

## Shares continue to provide good returns.

- The local and global share markets enjoyed another month of positive returns.
- The NZ dollar eased off the peak hit in early January.
- Bonds sold off globally, sending yields higher on fixed interest investments.

Equity markets globally continued to march upwards during January, with the main exception being the UK FTSE 100, which suffered a minor decline. Once again, the New Zealand sharemarket was one of the best performers, with the NZX 50 index returning just under 2.4% for the month, and setting new record highs during the month. The debate continues about the severity of the US slowdown, and for now, the weakness remains largely within the housing market. The US manufacturing outlook mixed, but providing an offset for the overall economy is the resilient US consumer. Confidence is now at its highest level since early 2002. Wage inflation pressures remain, and the US Federal Reserve Officials continue to be more concerned about inflation than any threat of economic weakness. The US sharemarket has posted positive returns for 7 consecutive months, and in January the S&P 500 index gained another 1.3%. The US dollar strengthened in January, gaining on all the Majors, and the Australian and New Zealand Dollars. US long-term bond yields continued to rise through January. NZ Bonds had a significant sell-off during the month, pushing yields up around 22 basis points. 10-year Government Bonds now yield around 6%. The Reserve Bank of New Zealand met in late January, and left the Official Cash Rate at 7.25%. However, the RBNZ signalled that "in the absence of clear indications of a moderation in housing and domestic demand, it is likely that further policy tightening will be required". The market now expects the RBNZ to raise the OCR in the coming months. High yields remain attractive, and offshore investors continue to show interest in buying NZ dollars to access investments. However, during the month, the New Zealand dollar has retreated from the peak in early January, which was just shy of \$US 0.71. The NZD is currently trading around US\$ 0.68. Over the long-term, we expect the NZ dollar to depreciate, but for now, the local currency is strong, and this could continue out into mid-2007, particularly if the RBNZ raises the Official Cash Rate.

Date	Instrument	31-Dec-06	31-Jan-07	Month %	Quarter %	Year %
Cash	NZ cash rate	7.25	7.25	0.00	0.00	0.00
	NZ 90-day bank bill	7.74	7.67	-0.07	0.10	0.13
	US 90-day bank bill	5.36	5.36	0.00	-0.01	0.68
	NZ - US 90-day bank bill	2.38	2.31	-0.07	0.11	-0.55
Fixed Interest	NZ 5-year gov't stock	6.35	6.37	0.02	0.18	0.55
	NZ 10-year gov't	5.82	6.04	0.22	0.12	0.36
	NZ 10-year swap	6.93	7.06	0.14	0.34	0.38
	AUS 10-year gov't	5.90	5.94	0.04	0.27	0.59
	US 10-year gov't	4.70	4.88	0.18	0.26	0.35
Equities	NZ - NZX50 (NZ\$)	4055	4153	2.4%	9.7%	23.9%
	AUS - All Ords (A\$)	5644	5758	2.0%	7.6%	18.0%
	JAP - Nikkei (¥)	17226	17383	0.9%	6.0%	4.4%
	UK - FT100 (£)	6221	6203	-0.3%	1.2%	7.7%
	US - S&P500 (US\$)	1418	1438	1.4%	4.4%	12.4%
	WORLD - MSCI (US\$)	1484	1500	1.1%	5.4%	14.2%
	MSCI in NZD (NZ\$)	2104	2181	3.6%	1.8%	13.2%
Exchange Rates	NZD/USD	0.705	0.688	-2.4%	3.5%	0.9%
	NZD/AUD	0.892	0.891	-0.1%	3.1%	-1.9%
	NZD/JPY	83.9	83.6	-0.3%	7.1%	4.3%
	NZD/GBP	0.359	0.351	-2.4%	0.2%	-9.0%
	NZD/EUR	0.536	0.531	-1.0%	1.6%	-5.8%
	NZ TWI	0.696	0.687	-1.3%	3.3%	-1.6%
	EUR/USD	1.315	1.296	-1.4%	1.9%	7.1%

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

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### Cash

- The RBNZ left the official cash rate on hold in January.
- The NZ 90-day bank bill continues to trade at levels indicative of a Rate hike from the RBNZ in March.
- The 90-day bank bill ended the month at 7.67, down 7 basis points for the month.
- the RBNZ signalled that “in the absence of clear indications of a moderation in housing and domestic demand, it is likely that further policy tightening will be required”
- Financial markets are currently fully pricing an increase in the Official Cash Rate in the coming months.
- The next RBNZ announcement is on March 8<sup>th</sup>.

### Fixed interest

- Local fixed interest rates increased over January.
- US rates remain choppy. 10-year yields rose 18 points in January, but have fallen 14 points in early February. The volatility is a result of conflicting concerns about the slowing US economy, but still present inflation concerns.
- US 10-year Government stock is now trading around 50 basis points shy of the 2006 peak, and 40 points off the lows.
- In contrast, the NZ 10-year rate is trading right at the top of the range for the last year.
- We expect a period of volatile sideways action in interest rate markets, including for NZ fixed rates.

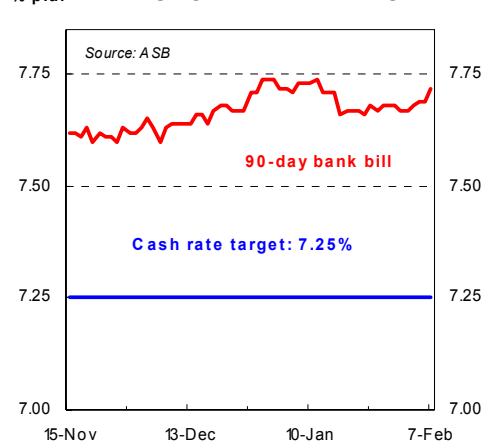
### Equities

- The upward momentum in global sharemarkets continued in January.
- Equity markets globally continued to march upwards during January, with the main exception being the UK FTSE 100, which suffered a minor decline.
- Once again, the New Zealand sharemarket was one of the best performers, with the NZX 50 index returning just under 2.4% for the month, and setting new record highs during the month.
- Offshore sharemarket gains were enhanced for local investors by depreciation in the NZ dollar. The MSCI index of world shares posted a 1.1% return in US dollars, and 3.6% in New Zealand dollars for the month.

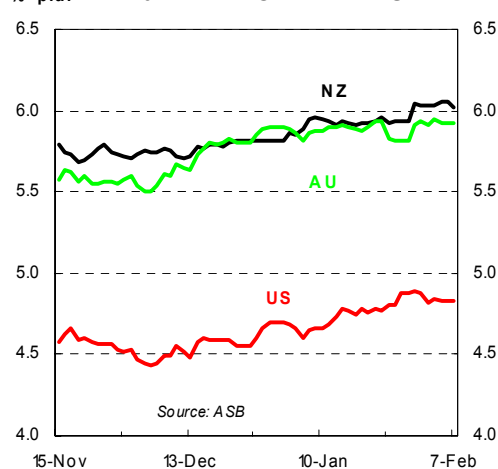
### Exchange rates

- The New Zealand dollar has retreated from the peak in early January, which was just shy of \$US 0.71.
- The NZD is currently trading around US\$ 0.68. Over the long-term, we expect the NZ dollar to depreciate, but for now, the local currency is strong, and this could continue into mid-2007, particularly if the RBNZ raises the Official Cash Rate.
- The focus remains on the relatively high interest rates on offer in NZ. The NZD traded between US \$0.68 and 0.71, and AUD \$0.87 and \$0.90 during the month.
- The 12 month expectation is for the NZ dollar downtrend to continue. However, a likely rate hike from the Reserve Bank of New Zealand will hold up the NZD.

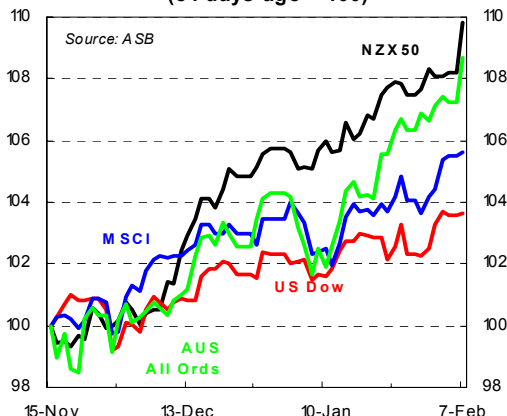
### NZ SHORT-TERM RATES



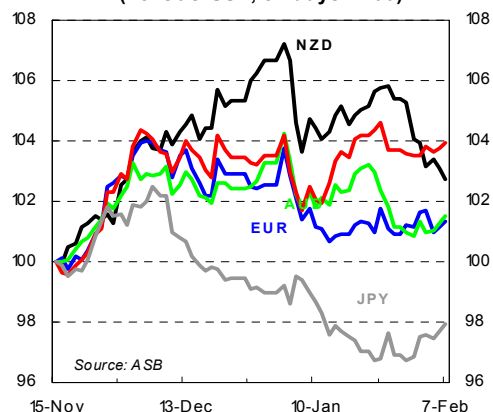
### 10-YEAR BOND YIELDS



### SHARE INDICES (84 days ago = 100)



### EXCHANGE RATE INDICES (versus USD, 84 days =100)



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