Bank of New Zealand

BNZ Weekly Overview

1 June 2006

FINANCIAL MARKETS DATA

	This week	Week ago	4 wks ago	3 maths ago	Yr ago	10 yr average
Official Cash Rate	7.25%	7.25	7.25	7.25	6.75	6.3
90-day bank bill	7.51%	7.51	7.51	7.50	6.99	6.6
10 year govt. bond	5.78%	5.80	5.80	5.70	5.64	6.5
1 year swap	7.46%	7.41	7.39	7.34	6.93	6.7
5 year swap	6.90%	6.82	6.87	6.72	6.48	7.1
NZD/USD	0.632	0.634	0.638	0.663	0.704	.57
NZD/AUD	0.844	0.842	0.839	0.892	0.931	.86
NZD/JPY	71.1	71.5	72.2	76.8	76.4	66.0
NZD/GBP	0.339	0.34	0.349	0.378	0.39	.35
NZD/EURO	0.495	0.496	0.505	0.555	0.571	.509

For addition to our emailing list for Thursday night receipt email "Subscribe WO" to tony.alexander@bnz.co.nz

Monthly Confidence Survey

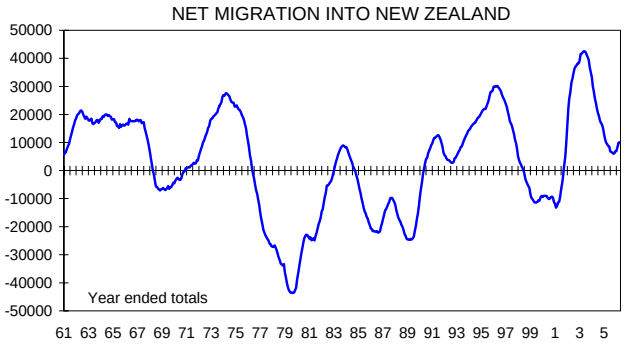
Once again it is time to run our survey of Weekly Overview readers. If time permits and if you have not already done so in the email used to send out the Weekly Overview on Thursday night then please cut and paste the URL below into your browser and let us know whether you believe the economy will get better or worse over the next of months. More importantly let us know how things are at the moment in your industry. Don't be afraid to write a paragraph as long as it is focused on your industry at the moment rather than a general ramble about the economy or the government.

http://www.closer.co.nz/bnzeconomist.asp

Helping You Through the Slowdown

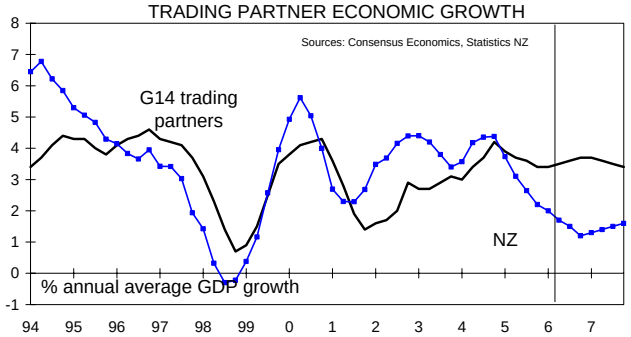
We think it is abundantly clear to everybody now that the New Zealand economy has finished its recent period of unusually strong growth and is tracking along at a below average pace. Slowdowns usually start in the export sector and feed through into the domestic economy. This time around is no exception and even as some parts of the exporting sector are now enjoying better returns as a result of the exchange rate going down we are starting to see greater pain appear in the domestic part of our economy. This also is a normal thing and is something we have specifically been warning about over the past two to three years when talking about the inevitable slowing in growth in New Zealand.

Already we have seen one particular manifestation of this slowing of the domestic sector with the debate about moving to Australia. Many quarters ago we predicted that this debate would appear in the second half of this year having not been around in any strong sense since the 1998 recession. When times tend to get tough here domestically we get indignant at all and sundry around us and in particular the government and start issuing threats to anyone who will hear us that we will move ourselves, our families, and our businesses to Australia. At the same time we get fewer people coming into New Zealand because they don't want to shift to a country wallowing in negativism and the migration numbers inevitably turn down.

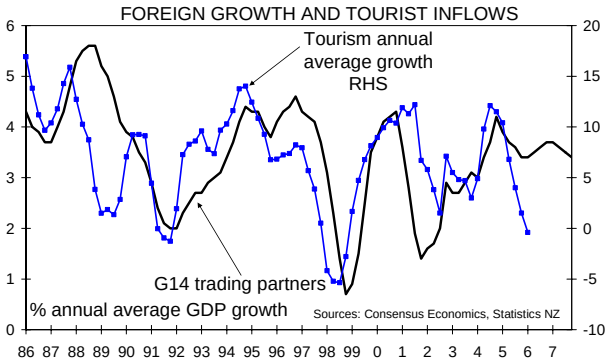


We are not yet convinced that the net migration flows will in fact turn negative this time around, partly because the tight labour market is likely to act as a slight insulating factor on the migration flows this cycle. However following on from the general media commentary surrounding the NBNZ Business Outlook survey released yesterday we have seen a bit more discussion about the economy falling over and things being really rough for an extended period of time. This sort of discussion is going to get worse and many of you are going to feel fairly depressed over the next 12 months.

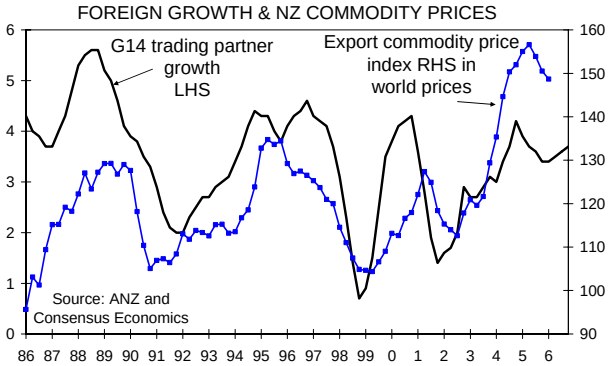
For the past three years we have been explicitly warning about this inevitable period of pessimism in the New Zealand economy and trying to get readers of the Weekly Overview prepared for it by noting the actual slowdown in our economy will not be as bad as people will think simply from reading the newspapers. We have been strongly noting that there are many insulating factors for our economy including relatively low fixed interest rates, high job security, infrastructure spending, easing fiscal policy, and a backlog of construction orders. More recently we have had a particularly important insulating factor come along. This is strong growth in our trading partners. On average they have grown by 3.1% per annum over the past six years whereas we have grown by 3.7% per annum. This year growth is expected to be 3.7% and next year approximately 3.5%.



The strong growth overseas helps explain why the fall in the New Zealand dollar has already led some manufacturers to note that they are receiving increased orders. It also makes us think that the traditional lag between a change in the New Zealand dollar and a change in tourist numbers will be shorter than usual and following what is probably going to be a hefty flow of Australians to our ski fields this winter we are likely to see an increase in general tourist numbers late this year and through the first half of 2007.



The strong growth in our trading partners also means that the scope for further declines in our farm commodity prices is looking increasingly limited. This will not stop farmers from continuing to cut back spending on tractors and suchlike as a period of consolidation is called for after many years of strong growth. But what is significant is that a key sector of our economy which traditionally during the downward leg of the cycle has gotten particularly weak and then hit through to the cities with a vengeance 18 months later is not slipping into a hole this time around.



Going back to the title of this section regarding helping you through this period of worsening pessimism, talk about shifting to Australia, discontent with the government, and the media soon picking up on bad corporate profitability stories, here are a few things to think about when it all looks bad sitting up in bed in the middle of the night.

If you have been in business for longer than six years then you know what a downturn in the New Zealand economy looks like. This means you have probably already taken moves to ensure your cash flows remain reasonable during the period of slow growth. If you have not done so already then turn your eyes away from the revenue statement and look at your expenses. When times are good we tend to lock in place a lot of unnecessary spending justifying it by saying the profit levels are so high it doesn't really matter that I'm getting the most expensive telecommunications or photocopy paper. Go through your expenses line by line and see what you can cut out first in terms of stopping it completely and then in terms of finding a cheaper alternative. A real estate agent spoken to yesterday indicated that this exercise had yielded her savings of $10,000 a month. You may also want to do what a lot of companies are doing at the moment and that is rather than cutting labour costs by laying people off hold on to those people and cut back on capital spending - temporarily at least.

If you have already taken these moves and feel certain that your cash flows will be acceptable over the next 18 months then give thought to what asset acquisition opportunities may appear in the near future. There will be many thousands of people who have only been in business over the past six years when growth has been surprisingly strong. They will currently not be taking any moves to address cash flow problems down the track. They will be maintaining high levels of personal drawings and updating the flash car every 12 months. They will not be noticing that the debtors ledger is getting bigger and the average time taken to pay is starting to blow-out. Some of them are going to fail and you may be able to acquire their business assets, their premises, and their people.

Watch out for forecasts that floating interest rates are going to plummet soon. One thing we have got right over the past two and half years has been our warning about upside risk to floating interest rates brought on by resource shortages in the New Zealand economy combined with the various insulating factors mentioned above. The people who are going to be most pessimistic in the near future are likely to be forecasting major interest rate cuts by the Reserve Bank. But we don't expect the RB to cut interest rates until March next year at the earliest and we see little chance that rates will go anywhere near as low as they did back in 1998. Specifically we think 90-day bank bills will fall from around 7.5% at the moment to perhaps 6% come 2008 rather than low points in the past near 4.75%. So be careful about people saying you should go on a floating rate debt structure at the moment because your costs will plummet very shortly. We doubt it. Instead keep an eye out for attractive fixed interest rates when the markets occasionally rally and recognise for instance that at the moment as a business borrower you can lock in a three year fixed interest rate less than half a percent above its average over the past five years. That's not too bad considering the uncertainty in the New Zealand and world economies at the moment.

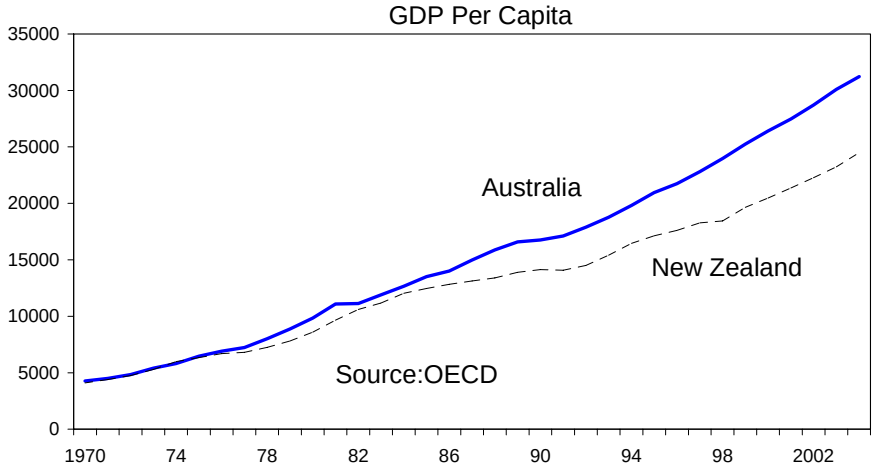
During a slowdown it is natural to think about how one will go about getting extra customers. But don't anticipate that two years down the track we will see a major rebound in the New Zealand economy as we have often seen in the past when a period of slow growth comes to an end. Resource shortages in New Zealand along with the lack of plummeting interest rates and a plummeting exchange rate will limit the speed of the improvement further out. This means it may be wise to take the opportunity over the next few months to consider business growth through better margin management and boosting productivity. The central theme in our talks three years ago when the economy was strong and we were warning about resource shortages was to forsake marketing efforts aimed at getting extra customers and instead boost selling prices because of the difficulties extra customers cause in having to find the resources to service them. Concentrate on what you may do when the economy does get a bit stronger with regard to putting up your selling prices. Even at the moment you may get away with a selling price increase because so many people expect it as a result of rising fuel costs. But more significantly from a strategic planning point of view focus on how you can boost employee productivity through things such as better ICT, premises, and maybe better machinery.

With regard to attracting new customers however take into account the fact that we anticipate slow growth averaging 1.7% per annum in the New Zealand economy over the next three years. A customer acquisition strategy will have to explicitly focus a lot more on getting people to switch from other suppliers to yourself. This may mean shifting your focus away from high brand and product awareness in the marketplace to focusing on how your product and your service is differentiated from alternative providers.

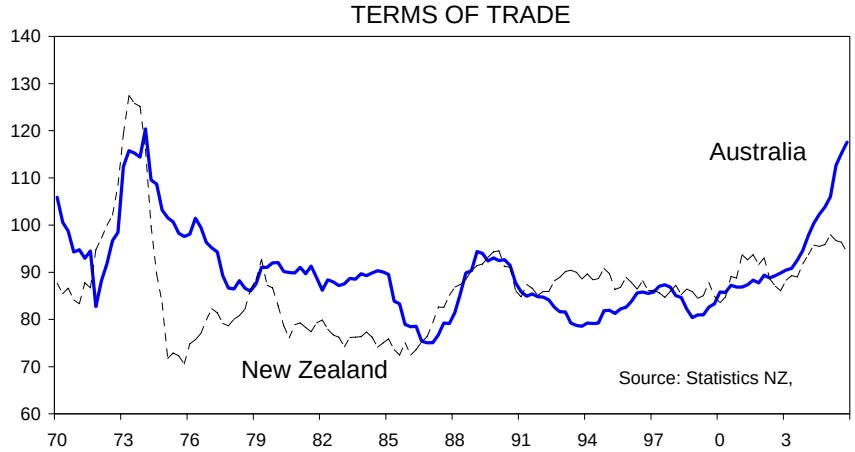
Perhaps the most important thing of all to keep in mind over the next two years while the domestic part of our economy goes through its rough patch is that we have been through this before and we always pop out again on the other side, led by the export sector. Take the opportunity provided by the pullback in customer growth to focus on what has now become a far more important determinant of business success going forward in New Zealand - managing scarce resource availability and raising productivity.

New Zealand versus Australia

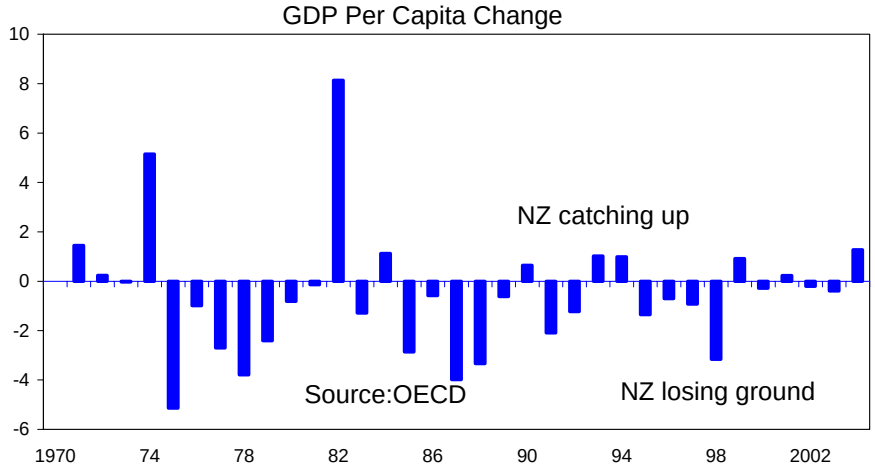
Here's an interesting graph for anyone interested in the progress of the New Zealand economy when compared with Australia. It is based on data from the OECD and shows gross domestic product per capita for both economies adjusted for exchange rate changes and inflation. In a relative sense the rot for New Zealand set in during the 1970s when our policy response to the first oil crisis was particularly bad and the entry of the United Kingdom into the European Community make things extra difficult for us.



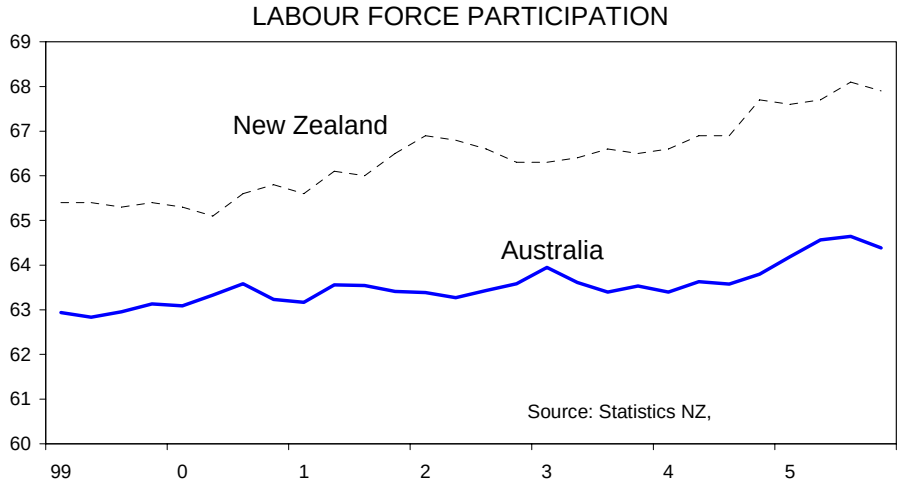
The second graph shows that the shock to New Zealand early in the 1970s was greater than for Australia. The terms of trade measures the size of the basket of imports one can purchase with an unchanging quantity of one's exports. Note the recent divergence in our terms of trade.



Going back to the first graph it looks as though the gap between income per capita in New Zealand and Australia has not been getting wider in recent times. In fact we can track this explicitly by looking at how much that gap changes each year. This is shown in the following graph. Observations below the zero line mean that the gap is widening and New Zealand income as a proportion of Australian average income per capita is getting worse. Recently we have had some positive movements in our favour and the years during which we have got worse the deterioration has not been all that much.



Can one conclude that it looks like per capita income in New Zealand may be catching up with Australia? We don't think so. Over the past six years on average the New Zealand economy has grown by about 3.7% per annum while the Australian economy has grown by about 3.2% per annum. This relatively good growth performance in New Zealand has contributed to the income per capita gap not getting any worse for a while. But we have closed the gap not through higher productivity, or something akin to higher profit per person. Instead we have put a far greater proportion of our working age population to work than in Australia. This is good from the point of view of getting our unemployment rate down but is not repeatable. The graph below shows that since 1999 Australia's participation rate has risen by 1.4 percentage points to 64.4% while New Zealand's rate has risen by 3.1 percentage points to a record 68.5%. Our unemployment rate has fallen from 7.1% at the start of 1999 to 3.9% while Australia's unemployment rate has fallen from a similarly high level of 7.3% but down to just 5.1%. We have only managed to stop the widening of the income per capita debt between New Zealand and Australia for a while by getting more of our relatives off the couch and into work.



Moving to China

Most of us are used to thinking about companies relocating their production facilities to China in terms of taking advantage of low labour costs. This is certainly a very compelling reason. But this week we came across a company which noted another key advantage to locating in China. They said that because of the lower frequency with which ships leave New Zealand ports and go to the destination they want it can take four months between an order being received from the likes of the United States to that product reaching the customer's door. In contrast by relocating their production facilities to China and taking advantage of far greater shipping frequency they have cut that four months down to between four and six weeks with far greater certainty that they will be able to get the product to the customer within a stated period.

Relative Comeliness

Finally at this point in the interests of marital bliss one feels obliged to state that just because one opines on the attractions of moving to Australia in terms of tax cuts and comely wenches* in TV advertisements does not mean that one considers New Zealand females not also to be exceedingly comely. In fact one can say that New Zealand females are very very comely indeed and compare very favourably with their Tasman cousins. Actually one fears the bigger problem in New Zealand is rugby players bearing handbags and blubbering like an Aussie cricketer or Prime Minister when hit with such.

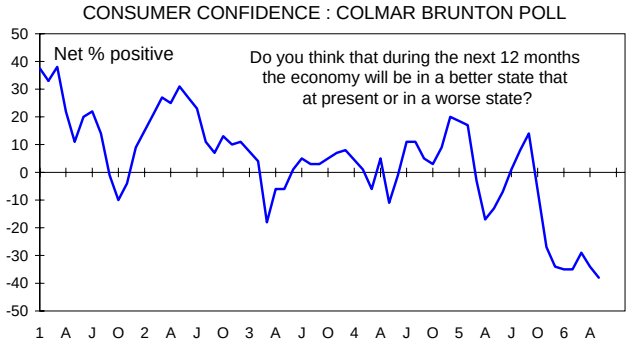
* At a media-covered conference this Tuesday in Christchurch.

THE WEEK'S ECONOMIC DEVELOPMENTS

Monday 29

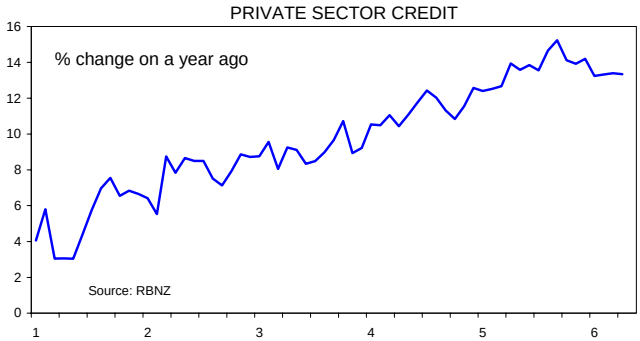
Consumer Confidence Deteriorates

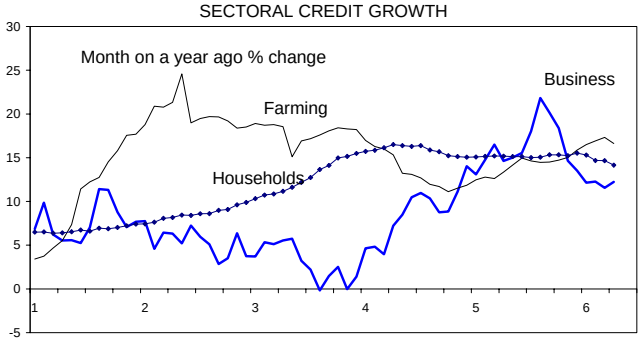
The One News Colmar Brunton poll revealed that during May consumer confidence about the economy over the next 12 months deteriorated to a net 38% pessimistic from a net 29% pessimistic in the last survey undertaken in March. The result is in line with our belief that the fall in the exchange rate while being positive for exporters and generally positively received in the business community is traditionally associated with poor feelings in the household sector. This comes about as people anticipate reduced affordability of overseas travel and expect higher prices for imported goods. For the latest month a contributing factor to the fall in sentiment is likely to be rising petrol prices and worries that they will go even higher.



Lending Growth Slows down

The annual rate of growth in lending to the private sector eased slightly in April to 13.3% from 13.4% in March. A year ago this rate of growth was 13.9% and the recent peak for this measure was 14.6% back in August 2005. So although there is a slowing in lending growth under way it is extremely mild. In seasonally adjusted terms lending to the household sector grew by 0.8% in April. This was a slowdown from growth of 1.1% in March and allowing for the impact of Easter it looks as though the monthly average rate of growth in household lending has slowed to close to 1% from levels nearer 1.2% a month a year ago. The annual rate of growth in lending to the household sector has now slowed down to 14.2% from 14.7% in March, 15.2% a year ago and a recent peak of 15.5% in December. The rate of growth is still relatively respectable and does not indicate any sort of a collapse in consumer spending. Placing this indicator alongside the above piece about consumer confidence falling away shows why we don't base a lot of our economic outlook in the short term on what business and consumer confidence surveys are saying. These surveys can be horribly misleading when it comes to translating them into actual spending decisions.





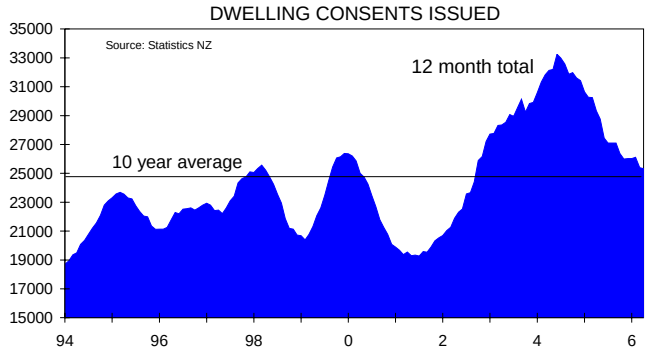
The annual rate of growth in lending to the business sector rose to 12.2% in April from 11.6% in March. This was down from 15.3% a year earlier. In the three months to April the volume of lending to the business sector was $3.1 billion. This was $373 million better than the same period a year earlier and indicates that businesses are not entirely closing up shop when it comes to capital expenditure. This is one area we are

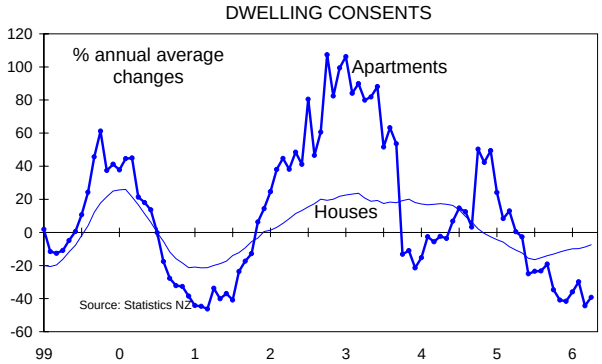
keeping quite a close eye on at the moment. In order to address cash flow concerns businesses are cutting back on capital spending rather than slashing payrolls as has often been the case during downturns in the New Zealand economy. The big question not so much for now but for 2007 is to what extent and with what speed businesses will resurrect their capital spending plans. This is where the government has to send very strong signals regarding infrastructure in particular. If you don't have confidence that the electricity will be there then what is the point of spending a few million dollars on new machinery? And what is the point of installing new computer systems and so on if you don't have confidence that the skilled staff needed to run things are going to stick around in New Zealand rather than shoot through to Australia. The way in which a government contributes to growth in the New Zealand economy these days needs to focus more on making sure key resources are available in a timely manner rather than allocating a few million dollars for improved marketing campaigns overseas. There is no point getting new customer orders if the people aren't there to fill them and in particular fill them at a good quality level.

Wednesday 31

Dwelling Construction Easing off

A downward trend in the number of dwelling consents issued by local authorities around New Zealand has reasserted itself in recent months. In April the seasonally adjusted number of consents issued was down by 6% following a 14.9% fall in March. The decrease means that over the past three months the number of dwelling consents has fallen in seasonally adjusted terms by 3.7% from the three months to January. While the numbers can be moved around quite substantially by large fluctuations in apartment building consents, when we exclude apartment buildings there is also clearly a downward trend in housing construction as well. Over the past three months in seasonally adjusted terms the number of housing consents was down by 5.7% from the three months to January. In the year to April the number of dwelling consents in total issued around the country was 25,330. This was down from 29,329 a year ago and a peak for this cycle of 33,251 in June 2004. That level of consents was the highest since about 1975.





Given that the average number of consents issued per annum over the past decade has been just over 24,500 we are still operating in a relatively strong environment. Our expectation is that with the domestic economy paring back further over the next 12-18 months and the Reserve Bank not cutting interest rates until March next year at the earliest we will see below average numbers of consents being issued shortly. But will it be a crash as such in the home building sector? We expect to see a few developers fall over because that is the nature of their business and many operate on relatively thin margins hoping to flick their properties on quite quickly. But we see little chance that the annual number of consents will fall anywhere near as low as last cycle when they got down to just over 19,000 in the middle of 2001.

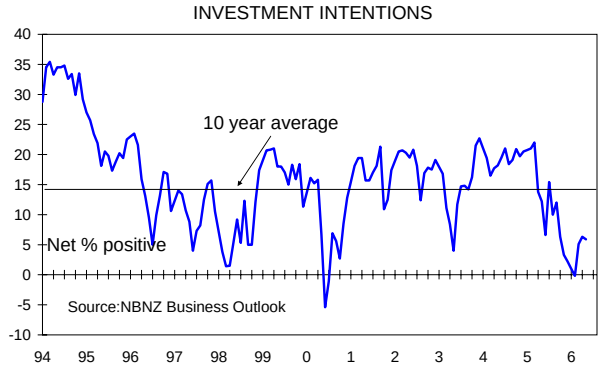
Commercial Construction Also Easing Off

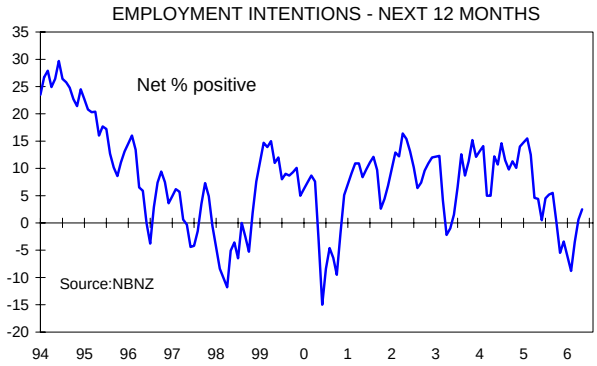
During April the value of non-residential building consents issued was $209 million. This was an 8.3% decrease from a year earlier and means that in the three months to April the value of consents issued was down by 9.3% from a year earlier. Allowing for non-residential construction costs rising about 5% per annum this suggests a volume decline in non-residential construction of over 13% per annum is currently underway. When one looks at individual building types the numbers can move around quite substantially and we think it is best to have a look at six-month blocks. For the country as a whole in the six months to April the value of

consents issued was down by 1.1% from a year earlier. Of relevance to the farming sector the value of farm building consents was up by 6.9%. So some mild growth is still occurring there though that growth rate is a lot less than in earlier years. Consistent with our view that businesses are attacking cash flow concerns by cutting back on capital spending the value of factory consents in the six months to April was down by almost 28% from a year earlier. Consent values for office buildings were down by over 9% while for shops and restaurants they were down by 16%.

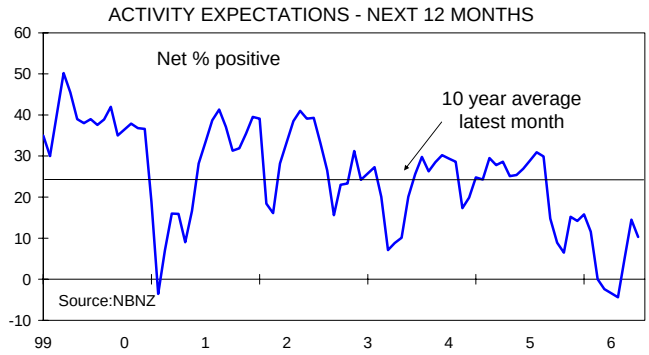
Businesses Remain Very Cautious

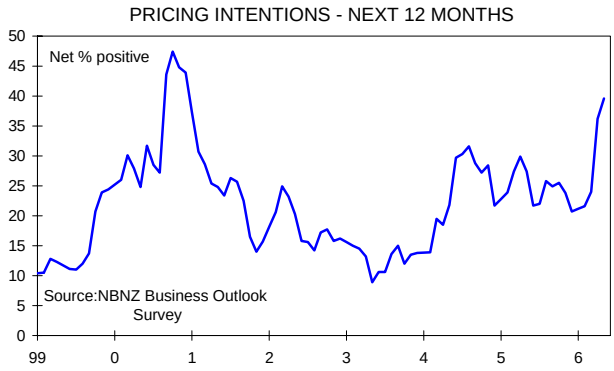
The monthly Business Outlook survey from NBNZ showed a net 31% of businesses in May expected the economy to get worse over the coming 12 months. This was essentially unchanged from the April survey and well below the average confidence reading for the past 10 years of -10%. Backing up our belief that this is not a downturn in the economy which will free up much capacity in the labour market the net proportion of businesses intending to take on fresh labour over the next three months rose to 2.5% from 0.6% in April and a 10 year average for the month of May of 4.8%. Intentions of investing were 5.9% from 6.3% in April and a 10 year average of 13.3%. This measure is not actually as weak as we thought it might be given the evidence of businesses cutting back on capital spending to get cash flows under control.





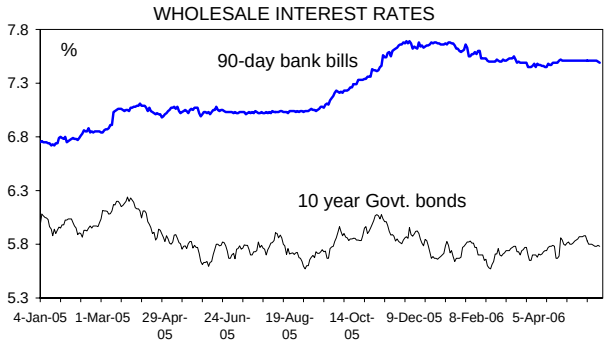
Undoubtedly reflecting the New Zealand dollar's sharp decline against the Australian currency over the past few months the net percent of manufacturers expecting higher exports improved to 37.7% in May from 34.4% in April where the April reading was essentially bang on the 10 year average. A net 10.3% of businesses said they expect their activity levels to pick up over the coming year. This was down from 14.5% in April and the 10 year average of 23%. As such this important indicator along with the subsidiary measures indicates below average growth in the New Zealand economy in the order of 1% to 1.5%. However in spite of the slow growth outlook inflation is a major issue and we doubt that the Reserve Bank will have taken any solace from this particular survey. The net proportion of businesses expecting to raise their selling prices over the coming 12 months rose to a five-year high of 39.6% in May from 36.2% in April and a ten year average of 20.6%. Average year ahead inflation expectations rose to 3.3% from 3.1% in April. An environment in which one's economy grows at a below average rate but inflation chugs along above average can be described as being in a state of stagflation. This is not stagflation as we came to know it during the 1970s when one might be in a recession yet inflation is 10%, but it is stagflation nonetheless.

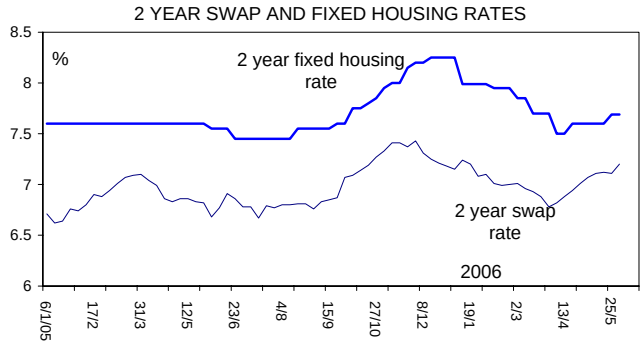




INTEREST RATES

Things are relatively quiet in the wholesale interest rate markets at the moment with no major changes in expectations for New Zealand monetary policy under way and no king hits in either direction from economic data. In the United States the markets are not receiving a string of unusually strong or unusually weak data which could greatly influence the Fed's thinking with regard to any future change in US monetary policy. This therefore is limiting movement in medium to long term fixed interest rates over there as well as an New Zealand. Having said that over the past week we have seen a wee increase in swap rates locally with the two year wholesale fixed borrowing cost rising to around 7.20% from 7.11% a week ago assisted by the Federal Open Market Committee's minutes last night indicating a greater chance of another rate increase in the United States than the markets had been thinking..





If I Were a Borrower What Would I Do?

At the moment our expectation is that the Reserve Bank will cut the official cash rate by 0.25% in March next year. As we approach the timing of the first rate cut we are likely to see short term fixed borrowing costs in the wholesale markets go down. That means that whereas the current two year swap rate is near 7.2% we expect a rate toward 6.5% early next year. Unless we see a large increase in margins this is likely to mean lower short term fixed interest rates come the first half of next year and possibly toward the end of this year as well. Does this mean one should hold off fixing at the moment and wait for a lower interest rate to come along? Probably not because the cost of holding is sitting at a relatively high floating mortgage rate and taking on extra uncertainty. There is of course a chance that with world inflation rising wholesale borrowing costs will not fall as much as we are currently forecasting come the end of this year.

BNZ Fixed Lending Interest Rates

	Housing	Average Past 5 yrs	Low Past	High 5 years
Float	9.55%	8.00%	6.70%	9.55%
1 yr	8.25	7.16	5.95	8.45
2	7.69	7.28	5.99	8.25
3	7.85	7.49	6.30	8.30
4	7.80	7.62	6.40	8.40
5	7.75	7.65	6.50	8.60
7	7.75	7.83	6.75	8.80

Note: Conditions may apply to these rates.

BNZ Term Deposit Rates

Days	$10-50K	$50-100K	$100-250k
30	3.00	3.00	5.25
90	6.20	6.25	6.30
180	6.80	6.85	6.90
1 yr	6.60	6.65	6.70
5 yr	6.10	6.15	6.20

HOUSING MARKET UPDATE

Fresh data may still be a bit thin on the ground but over the past week we have come across two people with slightly unpleasant stories regarding the strength of the housing market. One was a taxi driver. He has been trying to sell an investment property in Devonport since October last year and although cutting the price the place is still sitting on the market. We suggested he take it off the market for a month or so then put it back on because it looks like it's probably become stale. He also noted that he had an apartment in Auckland and recently sold it for $50,000 less than he paid.

Another person bought a set of flats last year for over $2 million and placed his own house on the market hoping to get about $2 million for it but the real estate agents were only bringing forward offers of $1.5 million. He is contributing about $1000 a week over and above what he receives in rents in order to service the mortgage on the flats and wondered whether he should sell the house now and get rid of the mortgage. We suggested that as long as he is reasonably certain about his cash flows over the next few years he may as well hold on to the properties and should get a capital gain further down the track. He was thinking of selling in 2010 and we said that didn't sound too unreasonable.

Speaking of 2010, apparently one commentator in the housing market is predicting that the next cyclical upturn in the housing market will occur in 2011. Given that that is five years away from now anything is possible so it's hard to take a strong position for such a view or against it. But apparently one thing he is saying is that in order to best profit from this next cyclical upturn one should at the moment buy twice as many houses as one thinks will be needed in order to meet one's particular goals over the medium to long-term. If a cyclical upturn is starting or if one is at what clearly appears to be a low point in the housing cycle then adopting such a strategy could be useful as long as one is highly confident that alternative cash flows will be available in case tenants prove hard to find or rent projections prove over-optimistic.

But we are not on the brink of a cyclical upturn, as he notes, and we are also not anywhere near the low point for this housing cycle. It seems far wiser to wait until that low point comes along before taking a risky, probably heavily debt financed, residential property position rather than adopting such a position at the moment when a cyclical downturn is only just getting under way.

Rent Expectations

Speaking of rent projections some people have forwarded the view that with house prices having gained on average 85% over the past five years while rents on average have only risen by 12% we are going to have a period of strong rental catch-up in the next two to three years which will restore yields on residential property back toward historical norms. The term Buckleys and none springs to mind once again. We are forecasting below average growth in the New Zealand economy over the next three years with the unemployment rate rising marginally while consumer confidence for much of the period is relatively weak and household income growth also on the weak side. We expect the recent improvement in net migration flows to reverse and deliver below average population growth in the next three years. We note that at the moment dwelling construction is still running at above average levels.

In this sort of environment it is very difficult to imagine rents rising by all that much. Instead, if residential property yields are to return to anywhere near where they used to be it is more likely to be through house prices either falling or sitting flat for an extended period of time while average rents perhaps rise at the rate of inflation. In reality we don't think average yields will return to where they were a few years ago. We believe a structural decline in yields on assets such as commercial and residential property has occurred with assistance from the likes of increased offshore investment in both sectors plus baby boomers getting themselves set for retirement.

Finally, just a reminder. If you are still thinking that house prices are rising at about a 10% per annum rate then think again. On average over the past three months the median dwelling sale price reported by REINZ has risen by 0.8% compared with the three months to January. This works out at an annualised house price

inflation rate of just over 3.1%. Given that inflation is running at 3.3% one could technically say that real house prices are already falling.

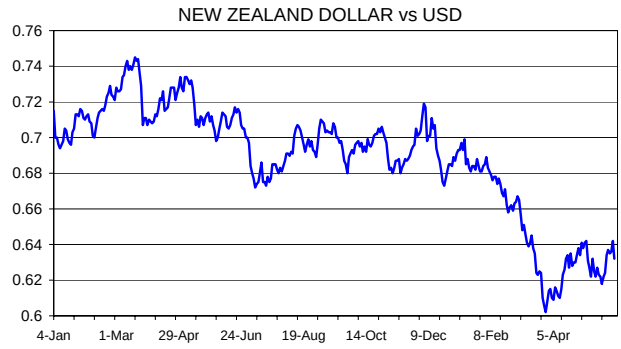
EXCHANGE RATES

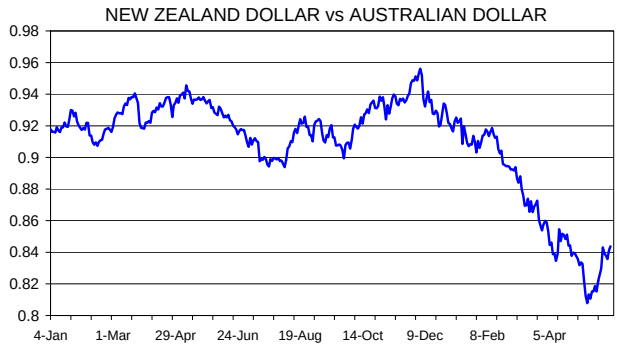
We are aware that toward the end of last year a great number of people took out foreign exchange contracts which would allow them to profit if the Kiwi dollar fell away. With the Kiwi dollar falling quite sharply in the first half of this year these people in most cases will be sitting on profits. The recent pullback in the exchange rate has led one or two people to ask us whether they should cut out of their contracts now or whether they should hold them to maturity - whenever that may be. Our opinion is that forecasting exchange rate movements over very short periods of time is essentially impossible and best left to those in the likes of dealing rooms who make it their profession. The recent recovery in the New Zealand dollar does not surprise us given the speed at which it fell in the early part of this year. In particular we believe there are many people who are unwinding positions put in place earlier involving buying the Australian dollar and selling the New Zealand dollar. At the moment they are closing these positions by selling Aussie dollars and buying New Zealand dollars and applying in particular strong upward pressure on the Kiwi Aussie cross rate.

This process may have just about reached its end but that does not give us any major insight into where the Kiwi dollar is going to go in the short term. Our expectation however is that over the next 12 to 18 months we will see further weakness in the New Zealand dollar on the back of steadily growing investor disappointment in New Zealand's low economic growth rate at a time of above average growth overseas and in particular in Australia, many billions of dollars worth of maturing Uridashi bond issues, and over 2007 a shrinking interest-rate differential.

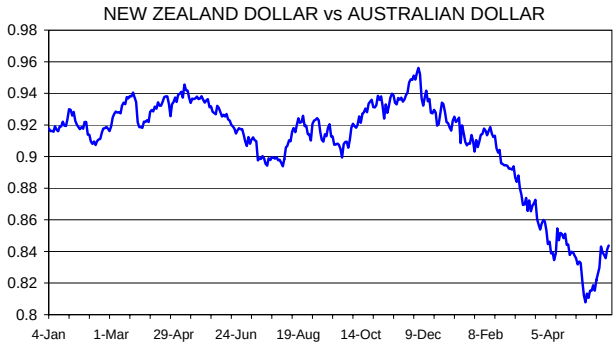
If one has a foreign exchange contract which matures within the next two to three months then one might consider cutting out of it when the Kiwi dollar next falls by two or three cents. But if one has a contract maturing, let's say in the first half of next year, then given the fundamentals we have just listed above it would seem best to avoid trying to make any decision on that at the moment and letting these various forces come into play and probably push the New Zealand dollar lower come the end of the year.

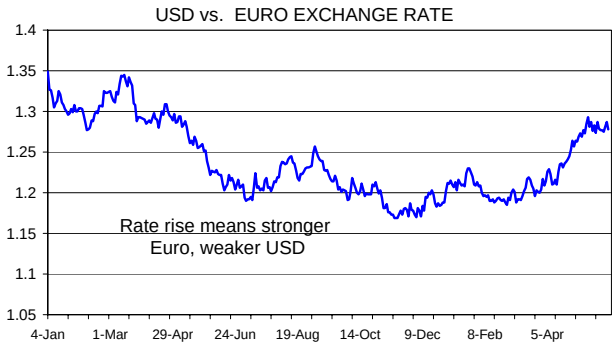
Over the past week the Kiwi dollar rose briefly to 64.3 cents on the back of weakness in the greenback and strong inflation data contained in the business confidence survey released yesterday. But overnight the greenback has strengthened on the back of some slightly more hawkish than expected comments in the Federal Reserve's deliberations about monetary policy and this has caused the Kiwi dollar to end today largely where it was a week ago near 63.2 US cents. Against the Australian dollar we have also ended unchanged near 84.3 cents with the Aussie dollar getting moved around a reasonable bet at the moment by a strong fluctuations in metals commodities prices.

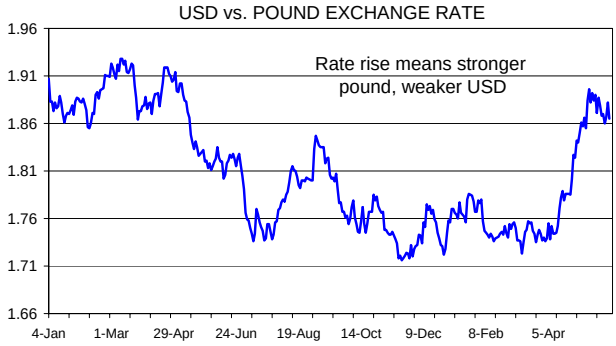


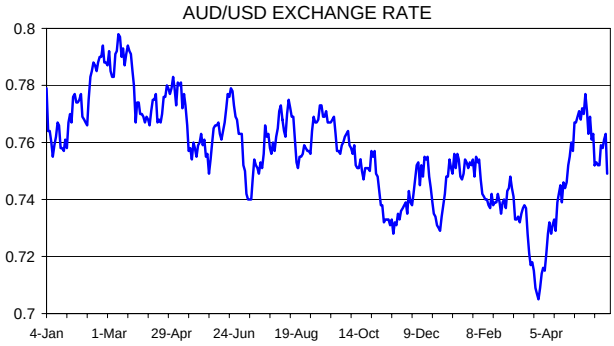


Next week the Reserve Bank of New Zealand will conduct their six weekly review of the official cash rate. We expect them to strongly signal that there is no scope for monetary policy to be eased in New Zealand for a substantial period of time. The risk is that this catches the market by surprise and leaves the Kiwi dollar still well supported in the short term. But as noted above we expect the Kiwi dollar will eventually resume its downward trend.









BNZ WEEKLY OVERVIEW

ECONOMIC DATA

All %		Latest qtr only	Previous qtr only	Latest year	Year ago	2 Yrs ago
Inflation	RBNZ target is 1% - 3% on average	0.6%	0.7	3.3	2.8	1.5
GDP growth	Average past 10 years = 3.3%	-0.1	0.1	2.2	4.4	3.4
Unemployment rate	Average past 10 years = 5.7%	3.9	3.6	.....	3.8	4.2
Jobs growth	Average past 10 years = 2.1%	1.1	0.0	2.6	3.4	3.2
Current a/c deficit	Average past 10 years = 4.9% of GDP	8.9	8.5	.....	6.7	4.3
Terms of Trade		-2.3	-0.4	-1.8	4.4	6.6
Wages Growth	Stats NZ experimental series	1.3	1.7	5.3	5.1	4.9
Retail Sales ex-auto	Average past 9 years = 4.2%.	0.9	1.2	5.6	7.1	5.9
House Prices	Long term average rise 4.2% p.a.	3.9	2.6	15.3	12.2	24.8
Net migration gain	Av. gain past 10 years = 13,000	+10,079	6,951yr	.....	9,349	25,712
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Consumer conf.	10 year average = 8%. Colmar survey	-38	-29	-27	-13	-11
Business activity exps	10 year average = 27%. NBNZ	10	15	0	9	25
Household debt	10 year average growth = 11.4%. RBNZ	14.2	14.7	15.3	15.2	16.5
Dwelling sales	10 year average growth = 4.6%. REINZ	-14.6	-2.9	3.9	-7.5	6.0
Tourist numbers	10 year average growth = 6.1%. Stats NZ	9.7	-3.0	-2.8	5.2	22.6
Floating Mort. Rate	10 year average = 8.5%	9.55	9.55	9.55	9.00	7.75
3 yr fixed hsg rate	10 year average = 8.2%	7.85	7.60	8.15	7.80	7.20

ECONOMIC FORECASTS

Forecasts at May 18 2006	**March Years**					**December Years**				
	2005	2006	2007	2008	2009	2004	2005	2006	2007	2008
GDP - annual average % change										
Private Consumption	5.8	3.9	1.4	0.4	1.1	6.5	4.6	1.7	0.5	0.8
Government Consumption	5.2	5.2	3.8	3.1	3.6	5.7	5.3	4.0	3.4	3.1
Investment	7.8	5.4	-1.2	1.4	3.6	13.2	4.3	-0.3	0.7	3.1
GNE	6.5	4.1	1.0	1.2	2.3	8.2	4.5	1.2	1.2	1.9
Exports	3.9	0.6	1.6	3.8	4.9	5.6	-0.3	1.2	3.4	4.6
Imports	13.7	4.9	0.1	2.2	3.3	16.6	6.4	-0.2	2.2	3.0
GDP	3.7	2.1	1.1	1.7	2.7	4.3	2.2	1.2	1.5	2.4
Inflation – Consumers Price Index	2.8	3.3	3.4	3.3	2.1	2.7	3.2	3.3	3.5	2.2
Employment	3.4	2.6	0.5	0.7	1.1	4.4	1.5	1.5	0.6	1.0
Unemployment Rate %	3.8	3.9	4.3	4.5	4.4	3.7	3.6	4.1	4.4	4.4
Wages	2.9	4.6	4.6	3.5	2.6	1.9	5.1	4.4	3.7	2.8
EXCHANGE RATE ASSUMPTIONS										
NZD/USD	0.73	0.64	0.59	0.57	0.59	0.71	0.70	0.60	0.56	0.59
USD/JPY	105	117	103	105	104	104	119	105	105	105
EUR/USD	1.32	1.20	1.23	1.23	1.21	1.34	1.19	1.24	1.22	1.23
NZD/AUD	0.93	0.87	0.80	0.81	0.84	0.93	0.94	0.80	0.80	0.83
NZD/GBP	0.38	0.36	0.33	0.32	0.34	0.37	0.40	0.33	0.32	0.34
NZD/EUR	0.55	0.53	0.48	0.46	0.49	0.53	0.59	0.48	0.46	0.48
NZD/YEN	76.8	74.6	60.8	59.9	61.6	74.2	82.7	63.0	58.8	61.8
TWI	70.7	65.6	58.9	57.7	62.1	69	71.9	59.7	56.9	62.1
Official Cash Rate	6.5	7.25	6.75	5.75	5.75	6.5	7.0	7.00	6.0	5.75
90 Day Bank Bill Rate	6.86	7.55	6.98	5.88	6.10	6.73	7.49	7.22	6.12	5.93
2 Year swap	6.82	7.0	6.18	6.04	6.18	6.61	7.24	6.33	6.02	6.15
10 Year Govt Bond	6.04	5.71	5.90	5.6	5.7	6.03	5.89	6.05	5.65	5.65

All actual data excluding interest & exchange rates sourced from Statistics NZ.

The BNZ Weekly Overview is prepared by Tony Alexander, Chief Economist at the Bank of New Zealand. Ph 04 474-6744.