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THE BERL FORECASTS PANEL

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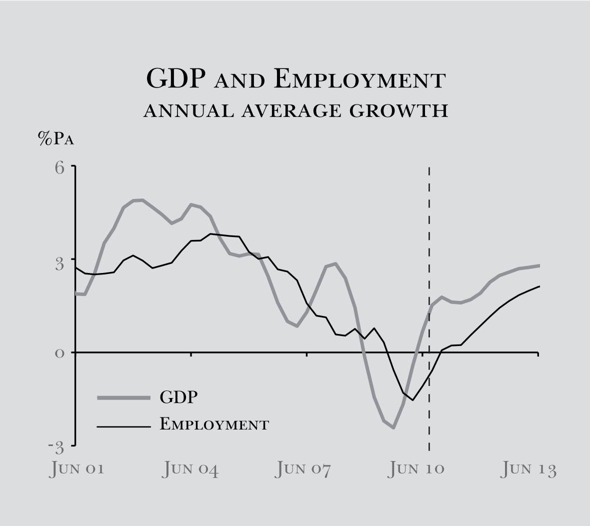
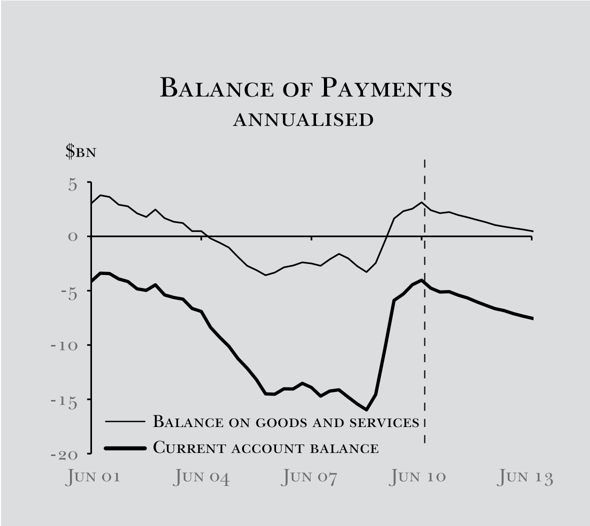
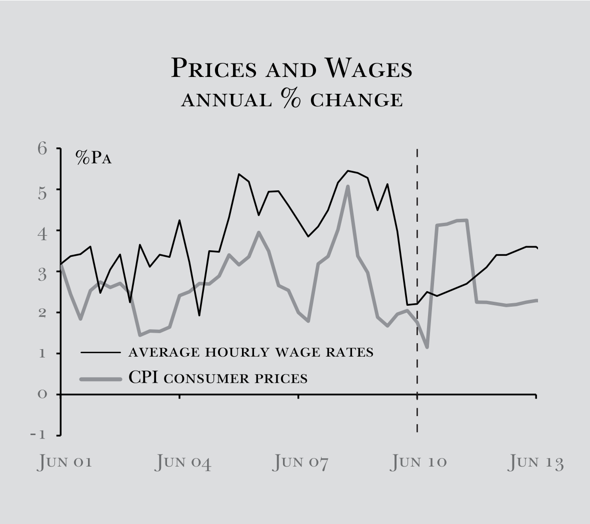
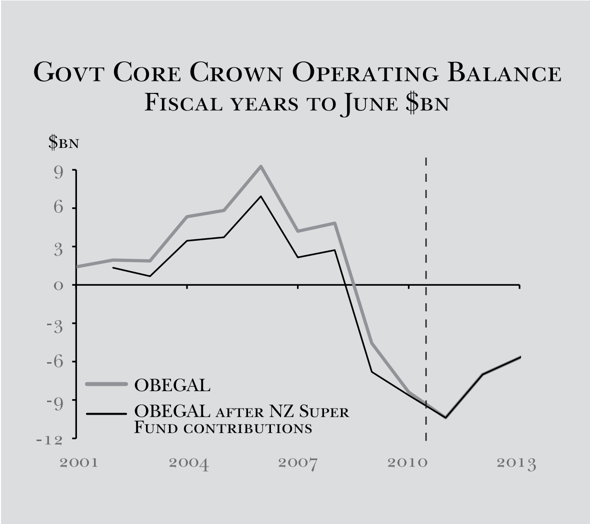
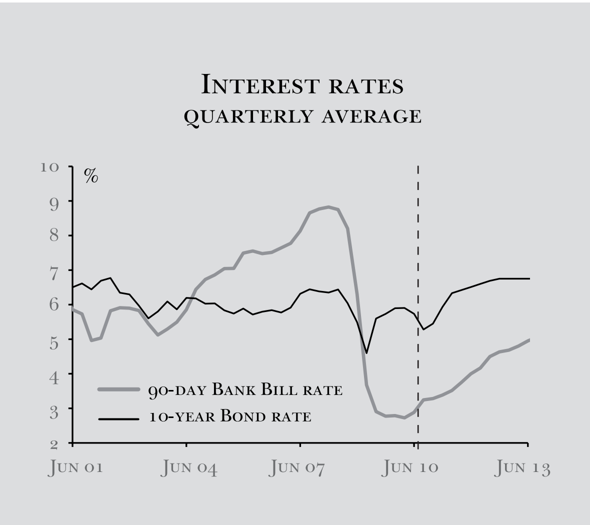
FORECAST SUMMARY

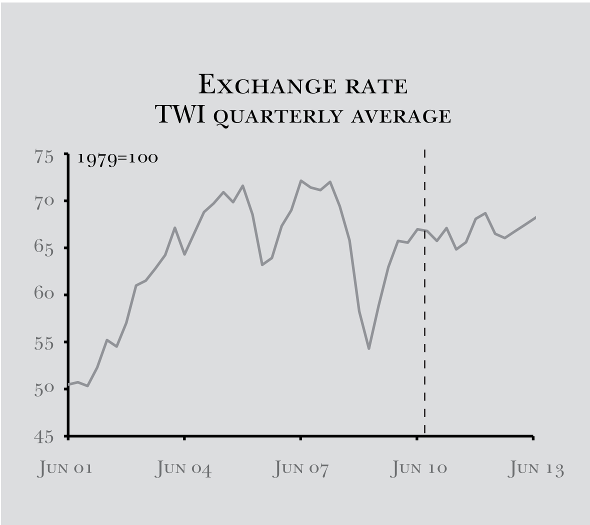












Detailed data tables (annual and quarterly figures) for the numbers and charts in this document are available to subscribers on request.

THE PICTURE

The New Zealand economy is finely perched between gradual, but slow, recovery and a double-dip downturn. The BERL SONZE basket indicates a net balance of zero – with 25 positives and 25 negatives. This is down from the heady heights of +12 recorded earlier this year – reflecting the short-term phantom recovery experienced in late-2009 and early 2010.

We do not forecast a double-dip recession, but caution that the risk of such an outturn is significant. Relevant factors include:

- the parlous state of the New Zealand manufacturing sector and a consequentially sombre employment outlook
- business investment spending missing in action, with credit supply difficulties continuing to impact
- an export recovery contingent on an extremely narrow group of high-performing commodities – but poor performances from large export earners meat and tourism
- an uncertain and volatile global environment
- a government fiscal situation increasingly reliant on optimistic growth projections to halt further deterioration.

On the plus side, the fortunes of the Australian economy remain a solid foundation for short-term growth, with the decline of the NZ$ against the A$ providing welcome news for New Zealand exporters to that market.

Official forecasts are now being revised downwards, acknowledging that the forecast recovery is not going to plan. Consequently, BERL forecasts are now much closer to the 'consensus' than was previously the case.

We expect:

- GDP growth to average 1.6% in the year to March 2011, rising to 2.3% in the following March year.
- Unemployment remaining above 6% until late-2012.
- Non-housing private investment to remain subdued.
- The income tax cut/GST rise package to make little difference to private spending behaviour.
- No further increases in the OCR until March 2011, with the OCR reaching 3.75% by December 2011.
- BoP current account deficit to begin deteriorating as growth gradually picks up.

Key Indicators: Forecast Summary And Comparisons

	2008	2009	2010	2011	2012	2013
Real GDP						
March year average % change						
BERL	2.8	-1.4	*-0.4*	*1.6*	*2.3*	*2.7*
Reserve Bank	2.8	-1.4	*-0.4*	*2.8*	*2.6*	*2.7*
Treasury	3.1	-1.4	*-0.3*	*3.2*	*3.1*	*2.9*
Unemployment rate						
March quarter %						
BERL	3.8	5.1	*6.0*	*6.5*	*6.3*	*5.8*
Reserve Bank	3.9	5.1	*6.0*	*6.0*	*5.5*	*5.3*
Treasury	3.7	5	*7.1*	*6.2*	*5.5*	*5.1*
Current account balance						
March year % of GDP						
BERL	-7.8	-7.9	*-2.4*	*-4.7*	*-6.6*	*-7.3*
Reserve Bank	-7.8	-7.8	*-2.4*	*-3.3*	*-3.6*	*-4.8*
Treasury	-7.8	-7.9	*-2.6*	*-4.4*	*-6.1*	*-7*
Employment FTE Growth						
March year average % of change						
BERL	0.6	0.8	*-1.5*	*0.2*	*1.4*	*1.6*
Reserve Bank	-0.3	0.8	*-0.1*	*1.4*	*2.3*	*2.2*
Treasury	0.8	0.9	*-1.6*	*0.2*	*2*	*2.1*
Export Volume Growth						
March year average % change						
BERL	3.0	-3.3	*2.8*	*1.9*	*3.2*	*3.6*
Reserve Bank	3.0	-3.3	*2.8*	*2.4*	*4.5*	*2.7*
Treasury	2.9	-3.4	*2.8*	*1.6*	*4.7*	*3.5*

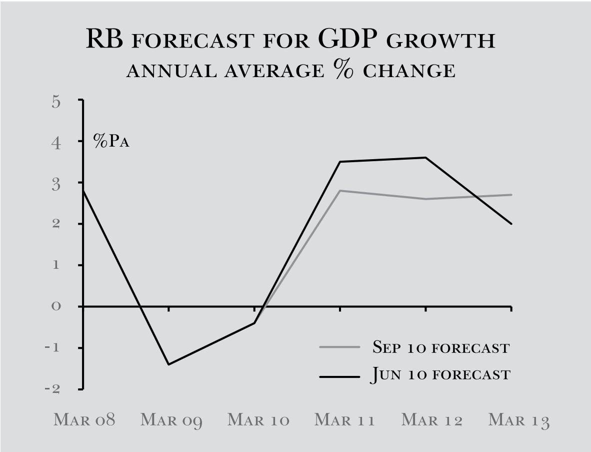
Reserve Bank : Monetary Policy Statement, September 2010
Treasury : Budget Economic and Fiscal Update, May 2010

COMMENTARY compiled by Ganesh Nana

RB REVISION CONFIRMS RECOVERY NOT GOING TO PLAN

The latest assessment of short-term economic prospects from the Reserve Bank (RBNZ) signal a re-think from their earlier forecasts. And the impact of the Canterbury earthquake is only part of the re-think.

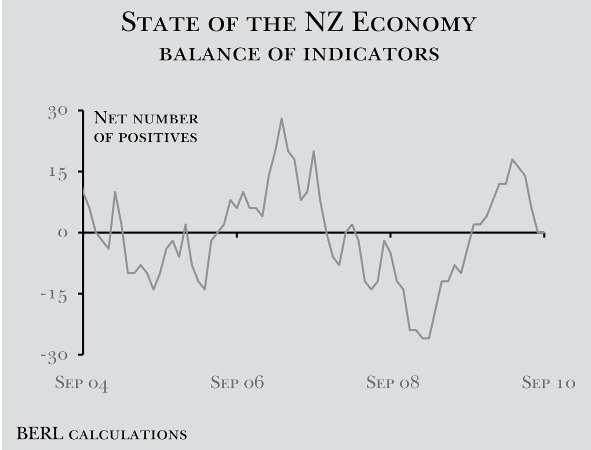
Occupying the minds of the RBNZ's over the past couple of months would have been a steady stream of data suggesting the recovery is not quite as strong as expected. This would apply to both the New Zealand as well as the global economy.



- In particular, the following are relevant:
- a renewed rise in unemployment
- an ongoing slump in manufacturing output
- a continuation of muted retail sales
- a slowing in migration inflows
- an export sector expansion dominated by only a few commodities
- little sign of a pickup in non-residential building consents, or business investment

All these factors (and more) have led the RBNZ to put on hold their planned rises in interest rate. Whereas the plan was for interest rates rising about 200 basis points by the end of next year, the new plan sees this trimmed to 80 basis points. Assuming no change in bank margins, this would put base business interest rates (currently averaging 10.1%) close to 10.9% by the end of 2011.

This revised interest rate track concurs with the RBNZ's now weaker expectations for GDP growth. An average of 2.8% growth is now expected for the year to March 2011 (down from a previously expected 3.5%). And the March 2012 year is now expected to exhibit a similarly modest to 2.6% growth.



CANTERBURY EARTHQUAKES LEAVE LONG-TERM COSTS

The Canterbury earthquakes have left the region's (and New Zealand's) economy significantly worse off. In addition, there are emotional, physical and financial scars. All will take time to heal.

From an economic perspective it is important to separate the short-term impacts, the infrastructure impacts and the longer-term effects on confidence, sentiment and business networks.

The short-term impacts will see a fall in production and spending. With many firms operating at less than full capacity due to building or equipment damage, bottlenecks in receiving supplies, or reduced demand as householders focus their attentions elsewhere, this effect is inevitable.

However, the extent of the short-term loss should not be overstated. With the CBD now re-opened and most other services restored, there is likely to be a quick return to full capacity production.

The spending side of the equation is likely to remain subdued for a bit longer, but emergency measures to support wages of small businesses will help ease this pressure. Similarly, concerted efforts with overseas agents to ensure the realistic story is told abroad (as opposed to some scare stories) should minimise the impact on tourism bookings.

But, the longer-term effects are potentially more damaging. The loss of some operators in the small business sector is inevitable, as the daunting task of rebuilding equipment, location and capacity may be too large for some. Remember also that some in this sector will be faced with repairing family and household losses, as well as rebuilding business structures.

This category applies equally to those in rural areas, facing damage to pasture, fields and farm buildings and equipment.

Many have pointed to the one-off boost to construction and ancillary sectors resulting from the re-building efforts. Rectifying transport, water and sewerage infrastructure will also provide significant work. Again, this boost should not be understated, as we note that the initial cost estimates of damage were quickly doubled over the week following the quake.

This phase of the Canterbury recovery could well take longer than anticipated. It remains a moot point as to whether the NZ construction sector can access sufficient capacity (both equipment and skilled labour) to undertake this task.

On the plus side, a lengthy infrastructure re-building program of activity could give the region's economy the boost to confidence, and so underpin efforts to restore business networks and enterprises.

The principal issue facing the government and the RB at present is their response to the Christchurch earthquake. What should not be done is for government and local authorities to finance programs from domestic source. Such an option would "crowd out" borrowers elsewhere, at a time when the productive sector is already being squeezed.

Instead, the government should rely on RB finance to meet whatever is required over and above that covered by insurance. An alternative is for government to increase its borrowing abroad, but this would result in more foreign debt at a time when foreign indebtedness, albeit private sector, is a major concern.

SELECTED MONTHLY INDICATORS
3 MONTH TOTAL % CHANGE ON SAME PERIOD PREVIOUS YEAR

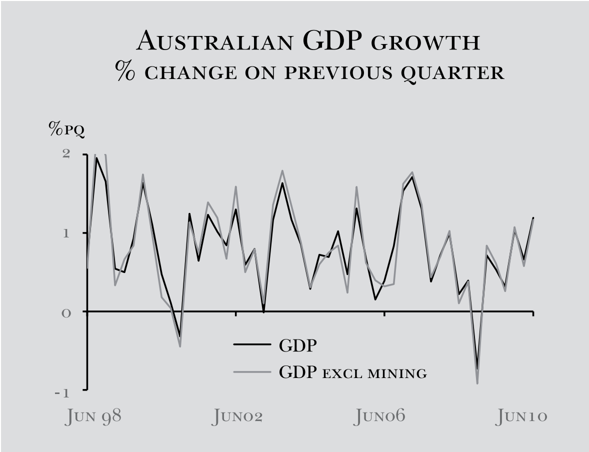
Month	Car registrations	Retail sales (exc mvs)	New dwelling permits	Intermediate imports Excl oil)	Capital imports (plant)	Visitor arrivals	Mach & eqpmt expts	NZBNZ Survey business confidence
Jan 10	6.0	2.0	25.4	-29.3	-27.1	4.1	-11.4	na
Feb 10	14.3	1.1	25.8	-22.0	-25.9	5.2	-1.7	50.1
Mar 10	25.8	1.3	32.3	-18.6	-20.4	5.6	-1.7	42.5
Apr 10	34.3	1.6	35.4	-13.4	-14.5	3.0	-3.5	49.5
May 10	34.0	1.1	27.7	-8.8	-12.5	1.5	1.4	48.2
Jun 10	35.4	0.9	23.5	3.1	-11.9	0.5	9.9	40.2
Jul 10	27.0	0.9	18.4	11.6	-6.3	3.7	14.8	27.9
Aug 10	23.3							16.4

Statistics NZ; NBNZ # net expecting improvement

AUSTRALIA PROVIDES THE POSITIVES

Across the Tasman, the story of Australian economic growth continues with barely a hiccup. Since the last official recession ended in more than 19 year ago, the Australians have put together 73 out of 76 quarters of economic expansion. The latest speed wobble was the recorded fall in the December 2008 quarter. However, the latest numbers suggest that experience is well and truly in the past.

Noticeably, received wisdom by some put a lot of this growth down to Australia's mining sector. But the evidence suggests there is little in this assertion. As the chart shows, the difference in GDP growth, with or without the mining sector is almost negligible.



From the New Zealand perspective, a strongly growing Australian economy is clearly good news. In addition, the decline of the NZ$/A$ cross rate, will be further welcome news for NZ exporters.

FINANCE COMPANY FAILURES LEAVE HOLE IN SMALL BUSINESS SECTOR

The demise of South Canterbury Finance (SCF), along with many other finance companies over the past couple of years, will have significant longer-term repercussions for the New Zealand economy. While many have focussed on the cost to the New Zealand taxpayer, the cost to NZ Inc seems to be overlooked.

The fall of SCF, leaves a large hole in the finance sector. Finance firms provide a key service in the development of New Zealand industry, businesses and the growth of regional economies. The flow of funds to these sectors is critical for long-term investment in and improvement of production and marketing capacity.

Putting aside worries as to their recent activities, the absence of South Canterbury Finance alongside the earlier demise of Allied Nationwide Finance and Hanover Finance (noting the activities of its much earlier incarnation Elders Finance) will be felt.

The restoration of a finance sector that satisfies the demands for investment and working capital from small business and regional sectors is a pre-requisite for the post-recession development of the New Zealand economy.

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	3.2	1.7	-1.4	-1.0	-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	2.7	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

AUSTRALIA

The Australian economy continues to pull ahead, with annualised GDP growth in the June 2010 quarter at 2.3%. GDP in the quarter was up 3.3% on the same quarter a year before.

This growth was caused by strong increases in public investment up 13.2% (on year earlier), dwelling investment up 11.3% and other investment up 4.7%. This suggests that the economy is also gearing up for growth, rather than relying on consumer spending to spur growth. Imports of goods and services were up very strongly, at 17.3%, while exports were up 4.7%. The industries contributing the most to the continued growth and recovery in Australia are the finance and insurance, mining, and health care and social assistance.

Unemployment has remained steady, sitting at 5.3% in July 2010 the same rate as in February 2010. The number of unemployed people is down 29,000 from July last year when the unemployment rate was 5.7%.

For the year ending in July 2010 the value of exports to China, Australia's biggest export market grew by 42.5%, fuelled by China's growing demand for raw materials. There have been increases in the value of exports to Australia's next three top export markets, with exports to Japan growing by 43.3%, South Korea growing 83.4% and India up 4.8%.

Tourism in Australia has been good for the three months to June, with an increase on short-term visitors up 1.4% on a year ago. Among the largest source countries for Australia, the strongest growth has been a 27% rise in visitors from China, a 19% rise in visitors from South Korea and a 2.2% rise in visitors from New Zealand. This is as expected given that the China and to a lesser extent South Korea economy's were less affected by the global recession, while the increase in kiwi visitors continues the trend of holiday's closer to home given the current economic conditions.

AUSTRALIA UNEMPLOYMENT RATE
% OF LABOUR FORCE

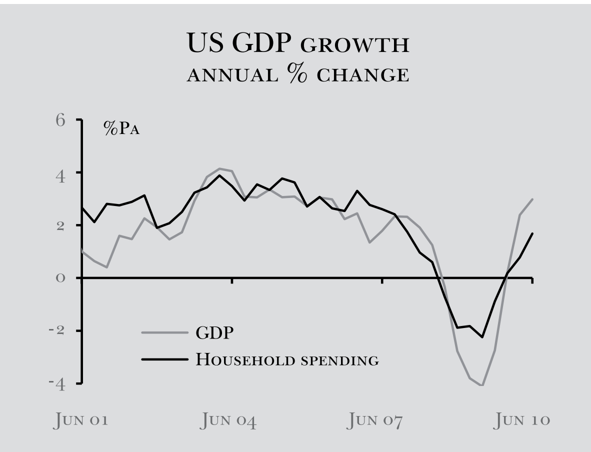
UNITED STATES

The United States economy is still in a slow recovery mode, with average GDP growth at just 0.7% for the year ending June 2010. GDP in the June quarter was up 3.0% over a year ago, which is a positive sign that the economy is recovering. This was the fourth consecutive quarter of growth in GDP for the United States.

Recent growth has been led by private domestic investment, up strongly at 23% increase over the past year (investment in equipment and software was a significant part of this). Also contributing to the improving GDP picture over the past year was a 1.7% increase in private consumption spending, with exports up 14.1% (the fourth consecutive quarter of growth in exports).

President Obama recently announced a proposed package with three measures to help the economy grow. The first measure will allow business to deduct the full cost of investment against their taxes if they make the investment within the next year. The second measure is making research and development tax credits permanent and the third measure is the federal government spending $50 billion on transport infrastructure. If these measures do go ahead it will add to the strong investment spending currently being seen in the United States and could underpin GDP growth over the near term.

In July 2010 the unemployment rate was 9.5%. While this is lower than the 10.1% recorded in October 2009, it is remains significantly higher than the pre-recession July 2008 rate of 5.8%. Overall there is some promise in employment figures with private sector employment adding another 71,000 jobs in July, slightly more than the 20,000 added in June. This increase in private jobs was overshadowed by public sector employment falling 202,000 in July, although most of that fall reflected the ending of temporary census-related jobs.



The Federal Reserve continues to hold interest rates at their current close-to-zero levels and, based on the current economic data, will probably continue to do so until early-2011

ASIA

CHINA

GDP numbers for the June 2010 quarter show Chinese economy expanded year-on-year at a rate of 10.3%. However, the 10.3% growth is lower (by 1.6%-points) that the previous quarter's figure due to industrial production and fixed asset investment slowing. This slowing was in response to a raft of tightening measures to rein in unsustainable growth. Growth in industrial production slowed down to 13.7% in June (on year-earlier levels), down from the 16.5% in May and 17.8% in April. On the other hand, growth on fixed asset investment eased to 25.5% over the first six half of 2010.

Median economic forecasts predict that China's trade surplus topped US$20bn for the third straight month in August. Exports are estimated to have exceeded imports by US$26.9bn, compared with US$15.7bn recorded the previous year. Shipments abroad increased by 35% and imports 27.5%. These increases indicate the China economy continues to steam ahead, and seems to be driven by both external and internal demand factors.

INDIA

Despite some of the world's largest economies having experienced a significant slowdown, there are emerging-market economies that continue to exhibit strong growth. India's economy is one of them with GDP growth of 8.8% for the June quarter (on the previous year), up from 8.6% in the previous quarter. This growth has been assisted by a recovery in agricultural output together with strong development in the industrial and nining sector. Agricultural output was up 2.8% on year-earlier levels mainly because of improved harvest, while there was a 12% rise in industrial production and a 9% surge in mining sector output.

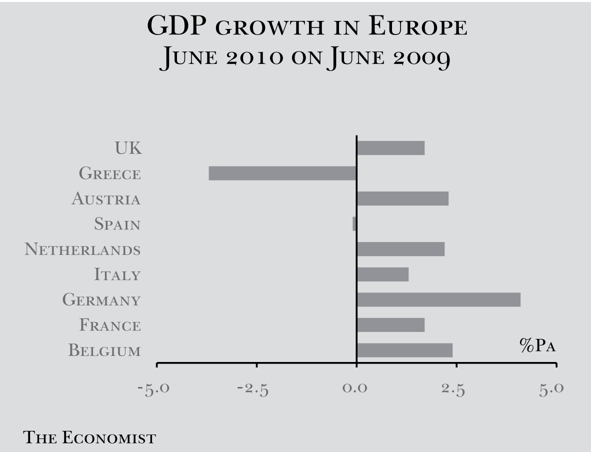
On the other hand, growth in private consumption spending eased to just 0.3% in the June quarter (on year-earlier levels) from 2.6% recorded in the March quarter. Growth in fixed investment spending eased considerably to 3.7% in the latest quarter, from 17.7% in the previous quarter.

JAPAN

Japan now seems to have relinquished its title of '2nd largest economy' to China. Economic growth in Japan slowed sharply in the last quarter. For the period June 2010 quarter, GDP grew by only 0.1%. Japan's GDP in current price terms went down to 0.9% on quarter, or an annualised 3.7%, to ¥118.5 trillion, or US$1.3 trillion, below China's recorded GDP of US$1.4 trillion.

As has been a familiar story, Japan's economy remains hamstrung by households who seem reluctant to spend. This is reinforced by ongoing deflation – as consumer prices in July were 0.9% below year earlier, in addition to the 2.2% decline experienced over the previous year. Further, global imbalances leading to the prospect of a weak US$ over the near term mean the relatively strong ¥ is likely to remain for some time to come.

EUROPE



There are tentative signs of a recovery in Europe, led by Germany and the UK and, to a lesser degree, France. However, there is still significant uncertainty around whether this growth will continue with pressures in other economies Greece, Spain and Portugal remaining. Significant spending cuts announced by the UK government could also have an impact on the recovery in the UK. Economic growth in 2010 s forecast to fall within the 1.4% and 1.7% range.

EUROZONE

Good news out of Europe is that the European Commission expects the Eurozone economy to grow almost twice as fast this year as previously thought. Therefore EU growth will be by 1.7% in 2010 instead of 0.9% forecast in May. And this is definitely an improvement on the 4.1% contraction of the EU economy experienced in 2009. This growth revision is in line with projections by the European Central Bank, which expected growth of between 1.4% and 1.7%.

Interestingly, the Eurozone is outperforming both the US and Japan. The Eurozone grew by 1.0% in the June quarter (quarter on quarter), compared to growth of 0.4% in the US and 0.1% in Japan.

Driving this growth has been the performance of Germany, and the spillover of this performance to other EU countries.

In the June quarter, the German economy grew by 2.2%, an annualised rate of close to 9%. This growth was driven by a combination of exports and investment by firms at home upgrading and expanding their capital stock. Unemployment in Germany has been steadily falling, and is now lower than it was when the crisis began.

Companies with strong ties to Germany, such as Austria and Netherlands, also posted strong growth. However, growth across the Eurozone as a whole is mixed, with countries such as Spain, Portugal and Greece still struggling. In particular, the Greek economy shrank in the latest quarter by 1.5%.

UK

According to the Nationwide Building Society Survey of Consumer Confidence, optimism is returning, with the index of sentiment rising five points in August to 61. The gauge of expectations rose 7 points to 84.

This confidence tends to be supported by the data. The UK economy grew by 1.2% in the second quarter of 2010, the third consecutive quarter of growth and the fastest pace in nine years. This gives growth of 1.7% for the year. Unemployment dropped slightly in the June 2010 quarter, down 0.2%-points to 7.8%.

Inflation, based on the CPI, remains subdued. Consumer price inflation stood unchanged in August at an annual 3.1%. Business investment declined by 1.6% on the quarter, although this remains 1.9% higher than the same period last year.

There is still significant uncertainty around the recovery, with gauges of services, manufacturing and construction falling in August. The recovery in the rest of Europe and the US is tentative at best. At the same time, the Chancellor of the Exchequer has outlined spending cuts and tax increases totalling £113bn. This is likely to put a significant dampener on the fledgling recovery.

LABOUR MARKET CONDITIONS

Labour Market Indicators 000s People						
June quarter	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Full-time employment	1,677	1,652	*1,669*	*1,679*	*1,710*	*1,751*
Part-time employment	507	514	*497*	*503*	*508*	*513*
Total employment	**2,184**	**2,166**	***2,166***	***2,182***	***2,218***	***2,264***
FTE employment growth %	0.6	-1.2	*0.6*	*0.7*	*1.8*	*2.3*
Unemployment	**88**	**134**	***155***	***164***	***164***	***152***
Official unemployment rate %	3.9	5.8	*6.7*	*7.0*	*6.9*	*6.3*
Labour force	**2,272**	**2,300**	***2,321***	***2,346***	***2,381***	***2,416***
Participation rate %	68.2	68.2	*67.8*	*67.9*	*67.9*	*68.1*
Not in labour force	1,059	1,073	*1,100*	*1,116*	*1,125*	*1,134*
Working age population	3,330	3,372	*3,421*	*3,461*	*3,506*	*3,549*

Statistics NZ and BERL calculations *BERL Forecasts*

Our perspective on the labour market is that it is weaker than others are suggesting. The volatility in data series is not helpful here, but looking beneath the headlines suggests a rapid turnaround is not imminent. Consequently, we expect a modest recovery in job numbers over the forecast horizon. Annual job growth should reach 16,000 by mid-2011, before rising gradually to a more respectable 40,000 by end-2012. This sees unemployment stuck uncomfortably close to 7% for the best part on the next couple of years.

As reported in our Monthly Monitor, Household Labour Force Survey (HLFS) for the June quarter provided little comfort to those looking for convincing evidence of a robust recovery taking hold. The quarterly rise in seasonally-adjusted unemployment numbers, along with little growth in employment, confirmed the existence of a 'phantom' recovery.

Headline numbers put employment numbers at the same as this time last year, while those officially unemployed were up 22,000 along with a 2,000 fall in the number in the 'other jobless' category (i.e. those who are jobless but do not meet the official definition of unemployed). A positive sign in the details was the shift from part-time positions to full-time positions – indicating a degree of resilience in the economic situation.

But the industrial composition of the employment change heightens our concerns. In particular, manufacturing employment has plummeted by nearly 20,000 (at a time when we are, allegedly, in the midst of an export-led recovery). Employment in building and construction was recorded as down 3,000 (at a time when, allegedly, there is a concerted effort to upgrade the nation's infrastructure deficit). Reductions in trade and accommodation employment – despite relatively positive visitor and guest night figures – further indicate the fragility of the incipient recovery. And reduced employment in the financial, professional and administrative services reflect subdued business activity in the domestic sector.

These employment reductions are balanced by a promising expansion in the primary (agriculture, forestry and fishing) sector. This is the first time primary sector employment has recorded growth on year earlier since March 2008. However, historical volatility of this particular component means it may be premature to ascribe too much to just one quarter's figure.

But, the largest contribution to holding up job numbers were some remarkable figures for public administration and education – together up by 27,000 on year-earlier levels. These are not one-off numbers, with public administration employment being noticeably higher than year-earlier since June 2009, and education higher since June 2008. The 27,000 number includes an astonishing year-on-year increase in recorded employment in the pre-school and school sector of more than 14,000.

These numbers appear to contradict the message of a public sector subject to significant budgetary constraints. Frankly, we are at a loss to explain (or believe) this figure and reinforces our concern of a fundamental weakness underlying the labour market.

More questions than answers also arise from the figures on the regional dimension. Here the survey data pointed to a decrease in jobs in Auckland by 10,200, compared with year-earlier levels. This is matched by an increase of 9,500 in the number of jobs outside Auckland. The Auckland number is consistent with the decline in manufacturing, while the non-Auckland numbers are more difficult to comprehend. Outside Auckland, the main changes in job numbers were in the Waikato (down 15,800), Otago (up 16,000) and, to a lesser degree, Northland (up 5,300). All other regions each recorded an annual change of less than 3,000.

Permanent And Long-term Migration 000s People						
Year ended June	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
Gross migrant inflow	85.2	88.3	*82.3*	*82.0*	*86.0*	*84.0*
Gross migrant outflow	80.5	75.7	*65.8*	*72.0*	*70.0*	*70.0*
Net migrant inflow	4.7	12.5	*16.5*	*10.0*	*16.0*	*14.0*
Statistics NZ						*BERL Forecasts*

MIGRATION

The net inflow of migrants has eased considerably to an annual rate of 15,000, having been over 22,000 at the start of 2010. This easing has been made up of an acceleration in the net outflow to Australia and a downturn in the net inflow from UK, Europe and the North Americas. There has also been a slight downturn in the net inflow from Asia, but this component has changed to a much lesser degree.

The change in flows across the Tasman is understandable given the performance of the Australian economy compared to that of New Zealand. Job numbers are significant here, with the Australian unemployment rate remaining well below the 6% rate – even during the midst of the global financial crisis.

The easing in the flows from UK and Europe is less understandable given the bleak economic situation in that part of the world. Conventional wisdom would suggest that families and individuals 'stay put' during bleak times and that may be the case for residents of the UK and Europe – although we might expect a growing flow of ex-pats from there arriving back in these shores.

We expect the current situation to see a further easing in migration inflows – dropping to an annual rate of under 10,000 through early 2011. Thereafter, we expect a modest, but gradual, rise towards a moderate 15,000 net annual inflow over the latter-half of the forecast horizon.

MONETARY SITUATION compiled by Allan Catt

MONETARY PRICES Quarter average

Quarter	TWI Jun 1979=100	90 day bank bill rate %	10 yr govt stock yield %	1st mortgage housing rate %	Business lending rate %
Mar 10	65.3	2.73	5.90	6.00	10.01
Jun 10	66.7	2.88	5.73	6.09	10.01
Sep 10	66.5	3.24	5.28	6.38	10.11
Dec 10	65.5	3.28	5.45	6.50	10.10
Mar 11	66.9	3.38	5.93	6.58	10.18
Jun 11	64.5	3.52	6.33	6.75	10.35
Sep 11	65.3	3.75	6.42	7.00	10.60
Dec 11	67.9	4.00	6.51	7.25	10.85
Mar 12	68.5	4.17	6.60	7.42	11.02
Jun 12	66.2	4.50	6.69	7.75	11.35
Sep 12	65.8	4.63	6.75	7.63	11.38
Dec 12	66.5	4.68	6.75	7.68	11.43
Mar 13	67.2	4.80	6.75	7.80	11.55
Jun 13	67.9	4.95	6.75	7.95	11.70

RBNZ BERL Forecasts

The Reserve Bank (RB) decision to leave the Official Cash Rate (OCR) at 3% had been widely expected in light of a weakening economy, worldwide market jitters, and more recently, the Christchurch earthquake and the collapse of South Canterbury Finance. In addition, the Reserve Bank of Australia's (RBA) decision to keep its OCR unchanged made it virtually inevitable

The 90-day rate and the TWI were at 3.21% and 67.5 just before the announcement and, with the Monetary Policy Statement (MPS) showing a more easing stance than expected, the immediate response of markets was to revise both rates downward to 3.17% and 66.7 respectively.

Compared with the June MPS forecast of an increase from 3.3% to 6.1% by March 2013, the revised progression has 4.7% as the March 2013 rate.

Implicit in these figures is a halving of the overall increase in the OCR from 280 points to 140. The rate of increase slows down in the later years but even in the near term – of particular interest to the markets – the next 25-points increase appears unlikely to occur before March 2011. Obviously, these figures should not be taken too literally, but they do reflect a major change in the RB's policy stance.

Interestingly, although their forecasts of GDP growth and inflation are revised downward, the reductions relate more to the current year (now half way through) and are not such as one might think would warrant such a change in stance. Indeed BERL's own forecasts are rather less optimistic.

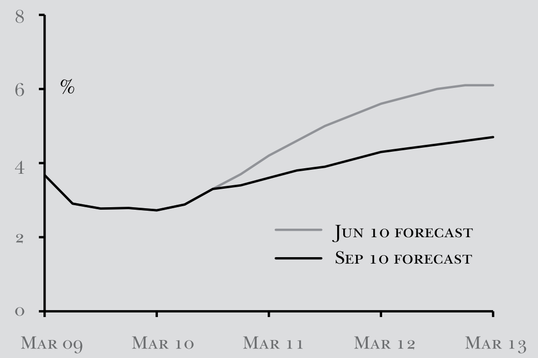
The principal issue facing the government and the RB at present is their response to the Christchurch earthquake. What should not be done is for government and local authorities to finance programs from domestic source. Such an option would "crowd out" borrowers elsewhere, at a time when the productive sector is already being squeezed.

Instead, the government should rely on RB finance to meet whatever is required over and above that covered by insurance. An alternative is for government to increase its borrowing abroad, but this would result in more foreign debt at a time when foreign indebtedness, albeit private sector, is a major concern.

Turning to the international scene, the most important development is the decision by the Japanese authorities on September 15 to resume its intervention in the foreign exchange market. Markets are still digesting the move but already the ¥ has declined by about 3% against the US$, notwithstanding doubts that such interventions can be successful.

The financial sectors and economies of Europe, Britain, the US and Japan are still fragile. It is not only the direct effects on exports that are important, but also the indirect effects on world confidence.

RB forecast for 90-day interest rate
Quarterly Average



INTEREST RATES

The 90-day wholesale rate had been declining ever since the last OCR review and, at 3.21% just before the announcement, it was signaling not just a zero increase this time but for the next as well. With the RB change in stance and the 90-day rate declining on the announcement to 3.17%, these expectations were more than fulfilled.

The level of 5.44% for the 10-year bond the day before the announcement reflected foreign market issues and, possibly, some expectation of increased demand for funds arising out of the earthquake. Thus a rise from 5.06% to the 5.30% level had taken place before the earthquake and the additional rise could reflect an anticipated increased demand for loans. However a decline after the announcement to 5.28% would suggest speculative influences had been the reason.

According to the latest RB data, retail interest rates have not fully responded to the 50-points increase in the OCR since June. Thus the average floating mortgage rate is up by 44 points to 6.45%, the base lending rate by 34 points to 10.35%, and the fixed deposit rate by 16 points to 4.71%. Similarly, we do not expect retail rates to remain unchanged in line with the OCR. Indeed we expect further rises in lending rates as the need for banks to build up capital reserves continues.

An impediment to increased liquidity internationally is the agreement on capital requirements under Basel III reached at a recent meeting of central bankers and regulators. Commercial banks are required to increase capital to a minimum of 8% of liabilities in stages over the period 2013-2018. While the direct effect on our major banks may be minimal because the Australian parent banks already have ratios above this level, we expect our banks to find it more difficult to obtain funds in view of large banks abroad having to respond.

The risks inherent in our already high overseas debt and continued reliance on foreign funding was recently commented upon by a Standard and Poor's executive. Our banks are finding it expensive and difficult enough to obtain funding without an increased risk of a ratings downgrade.

EXCHANGE RATES

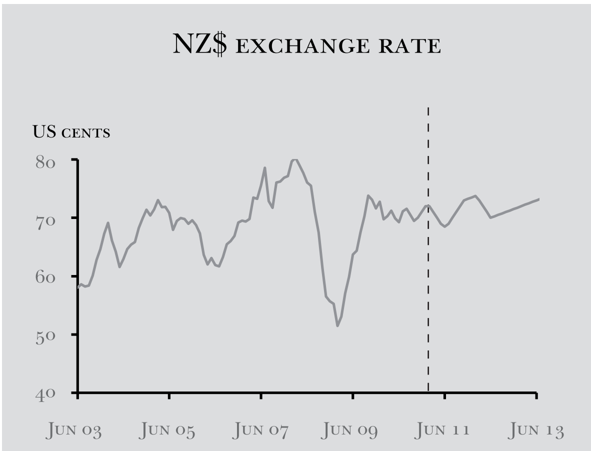
Over the past three months the TWI has fluctuated between 65 and 68 with an average for the period of 67. It was 67.4 immediately before the OCR announcement and the decline to 66.7 reflects an expectation of less OCR action for some time.

On the cross rates, the main feature in the past month has been a weakening of the US$ (and with it the Chinese Yuan) against the £, the ¥ and the A$. We expect this weakening to continue.

A major development is the Japanese authorities' resumption of foreign exchange market intervention. So far the ¥ has weakened against the US$ by about 3%, but ascertaining whether the authorities can prevail in the face of opposition from participants with big pockets requires more time.

Officially, obtaining a competitive advantage is not the objective, but rather to minimize the disadvantage due to speculation. It will be interesting to observe how successful the intervention is in minimizing speculation and, if so, whether it makes much difference to the rate.

The strength of the A$ has been evident throughout the three months and we expect it to continue. Although the RBA chose to hold its OCR unchanged at its last review, we believe continued strong Australian growth and a hint of inflation is likely to cause it to resume tightening next month. Coupled with a holding pattern for the New Zealand OCR, some further decline in the NZ$/$A$ cross-rate could result.



GDP GROWTH compiled by Amapola Generosa

While the dust has finally settled on the recession, a view of where the economy is heading remains clouded.

Many had been expecting that the New Zealand economy would recover strongly, with speedy GDP growth and a rosy future. Unfortunately, this becoming replaced by a much more anaemic outlook for the New Zealand economic growth. Global and domestic economic contraction has taking its toll on the country's growth trend.

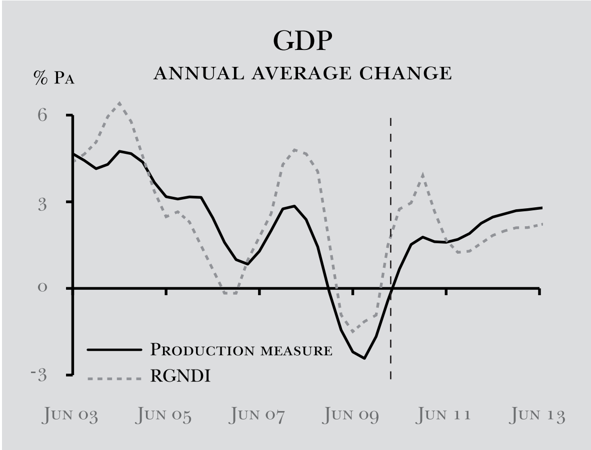
Data showing stagnant employment, subdued household consumption, declining manufacturing, and a weak housing market suggests that New Zealand is struggling to regain any growth momentum. This bring forth a couple of questions: 1) what has driven recent economic growth? and 2) what will keep us nearer to our growth average in 10 years?

Economic activity in the March 2010 quarter was up 0.6%, 1.9% higher than the same quarter a year earlier. It is clear that GDP growth is well above zero, that is the economy has stopped contracting. However, rate and composition of growth leads us to forecast more of a tepid expansion rather than anything that could be described as rosy. Looking closely at the data, we find that the modest growth is due to slowly recovering sectors, matched by rather both private and public sector spending.

Agriculture (up 2.3%) and electricity & utilities (up 3.8%) sectors, both recorded noticeable growth for the year to March 2010. The trade and finance sector is up 4.7%. Several other sectors contracted, including manufacturing (-6.5%) and wholesale trade (-6%). Transport and communication and the retail sectors also had an unimpressive performance.

Activity in the construction sector was recorded as 8.1% down on the same period a year ago. We expect that construction will continue to be negative (or subdued) growth, although a short-term impetus due to the rehabilitation of Christchurch after the recent earthquake is in store.

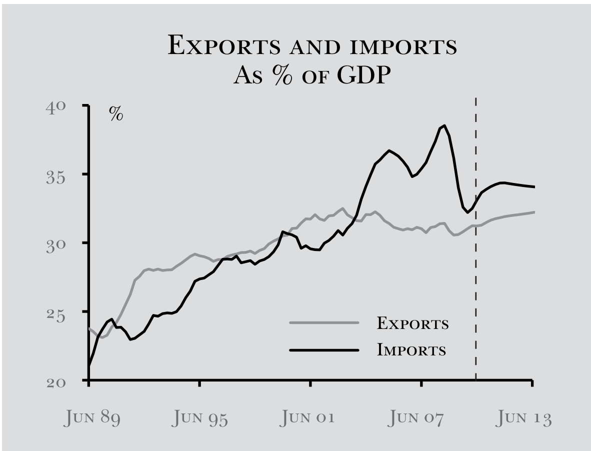
This picture of activity suggests that economic growth is likely to remain mixed. This scenario is exacerbated by prices remaining subdued, falling capital spending, and declining business confidence (a net 16.4% were positive in August 2010 compared to 34.2% a year earlier). Unless we observe an easing of credit availability together with a clearer outlook for business investment spending, domestic activity is unlikely to grow significantly faster. We expect that in the production side, real GDP growth 1.8% at the end of the year, and likely to meander in the 2% to 3% range over the forecast horizon.



On the expenditure side, GDP in March 2010 was 2.5% higher than year earlier. At the headline level, this increase was driven by exports volumes (up by 5.4% on the same quarter 2009), with government and household sector spending helping (up 2.3% and 2.4%, respectively). On the other hand, housing and business investment remains subdued. Construction activity in these sectors declined. Government investment was also down (5.7%) compared to the December 2009 quarter.

Looking beyond the short term, the year to March showed GDP up by 0.5% on the previous year. However, most of this small expansion can be attributed to the fall in import volumes – down 9.6% on the previous year, compared to only a 2.8% increase in export volumes.

Consequently, the import ratio (as a percentage of GDP) has declined dramatically to 32.5%, from a peak of 38.5% for the year to September 2008. The export ratio, however, has remained relatively unchanged at around 31%.



Credit supply in the past year is up in the agricultural sector by 2%, but its growth has been declining over the past months. In the business sector it

GDP EXPENDITURE ANNUAL AVERAGE % CHANGE

Year ended March	2008	2009	2010	2011	2012	2013
Private consumption	3.2	-1.1	*0.5*	*1.6*	*1.6*	*2.4*
Housing investment	4.4	-22.9	*-11.8*	*5.4*	*2.6*	*2.3*
Other investment	11.1	-4.7	*-14.0*	*1.7*	*3.4*	*2.4*
Government investment	-5.6	1.4	*1.9*	*5.8*	*9.1*	*3.5*
Government consumption	4.6	4.2	*1.5*	*0.7*	*0.3*	*1.3*
Gross National Expenditure GNE	4.9	-1.9	*-3.6*	*3.2*	*2.2*	*2.4*
Exports	3.0	-3.3	*2.8*	*3.0*	*3.3*	*3.3*
Imports	9.9	-4.6	*-9.6*	*6.7*	*2.9*	*2.2*
Gross Domestic Product GDP	**2.8**	**-1.3**	***0.5***	***1.7***	***2.3***	***2.7***

Statistics NZ *BERL Forecasts*

has contracted by 8% over the past year. With the inevitable negative effect of this contraction on business investment spending, the outlook for sustained productivity improvements remains bleak.

We forecast New Zealand's economic growth for the next few years to be gradual and fragile. The consensus is more optimistic, closer to 3% in 2010 and 2011. On the contrary, BERL forecasts a less than 2% expansion in the current March year. Along with a seemingly persistent credit constraint (as banks are hampered by low domestic savings and an stubbornly difficult external situation), economic growth will continue to tread wearily.

INFLATION compiled by Jason Leung-Wai

Our expectation is for inflation to remain relatively constrained at under 2%pa. Of course we are looking "through" the 2.5%-points increase in GST, which kicks from October. The GST rise should add around 2.2%-points to annual inflation over the next four quarters. After that, we expect inflationary pressures to ease in at just over 2% out to 2013.

Over the last five quarters, inflation (as measured by the CPI) has been subdued, running at under 2%pa for each of the last five quarters. We expect that the weak (or fragile) global and domestic economy is likely to keep prices down. Activity just isn't there. In particular, the housing market remains subdued, and employment growth is weak.

The following table shows the changes in the inflation indices over the last year and the last quarter. As we can see, there are no upward pressures apart from the input side of the Producers Price Index. And this is being driven by electricity, gas and water, and wholesale trade. Both of these industries have seen large declines in prices over the previous two years. You could argue that the electricity, gas and water industry is fairly volatile anyway, while wholesale trade is coming off some significant contraction in prices.

There are cautions though. GST could have real impacts on prices is if businesses see the rise as an opportunity to mask prices increases of their own. As well, there appears to be some groundswell for increases in the current set of wage negotiations.

The RB is keen to "reduce the stimulus" that its 3% rate is having on the New Zealand economy. However, based on the fragility of the global economy, little sign of any domestic recovery that we can see, and the subdued nature of the various indices, we foresee no reason for any increase in the OCR, at least this year.

CONSUMER PRICES

As noted in the summary, the CPI has been trending at less than 2%pa over the last five quarters, well down on the peak of 5.1% in September 2008. As well the quarter-on-quarter change over the last three quarters have all been small, suggesting even further easing in price pressures.

FOOD PRICE INDEX

The Food Price Index accounts for around a fifth of the CPI index, and it also has been relatively constrained. In fact, it dipped negative on an annual basis for several quarters, which last occurred in 2004.

Further, what has driven the small increase in food prices has been the fruit and vegetables sub-group, which is a volatile grouping being very weather dependant. Hence, you could suggest that underlying food prices are also likely to remain constant for the short-to-medium term.

CAPITAL GOODS PRICE INDEX

The Capital Goods Price Index (CGPI) has actually declined over the last two quarters, which is a pretty good signal that inflationary pressures are non-existent. In the latest quarter, the CGPI was down by 0.6% on the year, compared to a 4.1% increase the previous year.

Pushing the index up was residential building and other construction sub indices, which was offset by falls in the prices of plant machinery and equipment and transport equipment.

PRODUCERS PRICE INDEX

As noted earlier, the PPI is the only index that suggests inflationary pressures exist. In particular, this is on the inputs side of the ledger. However, as noted on the graph, there has been significant easing in the PPI over the last two years.

Inflation indices	Quarterly (monthly) movement	Annual movement
Consumer Price Index June 10 quarter	0.3%, down from 0.4%	1.8%; down from 1.9% previous yr
Capital Goods Price Index June 10 quarter	0.1%; up from -0.1%	-0.6%; down from 4.1% previous yr
Producer Price Index (outputs) Jun 10 quarter	1.1%; down from 1.8%	1.3%; down from 2.1% previous yr
Producer Price Index (inputs) Jun 10 quarter	1.4%; up from 1.3%	2.0%; up from -1.2% previous yr
Labour Cost Index (Salary & Wage) Jun 10 quarter	0.4%; up from 0.3%	1.6%; down from 2.9% previous yr
Food Price Index (monthly)	0.0% (Aug); 1.6% (Jul); 1.3% (Jun); -0.7% (May); -0.5% (Apr);	-0.2%; down from 4.6%; previous yr

Labour Costs And Wage Earnings Annual % Change						
March quarter	**2008**	**2009**	**2010**	**2011**	**2012**	**2013**
All sector salary & wage rates	3.4	3.3	1.5	*1.9*	*2.5*	*2.7*
Avge ordinary hourly earnings	4.5	5.3	2.2	*2.9*	*3.1*	*3.2*
Total weekly earnings	4.0	5.0	2.5	*2.8*	*3.0*	*3.0*

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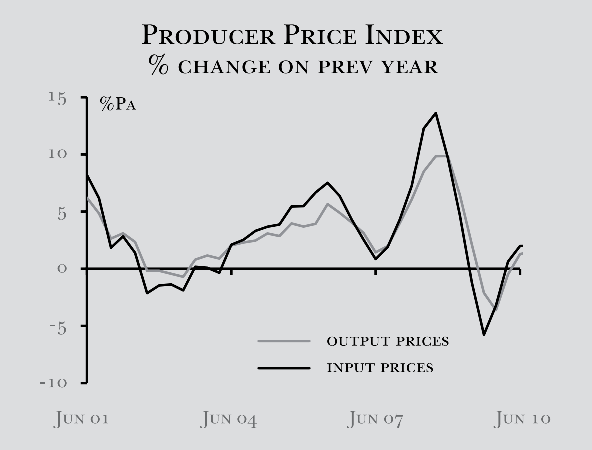


The key industries contributing to the increase in outputs prices were dairy product manufacturing, followed by livestock and cropping farming, wholesale trade, and meat and meat product manufacturing. The rise in dairy product manufacturing was due to higher export prices for whole milk powder, cheese, and butter. Higher cattle and lamb prices are cited for the increase in the livestock and cropping farming index.

On the inputs side, electricity generation and supply rose 7.1% in the year, although this follows a fall of 49.5% the previous year and a rise of 85.4% the year before that. A volatile sector indeed.

LABOUR COST INDEX

Labour costs account for around 16% of employers' total expenditure. Pressure from wages appears subdued, although there does appear to be an air of optimism that wage increases could be back on the table. However, this is forward looking, and the backward evidence suggests that wages are well in check.

In the June 2010 quarter labour costs rose by 0.4%; and by 1.6% on the year. The annual fall in salary and wage rate rises appear to have levelled off in the current quarter, declining from a high of 4.0% in the September 2008 quarter. However, public sector rates continue to fall, while private sector rates have increased in the latest quarter.

GOVERNMENT ACCOUNTS

The government accounts for the 11 months to May show core crown tax revenue up 0.5% on Treasury's earlier Budget forecast. Overall core crown revenue was up 0.4% on the Budget forecast, while core crown expenses were some 1.0% up.

Taking into account remaining items of revenue and spending, the OBEGAL (Operating Balance Before Gains and Losses) stood at a deficit of $4.7bn, compared with the Budget forecast of $5bn. As is normal, monthly figures can be erratic and timing issues (in terms of receipts and payments) can blur the overall picture. Thereafter, the annual accounts can also be influenced by one-off valuation adjustment (although the OBEGAL measure is specifically designed to remove these influences).

Similarly, the costs of the South Canterbury Finance bailout have (theoretically) been incorporated in the Treasury Budget forecasts. Clearly, some of the $1.8bn initial cost will be recouped on the realisation (or sale 'as a going concern') of SCF's assets. However, the timing of such a recouping is unknown. Consequently, the net cost imposition could well remain on the government's books over the short-to-medium term.

Nevertheless, the overall picture of the fiscal accounts remaining in deficit till 2014/15 as forecast in the Budget is unlikely to be altered. However, as we discussed in our Budget commentary, the Treasury forecasts are contingent, to a large degree, on their relatively optimistic forecasts for economic growth.

As we said at the time, should the actual recovery undershoot their growth forecasts there will be an inescapable negative impact on the government's fiscal position. Clearly, noting the realisation of late that the recovery is not quite going to plan, this risk is now considerable. However, we do not expect a wholesale blowout in the Government's deficit. But the likelihood of ongoing deficits beyond 2015 is high. Options should this outcome eventuate include a more assertive attack on levels of government spending (possible, but degree is unknown), and/or an unwinding of the tax cuts just implemented (extremely unlikely). If neither of these options are pursued, then the targeted reduction in government debt will be delayed/deferred.

Whether the deterioration would be sufficient to warrant the attention of the international credit rating agencies is, at this stage, unclear. This, however, underlines the importance of ensuring a sustained recovery in economic activity occurs. And the compounding issues to be faced (again) should economic growth stall further or, worse, a double-dip recession eventuates.

Government Net Revenue And Expenditure $m

Fiscal year ended June	2008	2009	2010	2011	2012	2013
Direct taxation	40,710	38,270	*33,910*	*34,125*	*36,445*	*39,035*
Indirect taxation	16,040	16,410	*16,740*	*19,785*	*21,530*	*22,485*
Miscellaneous	5,070	4,800	*5,755*	*6,350*	*6,490*	*7,010*
Total Revenue	**61,820**	**59,480**	***59,405***	***60,260***	***64,465***	***68,530***
as a % of GDP	34.0	32.2	*29.8*	*30.6*	*31.5*	*32.2*
Social security	17,875	19,380	*21,235*	*22,120*	*22,955*	*23,775*
Health and education	20,850	23,825	*24,915*	*26,035*	*25,940*	*25,930*
General expenditure	15,810	18,370	*16,275*	*19,265*	*18,740*	*20,195*
Debt servicing	2,460	2,460	*2,365*	*3,230*	*3,835*	*4,325*
Total Expenditure	**56,995**	**65,035**	***64,790***	***70,650***	***71,470***	***74,225***
as a % of GDP	31.3	34.7	*34.2*	*35.8*	*35.0*	*34.8*
OBEGAL	**4,825**	**-4,555**	***-8,385***	***-10,390***	***-7,005***	***-5,695***
OBEGAL as a % of GDP	2.6	-2.5	*-4.4*	*-5.3*	*-3.4*	*-2.7*
Pre-funding of NZS	2,105	2,245	*250*	*0*	*0*	*0*
OBEGAL after pre-funding	2,720	-6,800	*-8,635*	*-10,390*	*-7,005*	*-5,695*
Memo: Operating balance	3,890	-5,895	*-5,910*	*-9,080*	*-5,665*	*-4,315*

Statistics NZ — *BERL Forecasts*

MANUFACTURING

Whichever way you cut it, the manufacturing sector remains in the doldrums. Real activity (as measured by inflation-adjusted sales volumes from Statistics New Zealand) in the year to June were an average 2.3% lower than in the previous year. Excluding meat and dairy processing sub-sectors, activity was down 4%.

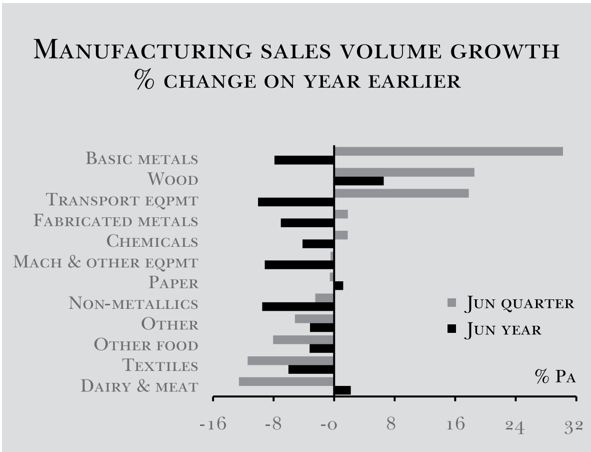
The latest Performance of Manufacturing Index (PMI) reflects the recent reversal of fortunes of the wider economy. Earlier positive indicators have been replaced with much more reserved figures. The average PMI for the three months to July is around 52, much closer to the 50 level (representing the divider between contraction and expansion) than earlier this year. On the regional dimension, only the Central region has a PMI 3-month average above 50 (at 56), with Northern, Canterbury and Otago regions all appearing to be in contraction according to this measure.

The Canterbury earthquake will have an impact on the numbers for September and October. The extent of this impact remains unknown, as is whether the impact is successfully limited to a short-term influence only.

Taking the latest quarter alone, total activity according to Statistics New Zealand was 3.7% below year-earlier levels, although excluding meat and dairy processing the activity was 0.8% up. However, numbers for the latest quarter indicate some erratic changes (with double-digit declines in the dairy & meat processing, and textiles sub-sectors, and double-digit increases in basic metals, wood and transport equipment sub-sectors). This leads us to encourage caution in relying on the short-term numbers.

However, the longer-term trends are incontrovertible. Activity in manufacturing for the year to June was only 1.7% up on that of a decade ago. And note, that is not 1.7% per annum, but 1.7% in total growth over the past ten years. Moreover, excluding dairy and meat processing, the remainder of the manufacturing sector has shrunk – it is now 7.5% smaller than it was in the year to June 2000. Within this figure is: a 30% contraction in the textiles sub-sector;, a static wood-processing sub-sector; a 2.5% decline in paper product manufacturing; a 27.5% less activity in basic metal industries; a 17.5% decline in structural, sheet and fabricated metal product manufacturing; a 3.5% fall in transport equipment manufacturing; and 2.5% decline in machinery and equipment manufacturing. Not a pretty story.

On the bright side, the exchange rate with Australia is now at an extremely attractive level for exporters into that market. Whether the remnants of the manufacturing sector are have the capability (or capacity) to benefit from this competitive position is arguable, if not academic.



BUILDING AND CONSTRUCTION

Much has been noted about the 'boost' to construction activity that will be provided by the need to re-build houses in Canterbury, as well as the region's infrastructure. Of course, there is argument as to whether this is a 'real' economic gain, as opposed to activity aimed at replacing lost assets. Undoubtedly, the earthquake destroyed wealth and, consequently, the region (and New Zealand) is worse off across all economic, social, community, and emotional dimensions.

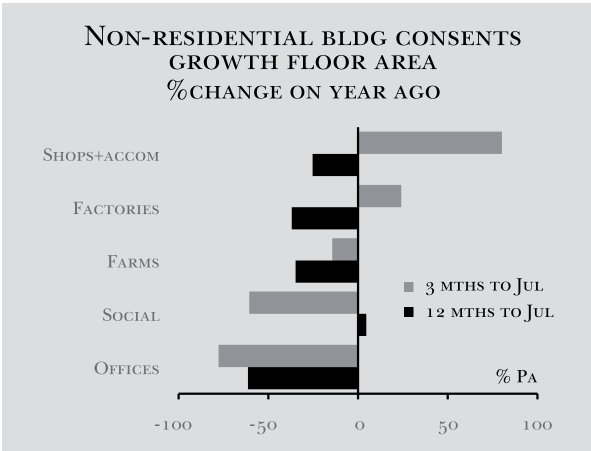
Equally without doubt, however, economic activity in the construction sector in terms of jobs and income generated over the short-to-medium term will be higher than otherwise would have been the case. Whether this boost provides the catalyst to not only replace lost assets, but to upgrade and renew assets remains to be answered. If this does accelerate the infrastructure investment program, without diverting investment effort from other sectors or regions, then there is potential long-term economic gain. From today's perspective however, this would seem an academic argument.

Of significantly more immediate importance is questions about the capacity of the building sector to cope with a re-construction program of this magnitude. While the house building sector has been operating at well below previous capacity over the past couple of years, there is the concern that that previous capacity has since migrated abroad. Similarly, the non-residential sector has also been subdued of late, although the national infrastructure program has provided a welcome fillip.

Latest numbers show residential consents climbed back to an annual rate of over 16,000, having reached a low of 13,600 in the year to September 2009. Of course, this remains well below the 25,000 considered to be the level for sustainable industry development, and that approximately necessary to meet demand arising from population growth. Given the easing of net migration inflows, along with ongoing modest employment and income growth, suggests a gradual increase in house building activity is on the cards. Consequently, we forecast a return to an annual rate of 20,000 consents by end-2011; and rising further to over 22,000 a year later.

As to non-residential activity, the year to July recorded consents by floor area some 31% below those of the previous year, while the latest three months had consents 27% below year-earlier levels. These numbers speak for themselves.

Within this sector, the largest declines are in the office buildings sub-sector with the latest three months 78% below year-earlier, and the latest year 61% down. For the year to July, the shops and accommodation, factories and farm buildings sub-sector were each more than 25% down. There is one positive short-term figure, with a large increase in shops and accommodation building consents in the latest three months. However, this figure should be read with caution given the erratic nature of this series. The longer-term figures are always more informative.



TOURISM compiled by Nathaniel Robson

Indicators on the health of the tourism sector tell somewhat conflicting stories. On the positive side, the sector achieved in June the milestone of an annual 2.5m visitor arrivals. On the downside, the average visitor in 2010 is spending considerably less than their counterpart in 2009. While visitor numbers are growing, the structure of tourism demand has shifted away from the high value holiday visitor that New Zealand successfully attracted in the 1990s.

New Zealand's hosting of the Rugby World Cup (RWC) will provide a welcome boost to tourism expenditure receipts, but beyond 2011 prospects for the sector are less clear. It took roughly eight years for visitor arrivals to grow from an annual 2m to 2.5m, but prior to that it only took four years to go from 1.5m to 2m. The recent lacklustre performance can be partly attributed to the financial crisis and ensuing recession, the influenza pandemic, and unfavourable exchange rates. The question is, beyond the 2011 RWC, will growth revert to that seen in the 1990s, or will it continue to be sluggish, reflecting perhaps that the tourism market has matured? We optimistically look to something in between.

International visitors
annual totals

Statistics NZ

Our assessment of the short-term prospects for the tourism sector is gradual improvement leading into 2011, with visitor numbers growth holding at a minimum of 4%pa for the 2010 calendar year and expenditure growth turning positive in the high season. Effects of the Canterbury earthquake on the sector are likely to be small and transitory. Some international visitors may be diverted away from Christchurch (with a flow-on effect to Queenstown) for the next few months.

The total number of holiday tourists grew 4.8% in the year to July 2010 compared to the previous July year. The comparable figure for visiting friends and relatives (VFR) tourism was 3.4%. At the same time however, overall expenditure per visitor fell 7% for each market segment.

Looking at the trends in the source composition of visitor arrivals reveals a key driver behind the fall in tourism expenditure. The majority of the growth in visitor arrivals is attributed to expansion in the Australian segment of the market. Australian residents account for 39% and 52% respectively of our holiday and VFR arrivals, and these segments grew on average 14.8% and 6.2% over the past year. Growth in visitors from our next two most important source countries, the UK and the USA, has been weak for VFR-type and negative for holiday-type visitors. The typical Australian visitor spends $1,700 during their visit: $2,400 by holiday tourists and $1,100 by VFR tourists, reflecting the fact that this latter group usually stays in private rather than commercial accommodation. In comparison, the average visitor from the UK and USA each spends around $3,000.

A promising sign has been the turnaround in visitor numbers from Asian sources. These had been declining since late 2008 in the case of China and mid-2005 for Japan, but have now turned positive. The typical holiday tourist from each of these countries spends $3,200 and $3,700 respectively during their visit.

A difficulty however is that the composition of visitor arrivals is not solely to blame for the depression in tourism expenditure. Of our top five sources, only visitors from China are spending more this year compared to last. The visitor spend by the average holiday tourist from China was 20% up in the year to July 2010, while comparable figures for the other sources were -0.3% (Australia), -6% (UK), -17% (USA), -22% (Japan). The Asian rebound being sustained and an improvement in Australian average spending leading into the high season would see the tourism expenditure indicators turn positive.

Guest nights growth
% change on year ago

Figures for commercial accommodation guest nights show that while overall tourism expenditure has been depressed, different regions and accommodation types have had quite different experiences over the last quarter. Overall guest nights in the June 2010 quarter were only 0.2% up on year earlier. However, Auckland and Queenstown had successful quarters with guest nights up 6% and 11%, respectively, while the other main tourist destinations suffered.

Interestingly, the only accommodation type to see improvement is hotels, which saw growth of 6.5%, while motels, backpackers, and holiday parks sold fewer guest nights. This seems inconsistent with the notion that holiday tourists are spending less on average, because the primary way to reduce expenditure would be to decrease the length of stay. The suggestion therefore is that tourists are cutting back on the other components of their travel costs.

Source country	% change (year to July 2010)		
	Total	Holiday	VFR
Australia	9.5	14.8	6.2
UK	-5.6	-10.0	0.3
USA	-2.0	-47	3.0
China	4.0	0.9	17.9
Japan	3.5	2.0	5.5
Germany	2.8	1.0	8.5
Korea	5.7	7.8	2.7
Canada	-2.2	-3.3	0.0
TOTAL	**4.0**	**4.8**	**3.4**

RETAIL TRADE

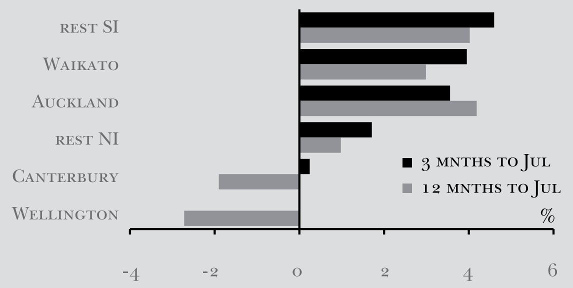
The retail sector is experiencing a prolonged period of little growth. Volumes for the year to June were 0.1% up on the previous year, although there was slightly higher growth of 1.2% if motor vehicles and related sectors are excluded. These figures are, however, than the previous 18 months where sales volumes were declining.

Amongst the components of retail industry, we note the core non-supermarket food and department store sectors as being hardest hit. These, along with the motor vehicles and related sector, have experienced the largest declines in terms of sales volumes over the past year.

In value terms, the growth in sales is similarly modest with only a 1.8% rise over the latest year, with the latest months being 2.5% up on year-earlier levels.

Across the regions, the latest figures are consistent in indicating Wellington and Canterbury as faring the worst. Sales turnover in these two areas were down 2% to 3% on the year, with the latest three months being flat on year-earlier levels. Clearly, the Canterbury figures will take even further time to recover following the earthquake. And the Wellington figures are likely to remain subdued as further rounds of public sector re-organisations add to the uncertain environment.

RETAIL SALES GROWTH
% CHGE ON YEAR AGO



RETAIL SALES
% CHANGE ON PREVIOUS YEAR

Quarter	VOLUME Total	VOLUME Excl motor vehicles	VALUES Total	VALUES Excl motor vehicles
Sep 09	-4.0	-0.9	-1.0	2.7
Dec 09	-2.9	-0.1	1.4	2.4
Mar 10	-0.8	1.3	3.0	1.3
Jun 10	0.5	1.3	1.5	2.0
Sep 10	*1.0*	*1.8*	*2.5*	*2.7*
Dec 10	*0.2*	*0.3*	*1.0*	*1.2*
Mar 11	*0.6*	*0.8*	*1.7*	*2.3*
Jun 11	*1.0*	*1.4*	*1.9*	*2.5*
Sep 11	*1.3*	*1.5*	*1.9*	*2.6*
Dec 11	*1.5*	*2.0*	*2.8*	*3.5*
Mar 12	*1.6*	*2.1*	*3.2*	*4.0*
Jun 12	*1.8*	*2.3*	*3.5*	*4.1*

Statistics NZ | *BERL Forecasts*

Meanwhile annual sales turnover growth of 3% to 4% in Auckland, Waikato and non-Canterbury South Island, indicate these regions are perhaps past the worst for the current cycle. However, growth will continue in a subdued, rather than accelerated, manner.

Indications are that the tax cut/gst rise package will do little short-term impact on retail trade. Ongoing muted employment and income growth, accompanied by continued uncertainty and confidence issues emanating from abroad, suggests the average household will keep a tight grasp of their wallets.

AGRICULTURE compiled by Michael Webster

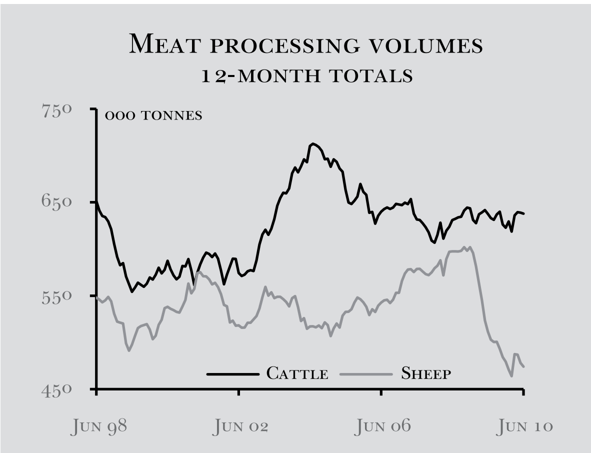
Reports from the agriculture sector are not overly enthusiastic.

MEAT AND WOOL

The newly rebranded Beef + Lamb New Zealand hedges its bets regarding estimated returns for the 2010-2011 season in their latest New Season Outlook. Again, the reason is the ever-volatile exchange rate situation, which continues to defy prediction, let alone economic fundamentals. Even in the relatively narrow band of 68 to 72 US cents, Beef + Lamb's estimated profits for farms changes from an average $54,000 per farm to $34,000 per farm. When considering that most farms have assets well into the millions, then even the more optimistic estimates do not provide particularly attractive returns on investment.

Clearly this is a primary reason why dairy farming is seen with envious eyes, comparatively speaking. Without doubt, the plight of the average sheep and beef farm is a key concern for the long-term future of one of our biggest export earners.

Meat volumes remain low, with exports falling 3.1% for the July 2010 year. Consequently, meat export values have declined 8.2%.



Slaughtering volumes are also weak, with sheep processing down 11.1% for the June 2010 year, though beef cattle slaughter has increased marginally, up 0.9%. Actual sheep stock number were up, increasing 2.5% to 33.2m in June 2010, due to farmers continuing to rebuild stock by retaining hoggets. Beef cattle numbers fell in the same period, down 1.3% to 3.9m, partly due to poor profitability forcing farmers to change to different land uses.

Beef + Lamb are moderately optimistic in regards to export markets, stating that while Europe and the US are sluggish, the emerging markets of Middle East, China and Russia are all showing strong demand. This may hold prices up over the 2010/11 season, but volumes will remain muted due to limited supply.

For the June 2011 year, we project an overall increase of volumes of 1.0%, coupled with a slight fall in prices, down 0.5%.

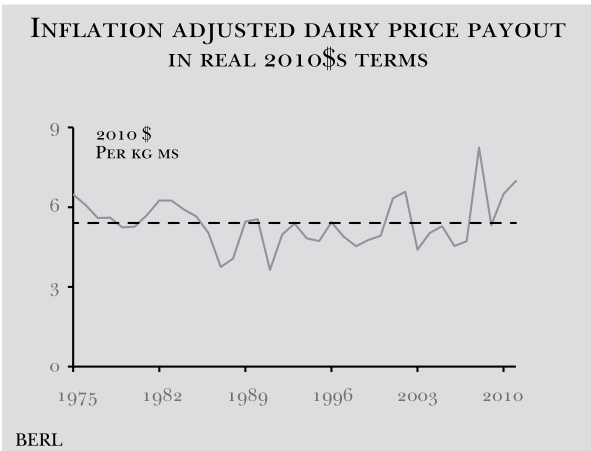
The failed South Canterbury finance will have some effect on farmers, as it was a source of funds for farming investment. This could make it harder for farmers to borrow money, at least in the short term.

The Otago Daily Times reported of a potential buyout of the cooperative Wool Grower Holdings, by two large meat producers – Alliance and Silver Fern Farms. Alliance Chairman Owen Poole said, "We've got an open mind because we are anxious for farmers to have an alternative positive income stream to support the meat side of their business". Certainly something must be done to make wool production profitable – perhaps investment by these heavy-hitters could help things along. Wait and see on this one.

For the year to June 2010, wool prices have fallen 7.3%, while volumes have increased 3.0%.

DAIRY

Renewed optimism about world demand, as signalled by the latest auctions, has led to a confirmation of the Fonterra's forecast dairy price payout. But it wasn't that long ago that a downwards revision of the forecast was seen as inevitable. The uncertainty as to global economic conditions, along with exchange rate considerations, form the background to this volatility.



August auctions showed falls of 13.9% and 8.3% in average prices. However, the latest auction in early September showed an increase in price of around 16.9%. Fonterra tentatively suggests that the market is signaling a "firmer tone".

While prices seem volatile, export volumes seem to be holding up well. Dairy tonnages reached a record high at 2.1m tonnes of product for the July 2010 year. Fonterra CEO Ferrier said that consistent demand allowed Fonterra to finish the financial year with tight inventories. He highlighted China specifically and Asia in general as the main positive influences.

For the July 2010 year, dairy volumes were up 11.7% and prices were up 0.6%. We expect that volume growth will slow, to around 3.0% for the June 2011 year, while prices will increase at a similar rate, around 1.0% for the year.

HORTICULTURE

KIWIFRUIT
Zespri's August forecast paints a mixed picture for kiwifruit at this early stage of the season.

CEO Lain Jager attributes poor pollination, along with the "very dry New Zealand summer", to lower volumes of kiwifruit that are smaller in size than last season's bumper harvest. However, Jager sees an upside – that dry conditions have improved the flavour of the fruit – which he says with translate into high returns per tray, "especially in taste-sensitive markets". Zespri projects an increase of 35c per tray for green kiwifruit, and 34c for gold, on last season. This increase comes despite a significant increase in freight (fuel) costs over the period.

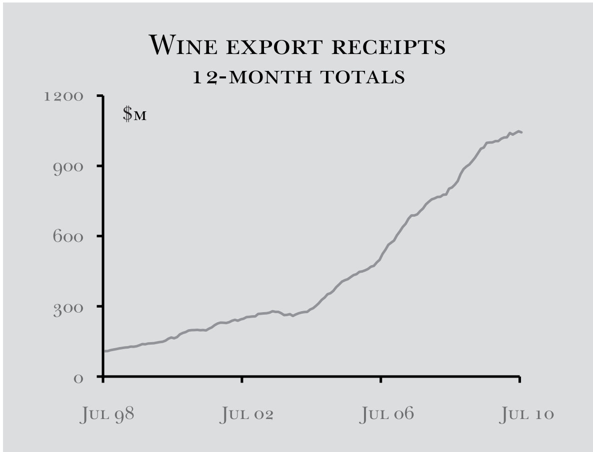
The general feeling is that the industry is doing relatively well in a bleak environment. However, we expect lower volumes of fruit, and this may translate to an overall reduction of kiwifruit receipts this season. We may not be able to rely on kiwifruit as the saving grace of the agriculture sector this time around. The projection for the June 2011 year is small change in price (up 2%) and an increase in quantity of 5%.

APPLES
We are not getting the most cheerful data around apples, this quarter. With weak demand in our key apple markets of US and the UK, both volumes and prices have fallen. Apple prices in July 2010 were 6.6% lower, and quantities down 14.6%, at a point where the majority of apples have been exported for the season. This was largely due to the fall in FOB values of our key export varieties: Braeburn was down a third compared with the previous year, while our biggest export variety Royal Gala was down 18%.

The relatively new variety Jazz continues to impress its market in Europe, with a 21% increase in volumes for the year, though prices remained unchanged.

Looking forward to the year to June 2011, we expect apple values to increase by 4.5% to around $339m. This projected value will be significantly lower than that seen at the previous peak of apple export values in mid-2009, when it reached over $400m.

On the good news front – a WTO ruling declaring Australia's regulations around the import of New Zealand apples illegal. However, the Australian Government looks set to appeal the judgment, so we will have to wait and see on this front. Even if they lose their appeal, Pipfruit NZ CEO Peter Beaven says that it would take until 2012 to get the Aussie export market operational.



WINE
The long predicted glut of wine exports on the international market is eroding prices in the sector. A survey done by the NZ Winegrowers Association confirmed this, showing that 2010 Marlborough Sauvignon Blanc was selling at 26% lower prices than the previous year's vintage. In contrast, Marlborough Pinot Noir has held its price over the same period.

Annual wine exports still remain over $1bn in the latest figures. In the June 2010 year, wine exports increased 4.7%, up to $1.02bn.

The 2010 vintage is estimated as being 266,000 tonnes, around 7% down from the previous year. Therefore we expect a dampening in export volumes for the June 2011 year. Coupled with weak prices, we could see lower export values for the coming season.

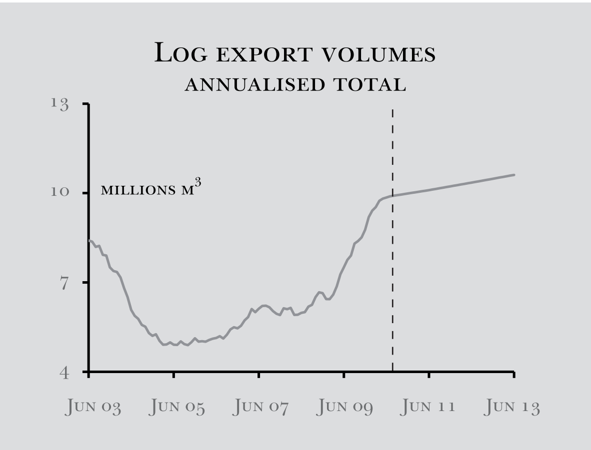
FORESTRY compiled by Wilma Molano

Logs, wood and wood products recorded the third largest increase in exports for the July month, up $49m (24 percent) on year earlier. Based on International Forest Industries, China is still the number one importer of logs, but demand from US and Canada is also beginning to grow again. For the three months to July 2010 export receipts were $160 million (26%) up on year-earlier.

LOGS

Log export volumes increased by 27.5% in the year to July and were up by 5.9% for the three months to July, compared to the same period last year. Similarly, a positive picture is painted by export values – with an increase of 34% for the year to July and 17% (on year-earlier) for the three months to July. While the rate of growth of forestry exports is declining, they remain amongst the leading lights of the overall export performance.

BERL forecasts for logs remains bright. We expect log export volumes and receipts to continue growing, especially to China, which is the number one log export destination.



TIMBER

Timber export volumes for the year to July were up 9.3%, with the latest three months being 5.5% up on year-earlier levels. Consequently, export revenues for the year are up over 10%, an increase of 29% for the three months to July compared with year earlier. Notably, the rate of growth of timber export receipts are increasing, partly due to robust growth in demand from Australia.

BERL forecasts for timber continues a modestly positive trend for export volumes and receipts. Clearly, there is a possibility of a noticeable improvement on this picture when the US economy generally, and building industry in particular, recover.

PULP

Export volumes for pulp for the year to July were a moderate 5.5% up on a year ago. But exports for the latest three months were an astonishing 48.6% up on year earlier. This has led to a remarkable 86% increase in export receipts over the latest three months compared, to the same period last year. These are promising signs from a sector that has been operating at very low levels since the mid-2000s.

EXTERNAL SECTOR compiled by Amapola Generosa

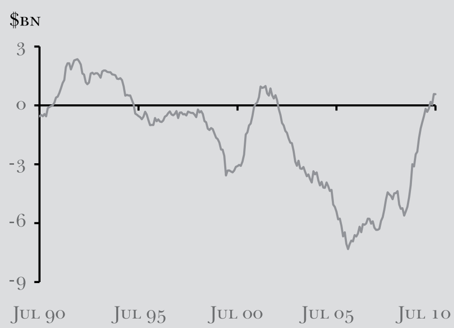
Latest figures point to a continuation of a slow and patchy performance by the New Zealand external sector.

Merchandise export trade totalled $41bn in the year to July. This is still 4% below that of the year earlier, but is now back above the total for the July 2008 year. Clearly the numbers are improving, with the three month to July 2010 showing merchandise receipts over 11% up on year-earlier levels. This growth is driven primarily by dairy exports. The country's export to its major trading partners: Australia, China, and South Korea.

On the import side, the merchandise payments total of $40.5bn for the year to July were 10.5% below those of the previous year. But, import figures are picking up with the latest three months being nearly 8% above year-earlier levels. The recent rise in import has been has been mostly in intermediate goods-chemicals and fertilisers as well as fuel and lubricants – up by 16% in July.

However, imports of capital goods (plant and machinery category) fell 6.8%. This is consistent with the decline in business sector investment.

MERCHANDISE TRADE BALANCE
ANNUALISED



STATISTICS NZ

On the plus side, the report of a $176m current account surplus for the March 2010 quarter is welcome news. This is the first positive result since second quarter of 2009. This surplus was helped by a $989m fall in the investment income deficit, relative to the December 2009 quarter.

In annualised terms, the current account deficit of $4.5bn (representing 2.4% of annual GDP) is a marked improvements on the $14.6bn deficit recorded a year earlier. However, as we have noted before, the fact that much of this improvement is attributable to a reduction in imports – as opposed to earning more export income – suggests that this improvement is more transitory than sustainable.

Recall that our current account position has fluctuated in a range of 4% to 8% of GDP over the previous five years. The export industry has not been able to gain enough momentum to catapult our growth an payments situation into a sustainable position. This is even more sobering when one notes that at the same time NZ has been experiencing a considerable improvement in our terms of trade.

BERL forecasts an export expansion at a slower pace than that expected by the Treasury and the Reserve Bank. The sector is expected to grow 4% this quarter. The current account deficit is expected to remain a thorny problem, despite a gradual rebalancing from domestic to external sector activity.

Of course, given the current account BOP position and international investment position, we should be expecting a much weaker NZ$. The fact that a currency decline does not appear imminent suggests the market mechanism on which we rely on remains somewhat faulty.

In summary, the New Zealand current account deficit has improved due to cyclical forces. This deficit is likely to widen as the New Zealand economy recovers into a growth phase. But, the much-mooted re-balancing of the New Zealand economy will require the external sector to contribute much more – that is, less spending on imports, increase income from exports, and more savings from the public and private sectors. And more. Much relies on a strong export sector, which would no doubt be helped by a stable and competitive value for the NZ$.

Merchandise Export Receipts $m

Year ended June	2008	2009	2010	2011	2012	2013
Dairy	8,756	8,970	8,834	*9,187*	*9,463*	*9,747*
Meat	4,777	5,665	5,197	*5,223*	*5,275*	*5,354*
Wool	628	579	553	*553*	*553*	*553*
Fish	1,230	1,405	1,348	*1,368*	*1,396*	*1,423*
Horticulture	2,000	2,258	2,147	*2,190*	*2,269*	*2,355*
Alcohol	863	1,049	1,120	*1,165*	*1,207*	*1,252*
Forestry products	3,424	3,757	4,072	*4,276*	*4,412*	*4,562*
Aluminium	1,373	1,024	985	*1,084*	*1,111*	*1,138*
Machinery & transport eqpmt	2,920	2,823	2,559	*2,636*	*2,728*	*2,824*
Petroleum	2,633	2,148	2,279	*2,439*	*2,512*	*2,587*
Other	9,480	10,950	9,550	*9,836*	*10,131*	*10,46*
Exports of Goods (fob)	**38,085**	**40,627**	**38,645**	***39,947***	***41,058***	***42,265***
% change	15.2	6.7	-4.9	*3.4*	*2.8*	*2.9*
as a % of GDP	20.9	22.0	20.4	*20.3*	*20.1*	*20.7*

Statistics NZ *BERL Forecasts*

Merchandise Import Payments $m

Year ended June	2008	2009	2010	2011	2012	2013
Food	3,321	3,801	3,559	*3,701*	*3,849*	*3,984*
Petrol & petroleum products	6,674	6,711	6,159	*6,652*	*6,984*	*7,299*
Non-electrical machinery	5,580	5,512	4,580	*4,740*	*4,883*	*5,029*
Electrical machinery	3,634	4,209	3,381	*3,499*	*3,622*	*3,749*
Transport equipment	6,395	5,271	4,669	*4,949*	*5,098*	*5,276*
Plastics	1,497	1,561	1,450	*1,494*	*1,531*	*1,577*
Textiles, clothing & footwear	2,113	2,314	2,127	*2,191*	*2,248*	*2,326*
Other	12,710	14,058	12,023	*13,051*	*14,016*	*14,683*
Imports of Goods (cif)	**41,924**	**43,437**	**37,948**	***40,277***	***42,230***	***43,923***
% change	8.4	3.6	-12.6	*6.1*	*4.8*	*4.0*
as a % of GDP	23.0	23.5	20.0	*20.4*	*20.7*	*21.5*

Statistics NZ *BERL Forecasts*

Balance Of Payments On Current Account $m

Year ended June	2008	2009	2010	2011	2012	2013
OT trade balance (fob-cif)	-3,839	-2,810	*697*	*-320*	*-1,172*	*-1,657*
BoP conceptual adjustments	1,936	3,338	*2,562*	*2,400*	*2,400*	*2,400*
BoP merchandise trade balance	-1,903	528	*3,259*	*2,080*	*1,228*	*743*
Services exports	12,889	12,432	*11,861*	*12,176*	*12,577*	*12,891*
Services imports	13,006	13,401	*11,985*	*12,300*	*12,762*	*13,145*
Services balance	-118	-970	*-123*	*-123*	*-185*	*-254*
Balance on goods and services	-2,021	-442	*3,136*	*1,957*	*1,043*	*489*
Investment income balance	-13,732	-10,793	*-7,619*	*-7,818*	*-8,144*	*-8,470*
Transfers balance	958	862	*444*	*444*	*444*	*444*
Current Account Balance	**-14,795**	**-10,371**	**-4039**	***-5,417***	***-6,658***	***-7,537***
as a % of GDP	-8.1	-5.6	*-2.1*	*-2.7*	*-3.3*	*-3.7*

Statistics NZ *BERL Forecasts*

THE STATE OF THE NZ ECONOMY September 2010

INDICATOR	PERIOD	LATEST DATA	UNIT	MEASURE	*YEAR AGO COMPARISON*	+ or - ?	
Employment	quarter	Jun 10	number (000s)	2,166	*2,166*	-	**GENERAL SITUATION**
growth			% chge on prev yr	0.0	-0.8	+	
LF participation rate	quarter	Jun 10	%	67.8	*68.2*	-	
Net permanent migration	3 month	Jul 10	number	-607	*4,126*	-	
Business confidence	month	Aug 10	net % optimistic	16.4	*34.2*	-	
Own activity outlook	month	Aug 10	net % optimistic	25.7	*26.0*	-	
Government OBEGAL	FY to date	May 10	$m	-4,742	*-1,209*	-	
Government net worth	spot	May 10	$m	97,274	*98,985*	-	
Milk powder, butter	3 month	Jul 10	tonnes (000s)	496	*561*	-	**EXTERNAL SECTOR**
& cheese growth			% chge on prev yr	-11.7	*59.6*	-	
Meat	3 month	Jul 10	tonnes (000s)	222	*230*	-	
growth			% chge on prev yr	-3.8	*-7.5*	+	
Logs and timber	3 month	Jul 10	000s m³	3,249	*3,051*	+	
growth			% chge on prev yr	6.5	*43.0*	-	
International visitors	3 month	Jul 10	number (000s)	470	*453*	+	
growth			% chge on prev yr	3.7	*-1.2*	+	
Merchandise receipts	3 month	Jul 10	$m	11,553	*10,368*	+	
growth			% chge on prev yr	11.4	*-3.7*	+	
Merchandise payments	3 month	Jul 10	$m	10,761	*9,971*	-	
growth			% chge on prev yr	7.9	*-16.6*	-	
Current account Balance of Payments	annual	Mar 10	% of GDP	-2.4	*-7.9*	+	
Net international assets	spot	Mar 10	% of annual GDP	-88.9	*-94.6*	+	
Performance of manufacturing index (PMI)	3 month	Jul 10	average index	51.9	*45.3*	+	**INVESTMENT & BUILDING ACTIVITY**
PMI new orders	3 month	Jul 10	average index	51.7	*48.3*	+	
Imports of plant and	3 month	Jul 10	$m	1,463	*1,562*	-	
Machinery growth			% chge on prev yr	-6.3	*-3.8*	-	
Real business investment	quarter	Mar 10	1996 $m	4,530	*4,561*	-	
growth			% chge on prev yr	-0.7	*-18.7*	+	
Non-residential building	3 month	Jul 10	number	469.9	*641.2*	-	
consents growth			% chge on prev yr	-26.7	*-32.9*	+	
House building consents	3 month	Jul 10	number	4,206	*3,552*	-	
growth			% chge on prev yr	18.4	*-20.5*	+	
Retail sales (excl mv)	3 month	Jul 10	$m	11,732	*11,627*	+	**DOMESTIC ACTIVITY**
growth			% chge on prev yr	0.9	*2.7*	-	
Motor vehicle new registrations	3 month	Jul 10	number	37,524	*29,535*	+	
growth			% chge on prev yr	27.0	*-26.7*	+	
Guest nights	3 month	Jul 10	number (000s)	5,828	*5,833*	-	
growth			% chge on prev yr	-0.1	*-0.4*	+	
Electricity generation	3 month	Mar 10	GWH	10,097	*9,571*	+	
growth			% chge on prev yr	5.5	*-4.4*	+	
Ready-mix concrete	quarter	Sep 10	000s m3	662	*828*	-	
growth			% chge on prev yr	-20.1	*-11.3*	-	
Consumer price inflation	quarter	Jun 10	% chge on prev yr	1.8	*1.9*	+	**FINANCIAL & MONETARY CONDITIONS**
Producer inputs price inflation	quarter	Jun 10	% chge on prev yr	2.0	*-1.2*	+	
NZX50 share prices	month	Sep 10	average index	3077	*3119*	-	
House sales	3 month	Jul 10	median days on mkt	44.3	*40.0*	-	
Credit card balances outstanding	3 month	Jun 10	% of retail sales	99.3	*99.7*	+	
Exchange rate TWI	month	Sep 10	average index	65.8	*64.3*	+	
90 day interest rate	month	Sep 10	average %	3.25	*2.77*	-	
90 day interest rate margin with Australia	month	Sep 10	basis points difference	-145	*-60*	+	

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