

Consumer confidence falls

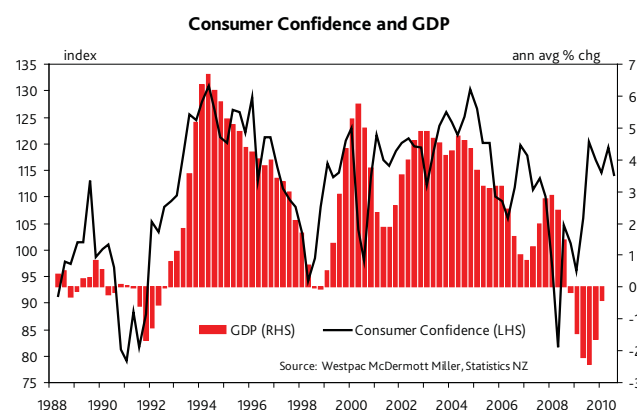
Q3 Westpac McDermott Miller Consumer Confidence Index: 114.1

- **Consumer confidence fell 5.2 points in the September 2010 quarter, to 114.1.**
- **Perceptions of both current and future conditions declined, but the key influence was a sharp drop in the short term economic outlook.**
- **The fall in confidence implies that growth in consumer spending will remain modest in the near term.**

The Westpac McDermott Miller Consumer Confidence Index declined in the September 2010 quarter, falling from 119.3 to 114.1. Confidence is now back at a similar level to that reported at the beginning of the year. An index number over 100 indicates there are more optimists than pessimists, while a number under 100 indicates that pessimists outnumber optimists. The margin of error in the survey is 2.5% at a 95% confidence interval. The survey was conducted between 1-12 September.

The decline in confidence this quarter is not surprising. Since June, the economic news has taken on a more negative tone, particularly in the global arena where a marked mid-cycle slowdown has occurred in the US, Japan and China. But more importantly, two key domestic events had the potential to weigh heavily on confidence in the quarter: the collapse of South Canterbury Finance, NZ's largest non-bank owned finance company; and, the 7.1 magnitude earthquake in the Canterbury region on 4 September. In that respect, it is surprising that confidence hasn't fallen by more. Certainly, the message seems to be one where consumers are weathering the recent spate of soft economic news (including a declining housing market and worse-than-expected unemployment) reasonably well.

The immediacy and unknown quantum of the earthquake meant that there was a lot for respondents to assimilate. It also raises the prospect of a bias amongst Cantabrian respondents. Only those in the Canterbury region who were physically able (i.e., they could get into their home to answer the phone) or willing (i.e., those less affected or traumatised) to respond did. Indeed, confidence in the Canterbury region lifted by almost 6 points this quarter, making Canterbury consumers the most confident in the country. That seems counterintuitive given the magnitude of the shock just experienced in the region. Still,



Consumer Confidence Indices

| | Sep-10 | Jun-10 | change |
|---------------------------|--------|--------|--------|
| Consumer Confidence Index | 114.1 | 119.3 | -5.2 |
| Present Conditions Index | 103.3 | 108.5 | -5.2 |
| Future Conditions Index | 121.3 | 126.5 | -5.2 |

removing Canterbury from the survey results reveals that even in its absence, confidence remained reasonably resilient, falling 6 points in the quarter to 113.1.

Survey details

Four of the five component questions declined this quarter. The most influential factor was a sharp fall in consumers' perceptions of the short term economic outlook. A net 3% of respondents now expect bad economic times over the next 12 months, a swift turnaround from the net 16% expecting good economic times last quarter. This is the first time since June last year that the pessimists have outweighed the optimists in response to this question.

Consumers also became a little more despondent about their own personal financial situation this quarter. A net 17% of respondents said they were worse off financially than a year ago, up from a net 14% last quarter. Again we need to put this result into perspective – at current levels, that is the second least pessimistic result since December 2007. In terms of the coming year, consumers remain optimistic, but less so than last

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quarter, with a net 13% expecting their own financial situation to improve over the next 12 months – down from 16% in the June quarter and the lowest since June 2009.

Consumer perceptions of their purchasing power became a little more subdued, with a net 24% saying now is a good time to buy a major household item, compared to a net 31% in the June quarter. Still, we need to put this result in perspective. At current levels, the reading is the second highest since June 2007. Thus, while not as positive as in June, it still suggests a strong willingness to spend.

The only question to record an improvement through the quarter was that relating to the five-year economic outlook. A net 54.5% expect good economic times over the next five years, up from a net 48% in June. At these levels, confidence in the medium term outlook is close to the record high of a net 63% reached in September last year, and well above the survey average of a net 31%.

Regional and demographic trends

By region, the drop in confidence was almost across the board, with particularly sharp declines recorded in the Bay of Plenty and Auckland. We note though, that at current levels Auckland remains the second most confident region in the country. In fact, by rural/urban grouping confidence remains the strongest in the cities, although the gap between rural and urban confidence is narrowing.

The exceptions to the drop in confidence this quarter were the Gisborne/Hawke's Bay and Canterbury regions, where confidence increased. In terms of the former, the rise in confidence almost fully reverses an out-of-sync decline last quarter. Meanwhile, as discussed above, we suspect the lift in confidence in Canterbury can in part be explained by a response bias.

By age, the fall in confidence was more pronounced among those aged 30 or over, and for those in the upper socio-economic group. By gender, the decline in confidence was greater amongst males. But, overall, males (114.3) remain more optimistic than females (110.8).

Consumer Confidence Data

| Region | Sep-09 | Jun-10 | Sep-10 |
|-------------------------------|--------|--------|--------|
| Northland | 109.2 | 111.4 | 109.3 |
| Auckland | 122.7 | 126.8 | 117.3 |
| Waikato | 119.8 | 116.0 | 111.8 |
| Bay of Plenty | 116.2 | 119.0 | 106.8 |
| Gisborne/Hawke's Bay | 115.3 | 104.8 | 107.8 |
| Taranaki/Manawatu-Wanganui | 119.4 | 119.0 | 110.9 |
| Wellington | 121.4 | 122.6 | 115.4 |
| Nelson-Marlborough/West Coast | 117.9 | 111.2 | 104.3 |
| Canterbury | 122.7 | 114.7 | 120.6 |
| Otago | 117.4 | 114.3 | 110.7 |
| Southland | 122.8 | 114.6 | 112.4 |

Implications

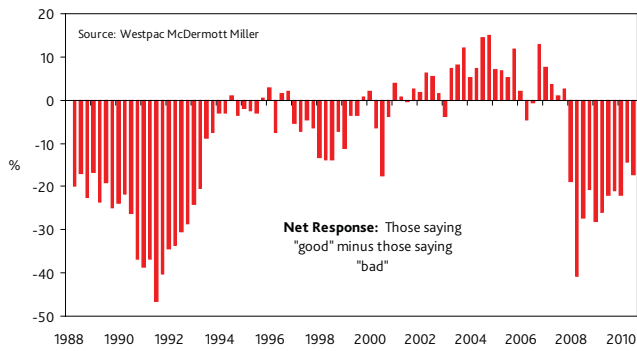
The September *Monetary Policy Statement* revealed a dramatic change in the RBNZ's assumptions of household behaviour. It has concluded that households are saving and paying down debt at a faster pace than thought three months ago. But more importantly, the shift is expected to be long lasting and in an environment where employment and income growth are gaining momentum. As such, the RBNZ has revised down its forecasts for real consumer spending, with growth expected to slow from 2.3% in the year to March 2011, to just 0.5% in March 2012.

In that respect, today's survey results challenge the RBNZ's view. Yes, confidence has fallen, but at current levels the Index remains above the long run average of 111.6 and is broadly consistent with annual average growth in real consumer spending of around 3%. Moreover, the level of the Index suggests that consumers still have a willingness to spend. At present, the ability to spend is being hampered by weak income growth. However, once that situation improves, as we and the RBNZ expect it will, it is hard to believe that consumers will not act. We continue to expect the pace of consumer spending growth to match that of income growth over the next couple of years.

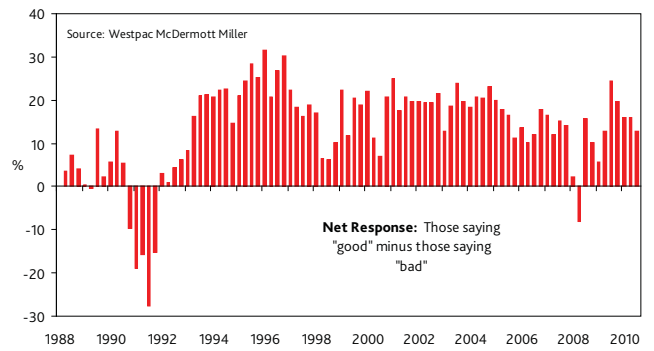
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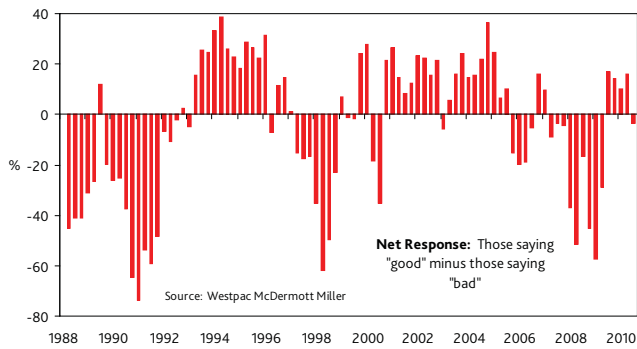
Are you better or worse off financially now than a year ago?



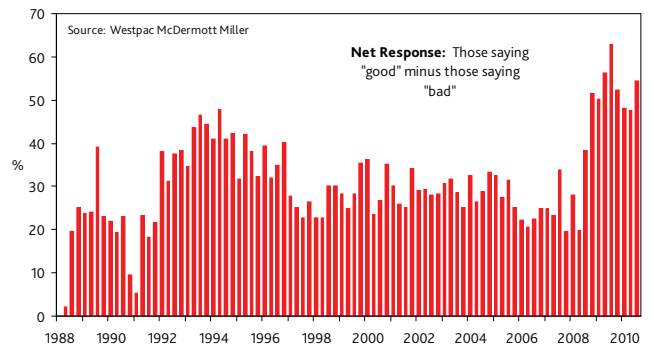
Do you expect to be better or worse off financially this time next year?



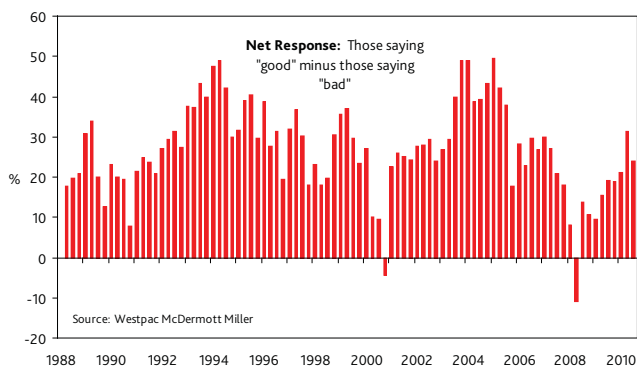
Do you expect good or bad economic times over the next 12 months in NZ?



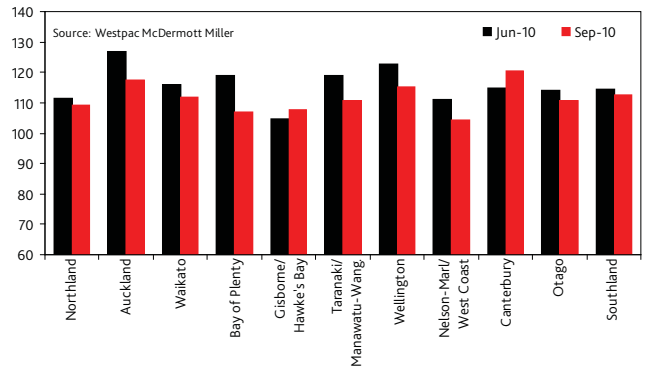
Do you expect good or bad economic times over the next 5 years in NZ?



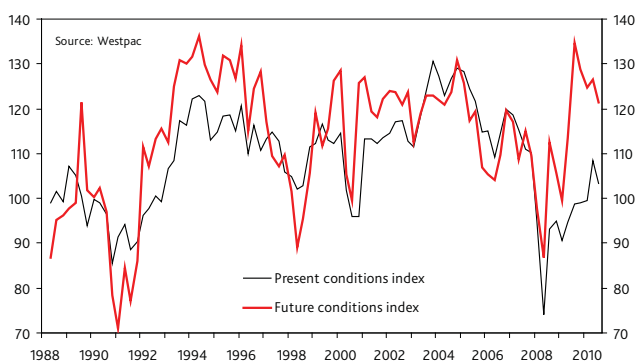
Is this a good or bad time to buy a major household item?



Regional Confidence



Present and Future Conditions Index



Consumer Confidence Data

| Quarter | Index |
|---------|-------|
| Jun-08 | 81.7 |
| Sep-08 | 104.8 |
| Dec-08 | 101.3 |
| Mar-09 | 96.0 |
| Jun-09 | 106.0 |
| Sep-09 | 120.3 |
| Dec-09 | 116.9 |
| Mar-10 | 114.7 |
| Jun-10 | 119.3 |
| Sep-10 | 114.1 |