see the corporate sector as under significant pressure from falling margins and softening demand. Although we are hesitant about ignoring the recent QSBO indicators, we remain wary at this juncture of placing too much weight on them. We still believe that the economic slowdown will be transferred to households through a turn in the labour market.

- **Profits are still down!** Despite an improvement in profit expectations in the QSBO (likely as a result of falling petrol prices), profits are down. As an indicator of corporate profits, the corporate tax take is 3.0 percent down on a year ago, while business investment is 5.2 percent below last year's levels.
- **Cost pressures remain strong.** Despite recent petrol price falls, margins remain under significant strain. Within the QSBO, the gap between the number of firms intending to increase their prices and those expecting higher costs in the next three months is largely unchanged from September and at an elevated level. Cost and margin pressure is more than a petrol phenomenon with rates, public sector charges, rents, wages, non-oil commodity prices, and regulatory imposed costs on the ascent.



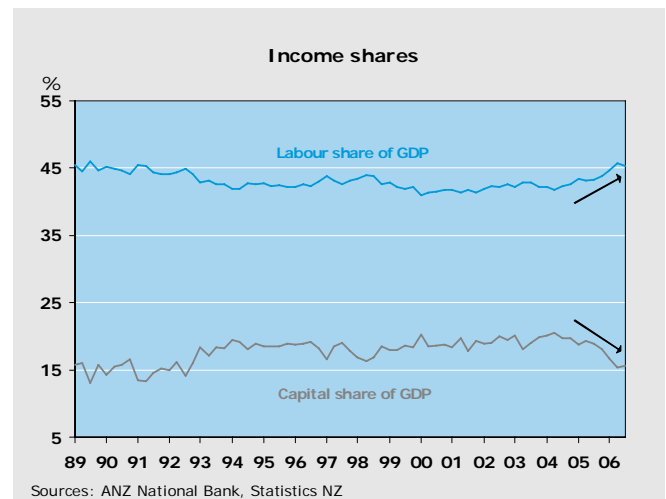
- **There is firm evidence of a strong cost focus across some organisations.** We can't go past the number of large corporates that are already starting to bite the bullet on the

rationalisation front (e.g. Telecom and Air New Zealand), and we suspect more is pending, albeit gradually.

- **Productivity performance is woeful.**

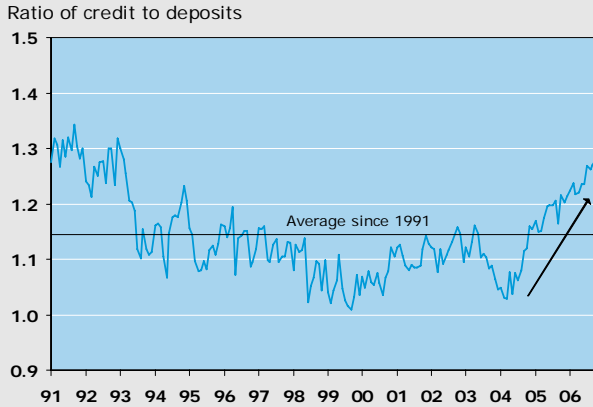


- **The respective shares of income are pervasive.** The share of income accruing to labour is close to a 15 year high and rising at the expense of capital. This ratio tends to creep up under a left-leaning government but are we about to see a new broom? (Interestingly, we note the same ratio in the US is showing capital's share near all-time highs, and there is speculation how this may change over time under the Democrat's congress policy prescription).



- **Watch for the economic impact of the Holidays Act from April 1.** Faced with the cost of additional leave provisions, we expect businesses to remain very coy about employment.
- **Liquidity is tightening.** As an indicator of liquidity for the business sector, the ratio of business credit to deposits has risen to its highest level since 1992 and indicates that cash-flow may be becoming a growing problem.

**Corporate liquidity**

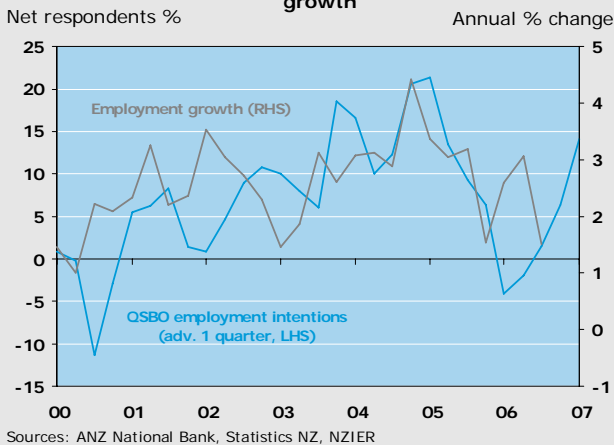


**The upshot**

Although recent QSBO indicators appear to be at odds with our view that a fall in corporate profitability will be passed onto the household sector through a turn in the labour market, we are maintaining the faith. Other indicators suggest the profit theme will progressively dampen labour demand, which already looks to be occurring in rural based areas.

- **The link between employment intentions and actual employment growth is loose.** What firms say they will do and what they actually do are two distinct things. Since 2000, the relationship between QSBO employment intentions and annual HLFS employment growth has been relatively weak; the relationship with quarterly employment growth is even weaker.

**Employment intentions and HLFS employment growth**



- **The QSBO misses a key sector of the New Zealand economy – agriculture.** We note that the employment intentions within the National Bank *Business Outlook* are weakest in the agriculture industry. The increase in employment intentions within the QSBO was also solely due to an increase in the upper North Island with both agricultural dominated regions of the lower North Island and South Island recording falls. This fall may suggest we are already seeing some signs of an easing in growth in rural areas. This suggests a gradually filtering through to the industries (such as manufacturing and services) in the rural districts, and from here progressively to the upper North Island. As the head of our rural bank notes, New Zealand is after all one big farm!

## INTEREST RATE STRATEGY

**Expectations of an OCR hike next week have been pared back after data this week failing to deliver a smoking gun. The market has moved from a 50/50 call to a 20/80 call.**

### Market themes...

- Weaker data moves market from 50/50 to 80/20 for next week's OCR decision.
- NZD supported on dips as offshore accounts continue to be hungry for yield.
- Lower oil prices to deliver inflation relief, and buy the RBNZ more time.

### Outlook...

The market remains on tenterhooks following generally weaker data seen this week, with CPI and retail sales offsetting stronger QSBO data. CPI came in at -0.2 percent, which was below market expectations of a flat result. Lower petrol prices was a key influence, with ex-petrol inflation still elevated. However, the encouraging aspect from a RBNZ point of view is that non-tradable inflation came in under the RBNZ's 1 percent forecast at 0.8 percent. Retail sales was slightly weaker than market expectations, down 0.2 percent versus an expected 0.1 percent decline. We agree that if the data is sliced and diced, then there is an undercurrent of inflationary pressure, but with two key releases (Q3 GDP end of December and Q4 CPI this week) undershooting the RBNZ's forecasts, we find it difficult to see a hike next week even allowing for the strength in the labour and housing markets.

Given what we have seen this week in terms of the data, we feel comfortable about being patient to enter into received side trades. We are of the view the RBNZ will leave rates on hold but continue to talk with a hawkish tone. Time seems to be on the RBNZ's side and by leaving the door open the RBNZ can view the HLFS and Christmas retail sales data in February. It is for this reason the market will continue to price in hikes.

Based on our view, we continue to hold six months bills versus being paid the NZ 2yr IRS. The front end of the swaps curve is expected to hold in the event of a no change decision, as the market will still look to price in a hike at the March meeting. In the event of a hike you'll have protection from a sell-off in the front dated swaps.

Gauges for NZ interest rates yields		
Gauge	Direction	Comment
RBNZ	↑	RBNZ's projected 90-day tuck is higher than the market at present.
NZ data	↔	Domestic data printing mixed.
Fed Funds	↔	Recent data printing stronger.
RBA	↑	Odds for a rate hike getting shorter.
US 10 year	↑	Market shrugging off stronger data.
NZ swap spreads	↓	Risks point wider with offshore demand for bonds.
Flow	↔	Lack of liquidity with market staying on the sidelines ahead of next week's OCR decision.
Technicals	↔	Tight ranges limiting technical picture.

### Borrowing strategies we recommend at present

A better than anticipated Q4 inflation number during the week has done little to alleviate the pressures facing borrowers out along the term yield curve. Ongoing demand to pay fixed continues as borrowers take the lower cost of funds available in the term curve. Focus next week turns to the *OCR Review* on Thursday. Although no rate hike is expected it is widely anticipated that the RBNZ will maintain its hawkish rhetoric based around inflation concerns through 2008. There is no change to our view that borrowers should continue to pay the 3-5 year part of the curve. Those with more dovish outlooks for interest rates through 2008 are encouraged to look at option based strategies that provide some downside potential.

### Trading themes we favour at present

We see value in going long out to 6 months and paying in the 2 year.

## OCR PREVIEW (DUE 9:00AM 25 JANUARY)

**We expect the Reserve Bank to leave the OCR unchanged at their January Review. While the tenor of the text is expected to remain hawkish with the door to a hike left open, market pricing looks to another increase in the OCR.**

**The Reserve Bank explicitly put a rate hike on the table in the December *Monetary Policy Statement (MPS)*.** The combination of strong housing market data and building momentum across leading economic gauges (such as business confidence) naturally saw the market price in a material probability of such an outcome.

**However, we expect the Reserve Bank to maintain a steady line and leave the OCR unchanged.** While there are clear signs of accelerating momentum, we remain equally mindful of:

- The recent run-up in the NZD, with the TWI 4.4 percent above the RBNZ's December forecasts.
- Two bell-wether releases – namely Q3 GDP and Q4 CPI – coming in below the RBNZ's forecasts.
- Core inflation measures, while elevated, are nonetheless easing. Non-tradable inflation declined to 3.8 percent – the lowest in 3 years, and various core inflation measures which the Reserve Bank monitors (trimmed mean, exponentially smoothed and factor model) also show a receding bias.
- An updated inflation track will be lower than presented in the December *MPS*. Short-term inflation latitude is being provided by lower petrol prices, with the March 2007 quarter result expected to be soft. The headline inflation rate is set to fall towards 1½ percent by mid 2007. While lower petrol prices are a one-off that the Reserve Bank has stated it will look through, it nonetheless reduces medium-term inflation pressure through easing pressure on inflation expectations (refer page 7).

**Collectively, these developments have in effect bought the Reserve Bank more time.**

We remain equally mindful of the additional policy traction they are receiving along the yield curve as international interest rates have moved up over recent weeks. As noted last week, fixed lending rates along the curve are over 8 percent, leaving borrowers with little place to run. We see this as a significant development as 2 to 3 months ago low global yields allowed the five year fixed rate to hit 7.5 percent, in effect giving borrowers an area to hide.

**Signs of accelerating growth – and hence more persistent pressure on medium-term inflation, will remain a sticking point.** Yet with the Reserve Bank's December *MPS* forecasts predicting a 0.7 percent GDP result for Q4 2006, and 0.6 percent for H1 2007, the evidence is far

from equivocal that momentum is building beyond this. Given that the Reserve Bank's near-term forecast overestimated growth by a wide margin, expect the Reserve Bank to remain firmly on datawatch mode and take a more conservative line on their next growth forecasts.

**The tenor of the statement will clearly remain hawkish** and the door to a further hike left wide open in such an environment. We expect the usual suspects from the December *Statement*, that further tightening cannot be ruled out and any easing is some considerable way off, to remain in the text.

**Market pricing looks to more than reflect this.** While expectations for a hike next week have diminished from 60 percent at one stage to 24 percent currently, there is still an 80 percent probability of one hike by mid-year priced in. In our eyes, given that there are early signs that the slowdown in economic growth is finally starting to ease non-tradable inflation, the Reserve Bank needs to be absolutely certain that economic activity is not only rebounding, but accelerating away before increasing the OCR.

### Expectations for OCR announcement dates as implied by market pricing

OCR dates	Change (bp)	Cummulative	Probability (+25bps)
Thu 25-Jan-07	6	6	24
Thu 8-Mar-07	9	15	60
Thu 26-Apr-07	0	15	60
Thu 7-Jun-07	5	20	80
Thu 26-Jul-07	0	20	80
Thu 13-Sep-07	-1	19	76
Thu 25-Oct-07	-4	15	60
Thu 6-Dec-07	-2	13	52

### Financial market implications...

We expect a 5 to 6 point rally in the front-end of the curve on a no change decision but the magnitude to clearly be capped by continued hawkishness, which will leave the market attuned to a potential March move. Yet if there is a surprise to be had in the tenor of the text, we suspect it is likely to come from a market that is perhaps looking for too much – particularly on the currency side, given that the favoured outcomes are either for a hike, or a hawkish stance that builds on December rhetoric.

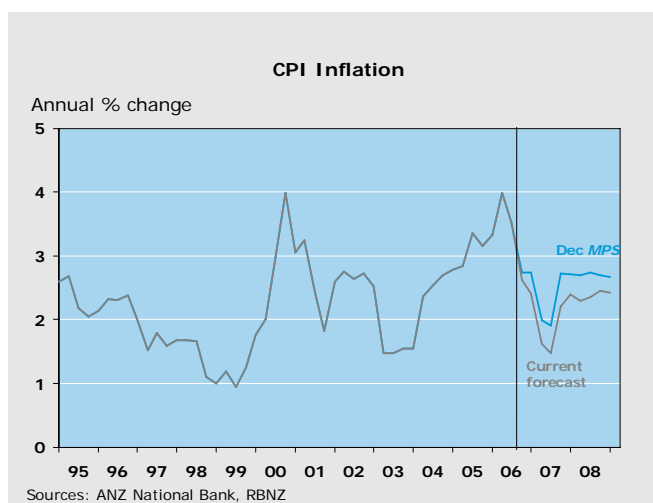
## INFLATION RELIEF

**Updated inflation forecasts at the Reserve Bank will show lower medium-term inflation pressure relative to their December *Monetary Policy Statement*. Presented with such a profile, we find it difficult to envisage the Governor raising rates next week.**

At the December *Monetary Policy Statement (MPS)*, the Reserve Bank threatened to hike interest rates in early 2007 over concerns about upward pressures on the medium-term inflation outlook. However, since then:

- oil prices have receded sharply (the Dubai oil price is currently below US\$50/bbl, a level the Reserve Bank did not expect to reach at all in their forecasts)
- the starting point for non-tradable inflation is lower
- growth, and hence the starting point for the output gap, is also lower
- the currency is 4.4 percent above the Reserve Bank's assumption.

All are key inflation suppressants. Counteracting this has been generally stronger signs of domestic activity, which implies elongated pressure on medium-term inflation through a more sticky output gap.



Using the Reserve Bank's inflation model calibration, we are able to generate an inflation forecast based on changes since the December *MPS*. We assume that:

- oil prices remain at current levels.
- the TWI will decline but remain at a higher level throughout the forecast period compared to the December *MPS*<sup>1</sup>
- the opening position for the output gap is marginally lower than in the December forecasts. In effect we have taken half the GDP error for Q3 to the output gap, and assume the outlook for GDP remains broadly similar to the December *MPS*.

<sup>1</sup> This is consistent with the methodology used by the Reserve Bank over previous *MPS* forecasts.

The forecasts generated show inflation heading down towards 1½ percent by mid-year, but more importantly the medium-term inflation forecast stays at below 2½ percent (compared to the 2.7 percent in the December *MPS*). The material change largely reflects the significant role assigned to inflation expectations, which has the highest weighting in the Reserve Bank's forecasting model.

We note that the updated medium-term inflation profile is roughly what the Reserve Bank forecast in their March and June *MPS* forecasts last year, when the Bank had a neutral stance on policy.

Of course the challenge to our revised forecast is the strength of forward looking indicators, which threatens to add to pipeline pressure through persistent pressure on the output gap. We note that the Reserve Bank's growth projections already incorporate a relatively optimistic 0.7 percent forecast for Q4 2006 and 0.6 percent for each quarter thereafter. Confidence gauges are broadly pointing to growth in line with this and we suspect the Reserve Bank will remain coy about revising such growth rates higher on an additional month's worth of tentative data.

However, even if the Reserve Bank's growth forecasts were to be revised higher, the revisions would need to be around 0.4 percentage points per quarter higher over the forecast period (or the potential growth assumption significantly revised down) to generate an inflation profile equivalent to the December *MPS*. This is something we find hard to buy into given that financial conditions remain tight.

Of course, oil prices provide a double-edged sword. A sharp increase could once again push inflation higher, and while it is a one-off, its impact on expectations cannot be completely looked through. However, it will take a material and sustained increase in oil prices to impact on inflation expectations sufficiently to deteriorate the medium-term inflation outlook. Similarly, a substantial fall in the currency will push tradable inflation higher and keep inflation expectations elevated. While both are potential risks to the inflation outlook, they will unlikely be treated as the central scenario in the Reserve Bank's deliberations.

### Financial Market Implications

Given that the Governor will be presented with a new inflation forecast profile showing less medium-term inflation pressure compared to the December *MPS*, we find it difficult to see him raising interest rates next week. While recent business confidence indicators point to economic activity accelerating, the Governor has time to wait and assess more incoming data to determine if recent momentum is indeed sustained or temporary.

## CURRENCY STRATEGY

**The NZD surprised with its resilience this week given data that shifted the risk profile for monetary policy to no-change from the RBNZ. We expect ratification of the no-change view next week to see the NZD/AUD and NZD/USD test 0.8760 and 0.6880.**

### Market themes...

- Domestic data points to no move from the RBNZ, yet the NZD remains supported.
- Oil prices continue to ease.
- US data continues to firm but yields look capped at present.
- BOJ holds but with a 6-3 vote a February move looks likely.

### Outlook...

This week's expected downward bias in the NZD failed to materialise despite the tenor of data firmly shifting the risk profile towards no move from the RBNZ. While the bond and swaps market has partly moved to reflect this (with the probability of a hike falling from 50 percent to 24 percent), the market has in effect just transferred the risk to a March hike, and the NZD remains supported by yield in this environment.

To us, the generally bullish view of the NZD will continue to be questioned on two levels.

- The NZ interest rate market remains more hawkish than our core views. A no-change decision – with hawkish overtures – is expected to set a weak bias to the kiwi over the week.
- Global interest rate sentiment continues to point to a closing yield differential. While longer dated US 2 and 10 year yields are facing resistance at 4.9 and 4.8 percent respectively, the bias for yields will remain up given the tenor of incoming US data, which is sharply testing the easing view. We see firming economic sentiment in the US as equally comforting for when the BOJ raises rates (with the committee already divided this suggests a February move is very likely), and if the RBA feels it needs to go again, with next week's CPI result likely to be key.

Capitulating international oil prices – down 4.7 percent over the week, following a 5.9 percent decline in the previous week – is currently a key global theme. You can slice and dice the currency impact on the NZD a number of ways ranging from terms of trade and hence currency positive, to inflation and hence yield and currency negative. Perhaps a key lesson is that it demonstrates from

another angle how quickly market sentiment can turn, and we remain very wary of the carry trade in this regard, particularly given where the risk profile for global interest rates looks to be gravitating.

From a technical perspective we expect the NZD to remain stuck in familiar ranges although no-change from the RBNZ this week is expected to see the NZD/AUD and NZD/USD test 0.8760 and 0.6880.

NZD vs AUD: monthly directional gauges		
Gauge	Direction	Comment
Fair value	↓	Fair value 0.85-0.88.
Yield	↓	Too much factored in for RBNZ and too little for RBA.
Commodities	↔	Hard continue to outshine soft but lower oil helping NZ
Partial indicators	↓	NZ domestic economy remains housing dominant while Australian strength looks broader based.
Technicals	↔	Topside capped at 0.8880. Initial resistance at 0.8760.
Sentiment	↔	No mans land.
Other	↑	Liquidity still plentiful. AUD positioning looks extreme.
<b>On balance</b>	↓↔	<b>Mildly bearish with the RBNZ not set to deliver. Aus CPI key.</b>

NZD vs USD: monthly directional gauges		
Gauge	Direction	Comment
Fair value – long-term	↓	Fair value 0.60. It may be higher given a structural shift in commodity prices.
Fair value – short-term	↔	NZD more fairly valued on commodity models.
Yield	↓	RBNZ supportive but US curve still too inverted.
Commodities	↔	Dairy prices are insulating the dairy sector but meat prices looking suspect.
Risk aversion	↑	Low.
Partial indicators	↔	Both economies have similar imbalances.
Technicals	↔	Support at 0.6880 critical.
AUD	↔	Just keep prodding but not progressing.
Sentiment	↔	Are we back to chasing the tallest pygmy?
Other	↔	Mixed messages from falling oil prices but could easily spillover.
<b>On balance</b>	↓↔	<b>RBNZ to hold and continued re-rating towards the Fed imply downside probing.</b>

## DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZDT)
22 Jan	AU	PPI (Dec) – qoq	0.2%	1.0%	13:30
		PPI (Dec) – yoy	-	4.0%	13:30
		New Motor Vehicle Sales (Dec) – mom	-	-0.9%	13:30
		New Motor Vehicle Sales (Dec) – yoy	-	-0.4%	13:30
	JN	Supermarket Sales (Dec) – yoy	-	-2.7%	18:00
	GE	Producer Prices (Dec) – mom	0.1%	0.0%	20:00
		Producer Prices (Dec) – yoy	4.5%	4.7%	20:00
23 Jan	US	Leading Indicators (Dec)	0.2%	0.1%	04:00
		Fed President Yellen speaks in Reno, Nevada on the economy	-	-	09:20
	JN	BoJ Monetary Policy Meeting Minutes (Dec)	-	-	18:00
	EU	ECB's Quaden and Gaspari speaks	-	-	00:00
		Industrial New Orders (Nov) – mom s.a.	1.1%	-0.6%	23:00
Industrial New Orders (Nov) – yoy		5.9%	12.5%	23:00	
24 Jan	US	Richmond Fed Manufacturing Index (Jan)		-6	04:00
		ABC Consumer Confidence (Jan 22)		-2	11:00
	AU	Conference Board Leading Index (Nov)	-	0.3%	12:00
		Consumer Prices (4Q) – qoq	0.2%	0.9%	13:30
		Consumer Prices (4Q) – yoy	3.6%	3.9%	13:30
		CPI Market Prices (4Q) – qoq	0.7%	0.7%	13:30
		CPI Market Prices (4Q) – yoy	2.3%	2.1%	13:30
		RBA Trimmed Mean (4Q) – qoq	0.7%	0.7%	-
		RBA Trimmed Mean (4Q) – yoy	3.1%	2.9%	-
		RBA Weighted Median (4Q) – qoq	0.7%	0.8%	-
		RBA Weighted Median (4Q) – yoy	3.2%	3.2%	-
		<b>NZ</b>	<b>Credit Card Spending (Dec) – yoy</b>	<b>-</b>	<b>7.8%</b>
	UK	BoE Governor King speaks in Birmingham	-	-	06:00
		Bank of England Minutes	-	-	22:30
		GDP (4Q Actual) – qoq	0.7%	0.7%	22:30
		GDP (4Q Actual) – yoy	2.9%	2.9%	22:30
	25 Jan	US	MBA Mortgage Applications (Jan 20)	-	-0.6%
<b>NZ</b>		<b>RBNZ Official Cash Rate (Jan 25)</b>	<b>7.25%</b>	<b>7.25%</b>	<b>09:00</b>
JN		Merchandise Trade Balance (Dec)	¥1200.0Bn	¥911.2Bn	12:50
		Adjusted Merchandise Trade Balance (Dec)	¥865.0Bn	¥991.1Bn	12:50
EU		ECB's Stark speaks in Brussels	-	-	18:00
		ECB Euro-Zone Current Account (Nov)	-	0.0Bn	22:00
		ECB Euro-Zone Current Account (Nov) n.s.a	-	-0.4Bn	22:00
GE		GfK Consumer Confidence Survey (Feb)	8.3	8.7	20:10

Continued over page

Date	Country	Data/Event	Mkt.	Last	Time (NZDT)
26 Jan	NZ	ANZ – Business NZ PMI (Dec)		55.4	00:01
	US	Initial Jobless Claims (Jan 21)	315k	260k	02:30
		Existing Home Sales (Dec)	6.25m	6.28m	04:00
		Existing Home Sales (Dec) – mom	-0.5%	0.6%	04:00
	JN	National CPI (Dec) – mom s.a.	0.0%	-0.1%	12:30
		National CPI ex-Fresh Food (Dec) – mom	-0.1%	0.0%	12:30
		National CPI (Dec) – yoy	0.3%	0.3%	12:30
		National CPI ex-Fresh Food (Dec) – yoy	0.2%	0.2%	12:30
		National CPI ex Food, Energy (Dec) – yoy	-	-0.2%	12:30
	EU	ECB's Gonzalez-Paramo speaks in Berlin			09:45
		Euro-Zone M3 (Dec) – yoy s.a.		9.3%	22:00
		Euro-Zone M3 (Dec) – 3 mth. avg. s.a.		8.8%	22:00
	CA	BOC Governor Dodge speaks on Monetary Policy and Developments in Global and Canadian Economies	-	-	07:00
Jan 27	US	Durable Goods Orders (Dec)	2.8%	1.6%	02:30
		Durables ex Transportation (Dec)	0.5%	-1.1%	02:30
		New Home Sales (Dec)	1050k	1047k	04:00
		New Home Sales (Dec) – mom	0.3%	3.4%	04:00

**Key:** AU: Australia, CA: Canada, EU: European Union, GE: Germany, JP: Japan, NZ: New Zealand, UK: United Kingdom, US: United States.

**Source:** Dow Jones, Reuters, Bloomberg, ANZ National Bank. All \$ values in local currency. Na= not available. (Note: all surveys are preliminary and subject to change).

## NEW ZEALAND DATA WATCH

**Key focus over next four weeks:** The big event is the Reserve Bank's *OCR Review* on Thursday 25 January. We expect interest rates to remain unchanged, but the talk to remain tough.

Date	Data/Event	Economic Signal	Comment
Wed 24 Jan (15:00)	Credit card billings (Dec)	Up	Credit cards expected to have been given a good workout over the holiday shopping season. Strong m/m increase expected, especially after the 0.9 percent decline in November.
Thu 25 Jan (09:00)	OCR January Review	No change	We don't see sufficient justification for the Reserve Bank to go. But the talk will remain tough.
Tue 30 Jan (10:45)	Building consents issued (Dec)	Holding up	A technical rebound expected from the surprising weakness in November. Trend to be modestly positive, but not accelerating away.
Tue 30 Jan (15:00)	Credit growth (Dec)	Up	Demand for household credit to remain strong, with another 1 percent increase expected.
Wed 31 Jan (10:45)	Merchandise trade (Dec)	Still imbalanced	Exports to be sluggish under a high NZD, but imports ex-fuel to remain high. Headline imports to be dragged lower by falling oil prices.
Fri 2 Feb (10:45)	External Migration (Dec)	Still strong	We're still a favorite destination for migrants, and strong labour market convincing more New Zealanders to stay home rather than seek greener pastures offshore. Another 1,000+ number expected.
Mon 5 Feb (10:45)	LCI and QES (Dec qtr)	Wages up	Wage growth expected to be strong with labour market still tight and demand for labour holding. Annual wage inflation rate may have peaked, but will stay high for some time.
Thu 8 Feb (10:45)	HLFS (Dec qtr)	Steady	Modest employment growth expected in line with confidence surveys, but unemployment rate to tick up slightly.
Thu 8 Feb (01:00)	ANZ Commodity Price Index (Jan)	-	-
Tue 13 Feb (10:45)	Capital Goods Price Index (Dec qtr)	Mixed	Construction prices are expected to continue rising while the high NZD should see plant and machinery prices fall.
Wed 14 Feb (10:45)	Producers Price Index (Dec qtr)	Payback	Firms expected to claw back some of their lost margins, but overall margins still under significant pressure overall.
Thu 15 Feb (10:45)	Retail Trade (Dec qtr)	Up	Anecdotal evidence suggests that consumers spent plenty this Christmas. Discounting should see a volume increase in the quarter.
<b>On Balance</b>		<b>Steady as she goes</b>	<b>Growth still one sided and in need of rebalancing.</b>

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## SUMMARY OF KEY MARKET FORECASTS

NZ FX rates	Actual		Current	Forecast (end month)						
	Nov 06	Dec 06	19 Jan 07	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08
NZD/USD	0.669	0.692	0.694	0.690	0.620	0.600	0.580	0.560	0.530	0.530
NZD/AUD	0.866	0.880	0.881	0.885	0.816	0.800	0.795	0.778	0.736	0.746
NZD/EUR	0.520	0.524	0.535	0.523	0.477	0.465	0.457	0.448	0.431	0.438
NZD/JPY	78.5	81.0	84.3	79.4	70.1	67.2	63.8	60.5	56.2	57.2
NZD/GBP	0.350	0.352	0.352	0.356	0.323	0.316	0.307	0.299	0.285	0.288
NZ\$ TWI	66.7	68.1	69.0	67.9	61.4	59.6	58.0	56.2	53.3	53.8
NZ interest rates	Nov 06	Dec 06	15 Jan 07	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08
OCR	7.25	7.25	7.25	7.25	7.25	7.25	7.00	6.50	6.00	5.50
90 day bill	7.61	7.66	7.67	7.70	7.50	7.40	7.00	6.50	6.10	5.60
10 year bond	5.72	5.78	5.91	6.00	6.00	6.20	6.10	6.20	6.40	6.50
International	Nov 06	Dec 06	15 Jan 07	Mar 07	Jun 07	Sep 07	Dec 07	Mar 08	Jun 08	Sep 08
US Fed funds	5.25	5.25	5.25	5.25	5.25	5.00	4.50	4.50	4.50	4.50
US 3-mth	5.37	5.37	5.29	5.25	5.00	4.75	4.60	4.60	4.60	4.60
AU cash	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25	6.25
AU 3-mth	6.39	6.38	6.45	6.40	6.40	6.40	6.40	6.40	6.40	6.40

## KEY RATES

	19 Dec	15 Jan	16 Jan	17 Jan	18 Jan	19 Jan
Official Cash Rate	7.25	7.25	7.25	7.25	7.25	7.25
30 day bank bill	7.60	7.60	7.61	7.54	7.56	7.56
90 day bank bill	7.64	7.64	7.71	7.66	7.67	7.67
NZGB 07/09	6.48	6.49	6.50	6.43	6.44	6.43
NZGB 11/11	6.22	6.23	6.29	6.24	6.25	6.24
NZGB 04/13	5.98	5.99	6.10	6.06	6.07	6.07
NZGB 12/17	5.78	5.78	5.93	5.89	5.91	5.92
1 year swap	7.80	7.80	7.83	7.78	7.78	7.76
2 year swap	7.56	7.56	7.63	7.59	7.59	7.58
5 year swap	7.15	7.16	7.24	7.22	7.22	7.22
RBNZ TWI	68.3	68.2	68.8	68.8	68.9	69.0
NZD/USD	0.6906	0.6902	0.6911	0.6911	0.6937	0.6943
NZD/AUD	0.8846	0.8836	0.8830	0.8830	0.8797	0.8802
NZD/JPY	81.48	81.48	83.48	83.48	83.65	84.23
NZD/GBP	0.3544	0.3532	0.3525	0.3525	0.3515	0.3514
NZD/EUR	0.5273	0.5272	0.5348	0.5348	0.5349	0.5348
AUD/USD	0.7807	0.7811	0.7827	0.7827	0.7886	0.7888
EUR/USD	1.3097	1.3093	1.2922	1.2922	1.2968	1.2982
USD/JPY	117.99	118.05	120.80	120.80	120.59	121.31
GBP/USD	1.9486	1.9544	1.9608	1.9608	1.9736	1.9756
Oil	62.19	63.40	51.23	51.23	52.30	50.51
Gold	616.48	617.75	624.05	624.30	632.75	628.90
Electricity Price Index	3.35	2.95	2.93	2.92	2.95	n/a

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