BNZ Weekly Overview

27 October 2011

Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

The Weekly Overview is written by Tony Alexander. The views expressed are my own and do not purport to represent the views of the BNZ. To receive the Weekly Overview each Thursday night please click here.
http://feedback.bnz.co.nz/forms/Fx-I8ploskSGWgjN_7WOAw
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A Concise Summary

This is the situation. NZ has averaged growth of 2.3% per annum the past decade but only grew 1.5% in the year to June. Our economy has performed poorly and has not grown faster than 3% since early-2006. After growing 0.5% in the 2010 December quarter and 0.8% in the March quarter we only managed 0.1% in the June quarter. Growth has stalled. Looking at partial measures we see there seems to be some growth in business investment, a recovery in housing has tentatively started with little price movement, but household spending growth is mediocre, export receipts are easing, and fiscal policy is tightening. Jobs growth is probably just over 1% p.a. and unemployment has been stuck near 6.5% for two years. Inflation is (artificially GST-boosted) high at 4.6%, the current account deficit is (artificially earthquake reinsurance) low at 3.7% of GDP, and monetary policy is very easy with a 2.5% cash rate.

This is what we expect. We face continued poor growth prospects until at some stage the rebuilding of Christchurch gets going, at some stage farmers spend record incomes rather than paying off debt, and at some stage householders ease back from deleveraging and catch up on durables spending. There are few signs that we are close yet to these things happening and as is occurring offshore growth forecasts are being cut. This implies delayed tightening of monetary policy in 2012, and greater difficulty for the government in reining in the large budget deficit. Credit rating risk remains downward, especially once the current account deficit rises again. The risks are largely negative surrounding three key areas.

1. In Europe politicians for now have largely cobbled together measures which will assuage investor concerns about sovereign debt. But with the EU perhaps back in recession downward revisions to tax receipts will likely produce an eventual resurgence of concerns and disturbance to bank funding flows and export demand.
2. In the United States politicians are proving themselves unable to address the large federal deficit and rising debt burden. Default is unlikely but household hopes that leaders might develop a growth strategy have collapsed and worries about consumer spending are curtailing business willingness to hire. House building is one-third its peak and less than half the 1990s average while households have lost US$7tn in housing wealth.
3. In China banks have large and growing undeclared bad debts, property prices are over-valued, inflation is high, SMEs are struggling under worsening debt availability and debt servicing costs and easing export growth, and social tensions are rising as income disparity grows. Capacity to respond to a Europe-sourced new financial crisis is very limited but barring a crisis plenty of scope exists for easing monetary policy and sustaining growth near 9% over 2012 – but in doing so problems will be shifted to the medium and long term.

These are the implications we have drawn. Continue to focus on debt reduction, anticipate a tightening of credit availability, keep inventories low and leasing & hiring contracts flexible, don't buy into strong growth until it arrives, but don't lose faith in NZ's long term prospects as growth in emerging countries will underpin primary sector exports and foreign direct investment in those sectors.

But remember a key thing we should all write down and stick on our walls as we anticipate and feel chuffed about decades of strong demand for our primary produce. It is invariably short term problems which cause companies to fail, not long term issues. Plan for the long term but live in the short term. Meaning, everything we say now about China and how great things there are for us are as valid now as they were on September 14 2008 just before Lehmans collapsed and the world went into its biggest crisis since the 1930s. These past 3-4 years have been all about our short term, not our long term prospects.

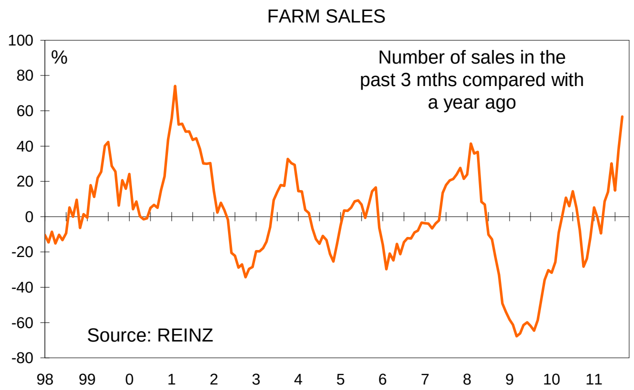
Remember that and you will understand why the next time you seek extra funding to expand your business the terms and credit availability will be different from 2008. It is all about being able to adapt to the short term shocks we know for certain will strike us in the coming decade. It is just that no field of expertise, not economics or astrology, can tell us what the shocks will be, when they will come, and how deep and protracted they will be.

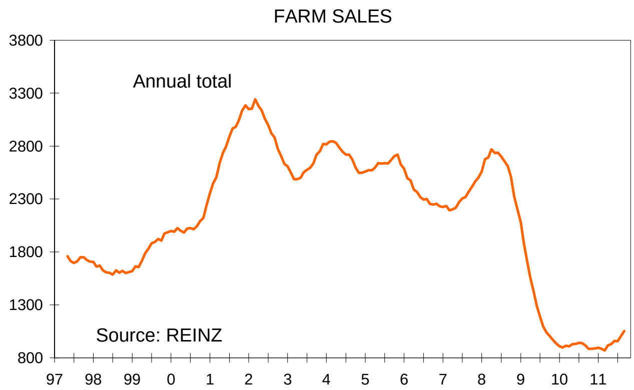
Plus here is another point to consider before everyone sits back and dreams of the Chinese version of our cargo cult mentality. Earlier this year I wrote a series of papers looking at work identifying New Zealand's impediments to growth and concluded that it is not so much our institutional structure which has meant we continue to underperform, but our culture. You will find these papers at www.tonyalexander.co.nz under the "What we Lack" tab. In the paper "Our Deficiencies Summarised" I note the following as one summarised deficiency.

"High dependence upon a primary sector export base, low medium to high-tech products in exports, and low export sector as a proportion of GDP.

- High export sector dependence upon the primary sector limits export growth as scaling up primary activities is difficult (in contrast with manufacturing, mining and services exports). Primary exports can experience large price fluctuations, face barriers into overseas markets, and have significant risks surrounding pests and diseases. Outputs are also generally easily replicable in other countries.
- Low levels of technology exports limits potential for clustering activities and vibrant interchange of ideas, though realistically this deficiency is more a reflection of other factors than a causal entity itself. The same goes for the low proportion of exports as a proportion of GDP."

In other words, growth in our primary sector is highly unlikely to spur wider growth in our economy, a fact many more people are recognising in the context of high export prices pushing he NZD higher and making other exporters and import competing businesses unprofitable. But we will not develop the two-speed economy which will ensure strong growth continues in Australia. Instead our inability to expand our primary sector as Australia can expand its mining sector means we will see happen in the farming sector that which has always happened – soaring land prices. In fact this time around with demand for land already apparent from Germans, Irish, Chinese, Singaporeans etc. escalating farm land prices look like one of the few certainties for the next few years. Awareness of this maybe explains why farm sales in September were almost double last year's level. Note how the second graph effectively shows that the rural real estate upturn has a long way to go.





This week the following material has been added to www.tonyalexander.co.nz

Weekly Newspaper Column http://tonyalexander.co.nz/newspaper-column/

Other Website Material

- **Weekly syndicated newspaper column** http://tonyalexander.co.nz/newspaper-column/
- **BNZ-REINZ Residential Market Survey** Released second week of each month. http://tonyalexander.co.nz/bnz-reinz-survey/
- **Real Estate Overview** Updated mid-late each month. http://tonyalexander.co.nz/bnz-reinz-survey/
- **Archived Weekly Overviews** www.bnz.co.nz/tonyalexander

Is Our Economy Getting Better or Worse?

In this section we look only at what the data are actually telling us and pay no attention to forecasts or intentions measures.

The data were mixed this week but if we look at the trends rather than the monthly changes which in our country go all over the place we see improving imports of capital goods, falling export receipts, and rising employment. Be very wary of over-extrapolating what is happening with our monthly and even quarterly numbers as there are so many disturbing factors in play from the February 22 earthquake, the March 10 Japan earthquake, the Rugby World Cup, the now approaching election, and some large fluctuations in confidence levels.

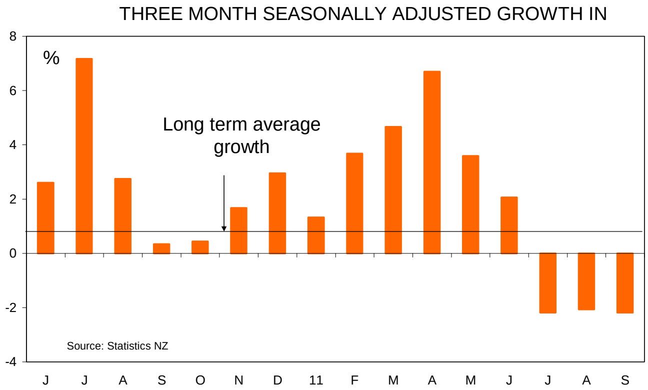
Are householders opening their wallets more?

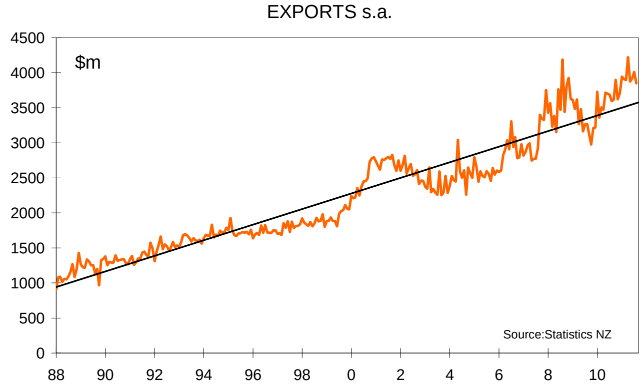
Nothing new this week to write about.

Is business output rising?

In the tourism sector yes with an 18% seasonally adjusted rise in visitor numbers in September. But this is of course the RWC effect and once that passes the numbers will drop away again from November. So picking the trend in inward tourism currently is very difficult but the risk is that with the NZD high and overseas worries growing the underlying trend is downward.

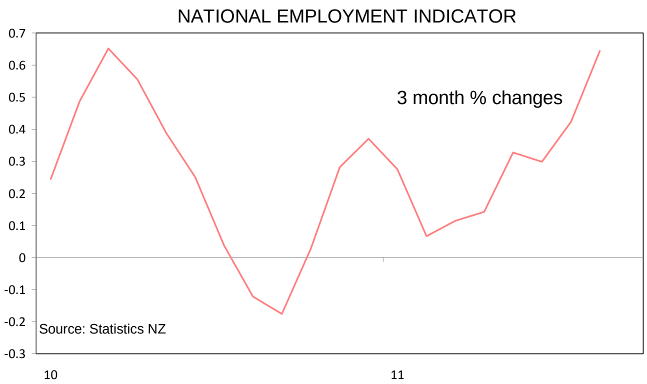
Seasonally adjusted merchandise export receipts improved 2.1% in September but with receipts falling 4.2% in August the three month moving change is a decline of 2.2% compared with growth of 2.1% in the June quarter and 4.7% in the March quarter.

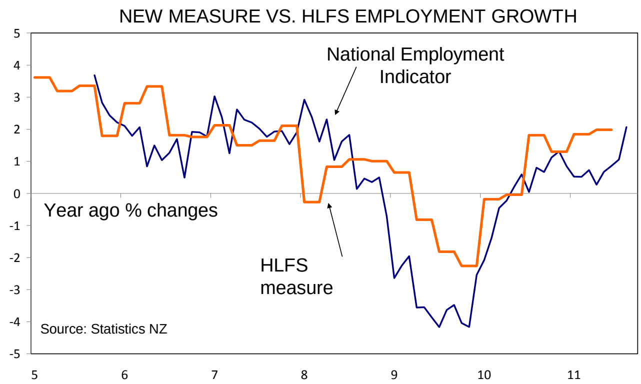




Are businesses hiring more people?

The answer is yes with the National Employment Indicator rising by a strong 1.1% seasonally adjusted to lie 2.1% ahead of a year earlier. Over the past three months growth has been 0.6% which is the strongest rate since March 2008. But, do these numbers mean the labour market is soaring and we will soon see a big surge in consumer spending? Not necessarily. There is a good chance job numbers were boosted in August by hiring ahead of the Rugby World Cup starting. Each part-time hire shows up in the series for instance.





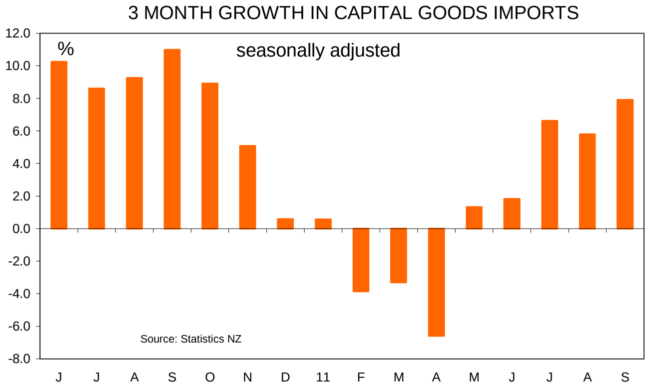
What this means is that we could see things ease back in October and in fact we fully expect that as it is very unlikely that a 1.1% rise in job numbers in a single one month period is a true reflection of what is happening in the labour market. Think of this for instance in the context of the United States where there are some 131mn people on non-farm payrolls. A 1.1% jobs rise in a month would be equivalent to over 1.4mn new jobs in a month which has never happened. So the NZ number of a 1.1% jobs gain for August is rubbish.

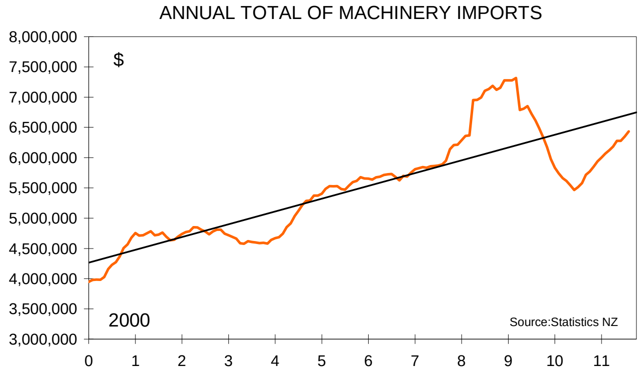
Nevertheless, the upward trend in hiring does support one of our key views which is that New Zealand's labour market is going to tighten up very quickly once economic growth accelerates over 2012 and we maintain our recommendation to employers to keep an eye out for good staff. Note that the NEI data is at national level only and is not available by region or industry.

Are businesses boosting their capital spending?

To see how businesses are feeling right now one can read our monthly BNZ Confidence Survey here. http://tonyalexander.co.nz/bnz-confidence-survey/

The value of capital goods imports fell in seasonally adjusted terms by 4.5% in September but the three month change is a healthy rise of 7.9% from 1.8% in the June quarter and a 3.3% fall in the March quarter. The trend here is up and that is a good thing in the context of the country needing investment to boost productivity.





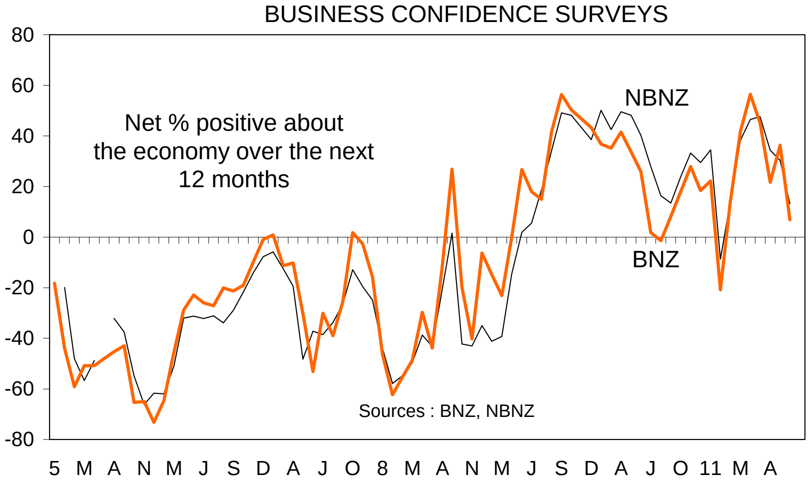
What Do The Leading Indicators Say?

In this section we look only at the factors which can at times give insight into where the economy is headed. Generally we will only cover newly released information.

Fonterra have revised down their projected payout for this current season by 45 cents to a range of $6.70 - $6.80. The change reflects the effects of a stronger exchange rate and will take about $700mn out of expected revenue to farmers which is the equivalent of about 0.3% of GDP. This can only work toward making farmers cautious for a longer period of time with regard to their spending and keep their focus on debt repayment. That is, the “at some stage” comment we have attached to increased spending/reduced debt repayment by farmers gets pushed out a bit further.

This is happening at the same time as the “at some stage” expectation for residential rebuilding in Christchurch is getting pushed into the second half of next year – as assumed by Treasury in the Economic and Fiscal Update which they released this week.

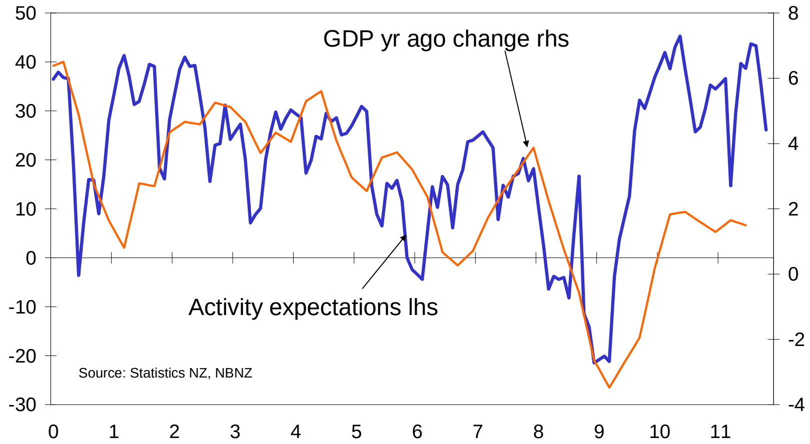
The NBNZ Business Outlook survey was released this week and it showed what we expected to see on the basis of our own monthly survey released three weeks ago – sharply reduced confidence about where the economy will be in a year’s time. Our measure fell from +36% to 7%, NBNZ’s from 30% to 13%.



The important own activity expectations measure fell from a net 35% positive to 26% which is still above the long term average of 21%. But we have a view that a disconnect has opened up between these sentiment measures and what the economy actually does because willingness to act on positive sentiment has been changed as a result of the recent global recession, credit tightening etc.

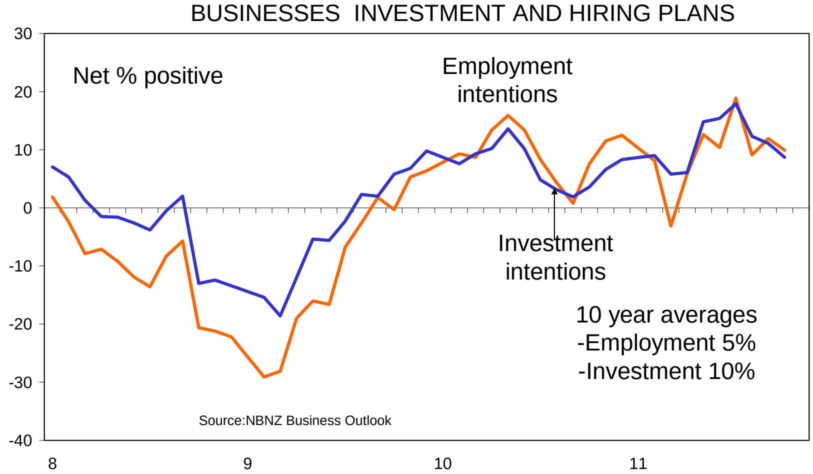
The following graph shows this change in the relationship between the expectations measure and GDP growth outcomes since 2009. Therefore, although you will be reading commentary suggesting that an activity expectations measure of 26% is consistent with 4% GDP growth, that would only be the case if the world were like it was before 2009. It is not and frankly a 26% reading is now more consistent with just 1.5% GDP growth – which is what we achieved in the year to June

ACTIVITY EXPECTATIONS & GDP GROWTH



Note that the employment intentions measure eased a tad to a net 10% positive from 12% which is still above average but not suggestive of particularly strong jobs growth and certainty not consistent with the 1.1% growth in job numbers in August reported in the National Employment Indicator. One suspects some seasonal adjustment issue may be in play there.

BUSINESSES INVESTMENT AND HIRING PLANS



Investment intentions eased to a six month low of 9% from 11% and this is worth watching because business investment has generally been strengthening as best we can tell up until now.

Worth watching also in the context of leading indicators is what is happening offshore. US consumer confidence has just crashed anew, worries about China have reached levels not seen since the late-2008 crisis, Europe may have slipped back into recession, and Australia could be on the cusp of a confidence whack as iron ore prices have fallen 30% recently and Chinese steel mills are closing down in response to reduced credit availability and fears of a construction collapse as apartment prices have started to fall.

Our strong theme here which we outlined in a 12 page lead article a few weeks ago is that much as we may be going to receive a boost from “at some stage” farmers increasing spending and “at some stage” Christchurch being rebuilt, if things tank overseas we will get walloped. Stay cautious.

INTEREST RATES

There was a significant piece of news relevant to interest rates this week in the form of the Consumers Price Index for the September quarter recording a 0.4% rise which was well below the 0.7% rise expected. Annual inflation is now at 4.6% from 5.3% and when the GST rise drops out next quarter will fall back below 3% we expect. In fact taking the GST rise out inflation is actually about 2.5% already, or even less that that looking at the core measure excluding food and energy which rose 3.1% in the year or about 1% excluding GST.

The news feeds well into our view that the need for the Reserve Bank to raise interest rates in the near future is minimal and reinforces the comment we made some weeks ago regarding the potential for no monetary policy tightening until even 2013. This week's formal view is they tighten in June. Fonterra's reduction in their payout forecast for this season also argues against the policy tightening case.

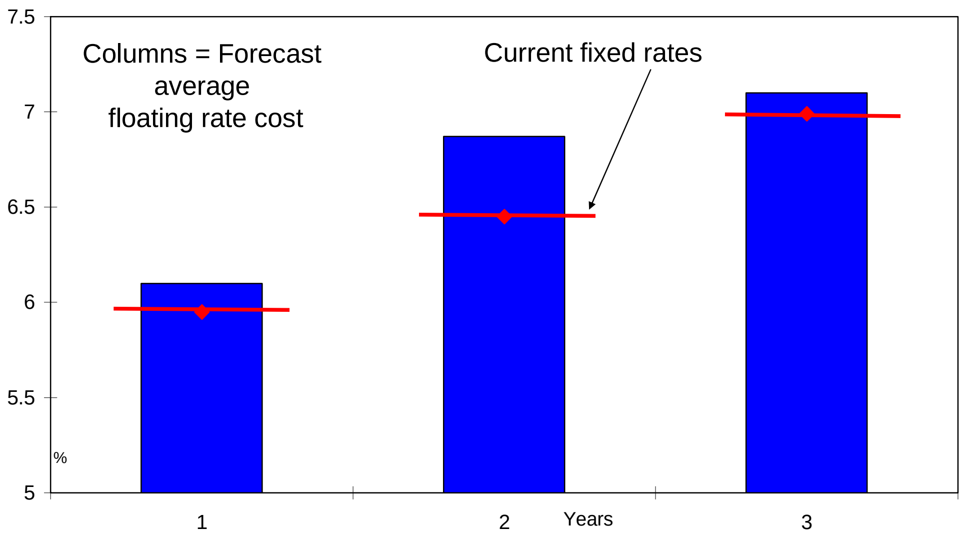
Unsurprisingly, as a result of the good inflation number wholesale interest rates have fallen this week as outlined in the table below. Oh, and on Thursday morning the RB fully met expectations by leaving their cash rate unchanged at 2.5%.

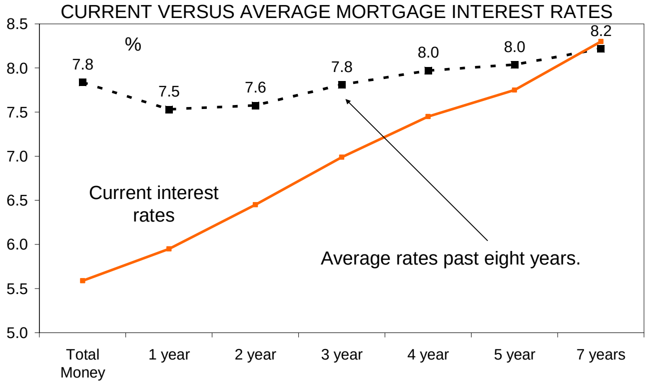
FINANCIAL MARKETS DATA

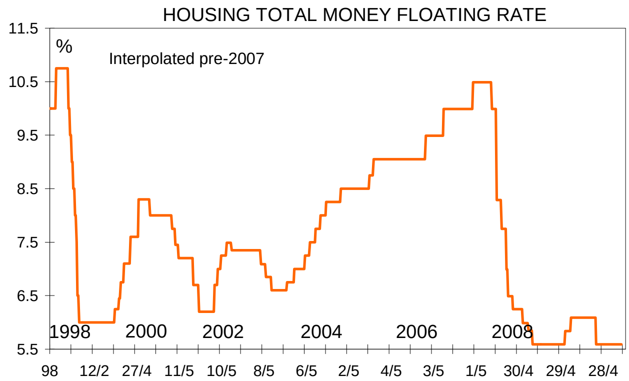
	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	3.00	5.9
90-day bank bill	2.75%	2.85	2.85	2.71	3.21	6.2
1 year swap	2.92%	3.01	3.00	3.28	3.48	6.0
3 year swap	3.38%	3.49	3.40	4.07	4.06	6.2
5 year swap	3.92%	4.05	3.84	4.61	4.44	6.4
180-day term depo	4.00%	4.00	4.50	3.60	4.90	6.0
Five year term depo	6.00%	6.00	6.00	6.00	6.75	6.5

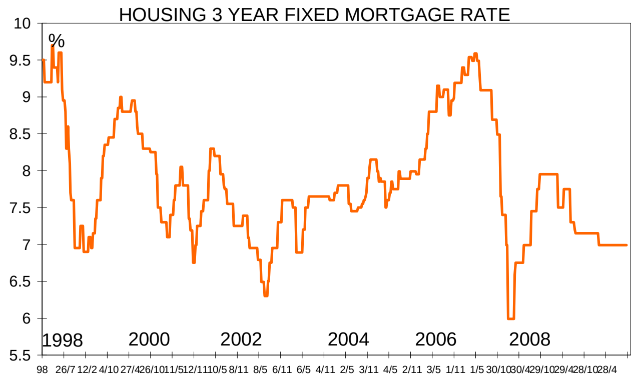
If I Were a Borrower What Would I Do?

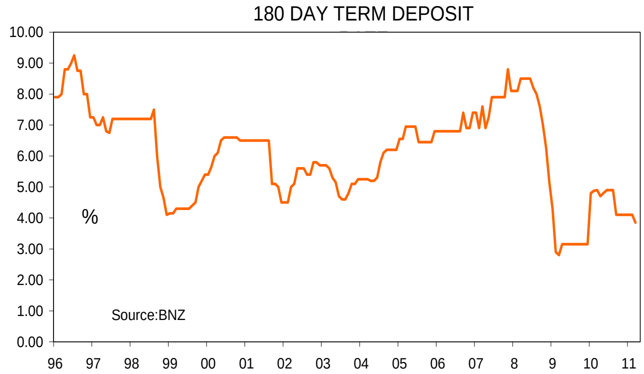
I would do what the Titanic did not. Lower than expected inflation just reinforces this view. However, as long stated, if I could get a two year rate at 6% or a three year rate at 6.25% I would fix – or rates close to those levels for close to those terms.











HOUSING MARKET UPDATE

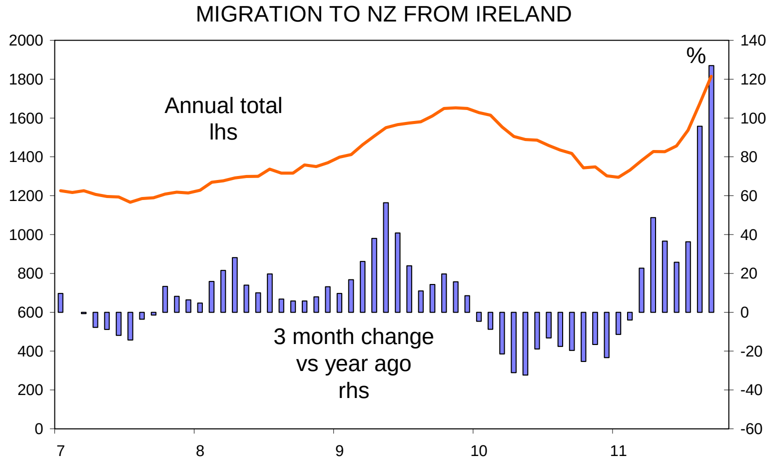
To view the most recent results of our monthly BNZ-REINZ Market Survey and read our monthly Real Estate Overview click here. http://tonyalexander.co.nz/bnz-reinz-survey/

Nothing Important

There was a net population loss from migration flows in September of 660 people in seasonally adjusted terms. This was a sharp change from the 120 gain in August and means that over the past three months the annualised loss has been running at 3,000. The actual year to date flow now stands at a 773 gain but as we have long warned this aggregate will soon turn negative. But also as we have warned, we think that it will not stay negative for a long period of time or get particularly large given that we see the NZ economy improving next year at the same time as in Australia the labour market gets hit by weakness in non-mining sectors.

The upshot however is that migration flows are now and for the next year will be acting as a restraint on strength in the NZ housing market.

Just for your guide, the number of Irish coming our way is finally heading skyward.



Are You Seeing Something We Are Not?

If so, email us at tony.alexander@bnz.co.nz with Housing Comment in the Subject line and let us know.

MAJOR OFFSHORE ISSUES

European Debt

In Brussels I attended a briefing by the Conference Board on the economic outlook for Europe and it ran like this. Assuming that a deal is cobbled together which for the moment satisfies the markets with regard to the three areas discussed below, Europe will grow at a slow rate of just 1.1% over 2012 from 1.6% this year and in the medium term continue to perform poorly as economies are suppressed by tightening fiscal policies and the effects which we learnt all about in NZ in the 1980s and early 1990s associated with necessary structural economic reforms aimed at boosting competitiveness.

Some general points from the extensive discussions surrounding the briefing are as follows.

The US has a 50% chance of slipping back into recession though the running assumption for most forecasters is that they will not. That assumption might seem a bit generous given the fall in confidence just recorded for consumers this week. But consumer confidence has been low for quite some time now so the new decline is not necessarily a signal of a fresh collapse in spending.

The main risks for China are considered to be medium to long term in nature. In the short term growth is expected to hold up with plenty of scope existing for the authorities to rapidly ease monetary and fiscal policies if needed to spread out over time the adjustments to rapidly growing problems associated with over-construction, bank debt, and over-valued property prices.

The global manufacturing cycle peaked early this year and has been trending down since, with clear fresh weakness evident in most of the PMIs released for October. Europe's manufacturing sector may be in recession.

A cyclical easing in a secular upward trend for commodity prices is underway. That is, long term prices are rising. But for now they are easing as growth forecasts get revised down, traders cut long positions, availability of finance to run such positions dries up.

United Kingdom firms have switched to a “wait and see” mode with regard to investment following a period when it had been rising. One senses the same sort of attitude in New Zealand.

Inflation rates globally are easing or set to ease as food and materials prices decline and this is taking pressure off monetary policies. Because changes in wealth are considered a less substantial influence on household spending in Europe than the United States this easing in cost of living increases will be one important factor behind household spending recording some growth in the coming year.

Ireland has an economy now growing with exports rising strongly on the back of a boost in competitiveness in spite of not having a currency which can decline. How? Internal devaluation, which means 15% - 20% falls in wages. This has happened because Ireland's economy is essentially modern competitive and flexible – able to adapt to change. In contrast the struggling Mediterranean economies are rigid, wages are falling only slightly, and resources struggle to move from uncompetitive to growing sectors. Hence since early this year Irish bond yields have been falling as investors have faith in the Irish economy and the ability of the government to service its debt and reduce it. The Irish government has also bitten the bullet and drastically tightened fiscal policy.

The UK is in a similar position with the markets giving the government the benefit of the doubt because of flexibility in the economy, rapid fiscal tightening, as well as the ability of the British pound to depreciate and assist the recovery effort.

But yields on Spanish, Greek and Italian debt have been rising on repayment fears associated with the inability of their economies to adjust to changing circumstances. Spain however is not generally on the radar when one talks of inability to roll over maturing debt because extensive moves have been made by the government to deal with bank problems and efficiencies. Government debt is around 60% of GDP rather than Italy's 120% and politics appears more stable than in Italy. The citizenry also see pain as necessary in the short term so there is an absence of rioting such as one sees in Greece, even though Spain's unemployment rate is over 20%. The Spanish economy and labour market are however still very regulated and it is not expected that growth will be particularly strong in the near future.

Italy's major problem is less bad fiscal policy (the primary surplus which excludes debt servicing is positive), but an extremely inefficient unadaptive economy which has performed very poorly over the past decade. Their problem is mainly an entrenched absence of growth.

France has a problem in that the do-nothing fiscal track involves a rising debt to GDP ratio. Fiscal tightening is needed in order to stop this and prevent a credit rating cut.

There are strong concerns about investors growing weary of Italian debt and the fact some €650bn worth must be rolled over in the next three years. The current European Financial Stability Facility can handle providing funding for Greece potentially out to 2020 if private sector investors won't touch their bonds. But there is no hope of bailing out Italy as things currently stand – hence the importance of leveraging up the EFSF.

For the entire Euro-zone growth slowed from 0.8% in the March quarter to 0.2% in the June quarter but some of that slowing was due to the interruption to global supply chains associated with the Japanese earthquake. That means there will be an upward bias to September quarter growth. In the December quarter which we now find ourselves in growth is however highly likely to be negative.

In the Euro-zone household savings rates are typically in the 10% - 15% range. Contrast that with New Zealand where courtesy partly of earthquake reinsurance payments we may have only just scraped into saving as opposed to dissaving territory for the year to March 2011.

Germany has benefited from the crisis in that interest rates are much lower than would otherwise be the case and in fact ten year government bond real interest rates are now negative. This helps drive a view that Germany should not begrudge helping out its recalcitrant southern cousins even though their economic management is lacking. In fact Germany has scope to ease fiscal policy as a helpful gesture.

One unique problem for Europe is that there is no pan-Europe banking system. Banks largely confine their operations to their own countries. That means those countries where imports exceed exports get funding not by local banks raising deposits from citizens of surplus countries (Greek banks getting retail deposits in Germany) but through the wholesale market. This is the interbank lending market which is far more important as a source of bank funding in Europe than it is in the United States. This gives a high vulnerability of European banks to jitters in the wholesale markets which American banks do not experience. This is why the recent collapse of Dexia bank happened – they have an especially high dependence upon interbank funding. They did not experience a run from retail depositors, just a sitting on their hands of other banks in cash surplus positions because of their financially frugal citizens.

This then is why the role of the European Central Bank in providing unlimited liquidity is so important and why much attention is being given right now to increasing liquidity having to be provided to French and Spanish banks. This is also why efforts to boost tier one capital ratios to 9% are not necessarily the issue – liquidity is the thing and the cost of it which is rising. Note also that Dexia flew through the stress tests of European banks undertaken earlier this year – and they still collapsed. There is high distain amongst economists for how worthless the stress testing exercises have been.

This affects us in New Zealand because we banks are in the same position. We are a large current account deficit country about to experience a fresh blowout in the deficit in the next three years. That means the financing requirement for us banks overseas will be rising and the recent decline in the proportion of our funding from offshore may not be sustained – hence one of the factors encouraging the recent credit rating cuts and why more may well be forthcoming if the easing in NZ household dissaving proves short-lived.

This bank financing and capital raising issue then cuts to the heart of one of the major concerns in Europe which I am trying to warn people (you) about also in New Zealand. If European banks are struggling to get private sector liquidity, and if they are to be forced to raise extra capital in the coming year, and if they must write off a higher proportion of their holdings of Greek debt than earlier thought (maybe 60% rather than 205), then one way to ease the burden is to shrink ones lending book. Credit conditions are set to retighten in Europe and one sees the same dynamic as highly likely to play out also in New Zealand in conjunction with a further widening of the gap between local wholesale interest rates (and the OCR) and bank lending rates due to rising funding costs for the 40% of our money (your debt) which e must get offshore.

Note that data this week for Europe have been poor with business confidence in Germany falling and the composite Purchasing Managers Index for the manufacturing and services sectors falling to its lowest level since mid-2009 and below the 50 mark. This implies recession in the Euro-zone.

Chinese Inflation

Growth is slowing but there has been little change in the level of concern recently regarding over-valued property prices, high debts, collapsing SMEs, social strife from widening income disparities, and excess infrastructure construction. The data are generally not considered reliable, understanding of the dynamics of the Chinese economy and the policy formation process is low, and with a leadership change next year policy uncertainty is greater than usual.

This week though there was a small bright sign in the form of the privately compiled (non-official) PMI for the manufacturing sector rising back into positive territory. One awaits the official version. Also, confidence has grown that the People’s Bank of China will soon ease monetary policy to cushion the economy not so much against slowing export growth stemming from rising labour costs, easing Western growth and a rising Yuan, but escalating debt issues. Sounds like Europe - except in China we are talking about banks losing money because of property lending rather than exposure to government bonds. That means then that the Chinese have replicated not the European problem, but the American one of too much lending for residential construction.

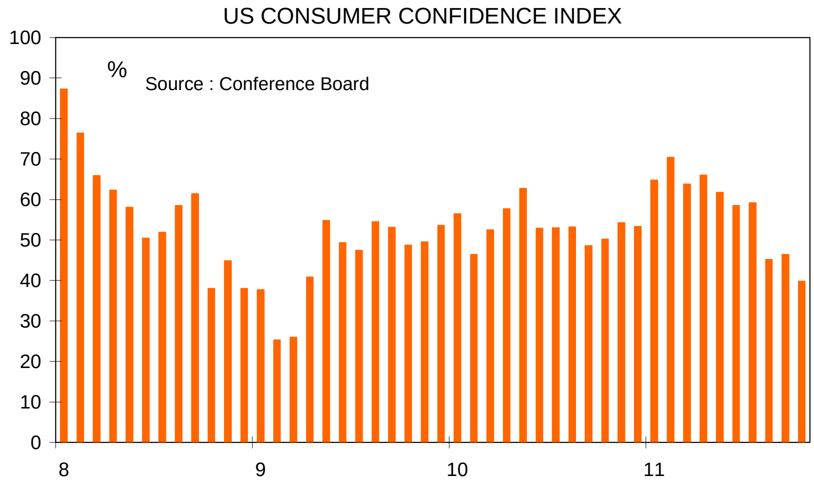
Just for your guide, here is 2010 data on where most of China’s exports go. Note that 24% of exports by value go to the EU and with some 25% of China’s US$3.2tn FX reserves in euros what happens in Europe is hugely relevant to China.

European Union	24%
United States	18%
Hong Kong	13%
Japan	8%
South Korea	4%
India	3%
Singapore	2%

https://www.uschina.org/statistics/tradetable.html

US Growth Momentum

Things are not looking as bad as they were a few weeks ago and few people are now talking about slipping back into recession. But no triggers or developments are apparent for consolidating growth above 3% and causing unemployment to track down from near 9%. The housing oversupply continues, consumers don't want to spend for fear of job losses and declining housing wealth. Large companies are cash rich, but SMEs are having trouble sourcing credit. Of worrying nature was the release of the monthly Conference Board measure of consumer sentiment which fell to a much lower than expected 39.8 in October from 46.4 in September. This is the lowest level for the survey in its 40 years barring a few months immediately after the Lehmans collapse.



Australian Growth

Same old story of a two speed economy with worries about retailing, housing, manufacturing and tourism, but decades-long boom in mining underway bringing a huge shift of resources in the economy and rapidly worsening skills shortages in WA in particular. But this means a very high vulnerability to changes in Chinese growth and risks there have shifted markedly to the downside recently bringing a 30% fall in iron ore prices which may delay commencement of some projects.

This week the major piece of news was the CPI for the September quarter coming in lower than expected bringing expectations that next week the RBA will cut its cash rate from 4.75% to 4.5%. A further cut is possible in February.

Aussie inflation is now 3.5% though the core rate preferred by the RBA is 2.5%. Common expectations are for headline inflation near 2% come the middle of next year.

Exchange Rates

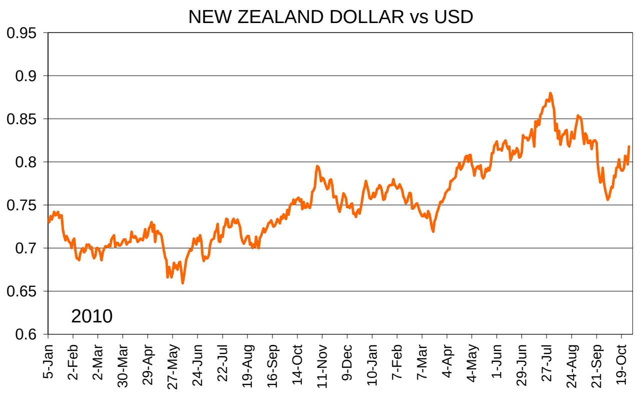
Exchange Rates	This Week	Week Ago	4 wks ago	Mths Ago	Yr ago	Consensus Frcsts yr ago*	10 yr average
NZD/USD	0.818	0.793	0.778	0.872	0.7485	0.689	0.629
NZD/AUD	0.766	0.779	0.794	0.796	0.7593	0.773	0.855
NZD/JPY	62.100	61.100	59.500	68.000	60.93	67.7	68.4
NZD/GBP	0.509	0.504	0.500	0.531	0.4723	0.448	0.368
NZD/EUR	0.578	0.575	0.576	0.601	0.5401	0.52	0.511
NZDCNY	5.194	5.043	4.981	5.619	4.987		4.83
USD/JPY	75.917	77.049	76.478	77.982	81.403	98.3	109.9
USD/GBP	1.607	1.573	1.556	1.642	1.585	1.54	1.705
USD/EUR	1.415	1.379	1.351	1.451	1.386	1.33	1.229
AUD/USD	1.07	1.02	0.98	1.10	0.99	0.891	0.737

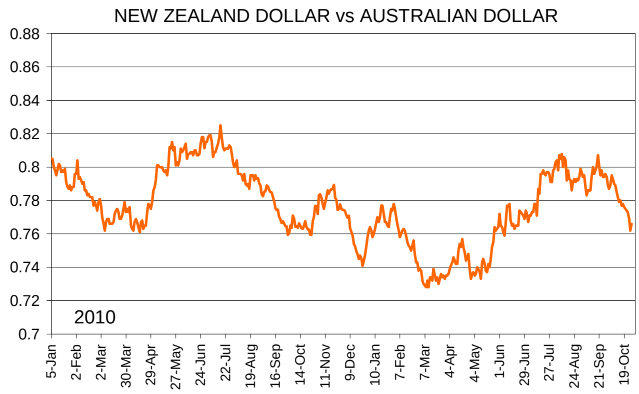
*Sourced from Consensus Economics. http://www.consensuseconomics.com/

Risk Aversion Dissipates – For Now

With investors giving the benefit of the doubt to European debt talks this week the NZD has risen against the greenback on a general movement toward risky assets around the globe. But we have fallen against the Aussie dollar mainly because our low inflation surprise was greater than their's. Having said that, the common expectation now is that the RBA will cut its cash rate next week by 0.25% to 4.5%.

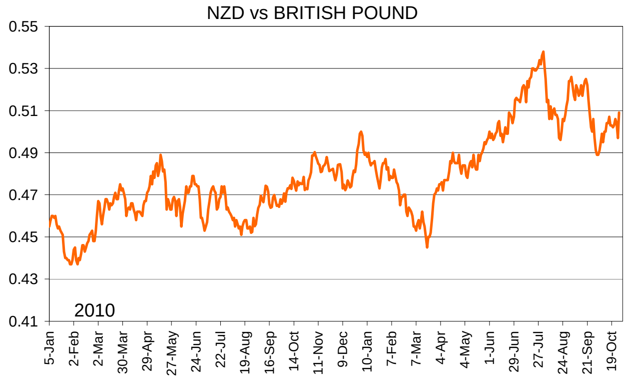
No time to write more plus one doesn't have to look far to find reasonable FX commentaries on the web these days. In the WO we concentrate on the areas in which we think we can add some value to the average SME operator and FX commentary is not an area we feel we can add all that much.





United Kingdom

The NZD has moved back above 50 pence on its way eventually to 55 – 60 pence assuming Europe does not implode.



Exchange Rate Assumptions

	2010	2011	Risk	2012	Risk
Year end					
NZD/USD	0.73	0.87		0.84	Higher
NZD/AUD	0.74	0.81		0.85	
NZD/YEN	64.2	68		72.0	
NZD/GBP	0.44	0.53		0.52	
NZD/EUR	0.51	0.60		0.60	
USD/JPY	88	78	Lower	86	Lower
GBP/USD	1.66	1.64		1.62	Higher
EUR/USD	1.43	1.45	Higher	1.40	Higher
AUD/USD	0.99	1.07		0.99	Higher

ECONOMIC DATA

All %		Latest qtr only	Previous qtr only	Latest year	Year ago	2 Yrs ago
Inflation	RBNZ target is 1% - 3% on average	0.4%	1.0	4.6	1.5	1.7
GDP growth	Average past 10 years = 2.6%	0.1	0.9	+1.5	0.5	-2.4
Unemployment rate	Average past 10 years = 4.8%	6.5	6.5	......	6.9	6.0
Jobs growth	Average past 10 years = 1.9%	0.0	1.3	2.0	0.0	-0.8
Current a/c deficit	Average past 10 years = 5.5% of GDP	3.7	3.6	......	2.5	5.6
Terms of Trade		2.3	0.8	7.0	12.7	-13.5
Wages Growth	Stats NZ analytical series	0.6	1.0	3.6	2.5	5.2
Retail Sales ex-auto	Average past 9 years = 3.9%.	1.0	1.0	1.3	1.9	-3.1
House Prices	REINZ Stratified Index	-0.2	1.1	-0.1	2.8	-0.9
Net migration gain	Av. gain past 10 years = 13,900	+773	3,867yr	......	13,914	17,043
Tourism – an. av grth	10 year average growth = 3.2%. Stats NZ	1.2	-0.1	1.2	3.9	-1.8
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Business confidence	BNZ survey	7	36	14	18	50
Consumer confidence	ANZ-Roy Morgan 100=neutral	113	113	101	116	120
Household debt	10 year average growth = 10.3%. RBNZ	1.2	1.2	1.5	2.4	2.6
Dwelling sales	10 year average growth = 2.5%. REINZ	21.1	21.1	-5.1	-33.1	43.7
Floating Mort. Rate	(TotalMoney) 10 year average = 7.9%*	5.59	6.09	6.09	5.59	6.49
3 yr fixed hsg rate	10 year average = 7.8%	6.99	7.15	7.15	7.95	5.99

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

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Key Forecasts

Dec. year		2010	2011	2012	2013
GDP	annual average chg	1.4	2.0 – 2.5	3.5 - 4.0	4.0 - 4.5
CPI	on year ago	4.0	3.0 – 3.5	2.5 – 3.0	2.5 – 3.0
Official Cash rate	end year	3.0	2.5	4.0 – 4.5	4.25 – 4.75
Employment	on year ago	1.3	2.0 – 2.5	2.0 – 2.5	2.0 - 2.5
Unemployment Rate	end year	6.8	6.0 - 6.5	5.0 - 5.5	<5.0

*extrapolated back in time as TotalMoney started in 2007