

Australia & NZ weekly

Week beginning 6 September 2010

- Australia: GDP supports further rate hikes, but not next week at RBA meeting.
- Australian data focus: July housing finance, August employment previewed.
- New Zealand: 16 Sep MPS a close call, but now expecting no OCR change.
- New Zealand data: wholesale trade, building work, manufacturing sales, ToT.
- US data: Labor Day shortened week with Beige Book and trade deficit due.
- Central bank meetings this week: RBA, BoJ, BoE to remain on hold; BoC and BoK to hike 25bp.
- Key economic & financial forecasts.

Information contained in this report was current as at 3 September 2010

GDP supports further hikes, but not next week

The Reserve Bank Board meets next week on September 7. The Board is almost certain to keep rates on hold.

Markets continue to be priced for a rate cut over the course of the next year. Current pricing puts the probability of a rate cut of 25bps at around 40% in the first half of 2011. In last week's note we strongly argued against the rate cut scenario emphasising our view that rates would rise by around 75bps next year following a welcome period of steady rates over the remainder of 2010. Early this week markets reached the point of pricing a 50% probability of a rate cut by year's end with that probability rising to 80% by early in 2011.

The release of the Australian national accounts carried a very strong message to markets that expecting that the next rate move in Australia would be down was riddled with danger!

The accounts reported that the Australian economy grew by 1.2% in the June quarter to push the annual growth rate up from 2.6% in the year to the March quarter to 3.3%. That compares with 1% growth in the year to the June quarter last year.

The picture painted of the Australian economy by the release has cast considerable light on the key puzzles surrounding Australia's economic outlook. The main challenge for the Australian economy has been whether we could emerge from a long period of below trend growth which had been essentially 'propped up' by the government sector. In 2009, around half the economy's growth was contributed by an increase in government spending. If we add the indirect multiplier effects of the stimulus policies the role of the government in 'holding together' the economy during that period was dominant.

For Australia, as the government withdraws its stimulus spending over the course of 2010 and 2011 (note that government investment spending fell by 0.2% in the June quarter after rising by around 44% through the previous year) we have needed to see a recovery in private sector spending to replace the government investment boost. We can be confident that mining investment will play a major role but it is only 4% of GDP. We need to see the household sector (around 55% of GDP) and services sector investment (around 10% of GDP) recovering. The most likely order of this recovery will be household spending followed by services investment as firms become more confident about their future domestic sales.

Recently, the lacklustre retail sales data had cast a pall over prospects for this key dynamic to evolve. The recent recovery in the Westpac-MI Consumer Sentiment Index provided some reason for optimism. The release of the household spending data for the June quarter provides even more grounds for optimism.

Household consumption increased by 1.6% in the quarter.

That compares with average reads of 0.05% in 2008; 0.7% in 2007 and 0.6% in the March quarter of 2010. Much of the growth in spending was in categories of spending we could describe as discretionary. In total, motor vehicle sales (23%); transport – mainly air transport (10%); recreation (24%); and financial services (17%) contributed 74% of the GROWTH in spending while representing only 28% of total consumer spending. The emphasis on discretionary spending is encouraging evidence that we are moving into a period of stronger household spending. With wage incomes rising by 2.9%

but being fully offset by higher interest payments and falls in other non wage incomes this boost to household spending is encouraging evidence that households are emerging from the very cautious approach to spending we have seen in recent years.

There was no parallel evidence that (non-mining) business investment is recovering. Private sector business investment contracted by 0.2% following a fall of 2.7% in the March quarter. We are not concerned about a sustained contraction in business investment. The recent CAPEX survey from the Australian Bureau of Statistics provided a very significant boost to the outlook for business investment. Every three months this survey includes a revised estimate of total business investment for the immediate financial year. The release on August 25 was the third estimate for 2010/11. We find that the third estimate is reasonably reliable.

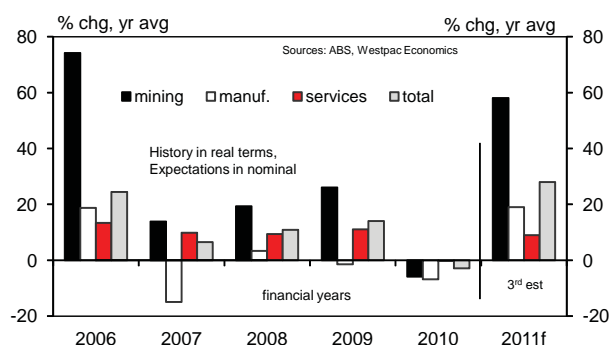
This estimate implies a 28% rise in the value of business investment in 2010/11 which was upgraded from a 19% rise in the previous estimate. There is not an exact match between the survey and the volume of investment as measured in the national accounts but our detailed analysis indicates that it is pointing to a very healthy increase of around 15% in business investment through the year. Not surprisingly, the implied 58% surge in mining investment is an important contributor. The improved outlook for the household sector, supported by the CAPEX survey, also gives us confidence to raise our outlook for investment growth in the all important services sector.

Note that despite strong growth in wage incomes (up 2.9%) overall household incomes contracted mainly because of interest rate increases during the quarter. Interest rates are certain to remain steady in the September quarter and, we believe it would be sensible policy for rates to remain steady in the December quarter as well. That will provide a sound backdrop for the resurgence in household spending to be sustained through 2010 as households enjoy a sustained period of rising incomes. With investment by the services sector set to gain some traction in the September and December quarter, stresses to capacity are likely to reemerge in the first half of 2011, requiring a resumption of the RBA's tightening cycle.

At present we are expecting rates to rise by 75bps during 2011. Markets will need to adjust a long way to accommodate that view.

Bill Evans, Chief Economist

CAPEX plans by industry



Data wrap

Q2 business indicators

- The key figure was the 18.9% jump in company profits in Q2. This highlights the boost to national income from the sharp rise in the ToT. A huge 62.7% jump in mining profits was the driver.
- It's important not to underestimate the significance of these numbers. Australia is in the midst of Commodity Boom Mark II. The latest ABS CAPEX survey suggest mining sector investment will increase by 58% in 2010/11, in response to these high prices.
- Wage incomes improved considerably over 2010H1, increasing by 2.2% in Q2, consistent with strength in the labour market.
- However, there was a downside surprise on business inventories. They fell 0.5% in Q2, subtracting 0.6ppts from growth.

Q2 current account deficit & net exports GDP contribution

- The current account deficit fell more than expected by \$10.817bn to \$5.640bn from \$16.457bn. This cut the qtrly deficit to just 1.7% of GDP from 5.0%, the lowest % since Q3 2001, but a markedly better 'quality' improvement. The Q3 2001 deficit reflected weak import volumes (-6.4%yr) while currently, import volumes are up 17.3%yr. The last time the deficit was this low with positive annual import volumes growth was Q1 1980.
- The trade deficit turned sharply to a surplus of \$6.497bn from a deficit of \$3.209bn previously. That's 1.9% of GDP, the highest % since Q2 1973. The jump reflected a 12.5%qtr leap in the terms of trade (with import prices up 1.5% with softer AUD, but export prices surging 14.2% led by bulks) and an acceleration in export volumes growth beyond that for import volumes.
- Export values jumped 20.6%qtr, while prices rose 14.2%. Export vols rose 5.6% (vs -0.7% prev). Rural vols rose 1.3% and non-monetary gold vols bounced 21.4%. Non-rural vols jumped 7.5% (vs -1.7% prev) with gains led by coal, fuels, metal ores and metals. Non-rural vols are up 9.5%yr (highest since Q3 2000).
- Import values rose 4.7%qtr. Prices rose 1.5% (weaker AUD). Vols rose 3.0% (vs +1.6% prev), but the detail implied better improvements in domestic demand. Consumption goods vols rose 4.4% (vs 1.1% prev) and capital goods vols rose 4.8% (vs 1.1% prev), with the aggregate held back by intermediate & other goods vols (0.2% vs 2.7% prev).
- Net exports add 0.4ppts to Q2 GDP growth vs -0.5ppts in Q1, the strongest contribution since Q1 2009. This improvement stems from much stronger export vols growth.
- The net primary income deficit reinforced the trade balance swing to surplus, falling to \$11.909bn from \$13.021bn. With the Australian equity market income return outperforming the US in Q2 (vs Q1 underperformance) higher net equity income outflows were expected, but they fell 14.3%. Higher debt income outflows were also expected with higher US short rates and the weaker AUD (partially offset by lower bond yields), but they fell 3.3%.

Jul retail sales

- Retail sales saw a better month in July, rising 0.7%, with May and June marked up from 0.2% to 0.4%. The net is a significantly more upbeat picture for retail which now shows trend sales growing at 5.2% annualised over the last 3 months.

- There were quirks in the detail, notably a sharp 5.3% rise in cafes & restaurants which may be valid given the hugely popular Masterchef TV series that was reaching its final stages in July. Other segments were more mixed with persistent weakness in other discretionary categories like household goods (-1.7%qtr) and department stores (-0.7%qtr).
- This has significantly altered the complexion of recent trends. What was a disconcertingly insipid rate of sales growth, travelling at close to stalling speed in per capita terms, now looks a little healthier. That said, the upturn is still underwhelming with consumer caution still an apparent restraining factor.

Jul dwelling approvals

- Dwelling approvals rose 2.3% in July (consensus -0.7%), ending a 3 month fall that had seen approvals slide 19.7% in total.
- The rise was mainly due to a 7.7% bounce in private sector units – a volatile segment. Activity here has clearly recovered from last year's lows. Private sector house approvals recorded a slight 0.1% dip in line with expectations and broadly confirming the moderating downtrend shown by finance approvals. Public dwelling approvals posted a 2.1% rise in July but had a much smaller impact on total approvals than in previous months.
- The state detail shows a more resilient picture for NSW and Vic with Qld notably weaker.
- The value of renovation approvals rose 3.2% (vs -7.0% prev) – oscillating around a flat trend so far this year. Private non residential building remains slumped with the value of approvals tracking a slight downtrend at very low levels excluding the stimulus-related burst of education building activity.

Jul private credit

- Private sector credit rose 0.1% in July (vs 0.2% prev), indicating a loss of momentum from the recovery evident over 2010H1.
- This is likely a temporary soft spot. The RBA is now on hold and positive fundamentals point to business credit turning the corner over the year ahead. Notably, Australia is enjoying a significant income boost from the ToT. That is likely to lift annual nominal GDP growth to 10% through 2010, up from 1% through 2009.
- Business credit, which is volatile month to month, fell 0.4% in July. However, over the last 3 months a picture of stabilisation is evident – as has been the case since the end of 2009.
- Housing credit was subdued in July, rising 0.5%. While representing an improvement from the 0.4% rise in June, it is clear that a lessening of stimulus has had a material impact.

Q2 GDP

- The economy expanded a very healthy 1.2%qtr, 3.3%yr in Q2. That was above market expectations (0.9%qtr).
- This is a very significant result. The key challenge for the Australian economy has been whether we can emerge from a long period of below trend growth which has been essentially "propped up" by the government sector. In 2009, around half the economy's growth was due to an increase in government spending. If we add the indirect multiplier effects of the stimulus policies, the role of the government in "holding together" the

Data wrap

economy during that period was dominant.

- For Australia, as the government withdraws its stimulus spending over the course of 2010 and 2011 (note that government investment spending declined by 0.2% in Q2 after rising by 44% over the previous year), we want to see a recovery in private sector spending to replace the government investment boost. We can be confident that mining investment will play a role, but it is only 4% of GDP. We need to see the household sector (around 55% of GDP) and services sector investment (around 10% of GDP) recovering. The most likely order of this recovery will be household spending followed by services investment as firms become more confident about future domestic sales.
- Recently the lacklustre retail sales data had cast a pall over prospects for this key dynamic to evolve. The recent recovery in the Westpac-MI Consumer Sentiment Index provided some reason for optimism. The household spending data for Q2 provides even more grounds for optimism. Household consumption jumped 1.6%qtr. That compared with average reads of 0.05% in 2008, 0.7% in 2009 and 0.5% in 2010Q1.
- Much of the growth in household spending in Q2 was in categories we could describe as discretionary. Together motor vehicle sales (23%); transport - mainly air transport (10%); recreation(24%); and financial services (17%) contributed 74% of the growth in spending while they represent only 28% of total consumer spending. The emphasis on discretionary spending is encouraging evidence that we are moving into a period of stronger household spending than we have seen recently. With wage incomes rising by 2.9% in Q2, but being fully offset in the period by higher interest payments and falls in other non-wage incomes, this boost to household spending is encouraging evidence that households are emerging from the very cautious approach to spending we have seen in recent years.
- By contrast, there was no evidence of a recovery in non-mining business investment. Total private business investment contracted by -0.2% in the quarter, although recent business investment surveys point to a strong overall investment outlook for 2010/2011. The improved outlook for the household sector provides reason to feel more confident about this prospect.
- Note that, despite strong growth in wage incomes (+2.9%), overall disposable household incomes contracted. That was

mainly because of interest rate increases during the quarter. Interest rates are certain to remain steady in the September quarter and, we believe, it would be sensible policy for rates to remain steady in the December quarter as well. That will provide a sound backdrop for the resurgence in household spending to be sustained through 2010. With investment by the services sector likely to gain some traction in the September and December quarters, stresses to capacity are likely to re-emerge in the first half of 2011. That will require a resumption of the RBA's tightening cycle.

Jul trade balance

- The July trade balance pulled back \$1.550bn from a record surplus of \$3.438bn to a surplus of \$1.888bn, well below consensus (\$3.1bn) but in line with our Westpac (bottom of the range) \$1.9bn forecast.
- Exports pulled back despite further aggregate price gains, with dips in bulks volumes after their Q2 surge. This gels with our forecast for flatter export volumes in Q3 after their Q2 jump, taking net exports back to a drag from GDP in Q3 after adding 0.4ppts to Q2 growth. But while bulks volumes pulled back sharply in July, they were more resilient relative to their Q2 average, and if we apply current trend growth to values for Aug and Sep and deflate by our Q3 price forecast, Q3 volumes can be resilient between flat and up 1%qtr, after their 5.6% Q2 leap.
- Exports fell 4.5% after a 6.4% rise previously, their first fall in five months, leaving trend growth robust at 2.0%qtr and 31.4%yr. Rural exports rose 4.6%, but non-rural exports fell 5.9%, with falls in bulks volumes. However, the dip in non-rural exports follows seven straight increases, including an 11.8% Jun rise, leaving trend growth strong at 2.3%qtr and 45.0%yr.
- Imports rose 1.6% after a 0.3% rise previously, suggesting higher volumes given the 2.9% AUD/USD appreciation would have dented prices. Despite the bounce in imports and pullback in exports, trend imports growth remained well below that for exports at 1.4%qtr and 13.5%yr. Also, the import rise was narrowly based, driven by intermediate and other goods, with lumpy defence aircraft imports. Consumption goods imports fell and capital goods were flat, leaving trend growth in capital goods (1.6%qtr) above consumption goods (0.8%qtr).

Round-up of local data released last week

Date	Release	Previous	Latest	Mkt f/c
Mon 30	Q2 company profits	4.3%	18.9%	5.8%
	Q2 business inventories, % chg	0.9%	-0.5%	0.4%
Tue 31	Q2 current account balance, AUDbn	-16.5	-5.6	-6.5
	Q2 net exports contribution to GDP, ppts	-0.5	0.4	0.3
	Q2 public sector demand	5.1%	1.3%	-
	Jul retail sales	0.4%	0.7%	0.4%
	Jul dwelling approvals	-3.3%	2.3%	-0.7%
	Jul private credit	0.2%	0.1%	0.3%
	RBA Assist. Gov. (Financial mkts) Debelle speech	-	-	-
Wed 01	Q2 GDP	0.7%	1.2%	0.9%
	Aug AiG PMI	54.4	51.7	-
Thu 02	Jul trade balance, AUDbn	3.438	1.888	3.1

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New Zealand: week ahead & data wrap

Tipped over the edge

We are changing our forecast to no change in the OCR at the 16 September *Monetary Policy Statement*. However, we'd emphasise that we still regard this review as a very close call.

By our count, a majority of economists are now picking a pause this month, and interest rate markets are pricing only a one in four chance of a rate hike. But where our view may differ – certainly from market pricing at least – is that we expect the September *MPS* to continue to hammer the message that the OCR will need to move higher as the economy recovers.

As the RBNZ noted in its July statement, the tone of the recent data warrants a more moderate pace and extent of tightening than was projected in the June *MPS*. By our estimates, that could see the OCR peaking in mid-2012 around the 5.00-5.25% range, compared to a 5.75-6.00% range previously. But from a starting point of 3.00%, that still doesn't leave a lot of room for the RBNZ to drag its feet.

As a result, this represents a change to the expected timing of hikes, not a downgrade to our overall interest rate projections. We had already acknowledged that a pause in the tightening cycle was likely at some point in the next few months – previously we had it pencilled in for December. But with the RBNZ facing a highly uncertain global environment, mixed signals on the domestic economy, and now the biggest financial sector failure in nearly two decades, bringing the pause forward to September is a low-risk option.

The failure of South Canterbury Finance, New Zealand's largest non-bank-owned finance company (though still only accounting for around 0.5% of financial sector assets), goes further towards making a pause the more tactful option for the RBNZ. But we should emphasise that this is because of the visibility of such an event, and the potential effects on confidence over the near term, not because of any lasting economic impact – which we don't think will be significantly different from zero. Bear in mind that the new information here is SCF's receivership (and the government's payout to depositors); any consequences have to be weighed against the alternative of the firm continuing to limp on as before.

Under the Retail Deposit Guarantee Scheme, around \$1.6bn will be paid out to depositors in coming weeks. A large share of term deposits tend to be held by retirees who rely on the regular interest income. So rather than being treated as a 'windfall' to be spent, we expect the vast majority of these funds will go towards similar investments – deposits at banks and building societies, and bonds from the higher-rated corporate issuers.

It's possible, but far from certain, that these funds could be recycled into new lending, thereby stimulating the economy. The issue is whether the main constraint on credit growth at present is supply or

demand; the evidence seems to be weighted towards the latter.

Access to finance is likely to be a sector-specific issue. While SCF has been portrayed as a major player in rural lending, this made up only 18% of its lending as at the end of 2009 – about the same share as the major retail banks. Its greater exposure was to property development, a sector that is already under pressure to evolve towards new methods of financing.

Finally, the net cost to the government after depositors are paid out and SCF's assets are sold is expected to be around \$600m. The 2010 Budget made provisions for a loss of this scale, so the fiscal projections and bond issuance programme should be unaffected.

On the data front this week, the news was mixed. Residential building consents rose 3.1% in July, but that was driven by a rise in the lumpy apartments component (specifically retirement units). Single-home consents fell by 5.3%, and are now below end-2009 levels. Tax changes, slower population growth and higher mortgage rates continue to have a cooling effect on the housing market relative to a year ago.

Business confidence fell in August, though only to levels more consistent with the pace of GDP growth seen to date. Confidence in housing construction was understandably weaker, while export-oriented sectors remain positive. With the GST increase looming on 1 October, nearly 50% of retailers said they intend to raise prices in the next three months, up from 40% in July.

The trade balance slipped into deficit in July, with dairy export volumes heading towards their seasonal low point, although prices remained firm. Imports were stronger than we expected, led by a substantial rise in capital goods (ex transport). We estimate that after adjusting for large one-offs such as oil rigs, imports of plant and machinery have now recovered more than half of their peak-to-trough decline – not bad at a time when businesses are supposedly reluctant to invest.

Dairy prices rose by nearly 17% in Fonterra's online auction, restoring about half of the drop over the previous four months. We suspect the magnitude of the increase reflects demand rather than supply, with buyers holding back on their purchases in recent months, in anticipation of a continued slide in prices as northern hemisphere production ramped up. However, the dramatic spike in wheat prices, due to drought in Russia, may have turned this sentiment around. We maintain our forecast for a total payout of around \$7/kg for this season. Along with bumper growing conditions that could see production up by 8-10%, this would see cashflows to dairy farmers up almost \$1.5bn in the year to October 2011 (to \$10.3bn).

Round-up of local data released last week

Date	Release	Previous	Latest
Mon 30	Jul merchandise trade NZDm	214	-186
	Q2 business inventories, % chg	27.9%	16.4%
Tue 31	Jul building consents	3.3%	3.1%
Wed 01	Aug ANZ commodity price index	-0.8%	-1.4%

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Data previews

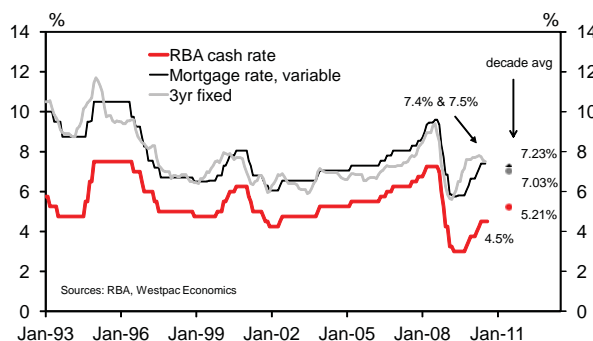
Aus RBA policy announcement

Sep 7, Last: 4.50%, WBC f/c: 4.50%

Mkt f/c: 4.50%, Range: 4.50% to 4.50%

- The RBA left the cash rate steady at 4.50% for the 3rd straight month in Aug, with the statement highlighting a more confidence central bank in the forecasts with "growth likely to be close to trend" and "inflation close to target", emboldened by the 'low' Q2 core CPI result. The current monetary policy setting was described as "appropriate" with loan rates near decade averages. The tone of the statement suggested preparation for an extended period of steady rates.
- With breathing room on inflation for now and the global outlook more uncertain (and waning US momentum), we see rates on hold for the rest of 2010. But with the SoMP GDP f/c's above trend in 2011 and 2012, and core inflation f/c to rise to 3%, the resource investment boom is seen pressuring supply capacity, and we see the tightening cycle resuming in 2011H1. Recent CAPEX plan upgrades reinforce this view.

RBA: borrowing rates have normalised



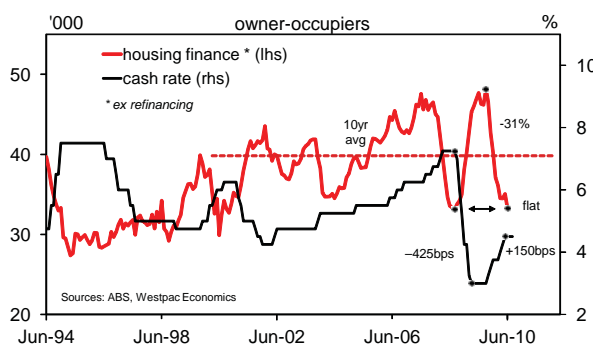
Aus Jul housing finance

Sep 8, Last: -3.8%, WBC f/c: 1.0%

Mkt f/c: 1.0%, Range: -2.0% to 2.5%

- Demand for housing finance is likely to gain a second wind over the remainder of 2010, with the RBA on hold from June.
- Finance to owner-occupiers is forecast to rise by 1.0% in July, following a 3.9% fall in June and a 31% drop in new lending from the peak of last September.
- Supportive of a second wind is a brightening of the consumer mood. The Westpac-MI Consumer Sentiment Index rebounded from a low of just 102 in June to 113 in July and rose to 119 in August. This is as labour market strength boosts household incomes and thereby improves housing affordability.
- As for Investors, the upward trend in finance faltered in June, with a 3.6% fall - to still be up 29% from the start of 2009. We expect the upward trend to resume in coming months.

Owner-occupier finance & the rate cycle



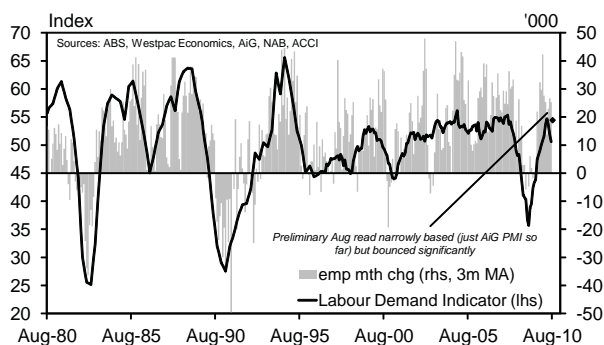
Aus Aug employment chg

Sep 9, Last: 23.5k, WBC f/c: 25k

Mkt f/c: 25k, Range: 6k to 55k

- Jobs rose 23.5k in July, slowing trend growth to 16.7k mth from a Nov-09 peak of 33.5k as employers utilise more of the spare capacity in existing labour. Average hours worked have trended up for 5 months. The softer monthly trend has still seen annual trend growth rise to 2.7%yr (highest since Jul-08), with medium term leads implying a 3%yr pace in 2010H2.
- The Election is a wild-card for Aug jobs, with the AEC said to have hired 70k for polling day. We expect minimal effect from this: the survey ran from 8th to 21st and relates to the week before the interview, so only 1/14th of the period could include polling day temps; temps on that day were not home to be surveyed; a large proportion of poll day temps are already otherwise employed; the same survey timing in Nov-07 saw a 50k PT jump, but that looked more like noise (followed -68k prev & no payback fall in Dec). Still, with our prelim. LDI up in Aug, we expect +25k, lifting annual trend growth to 2.8%yr.

Westpac Australian Labour Demand Indicator



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Data previews

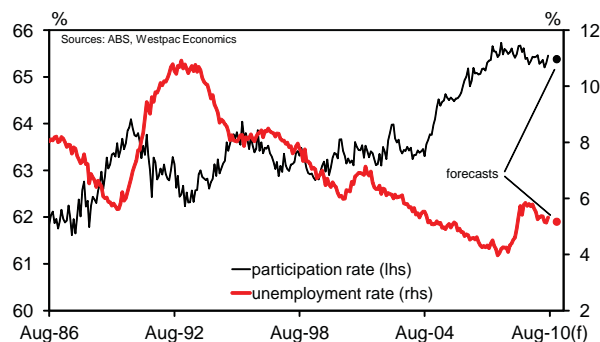
Aus Aug unemployment rate

Sep 9, Last: 5.3%, WBC f/c: 5.2%

Mkt f/c: 5.2%, Range: 5.1% to 5.4%

- With the recent rise in consumer sentiment, the participation rate rose 0.2ppts to 65.5%. That drove strong labour force growth of 48.1k, more than offsetting the jobs rise to lift the unemployment rate 0.2ppts to 5.3%. The trend unemployment rate continued to edge gradually lower (5.2% vs 5.8% a year ago), consistent with our view that continued strong labour force growth will leave the unemployment rate downtrend slow.
- Months of jobs growth around 25k following 0.2ppt rises in unemployment and participation rates have seen pullbacks in participation. But with a possible Election offset from temp workers, we f/c a small 0.1ppt dip to 65.4%. That sees weak labour force growth of around 7k, allowing a 25k rise in jobs to take the unemployment rate back to 5.2% from 5.3%. That could show as a 0.2ppt fall, as our two-decimal f/c is 5.17% vs 5.32% previously = a fall of 0.15ppts.

Unemployment and participation rates

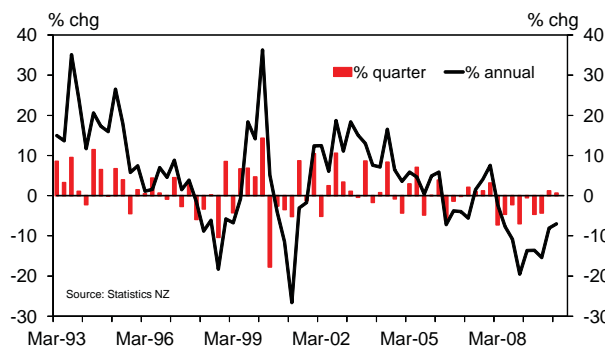


NZ Q2 real building work put in place

Sep 8, Last: +0.7%

- Total building work eked out only a small gain in the March quarter, as activity in the residential sector – which surprised on the downside (possibly finance-related, as consents indicated an increase of close to 6%) – only just offset a fourth consecutive decline in the non-residential sector.
- Consents suggest a modest gain in residential investment in the June quarter in the order of 3%. However, we see some potential for catch-up given the weak March quarter outturn.
- Private sector indicators of non-residential investment have maintained their usual volatility, but overall suggest a further decline in Q2. Government should provide some offset, given the increase in consents for hospitals and education buildings in the second half of 2009. However, we don't expect it will be enough to push total activity in the non-residential sector into positive territory. Our forecast is for a decline of 1%.

NZ real building work put in place

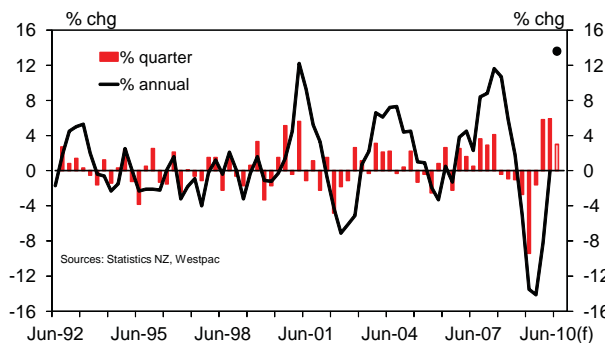


NZ Q2 terms of trade

Sep 10, Last: +5.9%, WBC f/c: +3.0%

- The terms of trade continues to claw its way back from the sharp decline seen during the global recession. Our forecast for the June quarter would put the index up 13.6% on a year earlier, and just 2% shy of its pre-crisis highs.
- We expect a 4.9% rise in export prices, with gains across the spectrum. Dairy exports continued to benefit from higher prices agreed earlier in the year, with an estimated 7% gain. Meanwhile, spot prices remained firm for the likes of meat, fish, logs and oil.
- Import prices are estimated to be up 1.8%, dominated by higher prices for petroleum products. The 2% rise in the exchange rate over the quarter is likely to have left prices broadly flat for manufactured goods.

NZ terms of trade



Data previews

US trade deficit on widening trend

Sep 9, Last: \$49.9bn, WBC f/c: \$50.1bn

- The US trade deficit widened \$7.9bn to \$49.9bn in June on a broad-based 1.3% exports fall and a 3.0% imports jump that was constrained by lower oil prices; ex-oil, imports rose 4.7%.
- Although industrial production and durable goods shipments posted solid growth in July, much of this was auto related (which is not a US export strength). However aircraft exports should be a positive. But elsewhere, there is not much evidence of renewed exports growth with June's softer ISM export reading maintained in July–August.
- Imports should not repeat June's gain in July given the economy has lost momentum, and US dollar appreciation has pushed import prices lower (but a bounce in the oil component is likely).
- A 0.5% rise in both exports and imports would lift the deficit to just over \$50bn in July.

US trade balance



Key data & event risk for the week ahead

		Last	Market median	Westpac forecast	Risk/Comment
Mon 6					
Aus	Aug TD-MI inflation gauge	0.1%	-	-	Soft start to Q3 slowed 3m pace to 0.89%; risk of CPI catch-up bounce.
	Aug ANZ job ads	1.3%	-	-	12mth uptrend has growth at 34.1%yr = strong jobs%yr into 2011H1.
Eur	Sep Sentix investor confidence	8.2	10.0	7.5	Investors starting to question euro growth story with US clearly slowing.
UK	Aug house prices %yr	4.9%	4.4%	-	Tentative date for Halifax series, due 6-10/9.
US	US Labor Day holiday	-	-	-	Last chance for the ladies to wear their white shoes; markets closed.
Tue 7					
Aus	RBA policy decision	4.50%	4.50%	4.50%	CPI room = rates "appropriate" & on hold Aug; further hikes likely 2011H1.
NZ	Q2 wholesale trade survey	2.3%	-	-	Further recovery expected, though may not match last quarter's pace.
Jpn	Bank of Japan decision	0.1%	0.1%	0.1%	Fizzer of an emergency meeting makes this a non-event we suspect.
Ger	Jul factory orders	3.2%	0.5%	2.0%	Still benefiting from weaker euro and global trade recovery.
UK	Aug BRC retail sales monitor %yr	0.5%	-	-	Same store sales were weaker in July, contrasting solid official data.
Wed 8					
Aus	Jul housing finance (no.)	-3.8%	1.0%	1.0%	RBA now on hold + labour mkt strength points to a 2nd wind.
NZ	Q2 building work put in place	0.7%	-	-	Potential for some catch-up in residential sector, meaning upside risk.
	Q2 real manufacturing sales s.a.	-2.7%	-	-	Dairy manufacturing affected by drought; non-agri continuing to recover.
Jpn	Jul machinery orders	1.6%	2.0%	-	Still adjusting to a major decline in May. Private core +17% from trough.
	Aug bank lending %yr	-1.8%	-	-	Lack of demand for credit is the key problem here.
Ger	Jul industrial production	-0.6%	1.0%	1.0%	Still some momentum from recent solid orders growth.
UK	Aug BRC shop prices index %yr	1.5%	-	-	Guide to part of CPI basket; often picks direction of annual CPI change.
	Jul industrial production	-0.5%	0.4%	0.9%	Bounce back in mining and oil likely due to seasonality issues.
US	Fed beige book	-	-	-	Fed's regional assessment of economic conditions.
	Jul consumer credit \$bn	-1.3	-5.4	-	Credit in decline as spending dwindles post fiscal stimulus.
Can	Jul building permits	6.5%	-6.0%	-	Canadian housing market is losing momentum on many indicators.
	BoC rate decision	0.75%	1.0%	1.0%	Further modest tightening but sluggish US means BoC to pause soon.
	Aug Ivey PMI nsa	54.0	55.5	55.0	Index typically rises in August for seasonal reasons.
Thu 9					
Aus	Aug employment chg	23.5k	25k	25k	Aug prelim LDI rise = 20k jobs; survey timing implies no big Election boost.
	Aug unemployment rate	5.3%	5.2%	5.2%	Jobs rise reinforced by 0.1ppt PR dip to 65.4%; downtrend very gradual.
NZ	Aug electronic card transactions	-0.2%	-	-	No hint of a pre-GST spending rush just yet.
Kor	Bank of Korea decision	2.25%	2.50%	2.50%	A hike every other meeting; Chinese PMI will help them over the line.
UK	Jul visible trade balance GBPbn	-7.4	-7.6	-	Will June's export jump be sustained?
	BoE MPC policy decision	0.50%	0.50%	0.50%	Rates on hold and no QE adjustment still the majority view.
US	Jul trade balance \$bn	-49.9	-47.8	-50.1	Nothing particularly unsustainable about Jun imports surge.
	US initial jobless claims w/e 4/9	472k	470k	475k	Holding below recent 500k peak but still indicating weak jobs mkt.
Can	Aug housing starts	-1.6%	-2.4%	-	Urban single family home starts down by around a third since March.
	Jul new house prices	0.1%	0.1%	-	Prices have been rising for the past year but may soon lose momentum.
	Jul trade balance C\$bn	-1.1	-1.0	-	Deficits in three of last four months.
Fri 10					
NZ	Q2 terms of trade	5.9%	-	3.0%	Moderate gains in commodity export prices across the board.
Chn	Aug trade balance USDbn	28.7	26.7	-	Imports soft in PMI, possible source of upside surprise.
	Jul NDRC house prices %yr (tentative date)	10.3%	9.3%	-	On a reasonably benign downward path with high regional diversity.
Inr	Jul industrial production %yr	7.1%	-	-	Core sectors firmed a little but composition less flattering.
UK	Aug producer prices %yr	4.7%	-	-	Core output measure.
US	Jul wholesale inventories	0.1%	0.4%	0.2%	Another early clue to extent of inventory contribution to Q3 GDP.
Can	Aug employment chg	-9k	17.8k	25k	Trend still positive but slowing as economic growth moderates.

Economic & financial forecasts

Interest rate forecasts

	Latest (Sep 03)	Sep 10	Dec 10	Mar 11	Jun 11	Sep 11
Cash	4.50	4.50	4.50	4.75	5.00	5.00
90 Day Bill	4.74	4.75	4.75	5.00	5.25	5.50
3 Year Swap	4.85	5.00	5.20	5.40	5.50	6.00
10 Year Bond	4.86	4.95	5.30	5.30	5.30	5.50
10 Year Spread to US (bps)	224	225	230	200	170	170

International

Fed Funds	0.125	0.125	0.125	0.125	0.125	0.375
US 10 Year Bond	2.62	2.70	3.00	3.30	3.60	3.80
ECB Repo Rate	1.00	1.00	1.00	1.00	1.00	1.00

New Zealand

Cash	3.00	3.00	3.50	3.75	4.25	4.75
90 day bill	3.22	3.30	3.80	4.20	4.70	5.20
2 year swap	3.80	3.90	4.30	4.80	5.20	5.60
10 Year Bond	5.28	5.10	5.40	5.70	5.90	6.00
10 Year spread to US	266	240	240	240	230	220

Exchange rate forecasts

	Latest (Sep 03)	Sep 10	Dec 10	Mar 11	Jun 11	Sep 11
AUD/USD	0.9072	0.88	0.90	0.92	0.90	0.88
NZD/USD	0.7139	0.70	0.72	0.75	0.75	0.74
USD/JPY	84.21	88	91	94	97	100
EUR/USD	1.2822	1.31	1.33	1.34	1.30	1.26
AUD/NZD	1.2708	1.26	1.25	1.23	1.20	1.19

Australian economic growth forecasts

	2009		2010		2011			Calendar years			
<i>* forecasts under review</i>	Q3	Q4	Q1	Q2	Q3f	Q4f	Q1f	2008	2009	2010f	2011f
GDP % qtr *	0.3	1.0	0.7	1.2	0.8*	0.9*	1.0*	-	-	-	-
ann change	0.8	2.6	2.6	3.3	3.8	3.7	4.0	2.2	1.2	3.3*	3.5*
Unemployment rate %	5.8	5.6	5.3	5.2	5.2	4.9	4.8	4.3	5.6	5.2	4.8
CPI % qtr	1.0	0.5	0.9	0.6	1.2	0.4	1.0	-	-	-	-
ann change	1.3	2.1	2.9	3.1	3.3	3.2	3.3	3.7	2.1	3.2	3.2
CPI underlying % qtr	0.8	0.6	0.8	0.5	0.7	0.6	0.8	-	-	-	-
ann change	3.5	3.2	3.0	2.7	2.6	2.7	2.6	4.3	3.2	2.7	3.1

New Zealand economic growth forecasts

	2009		2010					Calendar years			
	Q3	Q4	Q1	Q2e	Q3f	Q4f	Q1f	2008	2009	2010f	2011f
GDP % qtr	0.3	0.9	0.6	0.7	1.8	0.0	1.9	-	-	-	-
Annual avg change	-2.4	-1.6	-0.4	0.8	2.2	2.9	3.5	-0.2	-1.6	2.9	4.4
Unemployment rate %	6.5	7.1	6.0	6.8	6.5	6.2	5.8	4.6	7.1	6.2	5.6
CPI % qtr	1.3	-0.2	0.4	0.3	1.3	2.6	0.4	-	-	-	-
Annual change	1.7	2.0	2.0	1.8	1.7	4.6	4.6	3.4	2.0	4.6	2.4

Past performance is not a reliable indicator of future performance. The forecasts given above are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.