

TRENDS AND TENSIONS

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Page 2: Economic overview

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Page 5: Economic comment – reversing the trend

- > The Minister of Finance and Prime Minister have been explicit in signalling that the Government will not let the Treasury's December forecasts of ever increasing debt levels eventuate. While medium-term projections are prone to a huge degree of uncertainty, we look at some of the options available to achieve a declining debt track. Material changes across government and expense growth are required. This should keep Standard & Poor's at bay, but of course the challenge will be to deliver on the strategy. Prospects for fiscal consolidation fit with the RBNZ's lower for longer view.

Page 7: Economic comment – financial conditions update

- > Financial conditions have improved markedly in the past month. Credit markets continue to show signs of improvement, and equity markets have rallied strongly. Our Financial Conditions Indexes (FCI) are pointing to recoveries taking hold at the end of this year, assuming no relapse in global markets.

Page 8: Economic comment – global watch

- > More green shoots look to be sprouting in the US, with data generally coming out stronger than expected last week. A similar story also looks to be developing around the rest of the globe, but to a lesser extent. PMI gauges in the UK, Europe and Asia all recorded improvements.

Page 9: Interest rate strategy

- > Positioning and flow, and the emergence of "green shoots" have frustrated RBNZ Governor Bollard's attempts to get market interest rates lower. Don't be discouraged by the rise in rates, as this is not the market expressing a view on future policy.

Page 10: Currency strategy

- > The currency market continues to be closely correlated to the equity market of late, as money managers scramble to put cash to work. The loser has been the US Treasury market with yield differentials narrowing in the USD's favour. But the market is intent on punishing those who embark on QE and rewarding those who don't. The euro has exploded north on news that the ECB has no intention of printing money. The USD is firmly on the back foot, which means the NZD is on the front foot. Markets are beginning to trend, but this is very dependent on equities holding gains.

Page 11: Currency comment – effective exchange rates

- > As was the case in March, all the commodity adjusted real exchange rates we monitor became more restrictive in April.

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ECONOMIC OVERVIEW

Data tends to run in strings and the “green shoots” must be respected – for now. We now expect the RBNZ to pause in June before resuming easing in H2. It is still too early to say the green shoots will turn into something more substantial, and we see the market turning from one of *trends* to *tensions*. Data this week is likely to provide further evidence of stabilisation.

What’s ahead?

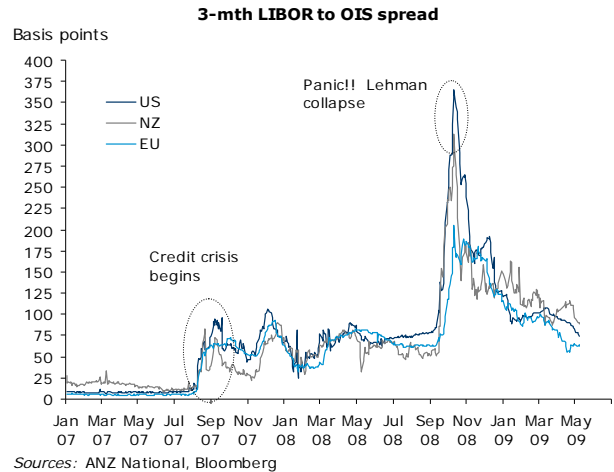
- > **April REINZ House Sales** (circa 12 May). The data is likely to confirm the anecdotes, with further improvement seen in house sales. Prices should remain under downward pressure though.
- > **April Food Prices** (Tuesday 1045 NZST). Volatile on a monthly basis and showing some persistence, but we expect annual growth to ease.
- > **RBNZ Financial Stability Report** (Wednesday 0900 NZST). The RBNZ will emphasise the strength of NZ’s financial system, although within the context of major economic challenges.
- > **March Retail Trade Survey** (Friday 1045 NZST). Total nominal headline sales are expected to rise by 0.5 percent in the month, with core spending also rising 0.5 percent. However, for the quarter, real spending is expected to tumble 1.7 percent.

What’s the view?

Recent data continues to point to stabilisation and the so-called “green shoots”. Data tends to run in strings and an improving trend is becoming more apparent by the day. Global equity markets have continued their march higher, risk appetites look to be mending, and economic data is finding a base (or at least pointing to slower rates of contraction), particularly in the US. Markets also seem to have shrugged off the news of the US banks’ stress test results showing the need for some banks to raise additional capital, and are continuing to price for recovery. This is all encouraging news, and it needs to be acknowledged. Confidence is an important pillar of any financial system and economy.

Even credit markets are thawing. LIBOR-OIS spreads (one measure of banks’ willingness to lend to one another) and credit default swap spreads (a measure of corporate default risk) are also well off their panic-driven extremes, although less improvement is apparent in the long-end of the yield curve. The Australian 5-year iTraxx index has fallen from a peak of over 450 basis points in

March, to now sit around 240 basis points. Yes, these measures still remain well above their pre-crisis levels – and we need to remain mindful of the level versus the change. But it is the trend that is dominating sentiment at present and it clearly shows that things are on the mend, or at least the Armageddon scenario has been averted.



The same also appears to be the case in NZ, and as we discussed in last week’s *Market Focus*, there are also definite signs that these green shoots are sprouting locally. The housing market is recovering (and REINZ data out this week is likely to reinforce this), business confidence has bounced and net migration flows are improving. Even the labour market data out last week was not as bad as feared. While employment tumbled 1.1 percent in Q1, the unemployment rate “only” rose to 5.0 percent as a number of workers leaving the labour force limited its rise. Compared with the deterioration in labour markets around the globe, NZ’s labour market remains relatively resilient, although it may also be a case of pending catch-up to come.

So what do we make of it all?

Trends have to be respected, and we are well aware of the tendency of data to run in strings, particularly considering the precipitous falls in Q4 2008. This string is hardly “positive” but anything that is less negative gives hope, and that’s what markets are trading on at present.

As noted last week, we remain suspicious about the ability of so-called green shoots to manifest into a sustainable recovery. Apart from the level-change dynamic we mentioned last week – with the latter good and the former still poor – we simply have not seen the improvements in key structural indicators to give us the confidence to start talking about a sustained and quality upturn.

From a markets perspective, we’d characterise it as an environment of shifting from trends to tensions. The trends in markets were pretty obvious over the past year. A rapidly deteriorating global

environment and aversion to risk meant equities, commodities, the commodity bloc currencies and interest rates in general were headed lower. Normally at the nadirs in the economic cycle, reflationary forces such as monetary policy and fiscal policy give the market confidence that once a turning point is reached, we can look forward to a sustained and quality upturn. History shows that economists under-estimate the recoveries just as they tend to under-estimate the troughs.

However, this cycle is different in a number of regards. First, it is the depth and scale of the downturn in the first-place, and second, it is accompanied by a financial crisis. As the IMF noted in their recent *World Economic Outlook*, synchronised global recessions associated with financial crises tend to take twice as long to recover and the growth rates during these recovery periods tend to be half those of a "typical" recovery. The market needs to appreciate the structural changes happening around the globe in the process of credit facilitation and creation. Credit markets are simply not what they were before the crisis, nor are they likely to be again – regulators will make sure of that! This removes a major source of demand for the global economy – the so-called credit accelerator dynamic. It will surely take time for major debt-fuelled consumption driven models of the West to transition to more earnings centric approaches. And the same goes for export-dependent nations, such as Japan, to do the reverse.

This expected transition from trends to one of tensions is another way of saying we are now trading ranges. We believe (and certainly hope) the worst of the credit crisis is behind us, but typical reflationary forces still face headwinds. We see these tensions in a number of avenues including:

- > Printing money versus the potential for inflation – a quick recovery killer if the market gets a whiff of it.
- > How do policymakers support market forces but make sure it never happens again?
- > Providing bailouts versus moral hazard issues. What are regulators going to want in return?
- > The dynamics of household de-leveraging versus the historic credit shock experience of corporate balance sheet rebuilding.
- > The global (specifically US) economy spending its way out of a spending induced jam courtesy of interest rate and tax cuts!
- > The monetary policy transmission mechanism versus the credit channel with lending standards still tight.

- > Rebuilding private sector balance sheets via public debt issuance, which is placing upward pressure on the long-end of the curve.
- > Signs of cyclical stabilisation but limited structural improvements across current account deficits in the West.

This combination leaves us acknowledging the improvement we have seen in some key cyclical gauges (and we also note that the Baltic Dry Freight Index is up 23 percent last week) – and hence the turn in some key trends across markets. But we are still mindful of inevitable tensions and structural forces, which we expect to manifest via continued volatility, but in a range fashion as opposed to trends.

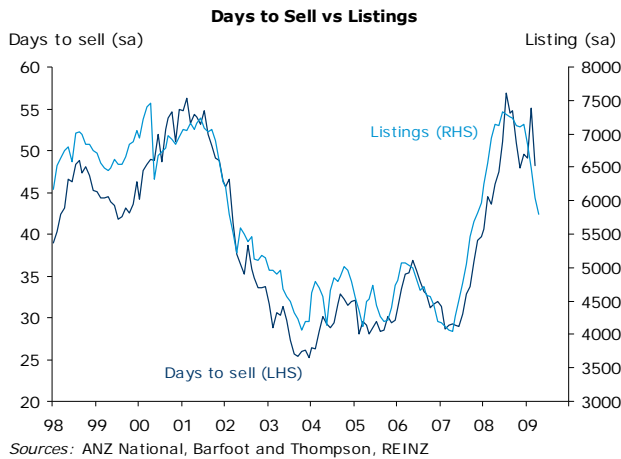
Whichever way we cut it in terms of looking at the catalysts and solutions to global malaise or economic cycle, one thing seems obvious: time will play a key role in the healing and recovery process.

In terms of our financial market views, respect for the string we are seeing in the data has led us to defer the June rate cut we were expecting, and shift it to H2 2009. This is based on our view that signs of green shoots will ultimately wilt. While a case can be made for the RBNZ continuing to ease immediately if they share a similar view to ours, the reality is that the RBNZ has delivered a massive front-loading of 575bps of cuts since July last year. There is less pressure to act with the OCR at 2.50 percent and certainly with the RBA on hold at 3 percent. With policy now in the glide-path, data becomes much more critical (and hence we respect recent signs of stabilisation). But importantly, the RBNZ will be well aware that policy is not getting the desired traction at present given where deposit rates sit. Higher deposit rates are limiting the pass through to lending rates, which will be a source of frustration for the RBNZ. Hence there is little point firing bullets willy nilly if you are not going to get any impact. Better to hold off and wait for another day.

The currency is also another frustrating leg but there is obviously little the RBNZ can do. Bigger global forces are at play. Suffice to say we are in no doubt the currency will take care of itself if global sentiment changes. While tempted to alter our currency view as well, given our changed view towards the RBNZ, we see little point at present given wider global forces. We would rather see how things evolve over the week ahead as opposed to react immediately.

Looking to the release calendar, we see domestic data as once again reinforcing a stabilisation and recovery theme – but at low levels. REINZ house sales data for April (as mentioned above) are likely to again show a reasonable increase in the number of house sales in the month. Barfoot and Thompson Auckland house sales showed an

impressive 33 percent seasonally adjusted increase in April. We don't expect this kind of bounce in total nationwide sales, as Auckland was the first to experience weakness so it is only natural to be the first out, but the direction will undoubtedly be up. The drop off in the number of listings also suggests that the median days to sell – a key indicator we watch – will continue to ease.



Retail spending data for March is also expected to show some signs of stabilisation. For the month, we expect total nominal sales to rise 0.5 percent, with a small rebound in motor vehicle retailing (following some large falls over previous months) a contributing factor. However, core spending (which strips out motor vehicle related industries) is also expected to rise by 0.5 percent. It has been clear of late that households have been saving the benefits of tax cuts and interest rate reductions. However, the bungy-cord, like in the housing market, is beginning to tighten and we expect spending to begin to find a base around these levels. As we mentioned last week though, the rate of change and the base (or level) effect needs to be distinguished. The quarterly real numbers are not expected to be so positive, with a large 1.7 percent contraction expected. This again lays the groundwork for our expectation that GDP again headed backwards in March quarter, and not by a small amount.

The final big domestic event this week is the RBNZ's *Financial Stability Report*. We are not expecting too many surprises from this. The RBNZ usually keep a reasonably distinct line between financial stability and monetary policy developments, although we all know that line has become very blurred given the credit nature of economic events. We will be looking for whether the Bank feels it worthy to comment on recent NZD and wholesale interest rate movements. The report itself is likely to state that NZ's financial system remains solid (particularly compared to global counterparts), albeit with the usual risks and the signs that bad debts are rising off low levels.

Internationally, there are a few pieces of information that will be of interest. In the US, retail sales, industrial production and CPI data will be a focus, as will be speeches from a number of Fed officials. In the UK, labour market data and the BoE's *Quarterly Inflation Report* will be interesting, while Euro-zone advanced March quarter GDP is expected to contract again.

Recent local data...

- > **Quarterly Employment Survey (March quarter):** Private sector ordinary time wages rose 1.1 percent. Seasonally adjusted paid hours fell 0.4 percent, while filled jobs fell 2.6 percent.
- > **Financial Statements of Government (nine months to March):** An underlying operating deficit (OBEGAL) of \$0.2 billion was recorded, \$1.3 billion below the *December Update* forecast, and largely due to lower than forecast tax revenue.
- > **Labour Cost Index (March quarter):** Quality adjusted private sector ordinary time wages rose 0.5 percent, taking annual growth to 3.0 percent.
- > **Household Labour Force Survey (March quarter):** Employment fell 1.1 percent. However, a 0.7 percentage point drop in the participation rate to 68.4 percent saw the unemployment rate only rise 0.3ppt to 5.0 percent.

REVERSING THE TREND

The Minister of Finance and Prime Minister have been explicit in signalling that the Government will not let the Treasury's December forecasts of ever increasing debt levels eventuate. While medium-term projections are prone to a huge degree of uncertainty, we look at some of the options available to achieve a declining debt track. Material changes across government and expense growth are required. This should keep Standard & Poor's at bay, but of course the challenge will be to deliver on the strategy. Prospects for fiscal consolidation fit with the RBNZ's lower for longer view.

The Government's Financial Statements for the nine months to March 2009, released last week, highlight the impact of a weak economic backdrop on the fiscal position. Tax revenue is running around \$0.7 billion below the central *December Update* forecast. The underlying operating balance (OBEGAL) is about \$1.3 billion below the same forecast and we estimate it is around \$1 billion below even the *December Update* downside scenario.¹ While this should not really come as a surprise, given that the Minister of Finance (MoF) stated a few weeks ago that *"the government's books are undoubtedly in worse shape now than Treasury predicted in the December downside forecast,"* it is still a worrying trend.

The downside scenario from the Treasury's *December Update* had underlying operating deficits being maintained above 4 percent of GDP for the foreseeable future and gross debt on a relentless march past 75 percent of GDP. However, the MoF and the Prime Minister (PM) have both been explicit in stating that this is not an acceptable outcome. The PM has been quoted as saying the Treasury's numbers *"had an upward-sloping debt curve that would have been unacceptable to the Government."* Along with the desire to have a declining debt track, the Government is very committed to avoiding a credit rating downgrade.

Holding the PM and MoF to their word, we update our modelling work, which we first presented in our 26 January edition of the *Market Focus* (a further update was provided on 23 February). Specifically, we look at the alternatives available to the Government to get gross debt on a declining trajectory (as a percent of GDP) over the medium-term, using the Treasury's Fiscal Strategy Model (FSM). Of course, medium-term projections are subject to a wide degree of uncertainty, so it is ultimately the trends that are important as opposed to the numbers themselves.

Using the downside scenario from the Treasury's *December Update* plus some adjustments to incorporate our own economic forecasts (which we feel will now be closer to the Treasury's central track in the upcoming *Budget*), we present six different scenarios below:²

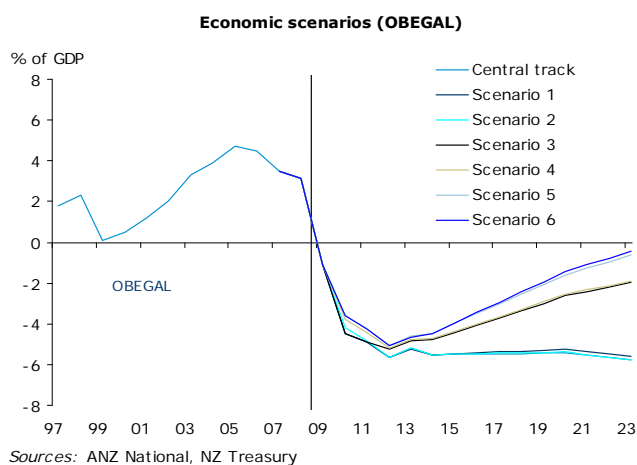
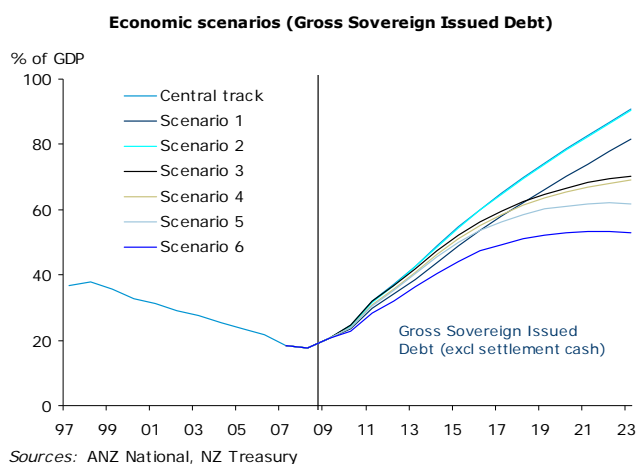
- > **Scenario 1: Suspend NZS Fund contributions.** This scenario assumes contributions to the NZS Fund are halted from the July 1st (the next fiscal year). The contributions had been running at around \$2 billion per annum over recent years.
- > **Scenario 2: Upfront cost savings.** The *December Update* assumed operating provisions of \$1.75 billion per annum for new spending and tax initiatives. This scenario assumes that the Government is able to find upfront cost savings of \$500 million. These savings are then "banked". However, the operating provision, or the growth in new expenditure, is maintained at \$1.75 billion.
- > **Scenario 3: A delayed cut to the operating provisions.** This scenario assumes that the operating provisions are cut by \$750 million to \$1 billion, but this does not occur until fiscal year 2012. This fits with the idea of fiscal policy still providing near-term support to the economy but then being removed to provide a credible medium-term strategy. While we use the term "cut", this scenario is really about growing expenditure more slowly. From fiscal year 2014 the \$1 billion provision grows in line with inflation, which is a step down from recent growth.
- > **Scenario 4: Upfront cost savings and a permanent cut to the operating provisions.** This scenario speaks for itself. As in scenario 2, the Government finds upfront costs savings of \$500 million that they are able to maintain. However, this scenario also assumes they commit to lower expenditure growth (or smaller provisions) going forward. As in scenario 3, the operating provisions are cut to \$1 billion, but this occurs immediately and is permanent.
- > **Scenario 5: More aggressive.** The same as scenario 4, except that the operating provisions are cut by a larger amount to \$750 million per year.
- > **Scenario 6: The combo.** This is a combination of scenarios 1 and 5.

So what does this analysis show?

¹ Operating Balance excluding Gains and Losses.

² This gives an opening operating balance estimate closer to 6 percent of GDP in fiscal year 2023 rather than the 4.5 percent of GDP flagged in the downside scenario.

Firstly, one off cost savings will not be enough. Scenario 2, or upfront costs savings of \$500 million, barely moves the projected debt track at all. Second, just halting contributions to the NZS Fund (scenario 1) is also nowhere near enough to see gross debt trend lower. What is required is something more material and scenarios four, five and six show that by permanently cutting the operating provisions, there are some reasonable changes to the gross debt projection. However, it looks as though it will take a reasonably large cut to the provisions (i.e. scenarios five and six) to get the gross debt track heading lower (and the operating balance back into the black), although it could hardly be called a trend.



The Prime Minister, in his pre-*Budget* speech last week hinted that this type of strategy would be the case, stating “...the Government will make some responsible decisions in this Budget. These will include delaying some steps in our economic plan that we would have rather made sooner. They will also include reducing the amount of extra spending available for future Budgets and making some savings in less effective areas of government spending.”

Assuming there is not much that can be done in the near-term to increase revenue (such as hiking taxes on high income earners, as has recently occurred in the UK), then the burden falls on the

expenditure side. This may sound relatively easy, since core government expenditure is around \$57 billion per year. If you exclude welfare spending (which the Prime Minister has said will not be touched) and spending on health, education (spending in those areas will increase due to natural cost pressures), police, defence and financing costs, then there is only \$11 billion of “core bureaucracy” to work with. Hence, actually cutting spending is not really an option. Rather it is about restraining growth.

The upshot

The blend of deferred NZS Fund contributions, less discretionary spending (or new initiative growth for things such as tax cuts), in combination with upfront cost savings looks like what is required to get the gross debt track heading lower. This will not be an easy task by any means and will require some tough decisions.³

The alternative – doing nothing – is simply unpalatable. To let debt rise unchecked – albeit off lows – would lead to an inevitable downgrade to the sovereign credit rating, which would mean higher interest rates for all. Moreover, while it’s convenient to borrow and lean on the Government’s balance sheet, we should not lose sight of the fact that this simply transfers a burden to the next generation, who ends up having to pay it back. Although we also need to acknowledge that the previous paying down of debt has placed us in a stronger position than otherwise would have been the case.

New Zealand is entering a period of inevitable fiscal consolidation. Like other pockets of the economy (including banking!), the Government is facing an environment that is different. Weak growth is eroding the tax base, and as the economy rebalances away from being debt and consumption centric to earnings focused, tax revenue will remain weak for a number of years. As the population ages, economic growth will invariably slow, hence a stronger focus on doing things smarter is required for prior growth rates to be maintained. And as the population ages, even greater spending pressure will come to bare, hence, the earlier the process of fiscal consolidation is started (although now is not the time to be aggressively cutting spending either) the better.

Finally, we also note that prospects for a material period of fiscal consolidation at some stage also fits with the RBNZ’s lower for longer view on interest rates.

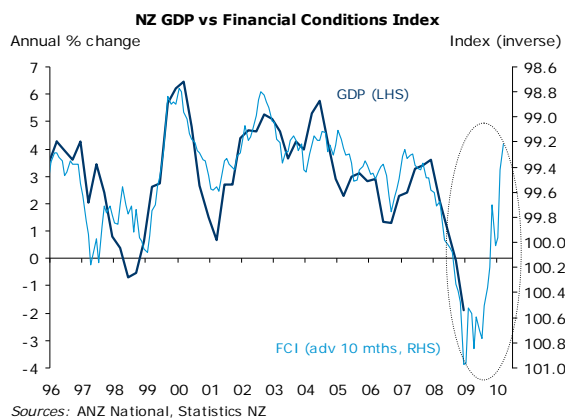
³ However, it must be stressed that our scenario results are merely indicative, and such long-term modelling is prone to a huge degree of uncertainty. It is possible to tweak the Treasury’s Strategy model in a number of other areas to yield different results.

FINANCIAL CONDITIONS UPDATE

Financial conditions have improved markedly in the past month. Credit markets continue to show signs of improvement, and equity markets have rallied strongly. Our Financial Conditions Indexes (FCI) are pointing to recoveries taking hold at the end of this year, assuming no relapse in global markets.

Happy days?

Traditional monetary conditions in NZ may have tightened courtesy of a stronger NZD and higher swap rates (despite the RBNZ cutting 50bp), but these were more than offset by improvements in equity prices and a narrowing in the credit default swap spread for the big four Australian banks (which we use as a proxy for the cost of funds). In addition, the most recent US Fed Senior Loan Officer Survey (which we use as a proxy for the supply of credit) showed the proportion of institutions tightening lending standards edging down, though still remaining elevated.

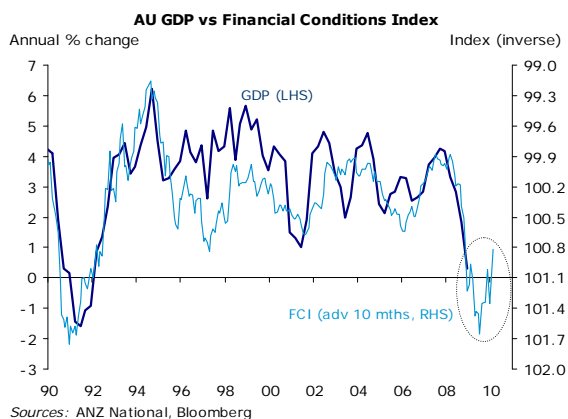


House prices continue to fall (based on the QV measure), while credit growth remains weak. But overall, our FCI for NZ has shown a substantial loosening over April and in the early part of May (based on current spot prices). Indeed, our FCI is pointing to a strong rebound with annual growth potentially heading towards 4 percent by late 2010, although this comes off a contraction of around 3 percent. However, we have to bear in mind when looking at growth rates that a base effect is at work here, and the economy is still set for some near-term weakness. We are of course very mindful that such measures will not capture structural aspects to this cycle, such as the mitigating effects that deposit rates are having on OCR cuts in so far as borrowing rates are concerned, nor the credit channel of monetary policy. Nonetheless, our FCI has proven to be a reliable indicator, and one we continue to watch.

Avoiding the hard landing?

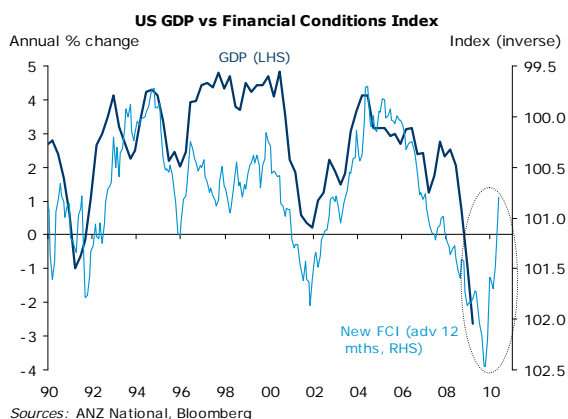
Australia's financial conditions tell a similar story to NZ's. The AUD and swap yields have moved higher

of late, while house prices have declined and credit growth remains weak. But the narrowing in the banks' credit default swap spread and strong rally in equities has seen financial conditions ease. Our FCI for Australia continues to point to a recession "lite", with the economy set to head back into positive growth by the end of the year, though the rebound is looking somewhat muted at this stage.



Those green shoots are sprouting

Our FCI for the US is still pointing towards further falls in GDP, but a turnaround is looking likely at the end of the year. The financial system appears to be on the mend, and US equities have rallied very strongly. The much talked about green shoots seem to be sprouting and looks consistent with our FCI, which is hinting of positive annual growth rates by early next year.



The upshot

Financial conditions are moving in the right direction, after having tightened massively since the credit crisis began. While our FCI is consistent with growth returning to positive territory, with monetary policy effectively near the end point (it is already there in the US), further easing is dependent on recent increases in equity markets being sustained, and credit markets continuing to improve. However, the big unknown is to what degree the traditional FCI linkages to the economy have changed, and this is an area we continue to research.

GLOBAL DATA WATCH

More green shoots look to be sprouting in the US, with data generally coming out stronger than expected last week. A similar story also looks to be developing around the rest of the globe, but to a lesser extent. PMI gauges in the UK, Europe and Asia all recorded improvements.

Country/ Area	Indicator	Market	Actual	Last	Outturn vs market	
Australia	House Price Index (1Q) – qoq	0.0%	-2.2%	-1.2%	Weaker	
	Building Approvals (Mar) – mom	2.8%	3.5%	8.0%	Stronger	
	RBA Cash Target	3.00%	3.00%	3.00%	In-line	
	Retail Sales (Mar) – mom	0.5%	2.2%	-2.0%	Stronger	
	Trade Balance (Mar)	1700M	2498M	1752M	Stronger	
	Employment Change (Apr)	-25.0K	27.3K	-37.2K	Stronger	
	Unemployment Rate (Apr)	5.9%	5.4%	5.7%	Stronger	
	US	Pending Home Sales (Mar) – mom	0.0%	3.2%	2.0%	Stronger
	Construction Spending (Mar) – mom	-1.6%	0.3%	-1.0%	Stronger	
	ISM Non-Manufacturing Composite (Apr)	42.2	43.7	40.8	Stronger	
	Non-Farm Productivity (1Q P)	0.6%	0.8%	-0.6%	Stronger	
	Unit Labour Costs (1Q P)	2.7%	3.3%	5.7%	Stronger	
	Continuing Claims (w/e Apr 26)	6350K	6351K	6295K	In-line	
	Consumer Credit (Mar)	-\$4.0B	-\$11.1B	-\$8.1B	Weaker	
	Change in Non-Farm Payrolls (Apr)	-600K	-539K	-699K	Stronger	
	Unemployment Rate (Apr)	8.9%	8.9%	8.5%	In-line	
	Average Hourly Earnings (Apr) – mom	0.2%	0.1%	0.2%	Weaker	
	Wholesale Inventories (Mar)	-1.0%	-1.6%	-1.7%	Weaker	
Euro-zone	PMI Manufacturing (Apr F)	36.7	36.8	36.7	In-line	
	PPI (Mar) – mom	-0.6%	-0.7%	-0.4%	In-line	
	PMI Services (Apr F)	43.1	43.8	43.1	Stronger	
	Retail Sales (Mar) – mom	0.1%	-0.6%	-0.3%	Weaker	
	ECB Interest Rate	1.00%	1.00%	1.25%	In-line	
UK	PMI Construction (Apr)	31.9	38.1	30.9	Stronger	
	PMI Services (Apr)	46.3	48.7	45.5	Stronger	
	BoE Interest Rate	0.50%	0.50%	0.50%	In-line	
	PPI Input (Apr) – mom	0.8%	-1.0%	1.3%	Weaker	
Asia Ex-Japan						
	<i>China</i>	CLSA Manufacturing PMI (Apr)	-	50.1	44.8	-
	<i>South Korea</i>	PPI (Apr) – yoy	-	1.5%	3.5%	-
	<i>Singapore</i>	PMI (Apr)	-	49.2	47.1	-
	<i>Hong Kong</i>	PMI (Apr)	-	44.3	42.7	-
		Retail Sales – Volume (Mar) – yoy	-6.8%	-9.3%	-13.9%	Weaker
	<i>Malaysia</i>	Exports (Mar) – yoy	-17.3%	-15.6%	-16.0%	Stronger
		Imports (Mar) – yoy	-26.7%	-28.7%	-27.6%	Weaker
	<i>Taiwan</i>	CPI (Apr) – yoy	-0.5%	-0.5%	-0.2%	In-line
		Total Exports (Apr) – yoy	-28.3%	-34.3%	-35.7%	Weaker
		Total Imports (Apr) – yoy	-37.9%	-41.2%	-49.5%	Weaker
	<i>Indonesia</i>	BoI Reference Rate	7.25%	7.25%	7.50%	In-line
		Money Supply – M2 (Mar) – yoy	-	20.3%	18.5%	-

INTEREST RATE STRATEGY

Positioning and flow, and the emergence of “green shoots” have frustrated RBNZ Governor Bollard’s attempts to get market interest rates lower. Don’t be discouraged by the rise in rates, as this is not the market expressing a view on future policy.

Market themes...

- > The market is struggling to reconcile the “green shoots” thesis with Dr. Bollard’s promise to keep the OCR at or below the current level.
- > Normally we respect market moves. But this time we’re sceptics, and doubt the RBNZ has changed its view. It may take time for the spirit of the Governor’s message to take hold.
- > March quarter retail sales data could be a tipping point – better data will reinforce the market’s optimistic bias, but a soft reading will play into the Governor’s hands.
- > Borrowers are starting to question the validity of the patience strategy – but we think it remains appropriate. Investors should consider curve trades over outright long strategies.

Review and outlook...

Swap rates have moved significantly higher in the past week, and the long end is actually higher than it was prior to the *OCR Review*. We don’t think this is a case of the market giving Governor Bollard the “cold shoulder”, but rather a reflection of market positioning and flow, not helped by the recent popularity of the “green shoots” thesis. Indeed, the Governor’s message was always going to have more impact if it spurred offshore receivers into action. However, this group of natural investors are conspicuously absent, potentially frightened by the “green shoots” thesis. At the same time, many local players are still likely to be nursing long positions courtesy of the rush to fix that occurred over March and April. As a result, the market has completely lacked any real follow-through, and yields are up a long way, and in some cases are higher than they were before the *OCR Review*. While this is disappointing, we wouldn’t read too much into it. It’s always dangerous to say that the market is wrong, and we’re not saying that. What we are saying is that if you think rising rates is the market saying the Governor is wrong, that’s probably not quite how it really is. Rates are rising because the market still has risk to clear. And while the RBNZ can (and probably will) use every opportunity to reiterate its “*OCR at or below the current level*” message, it will only really get traction over time, and possibly only once the green shoots start to wilt. Of course, some other intervention is possible, but for now we expect jawboning to be the preferred tactic.

Borrowing strategies we favour at present

We don’t believe that rising swap rates is a sign that the market is starting to get worried about the future of RBNZ policy. Just under two weeks ago the RBNZ said the OCR would remain at or below current levels until the second half of 2010. Not only was that statement categorical (as opposed to being conditional on anything, like the inflation outlook), but it is unlikely that anything in the past 10 days has changed the RBNZ’s mind. As such, we think it’s appropriate to stand by and see past rising yields, rather than panic. Option strategies also make sense at times like this.

Gauges for NZ interest rates

Gauge	Direction	Comment
RBNZ / OCR	↓↓	Timing isn’t right, but the spirit is. The higher rates go, the more they’ll fall.
NZ data	↔	HLFS wasn’t as weak as expected. Retail sales this week will be important.
Fed Funds/ front end	↔	FOMC acknowledges early signs of recovery.
RBA	↔/↑	RBA seems comfortable. But downside risks remain.
US 10 year	↔	Treasuries now trending higher, spooked by news.
NZ swap curve	↔/↑	The yield curve needs to steepen, and talk of “green shoots” just exacerbates it.
Flow	↔/↑	The market is completely void of receivers. Patience.
Technicals	↔/↑	Break above pre OCR Review levels unhelpful.

Market expectations for RBNZ OCR (bps)

OCR dates	Last week	This week
Thu 11-Jun-09	-15	-9
Thu 30-Jul-09	-25	-13
Thu 10-Sep-09	-29	-12
Thu 29-Oct-09	-26	-5
Thu 10-Dec-09	-24	-5
Thu 21-Jan-10	-14	+2
Thu 11-Mar-10	-12	+5

Trading themes we favour at present

Bollard’s comments got good traction in the days following the OCR Review, but now seem a distant memory. They’re still relevant, but in a market that’s scared, they won’t gain traction. We over-estimated the market’s ability to constructively heed to the Governor’s message, which has seen our preferred outright trade (long the 1yr OIS) give back gains. However, the curve has steepened significantly, and while we think this is a core trade, it could be time to take a breather.

CURRENCY STRATEGY

The currency market continues to be closely correlated to the equity market of late, as money managers scramble to put cash to work. The loser has been the US Treasury market with yield differentials narrowing in the USD's favour. But the market is intent on punishing those who embark on QE and rewarding those who don't. The euro has exploded north on news that the ECB has no intention of printing money. The USD is firmly on the back foot, which means the NZD is on the front foot. Markets are beginning to trend, but this is very dependent on equities holding gains.

Market themes...

- > Does the US want a lower USD? Technical breakouts of most currencies versus the USD.
- > CRB playing catch up? Huge increase last week.
- > FX markets loving the AUD at present, helping drag the kiwi undeservedly higher.

Review and outlook...

The NZD was turbo-charged last week as improving global sentiment saw risk trades return with a vengeance. This was shown by a rampant equity market (5 percent gain in May so far – what ever happened to “sell in May and go away”?), a near 10 percent gain in the CRB so far this month and the Baltic Dry putting on a 24 percent rise. The key 200-day moving average broke topside first in the AUD at 0.7250, followed by the NZD at 0.5880, and finally but very significantly in the EUR on Friday night at 1.3465. These are all important levels suggest new ranges going forward.

Last week we discussed the CRB and how it had not confirmed the move higher in commodity currencies. Well a 10 percent rally in just over a week suggests that the down side in the NZD is now more limited for the time being. The AUD and CAD also enjoyed a massive rally last week as the world realises inventories have fallen and increased production is required.

Employment data in Australia was impressive and NZ's was not as bad as feared, suggesting to the world we still have the ability to service our debts. We expect this part of the world to continue to benefit from any reserve building and switching out of the USD. Local data going forward this week includes housing market and retail sales, which are expected to show signs of stabilisation (though retail sales volume for the quarter is the wild card).

For all this good news, the FX market is leading the way. Debt, equities and commodities markets have also moved to fully price-in the good (better?)

news. We prefer the NZD to struggle this week but are keen to buy any dips to near 0.5800. We still see the AUD as the most over-valued at current levels and suggest the cross has potential to head towards 0.7950 this week. We see this week as a consolidation week and though we will run short positions from current levels, we will look to turn long on a 2 cent pull back. In simplistic terms, if you print money (i.e. QE) your money is not worth as much. The US is focused on internal issues and a lower USD is in their interest also. Further out, we still think the NZD faces headwinds. But provided equities can hold gains (which we have deep down concerns about, although are respecting the green shoots for now), the kiwi looks set to play in a range for now.

NZD vs AUD: monthly directional gauges		
Gauge	Direction	Comment
Fair value	↔	Top of range. No bad news priced in AUD.
Yield	↓	Yield advantage Australia.
Commodities	↔	Fonterra's revised payout good news for NZ.
Partial indicators	↔/↓	NZ data not as bad as feared, AU's even better.
Technicals	↔	0.7700 to 0.8000 range.
Sentiment	↔	Risk appetites back.
Other	↔	Is the FX market getting too far ahead of itself?
On balance	↔	Market happy at current levels.

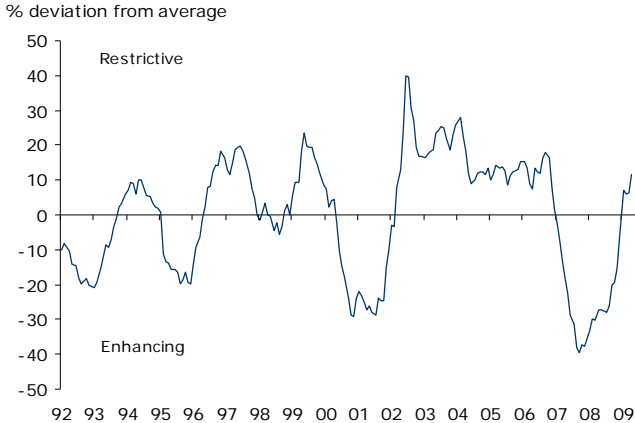
NZD vs USD: monthly directional gauges		
Gauge	Direction	Comment
Fair value – long-term	↔	At long term average.
Fair value – short-term	↔	Near cyclical fair value estimates.
Yield	↔/↓	Consolidating at narrow levels.
Commodities	↑	CRB monster week.
Risk aversion	↑	Risk back on the table.
Partial indicators	↔	Stabilisation occurring.
Technicals	↔/↑	Break of 200-day MA bullish sign.
AUD	↑	AUD on a rampage.
Sentiment	↑	Bullish but undeserved.
Other	↔	US stress test gives market confidence.
On balance	↔	0.58 cent key level.

EFFECTIVE EXCHANGE RATES UPDATE

We present an update of our real effective exchange rate measures across New Zealand's main export industries. The measures take into account the world prices of our exports (commodity prices in the case of commodity exporters), adjusted for currency movements based on their main destinations.

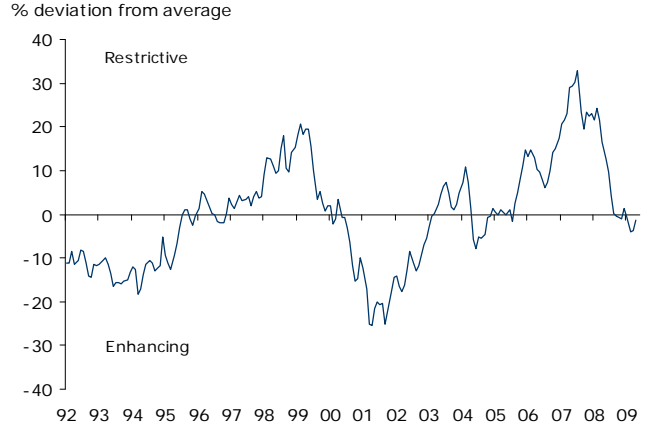
As was the case in March, all the commodity adjusted real exchange rates we monitor became more restrictive in April. A higher NZD (against all our major trading partners) over the month more than offset gains in world commodity prices. Large moves were recorded for the forestry and crude sectors, where the stronger NZD/JPY had a big influence. Conditions for both sectors remain well in "restrictive" territory. The higher NZD has also seen conditions in the horticulture, seafood, and services industries deteriorate, although their effective exchange rates still remain at "enhancing" levels.

Sector: Dairy ≈ 18% of exports



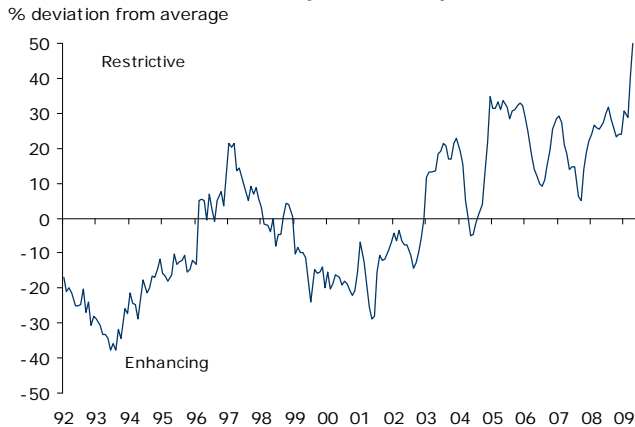
Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Meat ≈ 8% of exports



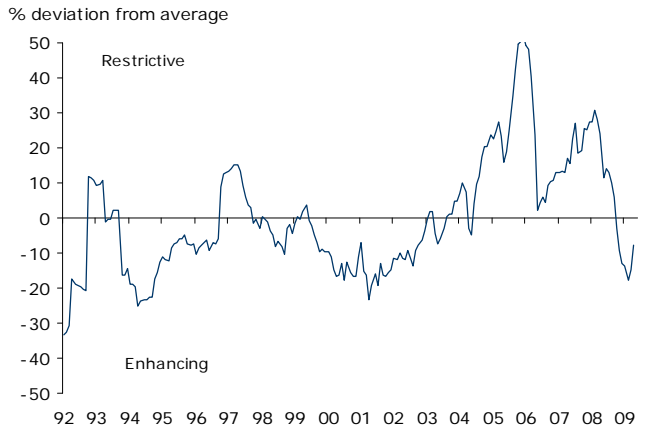
Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Forestry ≈ 10% of exports



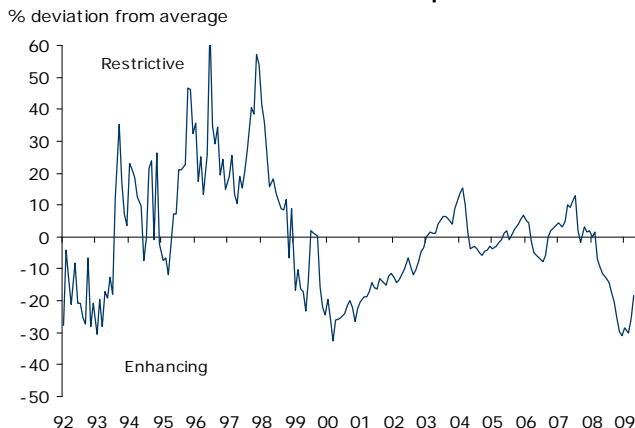
Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Horticulture ≈ 4% of exports



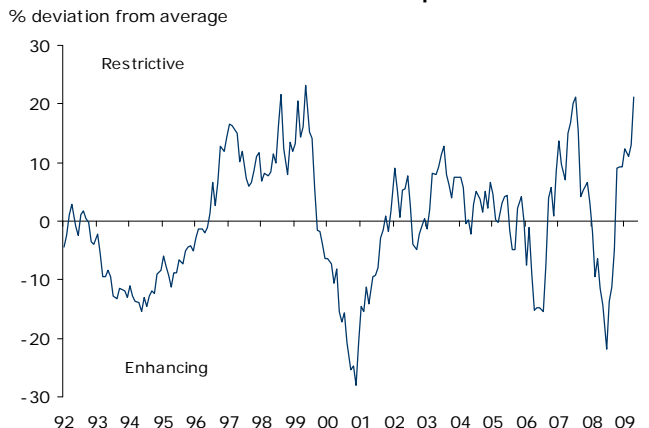
Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Seafood ≈ 3% of exports



Sources: ANZ National, Bloomberg, Statistics NZ

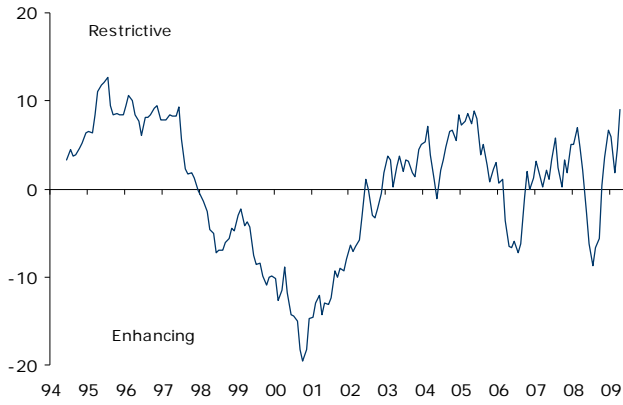
Sector: Crude ≈ 5% of exports



Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Manufacturing \approx 20% of exports

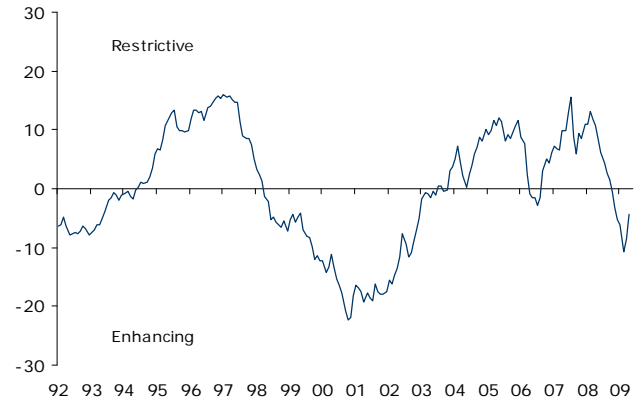
% deviation from average



Sources: ANZ National, Bloomberg, Statistics NZ

Sector: Services \approx 24% of exports

% deviation from average



Sources: ANZ National, Bloomberg, Statistics NZ

DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
11-May	NZ	Electronic Card Spending (Apr) - mom	-	0.3	10:45
	AU	NAB Business Confidence (Apr)	-	-13	13:30
		NAB Business Conditions (Apr)	-	-17	13:30
12-May	US	Bernanke Speaks on Financial Crises at Jekyll Island, Georgia	-	-	10:30
	NZ	Food Prices (Apr) - mom	-	0.5%	10:45
	UK	RICS House Price Balance (Apr)	-70.0%	-73.1%	11:01
		DCLG UK House Prices (Mar) - yoy	-13.0%	-12.3%	20:30
		Total Trade Balance (Mar)	-£3000M	-£3248M	20:30
		Industrial Production (Mar) - mom	-0.9%	-1.0%	20:30
	JN	Official Reserve Assets (Apr)	-	\$1018.5B	11:50
		Leading Index CI (Mar P)	77.0	75.0	17:00
		Coincident Index CI (Mar P)	85.8	86.0	17:00
	AU	Home Loans (Mar)	4.5%	0.4%	13:30
		Investment Lending (Mar)	-	-2.8%	13:30
		Value of Loans (Mar) - mom	-	2.7%	13:30
		Commonwealth Budget	-	-	21:30
	GE	Consumer Price Index (Apr F) - mom	0.0%	-0.1%	18:00
13-May	NZ	Fonterra Announces Outcome of Monthly Milk Powder Auction	-	-	-
		RBNZ Financial Stability Report	-	-	09:00
	US	Fed's Lockhart to Give Welcome and Open Financial Markets Conference	-	-	00:20
		Trade Balance (Mar)	-\$29.0B	-\$26.0B	00:30
		Fed's Rosengren to Speak on Risk Management at Jekyll Island Panel	-	-	00:30
		Monthly Budget Statement (Apr)	-\$20.0B	\$159.3B	06:00
	EC	ECB's Tumpel-Gugerell Speaks in Brussels	-	-	00:30
		Industrial Production ((Mar) - mom	-1.0%	-2.3%	21:00
	UK	NIESR GDP Estimate (Apr)	-	-1.5%	11:01
		Claimant Count Rate (Apr)	4.7%	4.5%	20:30
		Jobless Claims Change (Apr)	85.0K	73.7K	20:30
		Average Earnings inc bonus (Mar) - 3m/yoy	-1.0%	0.1%	20:30
		ILO Unemployment Rate (3mths) (Mar)	6.9%	6.7%	20:30
		BoE Releases Quarterly Inflation Report	-	-	21:30
	JN	Adjusted Current Account (Mar)	¥513.5B	¥673.4B	11:50
		Money Stock M3 (Apr) - yoy	1.4%	1.3%	11:50
		Eco Watchers Survey: Current (Apr)	30.0	28.4	17:00
		Eco Watchers Survey: Outlook (Apr)	-	35.8	17:00
	AU	Westpac Consumer Confidence (May)	-	8.3%	12:30
14-May	US	Import Price Index (Apr) - mom	0.5%	0.5%	00:30

Continued over page

Date	Country	Data/Event	Mkt.	Last	Time (NZST)
14-May cont.	US	Advance Retail Sales (Apr) - mom	0.0%	-1.2%	00:30
		Retail Sales Less Autos (Apr) - mom	0.2%	-1.0%	00:30
		Business Inventories (Mar)	-1.1%	-1.3%	02:00
		Fed's Lockhart to Make Closing Remarks at Financial Markets Meeting	-	-	04:00
	NZ	Business NZ Publishes Performance of Manufacturing Index	-	-	10:30
		Non Resident Bond Holdings (Apr)	-	73.2%	15:00
	AU	Consumer Inflation Expectation (May)	-	2.4%	13:00
	EC	ECB Publishes May Monthly Report	-	-	20:00
		ECB's Papademos Speaks at Conference in Vienna	-	-	20:00
15-May	US	Producer Price Index (Apr) - mom	0.1%	-1.2%	00:30
		PPI Ex Food & Energy (Apr) - mom	0.1%	0.0%	00:30
		Initial Jobless Claims (w/e May-10)	610K	601K	00:30
		Continuing Claims (w/e May-3)	6400K	6351K	00:30
	EC	ECB's Gonzalez-Paramo Speaks at University of Sevilla, Spain	-	-	03:30
		ECB's Stark Speaks at Conference in Berlin	-	-	04:20
		CPI (Apr) - mom	0.4%	0.4%	21:00
		GDP (1Q A) - qoq	-2.0%	-1.6%	21:00
	NZ	Retail Sales (Mar) - mom	-	0.2%	10:45
		Retail Sales Ex-Auto (Mar) - mom	-	-0.1%	10:45
		Retail Sales Ex Inflation (1Q) - qoq	-	-0.6%	10:45
	JN	Machine Orders (Mar) - mom	-4.7%	1.4%	11:50
		Domestic CGPI (Apr) - mom	0.1%	-0.2%	11:50
	GE	GDP (1Q P) - qoq	-3.0%	-2.1%	18:00
16-May	US	Consumer Price Index (Apr) - mom	0.0%	-0.1%	00:30
		CPI Ex Food & Energy (Apr) - mom	0.1%	0.2%	00:30
		Empire Manufacturing (May)	-12.0	-14.65	00:30
		Net Long-term TIC Flows (Mar)	\$30.0B	\$22.0B	01:00
		Industrial Production (Apr)	-0.6%	-1.5%	01:15
		Capacity Utilization (Apr)	68.8%	69.3%	01:15
		Fed's Fisher Speaks at Texas Bankers Association Conference	-	-	01:15
		University of Michigan Confidence (May P)	66.5	65.1	02:00

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

NEW ZEALAND DATA WATCH

Key focus over the next four weeks: Further signs of stabilisation is likely to be the theme for upcoming data. While encouraging, stabilisation doesn't necessarily mean recovery, and conditions are likely to remain challenging for some time yet. The *Budget* in a few weeks' time looks likely to contain some tough choices.

Date	Data/Event	Economic Signal	Comment
circa 11 May	REINZ House Sales (Apr)	Further signs of stabilisation	The data is likely to confirm the anecdotes, with further improvement seen in house sales.
Wed 13 May (09.00)	RBNZ Financial Stability Report (May)	No systemic risks	The RBNZ will emphasise the strength of NZ's financial system, although within the context of major economic challenges.
Fri 15 May (10.45)	Retail Sales (Mar)	Signs of stabilisation in monthly numbers	Total nominal headline sales are expected to rise by 0.5 percent in the month, with core spending also rising 0.5 percent. However, for the quarter, real spending is expected to tumble 1.7 percent.
Mon 18 May (10.45)	Producer Price Index (Mar qtr)	Slight improvement in margins	Lower oil and wholesale electricity prices are expected to see input prices fall slightly in the quarter. Output prices should hold relatively steady.
Thu 21 May (10.45)	International Travel and Migration (Apr)	Net inflow	Less NZer's choosing to leave will see net migration remain positive. Visitor arrivals will head lower again.
Tue 26 May (10.45)	Overseas Merchandise Trade (Apr)	Rebalancing continues	Another monthly trade surplus is expected as the domestic economy continues to de-leverage.
Wed 27 May (15.00)	NBNZ <i>Business Outlook</i> (May)	-	-
Thu 28 May (14.00)	<i>Budget Economic and Fiscal Update</i>	Ugly	The <i>Budget</i> should show a further sharp deterioration in the medium-term fiscal projections. Bigger deficits, more debt and larger bond tenders.
Thu 28 May (15.00)	Credit Growth (Apr)	De-leveraging	Household credit growth will remain subdued as de-leveraging continues. Business and rural lending is also likely to continue to show signs of moderation.
Fri 29 May (10.45)	Building Consents Issued (Apr)	Stabilising	The recent pick-up in house sales should see building consent issuance recover off its lows. Commercial consents though, will head lower.
Wed 3 Jun (10.00)	Financial Statements of the Government (10 months to April)	Further into the red	Lower tax revenue is expected to see the Government's underlying accounts head further into the red. Better returns in the month from Crown Financial Institutions will help stop the headline operating balance from deteriorating further.
Thu 4 Jun (15.00)	ANZ Commodity Price Index (May)	-	-
Tue 9 Jun (10.45)	Value of Building Work Put in Place (Mar qtr)	Still contracting	Residential building construction is likely to record another large quarterly contraction. Non-residential construction is expected to be largely unchanged.
Wed 10 Jun (10.45)	Overseas Trade Indexes (Mar qtr)	Terms of trade lower	Large falls in export commodity prices is expected to see the terms of trade fall in the quarter. Volume data is expected to confirm net exports will make a positive contribution to growth in the March quarter.
Thu 11 Jun (09.00)	RBNZ June <i>Monetary Policy Statement</i>	Temporary pause	While a case can be made for further immediate rate cuts, the green shoots need to be respected. However, we don't expect them to be sustained and hence rate cuts are likely to resume from H2 2009.
Fri 11 Jun (10.45)	Retail Trade Survey (Apr)	Finding a base	Second lot of tax cuts should give retail sales a bit of a kick.
On Balance		Base forming?	There is a strong base effect appearing in some data, which suggests Q2 is the nadir in the cycle. But the jury is out on the speed of recovery.

SUMMARY OF KEY ECONOMIC FORECASTS

	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
GDP (% qoq)	-0.3	-0.2	-0.5	-0.9	-1.5	-0.5	0.0	0.1	0.5	1.2
GDP (% yoy)	2.1	1.0	-0.1	-1.9	-3.1	-3.3	-2.9	-1.9	0.1	1.8
CPI (% qoq)	0.7	1.6	1.5	-0.5	0.3	0.7	0.6	0.6	0.5	0.5
CPI (% yoy)	3.4	4.0	5.1	3.4	3.0	2.1	1.1	2.2	2.4	2.2
Employment (% qoq)	-1.0	1.2	0.2	0.6	-1.1	-1.0	-0.9	-0.4	-0.2	0.0
Employment (% yoy)	-0.2	0.8	1.1	0.9	0.8	-1.3	-2.4	-3.4	-2.5	-1.5
Unemployment Rate (% sa)	3.8	4.0	4.3	4.7	5.0	5.6	6.4	7.0	7.5	7.7
Current Account (% GDP)	-8.0	-8.4	-8.7	-8.9	-8.6	-7.3	-6.5	-5.8	-6.0	-6.3
Terms of Trade (% qoq)	4.2	-0.4	-1.0	-0.9	-3.0	-3.1	-3.0	-2.3	-1.5	-1.0
Terms of Trade (% yoy)	11.6	10.7	5.8	1.8	-5.2	-7.8	-9.7	-10.9	-9.5	-7.5

KEY ECONOMIC INDICATORS

	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08	Dec-08	Jan-09	Feb-09	Mar-09	Apr-09
Retail Sales (% mom)	-0.7	0.3	0.3	-1.3	0.0	-0.6	-1.2	0.2
Retail Sales (% yoy)	2.5	-0.9	2.2	0.7	-4.1	-0.9	-3.7	-6.9
Credit Card Billings (% mom)	0.0	-0.3	1.2	-1.8	-0.9	-2.1	1.4	0.6	-3.1	..
Credit Card Billings (% yoy)	4.0	2.5	2.5	1.0	-1.0	-3.8	-2.4	-2.0	-5.0	..
Car Registrations (% mom)	-7.2	-3.7	11.1	-1.0	-19.7	12.7	-14.1	-15.1	7.3	-3.0
Car Registrations (% yoy)	-27.1	-30.5	-15.6	-19.9	-34.4	-23.7	-36.5	-44.6	-32.9	-41.0
Building Consents (% mom)	-1.2	-6.9	8.1	-19.4	3.8	-7.0	-12.9	11.6	-4.6	..
Building Consents (% yoy)	-34.4	-43.2	-28.4	-42.8	-39.7	-41.4	-51.7	-40.0	-34.5	..
REINZ House Price (% yoy)	-1.4	-5.7	-6.1	-4.3	-4.1	-4.8	-4.4	-2.2	-4.0	..
Household Lending Growth (% mom)	0.3	0.4	0.2	0.2	-0.1	0.2	0.2	0.2	0.1	..
Household Lending Growth (% yoy)	7.7	7.2	6.6	5.8	4.8	4.2	3.8	3.1	2.8	..
Roy Morgan Consumer Confidence	83.9	91.4	108.6	99.7	99.0	102.9	103.7	98.8	94.7	101.1
NBNZ Business Confidence	-43.2	-20.5	1.6	-42.3	-43.0	-35.0	..	-41.2	-39.3	-14.5
NBNZ Own Activity Outlook	-8.2	4.7	16.7	-11.4	-14.1	-21.5	..	-20.1	-21.2	-3.8
Trade Balance (\$m)	-797	-848	-1252	-994	-594	-341	-103	487	324	..
Trade Balance (\$m annual)	-4468	-4369	-5048	-5269	-5234	-5614	-5406	-5162	-4796	..
ANZ World Commodity Price Index (% mom)	1.8	-3.4	-5.1	-7.6	-7.4	-7.4	-4.3	-4.6	1.0	2.5
ANZ World Commodity Price Index (% yoy)	8.7	3.5	-2.1	-11.1	-18.3	-24.3	-26.5	-30.7	-31.4	-29.5
Net Migration (sa)	750	330	-40	20	-300	320	810	1600	1720	..
Net Migration (annual)	5201	4938	4403	4329	3569	3814	4538	6160	7482	..

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

SUMMARY OF KEY MARKET FORECASTS

NZ FX rates	Actual		Current	Forecast (end month)						
	Mar-09	Apr-09	11-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
NZD/USD	0.530	0.572	0.604	0.540	0.510	0.480	0.470	0.470	0.480	0.490
NZD/AUD	0.797	0.801	0.783	0.771	0.767	0.762	0.756	0.764	0.774	0.778
NZD/EUR	0.406	0.433	0.442	0.422	0.408	0.400	0.404	0.420	0.429	0.434
NZD/JPY	51.8	56.6	59.6	54.0	50.5	47.0	45.6	46.5	48.0	50.0
NZD/GBP	0.373	0.389	0.396	0.372	0.357	0.338	0.327	0.324	0.327	0.329
NZ\$ TWI	53.8	57.0	58.5	54.6	52.4	50.4	49.8	50.6	51.6	52.4
NZ interest rates	Mar-09	Apr-09	11-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
OCR	3.43	3.24	2.50	2.50	2.25	2.00	2.00	2.00	2.50	3.50
90 day bill	3.24	3.12	2.88	2.90	2.40	2.40	2.40	2.40	3.10	4.10
10 year bond	4.78	5.24	5.70	5.40	5.10	4.90	5.00	5.10	6.00	6.10
International	Mar-09	Apr-09	11-May-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10	Sep-10	Dec-10
US Fed funds	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00	1.50	2.00
US 3-mth	1.19	1.02	0.94	0.90	0.70	0.50	0.70	1.25	1.75	2.25
AU cash	3.25	3.00	3.00	3.00	2.50	2.00	2.00	2.00	2.00	2.75
AU 3-mth	3.14	3.08	3.16	3.20	2.30	2.30	2.30	2.40	2.60	3.30

KEY RATES

	8 Apr	4 May	5 May	6 May	7 May	8 May
Official Cash Rate	3.00	2.50	2.50	2.50	2.50	2.50
90 day bank bill	3.23	2.81	2.78	2.83	2.90	2.88
NZGB 07/09	3.01	2.70	2.80	2.79	2.83	2.83
NZGB 11/11	3.93	3.50	3.59	3.62	3.70	3.70
NZGB 04/13	4.52	4.28	4.37	4.40	4.55	4.56
NZGB 12/17	5.35	5.33	5.49	5.53	5.67	5.67
2 year swap	3.92	3.37	3.43	3.47	3.57	3.58
5 year swap	5.09	4.61	4.71	4.75	4.85	4.88
RBNZ TWI	57.3	56.7	56.7	56.9	57.6	58.1
NZD/USD	0.5738	0.5741	0.5761	0.5775	0.5870	0.5926
NZD/AUD	0.8101	0.7807	0.7795	0.7845	0.7807	0.7869
NZD/JPY	57.47	57.09	56.83	56.62	57.81	58.73
NZD/GBP	0.3902	0.3840	0.3840	0.3849	0.3881	0.3949
NZD/EUR	0.4344	0.4308	0.4306	0.4356	0.4415	0.4431
AUD/USD	0.7083	0.7354	0.7391	0.7361	0.7519	0.7531
EUR/USD	1.3208	1.3326	1.3379	1.3258	1.3295	1.3374
USD/JPY	100.16	99.45	98.65	98.05	98.49	99.10
GBP/USD	1.4707	1.4951	1.5004	1.5002	1.5126	1.5008
Oil	49.37	52.18	54.45	56.29	56.29	56.67
Gold	880.50	892.45	904.75	911.30	912.10	914.95
Electricity (Haywards)	4.95	6.96	3.42	13.27	9.71	4.61
Milk futures (US\$/contract)	86	86	86	86	85	85
Baltic Dry Freight Index	1463	n/a	1897	2065	2194	2214

NEW ZEALAND DISCLOSURE INFORMATION

The Bank (in respect of itself and its principal officers) makes the following investment adviser disclosure to you pursuant to section 41A of the Securities Markets Act 1988.

The Bank (in respect of itself and its principal officers) makes the following investment broker disclosure to you pursuant to section 41G of the Securities Markets Act 1988.

Qualifications, experience and professional standing

Experience

The Bank is a registered bank and, through its staff, is experienced in providing investment advice about its own securities and, where applicable, the securities of other issuers. The Bank has been selling securities, and providing investment advice on those securities, to customers as a core part of its business for many years, drawing on the extensive research undertaken by the Bank and its related companies and the skills of specialised staff employed by the Bank. The Bank is represented on many bank, finance and investment related organisations and keeps abreast of relevant issues by running seminars and workshops for relevant staff and having its investment adviser staff attend external seminars where appropriate. The Bank subscribes to relevant industry publications and, where appropriate, its investment advisers will monitor the financial markets.

Relevant professional body

The Bank is a member of the following professional bodies relevant to the provision of investment advice:

- New Zealand Bankers Association;
- Associate Member of Investment Savings & Insurance Association of NZ;
- Financial Markets Operations Association; and
- Institute of Finance Professionals.

Professional indemnity insurance

The Bank (and its subsidiaries), through its ultimate parent company Australia and New Zealand Banking Group Limited, has professional indemnity insurance which covers its activities including those of investment advisers it employs.

This insurance covers issues (including 'prior acts') arising from staff fraud, electronic crime, documentary fraud and physical loss of property. The scope of the insurance also extends to third party civil claims, including those for negligence. The level of cover is of an amount commensurate with the size and scale of the Bank.

The insurer is ANZcover Insurance Pty Limited.

Dispute resolution facilities

The Bank has a process in place for resolving disputes. Should a problem arise, you can contact any branch of the Bank for more information on the Bank's procedures or refer to any of the Bank's websites.

Unresolved complaints may ultimately be referred to the Banking Ombudsman, whose contact address is PO Box 10-573, Wellington.

Criminal convictions

In the five years before the relevant investment advice is given none of the Bank (in its capacity as an investment adviser and where applicable an investment broker) or any principal officer of the Bank has been:

- Convicted of an offence under the Securities Markets Act 1988, or the Securities Act 1978 or of a crime involving dishonesty (as defined in section 2(1) of the Crimes Act 1961);
- A principal officer of a body corporate when that body corporate committed any of the offences or crimes involving dishonesty as described above;
- Adjudicated bankrupt;
- Prohibited by an Act or by a court from taking part in the management of a company or a business;

- Subject of an adverse finding by a court in any proceeding that has been taken against them in their professional capacity;
- Expelled from or has been prohibited from being a member of a professional body; or
- Placed in statutory management or receivership.

Fees

At the time of providing this disclosure statement it is not practicable to provide accurate disclosure of the fees payable for all securities that may be advised on. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

Other interests and relationships

When a security is sold by the Bank, the Bank may receive a commission, either from the issuer of a security or from an associated person of the Bank. Whether that commission is received and, if received, its value depends on the security sold. At the time of providing this disclosure statement it is not practicable to provide a detailed list of each security that may be advised on, the name of the issuer of that security and the rate of the commission received by the Bank. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

In addition to the interest that the Bank has in products of which it is the issuer, the Bank, or an associated person of the Bank, has the following interests or relationships that a reasonable person would find reasonably likely to influence the Bank in providing the investment advice on the securities listed below:

- ANZ Investment Services (New Zealand) Limited (ANZIS), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. ANZIS may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- UDC Finance Limited (UDC), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. UDC may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- The Bank has a joint venture relationship with ING (NZ) Holdings Limited (ING). ING and its related companies may receive remuneration from a third party relating to a security sold by the Investment Adviser.

Securities about which investment advice is given

The Bank provides investment advice on the following types of securities:

- Debt securities including term and call deposits, government stock, local authority stock, State-Owned Enterprise bonds, Kiwi bonds and corporate bonds and notes;
- Equity securities such as listed and unlisted shares;
- New Zealand and overseas unit trusts;
- Share in a limited partnership;
- Superannuation schemes and bonds;
- Group investment funds;
- Life insurance products;
- Derivative products including interest rate and currency forward rate contracts and options; and
- Other forms of security, such as participatory securities.

PROCEDURES FOR DEALING WITH INVESTMENT MONEY OR INVESTMENT PROPERTY

If you wish to pay investment money to the Bank you can do this in several ways such as by:

- Providing cash;
- Providing a cheque payable to the relevant product or service provider and crossed 'not transferable'; or
- Making an automatic payment or payment through another electronic delivery mechanism operated by the Bank.

Investment property (other than money) may be delivered to the Bank by lodging the relevant property (for example, share certificates) with any branch of the Bank offering a safe custody service, or by posting (using registered post) the documents or other property to a branch of the Bank, identifying your name, account number and investment purpose.

Any investment money lodged with the Bank for the purchase of securities offered by the Bank, its subsidiaries or any third parties will be deposited in accordance with your instructions, to your nominated account or investment. Such money will be held by the Bank according to usual banking terms and conditions applying to that account or the particular terms and conditions relating to the investment and will not be held by the Bank on trust unless explicitly accepted by the Bank on those terms. Any investment money or property accepted by the Bank on trust will be so held until disbursed in accordance with your instructions. Any investment property lodged with the Bank will be held by the Bank as bailee according to the Bank's standard terms and conditions for holding your property.

Record Keeping

The Bank will keep adequate records of the deposit of investment moneys or property and all withdrawals and dealings with such money or property, using the account/investment number allocated to your investment. You may have access to those records upon request.

Auditing

The Bank's systems and operations are internally audited on a regular basis. The financial statements of the Bank and its subsidiaries are audited annually by KPMG. However, this does not involve an external audit of the receipt, holding and disbursement of the money and other property.

Use of Money and Property

Money or property held by the Bank for a specific purpose communicated to the Bank (e.g. the purchase of an interest in a security) may not be used by the Bank for its own purposes and will be applied for your stated purpose. No member of the Bank's staff may use any money or property deposited with the Bank, for their own purposes or for the benefit of any other person. In the absence of such instructions, money deposited with the Bank may be used by the Bank for its own purposes, provided it repays the money to you upon demand (or where applicable, on maturity), together with interest, where payable.

NEW ZEALAND DISCLAIMER

The Bank does not provide investment advice tailored to an investor's personal circumstances. It is the investor's responsibility to understand the nature of the security subscribed for, and the risks associated with that security. To the maximum extent permitted by law, the Bank excludes liability for, and shall not be responsible for, any loss suffered by the investor resulting from the Bank's investment advice.

Each security (including the principal, interest or other returns of any security) the subject of investment advice given to the investor by the Bank or otherwise, is not guaranteed, secured or underwritten in any way by the Bank or any associated or related party except to the extent expressly agreed in the terms of the relevant security.

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