

# Business Weekly

## Shutting the stable door

### This Week

Last week we commented on the stampede to fix mortgage rates and the pressure those flows were exerting on wholesale rates as banks had to re-jig their balance sheets.

The RBNZ eventually put out a [statement](#) on Wednesday, expressing its belief that “the rise in longer-term interest rates is unwarranted and inconsistent with the monetary policy outlook”. We agree that the lift in rates is inconsistent with the likelihood of short-term interest rates remaining low throughout 2009. However, the lift was entirely consistent with the laws of supply and demand.

The episode has revealed a practical dilemma for the RBNZ. It is reluctant to cut the OCR too much further, yet market reaction to this changed perception was one catalyst for higher mortgage rates. Going forward, very modest cuts (e.g. 25bp) will exert very little downward pressure on long-term rates but also risk minor repeats of this latest episode. Cutting by bigger amounts would do more to contain long-term rates for a period but very quickly put the OCR at the bottom end of the RBNZ’s comfort zone.

Should long-term rates remain too high for the RBNZ’s comfort it may need to consider other options. One is making a public commitment to keeping the OCR low for a long period, bolstering amongst borrowers, depositors and other financial market participants the expectation that short-term interest rates will be anchored at a low level. Doing so might help temper the demand for long-term borrowing to a degree and for a period of time. However, supply and demand forces are powerful, and sometimes words aren’t enough. Another possibility would be for the RBNZ, during times when the market is under pressure, to become active in the wholesale swaps market as a ‘receiver’: entering into swaps agreements to receive a fixed-rate payment for period in return for paying a floating payment. It was the relative dearth of these receivers when mortgage flows meant all the NZ banks needed to ‘pay’ fixed rates that caused swap rates to soar until the demand was met.

If you are a borrower what are your options? As we noted in last Tuesday’s [Home Loan Rate](#) report, the choice is no longer clear cut now that long-term rates have lifted so far so quickly. There is now a big trade-off to consider between remaining on very low floating/short-term rates against the certainty of high long-term rates. Which part of the spectrum suits will depend on your risk tolerance and cashflow priorities.

### Click here for:

[Foreign Exchange](#)

- NZD up on the USD, JPY and Euro. Little changed against AUD.

[Interest Rates](#)

- RBNZ jawbones interest rates, but the pay-side pressure remains.

[Week Ahead](#)

- NZIER Quarterly Survey of Business Opinion the highlight.

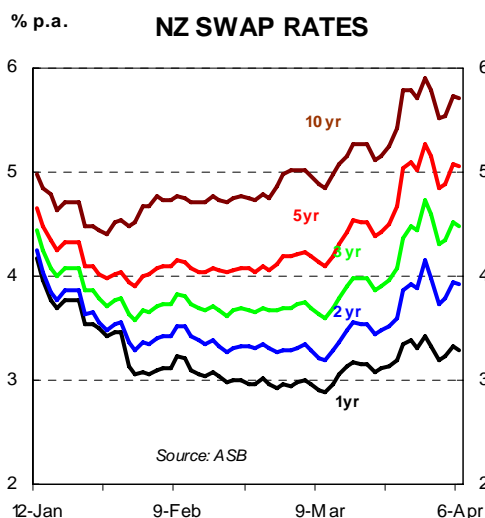
[Week in Review](#)

- Positive market mood continued offshore. RBNZ comments the local highlight.

[Global Calendars](#)

- FOMC minutes, RBA and BoE rate announcements the offshore highlights.

### Chart of the week



- Swap rates remain in focus these days. The wave of transfers from floating to fixed rate mortgages continues, and swap rates remain elevated as banks hedge their mortgage books in the swap market.
- The wave of almost panic-stricken mortgage rate fixing started in March and has seen an enormous amount of mortgage book ‘paying’ across the 2-5 year part of the swap curve, pushing all yields sharply higher. Corporates add to the pressure, as they lock in low long-term rates.
- As a result of this blow out in yields, the RBNZ issued a somewhat belated (but effective nonetheless) statement last Wednesday challenging the market’s move and perceptions of households. The RBNZ’s statement aimed to arrest the massive lift in swap yields, and calm a fairly frantic rush from borrowers to fix their mortgages. The result was a dip in swap rates last Wednesday, although ongoing paying pressure has seen rates lift off last Wednesday’s lows.

### 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

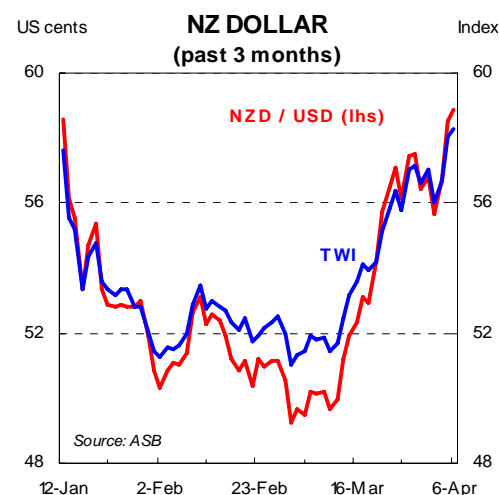
FX Rates	Current*	Week ago	Month ago	6 mth's ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.5888	0.5641	0.5013	0.6501	0.7827	FLAT/UP	0.5800	0.6050
NZD/AUD	0.8214	0.8207	0.7808	0.8651	0.8573	FLAT/UP	0.8100	0.8400
NZD/JPY	58.97	55.13	49.20	67.04	80.31	FLAT/UP	57.00	61.00
NZD/EUR	0.4354	0.4253	0.3986	0.4764	0.4999	FLAT/UP	0.4250	0.4450
NZD/GBP	0.3962	0.3960	0.3538	0.3694	0.3924	FLAT/UP	0.3900	0.4050
TWI	58.3	56.6	51.8	63.2	70.0	FLAT/UP	57.00	60.00

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

- The NZD lifted against the USD, Euro and JPY again last week, as the recent appetite for risk continued. The NZD was little changed over the week against the AUD and GBP.
- This week the RBA rate decision will be a key event for the NZD and AUD. The market is currently divided between expecting no change or a 50bp cut. An on-hold decision (the market expectation) would be a catalyst for AUD strength, and the NZD could get dragged along with the move. However, our Sydney-based economists expect the RBA to cut the cash rate by 50bp on Tuesday, raising downside pressure on AUD this week.
- The increased optimism about the world economy has pushed the USD lower, except against the JPY. The currency market appears to be ignoring the poor economic data when it is released. In the absence of a circuit breaker from any influential economic data this week, these trends are likely to continue.

### Short-term outlook:

Key data	Date	Time (NZST)	Market expects
Q1 NZIER QSBO	7/4	10.00 am	-
RBA Cash Rate Announcement	7/4	4.30 pm	3.25
FOMC minutes	9/4	6.00 am	-
Feb Retail Trade	14/4	10.45 am	-



**Potential currency movers from the US this week:** Potential currency movers from the US this week: consumer credit (7th), minutes from the Federal Reserve's previous meeting (9th NZT), jobless claims (9th). Speakers: Warsh (6th), Stern, Hoenig (9th).

### Medium term outlook:

- As a consequence of the financial market turmoil centred in the United States, USD weakness was expected in early 2009. Although this weakness was initially offset in part by concerns about other regions, improved sentiment in financial markets has seen risk appetites improve and the USD weaken.
- 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 will weigh on the NZD over the next 2-3 months, and a rating downgrade is a key downside risk to our forecast.
- RBNZ Governor, Alan 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	3.21	3.38	3.16	8.09	8.83	FLAT
2-year swap	3.92	4.15	3.29	6.84	8.16	FLAT
5-year swap	5.06	5.27	4.18	6.81	7.78	FLAT
11/11 gov't stock	4.46	4.56	3.80	5.64	6.46	FLAT
NZSX 50	2620	2642	2418	3183	3533	FLAT

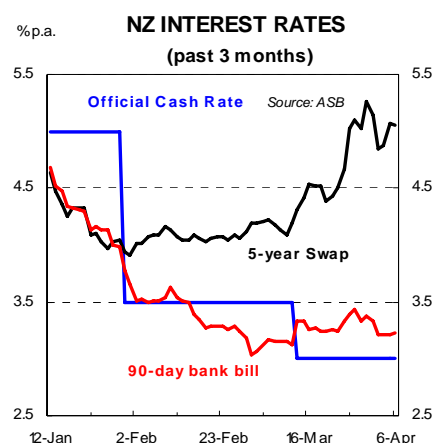
\* Current is as at 12pm Monday; week ago as at Monday 5pm

- The past week was a very volatile time for interest rate markets, with large intra-day moves. The key event was the RBNZ's unusual move of issuing an intra-meeting statement on Wednesday morning expressing its concern about the recent increase in longer term interest rates being 'unwarranted' and 'inconsistent' with their monetary policy outlook.
- The recent rise in longer-term mortgage rates simply reflects supply and demand. Since the RBNZ signalled the end of the easing cycle is close, there has been large demand from borrowers to lock in below average rates at longer terms. However, for every loan that is negotiated at a 5-year fixed rate, there must be a lender in the wholesale market willing to receive this interest rate for the next 5 years. This has put pressure on the wholesale swap market, where supply was already relatively thin at the longer end.
- Given the RBNZ's discontent, it has the option of cutting the OCR more aggressively than signalled (we are expecting only two more 25 basis point cuts) or becoming active in the wholesale markets. There will be a high threshold for either course of action. For the time being, the RBNZ can breathe slightly easier, as the demand for fixing appears to have eased slightly and interest rates across the yield curve have ended up lower than the start of the week.

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**Comment:** The RBA will be the key influence this week, with the market currently divided between expecting no change or a 50bp cut. Our flat bias reflects the markets uncertainty, although we slightly favour a cut. At home NZIER's Quarterly Survey of Business Opinion provides a very good guide for near term GDP.



- **Medium term outlook:** [\[Last Quarterly Economic Forecasts\]](#)
- The RBNZ cut the OCR by 'only' 50 basis points at the March OCR review and Monetary Policy statement. Sending a strong signal that it is slowing down the pace of rate cuts and is very reluctant to cut the OCR below 2.5%. The RBNZ has now cut 525 basis points off the OCR since July.
- Economic events since early March will not have changed the RBNZ's mind. However, financial market movements have seen monetary conditions tighten 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. The recent increase in the NZD and interest rates further undermines these forecasts.
- 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%.
- 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.

## NZ Data Preview: a look at the week ahead

Data	Date	Time (NZST)	Previous	Market expects	ASB expects
Q1 NZIER Business Opinion Survey	7/4	10.00 am	-77 (s.a.)	-	-
March QV House Price Change	9/4	-	-8.9%	-	-
Feb Retail Trade Survey	14/4	10.45 am	-1.1%	-	flat

### Q1 NZIER Business Opinion Survey

#### Previous: General Business Confidence - 77 (s.a.)

The Q4 Quarterly Survey of Business Opinion captured a collapse in business confidence in late 2008, and showed the weakest economic sentiment in the QSBO's 1970-onwards history. With a backdrop of falling activity, profitability, employment and investment, the survey results provided a strong warning that NZ's recession intensified in late 2008. General business confidence slumped under the weight of extreme pessimism, with net 77% expecting the general business situation to deteriorate. Own activity experienced in Q4 and expected activity for Q1 also proved absolutely dire.

We might see a slight recovery from the Q4 QSBO findings – in part because we all seem to be getting a bit more resilient to bad news! However, the monthly NBNZ business survey tells us businesses remained pessimistic in Q1, with very weak investment and employment intentions, and a contracting activity outlook. General business confidence and own activity expectations will remain firmly in negative territory. Investment intentions will be an important gauge the health of private sector activity in the first half of 2009.

### March QVNZ house price change.

#### Previous: -8.9% p.a.

Housing turnover has been sitting at low levels for the past six months or so, and we expect this weakness to continue in 2009, though low interest rates should stimulate some recovery in turnover over the year.

Prices are declining nationwide, and we expect this to continue over 2009.

Agent data show listings are at elevated levels, and a large overhang of unsold housing stock remains.

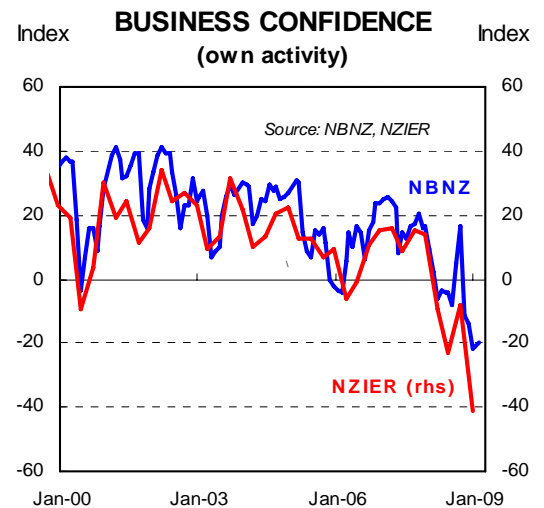
It is a buyer's market, and we expect price declines to reflect these conditions. QVNZ house prices showed national annual prices declined 8.9% in the year to February. We expect annual declines to remain in the 8-10% range in March.

### February Retail Trade Survey

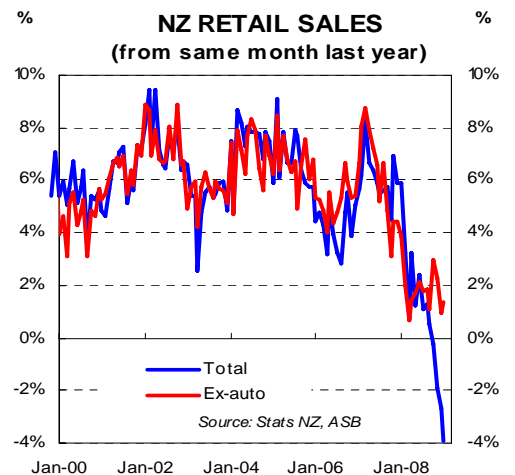
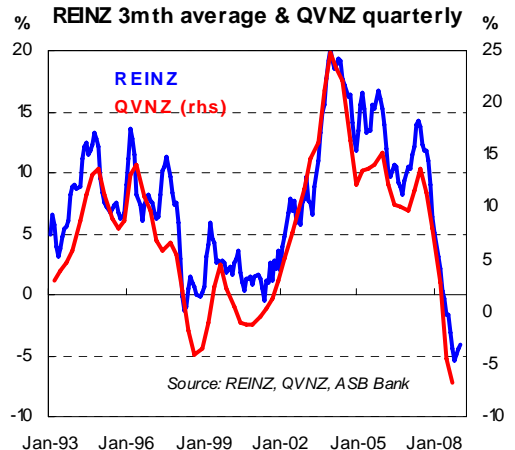
#### ASB f/c: flat

January retail sales posted a surprise decline, falling 1.1% owing to a very sharp drop in motor vehicle retailing, down 11% in January and down 24% on year-ago levels. Excluding the auto component, core retail sales increased just 0.3%, up only 1.4% on year-ago levels.

Looking to February's retail survey, petrol prices started to increase over late January, mostly due to the depreciating NZ dollar. 91-Octane lifted from a low of 132.9 in mid-January to 164.9 by mid-February. The rise in petrol prices is likely to see the spending on petrol retailing increase, at the expense of retailing elsewhere. Also providing some offset to the higher spend on petrol, vehicle registrations are pointing to another decline in motor vehicle retailing.



### NZ ANNUAL HOUSE PRICE GROWTH



## NZ Data Review: weekly recap

### NBNZ Business Outlook Survey

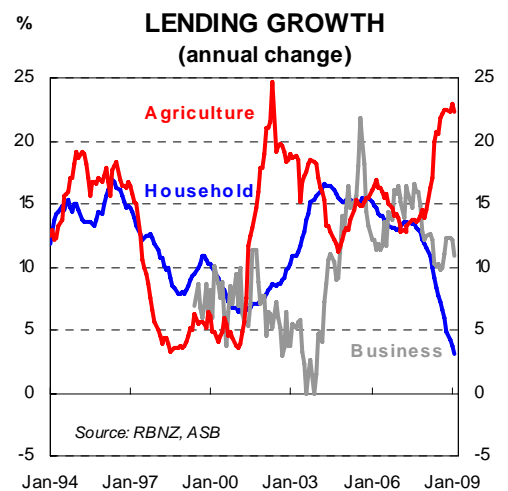
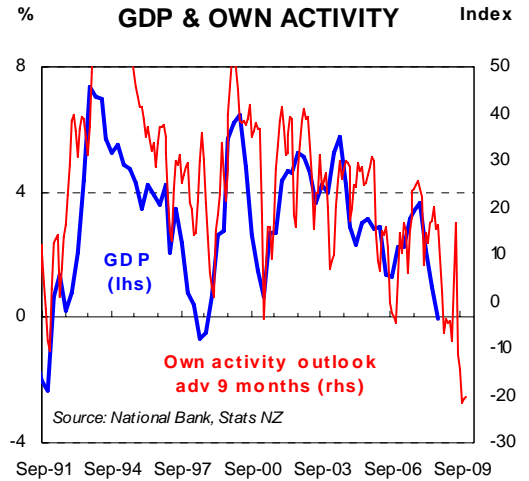
National Bank's latest monthly outlook survey remained weak in March. A net 39% expect deterioration in business conditions over the year ahead compared with a net 41% in February. Own activity expectations fell 1% in March. A net 21% are expecting tougher times for their own business over the year ahead. The result is only 1% off December's record low reading of -22.

The survey's composite growth indicator weakened further, and at current levels is consistent with -3% growth. (NBNZ's composite growth indicator uses the forward-looking activity indicators from the survey: own activity, investment intentions, employment intentions and profit expectations, combining them into a single index). In turn, the survey is consistent with our own outlook for economic contraction in all four quarters of 2009.

### RNBZ February credit growth

Annual household lending growth continues to decelerate, though in seasonally-adjusted terms the first 2 months of 2009 were fractionally stronger than the ending months of 2008. Lower interest rates appear to have brought some stability to household lending growth. Nevertheless, annual growth rates will continue to soften over the next few months, as the dollar amounts of fresh lending are only a small fraction of that seen in the first few months of 2008. Consumer lending has now flattened off.

Business lending growth has edged down after picking up in late 2008. Given the weakness in the economy lending growth is likely to moderate over the course of the year. Agriculture lending growth remains very robust at 22%, though is likely to slow noticeably over the rest of the year.



## Global Data Calendars

Note: Calendar 2 is in UK times. Add 11 hours for NZ times.

### Calendar – Australasia, Japan and China

Date	Time		Econ Event	Period	Unit	Last	Forecast	
	NZST						Market	ASB/CBA
Mon 06 Apr	13.30	AU	Engineering construction	QIV	q%ch	11.2	~	~
	13.30	AU	ANZ Job ads	Mar	m%ch	-10.4	~	~
	16.00	JP	BoJ monetary policy meeting	Apr	~	~	~	~
	17.00	JP	Leading index CI	Feb	Index	77.2	~	~
	17.00	JP	Coincident index CI	Feb	Index	89.6	~	~
Tue 07 Apr	~	JP	BoJ target rate	Apr	%	0.1	0.1	~
	10.00	NZ	NZIER business survey	QI	Index	-64.0	~	~
Wed 08 Apr	16.30	AU	RBA cash target	Apr	%	3.25	2.75	2.75
	~	NZ	QV house prices	Mar	y%ch	-8.9	~	~
	11.50	JP	Current account total	Feb	¥bn	172.8	~	~
	11.50	JP	Adjusted current account total	Feb	¥bn	258.0	~	~
	11.50	JP	Trade balance – BOP basis	Feb	¥bn	844.4	~	~
	12.30	AU	Consumer confidence	Apr	%	-0.2	~	~
	13.30	AU	Home loans- no of owner occ	Feb	m%ch	3.5	~	2.0
	13.30	AU	Value of all loans	Feb	m%ch	0.7	~	3.5
	17.00	JP	Eco watchers survey: current	Mar	Index	19.4	~	~
	17.00	JP	Eco watchers survey: outlook	Mar	Index	26.5	~	~
Thu 09 Apr	~	CH	Business climate index	QI	Index	107.0	~	~
	11.50	JP	Machine orders	Feb	m%ch	-3.2	~	~
					y%ch	-39.5	~	~
	13.00	AU	MI Inflation expectation	Apr	%	2.2	~	~
	13.30	AU	Employment change	Mar	'000	1.8	~	-10.0
13.30	AU	Unemployment rate	Mar	%	5.2	~	5.1	
13.30	AU	Participation rate	Mar	%	65.5	~	65.3	
Fri 10 Apr	~	JP	BoJ Monetary Policy Meeting Minutes for March					
Sat 11 Apr	~	CH	Trade balance	Mar	USD bn	4.8	~	~

## Calendar – North America & Europe

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

Date	UK		Econ Event	Period	Unit	Last	Forecast	
	time						Market	CBA
Mon 06 Apr	09.30	EZ	Sentix investor confidence	Apr	~	-42.7	~	~
	09.30	UK	Trade balance non EU	Feb	£bn	5,704	~	~
	10.00	EZ	PPI	Feb	m%ch	-0.8	~	~
	10.00	EZ	Retail sales	Feb	m%ch	0.1	~	~
	13.30	CA	Building permits	Feb	m%ch	-4.6	~	~
	15.00	CA	Ivey PMI	Mar	Index	45.2	~	~
Tue 07 Apr	09.30	UK	Industrial production	Feb	m%ch	-2.6	~	~
	10.00	EZ	GDP	QIV	q%ch y%ch	-1.5 -1.3	~ ~	~ ~
	20.00	US	Consumer credit	Feb	\$bn	1.8	-3.3	~
Wed 08 Apr	00.01	UK	Consumer confidence	Mar	~	43.0	~	~
	00.01	UK	NIESR GDP estimate	Mar	%	-1.8	~	~
	07.00	GE	Trade balance	Feb	€bn	8.5	~	~
	07.00	GE	Current account	Feb	€bn	4.2	~	~
	11.00	GE	Factory orders	Feb	y%ch	-37.9	~	~
	13.15	CA	Housing starts	Mar	'000	134.7	~	~
	15.00	US	Wholesale inventories	Feb	%	-0.9	-0.6	~
Thu 09 Apr	07.00	GE	CPI – EU harmonised	Mar	m%ch	-0.2	~	~
	09.30	UK	PPI	Mar	~	~	~	~
	09.30	UK	Visible trade balance	Feb	€mn	7,745	~	~
	09.30	UK	Total trade balance	Feb	€mn	3,585	~	~
	12.00	CA	Unemployment rate	Mar	%	7.7	~	~
	12.00	CA	Net change in employment	Mar	'000	-82.6	~	~
	12.00	UK	BoE announces rates	Apr	%	0.5	0.5	0.5
	13.30	CA	International goods trade	Feb	\$bn	-1.0	~	~
	13.30	CA	New housing price index	Feb	m%ch	-0.6	~	~
	13.30	US	Trade balance	Feb	\$bn	-36.0	-36.5	~
	13.30	US	Import price index	Mar	m%ch	-0.2	1.0	~
	13.30	US	Initial jobless and continuing claims					

ASB ECONOMICS  
Level 9, 135 Albert Street, Auckland

### ASB ECONOMICS

### PHONE

### FAX

#### Economics

Chief Economist	Nick Tuffley	<a href="mailto:nick.tuffley@asb.co.nz">nick.tuffley@asb.co.nz</a>	(649) 374-8604	(649) 302 0992
ASB Economist	Jane Turner	<a href="mailto:jane.turner@asb.co.nz">jane.turner@asb.co.nz</a>	(649) 374-8185	
CBA NZ Economist	Chris Tennent-Brown	<a href="mailto:chris.tennent-brown@asb.co.nz">chris.tennent-brown@asb.co.nz</a>	(649) 374 8819	

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