Bank of New Zealand

BNZ Weekly Overview

6 March 2008

FINANCIAL MARKETS DATA

	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	8.25%	8.25	8.25	8.25	7.25	6.2
90-day bank bill	8.84%	8.81	8.77	8.89	7.82	6.4
10 year govt. bond	6.28%	6.45	6.26	6.41	5.81	6.5
1 year swap	8.78%	8.82	8.78	8.86	7.94	6.6
5 year swap	8.08%	8.16	8.09	8.19	7.40	7.0

For addition to our emailing list for Thursday night receipt email "Subscribe WO" to tony.alexander@bnz.co.nz . To get off the list email 'Unsubscribe". We maintain only ONE emailing list so recipients receive both the Weekly Overview and Offshore Overview.

Monthly Survey Time

Many thanks to those people who have responded to our monthly survey in the past. The results give the earliest indication each month of what is happening with general sentiment about the New Zealand economy and as such are helpful to the likes of ourselves picking what is likely to happen with growth, the labour market, interest rates and exchange rate. The results are also important to the Reserve Bank. Plus feedback suggests we deliver many people a lot of voyeuristic pleasure in reading about what is happening with a wide range of industries in the New Zealand economy.

So if you have not already done so in the email used for sending out this week's Overviews please click on the URL below and let us know whether you think the economy will get better or worse over the next 12 months. And if time permits let us know what is happening in your particular industry at the moment. These comments may be your only opportunity to tell an audience beyond the people you work with and family members in the evening time what you are seeing out there in your industry.

http://survey.usuite.com/survey/7f801dd05f3742619b046cc119c15106.sur

This morning, as expected, the Reserve Bank left the official cash rate unchanged at the 8.25% level it was taken to in July last year. This level is 3.25% above where the rate was when rises started back in January 2004. The commentary from the Reserve Bank accompanying the no change outcome had something for everyone but on balance was neutral with a smidgeon of hawkishness. The RB noted that "The outlook for economic activity has deteriorated somewhat since we reviewed the OCR in January". They cited tighter credit conditions, weaker world growth, the drought and a sharper than expected deterioration in the housing market.

But they also said they expect inflation will remain high because of things such as the carbon emissions trading scheme, food and energy prices, the tight labour market, strength in commodity prices, higher government spending and tax cuts, and high inflation expectations. While noting that they see growth risks lying on the downside they see inflation risks remaining on the upside and that is the important bit when it comes to monetary policy setting.

Their conclusion at the end read as follows. “Given this outlook, we expect that the OCR will need to remain at current levels for a significant time yet to ensure inflation outcomes of 1 to 3 percent on average over the medium term.”

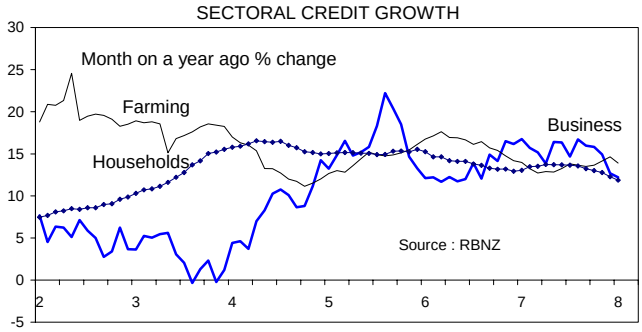
In other words no easing of monetary policy in New Zealand is remotely imminent. That means continuing strong interest rate support for the Kiwi dollar in an environment where tonight we might see a cut in interest rates in the United Kingdom and if not then probably at some stage in the next few months. And with United States interest rates likely to be cut again by 0.5% on March 18. But we suspect that as this year progresses and weaker data probably emerges we will see more sustained downward pressure on the exchange rate, then fixed interest rates, then floating interest rates last of all.

NZ ECONOMIC DEVELOPMENTS

Thursday 28

Lending Growth Slows down

The annual rate of growth in lending to the household sector fell to its lowest level in five years at 11.9% in January from 12.3% in December and 13.0% a year earlier. Growth has averaged 14.2% per annum over the past five years. In seasonally adjusted terms lending to the household sector over January grew by 0.7%. This was the same rate of increase as in December and is below growth which averaged 1.1% each month in the first half of 2007. These numbers are completely unsurprising considering what we know is already happening in the housing market and it's likely that the rate of growth in household lending will slow much further, especially with fixed interest rates increasing again recently and net migration numbers deteriorating further.



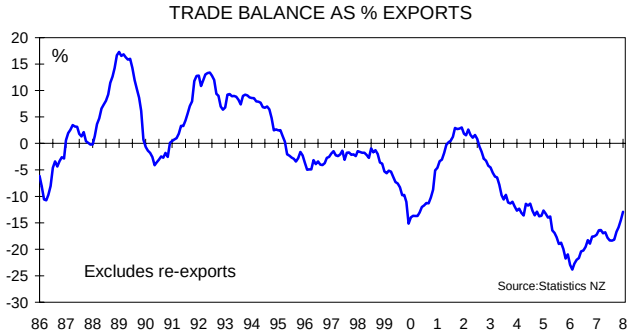
The annual rate of growth in lending to the business sector slowed to 12.2% in January from 12.7% in December and 16.8% a year ago. Growth has averaged 11.7% per annum over the past five years however so growth still appears to be running at slightly above average levels. However over the past three months business debt has declined by just over $100 million while in the same period a year earlier there was growth of $1.9 billion, two years ago $400 million, three years ago $2.9 billion, and four years ago $1 billion. The annual rate of change in business lending growth is therefore vastly understating the slowdown in lending which is underway. Having said that these numbers can get whacked around something wicked by large corporate financing deals and given the strength we are seeing in the issuing of consents for non-residential buildings and commercial vehicle registrations we don't think business capital spending is in as bad as state as the lending numbers would suggest.

In the farming sector the annual rate of growth in debt has slowed to 13.9% in January from 14.6% in December and 14% a year ago. Growth has averaged 14.9% the past five years so lending growth is below average. However growth in lending to the farming sector was $847 million over the past three months compared with $675 million for the same period year ago, $923 million two years ago, $465 million three years ago, and $131 million four years ago. Therefore these numbers are still relatively good which is what we would expect to see given the dairying boom and the boom in dairy conversions.

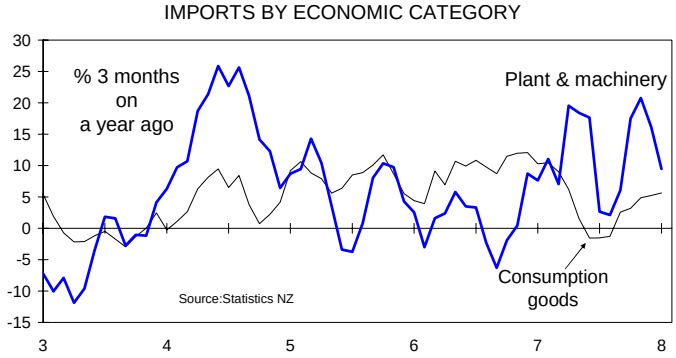
Friday 29

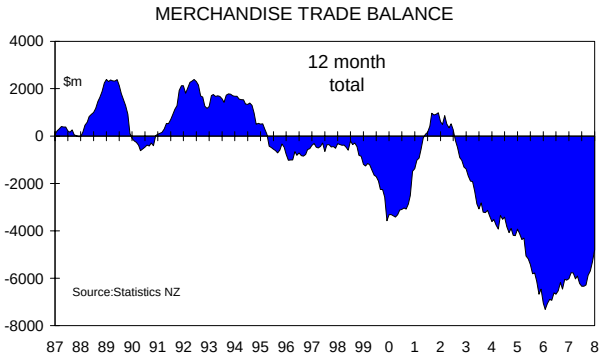
Trade Balance Improving - But It's All Oil and Dairying

New Zealand recorded a trade deficit in January of $320m. This might sound bad but it's actually very good because in January last year the deficit was $825 million and the year before that $894 million. This is actually the smallest January deficit since 2002 and means that the annual trade deficit has now declined to $4.8 billion from $6 billion a year ago. The deficit as a proportion of exports now stands at just 12.9% compared with 17.2% a year ago which was the lowest ratio since October 2004.



The value of exports in January was ahead 24% from a year earlier and in the three months to January annual growth was 23.3%. Full-year growth was 6.4%. Where is this wonderful growth in exports coming from? The total value of the increase in exports over the three months to January from a year earlier was $1.9 billion. A full $702mn worth of this was oil (812% increase) and another $1051mn was dairy products (58% increase). Everything else was just rats and mice. Meat exports were up only $60 million or 1.4%. Fish exports were down $10 million or 3.8%, wood $37 million or 7.4%. The biggest fall was a 95% decline recorded for weaved baskets – down $160,297. What next? The collapse of macramé?



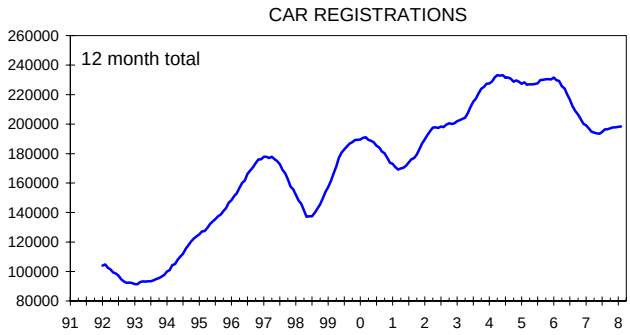


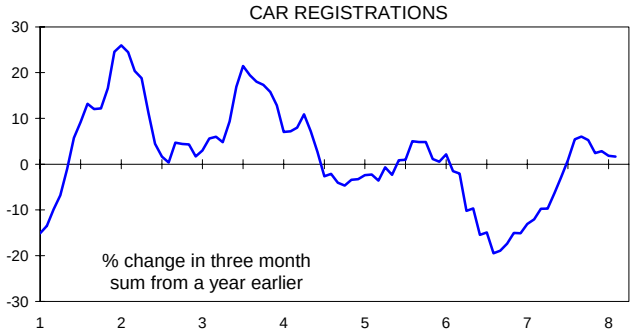
Somewhat challenging the view that the domestic economy is munted the value of imports of plant machinery and equipment in January was ahead 16% from a year ago with growth in the three months to January from a year ago a reasonable 9%. Consumer goods imports were ahead 6% for both the month and three-month periods on a year earlier.

Tuesday 4

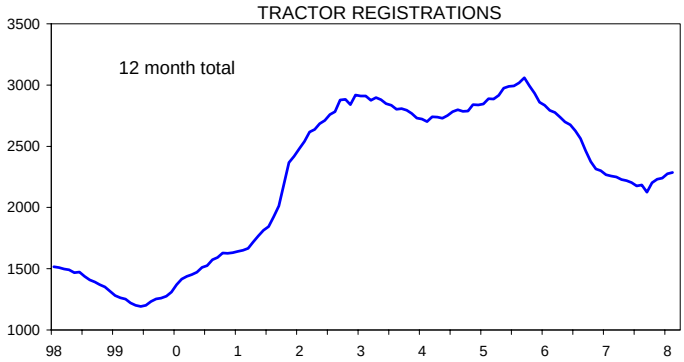
Vehicle Spending Still Firm

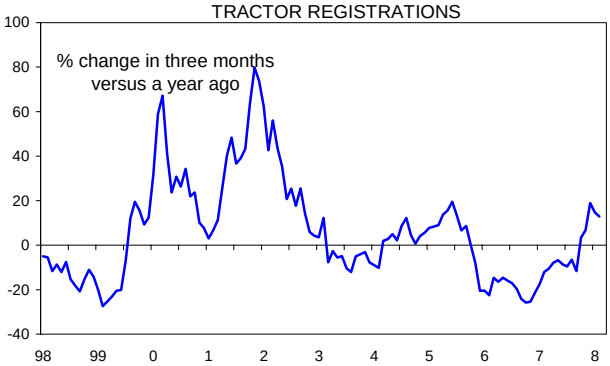
In February there were 15,201 cars registered around New Zealand. This was a rise of 1.9% from a year ago taking the rise for the three months to February to 1.7% from a year earlier. So there is some small growth underway which is quite reassuring considering the raft of worries hitting households at the moment and below average consumer confidence. In seasonally adjusted terms car registrations have been flat over the past three months and for the entire year to February regos were up 0.7% from a year earlier.



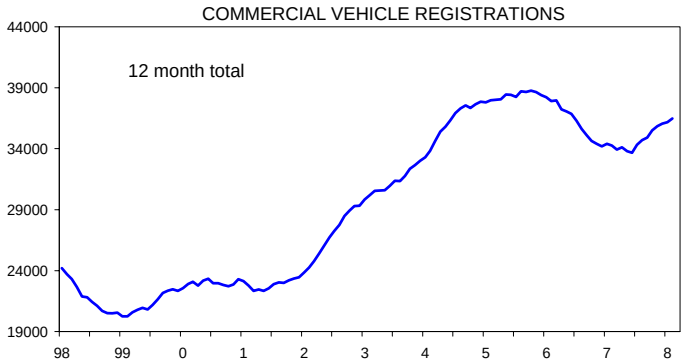


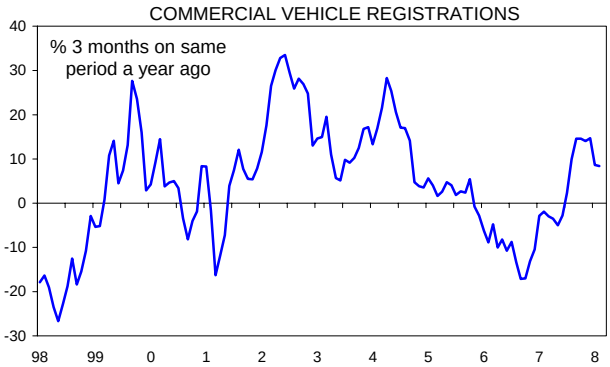
In February there were 150 tractors registered around the country. This was a 7.9% rise from a year ago which followed a 29% annual rise in January. Growth in this important area of farm expenditure is strong – and why not. Although the exchange rate is high and returns to sheep and beef low, dairy is booming and the high currency makes it a great time to buy a cheap piece of modern productivity-enhancing equipment from overseas. For the three months to February tractor regos were 13% ahead of a year ago and for the year to February they were up 1.4%.





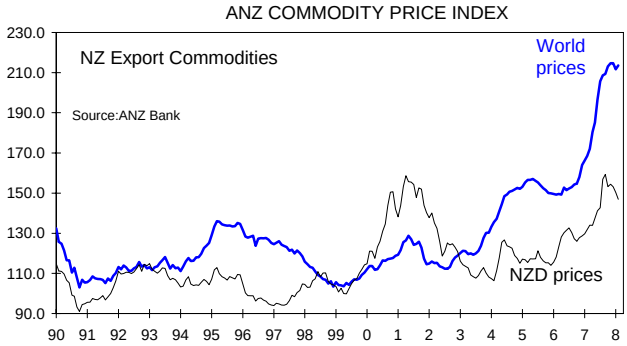
Finally, in a very positive sign for business investment the number of commercial vehicles registered around NZ in February was a healthy 11.4% ahead of a year earlier at 2,890. For the three months to February growth on a year ago was 8.4%, for the year as a whole 6.5%, and in seasonally adjusted terms growth has been flat. The result suggests that although businesses are expressing great concern about the outlook for the economy and their own businesses in surveys they remain willing to buy big lumpy machines.

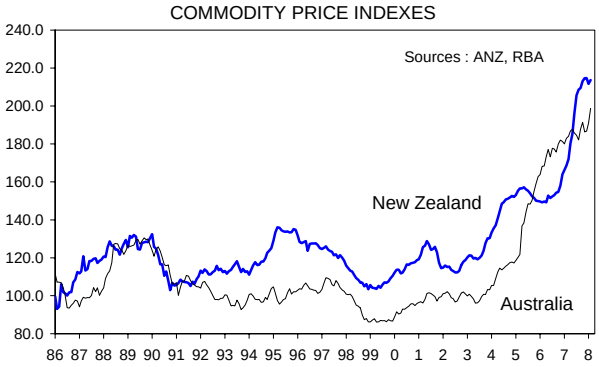




Commodity Prices Not Really Rising Any Longer

The ANZ Commodity Price Index in world price terms rose by 0.9% in February though if it wasn't for a 12% rise in aluminium prices caused by the snow storms in China the index would have fallen slightly. The index stands about 27% ahead of a year ago and 58% above its average level for the past ten years. This is very similar to Australia's commodity price index which currently stands some 64% above its ten year average. Prospects for the coming year look better over there than here however with their coal prices expected to double and iron ore prices forecast to rise over 65%.





As of January – ANZ are tardy these days and don't load the release to their website for ages – dairy prices were 63% ahead of a year ago, meat 9%, horticultural products down 5%, forestry products up 17%, seafood up 12%, and aluminium down 13%.

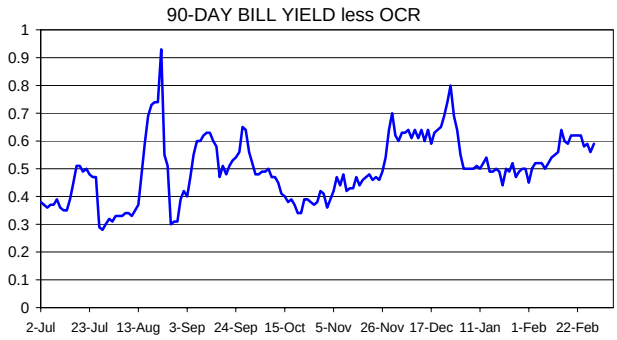
Thursday 6

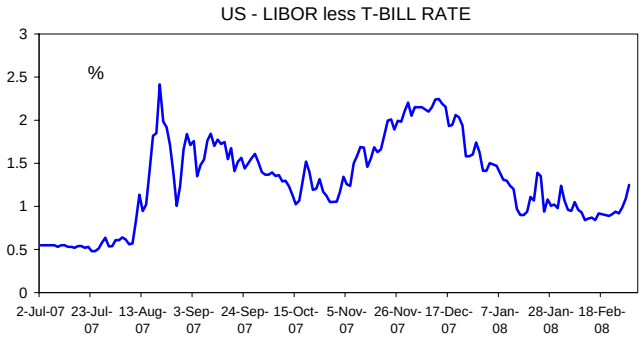
Monetary Policy Unchanged

As had been widely expected the Reserve Bank left the official cash rate unchanged at 8.25% this morning. While they noted that risks to growth going forward lie on the downside they stressed that inflation risks lie in the opposite direction with pressures coming from easing fiscal policy, rising food and energy costs, rising commodity prices generally, the tight labour market, high inflation expectations, and the upcoming carbon emissions trading scheme.

INTEREST RATES

Tensions have been returning to funding markets around the world over the past few weeks after they eased off over the second half of December with assistance from special liquidity injections by the likes of the Federal Reserve and ECB. Investors are cautious about where they place their money with reduced willingness to invest for medium to long time periods and an aversion to anything but top rating paper. There are a number of ways to measure this tension and the most basic one (though not the most accurate) is a simple comparison of the 90-day bank bill yield with the official cash rate. As the graph shows the gap opened up beyond the average 0.28% since 1999 in August last year and again in late-November. Tensions remain nowhere near as bad as back then but they have returned to a small degree both here and overseas.

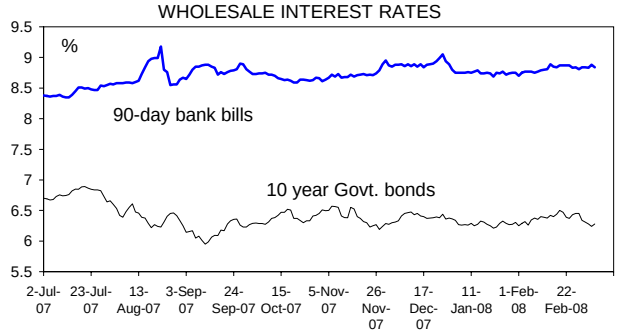


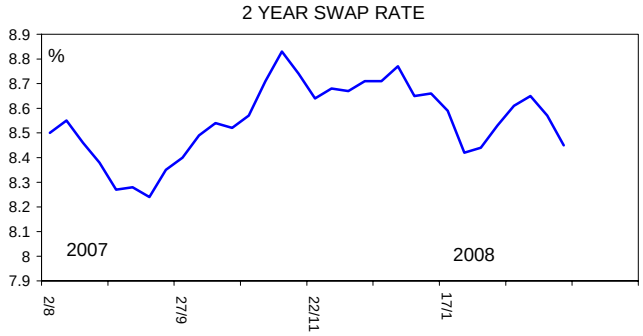


The second graph is a measure for US tensions showing the difference between the 3 month LIBOR and treasury bill rates. Risk aversion as measured by the line rising has increased recently.

The importance to borrowers of these tensions is that bank retail lending rates such as for floating and fixed rate mortgages, along with business lending rates including those tied to the wholesale yield curve, go up without any change in monetary policy. We have seen a manifestation of this recently with banks raising housing rates without any change in market expectations of monetary policy.

This afternoon the yield on 90 day bank bills finished well within the trading range seen for three months near 8.84% from 8.81% last week. 10 year government bond yields were however a tad lower than normal near 6.28% from 6.45% with downward pressure coming from the rally in the United States bond market on the back of weak economic data and more bad news for their housing market and financial institution capital bases.





Swap rates have the edged slightly lower over the week but as previously noted the previously stable relationship between these rates and fixed housing rates is not holding at the moment because of the extra funding costs associated with the credit crunch overseas.

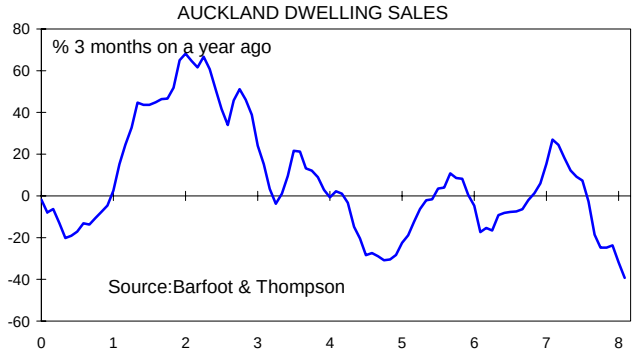
If I Were a Borrower What Would I Do?

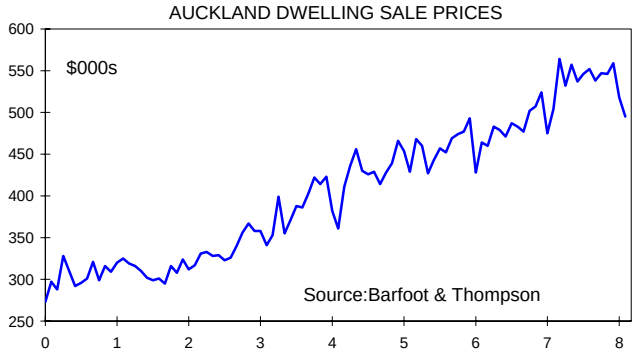
I would only fix one year. Other rates are too expensive and slowing growth means we expect lower interest rates in NZ from late this year through 2009.

HOUSING MARKET UPDATE

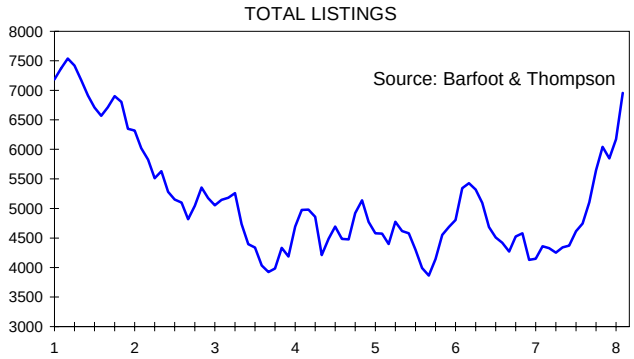
Barfoot & Thompson Data Weak

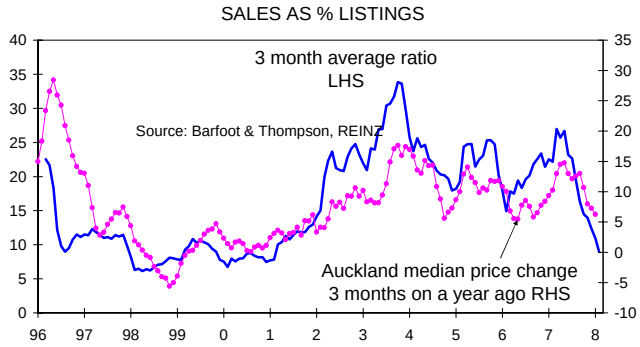
This week we received the monthly data from Barfoot & Thompson in Auckland. The numbers are ugly. In February they sold 603 dwellings. This was a decrease of 39% from a year earlier which followed a 42% fall in January and 37% fall in December. Unsurprisingly, with activity so weak prices are falling. The average dwelling sale price in February came in at $495,000 compared with $518,000 in January and $559,000 in December. The average price was 1.8% down from a year ago.





As previously noted, our belief is that for the moment and the next few months there are plenty of willing sellers (under-capitalised investors getting burnt off) while the buyers know they can stand back and wait for lower prices. In February the number of listings stood a massive 60% ahead of a year earlier at 6,956 dwellings. 2,049 fresh listings were received during the month. The ratio of sales to listings for February was just 8.7% which is the lowest reading for this time of year since 2000.





In the rental market things remain firm however with the average weekly rent in February of $382 being 7% higher than a year earlier. The number of lettings at 714 was 7.7% ahead of a year ago.

Overall the data show a housing market experiencing a long long overdue correction downward from unsustainable highs in terms of prices and sales levels. These sort of numbers are likely to continue through Winter and after that we expect more buyers to emerge from the bushes and cause the market to stabilise.

Speaking of which, last Friday we spent 20 minutes chatting with a reporter from a Sunday newspaper about the current fundamentals operating in the housing market. We started discussing the obvious negatives including weak migration numbers and high interest rates. But then we got on to the factors we listed here in the Weekly Overview a couple of weeks ago which we expect will eventually produce some improvement in the housing market further out. These are things like a shortage of rental accommodation around the country, estimates by the government that another 18,000 dwellings need to be built a year, decreasing dwelling construction seen in consent numbers and with developers having to cease business in the absence of finance, a more inflationary environment which will eventually encourage investors to seek inflation hedges like property, and a host of other factors.

So what was it that the reporter chose to put on page 1 of the newspaper? Not a single one of the positives and only one no-brainer comment about the migration numbers being weak. There is a definite bias out there in the media toward reporting only the negatives on the housing numbers so tomorrow we are likely to see some almost gleeful discussions about the weak Barfoot and Thompson numbers discussed here in conjunction with the Reserve Bank's warning this morning that they expect the official cash rate will need to remain at current levels for a significant period of time.

Exchange Rates & Foreign Economies

See the Offshore Overview

Data Sources

Interest rates & exchange rates RBNZ at	http://www.rbnz.govt.nz/statistics/
House mortgage data – RBNZ	http://www.rbnz.govt.nz/statistics/monfin/rbssr/rbssrpartE/data.html
House price information - REINZ	http://www.reinz.org.nz/reinz/public/market-information/market-information_home.cfm
NZ economic data, most from Statistics NZ	http://www.stats.govt.nz
Government accounts, NZ Treasury at	http://www.treasury.govt.nz/financialstatements/
Parliament, select committees, publications etc.	http://www.parliament.nz/en-nz

Want more detailed background information on the NZ economy? Start in these places.
http://www.treasury.govt.nz/economy/overview
http://www.oecd.org/country/0,3377,en_33873108_33873658_1_1_1_1_1,00.html
http://www.rbnz.govt.nz/monpol/statements/

http://www.fco.gov.uk/servlet/Front?pagename=OpenMarket/Xcelerate/ShowPage&c=Page&cid=1007029394365&a=KCountryProfile&aid=1019041559387

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	1.2%	0.5	3.2	2.7	3.2
GDP growth	Average past 10 years = 3.0%	0.5	0.8	2.7	1.6	3.1
Unemployment rate	Average past 10 years = 5.3%	3.4	3.5	.....	3.8	3.6
Jobs growth	Average past 10 years = 1.9%	1.1	-0.3	2.5	1.4	1.6
Current a/c deficit	Average past 10 years = 5.5% of GDP	8.3	8.2	.....	9.2	8.5
Terms of Trade		3.7	0.4	8.4	-1.3	0.9
Wages Growth	Stats NZ experimental series	1.6	1.2	4.9	4.9	5.1
Retail Sales ex-auto	Average past 9 years = 3.8%.	0.0	0.1	5.2	4.1	6.1
House Prices	Long term average rise 5% p.a.	0.3	2.8	11.4	10.1	14.0
Net migration gain	Av. gain past 10 years = 10,400	+4,804	7,520yr	.....	14,130	6,951
Tourism – an. av grth	10 year average growth = 5.0%. Stats NZ	0.5	0.9	2.3	1.4	1.3
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Consumer conf.	10 year average = 2%. Colmar survey	-16	-10	-8	-3	-35
Business activity exps	10 year average = 26%. NBNZ	2.4	18.2	16.7	25.7	-4.4
Household debt	10 year average growth = 11.3%. RBNZ	11.9	12.3	13.7	13.0	15.2
Dwelling sales	10 year average growth = 3.5%. REINZ	-32.1	-21.6	-11.3	19.4	-17.6
Floating Mort. Rate	10 year average = 8.1%	10.69	10.55	10.30	9.55	9.55
3 yr fixed hsg rate	10 year average = 7.9%	9.30	9.19	9.00	8.15	8.15

ECONOMIC FORECASTS

Forecasts at Jan 24 2008	**March Years**					**December Years**				
	2006	2007	2008	2009	2010	2005	2006	2007	2008	2009
GDP - annual average % change										
Private Consumption	4.6	2.6	3.3	0.5	1.7	4.9	2.4	4.1	0.7	1.2
Government Consumption	5	4.4	3.7	3.6	4.2	4.1	4.7	3.9	3.4	4.2
Investment	5.2	-2.3	4.1	1.5	2.7	3.9	-1.6	4.2	1.7	1.9
GNE	4.1	1	4.7	1	2.4	4.2	1	4.9	1.4	1.8
Exports	-0.1	3.1	2.1	3.7	3.8	-0.4	1.7	2.9	3.5	3.7
Imports	4.1	-1.7	8.3	3.4	3.1	5.4	-2.8	8.1	4	3
GDP	2.7	1.6	2.9	1.1	2.5	2.8	1.6	3	1.4	2
Inflation – Consumers Price Index	3.3	2.5	3.4	3.1	2.9	3.2	2.6	3.2	3	3
Employment	2.6	1.7	0.8	0.7	1.8	1.6	1.4	1.8	0.7	1.4
Unemployment Rate %	3.9	3.7	3.8	4.4	4.4	3.6	3.7	3.7	4.3	4.4
Wages	4.6	5.5	4.8	4.2	3.3	5.1	5.5	4.3	4.6	3.5
EXCHANGE RATE ASSUMPTIONS										
NZD/USD	0.64	0.7	0.76	0.67	0.61	0.7	0.69	0.77	0.69	0.62
USD/JPY	117	117	107	112	119	119	117	112	110	118
EUR/USD	1.2	1.32	1.47	1.38	1.31	1.19	1.32	1.46	1.4	1.32
NZD/AUD	0.87	0.88	0.87	0.82	0.79	0.94	0.88	0.88	0.83	0.79
NZD/GBP	0.36	0.36	0.39	0.37	0.34	0.4	0.35	0.38	0.37	0.35
NZD/EUR	0.53	0.53	0.52	0.49	0.47	0.59	0.52	0.53	0.49	0.47
NZD/YEN	74.6	81.9	81.3	75	72.6	82.7	81	86.3	75.9	73.2
TWI	65.6	68.6	70.4	64.6	61	71.9	68	71.6	65.8	61.7
Official Cash Rate	7.25	7.47	8.25	7.75	6.75	6.99	7.44	8.19	8	7
90 Day Bank Bill Rate	7.55	7.78	8.73	7.95	6.98	7.49	7.64	8.77	8.2	7.23
10 year Govt. Bond	5.71	5.91	6.3	6.1	6.3	5.89	5.77	6.38	6.1	6.25
2 Year Swap	6.99	7.76	8.29	7.23	6.65	7.24	7.48	8.58	7.46	6.7

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

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