Market Focus

New Zealand

24 November 2008

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Open possibilities

THE COW TRIPS OVER THE MOON

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Page 2: Economic overview

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Page 5: Economic comment – another dairy update

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Page 7: Economic comment – the regional gap

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Page 8: Economic comment – global watch

> Data was mixed across the globe last week, although some key US leading gauges continue to slow sharply, as does the labour market. Inflation appears to have well and truly turned, with CPI data lower than expected in the US, UK and Hong Kong last week.

Page 9: Interest rate strategy

> Interest rate markets rallied hard last week, both here and abroad. US Treasury bond yields dropped to a 45 year low last week, and with the RBNZ set to take the OCR to a historic low, we expect NZ interest rates to make new ground too. Inflation hasn't been completely eradicated, but it's no longer the primary concern.

Page 10: Interest rate comment – the impact of the RBNZ's new liquidity arrangements

> Recent changes to New Zealand's liquidity arrangements have had a material impact on money market interest rates. Since the announcement of the Term Auction Facility and the reintroduction of the Reserve Bank Bill tenders, the bellwether 3mth BKBM FRA rate has fallen by 87bps. While a part of that fall can be explained by expectations of more aggressive policy easings, a good chunk of it comes down to improved liquidity.

Page 11: Currency strategy

> Despite a late week recovery, sentiment towards the NZD remains weak, and US equity movements continue to dictate the kiwi's direction. Any short-term rebounds should be treated as such, with the medium-term trend still pointed downwards.

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ECONOMIC OVERVIEW

We have a lot of sympathy for a 150bps move by the RBNZ in December, given both the global scene and what we are seeing domestically. However, the currency and recent lowering of retail mortgage rates are sufficient to keep us in the 100bps camp, for now. But conditions are fluid, and our call is constantly being reviewed.

What's ahead?

> **Q4 RBNZ *Survey of Expectations*** (Tuesday 1500 NZDT). Falling petrol prices are expected to see the key 2-year ahead inflation expectations ease from its 3.0 percent reading last quarter.

> **October Overseas Merchandise Trade** (Thursday 1045 NZDT). Despite sharply lower oil prices, another large monthly trade deficit of $500 million is expected. Nevertheless, this should see the annual trade deficit improve slightly.

> **NBNZ November *Business Outlook*** (Thursday 1500 NZDT).

> **October Credit Growth** (Thursday 1500 NZDT). September housing lending growth was the weakest on record. Given the state of the housing market, we would not rule out a further slowing. Business and rural lending growth will remain at a higher level, although they are also likely to be easing.

> **October Building Consents** (Friday 1045 NZDT). The level of residential dwelling consent issuance will remain subdued. The bigger focus will be commercial issuance and we expect it to show further signs of easing.

What's the view?

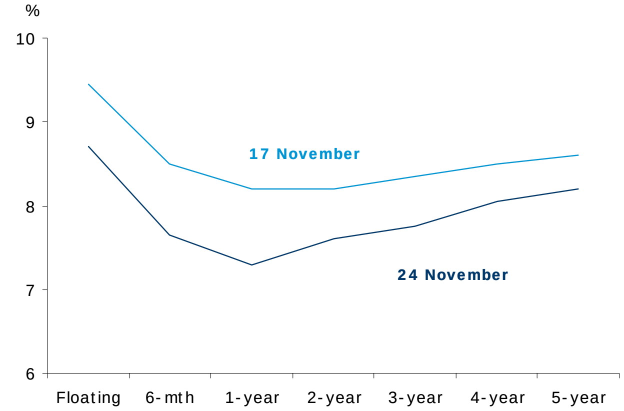
We won't simply regurgitate what is going on around the globe. Suffice to say the picture continues to deteriorate. And to such a degree that it has got a few commentators, and indeed the market, thinking about a 150bps cut by the RBNZ in December.

It's a view we have a lot of sympathy for. We've just completed our Roadshow around the country and there is no doubt the economy is weak. In fact, probably weaker than the downgrade we put into our growth forecasts only last week. Having "negative" momentum going into a global shock will only exacerbate the impact on the NZ economy. Then there is the credit-centric nature of the global shock itself and a large current account deficit the nation needs to fund. In the past week we have seen announcements that the national airline was reducing long-haul capacity by 8 percent, and the dairy payout for this season has been revised lower. At $6/kg milk solids, it is still a pretty good payout for the latter, but not at existing farm prices, which is the next leg of the asset price adjustment. Both clearly signal that NZ is already starting to see the flow-on effects of the pending global recession. The latest *Consensus Forecasts* have again downgraded the outlook for NZ's major trading partner growth to just 1.2 percent for the 2009 calendar year (the RBNZ assumed 2.4 percent at their September *MPS*). Further downward revisions are likely given the risks are all pointed down, and the fact that *Consensus Forecasts* tend to lag actual developments.

Something we are also keeping an eye on is market pricing. To be fair, it is a bit of a cop out as it implies you are merely following the market. But we suspect the reality is that now is simply not the time that central banks will want to "disappoint" the market. In fact, the tendency has been to do the opposite. Hence, the more the market firms on a 150bps move, the greater the temptation for the RBNZ to simply take the path of least resistance.

So what is holding us back from switching our call to 150? Four things. First, the currency, which has moved a long way even after allowing for commodity prices. Our financial conditions index has loosened markedly, and we will be providing an update next week. Second, is the material fall we saw in retail mortgage rates across the curve last week, which we suspect the RBNZ will take as evidence the transmission mechanism is working. Third, the RBNZ can take a bit of comfort from the positive impact that new liquidity arrangements are having on the market in terms of lowering wholesale rates. Simply tweaking the OCR is not the only mechanism they have been using to get rates down. Like other central banks the RBNZ has also taken measures to improve liquidity which has contributed to the decline in inter-bank interest rates. We are not sure this is well understood by market participants in some areas. Page 10 provides a summary of recent developments.

NZ mortgage borrowing curve



Sources: ANZ National

Finally, there is inflation itself. Sure, headline inflation is set to fall rapidly due to plummeting petrol prices, and we remain more attuned to downside as opposed to upside inflation risks given our global view. In fact it's amazing to see how people are now becoming fixated with the headline. But we are also mindful of history, and part of the reason NZ is in the current jam was because policy became centred on the headline rate as opposed to domestic generated pressure. For sure, the medium-term drivers of inflation are improving rapidly at present given the economic backdrop. Hence, the big picture for rates is lower. But the real issue is of course degree.

For now, and despite having a trigger finger, we remain in the 100bps camp. Apart from the global backdrop (which we do not expect any respite from) and a poor domestic scene, probably the biggest thing to keep an eye on between now and the December meeting well be the RBA. If the RBA deliver big again on 2 December (two days before the RBNZ's decision) with the Australian market (but not the economist community) pricing in a decent chance of a 150bps cut, that will take their cash rate to 3.75 percent. Now NZ at 5.5 percent (assuming the RBNZ cuts by 100bps) and Australia at 3.75 just wouldn't sit right. By no account does this mean the RBNZ should be slavishly following the RBA, as there is limited economic justification for doing so. But you have to recognise the reasoning behind the RBA delivering the sort of movements it has been delivering in the first place. A lot of it hinges around the global scene, especially Asia. And if the RBA is that worried – and discounting inflation pressures – then a nation with a stronger export reliance, negative momentum heading into the shock, and more extended land prices such as NZ, certainly needs to be on notice.

Looking forward to the events of this week, there are a couple of interesting local releases. The first is the RBNZ's Q4 *Survey of Expectations* on Tuesday. The 2-year ahead inflation expectations measure is the key gauge to watch. While it is likely to remain at a reasonably elevated level, we expect it to fall after hitting 3.0 percent in the September quarter. The sharp drop in petrol prices (which are both transparent and also purchased frequently), which will now drag down one year ahead inflation sharply (we are picking 2.7 percent), are likely to play a reasonable role in dampening inflation expectations. Hence, we need to take note of the survey itself. But also need to recognise that such surveys are at best partial measures as to where true inflation expectations sit, particularly across non-tradable areas.

The second is the National Bank *Business Outlook* for November, given its good lead characteristics for actual economic activity. Last month, confidence and the majority of activity indicators (own activity, employment, investment, profits), dived, as the full implications of the global financial turmoil hit home. Whether this is sustained in the November survey will have a key bearing on our expectations for GDP growth over the December quarter.

The other releases this week are overseas merchandise trade, credit growth and building consents for October. All are likely to reinforce a similar message in that the domestic economy remains very weak. In the trade data, we will be watching out for the capitulation in consumer goods imports which we have been expecting for some time. To date (with the exception of passenger car imports) consumer goods imports have held up at a much higher level than we would have expected considering that retail sales volumes have contracted over the first nine months of the year. This has resulted in a rise in inventory levels. Nevertheless, and despite the reasonable fall in global oil prices, we expect another trade deficit to be recorded for the month, which is typically the case for October.

Credit growth will undoubtedly remain weak. Last month household credit growth was just 0.2 percent – the lowest rate of growth since this series began in 1991. Compared to a year ago, household credit growth has slowed to just 6.7 percent, although if you look at the more timely 3-month annualised rate, growth has slowed to just 3.7 percent. Credit growth to businesses and rural are likely to remain at a more elevated level, although we suspect for the former this is being increasingly used for working capital purposes rather than investment.

In regards to credit growth, we were forwarded an interesting piece from an offshore investment bank noting the material differences between the rate of credit growth, and the change in the rate of credit growth[1]. People tend to focus on the former, although the relationship with final demand is relatively loose. A purer measure, which the researchers defined at the "credit impulse", is simply the change in the stock of credit to GDP compared to last period.

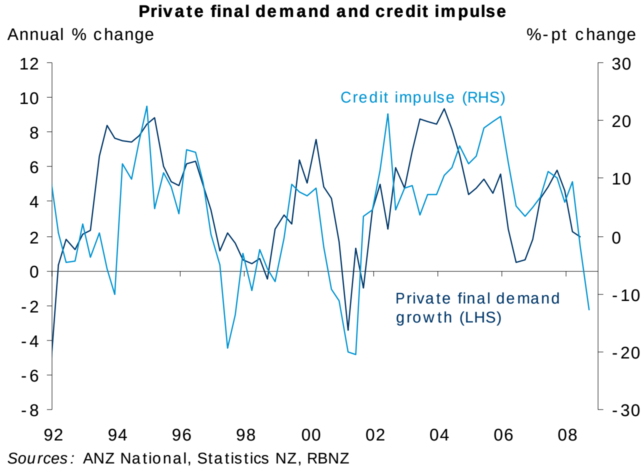
$$CI_t = \frac{c_t}{GDP_t} - \frac{c_{t-1}}{GDP_{t-1}}$$

where CI_t is the credit impulse and c_t is the change in the stock of credit.

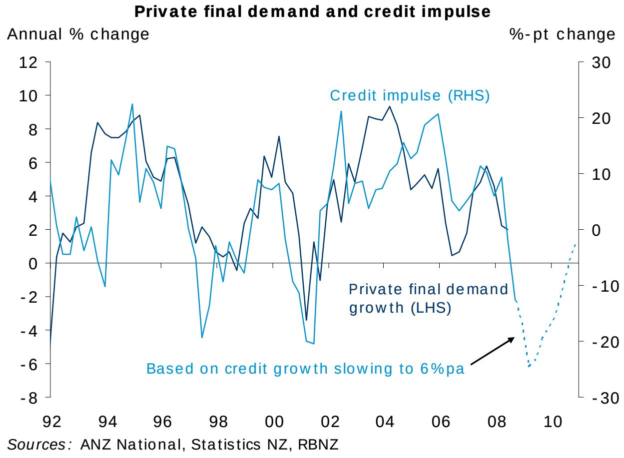
Using this approach we can map a pretty close relationship to final domestic demand. An obvious question though is which drives what? Over the past few years, it can be argued that due to rising asset prices (primarily housing) and the abundance

[1] Acknowledgement needs to go to Michael Biggs from Deutsche Bank for the framework and analysis on the US.

and relatively low price (i.e. interest rates) of credit, there was a self reinforcing spiral. The huge increase in mortgage equity withdrawal, where homeowners (encouraged by rising house prices which increased their equity) could "put it on the house" to fund consumption, is an example of this.



But we are now in a different environment, given global developments. And with asset prices falling, the spiral looks to be working the other way round now. Our calculation of the credit impulse shows that it has turned negative in the middle of this year. This, despite annual credit growth still running at 10 percent plus (although more timely 3 month annualised figures are far weaker). Again, it is new lending that is important (the flow) which helps fund activity, not the size of the existing stock. On the face of it, it suggests the potential for a pretty aggressive contraction in domestic demand. Standing back, a material adjustment is also consistent in improving NZ's external current account position.



The final piece of data out this week is residential building consents issued and they should remain at a subdued level in October. For the past three months we've seen residential consents settle around levels last seen in 1991. Clearly, there is going to be a lot of scrapping over a limited amount of work in 2009, particularly given that the economy is now 70 percent larger than in 1991!

We'll be closely eyeing the "pricing" gauge in the survey ($/m^2) to see what it is potentially indicating for construction costs. A key issue is also how commercial consent issuance holds up. We expect commercial consent issuance to also trend lower given the challenging credit backdrop and investment freeze that appears to be developing if recent business surveys are to be believed.

Internationally, there is a large amount of US data due for release this week (durable goods, personal income and spending, home sales and consumer confidence) and it is very likely to mirror recent releases by highlighting the fact that the US economy is heading backwards. Elsewhere around the globe the German IFO survey will be widely watched.

Recent local data…

Food Price Index (October): Food prices fell 0.3 percent in the month, although are still up 9.9 percent on a year ago.

Producer Price Indices (September quarter): Input prices rose 3.7 percent (13.6 percent on a year ago), while output prices rose 2.4 percent (9.8 percent on a year ago).

NBNZ *Regional Trends* (September quarter): Nationwide economic activity fell 0.1 percent, with the West Coast posting the weakest result.

External Migration (October): A net 10 people permanently migrated to NZ in October fully offsetting a net 10 people who left the country last month. Short-term visitor arrivals rose 0.7 percent, but are still down 3.3 percent on a year ago.

Electronic Card Transactions (October): Headline ECT sales rose 0.5 percent, while core sales rose 1.0 percent.

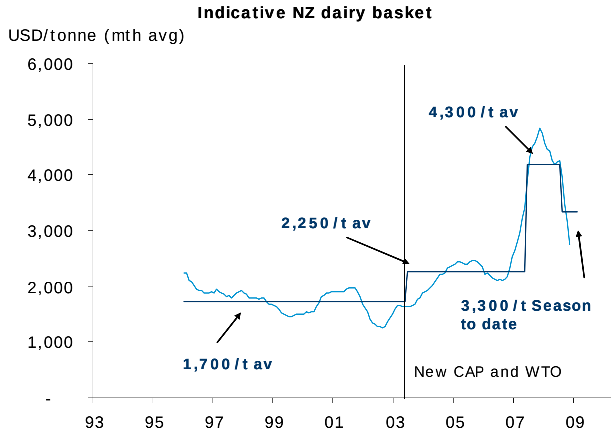
Credit Card Billings (October): Total billings on cards in New Zealand fell 1.1 percent, following a 0.9 percent rise in September.

ANOTHER DAIRY UPDATE

Fonterra last week announced a reduction in the forecast payout from $6.60 to $6.00 per kilogram of milk solids (kg ms). This is the second revised forecast, and it is unlikely to be the last for the season. The forecast fall in dairy income for 2008/09 will be significant for the economy.

Overview

Fonterra's announcement was not unexpected. USDA data released last Friday confirms the ongoing downward trend for a wider range of dairy commodities. Prices were down another five to eight percent in USD terms over the previous fortnight. The fall from the extra-ordinary high price around US$4,800/t achieved in November 2007 is now 43 percent to an estimated US$2,750/t. Anecdotally prices are lower than that.



Sources: ANZ National, USDA

There are now three important questions that need answered.

Where is the floor price and when will it be reached?

Much was made by many commentators 6 to 12 months ago about the structural change (i.e. permanent) lift to above historic levels for dairy prices. We made the point ourselves, but our step change was a bit smaller than some. We still think the step concept holds and are also sticking to our small step in the meantime.

The history and very nature of food production means that there will always be a significant degree of unpredictability in food prices regardless of where an underlying longer-erm price level might sit. There are currently extremes in instability in dairy (all!) commodity prices. Our medium-term view is for an average payout in the high $5/kg ms range and see little reason to change that.

As for timing of a floor we noted in our last Dairy update (10th November) that milk production is increasing in the US and the EU. Extra production appeared to be going into milk powders. Anecdotal evidence suggested the initial down turn in prices was an end user reaction to the price spike. More recently buyers were thought to be running inventory down to fine just in time margins. No one wants to commit to purchase of significant volumes or forward buy any commodity on a falling market. The availability and cost of credit may also be impacting on buyer cash flows and hence purchasing power. But eventually buyers have to make a purchase and will be aware that the availability of product starts to fall in Oceania after Christmas.

What is the impact on the economy?

The dairy payout is the result of twelve months trading and there is still eight months of Fonterra's current financial year to run. There is no need for panic but the signs are not good. The revised forecast is unlikely to be the last for the season given the state of flux in the market place. Anecdotally, prices are still falling, although the currency is providing somewhat of a buffer.

The cash advance payments to farmers were left unaltered. The cash effect of a lower payout in the 2008/09 financial year will be muted by the high final payouts from the 2007/08 year. The cash effect will bite more in 2009/10 when the final payout from 2008/09 will be lower. This is where attention will progressively turn.

$6/kg ms is still a good number on a historical basis and many dairy farmers will make reasonable profits given an average season. Every plus or minus $0.10/kg ms is approx $12,000 gross farm income on a conventional average owner operator basis. A $6 payout and normal production in the Waikato in 2008/09 will not be a lot different to 20 percent less production last season at a higher price. Remember; last year's income was dampened by drought. Hence, the collective impact this season of lower prices will be mitigated somewhat by higher volumes. But once again, this will turn attention and thinking to 2009/10 if volumes stabilise, and the payout is weaker again.

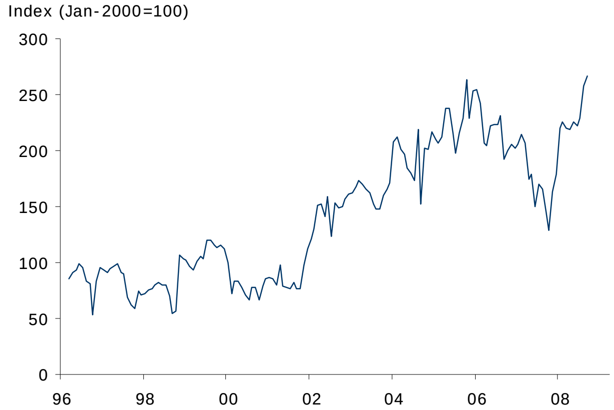
Conversely, a fall of a dollar plus /kg ms on an irrigated Canterbury property is significant in gross income terms (-20 percent) where production this year could be expected to be little different to last year. The bottom line in both instances is heavily influenced by the degree of control exhibited over expenditure.

The impact on the economy depends on what payout number you start from – last year's extraordinary $7.66, the first forecast of $7 or the second at $6.60/kg ms. Every plus or minus $0.10/kg ms is approx $120m gross farm income on a national basis or an estimated $350 to $500m spent on a multiplier basis. Either way the dollar numbers are starting to be significant for the economy, and a lot will depend on the "behavioural" aspect as the cheque books are shelved.

What is the impact on asset values?

We've noted it on numerous occasions. The expectation of continued high capital gains has been built into the purchase price of farm land. Cash return on capital has been unsustainably low. The last season saw a 40 percent jump in dairy land prices, broadly in line with the jump in the dairy payout, as the market focused on a one-year forward P/E. If a similar methodology is used over the coming season, we'd fully expect to see a sizeable correction in land prices. Attention needs to be wider than dairy land, with other classes of land also dragged up by the dairy factor.

Dairy prices to median dairy land prices



Sources: ANZ National, REINZ

Long-term, the benefits from agriculture have accrued into the price of land as opposed to cash-flow. Traditionalists continue to point to the historical experience that land prices have seldom fallen.

We'd challenge this on two levels. First, this rural land price boom has been the largest we've seen, so "historical" averages or experience seems a little pointless. Second, we'd argue in the current de-leveraging environment (and a once in eighty year event), that the historical "behavioural assumptions" may no longer apply. Successful businesses going forward will need to have far greater emphasis on traditional cash flow and have a bigger margin in the cash flow to provide a buffer for increased risk. This in itself implies potential for a more exaggerated correction in land prices.

While the overall rural balance sheet is solid, there will be pressure in certain pockets. An increased focus on cash combined with the tighter availability of credit will make buyers more choosey over what property they buy and how much they pay for it. We fully expect to see pressure on asset values and a return to more traditional earning ratios. This in itself is a good thing, but obviously not if you paid the top in the market.

In this environment, we expect even more frugal attention to the discretionary spend over a couple of years.

The upshot

Rural (dairy) incomes remain strong relative to history. The real issue is what has been capitalised into asset values. We expect to see considerable belt tightening, both from reduced flow (income) and falls in the value of the stock.

THE REGIONAL GAP

Resource pressures remain, with our regional output gap measures still positive, particularly for South Island regions. This reinforces the inflationary starting position for the economy. However, pressures are reducing, quickly in some instances, and it's synchronised across the country.

The linkage between excess demand and inflation pressure is well known. Economists frequently talk about the "output gap", noting that when the output gap is positive (i.e. actual economic growth exceeds "potential"), inflation pressures build. The period of strong growth recorded in New Zealand in recent years has seen a positive output gap open up and inflation pressures emerge. Seeing these pressures, the Reserve Bank tightened monetary policy by raising the Official Cash Rate.

We have updated our regional output gap measures to examine which regions are responsible for the inflation pressures that persist in New Zealand. To refresh readers' memories, the regional output gaps are estimated using data from the National Bank's *Regional Trends* and *Business Outlook* survey, and Statistics New Zealand's regional unemployment data.[1]

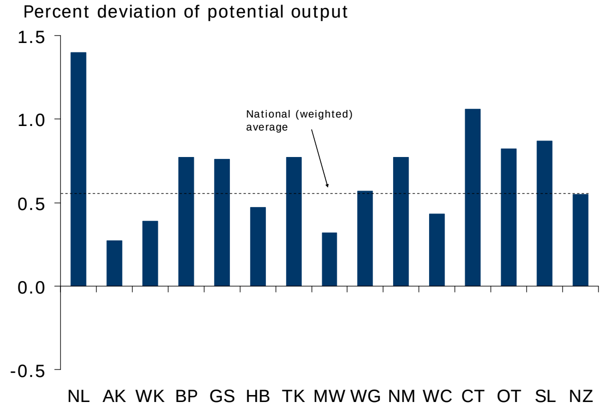
Here are some key messages from this analysis:

> A positive output gap still exists across the country as a whole. The three gap measures we use (activity, unemployment, capacity utilisation) all contributed evenly to the positive nationwide output gap in the quarter.

> All 14 regions reported a positive output gap in the September quarter, reinforcing the widespread nature of resource pressure. However, there was more disparity at the component level and it is interesting that some regions have started to record negative capacity utilisation gaps.

> The Auckland region recorded the lowest output gap in the September quarter, which is not surprising given the slowdown occurring in the housing market and other consumer-related sectors. Northland was again the standout to the other extreme, with an output gap much larger than most other regions. This is largely a result of still high capacity utilisation reported in that region. With the exception of the West Coast, all South Island regions are recording average output gaps above the national level, with Auckland, Waikato, Hawke's Bay and Manawatu-Wanganui the weakest of the North Island regions.

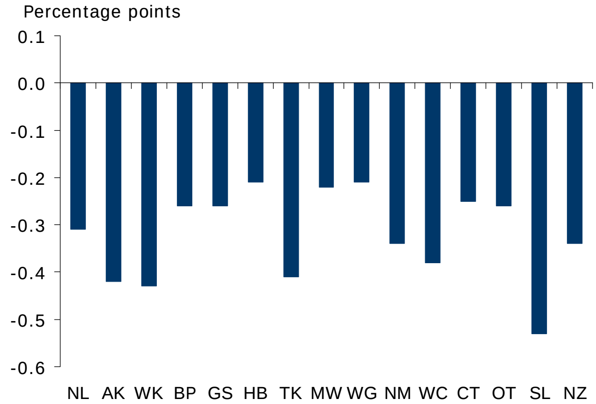
Estimate average regional "output gap" in Sep 08



Sources: ANZ National

> All the regions experienced a reduction in capacity pressures in the September quarter, with the Southland, leading the charge.

Change in regional output gaps over the past quarter



Sources: ANZ National

The upshot

While still positive, our output gap measures show that capacity pressures are easing across the country and in a reasonably widespread manner. This in itself is telling us something: the economy is now clearly into a synchronised downturn. Admittedly, the degree of easing is not as intense or aggressive as a lot of conventional and solely demand derived estimates (such as de-trending GDP) would suggest. But with confidence surveys now clearly flagging employment as the next leg to go, we expect the pace of easing to intensify going forward.

Note: NL=Northland, AK=Auckland, WK=Waikato, BP=Bay of Plenty, GS=Gisborne, HB=Hawke's Bay, TK=Taranaki, MW=Manawatu-Wanganui, WG=Wellington, NM=Nelson-Marlborough, WC=West Coast, CT=Canterbury, OT=Otago, SL=Southland.

[1] The estimates are generated using estimates of the output gap, unemployment gap (utilising Okun's Law) and a derived capacity utilisation gap from the National Bank business confidence survey. We chose a broad approach for two reasons. First it minimises some of the error that may surround simple regional activity statistics (which are only partial indicators). Second, the Reserve Bank uses a similar combination to derive its multivariate filter measure of the output gap for the entire economy. For each input we use a band-pass filter to derive the business cycle – a standard statistical technique that is available on modern statistical software. Individual output gap measures across activity, unemployment and capacity utilisation for each region are then given an equal weighting

GLOBAL WATCH

Data was mixed across the globe last week, although some key US leading gauges continue to slow sharply, as does the labour market. Inflation appears to have well and truly turned, with CPI data lower than expected in the US, UK and Hong Kong last week.

Country / Area	Indicator	Mkt	Actual	Last	Outturn vs market
US	Industrial Production (Oct) – mom	0.2%	1.3%	-3.7%	Stronger
	Producer Price Index (Oct) – mom	-1.9%	-2.8%	-0.4%	Weaker
	Net Long-Term TIC Flows (Sep)	$27.2B	$66.2B	$21.0B	Stronger
	NAHB Housing Market Index (Nov)	14	9	14	Weaker
	Consumer Price Index (Oct) – mom	-0.8%	-1.0%	0.0%	Weaker
	Housing Starts (Oct)	780k	791k	828k	Stronger
	Continuing Jobless Claims (w/e Nov 9)	3900k	4012k	3903k	Weaker
	Philadelphia Fed (Nov)	-35.0	-39.3	-37.5	Weaker
	Leading Indicators (Oct)	-0.6%	-0.8%	0.1%	Weaker
Euro-zone	PMI Manufacturing (Nov A)	40.5	36.2	41.1	Weaker
	PMI Services (Nov A)	45.0	43.3	45.8	Weaker
UK	CPI (Oct) – mom	0.1%	-0.2%	0.5%	Weaker
	Retail Sales (Oct) – mom	-0.9%	-0.1%	-0.5%	Stronger
	Public Finances (PSNCR) (Oct)	-2.5B	-4.9B	12.9B	Weaker
	M4 Money Supply (Oct P) – mom	0.8%	2.3%	1.7%	Stronger
Asia Ex-Japan					
Hong Kong	Unemployment Rate (Oct)	3.6%	3.5%	3.4%	Stronger
	CPI – Composite Index (Oct) – yoy	1.9%	1.8%	3.0%	Weaker
Singapore	Non-Oil Domestic Exports (Oct) – mom	-0.5%	-7.4%	-0.9%	Weaker
	GDP (3Q F) – qoq	-0.5%	-0.6%	-0.5%	Weaker
Thailand	Customs Exports (Oct) - yoy	-	5.2%	19.4%	-
	Customs Imports (Oct) - yoy	-	21.7%	39.4%	-
Philippines	Overnight Borrowing Rate	5.75%	6.00%	6.00%	Stronger
Indonesia	GDP (3Q) – qoq	3.38%	3.54%	2.49%	Stronger
Japan	GDP (3Q P) – qoq	0.0%	-0.1%	-0.9%	Weaker
	Leading Index CI (Sep F)	89.4	89.4	89.2	In-line
	All Industry Activity Index (Sep) – mom	-0.1%	-0.1%	-1.7%	In-line
	BoJ Target Rate	0.30%	0.30%	0.30%	In-line
Australia	Retail Sales Ex Inflation (3Q)	0.4%	0.1%	-0.2%	Weaker
	Westpac Leading Index (Sep) – mom	-	-1.0%	-0.%	-

INTEREST RATE STRATEGY

Interest rate markets rallied hard last week, both here and abroad. US Treasury bond yields dropped to a 45 year low last week, and with the RBNZ set to take the OCR to a historic low, we expect NZ interest rates to make new ground too. Inflation hasn't been completely eradicated, but it's no longer the primary concern.

Market themes…

> Global interest rate market sentiment has shifted quickly. Markets are no longer worrying that high inflation will limit central bank's capacity to cut rates, and are now starting to fret about deflation.

> While deflation isn't something we expect in NZ, the impact fear that it is having on global markets will be felt here.

> While it is appropriate that global yield curves are positively sloped, many had steepened in anticipation of a recovery, which we always felt wouldn't be forthcoming quickly.

Review and outlook …

The past week has been a momentous one. Just about any market you can think of is at a cyclical low at the moment, or just off it. What's more, it's no coincidence, and it all relates to the inevitable de-leveraging that must occur following the credit binge of the last seven years. NZ interest rates have followed global trends closely, and given the likelihood that the RBNZ takes the OCR to a new low this cycle, we see no reason why term interest rates won't make new lows this time around. This obviously stands to reason at the short end, which is more policy dependent. However, it looks likely at the long end too given both the synchronised nature of the global slowdown, and rapidly falling inflation expectations, which are a key determinant of long bond yields.

Given developments on the global inflation front, it's hardly surprising that long bond yields have fallen so rapidly. Similarly, it's not surprising that yields curves like the US have flattened significantly (although they remain at historically "steep" levels). We always felt the rapid steepening since mid September was always difficult to explain. Steepening is an inevitable part of the easing cycle, because long rates need to consider more than just the next cycle. But if the recovery is delayed, or set to be muted, then caution is warranted. We therefore expect global yield curves to continue to flatten (but remain positive) over the next few months as a slow recovery gets priced in. This phenomenon will also be at work in NZ too, and will help shift the entire term structure of interest rates lower, possibly beyond previous lows.

Borrowing strategies we favour at present

The entire term structure of New Zealand interest rates has collapsed over the past week. As a result, all wholesale interest rates from 3mth BKBM through to the 10yr swap are now below 6 percent. Despite the large falls seen to date, and the fact that most swap rates are now approaching post-OCR regime lows, the economic outlook suggests there's a very real possibility that swap rates will move to new lows this cycle. Not only do we expect the cash rate to go below previous lows, but the prospect of a slow recovery means that term interest rates are also much more likely to fall, as we've witnessed in the US market. Stick with the "game plan" and keep duration as short as possible.

Gauges for NZ interest rates

Gauge	Direction	Comment
RBNZ	↓↓	RBNZ unlikely to disappoint market. Calls for a 150bp cut are getting louder.
NZ data	↔/↓	2nd tier data last week didn't add to picture. *NBBO* this week will be a timely gauge.
Fed Funds/ front end	↔/↓	US bond yields are rallying hard, making historic lows.
RBA	↔/↓	Another 100bp cut in Dec puts pressure on RBNZ.
US 10 year	↔/↓	Expected rally has occurred, and is likely to continue.
NZ swap curve	↔/↑	Very gradual steepener. Will be a typical "bull steepener"
Flow	↔/↓	One way street – receivers.
Technicals	↔	6% was no barrier, 5% looms large for the NZ 2yr.

Market expectations for RBNZ OCR (bps)

OCR dates	Last week	This week
Thu 4-Dec-08	-105	-114
Thu 22-Jan-09	-170	-185
Thu 5-Mar-09	-213	-221
Thu 23-Apr-09	-223	-244
Thu 4-Jun-09	-223	-243
Thu 30-Jul-09	-214	-241
Thu 10-Sep-09	-208	-239

Trading themes we favour at present

The long awaited rally in US 10yr Treasuries finally occurred last week, and with a vengeance. As a result, the NZ/US 10yr spread (swap) has widened to around 252bps, which is worth considering as a narrowing trade. Stick with yield curve steepeners, although the pace of steepening is likely to slow as the long end reacts to global moves, and the likelihood of a more drawn out recovery. 12mth OIS still looks cheap, and will perform well if the RBNZ deliver a 150bp cut, which is a possibility.

THE IMPACT OF THE RBNZ'S NEW LIQUIDITY ARRANGEMENTS

Recent changes to New Zealand's liquidity arrangements have had a material impact on money market interest rates. Since the announcement of the Term Auction Facility and the reintroduction of the Reserve Bank Bill tenders, the bellwether 3mth BKBM FRA rate has fallen by 87bps. While a part of that fall can be explained by expectations of more aggressive policy easings, a good chunk of it comes down to improved liquidity.

Recent changes

The RBNZ has taken a number of steps to improve liquidity since the "credit crunch" began. These changes have included widening the range of acceptable collateral, a government guarantee on certain types of bank funding, the creation of swap lines with the US Federal Reserve, and most recently, the introduction of two new facilities – the Term Auction Facility (TAF), and Reserve Bank Bill tenders (which were announced on November 7th, and became operational on November 12th). The RBNZ has stated that it intends to use the TAF to inject cash on a weekly basis, against eligible collateral, for terms out to 12 months. Following each TAF, the RBNZ will then withdraw liquidity via an RB Bill tender, typically offering bills of terms around 3 months. The RBNZ has said that this latter operation will be used to partly or fully sterilise cash injected via the TAFs.

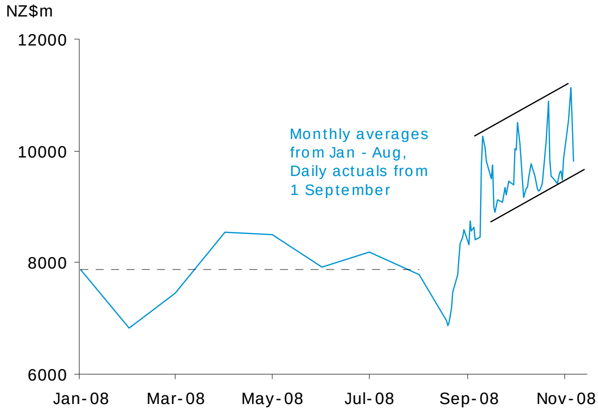
The detail

At first glance, the fact that the TAFs and the RB Bill tenders are being conducted in conjunction with one another would seem to suggest their impact may be muted. However there are some important aspects to note. First, the arrangements give the RBNZ the ability to inject more liquidity. Although the RB Bill tenders allow the RBNZ to withdraw liquidity injected via the TAFs, there is no obligation to do so. Second, the terms of the TAFs will typically be longer (out to 12 months) than the terms of the RB Bills tendered (typically 3 months). This should reduce the term premium in interbank funding. Third, by offering to inject liquidity against a wide range of collateral, and offering to withdraw liquidity via the sale of risk free assets, it's reasonable to expect credit spreads to narrow. Finally, the RBNZ has committed to keeping these facilities in place for 12 months (although they may be reviewed sooner if the situation improves). This adds credibility and confidence to the process.

Market Impact

The major change that has occurred since the TAF and RB Bill tenders have become operational has been the increase in settlement cash. As the chart below shows, daily settlement cash in the banking system has risen from an average of $7.9bn (dotted line) over the 8 months till the end of August to over $11bn last week.

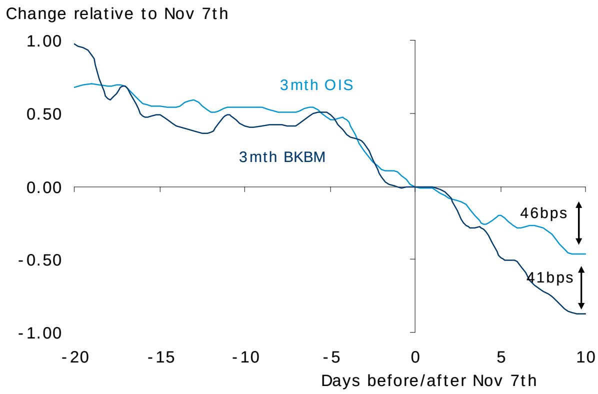
RBNZ Settlement Cash



Sources: ANZ National, RBNZ

So far the RBNZ have conducted two TAFs and two RB Bill tenders (on 12th and 19th November). The first TAF was for $500m and the second was for $1500m, making for a net injection of $2bn. By contrast, the first RB Bill tender was for $700m and attracted no bids, while the second, for $1000m attracted $975m of bids. As a result, these operations have injected a net $1025m. However, given the RBNZ conduct open market operations on a daily basis, it would be a mistake to observe these operations in isolation. That being said, the overall trend for settlement cash to rise is clear, as has the impact on money market interest rates. The other major factor driving interest rates lower has been changing expectations for the path of monetary policy. So while we noted that the bellwether 3mth BKBM rate had fallen 87bps since the RBNZ's November 7th announcement, not all of that is a result of improved liquidity. We estimate that 41 of the 87bps is a result of improved liquidity, and 46bps is as a result of expectations of looser policy, as the chart below demonstrates.

Changes in NZ Interest Rates



Sources: ANZ National, Bloomberg

CURRENCY STRATEGY

Despite a late week recovery, sentiment towards the NZD remains weak, and US equity movements continue to dictate the kiwi's direction. Any short-term rebounds should be treated as such, with the medium-term trend still pointed downwards.

Market themes…

> US equity market continues to dictate currency moves.

> US data continues to deteriorate, but USD still benefiting from safe-haven flows.

> Optimism surrounding pick for US Treasury Secretary likely short-lived.

Review and outlook…

Equity markets continue to dictate NZD movements and we see little change on the horizon. The economic dataflow continues to disappoint, and the hangover from the US big-three automaker's fate tied to a US$25b bailout being considered by the Senate did not help sentiment either. News that Timothy Geithner, current head of the US Federal Reserve Bank of New York, will be the next US Treasury Secretary helped lift sentiment. But as we have seen so often this past year, brief bouts of optimism proved to be short-lived.

So while the NZD managed to avoid heading below the key 0.52 level against the USD for now, sentiment towards the kiwi remains weak. The domestic newsflow points to what is to come – lower forecast dairy payout, more announced job cuts and a reduction in international air capacity due to lower demand from offshore. Given the still large external imbalance facing the economy, the big picture is pointed towards the NZD staying lower for a while.

But as always, we will not be seeing the NZD move lower in a straight line. We continue to remain wary of the potential for a short-squeeze higher and expect attention to return to the USD at some stage, particularly when it becomes increasingly clear that the US economy is set for big contractions in Q4 and possibly Q1 next year. After falling so far so fast, the possible rebound could take the NZD towards the 0.56-0.58 range. This is especially so with real money managers still sitting on a net short position on the NZD. Another possible cause for a near-term rebound in the NZD is the AUD. Though it has been dealt more harshly than the NZD because it has been singled out as a play on global recession fears, at least there is some support for the AUD in the form of the RBA, who have been very active in providing "liquidity" in the low 0.60s region. With so much bad news priced into the AUD, it is ripe for a big squeeze higher should the economic dataflow not come in as bad as feared, dragging the NZD up with it. But we remain of the view that the NZD will continue to underperform the AUD, given that it is the NZ economy that enters the global credit shock in a more vulnerable state compared to Australia.

Technically, the NZD's first resistance now is at 0.5460 which we expect to be tested early in the week with 0.5340 then 0.5280 to support the down side. The NZDAUD cross has a very defined range of 0.8400-0.8630 which should contain for the week ahead. The NZDEUR has broken below the key 0.4300 level, suggesting the USD strength of late is starting to wane with EUR the first currency to stabilise.

NZD vs AUD: monthly directional gauges

Gauge	Direction	Comment
Fair value	↓	Should be lower based on fundamentals.
Yield	↔/↓	Both RBNZ and RBA expected to ease aggressively.
Commodities	↔	Same for both.
Partial indicators	↓	NZ indicators still worse but Australia's not far behind?
Technicals	↔/↓	0.84-0.8630 range to hold.
Sentiment	↔	Risk appetites very fickle.
Other	↔/↓	RBA very active in market.
On balance	↓	**Should be lower but subject to global scene**

NZD vs USD: monthly directional gauges

Gauge	Direction	Comment
Fair value – long-term	↔/↓	Fair value estimate revised down to low 0.50s given external imbalance.
Fair value – short-term	↔/↓	Still above cyclical fair value level.
Yield	↔	Markets toying with greater than 100bps from RBNZ.
Commodities	↓	Dairy prices fell again.
Risk aversion	↔/↓	Fragile and fickle.
Partial indicators	↔/↓	Weak.
Technicals	↔/↓	0.5460 resistance to be tested.
AUD	↔/↓	AUD still looking vulnerable.
Sentiment	↔/↓	Very weak.
Other	↑	Still a US problem at heart.
On balance	↔/↓	**Near-term bounce possible but medium-term still bearish.**

DATA AND EVENT CALENDAR

Date	Country	Data/Event	Mkt.	Last	Time (NZDT)
24-Nov	GE	IFO - Business Climate (Nov)	88.7	90.2	22:00
		IFO - Current Assessment (Nov)	96.8	99.9	22:00
		IFO – Expectations (Nov)	81.0	81.4	22:00
	EC	Current Account SA (Sep)	-	-8.4B	22:00
		Industrial New Orders (Sep) - mom	-2.8%	-1.2%	23:00
25-Nov	US	Existing Home Sales (Oct)	5.00M	5.18M	04:00
		Existing Home Sales (Oct) - mom	-3.5%	5.5%	04:00
	NZ	**RBNZ 2-year Inflation Expectation**	**-**	**3.0%**	**15:00**
	JN	BoJ Monthly Report	-	-	18:00
	GE	GDP (3Q F) - qoq	-0.5%	-0.5%	20:00
		GfK Consumer Confidence Survey (Dec)	1.5	1.9	20:10
	UK	Total Business Investment (3Q P) - qoq	-1.9%	-1.0%	22:30
		BOE's King, Gieve, Bean, Barker, Sentance to Testify	-	-	22:45
	EC	OECD November Economic Outlook	-	-	23:00
26-Nov	US	GDP (Annualized) (3Q P)	-0.5%	-0.3%	02:30
		Personal Consumption (3Q P)	-3.1%	-3.1%	02:30
		GDP Price Index (3Q P)	4.2%	4.2%	02:30
		Core PCE (3Q P) - qoq	2.9%	2.9%	02:30
		S&P/CS Composite-20 (Sep) – yoy	-16.9%	-16.6%	03:00
		Consumer Confidence (Nov)	38.0	38.0	04:00
		Richmond Fed Manufacturing Index (Nov)	-26	-26	04:00
		House Price Index (Sep) - mom	-0.7%	-0.6%	04:00
	EC	ECB's Bini Smaghi Speaking in Madrid	-	-	06:00
	AU	DEWR Skilled Vacancies (Nov) - mom	-	-3.7%	13:00
		Construction Work Done (3Q)	-	-2.6%	13:30
	UK	GDP (3Q P) – qoq	-0.5%	-0.5%	22:30
27-Nov	US	Durable Goods Orders (Oct)	-3.0%	0.8%	02:30
		Durables Ex Transportation (Oct)	-1.5%	-1.1%	02:30
		Personal Income (Oct)	0.1%	0.2%	02:30
		Personal Spending (Oct)	-1.0%	-0.3%	02:30
		PCE Core (Oct) – yoy	2.2%	2.4%	02:30
		PCE Core (Oct) – mom	0.0%	0.2%	02:30
		PCE Deflator (Oct) - yoy	3.3%	4.2%	02:30
		Initial Jobless Claims (w/e Nov-23)	531K	542K	02:30
		Continuing Claims (w/e Nov 16)	4075K	4012K	02:30
		Chicago Purchasing Manager (Nov)	37.0	37.8	03:45
		U. of Michigan Confidence (Nov F)	57.5	57.9	04:00
		New Home Sales (Oct)	442K	464K	04:00

Continued over page

Date	Country	Data/Event	Mkt.	Last	Time (NZDT)
27-Nov cont.	**NZ**	**Trade Balance (Oct)**	**-1000M**	**-1183M**	**10:45**
		Imports (Oct)	**4.37B**	**4.35B**	**10:45**
		Exports (Oct)	**3.42B**	**3.17B**	**10:45**
		NBNZ Business Confidence (Nov)	**-**	**-42.3**	**15:00**
		Money Supply M3 (Oct) - yoy	**-**	**6.6%**	**15:00**
	JN	BoJ Monetary Policy Meeting Minutes for Oct. 14 and Oct. 31	-	-	12:50
	AU	Private Capital Expenditure (3Q)	-	5.7%	13:30
	GE	ILO Unemployment Rate (Oct)	7.1%	7.1%	20:00
		Unemployment Change (000's) (Nov)	-5K	-26K	21:55
		Unemployment Rate (Nov)	7.5%	-	21:55
	EC	Money Supply M3 (Oct) – yoy	8.1%	8.6%	22:00
		Business Climate Indicator (Nov)	-1.57	-1.34	23:00
		Consumer Confidence (Nov)	-25	-24	23:00
		Economic Confidence (Nov)	78.3	80.4	23:00
		Industrial Confidence (Nov)	-21	-18	23:00
		Services Confidence (Nov)	-8	-6	23:00
28-Nov	**NZ**	**Building Permits (Oct) - mom**	**-**	**8.4%**	**10:45**
	JN	Nomura/JMMA Manufacturing PMI (Nov)	-	42.2	12:15
		Jobless Rate (Oct)	4.2%	4.0%	12:30
		Household Spending (Oct) - yoy	0.82	-2.3%	12:30
		National CPI (Oct) - yoy	1.7%	2.1%	12:30
		National CPI Ex-Fresh Food (Oct) - yoy	1.3%	2.3%	12:30
		National CPI Ex Food, Energy (Oct) - yoy	0.3%	0.2%	12:30
		Industrial Production (Oct P) - mom	-2.5%	1.1%	12:50
		Retail Trade (Oct) - mom	-0.9%	-0.5%	12:50
		Vehicle Production (Oct) - yoy	-	4.2%	17:00
		Housing Starts (Oct) - yoy	29.5%	54.2%	18:00
		Construction Orders (Oct) - yoy	-	10.30%	18:00
	UK	GfK Consumer Confidence Survey (Nov)	-37	-36	13:01
	AU	Private Sector Credit (Oct) - mom	-	0.7%	13:30
		HIA New Home Sales (Oct) - mom	-	-1.8%	13:30
	EC	CPI Estimate (Nov) - yoy	2.4%	3.20%	23:00
		Unemployment Rate (Oct)	7.6%	7.50%	23:00

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: Domestic data remains very weak and likely to confirm that the economy is not yet at the trough. The big releases prior to the RBNZ's *Monetary Policy Statement* at the start of December are the National Bank *Business Outlook,* and the RBNZ's Survey of Expectations this week. Further out, we will receive the final partial indicators for Q3 GDP and these should reinforce the likelihood of another contraction.

Date	Data/Event	Economic Signal	Comment
Tue 25 Nov (15.00)	RBNZ Survey of Expectations (Q4)	Still high but easing	Lower petrol prices should see inflation expectations fall from the last read of 3.0 percent. They will still be high, but at least head in the right direction.
Thu 27 Nov (10.45)	Overseas Merchandise Trade (Oct)	Deficit	Another large monthly trade deficit is expected. We will be watching for signs of a capitulation in imports.
Thu 27 Nov (15.00)	NBNZ *Business Outlook* (Nov)	-	-
Thu 27 Nov (15.00)	Credit Growth (Oct)	Another record low?	September housing lending growth was the weakest on record. Given the state of the housing market, we would not rule out a further slowing.
Fri 28 Nov (10.45)	Building Consents (Oct)	Soft, watch commercial	The level of residential dwelling consent issuance will remain subdued. The bigger focus will be commercial issuance and we expect it to show further signs of easing.
Wed 3 Dec (15.00)	ANZ Commodity Price Index (Nov)	-	-
Thu 4 Dec (09.00)	RBNZ *Monetary Policy Statement*	100 basis point cut	While the domestic economy remains very weak, the global backdrop is dominating at present and warrants another aggressive interest rate cut.
Mon 8 Dec (10.45)	Value of Building Work Put in Place (Q3)	Another large contraction	Residential construction work is again expected to contract sharply in the quarter. Non-residential construction should hold up at a better level.
Wed 10 Dec (10.45)	Overseas Trade Indices (Q3)	Terms of trade down again	While oil prices started to fall in the September quarter, so to did the prices of NZ's commodity exports. This should contribute to another fall in the terms of trade.
circa 11 Dec	REINZ House Sales (Nov)	Sales stabilising, but prices still under downward pressure.	House sales may show some signs of recovery due to more realistic price expectations from vendors as well as lower mortgage rates. However, prices should remain under downward pressure.
Fri 12 Dec (10.45)	Retail Sales (Oct)	Underlying weakness	ECT and Credit Card data will provide some insight, but the underlying trend is likely to remain subdued.
Mon 15 Dec (10.45)	Economic Survey of Manufacturing (3Q)	Weak	Despite a lower NZD, recent PMI surveys have shown the manufacturing sector heading backwards.
Wed 17 Dec (15.00)	Westpac/McDermott Miller Consumer Confidence (4Q)	Pull-back as reality of economic situation hits home.	Following the large rebound in the previous survey, and despite lower petrol prices and mortgage rates, we expect the reality of the economic situation to hit home and for consumer confidence to pull back.
Thu 18 Dec (15.00)	NBNZ *Business Outlook* (Dec)	-	-
Fri 19 Dec (10.45)	External Migration (Nov)	Visitor arrivals likely to head lower.	While net migration has been effectively zero over the past two months, visitor arrivals are now the key to watch. They are likely to continue to head south given the global backdrop.
On Balance		**Key issue is the flow-on from the global scene.**	**Weakness now extending into Q4 and 2009 according to lead indicators.**

SUMMARY OF KEY ECONOMIC FORECASTS

	Dec-07	Mar-08	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10
GDP (% qoq)	0.9	-0.3	-0.2	**-0.5**	**0.3**	**-0.4**	**-0.2**	**0.2**	**0.3**	**0.7**
GDP (% yoy)	3.7	2.2	1.1	**-0.1**	**-0.7**	**-0.8**	**-0.8**	**-0.1**	**-0.1**	**1.0**
CPI (% qoq)	1.2	0.7	1.6	1.5	**-0.2**	**0.1**	**0.7**	**0.8**	**1.0**	**0.6**
CPI (% yoy)	3.2	3.4	4.0	5.1	**3.7**	**3.1**	**2.2**	**1.5**	**2.7**	**3.3**
Employment (% qoq)	0.9	-1.3	1.3	0.1	**-0.6**	**-0.4**	**-0.1**	**0.0**	**0.1**	**0.1**
Employment (% yoy)	2.5	-0.2	0.7	1.0	**-0.5**	**0.4**	**-1.0**	**-1.1**	**-0.4**	**0.1**
Unemployment Rate (% sa)	3.4	3.7	3.9	4.2	**4.7**	**5.1**	**5.5**	**5.8**	**6.0**	**6.3**
Current Account (% GDP)	-8.2	-8.0	-8.4	**-8.4**	**-8.7**	**-8.6**	**-7.5**	**-7.0**	**-6.6**	**-6.5**
Terms of Trade (% qoq)	2.9	4.2	-0.5	**-1.0**	**-2.0**	**-1.6**	**-1.8**	**-1.5**	**-1.1**	**-0.8**
Terms of Trade (% yoy)	8.8	11.6	10.6	**5.6**	**0.5**	**-5.1**	**-6.3**	**-6.8**	**-5.9**	**-5.2**

KEY ECONOMIC INDICATORS

	Feb-08	Mar-08	Apr-08	May-08	Jun-08	Jul-08	Aug-08	Sep-08	Oct-08	Nov-08
Retail Sales (% mom)	-0.7	-1.0	1.3	-1.1	0.9	-0.7	0.4	0.1	..	..
Retail Sales (% yoy)	7.7	-1.0	4.1	1.0	1.5	2.5	-0.9	2.2	..	..
Credit Card Billings (% mom)	0.4	-0.5	-0.3	0.5	-0.1	0.2	-0.2	0.9	-1.1	..
Credit Card Billings (% yoy)	7.5	5.8	5.5	6.0	4.0	4.2	2.4	2.4	1.1	..
Car Registrations (% mom)	-8.0	-12.7	11.4	-13.6	1.5	-6.9	-3.5	10.8	-1.2	..
Car Registrations (% yoy)	1.9	-13.2	-1.0	-20.6	-15.9	-27.1	-30.5	-15.6	-19.9	..
Building Consents (% mom)	-5.9	-14.0	81.4	-42.1	-12.6	-2.0	-6.8	8.4	..	..
Building Consents (% yoy)	-17.5	-27.0	30.6	-26.7	-46.0	-34.4	-42.9	-28.4	..	..
REINZ House Price (% yoy)	0.7	1.6	-1.1	-1.4	-2.2	-1.4	-5.7	-6.1	-4.3	..
Household Lending Growth (% mom)	0.9	0.4	0.4	0.5	0.3	0.3	0.4	0.2	..	..
Household Lending Growth (% yoy)	11.6	10.8	9.9	9.3	8.4	7.7	7.2	6.6	..	..
Roy Morgan Consumer Confidence	116.0	111.7	99.9	89.2	86.5	83.9	91.4	108.6	99.7	98.3
NBNZ Business Confidence	-43.9	-57.9	-54.8	-49.7	-38.7	-43.2	-20.5	1.6	-42.3	..
NBNZ Own Activity Outlook	2.4	-6.4	-3.8	-4.4	-4.0	-8.2	4.7	16.7	-11.4	..
Trade Balance ($m)	243	-43	-293	-169	-215	-804	-846	-1183	..	..
Trade Balance ($m annual)	-4422	-4526	-4604	-4782	-4479	-4475	-4374	-4985	..	..
ANZ World Commodity Price Index (% mom)	1.1	2.0	-0.3	0.9	0.0	1.8	-3.4	-5.1	-7.4	..
ANZ World Commodity Price Index (% yoy)	26.9	26.9	20.7	18.7	11.6	8.7	3.5	-2.1	-10.9	..
Net Migration (sa)	270	550	510	970	460	780	370	-10	10	..
Net Migration (annual)	4643	4678	4666	4931	4732	5201	4938	4403	4329	..

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

SUMMARY OF KEY MARKET FORECASTS

	Actual		Current	Forecast (end month)						
NZ FX rates	Sep-08	Oct-08	24-Nov-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
NZD/USD	0.677	0.613	0.538	0.580	0.550	0.530	0.500	0.490	0.480	0.490
NZD/AUD	0.822	0.881	0.851	0.841	0.809	0.803	0.806	0.845	0.842	0.845
NZD/EUR	0.470	0.458	0.427	0.464	0.451	0.442	0.424	0.430	0.436	0.467
NZD/JPY	72.1	61.9	51.6	55.1	50.6	48.8	48.0	48.0	48.0	49.0
NZD/GBP	0.375	0.360	0.361	0.382	0.367	0.358	0.347	0.350	0.343	0.350
NZ$ TWI	63.9	60.7	55.3	58.5	55.8	54.3	52.5	52.9	52.7	54.2
NZ interest rates	Sep-08	Oct-08	24-Nov-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
OCR	7.90	7.51	6.50	5.50	4.50	4.00	4.00	4.00	4.00	4.50
90 day bill	7.98	7.42	5.84	5.40	4.40	4.30	4.30	4.30	4.30	5.10
10 year bond	5.83	5.87	5.43	5.40	5.30	5.00	5.00	5.30	5.70	5.60
International	Sep-08	Oct-08	24-Nov-08	Dec-08	Mar-09	Jun-09	Sep-09	Dec-09	Mar-10	Jun-10
US Fed funds	2.00	1.00	1.00	0.75	0.75	0.75	0.75	1.00	1.25	1.50
US 3-mth	4.05	3.03	2.16	2.50	2.00	1.80	1.65	1.75	2.00	2.25
AU cash	7.00	6.00	5.25	4.75	4.25	4.00	4.00	3.50	3.50	3.50
AU 3-mth	7.32	5.81	4.43	5.10	4.40	4.20	4.20	3.80	3.80	3.80

KEY RATES

	21 Oct	17 Nov	18 Nov	19 Nov	20 Nov	21 Nov
Official Cash Rate	7.50	6.50	6.50	6.50	6.50	6.50
90 day bank bill	7.03	6.08	5.98	5.87	5.80	5.78
NZGB 07/09	5.50	5.27	5.20	5.17	5.17	4.95
NZGB 11/11	5.60	5.33	5.21	5.12	5.09	4.94
NZGB 04/13	5.74	5.55	5.44	5.32	5.29	5.13
NZGB 12/17	5.92	5.79	5.74	5.62	5.59	5.41
2 year swap	6.34	5.48	5.48	5.43	5.35	5.18
5 year swap	6.49	5.85	5.86	5.83	5.77	5.61
RBNZ TWI	61.2	56.8	56.4	56.3	55.6	54.5
NZD/USD	0.6176	0.5536	0.5512	0.5499	0.5415	0.5277
NZD/AUD	0.8849	0.8551	0.8527	0.8524	0.8486	0.8561
NZD/JPY	62.84	53.85	53.33	53.04	51.82	49.74
NZD/GBP	0.3594	0.3759	0.3678	0.3679	0.3621	0.3575
NZD/EUR	0.4633	0.4402	0.4367	0.4360	0.4331	0.4235
AUD/USD	0.6979	0.6474	0.6464	0.6451	0.6381	0.6164
EUR/USD	1.3330	1.2576	1.2623	1.2613	1.2503	1.2460
USD/JPY	101.75	97.28	96.76	96.46	95.70	94.25
GBP/USD	1.7186	1.4729	1.4986	1.4946	1.4954	1.4759
Oil	74.11	57.18	55.14	54.42	53.64	48.86
Gold	800.60	741.40	740.30	739.10	738.45	749.45
Electricity (Haywards)	14.45	4.95	5.26	5.08	5.83	5.48
Milk futures (US$/contract)	100	89	88	88	88	88
Baltic Dry Freight Index	1292	856	865	859	847	836

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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