ANZ RESEARCH

# NEW ZEALAND ECONOMICS
# MARKET FOCUS

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INSIDE



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## THE GRAND PLAN

### ECONOMIC OVERVIEW

Global developments continue to be the major focus for markets. While we expect decisive action by policymakers, and soon, we struggle to see a package that will ultimately "stick". A continued long, hard grind for the global economy will remain in the backdrop. Base momentum within the local economy continues to muddle along, with a stronger cyclical rebound being tempered by the reality of debt repayment in the new environment. The outlook for the remainder of the year is for a return to above-trend growth, boosted by the Rugby World Cup, but there will be payback in Q1 2012. We expect the tenor of NZ data to remain better than most, with attention this week on the September National Bank Business Outlook, which will reveal whether global events have had an impact on business sentiment and the willingness of firms to employ and invest.

### FINANCIAL CONDITIONS UPDATE

For most economies we monitor, financial conditions tightened further in September. While the story differs across countries, the general takeout of our FCI measures is that economic momentum is set to slow, albeit to different speeds. Moderate growth is in prospect for the US, UK and NZ. A more pronounced slowdown is in prospect for China and Australia, although helpful one-offs not captured in our FCIs are likely to provide support to economic activity. The outlook for Eurozone implied by our FCIs is poor, with economic momentum set to stall, and recession looming for economies on the Eurozone periphery and Italy.

### INTEREST RATE STRATEGY

Global fragility remains the key issue for markets. Hopes for a comprehensive solution have been buoyed by rumours over the weekend. But urgency seems to be the key missing ingredient, and it looks like Europe will continue to "muddle through" a little longer. With local data showing signs of less momentum than earlier thought, and risk appetite waning, we look to be in for more of the same – volatility and headline fatigue. The upshot: interest rates will stay lower for longer here.

### CURRENCY STRATEGY

The G20 meeting in Washington appears to have given the FX markets cause for (limited) cheer, with hope that Germany will finally cave in to pressure from global leaders to consider more drastic measures. Last week's FOMC statement has refocused FX markets on the poor global growth outlook, weighing heavily on risk currencies, equities and commodities. All of this week's focus will be on Europe as we await more headlines. Expect any risk rallies to be capped with markets continuing to trade off news-flow.

# ECONOMIC OVERVIEW

## SUMMARY

Global developments continue to be the major focus for markets. While we expect decisive action by policymakers, and soon, we struggle to see a package that will ultimately "stick". A continued long, hard grind for the global economy will remain in the backdrop. Base momentum within the local economy continues to muddle along, with a stronger cyclical rebound being tempered by the reality of debt repayment in the new environment. The outlook for the remainder of the year is for a return to above-trend growth, boosted by the Rugby World Cup, but there will be payback in Q1 2012. We expect the tenor of NZ data to remain better than most, with attention this week on the September National Bank Business Outlook, which will reveal whether global events have had an impact on business sentiment and the willingness of firms to employ and invest.

## THIS WEEK'S EVENTS

**SNZ Building Consents - August** (Friday, September 30, 10:45am). The number of dwelling consents is expected to climb by around 2 percent. Non-residential consent issuance of around $300m is expected.

**National Bank Business Outlook – September** (Friday, September 30, 1:00pm).

**RBNZ Credit Aggregates – August** (Friday, September 30, 3:00pm). Low rates of annual credit growth are expected. Annual growth of around 1 percent is expected for household and business credit, with agricultural sector credit likely to decline further.

## WHAT'S THE VIEW

**The global economy continues to deteriorate – rapidly.** Rather than focus on the latest twists and turns, we think it's useful to step back and have a look at what we need to see for stabilisation and recovery to emerge. Broadly there are six components:

- **Greece's problems need to be ring-fenced.** Our fiscal sustainability work (refer to our August 22 *Market Focus*) highlighted the mathematical difficulties Greece faces averting default (see table). Default of some form seems inevitable. The key from here is ensuring that default doesn't engulf some of the bigger nations that top our sovereign debt vulnerability rankings.

**GREECE**
**Primary (ex-interest) fiscal balance needed each year to stabilise sovereign debt at 60% of GDP in 10 years**

| REAL 10 YR YIELDS | REAL GDP GROWTH | | | | |
|---|---|---|---|---|---|
| | 0.00 | 1.00 | 2.00 | 3.00 | 4.00 |
| 5.00 | 11.4 | 10.4 | 9.4 | 8.4 | 7.4 |
| 4.00 | 10.4 | 9.4 | 8.4 | 7.4 | 6.5 |
| 3.00 | 9.4 | 8.4 | 7.4 | 6.5 | 5.5 |
| 2.00 | 8.4 | 7.4 | 6.5 | 5.5 | 4.6 |
| 1.00 | 7.4 | 6.5 | 5.5 | 4.6 | 3.7 |
| 0.00 | 6.5 | 5.5 | 4.6 | 3.7 | 2.7 |

% of GDP: Primary balance 2011: 2.6%. Net govt debt 2011: 124.8%

*Sources:* ANZ, National Bank, OECD

- **Action needs to be global and co-ordinated.** The big guns are rolling out with the G20 on board. The euro crisis is not merely a euro-centric event – it has the potential to engulf all and sundry.
- **More money** – a lot of it. If Greece is set to default, then pockets of the financial system in jurisdictions such as Europe would require recapitalisation. The rumour mill has it that European officials are working on a plan that would allow Greece to "default" on half of its debt. This default would, in turn, lead to massive losses among European banks, so the plan calls for the banks to be forcibly recapitalised from private funds where possible and by the European Financial Stability Facility (EFSF) where not. The next problem, contagion, is the real issue with a Greek default. To that end, the plan also calls for the EFSF to be leveraged, with the additional funds to provide financing (ring fencing) to Spain and Italy, as well as Ireland and Portugal. This is rumoured to be achieved by the ECB providing additional funds on the basis that the EFSF takes the "first loss" piece should any future losses be incurred.

  To effectively "firewall" Italy, as US Treasury Secretary Geithner put it, the plan may need to see the EFSF leveraged up to 2 trillion euros. These are huge numbers, way in excess of the IMF's war chest (thought to be US$384bn) and the existing EFSF (€440bn). Recall that the July changes to the EFSF (which expanded its powers, allowing it to buy sovereign debt and to lend to troubled banks) have yet to be ratified by all EU members. The attraction of the leveraged scenario is that "theoretically" it wouldn't need further parliamentary approval. However, with the original extension still to be approved, it is a risky strategy to have in the public domain. German

# ECONOMIC OVERVIEW

politicians seem to be in no hurry to embrace the concept, with some publicly voicing opposition to it. And there's the sticking point – nationalist-style political arguments are growing stronger by the day. As German Chancellor Merkel has found, bailing out the profligates abroad is not popular at home.

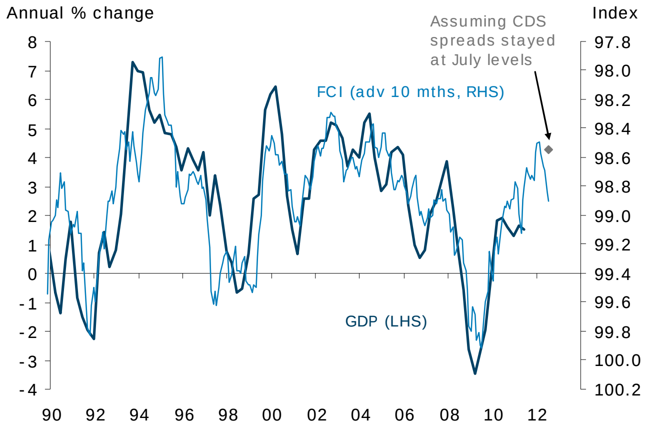
- **Speed is of the essence to restore confidence.** Deteriorating risk sentiment and asset prices are undermining financial conditions in key pockets of vulnerability such as Italy (refer page 6). This risks engulfing them in a negative spiral, where a negative gap between GDP growth and real yields exacerbates the debt issues.
- **Any rescue package needs to have "hooks",** whereby some of the pain is shared. Why? Moral hazard. The repeated pattern of busts and bailouts for the past twenty years needs to come to an end.
- **We need to see political stability.** The medicine will be unpalatable but it must be taken. Now is the time to put aside political and country divisions. European governments need to co-ordinate to broker a solution that will stick and which will reassure bondholders. US policymakers also must put aside partisan differences.

Will we see solutions? Yes. Will they ultimately stick, and have the sense of durability that could underpin a global upturn? This is where the real uncertainty resides. **We are entering an environment over the coming weeks where the distribution of possible outcomes involves massively fat tails – in either direction.** Decisive action could quickly see risk appetite return with a vengeance, with the NZD a huge beneficiary. Yet a failure to step up to the plate could set off a chain of events that could ultimately be very difficult to contain.

**In such a situation we continue to remind readers that the myriad of structural and cyclical influences, both here and abroad, will entail a long, drawn-out slog with ups and downs along the way**. In its recent forecasts the IMF has downgraded the outlook for global growth, with larger downward revisions for the United States and Europe. We put the odds on a global recession at 1 in 3 – and rising by the day.

There are a multitude of channels via which a weak world can affect the New Zealand economy. **While no one approach will be able to adequately capture the impact of each of these channels, our financial conditions measures provide a useful reference point.** They suggest the implied increase in bank CDS spreads, if it persists, has the potential to knock around 1½ percent off GDP growth over the next year – though this is mitigated somewhat by lower wholesale interest rates. We are closely watching export commodity prices to see the extent to which global ructions are likely to impact on our terms of trade, a key support factor. The support provided by a lower NZD is another positive, although the reasons why it has fallen (weaker global outlook) are not.

**NZ GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Statistics NZ

**In such an environment, policymakers (both here and abroad) will focus on mitigating the potential impact of tail risks.** Holding the OCR at exceptionally low levels in a worsening global environment will be a prudent strategy for New Zealand, but the upshot is likely to be a less than ideal mix of growth and higher inflation. At this point in time, this option appears to be the best choice among a bad lot. Of course central bankers, including our own RBNZ, will never admit to the concept of a little more inflation greasing the wheels of the economy as the endgame, but such an outcome looks inevitable.

**Given all of these events, high rates of volatility are to be expected, and the tepid Q2 GDP outturn, while unwelcome, was in this context not a bolt out of the blue.** That the New Zealand economy has managed to muddle along at an on-trend pace in the first half of this year, all things considered, is perhaps not as good as some such as ourselves had hoped for, but is a considerably better outcome than had seemed possible at the start of March when the OCR cut was made.

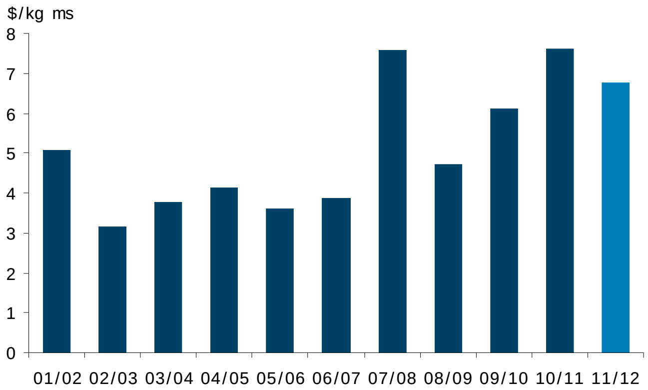
**Despite this loss of momentum in Q2, the New Zealand economy looks set to pick up over the remainder of the year:**

- There have been a number of recent reports pointing to a Rugby World Cup (RWC) related surge in card spending in early September. The tournament is expected to provide a sizeable boost to economic activity in the second half of this year.

# ECONOMIC OVERVIEW

- The Fonterra annual report reaffirmed the positive short-term outlook for dairy, with the milk payout (before retentions) of $8.25kgms confirmed for the 2010/11 season the highest on record. The unchanged milk price forecast for 2011/12 at $6.75/kgms is the third-highest on record and a vote of confidence in the industry. Whether this will be achieved in the current environment is unclear, with downside risks to the commodity price outlook growing. The *GlobalDairyTrade* auction last week showed a pullback in skim milk and fats, although encouragingly, whole milk powder prices held firm.

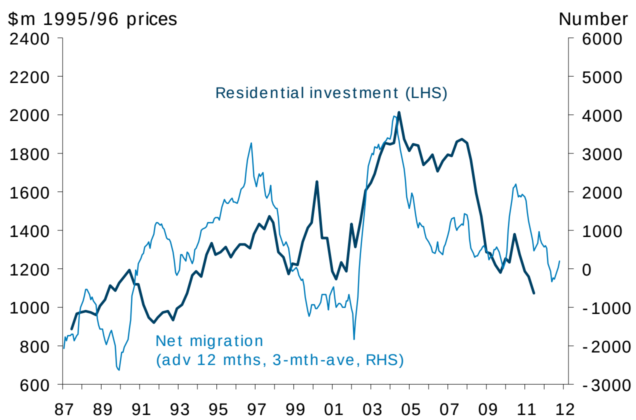
**Fonterra Milk Price Forecasts**




*Sources:* ANZ, National Bank, Fonterra

- A quicker than expected turnaround in net permanent and long-term migration in August was driven by a fall in net PLT departures as more people decided to stay put. We expect total (i.e. short and long-term) migration outflows to turn to net inflows over the next year or so. This will provide demand and supply-side support to the economy, including a boost to the housing market.

**Residential investment and net migration**



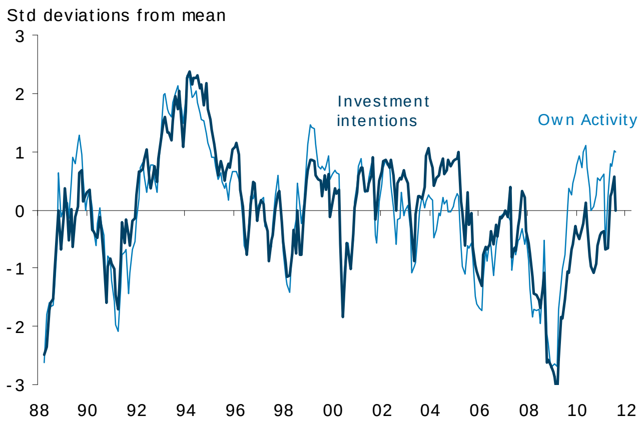

*Sources:* ANZ National, Statistics NZ

Strengthening housing market activity is expected to lead to a further recovery in August residential consent issuance, with scope for this sector to make up lost ground over the remainder of the year. Insurance issues continue to cast a cloud over the speed and timing of the Canterbury rebuild, which we expect to commence in the middle of next year. Ironically, reinsurance claims (and helpful statistical changes) have helped lower our measured net external indebtedness, which may (temporarily) help deflect unwanted attention on the part of ratings agencies.

The August merchandise trade data delivered a larger than expected deficit, but as a testament to the resilience in domestic demand this was driven by stronger than expected imports. **Encouragingly, for supply side capacity, capital goods imports firmed to $738m, their highest since August 2008. Export values have managed to hold up so far, but much will depend on the commodity price outlook. Downside risks around this are growing.**

**While the rest of 2011 is looking reasonably solid and the Christchurch rebuild should start to kick in over 2012, there is a risk of a soft patch in growth at the start of 2012, particularly if the global outlook continues to head south.**

**NBBO Own Activity and Investment intentions**




*Sources:* ANZ, National Bank

**We will continue to focus on forward-looking indicators.** Friday's National Bank Business Outlook will provide a timely update. We will be paying close attention to investment intentions to see if global ructions are causing firms to shelve plans. Construction sector intentions will also be of interest to see if this sector will soon become an outperformer or whether reported difficulties with insurance are likely to delay the ramp-up in economic activity. Replacing destroyed capital stock will not generate growth of the "feel good" variety, but it will provide a degree of economic support and will leave the economy better placed to capitalise on opportunities that will arise in better global times.

# ECONOMIC OVERVIEW

## RECENT LOCAL DATA

**SNZ Overseas Merchandise Trade – August.** There was a monthly trade deficit of $641m, with the annual trade surplus narrowing to $1,084m.

**SNZ International Travel and Migration – August.** A net permanent and long-term (PLT) inflow of 200 persons was registered, with the annual PLT inflow slowing to 2,257 persons. The annual net short and long-term population outflow eased to 15,060 persons. Overseas visitor arrivals climbed 8.0 percent s.a. (+4.7 percent y/y).

**RBNZ Credit Card Billings – August.** A 1.2 percent s.a. fall in credit card billings was reported. Spending on NZ issued cards fell 1.0 percent s.a., with spending on overseas issued cards declining 2.1 percent s.a.

**SNZ Current Account Balance – 2011Q2.** The quarterly current account deficit climbed to $921m, with the annual deficit at 3.7 percent of GDP. The net international investment position at the end of the June quarter was 70 percent of GDP.

**SNZ Gross Domestic Product – 2011Q2.** Production-based GDP increased 0.1 percent q/q (1.5 percent y/y). Expenditure-based GDP rose 0.1 percent q/q (0.7 percent y/y).

**Westpac Consumer Confidence – 2011Q3**. Headline consumer confidence was unchanged at 112 in Q3. Current conditions ticked up to 105.7 (previously 103.9), whereas future conditions eased to 116.3 (117.4).

# FINANCIAL CONDITIONS UPDATE

## SUMMARY

For most economies we monitor, financial conditions tightened further in September. While the story differs across countries, the general takeout of our FCI measures is that economic momentum is set to slow, albeit to different speeds. Moderate growth is in prospect for the US, UK and NZ. A more pronounced slowdown is in prospect for China and Australia, although helpful one-offs not captured in our FCIs are likely to provide support to economic activity. The outlook for Eurozone implied by our FCIs is poor, with economic momentum set to stall, and recession looming for economies on the Eurozone periphery and Italy.

## FINANCIAL CONDITIONS

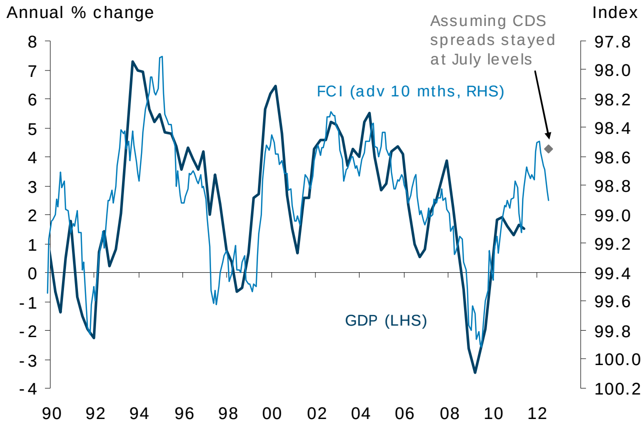
**We track financial conditions across an array of countries.**[1] While they do not track perfectly we generally find that the **historical relationship between financial conditions and GDP has been quite good for the countries we monitor.** Not only that, but financial conditions tend to give a reasonable lead on turning points in the cycle. An added advantage of our approach is that it is not a black box approach, and can help quantify the impact of each potential channel on base momentum.

**We acknowledge that indicators such as financial conditions have deficiencies.** Our FCI measures are a reduced form and do not capture all of the many influences on growth. What approach could! The relationship between the financial system and general economy is changing rapidly, and is set to continue doing so given the emergence of alternate policy tools and growing use of prudential policy. In such an environment we have been careful not to over-fit our FCIs, and have continued to use them to identify trends in momentum and potential turning points rather than as a forecasting tool. **As such, our FCI measures should be designed as an indicator of the level of base momentum within an economy.**

## MOMENTUM STILL BUILDING IN NZ THOUGH AT A LESSER PACE

**Our proprietary Financial Conditions Index (FCI) for NZ is supportive of a recovery over the next 12 months.** Very low interest rates and strong commodity prices form the basis of supportive financial conditions. A further relaxation in lending standards has helped. Offsetting these support factors has been a further widening in CDS spreads for the big four Australasian banks, which are now wider than during the global financial crisis. These are broadly considered a proxy for funding costs. Continued falls in NZ equity prices were also influential. To illustrate the impact of widening CDS spreads, the chart depicts what the FCI would have been if CDS spreads had remained unchanged at July levels. It shows around a 1½ percent hit to GDP growth from this channel alone. While this impact is more implied than real, given that it will not be an issue until banks need to source funding, the longer CDS spreads stay elevated, the more likely this is going to be an issue.

**NZ GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Statistics NZ

Tighter financial conditions imply annual GDP growth of around 2½ percent by mid next year. Given that our FCI does not incorporate the boost provided by the Rugby World Cup and earthquake reconstruction it should be interpreted as an indicator of base momentum. Despite global ructions the message provided by our FCI is still one of improving underlying momentum, albeit at a lesser pace than previously estimated.

## MODERATION IN AUSTRALIA

Australian financial conditions tightened further in September. A lower AUD, and falls to short-term interest rates and swap rates were offset by lower equity and commodity prices and widening CDS spreads.

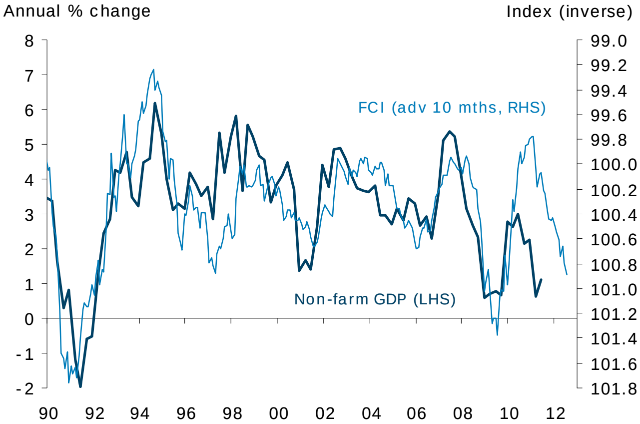
**Our Australian FCI is flagging just over 1 percent annual growth for non-farm GDP by mid 2012.** As our FCI does not include the impact of the Queensland floods and the forthcoming boost to mining investment (which the RBA estimates will account for about two-thirds of Australian growth

[1] A financial conditions index summarises a range of financial variables into a single series that can be used to predict the future path of the economy. Where available, our FCI includes the currency adjusted for commodity prices or terms of trade movements, interest rates, asset prices, credit growth and proxies for the cost and availability of credit.

# FINANCIAL CONDITIONS UPDATE

over the next few years), the actual growth profile will be quite different to that implied by financial conditions. The softening in growth momentum implied by tighter financial conditions is consistent with the commentary in the September RBA board minutes, which noted that despite strong national income growth and the pending boost from resource sector investment, the broader economy had been softer than earlier expected.

**AU GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Bloomberg

## US GROWTH TO RECOVER?

**Historical revisions of the US national accounts have prompted a revamp of our US FCI.** Our new FCI uses a more parsimonious specification, putting more weight on asset prices and actual rates faced by borrowers.

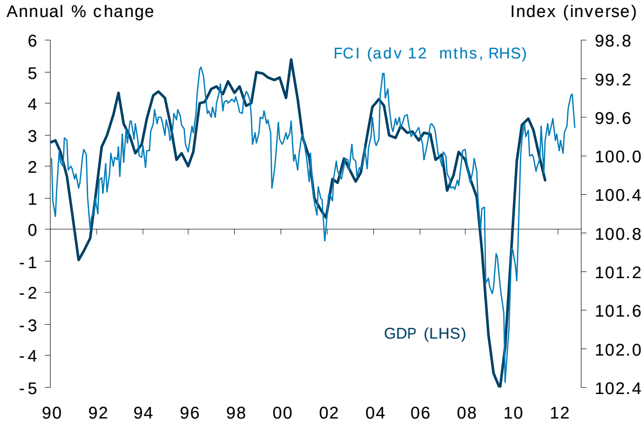
Included in our revamped FCI are the following variables:

- Real exchange rate adjusted for the terms of trade (10% weight)
- Real 30-year mortgage rate (10% weight)
- 2-year swap spread (35% weight)
- Real M2 credit growth (15% weight)
- Real S&P500 growth (10% weight)
- Real house price growth (20% weight)

Our revamped FCI tightened further in September, with overall conditions returning to May levels. Driving this tightening in recent months have been lower equity values, rising real mortgage interest rates (despite falls in Government bond yields), a widening in swap spreads, and more recent falls to house prices. The September tightening in our FCI was due to the rising USD and climbing real mortgage interest rates. Considering both of these are below historical averages, overall financial conditions remain consistent with a respectable pace of growth, with annual growth expected to reach around 3 percent in 12 months time.

**The reasonably solid picture implied by accommodative financial conditions has contrasted with the more circumspect tone implied by forward indicators and concerns of US policymakers.** The impasse over the US debt ceiling negotiations, subsequent credit downgrade and wrangling by US politicians over fiscal policy are likely to have weighed on confidence and economic activity. US Federal Reserve Officials have just announced "operation twist", that will extend the average maturity of its Treasury holdings, with the aim to flatten the US yield and help lower longer-term borrowing costs. Whether or not this will succeed and will be effective in reviving confidence and kick-starting the economy remains to be seen, but markets appear sceptical.

**US GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Bloomberg

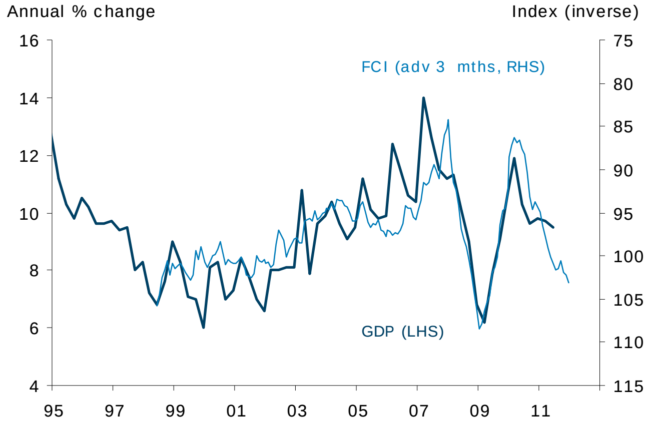
## CHINA SLOWDOWN LOOMING?

**Financial conditions in China tightened further in September.** They are now pointing to around 7 percent growth by the end of this year, which constitutes a harder landing for the Chinese economy. Chinese financial conditions have been progressively tightening since the start of last year. Driving this has been a combination of factors, including the rising real exchange rate, rising real lending rates and slowing rates of annual credit growth. Also contributing to the tightening have been falls in real equity and property prices, which account for half of the weightings in our Chinese FCI. While Chinese authorities have ample room to ease monetary policy and will continue to provide stimulus via other means (including funding local infrastructural projects) our FCI suggests that momentum is set to slow in the Chinese economy. While our FCI suggests fears over economic overheating are likely to subside over the coming

# FINANCIAL CONDITIONS UPDATE

months, slower Chinese growth will not be good news for commodity exporters such as NZ and Australia.

**China GDP vs Financial Conditions Index**

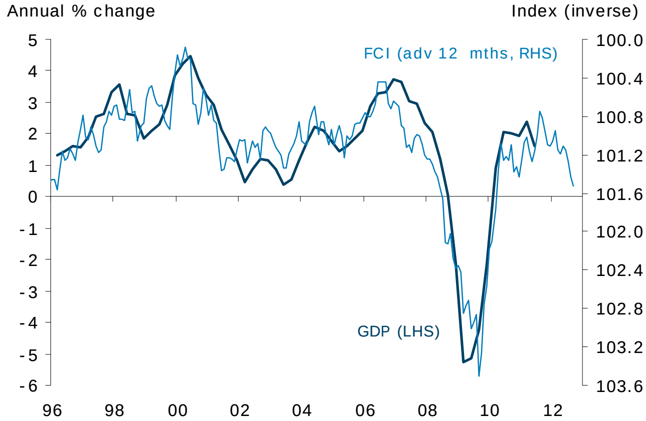



*Sources:* ANZ, Bloomberg

## HARD LANDING FOR THE EUROZONE IN PROSPECT BUT WITH COUNTRY DIVERGENCES

**Financial conditions in the Eurozone economy tightened in September.** A lower euro and falls to government bond yields were countered by falling equity values, lower credit growth, and widening swap spreads. Compared to a year ago the tightening in financial conditions has been driven by the strengthening euro and lower equity values.

**Eurozone GDP vs Financial Conditions Index**

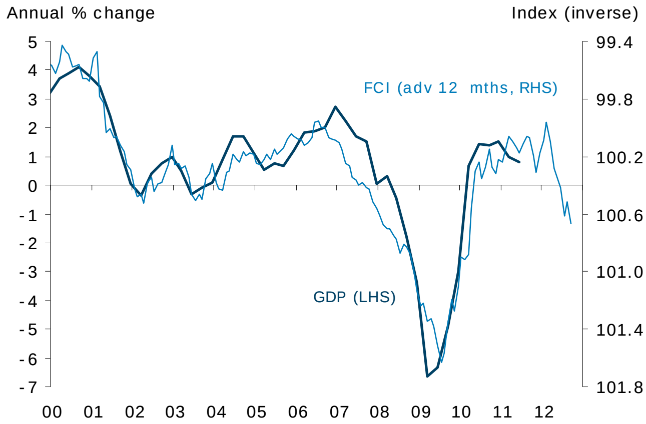



*Sources:* ANZ, National Bank, Bloomberg

**Our FCI implies a further slowdown in annual growth in the region, with the economy effectively stalling.** This is particularly concerning considering our FCIs do not fully capture the headwinds to growth provided by the planned fiscal austerity measures. Against this weak backdrop, there are continued country differences. Somewhat ironically, the low EUR and safe haven flows to German bunds appear to be benefiting German financial conditions.

By contrast, growth prospects for other economies in the region are looking shakier. By virtue of **their more challenging fiscal** positions, government bond yields remain higher in Spain and Italy, with last week's downgrade of Italy by S&P likely to add to future challenges. **Our FCI for Italy is clearly pointing to a fairly sizeable recession in the Italian economy.** The outlook is likely to be more dire than this, given that it does not directly incorporate the impact of the planned fiscal austerity measures.

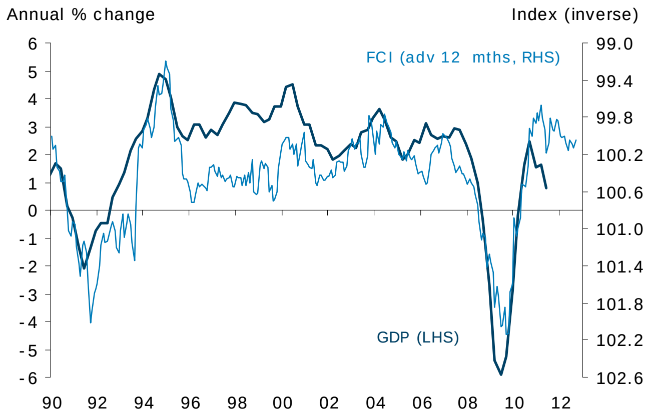
**Italy GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Bloomberg

## MODEST GROWTH IN THE UK

**UK GDP vs Financial Conditions Index**




*Sources:* ANZ, National Bank, Bloomberg

**September financial conditions eased marginally in the UK,** with climbing swap spreads and falling equity values offsetting an easing in government bond yields. UK financial conditions have tightened since June and are now pointing to around 2½ percent annual growth next year. Given the growth headwind provided by pending fiscal consolidation (not fully captured in our approach) our FCI has tended to overstate activity.

# FINANCIAL CONDITIONS UPDATE

## THE UPSHOT

The global economy is delicately poised. The recent tightening in financial conditions is not a welcome development and policymakers are now attempting to try and circumvent them. Downside risks to the global economy are building. **We will continue to pay close attention to our financial conditions measures for signs of further economic slowdown.**

Amongst the general trend, the disparate picture remains. **For the US, UK and NZ, our FCIs are still pointing to modest (but respectable) growth rates being achieved**. The outlook implied by our Eurozone FCI looks pretty grim, although strong country divergences are likely to remain.

Challenges to growth from looming fiscal consolidation are only partially captured by our financial conditions measures. As such, growth outturns for the US, UK and Eurozone are likely to continue undershooting those implied by our FCIs. Growth-supportive factors are expected to boost activity in Australia, NZ and China by more than implied by our measure.

# INTEREST RATE STRATEGY


## SUMMARY

Global fragility remains the key issue for markets. Hopes for a comprehensive solution have been buoyed by rumours over the weekend. But urgency seems to be the key missing ingredient, and it looks like Europe will continue to "muddle through" a little longer. With local data showing signs of less momentum than earlier thought, and risk appetite waning, we look to be in for more of the same – volatility and headline fatigue. The upshot: interest rates will stay lower for longer here.


## MARKET THEMES

- Global concerns completely dominate the outlook. Although there are rumours of a comprehensive EFSF and ECB backed bail-out (which involves a partial Greek default), it could be weeks before we see it.
- Urgency is key. The longer Europe "muddles through" the greater the negative impact on markets.
- Local events are not completely irrelevant, despite the scale of global events. Had they been more upbeat, they'd have had more of an impact. But last week's soft Q2 GDP only reinforced the bearish tone.

## REVIEW AND OUTLOOK

**Markets are awash with rumours of an initiative to comprehensively deal with Europe's mounting debt problems**. Media reports suggest the plan involves a managed default of Greece, with haircuts of up to 50 percent. Affected banks will be recapitalised by the EFSF, which will also be leveraged up with the help of the ECB, with the EFSF taking the "first loss" piece.

**The plan sounds ambitious – and it may even work. But given its contentiousness, it could be weeks away, and in the meantime, markets that are already suffering from headline fatigue will be buffeted by the news flow.** As always, timing is everything – and with crucial parliamentary votes across Europe needing to pass before concrete steps can be taken, **the next 4-6 weeks are likely to resemble the last few weeks: choppy and volatile. We will be keeping an eye on funding markets in particular – for this is a key transfer mechanism insofar as NZ is concerned.** CDS spreads have widened substantially of late, and it is critical that we see these markets normalise before we can declare things to be "business as usual".

The fallout from last week's Fed announcement of "operation twist" is also continuing. **This has seen US Treasury bond yields plummet to new lows**. **What matters for the market is that the Fed is now attempting to subdue long-term interest rates, and it has the firepower to do it.** With Europe still on the skids and US monetary policy directed further along the curve, **this will put more flattening pressure on the local yield curve.**

Let's not forget about local developments. Our suspicion is that stronger GDP data might have seen some of the tension (between better local conditions and poor global conditions) remain in place a little longer. But in the event, the data was soft and people are naturally starting to ask whether global uncertainty has had more of an impact here than first thought. One thing seems clear – **RBNZ rate hikes look a long time away, and like the Australian market, we would not be surprised to see the local market flirt with pricing in rate cuts, a reflection of the binary world in which we now reside. Things could turn around quickly, or get derailed further**.

**PREFERRED BORROWING STRATEGIES**

Volatility in global markets has seen local swap rates plummet, with all swap rates hitting record lows on Friday. But we would caution against using such a move as an opportunity to extend duration. Low rates help if you need or want to fix, but given the uncertainties, and the binary nature of the global outlook, we would strongly caution against introducing fixed expenses at the moment. Liquidity is far more important. Like the RBNZ, we are looking for "proof" that NZ will escape global turmoil relatively unscathed, and until we get this, our preference is to remain floating.

**GAUGES FOR NZ INTEREST RATES**

| GAUGE | DIRECTION | COMMENT |
|---|---|---|
| RBNZ / OCR | ↔ | RBNZ will be on hold till 2012 at the earliest. |
| NZ data | ↔ | Q2 GDP downside surprise. |
| Fed Funds / front end | ↔/↓ | FF on hold till mid 2013. Operation Twist won't see short end yields rise. |
| RBA | ↔/↑ | Next move could be a cut. |
| US 10 year | ↔ | Operation Twist has taken bond yields to record lows. |
| NZ swap curve | ↔/↓ | Flattening trend to continue. |
| Flow | ↔/↑ | Receivers dominating. |
| Technicals | ↔ | 2yr break of 3% significant. |

**MARKET EXPECTATIONS FOR RBNZ OCR (BPS)**

| OCR DATES | LAST WEEK | THIS WEEK |
|---|---|---|
| Thu 27-Oct-11 | +2 | -2 |
| Thu 8-Dec-11 | +9 | -1 |
| Thu 26-Jan-12 | +17 | 0 |
| Thu 8-Mar-12 | +28 | +2 |
| Thu 26-Apr-12 | +35 | +6 |
| Thu 14-Jun-12 | +37 | +7 |
| Thu 26-Jul-12 | +41 | +9 |

**TRADING THEMES WE FAVOUR AT PRESENT**

Swap curve flatteners remain appropriate in the current environment, even though they have gone a long way. Bonds are set to outperform in the next 6 weeks, with the index set to lengthen as the NZGS 11/11 rolls off. But we suspect the market will tread water ahead of the PREFU. It makes sense to consider being long the NZGS asset swap in anticipation given how far swap spreads have narrowed.

# CURRENCY STRATEGY

## SUMMARY

The G20 meeting in Washington appears to have given the FX markets cause for (limited) cheer, with hope that Germany will finally cave in to pressure from global leaders to consider more drastic measures. Last week's FOMC statement has refocused FX markets on the poor global growth outlook, weighing heavily on risk currencies, equities and commodities. All of this week's focus will be on Europe as we await more headlines. Expect any risk rallies to be capped with markets continuing to trade off news-flow.

## MARKET THEMES

- European repair plan eagerly awaited.
- Greek default looking imminent.
- Poor growth focus to continue to undermine commodity currencies.
- NZ business confidence an important focus this week.

## REVIEW AND OUTLOOK

**Although the quotes remain feisty, hope is rising that behind the scenes Germany may be falling into line with the view that extraordinary measures are required to repair the European debt situation.** Band-aid fixes need to give way to a coordinated comprehensive plan to contain contagion risk. While the prospect of significant official action might give the EUR some support in the short term, we should not forget that the process of unsterilised QE, if that is the route that gets pursued in the end, should put significant downward pressure on the EUR. The FX market's response to US QE (the USD was heavily sold) provides us with some insight (although our faith in the FX market to respond logically to these developments is not high).

**The Fed decided to "Twist and Shout", and while this was what markets was looking for, the Fed's downbeat view on the economy was latched onto by markets.** This undermined commodity currencies and saw risk sell off aggressively. In our view, the sell-off in commodity currencies represents a desire by risk-takers to significantly reduce exposures in these highly uncertain times, rather than any specifically negative view about the NZD and AUD.

**The RBA continues to be more upbeat than the financial markets about the Australian economy.** While this gave a little support to the AUD, the RBA was completely trumped by the Fed. With growth and Europe the primary concerns, risk off is the predominant theme. With no AUD specific news in the near-term, expect the AUD to be driven by offshore factors this week.

**The NZ Q2 GDP data release surprised with its weakness and got the NZD sell-off party started.** Risk off and growth concerns will continue to weigh on the NZD for now as we await business confidence data at the end of this week. Offshore events will continue to tug NZD in both directions with the European situation still the key focus. Overall, NZ's fundamentals look okay (including an upbeat Fonterra) so NZ exporters should treat further dips as buying opportunities.

**NZD VS AUD: MONTHLY DIRECTIONAL GAUGES**

| GAUGE | DIRECTION | COMMENT |
|---|---|---|
| Fair value | ↔ | Close to our fair value estimates. |
| Yield | ↑ | Opposing policy direction favours NZD. |
| Commodities | ↔↓ | Wary of cracks appearing here. |
| Partial indicators | ↔/↑ | Data still good in NZ. |
| Technicals | ↔↑ | Rangebound 0.7900 - 0.8050. |
| Sentiment | ↔ | Balanced. |
| Other | ↔ | Global sentiment big driver. |
| **On balance** | ↑ | **Yield and undervaluation support NZD.** |

**NZD VS USD: MONTHLY DIRECTIONAL GAUGES**

| GAUGE | DIRECTION | COMMENT |
|---|---|---|
| Fair value – long-term | ↓ | Above structural fair value of 0.67. |
| Fair value – short-term | ↔/↓ | Still above our cyclical fair value estimates. |
| Yield | ↑ | Official rates to stay low but investable yields support. |
| Commodities | ↔↓ | Starting to be wary of turns in key NZ-related commodities. |
| Risk aversion | ↓ | Global recession prospect driving risk off. |
| Partial indicators | ↑ | NZ data better, US data worsening. |
| Technicals | ↔ | Wide range continues 0.7510 - 0.7960. |
| AUD | ↓ | AUD undermined by data. |
| Sentiment | ↑↓ | Growth vs potential QE3 vs EU debt crisis = confusion. |
| Other | ↑↓ | Risk off, position squaring. |
| **On balance** | ↔↓ | **Global issues remain the focus.** |

# DATA EVENT CALENDAR

| DATE | COUNTRY | DATA / EVENT | MKT. | LAST | NZ TIME |
|---|---|---|---|---|---|
| 26-Sep | NZ | Trade Balance - AUG | -321M | -641m(a) | 11:45 |
| | NZ | Exports - AUG | 3.44B | 3.44b(a) | 11:45 |
| | NZ | Imports - AUG | 3.78B | 4.08b(a) | 11:45 |
| | GE | IFO - Business Climate - SEP | 106.5 | 108.7 | 21:00 |
| | GE | IFO - Current Assessment - SEP | 115.7 | 118.1 | 21:00 |
| | GE | IFO - Expectations - SEP | 97.3 | 100.1 | 21:00 |
| | UK | Nat'wide House prices sa (MoM) - SEP | 0.0% | -0.6% | 26 Sep – 1 Oct |
| | UK | Nat'wide House prices nsa (YoY) - SEP | -0.5% | -0.4% | 26 Sep – 1 Oct |
| 27-Sep | US | Chicago Fed Nat Activity Index - AUG | -0.40 | -0.06 | 01:30 |
| | US | New Home Sales - AUG | 294K | 298K | 03:00 |
| | US | New Home Sales MoM - AUG | -1.3% | -0.7% | 03:00 |
| | US | Dallas Fed Manf. Activity - SEP | -8.0 | -11.4 | 03:30 |
| | NZ | Corp Service Price Index (YoY) - AUG | -0.4% | -0.5% | 12:50 |
| | CH | Industrial Profits YTD YoY - AUG | - - | 28.3% | 15:00 |
| | GE | GfK Consumer Confidence Survey - OCT | 5.0 | 5.2 | 19:00 |
| | EC | Eurozone M3 s.a. 3 mth ave. - AUG | 2.0% | 2.1% | 21:00 |
| | EC | Eurozone M3 s.a. (YoY) - AUG | 2.0% | 2.0% | 21:00 |
| | UK | CBI Reported Sales - SEP | -15 | -14 | 23:00 |
| | CH | Leading Index - AUG | - - | 102.25 | 27-30 Sep |
| 28-Sep | US | S&P/CS Composite-20 YoY - JUL | -4.5% | -4.5% | 02:00 |
| | US | Consumer Confidence - SEP | 46.0 | 44.5 | 03:00 |
| | US | Richmond Fed Manufact. Index - SEP | -12 | -10 | 03:00 |
| | AU | HIA New Home Sales (MoM) - AUG | - - | -8.0% | 14:00 |
| | GE | Import Price Index (MoM) - AUG | -0.3% | 0.8% | 19:00 |
| | GE | Import Price Index (YoY) - AUG | 6.7% | 7.5% | 19:00 |
| | GE | Consumer Price Index (MoM) - SEP P | -0.1% | 0.0% | 28-29 Sep |
| | GE | Consumer Price Index (YoY) - SEP P | 2.4% | 2.4% | 28-29 Sep |
| 29-Sep | US | MBA Mortgage Applications - 23-SEP | - - | 0.6% | 00:00 |
| | US | Durable Goods Orders - AUG | -0.5% | 4.1% | 01:30 |
| | US | Durables Ex Transportation - AUG | 0.0% | 0.8% | 01:30 |
| | US | Cap Goods Orders Nondef Ex Air - AUG | -0.4% | -1.5% | 01:30 |
| | US | Cap Goods Ship Nondef Ex Air - AUG | - - | 0.2% | 01:30 |
| | JN | Retail Trade MoM SA - AUG | 0.2% | -0.3% | 12:50 |
| | JN | Large Retailers' Sales - AUG | -0.6% | 0.8% | 12:50 |
| | AU | Job vacancies - AUG | - - | -4.5% | 14:30 |
| | GE | Unemployment Change (000's) - SEP | -8K | -8K | 20:55 |
| | GE | Unemployment Rate (s.a) - SEP | 7.0% | 7.0% | 20:55 |
| | UK | Net Consumer Credit - AUG | £0.2B | £0.2B | 21:30 |
| | UK | Net Lending Sec. on Dwellings - AUG | £0.8B | £0.7B | 21:30 |
| | UK | Mortgage Approvals - AUG | 49.7K | 49.2K | 21:30 |
| | UK | M4 Money Supply (MoM) - AUG | - - | -0.1% | 21:30 |
| | UK | M4 Money Supply (YoY) - AUG | - - | -1.1% | 21:30 |
| | UK | M4 Ex OFCs 3M Annualised - AUG | - - | 3.5% | 21:30 |
| | EC | Business Climate Indicator - SEP | -0.12 | 0.07 | 22:00 |
| | EC | Eurozone Consumer Confidence - SEP F | -18.9 | -18.9 | 22:00 |
| | EC | Eurozone Economic Confidence - SEP | 96.0 | 98.3 | 22:00 |
| | EC | Eurozone Indust. Confidence - SEP | -5.0 | -2.9 | 22:00 |
| | EC | Eurozone Services Confidence - SEP | 2.0 | 3.7 | 22:00 |

Continued on following page

# DATA EVENT CALENDAR

| DATE | COUNTRY | DATA / EVENT | MKT. | LAST | NZ TIME |
|---|---|---|---|---|---|
| 30-Sep | US | GDP QoQ (Annualized) - 2Q T | 1.2% | 1.0% | 01:30 |
| | US | Personal Consumption - 2Q T | 0.4% | 0.4% | 01:30 |
| | US | GDP Price Index - 2Q T | 2.4% | 2.4% | 01:30 |
| | US | Core PCE QoQ - 2Q T | 2.2% | 2.2% | 01:30 |
| | US | Initial Jobless Claims - 24-SEP | 420K | - - | 01:30 |
| | US | Continuing Claims - 17-SEP | 3730K | - - | 01:30 |
| | US | Pending Home Sales MoM - AUG | -1.6% | -1.3% | 03:00 |
| | US | Pending Home Sales YoY - AUG | 6.3% | 10.1% | 03:00 |
| | US | Kansas City Fed Manf. Activity - SEP | - - | - - | 04:00 |
| | NZ | Building Permits MoM - AUG | -1.5% | 13.0% | 10:45 |
| | UK | GfK Consumer Confidence Survey - SEP | -33 | -31 | 12:01 |
| | JN | Job-To-Applicant Ratio - AUG | 0.65 | 0.64 | 12:30 |
| | JN | Overall Hhold Spending (YoY) - AUG | -2.8% | -2.1% | 12:30 |
| | JN | Jobless Rate - AUG | 4.7% | 4.7% | 12:30 |
| | JN | Tokyo CPI YoY - SEP | -0.2% | -0.2% | 12:30 |
| | JN | Tokyo CPI Ex-Fresh Food YoY - SEP | -0.1% | -0.2% | 12:30 |
| | JN | Tokyo CPI Ex Food, Energy YoY - SEP | -0.5% | -0.6% | 12:30 |
| | JN | Natl CPI YoY - AUG | 0.1% | 0.2% | 12:30 |
| | JN | Natl CPI Ex-Fresh Food YoY - AUG | 0.1% | 0.1% | 12:30 |
| | JN | Natl CPI Ex Food, Energy YoY - AUG | -0.6% | -0.5% | 12:30 |
| | JN | Industrial Production (MoM) - AUG P | 1.5% | 0.4% | 12:50 |
| | JN | Industrial Production YOY% - AUG P | 1.1% | -3.0% | 12:50 |
| | AU | RPData-Rismark House Px Raw - AUG | - - | -0.9% | 13:30 |
| | AU | RPData-Rismark House Px S.A - AUG | - - | -0.6% | 13:30 |
| | NZ | NBNZ Activity Outlook - SEP | - - | 43.3 | 14:00 |
| | NZ | NBNZ Business Confidence - SEP | - - | 34.4 | 14:00 |
| | AU | Private Sector Credit MoM% - AUG | 0.2% | 0.2% | 14:30 |
| | AU | Private Sector Credit YoY% - AUG | 2.8% | 2.7% | 14:30 |
| | NZ | Money Supply M3 YoY - AUG | - - | 6.3% | 15:00 |
| | CH | HSBC Manufacturing PMI - SEP | - - | 49.9 | 15:30 |
| | JN | Construction Orders (YoY) - AUG | - - | 5.7% | 18:00 |
| | JN | Annualized Housing Starts - AUG | 0.860M | 0.955M | 18:00 |
| | JN | Housing Starts (YoY) - AUG | 4.5% | 21.2% | 18:00 |
| | GE | Retail Sales (MoM) - AUG | -0.5% | 0.3% | 19:00 |
| | GE | Retail Sales (YoY) - AUG | -1.0% | -1.6% | 19:00 |
| | EC | Euro-Zone CPI Estimate (YoY) - SEP | 2.5% | 2.5% | 22:00 |
| | EC | Euro-Zone Unemployment Rate - AUG | 10.0% | 10.0% | 22:00 |
| 1-Oct | US | Personal Income - AUG | 0.1% | 0.3% | 01:30 |
| | US | Personal Spending - AUG | 0.2% | 0.8% | 01:30 |
| | US | PCE Deflator (YoY) - AUG | 2.9% | 2.8% | 01:30 |
| | US | PCE Core (MoM) - AUG | 0.2% | 0.2% | 01:30 |
| | US | PCE Core (YoY) - AUG | 1.7% | 1.6% | 01:30 |
| | US | Chicago Purchasing Manager - SEP | 55.5 | 56.5 | 02:45 |
| | US | U. of Michigan Confidence - SEP F | 57.8 | 57.8 | 02:55 |
| | US | NAPM-Milwaukee - SEP | 56.8 | 58.3 | 03:00 |
| | CH | PMI Manufacturing - SEP | - - | 50.9 | 14:00 |

Key: AU: Australia, EC: Euro-zone, GE: Germany, JN: Japan, NZ: New Zealand, UK: United Kingdom, US: United States, CH: China.
Sources: Dow Jones, Reuters, Bloomberg, ANZ, National Bank. All $ values in local currency.
Note: All surveys are preliminary and subject to change.

# LOCAL DATA WATCH

**Key focus over the next few weeks:** Global events continued to take precedence. The situation in Europe remains deeply troubling, with the risk of a global recession growing. Given the myriad of structural and cyclical factors at play, the tepid Q2 NZ GDP outturn, while unwelcome, was not a bolt out of the blue. The prospects of a stronger H2 remain good, with the Rugby World Cup a key support. However, we highlight the possibility of a weak first half of 2012 if earthquake reconstruction work is delayed. Encouragingly, dairy prices have not fallen by much as yet, with the upbeat Fonterra assessment temporarily allaying concerns that recent global wobbles would significantly dent the high milk price payout. We will continue to closely follow commodity price developments, with next week's ANZ Commodity Price Index of particular importance. Friday's September National Bank Business Outlook and next week's NZIER QSBO will give us an idea of how resilient the economy has been during the recent global volatility. The timing of the first OCR hike will be largely dependent on the global outlook, with the RBNZ likely to remain on hold until global volatility subsides. Higher domestic inflation is likely to be the sacrificial lamb. We expect the first OCR hike to take place in March 2012, but this is conditional on the global outlook improving – a big ask. Irrespective of the timing of the first OCR hike, the spirit of our assessment is for a gradual path of policy tightening and a historically low OCR endpoint.

| DATE | DATA/EVENT | ECONOMIC SIGNAL | COMMENT |
|---|---|---|---|
| Fri 30 Sep (10:45am) | Building Consents – Aug | Holding | A 2 percent increase in residential consents is envisaged. Non-residential consent values of around $300m are expected. |
| Fri 30 Sep (1:00pm) | National Bank Business Outlook - Sep | - - | - - |
| Fri 30 Sep (3:00pm) | RBNZ Credit Aggregates - Aug | Deleveraging | Low annual rates for household and business credit, with agricultural credit falling as farmers repay debt. |
| Mon 3 Oct (1:00pm) | ANZ Commodity Price Index – Sep | - - | - - |
| Tues 4 Oct (10:00am) | NZIER QSBO – 2011Q3 | Under pressure | Domestic confidence is likely to take a hit from the global gloom. But domestic focused indicators should hold up better, and indicators of capacity are likely to still warn of rising inflation pressure. |
| Wed 5 Oct | *GlobalDairyTrade* online auction | Holding | We expect dairy prices to hold firm at current levels. |
| Tues 11 Oct (10:45am) | Electronic Card Transactions - Sep | RWC boost | We expect a 2.5 percent increase in retail Electronic Card Transaction (ECT) spending underpinned by sizeable increases for hospitality and services spending. |
| Thur 13 Oct (10:45am) | Food Price Index – Sep | Up | A slight reversal from last month's fall is expected, with the 0.5 percent increase driven by higher meat and grocery prices. |
| Thur 13 Oct (1:00pm) | ANZ-Roy Morgan Consumer Confidence - Oct | - - | - - |
| Fri 14 Oct (10:45am) | REINZ Residential Sales - Sep | Up | We expect a 2 percent strengthening in house sales, with days to sale easing towards the high 30s. No change in prices is expected. |
| Fri 21 Oct (10:45am) | International Travel and Migration - Sep | RWC boost | A net permanent and long-term inflow of 300 persons is expected. Visitor arrivals are expected to surge 15 percent s.a. |
| Fri 21 Oct (10:45am) | RBNZ Credit Card Statistics – Sep | RWC boost | Card spending is expected to climb 2.5 percent, with spending on overseas issued cards surging. |
| **On Balance** | | **Local vs global** | **Domestic gauges for H2 should remain positive but global concerns suggest some caution further out.** |

# KEY FORECASTS AND RATES

| | Dec-10 | Mar-11 | Jun-11 | Sep-11 | Dec-11 | Mar-12 | Jun-12 | Sep-12 | Dec-12 | Mar-13 |
|---|---|---|---|---|---|---|---|---|---|---|
| GDP (% qoq) | 0.6 | 0.9 | 0.1 | **0.9** | **1.5** | **0.4** | **1.0** | **0.9** | **0.8** | **0.7** |
| GDP (% yoy) | 1.3 | 1.7 | 1.5 | **2.5** | **3.4** | **2.9** | **3.9** | **3.9** | **3.1** | **3.4** |
| CPI (% qoq) | 2.3 | 0.8 | 1.0 | **0.8** | **0.7** | **0.6** | **0.8** | **0.7** | **0.6** | **0.8** |
| CPI (% yoy) | 4.0 | 4.5 | 5.3 | **5.0** | **3.3** | **3.1** | **2.9** | **2.8** | **2.7** | **2.9** |
| Employment (% qoq) | -0.3 | 1.3 | 0.0 | **0.7** | **0.6** | **0.7** | **0.5** | **0.5** | **0.4** | **0.4** |
| Employment (% yoy) | 1.3 | 1.8 | 2.0 | **1.7** | **2.6** | **2.0** | **2.5** | **2.3** | **2.1** | **1.8** |
| Unemployment Rate (% sa) | 6.7 | 6.5 | 6.5 | **6.2** | **5.9** | **5.6** | **5.5** | **5.3** | **5.3** | **5.3** |
| Current Account (% GDP) | -3.5 | -3.6 | -3.7 | **-4.0** | **-3.7** | **-4.1** | **-4.3** | **-4.6** | **-4.9** | **-5.0** |
| Terms of Trade (% qoq) | 0.8 | 0.8 | 2.3 | **3.0** | **1.0** | **-0.9** | **-0.8** | **-0.8** | **-0.8** | **-0.8** |
| Terms of Trade (% yoy) | 12.3 | 6.7 | 7.0 | **7.1** | **7.3** | **5.5** | **2.3** | **-1.4** | **-3.3** | **-3.1** |

| | Dec-10 | Jan-11 | Feb-11 | Mar-11 | Apr-11 | May-11 | Jun-11 | Jul-11 | Aug-11 | Sep-11 |
|---|---|---|---|---|---|---|---|---|---|---|
| Retail ECT (% mom) | -0.9 | 2.4 | -0.1 | 1.5 | 1.4 | -0.7 | 1.1 | 0.3 | -0.7 | .. |
| Retail ECT (% yoy) | 4.4 | 5.7 | 6.2 | 6.6 | 10.0 | 6.8 | 9.0 | 8.0 | 8.4 | .. |
| Credit Card Billings (% mom) | -1.7 | 3.1 | -0.2 | 0.1 | 1.2 | 0.5 | 0.6 | 0.7 | -1.2 | .. |
| Credit Card Billings (% yoy) | 2.4 | 5.8 | 5.1 | 2.9 | 6.2 | 5.9 | 5.8 | 7.9 | 4.9 | .. |
| Car registrations (% mom) | -8.8 | 1.3 | -2.0 | 0.0 | -5.5 | 3.6 | -2.0 | -1.0 | 6.5 | .. |
| Car registrations (% yoy) | 6.4 | 6.8 | 2.8 | -1.0 | -10.5 | -3.7 | -9.5 | -6.0 | 1.9 | .. |
| Building consents (% mom) | -18.7 | 9.0 | -9.7 | 2.6 | -1.1 | 3.1 | -1.0 | 13.0 | .. | .. |
| Building consents (% yoy) | -26.5 | -14.6 | -28.9 | -26.0 | -32.3 | -21.9 | -25.4 | -15.7 | .. | .. |
| REINZ House Price Index (% yoy) | -1.6 | -2.6 | -0.7 | -1.8 | -0.4 | -0.7 | 0.0 | 0.5 | 0.7 | .. |
| Household Lending Growth (% mom) | 0.1 | 0.1 | 0.1 | -0.1 | 0.2 | 0.1 | 0.1 | 0.2 | .. | .. |
| Household Lending Growth (% yoy) | 1.6 | 1.5 | 1.5 | 1.2 | 1.2 | 1.2 | 1.2 | 1.2 | .. | .. |
| ANZ Roy Morgan Consumer Confidence | 112.2 | 117.1 | 108.1 | 101.4 | 101.4 | 103.3 | 112.5 | 109.4 | 113.3 | 112.6 |
| NBNZ Business Confidence | 29.5 | .. | 34.5 | -8.7 | 14.2 | 38.3 | 46.5 | 47.6 | 34.4 | .. |
| NBNZ Own Activity Outlook | 34.5 | .. | 36.6 | 14.7 | 29.5 | 39.7 | 38.7 | 43.7 | 43.3 | .. |
| Trade Balance ($m) | -218 | 9 | 184 | 583 | 1158 | 550 | 200 | 111 | -641 | .. |
| Trade Balance ($m ann) | 1172 | 909 | 765 | 741 | 1238 | 1019 | 998 | 1295 | 1084 | .. |
| ANZ World Commodity Price Index (% mom) | 1.6 | 4.3 | 2.7 | 4.7 | 1.6 | 0.4 | -1.2 | -0.2 | -1.2 | .. |
| ANZ World Commodity Price Index (% yoy) | 12.1 | 16.3 | 20.3 | 23.5 | 19.8 | 19.6 | 20.6 | 22.2 | 22.1 | .. |
| Net migration (sa) | 720 | 430 | 430 | -510 | -120 | -340 | -260 | -150 | 210 | .. |
| Net migration (annual) | 10451 | 8689 | 8249 | 6554 | 5508 | 4625 | 3867 | 2867 | 2257 | .. |

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

# KEY MARKET FORECASTS AND RATES

| | ACTUAL | | | Forecast (end month) | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| FX RATES | Jul-11 | Aug-11 | Today | Sep-11 | Dec-11 | Mar-12 | Jun-12 | Sep-12 | Dec-12 | Mar-13 |
| NZD/USD | 0.879 | 0.854 | 0.775 | 0.88 | 0.91 | 0.92 | 0.93 | 0.93 | 0.93 | 0.92 |
| NZD/AUD | 0.799 | 0.798 | 0.789 | 0.80 | 0.81 | 0.82 | 0.83 | 0.82 | 0.82 | 0.82 |
| NZD/EUR | 0.610 | 0.594 | 0.573 | 0.60 | 0.61 | 0.61 | 0.61 | 0.60 | 0.60 | 0.60 |
| NZD/JPY | 67.54 | 65.48 | 59.31 | 66.0 | 68.3 | 69.0 | 67.0 | 67.0 | 67.0 | 68.1 |
| NZD/GBP | 0.536 | 0.526 | 0.500 | 0.53 | 0.55 | 0.54 | 0.55 | 0.53 | 0.53 | 0.53 |
| NZ$ TWI | 74.2 | 73.0 | 68.9 | 74.1 | 75.9 | 76.3 | 76.7 | 75.8 | 75.8 | 75.7 |
| INTEREST RATES | Jul-11 | Aug-11 | Today | Sep-11 | Dec-11 | Mar-12 | Jun-12 | Sep-12 | Dec-12 | Mar-13 |
| NZ OCR | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 | 2.75 | 3.00 | 3.25 | 3.50 | 3.75 |
| NZ 90 day bill | 2.95 | 2.99 | 2.84 | 2.80 | 2.80 | 3.20 | 3.30 | 3.70 | 3.80 | 4.20 |
| NZ 10-yr bond | 4.93 | 4.52 | 4.23 | 4.40 | 4.40 | 4.50 | 4.60 | 4.80 | 4.90 | 5.00 |
| US Fed funds | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| US 3-mth | 0.26 | 0.33 | 0.36 | 0.35 | 0.35 | 0.35 | 0.35 | 0.35 | 0.35 | 0.35 |
| AU Cash Rate | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 | 4.75 |
| AU 3-mth | 5.07 | 4.87 | 4.76 | 4.90 | 4.90 | 4.90 | 4.90 | 4.90 | 4.90 | 4.90 |

| | 23 Aug | 19 Sep | 20 Sep | 21 Sep | 22 Sep | 23 Sep |
|---|---|---|---|---|---|---|
| Official Cash Rate | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 | 2.50 |
| 90 day bank bill | 2.88 | 2.82 | 2.82 | 2.80 | 2.81 | 2.81 |
| NZGB 04/13 | 3.01 | 2.98 | 2.96 | 2.99 | 2.87 | 2.81 |
| NZGB 04/15 | 3.58 | 3.47 | 3.45 | 3.49 | 3.35 | 3.26 |
| NZGB 03/19 | 4.32 | 4.23 | 4.21 | 4.23 | 4.11 | 4.01 |
| NZGB 05/21 | 4.49 | 4.43 | 4.41 | 4.42 | 4.34 | 4.24 |
| 2 year swap | 3.31 | 3.24 | 3.19 | 3.22 | 3.10 | 3.05 |
| 5 year swap | 4.12 | 3.89 | 3.83 | 3.85 | 3.73 | 3.66 |
| RBNZ TWI | 71.01 | 72.19 | 72.05 | 72.04 | 69.70 | 69.30 |
| NZD/USD | 0.8269 | 0.8221 | 0.8200 | 0.8234 | 0.7806 | 0.7766 |
| NZD/AUD | 0.7912 | 0.8035 | 0.8034 | 0.7974 | 0.7967 | 0.7941 |
| NZD/JPY | 63.50 | 63.24 | 62.74 | 62.87 | 59.70 | 59.46 |
| NZD/GBP | 0.5017 | 0.5240 | 0.5230 | 0.5201 | 0.5072 | 0.5024 |
| NZD/EUR | 0.5755 | 0.6019 | 0.6023 | 0.5921 | 0.5782 | 0.5753 |
| AUD/USD | 1.0451 | 1.0231 | 1.0206 | 1.0205 | 0.9797 | 0.9779 |
| EUR/USD | 1.4369 | 1.3658 | 1.3615 | 1.3720 | 1.3501 | 1.3501 |
| USD/JPY | 76.79 | 76.93 | 76.51 | 76.36 | 76.48 | 76.61 |
| GBP/USD | 1.648 | 1.569 | 1.568 | 1.573 | 1.539 | 1.545 |
| Oil (US$/bbl) | 84.30 | 87.97 | 85.67 | 86.76 | 80.51 | 79.85 |
| Gold (US$/oz) | 1903.7 | 1821.1 | 1777.5 | 1808.0 | 1747.0 | 1656.0 |
| Electricity (Haywards) | 8.43 | 6.55 | 9.74 | 8.31 | 6.50 | 9.75 |
| Baltic Dry Freight Index | 1565 | 1764 | 1795 | 1811 | 1884 | 1920 |
| Milk futures (USD) | 150.5 | 147.5 | 147.5 | 149.0 | 150.5 | 150.5 |

# IMPORTANT NOTICE

## NEW ZEALAND DISCLAIMER



## UNITED STATES DISCLAIMER



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