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THE BERL FORECASTS PANEL

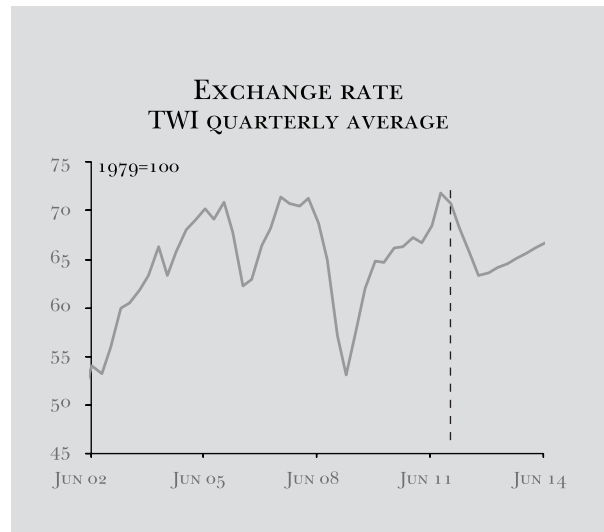
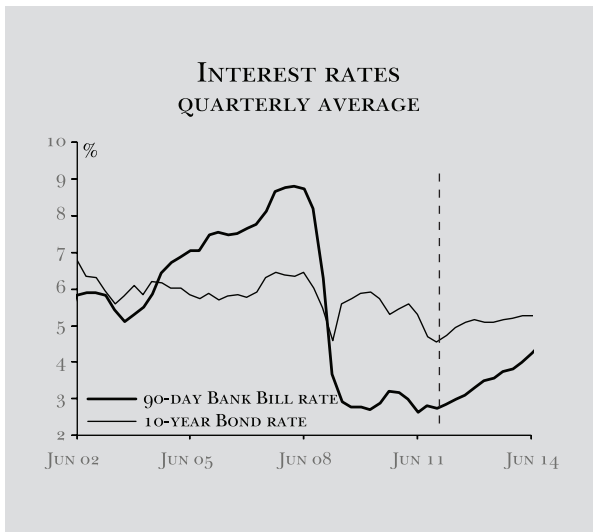
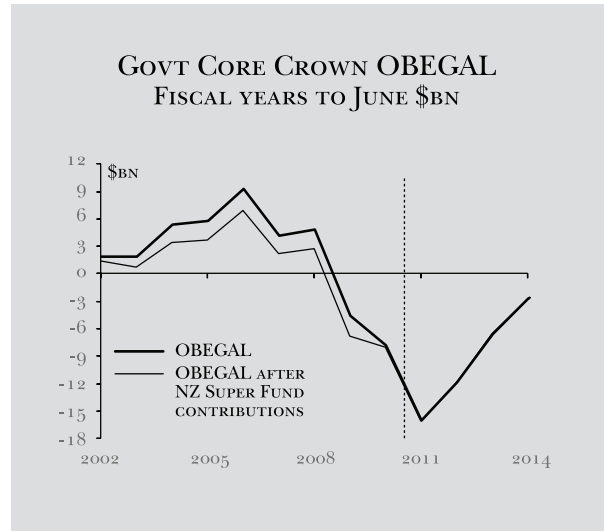
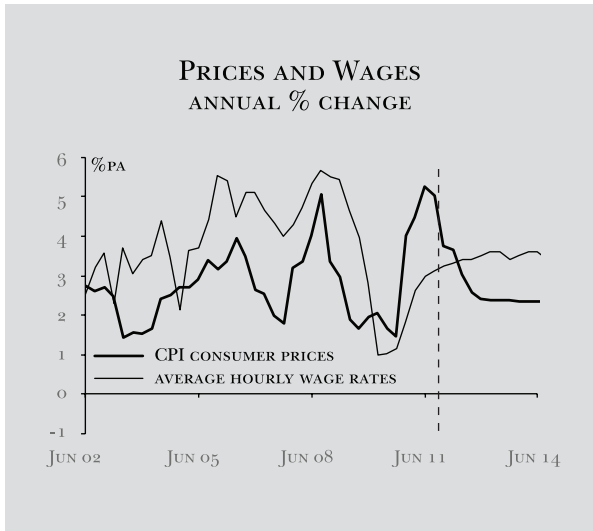
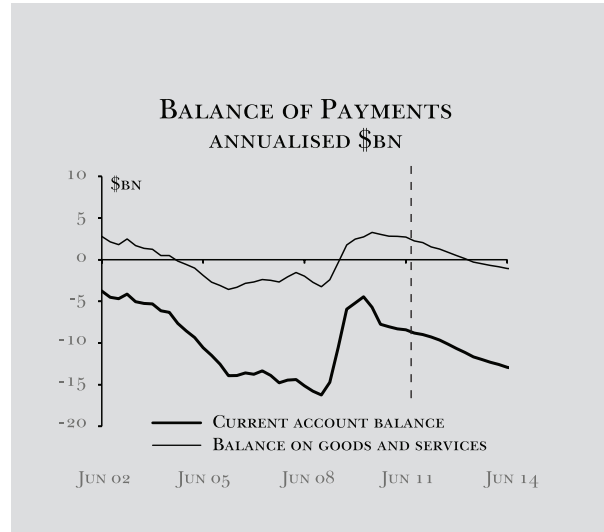
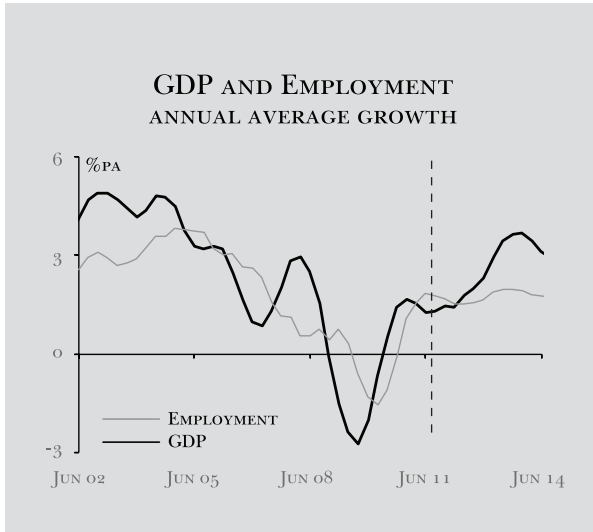
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FORECAST SUMMARY



Detailed data tables (annual and quarterly figures) for the numbers and charts in this document are available to subscribers on request.

THE PICTURE

- Uncertainty is the main word to litter this forecast.
- Many of New Zealand's economic indicators have recovered ground lost during the Global Financial Crisis. Employment and export revenue are among the indicators that underpin the story that the New Zealand economy has weathered the recession.
- In addition, some short-term indicators have also turned positive and so reinforce this story. For example, growth in business investment and the associated capital imports have recently turned positive, as has growth in non-residential building consents, and guest night numbers. Retail spending is also looking promising given data on the value of electronic transactions, and surveyed confidence figures continue to report a positive mood.
- However, many of the core activity indicators remain well below pre-GFC levels and belie the argument that the New Zealand economy has weathered the recession. In particular, the overall GDP measure of activity is still below that in December 2007. Further, business investment and residential construction remain well below that of three years earlier, while output from the manufacturing sector has sunk to be below that recorded in 2004.
- Looking ahead, global uncertainty arising from potential sovereign debt default in Europe, and a sluggish US economy, continue to impact through volatile financial and currency markets. This uncertainty will remain a feature of the economic environment for some time to come as a combination of economic and political factors suggest there is no quick fix readily available.
- Assuming that global factors do not deteriorate markedly, we see modest growth immediately ahead for the New Zealand economy. An acceleration in growth is expected as re-building activity in Christchurch gathers momentum in the latter half of calendar 2012.
- Export revenue continues to surge in line with ongoing favourable prices, but significant volume or activity growth is muted given reduced capacity in meat and wood processing. Business investment continues to recover lost ground, taking advantage of the relative cheapness of imported machinery and equipment. The combination of these effects sees little sustained improvement in the current account balance situation, with the external deficit settling near 5.5% of GDP towards the end of the forecast horizon.
- Increasingly loud calls for increases in official interest rates are likely as inflation pressures from abroad accumulate. However, ongoing uncertainty from the global financial situation should stay the hand of the Reserve Bank until well into 2012. Nevertheless, tighter finance markets abroad could well flow through to higher domestic interest rates, irrespective of official rate movements.
- A 'game-changing' event abroad in the form of a sovereign debt default, disintegration of the Euro area, or generalised financial upheaval, would lead to a significantly worse outlook for the New Zealand economy.

KEY INDICATORS: FORECAST SUMMARY AND COMPARISONS						
	2010	2011	2012	2013	2014	2015
Real GDP						
March year average % change						
BERL	-0.7	1.5	1.4	3.0	3.5	2.8
Reserve Bank	-0.7	1.5	2.8	3.1	3	
Treasury	-0.7	1.0	1.8	4.0	3.0	2.7
Unemployment rate						
March year %						
BERL	6.0	6.5	6.5	5.9	6.0	5.8
Reserve Bank	6.1	6.5	5.7	5.2	4.8	
Treasury	6	6.8	5.7	4.8	4.8	4.6
Current Account Balance						
March year % of GDP						
BERL	-2.4	-4.2	-4.5	-5.1	-5.4	-5.5
Reserve Bank	-2.4	-4.2	-3.5	-4.6	-5.4	
Treasury	-2.4	0.5	-4.1	-5.2	-6.8	-6.9
Export volume growth						
March year average % change						
BERL	4.7	1.8	2.0	2.2	3.3	3.5
Reserve Bank	4.7	1.8	3.9	1.6	2.6	
Treasury	4.6	1.9	3	2.9	2.2	2.1
Reserve Bank : Monetary Policy Statement, September 2011						
Treasury : Budget Economic and Fiscal Update, May 2011						

COMMENTARY compiled by Ganesh Nana

SELECTED MONTHLY INDICATORS

3 MONTH TOTAL % CHANGE ON SAME PERIOD PREVIOUS YEAR

Month	Car registrations	Electronic transaction values (RTS core)	Electronic transaction number (RTS core)	Capital imports (plant)	Visitor arrivals	Mach & eqpmt expts	NBNZ Survey business confidence#	Guest nights	New dwellg permits	Non-resid bidg permits FLOOR AREA	Credit card balances outstanding
Feb 10	14.3	2.8	5.6	-25.9	5.2	-1.7	50.1	3.5	25.8	-28.3	0.0
Mar 10	25.8	3.1	6.1	-20.4	5.6	-1.7	42.5	2.9	32.3	-19.0	0.8
Apr 10	34.3	3.1	6.4	-14.5	3.0	-3.5	49.5	1.6	35.4	-18.7	1.4
May 10	34.0	2.6	5.5	-12.7	1.5	1.4	48.2	-0.3	27.7	-19.3	1.8
Jun 10	35.4	2.3	5.3	-12.1	0.5	9.9	40.2	0.2	23.5	-28.6	2.3
Jul 10	27.0	3.1	6.0	-6.5	3.7	15.0	27.9	-0.1	18.4	-26.2	2.5
Aug 10	23.3	3.3	6.1	2.4	5.2	18.4	16.4	2.0	16.1	-6.8	3.0
Sep 10	18.1	3.7	5.6	18.2	3.0	13.4	13.5	-0.4	3.3	17.3	2.9
Oct 10	15.7	3.6	5.5	17.9	1.2	9.9	23.7	-1.0	-10.7	19.9	3.2
Nov 10	17.2	5.0	6.9	18.6	1.0	8.9	33.2	-0.2	-11.5	39.7	3.5
Dec 10	12.9	4.6	6.9	15.1	1.1	3.6	29.5	-0.8	-16.1	9.4	3.4
Jan 11	11.9	4.9	6.7	17.5	2.4	0.0	na	-1.2	-14.5	11.5	3.3
Feb 11	5.4	4.6	5.9	17.6	1.6	-4.0	34.5	-2.1	-24.8	-8.1	3.1
Mar 11	2.8	5.2	6.0	14.9	-2.4	-2.3	-8.7	-3.0	-25.3	-7.0	2.5
Apr 11	-2.9	6.4	6.4	13.8	-2.5	7.2	14.2	-3.6	-30.1	-13.9	2.3
May 11	-4.9	6.6	6.4	15.6	-3.2	9.0	38.3	-3.3	-26.0	0.9	2.2
Jun 11	-7.9	7.7	7.1	11.2	-1.1	7.8	46.5	-1.3	-26.0	14.8	2.3
Jul 11	-6.5	7.1	6.5	11.5	-4.7	4.4	47.6	1.1	-20.8	24.3	2.4
Aug 11	-4.7						34.4				

Statistics NZ; NZTA; NBNZ # net expecting improvement

Recent commentary suggests there is a general consensus that the New Zealand economy is doing fine, but it is the global situation that is the cause of potential grief. Or, in the quaint vernacular of financial market commentators, the source of significant downside risk to growth prospects for the New Zealand economy.

Removing the flowery language, it is true that some indicators suggest the New Zealand economy performed well and 'recovered' from the effects of the financial crisis. The primary indicators that lead to this conclusion are that employment numbers and export revenue have recovered, and are now back above their pre-crisis levels. In particular, job numbers for the year to June averaged 2.20m, above the 2.18m averaged in the year to June 2008. Merchandise export revenue totalled \$43.9bn for the year to June, well up on the \$40.8bn recorded in calendar 2008, having slumped to \$37.4bn in the following 2009 calendar year.

In addition, some short-term indicators also suggest the robustness of recent activity. For example, electronic transaction data indicates spending in core sectors of the retail industry is growing considerably. The three months to July

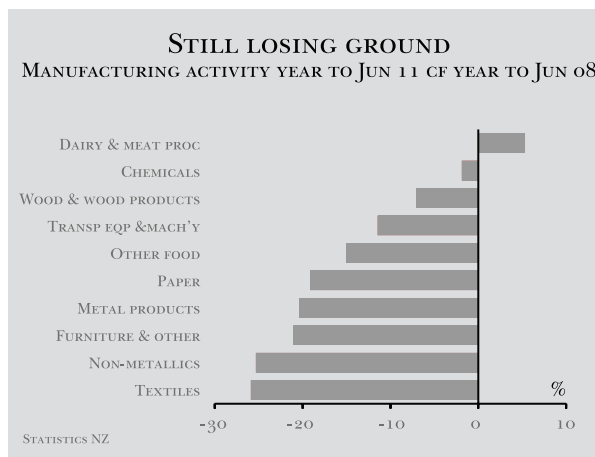
were up 7.1% on year-earlier levels. Similarly, growth in imports of capital equipment suggests business investment spending is also looking promising, as is the recovery in non-residential building consents. These are all consistent with the positive figures for surveyed business confidence.

Also promising is what appears to be a recovery in guest nights; although, this is inconclusive as the figure hides a large decline in international guest nights (latest three months down 7.7% on year-earlier levels). Similarly, the modest growth rates being recorded in outstanding credit card balances appear to signal behavioural changes, with ongoing reductions in the accumulation of debt being recorded.

But, there are many 'buts' in this argument – and that is before we even get to talking about the global situation. It is clear that many indicators – and their related sectors – are still in 'catch up' mode. That is, they are yet to claw back the lost ground incurred over the GFC-related recession. For example, real business investment is still some 11% below that in March 2008, while the overall GDP measure of production activity only just

reached \$34.2bn (in 1996\$ terms), still below the \$34.4bn recorded in the December 2007 quarter.

More worrisome is the continuing decline in residential house building, with latest data putting activity at an annual rate of 13,200 – well below the 25,600 recorded in calendar 2007. And despite the recent upturn in non-residential building consents, the 588m2 total for the three months to July remains significantly less than the 946m2 approved in the last three months of 2007. In addition, meat export revenue remains below earlier peaks, as are international visitor numbers and spending totals.



However, by far the most convincing rejoinder to those that believe the recession is behind us is the performance of the manufacturing sector. Not only is total output in the manufacturing sector down 9% on that of three years ago, but every sub-sector of the industry except dairy & meat processing is also noticeably operating below the level of three years ago. Indeed, there is scant evidence of a recovery underway, with eight of the 10 sub-sectors recording further declines in the latest year to June 2011. Only metal products, and transport, equipment & machinery reported some recovery over the latest year.

The picture is even more sobering if one encompasses a longer time frame, as total manufacturing output volumes measured currently at \$86.9bn (in September 2010 \$ terms) is well below the \$95.7bn registered in calendar 2004. That means this sector has been going backwards (i.e. in recession) for six and a half years. Sobering indeed.

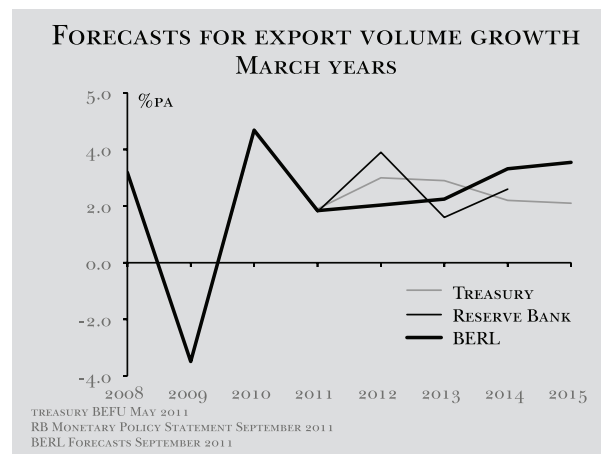
To add to this despair, New Zealand's policy officials are of the opinion that they have to look to the global economic situation for reasons to

justify postponing scheduled increases in interest rates. Nevertheless, it seems to suit some New Zealanders to continue to believe that our economic concerns are primarily the result of forces beyond our shores. Such a view, however, is consistent with the many who are convinced that there is little we can (or should) do about our predicament.

Meanwhile, the global currency financial markets have been in turmoil, with only glacier-like progress being made towards the required reforms and adjustments. Recent volatility in the world's exchange and sharemarkets reflect the underlying uncertainty. What is incredibly uncertain is the likely end-game – possibilities range from an orderly writedown of debts, coupled with stringent rules enforced on debtor nations, to sovereign debt default causing serious dislocation in financial markets and an almost inevitable and prolonged period of economic recession. In between lie the possibilities of expulsions of some debtor nations from the Euro zone; some creditor nations leaving the Euro and reverting to their local currencies; or more negotiated bailouts while the contagion seeps its way across other parts of Europe. And while the economic adjustment will be messy whichever end-game is played out, the political consequences of the adjustment process are equally uncertain.

Unfortunately, this uncertainty is likely to remain until European leaders decide to what lengths they are prepared to go to in order to protect their vision of a single European economy, united by a common currency.

For New Zealand, this uncertainty is reflected in an overvalued currency, as investors are attracted by higher interest rates – compared to those elsewhere – assisted by buoyant commodity



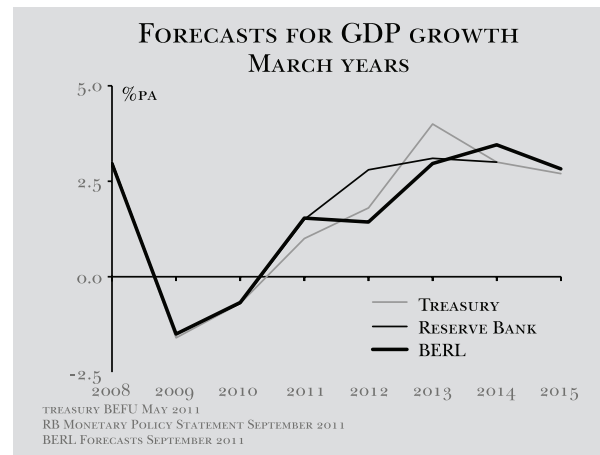
prices. This overvaluation will be tempered by intermittent volatility, as investors' appetite for risk waxes and wanes in response to the latest news (or rumour) from global markets.

Consequently, the outlook for New Zealand's economic prospects remain modest to moderate. The widely reported export-led recovery is lopsided, with long-term reductions in the processing capacities of the meat and wood sectors meaning fewer employment opportunities and an increasing reliance on the maintenance of high raw commodity prices. Indeed, overall volumes for the year to March 2011 recorded growth of only 1.8%. The Reserve Bank expects this to rebound to 3.9% in the current March 2012 year, before tapering off to 1.6% in the following year. We don't expect such a surge in volumes (although revenue is set to remain buoyant).

Without real export growth, the main component of growth in activity over the short term remains the Christchurch re-build. However, continued uncertainty as to the nature and timing of this re-build does provide little confidence that overall activity will continue to recover any more than at modest rates. The recovery in non-residential investment, a combination of private sector business investment as well as Christchurch related construction activity, is set to continue – in part riding on the back of the relative cheapness of imported machinery and equipment. Consumer confidence is reportedly sound, although spending remains subdued. While we expect a one-off bounce from Rugby World Cup spending, underlying uncertainties and volatility from abroad will ensure consumers remain tentative and subdued.

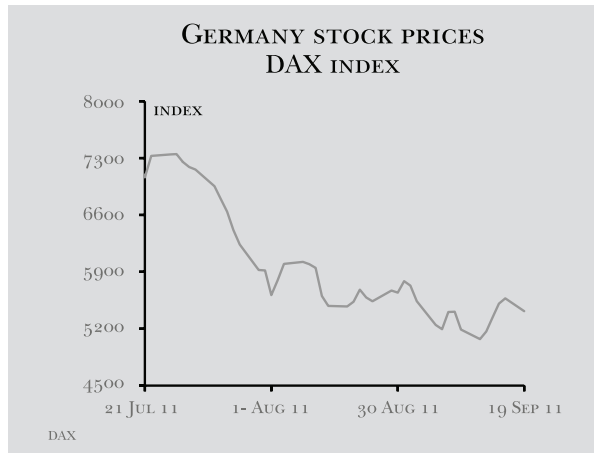
And while employment figures have recovered quickly in the post-recession period, we expect only modest job growth over the remainder of the forecast horizon. This prospect is reinforced by the likelihood of further reductions in public sector employment, along with ongoing contraction in the building construction sector (despite the prospective Christchurch rebuild).

Our forecasts are founded on the assumption that the global economy continues to operate in a situation of heightened uncertainty, but there is no 'game changer' in Europe that leads to the disintegration of the Euro area and/or significant further upheaval within its member states. If either of these were to eventuate, then we would undoubtedly be led to downgrade New Zealand's economic prospects from those stated here.



FEATURE – THE MESS THAT IS EUROPE

The latest turmoil on global currency and stock markets centres on the future of the European Union. It is no exaggeration to say that there are growing concerns as to the long-term sustainability of the Euro as the common currency for 17 of the 27 member states of the European Union.



Despite the arguably strong economic case for a common trading area with similar tax, policy and standards protocols, the political case for union remains strained. This strain shows through at times of economic tension, and clearly underlies the muddled approach of the authorities to the risks of sovereign default.

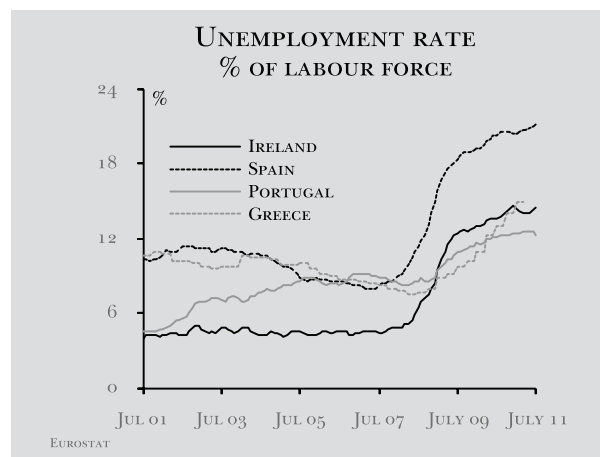
In a nutshell, if an economic system wishes to retain a single currency, then monetary and exchange rate policies within the area must be sufficiently harmonised for imbalances not to emerge. Where such imbalances are inevitable, then forces other than exchange rates and monetary policy must be available to reduce the imbalances.

In both the United States and the European Union, sluggish domestic recoveries are exacerbating the effects of the underlying issue of unsustainable fiscal deficits. The largest difference between these two is that while the US has one federal government deciding fiscal tax and expenditure policies, the EU has many. The significance of this difference is increased when 17 of the 27 members of the EU share one currency.

For the EU there are essentially two options facing the 17 members who wish to sustain their allegiance to the one currency. Either they align their fiscal policies, forcing member countries to adhere to previously agreed rules to keep fiscal deficits within a certain proportion of GDP, or the surplus members agree to continue to transfer funds and resources (i.e. lend/subsidise) to the

deficit members. These are the options in the absence of an exchange rate mechanism to rectify such imbalances. Unfortunately neither of these options are palatable in an economic sense or in the political dimension.

In the former option, forcing an adherence to fiscal rules (euphemistically labelled 'austerity' measures) is likely to lead to significant unemployment and associated social hardship in some member countries, if not unrest. Further, the latter option is now becoming increasingly politically charged with taxpayers in the member surplus countries no longer keen to continue funding the deficit countries. Of course, the blame for the flouting of the rules in the early half of the previous decade should not be laid all on the deficit countries. The surplus countries themselves were complicit in allowing such unsustainable borrowing to occur.



Attempts now continue to focus on avoiding default. If successful, this will then set the scene for an (hopefully) orderly writedown of the assets held by the surplus countries (in their banks and financial institutions). This reinforces the point that it is not just in the debtor nations that adjustments are required.

Recall, if you owe a couple of million dollars to the bank, then it is you who is in trouble. But, if you owe the bank a couple of billion dollars, then it is the bank who is also likely to be quite worried.

Addressing these imbalances will no doubt lead to significant hardship for many people in these countries. Consequently, the governments of these areas are unable (or unwilling) to make sufficient adjustments to convince finance markets that their imbalances are under control. Hence there are increasing political tensions as some areas grow uncomfortable with the level of

assistance that others require – especially if those other areas are perceived as not abiding by earlier agreed rules.

In such a situation, other countries within the common currency area are forced to 'step-in'; that is, if they wish to protect the sustainability of their currency. This is relatively straight forward in the case where there is one federal government. However, the European Union clearly does not fit this case.

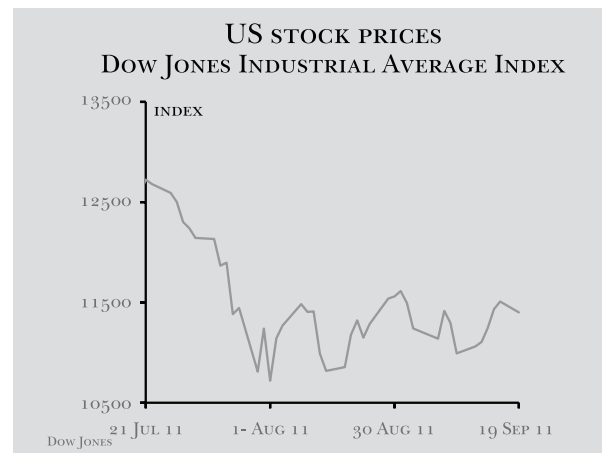
These heightened tensions were reflected recently when Netherlands Prime Minister Rutte called for more powers for the EU to enforce budget rules on member countries. He went so far as to suggest a new EU "Commissioner for Budgetary Discipline" who would have the ultimate sanction and be able to force countries to leave the Euro if they do not submit to the agreed rules. These comments follow calls by French President Sarkozy and German Chancellor Merkel for "true economic governance" across the Euro zone countries. Reading between the lines, some are now asking is a single currency worth it?

In the economic world, this political uncertainty is reflected in volatility. And this volatility is not restricted to Europe. For, if there is one thing that finance and currency markets do not like, it is political uncertainty.

The last couple of months have seen the major stock market indices gyrate daily, as brokers and investors respond to any morsel of information (whether rumour or real) and act in a seemingly knee-jerk manner. This behaviour is typical of an uncertain environment.

Associated with the uncertainty is a move towards assets and investments that are perceived to be relatively 'safe'. Consequently, the price of precious metals has soared, as has the value of the Swiss Franc. The latter has led to Swiss authorities taking action to stem the appreciation in its currency because of its negative impact on Swiss exporters.

With their currency seen to be a 'safe haven', reflected in the unprecedented (and contrary to all economic textbooks) feature of short-term nominal interest rates turning negative, Swiss authorities have been compelled to take action. This has seen a move to put a ceiling on the Swiss Franc in order to protect the competitiveness of their



export sector, with an extraordinary pledge from the Swiss National Bank that it is "... prepared to purchase foreign exchange in unlimited quantities", and will enforce its exchange rate ceiling "...with the utmost determination". It further states that "... doing nothing would almost certainly inflict tremendous long-term damage on our economy. With today's measure, the Swiss National Bank is acting in the interest of the country as a whole."

For New Zealand, our key policy question should not be when to raise interest rates, but why? The appropriateness of an inflation-target foundation to our macro policy framework may have been a no brainer two decades ago following two decades of double-digit annual average rates of inflation. But, in today's world, where concerns over inflation seem minor compared with the finance, monetary, and debt issues that have already been responsible for the Global Financial Crisis.

Yes, the world has changed, and the sooner we realise this the sooner we will be able to make the necessary adjustments.

GLOBAL SITUATION compiled by Jason Leung-Wai, Hugh Dixon and Wilma Molano

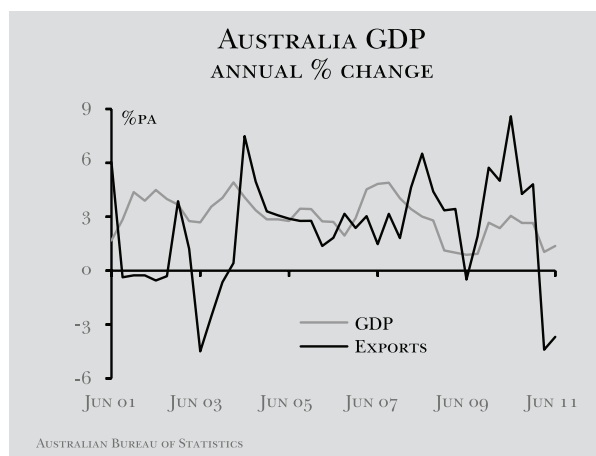
THE WORLD SCENE CONSENSUS FORECASTS

	REAL GDP % CHANGE			CONSUMER PRICES % CHANGE		
	2009	2010	2011	2009	2010	2011
Australia	1.3	3.0	3.4	1.8	3.1	3.0
China	8.7	10.2	9.0	-0.7	3.3	3.5
Hong Kong	-2.8	5.6	4.7	0.6	2.6	3.1
India	7.4	8.3	8.5	12.4	8.6	6.3
Indonesia	4.5	5.9	6.0	4.8	4.7	5.9
Japan	-5.3	3.9	1.4	-1.4	-0.7	0.2
Malaysia	-1.7	6.9	5.2	0.6	2.1	2.6
New Zealand	-1.6	2.8	3.4	2.1	2.9	2.7
Singapore	-1.3	9.1	5.0	0.6	2.8	2.5
South Korea	0.2	5.5	4.3	2.8	2.9	3.2
Taiwan	-1.9	6.5	4.5	-0.9	1.4	1.8
Thailand	-2.2	5.1	4.4	-0.9	3.6	3.1
Asia/Pacific	1.5	6.3	5.2	0.9	2.3	2.5
North America	-2.4	3.3	3.1	-0.2	1.8	1.7
Latin America	-1.9	4.5	3.9	5.5	7.7	7.0
Western Europe	-4.2	1.1	1.5	0.6	1.6	1.5
Eastern Europe	-5.5	3.8	4.1	6.6	6.0	5.6

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AUSTRALIA

The underlying resilience of the Australian economy has been showcased again in the June quarter GDP results. After a 1.2% drop in quarterly GDP growth in the March 2011 quarter, GDP grew 1.2% in the June 2011 quarter. This quarterly increase in economic activity came predominantly from two sources: the manufacturing sector (up 2.8%) and the transport and postal sector (up 4.4%). The drop in GDP in the March 2011 quarter was heavily influenced by the mining sector. This sector was badly affected by adverse weather events at the end of the 2010. Commentators were expecting the mining sector to rebound this quarter, unfortunately the sector experienced a small decline of 0.02%.



The quarterly unemployment rate was 4.9% in the June 2011 quarter, down from the revised figure of 5.0% in the March 2011 quarter. This June quarter figure is also down on the same quarter last year, as the unemployment rate in the June 2010 quarter sat at 5.2%. However, unemployment data for July has the unemployment rate rising in the short run to over 5% again.

Housing consents for the year to July have fallen by 2.1% to 155,000 new consents. This is the first annual monthly decrease in consents since December 2009. Continuing with large item purchases, annual motor vehicle sales of new cars was down 1.9% in July. This is the second month in a row that annual sales have fallen. Lastly, annual retail trade sales figures increased by just 2.4% to the month of July. Retail sales growth has not been this slow since the early 1980s.

These monthly statistics are showing a possible slowdown in demand for goods from Australian consumers, which if it continues over the next quarter could start to impact on the growth of the Australian economy. This will mainly depend on global economic news and decisions which can impact on the confidence of Australian consumers to spend their money.

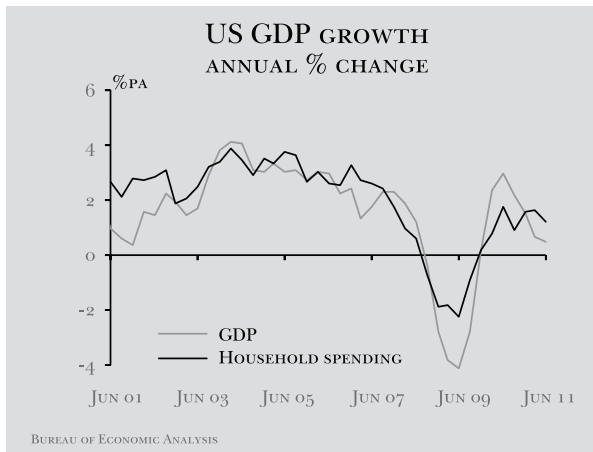
UNITED STATES

Commentary in regards to the US economy is currently focused on whether or not the US will end up in a double-dip recession. David Leonhardt of the New York Times reported on September 7, “[I]f history is a guide, the odds that the American economy is falling into a double-dip recession have risen sharply in recent weeks and may even have reached 50 percent.”

Events in recent months have done much to fuel this debate. The US government avoided, by just a few hours, putting a stop on government expenditure on already incurred obligations when both republican and democrat parties agreed to raise the US debt ceiling. The deal reached will see US\$917 billion cut from federal spending this year. Come November, a super committee of 12 will then decide if US\$1.5 trillion in federal spending cuts will go ahead in 2012.

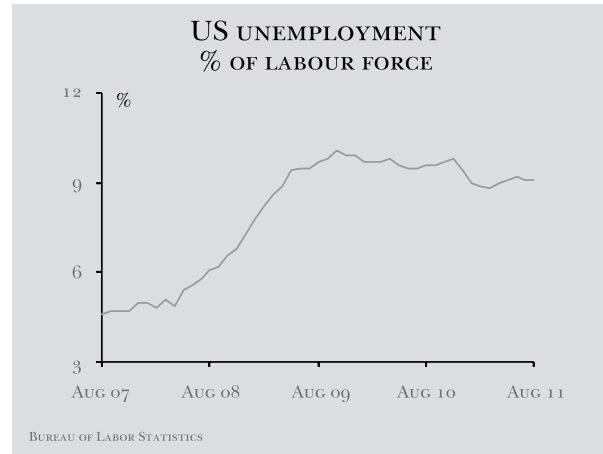
On August 5, one of the three main credit rating agencies, Standard & Poors, downgraded the rating of the US government from AAA to AA+. This downgrade was due to a belief by Standard & Poors that the debt ceiling package did not go far enough in cutting government spending. Standard & Poors wanted at least \$4 trillion in spending cuts. Despite this downgrade US Treasury bills are still seen as one of the safest investments, with yields falling to a low of 2.39%.

The US economy recorded a 0.2% increase in quarterly GDP in the June 2011 quarter. This is only slightly better than the 0.1% growth in the March 2011 quarter. This is a continuation of the low increases in quarterly GDP experienced in the US since the middle of 2010. Annual GDP growth for the June 2011 quarter was just 0.5%; this is lower than the annual growth seen in the previous quarter, when the March 2010 quarter had annual growth of 0.7%.



Unemployment in the US was 9.1% in the June 2011 quarter, up from 8.9 percent in the March 2011 quarter. This slight increase in the unemployment rate brings an end to the recent run in improving unemployment figures, which saw unemployment fall from 10% in December 2009 to 8.9% last quarter.

Monthly unemployment data for July and August 2011 has the unemployment rate stable, at 9.1%. For the month of August, non-farm job growth was 0% for the month, after increases every month since September 2010. This latest monthly unemployment data is concerning given that the US economy needs to create more jobs if it is to avoid a double-dip recession.



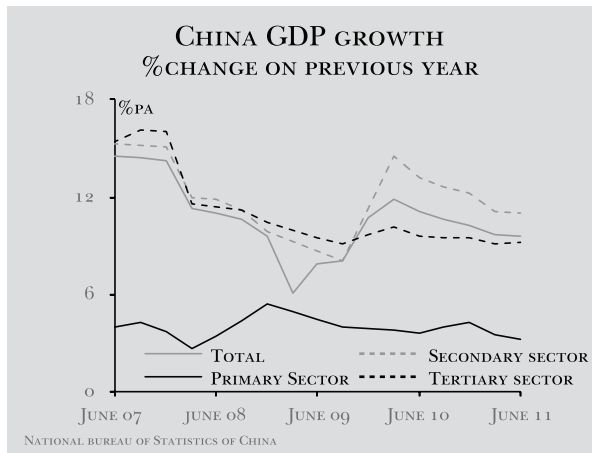
ASIA

CHINA

Export growth continues to be a major component of China’s rapid economic growth. In the June 2011 quarter, GDP in China grew by 9.6% when we compare quarterly figures year-on-year. This growth is being driven by the manufacturing sector. Output from industrial production in the June 2011 quarter was faster than expected, rising 15.1% from a year earlier.

China reported a trade surplus equivalent to US\$31.5bn in July 2011. However, in August the consumer price index was up 6.2% year-on-year, with food prices up 13.4% and non-food prices up 3%. In addition, the prices of services grew by 3.4% compared to year earlier levels.

While China is unlikely to fundamentally change its monetary tightening policy, analysts expect that China may make concessions in regards to loans for the construction of affordable housing and for small and medium enterprises. Experts



say that Beijing may relax its current tightening policy to some extent. This is because of a wave of factory closures in its southern regions, which has become a problem that the Government could not afford to ignore.

Commentators say that through the first half of 2011, the Chinese authorities continued to take steps to prevent overheating and steer the economy towards a soft-landing. Under a mix of monetary and macro-prudential measures, China GDP growth has moderated, but with enough momentum remaining from fiscal support. This will keep the economy under control and balanced in the face of external headwinds from high oil and commodity prices and the impact of the earthquake in Japan. These efforts, however, have failed to prevent inflation from rising well above the authorities' comfort zone. Markets remain on edge about the risks of a more abrupt slowdown, all the more so given heightened risks to the global economy.

JAPAN

GDP in Japan contracted by 1.0% in the June 2011 quarter compared to the same quarter in the previous year. Japan's economy shrank more than initially thought in the April to June period due to weaker-than-expected capital investment in the wake of the March 11 earthquake and tsunami.

Capital investment, the amount companies spend on new assets, slid 0.9% from the previous quarter, down from 0.2% growth in the preliminary data. Private consumption, which makes up some 60% of Japan's GDP, edged down 0.02% which was worse than the expected 0.07% decline. It seems Japanese consumers' wallets are tightly sealed after the disaster for such products as cars.

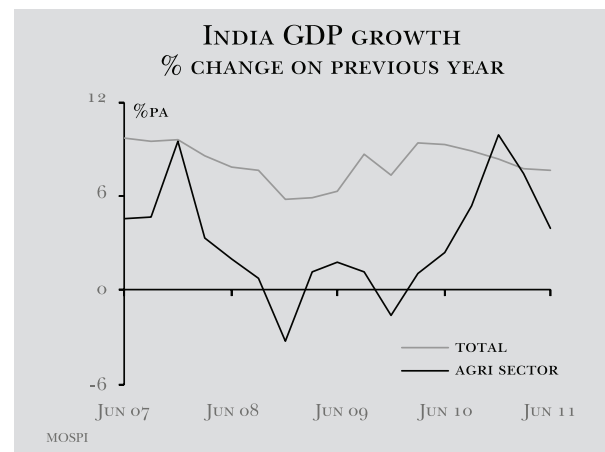
The unemployment rate stood at a worse-than-expected 4.7% in July, up 0.1% on the previous month. This figure excludes the disaster-hit northeast of the country. The number of employed decreased by 200,000 in July 2011 to sit at 59.73 million, a decline of 3% from the previous year.

Japan's exports fell for the fifth straight month in July as the country contends with a strong yen and the ongoing impact of the March earthquake and tsunami. Exports fell 3.3% from a year earlier to ¥5.78tn (US\$75.6bn). Exports are a key driver of the world's third largest economy, and the country is hoping that overseas demand will help it bounce back from the March 11 disaster.

In spite of these economic indicators, commentators believe that the Japanese economy has been recovering from the effects of the earthquake earlier in the year. Industrial production was up in June and manufacturers reported growth in new orders and modest job growth in July along with easing cost inflation. The sustainability of the recovery though may be under question as new export orders fell for the fifth successive month reflecting sluggish overseas demand, especially from China and the US.

INDIA

India's economy grew 7.7% in the three months from April to June, compared with the same period of 2010. It was India's weakest growth for six quarters, but still better than expected. This slowdown is expected to continue as India's central bank continues to raise interest rates to control inflation. The Reserve Bank of India (RBI) has raised interest rates 11 times since March 2010. Inflation in July was 9.22%, which was well above the RBI's target rate of 4% to 4.5%. The sector breakdown showed that the construction sector had been one of the worst-performing parts



of the economy. Construction grew at an annual rate of 1.2% in the second quarter, down from 8.2% in the previous quarter, as rising interest rates and delays in planning approvals held up building projects. The manufacturing sector grew 7.2%, an improvement from the previous quarter, but well below the 10.6% in the second quarter of 2010.

Past evidence indicates that the Indian economy, largely domestically driven, will remain generally unaffected by another global crisis. The RBI maintains the belief that the Indian economy, although not insulated, will weather any potential turmoil. Policy makers are confident too that the latest debt-crisis scare will not affect the Indian growth pattern, and continue to maintain their current GDP forecast of 8.0% for the current fiscal year.

The global release of the Trade and Development Report 2011 supports this positive stance. The United Nations Conference on Trade and Development (UNCTAD) said the Indian economy will grow by 8.1% in 2011, compared to 8.6% in 2010. This growth is despite a slowdown in developed nations and many other countries. Further, the report states that in South Asia, India continues to pursue rapid economic growth (close to 8%), based mainly on strong domestic consumption and investment, but also on the positive contribution of net exports.

HONG KONG

Hong Kong's economy expanded at a slower pace in the second quarter of 2011. GDP rose 5.1% year-on-year in the second quarter compared to economist expectations that economic activity would rise 6%.

Exports 'decelerated noticeably' in the second quarter of 2011 (0.2% y-o-y), recording almost no growth compared with a year earlier. This reflects slower demand in key overseas markets and production disruptions from the Japanese tsunami.

Despite this slower pace, the statistical department in Hong Kong has maintained their growth forecast for 2011 at 5-6%. Their prediction for core inflation was left unchanged at 5.5%, while the outlook for headline inflation was untouched at 5.4%.

EUROPE

Greece and Italy continue to dog Europe and it could be argued that the Euro zone is in crisis. Their inability to push through tougher budget measures, combined with Germany's hardening stance against providing more support, is resulting in a debt crisis, with investors moving cash to less risky assets. This has led the Swiss National Bank to put an exchange rate cap on its currency, which being seen as a safe haven, has appreciated by a third against the Euro.



The repercussions are global; and there is a chance that it could escalate into another global recession with the S&P 500 down almost 15% from its 2011 high due to the Euro zone crisis.

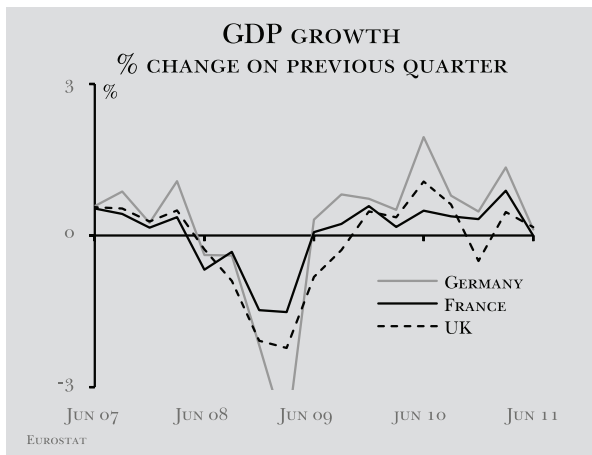
Unemployment in the Euro zone has remained relatively steady at around 9.4%. In Germany, unemployment has been falling steadily, and is currently at 6.2%. At the other end of the spectrum, Spain has an unemployment rate of over 20%, and Ireland has an unemployment rate of 14.1%.

Annual GDP was up 1.7% in the June quarter 2011. Looking at the major players, GDP growth was 2.8% in Germany, 1.6% in France, and 0.8% in Italy.

Inflation in the EU area was down to 2.9% in the year to July 2011, from 3.1% in the year to June 2011. The lowest 12-month averages up to July 2011 were registered in Ireland (0.3%), Sweden (1.6%), the Czech Republic and the Netherlands (1.9% each), and the highest in Romania (7.6%), Estonia (4.9%) and Greece (4.3%).

UK

The UK economy is performing poorly with high unemployment and inflation, and low growth. The Bank of England cut its estimate for 2011 to 1.4% from 1.75%, with governor Mervyn King saying the outlook for the global economy had "deteriorated". On a positive note, latest quarter growth was higher than in both Germany and France.



The UK economy grew by 0.2% in the second quarter of 2011. This gives GDP growth for the year to June 2011 of just 0.7%. Meanwhile, the number of people unemployed in the UK rose by 38,000 to 2.49 million in the three months to June 2011, taking the jobless rate from 7.7% to 7.9%.

Inflation in July, as measured by the Consumer Prices Index, increased to 4.4% from 4.2% in June. This is more than double the 2% target rate.

Many are blaming the poor performance on the Government's economic strategy, which includes significant public spending cuts. Between December 2010 and March 2011 an extra 104,000 jobs were created in the private sector, taking the total to 23.08 million. Meanwhile, the number of people in public sector employment declined over the same period by 24,000 to 6.16 million. Others are blaming it on the 50% tax rate on high earners. Officials are blaming it on the Euro zone crisis.

LABOUR MARKET CONDITIONS compiled by Kel Sanderson

EMPLOYMENT

When we think of all the reasons to expect uncertainty and negative sentiment in business and consumer outlook, it is quite remarkable that the New Zealand labour market has overcome the contraction from 2008 to 2010 and is quite stable and sound. Despite this, there are still some significant negative factors, such as the drop in employment in the 15 to 19 year old age group; the swing back into net migration outflows after 10 years of mostly-strong net inflows; and the major reduction in employment in the building construction industry, just when we will need these people to tackle the massive Christchurch re-build

The differences we highlighted last quarter between the Household Labour Force Survey (HLFS) and the Quarterly Employment Survey (QES) measures of employment continue. The QES, which omits the self-employed and agriculture sector, is sitting around the margin of error with a 0.4% increase in the year to June 2011. It appears 'corporates' have reduced their employment of part-time staff by 0.6% or about 3,000 people. The HLFS on the other hand includes agriculture and self-employed, and has consistently increased by nearly 2% per annum for the last two years. In the year to June 2011, the HLFS showed that the number employed part-time increased by 3.5% or 17,500 people.

A comparison of the two surveys indicates that people who are having their part-time employment ended by the corporates may remain in part-time employment on a sole-trader basis. This is the sort of behaviour we see when the Government and large business corporates cut back their staff, and a number of people obtain part-time self-employment as consultants, agents for insurance or real estate etc. If the economy does not recover, this group will join the unemployed in some months' time.

The industries that are steadily continuing to increase their employment by a small amount in the corporate and the self-employed areas are the wholesale, storage and transport industry group, education and training, and to a lesser extent health and welfare.

The construction and professional services industries show that corporates have retained or grown staff while the industry as a whole has

lost staff. This implies a major reduction in the self-employed. The corporate section in both industries has grown a little, by 8,000, while employment in the overall industries has reduced by 18,000 people. It would seem that the number of self-employed could possibly have reduced by up to 26,000 people in these two industries. In construction, information coming in indicates that the corporates are cutting their tender prices in an attempt to remain in business and with staff for when the Christchurch re-build finally eventuates. This is hard for the self-employed to counter, as few have access to medium-term finance to bridge this gap.

The processing and manufacturing industry and hospitality has seen changes in the opposite direction. The corporates have been squeezed and reduced employment by 16,000 people, while total industry employment has increased by 12,000 people. This could imply that there are up to 28,000 more people self-employed in these industries than there was 12 months ago. This will no doubt include a lot of the increase in part-timers identified in the overall HLFS data.

Changes in the composition of employment is an important indicator of the direction of future employment forecasts. The large increase in the part-time employed is likely to be partially lost after the Rugby World Cup, and after the coming summer visitor season.

We do not expect the Christchurch re-build to be underway until mid 2012. Consequently we are forecasting a slack labour market for most of the first half of 2012. Thereafter the migration flow should return to positive again. This will apparently be bolstered by Irish tradespeople recruited for Christchurch, to replace the tradespeople emigrating at present.

We are forecasting a fairly lacklustre range of employment increases for the next four years, in the range of 1.6% to 1.9% per annum. This steady growth, balanced with low increases due to low net inward migration, will see the unemployment rate trend down from 6.4% of the labour force in June 2011, to 4.9% in 2015.

UNEMPLOYMENT

While we have forecast the unemployment rate in June of each year to trend down from 6.4% in 2011 to 4.9% in 2015, the rates will be higher in

March quarter 2012. This is partly because of when people leave full-time study to join the labour force; but also in the case of 2012 it is being influenced by the part-time work associated with RWC 2011 and the summer season stripping out of employment. We expect that unemployment could be up to 7% in the March quarter of 2012. As the economy struggles for a slow recovery, unemployment could again be close to 7% in March quarter 2013. Thereafter we expect the rate to sit mostly in the 5% to 6% range, as we have been forecasting for some time.

Even the low forecast at 4.9% of the labour force by June 2015 is still well above the 3.6% rate that we had for much of the time from 2004 to 2007. Therefore the 4.9% rate should not raise concerns of a potential for wage-driven price inflation. (However as we have noted before, we would expect to see both wage and price increases in the construction sector to attract resources and skills for the Christchurch re-build.)

MIGRATION

We have pointed out many times that the direction and level of net migrant flow is a barometer of the attractiveness of New Zealand as a place to live. There also seems to be a close interaction between the flow of migrants and the growth in GDP in the economy. In the past there has been a lag which indicates that increased levels of GDP apparently increased the attractiveness for people to stay, and or to come to New Zealand. This has generated an increased net inflow of migrants

about 18 months later. We could have hoped by now to be emerging with a sound, positive vision for New Zealand's attractiveness for future growth opportunities. Instead we are stuck in the expenditure-cutting mindset.

Auckland, far from showing itself off as a 21st Century global city, showed the world that it may be a great place when you get into the centre, but don't expect 21st Century infrastructure to get you there. Many of the RWC2011 visitors may have been tempted to pocket their return air tickets for use later. Most will probably now say 'We MUST get back there for a holiday when there aren't so many people there, or when they get a Rapid Transit network.'

We expect the net migrant outflow to Australia to increase further from the present 30,000 per year to about 35,000 by 2011 year-end. This is greater than can be balanced by the reasonably solid inflows from Europe, Asia and the Americas. We therefore expect a net outflow of long-term migrants of about 2,000 people for calendar 2011, and forecast that it will stay at about the same level for the year ended June 2012. Thereafter it should firm back to our previous non-visionary forecasts of about 8,000 to 11,000 net inflow from 2013 to 2015.

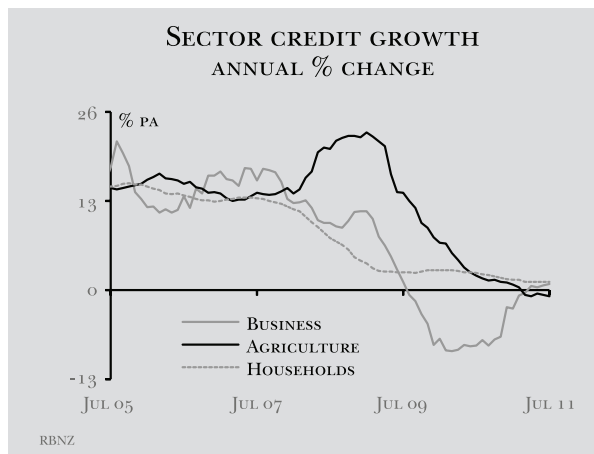
Of course the emergence of a visionary, not to say revolutionary government from the upcoming election could really increase our attractiveness, and our future economy. A Tui vision!

LABOUR MARKET INDICATORS 000S PEOPLE						
June quarter	2010	2011	2012	2013	2014	2015
Full-time employment	1,669	1,694	1,724	1,761	1,793	1,825
Part-time employment	497	514	519	523	527	531
Total employment	2,166	2,208	2,243	2,284	2,320	2,356
FTE employment growth %	0.6	1.7	1.7	2.0	1.7	1.7
Unemployment	155	150	141	130	125	120
Official unemployment rate %	6.7	6.4	5.9	5.4	5.1	4.9
Labour force	2,321	2,358	2,384	2,414	2,445	2,477
Participation rate %	67.8	68.1	68.3	68.4	68.5	68.6
Not in labour force	1,100	1,103	1,108	1,116	1,125	1,136
Working age population	3,421	3,461	3,492	3,530	3,570	3,612
Migration						
Gross migrant inflow	82.3	84.0	80.0	82.0	85.0	85.0
Gross migrant outflow	65.8	80.1	82.0	74.0	74.0	74.0
Net migrant inflow	16.5	3.9	-2.0	8.0	11.0	11.0
Statistics NZ						BERL Forecasts

MONETARY SITUATION compiled by Ganesh Nana

The monetary situation is dominated by the European debacle, as adjustments to debt imbalances lead to considerable uncertainty and, so, volatility in global markets. For New Zealand, this environment has underpinned an overvaluation in the NZ\$ exchange rate, which has been reinforced by ongoing higher commodity prices. Consequently, these effects have deferred increases in the Official Cash Rate, as the Reserve Bank (RB) considers it prudent to await the outcome of the current global turmoil. Nevertheless, the tightening of credit flows abroad – a reflection of the ‘flight to safety’ – is likely to impact on domestic interest rates, irrespective of moves in the OCR.

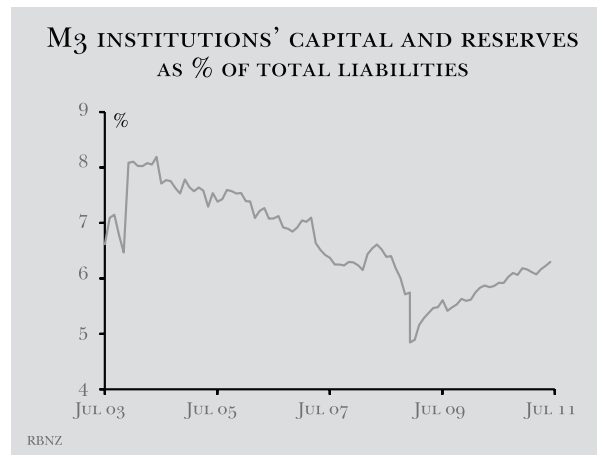
Yes, this is very much a feeling of déjà vu. Remember 2008, when the uncertainty around the value of those ‘sub-prime’ assets on the balance sheets of certain US financial institutions caused a ceasing up financial flows? There is now a risk of a repeat dose, as European financial institutions (primarily German and French) look to assess the real value (i.e. the likelihood of repayment) of loan assets to Greece, Spain, Portugal, Italy and, to a lesser extent, Ireland. Hence, current efforts are focussed on staving off default, which would definitely cause considerable upheaval not only throughout Europe, but globally. If default is avoided, then there will be a focus on the necessary (but hopefully orderly) writedown of the assets – i.e. an agreed repayment plan.



For New Zealand, the post-2008 credit crunch continues. Data for July shows credit available to non-agriculture business was up 0.9% on year earlier, having declined considerably over the previous couple of years. Credit for the agriculture sector has declined by 0.9%, while

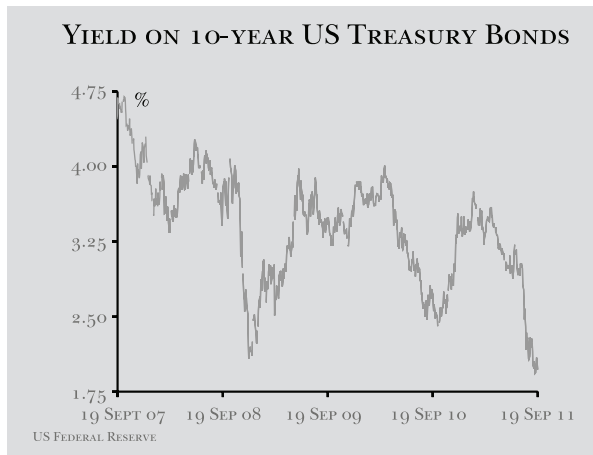
household sector credit has expanded 1.2%. Not only are these rates of growth well below those experienced in earlier times, which were admittedly unsustainable, they continue to be negative in real terms. This reflects, in part, influences from the demand side with the only modest rate of recovery in economic activity.

A companion picture shows the NZ banking sector also continuing to restructure its balance sheets in the wake of the 2008 crisis. This is the influence from the supply side. From a previously-accepted ‘norm’ of about 8%, the sector’s reserve ratio had declined over the pre-crisis years to just below 6% before plummeting to a precarious 4.8% during the height of the crisis. The last three years has seen reserves restored to above 6% – consistent with the much reduced rate of growth in credit. However, this adjustment process remains (arguably) a ‘work in progress’.



A further impact of the recent turmoil from abroad has been the impact on long-term interest rates. Globally these have plummeted, with the yield on 10-year US Treasury Bonds now under 2%, as the rush to ‘safe’ assets has pushed up demand, and so the price, for these investments. Note that this yield is even below the depths reached during the 2008 crisis.

It is ironic, to say the least, that this response occurred simultaneously with a downgrade by S&P in the credit rating of these very same bonds. The conclusion that investors see few alternative options reinforces the uncertainty that surrounds the financial world. In other words, these long-term rates are also a reflection of the reduced returns (and profitability) that investors expect on other assets (and businesses). In turn, this reflects



concerns that the US and European post-2008 recoveries are not only muted but there is, indeed, a possible return to a recessionary environment.

Consequently, New Zealand long-term interest rates have also declined – with the yield on 10-year Government bonds falling to 4.5%, from 5.7% in April.

Many commentators continue to point to New Zealand's OCR as being at 'historically' low levels. A more relevant observation would be that our short-term rates are amongst the highest in the OECD. This factor further reinforces the overvaluation in the NZ\$, as investors look for higher yielding assets that are perceived to be relatively safe.

As a result, much of the inflation-fighting work of monetary policy is being undertaken by the exchange rate through its dampening effect on import prices. This situation is likely to continue over the immediate short term, given the expectation that New Zealand's short-term interest rates will remain higher than those of close competitors. A dampening effect on the NZ\$ will arise if there are significant falls in commodity prices, although we see this as occurring gradually over the forecast horizon as opposed to any sudden or dramatic realignment.

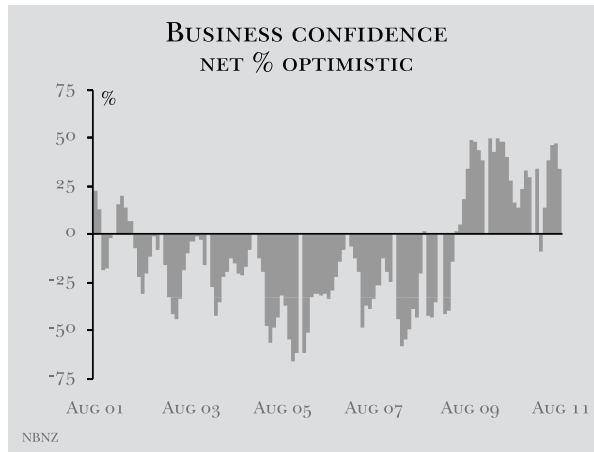
So, New Zealand's monetary conditions are set to remain dominated by an overvalued exchange rate, interest rates that are higher than those abroad, with credit growth relatively subdued as a result of both domestic demand and global supply reasons.

MONETARY PRICES QUARTER AVERAGE					
Quarter	TWI Jun 1979=100	90 day bank bill rate %	10 yr govt stock yield %	1st mortgage housing rate %	Business base lending rate %
Mar 10	65.3	2.73	5.90	5.90	9.89
Jun 10	66.7	2.88	5.73	5.98	9.88
Sep 10	66.9	3.22	5.31	6.31	10.10
Dec 10	67.8	3.18	5.46	6.39	10.24
Mar 11	67.2	3.00	5.58	6.23	10.19
Jun 11	69.1	2.65	5.32	5.90	10.08
Sep 11	72.3	2.80	4.71	5.90	10.02
Dec 11	71.4	2.75	4.55	5.90	10.00
Mar 12	68.8	2.83	4.75	5.98	10.08
Jun 12	66.2	3.00	4.95	6.15	10.25
Sep 12	64.0	3.10	5.08	6.10	10.20
Dec 12	64.2	3.33	5.15	6.33	10.38
Mar 13	64.7	3.50	5.10	6.50	10.55
Jun 13	65.2	3.58	5.08	6.58	10.58
Sep 13	65.7	3.75	5.17	6.75	10.75
Dec 13	66.2	3.83	5.20	6.83	10.83
Mar 14	66.7	4.00	5.27	7.00	11.00
Jun 14	67.3	4.25	5.27	7.25	11.25

RBNZ BERL Forecasts

GDP GROWTH compiled by Amapola Generosa

Our economic performance over the last few quarters has been significantly buoyed by record-low interest rates, favourable terms of trade, and growth in business investments. However, global events such as the worsening European debt situation and weakening Asian demand for our export products, paired with subdued domestic demand, means that the latest official GDP figures suggest, at best, sluggish and fragile economic growth.



GDP in the year to March 2011 was up 1.1%, while quarter-on-quarter growth was a more subdued 0.8%. Although positive, the data suggests that economy activity is far from picking up. Domestic spending is subdued as households and businesses remain cautious and bent on reducing debt.

The annual increase in economic activity came predominantly from the wholesale trade and service utilities sectors. A modest contribution also came from the manufacturing sector. On the other hand, production in the agriculture and construction sectors was down 1.8% and 1.0% respectively.

Looking at the quarterly numbers, the largest increase in value-added activity was from the manufacturing sector. This expansion was due to solid growth from machinery

and equipment (up 15.91%), and the metal manufacturing (up 8.8%) sectors. The wholesale and other service sector also contributed to quarterly growth.

Output in the construction sector failed to pick up, dropping 4.3% between the March 2011 and December 2010 quarters. This is reflected in building consent numbers, where both residential and non-residential building consents continue to fall.

On the expenditure side, growing business confidence has been reflected in business investment. In the year to March 2011, business investment grew 11.5%. However, this optimism in business investment was partly offset by pessimism in housing investment, with a 6% contraction in housing investment.

On a quarterly basis, public and private sector investment, and import spending was down, while domestic consumption was modest. Public sector spending is strong, but private spending remains weak. Household spending was up only 1.5 % in the year to March 2011, and 0.5% over the December 2010 quarter.

Households may have started catching up on deferred purchases, but have remained cautious in spending and using their credit cards. Monthly household credit growth remained flat over the quarter, and households are relying on income growth to support their spending rather than credit card companies. These trends suggest weak domestic demand, contributing further to the economy's sluggish growth.

Overall, weak domestic demand and global uncertainty mires a speedy economic recovery for New Zealand. The Euro crisis and softer global growth is expected to dampen economic growth in the second half of the year. While New Zealand watches and waits for the potential outcomes of the Euro crisis, bringing our economy back onto the fast track to sustainable long-term growth remains a challenge. We expect the Rugby World Cup to boost local spending and, hopefully, offset the impact of uncertainties on the global front over the next two quarters. But, the Rugby World Cup is a one-off boost rather than a sustainable path to recovery.

GDP EXPENDITURE ANNUAL AVERAGE % CHANGE						
Year ended March	2010	2011	2012	2013	2014	2015
Private consumption	0.3	2.0	0.8	1.5	2.1	2.6
Housing investment	-13.2	2.1	-7.8	25.1	32.4	2.3
Other investment	-13.2	11.9	11.0	4.8	2.6	2.6
Govt investment	1.2	-4.4	5.5	17.8	12.5	3.2
Government consumption	0.3	3.2	2.2	1.2	1.2	1.2
Gross National Expenditure GNE	-3.9	4.4	2.4	3.8	4.1	2.5
Exports	4.7	1.8	2.0	2.2	3.3	3.5
Imports	-9.5	10.3	3.7	4.8	5.1	2.4
Gross Domestic Product GDP	1.1	1.7	1.2	3.0	3.5	2.8
Statistics NZ						BERL Forecasts

INFLATION compiled by Jason Leung-Wai

Annual inflation, at 5.3% as measured by the Consumers Price Index, was at its highest level since June 1990 (7.6%). Both peaks, however, included a 2.5% rise in GST.

Excluding GST, the rate, while still facing upward pressure, remains within the RBNZ target range.

Apart from the Consumers Price Index, the Producer Price Index is also suggesting upward price pressures. On the year, output prices have risen 4.5%, while input prices have risen 4.8%. Higher petrol, food, and electricity prices are hitting the general consumer hard and putting pressure on the prices of other goods and services. However, price pressures are generally being kept in check by national and global uncertainty around growth prospects, and an appreciating NZ\$/US\$ that is making imported goods and services cheaper.

We expect New Zealand businesses to remain cautious in setting domestic prices due to uncertainty in the global economy and its flow-through effects on the domestic market. This is reflected in Capital Goods, Producers Prices and Labour Cost indices, which are all relatively restrained. Hence, we forecast that the CPI has hit a high for the year and will return to around 2.5 percent from September 2012.

CONSUMERS PRICE INDEX (CPI)

Consumer prices were up 1.0% on the previous quarter and up 5.3% on the same quarter a year ago. As we continue to stress, the annual rate includes an additional 2.3% in December from the increase in GST.

The figure shows the increase in the CPI as well as the increase less the GST rise. With GST

LABOUR COSTS AND WAGE EARNINGS ANNUAL % CHANGE

Quarter	food	housing & utilities	hhd contents & services	transport	recreation & culture	All groups
Jun 10	-0.7	1.7	-2.0	5.8	-0.8	1.7
Sep 10	0.1	2.4	-2.3	3.7	-1.4	1.5
Dec 10	4.6	3.8	-0.4	6.6	1.1	4.0
Mar 11	4.8	4.0	-1.0	8.2	0.8	4.5
Jun 11	7.0	4.4	0.8	11.0	1.9	5.3
Sep 11	6.5	4.2	1.8	9.0	2.0	5.0
Dec 11	5.5	3.5	1.0	6.8	0.0	3.7
Mar 12	5.0	3.5	3.2	5.5	2.6	3.7
Jun 12	4.5	3.0	2.2	2.8	2.7	3.0
Sep 12	3.0	3.0	2.0	2.4	2.7	2.6
Dec 12	2.3	3.1	2.0	2.0	2.7	2.4
Mar 13	2.0	3.1	2.0	2.0	2.7	2.4

Statistics NZ

BERL Forecasts

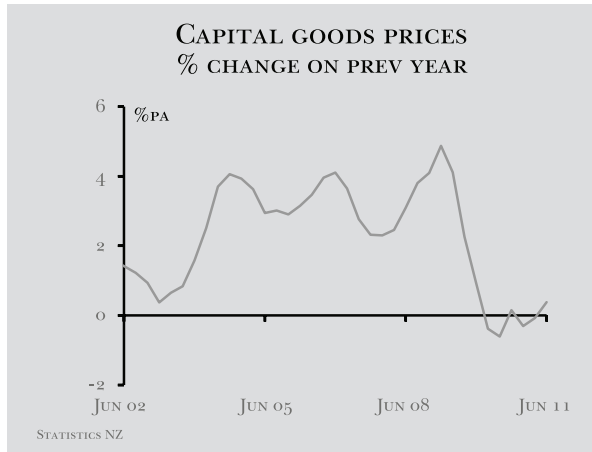
excluded, the rate of inflation remains within the RBNZ Target range.

This is not to say that there isn't upward pressure, because there is. This pressure, however, is being driven by distinct items and events that we do not have much influence over. Transport costs are up 2.7% on the quarter and 11% on the year. This has been driven by petrol prices that are 20% higher than a year earlier. Food prices are up 1.1% on the quarter and up 7.0% on the year. Vegetable prices, affected by weather patterns, are up 19.7% on the year. Higher commodity prices and increased transport costs have seen other food

INFLATION INDICES	QUARTERLY (MONTHLY) MOVEMENT	ANNUAL MOVEMENT
Consumer Price Index Jun 11 quarter	1%; was 0.8%	5.3%; was 4.5%
Capital Goods Price Index Jun 11 quarter	0.5%; was 0.2%	0.4%; was -0.1%
Producer Price Index (outputs) Jun 11 quarter	1.4%; was 1.7%	4.5%; was 4.2%
Producer Price Index (inputs) Jun 11 quarter	20.9%; was 2.2%	4.8%; was 5.3%
Labour Cost Index (Salary & Wage) Jun 11 quarter	0.4%; was 0.5%	1.9%; was 1.69%
Food Price Index (monthly) Jul 11 month	2%; was 1.4%	7.9%; was 7.5%

items increase as well. Housing and household utility prices are up 0.9% on the quarter and 4.4% on the year. Electricity prices are up 7.8%, while new house purchases are 3.4% higher than a year earlier.

Unfortunately these are items that are difficult for the average consumer to bypass or ignore, so everyone is feeling the pinch.



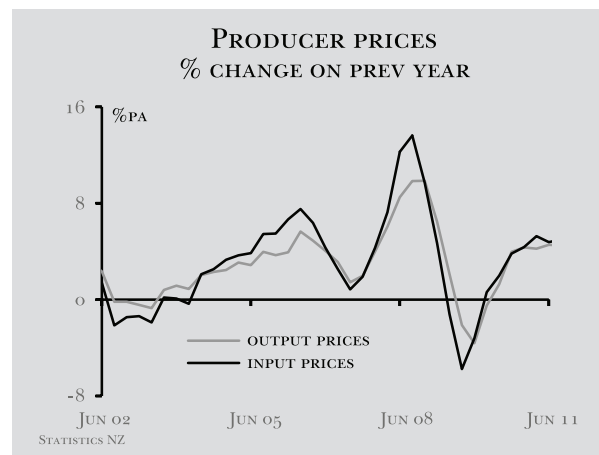
CAPITAL GOODS PRICE INDEX (CGPI)

The CGPI is an overall index of the price level of capital goods purchased by producers of goods and services. The CGPI rose 0.5% in the June 2011 quarter, which takes the annual increase to 0.4%. As shown in the graph, the CGPI has dropped significantly since 2009 and is only now starting to show upward pressure.

The greatest upward pressure comes from the Civil Construction price index, which was up 2.8% on the quarter and 5.3% on the year. This is due to a strong portfolio of infrastructure investment and maintenance, with much of the rise coming from roading related construction and pipelines. Residential buildings prices have also increased by 0.8% on the quarter and 1.1% on the year. Otherwise, the other sub indices have all remained relatively subdued, with the plant, machinery, and equipment index down 0.6% on the quarter and 2.5% on the year.

PRODUCERS PRICE INDEX (PPI)

The PPI measures changes in prices for goods and services produced in New Zealand (known as outputs) and changes in the costs of production, excluding labour and depreciation costs (known as inputs).



OUTPUTS

PPI Outputs are on the rise again, up 1.4% on the June 2011 quarter and 4.5% on the year.

The largest upward contribution on the quarter came from the petroleum and coal product manufacturing index, which was up 10.5% on the quarter and up 21.3% on the year. Dairy product manufacturing prices were up 5.1% on the quarter and up 7.3% on the year, with higher prices for milk powder the greatest influence.

At the other end of the spectrum, prices for telecommunication and internet services decreased by 6.1% on the quarter and 8.3% on the year.

INPUTS

PPI Inputs prices are also beginning to gain momentum, rising 0.9% on the quarter and 4.8% on the year. Manufacturing contributed 41% of the increase in the PPI input prices for the quarter, although dairy product manufacturing fell by 1.8%.

Meat and meat product manufacturing prices rose 5.5% in the June 2011 quarter. The fifth consecutive rise saw an annual price increase of 18.1%. The major influence has been higher prices for livestock – both lamb (up 37.4% on the year) and cattle. Higher wool prices (73.8% on the year) has seen the textile, leather, clothing and footwear manufacturing index rise 8.4% on the quarter and 20.1% on the year.

Petroleum and coal manufacturing prices are up 16.8% on the year, following on from a 26.7% increase in the previous year. Driving prices up has been the higher price of imported crude oil.



LABOUR COST INDEX

Salary and wage rates (including overtime) were up 0.4% on the quarter and 1.9% on the year. Overtime wage rates were up 2.3% on the year. Annually, labour costs have been rising very slowly since the March 2010 quarter and have currently stalled at 1.9% for the second quarter in a row.

Private sector salary and wage rates are rising faster than in the public sector. Private sector rates increased by 2.0% on the year compared to 1.5% for the public sector. Private sector rates have increased faster than the public sector for each of the last four quarters. Before this year, public sector rates had grown faster than private sector rates for nine consecutive quarters.

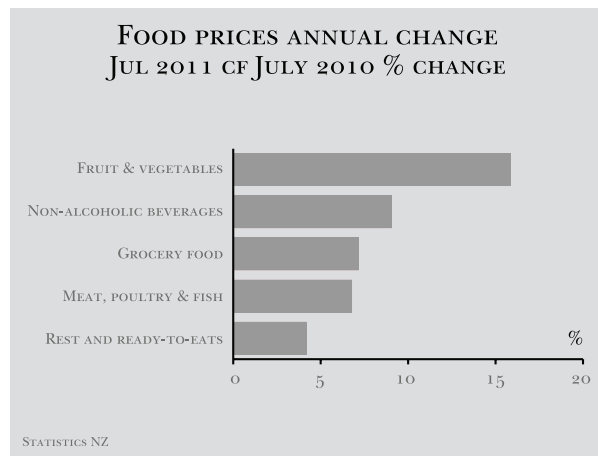
Looking at industry rates, the largest rises over the year were in professional, scientific, and technical services (up 3.1%); and metal product manufacturing (up 2.8%). The main reasons for the rises were to match market rates as well as to reflect the cost of living.

In terms of occupation, the largest rises over the year were for managers, professionals, technicians, and trades workers (up 1.9%) and service, clerical and sales workers (up 1.9%); and machinery operators, drivers, and labourers (up 2.1%). Big winners due to collective employment

agreements coming into effect were factory process workers (up 2.6%) and automotive and engineering trades workers (up 2.4%).

FOOD PRICE INDEX

Food prices were up 2.0% on the month, and 7.9% on the year (although this includes 2.2% due to the increase in GST in October). Annual food prices have been increasing each month for the last six months. Vegetable prices typically rise during the winter months.



The greatest increase this year has been from fruit and vegetables (up 15.9%), led by higher prices for tomatoes (up 52.2%), lettuce (up 54.4%) and capsicums (up 47.3%), all key salad ingredients. Tomato and capsicum prices were influenced by the Queensland floods earlier this year.

LABOUR COSTS AND WAGE EARNINGS ANNUAL % CHANGE						
March quarter	2010	2011	2012	2013	2014	2015
All sector salary & wage rates	1.5	1.9	2.1	2.2	2.1	2.2
Avg ordinary hourly earnings	1.0	2.6	3.3	3.6	3.6	3.6
Total weekly earnings	0.9	4.0	3.9	3.2	3.0	3.0
Statistics NZ						BERL Forecasts

GOVERNMENT ACCOUNTS compiled by Adrian Slack

The Budget Economic & Fiscal Update (BEFU) 2011 in May suggested that total Crown tax revenues in nominal terms would rise by 1.3% in the year to June 2011, while expenditure would rise by 13.7%. While the annual accounts won't be out until October, the figures for the 11 months to May 2011 suggest that the actual outcome may be slightly better than forecast.

Core Crown tax revenue for the 11 months to May 2011 was broadly in line with the forecast, falling below by \$295 million at \$51,868 million. Tax revenue is an accrual measure, and cash receipts provide a slightly more positive picture of the flows into the Government's coffers. Actual tax receipts were \$329 million (0.7%) higher than forecast. Much of this variation came from GST receipts being higher and refunds being lower than expected. Treasury puts this down to higher than forecast private consumption. So it is possible that the year-end deficit will be slightly above forecast.

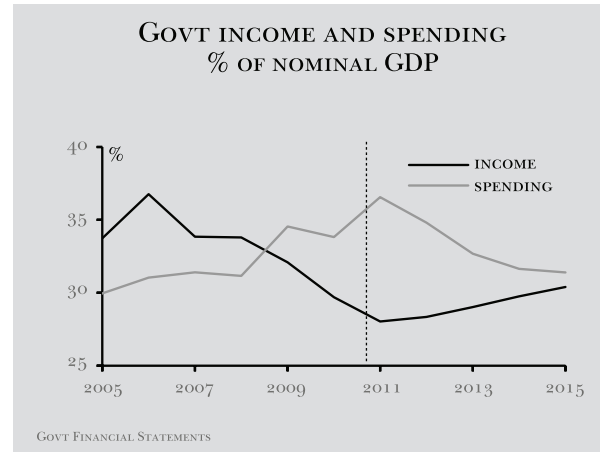
Core Crown expenses to May 2011 were almost 1.2% (\$770 million) lower than the 11 month forecast. This may be due to the fiscal restraints being driven home across the central government departments as part of the current government's austerity drive. While unemployment benefits were on forecast, the major variance within the social assistance accounts was family tax credit payments coming in \$87 million below forecast.

On balance, however, we have been conservative about factoring the reported variances in the 11 month accounts into the forecasts. Given the variances' size, they could be put down to statistical and reporting discrepancies.

One notable exception is the variance in the May month end statements that record net losses of \$2.67 billion compared with the forecast \$3.36 billion. Adding this net loss to the OBEGAL (Operating Balance Excluding Gains and Losses) of \$1.25 billion, for the 11 months to May, gives an operating balance of \$3.92 billion. As a result, the actual operating balance to date is well below the 11 month forecast of \$5.09 billion.

Given the recent shock to the financial markets, there may be a negative variance in the discrepancy between the forecast and actual gains and losses figure, which captures changes in the valuation of the Government's financial assets and liabilities. While this won't affect the OBEGAL it will come

through in a lower than expected operating balance deficit, which could cause some concern amongst those monitoring the Government's commitment to rapidly bring the accounts back into the black.



We see a short-run issue and a long-run risk that we have not seen allowed for in the Government's policy settings and accounts yet. First, the Christchurch Earthquake recovery is set to cost \$3-4 billion more than originally anticipated. This will negatively impact on the Operating Balances track back to surplus in the short-term. This is not news. But, if there is more bad news brought onto the Government's accounts in the next update, then this could lead to a substantial negative revision in the outlook for the accounts and consequently in international investor sentiment, which could affect the risk rating applied to New Zealand and thus the cost of our debt.

The long-term risk is that the EQC's reserve fund has been completely wiped out by the Christchurch Earthquake. This is a large asset to drop off the Government's ledgers and it exposes the Government, as it no longer has a buffer against the possibility of some future awful event.

We have not yet seen any serious discussion on how the Government intends to change its policy settings to rebuild the EQC's fund. But it must as part of a fiscally prudent long-term strategy. Given the short-term risk around delaying the recovery in the Government's accounts, it may be playing off the short-term risk (of worrying the market about a slower than expected return to surplus) against a long-term one, by holding off on such a policy announcement. But there must be some anxious analysts at Treasury as well as some pensive politicians in the Beehive.

Looking ahead, our forecasts are underpinned by the official May forecasts. We have adjusted our tax forecast down slightly in light of our belief that the Christchurch recovery will take longer to bed in than Treasury has anticipated. But higher than expected RWC patronage may help boost domestic and international visitor consumption, which could yet see GDP rise more quickly than we forecast. We then have GDP growing more quickly than the Treasury forecasts in the medium term, which boosts our revenue forecasts.

Mirroring the difference in GDP forecasts, we expect unemployment to stay higher than Treasury in the near term but to be slightly lower in the medium term. This flows through accordingly to our expenditure forecasts.

The core Crown deficit is forecast to top \$16 billion in the year to June 2011, as measured by the OBEGAL. This is around \$200 million greater than Treasury's forecast. But it could be even higher depending on how the over-runs on the Christchurch recovery cost are accrued in the accounts over the upcoming years. The higher deficit reflects revenue being slightly lower (-\$160 million) and expenditure slightly higher (\$45 million) than Treasury's BEFU forecast.

When we add the Treasury's \$4.95 billion forecast of net gains to the OBEGAL deficit, this brings the Government's operating balance down to a forecast deficit of \$11.1 billion for fiscal 2011. As noted, however, we see a downside risk and the gains might be less than anticipated. This would affect the size of the deficit, and the track back to the black for the Government's accounts.

We set aside the long-term issue of how the Government will address the cost of rebuilding the reserve fund after it has rebuilt Christchurch in this forecast. But we note that the required policy change will impose a cost either on the Government's accounts or on New Zealander's directly.

Our medium term forecast is for a positive mix of revenue growth as the recovery beds in and restrained expenditure growth under the stewardship of a National government coalition (this should not be construed as an election forecast but rather aligning with the official forecasts). We forecast an OBEGAL deficit persisting out to 2015, but net financial gains may bring an Operating Balance surplus of around \$1 billion in fiscal 2014/15.

GOVERNMENT NET REVENUE AND EXPENDITURE \$M						
Fiscal year ended June	2010	2011	2012	2013	2014	2015
Direct taxation	33,895	31,955	34,250	37,185	40,410	43,185
Indirect taxation	16,850	18,245	19,590	21,120	22,565	23,870
Miscellaneous	5,470	5,650	5,695	6,290	6,890	7,755
Total Revenue	56,215	55,850	59,535	64,595	69,865	74,808
as a % of GDP	29.7	28.0	28.3	29.0	29.8	30.4
Social Security	21,185	22,220	23,035	23,825	24,540	25,465
Health and Education	24,850	25,815	26,610	26,600	26,320	26,470
General Expenditure	15,665	21,730	19,770	17,985	18,275	20,075
Debt Servicing	2,310	3,080	3,715	4,325	4,700	5,255
Total Expenditure	64,010	72,845	73,130	72,735	74,285	77,266
as a % of GDP	33.8	36.6	34.8	32.7	31.6	31.4
OBEGAL	-7,795	-16,995	-13,595	-8,140	-4,420	-2,458
OBEGAL as a % of GDP	-4.1	-8.5	-6.5	-3.7	-2	-1
Pre-funding of NZS	250	0	0	0	0	0
OBEGAL after pre-funding	-8,045	-16,995	-13,595	-8,140	-4,420	-2,458
Memo: Operating balance	-7,000	-12,040	-11,975	-6,405	-2,590	-515
Govt Financial Statements						BERL Forecasts

MANUFACTURING compiled by Fiona Stokes

Employment in manufacturing grew by 5,100 between the June 2010 quarter and the June 2011 quarter according to the latest HLFS results. This growth was spread across a variety of occupations.

In the major occupation groups employment grew in machinery operators and drivers (up 13,000), and labourers (up 900). Within these occupations, job growth occurred among stationary plant operators, storepeople, packers and product assemblers, and factory process workers. Overall, there was a slight decline in the number of people employed as trades workers and technicians and this is also seen in manufacturing occupations. The number of people employed as food and textile factory workers grew slightly during this period, while those in the printing and wood trades had small declines.

This positive employment growth has been reflected in the manufacturing surveys that we monitor. However, underlying uncertainty in regards to the exchange rate and our markets beyond Australia and China continues to hold back expansion.

The New Zealand Manufacturers and Exporters Association Survey of Business Conditions indicates that domestic manufacturing sales increased by 11.2% in July 2011 and compared to July 2010 figures, while manufacturing export sales increased by 16.4%. Overall, total sales increased by 13.5% y-o-y and net confidence among the businesses surveyed was up.

Despite these improvements in export sales, members remain concerned about the exchange rate, continued disruptions caused by the Canterbury earthquake in February, and the effect of global uncertainty on the demand for New Zealand export products.

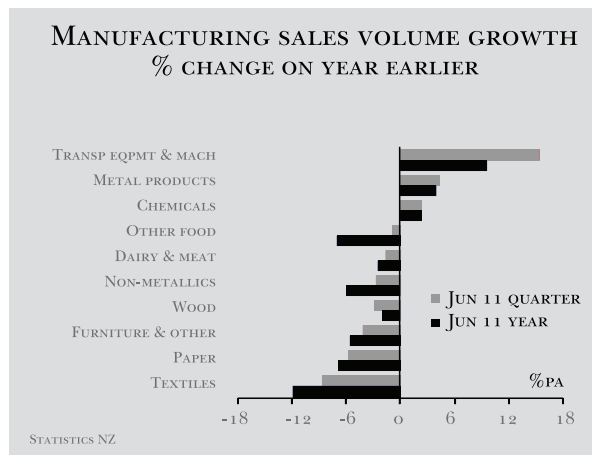
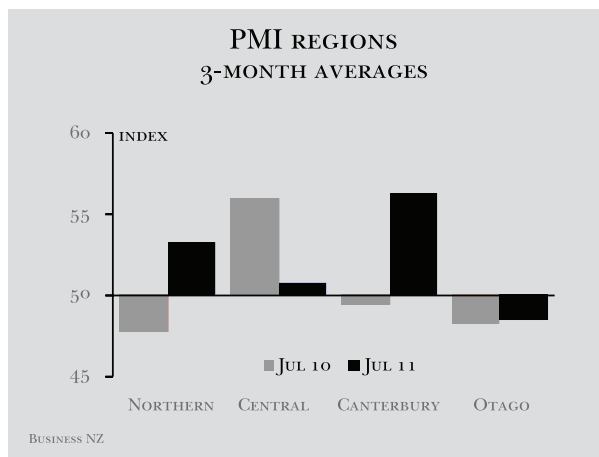
The BNZ-Business NZ seasonally adjusted PMI stood at 53.2 in July, indicating manufacturing

activity is expanding. Each of the indices that make up the PMI were also above 50 in July, with the highest being new orders, sitting at 56.0. In regards to three-monthly averages, the PMI stood at 53.0 in July, and production, employment and new orders were also all sitting above 50.

At a regional level, comparing three-monthly averages year-on-year, the Otago region continues to struggle while results from the Central region indicate ongoing expansion.

Unfortunately, manufacturing sales volumes in the June 2011 quarter are not quite as positive as the employment figures. Comparing the June 2011 quarter with the same quarter in 2010, sales volumes were predominantly negative. The exceptions, as shown in the figure, were transport equipment, machinery and equipment manufacturing, metal product manufacturing, and chemical product manufacturing.

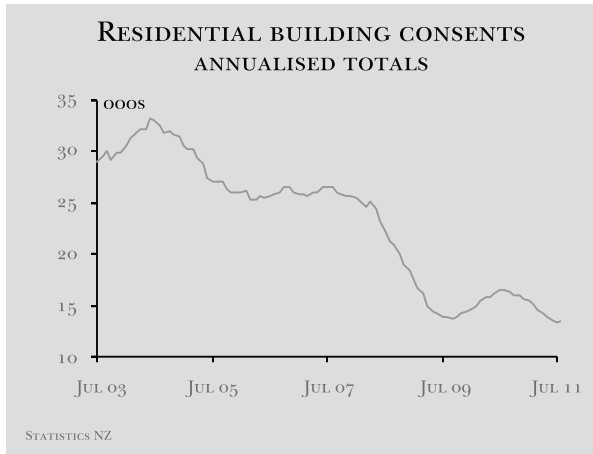
The usual star players in manufacturing – dairy and meat, and other food – have not fared well over the quarter or the last 12 months. A decline in cattle and sheep slaughtering is reflected in manufacturing sales volumes, along with our continued export of logs rather than manufactured wood products.



Europe's debt crisis continues to impact on the international manufacturing surveys we monitor. JPMorgan Global Manufacturing & Services PMI sat at 52.3 in June 2011, a slight decline from the 53.0 seen in May 2011. Global manufacturing activity is slowly growing, but lopsidedly. As mentioned in our previous edition, manufacturing in the Euro zone is expanding but this is mainly due to slowly expanding activity in France and Germany. Output from Japan, China and the UK continues to also be positive but at a lower rate than previously. Unsurprisingly to those of us following events in Europe, business conditions in Italy, Spain and Ireland are continuing to decline and with it their manufacturing industries.

BUILDING AND CONSTRUCTION compiled by Fiona Stokes

Residential building construction is continuing its downward slide. Throughout 2011, the number of consents issued each month has sat between 900 and 1,200. In July 2011, 1,200 residential consents were issued. This brings the three-month running total for consents to just 3,330. Moreover, the 12-month running total in July was just 13,200 – as a comparator 22,500 residential building consents were issued in July 2008.

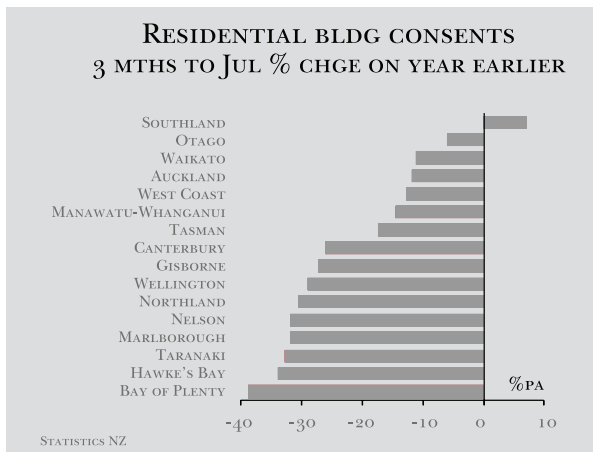


When we look at the 12-month percentage change with a year earlier, residential building consents in the North Island were down 18% in July 2011. In the South Island this percentage change was greater, with South Island residential building consents down 21.6%.

Comparing the three months to July 2011 with the same period in 2010, we can see how residential building consents have declined dramatically nationwide. Only Southland managed to show any improvement.

Residential consents in the three months to July 2011 were down 29% in the Wellington Region compared to this time last year. Consents in regions such as Nelson, Marlborough, the Hawke's Bay and Taranaki were also down over 30%.

We would expect house prices to be rising now due to the low number of new homes being added to our housing

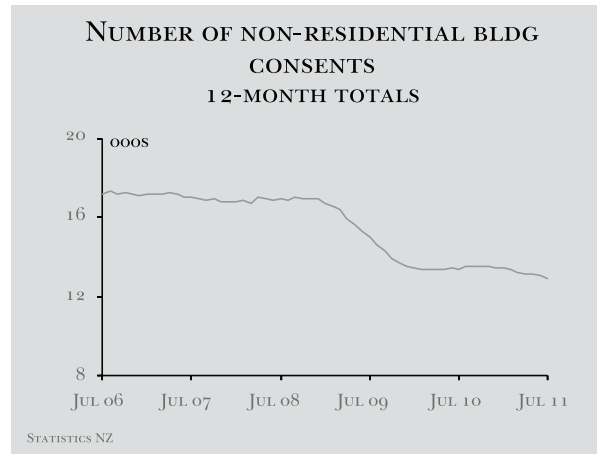


stock. However, demand for property remains soft and Quotable Value data indicates national property values in July 2011 were 0.4 percent below the same time last year.

Industry associations such as the Registered Master Builders Federation have understandably expressed concerns about the low number of building consents. These concerns centre on the impact this will have on industry capability in the medium to long-term. This concern is supported by the latest employment figures. The main employment losses reported in the HLFS for the June 2011 quarter were from the construction sector, which lost a further 13,000 employees.

Currently there is not a skills shortage. However, the Registered Master Builders Federation argues that if skilled staff continue to be lost, the industry will face problems in the medium to long-term. This will be exacerbated due to the Canterbury rebuild, the large amount of leaky home repair work to be undertaken, the potential housing shortages that will occur in the Auckland Region, and a general increase in construction activity as the economy recovers.

Building construction is a sector of SMEs. While this allows some flexibility in terms of tradespeople being able to adapt and move to find work, this becomes difficult when consents are down across the board. For example, there has also been a decline and plateau in the number of non-residential consents. The 12 month running total for non-residential consents sat at 12,800 in July 2011. And again as a comparator, this figure was almost 17,000 in July 2008.



It is well known that building construction is a cyclical industry. As mentioned above, a general increase in construction activity is expected as the economy recovers but the question remains, when will this happen? Demographic factors such as household formation and migration rates may force the number of residential consents up, but few New Zealanders are currently motivated to build or take on the debt required to build. As such we are forecasting that the 12-month running total for residential building consents will sit at 16,100 in July 2012 before moving towards 23,000 in July 2013.

TOURISM compiled by Nathaniel Robson

The Rugby World Cup is now underway and suppliers of services to the tourist market are finally receiving some relief from the slumped demand caused by the global recession, the earthquakes in Christchurch and Japan, and flooding in Australia.

The prospects for the sector in the short-term are very good, with visitor numbers and spending associated with the RWC already exceeding expectations. What will happen after the event is somewhat less certain; although, there is the potential for a strong summer season given the timing of the RWC. Many international visitors from China and other countries ambivalent towards rugby may have been crowded out of the present market. Hopefully most will opt for a later visit rather than none at all.

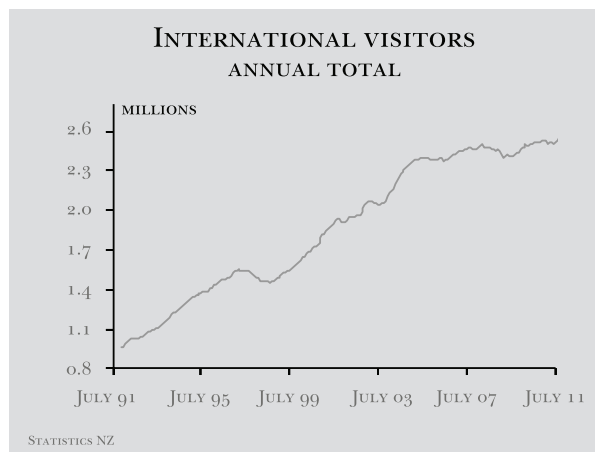
In the medium to long-term, the international visibility afforded to New Zealand by the RWC should help to lift visitor numbers, and the investment in infrastructure leading up to the event will also provide long-term benefits to the sector.

However, there are risks associated with the RWC and its aftermath. And while the timing of the event within the year is perhaps ideal, the timing overall is not. Recent international and domestic economic conditions, including the high NZ dollar, may have curtailed some of the potential gains to be made from the RWC. The event can also be as bad for our reputation as it is good. This is a particularly important consideration when capacity limits are reached and not managed well. The failure of planning and organisation in Auckland on the first night of the tournament is a case in point. Finally, there is the risk that the trends present in the tourism sector data for the first half of this year will resume once the Cup has been lifted. This data includes the number of international visitor arrivals

for the year ended July 2011, average expenditure per visitor for the year ended June 2011, and sales of guest nights in commercial accommodation for the June quarter, each compared to the respective measure from 12 months prior.

Visitor numbers dipped slightly below 2.5 million for the year to July 2011, a decrease of 0.5 percent on the analogous figure to July 2010. Large falls in holiday tourist arrivals from Australia (down 9%), the UK (-15%), the USA (-5%) and Japan (-16%) were largely offset by rapid growth in the Chinese holiday segment (up 27%) and Australian VFR (Visiting Friends and Relatives arrivals, up 3.5%). The overall result for Australian visitors over the period was a fall of 1.2%. Similarly for the rest of our top five sources of international tourists, overall visitor arrivals broadly followed the pattern of holiday visitors.

The main concern here is the depressed state of the Australian holiday segment, despite the \$NZ-\$AUS exchange rate not being especially unfavourable and their economy doing reasonably well. Indeed, over the same period short-term departures from Australia were up 11%. The trans-Tasman flight disruptions created by the volcanic ash cloud from Chile in June and a lull in demand in the lead-up to the RWC can only partially explain New Zealand's below average share of these outbound tourists



Source country	% change (year to July 2011)		
	Total	Holiday	VFR
Australia	-1.2	-9.0	3.5
UK	-11.2	-15.0	-9.1
USA	-2.9	-5.3	-4.5
China	22.2	26.6	15.4
Japan	-11.5	-15.7	3.1
Germany	0.0	-2.6	1.5
Korea	-5.4	2.4	-10.9
Canada	-0.5	-5.8	4.2
TOTAL	-0.5	-3.9	0.7

With visitor numbers arising from the RWC now being forecast to reach 95,000, arrivals may be up at least 3.5% for the calendar year. This means visitor numbers could be running at about 2.61 million per annum by the end of 2011. Growth in visitor arrivals is likely to ease somewhat through 2012, possibly even appearing flat by the end of the year. What will be interesting over this period is the performance of the Chinese holiday segment compared to that of the UK and the USA. If these latter two markets do not remain buoyant after the RWC, we may well see China overtake them to become our second largest source of holiday tourists.

Spending by international visitors has also fallen 6.5% to \$5.56 billion in the year to June 2011. Since visitor numbers have fallen 0.5% over approximately the same period, this indicates a fall in the average spend per-visitor. Indeed, figures from the International Visitor Survey show that average spending has fallen about \$190 to \$2,419 per person over the period.

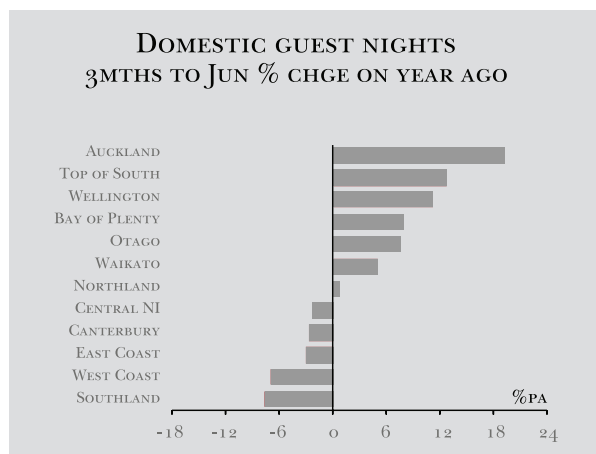
Spending per head by visitors from our top five source countries has fallen, both for the holiday and VFR segments, and overall. For Australia in particular, the average spend of holiday and VFR tourists was down 8% to \$2,186 and 10% to \$979 respectively. There were two exceptions to this trend however: Chinese VFR spending was up 8% to \$2,816 and Japanese holiday spending was up almost 9% to \$3,960. Nevertheless, the overall average spend per visitor from China and Japan was strongly negative (-10% and -19% respectively). For China, the VFR segment is too small to make any difference relative to the holiday segment; but in the case of Japan, the increase in spending by holiday tourists was more than offset by cutbacks by Japanese VFRs, business travelers, and students.

The recent experience in per-visitor spending can be seen as part of a longer-term trend. This measure reached a peak of \$3,289 in 2002. Since then, visitor numbers have risen 600,000 but expenditure has fallen \$100 million. It is unlikely that the RWC by itself will reverse this trend.

Commercial accommodation data for the June quarter indicates a continuing drop-off in the purchase of guest nights by international visitors, down 8% on the same quarter last year. This was partially offset by positive growth in domestic guest nights, up 3%. However, the experiences

across regions and accommodation types varies markedly.

Canterbury has suffered the most losses, with guest night sales to domestic tourists down 7%, and international guest nights down 40%. Other South Island regions have also been negatively affected. The only respite has been a return to growth for the top of the South, and domestic tourists partially replacing internationals in Otago, especially Queenstown.



A similar story goes for the Bay of Plenty (Rotorua), where growth in domestic guest nights has almost offset the drop in international guest nights. The opposite has occurred in Northland. In the end it is the main centers of Auckland and Wellington that have enjoyed the most growth with overall guest nights increasing 12% and 7% respectively.

The accommodation types that have benefited from the shift in the market towards domestic guest nights are motels and holiday parks, which have seen growth of 4% and 3% respectively, while sales by hotels and backpackers have fallen 7% and 5%. Canterbury hotels' and backpackers' sales were down more than 50% while that of motels was up 27%. Guest nights in holiday parks were up across the board, with increases of over 10% in Auckland, Rotorua, and Queenstown.

same time, domestic residents choosing to holiday at home rather than abroad is good news for the tourism sector. There may in fact be more good news on the way: July 2011 guest night figures, just released as this report goes to press, indicate across the board improvements over the June figures, with overall guest nights turning positive (up 1.1% compared to the July 2010 quarter) on the back of stronger domestic sales (up 6.4%).

Regions and accommodation types that were doing well according to the June figures are doing even better in the July figures, and those that were not doing so well are seeing some improvement in their situation.

Any good news of a sustained improvement in domestic tourism spending is going to be swamped in the data by the RWC for the rest of this year. Once things get a bit more back to normal it will be interesting to see how things play out. One thing is certain however: hosting the RWC has created many opportunities for New Zealand. How we capitalize on those opportunities is ultimately up to us.

With overall guest nights down 1.3% in the June quarter compared to the same quarter last year, we can see that the lower average visitor spend has partly manifested itself in shorter stays (in commercial accommodation, at least). At the same time, domestic residents choosing to holiday at home rather than abroad is good news for the tourism sector. There may in fact be more good news on the way: July 2011 guest night figures, just released as this report goes to press, indicate across the board improvements over the June figures, with overall guest nights turning positive (up 1.1% compared to the July 2010 quarter) on the back of stronger domestic sales (up 6.4%). Regions and accommodation types that were doing well according to the June figures are doing

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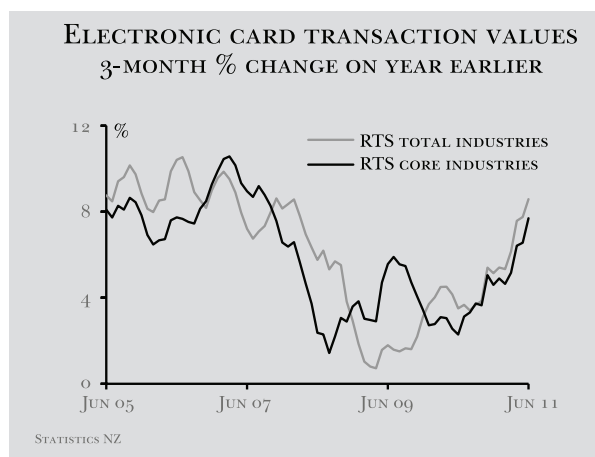
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RETAIL TRADE compiled by Adrian Slack

Retail trade sales are an important barometer of how New Zealand consumers and businesses are feeling and what they are doing to get their house (or business) in order. The readings coming from the statistics reveal some trends.

First, the recovery – in New Zealand at least – is continuing within retail trade and in most parts of the wider economy. Core retail sales turnover rose by 2.0% and volumes by 1.2% in the year to June 2011. That values are rising quicker than volumes is a sign of some retail price inflation. The retail trade deflator measured a modest average annual price increase for retail goods of 2.1%. This is certainly not run-away inflation, but might be interpreted as a healthy sign that some retailers at least are cutting prices and margins. Indeed, in the last quarter, 11 out of the 15 retail trade industries experienced inflation.

Another trend is that households are continuing to de-leverage, preferring to spend the money they have rather than the money they don't. For example, we can see this in the debit/credit figure below on electronic card transactions. Transactions by debit card rose by 7.1% in the year to June, but those by credit card by 3.6%. That credit transactions are growing, particularly when compared with a restrained 0.7% in the year to June 2010, could be taken as a positive indicator of consumer confidence.



This indicator is reinforced by the growth in motor vehicle sales (MVS). Actual MVS grew by 2.6% in the last quarter in nominal terms and by 0.4% in real terms. As MVS are generally a bellwether for consumer and business confidence, this is a reassuring sign. Admittedly, part of this pick-up will be off the back of the disruption of car imports from Japan. But MVS have risen enough to be back on to the pre-GFC crisis trend.

There was a generalised increase in retail sales across the country, but with greater strength in the North Island. Compared to the same quarter a year ago, Auckland (5.7%), Waikato (4.8%) and Wellington (7.7%) lead the country in terms of sales growth, while Canterbury also delivered a moderate increase (3.0%). The hinterlands of the North and South Islands, however, had growth rates of around 1.3-1.4%. Given the industry as a whole experienced inflation of more than 2%, although values may have risen, the volume of sales is likely to have decreased in these areas.

Nonetheless, retailers should still be cautious. Despite the recovery in sales values, there appears to be a secular downward trend in retail spending as a proportion of overall private sector consumption expenditure. So despite some recovery in consumer spending overall, retail spending as a proportion of both consumption expenditure and GDP has fallen and is remaining relatively flat. This implies that the retail trade sector now plays a slightly smaller role in the economy.



While people are now holding onto their jobs, employment growth remains modest, and is likely to do so until the boost from Christchurch's reconstruction provides its near term stimulus. Combined with a subdued housing market and restraint on growing credit the outlook for the retail trade sector is for modest growth. The Rugby World Cup will have a direct boost to the tourism sector, which will benefit the accommodation and food retailing sectors, as well as the flow on to other tourism-related industries. It may also have some persistence by raising New Zealand's profile, which may continue to lift international visitor arrivals beyond the Cup.

Over the medium term, if the global economy holds together, then Christchurch's reconstruction combined with a generalised recovery will lift retail sales. If primary exports continue their current growth pattern, then this will also help push some income into the provinces which may also help retailers in the hinterlands.

The forecast is for moderate growth in retail sales volumes of 1.0% in the September 2011 quarter compared to the same quarter a year ago, and 1.6 percent in the core industries with the spike generated by the RWC and the build-up of reconstruction activity in Christchurch. We expect core retail sales volumes to grow persistently across 2012. The reconstruction efforts will continue to have an increasingly positive effect on the retail trade sector towards the later part of 2012 and on into 2013. This is likely to benefit the core industries more than the vehicle retailers. The 2013 September quarter-on-previous-quarter forecast is for 2.0% growth in volumes across the sector, and a 2.2% per annum expansion in the core industries.

RETAIL SALES				
% CHANGE ON PREVIOUS YEAR				
Quarter	VOLUME		VALUES	
	Total	Core	Total	Core
Sep 10	1.9	1.5	3.3	2.0
Dec 10	-0.1	0.3	1.5	0.7
Mar 11	0.8	1.4	3.4	2.4
Jun 11	1.1	1.9	4.1	3.1
Sep 11	1.0	1.6	4.2	3.2
Dec 11	1.3	1.5	4.0	4.0
Mar 12	1.3	1.4	3.8	3.8
Jun 12	1.4	1.6	3.6	3.5
Sep 12	1.6	1.7	3.8	3.8
Dec 12	1.8	2.0	4.0	4.0
Mar 13	2.3	2.5	4.0	4.0
Jun 13	2.5	2.7	4.3	4.3
Sep 13	2.0	2.2	4.5	4.5
Dec 13	2.2	2.4	4.5	4.5
Mar 14	2.6	2.9	4.8	5.0
Jun 14	2.4	2.6	4.9	4.9

Statistics NZ

BERL Forecasts

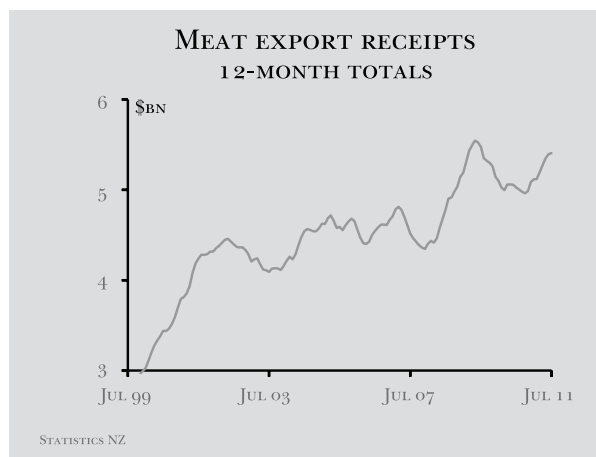
AGRICULTURE compiled by Kelly Dustow

DAIRY

When looking at Fonterra's Global Dairy Trade online trading statistics, it appears that the prices for Skim Milk Powder and Whole Milk Powder have declined in recent trades. Cheese was one of the recent products to be added to the trading system, and prices have declined here also. Despite these recent trends, dairy export receipts (which includes milk, butter and cheese) have increased by 26.5% on year earlier levels for the year ending July 2011. Dairy export volumes were also up for the year ending July 2011 by 5.03% on year earlier levels. Despite prices slowing, volumes appear to be increasing to fill the global demand. Fonterra has recently confirmed its forecast payout of \$7.15-\$7.25 before retentions.

MEAT AND WOOL

For the year ending July 2011, the good news continues for meat as export receipts are up 7.6% on year earlier levels. Over the same period, export volumes are down 6.14%, which again, is not a surprise given cattle and sheep slaughtering was down 3.1% and 3.9% respectively. Despite, Beef & Lamb NZ recording static numbers for beef, it is certain that stock numbers will increase this season due to high international prices. These high prices are expected to continue due to reduced global supply, particularly from the US, and increased demand from Asia and the Middle East due their middle classes becoming wealthier and demanding more protein.



It is a good year to be in sheep farming, with prices still high, up 30.22% on year earlier levels for the year ending July 2011. However, the quantity of wool exported during this period decreased 9.49%. This was predominantly due to low stock numbers rather than prices; according to Beef & Lamb NZ's Economic Service stock numbers'

survey, stock was down 2.1% on last year for the year ending June 2011. However, Beef & Lamb NZ are predicting an increase in lambing percentages for the current season, as last year they were down due to severe weather.

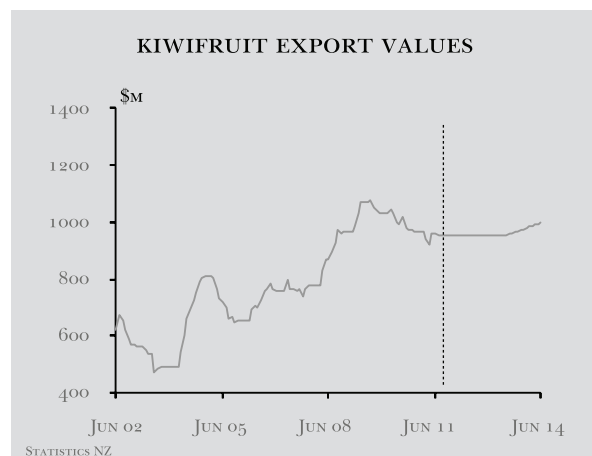
HORTICULTURE

KIWIFRUIT

At a recent ZESPRI annual meeting, Chairman John Loughlin indicated that given currency volatility and the global economic instability, the kiwifruit industry had satisfactory returns at the end of the 2010/11 season.

ZESPRI is forecasting that future returns on a per tray basis are expected to decrease over the next season, but returns per hectare for growers will hopefully improve due to increases in productivity. We have therefore adjusted our forecast to reflect these sentiments, as well as concerns around the influence of the vine disease, PSA.

The latest statistics for the kiwifruit industry are less than favourable, with quantities, receipts and prices all down on the previous year for the year ending July 2011. That is, kiwifruit export quantities were down 3.3%, export receipts were down 6.7%, and prices were down 3.5%. It is hard to pinpoint an exact reason for this decline, as export quantities before this were performing quite well. For just the month of July, export quantities were down 7.4% compared to July 2010. There could be several explanations for this, i.e. less demand from Europe due to their debt crisis; however, one that springs to mind is the vine disease PSA, which is meant to be more virulent during the winter months.



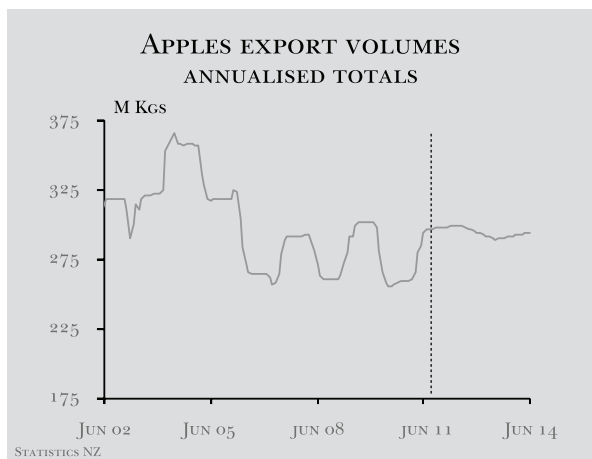
APPLES

For the year ending July 2011, apple export values were up 11.8% from last year. Most of this rise comes from increased export volumes rather than higher prices, with volumes increasing 16%. Again, prices seem to keep sliding, down 3.6% from last year.

Unfortunately, data is not available to display the early signs of apples exports to Australia, with the first exports sent late August. The recent leaf curling midge found in a carton by Australian inspectors in New Zealand has heightened concern over the exports. There are reports that state governments in Victoria, Tasmania and South Australia are looking into options to ban apple imports in order to protect their industry from apple Fireblight. Given Australia is a part of the World Trade Organisation, this would be an unfavourable move, considering the probability of Fireblight getting through, the economic benefits such as lower prices for consumers, and encouraging efficiency that New Zealand trade can bring. Therefore, depending on whether the apple industry can continue increasing volumes, we believe that exports will continue to increase, unfortunately these benefits won't be truly seen until next season.

WINE

For the year ending July 2011, wine prices were down 5.33% on year earlier levels. However, export receipts were up 5.35% over the same period, mainly due to increased export volumes. Export volumes have increased by 11.27% due to favourable weather conditions and larger harvests. In the Wine Growers NZ annual report for 2011, it mentions that the increase in volumes was due to clearing previously built-up stock. Subsequently, the industry is concentrating on moving into premium markets in Asia, the US, Mainland Europe and Canada. However, with prices declining significantly, and at the lowest level that they have been since 1998, we are predicting prices to continue to fall as wine continues to flood markets internationally.

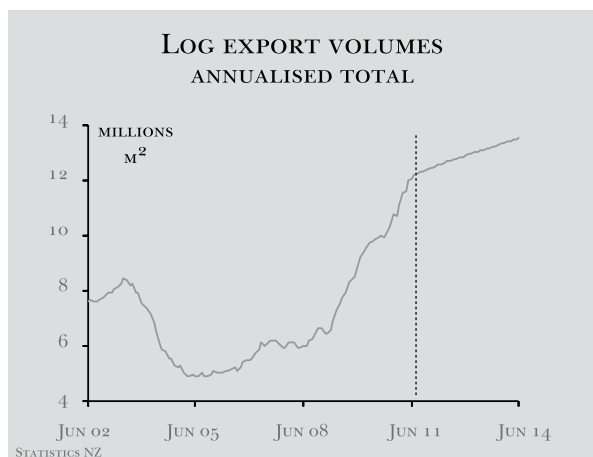


FORESTRY compiled by Wilma Molano

Across our various commodities, logs and timber had the fourth largest year-on-year export growth at 21.8%, with a value of \$2.6bn in year ending July 2011. Overall, however, logs, timber and pulp have all had variable performances. Log export receipts continue to increase due to rising volumes (annualised total) and prices (annual average), while timber and pulp are down in terms of volume and price.

LOG

Log export volumes and prices were up 23.3% and 11.5%, respectively, in the year to July 2011. Log export volumes were up 21.5% while log prices were also up 10.7% over the same quarter in the previous year. This is equivalent to a 2.3 million cubic metres increase from last year's total exports of 9.9 million cubic metres.



Thus, we expect log export volumes to remain positive until the end of 2011. Demand from China is expected to be maintained as 2011 progresses, owing mainly to economic growth, continued urbanization, and the ongoing effect of the Russian log export tax. China has reduced its importation of logs from Russia since the imposition of a 25% softwood log export tax in 2008. Moreover, concessions provided by the Chinese government in regards to loans for the construction of affordable housing is also driving the high demand for logs from New Zealand. Raw-log sales to China have risen 58% in the last four months to June, to almost \$420mn, with export log prices increasing more than 20% over the last two years. China now takes almost two-thirds of New Zealand's log exports and accounts for almost all the growth in this market. However, we would note that the Indian and Japanese markets have the potential to expand because of strong economic growth in India and earthquake rebuilding in Japan.

TIMBER

Timber export volumes for the year to July 2011 were up 4.7% year-on-year, but were down 5.2% when we compare the results for this quarter with year-earlier levels. Export revenue for the year was down to 1.7%, which is

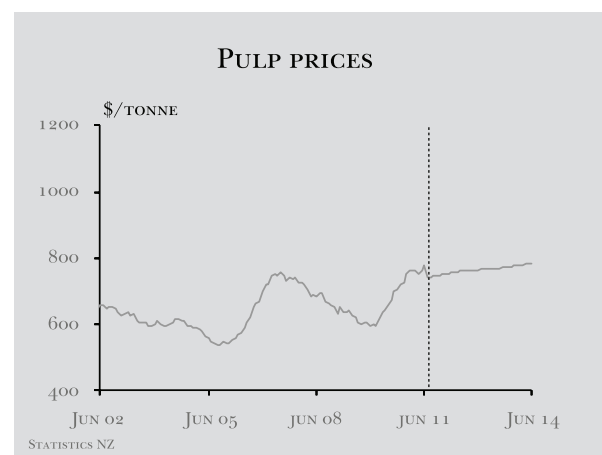
a decrease of almost 20% for the three months to July compared with year earlier.

The Situation and Outlook for New Zealand Agriculture and Forestry (SONZAF) 2011 reported that housing construction in Australia and the US was still at low levels, suggesting a less promising situation for the New Zealand timber industry. While the Chinese government is making good concessions regarding housing loans for the construction of affordable houses, as mentioned above, it is importing raw-logs rather than sawn timber. According to the NZ Timber Industry Federation, timber-processing opportunities are being transferred from New Zealand to China as a result of this, and this can be seen in the big rise in log exports and subsequent dive in processed wood. If this trend continues it will be more pressure on New Zealand wood processors who are already being squeezed by a drop in building construction activity.

The future of timber export is not as promising as logs since the increase in unit price is almost flat if not increasing slowly. However, we hope against hope that beyond 2012, the demand for NZ timber will increase as a result of recovery in Australia and the US and increase in demand from Japan for earthquake re-building.

PULP

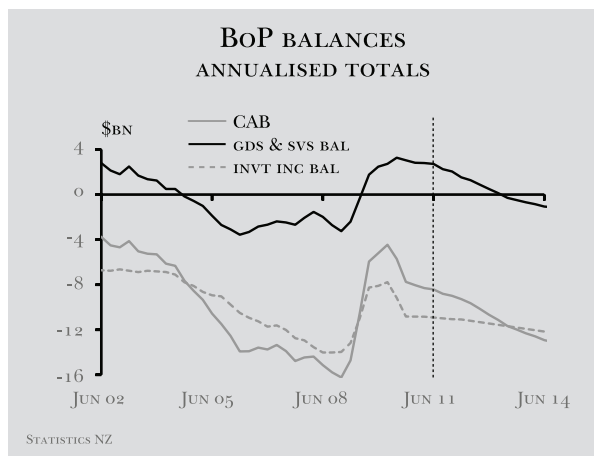
Year-on-year, pulp export volumes were down 0.1% in July 2011. This decline grows to 19.2% when we compare export volumes to the same quarter last year. Historically, pulp's contribution to export receipts is marginal when compared to timber and logs. And for the past three years, the percentage change in export quantities has been negative. The only source of increase in pulp export receipts has been in the increase in unit price. However, the latest overseas merchandise trade statistics show that there has been an increase in wood pulp and waste paper exports to Japan. Overall, we are forecasting export volumes of pulp to be static, with marginal gains in export revenue coming from improved prices in the international market.



EXTERNAL SECTOR compiled by Amapola Generosa

The struggle to avoid recession and stay afloat is significantly underpinning New Zealand's favourable terms of trade and a healthy trade surplus.

The latest trade figures from Statistics New Zealand show that New Zealand reported its first trade surplus for two decades in the month of July. This was due to global demand for dairy products stoking the nation's export receipts.



The value of exports outstripped imports by \$129 million (about 3.5% of the total value of exports) in July 2011. This took the monthly trade surplus annual surplus to \$1.31 billion, which is well above the expectations of \$1.1 billion. The July trade surplus was surprisingly strong and was largely due to a weakness in oil imports.

Merchandise exports rose to \$3.7 billion, up 12.8% compared to July 2010. This was on the back of higher receipts for dairy exports and greater volumes of our dairy products sold offshore. The value of imported goods, at \$3.5 billion in July, was up 11% on the same month last year. On an annual basis the growth in imports was well below the growth seen over the last two quarters. This is unsurprisingly given the strong New Zealand dollar, which made the importation of goods more expensive and eroded exporters' returns. The trade-weighted index of major trading partners' currencies rose 3.4% in July, and was 8.2% higher compared to the same month a year ago.

Over the last 12 months, export receipts for milk powder, butter and cheese have grown by 26.5%, to \$11.4 billion. The volume of milk powder, butter and cheese exports also rose 9.6%, compared to July 2010. Export receipts for casein and

caseinates rose 13% during this period, to \$723 million. This was during New Zealand's off-season, and at a time when dairy prices fell 0.9% to a trade-weighted US\$3,660 per metric tonne in the latest Fonterra Cooperative Group's online trading platform. Crude oil exports rose 22% to \$212 million in July; but have dropped over the last 12 months by 3.2% to sit at \$2.04 billion.

Overall, New Zealand's annual merchandise exports have gained almost 13% over the past 12 months to \$44 billion.

Despite weaker growth in Australia due to flooding and subdued retail prices, New Zealand's export receipts to Australia rose 8.5% in July to \$897 million. This growth was mainly due to crude oil and refrigeration equipment exports. Also, Chinese export sales increased 3.6% to \$387 million. Exports to emerging countries like India showed impressive growth, export receipts more than doubled to \$112 million in July.

On the import side, the value of petroleum imports has increased 17.1% to an annual \$4.6 billion. Machinery and equipment imports also rose 15% to annual \$6.3 billion. That led about \$100 million increase in July imports of capital goods (up 26.5% in annual terms), which was largely made up of electronic equipments. Transport equipment also increased, up \$116 million, or 4.5% in annual terms. Total imports in July reached \$3.4 billion, down 3.5% compared to the same month a year ago. The decline in monthly imports compared to year ago level is due to lower consumer and transport import spending. But on a year-on-year comparison, imports increased about 11.6% percent. In general NZ imports import spending remains strong. The strong spending on capital imports points to optimism in the business sector—an encouraging sign a sluggish economy will certainly welcome.

With subdued domestic spending, the external sector has kept the NZ from slipping again to recession, and managed to keep economic growth to a flat, yet above the "no growth" level. However, the sector is exposed to some risks. One is the relatively strong NZ dollar. Since 2009, it has appreciated by almost 80% (from 0.49 to its peak in August 2011 at 0.88 to a US\$). This had been hurting exporters, and reducing competitiveness of NZ exports. If the declining trend continues, exporters will worry less about competitiveness and lower demand for NZ exports. Second,

slowing down of the economies of its major trading partners might lead to lower export volumes to these countries. Japan is still recovering from the natural disaster that hit the country earlier this year, and China adopting tighter monetary policies to moderate its growth and control inflation. The debt problem in Europe is also like to cause NZ exports in the region to contract. Another is the volatility of export prices. Falling export prices with surging import prices likely to weaken NZ terms of trade. Case in point: Recent milk auctions by Fonterra Co-Operative Group Ltd. have seen dairy prices decline. Moreover, the country's terms of trade remains favourable, but with a relatively strong NZ\$, competitiveness of NZ exports likely to erode.

Looking ahead, merchandise trade threatens to return to deficits because the global economy is fragile. Although economies of New Zealand's major trading partners, Australian and Asian, remained robust, the country's export performance may suffer from flow-on impact as the global economy goes on a softer patch. Given the large number of uncertainties around the global situation, the Reserve Bank is likely to keep interest rate to remain at its currently low level until the end of the year.

MERCHANDISE EXPORT RECEIPTS \$M						
Year ended June	2010	2011	2012	2013	2014	2015
Dairy	8,835	11,330	11,670	11,903	12,260	12,690
Meat	5,197	5,553	5,664	5,749	5,835	5,922
Wool	554	718	718	722	725	729
Fish	1,349	1,507	1,522	1,552	1,583	1,615
Horticulture	2,147	2,202	2,235	2,285	2,342	2,412
Alcohol	1,120	1,189	1,248	1,298	1,350	1,397
Forestry products	4,072	4,763	5,239	5,554	5,776	5,978
Aluminium	985	1,178	1,207	1,237	1,268	1,300
Machinery & transport eqpmt	2,559	2,771	2,896	2,997	3,087	3,180
Petroleum	2,280	2,156	2,328	2,444	2,542	2,618
Other	9,542	10,524	10,840	11,198	11,567	11,949
Exports of Goods (fob)	38,641	43,890	45,567	46,939	48,336	49,790
% change	-4.9	13.6	3.8	3.0	3.0	3.0
as a % of GDP	20.4	22.0	21.7	21.1	20.6	20.2
Statistics NZ						BERL Forecasts
MERCHANDISE IMPORT PAYMENTS \$M						
Year ended June	2010	2011	2012	2013	2014	2015
Food	3559	4035	4196	4343	4495	4652
Petrol & petroleum products	6159	6971	7424	7833	8185	8512
Non-electrical machinery	4581	5246	5508	5839	6014	6164
Electrical machinery	3381	3789	3960	4178	4324	4410
Transport equipment	4670	5702	5930	6167	6383	6511
Plastics	1450	1532	1578	1626	1674	1708
Textiles, clothing & footwear	2127	2316	2385	2468	2555	2619
Other	12013	13074	14162	15543	16463	17124
Imports of Goods (cif)	37940	42665	45144	47996	50093	51701
% change	-12.7	12.5	5.8	6.3	4.4	3.2
as a % of GDP	20.0	21.4	21.5	21.6	21.3	21.0
Statistics NZ						BERL Forecasts
BALANCE OF PAYMENTS ON CURRENT ACCOUNT \$M						
Year ended June	2010	2011	2012	2013	2014	2015
OT trade balance (fob-cif)	701	1,225	424	-1,057	-1,757	-1,911
BoP conceptual adjustments	2,555	2,155	1,600	1,600	1,600	1,600
BoP merchandise trade balance	3,256	3,380	2,024	543	-157	-311
Services exports	12,219	12,356	12,761	13,080	13,407	13,742
Services imports	12,200	13,015	13,504	13,909	14,310	14,705
Services balance	18	-659	-743	-829	-903	-963
Balance on goods and services	3,274	2,721	1,280	-287	-1,060	-1,273
Investment income balance	-9,170	-10,903	-11,206	-11,662	-12,139	-12,639
Transfers balance	188	-235	280	280	280	280
Current Account Balance	-5,707	-8,418	-9,645	-11,669	-12,919	-13,632
as a % of GDP	-3.0	-4.2	-4.6	-5.2	-5.5	-5.5
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ISSN 1170-4861

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