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GDP growth (%)	2008	2009(f)	2010(f)	2011(f)
Australia	4.0	2.1	-0.9	0.7
New Zealand	3.2	0.2	-2.8	2.4
United States	2.0	1.1	-2.6	1.8
Euro zone	2.6	0.7	-2.4	0.4
Japan	2.4	-0.7	-3.8	0.4
China	13.0	9.1	6.9	8.5
Other East Asia*	6.0	3.2	0.4	4.4
World (PPP)	5.0	3.0	-0.1	3.0

*Asia excl. Japan & China

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Overview

Saul Eslake, Chief Economist

The global economic outlook remains grim

Near-term prospects for the global economy have continued to deteriorate over the first few months of this year. In company with institutions such as the IMF and the World Bank, we now expect that the global economy will contract this year, for the first time since the end of World War II. And the ensuing recovery, which we expect to have begun by the turn of the year, is likely to be unusually slow and gradual.

Vicious wealth, inventories and trade cycles

With most countries now having released national accounts data for the final quarter of 2008, the contours of the dramatic downturn in economic activity in the second half of last year – and which has continued into the first half of 2009 – have become clearer.

US household net worth dropped by 9% in the fourth quarter of last year, bringing the cumulative decline since mid-2007 to 20%. This is, by a wide margin, the largest fall in personal wealth in the US since at least the end of World War II (by contrast, net worth dropped by 9.8% over the 2½ years following the peak of the 'tech bubble' in March 2000, by just 2.5% after the October 1987 sharemarket crash, and by 3.6% during the first oil shock and bear market of 1974). As a proportion of annual personal disposable income, US household net worth has fallen by 155 percentage points (ppt) since the onset of the sub-prime mortgage crisis, taking it back to where it was in mid-1995.

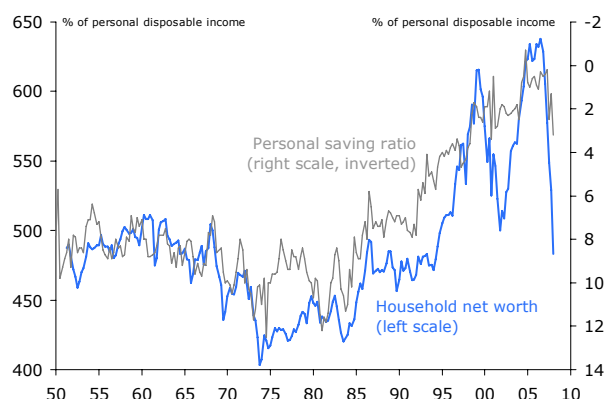
The net worth of the non-financial corporate sector has also declined by 7% since mid 2007. This is slightly less than the 8.6% decline which occurred (over a considerably longer period) in the early 1990s, but is otherwise the largest fall in corporate net worth since at least the early 1950s.

Much the same appears to have occurred in the UK. UK household net financial worth (ie. excluding real estate) fell by 16% between the second quarter of 2007 and the third quarter of 2008; given the further decline in financial asset values since then, and the fall in house prices since mid 2007 (of between 10 and 22%, depending on which measure is used), overall household net worth may have fallen by at least as much in the UK as in the US.

Net wealth is also likely to have declined, albeit by smaller proportions, in most other countries.

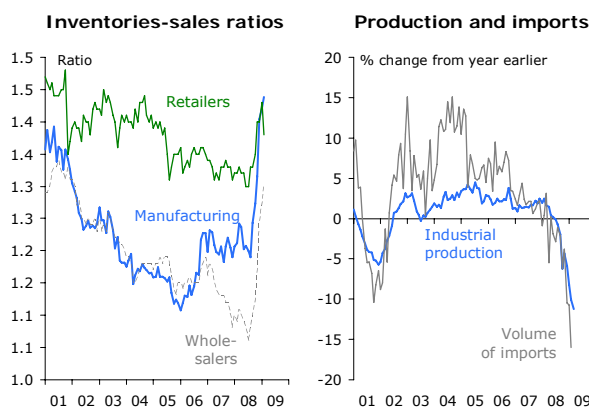
These dramatic declines in net worth prompted a surge in household saving and abrupt falls in household spending, especially on items which typically involve borrowing, such as motor vehicles and housing.

The slump in household net worth ...



Sources: US Federal Reserve; Bureau of Economic Analysis.

... has prompted vicious stock and trade cycles



Sources: US Commerce Department; Federal Reserve Board.

The dramatic declines in spending on consumer durables and housing in turn led to an unanticipated surge in retailer and producer inventories.

And this is where the declines in wealth combined with the financial crisis to produce the economic firestorm which spread across the world in the latter part of last year. Inventories have to be financed; they absorb working capital. Yet a major consequence of the financial crisis has been that businesses have found it much more difficult to access additional debt finance. Hence businesses confronted by an unexpected surge in inventories have been obliged to make drastic cutbacks in outgoing orders or in production.

With manufacturing supply chains having become increasingly globalized over the past two decades, it was inevitable that this inventory cycle would be transmitted rapidly around the world through a slump in merchandise trade. Moreover, since merchandise trade is also heavily dependent on finance (given the lags between the shipment of goods and the receipt of payment for them), the impact of the financial crisis on the availability of trade finance magnified the decline in merchandise trade flows.

Trade slump drags Asia into the vortex

Over the past decade, East Asian governments have sought to insulate themselves from a repetition of the abrupt reversal in private capital flows which induced the 1997-98 crisis by accumulating much larger foreign exchange reserves than were previously thought necessary. In pursuit of that goal, most East Asian countries have maintained large current account surpluses and, in some cases, undertaken significant intervention in foreign exchange markets. In so doing, many Asian countries inadvertently made themselves as vulnerable to an abrupt decline in trade flows as they previously were to an abrupt reversal in capital flows.

Most East Asian countries, other than China, have experienced year-on-year declines in their exports of between 15 and 42%. For economies where exports represent a very large proportion of GDP (such as Korea, Taiwan, Malaysia and Singapore), or where exports have been the most important source of economic growth in recent years (most notably Japan), the result has been much sharper contractions in economic activity than in the US or Europe, where the financial crisis originated.

China has also been affected by the global trade slump, although less so than other East Asian countries (indeed China's imports, including from other Asian countries, have fallen more than its exports). However the abrupt slowdown in China's economy in the second half of last year owes more to the collapse of China's own construction bubble.

There are some encouraging indications that the fiscal, monetary and other policy actions undertaken by the Chinese authorities since November last year are beginning to take effect. But recovery elsewhere in Asia will require a sustained increase in domestic demand, as well as a revival in demand from Western economies.

The financial crisis is still not yet over

Despite the rally in equity markets during March, the global financial crisis is not yet 'over'; and it will not be 'over' until confidence in the solvency of the global banking system has been restored. That in turn requires credible programs to ensure that banks have enough capital to support 'normal' levels of lending after providing for the impact of the economic slump on the assets which remain on their balance sheets.

The Public-Private Investment Program unveiled by US Treasury Secretary Geithner in late March appears to provide much more credible detail as to the means by which 'toxic assets' will be removed from the balance sheets of American banks, and as such may represent a key step in drawing the crisis to a close. At the time of writing, however, it remains unclear to what extent the program will draw in private capital in sufficient volumes.

Unconventional economic policy is vital

The current slump in the United States and Europe has in several key respects more in common with the economic downturns of the 19th and early 20th centuries – which were generally termed 'depressions' or 'panics' – than with the 'recessions' that have occurred at regular intervals in most advanced economies since 1945.

Most post-war recessions were induced by tight monetary policy; and recovery from them has been prompted by easier monetary policy, sometimes accompanied by easier fiscal policy, which has eventually succeeded in inducing the private sector to resume borrowing and spending. By contrast, monetary policy played very little role in inducing the current downturn; rather, it has resulted primarily from a collapse in asset prices and an abrupt reduction in both the demand for and supply of credit. This, emphatically, does *not* mean that the current slump must inevitably turn out to be as deep or as protracted as the Great Depression of the 1930s. But it *does* mean that the macro-economic policies which have worked in post-war recessions will probably not work in current circumstances. And it also means that governments and central banks *have* to implement policies which, in more 'normal' circumstances, would be considered risky or even 'irresponsible'.

In that context, the willingness of central banks to engage in 'quantitative easing' (or 'printing money' as it is often depicted) in order to expand their balance sheets, including by purchasing government bonds, is appropriate rather than 'irresponsible'. In particular, comparisons with Weimar Germany or present-day Zimbabwe (where 'printing money' in the context of a collapse in the 'supply side' of the economy led to hyper-inflation) border on being fatuous. The situation in the US, the UK and Japan (among others) today is one of deficient demand, not deficient supply. Rising inflation (let alone hyper-inflation) is a remote possibility in such circumstances; indeed, deflation looms as a greater risk than inflation in the period immediately ahead, and deflation is much harder to cure than inflation.

Central banks do need to formulate 'exit strategies' from 'quantitative easing' to guard against the possibility of rising inflation once the financial system returns to normal; and governments need to devise credible strategies for restoring fiscal sustainability once economic recovery begins (strategies which may well entail tax increases). But the alternative to what central banks and governments are now groping towards is *not* standing back and allowing the slump to run its course; rather, it is rising public pressure (in the face of mounting unemployment and other forms of economic distress and social unrest) for protectionist and other measures which would not only be economically devastating but also threaten the maintenance of peaceful relations among nations.

Australian Economic Outlook

Warren Hogan and Katie Dean

An extended period of weakness

The Australian recession has begun. Australia has lagged most other parts of the world in entering this deep and synchronized global downturn. But the drivers and characteristics of the slowdown here are essentially the same as in other parts of the world; a sharp adjustment in the availability and cost of credit, corporate and household balance sheet consolidation due to the repricing of risk and sharp falls in wealth and a capitulation in exports. A healthier local financial sector (which has precluded an economy-wide credit crunch) and an aggressive (and early) countercyclical macroeconomic policy response should allow Australia to avoid the devastating depth of the downturns occurring in the G7. But an extended period of economic contraction and rising unemployment now looks unavoidable.

GDP is likely to contract by around 1.0% in 2009, with at least two and possibly four quarters of negative growth (including the 0.5% contraction in the December quarter 2008). We expect the impact of counter-cyclical policy, as well as some recovery in the global economy (especially China), will allow the Australian economy to start to stabilise by the end of 2009. But the recovery over 2010 is likely to be slow and soft, with GDP growth of just ¾% expected. Continued household and business balance sheet consolidation, locally and globally, means Australian economic growth may struggle to return to trend growth before late 2011.

As the economy slows, the unemployment rate is likely to rise to a 12-year high of 8¼% by late 2010. This rate may rise towards 9.0% should labour force participation rates either stabilise at current record highs or increase further. This could occur if individuals seek to extend their working lives or if second-income earners re-enter the labour force to try to restore 2008's unprecedented loss of household wealth. A higher unemployment rate that it is driven by higher labour force participation does not pose the same downside risks to the economy as a rise in unemployment that is driven by falling employment. Larger than expected job-shedding, akin to the 1990s recession, remains the biggest downside risk to the Australian economy over the next 18 months.

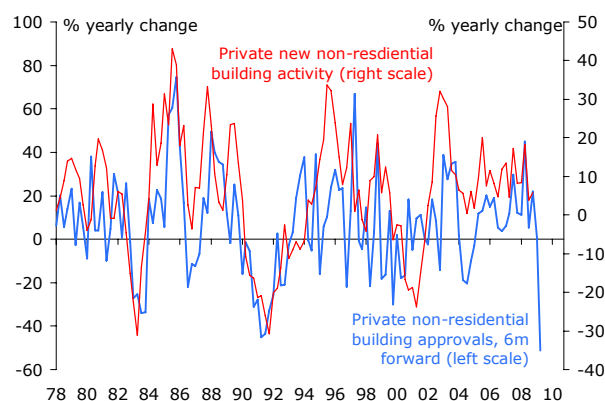
Businesses to drive the next leg down

To date the slowdown in the Australian economy has been driven by weaker exports, a large shock to our manufacturing sector and by household balance sheet repair, as consumers save not spend. Business balance sheet repair, and its impact on business spending plans, in particular large-scale investment projects, will lead the next leg in this slowdown. While Australian corporate balance sheets are in good shape, this will do little to drive

new spending when the outlook has deteriorated so materially and when credit is not only more expensive (in terms of risk margins) but more difficult to access. In this environment, businesses will follow the lead of households; pull back spending and debt accumulation to protect their balance sheets.

The abrupt shock to credit and economic conditions saw private non-residential building approval values plummet by 60% YoY in January, led by a 70% collapse in commercial property approvals. The chart below shows that in quarterly YoY terms, approvals are falling more deeply than the 1990s recession. In the 1990s new private non-residential building fell 51% peak to trough, contracting in 16 out of 18 quarters and dragging 2.4ppts from GDP growth. A record high level of work in the pipeline may prevent a similar sized collapse this time around. However these leading indicators still point to large double-digit declines in activity in this sector over 2009 and 2010. With approvals yet to bottom, the danger of an even deeper fall is high.

Non-residential building approvals yet to bottom



Sources: ABS and ANZ.

N.B. The value of building approvals is deflated by ANZ using the National Accounts IPD for new private non-residential building activity.

Business investment cycles take time given the lags involved between initial decisions and ultimate activity. For these reasons they are also slow to respond to either stimulatory macroeconomic policy or changing economic conditions. The typical business investment cycle in Australia lasts for 3 to 4 years. This suggests we may not see private investment meaningfully contribute to Australian economic growth much before 2012.

No longer able to rely on households

During previous business investment downturns, the Australian economy has been able to rely on a debt-fuelled household sector to drive growth. This is no longer the case. Heightened concerns over unemployment and a 10% fall in household wealth (the largest in several decades) are fuelling a more cautious approach to borrowing and spending and an aggressive approach to balance sheet repair. In the last twelve months, the household savings ratio (savings as a proportion of disposable income) has increased from 0.5% to 8.5%, the highest level

since the 1990s recession. Not only do we anticipate the savings ratio to rise further above 10%, we expect it will stay at this elevated level for the foreseeable future. An enduring legacy of today's crisis will be that over the next 3 to 5 (and possibly 10) years average household consumption growth will be notably lower than in the last decade. This will constrain the economy's ability to rebound quickly and is a key reason behind our subdued overall economic outlook.

The appropriate policy response from here

Local policy efforts to counter the global financial crisis (GFC) have taken many forms. Traditional policy tools have been deployed in the form of lower interest rates and increased government spending. The Commonwealth has also moved to use its credit rating to ensure the smooth functioning of these traditional policy tools. The government guarantee of bank liabilities has allowed the Australian banking system to continue to access funds in global markets and thus continue to provide credit to corporations and households. Importantly, this has allowed the Australian banks to pass on most of the RBA's interest rate reductions.

Disruptions to global capital markets and the emergence of bank guarantees have increased the cost of funding for Australian State governments. More recently, the downgrade to Queensland's credit rating has seen underlying liquidity conditions in the State government bond market heavily affected. This led to concerns not just about the cost of raising funds for State governments, but the ability to meet large borrowing programs critical to the funding of capital expenditure programs.

With the underlying budget position of most State governments moving into deficit due to the economic slowdown, an inability to access global markets put government expenditures at risk as well as jeopardising prospects for on-going infrastructure investments. Although the details of the government guarantee for the States is still in progress the Commonwealth move to guarantee the borrowings of State governments has effectively shored up a important element in fiscal spending.

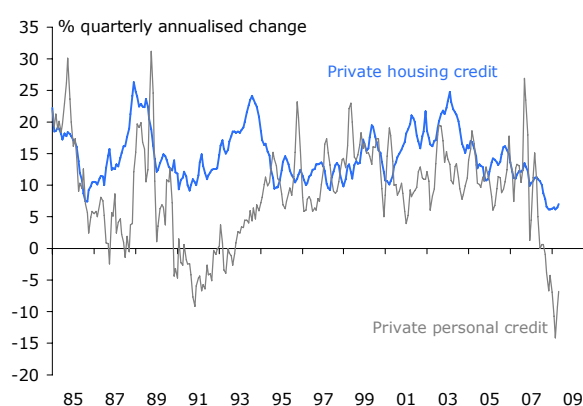
The emphasis of counter-cyclical macro-economic policy in Australia over the next 6 to 12 months is likely to be increasingly skewed towards fiscal policy. Although the RBA has maintained an interest rate well above most other industrialised countries in recent months, the benefits of further significant rate reductions are not as clear.

As outlined above, Australia, like most industrialised economies, is in the process of a household balance sheet consolidation after an extended period of expansion. While the primary focus of policy efforts thus far has been to avoid a cataclysmic seizure of local credit markets (including bank lending), the role of policy is not to fight a necessary adjustment across the economy, but rather to promote an

orderly process. At the very least monetary policy shouldn't be used to try and fight the adjustment by reflating a sector of potential vulnerability.

In terms of household delevering the RBA credit numbers confirm that most of the work is being done outside of housing. The chart below shows that personal credit growth (credit cards, unsecured lending and margin loans) is declining while mortgages growth is still growing, albeit at a slower pace. While it is critical to avoid a disorderly de-leveraging in the housing sector (as this is what is driving so many of the problems in the US and the UK), it is disingenuous to think that driving up household debt is a sustainable response to the current risks facing the Australian economy.

Households are de-leveraging outside of housing



Sources: RBA and ANZ

The policy emphasis is shifting from containing the direct financial shock from the GFC (avoiding a credit crunch) to limiting the impact on the real economy or more specifically containing the extent to which the unemployment rate is likely to rise. Rather than re-leveraging household balance sheets policy should now be focused on assisting the process of balance sheet repair. To do this against a backdrop of weakening economic activity and rising unemployment, the government can look to boost income growth via direct stimulus. While this can come in many forms, including tax cuts, it appears that the use of one-off payments is the preferred method largely (and rightly) because one-off payments do not have an on-going negative impact on the budget position.

For the RBA, this suggests a slower and more modest approach to rate cuts from here. The central bank is likely to want to maintain the flexibility to respond as the economy weakens further later in the year. We expect the official cash rate will fall another 125bp to 2.0%, but believe that the reduction will occur in smaller increments of 25bp or 50bp, and that the low point may not be reached until the end of 2009. With any economic recovery likely to be subdued over 2010, we expect official rates will remain at these low levels for an extended period. At this stage we think it unlikely that official rates will rise before late 2010.

New Zealand Outlook

Philip Borkin

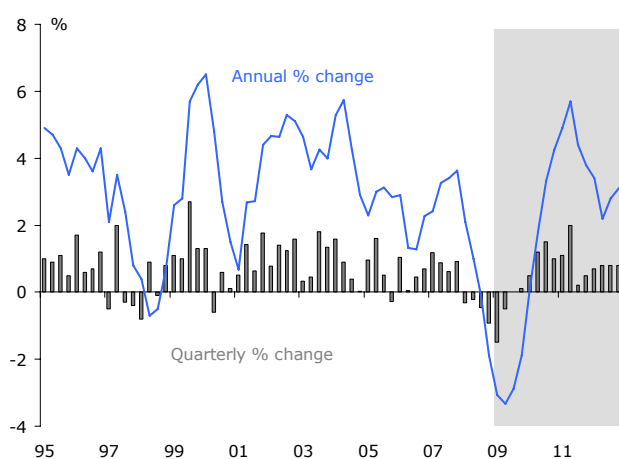
A structural as well as a cyclical adjustment

The New Zealand economy is yet to find a base. Business confidence surveys are either at, or near, historical lows. Employment intentions are tumbling and investment plans are being shelved. Corporate tax revenue has capitulated. Consumer sentiment is also very subdued despite falling mortgage rates, tax cuts and lower petrol prices. Car registrations are at their lowest level since 1994 and building consents in January fell to their lowest level since 1965.

It is now likely that the recession, which began in the March 2008 quarter, will extend to five, possibly six, quarters as the full impact of the global downturn is felt. This follows a largely domestic and drought-driven recession over the first half of last year. The last time New Zealand experienced such a string of negative quarters was during the oil shock of the 1970s.

We expect the New Zealand economy to contract by 2.8% this calendar year. The economy is void of any key engines of growth over 2009, as the combination of deleveraging restrains the domestic economy, and the flow on from a weak global environment hampers the export sector.

A deeper downturn (New Zealand GDP)



Sources: Statistics NZ, ANZ

The outlook for this year is dominated by four dynamics:

- > A credit centric shock. Despite signs that global credit spreads have eased and major central banks are embarking on quantitative easing to keep longer dated yields down, credit markets are still far from normal. It is no longer a question of price. We are in a world where capital is scarce and this is not about to change for some time.

- > A deep global recession, which started at the end of last year and is set to last throughout most of this year.
- > A structural change in the pricing of risk, with a clear shift in the balance of power away from borrowers and towards savers and investors. New Zealand is already seeing this via changes in retail deposit rates, which now sit materially above the wholesale interest rate curve.
- > New Zealand's heavy reliance on offshore capital, which is evident via a large current account deficit and large net external liability position. The latter, at 93% of GDP, is a key source of vulnerability in the current global environment and needs to be reduced.

Essentially, the New Zealand economy faces a structural adjustment at a time when it is going through a cyclical one. This structural adjustment sees the economy rebalancing away from debt-fuelled consumption towards more earnings-centric growth (i.e. exports). This results in anaemic consumption growth for a number of years and a sharp improvement in the household savings rate.

Hence, consumers will no longer be the main driving force for growth. This is despite improved disposable incomes from tax cuts and lower mortgage repayments. The deteriorating labour market and rising unemployment rate (we are forecasting it to reach close to 8% by the middle of 2010) increase the likelihood that households save any windfall gains, rather than spend them. We are forecasting a 1.4% fall in consumption for this calendar year, and only mild 0.7% growth next calendar year.

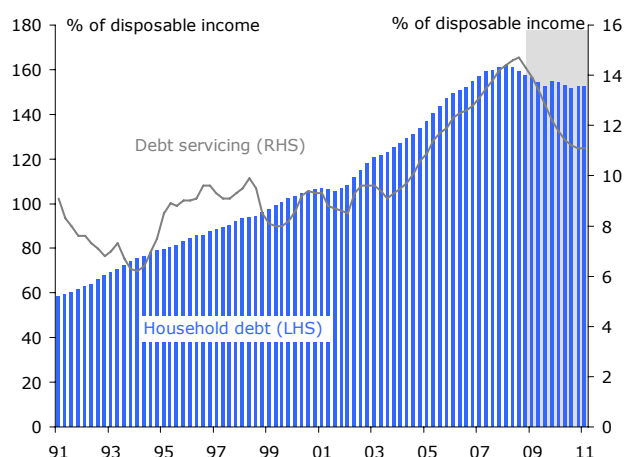
Business sector to do it tough

Businesses face a very tough and challenging year, as both domestic and external demand wanes. Profitability is well down and firms have already responded by putting a freeze on hiring and investment at the end of last year. Firms exposed to domestic demand (e.g. retail and housing) have fared poorly as the recession intensified, but increasingly it will be exporters that will feel the effects of the global recession in the form of reduced or cancelled export orders. Thankfully, business sector balance sheets are healthy.

But with topline revenues continuing to head backwards, the recession lasting longer than normal and balance sheet preservation becoming a priority, the onus will increasingly turn towards costs in order for firms to stay profitable. We foresee negative employment growth throughout 2009, and likewise for business investment. The latter will reduce the potential growth rate of the economy and hamper the eventual recovery when it comes. Employment and investment intentions already sit at historical lows. These are the next leg of the cycle to watch.

Despite the pressure on businesses, we need to remain mindful that a household debt correction story is at the heart of this economic cycle. It is household balance sheets that need to be repaired. Household debt-to-income increased from 60% to close to 160% between 1991 and 2008. Debt servicing increased from 8% of disposable income to over 14% currently. Housing represents 75% of total assets. These dynamics were a reflection of the “old” macro environment where credit was cheap and freely available. This allowed New Zealand to run large current account deficits.

Household debt and servicing levels remain high



Sources: RBNZ, ANZ

Macro-framework working but not enough

New Zealand's macro-framework has responded via interest rate cuts, expansionary fiscal policy and a lower currency. New Zealand's financial system remains sound, a major differentiating factor from the United States and other nations. But facing the deepest global recession in half a century, the policy responses to date can only ever help take the sharp edges off the recession. New Zealand still stands out as being vulnerable given our reliance on exports and offshore capital. We are also mindful that monetary policy is rapidly losing traction given fierce competition for deposits and funding in general. And pressure on the Government to maintain its sovereign credit rating means they cannot simply go on an unfettered spending or tax cut binge.

Looking for a 2010 recovery

The economy will come out of recession in the second half of the year, but a sustained recovery will be a mid 2010 story. Though we expect positive growth rates from the second half of this year, it will not feel like a recovery initially. Indeed, growth will be subdued heading into early 2010 as the economy remains in the deleveraging process. It will not be until mid 2010, by which time the unemployment rate would have peaked and the global economy started to mend, that the economy will embark on a sustained recovery and start posting strong quarterly growth rates.

Pent up demand will fuel the initial rebound, as building consents play catch up to underlying housing demand, consumers replace durable goods, and businesses upgrade their depreciated plant and machinery equipment. These are natural pro-cyclical forces that, once unleashed, will see the economy temporarily expanding well above its trend growth rate. And let us not forget the Rugby World Cup being held in NZ in 2011. Preparations in the lead-up for the event will further add to activity, and we can expect a surge in visitors for the event, leading to a boost in services exports. We see the economy performing strongly in 2011.

Key financial market views

The official cash rate (OCR) has been cut a cumulative 525bp since July last year to a record low of 3%. Facing the biggest financial crisis in a generation, with credit hampering the monetary policy transmission channel and the weakest period of world growth since WWII, this type of policy response has clearly been warranted.

While there are few signs that the New Zealand economy (and the world for that matter) is finding a base and risks to economic outlooks still appear skewed to the downside, the ultimate end-point for RBNZ policy is approaching. The RBNZ Governor has ruled out near zero rates due to a need to maintain competitiveness in global capital markets. We envisage an OCR trough of 2.5% by mid-year. With inflation not a concern and growth expected to be weak for some time, we see rates remaining at low levels for an extended period, with the tightening cycle not occurring until late 2010.

A weaker currency is a prerequisite to the adjustment process the New Zealand economy needs to go through and for the recovery to take on a sustained look. With fiscal policy somewhat constrained in its ability to provide additional counter-cyclical support and monetary policy nearing the end of the easing cycle, the critical shock absorber that must adjust is the currency. Years of the currency remaining above its historical average has led to a deteriorating goods and services trade balance. We simply see the reciprocal going forward, as the currency follows its normal path of moving further than what is typically expected as the adjustment takes time.

Our forecasts have the NZ\$ falling to the mid 40s against the US\$. It will not be a smooth ride down, with expected bouts of technical rebounds and short squeezes along the way. On a trade-weighted index (TWI) basis, we are forecasting a period where it goes below 50. But to be fair, a lot of this assessment is based on what we think needs to happen.

Emerging Asia: Nearing the Bottom?

Paul Gruenwald and Tamara Henderson

The pace of activity is still declining across much of emerging Asia. The Newly Industrialised Economies (NIEs) continue to be hit the hardest by the crisis. Meanwhile, growth in parts of the ASEAN group, while below trend, looks somewhat more robust. China and India enjoy the highest growth rates in the region, although growth is well below pre-crisis levels.

Our Asian split call therefore remains valid. Moreover, this pattern looks set to continue throughout 2009, or as long as the weakness in advanced country demand persists. China is a key exception to current regional trends, as we note below.

No consumption, no growth

Excepting China, data in the first quarter of 2009 have showed little or no improvement from the fourth quarter of 2008. Exports and imports continue to contract at double digit rates and manufacturing activity is in sharp decline. More generally, activity seems to still be losing momentum.

The only expenditure component showing resilience in some economies is consumption. Indeed, “no consumption, no growth” would seem to be a fair characterisation of the region at the current juncture.

China, India, Indonesia, the Philippines and Vietnam would all appear to have a degree of consumption momentum in early 2009 and these are the best performing economies in the region.

Given the sharp deterioration in trade performance and manufacturing noted above, it is not entirely clear why consumption is holding up better in some economies but not others. Consumption growth does appear to be negatively correlated with the openness of the economy and the level of per capita income, but that remains a conjecture. Given the “one pillar” nature of growth in these economies, the sustainability of short-term momentum remains a risk in our view.

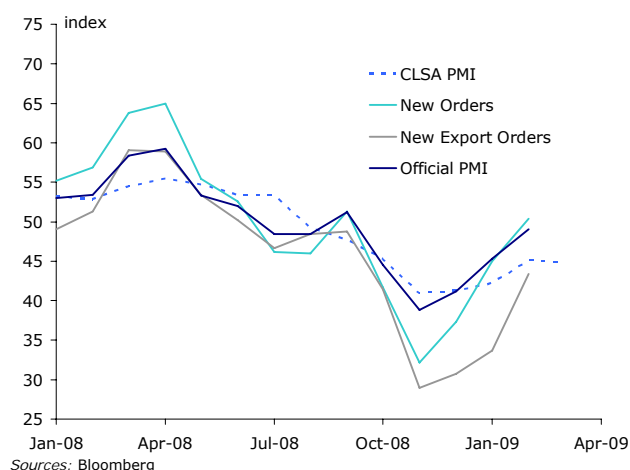
China is stabilising, but not yet recovering

The emerging Asian economy showing the clearest signs of stabilisation is China. Following the announcement of the authorities’ stimulus plan in November 2008, a number of key indicators have turned around in recent months.

First, government and private sector purchasing managers’ indices (PMIs) currently show that business conditions in China across a number of metrics are close to neutral. (Export orders are a notable exception.)

It is important to underscore that while PMIs have increased from their late 2008 lows, they are still at or below the 50 level. Thus, the recent improvement in PMIs should be interpreted as showing that business conditions are no longer deteriorating, but not yet improving.

China’s PMIs have turned the corner...



An array of additional indicators also suggests that the Chinese stimulus plan is gaining traction. Bank lending has picked up sharply, reflecting loans for working capital as well as medium to longer term loans to state owned enterprises (SOEs). Also, government fixed asset investment has picked up, electricity and steel production have turned around and the importation of base metals is beginning to rise.

In order to reach its 8% growth target, China will need to increase growth from about zero in the fourth quarter of 2008 to 2% per quarter. This challenge will, ironically, be aided by the quasi-command structure of the economy (large state owned banks and enterprises). We expect GDP growth rate to reach the 8% level (YoY) during the second half of the year, but retain our call for 2009 year-average growth to be in the 6½ to 7% range.

Policy: Fiscal centre stage

Policymakers in emerging Asia have responded aggressively and, for the most part, appropriately to the crisis so far. Going forward, we expect a further easing of policy stances, with more reliance on fiscal policy.

Monetary policy was the first line of defence for many policymakers in the region. Policy rates were lowered, often aggressively as in Korea and Taiwan, to help ease financial conditions and alleviate pressure on bank balance sheets. However, as we have seen elsewhere, monetary policy may not be the best tool to address a widespread lack of aggregate demand.

Fiscal stimulus plans in the region appear to be well structured. The focus is appropriately on generating new expenditure either through infrastructure spending or targeted tax and transfer plans. Most

governments in the region (India being the main exception) have adequate fiscal space in which to manoeuvre. The key will be to implement the plans in a timely manner and for those economies that need the largest fiscal boost to actually spend (e.g. Korea).

Well positioned for a recovery

Emerging Asia cannot resume trend growth absent a recovery in foreign demand. As this crisis has taught us, the region to varying degrees remains dependent on exports and the associated manufacturing activity for growth. Independent domestic demand has been shown to be more modest than anticipated and the related notion of “decoupling” in our view was a bit oversold.

Overall, the region is well positioned for a recovery. The productive capacity for servicing external demand remains intact, corporate balance sheets appear to be in good shape and bank balance sheets (excepting Korea) look relatively strong given what has happened elsewhere in the global economy. Loan-to-deposit ratios are well below unity, emerging Asia largely avoided toxic assets (and holds less than 2% of the global total) and non-performing loans remain quite modest, although these would be expected to rise reflecting the sharp growth slowdown. Nonetheless, the supply of funds from banks should not be an impediment to growth once the demand for credit recovers.

Currencies and rates

Risk appetite is in the driver’s seat for currencies and rates in emerging Asia excluding Japan (AXJ), with individual country fundamentals providing limited diversion. Risk appetite recovered in March, sparking an 8.5% rally in the S&P500 (18% from the March low), and a 2.8% rally in AXJ currencies versus the US dollar.

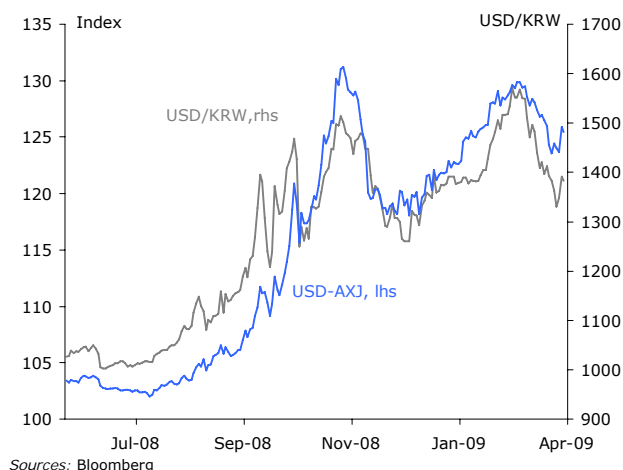
However, risk appetite can be quite fickle — begging the question, where do we go from here? Range trading seems a likely scenario for emerging Asia in Q2. On the one hand, sporadic cracks in the “ice” are appearing both in the financial sector and in the data for the real economy. As fiscal stimulus programs gain more traction, there will be more signs of stabilisation, if not outright improvement. This will buoy the optimists, capping fears to the downside.

On the other hand, global economic activity remains quite “frozen”, many challenging hurdles remain in terms of getting the private sector back to “normal,” and further fallout is likely. This will buoy the pessimists, capping hopes to the upside. Altogether, such mixed signals should trap markets in a range—albeit a wide range given the high degree of uncertainty that persists.

The outlook for range-bound trading in equity markets in Q2 suggests that USD-AXJ will re-test recent cyclical highs. As the more liquid vehicle for

expressing general fear (and most recently, hope) in emerging Asia, the Korean won (KRW) should continue to lead the way in terms of volatility. Ultimately, we expect the Korean won to outperform AXJ in 2009, although the ride lower in USD-KRW will be bumpy.

Won to outperform in 2009



At the other extreme in terms of volatility, the Chinese renminbi (CNY) has been rock steady since the middle of 2008. Meanwhile, speculation surrounding a possible devaluation has evaporated amid signs that China’s economy may have bottomed, along with a revealed preference (in terms of actions, not just words) on the part of authorities to keep USD-CNY stable — as our calculations suggest that the authorities were having to sell USD to maintain stability. We maintain the view that USD-CNY will remain in a holding pattern until Chinese authorities are confident that sufficient growth momentum has been restored (although this is unlikely to materialise in 2009).

Range bound activity in equity markets would suggest similar conditions in emerging Asian rates markets, many of which are significantly affected by risk appetite. Asian rates already face cross winds from the likelihood of further central bank rate cuts in emerging Asia combined with concerns about digesting extra supply from fiscal stimulus programmes. However, such conditions are mutually supportive of curve steepening. Quantitative easing has flattened the US and UK Treasury curves, but unlike the Federal Reserve and the Bank of England, most emerging Asian central banks have plenty of remaining ammunition to cut interest rates further, if necessary.

International & FX Outlook

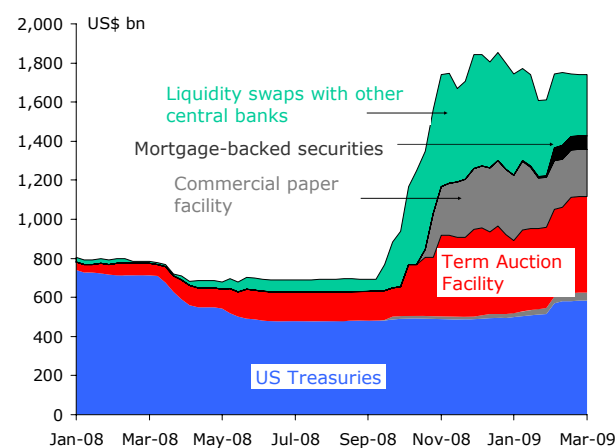
Amy Auster

A global “reserve” currency

Since our last quarterly publication, the US Federal Reserve has launched full throttle at quantitative easing (QE). The balance sheet of the US central bank will perhaps triple, to hold as much as US\$3.3tr in assets from around US\$850bn prior to 2008. The funding to purchase these assets will come from an expansion of liabilities, accomplished by the Fed “printing” money to add excess reserves to the mandatory reserve requirements that commercial banks deposit at the Fed. Asset purchases span a range of securities, but will include US Treasury notes and bonds.

The chart below depicts the state of the Fed’s balance sheet as at mid-March 2009. Holdings of US Treasuries, which used to comprise about 90% of the Fed’s balance sheet, now comprise less than 30%. Substantial room has been made for the Fed’s so-called “liquidity facilities” such as the programs to buy commercial paper, auction credit to deposit-taking banks and offer US\$ swaps to other central banks. The current holdings of mortgage-backed securities and US Treasuries is only about 30% of the Fed’s balance sheet, but this will expand significantly in the months ahead.

Balance sheet assets of the US Federal Reserve



The Fed’s move to embrace QE has once again raised speculation about the suitability of the US\$ as a global “reserve currency.” Notably, People’s Bank of China Governor Zhao Xiaochuan suggested the International Monetary Fund could manage a global reserve currency against which other currencies could be benchmarked. The vehicle for this currency would be the IMF’s existing SDRs, or Special Drawing Rights, which are a derived unit of account that the IMF uses to express the value of its financial transactions with its shareholders and borrowers. The value of an SDR unit is itself determined by a currency basket comprised of US dollars, pound sterling and yen.

The enduring influence of US\$

The debate about whether the US dollar is a suitable global reserve currency is interesting, but is very unlikely to have real-world implications for years to come. To understand why, it is important to first define what we mean by “reserve currency.” The most simple definition is that a reserve currency is one that is held by other central banks as the denomination of the foreign exchange reserves held on a central bank’s balance sheet. FX reserves held by central banks are usually invested in assets, such as government bonds. The most common reason why central banks accumulate FX reserves and buy assets with these reserves is that they are continually purchasing foreign currency in order to influence (in a downward direction) the value of their own exchange rate.

The table below shows the currency composition of all central bank reserves globally. The US dollar is the dominant global reserve currency, but it is not the only one – currencies such as the euro, pound, yen and Swiss franc are also widely used as reserve currencies. Many central banks also hold gold. It is also worthwhile to note that the proportion of US\$-denominated allocated global central bank holdings rose from 1995 to 2000, but have since declined. The euro has been the primary beneficiary of the decline in US\$ and ¥ holdings.

Currency composition of central banks’ reserves

Currency	1995	2000	2007
USD	59%	71%	64%
EUR	n/a	18%	26%
GBP	2.1%	2.8%	4.7%
JPY	6.8%	6.1%	2.9%
CHF	0.3%	0.3%	0.2%

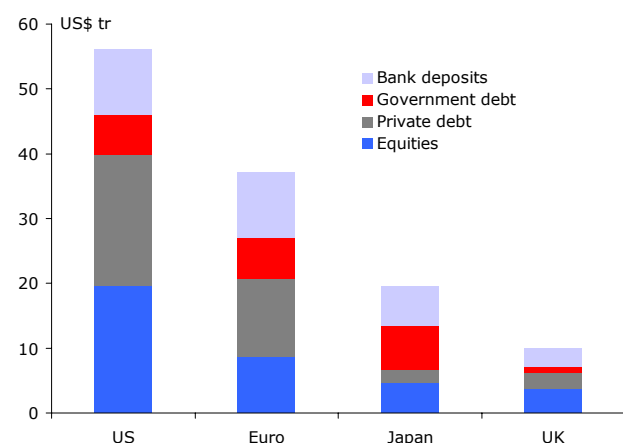
Source: IMF’s COFER database

Why would central banks continue to hold the majority of their reserves in US dollars? There are several reasons. First, the US is the largest economy in the world and therefore one of the largest export markets for most other countries. The centrality of the US dollar to global trade cannot be overlooked in this regard. There is no way to get around the fact that the value of any domestic currency against the US dollar will remain important so long as the US economy remains a dominant importing market.

Second, and perhaps more importantly in terms of central bank reserve management, the United States is also the dominant global capital market, as can be seen in the chart below. That is to say, US dollar-denominated assets comprise roughly 50% of all tradeable financial securities across the bond and equity markets. Importantly in relation to its status as a global reserve currency, 46% of the global debt markets are denominated in US dollars, versus 32% for the euro and 15% for the yen.

The dominance of the US\$-denominated asset market provides two reasons for central banks to hold US dollars. The first is that to “underweight” US\$ assets would be to undertake quite an aggressive approach to managing FX reserves – whereas central banks need to ensure minimal losses to their portfolios. The second reason is that since the US\$ asset market is largest, it is also the most liquid – allowing central banks to buy and sell their assets without disrupting markets.

Comparison of global financial stock



Sources: McKinsey's Global Institute – Mapping Capital Markets report

The euro alternative

While the US\$ remains the dominant global reserve currency, there is no question that the euro has emerged as an alternative. A question dominating the global currency markets at present is whether the euro can overtake the US dollar to become the dominant global reserve currency. Speculation that central banks will actively prefer the euro to the US dollar has been one of the drivers of euro strength in recent years. The Fed's move toward quantitative easing in March has raised speculation around this question to a new level.

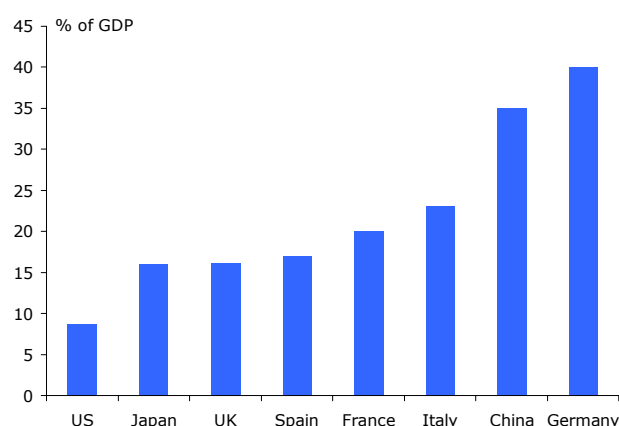
There are several problems with turning to the euro as the dominant global reserve currency. The first is that the euro-denominated capital markets are still smaller than those of the US\$, offering less choice to investors and less liquidity. This may change, but such changes take time. The second problem is that there is absolutely no guarantee that the ECB will not pursue its own version of quantitative easing, as all of the other global reserve currencies (the US dollar, the pound sterling, the yen and the Swiss franc) have already done. Though there has been much focus on the borrowing needs of the US government due to the global crisis – and concern about its ability to raise this much cash – the Euro area also has a lot of fundraising to do.

If the IMF's estimates are correct and the US needs to raise say 10% of GDP in bonds to pay for its bank support and fiscal stimulus program, this is about US\$1.4tr, or about a 23% rise in the stock of traded US Treasury debt. If the Euro area needs to raise 6.5% of GDP in bonds for its bank support and fiscal stimulus programs, this is about US\$907bn, or a 15% rise in the stock of Euro government traded

debt. In other words, both of the major global reserve currencies risk being devalued by the needs of their governments to expand the money supply in order to stimulate economic growth.

The euro may be under more pressure than the US dollar to depreciate in the coming months for one simple reason – the Euro-area economies are far more reliant upon exports for their economic growth than is the US. While a weaker euro may not generate higher export volumes in an environment of very weak demand, a weaker currency does help to improve the *profitability* and balance sheet health of European export firms. The chart below highlights the ratio of exports to GDP across major economies, and the extent to which the local currency has moved versus the US dollar since the euro hit its peak of €/US\$1.5938 on 14 July 2008.

Exports as a share of GDP



Sources: Datastream, ANZ

Outlook for the A\$

In the years to come, the A\$ also has the potential to emerge as a minor global reserve currency. Asian central banks are holders of Australian dollar denominated assets, but the very small size of the Australian government bond market means these holdings barely register as a share of overall central bank holdings. The expansion of the Commonwealth Government bond market in the coming few years could see central bank holdings of A\$ assets rise.

Would such a phenomenon cause the A\$ to rise in value? Possibly, though the simultaneous expansion of government debt markets elsewhere may dwarf what is happening in Australia. In the meantime, the Australia dollar traded in an A\$/US\$0.6250 – 0.6850 for much of the past quarter. Most recently, the renewed weakness of the USD and stabilisation of traded commodity prices such as copper and oil have given the AUD a lift towards A\$/US\$0.7200.

Despite the strength of late, we still expect the A\$ to depreciate against the US\$ over time. This view is based on the expectation that the RBA rate cuts will resume and commodity prices remain flat. The main risk to the view is the potential for a more rapid global recovery, leading to a significant surge in traded commodity prices. In that event, the A\$/US\$ could lift to 0.7250 and beyond.

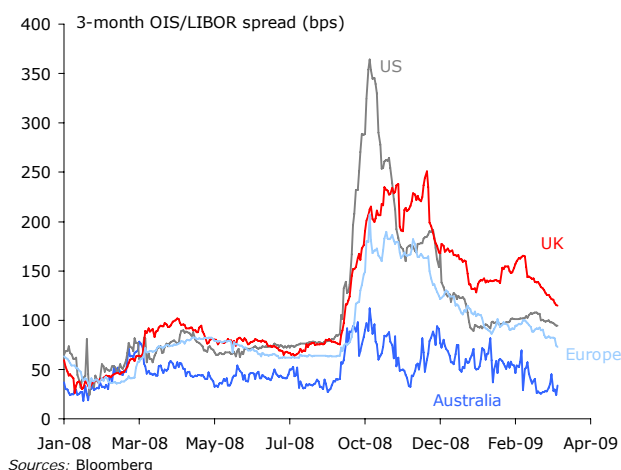
Global Capital Markets

Warren Hogan, Tony Morriss and David Croy

Conditions in financial markets have improved somewhat in the first quarter of 2009, culminating in a strong rally in assets market over the month of March. Equities, commodities and credit spreads all improved in the month, the first signs of genuine improvement in financial conditions since the collapse of Lehman Brothers in September.

This is despite continued weakness in global economic data including further increases in unemployment across the industrialised world. While the economic challenges facing the global economy suggest caution in calling a recovery in asset markets, the latest developments at the very least suggest a normalisation in the basic functioning of core financial markets. This is an important development as it reflects a moderation in systemic financial risks and an improvement in the efficiency of the financial markets; themselves necessary conditions for an eventual recovery.

Market spreads have improved



As long as global growth expectations remain under downward pressure we would not expect to see a sustained increase in the values of risky assets. Investor sentiment has been profoundly impacted by the collapse in financial markets over the past year. Important questions around asset allocation, diversification and what actually constitutes liquidity in investment portfolios are likely to see investor preferences skewed towards low risk investment markets for some time to come. Equity markets, sub-investment grade bonds and property will continue to under-perform long-term historical returns in this environment.

Sovereign bond markets to dominate the capital markets for the foreseeable future

It is quite clear now that the borrowing requirements of governments across the industrialised world will result in the capital markets being dominated by sovereign bond issuance over the next few years. In the US and Europe, weak

economic growth, discretionary fiscal stimulus and the use of public money to support the financial sector have resulted in government deficits much larger than is typical in an economic recession.

As an example, the UK Debt Management Office has averaged new issuance of around £15bn a year for the past decade. In the current financial year and next this will increase to £130bn. To put this in perspective, this is the largest new issuance program since the last recession (1992/93) which totalled £43bn. This pattern is being repeated across the industrialised world with the countries most vulnerable to a downgrade of the AAA sovereign credit ratings being Spain, the UK and the US. Ireland was downgraded in March.

In Australia, the Government has seen a rapid deterioration in the budget, combined with a large fiscal stimulus. But absent the need to provide direct financial support to banks or industry, the projections for bond issuance remain consistent with past recessions. The government is expecting a deficit of around \$35bn in 2009-10. Although we expect this to increase to something above \$50bn following the May Budget, this will still only take government bonds on issue to \$135bn in June 2010 (up from \$60bn at June 2008). To contrast with the UK; the Gilt market is expected to increase from £450bn at March 2008 to £750bn in March 2010. Australia's net debt position is expected to rise to 5% in 2011-12, compared to 50% for Germany and the UK, 65% for the US and 90% for Japan in 2010.

Quantitative easing for countries with surging bond supply

The US, Switzerland and the UK have all announced plans for the central bank to buy government bonds by expanding the size of the central banks' balance sheet. In its simplest form these central banks will print money (albeit electronically) to buy government bonds. This is a form of quantitative easing (QE). Although much debate remains around the objectives and likely implications of QE, the motivation to buy government bonds in a period of 'super' issuance relates to the desire to take pressure off term interest rates and reduce the crowding out effects on private sector issuers.

The Federal Reserve has announced plans to buy US\$300bn of Treasury securities over the six months to September. This compares to new issuance of around US\$1.1trn for the period. In the UK, the BoE is planning to buy £75bn of Gilts over the next three months.

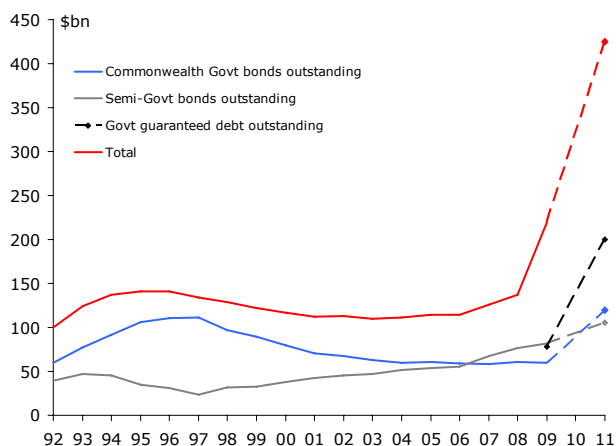
The immediate market reaction to the Federal Reserve's announcement to buy Treasury securities was a large drop in term bond yields (higher prices). While these policies run the risk of generating inflation as the economy recovers, the short-term objective of containing the rise in term rates appears to have been met. As such, we have revised our forecast for global term interest rates.

We expect 5 and 10-year rates to remain stable for the next six months before rising in 2010 on the expectation of an economic recovery and the risk that QE is not removed from the system quickly enough.

A new asset class: government guaranteed bank debt

A new fixed income asset class has merged over the past six months with the implementation of government guarantees (GG) for banks in most major industrialised countries. The Australian government program commenced on 28 November 2008. Since then the Australian banks have issued approximately A\$80bn in term securities under the guarantee. Globally, we estimate that over A\$700bn in GG issuance has occurred. Most of the issuance has been by US banks in US\$ followed by European banks in Euros. Australian banks have issued mainly in US dollars, yen and Australian dollars.

Government guaranteed assets on the rise



Sources: AOFM and ANZ

This has been an important element in shoring up the funding of the Australian banking system given that around 25% of bank liabilities are in the form of term funding. We do not expect the GG market to suddenly go away. Over the next 18 months (assuming the GGs continue to be used) we expect Australian banks to issue a further \$A200bn in term securities, largely to refinance previous non-guaranteed debt. In Australia the GG bank market already rivals the Commonwealth Government Securities (CGS) market in size. However, we believe that investors will continue to favour the CGS market due to greater liquidity.

Federal government offers guarantee to the States

A major development for domestic debt markets has been the decision by the Commonwealth to offer a range of guarantees to the States to support their ability to access credit markets. This will make it easier for the States to deliver on existing infrastructure plans to support economic growth into 2010. States' access to markets had been more difficult since the introduction of guarantees for

bank debt and the surprise downgrade of Queensland's credit rating in February.

States with an AAA rating (NSW, VIC, WA & SA) can pay a 15bp fee to cover existing debt and 30bp for new debt while AA+ rated States (QLD and TAS) can pay 20bp and 35bp respectively. This is for domestic debt only. This represents comprehensive support for the States ability to borrow at reasonable rates. The deal is positive for Queensland as the 5bps pricing of the guarantee is very tight between AAA and AA+ ratings.

This decision represents explicit AAA sovereign support for the States although there is some uncertainty surrounding the plan as it is not yet clear which States will decide to take the opportunity to cover existing debt.

New Zealand rates to stay low, despite opposing forces

New Zealand long term interest rates are once again subject to conflicting forces. On the one hand, a steadily rising New Zealand Government Securities (NZGS) issuance schedule is set to place upward pressure on yields (as has been the case elsewhere). In this regard, recent developments haven't been encouraging. Indeed, Treasury have recently stated that "risks have increased that economic growth will be below Treasury's downside scenario in the December Update in both 2009 and 2010". Given this starting point, and our weak economic forecasts, we now expect the 2009 and 2010 bond programmes to be NZ\$8.9bn and NZ\$11.2bn respectively. These compare to estimates of NZ\$4.6bn and NZ\$7.7bn in the Treasury's December Update.

However, on the other hand, the Reserve Bank of New Zealand (RBNZ) have made it clear that monetary policy is set to be accommodative for some time, noting on April 1st that "we are projecting interest rates to remain at relatively low levels for an extended period". This comment was in response to the meteoric rise in term interest rates that had occurred over March. While the RBNZ wouldn't typically comment specifically on short-term market movements, in this case, they felt compelled to do so. Not only had the market moved a long way very quickly, but the move was potentially de-stabilising, and was completely inconsistent with the RBNZ's expectations.

We don't expect regular comment from the RBNZ in future, but the fact that they did feel the need to comment suggests that the Bank have a strong desire for term swap rates to remain low, and more accurately reflect the likelihood of the official cash rate (OCR) at low levels for an unusually long time. We expect this to be the more dominant force, at least over the next few quarters while other major economies conduct quantitative easing. The opposing forces are also likely to be reflected in lower swap spreads.

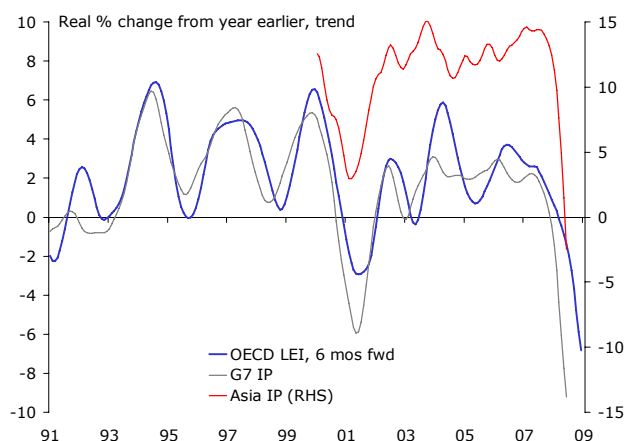
Commodities Outlook

Mark Pervan, Doug Whitehead and Julie Toth

Demand plummets, supply slower to react

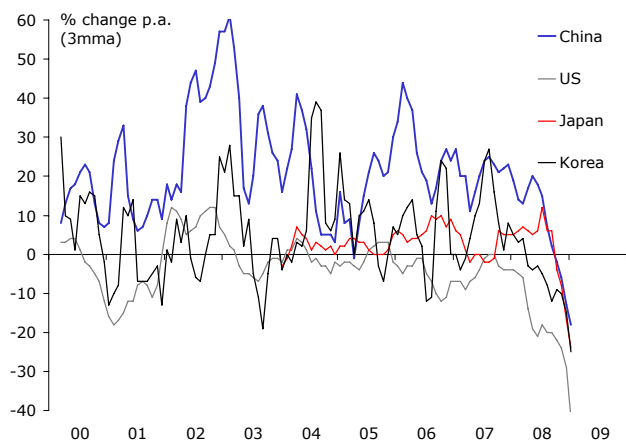
Over the past six months, global demand for energy, metals, bulks and minerals for industrial production, construction and other consumption purposes has tumbled to their lowest in a generation. Global automotive production for example, looks likely to fall by an unprecedented 20% in 2009. But with supply of many commodities slow to adjust, inventories are building for certain key products, including oil, steel and aluminium.

Industrial production has crashed world-wide



Sources: Datastream and ANZ Economics & Markets Research

Automotive production* has tumbled over 20%

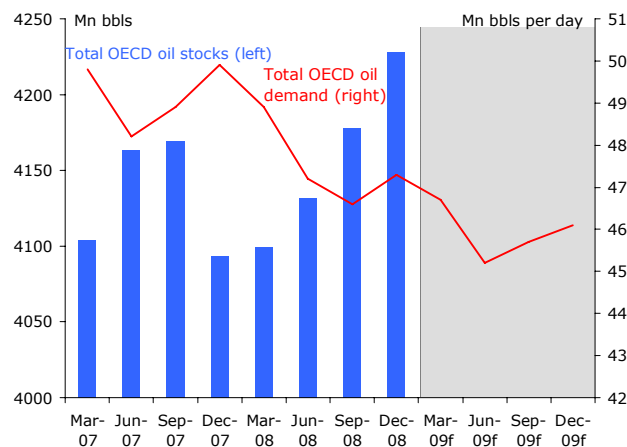


* Auto production indexes. Sources: Bloomberg

In March, the International Energy Agency (IEA) and OPEC cut their 2009 forecasts for oil demand for a seventh month and reduced supply estimates, as the global economic slump saps consumption and kills off new investment in oil and gas fields. Both organizations now see demand slumping by more than 1 million barrels a day this year. The IEA, adviser to 28 nations, reduced its global demand forecast to 84.4 million barrels a day, a decline of 1.25 million barrels from 2008. OPEC's estimate dropped to 84.6 million barrels, down 1.01 million barrels.

In the meantime, however, OPEC members may not be cutting production fast enough to match falling demand. A report from Petrologistics claims OPEC has delivered only 75% of agreed output cuts since September, as Iran, Angola and Venezuela continue to pump oil above the agreed levels. In conjunction with the US' growing crude oil stockpile — now at 356.6mmbbls, its biggest since 1993, according to the US Energy Information Administration (EIA) — and continuing weak demand, these supply issues will continue to destabilise oil prices.

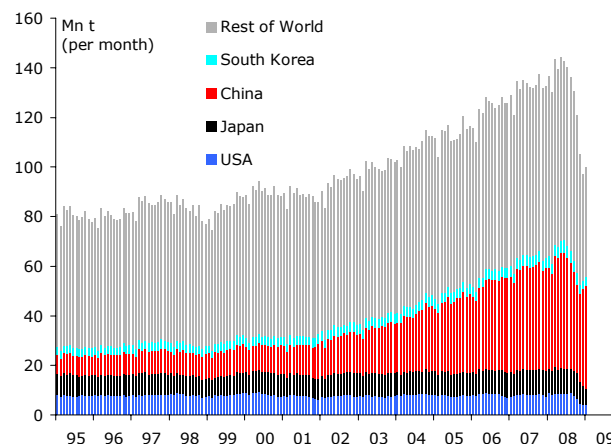
OECD oil stockpiles are rising as demand falls



Source: International Energy Agency

Demand for steel — and therefore iron ore — has also plummeted rapidly. In Germany (Europe's largest steel producer and seventh largest globally), annual steel output is now set to fall below 40mt in 2009 for the first time since 1993, as new orders plunged 47% in the final quarter of 2008 (the biggest drop in the post-war era). Japanese steel production has fallen at a similarly rapid rate, down more than 35% (YoY) by January 2009. Globally, steel production is estimated to have fallen a massive 60% (YoY) to January 2009, taking base metal prices down by a similar magnitude.

Global steel production has dropped 25%



Source: Bloomberg

A similar story is evident in aluminium markets, with Japanese demand for aluminium (used in packaging and especially in car and transport production), expected to fall about 11% in the 2009-10 Japanese

financial year, to its lowest level since 1986. LME inventories are building up as a result (above 3.4mt) and are set to peak later in 2009, by which time planned Russian cutbacks (17% of global capacity) will begin to take effect.

Energy and bulks face extended volatility

Prices for most hard commodities bottomed out in December 2008, with the combined delivery of Chinese and US stimulus packages restoring some confidence to the heavily battered market.

The question now for commodities is: can prices head onwards and upwards from here? We think not. Demand fundamentals for commodities – essentially the global growth rate – will be the worst in 2009 since WWII. Supply responses are being made, but they typically lag and underestimate the demand adjustments being made by large margins.

The commodity price trough is therefore likely to be extended and volatile, with a number of false recoveries triggered by perceived early signs of stimulus boosting demand and activity. Equity market bear rallies will also blur the landscape.

The best case scenario for commodities looks like a sustained (albeit mild) recovery from the September quarter of 2009. A recovering US equity market appears to be having a positive impact on commodities currently, but may well retrace ahead of the second quarter reporting season in June and July, which is expected to be very poor.

Under these conditions, precious metals and the less demand-elastic softs market should outperform energy, metals and bulks over the next 3 to 6 months. The oil and base metal markets will feel the pinch of a bear-rally correction, while the bulks (coal and iron ore) will nurse hangovers from a tough contract price negotiation season.

Agricultural commodities are best placed

Agricultural commodities have been underperforming over the last quarter. The global economic environment is finally beginning to impact their demand outlook and with an extended downturn forecast, upside potential will be limited to supply driven rallies. However, last quarter's performance must be put into context, with prices coming off a higher base than other commodity sectors. Once again, the softs remain the best placed amongst the Agricultural commodity complex. Coffee, cocoa and sugar are facing supply/demand deficits in 2009, which should at the very least provide a stable base for positive price movements.

Grains prices remain on the defensive

Initially, demand prospects for grains markets were expected to remain robust. But the current economic atmosphere is placing growing pressure on demand prospects. Already we have seen corn

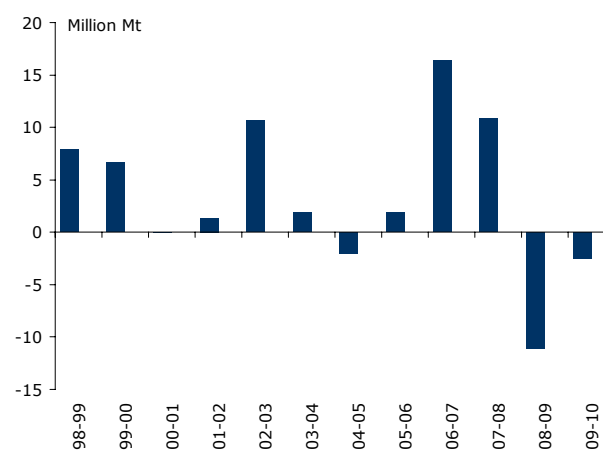
usage by the US ethanol industry decline significantly; this combined with reduced livestock numbers globally - which has reduced demand for feed grains - should lead to world feed grain stocks increasing considerably. Corn is also struggling to compete with low priced alternative feed grains. Supplies of barley and feed quality wheat remain plentiful and competition will continue to keep feed grain prices on the defensive.

Conversely, demand for wheat remains relatively healthy, due mainly to its classification as a food staple. But the strong production experienced in the 2008-09 crop year will see carryover stocks increase, alleviating the tight market conditions experienced in 2006-07 and 2007-08. Looking ahead to 2009-10, plantings are expected to decline globally by 3.5%. Using trend yields this translates into a 40Mn t reduction in production. While reduced 2009-10 supplies will mostly offset by a large 2008-09 carryout, the wheat market remains vulnerable to any supply-side shocks, which could prompt a weather driven rally. However we view these rallies as selling opportunities, as the underlying trend remains bearish.

Sugar still well positioned

The global sugar market remains in a strong position fundamentally. The world's second largest producer, India, will see a 46% reduction in domestic production, leading to India becoming a significant net importer in 2008-09. Lower production by other key exporters such as Australia and Thailand will also help to underpin prices. On the consumption side, sugar surprisingly has the lowest income elasticity of the agricultural commodities, meaning demand will remain robust throughout the economic downturn. In total the global sugar market is forecast to go into deficit in both 2008-09 and 2009-10 resulting in substantial stock draw-downs. While the fundamental picture is positive, a stronger USD should limit upside at or around US14¢/lb.

World sugar production goes into deficit



Sources: F.O. Licht & ANZ Commodities Research

International Economic Growth Forecasts

GDP	2007	2008(e)	2009(f)	2010(f)	2011(f)
US	2.0	1.1	-2.6	1.8	2.2
Japan	2.4	-0.7	-3.8	0.4	0.7
Germany	2.6	1.0	-2.9	0.7	1.4
France	2.1	0.7	-1.7	0.8	1.1
Italy	1.5	-1.0	-3.0	0.4	0.4
UK	3.0	0.7	-2.9	0.9	1.6
Canada	2.7	0.5	-1.6	1.4	2.4
G7	2.2	0.6	-2.8	1.2	1.7
Spain	3.7	1.2	-2.7	-0.3	1.6
Euro zone	2.6	0.7	-2.4	0.4	1.2
Australia	4.0	2.1	-0.9	0.7	2.9
New Zealand	3.2	0.2	-2.8	2.4	4.7
Developed countries	2.4	0.7	-2.6	1.1	1.7
China	13.0	9.1	6.9	8.5	10.0
Korea	5.1	2.3	-2.9	4.0	5.0
Taiwan	5.7	0.2	-1.8	3.9	4.6
Indonesia	6.3	6.1	4.5	5.1	6.4
Thailand	5.0	2.5	1.9	3.9	5.6
Hong Kong	6.3	2.6	-1.8	4.2	4.7
Malaysia	6.3	4.7	2.1	4.2	6.0
Singapore	7.8	1.3	-3.0	3.4	5.6
Philippines	7.1	4.6	1.4	3.9	5.1
Vietnam	8.5	6.4	6.6	7.5	7.0
East Asia excl. Japan & China	6.0	3.2	0.4	4.4	5.6
East Asia excl. Japan	10.2	6.8	4.5	7.0	8.4
India	9.2	7.4	5.3	6.9	8.0
South Asia	8.7	6.9	4.9	6.4	7.3
Eastern Europe	7.2	5.3	-0.3	2.4	3.6
Latin America	5.7	4.1	0.4	2.6	2.6
Emerging countries	8.4	5.9	2.9	5.3	6.3
World (PPP)	5.0	3.0	-0.1	3.0	3.9

Australian and New Zealand Economic Forecasts

	Annual % change (period average)				Quarterly % change			
	2008	2009 (f)	2010(f)	2011 (f)	Mar-09(f)	June-09(f)	Sep-09(f)	Dec-09(f)
Australia								
GDP	2.1	-0.9	0.7	2.9	-0.5	-0.1	0.0	0.1
Household consumption	2.1	-0.2	0.7	2.6	-0.3	0.1	-0.1	-0.2
Dwelling investment	2.0	-5.1	9.6	11.0	-4.1	-2.1	0.9	2.8
Business investment [^]	12.8	-7.6	-17.5	1.5	-1.9	-5.2	-5.9	-6.7
Public demand [^]	5.1	3.4	5.2	2.9	0.6	0.9	1.9	1.9
<i>Domestic final demand</i>	4.1	-1.2	-0.7	3.0	-0.6	-0.8	-0.6	-0.6
Net Exports (cont. to growth)	-1.4	1.7	1.4	-0.8	0.0	0.4	0.6	0.7
Inflation: Headline CPI	4.4	2.6	2.8	2.7	0.9	0.4	0.9	0.9
Core	3.6	2.1	2.7	2.6	0.8	0.7	0.7	0.7
Wages (Wage Price Index)	4.2	3.9	3.4	3.6	0.9	0.9	0.9	0.8
Employment	2.2	-0.3	-1.1	1.5	-0.1	-0.3	-0.4	-0.5
Unemployment rate (%)	4.2	6.0	8.1	8.3	5.1	5.6	6.3	7.0
Current account balance (A\$ bn)	-50.1	-36.4	-42.6	-53.7	-5.3	-8.4	-11.6	-11.0
(% of GDP)	-4.2	-3.0	-3.5	-4.2	-1.8	-2.8	-3.9	-3.7
New Zealand								
GDP	0.2	-2.8	2.4	4.7	-1.5	-0.5	0.0	0.1
Inflation: Headline CPI	4.0	2.2	2.4	2.5	0.3	0.8	0.6	0.7
Wages	5.0	3.4	1.7	1.6	0.8	0.7	0.5	0.4
Employment	0.6	-1.7	-0.7	2.1	-1.0	-0.8	-0.4	0.0
Unemployment rate (%)	4.1	6.3	7.6	7.0	6.1	6.8	7.3	7.7
Current account balance (NZ\$ bn)	-16.0	-10.3	-10.0	-10.0	-2.9	-2.5	-2.4	-2.4
(% of GDP)	-8.9	-5.9	-5.5	-5.2	-8.7	-7.4	-6.6	-5.9

[^] Excluding second-hand asset sales

Financial Market Forecasts

	Annual (period end)				Quarter (period end)			
	2008	2009(f)	2010(f)	2011(f)	Mar-09	Jun-09(f)	Sep-09(f)	Dec-09(f)
Interest rates (% p.a.)								
<i>Australia</i>								
Cash rate	4.25	2.00	2.75	4.75	3.25	2.75	2.50	2.00
3-year bond rate	3.07	3.05	4.65	5.20	3.40	3.25	3.20	3.05
10-year bond rate	3.99	4.15	5.35	5.40	4.42	4.35	4.30	4.15
<i>New Zealand</i>								
Official cash rate	5.00	2.50	4.00	5.80	3.00	2.50	2.50	2.50
10-year bond rate	4.90	4.30	5.70	6.40	5.40	4.40	4.30	4.30
<i>United States</i>								
Fed funds rate	0.25	0.25	2.00	4.25	0.25	0.25	0.25	0.25
3-year bond rate	0.76	0.85	2.75	4.50	0.80	0.75	0.80	0.85
10-year bond rate	2.21	2.70	4.15	5.00	2.66	2.65	2.65	2.70
<i>Europe</i>								
ECB refinace rate	2.50	1.25	2.50	3.00	1.50	1.25	1.25	1.25
BoE repo rate	2.00	0.50	2.00	3.50	0.50	0.50	0.50	0.50
Exchange rates								
A\$/US\$	0.70	0.54	0.60	0.70	0.69	0.62	0.58	0.54
NZ\$/US\$	0.58	0.45	0.46	0.52	0.56	0.49	0.47	0.45
A\$/¥	63.68	55.08	67.20	80.50	68.41	62.00	58.58	55.08
A\$/€	0.50	0.49	0.53	0.57	0.52	0.50	0.49	0.49
A\$/£	0.48	0.36	0.35	0.35	0.48	0.42	0.39	0.36
A\$/NZ\$	1.21	1.20	1.30	1.35	1.24	1.27	1.23	1.20
US\$/¥	90.6	102.0	112.0	115.0	99.0	100.0	101.0	102.0
€/US\$	1.40	1.10	1.14	1.22	1.33	1.25	1.18	1.10
A\$TWI	55.60	47.09	51.39	58.18	57.40	52.85	49.89	47.09

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