

Business Weekly

Economy down, mortgage rates up

ECONOMICS

This Week

Production GDP declined -0.9% in the December quarter. Accentuating the positives, the fall was marginally smaller than the 1.1% we had expected. And, the extent of the fall was also mild compared to the substantial contractions reported in many other countries, particularly the hard-hit exporters in Asia.

The goods-producing sector bore the brunt of the decline, with manufacturing and construction falling sharply. Exports contracted sharply, with tourism exports in particular struggling over Q4. Consumer spending remained flat, although demand for cars has dropped dramatically. The pleasant surprise and silver lining in the result was the strength of the dairy recovery and resilience in the services sector.

We expect the economy to remain in recession for much if not all of 2009. The lagged effects on demand from credit crisis fall-out have yet to work through the economy. However, we have revised up our forecasts a touch. Towards the end of this year we expect some confidence to return and the economy to bottom out. Government spending on infrastructure projects will help support overall fixed investment, and the relatively low exchange rate should help maintain New Zealand's export competitiveness.

The outcome was close to the RBNZ's March MPS expectations and is unlikely to change the RBNZ's overall view of the weakness in the economy. If anything, the recent lift in the NZ dollar would be more in focus – given the RBNZ's outcome assumes prolonged weakness in the exchange rate. The recent jump in long-term fixed mortgage rates (see Chart of the Week) has also delivered tighter monetary conditions, though the RBNZ probably sees households and businesses as still having a range of very low rates to choose from.

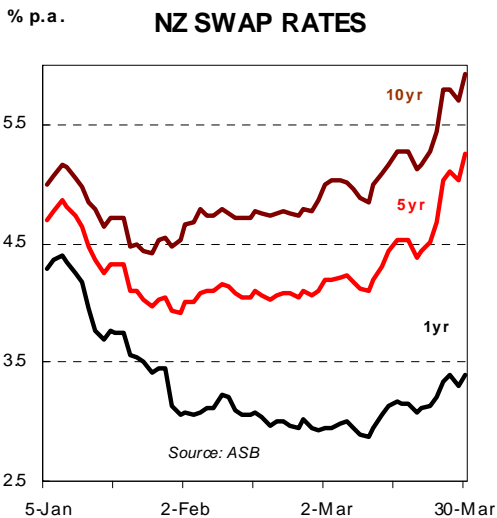
The mortgage market last week was a case of too many people trying to cram through the same entrance at the same time. Long-term mortgage rates have now rocketed to levels that in our view are no longer attractive outright, though still provide long-term certainty at an ok cost. If you haven't already made the jump it might be worth holding off or looking at shorter terms (e.g. 2-3 year) rather than acting in haste.

Over the rest of the week we have a range of second-tier data that includes credit growth, business confidence and the Crown accounts. February's NBNZ confidence result showed some signs of stability, and further stability or slight improvement will be a sign that the rate of economic contraction is not getting faster. US events, such as Friday's Payrolls and a Bernanke speech on the Fed's balance sheet, are the key ones.

Click here for:

- [Foreign Exchange](#) • NZD little changed against USD but up on other crosses.
- [Interest Rates](#) • Local rates sharply higher over the week.
- [Week Ahead](#) • Credit figures, business confidence, crown accounts
- [Week in Review](#) • Q4 GDP shrinks by 0.9%, current account deficit hits 8.9% of GDP
- [Global Calendars](#) • US Payrolls, US house prices, speeches by Fed officials

Chart of the week



- Swap rates have increased strongly over the past few weeks, which in turn has led to an increase in the longer-term mortgage rates.
- At the March MPS the RBNZ sent a strong signal that it is very close to the end of the easing cycle. Expectations are for the cash rate to be cut to 2.5%, which is higher than markets had been previously expecting, which caused longer rates to increase.
- In addition, there has been upward pressure on bond yields globally as markets anticipate a large increase in the supply of bond issuance from both corporates and governments over the next year.
- Recent increases in mortgage rates have increased demand to fix mortgages at current low levels. This demand is placing pressure on the swap rates, particularly at the 2-5 year range.

General Advice Warning

As this report was prepared without taking into account your objectives, financial situation or particular needs, you should not take any action in reliance of this report without considering your particular circumstances and, if necessary, obtaining professional advice.

Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	6 mths ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.5683	0.5650	0.5054	0.6850	0.8045	FLAT/DOWN	0.5600	0.5800
NZD/AUD	0.8219	0.8100	0.7833	0.8262	0.8730	FLAT/DOWN	0.8100	0.8250
NZD/JPY	55.67	54.42	49.30	72.91	80.21	FLAT/DOWN	53.00	57.00
NZD/EUR	0.4277	0.4134	0.3972	0.4724	0.5093	FLAT/DOWN	0.4150	0.4350
NZD/GBP	0.3977	0.3893	0.3541	0.3746	0.4007	FLAT/DOWN	0.3900	0.4000
TWI	56.9	55.9	52.0	64.5	71.4	FLAT/DOWN	54.00	58.00

Weekly support and resistance levels * Current is as at 12pm Tuesday; week ago as at Monday 5pm

- The NZD lifted on all the crosses last week, but was relatively stable against the USD compared to recent weeks. The NZD took last week's deteriorating Current Account Deficit and weak Q4 GDP data in its stride, and remained relatively strong. NZD hit the USD weekly highpoint of US 0.58 on the 26th, and hovered near the figure during NZ trade, but drifted off in London and NY trade on Friday night and is now down over 1 cent against the USD.
- After Tuesday's NBNZ business outlook survey, there is a dearth of local news, and the NZD will likely take its direction from offshore. We expect the NZD to trade sideways over the week, with risks to the downside after the remarkable rise over the past month.
- The European Central Bank's (ECB) interest rate meeting this week is likely to be pivotal for currency markets. We expect the ECB to announce it will buy government bonds and cut interest rates. EUR came under pressure last Friday after concerned comments from the German Finance Minister Steinbrueck. The G-20 meeting will also be keenly watched. A global approach to regulation is a possible outcome from the meeting which starts on 2 April in London.

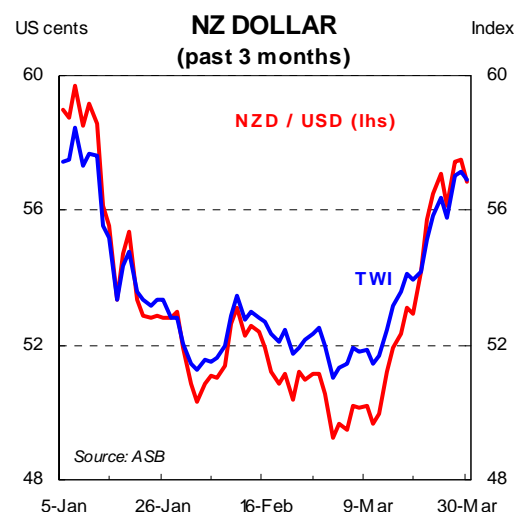
Short-term outlook:

Key data	Date	Time (NZST)	Market expects
March NBNZ Business Confidence	31/3	3.00 pm	-42.2
Crown Accounts	3/4	10.00 am	-
G-20 meeting	2/4		

Potential currency movers from the US this week: house prices, consumer confidence (31st), ADP employment survey, ISM manufacturing survey (1st), jobless claims, factory orders (2nd), non-farm payrolls, ISM services survey (3rd). Speakers: Plosser (31st), Bernanke (3rd).

Medium term outlook:

- As a consequence of the financial market turmoil centred in the United States, USD weakness was expected in early 2009. However, weakness is being offset in part by concerns about other regions.
- It is likely there has been an over-reaction by both the bond and currency market to the announcement the Fed will begin buying \$300 billion of long-term US treasuries as part of its quantitative easing (or credit easing) policy.
- This would mean we expect to see EUR, GBP, and JPY retrace some of March's large gains. We are also likely to see a pullback in the NZD/USD and to a lesser extent the NZD/AUD.
- However, we are also comfortable with our current forecast that the NZD and AUD are finding a bottom and will begin a slow appreciation over the course of 2009, rather than revisit and break through the lows seen in early 2009.
- NZD/USD and AUD/USD will lift as the USD eventually depreciates. But both the Australian dollar and the New Zealand dollar will remain weak vis-à-vis the major cross rates while global growth remains weak. Ratings concerns add to the weight on the NZD right now, and a rating downgrade is a key downside risk to our forecast.
- RBNZ Governor, Allan Bollard, revealed to the New Zealand Parliamentary Finance and Expenditure Select Committee on 4 March, the RBNZ were in the process of reducing the RBNZ's foreign exchange reserves from \$5 billion down to a benchmark rate of \$1 billion. Bollard also went on to say that the RBNZ aimed to intervene both at the top and bottom of the cycle to try and stabilise the exchange rate.



[\[Last Quarterly Economic Forecasts\]](#)

Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	3.00	3.00	3.50	7.50	8.25	FLAT
90-day bank bill	3.38	3.25	3.19	8.02	9.04	FLAT
2-year swap	4.13	3.52	3.27	6.97	8.29	UP
5-year swap	5.25	4.51	4.12	6.89	7.87	UP
11/11 gov't stock	4.49	3.99	3.88	5.62	6.50	UP
NZSX 50	2629	2591	2488	3248	3430	FLAT

* Current is as at 12pm Monday; week ago as at Monday 5pm

- 90-day rates lifted 13bp over the past week. The market has pared back the expectation of a rate cut from the RBNZ on 30 April: A 25bp cut is no longer fully priced in.
- Longer-term interest rates got hammered up last week through a number of events. The series of increases in long-term mortgage rates has progressively prompted more borrowers to fix. In addition, comments by the RBA Governor made the market less certain the RBA would cut at its upcoming meeting, pushing Australian interest rates higher. US Treasury yields have also been drifting up after plunging on the Fed's announcement it would buy US\$300bn of T-bonds over the 6 months (against that the Treasury issued \$98bn last week alone).
- In the closing days of last week the flow of fixed-rate borrowers was so extreme that it pushed swap rates up very sharply. That pressure continued on Monday morning. The lift in long-term swap rates triggered further increases in Government bond yields. Investors holding bonds have reduced their bond holdings in favour of receiving swap rates at the relatively high rates now obtainable.

Short-term outlook:

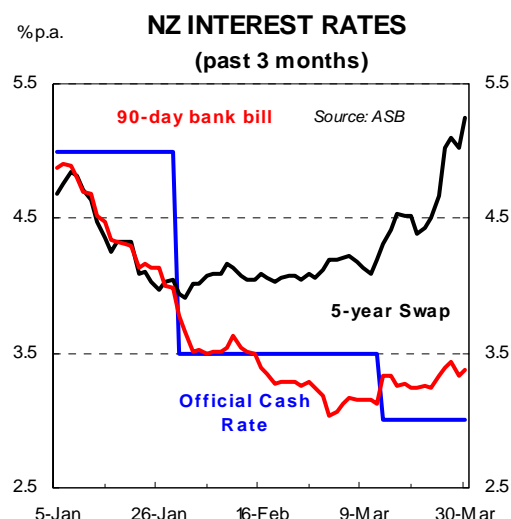
Key data	Date	Time (NZST)	Market expects
Feb NZ Govt Financial Stmt	3/4	10.00 am	-

Comment: Quiet week ahead for local data, the focus is now on April 7th – when we get both the Quarterly Survey of Business Opinion and the RBA cash rate announcement.

Medium term outlook:

- The RBNZ cut the OCR by 'only' 50 basis points at the March OCR review and Monetary Policy statement. The RBNZ has now cut 525 basis points off the OCR since July. The RBNZ sent a strong signal that it is slowing down the pace of rate cuts and is very reluctant to cut the OCR below 2.5%.
- Economic events since early march will not have changed the RBNZ's mind. However, conetary conditions have tightened appreciably since the MPS.
- In our view, the RBNZ's medium-term growth forecasts remain optimistic, with the economy exiting the recession by mid-2009 (we think end-2009 more likely). However, the RBNZ acknowledged the risk that the recovery may occur later and be more protracted than it anticipates.
- The RBNZ appears to have put a lot of weight on monetary and fiscal stimulus. The RBNZ are hoping for tax cuts, lower interest rates and the lower exchange rate to support the economy throughout the latter part of 2009. In particular, the RBNZ has a comparatively shallow downturn in business investment and a very strong recovery in export volumes (particularly given the extent of weakness in trading partner demand).
- The RBNZ's forecasts suggest a 2.5% OCR trough and two 25bp cuts over the April and June meetings seems the more likely path the RBNZ will take. Continuing to cut but only moderately buys the RBNZ some time whilst it assesses whether the bad news in coming months is no worse than expected or looking comparatively grimmer. As we think the RBNZ will have to revise down future growth forecasts there remains a possibility of the cash rate still going to 2%.
- Key signals to watch over coming months will remain the world outlook in general relative to RBNZ expectations, more specifically the state of the US housing market, and domestic private sector demand.
- The RBNZ has made it pretty clear it is not currently entertaining the use of alternatives policy measure (such as Quantitative Easing undertaken by other central banks) and has also discounted the likelihood of NZ rates dropping near zero. RBNZ is expecting extended weakness in the NZD to do much of the work for the Bank.

[\[Last Quarterly Economic Forecasts\]](#)



NZ Data Preview: a look at the week ahead

Data	Date	Time (NZST)	Previous	Market expects	ASB expects
Feb RBNZ Credit Aggregates	30/3	3.00 pm	-	-	-
March NBNZ Business Confidence	31/3	3.00 pm	-42.2	-	-
Crown accounts, 8 months to February	3/4	10.00 am	-	-	-

Tuesday 30 March

March NBNZ Business Confidence

Previous -42.2 (General) -20.1 (own activity)

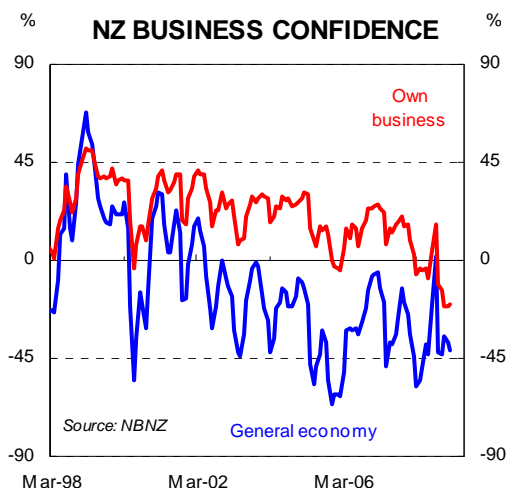
Business confidence remained weak in February, with general pessimism spreading. There was a slight improvement in the own activity outlook, however with net 20.1% expecting trading conditions to deteriorate the survey remains well into recession territory.

While business confidence remains weak and consistent with further declines in GDP it was somewhat reassuring to see the outlook had not deteriorated significantly since the previous survey. Policy response in the form of lower interest rates and fiscal stimulus are possibly helping improve confidence at the margin. Over the past few weeks we have seen market sentiment improve, particularly overseas as more details of government rescue packages have been released. Nonetheless, with demand remaining weak business confidence is likely to remain very weak for much of this year.

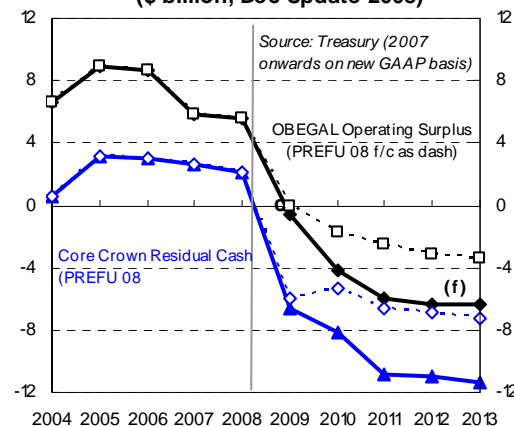
Friday 3 April

The Operating Balance excluding gains/loss (OBEGAL) for the 7 months to January 2009 was \$839mn behind the dated forecasts published in October (for the 6 months to December 2008 the balance was \$1.1 billion behind forecast). Consequently, the residual cash balance was running at a deficit of \$5,776m (\$8.26bn to Dec) and is \$1,069mn behind forecast (\$856mn to Dec).

The forecast comparisons made by Treasury are relative to the very outdated Pre-Election Update from early October, NOT the December Update. (The Treasury is required by law to report against the latest full economic and fiscal update, and the December Update was only partial). It is less clear how the actuals are tracking relative to the December Update. Qualitatively, the outcomes are weaker, given that the variances to forecast are slightly larger than the variances between the full-year October PREFU and December Update forecasts.



NZ KEY FISCAL BALANCES (\$ billion, Dec Update 2008)

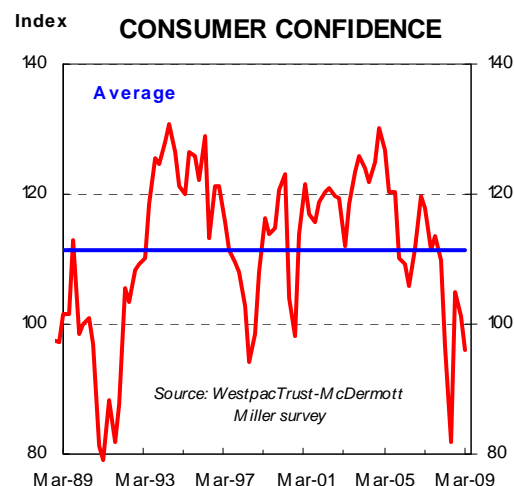


NZ Data Review: weekly recap

Q1 Consumer Confidence

Headline consumer confidence dipped back below 100, falling to 96 from 101.3 in Q4 2008. The headline, at 96 reflects pessimists outnumbering optimists, and is below the long run average reading of 111.

Although the cashflow situation has improved for many households over the last 6-12 months as mortgage rates have declined and petrol prices have eased, households have other worries right now. Unemployment is on the rise, house prices are falling, and every day households have a smorgasbord of gloomy economic news stories to digest. Reflecting the mood, only a net 10% of respondents said now is a good time to buy major household items. This is well down on the boom years for retailers a few years ago when around 50% of respondents were positive about perceived purchasing power. The survey is consistent with the weak consumption profile within our GDP forecasts for 2009.



Q4 Current Account Deficit

The current account deficit widened to 8.9% of GDP from 8.6% in Q3. The overall deficit was close to expectations, though the mix slightly different to our expectations. The goods trade balance held up better through stronger exports and softer than expected imports. The services trade balance was noticeably weaker. In part travel export earnings weakened with weaker tourism receipts, while imports of services were comparatively strong through higher freight costs. The investment income balance was also slightly weaker, largely as foreign direct investment income inflows took a hammering.

The extent of the deficit has been catching the eye of credit rating agencies and the expansion of the annual deficit could cause some concern (even if it was widely expected). However, a longer-term perspective should see a focus on the strong likelihood of the deficit reducing before too much longer. Moreover, the seasonally adjusted quarterly deficit did narrow over the second half of 2008.

Q4 GDP

Q4 GDP came in at -0.9% - slightly better than our expectation of -1.1% and the market expectation of -1.0%. GDP is now down -1.9% on year ago-levels and annual average growth has slowed to a pace of 0.2%. The goods-producing sector bore the brunt of the decline, with manufacturing and construction falling sharply. Exports contracted sharply, with tourism exports in particular struggling over Q4. Consumer spending remained flat, although demand for cars has dropped dramatically. The pleasant surprise and silver lining in the result was the strength in the dairy recovery and the resilience in the services sector (in particular finance insurance and business services).

We expect the economy to remain in recession throughout 2009. The lagged effects on demand from the credit crisis fall-out are still to work through the economy.

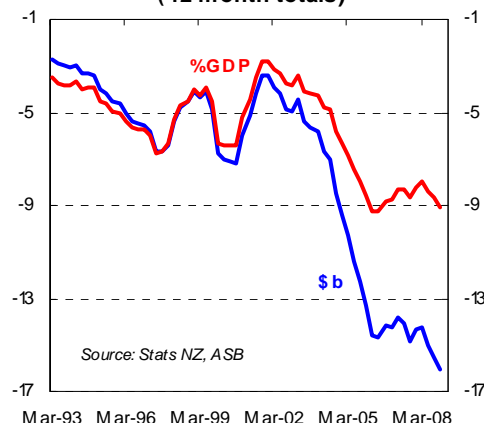
Feb Building Consents

The 11.6% mom rebound in dwelling consent issuance was driven entirely by a jump in apartment consents to their highest level since last September (193 in Feb vs. 67 in Jan.). Wellington had 137 apartment consents, with those apartments accounting for both the bulk of nation-wide apartment consents and the majority of Wellington's dwelling consents (215 in total).

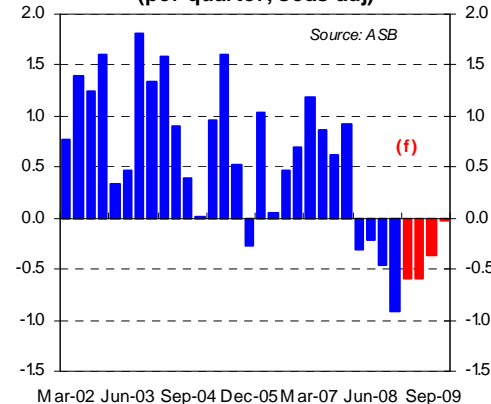
The level of ex-apartment consents remains very weak, though with a 0.3% increase did break a 9-month run of declines. In total, recent dwelling consent issuance points to another sizable contraction in housing construction in early 2009: we expect an 11% qoq decline in Q1 to follow the reported 14% decline in Q4.

The value of non-residential consent issuance remains, in contrast, more resilient: up 5.9% compared to February 2008 though down 5.3% when comparing the 3 months to February with the 3 months to November. We expect non-residential building construction will soften over 2009 after a fairly flat 2008, but the downturn will be milder than the marked slowing on the residential side.

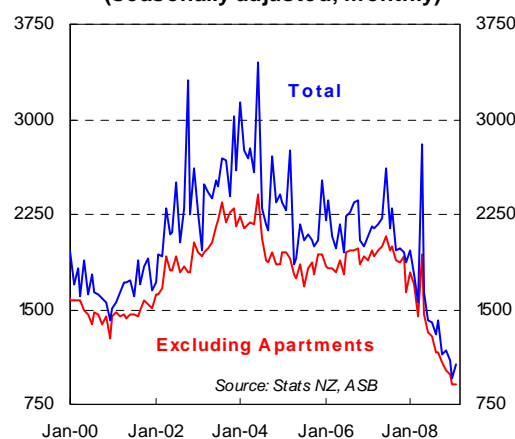
CURRENT ACCOUNT BALANCE
(12 month totals)



NZ GDP GROWTH
(per quarter, seas adj)



NZ DWELLINGS CONSENTED
(seasonally adjusted, monthly)



Global Data Calendars

Note: Calendar 2 is in UK times. Add 13 hours for NZ times.

Calendar – Australasia, Japan and China

Date	Time		Econ Event	Period	Unit	Last	Forecast		
	NZT						Market	ASB/CBA	
Mon 30 Mar	17.00	JP	Vehicle production	Feb	y%ch	-41.0	~	~	
Tue 31 Mar	12.30	JP	Jobless rate	Feb	%	4.1	~	~	
	12.30	JP	Job-to-applicant ratio	Feb	%	0.7	~	~	
	12.30	JP	Household spending	Feb	y%ch	-5.9	~	~	
	13.30	AU	Private sector credit	Feb	m%ch	0.6	0.5	0.4	
					y%ch	6.1	5.8	5.7	
	14.30	JP	Labor cash earnings	Feb	y%ch	-1.3	~	~	
	15.00	NZ	NBNZ business confidence	Mar	Index	-41.2	~	~	
	18.00	JP	Housing starts	Feb	y%ch	-18.7	~	~	
	18.00	JP	Annualised housing starts	Feb	saar	1.0	~	~	
	18.00	JP	Construction orders	Feb	y%ch	-38.3	~	~	
	18.00	JP	Small business confidence	Mar	Index	25.0	~	~	
	Wed 1 Apr	11.30	AU	Ai Group PMI	Mar	Index	31.7	~	~
		12.50	JP	Loans and discounts corp	Feb	y%ch	3.8	~	~
12.50		JP	Tankan large manufacturers index	Q1	Index	-24.0	-55.0	~	
12.50		JP	Tankan large manufacturing outlook	Q1	Index	-36.0	-52.0	~	
12.50		JP	Tankan non-manufacturing	Q1	Index	-9.0	-26.0	~	
12.50		JP	Tankan non-manuf outlook	Q1	Index	-14.0	-25.0	~	
12.50		JP	Tankan large all indust Capex	Q1	%	-0.2	-12.0	~	
13.00		AU	DEWR skilled vacancies	Mar	m%ch	-11.0	~	~	
13.30		AU	Retail sales	Feb	m%ch	0.2	-0.5	-1.2	
13.30		AU	Building approvals	Feb	m%ch	-3.7	1.5	3.0	
				y%ch	-33.5	~	-29.0		
15.30	CH	CLSA manufacturing PMI	Mar	Index	45.1	~	~		
18.00	JP	Vehicle sales	Mar	y%ch	-32.4	~	~		
Thu 2 Apr	13.30	AU	Trade balance	Feb	\$mn	970.0	700	1,500	
Fri 3 Apr	11.30	AU	CBA/Ai Group PSI	Mar	Index	32.2	~	~	
Sat 4 Apr	14.00	CH	PMI manufacturing	Mar	Index	49.0	~	~	

Calendar – North America & Europe

Please note all days and times are UK time, not local release day/times

Date	UK			Period	Unit	Last	Forecast	
	time	Econ	Event				Market	CBA
Sat 28 Mar	13.00	GE	IFO Mar. Business Climate Survey by Industry (Table)					
Mon 30 Mar	04.03	GE	Retail sales	Feb	m%ch	-0.9	~	~
	09.30	UK	Net consumer credit	Feb	£bn	0.4	0.4	~
	10.00	EZ	Business climate indicator	Mar	Index	-3.5	-3.3	~
	10.00	EZ	Consumer confidence	Mar	Index	-33.0	-33	~
	10.00	EZ	Economic confidence	Mar	Index	65.4	65.8	~
	10.00	EZ	Industry confidence	Mar	Index	-36.0	-35	~
	10.00	EZ	Services confidence	Mar	Index	-23.0	~	~
	15.30	US	Dallas Fed manuf activity	Mar	%	-57.3	~	~
Tue 31 Mar	00.01	UK	GfK consumer confidence	Mar	Index	-35.0	-35	~
	08.55	GE	Unemployment change	Mar	'000	40.0	~	~
	08.55	GE	Unemployment rate	Mar	%	7.9	~	~
	13.30	CA	GDP	Jan	m%ch	-1.0	-0.6	~
	14.00	US	S&P/CS home price index	Jan	Index	150.7	~	~
	14.00	US	S&P/CS composite-20	Jan	y%ch	-18.6	-18.5	~
	14.45	US	Chicago purchasing manager	Mar	Index	34.2	34.5	~
	15.00	US	Consumer confidence	Mar	25.0	28.0	~	~
Wed 1 Apr	15.00	US	NAPM-Milwaukee	Mar	Index	29.0	~	~
	08.55	GE	PMI manufacturing	Mar	Index	32.4	~	~
	09.00	EZ	PMI manufacturing	Mar	Index	34.0	34	~
	09.30	UK	PMI manufacturing	Mar	Index	34.7	35	~
	10.00	EZ	Unemployment rate	Feb	%	8.2	8.3	~
	13.15	US	ADP employment change	Mar	'000	-697.0	-650	~
	15.00	US	ISM manufacturing	Mar	Index	35.8	35.8	~
	15.00	US	Pending home sales	Feb	m%ch	-7.7	-2.0	~
Thu 2 Apr	15.00	US	ISM prices paid	Mar	Index	29.0	32.5	~
	15.00	US	Construction spending	Feb	m%ch	-3.3	-2.0	~
	09.30	UK	PMI construction	Mar	Index	27.8	~	~
	12.45	EZ	ECB announces interest rates	Apr	%	1.5	1.0	1.0
	13.30	US	Initial jobless and continuing claims					
Fri 3 Apr	15.00	US	Factory orders	Feb	%	-1.9	-1.2	~
	08.55	GE	PMI services	Mar	Index	41.7	~	~
	09.00	EZ	PMI composite	Mar	Index	37.6	~	~
	09.30	UK	PMI services	Mar	Index	43.2	43.8	~
	13.30	US	Change in non-farm payrolls	Mar	'000	-651.0	-660.0	~
	13.30	US	Unemployment rate	Mar	%	8.1	8.5	~
	13.30	US	Change in manuf payrolls	Mar	'000	-168.0	-160.0	~

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