

RT

## THE WEEK AHEAD

23 January 2012

"Hope and fear continue to do battle. Hope that global growth, led by the largest economy in the world, the US, is slowly recovering. Fear that Europe remains in crisis, with a series of credit downgrades looming."

That was what we said on 19<sup>th</sup> December, and although those themes have not changed, hope does seem to be winning the battle at present. The credit downgrades expected did eventuate. S&P moved against 16 members of the EU, but as it was so anticipated, the impact was temporary.

The moves from the ECB to assist the banks have had a major impact. The ECB lent a huge EUR489b in 3y funding. A total of 523 banks borrowed money at the tender with the final demand well above the EUR310b polled by Reuters. The funding was provided in the hope that a credit crunch can be avoided and that the money may be used to buy Italian and Spanish debt. Indeed, as can be seen in the chart below of 2 year Italian bonds, that is indeed happening, with solid bond auctions in Spain and France as well boosting investor appetite for European risk assets.

As well, recent data in Europe has been positive. The euro zone posted its biggest trade surplus since mid-2009 in November, as exports grew at more than twice the rate of imports and signalled that the European economy may escape a prolonged downturn. The surplus was the biggest monthly gain since July 2009, and in seasonally-adjusted terms, the surplus was the largest since July 2004.

German business sentiment in the IFO monthly survey of some 7,000 companies rose to 107.2 in December from 106.6 in November, defying expectations for a decline and underscoring the strength of Europe's largest economy. The Mannheim-based ZEW economic think tank reported that German analyst and investor sentiment posted a record rise in January. The ZEW report was the latest to paint a brighter picture of the economy. **So Greek worries aside, Europe is not as bad as has been painted.**

In the US, the outlook is also improving. US home sales hit an 11 month high in December and the number of properties on the market was the fewest in nearly 7 years, pointing to a nascent recovery in the housing sector. There were 2.38m unsold homes on the market last month, the fewest since March 2005. That represented 6.2 months supply at December's sales pace, the lowest since April 2006 and down from 7.2 months supply in November. A

supply of 6 months is generally considered ideal and anything higher suggests prices will decline further. **Housing matters, as when it looks to stabilise and move higher, so can the rest of the US economy.**

In Asia, China's economy grew at 8.9%, slightly stronger than the 8.7% that Reuters polls had expected. Even so, it was the weakest pace in 2½ years and may give Beijing yet another reason to gently ease monetary policy, most likely by reducing the amount of reserves that large banks must hold. The HSBC flash manufacturing purchasing managers index (PMI), the earliest indicator of China's industrial activity, stood at 48.8 in January, a three-month high and a slight improvement on the 48.7 final reading of the December index. **Even so, stand by for more easing from Chinese authorities.**

In Australia employment surprisingly fell 29,300 in December, but had little longer term impact. Producer prices rose 0.3% in Q4, a touch below forecasts of a 0.4% increase. Key data this week is the CPI on Wednesday. A tame number would cement expectations for an interest rate cut at the RBA's 7<sup>th</sup> Feb policy meeting.

In New Zealand, international milk prices rose for the first time in 3 auctions. Fonterra's Global Dairy Trade-TWI, which covers a range of 30 products and contract periods on offer, rose 1.5%, with an average selling price of USD3,701 per tonne. That followed a 0.7% decline in the previous auction. The index has fallen about 22% since hitting a near 4 year peak in March last year as global commodity prices have retreated. But the real surprise last week was annual inflation falling 0.3% in Q4, to be 1.8% higher than a year ago. That was the first decline in 2 years and backs the view that interest rates will stay low for longer, with no change expected from the RBNZ this week.

Italian 2 year bonds, over the worst?



MAJORS			
	Spot rate	19-Dec-11	Change
NZD/USD	0.8057	0.7572	0.0485
AUD/USD	1.0468	0.9902	0.0566
EUR/USD	1.2882	1.2999	-0.0117
USD/JPY	77.04	78.12	-1.08
GBP/USD	1.5541	1.5480	0.0061
USD/CAD	1.0142	1.0407	-0.0265
USD/SEK	6.7982	6.9434	-0.1452
RBNZ TWI	71.69	68.16	3.53

CROSS RATES			
	Spot rate	19-Dec-11	Change
NZD/AUD	0.7691	0.7643	0.0048
NZD/EUR	0.6253	0.5823	0.0430
NZD/JPY	62.07	59.15	2.92
NZD/GBP	0.5183	0.4890	0.0292
NZD/CAD	0.8171	0.7880	0.0291
NZD/SEK	5.4773	5.2575	0.2198
AUD/EUR	0.8126	0.7618	0.0509
AUD/JPY	80.65	77.35	3.29

SPOT RATES - EXOTICS			
	Spot rate	19-Dec-11	Change
USD/HKD	7.7608	7.7846	-0.0238
USD/MYR	3.1050	3.1750	-0.0700
USD/NOK	5.9323	5.9777	-0.0454
USD/SGD	1.2719	1.3066	-0.0347
NZD/HKD	6.2529	5.8945	0.3584
NZD/MYR	2.5017	2.4041	0.0976
NZD/NOK	4.7797	4.5263	0.2533
NZD/SGD	1.0248	0.9894	0.0354

Source REUTERS



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2012 starts with similar themes that 2011 ended. All eyes remain on Europe as the Greek drama drags on. The best that can be hoped for is eventually an orderly exit from the Euro. In anticipation of more dramas, the global short position in the Euro is the highest on record – nonetheless the euro is currently making upward progress. This is not a surprise with all the bad European news in the market and the downgrades behind us, for now. In comparison, the antipodean currencies look attractive.

## United States

- Wednesday** - 2012 State of the Union Address  
 - Dec pending home sales  
 - FOMC rate decision
- Thursday** - Dec durable goods orders
- Friday** - Q4 GDP advance % annualized  
 - Jan UoM consumer sentiment

## Australia

Since our last report on 19 December the AUD/USD has jumped 564 points, confirming our end 2011 view that the AUD was set to improve in 2012. China continues to track positively and it is from this direction that the influence on the AUD remains. A break above resistance at 1.0500, only 50 points away, puts the AUD/USD in an uptrend and sees 1.0700 as the next target. The NZD/AUD has gained 50 points but remains in a 0.75-0.78 range and importers and exporters would continue to target the extremes of this range to add further to cover.

- Wednesday** - Q4 CPI  
**Thursday** - Australia Day public holiday

## New Zealand

The NZD/USD has gained 486 points since 19 December as risk traders regain confidence in the currency and the region. The NZD/USD has broken out of the downtrend and needs to break 0.8200 to become an uptrend. Remember that the NZD/USD 21 year annual average change is 17.63%. Importers would be adding to cover needs at these levels, but only for the next 1-2 months. Exporters would use any European inspired weakness back toward 0.7800 to further add to cover.

- Thursday** - RBNZ Official Cash Rate  
**Friday** - Dec Merchandise Trade Balance

## Asia

The USD/JPY, in contrast to all the other major currencies has changed little since the end of 2011 –

down by 110 points. There seems to be no reason at this stage to expect this lethargy to abate. The NZD/JPY has by contrast risen sharply by 275 points over the same period. Exporters should retain the policy of adding to cover as it matures where they can get an outright forward price below 60.00. Importers would already have taken some cover at 62.00, and be looking to further add on spot rates around 64.00. Chinese New Year this week will keep Asia range bound.

- Monday** - Bank of Japan decision

## Europe & UK

The EUR has eased back by 100 points since 19<sup>th</sup> December but significantly more recently has made solid gains after a look down toward 1.2600. Sellers of the euro are becoming nervous as despite all the bad press about Europe the currency has ceased its late 2011 plummet. We may well be starting to see the currency settle into a 1.2800 - 1.3200 range with the bias towards the upside rather than the downside. The NZD/EUR has surged by 430 points since mid December, at one stage hitting all time highs of 0.6299 – in 2008 this rate hit 0.3892. Current levels around 0.6200 should be used by importers for longer term cover, whilst exporters would look for a revisit of levels under 0.6000.

- Tuesday** - EUR - Nov industrial orders  
**Wednesday** - GER - Jan IFO business climate index

	Trend	Support 2	Support 1	Resistance 1	Resistance 2
NZD/USD	Flat	0.7370	0.7880	0.8200	0.8571
NZD/AUD	Flat	0.7300	0.7500	0.7800	0.8000
NZD/JPY	Flat	57.00	58.19	62.00	64.50
NZD/EUR	Up	0.5800	0.6050	0.6300	0.6400
AUD/USD	Flat	0.9659	1.0000	1.0500	1.0700
AUD/JPY	Down	72.00	77.00	81.00	84.00
USD/JPY	Flat	75.00	76.50	78.25	80.00
EUR/USD	Down	1.2400	1.2600	1.3000	1.3500

FORWARDS	1 Mth	3 Mths	6 Mths
NZD/USD	-0.0018	-0.0050	-0.0097
AUD/USD	-0.0040	-0.0106	-0.0197
EUR/USD	0.0001	0.0005	0.0013
USD/JPY	-0.02	-0.08	-0.19
GBP/USD	-0.0004	-0.0013	-0.0028
USD/CHF	-0.0005	-0.0015	-0.0032
NZD/AUD	0.0012	0.0030	0.0051
NZD/EUR	-0.0015	-0.0041	-0.0083
NZD/JPY	-0.16	-0.45	-0.89
NZD/GBP	-0.0010	-0.0028	-0.0053
NZD/CHF	-0.0020	-0.0059	-0.0116

COUNTRY	OFFICIAL OVERNIGHT RATE
NEW ZEALAND	2.50%
AUSTRALIA	4.25%
EUROPE	1.00%
JAPAN	0.10%
UNITED KINGDOM	0.50%
SWITZERLAND	0.00% - 0.75%
UNITED STATES	0.00% - 0.25%
GOLD	1667.25
SILVER	32.34
BRENT OIL	108.94

90 DAY BILLS	Change from last 19 Dec 11	3 YEAR SWAPS	Change from last 19 Dec 11
2.80	0.00	2.96	0.16
4.45	-0.25	3.88	0.16
1.08	-0.23	1.26	-0.15
0.10	0.00	0.36	-0.02
0.99	0.03	1.31	-0.02
-0.05	0.00	0.15	0.00
0.50	0.02	0.68	-0.09

Source REUTERS