

Business Weekly

Out of the Noughties

This Week

Ten years on from when we wondered if our computers would ever turn back on the chronometer has turned over another big figure. For the first Weekly of the year we look some broad trends the move out of the Noughties is likely to bring.

NZ's economic recovery as reported so far has been more stabilisation than anything else. Very weak growth of 0.2% qoq in Q2 and Q3 still left a number of industries going backward. Over 2010 recovery will take firmer hold, though we see the recovery as a progressive lift in the growth rate rather than an explosive rebound. Although the recovery is initially household led (mainly through the housing market), some of the past two years' thrifty habits will persist as far as retailing goes. Housing construction is one area, however, that is likely to perform strongly. Business expenditure should start to recover in early 2010 after being impacted for much of 2009 by businesses' responses to deepening recession. However, there is still a degree of spare capacity in the short term, muting the need for expansion of productive capacity. In the short term government infrastructure work will continue to underpin construction activity. Export prospects will gradually brighten over the year, aided by close proximity to Australia, but the NZ dollar will remain a handbrake for some export destinations.

In NZ and globally there will be increasing attention on exit strategies from both the monetary and fiscal actions of the past 15 months. Higher interest rates are a matter of when not if (April to July the most likely window for the start in NZ). But turning around government fiscal positions will be the big elephant in the room – not just for next year. Investors are likely to discriminate between those governments demonstrating credible plans or actions to contain ballooning debt and those that don't. Being perceived as taking appropriate action will be important to contain the costs of servicing both government and private sector debt. Signals from NZ's Government and December's Half Year Fiscal Update suggest NZ will be one of those countries focussing on stemming the tide of red ink, important given NZ's high level of external indebtedness. In contrast, Greece is getting the wrong sort of attention and this year's UK election could keep UK bond investors wary.

Globally the first few years of this decade will be shaped heavily by the twin legacies of high household debt built up in the lead-up to the financial crisis and the monumental surge in government debt in response to the crisis. The pace of recovery in many Western countries will be constrained by these adjustments, which will take a long period of time to work through. But this decade is starting off better than the last one ended.

Click here for:

[Foreign Exchange](#)

- NZD lifted over the holiday period, and is back trading around USD 0.74

[Interest Rates](#)

- Interest rates lifted slightly over the holiday period.

[Week Ahead](#)

- NZIER's business survey, building consents and electronic card data due.

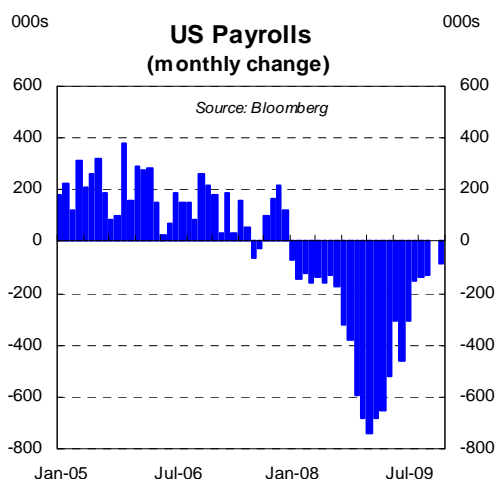
[Week in Review](#)

- November trade figures show the annual deficit continues to narrow.

[Global Calendars](#)

- UK, EZ & US CPI and Industrial Production, ECB rate decision, Beige Book due.

Chart of the week



- In the US the rate of job losses has been slowing for a number of months, though December's 85,000 job losses was a much weaker outcome than the flat outcome expected. As a partial offset November's 11,000 loss was revised to a 4,000 employment gain.
- The unemployment rate remained at 10%, but would have risen if it was not for a drop in labour market participation to 64.6%, a 24-year low.
- The rate of underemployment (which includes those in part-time work wanting to work longer hours or those who would like to work but have become discouraged from looking) rose to 17.3% from 17.2%.
- A separate report last week showed Europe's unemployment rate unexpectedly increased to 10%, which is the highest in 11 years.

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	0.7399	0.7225	0.7266	0.6237	0.5917	FLAT/UP	0.7250	0.7450
NZD/AUD	0.7960	0.8079	0.7932	0.8040	0.8359	FLAT/UP	0.7900	0.8050
NZD/JPY	68.48	66.76	64.46	57.62	54.00	FLAT/UP	67.50	69.50
NZD/EUR	0.5126	0.5036	0.4934	0.4480	0.4332	FLAT/UP	0.5050	0.5150
NZD/GBP	0.4603	0.4493	0.4454	0.3871	0.3895	FLAT/UP	0.4500	0.4650
TWI	67.0	66.1	65.2	59.2	57.7	FLAT/UP	66.00	68.00

^Weekly support and resistance levels * Current is as at 11am Monday; week ago as at Monday 5pm

- The shortened weeks through-out the Xmas and New Year period have seen an appreciation of the antipodean currencies. A lack of liquidity, an increased interest in JPY as a funding currency against the AUD and NZD, and a stronger than expected Australian retail trade report (last Thursday) all helped boost to the AUD & NZD.
- The highlight of last week was US Non-farm Payrolls on Friday. The weaker than expected report saw a broad USD sell off. The USD posted its biggest weekly loss since November against the majors, as the weak data weighed heavily on the greenback. The weakness saw the NZD testing the 0.7400 level.
- Expectations that the Federal Reserve will keep rates on hold for the foreseeable future have held the USD down. But we believe the US economy is close to a self-sustaining albeit weak recovery. The Fed has stated they will look at three indicators to help decide when to begin raising its funds rate: inflation, inflation expectations and resource utilisation (capacity utilisation and labour market). This week markets receive the latest readings for the CPI, capacity utilisation and jobless claims. These indicators are likely to further confirm the economy is slowly recovering and the risks are tilted to a modest recovery in the USD this week, which would cap the recent NZD rally.

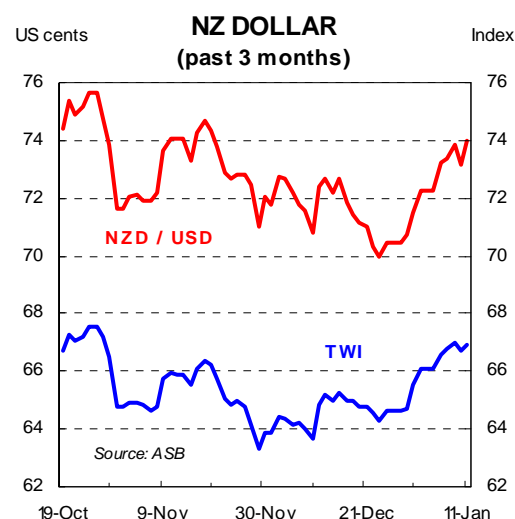
Short-term outlook:

Key data	Date	Time (NZST)	Market expects
NZIER Q4 QSBO	12/1	10.00	-
Nov Building Consents	14/1	10.45 am	-
AU Dec Employment Report	14/1	1.30 pm	+10 k

Potential currency movers from the overseas this week: US trade balance (12th), UK, EZ industrial production, Federal Reserve's Beige Book of business conditions (13th), ECB rate decision, US retail sales, jobless claims (14th), CPI, industrial production, capacity utilisation, consumer confidence (15th). Speakers: Bullard (10th), Lockhart (11th), Fisher, Plosser (12th), Evans (13th), Lacker (15th).

Medium-term outlook: [Last Quarterly Economic Forecasts](#)

- We continue to expect the NZD to appreciate further against the USD over the first half of 2010. The story remains primarily one of USD weakness, also overlaid by some Downunder strength.
- We expect the USD to remain under pressure until the Federal Reserve starts to unwind its policy stimulus: the earlier that starts the sooner the NZD's rise is likely to be capped.
- The reasons for the expected USD weakness remain similar to the drivers in place since mid-March 2009, namely:
 - US residents increase their offshore investment, encouraged by improvement in the global economy, with USD liquidity demand and safe-haven buying also no longer boosting the USD.
 - Diversification out of USD is expected to occur due to concerns about US government debt.
 - And, related, concern about the USD's future role as a reserve currency.
- In late 2009 the USD has responded positively to strong US data - a change from the pattern of the preceding 8 months. There is a risk that the USD troughs a lower level than our current forecasts imply.
- The NZD is also likely to mildly outperform other major currencies in the ongoing environment of improving global growth prospects and rising commodity prices. Outright weakness in the Pound will continue to hold the NZD/GBP rate at very elevated levels. The Pound, like the USD, is being weighed down by debt concerns and the state of its financial sector – both of which have ramifications for the future growth rate of the economy.
- The buoyant Australian dollar is also likely to contribute to an overall strengthening of the NZD. The RBA is likely to continue lifting its cash rate back to a less stimulatory level. Rising interest rates there will lift the AUD.



Interest Rate Market

Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	2.50	2.50	2.50	2.50	5.00	FLAT
90-day bank bill	2.79	2.80	2.78	2.80	4.70	FLAT
2-year swap	4.61	4.63	4.68	3.72	4.32	FLAT
5-year swap	5.57	5.61	5.63	5.19	4.72	FLAT
5-year benchmark gov't stock	5.47	5.53	5.51	4.68	4.40	FLAT
NZSX 50	3304	3219	3128	2737	2757	UP

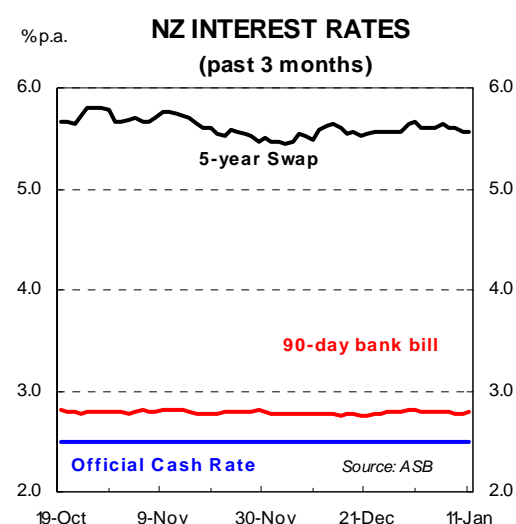
* Current is as at 11.00 am Monday; week ago as at Monday 5pm. Please note that we have recently changed the NZ govt 5-year benchmark bond to April 2015 maturity (from April 2013). This does cause some distortion in the comparison against the previous levels (i.e. month ago).

- The NZ yield curve has flattened slightly since the 21st of December, with the 1-year swap rate lifting 10 basis points and the 5-year up 3 basis points.
- Q3 GDP, released on 23rd of December, was close to market expectations and had had little impact on market pricing. Nonetheless, historical downward revisions to GDP over 2006 have policy implications (in our view). The revision suggests a lower non-inflationary rate of growth, which reinforces our view that the RBNZ will need to begin lifting the OCR by April (for more detail see [GDP report](#)).
- US 2-year Treasury yields rose sharply over the last two weeks of December, lifting from 0.9% to just over 1.1%. US\$118bn worth of 2, 5 and 7-year Treasury notes auctioned between 29th and 31st December, typically an illiquid period in the market, exacerbated the lift. Yields have since eased back, falling 17 basis points over the past week and dipping below 1% after the disappointing US Payrolls report.

Short-term outlook:

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NZIER Q4 QSBO	12/1	10.00	-
Nov Building Consents	14/1	10.45 am	-
AU Dec Employment Report	14/1	1.30 pm	+10 k
Dec Electronic Card Transactions	15/1	10.45 am	-
Dec REINZ House Sales and Prices	18/1	10.00 am	-

Comment: The NZIER Q4 Business Opinion Survey is the local highlight of the week, containing a range of important near-term economic indicators, although is not typically a market mover. Australian December Employment report will be more closely watched given future rate hikes are now more data dependent. REINZ data next Monday will give the RBNZ more food for thought, as it balances housing-related strength in the economy against the weak export outlook.



Medium term outlook: [\[Last Quarterly Economic Forecasts\]](#)

- The RBNZ continues to hold the cash rate at 2.5%. The RBNZ adopted a more hawkish tone at the December Monetary Policy Statement. The RBNZ now recognises the stronger economic outlook and the risks to inflation moving toward the upside. The RBNZ has moved forward its expected tightening to the middle of 2010, with the 90-day interest rate track now increasing from Q3 2010.
- The RBNZ has revised up its view on the economic outlook, with the composition of growth now more household led. The move acknowledges the recent strength in house prices as well as the improvement in consumer and business confidence. The RBNZ notes there is upside risk to spending growth given the strength of house prices, although points the weakness in household credit growth as indicating cautious consumer behaviour.
- The RBNZ has become more concerned on future inflation pressures, noting it has been surprised by the extent non-tradable prices have held up. The recession has not triggered a period of muted inflation; it merely appeared to wipe out the excess inflation pressure from the economy. There is no longer much scope for the RBNZ to absorb upside surprises to the inflation outlook other than to lift rates earlier than currently intended.
- The next move in the OCR is up, it's just a matter of when. We continue to expect the RBNZ will hike by April next year, as the strength in the housing market continues to test the RBNZ's patience. The RBNZ has a substantial amount of policy stimulus to unwind, the first steps are likely to be bigger (i.e. 50 basis point moves).

NZ Data Preview: a look at the week ahead

Data	Date	Time (NZST)	Previous	Market expects	ASB expects
NZIER Quarterly Survey of Business Opinion	12/1	10.30 am	35.8	-	-
Core Building Consents - November	14/1	10.45 am	+11.2%	-	+0.5%
Electronic Card Transactions - December	15/1	10.45am	+0.7%	-	-
REINZ House Sales and Prices (yoy house prices)	18/1	10.00 am	+6.6%	-	-

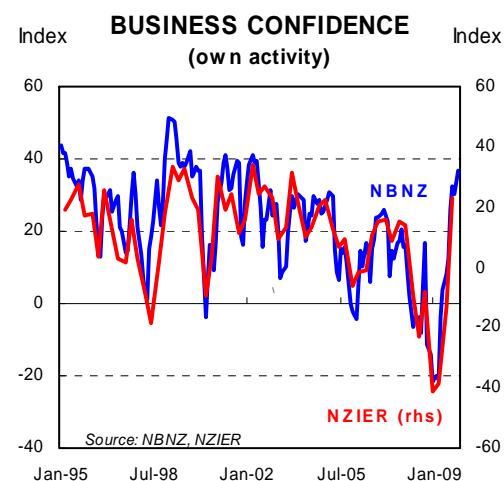
Tuesday 12 January

Q4 NZIER Quarterly Survey of Business Opinion

Previous: Headline 35.6, Own activity 26.6

While the monthly National Bank Business Outlook has shown a dip in headline business confidence in recent months, own activity expectations (which have typically been a more useful indicator for economic growth) have continued to climb. Accordingly, we expect the QSBO to show continued improvement in business confidence for the December quarter.

This reflects increased optimism amongst businesses that a gradual recovery in economic conditions is underway, which in turn has underpinned firms' expansion plans. We expect the improvement in investment and hiring intentions to flow through to real activity later this year.

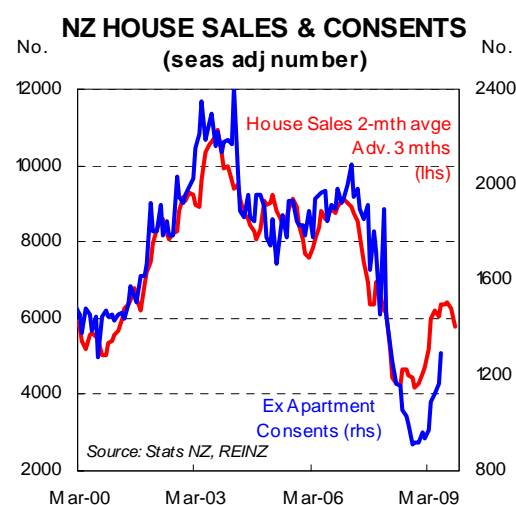


Thursday 14 January

November Building Consents

Previous: Core consents +11.2% MoM. f/c +0.5%.

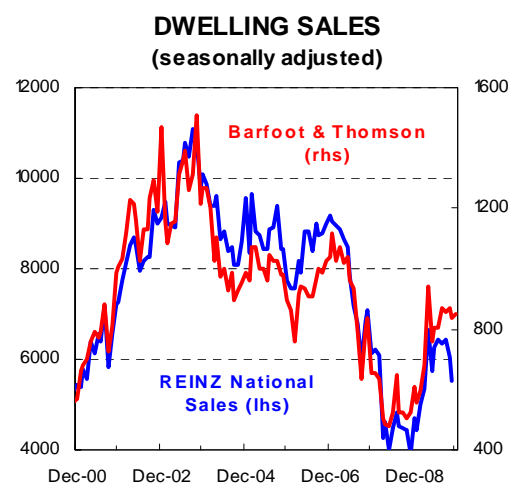
Dwelling consent issuance continues to make slow improvement. Total consent issuance increased 21% in October on year-ago levels, and was flat against September. In October, ex-apartment consents were up 23% on year-ago levels, and up 11.2% on September. Core consent issuance is now 77% up off its lows earlier in 2009. However, the recovery in residential construction is sluggish compared to the recovery in housing prices and demand. Low interest rates, improving sentiment and an increase in net migration have underpinned a lift in demand for housing. The recent increase in house prices should help stimulate new construction. Our residential forecasts are based on a steady pick-up in consent issuance over the next six months. Non-residential consents have remained comparatively steady over the past 18 months, and we expect this to continue.



Monday 18 January

REINZ House Sales and Prices

November REINZ data showed a low number in days to sell and relatively low turnover. Over the past 3 months the REINZ Monthly Housing Price Index has increased by 4.1%, and is up 6.6% on year-ago levels. We expect December's price data to continue show this trend. November's housing data painted a picture of strength in prices, but modest activity levels. There were also some very tentative signs that the momentum is slowing, with days to sell lifting fractionally as turnover slowed. However, Barfoot & Thompson December sales for the Auckland region showed turnover was up 1.6% on November (seasonally adjusted). B&T figures suggest that nationwide REINZ turnover will be roughly flat/slightly up in seasonally-adjusted terms relative to November. Mortgage approvals for December also showed some recovery on November in seasonally-adjusted terms.

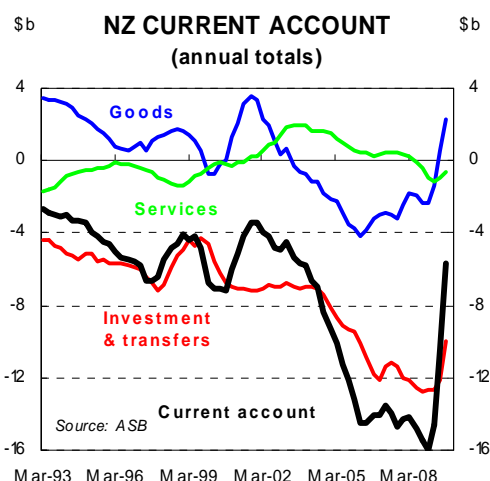


NZ Data Review: weekly recap

Balance of Payments – September quarter

The current account deficit narrowed dramatically in Q3 to 3.1% of GDP, smaller than market expectations of 3.5% of GDP. The quarterly deficit of \$1.41 billion (very close to our own forecasts of \$1.36 billion) was a substantially smaller deficit than normal, driven by one-off tax provisions by a number of Australian-owned Banks. The fall in profits resulting from these provisions saw the investment income deficit narrow sharply.

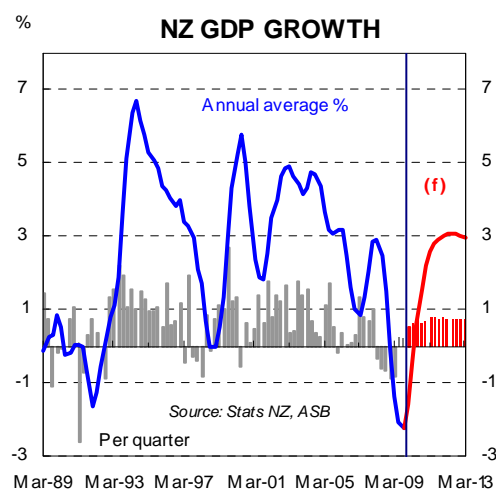
Excluding the one-off tax provisions, the underlying narrowing current account deficit has been largely driven by the weaker New Zealand economy. The lift on the trade side owes mostly to weaker import demand. On the income side, weaker profitability has reduced the outflow of profits to foreign-owned NZ companies. As the economy improves over 2010 and profitability and import demand recovers these trends are likely to reverse.



Gross Domestic Production – September quarter

GDP came out relatively close to expectations, increasing 0.2% over Q3, a fraction weaker than the market expectation (+0.4%) and a touch stronger than our own forecast (flat).

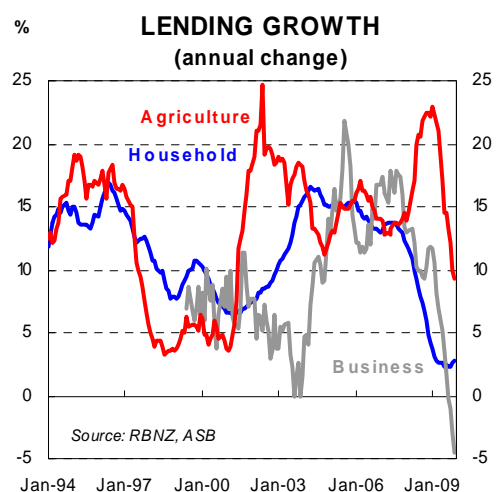
The report confirmed that the economy stabilised during the middle of 2009, although the recovery is not yet widespread as the results by sector remain patchy. The pick-up in housing demand (underpinned by stronger population growth) is leading the recovery with continued growth in areas related to stronger housing turnover as well as housing-related retail spending. However, the strength is yet to flow through to stronger housing construction. Manufacturing activity and business investment also continue to drag, although recent improvements in business confidence suggests a recovery over 2010 is imminent. Although, the recovery over 2010 is likely to be relatively subdued (compared to previous recoveries), it still has potential to be reasonably inflationary, and more so than the RBNZ are currently projecting.



RBNZ Credit Aggregates - November

Mortgage lending growth continues to sit near \$500mn per month. November's \$491mn of net new lending was down slightly relative to October, mirroring softer house sales (seasonally adjusted). RBNZ mortgage approvals dipped in November by our seasonally-adjusted estimate before recovering in December, implying lending may have finished the year in reasonable shape for the time of year. Consumer lending grew in November, only the second month of 2009 to register a higher balance than in the preceding month. Annual growth in consumer lending remains deeply negative, reflecting the added caution that has gripped consumers. Consumer credit does generally lift in the lead-up to Christmas and November's \$80mn lift was slightly more than half the average lift of the preceding 5 years.

Household credit growth is continuing to recover gradually, though at this point the pace will not concern the RBNZ much. Meanwhile, businesses' demand for credit remains weak, reflecting the cut-back by businesses on capital expenditure.



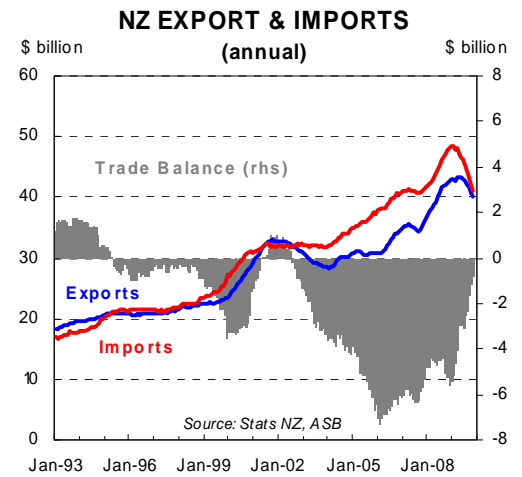
Trade Balance - November

The Trade Balance posted a deficit of \$269 million in November, bringing the annual trade deficit down to \$846 million from \$1.12 billion in October. The sharp improvement in the trade balance over the past year mostly owes to the sharp drop in import values (due to very weak domestic demand), compared to a more muted decline in exports.

Dairy exports remain 25% below year-ago levels, due to the sharp decline in dairy prices as the financial crisis intensified in 2008. More recently, dairy prices have begun to recover on spot markets, which has boosted the value of dairy exports over the past few months.

Much of the decline in imports over the past year is due to a 34% decline in intermediate goods. Declines within this category have been widespread, owing to both lower prices and volumes, with the largest contribution to the decline coming from lower oil prices.

As the NZ economy begins to recover over 2010, import demand is likely to pick up and limit further improvements in the trade deficit.



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 11 Jan	~	CH	Trade balance	Dec	US\$bn	19.1	20.9	~
	12.30	AU	TD Securities Inflation	Dec	m%ch	0.3	~	~
					y%ch	2.1	~	~
Tue 12 Jan	10.00	NZ	NZIER business opinion	QIV	Index	36.0	~	~
	14.50	JP	Adj Current Account Total	Nov	¥bn	1,376	~	~
	14.50	JP	Trade Balance - BOP Basis	Nov	¥bn	949.0	~	~
	13.30	AU	Housing finance	Nov				
			No of own-occupiers		m%ch	-1.4	~	-6.0
			Value of all loans		m%ch	-1.7		-4.0
Wed 13 Jan	13.30	AU	Lending finance	Nov	m%ch	-1.7	~	~
	13.30	AU	Labour force	Dec				
			Employment change		'000	31.2	~	25.0
			Unemployment rate		%	5.7	~	5.9
			Participation rate		%	65.2	~	65.3
	19.00	JP	Machine Tool Orders	Dec	y%ch	-8.4	~	~
Thu 14 Jan	10.45	NZ	Building consents	Nov	m%ch	11.7	~	0.5
	12.50	JP	Machine Orders	Nov	m%ch	-4.5	~	~
					y%ch	-21.0	~	~
	12.50	JP	Domestic CGPI	Dec	m%ch	0.1	~	~
				y%ch	-4.9	~	~	
Fri 15 Jan	10.45	NZ	Card spending	Dec	m%ch	0.7	~	~

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
Mon 11 Jan	13.15	CA Housing starts	Dec	'000	158.5	160.5	~
	13.30	CA Building permits	Nov	m%ch	18.0	-1.5	~
Tue 12 Jan	00.01	UK RICS House Price Balance	Dec	%	35.0	37	~
	09.30	UK Total Trade Balance	Nov	£mn	-3,213	-3,000	~
	09.30	UK DCLG UK House Prices	Nov	y%ch	-2.2	0.6	~
	13.30	CA Int merchandise trade	Nov	\$bn	0.4	0.8	~
	13.30	CA New housing price index	Nov	m%ch	0.3	~	~
	13.30	US Trade Balance	Nov	\$bn	-32.9	-34.8	~
Wed 13 Jan	~	UK NIESR GDP Estimate	Dec	%	0.2	~	~
	09.30	UK Industrial production	Nov	m%ch	0.0	0.3	~
	10.00	EZ Industrial production	Nov	m%ch	-0.6	0.6	~
	19.00	US Monthly Budget Statement	Dec	\$bn	-51.8	-70.4	~
	19.00	US Fed's Beige book	~	~	~	~	~
Thu 14 Jan	07.00	GE CPI	Dec	m%ch y%ch	0.7 0.8	0.7 0.8	~ ~
	12.45	EZ ECB announces interest rates	Jan	%	1.0	1.0	1.0
	13.30	US Advance Retail Sales	Dec	m%ch	1.3	0.4	~
	13.30	US Retail Sales Less Autos	Dec	m%ch	1.2	0.3	~
	13.30	US Retail Sales Ex Auto & Gas	Dec	m%ch	0.6	~	~
	13.30	US Initial jobless claims	Jan	'000	434	~	~
	13.30	US Continuing claims	Jan	'000	4,802	~	~
	13.30	US Trade balance	Nov	€bn	6.8	~	~
Fri 15 Jan	10.00	EZ CPI	Dec	m%ch	0.1	0.3	~
	13.30	US CPI	Dec	m%ch	0.4	0.2	~
	13.30	US CPI ex food & energy	Dec	m%ch	0.0	0.1	~
	13.30	US Empire Manufacturing	Jan	Index	2.6	11.3	~
	14.15	US Industrial Production	Dec	%	0.8	0.5	~
	14.15	US Capacity Utilization	Dec	%	71.3	71.8	~
	14.55	US U. of Michigan Confidence	Jan	Index	72.5	73.8	~

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