

## Oil higher after historic agreement

- Oil marks a 15% increase in price following OPEC's production cut.
- Reserve Bank of New Zealand's Financial Stability Review keeps debt-to-income loan measures on the table.
- Government's Half Year Economic Update could provide some clues on how to fund the earthquake rebuild.

**Oil has turned-tail over the last week.** After weeks of being under pressure, **its price increased over 15% in a matter of hours.** This followed OPEC's (Organization of the Petroleum Exporting Countries) historic agreement last Wednesday to limit the production of its members, as well as some associates. **The cut in global supply had the desired effect on the price of the commodity.** Oil rose to just-shy of \$52/brl in the hours following the announcement, some distance from the \$45 it sat at the day before the meeting took place, underlining just how pessimistic markets were that a deal could be signed off after weeks and weeks of speculation. **The agreement will start to lift petrol prices in the near future** (they already appear a few cents higher based on anecdotal evidence), providing a source of inflation for the Reserve Bank of New Zealand. This could keep any further talk of rate cuts firmly off the table for the near future.

**The RBNZ's Financial Stability Review (FSR) delivered a generally upbeat assessment of the economy.** However, dangers in the housing market were still highlighted and as such, the **RBNZ kept the possibility of Debt-To-Income restrictions on the table.** At this stage such measures, which would limit the amount an individual could borrow to fund a property purchase, based on their income, still need to be given the green light by the Finance Minister. The exact definitions and implementation method also need to be further investigated. **Given the time it would take for all this to be completed, it appears such measures are still some months off.** This would also bring any potential implementation close to next year's election, something the Government may wish to avoid. However, the RBNZ is politically neutral and such issues should not be part of its considerations.

Looking ahead, **the Half Year Economic and Fiscal Update (HYEFU) is due Thursday.** This should show the government's books continue looking healthy and that the economy is growing robustly. The 2015/16 surplus (OBEGAL) was \$1.2bn higher than forecast and the 3 months to September were running \$0.7bn ahead of forecast, i.e. on track for another operating surplus. Moreover, the earthquake bill looks manageable at this stage, although is still subject to revision. **The Treasury estimates the cost will be between \$2bn and \$3bn,** i.e. not material enough to change the overall fiscal picture for New Zealand as a whole. Combined with low and falling government debt, this means the government has plenty of Fiscal choices. There is also the possibility the government issues more bonds to deal with the up-front cost of the earthquake. Even so, John Key has hinted at measured tax cuts, which may include a family package, i.e. increases to Working for Families (incl. Accommodation Supplement). Other broader priorities are set to remain, including the running of surpluses and the repaying of debt.

### Foreign Exchange

- NZD back on the up.

### Interest Rates

- NZ interest rates continued to lift on the back of US interest rate moves.

### Week Ahead

- Government Half Year Economic Update, GDT dairy auction.

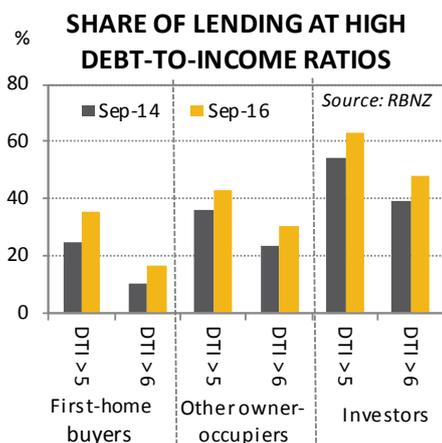
### Week in Review

- Oil rises, RBNZ's financial stability review keeps debt-to-income measures on the table.

### Global Calendars

- Reserve bank of Australia rates decision.

## Chart of the Week: Debt-To-Income ratios moving higher



With Loan-To-Value (LTV) measures already in place, **the next potential method for the RBNZ to control the housing market looks to be Debt-To-Income (DTI).** The chart shows that over a period of just 2 years, **the share of lending for loans considered to be high DTI has increased for all category of buyer and for each category of high DTI loan.**

**Should the RBNZ mirror the level introduced by the Bank of England a few years ago, of 4.5 times income, then over 60% of investors would be impacted,** over half of owner-occupiers and just under half of first time buyers. This could cause a major change in the ability of all buyers to complete a purchase and take much of the heat out of the market. However, while some would welcome the move, owners and investors may not appreciate the change as much.

**Of course, the level the RBNZ plumps for will be key.** The graph shows that if it selected 6 times income, it would be investors seeing the impact much more than the other two groups.

## Foreign Exchange Market

FX Rates	Current*	Week ago	Month ago	6 mths ago	Year ago	ST Bias	Support^	Resistance^
NZD/USD	0.7131	0.7076	0.7313	0.6829	0.6683	UP	0.6980	0.7300
NZD/AUD	0.9567	0.9467	0.9517	0.9436	0.9125	FLAT	0.9400	0.9680
NZD/JPY	80.90	79.24	75.37	74.16	81.89	UP	79.80	82.20
NZD/EUR	0.6691	0.6642	0.6591	0.6120	0.6112	UP	0.6600	0.6800
NZD/GBP	0.5611	0.5655	0.5862	0.4738	0.4419	FLAT	0.5530	0.5700
TWI	78.6	77.7	78.3	73.6	72.2	UP	76.00	79.00

^Weekly support and resistance levels \* Current is as at 9.30 am Monday; week ago as at Monday 5pm.

The **NZD finished the week higher against most of the major crosses**. The NZD outperformed the AUD early in the week and held onto gains as the **AUD was weighed by weaker commodity prices** for iron ore and coking coal. The RBA meeting and Australian GDP are key event risks for the NZD/AUD this week.

The **US employment report was mixed** in terms of implications. The **weaker-than-expected wage data may limit USD strength** in the near term. We expect the **NZD/USD to remain buoyed by higher dairy prices and USD consolidation**.

The **EUR direction for the week will depend on the Italian referendum results**. If Italians reject the referendum on constitutional reform (a simple majority of "No" votes is necessary) like the polls suggest, **EUR may come under more downside pressure on heightened political uncertainty**.

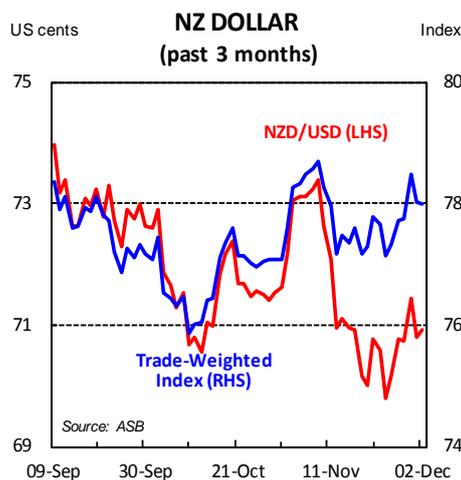
### Short-term outlook:

### Key data

### Date

### Time (NZT)

### Market



Italian Referendum Results

5/12

11.30am

-

RBA Rate Announcement

6/12

4.30pm

1.5%

Global Dairy Trade auction

6/12

Overnight

+3-5%

Economic Survey of Manufacturing, Q3

7/12

10.45am

-

AU GDP Q3 % qoq

7/12

4.30pm

0.2

Electronic card spending, Nov %mom

9/12

10.45am

0.4

**Key events: NZD:** Q3 manufacturing activity, Global Dairy Trade auction (Wed).

Treasury Half-year Economic and Fiscal Update (Thurs); electronic card spending (Fri).

**AUD:** Q3 balance of payments, RBA meeting (Tue); Q3 GDP (Wed); Oct home loans (Fri). **USD:** Nov ISM non-manufacturing (Tue). **CNY:** Nov FX reserves (Wed); Nov trade balance (Thu); Nov CPI (Fri). **JPY:** Oct labour cash earnings (Tue); Oct balance of payments (Thu); Q3 final GDP estimate (Fri). **EUR:** Italian referendum, Oct retail sales (Mon); Q3 final GDP estimate (Tue); ECB meeting (Thu). **GBP:** Nov services & composite PMIs (Mon); Oct industrial production (Wed).

**Speakers:** RBNZ Governor Wheeler testimony to select committee on the Annual Report (Wed). **FOMC:** voter Dudley, non-voter Evans & voter Bullard (Tue). **BoJ:** Kuroda (Mon).

### Medium-term outlook:

### Last Quarterly Economic Forecasts

In late October we tweaked our near-term FX forecasts but left the medium-term forecasts broadly unchanged. The NZD remains supported by relatively high Terms of Trade, relatively high interest rates, increased offshore investor demand and a structural improvement in the current account deficit. **Given the RBNZ signalled it has finished its easing cycle at the November MPS, we see little sustained downward pressure on NZD given the support from the previously mentioned factors, barring any developments from the November 14 earthquake.** Over 2017, we expect the NZD/AUD to remain in a relatively high range of 0.93-0.96.

Meanwhile, we see the NZD/USD remaining elevated in a range of 0.70-0.73. We believe the USD has peaked and will drift slightly lower over 2017. However, there is still considerable uncertainty about the impact incoming President Trump will have.

We revised our GBP forecast lower in late October as the weakness in the GBP occurred somewhat earlier than expected. We believe the fundamental down-trend in the GBP will remain intact, and expect the NZD/GBP to continue to gradually lift toward the mid-0.60's by 2018.

In the near term we continue to see NZD/JPY hold above 70. Further out, the prospect for more BOJ easing should weaken the JPY, pushing NZD/JPY above 85 in 2017.

## Interest Rate Market

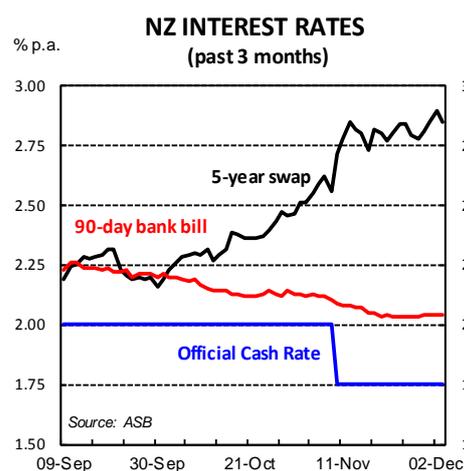
Wholesale interest rates	Current	Week ago	Month ago	6 mths ago	Year ago	ST Bias
Cash rate	1.75	1.75	2.00	2.25	2.75	FLAT
90-day bank bill	2.04	2.03	2.13	2.40	2.88	FLAT
2-year swap	2.29	2.29	2.25	2.32	2.79	UP
5-year swap	2.85	2.79	2.55	2.50	3.13	UP
5-year benchmark gov't stock	2.56	2.44	2.30	2.16	2.96	UP
NZSX 50	6905	6904	6708	7024	6095	UP

^Weekly support and resistance levels \* Current is as at 9.30am Monday; week ago as at Monday 5pm.

**Last week got off to a slower start in interest rate markets**, with limited data to drive rates in either direction. In saying this, **New Zealand interest rates continue to be largely at the mercy of international moves**. Domestic events, including the RBNZ's Financial Stability Report, had little impact on rates over the week. However, a lot of attention was paid to any oil-related comments ahead of Wednesday night's OPEC meeting in Vienna. Indeed, comments ahead of the meeting cast doubt on an agreement being reached and pushed longer-term yields lower. This move was quickly unwound with the news that **OPEC had managed to come to an agreement to lower oil production over the first half of 2017. US 10-year yields pushed above 2.40% and longer-term New Zealand yields also followed higher**.

**Encouraging US data in the latter half of the week provided a further boost to interest rates**. ADP employment and US personal income data on Wednesday supported yields. Interestingly, while Non-farm Payrolls were close to expectations, markets focused on the lower than expected hourly earnings data which erased some of the week's moves.

### Short-term outlook:



### Key data

	Date	Time (NZT)	Market
Italian Referendum Results	5/12	11.30am	-
RBA Rate Announcement	05/12	4:30 pm	1.5%
GlobalDairyTrade Auction	05/12	overnight	-
AU GDP, Q3, %qoq	06/12	1:30 pm	0.2

**Comment:** As we kick off another week, focus will initially be on the results of the Italian constitutional referendum (due today). Polls are suggesting that the referendum will be rejected, in which case Prime Minister Renzi may resign. Such an income risks throwing Italy into political turmoil. Locally, Tuesday night's GlobalDairyTrade auction will be closely watched. If further modest gains are achieved (as we expect), rates could move higher still. RBNZ Governor, Graham Wheeler, is also speaking to the Select Committee on Wednesday. However, this appearance is unlikely to be market moving. Elsewhere, the RBA rate announcement on Tuesday is unlikely to move interest rate markets too much unless the statement contains a change in message. Also in Australia, Q3 GDP is due. A solid result here is likely to see expectations for any additional easing by the RBA unwind further.

### Medium-term outlook:

### Last Quarterly Economic Forecasts

**The RBNZ cut the OCR to a record-low 1.75% as widely expected, on November 10.** In addition, **the RBNZ reduced its easing bias** to "numerous uncertainties remain, particularly in respect of the international outlook, and policy may need to adjust accordingly." At the same time, the RBNZ signalled that it was not expecting to cut interest rates any further in its new OCR forecast track.

**While the RBNZ remains concerned about the strength of the NZD, the inflation outlook has improved since September.** Inflation is likely to be back within the 1-3% target band at the next read (due January) and economic growth is running at an above-trend pace. However, the RBNZ remains aware that the risks remain skewed to the downside. Interestingly, the RBNZ reminded that, if the NZD exceeds the RBNZ's assumptions going forward, it is the reasons for that lift that matter for any response. For example, stronger NZ fundamentals wouldn't imply a need for offsetting OCR cuts. However, further lifts in the NZD for other reasons, falling inflation expectations, bank funding costs and any deterioration in the global growth outlook could force the RBNZ into cutting the OCR beyond 1.75%.

**We now expect the RBNZ to remain on hold for the foreseeable future. However, recent events including Donald Trump's successful US Presidential campaign and North Canterbury's 7.5 magnitude earthquake on the 14<sup>th</sup> of November, have increased the degree of uncertainty.**

## Key international data for the week ahead

Data	Date	Time (NZT)	Previous	Market expects	ASB expects
Australia Company Operating Profits, Q3, %qoq	05/12	1:30 pm	6.9	3.0	1.0
Australia Current Account Balance, Q3, \$bn	06/12	1:30 pm	-15.5	-13.5	-15.0
Reserve Bank of Australia Interest Rate Decision, %	06/12	4:30 pm	1.5	1.5	1.5
Australia GDP, Q3, %qoq	07/12	1:30 pm	0.5	0.2	0.2-0.4
China Foreign Reserves, November, USD bn	07/12	-	3,121	3,066	3,192
Australia Trade Balance, October, \$bn	08/12	1:30 pm	-1.2	-0.6	-0.5
China Exports, November, %yoy	08/12	-	-3.2	-1.0	-1.0
European Main Refinancing Rate, %	09/12	1:45 pm	0.0	0.0	-0.4
Australia Owner-Occupier Loan Value, October, %mom	09/12	1:30 pm	0.9	-	-0.1
China CPI, November, %yoy	09/12	2:30 pm	2.1	2.2	2.1

We expect a modest 1.0% rise in Australia's company profits following a 6.9% jump last quarter. Higher commodity prices imply that mining profits are likely to be less of a drag.

We expect a slight improvement in Australia's Q3 balance of payments. Net exports are likely to make a 0.2ppt contribution to Q3 GDP growth following a very soft Q2 outcome.

We expect the Australian cash rate to remain unchanged at the RBA's forthcoming meeting. With the economy growing at a moderate pace, the RBA has time to wait and assess the impacts of the 2016 rate cuts on the inflation outlook.

Australia's GDP is likely to have expanded by a relatively soft 0.2-0.4% over Q3. While dwelling construction and public spending have boosted growth, a downturn in business investment is weighing heavily on growth.

The strengthening of the USD against other currencies resulted in a negative valuation effect on China's FX reserves during the month of November.

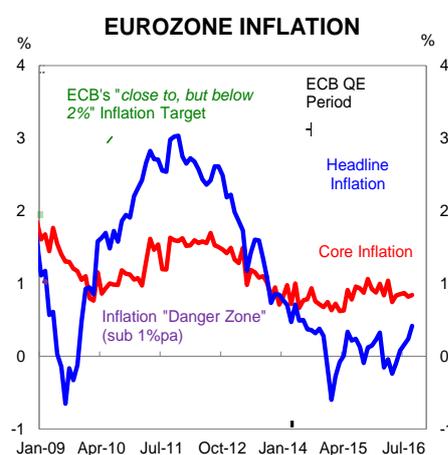
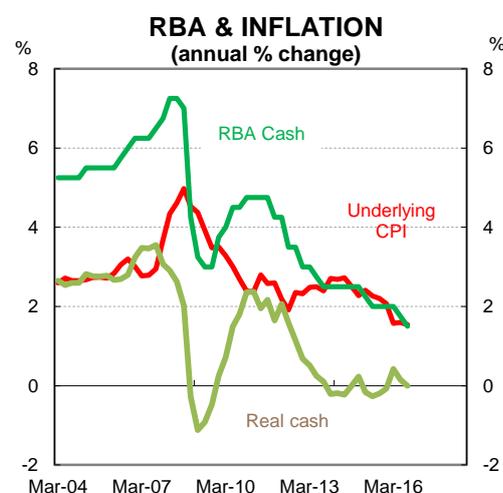
Australia's trade balance is likely to have narrowed in October with higher commodity prices lifting exports and a lift in the Australian dollar pushing imports lower.

China's current account surplus is stabilising at around 2.5% of GDP. Demand for China's exports is improving, according to the PMI survey. Recovering commodity prices are supportive of China's import growth.

Australia's housing finance approvals for owner-occupiers remain high. However, approvals for investors are down almost 20% from their peak. We expect modest falls in the number and value of loans in October.

China's vegetable price growth slowed over the month of November. This should take China's CPI to 2.1% for the month.

No policy changes are expected from the ECB in December. However, the governing council is expected to assess the options available to ensure a "smooth implementation" of the current asset purchase programme at this meeting. The ECB will also release its new macroeconomic projections prepared jointly with Euro-area national central banks. These projections will extend to 2019. Importantly, the ECB will likely highlight again it "remains committed to preserving a very substantial degree of monetary accommodation" and that "the risks to the Euro-area growth outlook remain tilted to the downside".



# NZ Data Preview: a look at the week ahead

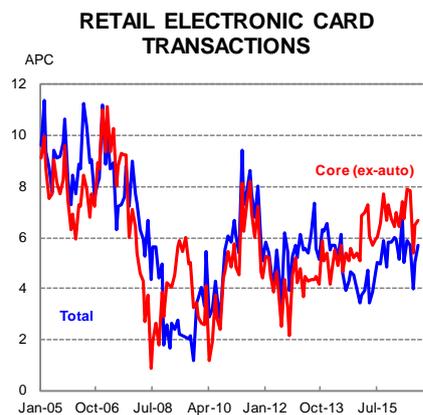
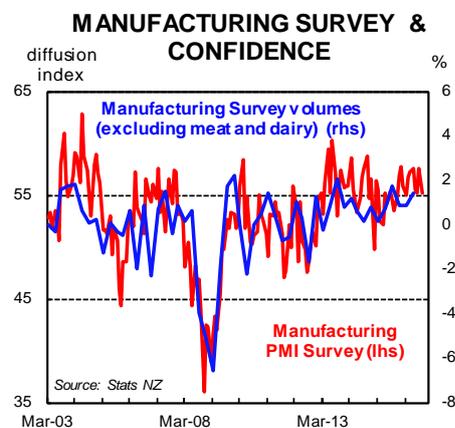
Data	Date	Time (NZT)	Previous	Market expects	ASB expects
GlobalDairyTrade auction, whole milk powder, % change	06/12	Overnight	+3.2	-	+2 to +4
Manufacturing Survey, sales volumes ex-meat & dairy, Q3, %qoq	07/09*	10.45 am	+1.4	-	-
Electronic Card Transactions, November, %mom	09/12*	10:45 am	0.6%	-	0.4%

**\* NOTE: All Statistics NZ dates data release dates are subject to revision following the recent earthquakes and closure of Statistics NZ's head office.**

Overnight Tuesday, the latest **GlobalDairyTrade** auction takes place. **We expect prices to post further modest gains at this auction as NZ production remains weak.** Current futures pricing suggests a whole milk powder price rise in the 2% to 4% range. We expect global dairy prices to remain firm over the remainder of the season, reflecting weakening global and NZ dairy supply.

The **manufacturing PMI continues to hold up at expansionary levels** and points to 1% growth in ex-meat and dairy manufacturing production. We use sales and inventory from the **Economic Survey of Manufacturing as an indicator for Q3 GDP ex-meat and dairy manufacturing production.** Manufacturing activity has been supported by strong construction activity and growth in other investment demand. Meanwhile, a drop in slaughter and milk production will likely see a fall in meat and dairy manufacturing volumes.

**Electronic card spending data could be impacted by the recent earthquake in a number of ways.** While the damage could have limited the ability of many people to spend, it may also have pushed others into spending on items they would normally not have. There is also the potential that data collection itself could have been disrupted. This comes on top of a few months of disrupted data, after adjustments by Stats NZ in August and September, mainly in durables. **Given all this, we are looking for spending growth to maintain its overarching robust upward trend,** but there is plenty of scope for volatility within the varying components.



# Data Recap: weekly recap

Data	Date	Actual	Market forecast	ASB Forecast
RBNZ Financial Stability Report	30/11	-	-	-
Credit Growth, October, household, %mom	30/11	0.6	-	-
ANZ Business Confidence, November, Index	30/11	20.5	-	-
Building Consents, October, residential, %mom	30/11*	n.a.	-	-
Terms of Trade, Q2, Index, % change	1/12*	-1.8	0.0	0.0
Value of Building Work, Q3, %qoq	2/12*	n.a.	2.2	2.3

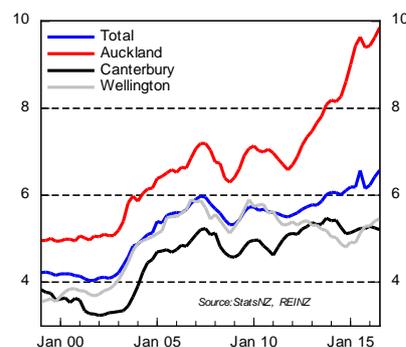
The RBNZ did not announce any new financial stability policy measures at the release of the November Financial Stability Report. The RBNZ has noted again that it has **asked the Finance Minister to include a Debt to Income (DTI) tool** in the memorandum of understanding that covers macro-prudential policy. As yet there has been no decision announced by the Finance Minister. **We don't expect any further macro-prudential action for some time. The RBNZ still sees risks to the financial system via housing and dairy.** On the monetary policy front **we continue to expect the RBNZ to keep the OCR on hold at 1.75%** for the foreseeable future.

**Housing credit growth remains robust in October**, but off its recent highs. On an annual basis, housing credit growth remains above 9.0%. The RBNZ's most recent housing LVR lending restrictions appear to be weighing on demand, most notably investors. **Consumer credit growth** picked up in October, with annual lending up 3.3% and back to levels seen earlier in the year. **Business credit growth** lifted again in October, with lending now 8.0% up on year-ago levels, the highest annual growth rate since February 2009.

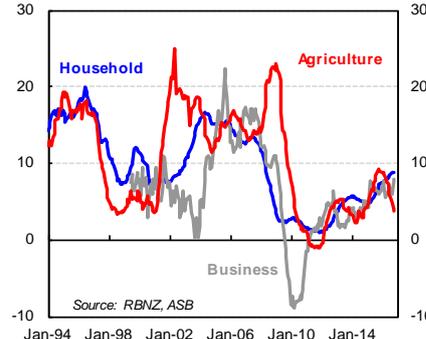
**Business confidence moved lower again in November, an unsurprising development considering the North Canterbury earthquake and US election.** However, there has been a strong improvement in agricultural optimism, one of only two sectors to improve. That is quite a turnaround for agriculture, usually the most pessimistic sector, but Fonterra's upward revision of its milk price forecast for this season to \$6/kg from \$5.25/kg on November 11 may have been the spur.

**The Terms of Trade (ToT) fell 1.8% over the June quarter, greater than our expectations and those of the market. The data release was again a limited version**, as Stats NZ continues to come back online following the North Canterbury earthquake. **The decline in Q3 export prices was driven by dairy and meat.** However, looking forward, dairy prices are already on the way back up, as evidenced by Fonterra's recent upward revision in the milk price forecast for this season. **Meanwhile, import prices reversed last quarter's move, declining 1.0% after Q2's 0.2% rise.** Despite the weak result, **we still estimate that the ToT have now passed their cyclical low and will lift over the next year as dairy shipments start to reflect higher prices.** Moreover, we expect low global inflation to continue to underpin the ToT.

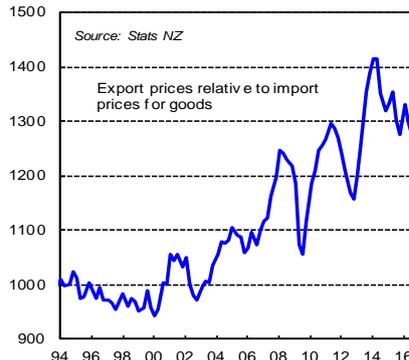
HOUSE PRICE TO INCOME



LENDING GROWTH (annual change)



NZ TERMS OF TRADE



## Global Data Calendars

## Calendar - Australasia, Japan and China

Date	Time (NZT)	Eco	Event	Period	Unit	Last	Forecast	
							Market	ASB
Mon 5 Dec	11:30	AU	AiG Performance of Services Index	Nov	Index	50.5	~	~
	13:00	NZ	ANZ Commodity Prices	Nov	m%ch	0.2	~	~
	14:00	NZ	Treasury Monthly Economic Indicators	Nov	~	~	~	~
	14:45	CH	Caixin China PMI Services	Nov	Index	52.4	~	~
	13:30	JN	Nikkei PMI Composite	Nov	Index	51.3	~	~
	16:45	JN	BoJ Kuroda speaks at Europlace, Tokyo					
	18:00	JN	Consumer Confidence Index	Nov	Index	42.3	~	~
Tue 6 Dec	12:00	NZ	QV House Prices		y%ch	12.7	~	~
	13:30	AU	Current Account (Balance of Payments)	Q3	AUDbn	-\$15.5	~	-\$15.0
	16:30	AU	RBA Cash Rate Decision	Dec	%	1.50	1.50	1.50
Wed 7 Dec	10:45	NZ	Manufacturing Activity	Q3	q%ch	2.2	~	~
	11:30	AU	AiG Performance of Construction Index	Nov	Index	45.9	~	~
	13:30	AU	GDP	Q3	q%ch	0.5	~	0.2-0.4
	18:30	AU	Foreign Reserves	Nov	AUDbn	64.9	~	~
	14:30	CH	Foreign Reserves	Nov	USDbn	3120.7	~	~
	18:00	JN	Leading Index	Oct P	Index	100.3	~	~
Thu 8 Dec	13:30	AU	Trade Balance	Oct	AUDmn	-1,227	~	-500
	14:30	CH	Trade Balance	Nov	USDbn	49.1	~	~
	12:50	JN	BoP Current Account Balance	Oct	¥bn	1821	~	~
	12:50	JN	GDP SA	Q3	q%ch	0.5	~	~
Fri 9 Dec	10:45	NZ	Card Spending Retail	Nov	m%ch	0.6	~	0.4
	~	NZ	REINZ House Sales	Nov	yr%ch	-14.2	~	~
	13:30	AU	Home Loans Total	Oct	m%ch	1.6	~	-1.6
	12:30	JN	Machine Tool Orders	Nov P	y%ch	-8.9	~	~
	14:30	CH	CPI	Nov	y%ch	2.1	~	~

\*P = Preliminary

## Calendar - North America &amp; Europe

Date	Time (UKT)	Eco	Event	Period	Unit	Last	Forecast		
							Market	ASB	
Mon 5 Dec	08:00	EU	PMI Services	Nov	Index	54.1	~	~	
	09:00	EU	Retail Sales	Oct	m%ch	-0.2	~	~	
	15:00	US	Market US Services PMI	Nov F	Index	54.7	~	~	
	15:00	US	ISM Non-Manufacturing Composite Index	Oct	Index	54.9	~	~	
Tue 6 Dec		EZ	GDP	Q3	q%ch	0.3	~	~	
	13:30	US	Trade Balance	Oct	\$USbn	-36.4	-39.4	~	
	13:30	US	Factory Orders	Oct	m%ch	0.3	0.1	~	
	13:30	US	Factory Orders ex transportation	Oct	m%ch	0.6	~	~	
	13:30	US	Non-farm Productivity	Q3 F	qtr%ch	3.1	3.2	~	
	13:30	US	Unit Labor Costs	Q3 F	qtr%ch	0.3	0.3	~	
	13:30	US	Durable Goods Orders	Oct F	m%ch	4.8	~	~	
	13:30	US	Fed's Dudley speaks						
Wed 7 Dec	08:30	UK	Industrial Production	Oct	m%ch	-0.4	~	~	
	18:30	US	Consumer Credit	Oct	\$USbn	19.3	15.0	~	
		CA	Bank of Canada (BoC) Rates Decision	Dec	%	0.5	0.5	0.5	
Thu 8 Dec	~	EZ	Eurozone ECB refin rate	Dec	%	0.0	0.0	0.0	
	07:00	UK	RICS House Price Balance	Nov	m%ch	~	~	~	
Fri 9 Dec	09:30	UK	Trade Balance	Oct	£mn	5,221	~	~	
	09:30	UK	Construction Output	Oct	m%ch	0.3	~	~	
	12:00	US	Initial Jobless Claims –week ending 3 Dec	~	'000k	-56.1	-59.0	~	
	12:00	US	Wholesale inventories	Oct F	m%ch	-0.4	~	~	
	12:00	US	Wholesale trade sales	Oct	m%ch	0.2	~	~	
	12:00	US	Uni of Michigan Sentiment	Dec P	Index	93.8	~	~	
		US	US Fed's Bullard, Evans and Dudley speak at various venues across US						

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