

# NEW ZEALAND ECONOMICS ANZ PROPERTY FOCUS

OCTOBER 2010

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## MESSAGE IN A BOTTLE

### SUMMARY

Our monthly *Property Focus* publication is aimed at providing an independent appraisal of recent developments in the property market. This month we include our latest forecasts for the NZ economy and look at the impact of the earthquake on house sales in Canterbury.

### THE MONTH IN REVIEW

The housing market remains weak, with sales and average selling prices dropping further in September. Add to this a slowing in net migration and the outlook isn't that great. We're expecting a pickup in 2011 to be our oasis in the desert.

### PROPERTY GAUGES

Last month's earthquake has dented a housing market that was already struggling in a deleveraging environment and a slow down in net inward migration. Overall, housing market activity is lost at sea and struggling to keep its head above water. Will next year be the uncharted island that will save it?

### ECONOMIC COMMENTARY – BUILDING A BASE FOR A BETTER 2011

The economic recovery is ongoing, but extremely patchy. We expect a substantive recovery to emerge in 2011 as the process of balance sheet repair nears an end, earthquake reconstruction work continues, the labour market recovery strengthens, higher rural incomes filter through, and benefits of the global recovery flow-through into export incomes. However, this outlook remains contingent on the projected global recovery eventuating. The five year picture is one of modest growth, reflecting a sustained period of structural change across NZ.

### MORTGAGE BORROWING STRATEGY

Mortgage rates have held steady over the past month, with fixed rates having already been cut earlier in September and the OCR having been left on hold at 3 percent at the RBNZ's last *Monetary Policy Statement*. Looking ahead, we expect mortgage rates to be fairly stable. Floating rates are likely to be unchanged as long as the RBNZ remain on hold, and at this stage we expect that to be until March 2011. However fixed rates are at the mercy of global interest rates.

### FEATURE ARTICLE – CANTERBURY PROPERTY SALES: SHAKEN AND STIRRED

The REINZ has recently published the first snapshot of Canterbury's real estate market following the devastating earthquake in early September. Not surprisingly, the number of homes sold has fallen in all of the affected localities reported in Canterbury. However, the average selling price, for the properties that did transact were mixed, with some areas reporting a strengthening over the month.

# THE MONTH IN REVIEW

## SUMMARY

The housing market remains weak, with sales and average selling prices dropping further in September. Add to this a slowing in net migration and the outlook isn't that great. We're expecting a pickup in 2011, as the economy gains some momentum, to be our oasis in the desert.

## SNZ BUILDING CONSENTS – AUGUST

**August dwelling consent numbers were weak**, with consent issuance for July revised lower to boot. Smoothing through some of the monthly volatility, the three month average number of new dwelling consents in August were 5.7 percent lower compared to the previous three months. On an ex-apartment basis the fall was larger (down 9.0 percent compared to three months earlier). The floor area of residential consents (which is a better indicator for the residential investment component of GDP) fell by 8.7 percent in August, with the floor area in the three months to August now 12 percent down on the previous three months. In the three months to August the seasonally adjusted value of residential issuance was broadly unchanged on the previous 3 months. Consents on alterations and additions firmed by 4.9 percent, whereas the value of consents for new dwellings fell by 1.6 percent.

Six months on a leaky boat, lucky just to keep afloat.

## REINZ HOUSING DATA – SEPTEMBER

**House sales dropped 6.7 percent in September, with the Canterbury earthquake exacerbating the decline.** Excluding Canterbury the number of house sales decreased 3.2 percent from August. The September fall follows a number of subdued months, with sales volumes 19 percent below April levels. Prices fell 0.8 percent in seasonally adjusted terms in September. The volatility in prices may partly be a consequence of the low volume of sales and earthquake related disruptions. **The median days to sell ticked up to 45 days.** Earthquake related disruptions and low sales volumes caution against putting too much weight on this. We estimate that the seasonally adjusted median days to sell for properties outside the Canterbury/Westland region was unchanged at 47 days. The tone remains one of housing market weakness with median days to sell considerably above the mid 30s range that was apparent at the end of last year and at the start of 2010. This is likely to continue to provide further downward pressure on house prices.

A Titanic sized drop in the number of house sales.

## NET MIGRATION – AUGUST

Permanent and long-term (PLT) arrivals were broadly unchanged, increasing by just 0.1 percent for the month, whereas departures increased by 0.8 percent.

**Annualised net PLT immigration has eased** from just over 21,000 persons in the three months to January to just under 8,000 persons in the three months to August. A strong upward trend in departures to Australia is evident with PLT departures in the 3-months to August up 7.4 percent. This remains a key risk to continuing positive net immigration inflows.

The crew of the SS Minnow have washed up on Gillard's Island.

## ASSESSMENT

The low number of house sales suggests there is not a lot of optimism currently in the housing market. The slowing in the economy over the last few months is likely to instil greater caution by buyers. Although fixed-term mortgage rates have fallen considerably since the start of the year, this does not appear to have an appreciable impact on the housing market as yet, with variable rate mortgages still the best game in town but this may be changing (*refer to our analysis on page 10*). The RBNZ expects to remain on the sidelines until early 2011 and support from net immigration may soon wane, given that departures to Australia are on the rise.

Navigating through choppy water.

## PROPERTY GAUGES

Last month's earthquake has dented a housing market that was already struggling in a deleveraging environment and a slow down in net inward migration. Overall, housing market activity is lost at sea and struggling to keep its head above water. Will next year be the uncharted island that will save it?

We use ten gauges to assess the state of the property market, and for signs that changes are emerging.

**AFFORDABILITY.** For new entrants into the housing market, we measure affordability using the ratio of house prices-to-income (adjusted for interest rates), and mortgage payments as a proportion of income.

**SERVICEABILITY / INDEBTEDNESS.** For existing homeowners, serviceability relates interest payments to income, while indebtedness is measured as the level of debt relative to income.

**INTEREST RATES.** Interest rates affect both the affordability of new houses and the serviceability of existing mortgage payments.

**MIGRATION.** A key source of demand for new housing.

**SUPPLY-DEMAND BALANCE.** We use dwelling consents issuance to proxy supply. Demand is derived via the natural growth rate in the population, net migration, and the average household size.

**CONSENTS AND HOUSE SALES.** These are both key gauges of activity in the property market.

**LIQUIDITY.** We look at growth in Private Sector Credit relative to GDP to assess the availability of credit in supporting the property market.

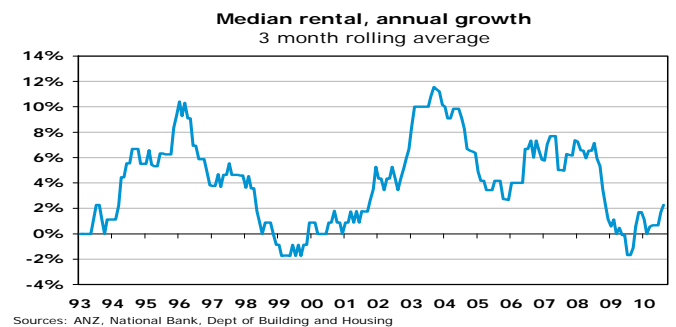
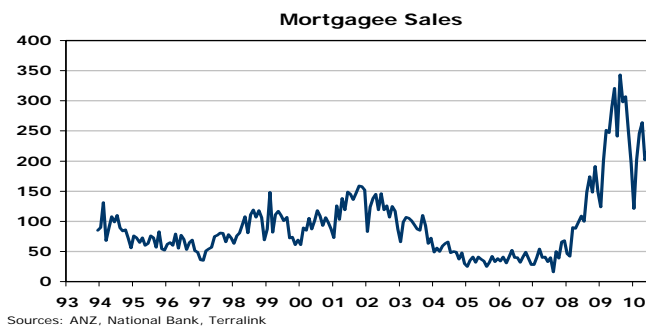
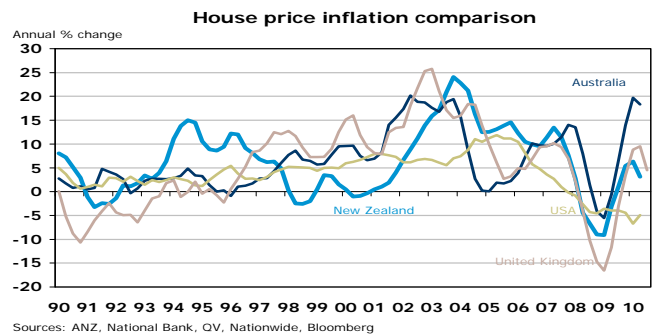
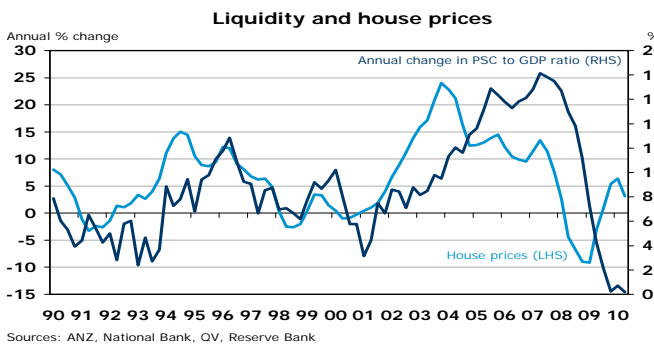
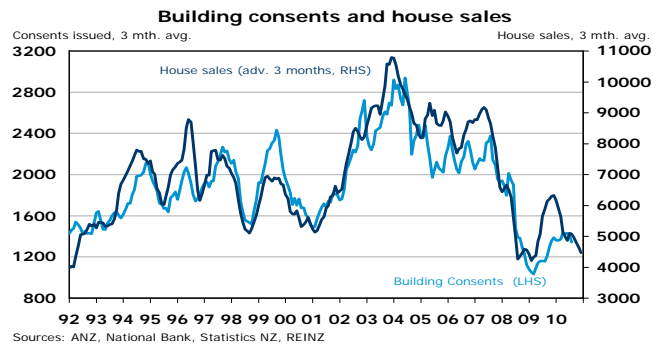
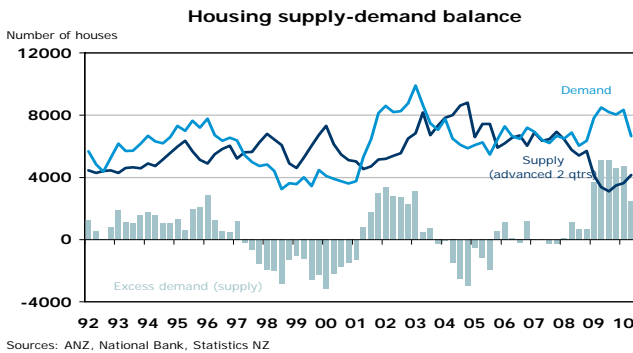
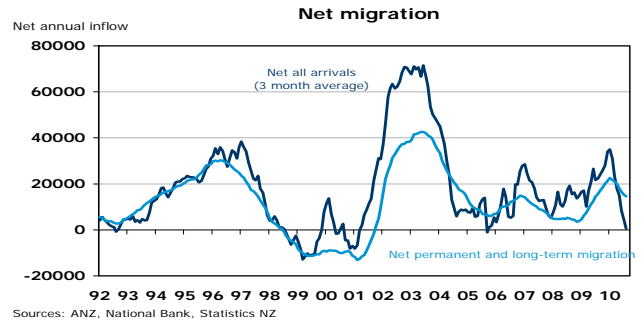
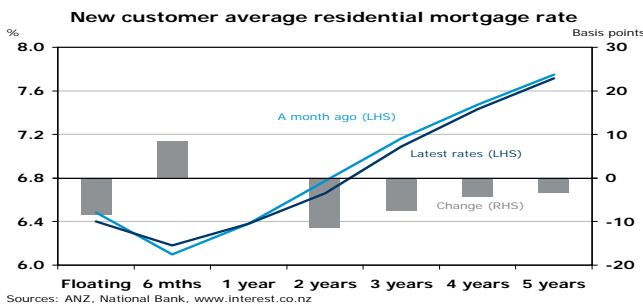
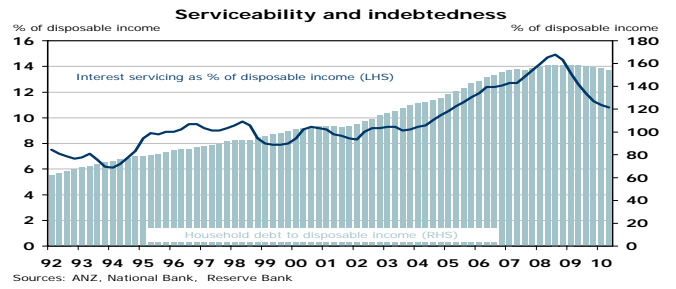
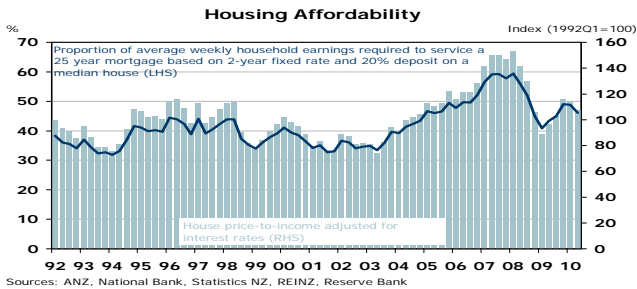
**GLOBALISATION.** We look at relative property price movements between New Zealand, the US, UK and Australia in recognition of the important role that globalisation is playing in NZ's property cycle.

**MORTGAGEE SALES.** We look at how mortgagee sales are tracking for an indication of distress in the property market.

**RENTAL GROWTH.** We look at growth in the median market rent as an indication of whether it is a better time to buy versus rent, and how rental yields are shaping up for the property investor.

Indicator	Level	Direction for prices	Comment
Affordability	Improving	↔/↓	Affordability is the best it's been in 12 months.
Serviceability / indebtedness	Deleveraging	↓	Interest servicing has eased to a five-year low.
Interest rates	Lower	↔	Excluding the 6 month maturity, the curve was lower than last month.
Migration	Constrained	↔	Net <i>Permanent &amp; Long-Term</i> migration is down to its lowest annual total for a year and the <i>All Visitors</i> figure has just only remained on the positive side of the ledger.
Supply-demand balance	Closing the gap	↔/↑	Still wide but the gap is the narrowest for 18 months.
Consents and house sales	Lack of action	↔/↑	Drifting down.
Liquidity	Stall speed	↓	As a ratio to GDP, credit has all but stalled.
Globalisation	Turned the corner	↔	House price growth in Australia slowed to only (!) 18.4 percent — four times New Zealand's rate of growth.
Mortgagee sales	Lifting	↔	Lifted in July and remains elevated.
Median rent	Gaining momentum	↔	Strongest rate of increase since December 2008.
<b>On balance</b>		↔/↓	<b>Feeling the effects of the quake and fewer migrants.</b>

# PROPERTY GAUGES



## ECONOMIC COMMENT: BUILDING A BASE FOR A BETTER 2011

This month we replace our normal one page snapshot on the economy with a more expansive economic assessment, based on our latest quarterly economic forecasts.

The economic recovery is ongoing, but extremely patchy. Deleveraging remains pervasive as households, farmers and businesses concentrate on improving their balance sheets. We still expect a substantive recovery to emerge in 2011 as the process of balance sheet repair nears an end, earthquake reconstruction work gets underway, the labour market recovery strengthens, higher rural incomes eventually filter through, and benefits of the global recovery flow-through into export incomes. However, this outlook remains contingent on the projected global recovery eventuating. Within the spirit of a strong 2011, the five year picture is one of modest growth, which in part reflects a sustained period of structural change across the economy.

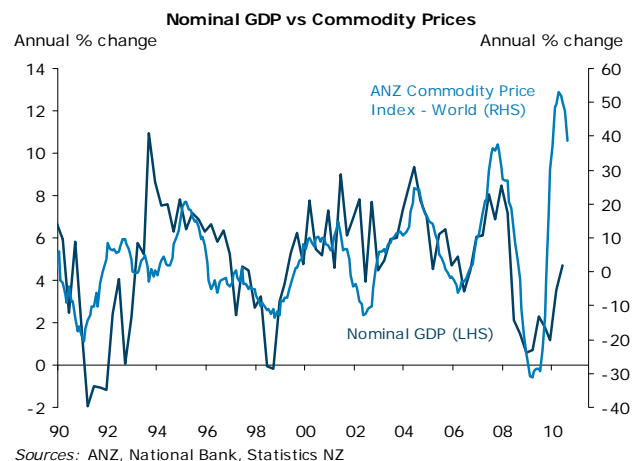
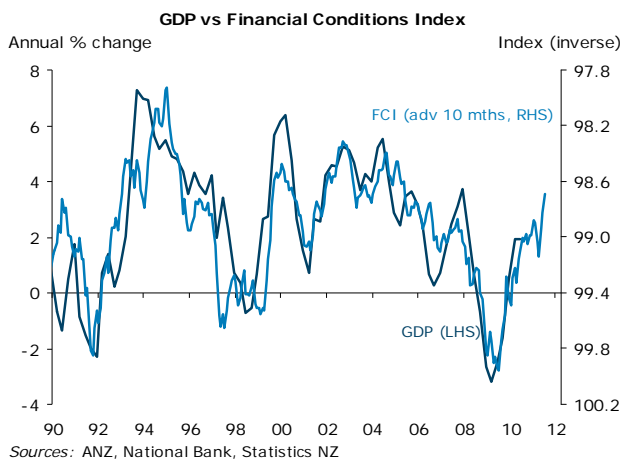
### THE BIG PICTURE

**The New Zealand economy is facing an elongated period of structural change as it rebalances away from a spending centric model towards more balanced growth.** During this period, the trend rate of growth will be lower. We are forecasting growth of 1.9 percent and 3.9 percent for calendar 2010 and 2011 respectively. Deleveraging remains a dominate influence on the business cycle. It is constraining growth in 2010, but the process of balance sheet repair raises the potential for some pent-up demand to be unleashed in 2011, but within the spirit of a subdued five-year picture.

**We have regularly characterised the post-credit crisis as a “bathtub with waves” shaped cycle, and the spirit of this remains intact.** There are massive tensions within the global financial system, and despite record monetary and fiscal policy stimulus supporting the global economy, you simply don't emerge from a credit crisis in the space of two years completely unscathed. There is much work still to be done. These include the process of global rebalancing, implementing regulatory changes, and navigating monetary and fiscal policy so that they support near-term prospects, but do not undermine the medium-term outlook. In practice, this is a tall order to deliver on and is adding additional layers of uncertainty and wider than usual error bands around the forecasts.

### INITIALLY A SLOW RECOVERY

**The gradual recovery of the New Zealand economy continues.** Normal cyclical dynamics, policy support and inventory rebuilding have played a key role. Higher bank funding costs have placed a wedge between the OCR and actual borrowing rates to households and firms. Nonetheless, overall borrowing rates remain below historical averages. Despite tentative signs that the demand for credit is returning, credit conditions remain tighter than during the boom years. Momentum is being restrained by structural headwinds. Deleveraging remains pervasive as households, farmers and businesses concentrate on improving balance sheets.

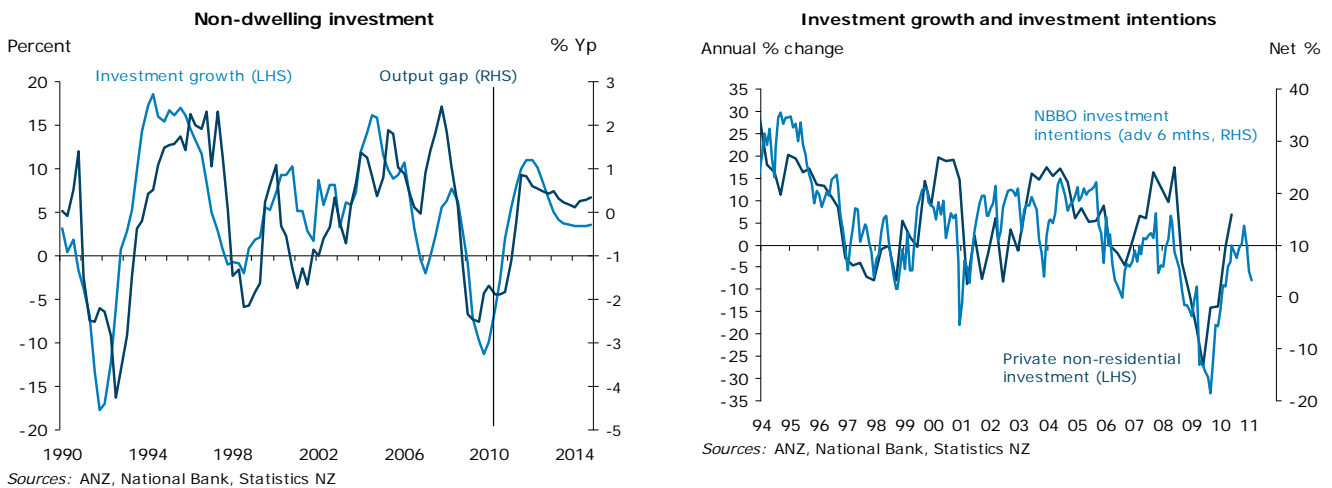


**The process of balance sheet repair has further to run.** Household debt to income has fallen from at peak of 159 percent in late 2008 to 154 percent currently. NZ's net external debt has fallen from 91 to 86 percent of GDP. Such dynamics tell us structural headwinds are abating. However, external and household debt remain very high and are a source of potential vulnerability. The household sector still has a negative savings rate and rural sector debt is 25 percent of GDP, with dairy sector debt rising from \$12 to \$29 billion in six years. This compares to total sector income (before expenses) of around \$10bn. As such, the industry is heavily leveraged. Such forces are restraining the potential for pent-up demand and a pro-cyclical recovery from being unleashed.

## ECONOMIC COMMENT: BUILDING A BASE FOR A BETTER 2011

We see ongoing growth in the near-term outlook, but of a patchy nature and certainly at a slower rate than would normally be expected at this stage of the cycle. The usual base effects are supporting growth, but for now business and residential investment remains restrained. Manufacturing had earlier been one of the stronger performers and has mirrored the robust recovery in manufacturing seen in our major trading partners courtesy of re-stocking, although of late momentum in the New Zealand manufacturing sector has slowed. Stocks have been rebuilt, but final demand is still weak.

The domestic housing market still remains subdued and we doubt this picture will change soon. With price expectations of buyers and sellers still poles apart, sales volumes remain low. Prices have barely budged since September last year. These factors will keep residential investment in check, with consents close to cyclical lows as a proportion of the housing stock. Recent declines in fixed mortgage interest rates are expected to prop up the market over the next few months. But the stark reality for house prices is that low affordability and weak balance sheets are proving more influential than pending supply-demand imbalances. Of course, all property doesn't come under this generalisation, but as a broad principle it applies.



**Business confidence remains respectable, but sub-components are flagging a lack of conviction.**

Firms remain relatively upbeat when looking at their own business prospects, but of late we've seen a worrying easing in firms' appetite to invest and hire. Both are critical elements for the recovery to broaden but are missing in action at present. Weakness in business investment is not just problematic for the demand side of the equation, but what it foretells of in terms of building supply-side capacity. Current weakness does not bode well for the economy's capacity in 2011-2013.

**The Canterbury earthquake proved to be costly.** Thankfully there was no immediate loss of life, but the magnitude 7.1 earthquake on September 4 caused significant damage to property and the productive capital stock. Latest official estimates place the cost of damage at \$4bn (0.6 percent of New Zealand's net capital stock). The rebuild will create growth per se, but this merely replaces lost capital so the growth is more technical than real. Around one third of this is from repairing the estimated 100,000 affected dwellings that have suffered damage as a result of the quake. Damage to infrastructure, residential structures and contents above the EQC threshold (\$120,000 plus GST) and non-residential structures very quickly make up the remainder. While insurance companies are likely to pick up some of the tab, the government and affected households and businesses are likely to be significantly out of pocket and balance sheet wealth has taken a hit.

**The earthquake is expected to contribute to volatility in economic activity.** With the Canterbury region accounting for 15 percent of NZ's GDP, earthquake disruptions are likely to temporarily weigh on economic activity, particularly in Q3. Some aspects will spill into 2011, such as the flow-on for tourism, but this should be more than offset by reconstruction related activity in 2011. Overall, we expect the net impact of the earthquake to add 0.5 percent to GDP.

**The patchiness of the recovery and the need to provide ongoing policy support is expected to see the RBNZ remain on the sidelines for the rest of 2010.**

**Despite near-term challenges, we are still seeing some positive signs.** First-up, we take weakness in housing and retailing as a positive for 2011. They foretell of balance sheet repair and set the scene for a more

## ECONOMIC COMMENT: BUILDING A BASE FOR A BETTER 2011

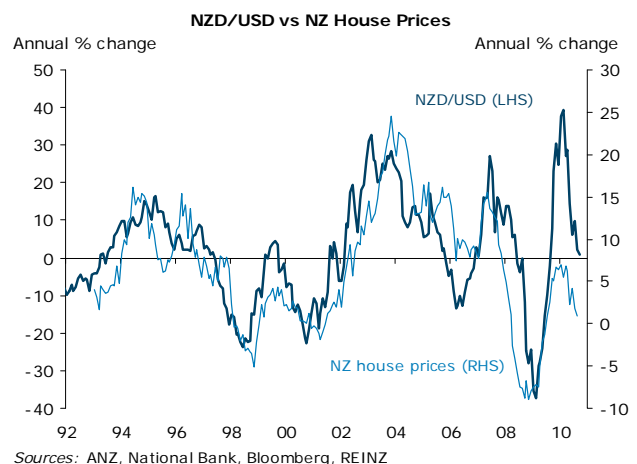
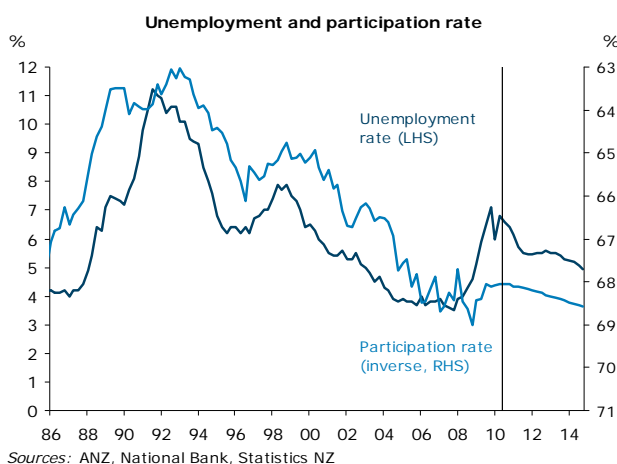
durable upturn. Resources are in the process of shifting to the earning side of the economy from the spending side. High export commodity prices continue to provide support. Export commodity prices are just shy of record highs and remain at historically high levels in globally inflation adjusted terms. Furthermore, commodity price strength has been more broad-based and not just confined to dairy. Whilst global dairy export prices are around a tenth off April levels, supply shortages and higher feed costs are expected to underpin robust prices for some time to come.

### Among our trading partners, strong momentum remains evident in Asia (ex-Japan) and Australia.

These economies are becoming increasingly influential for NZ.Inc, taking around 55 percent of our merchandise exports as opposed to 35 percent two decades ago. Stronger demand from these markets is supporting our commodity based exports, with dairy, meat and forestry exports now accounting for nearly half of total merchandise exports.

Manufacturing sector exports have been benefiting from the global recovery in manufacturing activity as inventories are rebuilt. Strong demand from Australia and the low NZD/AUD exchange rate are also providing support. However, a high NZD relative to the GBP and EUR is appearing to adversely impact visitor arrivals and tourism spending from Europe, as well as exports to those destinations.

**The labour market has turned the corner and is in subdued net job creation mode. But demand is very segmented across industries.** New Zealand labour market data has been notoriously volatile of late and if we are to believe the statistics (which we don't), unemployment fell from 7.1 percent at the end of 2009 to 6 percent in Q1 2010 and rose back to 6.8 percent in Q2. What we know is that leading surveys of employment have softened of late as some caution re-emerges. But industry contacts suggest a better underlying picture and a very segmented market with strong demand for some industries but poor demand for others. Official numbers of registered unemployed are starting to ease – albeit very slowly. Hours per employee remain lower than average (33.5 hours versus a historical average of 34.7 and a trough of 33.0). So firms have been increasing their demand for labour via longer hours and there is scope for more of this to come. Gross earnings are up 4.6 percent on a year ago, which when combined with a flat retailing environment is allowing households to allocate more to saving and repairing balance sheets. Net-on-net the underlying unemployment rate looks to be slowly easing. This is a positive, but still a far-cry from sub-6 percent unemployment rates that fosters real job security and strong wage demands.



### STRONGER 2011

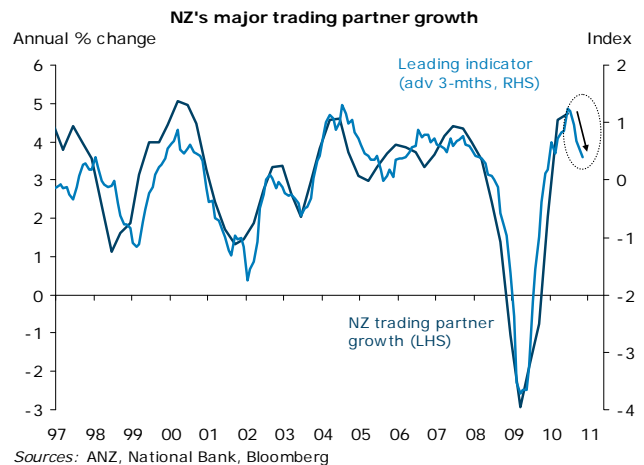
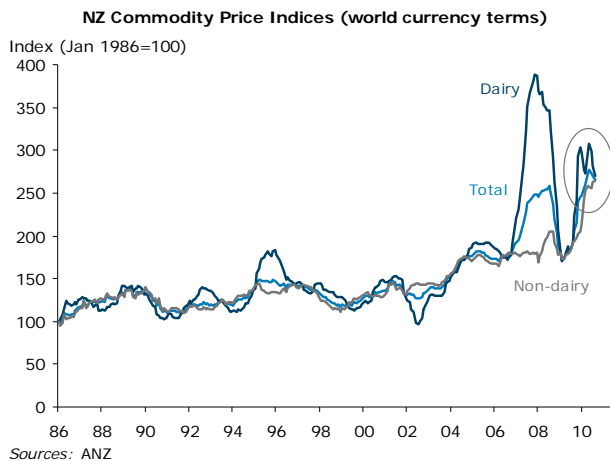
**We are far more optimistic about prospects for 2011.** We have always taken a sub-consensus view on 2010 growth and an above-consensus view for 2011, and see little reason to change our stance. Our stronger assessment for 2011 is premised on:

- The income boost from higher export prices aiding the economy, with the labour market also firming.
- The process of balance sheet repair in 2010 and weakness in some sectors allowing a lower base for growth to spring from.
- Reconstruction work from the September 2010 Canterbury earthquake will boost residential and non-residential construction activity.

## ECONOMIC COMMENT: BUILDING A BASE FOR A BETTER 2011

- A cyclical rebound in business and residential investment starts. Improving corporate and household balance sheets will be influential.
- A strengthening in trading partner growth and boost from the Rugby World Cup.
- Supportive financial conditions. Despite the recent global malaise, financial markets have moved accordingly (expectations for a higher OCR have been pushed out), and this should support activity in 2011.
- An element of pent-up-demand ready to be unleashed. We still believe deleveraging remains a key constraint on the business cycle. However, we struggle to see consumers keeping their wallets perennially shut. With the current account deficit at 3 percent of GDP, there seems some scope for pent-up demand to occur before we get into the worry zone of 4½ to 5 percent deficits (beyond that zone net external debt relative to the size of the economy starts to rise).

**A more broad-based recovery is expected to eventuate, with the economy growing at a robust above trend rate.** The income boost provided by higher export commodity prices will now be more broad-based across various sectors. We continue to assume a fair chunk of the proceeds will be used to repair rural balance sheets and retire outstanding debt. But we also suspect a fair portion of the proceeds will be spent on critical investment, maintenance and expenditure.



**Our forecasts assume that the earthquake reconstruction work will take up to five years to fully complete, with around half of the work completed by early 2012.** Initially this is likely to coincide with the foreshadowed cyclical rebound in residential and business investment activity. Implicit in our projections is the assumption that there will be enough spare capacity in the construction sector to handle both of these competing demands. We also assume that the Canterbury region will be able to secure the necessary capacity to carry out the work. At present there is considerable spare capacity within the construction sector with the floor area of residential consent issuance approximately one third below historical averages as a portion of the dwelling stock.

However, the rebound in activity is likely to be hamstrung by the wider effects of the earthquake. Despite insurance companies and EQC picking up much of the tab, household balance sheets have not escaped the quake unscathed altogether. Moreover, the likes of tourism flows are likely to be impacted into 2011, house prices in certain Christchurch suburbs will come under pressure, and no doubt we'll see higher insurance premiums across the whole country after the quake, which siphons consumer spending power.

**Furthermore, there remains some tension within the outlook.** While progress is being made at rebalancing the economy, the job is not yet complete. Low domestic interest rates and subdued business profitability had previously helped to narrow the current account deficit and arrest the trend increase in external indebtedness. However, as corporate profitability and the demand for imports recover, we still expect to see a widening current account deficit over the forecast horizon. Rising external debt leaves New Zealand vulnerable and emphasises how important it is for us to get our house in order.

**Also driving a widening in the current account deficit will be a strengthening in consumer spending in 2011.** Key to this will be an improving labour market. We see employment following the improvement in hours worked, with the unemployment rate to gradually decline towards 5½ percent by the end of next year.

## ECONOMIC COMMENT: BUILDING A BASE FOR A BETTER 2011

Wage growth will also start to firm as additional capacity in the labour market is used up. Strengthening residential investment and a recovering housing market will also underpin demand for consumer durables.

**We expect a pick-up in business investment by mid-next year** as profitability increases and the narrower margin of spare capacity facilitates more capacity enhancing investment. The improvement in business investment is forecast to be broad based, with plant and machinery and transport equipment set to feature prominently. Implicitly, this judgment is premised on the view that the current weakness in surveyed business investment intentions is temporary. Non-residential construction is expected to lag the improvement in other components, with earthquake reconstruction work proving support at the margin. Also providing some support will be the cut to the company tax rate from 30 percent to 28 percent from April next year. Export activity will also be underpinned by a broadening in trading partner demand. Commodity exports should continue to benefit from strong demand from emerging economies, although biological constraints will limit the volume response. Services exports are due to benefit from the 2011 Rugby World Cup and the labour market recovery in key overseas tourist markets. Manufacturing exports should continue to receive additional support from the recovering global economy, not to mention a favourable NZD/AUD exchange rate.

**The strengthening evident in economic activity and underlying inflationary pressures are expected to prompt the RBNZ to resume policy tightening.** Our projections assume a series of measured 25 basis point hikes from March next year, although we acknowledge the possibility of moving in 50 basis point chunks could not be ruled out altogether. We forecast the OCR to peak below 5½ percent this cycle, although there is the risk of a higher peak if the RBNZ leaves the policy tightening too late.

### THE FIVE YEAR STORY

**Beyond 2011 we assume a sedate period of growth.** This reflects the wider rebalancing process for the economy as growth in the tradable sector closes in on the non-tradable sector, or the economy seeks the holy grail of economics, namely more balanced growth. This journey is expected to be punctuated by volatility and we are under no illusions about the challenges ahead. Some of this volatility is going to be determined by economic issues, opportunities and challenges. But behavioural dynamics will also be prevalent. We are talking about a generational shift in attitudes towards housing, saving and investing. Moreover, challenges and the opportunities the economy faces are also coming at a time when demographics are working against us. There is a huge portion of the nation's capital tied up in the 55 to 65 age bracket and one immediate challenge here will be firing them up for the opportunities that beckon.

### RISKS

**Like any economic assessment, there are the normal risks and caveats.** We assume that global economic activity evolves broadly as projected. Our projections assume that supply-side capacity will be sufficient to accommodate a modest strengthening in growth from early next year. We also assume that net immigration inflows remain positive. Implicit in our forecasts is the assumption that the NZD plays a buffering role and does not overtly strengthen and hamper the rebalancing of the economy.

**Beyond these, we remind readers of the underlying spirit of our forecasts: the world and NZ.Inc are undergoing a period of profound change.** Events of 2008, 2009 and 2010 are the start of a long journey. **The economic outlook is more positive. But the speed we can grow will still be capped for some time by the decisions we have made in the past, and the time it takes to get our house in order.**

Calendar years	2007	2008	2009	2010(f)	2011(f)	2012(f)	2013(f)
Real GDP	2.8	-0.2	-1.7	1.9	3.9	2.6	2.0
Employment	1.9	0.6	-1.1	0.7	2.0	1.6	1.5
Unemployment Rate (Dec qtr)	3.5	4.6	7.1	6.4	5.4	5.6	5.3
Terms of trade (SNA basis)	5.9	2.5	-6.8	8.4	3.2	-1.4	-1.1
CPI Inflation	3.2	3.4	2.0	4.6	3.0	2.4	3.1
Current Account (as % of GDP)	-8.1	-8.8	-2.9	-3.0	-3.6	-4.4	-5.0
TWI	71.8	56.2	66.3	66.2	69.1	65.5	67.2
NZD/USD	0.77	0.58	0.72	0.71	0.72	0.67	0.68
NZD/AUD	0.88	0.82	0.81	0.76	0.77	0.77	0.83
Official Cash Rate	8.25	5.00	2.50	3.00	4.25	5.25	5.25
90-day bank bill rate	8.9	5.1	2.8	3.3	4.7	5.5	5.5
10-year bond rate	6.4	4.6	5.8	5.2	6.2	6.3	5.9

# MORTGAGE BORROWING STRATEGY

Mortgage rates have held steady over the past month, with fixed rates having already been cut earlier in September and the OCR having been left on hold at 3 percent at the RBNZ's last *Monetary Policy Statement*. Looking ahead, we expect mortgage rates to be fairly stable. Floating rates are likely to be unchanged as long as the RBNZ remain on hold, and at this stage we expect that to be until March 2011. However fixed rates are at the mercy of global interest rates. Although we expect global rates to continue edging lower, particularly if the US Federal Reserve pursues additional quantitative easing (QE), if they choose not to, rates could snap substantially higher. This risk, along with attractive break-even rates, suggests it may be worth fixing some portion of mortgages for 1 year or 2 years.

## OUR VIEW

With floating rates likely to be stable for some time, there is very little to think about for borrowers who are happy to remain on a variable mortgage. Indeed, not only are floating rates unlikely to rise till next year, but as it is the cheapest rate on the mortgage rate curve, it's an easy choice. The question is, **if you are on a floating rate, or your existing floating rate is about to expire, is it worth considering switching to a fixed rate?** As always, the answer is a complex one, and it depends on your individual circumstances. However, generally speaking, **we do think there is some value in fixing a portion of mortgage debt particularly in the 1 and 2 year tenure.** We say this for two main reasons. First, breakeven analysis shows that even a gradual series of rate rises like that projected by the RBNZ will see floating rates rise quickly enough to make fixing beneficial. Second, although the risk of a snap higher in global rates is low, if it were to occur, the effect of it would be enormous, and any strategy needs to recognise this, particularly as the "step up" into shorter term floating rates is now so low.

As noted earlier, **breakevens look attractive for some of the shorter term fixed rates, in particular the 1 year and 2 year.** Indeed, although the 6 month rate is only 15bps above the floating rate, we see little value in it because we see limited scope for the RBNZ to raise the OCR in the next five months. Even if the RBNZ does raise rates in March, it's likely to lead to a 25bp rise in the floating rate, so we see little point in paying an additional 15bps for the next 6 months to protect against the possibility of the rate being 25bps higher for the last month. Similarly, we also see **limited value in the 18 month rate**, as it is only 4bps less than the 2 year rate. If you think rates are headed higher, with such a small differential, you may as well fix for 2 years and get an additional 6 months protection in return for just 4 extra basis points. That being the case, how do the rest of the fixed rates stack up?

Regular readers will be familiar with our breakeven analysis, which we use to gauge the potential value in a chosen strategy. As we always reiterate when we introduce the concept, breakeven analysis doesn't help much when it comes to choosing between fixed and floating, but it is helpful when considering a set of fixed rates over a given timeframe. By comparing the choices available, **breakeven analysis provides a set of figures showing where rates need to be in future to make two strategies equivalent**, enabling better choices. Indeed, when thinking about the next 2 years, there are several choices you might consider if you wanted to fix. For instance, you might consider fixing for 2 years; or a "split" strategy like fixing for 1 year, and then for another year in 1 year; or fixing for 6 months, and then again in 6 monthly intervals over the remaining 18 months, and so on. Breakeven analysis allows you to compare these strategies against one another, and the table below shows breakevens as they currently stand. To illustrate the current situation, when thinking about the next 1 year as a time horizon, you might be contemplating whether it is better to remain floating, be fixed for 1 year at 6.45%, or to fix for 6 months at 6.35%, with a view to re-fixing in 6 months for another 6 months.

Mortgage Rates		Breakevens			
Term	Current	in 6mths	in 1yr	in 18mths	in 2 yrs
Floating	6.20%				
6 months	6.35%	6.55%	7.05%	6.81%	7.72%
1 year	6.45%	6.80%	6.93%	7.26%	7.92%
18 months	6.65%	6.80%	7.19%	7.55%	8.06%
2 years	6.69%	7.03%	7.43%	7.74%	8.21%
3 years	7.10%	7.43%	7.78%	8.04%	8.37%
4 years	7.45%	7.73%	8.01%		
5 years	7.70%				

## MORTGAGE BORROWING STRATEGY

At the moment, the 6 month breakeven in 6 months is 6.55%. That's only 0.20% above the current 6 month rate, and with the RBNZ set to lift the OCR by 25bps by then, chances are the 6 month rate will be above 6.55% in 6 months. As such, the 1 year rate looks attractive. Similarly, as it was last month, the 1 year breakeven in 1 year's time is at 6.93%. That's just 0.48% above the current 1 year rate, which isn't much, especially when you consider that the RBNZ is almost certain to lift the OCR by at least that amount (i.e. at least 2 rises of 25bps) over the next year. The 2 year rate also looks reasonably attractive.

However, when we compare longer term fixed rates against their breakevens, we find that the RBNZ would have to raise rates by a long way to make long term fixing beneficial. Indeed, when considering the next 3 years as a time horizon, you could, say, fix for 3 years at 7.10%, or fix for 1 year at 6.45% with the intention of re-fixing for the final 2 years in 1 year. So long as the 2 year rate is 7.43% or less in 1 year's time, the latter will be the better strategy in hindsight. The thing is, 7.43% is 0.74% above the current 2 year rate of 6.69%. That not only suggests that the RBNZ would need to raise the OCR by 3 times in the next year, but it also means that the 2 year will need to move up by as much as the OCR. However, we know that it typically doesn't. Indeed, **while short rates like the 6 month and 1 year tend to be very closely correlated with the OCR, longer maturities tend to be influenced by other factors**, including offshore interest rates.

The other main consideration borrowers ought to be aware of is the impact global interest rates are having on local rates, particularly fixed rates. There is no denying that the local interest rate market was comforted by the RBNZ's decision to leave the OCR on hold in September, and their admission that future OCR rise will be much more muted than originally envisaged. And while this has helped push local interest rates lower, the reality is that **NZ interest rates wouldn't be anywhere near where they are now had global interest rates not fallen so aggressively in the past six months**. Indeed, US 10 year Treasury yields have dropped from 4% to 2.5% since April, initially as the US economy started to show signs of slowing, and more recently in anticipation of further quantitative easing (QE). Sometimes known as "printing money", QE would involve the US Federal Reserve purchasing US Treasury Bonds in large quantities, with the intention of lowering bond yields, and flooding markets with liquidity. If the Fed does indeed "do" QE, and many expect they will at the November 3<sup>rd</sup> FOMC meeting, US bonds yields will probably fall. However, how far they fall depends crucially on how much QE is already "priced in". This leaves the market vulnerable to the Fed not adopting QE, or delivering a QE "package" that does not meet with the market's approval. If this occurs, rates may snap violently higher – in what markets sometimes call a classic "buy the rumour, sell the fact" move. Such an outcome would have obvious knock on effects here in New Zealand, and while it is a risk, rather than our core scenario, it must be considered simply for the fact that the impact would be large.

Finally, it's worth pointing out that the outright level of mortgage rates remains low. Remaining floating has its advantages, not in the least because it is cheap. But while fixed rates are more expensive than floating rates, the fact remains that there are upside risks (both in terms of eventual RBNZ rate hikes and from offshore markets). **If certainty is desirable, now is a pretty good time to consider fixing, especially for shorter terms like 1 or 2 years.**

# CANTERBURY PROPERTY SALES: SHAKEN AND STIRRED

## SUMMARY

The Real Estate Institute of New Zealand has recently published the first snapshot of Canterbury's real estate market following the devastating earthquake in early September. Not surprisingly, the number of homes sold has fallen in all of the affected localities reported in Canterbury. However, the average selling price, for the properties that did transact were mixed, with some areas reporting a strengthening over the month.

## HOUSE SALES SHAKEN

Last month we looked at the importance of the Canterbury economy and the ramification of the earthquake. This month we have the first return of real estate sales data for the region following the earthquake. As the earthquake struck relatively early in September, there are three uninterrupted days included prior to the earthquake. But we look through these three days and gauge the impact of the earthquake across the regions of Christchurch and Canterbury, as reported by the Real Estate Institute of New Zealand.

In the following table we compare the number of house sales in September with the same figure a year earlier. The right-hand column is the percentage change between the two columns. **The immediate feature, and not surprisingly, is that all regions recorded a drop in sales.**

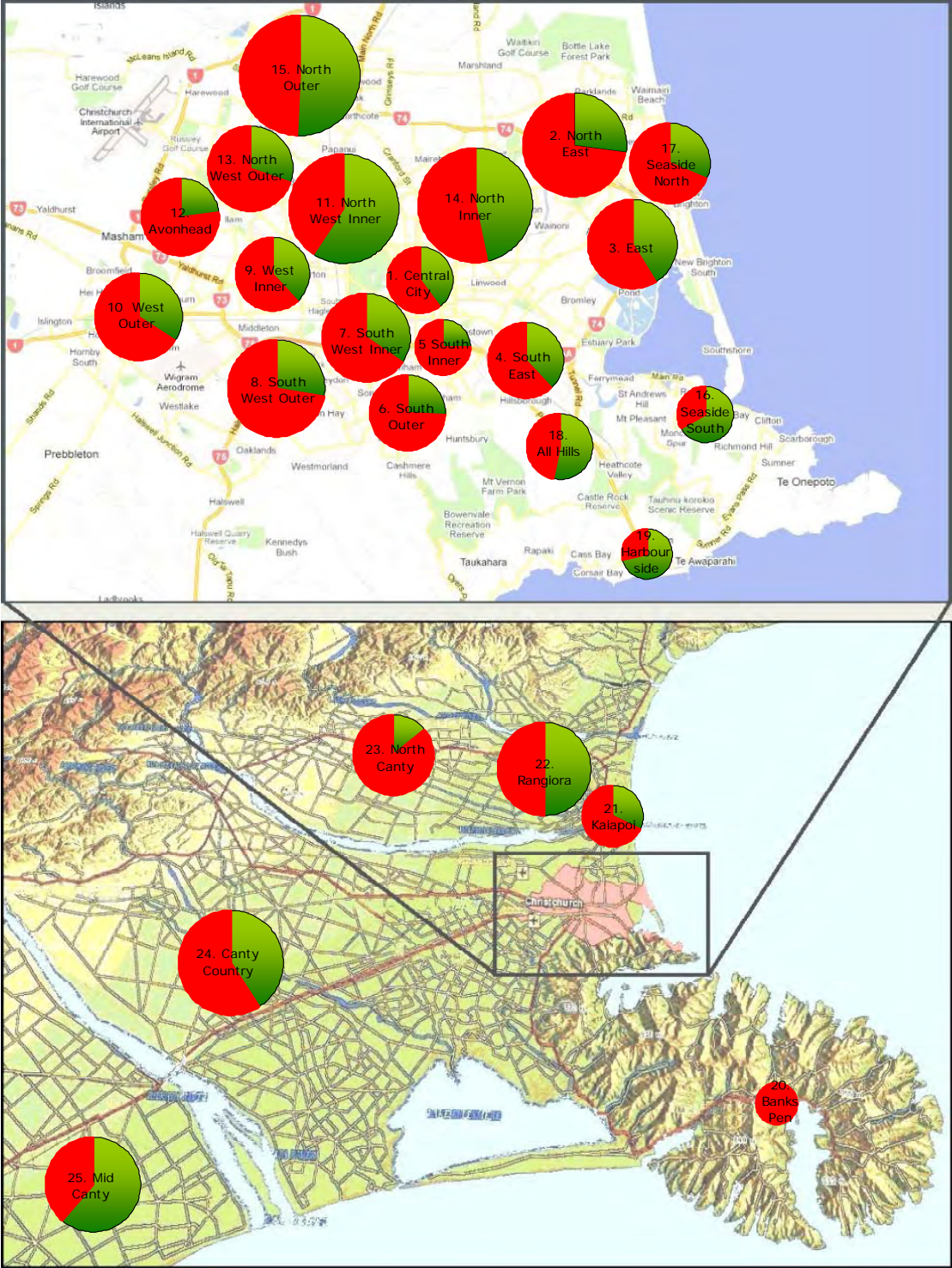
	Locality	Number of House Sales in September 2009	Number of House Sales in September 2010	Percentage change from a year ago
1	Central (Inside,4 Avenues)	25	10	-60%
2	Nth East (Avnda/Avsi/Bur/Park)	59	16	-73%
3	East (Aran/Bxly/Brom/Linwd)	39	16	-59%
4	Sth East (Hthct/Opawa/Wlstn)	21	8	-62%
5	Sth Inner (Sydhm/Wlthm)	20	5	-75%
6	Sth Outer (Beck/Bow/Casfl/Stma)	27	7	-74%
7	S/W Inner (Addtn/Smfld/Sprey)	23	8	-65%
8	S/W Outer (Hlsw/Himtn/Hnhy)	51	14	-73%
9	West Inner (Ricc/Upper Riccn)	29	11	-62%
10	West Outer (Heih/Hby/Sckbn/Tem)	38	13	-66%
11	N/W Inner (Fendn/Ilam/Meriv)	47	28	-40%
12	Avonhead	26	6	-77%
13	N/W Outer (Brynd/Burns)	33	10	-70%
14	Nth Inner (Dal/Rich/Shly/Stalb)	58	27	-53%
15	Nth Outer (Bfst/Bish/Pap/Redwd)	57	29	-49%
16	Seaside Sth (Rdcfs/Sumfl)	6	4	-33%
17	Seaside Nth (Nb/Nthbeach/Sthnb)	35	11	-69%
18	All Hill (Cash/Clh/Mtp/Scar/Wm)	17	9	-47%
19	Harbourside (All Lytl&Harbour)	7	5	-29%
20	Banks Pen (East Of Motukarara)	2	0	-100%
21	Kaiapoi	22	7	-68%
22	Rangiora	38	19	-50%
23	Nth Cant (All Nth&W Ofnthwaimk)	29	4	-86%
24	Cant Ctry (All oth W&S To Midcan)	49	20	-59%
25	Mid Canty (Rakaia/R-Rangitata R)	41	25	-39%
	<b>TOTAL ALL LOCALITIES</b>	<b>799</b>	<b>312</b>	<b>-61%</b>

Source: ANZ, National Bank, Real Estate Institute of New Zealand

We present the data as a graphic on the following page, which reflects visually where the largest reductions have been. The size of each pie graph overleaf represents the relative number of house sales in each locality over the twelve months to August 2010. The green slice represents the number of sales in each locality in September 2010 as a percentage of the figure recorded in September 2009.

# CANTERBURY PROPERTY SALES: SHAKEN AND STIRRED

Reduction in house sales in earthquake affected areas



The larger the fall in house sales is represented with a greater proportion in red. The greatest drop was in Banks Peninsula, but given the low number of sales this drop isn't very significant. **The next largest fall was measured in North Canterbury, with sales falling from 29 last year to just 4 in September.** Avonhead suffered the next largest fall in sales, falling 77 percent, and was closely followed by the southern suburbs of Sydenham, Waltham, St Martins and Beckenham.



## CANTERBURY PROPERTY SALES: SHAKEN AND STIRRED

The least affected localities were further away from the epicentre of the earthquake. House sales in Lyttelton harbour and the southern seaside suburbs dropped by about a third from the same month a year earlier. The next least affected area was mid-Canterbury. House sales in the northwest suburbs of Fendalton, Ilam and Merivale were relatively firmer than all of the other Christchurch city suburbs.

### SELLING PRICES STIRRED

**While the number of house sales was weaker across the board, the average selling prices were mixed.** In the table below we have summarised the average selling price in each locality in the latest four months. The percentage change in the right-hand column is calculated between the average selling price in the three months to August and that recorded in September. Fourteen of the 25 localities recorded weaker average selling prices, one region had no sales and ten recorded higher prices.

Locality	Average Selling Price			Average for the 3 months Jun-Aug	Average selling price in September	Percentage change
	June	July	August			
Central (Inside, 4 Avenues)	\$513,846	\$360,813	\$499,500	\$469,726	\$291,910	-38%
Nth East (Avnda/Avsi/Bur/Park)	\$347,431	\$350,285	\$393,743	\$362,462	\$379,500	+5%
East (Aran/Bxly/Brom/Linwd)	\$238,186	\$256,809	\$259,222	\$249,816	\$246,682	-1%
Sth East (Hthct/Opawa/Wlstn)	\$286,357	\$332,739	\$290,500	\$307,736	\$257,813	-16%
Sth Inner (Sydhm/Wlthm)	\$219,778	\$202,778	\$226,286	\$215,480	\$260,800	+21%
Sth Outer (Beck/Bow/Casfl/Stma)	\$362,156	\$452,136	\$371,559	\$401,055	\$354,714	-12%
S/W Inner (Addtn/Smfld/Sprey)	\$316,667	\$299,353	\$297,272	\$305,146	\$327,631	+7%
S/W Outer (Hlswl/Himtn/Hnhy)	\$423,586	\$393,467	\$387,000	\$402,521	\$374,393	-7%
West Inner (Riccn/Upper Riccn)	\$417,000	\$347,891	\$339,454	\$377,157	\$305,424	-19%
West Outer (Heih/Hby/Sckbn/Tem)	\$349,838	\$314,236	\$295,375	\$319,084	\$291,873	-9%
N/W Inner (Fendn/Ilam/Meriv)	\$701,211	\$551,448	\$543,198	\$603,817	\$588,364	-3%
Avonhead	\$411,000	\$352,650	\$370,377	\$381,545	\$365,083	-4%
N/W Outer (Brynd/Burns)	\$398,500	\$439,439	\$456,933	\$431,135	\$349,460	-19%
Nth Inner (Dal/Rich/Shly/Stalb)	\$332,460	\$315,232	\$306,779	\$319,925	\$329,726	+3%
Nth Outer (Bfst/Bish/Pap/Redwd)	\$385,037	\$364,395	\$354,455	\$367,853	\$405,138	+10%
Seaside Sth (Rdcfs/Sumfl)	\$512,709	\$614,200	\$658,214	\$599,909	\$524,750	-13%
Seaside Nth (Nb/Nthbeach/Sthnb)	\$339,443	\$334,521	\$337,065	\$336,662	\$287,864	-14%
All Hill (Cash/Cih/Mtp/Scar/Wm)	\$619,789	\$589,167	\$504,875	\$578,938	\$807,083	+39%
Harbourside (All Lytlh&Harbour)	\$513,417	\$419,150	\$343,486	\$420,713	\$452,400	+8%
Banks Pen (East Of Motukarara)	\$372,500	\$333,500	\$300,125	\$326,563	n.a.	n.a.
Kaiapoi	\$337,071	\$268,042	\$322,267	\$311,451	\$381,000	+22%
Rangiora	\$353,696	\$323,923	\$352,006	\$342,546	\$315,184	-8%
Nth Cant (All Nth&W Ofnthwaimk)	\$306,500	\$304,632	\$291,345	\$301,050	\$335,000	+11%
Cant Ctry (All oth W&S To Midcan)	\$390,175	\$358,390	\$361,988	\$370,653	\$419,985	+13%
Mid Canty (Rakaia/R-Rangitata R)	\$279,495	\$255,103	\$261,308	\$266,741	\$261,400	-2%
<b>TOTAL ALL LOCALITIES</b>	<b>\$386,601</b>	<b>\$359,900</b>	<b>\$367,661</b>	<b>\$371,579</b>	<b>\$372,873</b>	<b>0%</b>

Source: ANZ, National Bank, Real Estate Institute of New Zealand

**The largest fall in house prices was measured in the central city**, where the average selling price dropped 38 percent. Falls were generally recorded in most of the city suburbs, with the odd exception of some inner suburbs in the south and north. **The hillside areas led the localities to register a rise in average selling prices**, lifting 39 percent on the preceding three months. The gains tended to be in areas further away from the CBD. Intriguingly the second largest gain was measured in Kaiapoi, one of the regions to suffer some of the worst damage. Overall, there was little change in the selling price across the entire region.

We caution against readers putting too much weight onto these price statistics as they are **strongly influenced by the composition of properties sold**. This is likely to be more evident in episodes where dwelling sales are at very low levels, such as in recent months.

We'll be keeping a close eye on the real estate statistics in the earthquake zone over coming months and will report on any trends that may develop in later issues of *Property Focus*.

## KEY FORECASTS

Weekly mortgage repayments table (based on 25-year term)

		Mortgage Rate (%)													
		5.75	6.00	6.25	6.50	6.75	7.00	7.25	7.50	7.75	8.00	8.25	8.50	8.75	9.00
Mortgage Size (\$'000)	200	290	297	304	311	319	326	333	341	348	356	364	371	379	387
	250	363	371	380	389	398	407	417	426	435	445	455	464	474	484
	300	435	446	456	467	478	489	500	511	522	534	545	557	569	581
	350	508	520	532	545	558	570	583	596	610	623	636	650	664	677
	400	580	594	608	623	637	652	667	682	697	712	727	743	758	774
	450	653	669	684	701	717	733	750	767	784	801	818	836	853	871
	500	725	743	761	778	797	815	833	852	871	890	909	928	948	968
	550	798	817	837	856	876	896	917	937	958	979	1000	1021	1043	1064
	600	870	891	913	934	956	978	1000	1022	1045	1068	1091	1114	1137	1161
	650	943	966	989	1012	1036	1059	1083	1108	1132	1157	1182	1207	1232	1258
	700	1015	1040	1065	1090	1115	1141	1167	1193	1219	1246	1273	1300	1327	1355
	750	1088	1114	1141	1168	1195	1222	1250	1278	1306	1335	1364	1393	1422	1451
	800	1160	1188	1217	1246	1274	1304	1333	1363	1393	1424	1454	1485	1517	1548
	850	1233	1263	1293	1323	1354	1385	1417	1448	1480	1513	1545	1578	1611	1645
900	1306	1337	1369	1401	1434	1467	1500	1534	1567	1602	1636	1671	1706	1742	
950	1378	1411	1445	1479	1513	1548	1583	1619	1655	1691	1727	1764	1801	1838	
1000	1451	1486	1521	1557	1593	1630	1667	1704	1742	1780	1818	1857	1896	1935	

Housing market indicators for September 2010 (based on REINZ data)

	House prices (Ann % change)	3mth % chng	No of sales (s.a.)	Mthly % chng	Avg days to sell (s.a.)	Comment
Northland	5.7	1.7	88	(-5%)	59	Days to sell returns to a more normal level
Auckland	-1.2	0.2	1,569	(+2%)	39	The median time to sell hits an 18-month high
Waikato/BOP/Gisborne	-0.2	0.2	559	(-7%)	65	Second slowest location to sell a house
Hawke's Bay	0.3	-4.1	159	(-4%)	55	Recorded the weakest 3 mthly percent change
Taranaki	-3.5	-1.4	224	(+6%)	59	Median selling price dropped to a 12-mth low
Manawatu-Wanganui	-4.7	-0.7	127	(-12%)	61	The lowest annual change in house prices
Wellington	5.4	1.9	497	(-7%)	41	The third strongest lift in house prices in NZ
Nelson-Marlborough	-2.1	-1.6	173	(+11%)	45	A strong lift in the number of house sales
Canterbury/Westland	-4.5	-1.7	414	(-38%)	41	Earthquake affected drop in house sales
Otago	15.2	2.1	77	(-11%)	67	The strongest annual rise in house prices
Central Otago Lakes	-3.1	1.6	192	(-7%)	53	The days to sell is at a 15-month high
Southland	-2.6	4.4	154	(+30%)	36	Strongest increase in house sale numbers
NEW ZEALAND	-0.1	0.1	4,216	(-7%)	45	Weighed down, even more so after the quake

## Key forecasts

Economic indicators	Actual			Forecast						
	Mar 10	Jun 10	Sep 10	Dec 10	Mar 11	Jun 11	Sep 11	Dec 11	Mar 12	Jun 12
GDP (Ann Avg % Chg)	-0.4	0.7	1.6(f)	1.9	2.0	2.4	3.0	3.9	4.3	4.1
CPI Inflation (%)	2.0	1.7	1.5	4.1	4.4	5.2	4.9	2.9	2.8	2.5
Unemployment Rate (%)	6.0	6.8	6.6(f)	6.4	6.1	5.7	5.5	5.4	5.5	5.5
Interest rates	Actual			Forecast (end month)						
	Aug 10	Sep 10	Latest	Dec 10	Mar 11	Jun 11	Sep 11	Dec 11	Mar 12	Jun 12
Official Cash Rate	3.00	3.00	3.00	3.00	3.25	3.75	4.00	4.25	4.75	5.25
90-Day Bank Bill Rate	3.3	3.2	3.2	3.3	3.7	4.2	4.3	4.7	5.2	5.5
Floating Mortgage Rate	6.3	6.4	6.4	6.4	6.7	7.2	7.4	7.6	7.9	8.4
1-Yr Fixed Mortgage Rate	6.3	6.4	6.4	6.5	6.8	7.1	7.2	7.6	8.0	8.2
2-Yr Fixed Mortgage Rate	6.9	6.7	6.7	6.7	7.1	7.4	7.5	7.9	8.2	8.3
5-Yr Fixed Mortgage Rate	7.8	7.7	7.7	7.8	8.0	8.2	8.2	8.4	8.5	8.5

## IMPORTANT NOTICE

### 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.
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### 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:



## IMPORTANT NOTICE

- 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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