NEW ZEALAND ECONOMICS
ANZ CREDIT FOCUS

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INSIDE

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REBUILDING

FEBRUARY IN REVIEW

Middle Eastern street protests dominated global headlines in February, and continue to simmer across the region, driving up oil prices. Libya now hangs in the balance. Fed Chair Bernanke appeared to be in no hurry to alter policy, but there is growing division among the BOE's MPC. The earthquake in Christchurch on February 22nd was the major local event, and has led to a rapid swing in monetary policy expectations.

ECONOMIC AND MARKET BACKDROP

The Christchurch earthquake has changed the whole economic picture. We expect at least a 1 percentage point hit to Q1 GDP growth, with more likely in Q2. The rebuild effort will be massive, but significantly delayed. Meanwhile, the income-generating part of the economy continues to be underpinned by high commodity prices. The two-speed economy theme just got turbo-charged, something the RBNZ will be mindful of. A cut is likely on March 10, but with global inflation rising, rates cannot stay low forever.

PERFORMANCE MONITOR

The ANZ Govt Bond Index was the poorest performing index in February. Although most NZGS yields fell over the month, yields on the NZGS 3/19 and 5/21 bonds rose slightly, with duration contributing very little overall to returns. By contrast, the inversion of swap spreads and a rapid swing in monetary policy expectations drove significant outperformance of the ANZ swap and credit indices.

SWAP AND BASIS SWAP SPREAD UPDATE

Swap spreads have moved back toward historic negative extremes at the long end of the curve. Much of the movement came after the Christchurch earthquake, and in our view is reasonably well justified, particularly at the long end. We would also caution against generalising, as we do expect short end spreads to normalise on the back of increased liquidity. Basis swap spreads have contracted, and are likely to continue doing so as credit growth and offshore issuance slows down.

GOVERNMENT BOND TENDER WATCH

The DMO issued $1.1bn of bonds in February, taking total issuance for the fiscal year to date to $11.1bn, keeping issuance well ahead of schedule for this fiscal year to date. The fact that the Crown has pre-funded to this degree is good news given the Christchurch earthquake, with much larger borrowing programmes likely over the next few years. Although overall bid cover improved and tail width narrowed, the overall duration of risk sold was lower, and for the first time ever, a tranche of bonds attracted no bids.

SPECIAL REPORT: CHRISTCHURCH EARTHQUAKE

We present a summary of our previously published special report on the Christchurch earthquake, which is available on request, or on our Bloomberg page, ANZR2 <Go>.

FEBRUARY IN REVIEW

SUMMARY

Middle Eastern street protests dominated global headlines in February, and continue to simmer across the region, driving up oil prices. Libya now hangs in the balance. Fed Chair Bernanke appeared to be in no hurry to alter policy, but there is growing division among the BOE's MPC. The earthquake in Christchurch on February 22nd was the major local event, and has led to a rapid swing in monetary policy expectations.

- Street protests in Egypt that had started in late January escalated dramatically, and by early February at least a million people had rallied across towns and cities in Egypt, calling for an end to President Mubarak's rule. The army responded by saying that it would not fire on protesters, who they believed had legitimate grievances, and the right to protest. The President later stood down, and the success of the protesters led to protests elsewhere.
- Cyclone Yasi did significant damage to Queensland early on in February, bringing with it massive waves and gusts of up to 290 km/h, adding to Australia's weather woes.
- Early-in-the-month data in the US had a decidedly upbeat tone about it, with the ISM manufacturing survey jumping from 58.5 to 60.8, only to be matched by a jump from 57.1 to 59.4 from its non-manufacturing counterpart. At these levels, they are at their highest levels in 5 years.
- However, US employment data was mixed. Non-farm payrolls rose by only 36k in January, well below expectations of a 145k increase. However, the unemployment rate unexpectedly fell from 9.4 to 9.0 percent – still a scary number but at least heading away from double digits. Optimists ascribed much of the payroll's weakness to the severe winter storms that hit the US, focussing instead on the 589k increases in employment from the household survey measure.
- The UK Government announced that it would temporarily charge banks 0.1 percent on short-term liabilities and 0.05 percent for long-term liabilities in March and April. This levy will enable the government to raise £2.5b in the April financial year. The UK financial services industry generates about 12 percent of UK tax revenue according to some estimates. The aim of the government is to raise £10b by 2015 by taxing bank balance sheets as a means to narrow the UK fiscal deficit.
- The PBOC raised the one year lending rate from 5.81 percent to 6.06% in early February, delivering the second hike in just over six weeks, and illustrating the challenge authorities have in offsetting stubbornly high inflation. With higher food prices set to push annual CPI inflation to 5.3 percent in January, analysts fear this rate hike will not be the last. The deposit rate (at 3 percent) remains almost 2 percentage points less than annual inflation, which does little to encourage saving.
- Fed Chair Ben Bernanke maintained a guarded tone in written testimony in front of the House Banking Committee. He said that there was increased evidence that a self-sustaining recovery in consumer and business spending may be taking hold. However, "until we see a sustained period of job creation, we cannot consider the recovery to be truly established". While the sharp drop in the unemployment rate was "grounds for optimism", the economy has only regained one million of the nearly nine million jobs lost during the recession. Furthermore,

"with output growth likely to be moderate for a while and with employers still reluctant to add to their payrolls, it will be several years before the unemployment rate has returned to a more normal level". He added that "inflation is expected to persist below the levels that Federal Reserve policymakers have judged to be consistent" with their mandate, suggesting the Fed is in no hurry to scale back QE2.

- Moody's reaffirmed its Aa2 sovereign credit rating for Japan, but warned that a lack of progress on the reform front would be viewed negatively. Last month S&P downgraded its Japanese sovereign rating, for the first time in nine years.
- The Bank of England kept interest rates and their Asset Purchase Programme unchanged at its February meeting. Although we didn't know at the time, the minutes later revealed some very different views on the outlook and policy path by members of the MPC.
- Egyptian President Hosni Mubarak reluctantly stood down over the weekend of 12-13th February, having lost the support of the army, causing jubilation on the streets.
- Axel Weber, head of the Bundesbank, inflation hawk, and heir apparent to Jean Claude Trichet as head of the ECB, announced he will be resigning at the end of April. His departure comes at an interesting time, and throws the field open to potential candidates to succeed Trichet when his term as ECB President expires on October 31st,
- US President Obama proposed to halve the US fiscal deficit by 2013 and to shave US $1.1 trillion off the deficit over the next decade. It meets the pledge the US made at the G20, and while two-thirds of the savings will come from spending cuts, the Republicans plan to make high government spending a 2012 presidential election issue.
- UK inflation surged in January following the increase in VAT, taking the annual headline reading to 4.0%, twice the Bank of England's 2.0% target. Despite this, BOE Governor King appeared in no hurry to raise the Bank Rate, noting in his open letter to the Chancellor of the Exchequer (and confirmed in the inflation report the following day) that he expected inflation would likely be back near the Bank's 2% target in 2 year's time. However, King did add that he "did not wish to conceal that there are real differences of view within the Committee", as the minutes later revealed.
- Middle East protests started spreading. First it was Tunisia; then Egypt, and in February, protests spread to Yemen, Bahrain and Libya, with the citizenry calling for democracy. We're no experts on Middle East politics, but at face value, a clear trend is emerging, and the consequences for oil could be significant, particularly now that key US allies (Bahrain) and oil producers (Libya) are in the mix.
- Brent crude steadied close to a two and a half year high on Middle East tensions. Discontent over rising food prices, high youth unemployment and high levels of corruption have been the major catalysts, with fears that sectarian divisions could further escalate conflicts. News that two Iranian war ships were to go through the Suez Canal only served to increase tensions, in what Israel described as "a provocation".
- Federal Reserve Bank of Dallas President Richard Fisher said he'll be among the first to recommend tighter policy as the economy improves, but added that one possible first step may be the sale of some of the

Fed's Treasury bonds acquired during QE. "One could make an argument that the most logical thing to do is to undo what you did last". Exit strategies still seem distant, but we need to keep them in the back of our minds. If this were to be how things eventuated, it would pose serious challenges to the textbook theory that the yield curve ought to flatten prior to policy tightening.

- The State Bank of Vietnam raised the refinancing rate from 9 percent to 11 percent. Inflation, at 12 percent, remains considerably above the 7 percent target. This is the second hike since November.
- China raised the bank-reserve requirements for the eighth time in 12 months in response to higher inflation pressures. The yuan immediately strengthened to its highest level since 1993.
- The February G20 meeting saw countries dish out more unwanted advice to each other regarding easing the global imbalances that many see as being at the heart of the global financial crisis. Federal Reserve Chairman Ben Bernanke had another crack at "some countries" who maintained undervalued currencies, causing "unbalanced and unsustainable" patterns of global spending. He did concede, however, that some other unnamed countries needed to do their bit by, among other things, "putting fiscal policies on a more sustainable trajectory". China for their part are angry that the US quantitative easing programme is sending a flood of money abroad looking for better returns, putting pressure on their exchange rate. After much debate, G20 finance ministers agreed on a non-binding "scorecard" to highlight economic imbalances. China objected to foreign reserves and current account balances being included, the two measures on which its growth is most obviously imbalanced. The next challenge is to create guidelines from these scorecards.
- Political unrest continued to spread in the Middle East, and in some cases have been met by a heavy-handed government response. Indeed, governments have cracked down with varying severity on protests in Yemen, Algeria, Libya, Bahrain, Iran, Djibouti, Kuwait and Jordan, worried that protests may gather the kind of momentum that toppled the leaders of Tunisia and Egypt. High food prices have played a part in the unrest – hungry people are angry people – and this is perhaps just a foreshadowing of the political instability that higher food prices can bring.
- Tensions in Libya continued to escalate, and by late February anti government protesters/rebels had taken the city of Benghazi. Muammar Gaddafi responded by ordering an air force plane to bomb the nearby oil fields, but the pilot apparently refused, and ejected instead. Other air force pilots have defected, flying their planes to Malta, but Gaddafi remains defiant, and has said he will stay in Libya, preferring to die as a martyr.
- The Bank of England inched closer to raising rates. Minutes from the BOE's February meeting showed that another MPC member (Dale) joined Sentance and Weale in calling for a rate hike. Sentance also "upped" his call from a 25bp hike to a 50bp hike, citing inflation concerns. And while opposing dissenter Posen continued to call for an extension to the Asset Purchase Facility, the minutes noted that "Of those members not favouring a rise in Bank Rate, some thought that the case for an increase had nevertheless grown in strength".

FEBRUARY IN REVIEW

MAJOR NZ EVENTS (IN CHRONOLOGICAL ORDER)

- Dairy prices rose at Fonterra's early February globalDairyTrade auction, with average prices rising 7.2 percent to US$4,246 per tonne. At this level, average prices reached their highest levels since the first auction in July 2008, prior to the GFC.
- Statistics NZ reported that the unemployment rate rose from 6.4% to 6.8% in Q2, reversing the prior quarter's decline, and raising questions over the state of the jobs market.
- Dairy prices surged at Fonterra's mid February globalDairyTrade auction. The 3.9 percent increase in the average price US$4,540 per tonne was the highest since auctions began, and contributed to yet another rise in the ANZ commodity price index to a new record high. A "perfect storm" of limited supply, firm demand and US dollar were in evidence. Larger rises were evident for shorter-term contracts.
- Fonterra increased its forecast payout range (before retentions) for the 2010/11 season from $7.30-$7.40 to $7.90-$8.00 on the 22nd February. The forecast payout incorporates a forecast milk price of $7.50 per kilogram of milk solids (kg MS), 60 cents higher than the previous forecast; and a distributable profit range for the 2011 financial year of 40-50 cents per share (unchanged from previous forecast). Fonterra reduced the target dividend range to 25-30 cents per share (previously 25-35 cents per share). As a consequence, Fonterra now forecasts that a 100 per cent share backed farmer will receive, on a cash basis, a total of $7.75-$7.80, with the balance of distributable profit being retained by the Co-operative. The latest increase, combined with a 30 cents increase announced last December, means the forecast Milk Price for 2010/11 is now 90 cents higher than the season's opening forecast of $6.60 per kg MS, and $1.40 ahead of the 2009/10 season..
- Christchurch was hit by a magnitude 6.3 earthquake at 12.51pm on February 22nd. The quake caused significant damage, with at least 163 confirmed deaths, and a final death toll expected to be close to 200 people. The damage estimate stands at $15bn at the moment, on top of an estimated $5bn of damage from the September 4th quake.

ISSUANCE

February saw a pick up in issuance after the slow start to the year. This was predominantly in the stronger AA credit space with issuance in wholesale format coming to market. The Kauri market also witnessed its first issue in six months with conditions remaining challenging for that market.

Issuance over the Previous Month (in chronological order)					
Issuer	Rating	Amount	Coupon/ Yield	Tenor	Spread
Rentenbank	AAA	$50m	5.59%	3.6yrs	Swap + 54
ANZ National	AA	$100m	6.85%	7.0yrs	Swap + 180
ANZ National	AA	$150m	6.315%	5.0yrs	Swap + 165
Watercare Services	AA	$150m	5.74%	4.0yrs	Swap + 133
Wellington City Council	AA+	$25m	FRN	5.0yrs	BKBM + 130

FEBRUARY IN REVIEW

UPCOMING MATURITIES

Details of Forthcoming Bond Maturities				
Issuer	Rating	Maturity	Coupon %	Amount
Auckland CC	AA	15/03/11	FRN	$50m
Powerco	BBB	29/03/11	6.22%	$100m
Dunedin City Treasury	AA	15/04/11	8.70%	$90m
Westpac	AA	18/04/11	8.87%	$362m
Westpac	AA	18/04/11	FRN	$269m
Fonterra Co-Operative	AA-	21/04/11	6.64%	$100m
ANZ National	AA	27/05/11	FRN	$170m
ASB	AA	21/05/11	FRN	$325m
ASB	AA	23/05/11	8.42%	$158m
BNZ	AA	20/05/11	FRN	$170m
Morgan Stanley	A+	30/05/11	FRN	$75m

NOTABLE RATINGS ACTIONS*

2 February – Fitch Ratings affirmed stable ratings on two tranches of **Sapphire IV NZ Series 2007-1 Trust** that Fitch had downgraded during the prior quarter due to 'poor performance of the transaction'.

7 February – S&P released a bulletin outlining if the NZ government was to sell minority stakes in the three state-owned generator retailers – **Mighty River Power Ltd** (BBB+/Negative/-), **Genesis Power Ltd.** (BBB+/Stable/-), **and Meridian Energy Ltd**. (BBB+/Stable/A-2, that there was unlikely to be any effect on the rating uplift that has been applied due to the 'important' role the three are seen to play in the NZ economy.

11 February – Watercare Services Ltd. (A/Positive/A-1) received an 'AA' rating for the unsubordinated, unsecured, wholesale bonds to be issued the following week. S&P noted that the rating reflects their 'expectation that the bonds will have the benefit of the guarantee' from Auckland Council (AA/Stable/A-1+).

16 February – Moody's placed NZ major banks' ratings on review for downgrade. Long-term senior unsecured debt and deposit ratings of **ANZ National Bank Ltd., ASB Bank Ltd., and Westpac New Zealand Ltd**. were placed on review due to the 'structural sensitivity to wholesale funding market conditions', Moody's stated. The review follows a similar placement of the parent banks.

22 February – Fitch affirmed **Contact Energy Ltd** at 'BBB' with a stable outlook. Fitch noted that Contact's 'commitment to additional generation capex will not materially weaken its credit profile'.

22 February – Fitch commented on the immediate impact of the Christchurch earthquake, that the event was 'not likely itself to trigger [a] negative action'.

FEBRUARY IN REVIEW

23 February - Moody's stated, after the Christchurch earthquake, that it did not see an immediate impact on **New Zealand's sovereign credit rating**. They added that the earthquake was likely to have a larger effect on the NZ government than the previous earthquake, but noted that debt levels were well below the median of other Aaa-rated governments.

23 February – S&P made comments that the Christchurch disaster would place 'further downward pressure on the earnings of the general insurers in New Zealand, but the capital strength and extensive reinsurance protection of insurers would limit negative rating pressure at this stage'.

24 February – Following the earthquake, Fitch and Moody's both noted that there would be no immediate rating impact on **NZ and Australian insurers**. Moody's advised that the full cost was still unclear.

24 February – **The Earthquake Commission** (AAA/Stable/-) had its ratings affirmed by S&P. S&P stated that the EQC had significant exposure to the earthquake in Christchurch, but that given that the EQC is financially well structured the obligations will be able to be met. Furthermore, S&P suggested that the NZ government could be called upon for further legislative support.

25 February – S&P released a statement regarding **New Zealand's sovereign credit rating**, (AAA/Negative/A-1+), as well as the ratings of **Christchurch City Council** (CCC, AA+/Negative/A-1**+), Christchurch City Holdings Ltd**. (AA+/Negative/A-1+), and **Christchurch International Airport Ltd.** (CIAL, A-/Stable/A-2). The statement noted that the ratings on the entities were not immediately impacted. S&P expected that the government had 'sufficient flexibility to absorb additional fiscal costs without a negative impact on its creditworthiness'. In terms of CCC, S&P views that the council has the capacity to take on additional debt but that ratings pressure may come from either a significant deterioration in 'revenue of both the council [and] the regional economy'. CIAL's operations were largely unaffected by the earthquake, and S&P expected that CIAL would see reimbursement via insurance. Ratings pressure would come upon CIAL if tourism received negative sentiment and 'prolonged negative impact on passenger traffic'.

25 February – Given the earthquake in Christchurch, S&P advised that there may be downward pressure on financial sector ratings, 'particularly those in the Canterbury region'. S&P elaborated that the medium to long-term effects on the broader NZ economy are not yet clear.

** Sources: Bloomberg, Reuters, Standard & Poor's RatingsDirect, Moody's, Fitch Ratings, ANZ.*

ECONOMIC AND MARKET BACKDROP

SUMMARY

The Christchurch earthquake has changed the whole economic picture. We expect at least a 1 percentage point hit to Q1 GDP growth, with more likely in Q2. The rebuild effort will be massive, but significantly delayed. Meanwhile, the income-generating part of the economy continues to be underpinned by high commodity prices. The two-speed economy theme just got turbo-charged, something the RBNZ will be mindful of. A cut is likely on March 10, but with global inflation rising, rates cannot stay low forever.

Early indications for the New Zealand economy in 2011 had looked relatively promising. Financial conditions remain extremely supportive. Commodity export prices continue to hit record highs. Consumer confidence was lifting and the housing market appeared to be stabilising. Investment looked set to recover from cyclical lows.

But the outlook changed completely with the Christchurch earthquake of February 22. Beyond initial disruption effects, the hit to wealth was immense; the rebuild effort will be enormous. While rebuilding counts as economic growth, much will come at the cost of growth elsewhere. It will also be significantly delayed by bottlenecks in insurance assessments and, this time, by big picture planning requirements. Very few houses have been built in the past couple of years, and housing shortages are now going to be an issue in both the south and the north.

The two speed economy theme just became extreme. Some parts of the economy are doing extremely well. Commodity prices are at record highs and it isn't just dairy prices this time. Normally a boom in our terms of trade presages boom times in the economy. Not this time, but it's still a big income boost. New Zealand will need it to help absorb the shock of the earthquake.

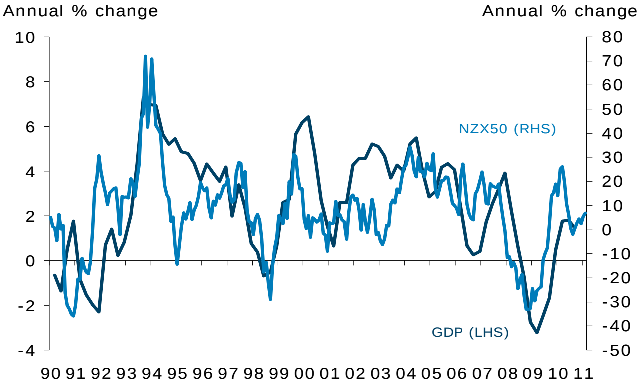
Retailers will continue to struggle, especially in Christchurch. Earthquake wealth destruction (via under-insurance, falls in land prices in some areas and an inability to sell some properties at any price), will be reinforced by negative confidence impacts. And this comes on top of high food prices, still-high household debt, and now a petrol price above $2/litre, the generally recognised pain threshold. Put all that together and a mortgage rate cut isn't going to get NZ consumers spending.

The RBNZ faces a tricky time, with a single blunt tool to address disparate conditions in different sectors. If the housing market gets a head of steam up due to shortages, on top of sharp rises in the price of food and energy, then they will be looking at an inflation problem not too far down the track unless it takes preventative action. A rate cut is likely on March 10, but rates will not stay low indefinitely, with policy set to be normalised in 2012.

Indicator	Level	Direction	Comment
Hi-low beta stock index	Elevated	Rising	The trend rise in the NZX is encouraging, but may be optimistic.
Sovereign risk	AA+	At risk	Our gauge has improved, but fiscal position will deteriorate significantly.
Macro momentum	Mildly positive	Earthquake a game changer	Bus confidence and anecdotes were picking up -the quake changed that.
Financial conditions	Supportive	Improving	Financial conditions just got easier, but that needs to after the quake.
Risk aversion	Neutral	Stable	Markets are back to fairly normal levels of risk aversion.
Cost of credit	Elevated	Stable	Local bank CDS spreads remain stable. Credit growth set to slow.
Liquidity conditions	Illiquid still	Improving	Set to improve sharply as Chch insurance payouts see loans repaid.

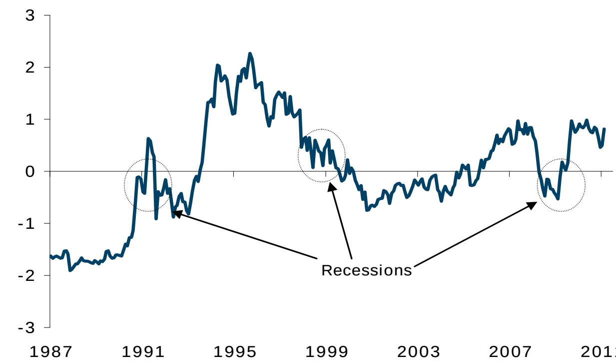
ECONOMIC AND MARKET BACKDROP

NZ equity market returns and GDP



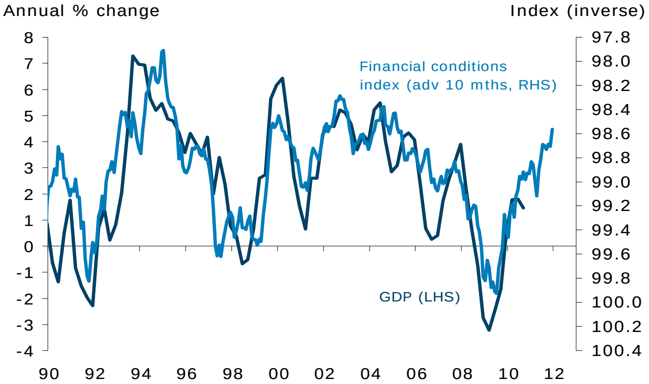
Sources: ANZ, Statistics NZ, Bloomberg

Equity beta



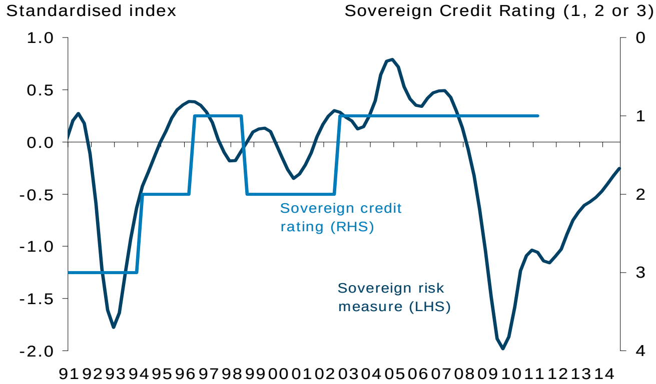
Sources: ANZ, NZX

Financial conditions and GDP



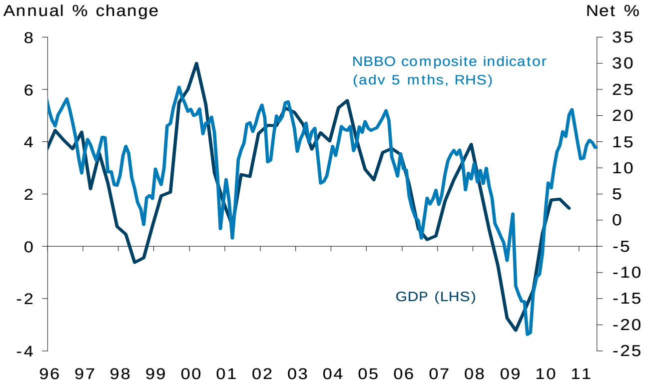
Sources: ANZ, Statistics NZ

Sovereign risk gauge



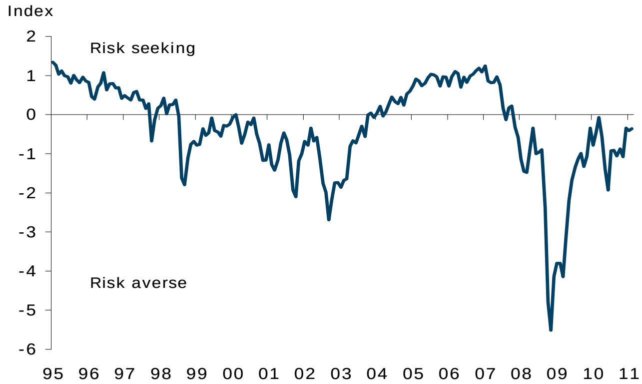
Sources: ANZ, NZ Treasury

NBBO composite indicator and GDP



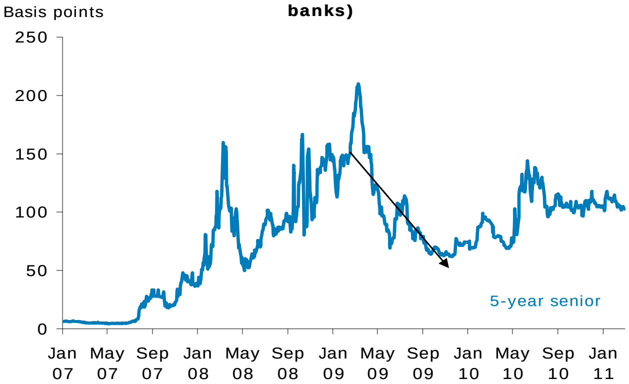
Sources: ANZ, Statistics NZ

Composite risk aversion measure



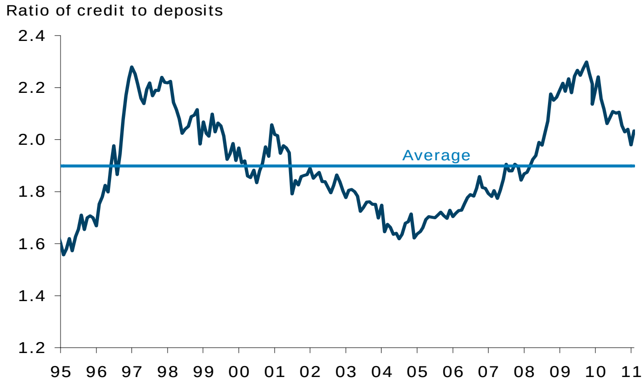
Sources: ANZ, Bloomberg

Cost of credit (CDS spread for 'Big-4' Australian banks)



Sources: ANZ, Bloomberg

Corporate (business) liquidity



Sources: ANZ, RBNZ

PERFORMANCE MONITOR

PERFORMANCE MONITOR – ANZ DEBT INDICES

The ANZ Govt Bond Index was the poorest performing index in February. Although most NZGS yields fell over the month, yields on the NZGS 3/19 and 5/21 bonds rose slightly, with duration contributing very little overall to returns. However, NZGS bonds put in an exceptional performance in January – recall the NZGS 5/21 bond rallied a staggering 39.5 basis points. By contrast, the inversion of swap spreads and a rapid swing in monetary policy expectations (from expecting a hike by October to expecting a cut in March) has led to a large rally in swap and corporate bond yields, driving significant outperformance of the ANZ swap and credit indices.

ANZ Index Returns for Periods Ended Last Month

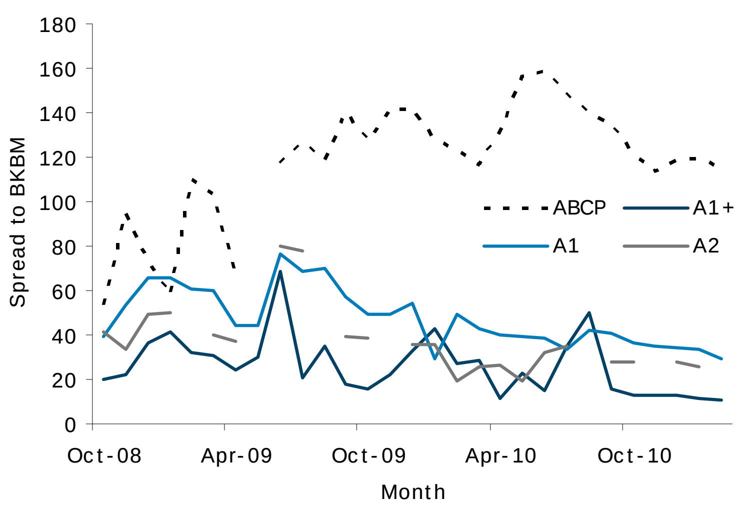
Index	Last month	Last 3 months	Last 12 Months
ANZ Govt Bond Index	0.72%	2.25%	6.59%
ANZ All Swap Index	1.44%	2.64%	8.34%
ANZ Corp A Grade	1.59%	2.81%	8.55%
ANZ Corp Investment	1.62%	2.90%	8.83%
NZX 50 Gross Index	0.95%	3.25%	6.79%

Source: Bloomberg and NZX

COMMERCIAL PAPER

- February was a strong month for commercial paper. Volumes increased to 463.4m being tendered (from 273.0m in January). Spreads were tighter across the board, with A-1+ tenders averaging +10.7.
- Auckland Council came to market with their debut tender that went very well. With the 100.0m tender, bids were covered 2.95x.
- February saw further issuance from unrated councils ahead of the proposed bond bank. This is expected to continue, such paper is favoured by a number of investors who perceive them as offering additional spread for a similar risk to that of the larger rated councils.

CP Credit Margins



Continued overleaf /

PERFORMANCE MONITOR

3-month Commercial Paper Margins for the Previous Month				
Margin	A-1+ (excl ABCP)	A-1	A-2	A1+ ABCP
Median	10.8	29.0	-	114.7
Low	8.5	29.0	-	113.7
High	12.1	29.0	-	115.7

Source: ANZ

Upcoming Commercial Paper Maturities			
Issuer	Rating	Maturity	Amount
WCC	A-1+	1-Mar	$5.0m
Telstra	A-1	9-Mar	$50.0m
Chch City Hold	A-1+	7-Mar	$22.0m
DCT	A-1+	21-Mar	$11.0m
Hutt City	A-1+	21-Mar	$11.0m
NPDC	A-1+	9-Mar	$10.0m
NZ Post	A-1+	2-Mar	$20.0m
Watercare	A-1+	21-Mar	$35.0m
WCC	A-1+	1-Mar	$5.0m
WRCH	A-1+	14-Mar	$40.0m
RFS	A-1+*	23-Mar	$24.0m
AIAL	A-2	15-Mar	$20.0m

Commercial Paper Issuance Details for the Previous Month				
Issuer	Rating	Maturity	Amount	Weighted Average Margin (bps)
CCC	A-1+	29-Apr	$5.0m	12
Telstra	A-1	4-May	$76.0m	29
NZ Post	A-1+	3-May	$20.0m	8.5
CHCH City Holdings	A-1+	9-May	$26.0m	12
RFS	A-1+*	9-May	$22.7m	115.7
Transpower	A-1+	16-May	$45.0m	11
NPDC	A-1+	19-May	$10.0m	10
NPDC	A-1+	19-May	$10.0m	10
RFS	A-1+*	23-May	$22.7m	113.72
Watercare	A-1+	30-May	$40.0m	12.1

** Asset-backed*

RELATIVE VALUE MONITOR

RELATIVE VALUE MONITOR

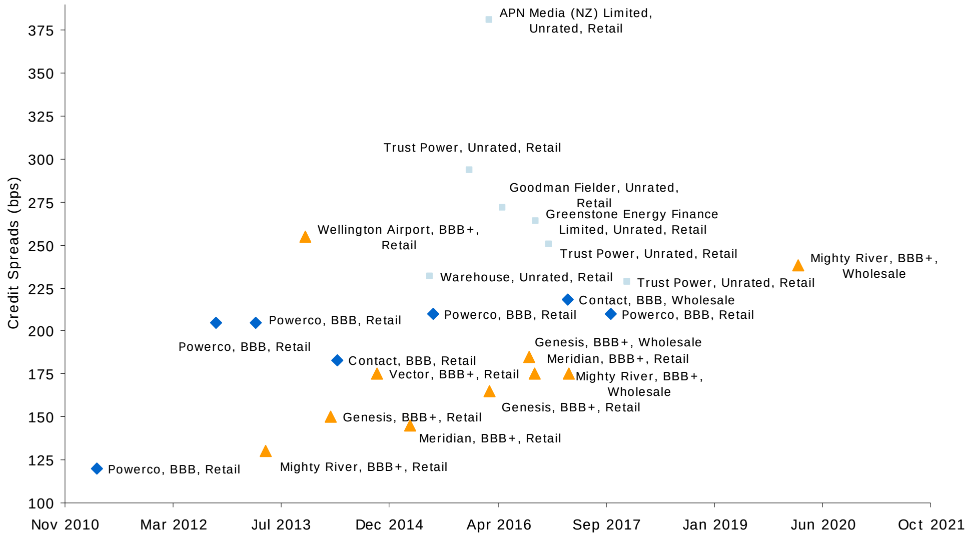
The aggressive move lower in underlying swap yields has presented investors with attractive buying opportunities as bond yields have struggled to keep pace and spreads have marched wider. This window of opportunity may be short-lived as local banks seem intent in lowering term deposit rates and investors scramble for higher yielding products. In this section we analyse some of the relative value opportunities that currently exist in the market bearing in mind that some of the issues displayed above may have distortions due to a lack of supply.

In the BBB+ sector, the Vector 7.80% Oct 14's which sits well above its BBB+ rating peers. The Wellington Airport Nov 13's are trading at a wider spread, but bear in mind that there is extremely limited volume available on the NZDX at the spreads shown below.

Energy companies Contact and Powerco make up the BBB sector. The scatter plot below of the relative curves suggests Powerco represents the better value in the shorter tenor bonds.

With no common rating, it might be considered a little tenuous to draw conclusions from the spread/maturity placement of the unrated securities. Nevertheless it is difficult to ignore the current spread on offer from the APN Media 7.86% Mar 16s. The bonds issue margin of 3.10% determined a 7.86% coupon when it was set on the 15th December 2010. Underlying interest rates around that time represented 7 month highs and the unrelenting rally in yields since APN's rate set is a likely contributor to the blow out in spread to a current level of 395bp (generating an outright yield of around 8.30%). The Christchurch quake has recently accelerated the move lower in underlying swap yields and has led markets to price in short term rate cuts by the RBNZ – if this eventuates and should deposit rates follow suit, APN may be just the type of asset investors consider in their search for better yield.

Senior BBB / Unrated Corporate Credit Spreads February 2011



Source: ANZ

SWAP AND BASIS SWAP SPREAD UPDATE

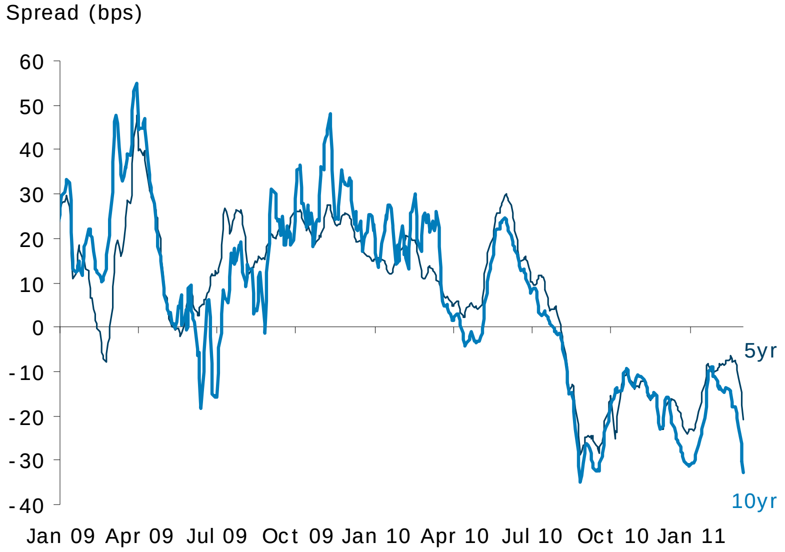
SUMMARY

Swap spreads have moved back toward historic negative extremes at the long end of the curve. Much of the movement came after the Christchurch earthquake, and in our view is reasonably well justified, particularly at the long end. Bond issuance will rise, but the market can probably absorb this, making it less likely that swap spreads plumb to more negative extremes. We would also caution against generalising, as we do expect short end spreads to normalise on the back of increased liquidity. Basis swap spreads have contracted, and are likely to continue doing so as credit growth and offshore issuance slows down.

SWAP SPREADS

Swap spreads remain volatile, having normalised over January, only to then invert over February, moving sharply negative in the days following the quake as the chart below demonstrates.

NZD Swap Spreads



Sources: ANZ, Bloomberg

Regular readers will recall we took a mildly negative view on swap spreads last month, noting that while the arguments in favour of more inverse spreads were stronger, there were a number of opposing forces at play. Indeed, while we felt the steep slope of the swap curve and tighter fiscal policy discouraged swap paying (thus arguing for more inverted swap spreads), we were mindful of the potential for a pick up in inflation and the erosion of confidence in global central bank's ability (or desire) to do anything about it to lead to increased swap paying interest. Similarly, as we move closer to the point where the RBNZ was poised to raise rates, it was reasonable to expect pay side pressure to increase.

We also noted last month that the DMO's strategy of satiating investor demand for NZGS (what we called "feeding the ducks while they're quacking" – which frankly, we'd do too if we were in charge) made swap spreads a directional.

Not surprisingly, things have changed since the Christchurch earthquake. Of course, the steeper curve and prospect of rate cuts means pay side

SWAP AND BASIS SWAP SPREAD UPDATE

interest virtually evaporated, reinforcing calls for more inverted swap spreads. Similarly, the potential for significantly larger NZGS issuance also argues for more inversion. But it is far too sweeping to leave it at that. For one, the market appears to be keen to continue acquiring NZGS, as demand in the Feb 24th tender (and for that matter, the March 3rd tender) attest to. With $2bn of pre-funding in the tin, so to speak, it is arguable that the market can easily absorb significant additional issuance over the next few years. That's not to say the marginal impact won't be for spreads to invert, but we just need to be careful not to blow it out of proportion.

One thing that will probably have to change is the way the DMO tenders the bonds – the so-called "feed the ducks" strategy. When demand is strong and you're pre-funded, you can do that. Not only can you give the market the volume it wants, you can give it the mix of maturities it wants too. But as the funding requirement grows, this luxury may not be available, and as we note in the next section, there is an imperative to term out new funding. At the margin, this does add to the pressure for swap spreads to invert.

But as noted, we need to be careful not to generalise. Indeed, we'd expect this pressure to be concentrated at the long end, and in fact, we would not be surprised to see short end swap spreads narrow (i.e. become less negative). This is because we do think the DMO will look to concentrate more on long end issuance, and because the long end is where most of the "flighty" positions are concentrated. Reserve managers are less likely to vacate the market following the quake. After all, for now, rating agencies seem relaxed, and outright yields continue to fall. Better still, with the curve steepening, roll and carry have picked up considerably, adding to the allure. But the most important differentiator is the potential impact of global reinsurance flows into NZD. Analysts expect the Christchurch quake to be the largest global insurance event in 3 years. Although it will take months (or even years) for reinsurance claims to be settled, prudence suggests they start to get hedged up fairly soon, which in practice means a substantial increase in asset allocation into NZD assets. This additional liquidity has to go somewhere, and we expect short-medium dated NZGS to be the prime candidates. In terms of the trade-off between yield/roll/carry and the desire to avoid substantial duration (given the need to payout within the next few years, not decades) the "sweet spot" is the NZGS 4/13s, which have the highest Roll per month, and attractive carry. As a result, we believe there is a strong case for the swap spread curve to invert, with long end spreads inverting, and short end spreads coming in.

BASIS SWAPS

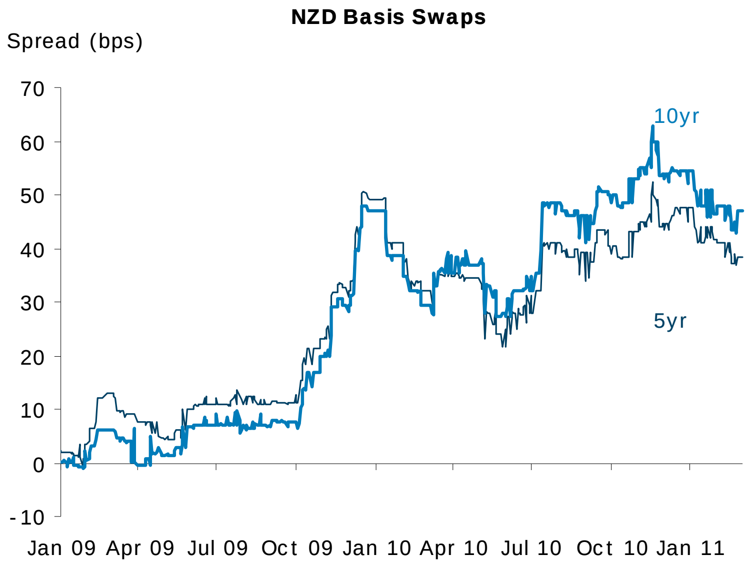
Basis swaps spreads continue to narrow, continuing the trend since late November. As we noted last month, this has been driven by a slowing up of offshore deals by local corporates, and the availability of relatively cheap short term offshore bank funding Recent developments are likely to exacerbate this, and we expect basis swap spreads to continue narrowing, with 5-10 year spreads likely to revert back towards 20-25bps. Indeed, not only has Westpac postponed plans to issue €1bn of covered bonds (under its new €5bn programme), but overall system credit growth is likely to be seriously dented by the Christchurch earthquake. Broadly speaking, this stems from two factors.

The first is the likelihood that the weaker economy leads to slower credit growth (both business and household). The government has made it clear

SWAP AND BASIS SWAP SPREAD UPDATE

that it will prioritise spending, and even before the quake there was talk of belt tightening, with savings the key theme of Budget 2011. But with wild media speculation that things like Working for Families and interest free student loans may be in line for the chop, this may lead to an acceleration of deleveraging. This is an example of the ripple effect, and of how what has happened in Christchurch will affect everyone in NZ. Businesses are certainly likely to pare back sales forecasts, and will be more cautious about taking on more debt.

The second factor affecting system credit growth is the involuntary deleveraging that will inevitably occur for property (be it residential or commercial) damaged by the quake. Indeed, we would expect the majority of households and businesses indemnified by insurance to repay any debt owing on their property, effectively leaving them cashed up. And to the extent that surplus funds end up in term deposits and the like, this in effect doubles the impact (i.e. the headline funding requirement falls by the amount repaid, plus the amount put on deposit). Furthermore, it could take some time before they decide to buy another property, if they do so at all. Householders may be inclined to rent, and some small businesses may simply call it quits. But the bottom line is, bank balance sheets are likely to remain static or even shrink in the near term, lessening the need to raise funds offshore.



Sources: ANZ, Bloomberg

GOVERNMENT BOND TENDER WATCH

SUMMARY

The DMO issued $1.1bn of bonds in February, taking total issuance for the fiscal year to date to $11.1bn, keeping issuance well ahead of schedule for this fiscal year. The fact that the Crown has pre-funded to this degree is good news given the Christchurch earthquake, with much larger borrowing programmes likely over the next few years. Although overall bid cover improved and tail width narrowed, the overall duration of risk sold was lower, and for the first time ever, a tranche of bonds attracted no bids.

As a general rule, the weekly bond tenders have continued to go reasonably well, with total issuance for the month (and a month with just 4 tenders at that) over $1bn for the 7th month in a row. As a result, issuance is $2.1bn ahead of schedule for the 8 months in the fiscal year to date (assuming a $13.5bn programme). As it stands, the DMO is scheduled to issue a further $13.5bn of bonds in 2011/12 as well. But that was before the Christchurch earthquake. And while it is too soon to say with any clarity what impact the quake will have on the Crown's finances, it's fair to assume that overall issuance over the next 5 years is set to be ramped up significantly, so it's a good thing that funding is running ahead of schedule.

Closer analysis of the weekly tenders does not suggest that buyers have been scared off by the quake – and reassurances by credit rating agencies have certainly helped. Indeed, on the basis of bid cover, the weakest tender was the 10th February tender, which attracted just $274m of bids for $200m of bonds, and ended up being re-allocated. In that regard we view the failure of the 2015 tranche in the 24th February quake as a freak occurrence, as opposed to signalling anything sinister.

Looking ahead, we expect three broad trends or themes to develop:

1. **Ongoing large-scale issuance**. As noted, it's too soon to assess the scale of the impact the quake will have on Crown finances. However, the Prime Minister has said that the government is committed to providing whatever resources are needed to rebuild Christchurch, and will thus shoulder a lot of the burden. For instance, if we assume that the current estimate of $15bn is somewhere in the ball park, and we further assume that a third of that is damage to infrastructure, which would be a Crown obligation (with the EQC, private insurance and reinsurance liable for damage to housing; and private insurance and reinsurance picking up the tab for damage to commercial buildings), then the direct impact on the Crown could be around $5bn. Add to this the immediate cost of relief and the emergency fiscal package (perhaps $200m) and the adverse impact of a slower growth (perhaps $1bn per annum for a couple of years assuming a 2% level hit to growth) and the all-up impact may be as much as $7-8bn. Of course, not all of this will arise immediately, and as noted, the DMO have pre-funded to the tune of $2bn, and there will be offsets as the Crown looks to re-prioritise spending. Bit the bottom line is, the market is going to have to get used to $1bn+ per month of issuance for a lot longer than currently projected (the HYEFU has issuance falling to $10bn by 2014/15).

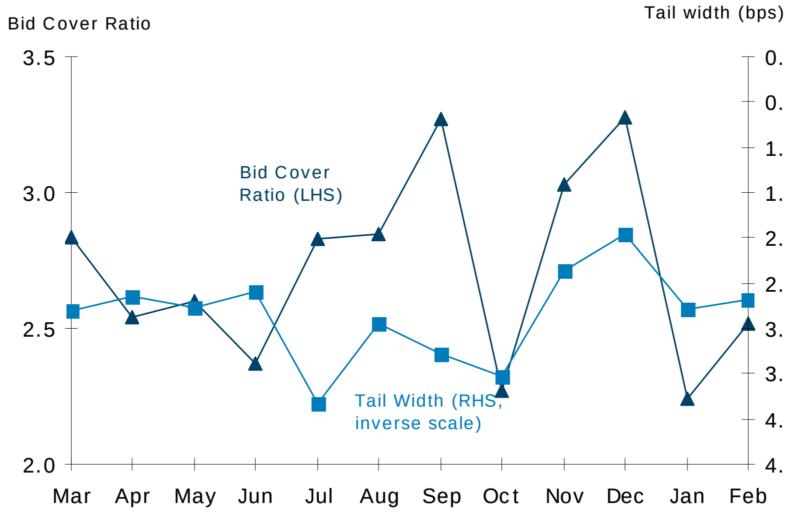
2. **A desire to term out the duration of funding**. Issuing more bonds is one thing, but care needs to be taken with regard to the maturity profile. The DMO has already increased the tranche sizes twice, and is now targeting $10bn per issue. With benchmark maturities every two years on average, this means the DMO need to issue $5bn per annum just to refinance maturities. If we add in the one-off impact of the quake to the issuance schedule, and the bonds issued as a result are

GOVERNMENT BOND TENDER WATCH

not of sufficiently long duration, the refinance risk will rise dramatically. As such, we expect to see more long bonds issued, and for at least one new benchmark long bond to be announced fairly soon. It's also worth adding that given that much of the additional funding requirement relates to infrastructure funding, it makes sense to raise longer duration funding. It makes even more sense given how low bond yields are at the moment.

3. **Innovation**. Expect the Crown to use innovative ways to raise funds. By definition, this could mean anything, and the market is already talking about things like disaster bonds and increased offshore funding. And of course there's always the old trick of selling the family silver (i.e. the SOE's). This would seem a prudent first step.

NZGS Tender Statistics - Last 12 months



Sources: ANZ, NZDMO

Summary of NZGS Issuance for the Previous Month						
Date	**Bonds Offered**	**Bid Cover**	**Tail ~**	**Tension ^**	**Bids Accepted**	**Comment**
3 Feb	\$50m 2015 \$200m 2019 \$150m 2021	1.5 2.5 2.8	4 4 3	+2.0 +0.5 -0.5	\$50m \$200m \$150m	Demand for long end bonds reasonable, 2013s not really in demand.
10 Feb	\$50m 2017 \$100m 2019 \$50m 2021	1.4 1.1 1.9	1 4 3	+2.5 +2.5 +1.0	\$35m \$100m \$65m	Not brilliant. Poor bid cover, with wide tails and poor price tension.
17 Feb	\$100m 2013 \$50m 2019 \$50m 2021	2.7 2.7 4.4	1 2 3	+0.0 -0.5 -1.5	\$100m \$50m \$50m	Reasonable tender. Long end demand clearly evident.
24 Feb	\$50m 2013 \$50m 2015 \$50m 2019 \$150m 2021	2.0 0.0 4.9 2.7	1 N/A 2 3	-1.0 +0.0 -1.0 +1.0	\$75m \$0m \$75m \$150m	Failure of 2015 tranche a fluke. Bid cover good, especially as it was just 2 days after the quake.
Total	**\$1,100m**	**2.52**	**2.69**	**+0.39**	**\$1,100m**	**Overall price tension has slipped relative to past 3 months**

Source: ANZ, Debt Management Office.

~ Tail refers to the total "width" of the successful range. For example, if the successful range is 5.70% to 5.73%, the tail is considered to be 4bp, spanning 5.70%, 5.71%, 5.72% and 5.73%

^ Tension refers to the "width" of the successful range using the market mid rate during bidding as the lower bound. This removes the distortion "below market" bid can have on tails. Using the same example as above, if the market mid rate was at 5.72% during bidding, the tension is considered to be 2bp, spanning 5.72% and 5.73%. That's a better representation of what happened, as although the tail was 4bp wide, it was because some bids were below market.

SPECIAL REPORT SUMMARY – CHRISTCHURCH EARTHQUAKE

SUMMARY

What follows is a summary of our recently published special report on the Christchurch Earthquake. The full report is available on request, or for Bloomberg subscribers, on our page ANZR2 <Go>.

- The government's early estimate of the direct cost of the earthquake in terms of destroyed infrastructure and buildings is $15 billion. This is in addition to the $5 billion bill from the September quake.
- The near-term impact on the economy will be significant. As a starting point, we are assuming a minimum 0.5 percent hit to Q1 GDP growth, but this is based on some fairly conservative assumptions. Numbers closer to 1 percent seem more intuitive. Adverse effects on confidence could exaggerate this further and impact on Q2 as well.
- The rebuild effort will be huge, but it will be significantly delayed, protracted (five years plus), and stymied by resource shortages. Not everything that was destroyed will be rebuilt.
- Our expectations of the economy being at a turning point in Q1 2011 have been pushed out by six months. We are back to square one in terms of the rebuild effort. There will again be significant unavoidable bureaucratic delays to getting work underway, although having experience and people on the ground from the September quake should help. Instigating a state of emergency signals a faster response time.
- The broader impacts on the economy (nationwide confidence, net migration, resource shortages, insurance industry responses, asset values, tourism) are much more difficult to estimate. But they will be negative, substantial, and long lasting.
- The financial burden of the earthquake will be massive. The Government will return to surplus much more slowly. A credit downgrade seems inevitable, though we are talking about margins of excellence in terms of AA versus AA+ (foreign currency rating).
- We are encouraged by the coordinated responses we are seeing. But this must be viewed in context of the need: this event is bigger than *Ben Hur*. Watch for business sector initiatives to support fiscal policy too.
- Fiscal policy and aid on the ground needs to do most of the work in regard to responding to Tuesday's events. We expect a sizeable package next week. Immediate attention needs to turn to microeconomic policies that could assist in helping the reconstruction effort. This includes greater incentives to get people into skilled trades.
- Monetary policy plays second fiddle to fiscal policy in events like this, but should still do its part. The RBNZ has every justification to cut the OCR. We believe they should cut rates by 50bps, with at least 25bps of this coming at the March *Monetary Policy Statement*. We see little prospect of policy restarting a process of normalisation until 2012.
- Financial markets have responded quickly and appropriately, with the exchange rate and interest rates down sharply. We expect to see the yield curve steepen further.

MONTH END CORPORATE BOND PRICING

Issuer	S&P Rating	Maturity	Coupon (%)	Mid yield (%)	Spread to swap	Spread to Govt
NZ Government	AAA	15-Nov-11	6.00%	2.75%	12	
NZ Government	AAA	15-Apr-13	6.50%	3.57%	-17	
NZ Government	AAA	15-Apr-15	6.00%	4.42%	-30	
NZ Government	AAA	15-Dec-17	6.00%	5.14%	-38	
NZ Government	AAA	15-Mar-19	5.00%	5.42%	-46	
NZ Government	AAA	15-May-21	6.00%	5.64%	-40	
ANZNB Callable sub	AA-	15-Sep-11	7.16%	5.41%	255	264
ANZNB Callable sub	AA-	2-Mar-12	7.60%	5.27%	240	235
ANZNB Callable sub	AA-	23-Jul-12	8.23%	5.40%	235	225
ANZNB Senior	AA	18-Sep-12	5.63%	4.13%	100	89
ANZNB Senior	AA	18-Jun-13	6.32%	4.61%	114	97
ANZNB Senior	AA	9-Jun-14	8.50%	5.14%	128	108
ANZNB Senior	AA	31-Mar-15	6.60%	5.58%	147	118
ANZNB Senior	AA	13-Jul-15	6.51%	5.74%	155	125
ANZNB Senior	AA	16-Feb-16	6.32%	5.97%	162	132
ANZNB Senior	AA	16-Feb-18	6.85%	6.58%	178	140
AfDB	AAA	28-Feb-13	7.75%	3.74%	40	24
AMP	A-	15-May-14	9.80%	6.72%	290	269
ASB Bank	AA	23-May-11	8.42%	3.43%	60	71
ASB Bank	AA	16-Jul-13	8.52%	4.68%	118	100
ASB Bank	AA	18-Nov-13	5.51%	4.89%	124	107
ASB Bank	AA	17-Sep-14	8.22%	5.27%	133	109
ASB Bank	AA	20-Oct-15	6.10%	5.83%	157	127
ASB Bank Callable sub	AA-	15-Jun-11	7.03%	5.19%	235	245
ASB Bank Callable sub	AA-	15-Nov-12	8.77%	5.40%	220	207
Asian Development Bank	AAA	29-Jan-14	5.38%	4.03%	30	12
Auckland Healthcare	AA	15-Sep-15	7.75%	5.31%	108	78
AIAL	A-	29-Jul-11	6.83%	3.85%	100	109
AIAL	A-	7-Nov-12	7.19%	4.54%	135	122
AIAL	A-	28-Feb-14	7.25%	5.32%	155	138
AIAL	A-	27-Nov-14	7.00%	5.56%	155	130
AIAL	A-	7-Nov-15	7.25%	5.82%	155	125
AIAL	A-	15-Nov-16	8.00%	6.10%	158	125
Auckland CC	AA	15-Nov-11	8.50%	3.44%	57	69
Auckland CC	AA	24-Mar-14	6.42%	4.89%	110	92
Auckland CC	AA	24-Mar-15	6.28%	5.26%	115	87
Bank of America Corp	A	8-Mar-12	7.53%	5.13%	225	220
Bank of New Zealand	AA	15-Sep-11	7.50%	3.50%	64	73
Bank of New Zealand Callable sub	AA-	15-Jun-12	8.42%	5.30%	230	221
Bank of New Zealand	AA	15-Sep-12	7.50%	4.12%	100	89
Bank of New Zealand	AA	27-May-13	8.56%	4.61%	116	99
Bank of New Zealand (GG)	AAA	20-Feb-14	4.78%	4.32%	56	39

MONTH END CORPORATE BOND PRICING

Issuer	S&P Rating	Maturity	Coupon (%)	Mid yield (%)	Spread to swap	Spread to Govt
Bank of New Zealand	AA	27-May-15	8.68%	5.70%	155	125
Bank of New Zealand (CB)	AAA	30-Jun-15	6.00%	5.22%	104	74
Bank of New Zealand	AA	13-Aug-15	6.17%	5.78%	157	127
Bank of New Zealand	AA	15-Sep-16	6.91%	6.16%	168	136
Bank of New Zealand (CB)	AAA	30-Jun-17	6.43%	5.91%	125	89
CHCH City Council	AA+	2-Nov-12	5.75%	3.96%	77	65
CHCH City Council	AA+	20-Apr-15	6.08%	5.38%	125	96
Citigroup Inc	A	18-May-12	7.83%	5.37%	240	233
Contact Energy	BBB	15-May-14	8.00%	5.82%	200	179
Contact Energy	BBB	13-Apr-17	7.86%	6.76%	215	180
Council of Europe	AAA	15-Nov-11	7.75%	3.12%	25	37
Council of Europe	AAA	12-Jun-14	5.50%	4.35%	49	29
Council of Europe	AAA	30-Apr-18	7.50%	5.59%	75	37
Dunedin City Tsy	AA	15-Apr-11	8.70%	3.20%	35	48
Dunedin City Tsy	AA	14-Jun-13	5.56%	4.32%	85	68
Dunedin City Tsy	AA	15-Nov-16	6.79%	5.72%	120	87
Dunedin City Tsy	AA	15-Oct-17	7.81%	5.98%	125	89
Dunedin City Tsy	AA	17-Dec-18	6.85%	6.27%	135	90
EIB	AAA	31-Jul-12	7.75%	3.34%	28	18
EIB	AAA	19-Feb-13	5.00%	3.68%	35	20
EIB	AAA	15-Dec-17	7.50%	5.53%	77	39
EDC	AAA	23-Jun-11	7.50%	3.09%	25	35
Eurofima	AAA	22-May-13	7.13%	3.95%	51	34
Fonterra Cooperative	A+	21-Apr-11	6.64%	3.34%	50	62
Fonterra Cooperative	A+	21-Apr-14	6.86%	5.06%	125	106
Fonterra Cooperative	A+	10-Mar-15	7.75%	5.42%	135	104
Fonterra Cooperative	A+	4-Mar-16	6.83%	5.74%	138	108
Genesis Energy	BBB+	15-Mar-14	7.25%	5.28%	150	132
Genesis Energy	BBB+	15-Mar-16	7.65%	6.02%	165	135
Genesis Energy	BBB+	15-Sep-16	7.19%	6.30%	182	150
IADB	AAA	15-Apr-15	7.50%	4.45%	33	3
IADB	AAA	15-Dec-17	6.25%	5.31%	55	17
IAG	A+	21-Nov-12	9.11%	6.91%	370	357
IBRD (World bank)	AAA	16-Jul-12	7.06%	3.20%	15	6
IBRD (World bank)	AAA	30-Jul-14	7.50%	4.20%	30	8
IBRD (World bank)	AAA	15-Dec-14	5.38%	4.33%	31	5
IFC	AAA	23-Aug-12	7.75%	3.27%	17	7
IFC	AAA	19-Mar-15	5.38%	4.46%	36	7
IFC	AAA	15-Dec-17	6.25%	5.30%	54	16
Kiwibank Ltd Callable sub	A+	20-Mar-12	7.72%	5.24%	235	229
Kiwibank Ltd Callable sub	A+	30-Sep-13	8.75%	5.89%	230	212
Kommunalbanken	AAA	3-Jul-14	5.75%	4.44%	56	35
Manukau CC	NR	15-Sep-15	6.90%	5.48%	125	95

MONTH END CORPORATE BOND PRICING

Issuer	S&P Rating	Maturity	Coupon (%)	Mid yield (%)	Spread to swap	Spread to Govt
Manukau CC	NR	29-Sep-17	6.52%	6.07%	135	99
Meridian Energy (MEL010)	BBB+	16-Mar-15	7.15%	5.65%	155	126
Meridian Energy (MEL020)	BBB+	16-Mar-17	7.55%	6.29%	170	135
Merrill Lynch (BofA)	A	4-Sep-13	7.16%	5.71%	215	197
Mighty River Power*	BBB+	15-May-13	8.36%	4.72%	130	112
Mighty River Power	BBB+	12-Oct-16	7.55%	6.25%	175	143
Morgan Stanley	A	6-Sep-12	6.86%	5.21%	210	199
Morgan Stanley	A	30-May-14	7.95%	6.32%	247	227
Municipality Finance	AAA	10-Jun-11	7.73%	3.14%	30	40
NIB	AAA	26-Feb-14	5.25%	4.11%	35	17
NIB	AAA	15-Apr-15	7.50%	4.61%	49	19
NZ Post	AA-	15-Nov-11	7.10%	3.47%	60	72
NZ Post Callable sub	A	15-Nov-14	7.50%	6.97%	297	273
Powerco Limited*	BBB	29-Mar-11	6.22%	4.38%	150	158
Powerco Limited*	BBB	28-Sep-12	6.59%	5.13%	200	188
Powerco Limited*	BBB	29-Mar-13	6.39%	5.36%	200	182
Powerco Limited*	BBB	29-Jun-15	6.53%	6.21%	205	173
Powerco Limited*	BBB	28-Sep-17	6.74%	6.79%	210	171
QTC	AA+	18-Sep-17	7.13%	5.51%	80	43
Rabobank NZ	AAA	15-Aug-11	7.65%	3.51%	65	74
Rabobank NZ	AAA	3-May-12	7.68%	3.67%	72	65
Rabobank NZ	AAA	19-Apr-13	5.47%	4.25%	85	68
Rabobank NZ	AAA	4-Sep-14	6.32%	4.93%	100	77
Rabobank NZ	AAA	4-Sep-14	6.32%	4.93%	100	77
Rentenbank	AAA	15-Nov-11	6.69%	3.13%	26	38
Rentenbank	AAA	15-Apr-13	7.75%	3.81%	41	24
Rentenbank	AAA	23-Sep-14	5.59%	4.49%	54	31
Rentenbank	AAA	15-Dec-17	7.49%	5.54%	78	40
Solid Energy	NR	7-Dec-16	8.00%	6.73%	220	187
Tauranga CC	A+	2-Dec-13	7.05%	4.71%	105	87
Tauranga CC	A+	15-Apr-16	6.25%	5.64%	125	95
Telecom (TCNZ Finance Ltd)	A	22-Mar-13	6.92%	5.27%	190	174
Telecom (TCNZ Finance Ltd)	A	15-Jun-13	8.50%	5.77%	230	213
Telecom (TCNZ Finance Ltd)	A	15-Jun-15	8.65%	6.17%	200	170
Telecom (TCNZ Finance Ltd)	A	22-Mar-16	7.04%	6.37%	200	170
Telstra Corp Ltd	A	24-Nov-11	6.99%	3.65%	78	89
Telstra Corp Ltd	A	24-Nov-14	7.15%	5.40%	140	115
Telstra Corp Ltd	A	11-Jul-17	7.52%	6.39%	172	137
Toyota Finance NZ	AA	5-Aug-11	7.34%	3.40%	55	64
Transpower Finance	AA	12-Nov-19	7.19%	6.20%	115	71
Transpower Finance	AA	10-Jun-20	6.95%	6.30%	117	75
Vector Ltd (VCT050)	BBB+	15-Oct-14	7.80%	5.82%	190	161
Waitakere CC	AA	30-Mar-12	5.50%	3.64%	75	67

MONTH END CORPORATE BOND PRICING

Issuer	S&P Rating	Maturity	Coupon (%)	Mid yield (%)	Spread to swap	Spread to Govt
Waitakere CC	AA	2-Oct-14	6.68%	5.11%	115	92
Warehouse (WHS010)	NR	15-Jun-15	7.37%	6.77%	260	230
Watercare Services	AA	19-Oct-11	6.86%	3.41%	55	65
Watercare Services	AA	15-May-14	6.79%	5.02%	118	99
Watercare Services	AA	16-Feb-15	5.74%	5.39%	131	104
Watercare Services	AA	18-May-16	7.14%	5.79%	138	108
Wellington International Airport	BBB+	15-Nov-13	7.50%	6.19%	255	237
Wellington Regional Council	AA	17-Feb-12	6.21%	3.44%	57	54
Wellington Regional Council	AA	16-Dec-13	5.60%	4.48%	80	62
Westpac NZ	AA	18-Apr-11	8.87%	3.47%	63	75
Westpac NZ	AA	19-Dec-11	7.24%	3.52%	65	72
Westpac NZ	AA	28-Nov-13	7.05%	4.81%	115	98
Westpac NZ (GG)	AAA	22-Jul-14	5.74%	4.44%	55	33

Note: (*) denotes quarterly coupons; (a) denotes price

MONTH END HYBRID BOND PRICING

Unrated and Hybrid Issues	S&P Rating	Maturity	Coupon (%)	Mid yield (%)	Spread to swap	Spread to Govt
ANBHA	A+	Perp		106.40		
APN Media (NZ) Ltd	NR	15-Mar-16	7.86%	8.07%	373	340
ASBPA	A-	Perp		72.00		
ASBPB	A-	Perp		71.50		
BISHA	A+	Perp		104.50		
BNZ Income Sec (II)	A+	Perp		106.50		
Prime Infrastructure (PIN020)	Ba3	30-Nov-12	9.00%	10.10%	688	675
CBA	A+	15-Apr-15	8.82%	92.50		
Fairfax	BBB	15-Jun-10	8.43%			
Fletcher Building (FBU190)	NR	15-Mar-11	7.55%	8.00%	505	509
Fletcher Building (FBU210)	NR	15-Mar-12	7.50%	6.85%	397	391
Fletcher Building (FBF050)	NR	15-May-14	9.00%	7.15%	331	312
Fletcher Building (FBF060)	NR	15-May-16	9.00%	7.30%	290	259
Fonterra Perpetual	A	Perp	8.52%	85.00		
Goodman Fielder NZ Ltd	NR	16-May-16	7.54%	7.03%	265	232
GPG* (GFN030)	NR	15-Nov-12	8.30%	8.60%	541	527
GPG* (GFN020)	NR	15-Dec-13	9.00%	8.70%	504	485
Greenstone Energy (GEF010)	NR	15-Oct-16	7.35%	7.32%	282	249
Infratil* (IFT140)	NR	15-May-11	8.25%	8.25%	543	553
Infratil* (IFT040)	NR	15-Nov-11	8.50%	8.40%	554	565
Infratil* (IFT060)	NR	15-Nov-12	7.75%	8.10%	491	477
Infratil* (IFT070)	NR	15-Sep-13	8.50%	8.30%	474	455
Infratil* (IFT013)	NR	15-Nov-15	8.50%	8.30%	404	372
Infratil* (IFT090)	NR	15-Feb-20	8.50%	9.20%	415	369
Infratil	NR	Perp	9.00%	61.00		
Kiwi Capital Securities	BBB	Perp		102.00		
Rabobank (RBOHA)	AA-	Perp		77.00		
Rabobank (RCSHA)	AA-	Perp		106.90		
Sky City* (SKC030)	NR	15-May-15	7.25%	7.50%	338	306
SKY TV (SKTFA)	NR	16-Oct-16	8.34%	90.00		
Trustpower* (TPW020)	NR	15-Sep-12	8.50%	6.95%	384	372
Trustpower* (TPW060)	NR	15-Mar-14	8.50%	6.95%	319	299
Trustpower*	NR	15-Dec-14	7.60%	6.47%	247	219
Trustpower*	NR	15-Dec-16	8.00%	6.99%	248	212
Trustpower* (TPW100)	NR	15-Dec-17	7.10%	7.15%	241	201
Vector Ltd (VCT040)	BBB-	15-Jun-12	8.00%	6.40%	340	331
Works Infrastructure* (WKS010)	NR	15-Jun-12	9.80%	19.50%	1651	1641
Works Finance (WKS020)	BBB-	15-Sep-12	9.65%	7.56%	445	433
PGG Wrightson* (PWF030)	NR	8-Oct-11	8.25%	6.70%	385	394

Note: (*) denotes quarterly coupons; (a) denotes price

IMPORTANT NOTICE

NEW ZEALAND DISCLOSURE INFORMATION

The Bank (in respect of itself and its principal officers) makes the following investment adviser disclosure to you pursuant to section 41A of the Securities Markets Act 1988.

The Bank (in respect of itself and its principal officers) makes the following investment broker disclosure to you pursuant to section 41G of the Securities Markets Act 1988.

Qualifications, experience and professional standing

Experience

The Bank is a registered bank and, through its staff, is experienced in providing investment advice about its own securities and, where applicable, the securities of other issuers. The Bank has been selling securities, and providing investment advice on those securities, to customers as a core part of its business for many years, drawing on the extensive research undertaken by the Bank and its related companies and the skills of specialised staff employed by the Bank. The Bank is represented on many bank, finance and investment related organisations and keeps abreast of relevant issues by running seminars and workshops for relevant staff and having its investment adviser staff attend external seminars where appropriate. The Bank subscribes to relevant industry publications and, where appropriate, its investment advisers will monitor the financial markets.

Relevant professional body

The Bank is a member of the following professional bodies relevant to the provision of investment advice:

- New Zealand Bankers Association;
- Associate Member of Investment Savings & Insurance Association of NZ;
- Financial Markets Operations Association; and
- Institute of Finance Professionals.

Professional indemnity insurance

The Bank (and its subsidiaries), through its ultimate parent company Australia and New Zealand Banking Group Limited, has professional indemnity insurance which covers its activities including those of investment advisers it employs.

This insurance covers issues (including ‘prior acts’) arising from staff fraud, electronic crime, documentary fraud and physical loss of property. The scope of the insurance also extends to third party civil claims, including those for negligence. The level of cover is of an amount commensurate with the size and scale of the Bank.

The insurer is ANZcover Insurance Pty Limited.

Dispute resolution facilities

The Bank has a process in place for resolving disputes. Should a problem arise, you can contact any branch of the Bank for more information on the Bank’s procedures or refer to any of the Bank’s websites.

Unresolved complaints may ultimately be referred to the Banking Ombudsman, whose contact address is PO Box 10-573, Wellington.

Criminal convictions

In the five years before the relevant investment advice is given none of the Bank (in its capacity as an investment adviser and where applicable an investment broker) or any principal officer of the Bank has been:

- Convicted of an offence under the Securities Markets Act 1988, or the Securities Act 1978 or of a crime involving dishonesty (as defined in section 2(1) of the Crimes Act 1961);
- A principal officer of a body corporate when that body corporate committed any of the offences or crimes involving dishonesty as described above;
- Adjudicated bankrupt;
- Prohibited by an Act or by a court from taking part in the management of a company or a business;
- Subject of an adverse finding by a court in any proceeding that has been taken against them in their professional capacity;
- Expelled from or has been prohibited from being a member of a professional body; or
- Placed in statutory management or receivership.

Fees

At the time of providing this disclosure statement it is not practicable to provide accurate disclosure of the fees payable for all securities that may be advised on. However, this information will be disclosed to you should you seek advice from one of the Bank’s investment advisers on a specific investment.

Other interests and relationships

When a security is sold by the Bank, the Bank may receive a commission, either from the issuer of a security or from an associated person of the Bank. Whether that commission is received and, if received, its value depends on the security sold. At the time of providing this disclosure statement it is not practicable to provide a detailed list of each security that may be advised on, the name of the issuer of that security and the rate of the commission received by the Bank. However, this information will be disclosed to you should you seek advice from one of the Bank’s investment advisers on a specific investment.

In addition to the interest that the Bank has in products of which it is the issuer, the Bank, or an associated person of the Bank, has the following interests or relationships that a reasonable person would find reasonably likely to influence the Bank in providing the investment advice on the securities listed below:

- ANZ Investment Services (New Zealand) Limited (ANZIS), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. ANZIS may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- UDC Finance Limited (UDC), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. UDC may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- OnePath (NZ) Limited, as a wholly owned subsidiary of the Bank, is an associated person of the Bank. OnePath and its related companies may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- Direct Broking Limited (DBL), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. DBL may receive remuneration from a third party relating to a security sold by the Investment Adviser.

Securities about which investment advice is given

The Bank provides investment advice on the following types of securities:

- Debt securities including term and call deposits, government stock, local authority stock, State-Owned Enterprise bonds, Kiwi bonds and corporate bonds and notes;
- Equity securities such as listed and unlisted shares;
- New Zealand and overseas unit trusts;
- Share in a limited partnership;
- Superannuation schemes and bonds;
- Group investment funds;
- Life insurance products;
- Derivative products including interest rate and currency forward rate contracts and options; and
- Other forms of security, such as participatory securities.

Procedures for dealing with investment money or investment property

If you wish to pay investment money to the Bank you can do this in several ways such as by:

- Providing cash;
- Providing a cheque payable to the relevant product or service provider and crossed ‘not transferable’; or
- Making an automatic payment or payment through another electronic delivery mechanism operated by the Bank.

Investment property (other than money) may be delivered to the Bank by lodging the relevant property (for example, share certificates) with any branch of the Bank offering a safe custody service, or by posting (using registered post) the documents or other property to a branch of the Bank, identifying your name, account number and investment purpose.

Any investment money lodged with the Bank for the purchase of securities offered by the Bank, its subsidiaries or any third parties will be deposited in accordance with your instructions, to your nominated account or investment. Such money will be held by the Bank according to usual banking terms and conditions applying to that account or the particular terms and conditions relating to the investment and will not be held by the Bank on trust unless explicitly accepted by the Bank on those terms. Any investment

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money or property accepted by the Bank on trust will be so held until disbursed in accordance with your instructions. Any investment property lodged with the Bank will be held by the Bank as bailee according to the Bank's standard terms and conditions for holding your property.

Record Keeping

The Bank will keep adequate records of the deposit of investment moneys or property and all withdrawals and dealings with such money or property, using the account/investment number allocated to your investment. You may have access to those records upon request.

Auditing

The Bank's systems and operations are internally audited on a regular basis. The financial statements of the Bank and its subsidiaries are audited annually by KPMG. However, this does not involve an external audit of the receipt, holding and disbursement of the money and other property.

Use of Money and Property

Money or property held by the Bank for a specific purpose communicated to the Bank (e.g. the purchase of an interest in a security) may not be used by the Bank for its own purposes and will be applied for your stated purpose. No member of the Bank's staff may use any money or property deposited with the Bank, for their own purposes or for the benefit of any other person. In the absence of such instructions, money deposited with the Bank may be used by the Bank for its own purposes, provided it repays the money to you upon demand (or where applicable, on maturity), together with interest, where payable.

NEW ZEALAND DISCLAIMER

The Bank does not provide investment advice tailored to an investor's personal circumstances. It is the investor's responsibility to understand the nature of the security subscribed for, and the risks associated with that security. To the maximum extent permitted by law, the Bank excludes liability for, and shall not be responsible for, any loss suffered by the investor resulting from the Bank's investment advice.

Each security (including the principal, interest or other returns of any security) the subject of investment advice given to the investor by the Bank or otherwise, is not guaranteed, secured or underwritten in any way by the Bank or any associated or related party except to the extent expressly agreed in the terms of the relevant security.

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