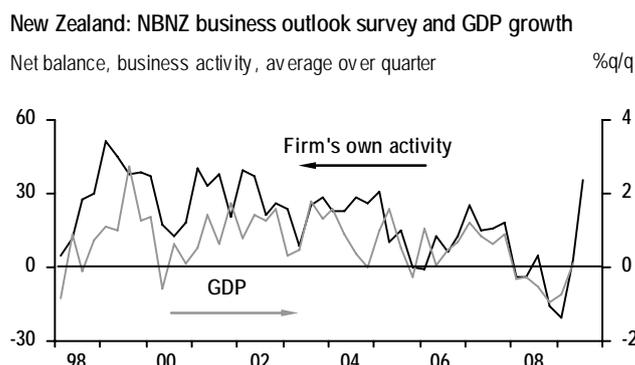


New Zealand Economic Update

NBNZ business confidence

- **Business confidence jumped 14.9 points in September**
- **Nearly half of those surveyed expect conditions to improve**
- **Near-term GDP growth will be solid**

The NBNZ business confidence survey jumped an impressive 14.9 points in September to 49.1 (J.P. Morgan 40). The substantial improvement can be attributed to a myriad of factors, but first and foremost can be put down to recent news the New Zealand's prolonged recession finally ended in 2Q. The headline reading of confidence suggests that a net 49% of respondents expect better times ahead, the highest reading since 1999. Further, the all important firms' own activity outlook also posted a significant rise, jumping from 26.0 to 32.2 in September, signaling the Kiwi economy will continue to expand solidly in coming quarters (chart).



Profit expectations improved markedly in September, with a net 8% of respondents expecting profits to rise over the next 12 months. This explains, in part, why employment intentions continued to recover. The survey today showed that a net 2% of respondents expect to increase staff over the year ahead, marking the first positive reading in 18 months. Marked improvements were also recorded in commercial construction, with 11% of respondents expecting conditions in that sector to improve over the next year. Surprisingly, though, respondents were less optimistic compared to last month about the outlook for residential construction, with a net 39% of firms expecting to see improvements in the sector (down from 48%). With recent data showing house prices increasing, market turnover rising, and the number of days to sell a house heading south, we suspect that this component of the survey will trend higher in coming months.

The NBNZ said today that the last time the components of its survey have surged "this far, this fast" was following the Asian crisis in the late 1990s. Back then, it said, the RBNZ watched the economy firm and resource pressures intensify for more than a year before taking action. Then,

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between January and May in 2000 the RBNZ delivered a total of 200bp of policy tightening. We believe that the RBNZ will remain on the sidelines for some time this time around also, despite the better than expected run of data in recent weeks. Our forecast remains that the RBNZ's next tightening cycle will begin in July 2010. By then, Governor Bollard should be confident that the recovery underway has enough momentum to withstand higher interest rates.

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