

BNZ Weekly Overview

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.

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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-l8ploskSGWgjN_7WOAw

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Just A Quick Point

For those thinking about where strong growth will lie in the planet over the next five years at least it pays to think in these terms. There is little chance fast growth will appear in the United States or Europe. That is not a view based upon an extrapolation of leading indicators but simply a recognition that the need to rein in fiscal deficits and take interest rates toward higher levels is so great any time firm growth approaches both policies are likely to be tightened.

That is, the US has a fiscal deficit near 10% of GDP and the stronger growth in GDP turns out the stronger the opportunity to rein in spending at a faster clip so ammunition is created in case another short term stimulatory package is needed down the track. In Europe investors are tired of ineffectual politicians unwilling to risk voter backlashes by reining in deficits, but that wariness of investors is placing the whole European economic and political model at risk. Recognising this those with an eye to the long term rather than the next election will ensure pressure remains to rein in spending more rapidly if and when strong growth looks imminent.

The same goes for central banks who desperately want to build interest rate buffers in case they need to one day once again make emergency rate cuts. If they see good growth ahead we can expect rate rises and explicit acknowledgement that although rises will crimp the expected good growth it is in the interests of improving monetary effectiveness and robustness against shocks.

Nothing more to write – still catching up on sleep after flying to the UK. Its cold here.

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.

Nothing new, so here are some summaries.

Are householders opening their wallets more?

We have no fresh information this week so here is a recap of household spending measures. They are mainly weak. Spending using debit and credit cards rose only 1.1% during the September quarter in seasonally adjusted and nominal terms. Allowing for inflation that means minimal volume growth if any. Household debt is averaging only 0.1% growth a month and for each the four months ending August lending for non-housing purposes declined. Registrations of cars in the three months to September were down 11% from a year earlier (pre-GST buying boosted last year though), and by over 5% in seasonally adjusted terms from the June quarter.

Dwelling sales in seasonally adjusted terms were up 2% in the September quarter. However this was a slowdown from 10% growth in the June quarter and the month of September recorded a fall of 2.3%. The improvement in residential real estate sales has slowed down though has not quite yet stalled. The number of consents issued for new houses to be built however was ahead 7.6% seasonally adjusted in the three months to August or by 16.2% if one includes the volatile apartments sector.

In addition we have the anecdotes regarding current retailing conditions submitted in our BNZ Confidence Survey. For the October survey complete two weeks ago 15 of the 21 replies from retailers noted current conditions as being weak.

Our interpretation of these indicators is that they show New Zealand consumers with their hands in their pockets by and large unwilling to spend.

Is business output rising?

No fresh data

Are businesses hiring more people?

Next Tuesday we will get the most up to date numbers on this from the Statistics NZ National Employment Indicator which is based on full population numbers of wage and salary earners reported to IRD by all employers each month. What we know at the moment is that in July the number of jobs was up 1% from a year earlier but down from June in seasonally adjusted terms by 0.3%. In the three months to July job numbers grew by 0.35% compared with 0.14% three months earlier and 0.24% three months before that. The data hint at an underlying trend toward accelerating growth in job numbers but the 1% pace is not

enough to make a dent in the 6.5% unemployment rate and if August is flat then the short term pace of improvement will drop away to less than 2% again. We read the data as showing jobs growth is weak

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/>

This question is always hard to answer in an up to date sense because we lack data which we think really give insight into what is happening. What we know is that the number of commercial vehicle registrations in the September quarter was about flat in seasonally adjusted terms after rising 16% six months earlier. But registrations in September were 32% stronger than a year earlier so maybe that is indicating a new lift. The value of consents issued for the construction of business-type buildings was about flat in the six months to August compared with a year earlier. However consents for farm buildings were ahead 24% so maybe this indicates a lift in farm investment at least. The value of imports of capital equipment in the three months to August was ahead 6.4% seasonally adjusted from the three months to May. So maybe there is some growth.

We also know that while tractor registrations in the September quarter were flat, farm sales for the same period were ahead 57% from a year earlier though flat from the June quarter.

Finally, business sector debt was only 1% of a year ago in August (farming down 0.6%). And in the three months to August business debt fell \$670mn (farming grew \$571mn).

The data suggest to us that things are picking up in the farming sector but across all sectors the picture is of mild growth perhaps.

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.

Nothing to write this week.

INTEREST RATES

Growth vs. Economic Slack

In a nutshell this is what drives inflation along with institutional arrangements, imported inflation, and exchange rate changes. If you want to forecast monetary policy you need to monitor these things. So we will, adding stuff here when we learn it. The current common view is rate tightening from March. Have we learnt anything this week which alters this outlook?

No fresh useful data to allow us to say much here has appeared this week.

Other Inflation Influencers

Rate Movements This Week

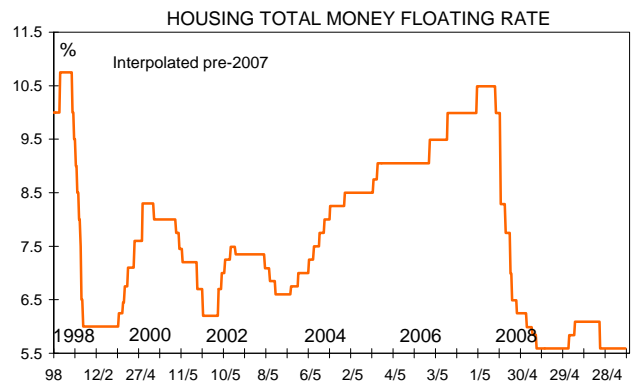
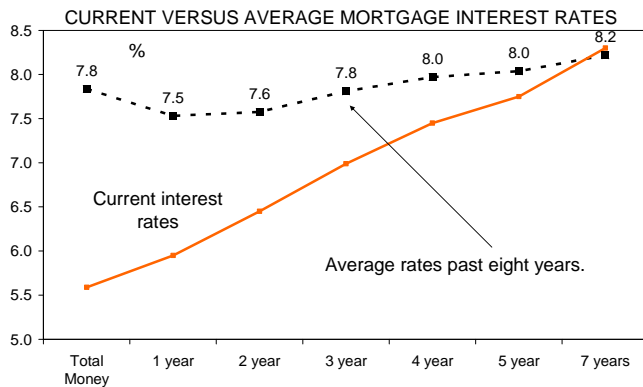
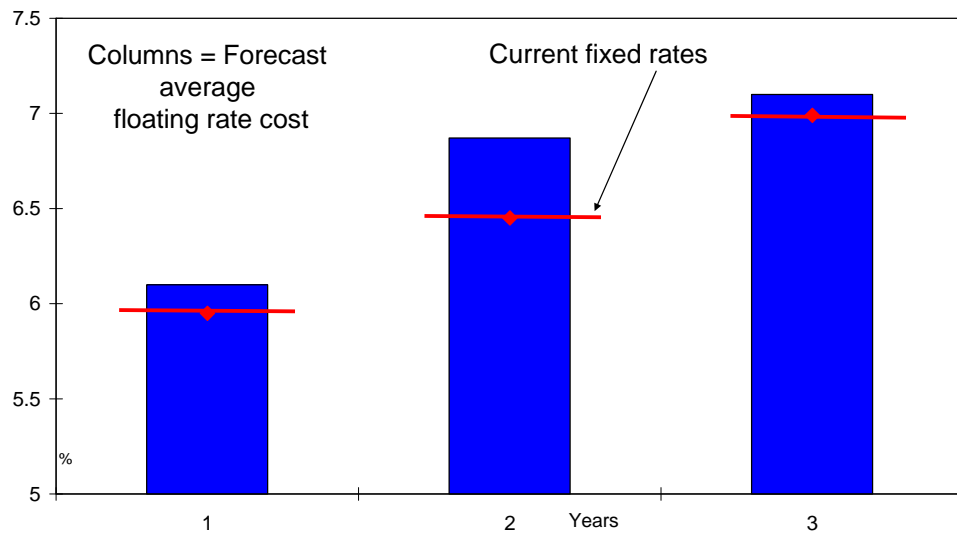
There have been no substantial movements in wholesale interest rates this week. Some of the deep growth worries have ebbed and expectations for the Reserve bank not touching the cash rate until 2013 have backed off thus putting a little bit of upward pressure on swap rates. Next week the Reserve Bank review their 2.5% cash rate and no change is expected given their recent expressions of concern about developments offshore.

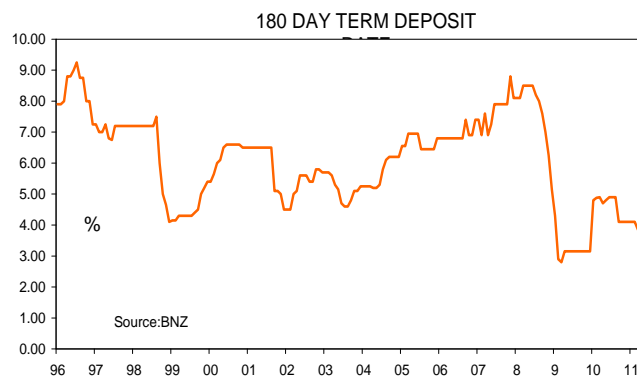
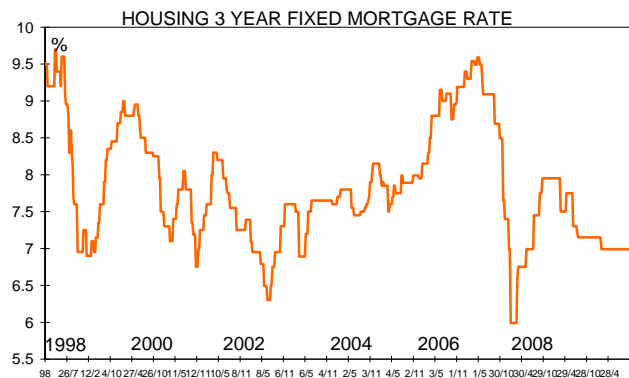
FINANCIAL MARKETS DATA

	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	3.01%	3.03	3.02	3.26	3.47	6.0
3 year swap	3.49%	3.44	3.46	4.05	4.05	6.2
5 year swap	4.05%	3.99	3.91	4.59	4.42	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 act (verb) like the quantity of money (noun) that one puts in the till first thing each morning. (It rhymes with bloat)





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 New

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

On Monday night the German Finance Minister dashed hopes for a quick fix to the European debt problem by warning this weekend's meeting of EU leaders would not likely result in a comprehensive solution to the crisis.

Standard and Poors cut Spain's credit rating by one notch from AA- to AA while Moodys cut it by two notches while also noting downside risks to France's rating. Their warning helped push the difference between 10 year bond yields in France and Germany to a ten year high. A lot of their concern will centre around the cost of France of bailing out its banks when Greece defaults – hence why the French want pooled money to do the job (use the EFSF) whereas the Germans favour forcing banks to first source private equity.

Chinese Inflation

The authorities took a move to clamp down on what is called shadow financing this week. This is finance supplied to generally small to medium sized companies and individuals by non-bank entities able to get around the rules restricting bank lending. One Chinese economics firm estimates that such lending account for 40% of all new loans in the first half of this year. As those bank rules have been aggressively tightened over the past year in order to stem credit growth and fight inflation cash-strapped companies have been forced to turn to shadow lenders to get finance banks can no longer supply them.

The trouble is that the interest rates charged are usually high if not usurious and an increasing number of companies are going bankrupt because they can no longer afford the debt servicing costs. To give monetary policy greater influence on economic activity and to stem the company collapses and suicides being caused

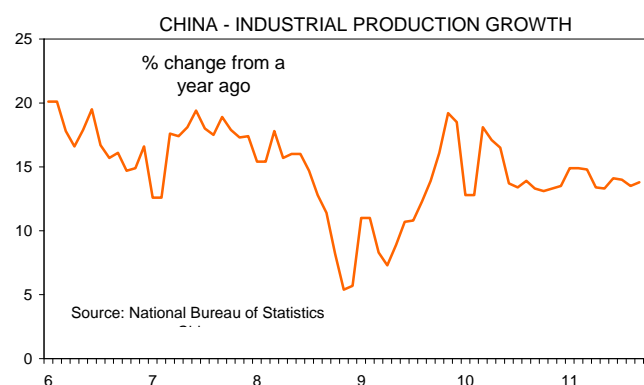
by shadow lending the authorities will prohibit any participation by bank employees in such lending – the issue there being that much of the money the shadow lenders supply itself comes from banks looking to get around lending restrictions. There will also be crackdowns on usurious interest rates and shadow lending generally.

What will be the outcome? On the face of it more firms going under earlier because finance dries up sooner. But the element of the vulnerable being ripped off by usurious money lenders will be reduced. However the Chinese government has also unveiled measures aimed at improving the flow of funds from banks to SMEs. The trouble there however is that China’s total banking sector is looking to be in worse and worse shape courtesy of some very bad lending and as investor shave been selling bank shares one of the State’s sovereign wealth funds has been stepping into the market to buy them – thus artificially propping up share prices.

This is great for those investors who want to reduce their exposure to a sector facing increasing problems. But such actions cannot hide the deteriorating fundamentals of the banking sector related to losses building and likely to accrue on property loans in particular. As bank lending tightens but buyers back away from pre-purchasing developers’ apartments amidst growing talk of a price bubble bursting developers will find themselves strapped for cash and having to aggressively discount apartments to generate revenue – in other words promote a price collapse spiral which will hit banks harder and harder, lead to further reduction in credit availability and so on. The United States once house prices started falling in mid-2006 in other words.

One important point to note here is that growing concerns about financing in China means there is very little chance that in the event of European collapse the Chinese would be able to loosen bank lending rules as happened in 2009. Problems they are fighting now largely stem from the instruction issued back then to banks to go forth and lend large – inflation, excess construction, displacement of people from their land, over-valued properties, high local authority debt exposure, high business debt levels, rising dependence upon shadow financing.

On the data front we learnt this week that China’s monthly trade surplus fell to a five month low with annual export growth at a seven month low in September of 17.1%. The rising Yuan coupled with a slowdown in advanced economies’ growth rates is causing a slowing in growth of China’s export sector and that will undoubtedly be making the authorities less willing to tolerate any pick up in the rate of appreciation of the Yuan.

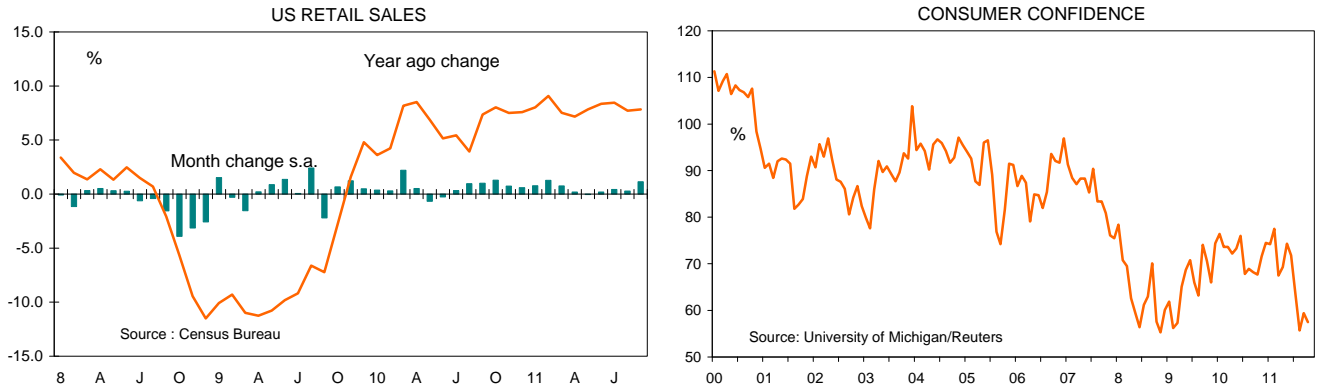


We also found out on Friday night that China’s annual rate of inflation eased to 6.1% in September from 6.2% in August.

The Chinese economy grew 9.1% in the September year from a year earlier which was down from 9.5% growth in the June quarter and a tad slower than expected. Industrial production growth in September from a year ago was 13.8% from 13.5% in August. Investment in fixed assets was up 24.9% from a year ago from 25% growth in August, and retail sales were ahead 17.7% from 17%. All reasonable numbers telling a story of an economy broadly slowing down but not at a yet worrying clip. The worries instead surround property prices, debt, and longevity of high inflation.

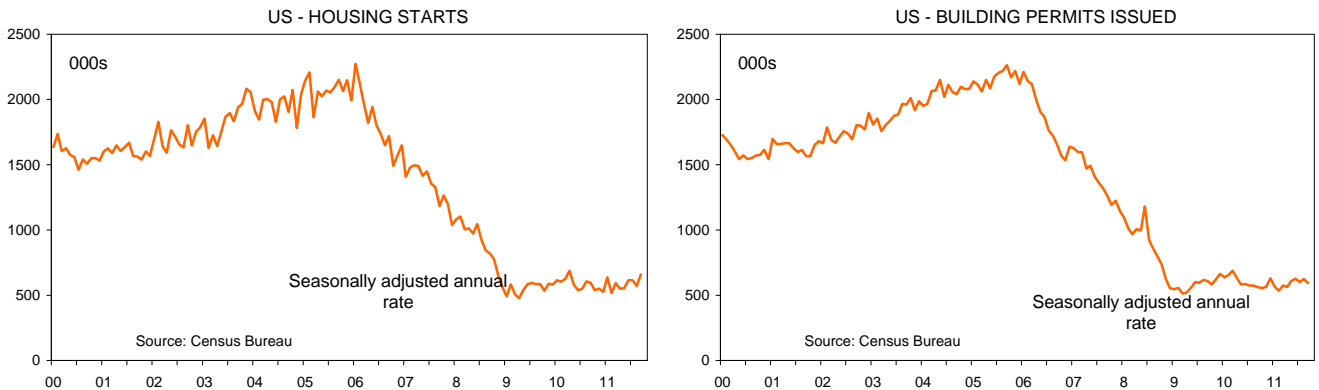
US Growth Momentum

The run of largely better than expected data has continued in the US over the past week with the best piece being retail sales which rose by a firm 1.1% in September rather than the 0.7% which had been expected. Sales excluding automotive sectors were ahead 0.6% in the month after gaining 0.5% in August and 0.4% in July. So it would appear that there is actually some strength developing in US consumer spending. The big question then is whether, seeing this, businesses will decide the time has come to start raising staff numbers again and boosting capacity. Related to that is the issue of whether the recent spending growth of about 8% from a year ago can continue if jobs growth does not pick up.



And things get a bit hard to figure out when one looks at the latest consumer confidence reading. The early estimate of confidence in October in the University of Michigan survey fell to 57.5 from 59.4 in September and an expected result of 60.2. Note the way in which retail spending growth has not been at all well correlated with confidence readings since June. The confidence measure actually suggests spending growth will soon plummet and that could easily dissuade retailers from boosting hiring in the short term.

There was a hint of housing getting better in the annualised number of housing starts rising unexpectedly to 658,000 in September from 572,000 in August. Note the low level of activity however shown in the graph here. Plus, the dwelling permits measure which is more forward looking fell in the month by 5%.



Australian Growth

Maybe next week.

Exchange Rates

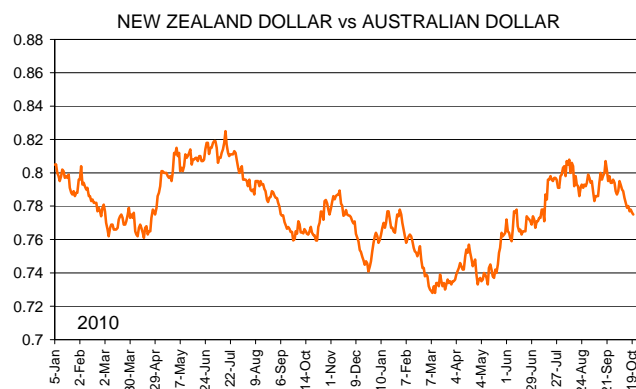
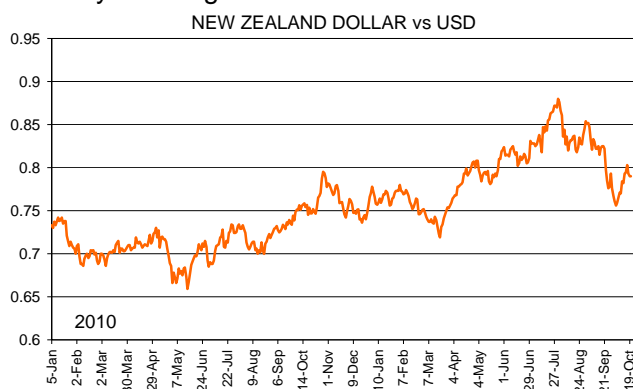
Exchange Rates	This Week	Week Ago	4 wks ago	Mths Ago	Yr ago	Consensus Frcsts yr ago*	10 yr average
NZD/USD	0.793	0.790	0.825	0.855	0.7452	0.689	0.629
NZD/AUD	0.779	0.775	0.807	0.798	0.7676	0.773	0.855
NZD/JPY	61.100	60.600	63.200	67.800	60.83	67.7	68.4
NZD/GBP	0.504	0.502	0.525	0.530	0.4746	0.448	0.368
NZD/EUR	0.575	0.575	0.603	0.605	0.5425	0.52	0.511
NZDCNY	5.043	5.040	5.269	5.526	4.951		4.83
USD/JPY	77.049	76.709	76.606	79.298	81.629	98.3	109.9
USD/GBP	1.573	1.574	1.571	1.613	1.570	1.54	1.705
USD/EUR	1.379	1.374	1.368	1.413	1.374	1.33	1.229
AUD/USD	1.02	1.02	1.02	1.07	0.97	0.891	0.737

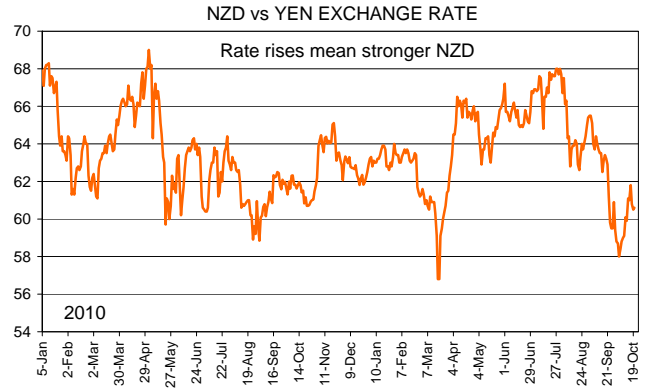
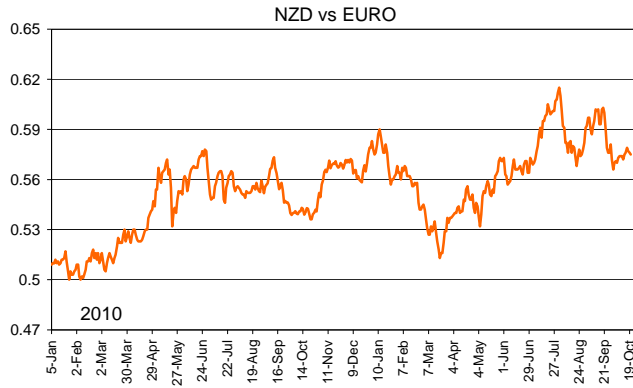
*Sourced from Consensus Economics. <http://www.consensuseconomics.com/>

Steady – For Now

The Kiwi dollar has ended the week where it started against the greenback near 79 cents and is little change don the crosses. That means of course that all the exchange rates we note above are broadly where they were a week ago. That is because we are going through a calm period at the moment where traders feel a rescue package will be put together for Europe and that recession will be avoided there and in the US partly because recent data have been better than expected. But generally fresh news has been absent and one can see a situation where the markets could easily get a fresh bout of the heeby geebies and move away again from risky currencies to current safe havens of the USD, JPY and CHF (Swiss franc).

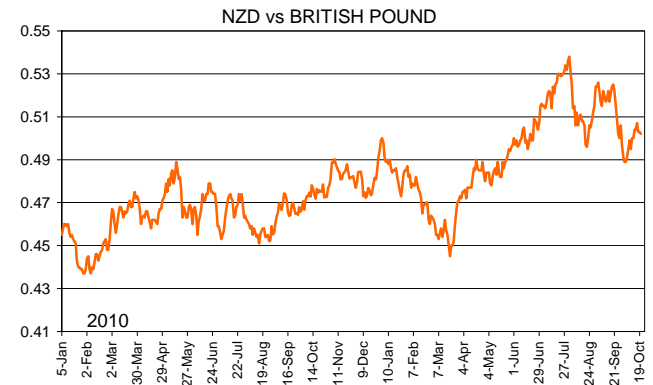
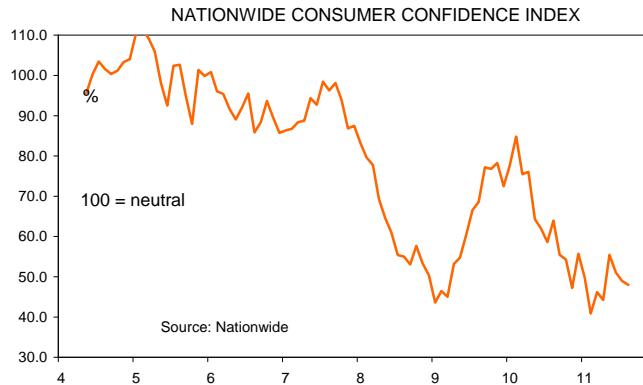
In other words, don't be fooled by the stability. This is all I am going to write there this week. I am in London right this moment and will be writing some deeper stuff about the crisis in the next couple of weeks before passing though Osaka and Beijing. The focus of everyone this coming week will be the EU Summit to be held over the weekend. The task for today however is identify a good place to watch the RWC final on Saturday morning.





United Kingdom

The monthly Nationwide Consumer Confidence Index eased one point in August to sit at 48 from 49 in July. Considering the turbulence surrounding Europe the result is not all that bad. In fact the Spending Index rose to 79 from 72. But at 48 the overall sentiment reading is still extremely low and suggestive of continued weakness in UK household spending in the near future. Commentary over here is decidedly on the downbeat side with regard to the state of the UK economy.



Inflation in the UK has just hit a near 20 year high of 5.2% but the Bank of England expect it to fall below 2% within a year as many one-offs leave the calculation. Hence they see little problem with planning to inject £75bn into liquidity in the next four months through a third round of bond purchasing.

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	1.0%	0.8	5.3	1.7	1.9
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	+2,257	4,625yr	14,507	15,642
Tourism – an. av grth	10 year average growth = 3.2%. Stats NZ	-0.6	0.9	-0.6	4.4	-2.8
		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.

The BNZ Weekly Overview is prepared by Tony Alexander, Chief Economist at the Bank of New Zealand. Ph 04 474-6744 tony.alexander@bnz.co.nz www.tonyalexander.co.nz

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

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