BNZ Weekly Overview

ISSN 2253-3672

31 January 2013

Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

The Weekly Overview is written by Tony Alexander. The views expressed are my own and do not purport to represent the views of the BNZ. To receive the Weekly Overview each Thursday night please click here.
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Visit To Singapore

I have screeds of leave to use up which was accrued during the global financial crisis. That means that I'll not be doing as many talks around the country for the next 3 – 4 years as in the past as I will be hopping overseas more. In that vein I shall be in Singapore and available to chat to anyone interested in catching up with what is happening back in New Zealand between March 11 and 15. So if you'd like to catch-up or even gather some folk together for a talk email me. tony.alexander@bnz.co.nz

This week we have seen the Reserve Bank confirm that the cash rate will stay at 2.5% but note that with some things improving overseas and the housing market rising, they are keeping an eye on the drivers of inflation. The NZ dollar rose 0.5 cents on those comments and in the FX section we discuss why the NZD is firm and probably will rise above US 90 cents this year.

In the Housing section we look at the idea of minimum loan to value ratios and why the Reserve Bank won't introduce them – or if they do they will be small.

But first, some comments from my family holiday at Broadbeach on the Gold Coast – written before tropical cyclone Oswald paid an unwelcome visit.

I love it here. The beach is close, there is shopping if you want it, restaurants if you eat out, nightclubs if that is your thing, and transport very handy by bus, train, or even the airport just down the road if you're prepared to pay the extra compared with flying in and out via Brisbane. We always go through Brisbane because of the cost, frequency of flights, and I quite like the hour and a half train trip from the airport terminal down to Nerang or Robina. A light rail system is being installed ahead of the Commonwealth Games set for 2018 so it will soon be even easier to move around.

There is clearly a glut of property over here courtesy of a number of large upmarket apartment buildings being finished within close time of each other (Oracle, Hilton) and the general weakness in Australia's housing market for a number of years now. If you are in the market for an apartment then while they are not cheap they are better priced than last year with the Hilton in the middle of Surfers Paradise for instance cutting some prices over 30%. You can even pick up a whole floor in the Oracle now for only $3.7mn compared with over $6mn before. We'll probably just take the one.

This visit we did not go to any theme parks. I'm sure the kids enjoy the rides but frankly they don't go on enough, myself and my wife do not go on any at all, if it is a hot day you end up crushed by the heat driven down into you then back up again from the concrete, and for a family of seven the cost is just huge.

The highlight of the trip was as always swimming at the beach in beautiful waves and each day getting on the sand was the priority. There is always the risk of being stung by jellyfish but this time around there were only a small number of the small blue ones washed up on the beach. Instead there were tens of thousands of beautiful large blue ones which can cause an irritation and itch but not outright wasp-like sting as the small ones do.

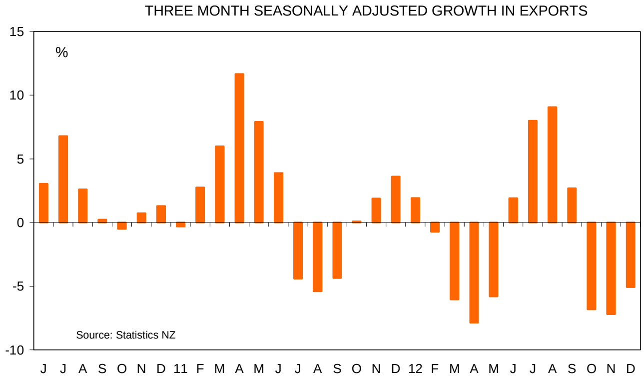
It was fascinating on one of the afternoons having a great time body surfing yet over a 20 minute period from first spotting them in rising waves as the tide was coming in watching the big blue jellyfish slowly advance toward the shore. As soon as they reached the sand bar those of us furthest out were on and we headed in everyone else got out of the water as well. At that point it became a fantastic community gawping and laughing session as people dared each other to advance in the shallow water and get as close as they could to the small number of blue blobs with thick finger tentacles which made it into the shallows. I guess the same goading would not have taken place had we exited the water because of a shark.

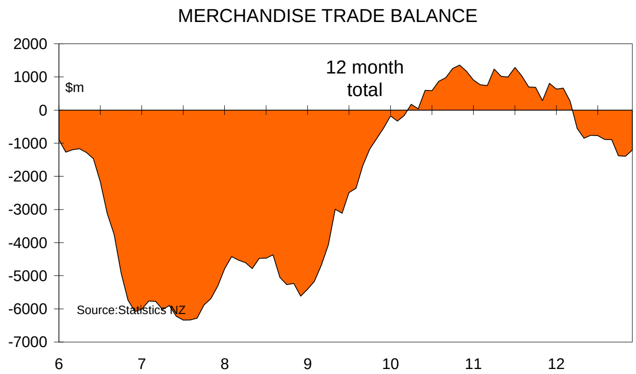
Enough of that. Back to the boring stuff. Here is some economic commentary and analysis.

Recent Economic Data

Export Trend Not Good

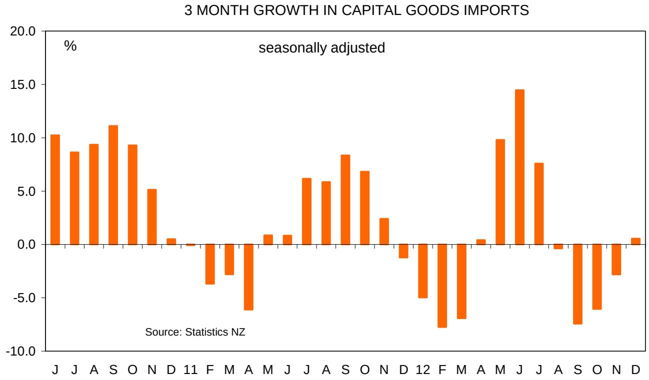
In seasonally adjusted terms NZ exports fell by 5.1% during the December quarter though things are not quite as bad as that annualised 21% fall would suggest given monthly gains of 14% and 5% in November and December respectively. The trend can be hard to pick in NZ exports but the fact that receipts for the entire year were down by 3.5% suggests the economy is not being driven forward on the back of a good solid lift in exports which will take care of our current account and offshore liabilities issues.



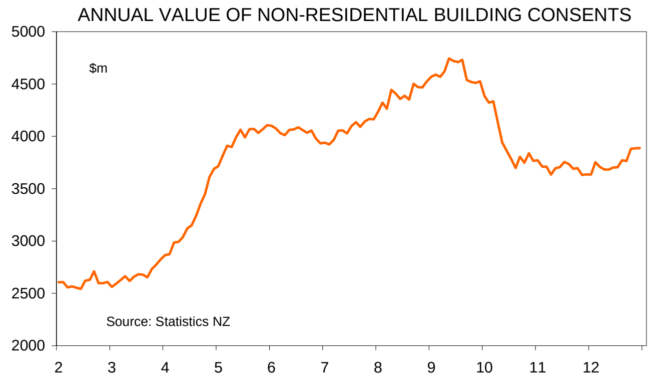


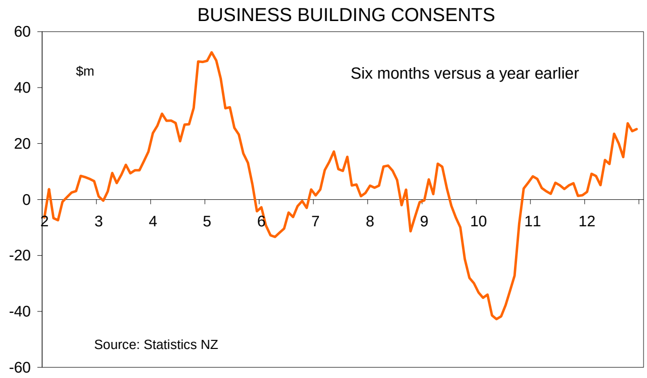
Business Construction Rising

The value of imports of capital equipment – which we try to use as a short-term proxy for changes in business investment – fell by 0.8% seasonally adjusted in the December quarter after falling 2.6% in the September quarter. That suggests that businesses are not really gearing up for better times – especially as they high NZ dollar would normally be encouraging higher imports of cheap foreign machinery.



We can take as another really rough gauge of business investment the short-term changes in the value of consents issued for the construction of non-residential buildings. The value rose 6.9% during all of 2012, and was ahead almost 10% in the second half of the year compared with the year before. Excluding as best one can the value of consents issued for government buildings we get business consent growth of a strong 25% in the past six months and 19% for the year. These are quite positive numbers and more firm growth is likely once the Christchurch rebuild gets going.





INTEREST RATES

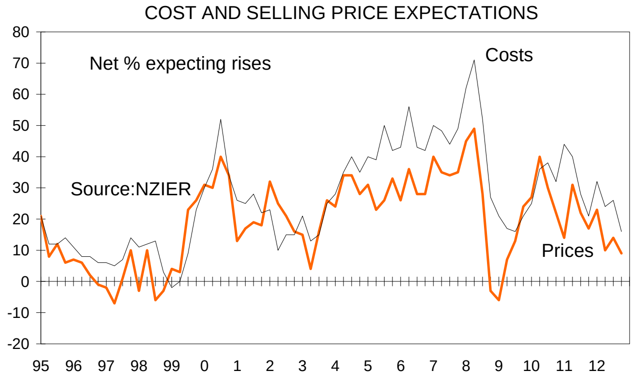
This morning the Reserve Bank undertook their six weekly review of the official cash rate and as had been near universally expected they left it unchanged at the 2.5% level it has been at since they cut it from 3% in March 2011 following the Christchurch earthquake and a string of weak economic data. http://www.rbnz.govt.nz/news/2013/5122707.html Their comments were marginally though not substantially more hawkish than expected. They noted

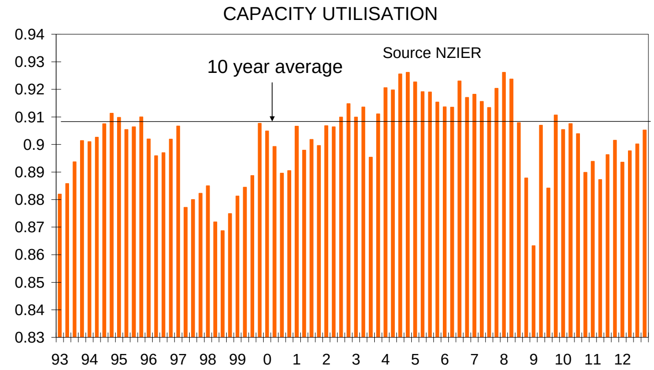
"Global growth is set to recover in 2013…
global financial market sentiment is positive…
recent data on business confidence and construction activity suggest GDP growth is recovering…
House price inflation has increased and we are watching this and household credit growth closely.
Overall, we expect economic growth to strengthen over the coming year, reducing spare capacity and bringing inflation slowly back towards the 2 percent target midpoint.
On balance, it remains appropriate for the OCR to be held at 2.5 percent."

The chances are good that the rate will still be 2.5% come the end of this year. They are unlikely to cut it even though some sectors of our economy are suffering from the high exchange rate (http://www.radionz.co.nz/news/political/126654/exporters-tell-inquiry-of-threat-from-high-dollar) and employers are still generally reluctant to hire people – as evidenced by the 7.3% unemployment rate registered for the September quarter – assuming it is accurate.

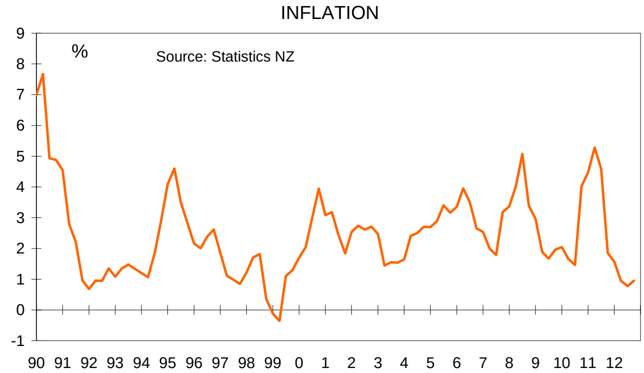
Their reluctance will be driven by the reconstruction of Christchurch and a wide range of other factors which will be driving the construction sector and therefore the overall economy in the coming year or three. Rising sharemarkets around the world may also be signalling faster growth down the track (though money printing is a factor also), and most forecasts are for this year to be marginally better than last internationally.

Equally, the Reserve Bank are unlikely to raise the cash rate before the end of the year because of the inflation-restraining effect of the high and probably rising NZ dollar, because we have all got egg on our faces calling recovery before it has actually appeared in the past four years, and because cost and selling price expectations are quite low while capacity utilisation measures show nothing inflationary.



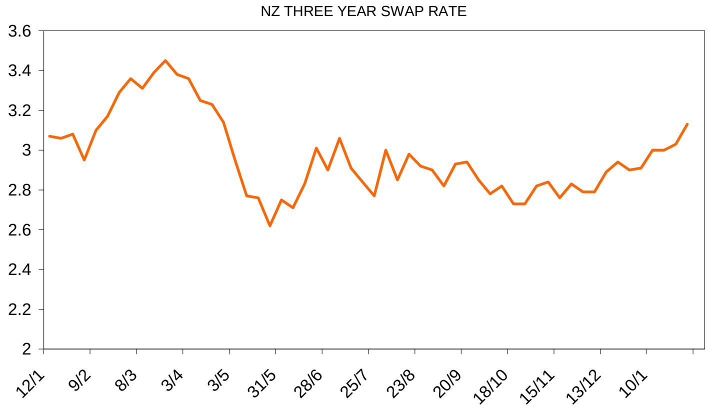


As reported by Statistics NZ a couple of weeks ago also, (http://www.stats.govt.nz/browse_for_stats/economic_indicators/CPI_inflation/ConsumersPriceIndex_MRDec12qtr.aspx)actual inflation is very low at just 0.9% with the CPI falling 0.2% in the December quarter. For most core measures the result stays low with the 10% trimmed mean gauge unchanged in the quarter and ahead only 1% from a year earlier, and the CPI excluding food and household energy measure up 0.3% and 1.1%. However the non-tradables measure rose 0.3% in the quarter and 2.5% for the year which shows the large effect which the NZ dollar and falls in commodity prices have had on suppressing inflation.



The most interesting driver of interest rate changes this year is frankly not going to be our monetary policy or the state of the NZ economy. It will be the extent of rises in medium to long term interest rates around the world as investors desert government bonds and go into risky assets like equities (and the NZ dollar). There is no way of forecasting how big this impact will be therefore there is no way a person should place any great reliance upon any particular forecast of how much fixed interest rates will rise this year, when, and at what speed.

They are simply going to up we believe but with falls also likely as investors will undoubtedly receive more scares regarding global growth prospects for the coming year. In fact this week these offshore rates have jumped up with the US ten year government bond yield above 2% for the first time since April last year. The NZ three year swap rate has jumped to 3.13% from 3.03% last week and 2.91% four weeks ago.



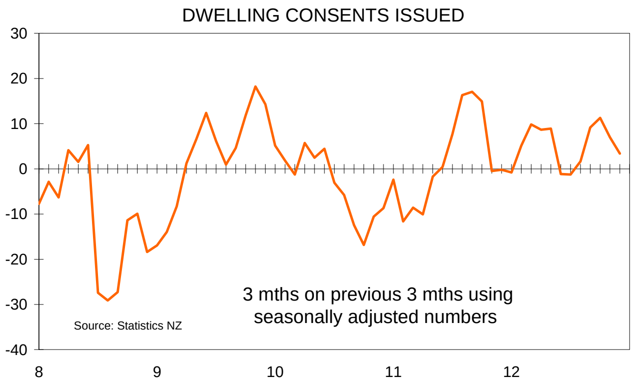
FINANCIAL MARKETS DATA	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	2.50	5.4
90-day bank bill	2.70%	2.67	2.66	2.67	2.76	5.7
1 year swap	2.81%	2.71	2.70	2.63	2.72	5.8
3 year swap	3.13%	3.02	2.91	2.82	2.95	6.1
5 year swap	3.43%	3.33	3.21	3.11	3.34	6.3
7 year swap	3.74%	3.64	3.53	3.43	3.73	

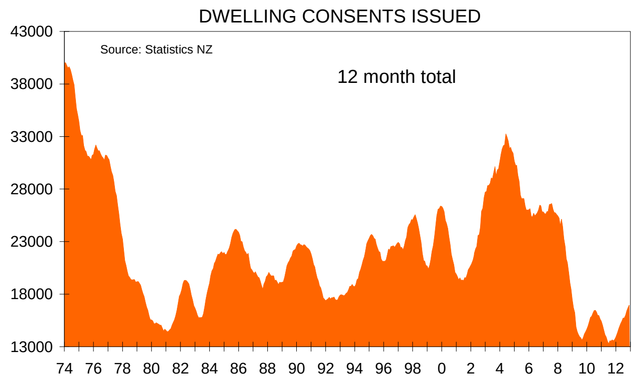
HOUSING MARKET UPDATE

As predicted here quite some time ago the discussion regarding New Zealand's housing sector has shifted decidedly into that of a housing crisis involving a physical lack of property and poor affordability of available stock. You know things are desperate when the Greens propose a policy of rent-to-buy for state housing occupants. http://www.radionz.co.nz/news/political/126352/housing-group-says-greens'-plan-innovative

What are the chances of a substantial policy change which will radically alter the house supply and pricing problem? Nil and bucklies. Labour's proposed solution of the construction of 100,000 houses over a ten year period with construction cost savings of 30%- 40% holds little chance of being achieved through reliance on bulk purchasing to cut costs.
(http://www.nzherald.co.nz/politics/news/article.cfm?c_id=280&objectid=10858231 But should they embrace alternative construction methods then such an outcome could be possible and if I were them I would be chatting with those who are aware of such alternatives and involve urban planners who can give advice on how to avoid a repeat of the state housing ghettos created in earlier decades.

With regard to fresh information received on the state of New Zealand's housing market over the past couple of weeks we have little new in hand apart from the number of consents issued for the construction of new houses rising in seasonally adjusted terms by 9.4% in December to be ahead 3.4% for the quarter. Taking out apartments the changes were -1% and 6.2% respectively and that latter number shows us that there is a good underlying upward trend in "real" construction as it were rather than just the latest possibly-to-go-bankrupt-later developer getting cash out of someone to build a new block of cubby-holes in Auckland, or a new old folks home going up on the Kapiti Coast.





I learnt this week that a room for one's mother-in-law in a good Kapiti Coast village costs $235 a night. She gets four weeks free a year which allows us to have a decent holiday – apart from tropical cyclone Oswald dumping on us on the Gold Coast.

Minimum Loan Value Ratios

Is it likely that the Reserve Bank will try to prick the hastening rise in house prices by imposing a minimum LVR requirement? That is, will buyers have to stump up with a minimum deposit of 20% or 30% or 50% of the house purchase price? That is very unlikely for the following reasons. http://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=10861410

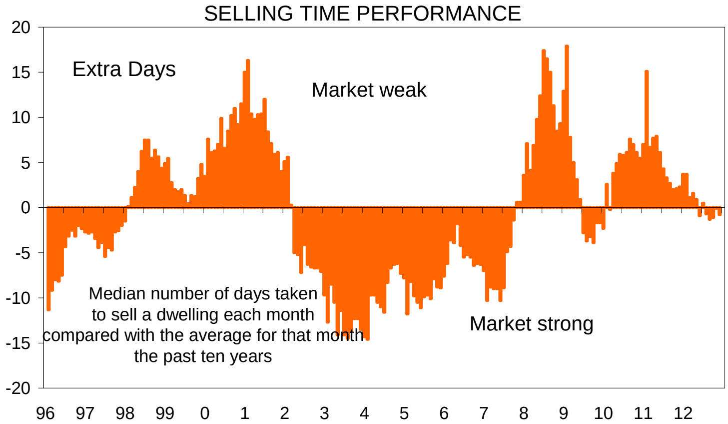
There is no evidence that the rise in house prices is being driven by speculative forces. That is, we have no data series showing us the split between those buying their first home, those trading up, those trading down, those simply shifting for whatever reasons, and those making an investment and of that latter group those doing it for long term yield versus short-term capital gain.

In fact all we can do to try and get a feel for this split is to look at the results of our BNZ-REINZ Residential Market Survey – the last one of which was conducted in the first week of December and the next one of which we shall do in just over a week's time. The question 'What are the main reasons people are buying" produced the following percentage split in responses. Only 0.4% of all reasons given by responding agents fall into the category of investing.

	Latest %	**Month Ago %**	**Average %**
Fear of missing out/Feel time is right for prices	9.7	8.9	10.7
Trading up	10.9	11.0	13.4
Trading down	11.0	9.9	15.0
Shifting into town	10.9	11.5	14.5
Arriving from overseas	4.6	4.0	5.4
Relationship breakdown	7.8	8.6	11.2
Commuting costs	1.3	1.9	2.3
Schooling	7.2	6.4	7.9
Want closer proximity to shops	2.1	2.4	2.1
Want closer proximity to relatives	2.0	2.2	2.6
Want closer proximity to health care services	1.9	1.7	2.0
Investing	0.4	0.3	0.4
First home	14.7	14.2	4.7
Earthquake	0.3	0.5	1.3
Good interest rates	14.0	14.6	3.9
Other	1.4	1.8	2.9

There is also an absence of evidence of active quick trading of properties as one would expect to see were the market being driven by a quick gain mentality. In December the number of days taken to sell a dwelling was 32 which was only 0.8 days faster than the ten year average. November was 0.1 days faster and

October 1.1 days. This measure showed sales 14 days faster than average in early-2004 and 10 days in early-2007.



However there is evidence of sales growth picking up with seasonally adjusted sales roughly estimated to be up near 10% during the December quarter. Annual sales of 74,000 dwellings exactly in 2012 are still well away from the early-2004 peak of 121,000 though up from 61,269 over 2011.

More importantly however when considering the argument against compulsory minimum LVR is this. The impact will be felt most keenly by young people who will have far less ability to raise a deposit than those who have owned a home for home time and reduced their mortgage while watching their house price rise. Their ability to use their existing mortgage to raise a deposit will be strong and their incentive to buy an investment property to rent out will be enhanced as the number of young and low income people who will be forced to rent for a much longer period of time will be vastly increased.

Could a minimum LVR be easy to get around? If one could borrow the deposit then yes. But if proof of having saved the deposit is required that would be an impediment to getting around the barrier – unless one could front with money advanced by a relative. In that case the borrowing would need to be channelled through them. But they would have to be willing to increase their own mortgage to do that and that could be a strain for many for a variety of reasons.

Imposing a minimum LVR requirement therefore would be an exercise undertaken in the absence of any evidence that speculative forces are driving the market, and would place home ownership and getting a foot on the ladder even further out of reach for young people and those without friendly cash-happy parents.

Home Affordability

I bet you think that because I've put this sub-section title here I'm going to write about the just released Demographia international home affordability survey. http://www.newgeography.com/content/003413-demographic-and-economic-challenges-the-9th-annual-demographia-international-housing-affordability-survey Wrong. This measure and all other one's focussed on affordability give exactly zero insight into where house prices are going. They show the impact of house price rises, not the causes. In fact if you have been a follower of such measures you probably were one of those people who five years ago were forecasting massive declines in NZ house prices simply because they were "too" high and "should" go down. Such factors are not things which drive market-influenced prices.

That is, there are very few people in the housing market who will refrain from buying a house simply because they "should" go down in order to benefit society.

But if you are interested in affordability measures – go for your life. They reveal a deteriorating situation in New Zealand which is damaging and will damage further our social fabric with the cost borne disproportionately by certain groups. But most votes lie with those already owning a home so the electorate is not going to vote for a party promoting a policy of reducing their wealth by forcing house prices down 30%. As my kids would say – durrr.

Or, as central bankers would say – we (they) are engaging in quantitative easing in order to forestall further downturns in economies and promote growth in asset prices which by boosting perceived wealth will boost household spending and the willingness of businesses to hire and invest. In other words – much as NZ house prices are "too" high, our central bank at the end of the day is a mid-ranking member of a global pack and the alpha has suggested everyone should do their bit to get asset prices up not down. Our member will obey even though there will be social consequences and in spite of (for a few more quarters) expressions of concern about high house prices in the likes of this morning's review of the official cash rate.

This is not to say that other policies aimed at improving the housing situation are unworthy. Promoting home ownership by state house tenants is a good thing (as long as there is no purchase subsidy), and accelerated government house building is a good move as well (though Labour's bulk purchase discount forecasts seem optimistic). The only way to really change the home affordability situation is to go back to the 1960s and 1970s when finance was hard to get, the economy was rigid and deteriorating, and people were getting well shot of the place. Now we rank quite highly with regard to economic measures (apart from productivity and incomes which frankly seem to be the most important measures) and net migration inflows are about to turn positive. http://www.nzherald.co.nz/nz/news/article.cfm?c_id=1&objectid=10861675

I did an extended radio interview on the housing sector this week (Radio NZ http://www.radionz.co.nz/national/programmes/morningreport/audio/2544835/auckland's-housing-problems-may-get-worse while standing just off the beach out of the wind at Broadbeach on the Gold Coast. The interview came right at the end of a one hour window of opportunity – about the first in three days – to get partner plus five kids out of the unit and walking along the beach before the next remnant of tropical cyclone Oswald dumped more wind and rain on the place.

The beach was filled with foam and the kids absolutely loved it. Thankfully the foam was not as deep as that which completely hid a car which emerged from it and almost ran a couple of people over further north– it will be on Youtube I am sure. Try http://www.npr.org/blogs/thetwo-way/2013/01/28/170464408/video-look-out-car-suddenly-emerges-from-foam-on-highway While writing this particular section on Tuesday morning the weather has cleared, schools have restarted in Australia, and people are out clearing paths, fallen trees, destroyed awnings, and getting gunk out of pools.

When we go on holiday over here we usually – though not always – stay at the Breakfree Diamond Beach Resort which is just south of Broadbeach and a short walk to the beach crossing just one minor road. http://www.breakfree.com.au/diamond-beach/ The cost is usually between $300 and $400 a night for all of us, it is easy to get to via plane into Brisbane (avoid Gold Coast Airport as the flights cost too much and the airport closes in bad weather), train down to Nerang or Robina Station, then bus, taxi, or prearranged Airtrain shuttle from there. http://www.airtrain.com.au/

The pool complex is very good and any minute now I'm going to close the lid on this damn machine, check out, then we'll spend a couple of hours beside the pool before heading to Brisbane Airport again with a bus replacing part of the train journey because of the effects of the cyclone on the rail network.

If I Were A Borrower What Would I Do?

Swap rates have jumped up this week on the back of a sell-off in US bond markets as money switches into equites and a slightly more hawkish than expected OCR review from the Reserve Bank this morning. The implications for fixed housing rates are fairly obvious – they will soon be rising unless world worries soar again.

I would take a good look at the newly lowered medium to long term fixed interest rates (by some, not all lenders) and ask myself how much of a premium I would be prepared to pay for certainty in these still very uncertain times. Although I do not expect the RBNZ will raise the official cash rate and therefore push up floating mortgage rates until next year, it could be seriously worth locking half of one's mortgage in at a three year-plus rate just in case rates rise a lot later this year around the world. But to repeat, uncertainty about rate movements remains as bad now as four years ago so do not place much reliance upon anyone's interest rate forecasts when you make your risk management decision. https://www.bnz.co.nz/personal-banking/home-loans/mortgage-rates-and-fees#source=RD+old-redirect

OFFSHORE

The IMF this week released their latest prediction for world growth with a pick of 3.5% which is a minor improvement from 3.2% they estimate was achieved last year. This slight improvement is in line with most other forecasters and shows that while one can start to think in terms of the worst of the dragged out effects of the GFC being over, it is too soon to start talking in terms of normality and good fundamental growth drivers. The fact that central banks are printing more and more money and a de facto beggar-thy-neighbour currency war is in play says clearly that the fundamentals for growth are in fact still very fragile – which then calls into question the steadiness of the rise in sharemarkets currently underway. http://www.imf.org/external/pubs/ft/survey/so/2013/NEW012313A.htm

In Australia the RBA has cut its cash rate by 1.75% over the past year and a half but while this has alleviated financing costs for the business sector and households, it has not spurred an acceleration in growth. In particular the tourism sector remains depressed by a currency held high by investors avoiding much of the rest of the planet. The manufacturing sector is similarly affected. Many large companies in the minerals sector have pulled back on their capital spending plans in light of last year's surge in worries about world growth, worries about China in particular, and some hefty falls in key commodity prices. Household spending on retail goods and services continues to show only weak growth bringing ongoing rationalisation of firms in the sector – as is happening in the UK also – with an increasing drift in spending to online formats further undermining spending in traditional physical outlets.

The housing market has shown little indication of being boosted by the large decline in interest rates with latest data not yet leading to a full conclusion that things are improving.

Businesses indicated in the quarterly Australian Chamber of Commerce survey that they have their lowest levels of investing in 15 years.

With regard to inflation and monetary policy the markets are pricing in 0.5% worth of cuts this year with a reasonable chance seen of a cut in the first week of February. The case for cuts (the cash rate currently is 3% and was 4.75% a year and a half ago) was boosted last week by the annual inflation rate sticking at 2.2% in calendar 2012 with prices for imported goods falling 0.4% during the year courtesy of the continuing high Australian currency.

In Japan the Bank of Japan has met expectations by announcing an increase in its inflation target from 1% to 2%. But as it has done for over two decades it frustrated government hopes for monetary expansion by delaying planned expansion of its balance sheet by some 14 trillion yen each month until January 2014. The net effect will actually only be an addition to the money supply of only 10 trillion Yen for the entire year due to already purchased bonds maturing. That will be less than the monetary addition planned this year and achieved last year.

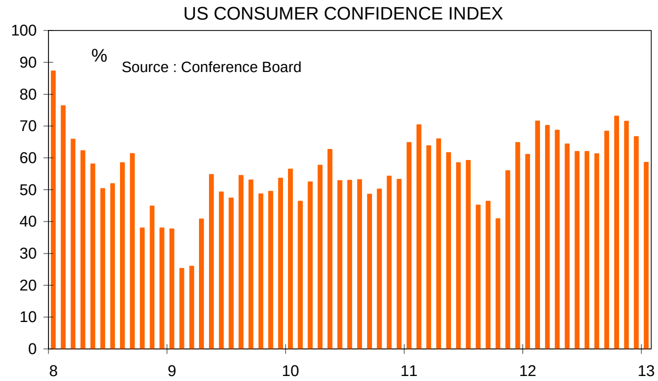
Will these mediocre efforts plus the 10 trillion Yen fiscal stimulus kick-start growth in Japan out of a two decade slump? Probably not given the absence of measures to deregulate the economy in important sectors such as healthcare, continuation of cronyism with regard to support for agriculture and feeding of contracts to construction "friends" and maybe the nuclear industry, and the explicit reliance upon a depreciated Yen. That is, old theory says depreciating the Yen will bring much higher demand from the huge US market. However with US consumers having changed their spending habits it is very unlikely that the impact on demand for Japanese goods and services in response to a weaker Yen will be anything like it was in the past.

In addition, encouragement of Japanese consumers to spend is going to prove fruitless potentially this year with the Bank of Japan forecasting that consumer prices will fall 0.2% over 2013 and rise just 0.4% next year. The incentive to buy goods in order to beat price rises will simply not be there.

Plus, as many commentators have noted, the fiscal stimulus package follows 15 earlier ones which failed, so anticipating success this time around when the country has finally started its shrinking population phase (129 million heading down to 86 million) is somewhat optimistic.

In the United States we received some further evidence of improvement in the housing market. The annual number of home sales hit its highest level in five years over 2012 with 4.65 million sales. This was a rise of 9% from 2011 and the best result since 2007's 5 million sales. Sales in the month of December were 13% ahead of a year earlier though down a small 1% from November. The median dwelling sale price came in 11.5% higher than a year earlier though was still 22% below the early-2006 peak.

However some doubts about the sustainability of recent good retailing numbers have been sown by a sharp drop in consumer confidence to a reading of 58.6 in January from 66.7 in December for the Conference Board index.



Plus the December quarter national accounts released last night came in much weaker than expected with a 0.1% annualised fall in GDP following a 3.1% result for the September quarter and expected growth of 1.1%. However the result is not quite as bad as it looks as it was driven by a run-down of inventories and the biggest quarterly fall in defence spending in four decades at 22.2%. Excluding these two factors growth would have been an acceptable 2.5% - or even more allowing for the effects of Hurricane Sandy.

In fact corporate spending on software and equipment rose at an annualised pace of 12.4%, residential building was up 15.3% and 11.9% for the entire year,

There was another piece of good data on the Chinese economy released over the past week – this time the HSBC PMI which rose by more than expected to a two year high of 51.9 in January from 51.5 in December. The rise is important as it signals good growth in the all-important export-focused manufacturing sector and being a private sector calculated number rather than the official PMI measure goes some way to offsetting worries about data accuracy sparked by the export numbers which do not match up with import data supplied by other countries.

Here is my monthly article on China's economy written for the NZ China Trade Association
http://newsletter.nzcta.co.nz/lt.php?id=cE9TUV0AAQZcTlRYVw8aUwMAAFM%3D

Exchange Rates

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average
NZD/USD	0.836	0.842	0.819	0.821	0.819	0.67
NZD/AUD	0.803	0.799	0.789	0.792	0.773	0.85
NZD/JPY	76.2	74.5	70.3	65.3	62.5	69.6
NZD/GBP	0.529	0.531	0.506	0.51	0.522	0.388
NZD/EUR	0.616	0.632	0.619	0.633	0.624	0.52
NZDCNY	5.20	5.24	5.10	5.12	5.17	4.99
USD/JPY	91.15	88.48	85.84	79.54	76.31	105.7
GBP/USD	1.58	1.59	1.62	1.61	1.57	1.72
EUR/USD	1.36	1.33	1.32	1.30	1.31	1.28
AUD/USD	1.04	1.05	1.04	1.04	1.06	0.788
USD/RMB	6.2204	6.2185	6.2322	6.2405	6.3144	7.56

Kiwi Firm – To Stay That Way

The Kiwi dollar, like the Australian currency, is a high beta asset which tends to show higher than average change in response to shifts in market sentiment. Actually the situation is a bit more complicated than that because across the entire scene currency movements are a zero sum game with a rising currency always being offset by one that is falling. Nevertheless, as a highly volatile currency the NZD tends to rise when investors feel happy about the world around them and purchase risky assets.

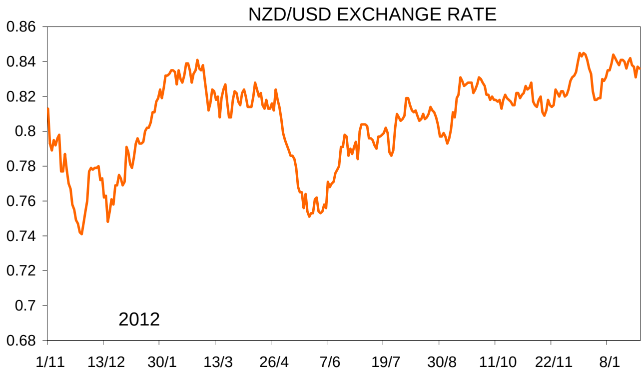
This generates a fairly good correlation at times between changes in global sharemarkets and changes in the NZ dollar – and that is where one needs to exercise some caution with regard to thoughts about the NZD's progress over the coming five years.

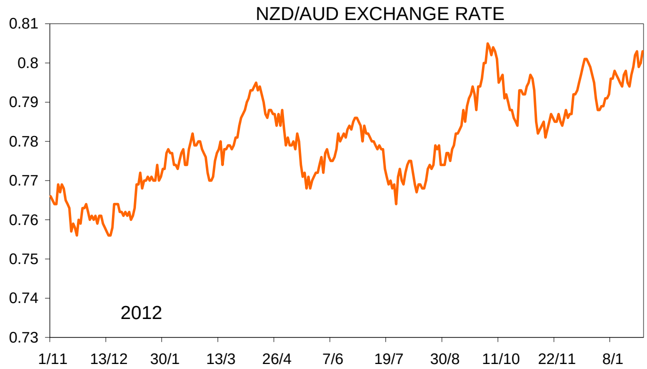
For the moment the NZD is being held up partly by money printing of foreign currencies and partly by rising offshore sharemarkets associated with improving sentiment. The issue however is that these two factors are largely the same in that money printing is what is primarily driving sharemarkets upward. Research by an American business economist Dave Rosenberg has found that before the Fed started expanding its balance sheet there was just a 20% correlation between its growth and the S&P 500. Since money printing started the correlation has risen to a startling 86%. US share prices on average rose 12% last year in spite of no earnings growth.

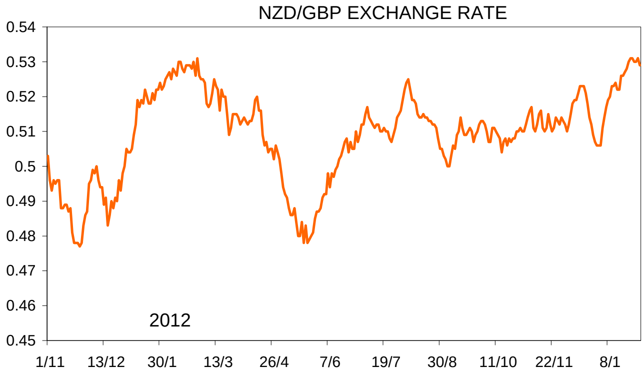
The implication one is invited to draw from Mr Rosenberg's research is that when the money printing stops the sharemarket will fall – and so will the NZ dollar. Therefore if you want to stake out a strong position on how the NZD is going to track over the next five years you need to state a profile for the Fed.'s money printing operations – and probably do the same for the other major central banks as well. Good luck with that.

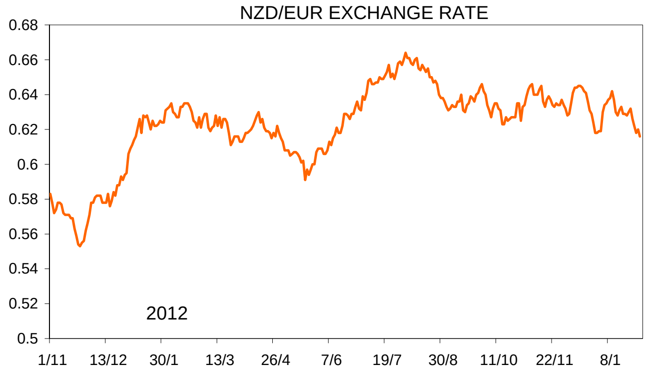
For now, last night the Fed. confirmed that they have as yet no plans to stop their monthly US$85bn worth of purchases of US securities. That means continued devaluation of the greenback's worth relative to currencies of countries not trying to boost house and other asset prices by printing money which they hope banks will lend like they did in the 2000s.

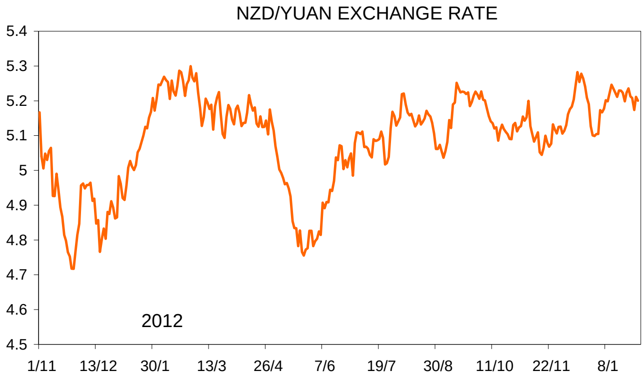
And this morning the slightly more hawkish than expected comments on monetary policy by the Reserve Bank caused the NZD to rise by half a US cent. Get used to it and remember the warning we have long given here. The Kiwi dollar basically always rises when the RB tightens monetary policy (almost). They have yet to start doing so. They will do so before most other central banks. As the time for tightening approaches the Kiwi dollar will rise higher and probably breach US 90 cents before the end of the year.

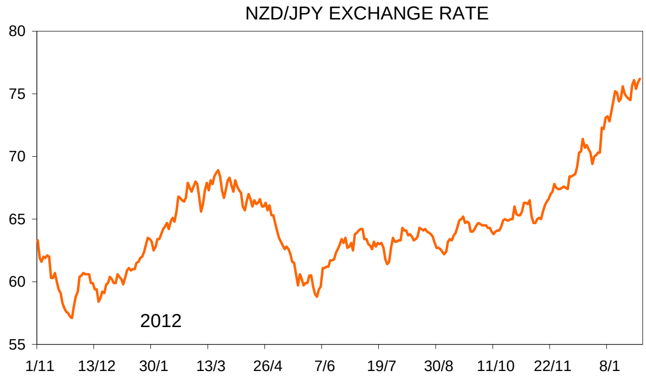












Is there anything the government can do about it? Apart from levying a special tax on offshore investors purchasing NZ financial instruments and taxing bank borrowing offshore there is nothing. Cutting interest rates when we are on the cusp of the biggest building boom since the early-1970s, there is a housing shortage, businesses struggle to get skilled labour, and house prices are already rising firmly would be very unwise. Printing money would be plain stupid as the intent of central banks in doing that is that commercial banks, finding themselves awash with cash, ease their lending criteria and push money out the door to borrowers trying to load them up with more and more debt so they spend and drive imports of retail goods (thus blowing out the current account deficit) and push house prices even further out of reach of average Kiwis.

Offshore with regard to currency movements we have seen the Yen weaken further on confirmation of a change in the inflation target from 1% to 2%. The Euro has firmed slightly on reduced worries about the financial situation – but little change in worries about the state of the European economy this year. The Aussie dollar is about where it was a week ago.

Key Forecasts

Dec. year		2011	2012	2013	2014
GDP	annual average chg	1.5	2.0-3.0%	2.0 – 2.5	1.0 – 2.0
CPI	on year ago	1.8	0.9	1.0 - 2.0	2.0 – 2.5
Official Cash rate	end year	2.5	2.5	2.5 – 2.75	2.75 – 4.25
Employment	on year ago	1.6	-0.5 – 0.5	1.0 – 2.0	0.5 – 1.5
Unemployment Rate	end year	6.4	7.0 – 7.5	6.0 – 7.0	6.0 – 7.0

The Weekly Overview is written by Tony Alexander, Chief Economist at the Bank of New Zealand. The publication is sent to 27,000 subscribers each week and is one of a stable of regular releases which include the

- monthly Growing With China publication, http://tonyalexander.co.nz/topics/china/
- monthly BNZ Confidence Survey, http://tonyalexander.co.nz/topics/surveys/bnz-confidence-survey/ and the
- monthly BNZ-REINZ Residential Market Survey. http://tonyalexander.co.nz/topics/surveys/bnz-reinz-survey/ This latter survey provides information from a survey of over 10,000 licensed real estate agents on the current state of the residential property market in New Zealand.
- He also produces a monthly column for the NZ Property Investor magazine, http://www.propertyinvestor.co.nz/ and
- writes a monthly column for the NZ China Trade Association. http://www.nzcta.co.nz/
- Most of these publications plus research into impediments to NZ's economic growth are available on his website. www.tonyalexander.co.nz
- Discussion of New Zealand's relationship with China can be found here. www.facebook.com/TonyAlexanderNZ

Tony Alexander has been Chief Economist at the BNZ since 1994 and apart from publications and advising management spends considerable time on the road around New Zealand making presentations and speaking with the media. He travels to the UK and Europe twice a year to assess economic conditions and present at numerous functions, has five children, tramps, and his partner Dr Sarah Farquhar runs the early childhood education network www.childforum.com

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