



NEW ZEALAND ECONOMICS NBNZ PROPERTY FOCUS

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2012: DRAGON OR DRAGGING?

SUMMARY

Our monthly *Property Focus* publication provides an independent appraisal of recent developments in the property market.

THE MONTH IN REVIEW

A steady lift in December house sales volumes is consistent with earlier indicators pointing to a pick-up in housing market activity, underpinned by low mortgage interest rates and continued recovery from Rugby World Cup induced lulls. It is encouraging to see the property market responding to the additional support of interest rates remaining lower for longer. Given their historically low levels, we expect dwelling consents to firm over 2012. However, a weak global and labour market backdrop could act to slow the recovery in construction sector activity.

PROPERTY GAUGES

House sales ended last year with a lift in momentum, but building activity has yet to show the same degree of recovery. Our property gauges continue to give mixed signals on the outlook, a reflection of a myriad of forces shaping the outlook. We continue to err more towards structural measures, particularly given the global backdrop, and these point to a cap on the potential for a sustained pickup in momentum.

MORTGAGE BORROWING STRATEGY

Recent falls in fixed mortgage interest rates have significantly added to the appeal of fixing, with almost nothing separating carded floating, 1 year and 2 year rates. Certainty has therefore just become substantially cheaper. With the OCR unlikely to go lower, it is difficult to imagine the overall term structure of mortgage rates falling much further, suggesting there may be merit in fixing. However, this needs to be weighed up against floating rate discounts that often come up, which may make remaining floating more attractive for a little longer yet.

FEATURE ARTICLE – KEY THEMES FOR 2012

Key themes that will play an influential role in determining New Zealand's economic prospects over the year ahead include: Deleveraging headwinds; Transitioning via differentiation; Sovereign risk; Economic tensions – the interaction of five shocks; Asia – with opportunity comes vulnerability; The grand finale – game theory at play; and Desynchronisation. The collection portends a repeat of 2010 and 2011, namely, sideways movements.

THE MONTH IN REVIEW

A steady lift in December house sales volumes is consistent with earlier indicators pointing to a pick-up in housing market activity, underpinned by low mortgage interest rates and continued recovery from Rugby World Cup induced lulls. It is encouraging to see the property market responding to the additional support of interest rates remaining lower for longer. Given their historically low levels, we expect dwelling consents to firm over 2012. However, a weak global and labour market backdrop could act to slow the recovery in construction sector activity.

REINZ, HOUSE SALES – DECEMBER

Finished 2011 on a stronger note

Nationwide house sales continued to rebound in December, rising 4.4 percent seasonally adjusted on top of the 6.6 percent s.a. rise in November. The increase in sales volumes was broad-based, with all but three regions recording an increase. Monthly sales growth surged in Manawatu/Whanganui, Taranaki and Otago, but fell in Hawke's Bay, Nelson and Northland. A low inventory of suitable properties on offer is supporting prices, with buyers competing for the low number of properties available. The REINZ House Price Index rose 0.6 percent s.a., with annual house price inflation picking up to 3.1 percent. However, the median days to sell, at 39 days, remains well above the sub-35 range seen when the market was at full steam back in 2007.

STATISTICS NZ, BUILDING CONSENTS – NOVEMBER

Remains in the doldrums

The number of dwelling consents fell 6.4 percent s.a. in November. However, the fall should be seen in context of a 10.7 percent jump the previous month. **Consents are thus volatile, but they are trending up, albeit slowly.** On an ex-apartment basis, consent numbers fell 2.6 percent s.a. Dwelling consent numbers remain more than 40 percent below historical averages as a proportion of the housing stock.

RBNZ, MORTGAGE BORROWING TRENDS – NOVEMBER

Getting more bang for your buck

Around 60 percent of the total value of registered bank mortgages are on floating, which is the highest proportion since at least the early 1990s. With the inclusion of mortgage fixed for terms of one-year or less, this proportion climbed to 84 percent. This increased policy traction will encourage the RBNZ to stay on the sidelines for longer, comfortable in the knowledge that OCR moves in either direction are likely to filter through quickly into actual borrowing costs.

STATISTICS NZ, MIGRATION – NOVEMBER

Slip sliding away

The most recent migration data showed a much smaller net permanent and long-term PLT outflow of 60 persons s.a., taking the annual net PLT outflow to 568 persons. Visitor arrival numbers fell 11.6 percent s.a. as Rugby World Cup visitors departed. **Weaker migration numbers will detract from demand pressure** and will provide less support to the housing market at the margin.

RBNZ, CREDIT GROWTH – NOVEMBER

Pancake palace

Household mortgage lending was unchanged in the month of November, which followed three successive months of 0.1 percent growth. Consequently, annual growth in mortgage lending slipped further to a new record low of 1.1 percent.

RBNZ, MORTGAGE APPROVALS – MID JANUARY

Approval rating

Towards the end of last year **the rate of increase in the number of mortgage approvals pushed above 10 percent, when compared to the same period a year earlier.** A greater rise has been noted in the *value* of mortgage approvals, increasing 30 percent from a year earlier.

PROPERTY GAUGES

House sales ended last year with a lift in momentum, but building activity has yet to show the same degree of recovery. Our property gauges continue to give mixed signals on the outlook, a reflection of a myriad of forces shaping the outlook. We continue to err more towards structural measures, particularly given the global backdrop, and these point to a cap on the potential for a sustained pickup in momentum.

We use ten gauges to assess the state of the property market, and to look for signs that changes are in the wind.

AFFORDABILITY. For new entrants into the housing market, we measure affordability using the ratio of house prices-to-income (adjusted for interest rates), and mortgage payments as a proportion of income.

SERVICEABILITY / INDEBTEDNESS. For existing homeowners, serviceability relates interest payments to income, while indebtedness is measured as the level of debt relative to income.

INTEREST RATES. Interest rates affect both the affordability of new houses and the serviceability of existing mortgage payments.

MIGRATION. A key source of demand for housing.

SUPPLY-DEMAND BALANCE. We use dwelling consents issuance to proxy growth in supply. Demand is derived via the natural growth rate in the population, net migration, and the average household size.

CONSENTS AND HOUSE SALES. These are both key gauges of activity in the property market.

LIQUIDITY. We look at growth in private sector credit relative to GDP to assess the availability of credit in supporting the property market.

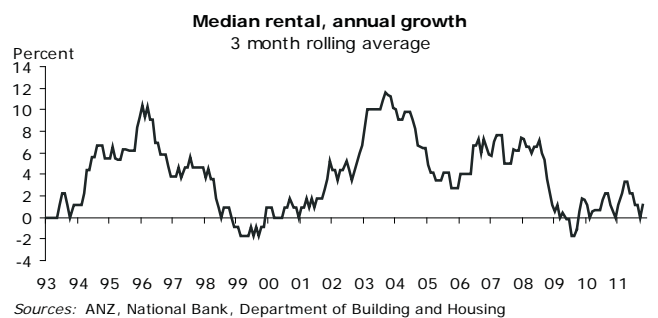
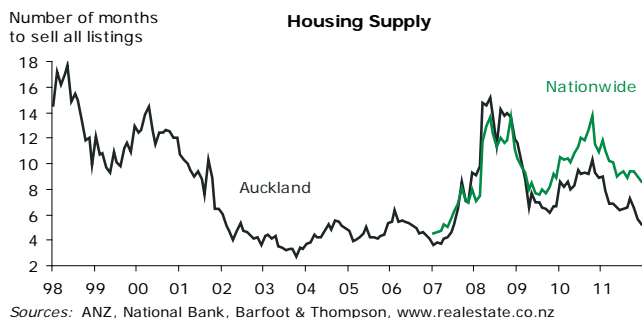
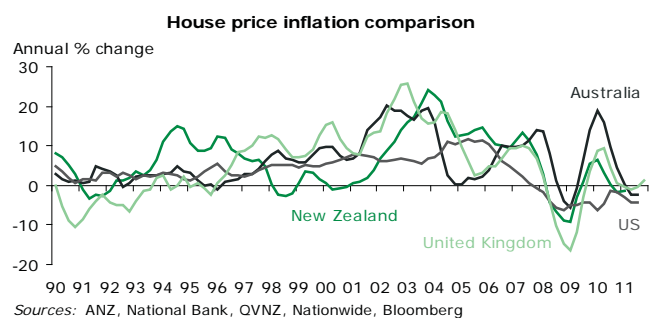
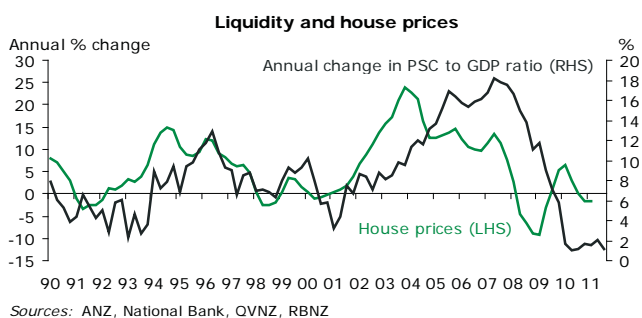
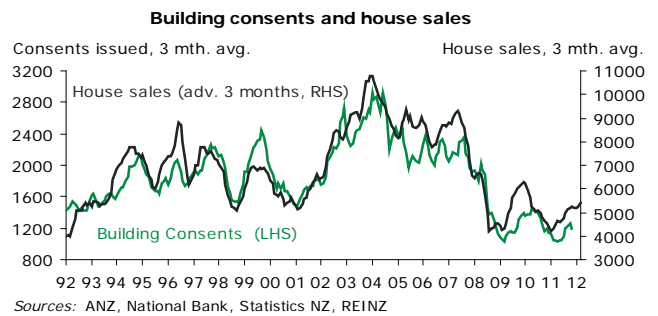
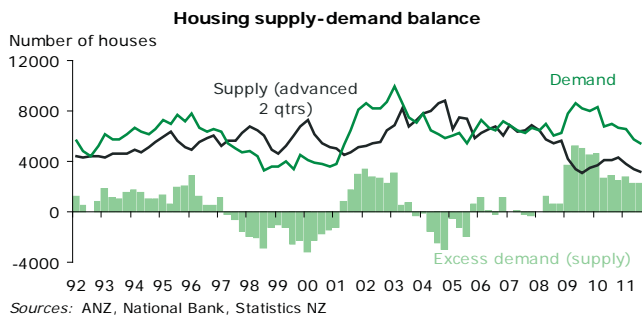
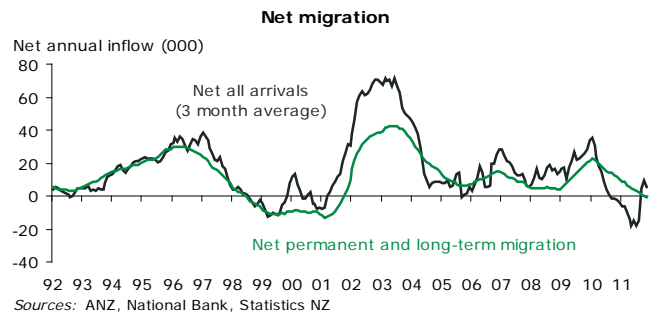
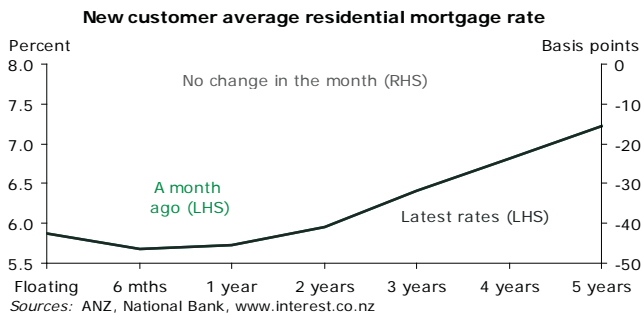
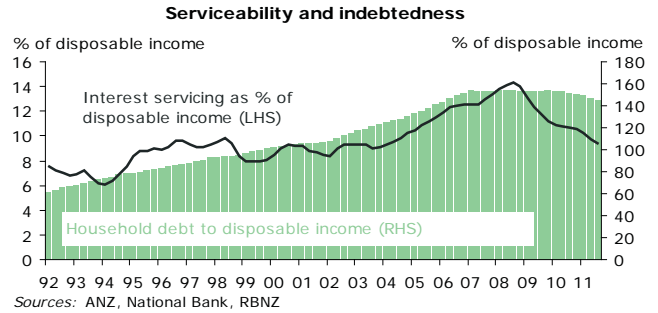
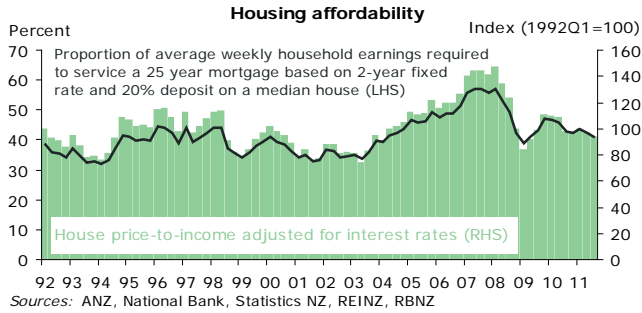
GLOBALISATION. We look at relative property price movements between New Zealand, the US, UK and Australia in recognition of the important role that globalisation is playing in NZ's property cycle.

HOUSING SUPPLY. We look at the supply of housing listed on the market, recorded as the number of months needed to clear the housing stock. A high figure indicates that buyers have the upper hand.

RENTAL GROWTH. We look at growth in the median market rent as an indication of whether it is a better time to buy versus rent, and how rental yields are shaping up for the property investor.

Indicator	Level	Direction for prices	Comment
Affordability	Turning?	↓	House prices remain expensive relative to incomes, even after allowing for low interest rates.
Serviceability/ indebtedness	Low	↓	Household claims (i.e. debt) to disposable income have slipped to a five-year low but this is still not low enough.
Interest rates	Low	↔/↑	Lower fixed mortgage interest rates will provide support at the margin, but floating remains the most attractive option for many.
Migration	Dropping	↓	Net migration continues its drift into the negative side of the ledger.
Supply-demand balance	Gappy	↔/↑	A sizeable gap persists, but is slowly closing.
Consents and house sales	Sales lifting	↔/↑	House sales ticked up, but building consents are still making only a hesitant recovery.
Liquidity	Uninspired	↔/↓	A continuation of low borrowing growth.
Globalisation	On the up?	↔/↓	Global growth forecasts are generally being revised down.
Housing supply	Flattish	↔/↑	Nationwide listings remain steady but are picking up in Auckland.
Median rent	Pinned down	↔/↓	Increasing rental growth is pushing rental yields up but these remain low.
On balance	Emerging	↔	Early signs of momentum building but will it continue in 2012? We are sceptical of a borrow-and-spend recovery taking hold.

PROPERTY GAUGES



MORTGAGE BORROWING STRATEGY

SUMMARY

Recent falls in fixed mortgage interest rates have significantly added to the appeal of fixing, with almost nothing separating carded floating, 1 year and 2 year rates. Certainty has therefore just become substantially cheaper. With the OCR unlikely to go lower, it is difficult to imagine the overall term structure of mortgage rates falling much further, suggesting there may be merit in fixing. However, this needs to be weighed up against floating rate discounts that often come up, which may make remaining floating more attractive for a little longer yet.

OUR VIEW

Recent substantial falls in shorter term fixed rate mortgage rates have all but levelled the difference between the choices out to 2 years. Indeed, at the moment, if we exclude the less popular 18 month term, borrowers can choose to float or fix for anywhere between 6 months and 2 years and expect to pay between 5.65 percent and 5.79 percent. **Of note too, both the 6 month and the 1 year rate are now lower than the floating rate.** This is a significant change from a month ago, when the floating rate was the lower rate, and when the spread between floating and the 2 year mortgage interest rate was 0.35 percent. By contrast, **there has been no change in 3 year+ fixed rates, and as such, rates step up steeply beyond 2 years, making them less attractive.**

Regular readers will recall that for some time we have flagged the value **many borrowers place on certainty. Whereas this has come at a cost over the past few years (courtesy of fixed rates being higher than the floating rate), this now comes at a discount for some terms.** On its own, this is not sufficient rationale to fix, but it does tilt the playing field, so to speak. For those who do value certainty, the difference between the 1 year rate and the 2 year rate (only 0.09 percent) is unlikely to be enough of a deterrent to choosing the latter – and we tend to agree. In our view, when rates are that close, doubling the term seems to be a much more significant consideration than the 9 point margin.

Certainty is, of course, not the only consideration. Indeed, we can think of at least two other considerations that ought to be reflected upon. **The first and possibly the most obvious is the risk that mortgage rates could move lower yet. This could happen, particularly if things get really nasty overseas (think the European debt crisis, Greece and the euro, etc).** However, **this is not our core view,** and in fact, we must admit that we have been pleasantly surprised at how constructively markets have handled major surprises recently, like news that S&P had downgraded 9 European sovereigns. One could be forgiven for

expecting the market to react badly, but it took it in its stride. **The point is markets are expecting the worst already, so things have to get really ugly if full-blown panic is to set in.** We are also mindful of local considerations, and ironically, **the very fact that fixed mortgage rates have fallen without the OCR coming down takes the heat off the RBNZ to cut the OCR.** What's more, households continue to benefit en masse as historic fixed rate mortgage roll off and reset at new, lower rates.

The other main consideration is discounting, which banks offer occasionally. The discussion so far has concentrated on carded rates, but if discounts are available, these need to be factored in. **If floating discounts are offered, with the OCR likely to be on hold for some time, it may be worthwhile staying floating for a little longer, keeping a close eye on how rates change.**

Mortgage Rates		Breakevens			
Term	Current	in 6mths	in 1yr	in 18mths	in 2 yrs
Floating	5.74%				
6 months	5.65%	5.75%	6.27%	5.49%	7.44%
1 year	5.70%	6.01%	5.88%	6.47%	7.77%
18 months	5.89%	5.84%	6.40%	7.01%	7.80%
2 years	5.79%	6.24%	6.83%	7.22%	7.91%
3 years	6.45%	6.82%	7.23%	7.63%	8.22%
4 years	6.85%	7.23%	7.64%		
5 years	7.25%				

For the sake of continuity, we have included our breakeven table as usual. It shows where rates need to be in future in order for one strategy (e.g. fixing for 2 years) to be better than another (say fixing for 1 year, then re-fixing for another year in 1 year). With so little difference between the shorter-term rates, and the 18 month rate out of line, our breakevens look a little odd this month. But **what they do show is that interest rates still need to rise mildly in order for one to be better off fixing.** In particular, they show that **interest rates need to rise rapidly for it to be worthwhile fixing for longer terms like 4 and 5 years; hence we do not favour such strategies.**

Broadly speaking then, **in the absence of discounting on floating rates, our preference is to opt for the 2 year rate,** which offers a good balance between certainty and cost (just 4 points above floating). **If discounts are available, our preference is to stay on floating for a little longer,** and fix once it becomes clearer that the general direction for interest rates is higher. Right now, our core view is that they are unlikely to fall, and that's not the same as saying they will rise.

FEATURE ARTICLE – KEY THEMES FOR 2012

SUMMARY

In this article we discuss seven key themes that we expect to play an influential role in determining New Zealand's economic prospects over the year ahead include: Deleveraging headwinds; Transitioning via differentiation; Sovereign risk; Economic tensions – the interaction of five shocks; Asia – with opportunity comes vulnerability; The grand finale – game theory at play; and Desynchronisation. The collection portends a repeat of 2010 and 2011, namely, sideways movements.

The housing market cannot be divorced from wider economic developments and we are at the whims of global forces. Prospects are linked. Our key aim in writing this article is to alert our readers to some of the wider economic forces at work, inherent tensions that exist within the economic system and what themes we see as influential over the year ahead. We've chosen seven key themes. They are by no means exhaustive. We'd need a book to cover the myriad of influences on the economy and housing market. Rather we've decided to focus on what we consider the most relevant. The themes are:

- **Deleveraging (still);**
- **Transitioning via differentiation;**
- **Sovereign risk;**
- **Economic tensions: the interaction of numerous shocks;**
- **Asia – with opportunity comes vulnerability;**
- **Game theory at play – looking for a mandate to bite the bullet;**
- **Desynchronisation.**

THEME 1: DELEVERAGING HEADWINDS

Call it "that old chestnut", call it what you will. But don't dismiss it. **Deleveraging is certainly a familiar theme, but it still remains at the top of our list of key considerations.** Of course, we have been deleveraging for three years now, but it's far from over (NB: we define deleveraging as a drop in debt to income ratios as opposed to falling nominal debt levels). Our view is based on three simple considerations:

1. **We came to the end of a multi-decade leveraging supercycle across Western society in 2008.** Credit growth cannot expand by 2 to 3 times the rate of nominal GDP or income for a sustained period. Penance beckons. The consequences and necessary "healing" include: bank deleveraging in Europe; fiscal austerity; negative feedback effects on the real economy; more regulation – without invoking unintended

consequences; and social fallout. These consequences are only now starting to be felt.

2. **New Zealand was binging at the party** like a host of others. Hence the hangover.
3. **A sustained improvement in structural barometers is a precursor to sustained cyclical recovery.**

So where does NZ stand? It is worth summing up what we have seen in the past three years.

- After a recession and a tepid recovery, the **New Zealand economy is the same size as it was in 2007 in real terms.** In real per capita terms we are almost 5 percent smaller.
- **Commodity prices have lifted strongly since 2008,** giving a huge boost to rural incomes, and mitigating what could have been a nasty hit to heavily indebted parts of the rural sector.
- **House prices are around 2½ percent below their peak** in nominal terms. They've fallen, recovered, fallen and moved sideways, but not collapsed.
- **The household saving rate has improved** from -7.5 percent of disposable income in March 2007 to +2.8 percent in September 2011.
- **The current account deficit has fallen** from 8.9 percent of GDP at the end of 2008 to 4.3 percent as of September 2011.
- **Net external debt has fallen** from 84.7 percent of GDP in March 2009 to 72.9 percent of GDP as of September 2011.
- **Households have deleveraged.** Household debt to income has fallen from a peak of 154 percent in mid 2008 to 144 percent in September last year.
- **We've seen tax and regulatory changes.**
- **The fiscal position has deteriorated markedly.**
- **Our credit rating has been downgraded** by both Fitch and Standard & Poor's.

Although we can take heart from the improvement in many of these metrics, it has come at a cost. The retailing environment has been poor and trading is still tough. While housing market volumes have stabilised, sales in the past 6 months remain around 36 percent lower than levels seen in 2005-07. These sectors will remain the sacrificial pawns in getting the economy back on its feet.

Of course, the big question is, are we there yet? The short answer is no.

Where do we need to be to set the stage for the good times to roll again?

FEATURE ARTICLE – KEY THEMES FOR 2012

- **The global scene needs to stabilise.**
- **Net external debt needs to get below 60 percent of GDP.**
- **The household saving rate probably needs to be north of 5 percent of income.**
- **Fiscal deficits need to turn into surpluses.**
- **Housing affordability needs to improve further.**

There are a host of other dynamics that could assist. For instance a sustained lift in productivity growth would not go amiss. But turning the dial and trend here will take time.

2011 was dominated by a deleveraging headwind and we expect the same dynamic to be influential in 2012. As economists that means we're paying more attention to the structural indicators as opposed to the daily barrage of cyclical measures. It is progress in the former that will ultimately unlock a sustained lift in the latter. Until then, cyclical barometers will merely oscillate as opposed to trend upwards. This means we pay more attention to the balance sheet over the supply-demand figures that property bulls points to as driving prices materially higher.

What about the intensity of the deleveraging dynamic? **We expect headwinds to be as intense as they were between 2009-2011, but with a couple of twists.**

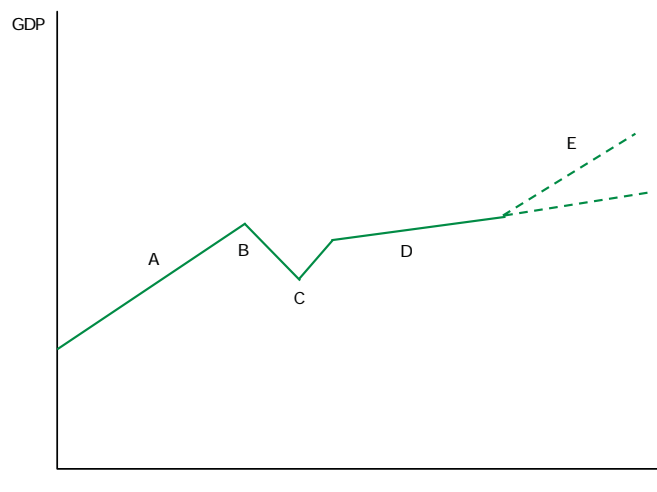
- **There will be a shift in the mix.** Rural sector deleveraging is ongoing but lessening in intensity as the commodity price boom filters through and rural land prices stabilise. Nominal business borrowing collapsed by more than 3 percent between April 2009 and July 2010, but has since recovered. Conversely, fiscal retrenchment is only beginning (there are huge lags) and households still need to get their finances in order.
- **The intensity will be strongly influenced by the global scene** (as a driver of income generation).
- **We have to acknowledge that income growth needs to exceed cost (spending) growth for a sustained period.** If income slips, so too will prospects for spending and the converse applies. Our working assumption is that we need to see something akin to "negative jaws" of 2 percent; which means spending growth 2 percentage points below income generation. That's a big gap.

THEME 2: TRANSITIONING VIA DIFFERENTIATION

Last year we identified **five stages in the current economic cycle**, and they still apply. **The first**

stage (A) was the "old normal", the 2002 (or even as far back as the early 1990s) to 2007 period, where growth **was driven by excessive borrowing** and risk-taking. This led to asset price bubbles and unsustainably high wealth-induced spending, or artificial wealth. **Stage B over 2008-09 saw the inevitable initial purging** that followed such excesses. **Stage C** was the healing or recovery process that we saw in late 2009 and first six months of 2010, helped by aggressive policy action and an inventory rebuild. "Healing" or "recovery" is probably a bit optimistic: more like **stabilisation** following capitulation, and a recoil off lows.

The New Zealand (and global) economy entered stage D – which we call "transition", around the middle of 2010. Normal pro-cyclical forces and drivers of the business cycle, such as consumer spending, failed to kick on and take the inventory rebuild into something of substance. That's because there's a debt "supercycle" and payback dynamic that is overwhelming the usual cyclical forces. This period is where the economy transitions on a number of levels, including **altering the mix of growth (rebalancing)** and also paying penance for prior sins, i.e. **lowering debt** as a share of GDP across Western society. This entails **a period of stuttering and "grumpy" growth (D)** as stylised below. In the final stage (E), trend growth rates (the slope) will be at least partly a reflection of the choices made in the transition stage.



The economy is expected to remain in the transition stage for a number of years. We are not talking booms to busts, but rather a period of grumpy growth. Transition will involve a number of dynamics:

- **A capped rate of growth**, as a leveraging tailwind is replaced by a deleveraging headwind. Put simply, the slope of D is less than A.
- **A different mix to growth.** You can't borrow and spend your way out of a debt-induced jam.

FEATURE ARTICLE – KEY THEMES FOR 2012

So spending sectors of the economy need to underperform.

- **The re-mobilisation of resources**, including labour and capital, across sectors, as a spend-centric model is replaced by a more balanced model for growth. Capital and labour does not respond instantaneously. It will be messy.
- **Economic wobbles.** Time is the only true healer. We're in the hands of the politicians globally to make the tough decisions.

So what determines the rate of growth in the transition stage? **The weaker the balance sheet, the greater the deleveraging headwind** holding back near-term growth. NZ is somewhat saddled here by its sins of the past. Having more flexibility across your economy in areas such as the labour market and a floating currency can assist by allowing resources to adjust more readily. On this front, NZ stands strong.

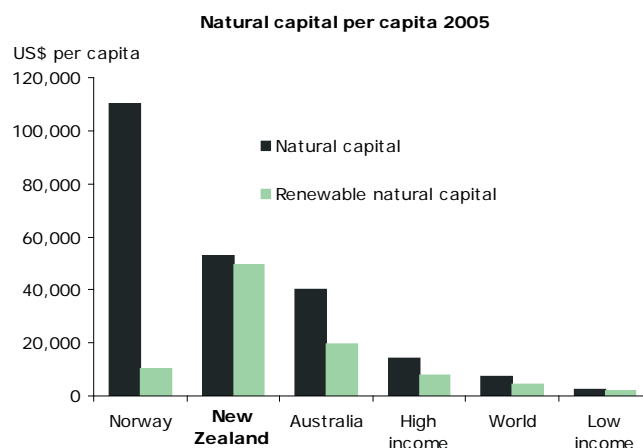
Economists can probably point to 80-odd factors that determine growth. The problem is that it's difficult to disentangle the causality, for a lot of so-called growth determinants (such as investment) are key components of GDP themselves. We know that traditional dynamics such as population and productivity will of course be influential. **Depopulation in Christchurch, the allure of Australia and sub-par productivity performance are challenges for NZ.**

Increasingly key for an indebted nation will be differentiation, i.e. convincing investors that you're on the right track. Nothing is a problem until markets think you are a problem, and as Ireland, Greece, Italy and other highly indebted countries will bear witness to, problems can turn exponentially ugly in a very short time. We see differentiation as a major factor determining both the rate of growth in the transition stage, and the volatility around it. Investors are eyeing the scene with confusion, and New Zealand is facing a marketing challenge of crucial importance.

We see differentiation occurring on a number of levels.

- **Natural endowment.** It is easier to transition if you have strategic areas of excellence, or areas of comparative advantage. This makes it possible to get debt to GDP down by raising GDP, a far preferable adjustment path to scrimping.

NZ ranks 8th in the per capita natural resources stakes globally, a few notches higher than Australia, who are often deemed the lucky country. And in terms of per capita renewable natural capital, we lead the world.



Source: The World Bank "The Changing Wealth of Nations" 2010

There are, however, tensions between some of our endowments. Unlocking them is not easy. You wouldn't want one area of strategic excellence such as mining to undermine another such as tourism, so sensible regulatory heads are required. However, just like successful businesses need something in their offering that is "different" (whether that be brand, relationships, or a better service proposition), the same applies for a nation. New Zealand has this in spades and it's critical, **for the more you pull an income-generating lever, the less pressure there is for austerity, and the better the prospects are for spending sectors of the economy, including housing.**

- **The political framework.** New Zealanders tend to take their lack of corruption and well-functioning political system as a given. But it matters. And while democracy may be "the worst system of governance except for all the others" in that it rewards short-term thinking, we are encouraged by the consistency being shown across the political spectrum towards fiscal savings and responsibility. If you want to see political fragmentation and institutions that are conducive to gridlock, look no further than the US and Europe. Our system is not perfect but it's better than most.
- **Evidence that society is "getting it".** Leadership can only take you so far – habits have to change on the ground. Our economic performance, after all, reflects the decisions of 4 million individuals, whether that's their borrowing, spending, or voting decisions. Japan's lost decade epitomises a refusal to bite the bullet. It appears in New Zealand the critical mass is now tilting towards the necessary structural change. Witness the continued uptake of KiwiSaver despite reduced incentives, the focus on fiscal responsibility in the 2011 election, a refreshingly non-hysterical discussion of the possibility of raising the retirement age beyond the age of 65... such signals

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don't guarantee that society is willing to do the hard yards but they flag that things are moving in the right direction.

- **Microeconomic reform.** Microeconomic issues are often overlooked when assessing the macroeconomy, but as stated, the economy is the summation of its parts. It is crucial to get the right incentives in place. Tax policy is a biggie here, as well as welfare policy design, the ease of starting a business, property rights, balancing public and private interests, and avoiding corruption and rent-seeking (moulding one's economic activity around maximising returns from distortionary policies, rather than true economic profit). As a general rule NZ is pretty good in this area, whereas the real issue for a host of nations is microeconomic reform, and altering behaviour at the firm and individual level. Moreover, we're seeing continued tweaks. Over time, the benefits will accrue.

These factors do not deliver nirvana. Nothing does. But in a world that is "transitioning", differentiation through showing competency and maintaining confidence is key. **Such differentiation allows you to remain in control of your own destiny (and adjustment).** The alternative is the likes of Greece.

THEME 3: SOVEREIGN RISK

2008 was a credit crisis across the financial system, and unsustainable levels of debt to GDP were at the heart of the problem. Between 2008 and 2011 the private sector began to improve balance sheets. However, **the ratio of debt to GDP in most Western societies is now higher than in 2008.**

Private sector deleveraging has simply been replaced by sovereign and government leveraging. Some of this was a forced "socialisation" of the 2008 crisis. The average level of net government debt across the OECD rose from 43.9 to 62.5 percent of GDP between 2008 and 2011 and is expected to continue rising.

With attention now focused on sovereigns, two years ago we developed an indicator to assess sovereign debt vulnerability in an objective manner (sovereign risk was one of our key themes at the start of 2011). Without having the massive resources of a rating agency, we simply assess each country on the basis of two broad criteria. First, we looked at "bad" or "worry" variables – things like government debt, the fiscal balance, the current account, net external debt and the unemployment rate. But we also recognised that there would be offsets, and looked at things that may buy you a bit of time – GDP per capita, population, the existence of a floating exchange rate, political stability, competitiveness etc. By comparing one set of criteria against the other, we arrived at a "net" score giving a simple metric of vulnerability for key nations.

The table below summarises the results. Nations are ranked according to the overall score, which is the net of the unfavourable and favourable numbers. But remember, this is a peer group comparison, so if everyone improves their lot, overall scores will improve. **Because investors have a choice as to where they invest, what matters most is a country's overall placing on the table.**

Country	Overall Score	Overall Rank	Prior Rank (mid 2011)
Norway	40%	1	1
Switzerland	30%	2	2
Australia	17%	3	3
Denmark	17%	4	5
Sweden	13%	5	6
Singapore	11%	6	4
Taiwan	11%	7	7
Luxembourg	10%	8	8
Canada	8%	9	9
NZ	2%	10	10
Korea	-1%	11	14
China	-1%	12	13
Czech Rep	-2%	13	15
Japan	-2%	14	12
Hong Kong	-3%	15	11
USA	-3%	16	16
Finland	-5%	17	17
Germany	-5%	18	18
Austria	-9%	19	19
Netherlands	-11%	20	20
Malaysia	-12%	21	22
Hungary	-12%	22	25
Thailand	-12%	23	24
Poland	-13%	24	21
Iceland	-15%	25	23
UK	-16%	26	26
India	-16%	27	27
Philippines	-18%	28	28
Vietnam	-21%	29	29
Indonesia	-22%	30	30
Belgium	-24%	31	32
Italy	-24%	32	31
France	-29%	33	33
Slovakia	-29%	34	34
Ireland	-30%	35	35
Spain	-38%	36	36
Portugal	-42%	37	37
Greece	-59%	38	38

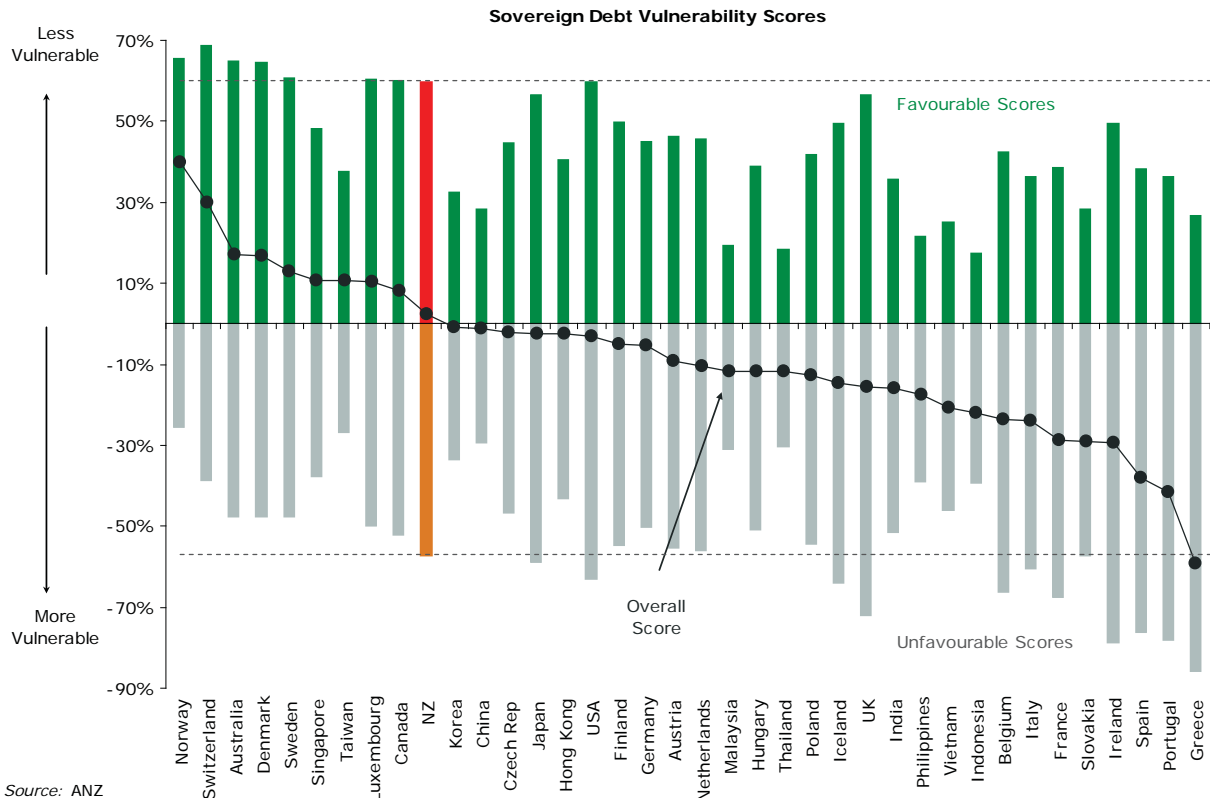
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Our rankings highlight several consistent points:

- **Europe continues to dominate the problem end of the spectrum** and it's a reflection of both unfavourable and poor favourable characteristics. By contrast, Switzerland, Scandinavia, and the commodity countries dominate the top end. China and the more developed Asian economies are in the top half of the table.
- Big countries (like the US and UK) remain mid-table. They **have serious fiscal issues, but this is offset somewhat by positive factors**.
- There has been some minor position shifting in terms of rankings in the middle of the table, but those at the top and bottom have tended to stay put. **Those in the hock are still in the hock, and those that were never in it have not been dragged in.**
- **NZ remains reasonably placed.** It ranks below average (26th) for unfavourable characteristics, a reflection of a high net external debt position and fiscal blowout in 2011, but has an above-average ranking (9th) for favourable characteristics.

All of this leaves us with a strong feeling that the situation has not improved. There has been much talk, and arguably more "muddling through". **But at some stage, push will come to shove, and tough decisions will need to be made.**

The experience of Italy is demonstrative of how quickly a tailspin can develop. Once confidence is lost, borrowing costs rise, financial conditions tighten, and recessions beckon. This only lifts the debt burden further, forcing politicians to implement austerity measures, potentially plunging the country into a deeper recession, and confidence deteriorates further, and **before you know it the downward spiral is in motion.** Remember, Italy is the 8th biggest economy around the globe and at last count the third largest borrower in the bond market.



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Italy, then, is a clear example when the market calls time; the game is up, hence the importance of policymakers being on their game. **In practice, this means putting our fate in the hands of politicians. Even with the best intentions, they may not be able to deliver the credible outcomes the market so desperately craves. It's not easy balancing the demands of the populous (who vote you in and out) with the market (which you depend on for financing).**

Although New Zealand ranks fairly well overall, we are not above scrutiny by global markets and can't be complacent. We are more "plugged in" to the global economy through trade and financial markets than ever. **The "Six C's" are crucial barometers for New Zealand – namely contagion risks (we need to be doing the basics well), confidence (growth), cost of credit (offshore borrowing), China (can it remain immune?), commodity prices (okay for now) and the currency (up and down like a yo-yo).** Witness, for example, swings in sentiment and pricing on all six of the C's that have occurred over the past year as financial markets have swung from optimism to pessimism regarding Europe. **We are simply dreaming if we think a significant shock in Europe won't cause shock waves here. The six C's are metrics that bear watching closely.**

THEME 4: ECONOMIC TENSIONS – THE INTERACTION OF FIVE SHOCKS

The economic outlook is arguably more complicated than any time in New Zealand's economic history. Theme 1 detailed the **structural headwinds** the economy is facing. Restoring a modicum of health to the national balance sheet is a prerequisite to any sort of cyclical upturn taking hold. This is shock 1. That means any talk of a supply-demand imbalance, housing-led upturn, or borrowing and spending our way to nirvana is premature. On top of this we have a **weak and volatile global scene** to contend with (shock 2). We can add to that three other material shocks and tensions.

- **Rebalancing.** The economy remains lopsided, with excessive concentration in spendthrift activity, and this is at the expense of earning. Since 2004 activity in the tradable sector has gone backwards, and income growth has not kept up with spending. It will take years for resources (i.e. labour and capital) to respond to different price signals, for opportunities to be unlocked, and the DNA of society to change.
- **A positive income shock.** We're seeing structurally higher demand for commodities, which has seen our goods terms of trade hit a 37 year high. Asia is increasingly relevant for New Zealand as an export market, with Asia ex-Japan

now accounting for a third of merchandise exports, versus a quarter a decade ago. We're getting better connected in regard to the Asian region, with a free trade agreement with India currently under negotiation. But we must add a note of caution here: with exposure to the upside of Asia's potential comes vulnerability to adverse turns. And there are plenty of pundits picking an adverse turn for China in the next 12 months (see Theme 5).

- **The Canterbury earthquakes.** The impact channels are endless. Relative to the size of the economy, the estimated cost (more than 10 percent of GDP) is unrivalled globally. A lot of wealth has been destroyed and we see it as accentuating the structural change in households' savings behaviour. Canterbury's population will not be the same, but the South Island needs it as a hub. We expect a net migration outflow from the region in 2012 but an inflow once the rebuild starts. There will be a massive construction response, but the ground needs to stop shaking first and Christchurch's events will alter building and insurance standards nationally. And in reality, much of what was lost cannot or will not be rebuilt, at least not in Christchurch. Nonetheless, we need to rebuild a lot of destroyed domestic capital at a time resources also need to be deployed to tradable-centric areas (refer above). This risks blowing out the current account deficit unless consumption as a share of GDP drops. Over time the costs of Canterbury will hit consumers' pockets via increased levies, higher insurance premiums and reduced government spending in other areas.

These shocks are complementary in some facets but opposing in others. Deleveraging is deflationary. Commodity income shocks and natural disasters are not (indeed, we'd put some of the current Auckland housing inflation down to earthquake migration). The income shock is helping New Zealand get its balance sheet back in order via income generation (by getting the debt to GDP ratio, the current account deficit, and the consumption to income ratio down). Conversely, rebuilding Canterbury will involve dedicating huge amounts of resources to rebuilding domestic capital (i.e. housing and infrastructure) at a time when we're also supposed to be investing in other regions and sectors to address our national indebtedness.

To put these shocks in perspective in terms of their significance, issues such as the leaky home/building crisis, which hasn't gone away and is hugely relevant, doesn't make our top five (deleveraging, the global scene and the three above). And if we were ranking economic developments by national significance, PSA – which is decimating the gold kiwifruit industry – would not even make the top ten.

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That is not to belittle the kiwifruit industry or those facing large leaky building repair bills. It's to underline **the mammoth scale of the forces buffeting the New Zealand economy** at present.

The interaction of these shocks will see **more volatility across the New Zealand business cycle than is normal, amidst a lower trend growth rate**. It will be difficult to get a steer on the true state of affairs. Data will be murky. A lot will have to be taken on faith. **Sectors across the economy will move up and down, depending on which shock is dominating at the time**. Probably the clearest trend will be a lack of one.

This also portends challenges for policymakers as they face off against voters with expectations based on a debt-accumulating world that no longer exists. Fine-tuning the supply-side capacity of the economy will take on particular importance. Things like rebuilding Christchurch and rebalancing require at their core the remobilisation of resources, and getting the right incentives in place in areas such as education will be critical. There will be trade-offs in dealing appropriately with these shocks, and **a long-term view will be key to achieving the best outcomes**. Navigating numerous shocks simultaneously ups the ante on true leadership to prevail over populism. We hope cool heads prevail and that enough of society grasps the big picture.

THEME 5: ASIA – WITH OPPORTUNITY COMES VULNERABILITY

The economic opportunities in Asia and even a little further up the silk route in the Middle East are unprecedented for a number of sectors that New Zealand excels in. The "food story" of large populations increasing their protein and fat consumption, with limited key natural endowments to meet these needs, has been well documented. This is further energised by rising incomes in the middle class, urbanisation, and the modernisation of their

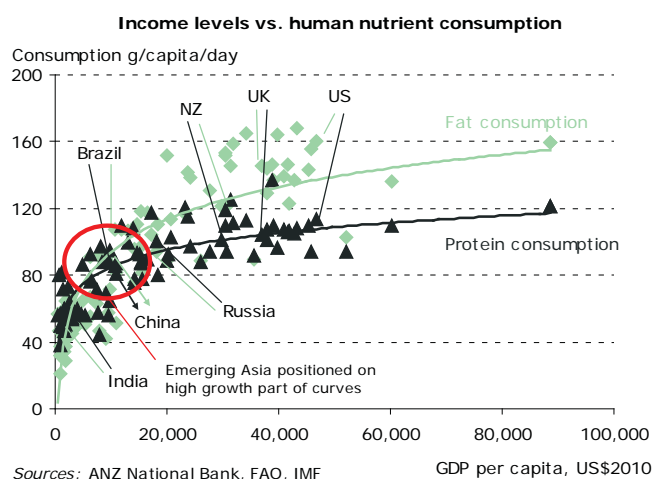
food industries. The Asia-Pacific region now makes up 55 percent of New Zealand's total merchandise trade, up from 42 percent 10 years ago.

Tourism is another benefactor. Total tourism numbers from Asia (excluding Japan) have increased by 23 percent over the last 10 years.

Things such as rising connectivity, our close geographical position and the rise of e-commerce will continue to facilitate these prospects. An increasing number of bilateral agreements with key countries such as China have opened the door for New Zealand's wares. The countries with which New Zealand has a FTA cover 2 billion people (29 percent of global population), 16

Country	GDP US\$bn in current prices	Population (millions)	Average real GDP growth past 10-years	% of NZ exports	% of NZ imports
FTA in force or about to be in force					
Australia	1,507	22.5	3.0	22.6	16.3
Singapore	266	5.3	6.3	1.7	4.8
Thailand	339	64.3	4.5	1.6	3.0
Brunei	16	0.4	1.4	0.0	0.9
Chile	243	17.4	4.1	0.1	0.1
China	6,988	1348.1	10.6	12.4	15.8
Myanmar	50	62.4	9.8	0.0	0.0
Philippines	216	95.8	5.0	1.6	0.3
Vietnam	122	89.3	7.2	0.9	0.6
Cambodia	13	14.4	7.7	0.0	0.0
Indonesia	834	240.5	5.5	1.9	1.3
Laos	8	6.6	7.5	0.0	0.0
Malaysia	248	28.7	5.1	1.8	3.3
Hong Kong	247	7.2	4.6	1.6	0.4
Total				46.3	46.8
FTA under negotiation					
Bahrain	26	1.1	5.6	0.1	0.1
Oman	67	3.1	4.5	0.1	0.8
Kuwait	171	3.7	6.0	0.2	1.2
Saudi Arabia	560	28.2	3.9	1.5	1.4
UAE	358	5.4	5.8	1.1	1.6
Qatar	173	1.8	14.4	0.1	1.8
Korea	1,164	49.0	4.2	3.5	3.2
India	1,843	1206.9	7.8	2.1	0.8
Russia	1,885	142.4	4.8	0.7	2.6
Belarus	58	9.4	7.5	0.0	0.0
Kazakhstan	180	16.5	7.6	0.0	0.0
Peru	168	30.0	6.3	0.2	0.1
US	15,065	312.9	1.6	8.3	11.1
Total				17.9	24.7

Sources: ANZ, IMF, Statistics NZ



Sources: ANZ National Bank, FAO, IMF

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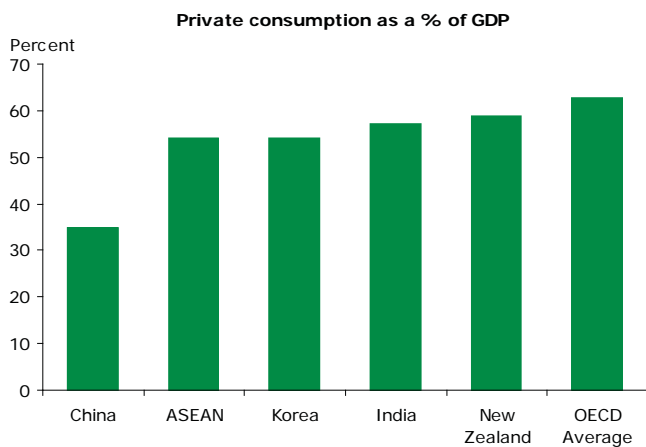
percent of global GDP (in current prices), account for almost half of New Zealand’s merchandise trade, and, importantly, have been growing at a much faster rate than global growth. The FTAs New Zealand now has under negotiation cover 1.8 billion people (26 percent of global population), 31 percent of global GDP and currently account for around 18 percent of our trade. If all of them prove successful, then New Zealand will have free access to 56 percent of the world’s population, accounting for close to half of global GDP. This represents a big playground for a country of just 4.4 million people.

In many cases, we have been the first across the line, or in the lead, which allows us to establish a beachhead versus our competitors.

However, while Asia has been a strong focus opportunity-wise for investors, particularly since 2008 and there are further opportunities to exploit, Asia is not immune to what is happening elsewhere in the world. It is subject to business cycles, and countries such as China have their own unique structural economic issues that need to be addressed. With New Zealand more reliant on Asia, we are also increasingly susceptible to what happens there.

Key issues to keep an eye on in Asia in 2012 will be:

- 1. Growth and trade.** The more open economies are more sensitive to changes in global growth and have greater downside risks. This means we can’t divorce China *et al* from European developments.
- 2. Private consumption.** Asia must progress towards more economic growth coming from private consumption instead of being reliant on the traditional export and investment model.



Sources: ANZ, National Bank, The World Bank

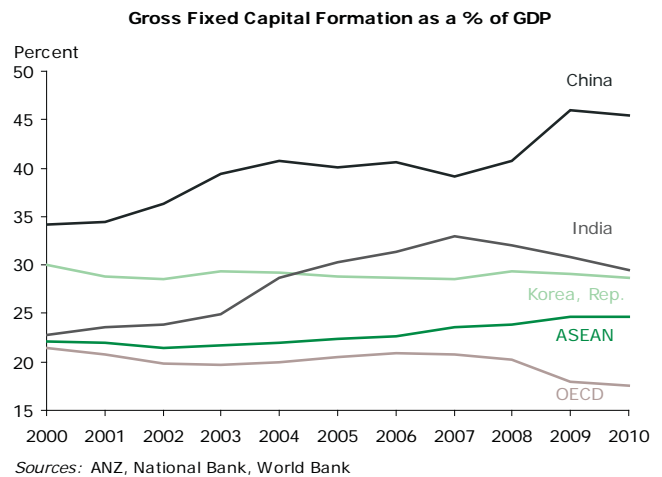
- 3. Financial tail wags real dog.** Market turbulence lowers asset values, confidence, and growth. Our financial conditions measures for Asia have a high

weight on asset prices; in some cases they are extreme. This high correlation in itself leaves us uneasy regarding how much of the Asia growth story may have gotten ahead of itself.

- 4. Bank funding.** Financial systems that rely on wholesale funding (loan/deposit > 100 percent) are at risk if inter-bank flows dry up.

Many of the economies in Asia have been through a tightening of macro and fiscal policy over the last 12 months to dampen down inflationary flames. In many countries, monetary policy was “behind the curve” in 2011. **With growth in a cyclical downturn, inflation still persistent in some economies, and a deterioration in Europe’s economic prospects (Asia’s largest trade partner), walking the tightrope of keeping inflation under control but not overshooting the mark and choking off economic growth will be tricky.**

This is especially the case where the traditional model for growth in many cases has been export-led industrialisation, supported by weak currencies. It has produced high net export and fixed capital investment shares and a lower consumption share of GDP. The squeeze could come on very quickly should trading partner demand dry up, especially for those economies that are more open.



Longer-term, net exports, fixed capital investment and saving need to fall as a share of GDP, while private consumption needs to sharply rise. This is a particular issue for China but is also a familiar theme for many other ASEAN countries where private consumption as a percentage of GDP is well below the OECD average. The challenge of increasing private consumption before the investment boom turns into a bust cannot be overstated in countries such as China that are still heavily controlled by the State. **High saving rates and low private consumption are structural issues that will take years of politically difficult reform to change.**

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If financial market turbulence and policy responses hit capital investment growth, this would have a disproportionate effect on growth in countries such as China and India. The lead indicator of such a change will be international prices for key hard commodities such as copper, iron ore, nickel and the like, with China now consuming 40-50 percent of global trade in these products. Late 2011 falls in these metals may be telling.

The other challenge that could possibly hurt the credit cycle and growth in some Asian economies is European banks massively contracting their balance sheets by calling in, or not rolling over, loans. In general, European banks' gross assets in Asian economies rarely exceed 10 percent of total outstanding domestic credit. Loan-to-deposit ratios in most of Asia are well under 100, implying low reliance on offshore wholesale funding. However, India, Vietnam, Korea and Australia, despite recent improvements, are the most vulnerable if this were to occur.

THEME 6: THE GRAND FINALE – GAME THEORY AT PLAY

The challenges for the global economy are well documented. There is simply too much debt. A host of governments face solvency challenges. The global economy is unbalanced: excessive saving in the East is financing consumption largesse in the West. Governments have been on a borrowing bender.

Solutions are easy to identify; it is implementation that is difficult, for we are in the realm of politics and there is a group dynamic to it, as well as a host of considerations that go beyond pure economics. Witness trade tensions between the US and China; the furore over a financial transactions tax between the UK and France/Germany; uncertainty over pending bank regulation including Basel III; street protests against austerity measures; the rise of nationalist parties in Europe *et al.* These are non-trivial tensions that illustrate the difficulty getting a truly unified response.

The global economy is desperately looking for leadership. Probably the most important aspect of the leadership challenge is achieving significant fiscal austerity to demonstrate solvency.

Will politicians make the hard decisions? So far they have avoided them as much as possible, so far. The Eurozone crisis unfolding at present, if left unchecked, could quickly engulf the US next. Doing nothing is not an option. But this does not necessarily mean the "right" thing will be done. **Rather than go into the ins and outs of the various challenges in a political sense – which are huge – we turn to game theory,** and in particular the prisoners' dilemma, which illustrates the **tension between**

group and self interest. This dynamic is played out time and time again around the globe. Remember, global problems require truly global solutions.

This is how it works. Two men are arrested on suspicion of robbing a bank, but the police do not have enough evidence for a conviction. Following the separation of the two men, the police offer both the same deal – if one testifies against his partner (defects), and the other stays quiet (co-operates with his partner), the betrayer goes free and the co-operator receives the full 5 year sentence. If both remain silent, both are sentenced to only 6 months in jail on a minor charge. If each 'rats out' the other, each receives a 2 year sentence. Each prisoner must choose to either betray or remain silent; the decision of each is kept quiet. What should they do?

	Prisoner 2 stays silent (co-operates)	Prisoner 2 confesses (defects)
Prisoner 1 stays silent (co-operates)	Each serves 6 months in jail	Prisoner 1: 5 years Prisoner 2: goes free
Prisoner 1 confesses (defects)	Prisoner 1: goes free Prisoner 2: 5 years	Each serves 2 years

The best outcome for the prisoners is that they both stay silent or "co-operate" with each other, as this minimises their jail time. However, a closer look at the payoff matrix reveals a range of possible outcomes. Consider prisoner 2. They don't know what prisoner 1 will decide. If prisoner 1 stays silent, they are best to confess, going free rather than serving 6 months. If prisoner 1 confesses, they are still best to confess (2 years rather than 5 years). Individually, the optimal strategy for both prisoners is therefore to confess, even though this leads to a worse outcome for both of them than staying silent.

Politicians face a similar situation when trying to agree on solutions to the global problems.

Where tension exists between a country's own best interest and the group's best interest, a less than optimal solution is highly likely. This is especially the case in Europe where the monetary union exacerbates the situation, limits the available solutions, and heightens the trade-offs between the optimal and actual outcomes of decisions. Each country is looking out for its own banking sector, its own export sector, and its own credit rating. Worse still, each politician is looking out for their own re-election chances. The UK's recent decision to opt out of the EU-wide negotiations on a new fiscal treaty was a case where self-interest (avoiding curbs on London as a financial hub) trounced group interest (a unified front).

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So how does the grand finale look? We are not sure. The *hope* is that enough will be done to head off problems before they arise. The *fear* is that a) the later you leave it the more exponentially difficult the decisions become (and for politicians there are no easy choices in 2012), and b) individual interest will dominate group interest, and the combination will lead to **an accident of sorts before mandates are given to make the hard choices – whether that’s a true political mandate, or sheer will forcing through the tough leadership solutions regardless of the damage it does to politicians’ re-election chances.** Upcoming elections (Finland, Greece, Russia, Slovakia, and France in the first half of this year alone) may be preventing politicians from making the tough calls now, but they are also an opportunity. It’s easier for a new Government to implement unpopular measures and blame their predecessors for making it necessary.

Can an accident be averted? Yes. Theme 2 – “Transitioning via differentiation” applies. It’s about showing competency, confidence and credibility. Going back to our Prisoners’ Dilemma example and application of game theory, if the game is played repeatedly, players can ultimately end up with the “Pareto Optimal Solution”. Oil cartels succeed, even though everyone at any given time has an incentive to “defect” by increasing their production, because everyone is in it for the long haul. Arguably, the 2008 GFC should serve as the “lesson” regarding short versus long-term thinking. **Yet when we consider the cultural and attitude differences in the West and the East,** and prospects for Europe corraling 17 euro member nations (and 27 in the EU) into some sort of fiscal union, which is required for the euro to survive, well, **it just seems a bit of a stretch.**

THEME 7: DESYNCHRONISATION

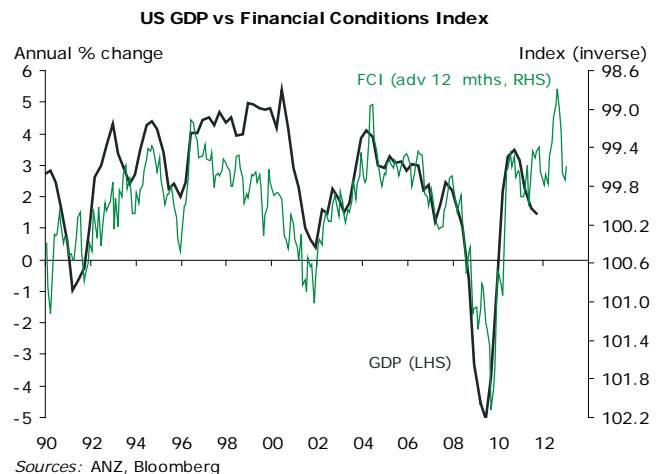
As a baseline assumption we view the world as “coupled” in a growth sense, such is the strength of trade and financial linkages. Historically, Western economy business cycles have tended to be well correlated. The emergence of China as an economic powerhouse has added a twist to this – they were a key source of global stabilisation in 2009 – but has not fundamentally altered the core proposition of coupling.

However, we are also mindful of growing disparities in terms of growth prospects across key regions that point to the possibility of decoupling. **To give us a steer, we track financial conditions across an array of countries.**¹

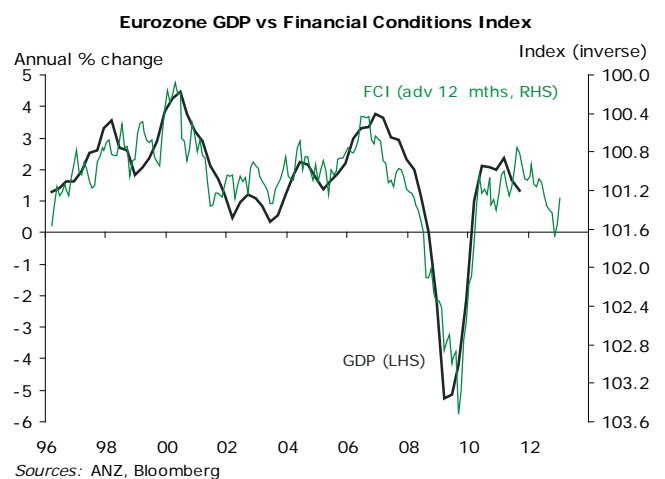
¹ Our financial conditions index summarises a range of financial variables into a single series that can be used to predict the future path of the economy. Where available, our FCI includes the currency adjusted for commodity prices or terms of trade movements, interest rates, asset prices, credit growth and proxies for the cost and availability of credit.

A quick look at our financial conditions measures across key regions highlights the disparities.

- **Prospects for the US look fairly solid.** The “level” of conditions has come back thanks to an unwind of the surge in M2 money supply (i.e. QE2), but they still point to growth of around 3 percent.



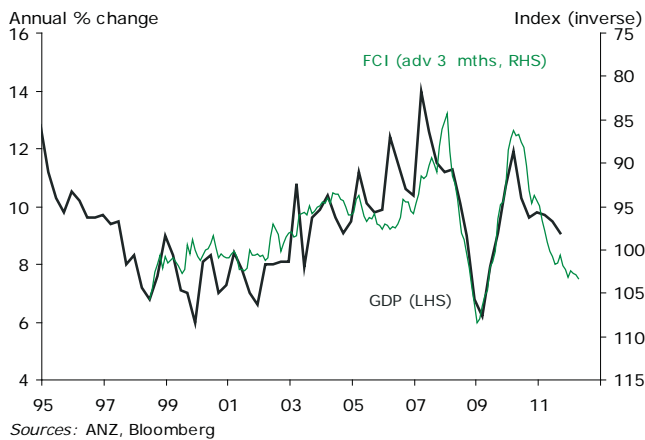
- By contrast, **our Eurozone FCI is pointing to a sharp slowing in European growth,** and the possibility (we would say inevitability) of recession.



- **Our FCIs are flagging a slowdown in China** too, adding weight to fears that some moderation lies ahead.

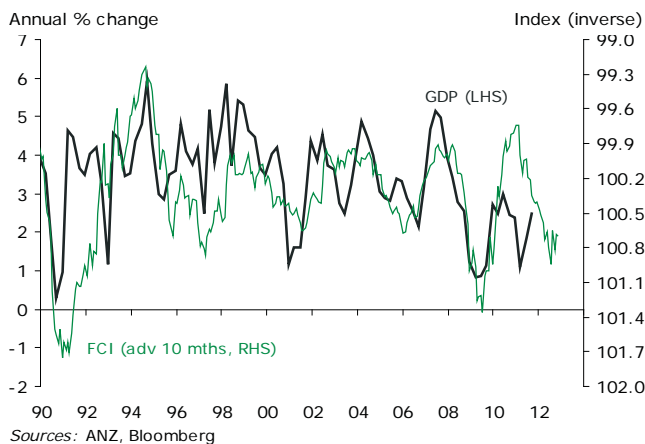
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China GDP vs Financial Conditions Index



- **Our FCIs also point to some moderation in Australia.**

AU GDP vs Financial Conditions Index



We admit that indicators such as financial conditions have limitations. Our FCIs are simple, high-level, and do not capture all of the many influences on growth, but then again, what approach could, especially when confidence and risk appetite are such key drivers, and we are in the midst of a once in a generation structural realignment! **Our FCI measures should be interpreted as an indicator as to the direction for base momentum within an economy, as opposed to the general rate of growth itself.**

The messages across our financial conditions measures are simple.

- **Regions face divergent prospects.**
- **Diverging prospects means more uncertainty.**
- **Beware nations that can't achieve 2 percent growth; a debt spiral may beckon.** Debt and

deleveraging will be a significant determinant of growth prospects. But you need sufficient growth (the denominator in debt/GDP) to keep the debt burden in check. Countries where prospects for nominal GDP are below borrowing costs are in a pickle.

THE UPSHOT

So what do all these themes in aggregate mean for the New Zealand economy and property market in particular?

- A bumpy year, particularly for the domestic economy and housing market (Themes 1, 2, 3, 4). We've pencilled in 2 percent growth for the real economy and a subdued housing market price-wise. It's enough to get by and help slowly push the unemployment rate lower. This also means another year where the housing market moves sideways in aggregate, albeit with continuing regional differences (see below).
- New Zealand will still perform better than most across the OECD (Themes 2, 3 and 5). Two percent growth is not stellar but relative to others New Zealand will look solid.
- There is still more downside risk than up (Themes 3 and 6). Where the world goes, NZ follows. We're in the hands of the European politicians.
- Fiscal policy (number 2 The Terrace) to supercede monetary policy (number 1 The Terrace) in importance (Themes 2, 3 and 5). We can remain masters of our own destiny to a degree. The NZ Treasury need to take a stronger role in the leadership space. Watch for more structural reform aimed at rebalancing the economy. In the housing area this could include more extensive examination of things like construction costs and factors influencing section prices.
- A lack of clear trends across financial market variables (Themes 2, 4 and 7).
- Interest rates to remain lower for longer (Themes 1, 3 and 4).
- Regional housing market divergences to mirror divergent themes and economic tensions (Themes 1, 2, 3, 4 and 5). Auckland has an intra-regional head off steam but also faces more deleveraging and affordability headwinds. A better rural cheque-book bodes well for rural regions but these are also low population growth areas. Wellington property faces a fiscal discipline headwind.

KEY FORECASTS

Weekly mortgage repayments table (based on 25-year term)

Mortgage Size (\$'000)	Mortgage Rate (%)														
	5.00	5.25	5.50	5.75	6.00	6.25	6.50	6.75	7.00	7.25	7.50	7.75	8.00	8.25	
200	270	276	283	290	297	304	311	319	326	333	341	348	356	364	
250	337	345	354	363	371	380	389	398	407	417	426	435	445	455	
300	404	415	425	435	446	456	467	478	489	500	511	522	534	545	
350	472	484	496	508	520	532	545	558	570	583	596	610	623	636	
400	539	553	566	580	594	608	623	637	652	667	682	697	712	727	
450	607	622	637	653	669	684	701	717	733	750	767	784	801	818	
500	674	691	708	725	743	761	778	797	815	833	852	871	890	909	
550	741	760	779	798	817	837	856	876	896	917	937	958	979	1,000	
600	809	829	850	870	891	913	934	956	978	1,000	1,022	1,045	1,068	1,091	
650	876	898	920	943	966	989	1,012	1,036	1,059	1,083	1,108	1,132	1,157	1,182	
700	944	967	991	1,015	1,040	1,065	1,090	1,115	1,141	1,167	1,193	1,219	1,246	1,273	
750	1,011	1,036	1,062	1,088	1,114	1,141	1,168	1,195	1,222	1,250	1,278	1,306	1,335	1,364	
800	1,078	1,105	1,133	1,160	1,188	1,217	1,246	1,274	1,304	1,333	1,363	1,393	1,424	1,454	
850	1,146	1,174	1,204	1,233	1,263	1,293	1,323	1,354	1,385	1,417	1,448	1,480	1,513	1,545	
900	1,213	1,244	1,274	1,306	1,337	1,369	1,401	1,434	1,467	1,500	1,534	1,567	1,602	1,636	
950	1,281	1,313	1,345	1,378	1,411	1,445	1,479	1,513	1,548	1,583	1,619	1,655	1,691	1,727	
1000	1,348	1,382	1,416	1,451	1,486	1,521	1,557	1,593	1,630	1,667	1,704	1,742	1,780	1,818	

Housing market indicators for December 2011 (based on REINZ data)

	House prices (ann % change)	3mth % change	No of sales (s.a.)	Mthly % change	Avg days to sell (s.a.)	Comment
Northland	-0.9	0.3	121	(-2%)	61	Sale price slips 19 percent below the all time high
Auckland	6.7	0.2	2,137	(+4%)	35	The joint strongest annual growth in sale prices
Waikato/BOP/Gisborne	-3.0	-0.1	799	(+8%)	54	Sale numbers lift to a two-year high
Hawke's Bay	-5.1	1.6	167	(-7%)	63	Noteworthy deterioration across all of the indicators
Taranaki	0.6	1.7	301	(+21%)	44	Sale number hit highest level since August 2009
Manawatu/Whanganui	6.1	6.0	174	(+9%)	47	The median sale price hit an 18-month high
Wellington	-3.3	2.6	592	(+1%)	38	Prices at similar level to where they started the year
Nelson/Marlborough	1.5	5.1	214	(-2%)	42	Loss of momentum over final month of the year
Canterbury/Westland	6.7	1.6	818	(+0%)	34	The joint strongest annual growth in sale prices
Central Otago Lakes	5.2	-1.2	85	(+5%)	75	Fickle prices lift in month but weaker over 3 month avg
Otago	4.7	1.2	232	(+9%)	37	Time to sell remains below long-run average of 40 days
Southland	6.0	13.5	133	(+2%)	35	Distinct lift in prices over last three months
NEW ZEALAND	1.0	1.4	5,700	(+5%)	39	NZ house sales continued to rebound in December

Key forecasts

Economic indicators	Actual			Forecast						
	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13
GDP (Ann Avg % Chg)	1.1	1.3	1.6(f)	1.7	2.0	2.0	2.1	2.4	2.7	3.1
CPI Inflation (%)	5.3	4.6	1.8	1.7	1.5	1.9	2.6	2.7	2.6	2.7
Unemployment Rate (%)	6.5	6.6	6.5(f)	6.5	6.2	6.1	6.1	6.1	6.1	6.1
Interest rates	Actual			Forecast (end month)						
	Nov-11	Dec-11	Latest	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13
Official Cash Rate	2.50	2.50	2.50	2.50	2.50	2.50	2.75	3.25	3.50	3.75
90-Day Bank Bill Rate	2.7	2.7	2.8	2.7	2.8	2.8	3.2	3.7	3.8	4.2
Floating Mortgage Rate	6.0	6.0	6.0	6.0	6.0	6.0	6.2	6.6	6.7	6.9
1-Yr Fixed Mortgage Rate	5.8	5.8	5.8	5.8	5.9	5.9	6.2	6.5	6.6	7.0
2-Yr Fixed Mortgage Rate	6.0	6.0	6.0	6.0	6.1	6.1	6.5	6.6	6.7	7.0
5-Yr Fixed Mortgage Rate	7.2	7.2	7.2	7.3	7.2	7.2	7.2	7.1	7.0	7.2

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