ASB

Markets Monthly

Local factors ignored as global forces dominate

- **New Zealand markets remain at the mercy of global forces.**
- **Although high NZ interest rates and slowing NZ growth will eventually extract a local response.**
- **Share prices have rebounded from mid March lows but market participants remain nervous.**

Global financial forces – in particular concerns about global financial firms and about the US economy – continued as the major theme over March. Markets for financial instruments and for commodities were volatile while New Zealand rate and price movements were largely dictated by the alternating international waves of fear and optimism.

The month started on a negative note as evidence of a US economy in recession mounted and as funding problems and credit downgrades occurred for some financial firms. Equities globally and the US dollar came under selling pressure. The turning point came mid month when large US investment bank Bears Stearns faced collapse and was baled out with the help of the US central bank. Following several policy initiatives by the "Fed", share prices tended higher in the second half of the month and fixed interest rates stabilised at the new lower level. But, overall, market participants remain nervous and it is very likely that more stories of difficulties will emerge – within financial markets, within the US 'real' economy, and eventually within other economies (as implied by the IMF this week putting the chance of a global recession at 1-in-4).

While local factors were dominated by global forces, there remains a growing tension between interest rates and profitability. Local interest rates remain high and there was only marginal repricing by 31 March of the prospect for lower interest rates this year, largely due to the Reserve Bank's warning that their current monetary policy stance will persist. But the evidence also mounts of a slowing local growth rate, falling housing activity and lower profit prospects, both within the export and the domestic sectors of the economy. The slowing local growth rate is likely to be of influence over the next few months, showing as greater expectations of lower interest rates and of a lower NZ dollar. Local equity markets are likely to continue taking their major cue from global equity markets.

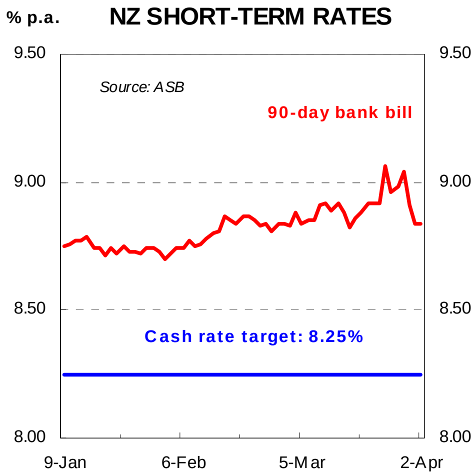
Date	Instrument	31-Mar-08	Month %	Quarter %	Year %	5-Year %
Cash	NZ cash rate	8.25	0.00	0.00	0.75	2.50
	NZ 90-day bank bill	8.91	0.07	0.02	1.00	3.09
	US 90-day bank bill	2.69	-0.38	-2.04	-2.66	1.42
	NZ - US 90-day bank bill	6.22	0.45	2.06	3.66	1.67
Fixed	NZ 5-year gov't stock	6.51	-0.37	-0.59	-0.09	1.02
Interest	NZ 10-year gov't	6.43	0.03	0.01	0.48	0.44
	NZ 10-year swap	7.64	-0.07	-0.12	0.37	1.24
	AUS 10-year gov't	6.10	-0.25	-0.26	0.20	0.77
	US 10-year gov't	3.44	-0.33	-0.64	-1.21	-0.37
Equities	NZ - NZX50 (NZ$)	2535	-4.3%	-15.4%	-19.5%	31.2%
	AUS - All Ords (A$)	5410	-4.7%	-15.7%	-9.5%	89.9%
	JAP - Nikkei (¥)	12526	-7.9%	-18.2%	-27.5%	57.1%
	UK - FT100 (£)	5702	-3.1%	-11.7%	-9.6%	57.8%
	US - S&P500 (US$)	1323	-0.6%	-9.9%	-6.9%	55.9%
	WORLD - MSCI (US$)	1437	-1.2%	-9.5%	-5.1%	92.0%
	MSCI in NZD (NZ$)	1786	0.0%	-12.8%	-15.8%	32.0%
Exchange	NZD/USD	0.805	-1.2%	3.8%	12.8%	45.5%
Rates	NZD/AUD	0.874	1.5%	-0.8%	-1.1%	-4.7%
	NZD/JPY	80.7	-5.5%	-7.3%	-4.0%	22.2%
	NZD/GBP	0.401	-2.2%	3.2%	10.4%	14.4%
	NZD/EUR	0.510	-5.1%	-3.1%	-4.7%	-0.3%
	NZ TWI	0.714	-2.6%	-0.9%	2.3%	17.2%
	EUR/USD	1.579	4.1%	7.1%	18.3%	45.9%

Equity indices are the respective end of month closes. Interest rates and exchanges rates are at 5pm NZ.

Chris Tennent-Brown – CBA NZ Economist – 649 374 8819 – chris.tennent-brown@asb.co.nz

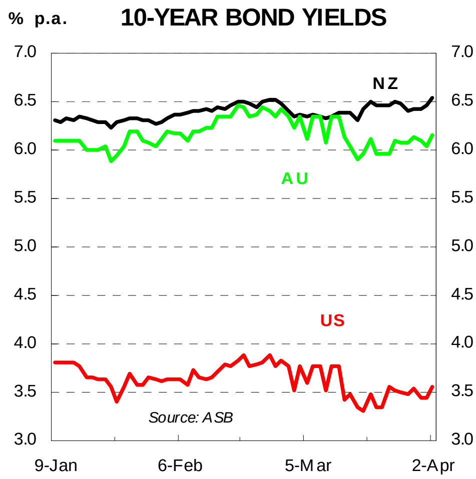
Cash

- The Reserve Bank of New Zealand (RBNZ) retained the 8.25% p.a. Official Cash Rate (OCR) at the March Monetary Policy Statement (MPS).
- Later in the month Governor Bollard also reiterated the RBNZ view that "we think the current setting of 8.25 percent with a flat outlook remains appropriate".
- Market pricing is for no change to the OCR in the next few months, but the odds of a late 2008 easing were put higher by the end of March.
- Global financial market tensions continued in March to push interbank interest rates above the typical premium to the OCR, being largely responsible for the higher bank bill yields recorded over March.



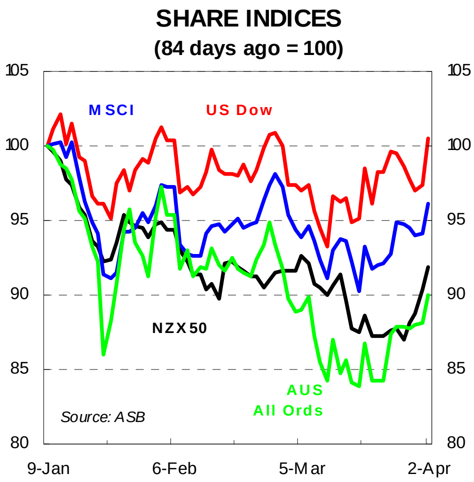
Fixed interest

- Local fixed interest investments were mixed over March. Most local fixed interest rates were lower by month end but not the 10-year Government Stock yield plotted opposite.
- The general global yield decline came mid March when US investment bank Bear Stearns encountered funding difficulties and around the time of the US central bank policy committee dropping the US overnight target rate by another 0.75% (to 2.25% p.a.).
- Towards the end of the month fixed interest yields did drift higher, following a rebound in global share prices.
- More generally, local fixed government rates and bank swap rates remain in a broadly sideways pattern, maintaining the levels reached last August.



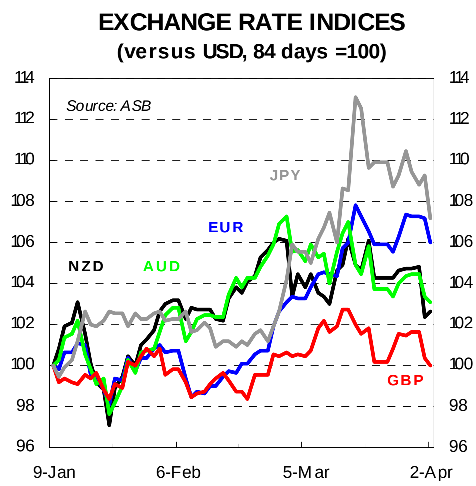
Equities

- Equity markets remained volatile during March with the lead still provided by US share markets.
- The general trend was downward in the first half of the month, with financial share prices in particular hard hit.
- The trend turned upwards in the second half of the month, following various policy initiatives by the US central bank to reduce the risk of a large bank failure in the US.
- The NZ market largely followed this international trend.
- Over the month the negative first half generally out-weighed the more positive second half, the NZ 50 Index being down for the month and a number of local share prices posting falls greater than 10% (although several reported price increases, such is the mixed nature of shares in general).



Exchange rates

- The volatility evident in other financial markets occurred in the currency markets, particularly against the Japanese yen.
- Both the yen and euro climbed to new recent highs against the US dollar, before retreating after the Fed easing.
- NZ dollar movements largely followed moves of offshore exchange rate, with the correlation between the NZ and Australian dollars noticeable.
- Although the RBNZ's warning of continued high interest rates in the first week of March probably contributed to the NZ dollar out-performing the Australian dollar over the next two weeks.
- The NZ dollar was largely unaffected by reports during the month of NZ activity and confidence decelerating in recent weeks.



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ASB ECONOMICS
Level 9, 135 Albert Street, Auckland

ASB GROUP ECONOMICS			PHONE	FAX
Chief Economist	Nick Tuffley	nick.tuffley@asb.co.nz	(649)374 8604	
CBA NZ Economist	Chris Tennent-Brown	chris.tennent-brown@asb.co.nz	(649) 374 8819	(649) 302 0992

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