

# BNZ Weekly Overview

## Mission Statement

To help Kiwi businesspeople and householders make informed financial decisions by discussing the economy and its implications in a language they can understand.

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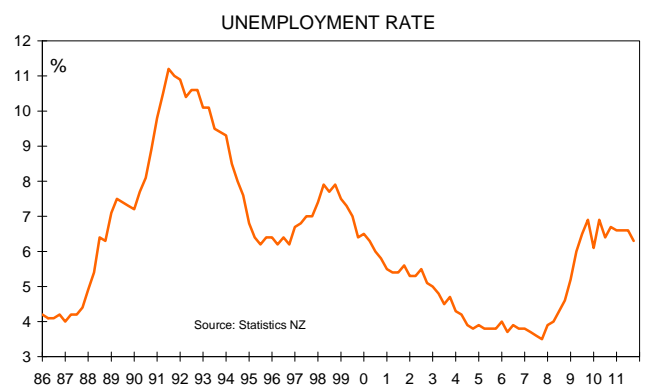
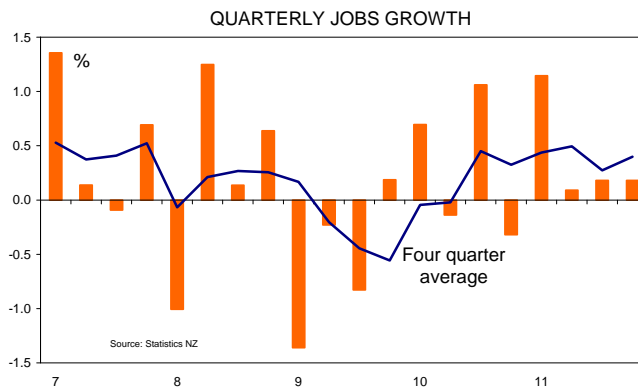
The Weekly Overview is written by Tony Alexander. The views expressed are my own and do not purport to represent the views of the BNZ. To receive the Weekly Overview each Thursday night please click here.

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## Labour Market Weak

My view is that the economy is struggling to grow anywhere near trend and that view received support this morning in the form of the quarterly Household Labour Force Survey. Rather than rising 0.4% during the December quarter as the markets had been expecting job numbers only rose by 4,000 or 0.2% to be 1.6% up from a year earlier. This poor 0.2% performance followed the 0.2% September quarter rise and 0.1% June quarter rise. Jobs growth in New Zealand has almost ceased. Imagine the results had there been no growth boosting mana lifting Rugby World Cup!



Yet the unemployment rate fell in the quarter to 6.3% from 6.6% in the September quarter. Why? Because the participation rate (the proportion of the working age population in work or actively looking for it) fell to 68.2% from 68.4%. This is still a high rate by world standards but does suggest some discouraged people left the labour force late last year.

Worse than the tiny 0.2% quarterly growth in job numbers was a large 1.4% fall in hours worked. Hours worked were ahead 0.5% from a year earlier and this measure can be very volatile on a quarterly basis.

The results are fairly weak but we have to be careful about reading too much of negative import into them. The HLFS has become a rather volatile survey on a quarter to quarter basis over the past few years and the December quarter result probably contains some effect from the Rugby World Cup. So concluding that growth has stopped completely in the economy would not be valid. But the negative results outside of exporting and tractor registrations do seem to be adding up somewhat so one must be a tad cautious. To whit...

- 0% growth in core spending using debit and credit cards over the December quarter.
- 1% fall in dwelling consents issued during the December quarter.
- 5% fall from a year ago in the value of non-residential building consents issued during the December quarter.
- Near 10% seasonally adjusted fall in commercial vehicle registrations during the three months to January.
- 1% s.a. fall in the value of imports of capital goods during the December quarter.
- Net migration outflows are getting more negative.

But

- Car registrations have risen near 10% s.a. over the past three months.
- Tractor registrations have risen also near 10% s.a.
- Exports s.a. were up 4.5% s.a. in the December quarter.
- Farm sales in the December quarter were 66% ahead of a year ago.
- Dwelling sales were ahead 5% s.a. during the December quarter.

And looking ahead, both our monthly business Confidence Survey and the ANZ Roy Morgan Consumer sentiment survey have improved in the past month, US data have looked good, Australia looks so good the RBA have stopped cutting interest rates for now, China and Asia more broadly appear to be having a soft-landing, though Europe remains a line call on a daily basis.

Factoring in the clear strength in our BNZ-REINZ Residential Market Survey released earlier today, but the obvious restraint from the high NZ dollar, then scratching heads over when farmers spend more generally on retail goods, when the Christchurch rebuild kicks into gear, and when we all sit back and feel comfortable with our debt levels and one struggles to find justification for either the recession scenario this year or an above trend growth outcome.

Mediocrity frankly looks like ruling for another year and that suggests little need for great concern about interest rates jumping up much this year though some increases are likely. It might appear to suggest that employers can relax about finding staff. But with worsening net migration outflows – especially to Australia – and naturally slowing labour force growth in New Zealand as population aging gathers pace, employers are going to struggle. They had best think about what their offshore recruitment strategy is.

Mediocrity might also suggest housing market weakness. But with construction near a four decade low the existing shortage is worsening so prices and rents are going to rise, accommodation shortages and related social problems will worsen, and eventually the get rich quick schemes based around property development will return.

But why worry? The government have sunk their political capital gained at last year's general election into building an economic growth and development strategy centred around state asset sales which will drive innovation, productivity growth, higher wages, a shift in resources into value-added exporting, higher research and development, entrepreneurship, openness to foreign capital, and good times for all. Or am I missing something here?

## Is Our Economy Getting Better or Worse?

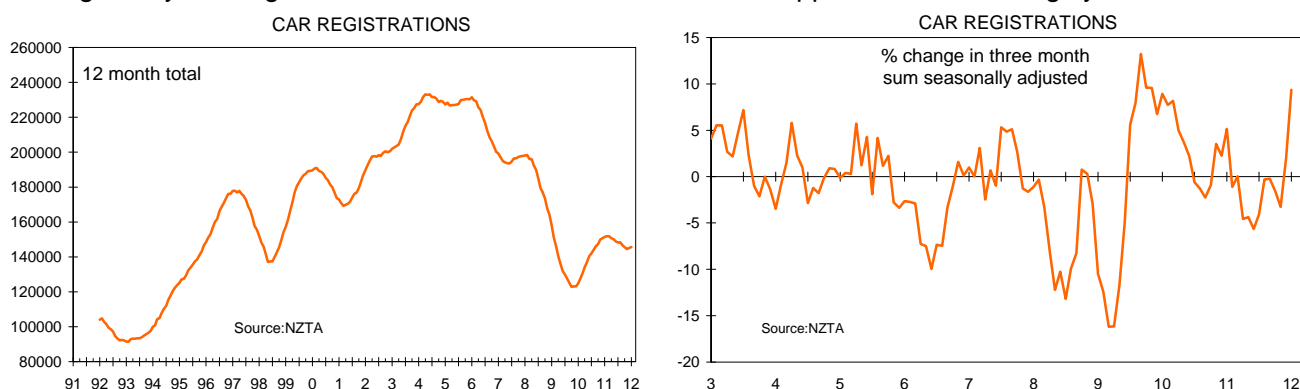
In this section we look only at what the data are actually telling us and pay no attention to forecasts or intentions measures.

Better but at a very slow pace. That means we are losing ground relative to all but the countries mired in government debt holes.

### Are householders opening their wallets more?

#### **A tad**

In January there were 13,874 cars registered around the country which was a small 4% rise from a year earlier. Some strength has returned to this measure with a rough seasonally adjusted rise in registrations of almost 10% over the past three months following a 2% fall in the previous quarter and 4% fall before that. This sounds good, but the sharp turnaround is not consistent with other indicators of consumer spending therefore while we slot this measure on the positive side of our consumption T account, it remains outweighed by the negative side for now. The household focus appears to remain largely on debt reduction.



### Is business output rising?

If we are talking about inward tourism then the answer is no because in the December quarter visitor numbers fell 3.5% seasonally adjusted. But this followed a 17.7% rise during the September quarter with both periods moved about by the Rugby World Cup. In the year of 2011 all up visitor numbers grew by 2.9% so we can say that the underlying trend is upward. But we will need to wait a tad longer to be clear of the RWC effects and then we will get a clearer picture. The risk clearly is that with the NZD at high levels, woe in Europe and the UK, and Aussies finding their currency going a long way elsewhere in the world, that the tourism sector will experience tough though not necessarily onerous conditions this year.

### Are businesses hiring more people?

#### **Not really.**

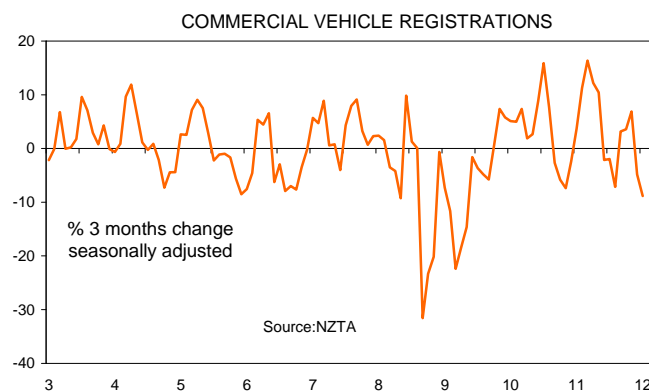
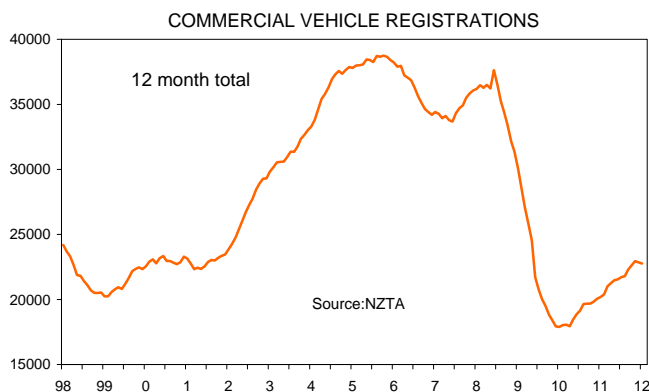
This morning the quarterly Household Labour Force Survey was released and it showed only 4,000 more people in work in the December quarter than the September quarter seasonally adjusted, and only 10,000 more than in the March quarter. That is an extremely mediocre performance which should leave retailers concerned about sales growth prospects in the first half of this year while capping some of the enthusiasm in the housing market.

### Are businesses boosting their capital spending?

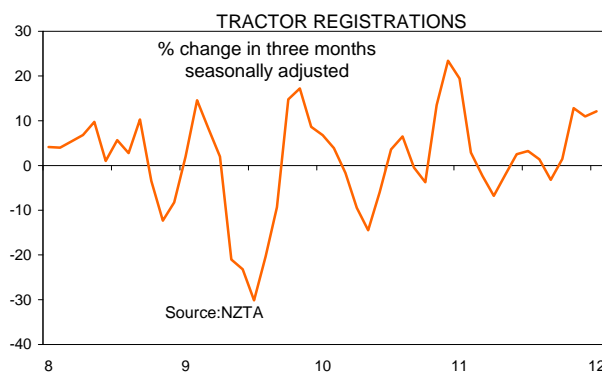
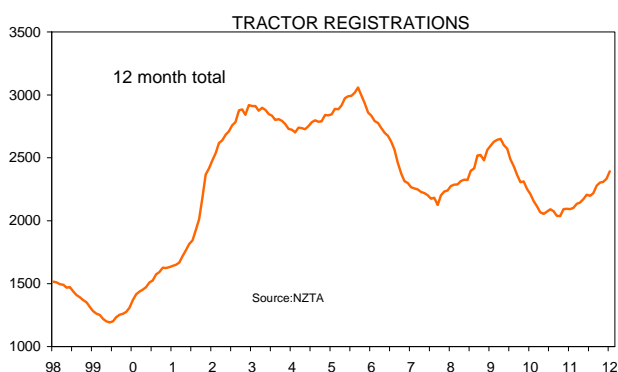
#### **For equipment yes. Buildings = mixed.**

To see how businesses are feeling right now one can read our monthly BNZ Confidence Survey here. <http://tonyalexander.co.nz/bnz-confidence-survey/>

There were 1,379 commercial vehicles registered in January which makes for a 6% fall from a year earlier and near 10% fall in seasonally adjusted terms in the three month period. As with the decrease in the value of imported machinery this measure is suggesting that a surge in business investment over much of 2011 could be flattening out. But gauging what is happening with business capital spending is very difficult so we think one cannot justifiably claim as yet that a recovery in capex has stalled. We await additional data.



With regard to that most up to date measure of what farmers are doing with their money, tractor registrations, there was a 39% rise between January 2011 and January this year. In the year to January regos were up by 14% and in rough seasonally adjusted terms regos have risen near 10% in the past three months.



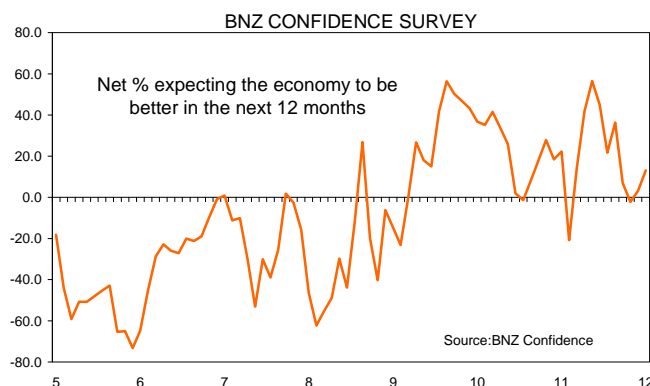
So, in contrast to the declining commercial vehicle registrations measure this indicator is strengthening and that is an important thing. The most basic economic cycle in New Zealand comes from the rural sector in the form of rising receipts for farmers eventually leading to increased debt repayment, then maintenance spending, then capital spending at perhaps the same time as land buying, then generalised buying of consumer goods as kitchens etc. get upgraded. The upswing in tractor registrations and the feedback received in our monthly Confidence Survey leaves us hopeful that the overall NZ economy this year will receive a boost from higher farmer spending.

Then again, wouldn't it be good if farmers took their extra income and invested it in turning themselves into high value product manufacturers rather than commodity gatherers and producers of blended inputs which foreign companies slap their labels on and sell for high prices offshore. To move up the value curve requires capital. That requires either investment from outsiders, sacrificing consumption for long term wealth gain (farmers well know how to do that), or handing the basic product to others more focussed on foreign markets and willing to turn it into high profit products if Kiwi farmers refuse to. Meaning... if neither of the first two happen the chances are that in not many years time we could see a further substantial lift above 770 million litres per annum in the quantity of milk Fonterra must make available to other companies to have a go with. Anyone up for an infant formula plant? The 770 hasn't all been allocated yet as far as I know.

## What Do The Leading Indicators Say?

In this section we look only at the factors which can at times give insight into where the economy is headed. Generally we will only cover newly released information.

Our monthly BNZ Confidence Survey found a small rise in sentiment to a net 13% positive about the economy over the coming year from 3% in the previous survey taken in the first week of December. The result is positive in that it represents the second increase in a row and is above the 0% level. But it is hardly stellar by the standards of the past few years and means we see little reason at this stage for believing that the NZ economy is going to power ahead at a faster than average pace this year. In fact there is little on the horizon which one would suggest could act as a circuit breaker for householders who still appear determined to get their debt levels down.



The most recent credit growth data show that in the business, farming, and household sectors attention remains on containing debt growth. Our survey also reveals that although there are some signs of rising farmer spending (clear in rising tractor registrations noted above) the bulk of farmers still appear strongly determined to get their debt levels down – and who can blame them? The history of the past few years shows that shocks come along with rather high frequency and even during times when commodity prices are high there is the ever present risk of poor weather conditions as many down south have experienced this year, or disease as being experienced by the Kiwifruit sector currently.

The world has changed and credit availability is (one hopes) never going back to where it was ahead of the 2008 crisis and wise businesses are adjusting to that change in the ability and willingness of financiers to lend by easing down their debt levels. That means that increasingly reliance will need to be placed upon capital and thankfully just at a time when we are going to be needing more of it more is being made available from China. The trick of course as anyone in the merchant banking area knows is matching up the two sides of the transaction with regards to terms, amount, expectations etc.

In the case of China it is often the case that the amount which investors wish to place is far greater than the amount Kiwi firms want or can usefully use. Or it is the traditional case that Kiwi entrepreneurs will accept slower growth rather than giving away both part control of the company and sacrificing profit if there plan is to sell the business after a few years (as in the book I have just finished reading “Chicken Lips, Wheeler Dealer and the Beady Eyed MBA” by Frank Farwell.

## INTEREST RATES

Unless Europe falls over we have probably seen the lows in wholesale fixed borrowing costs for this cycle – not that there is a cycle as such. It is more a lengthened period of time in which we wait for the mediocrity and downward risks of the post-2009 recession period to end. The data coming out of the United States are looking generally acceptable – hence improving share prices, Asia appears to be having a soft landing, Australia looks good in aggregate though some sectors are struggling badly, and although here in NZ we are not thriving there are some positive trends underway.

There is no way of telling at what pace long term borrowing costs will rise so all we are really saying is that the risk reward trade-off for business borrowers holding off longer before fixing has shifted more in favour of biting the fixing bullet now. We say this even though there is little chance of floating rate borrowing costs rising all that much this year. But there is a chance that the RBNZ raises the official cash rate before the end of the year and there is a chance that rising borrowing costs offshore will force banks to raise rates without a monetary policy change.

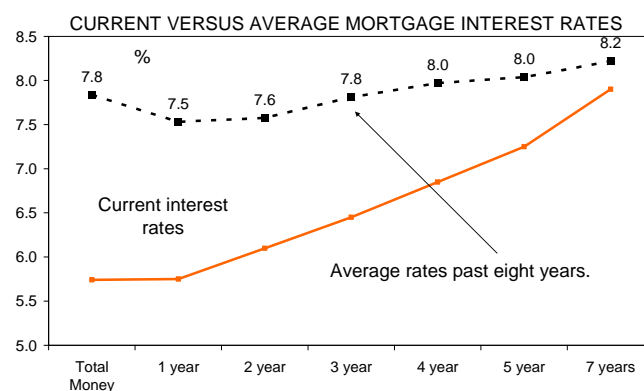
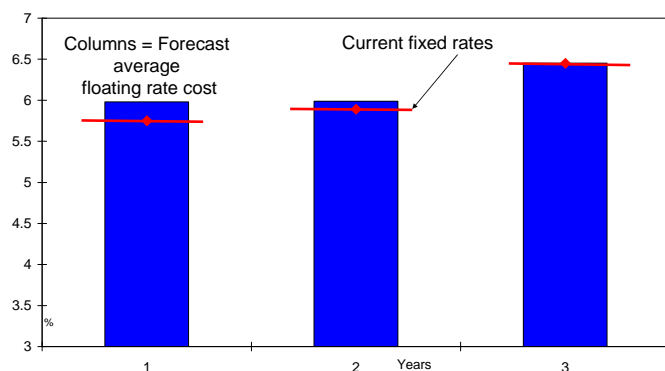
This week swap rates have crept higher due largely to the Reserve Bank of Australia leaving its cash rate at 4.25% on Tuesday rather than cutting it as the markets had largely expected.

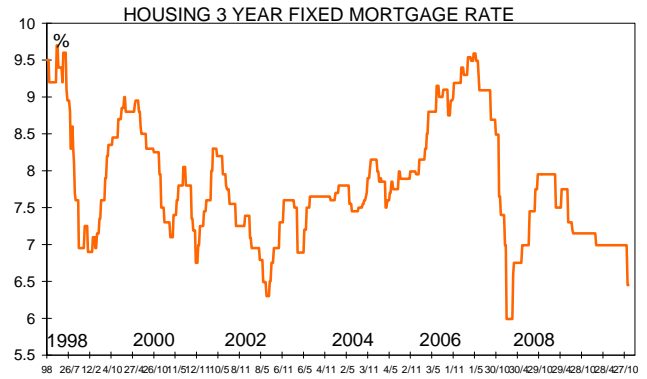
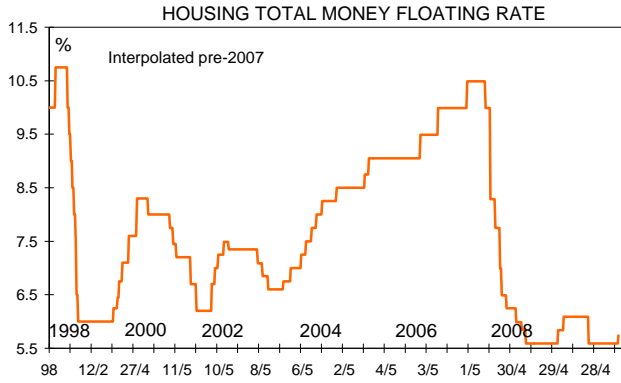
FINANCIAL MARKETS DATA						
	This week	Week ago	4 wks ago	3 months ago	Yr ago	10 yr average
Official Cash Rate	2.50%	2.50	2.50	2.50	3.00	5.4
90-day bank bill	2.77%	2.75	2.76	2.74	3.22	5.7
1 year swap	2.82%	2.72	2.80	2.92	3.43	5.8
3 year swap	3.10%	2.92	3.07	3.36	4.25	6.1
5 year swap	3.53%	3.34	3.52	3.87	4.76	6.3
180-day term depo	4.00%	4.00	4.50	3.60	4.90	5.7
Five year term depo	5.85%	5.85	6.00	6.00	6.75	6.4

### If I Were a Borrower What Would I Do?

I remain happy floating but would be keeping an eye out for discounted fixed rates. Banks are finding credit demand to be far weaker than anticipated and there is always the risk that some will decide meeting old lending growth targets remains optimal and they will adjust interest rates to try and achieve them – like retailers discounting stock. So I could easily be enticed away from floating. The rule I ran with last year was that I would fix two years if given a rate of 6%, or fix three years if given 6.25%. Both rates are available in the marketplace now (and so a big raspberry to those who last year said it was silly putting in such a statement as there was no chance of seeing such rates again).

But would I take one of these rates? Not necessarily because I think I can do better and would look to snap up a bargain out to four or five years taking the view that the world will not implode. So I shall sit floating waiting for a bit more of a rate discounting war while keeping a very close eye on news from offshore just in case the planets line up for the better all of a sudden.





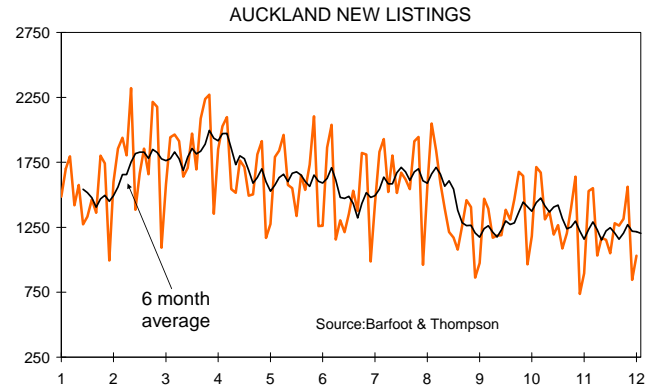
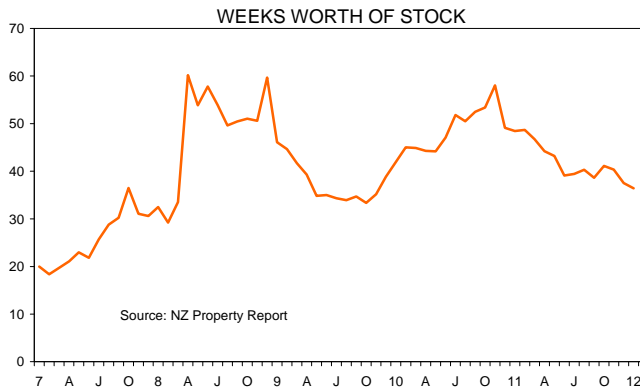
## HOUSING MARKET UPDATE

To view the most recent results of our monthly BNZ-REINZ Residential Market Survey [click here.](http://tonyalexander.co.nz/bnz-reinz-survey/)

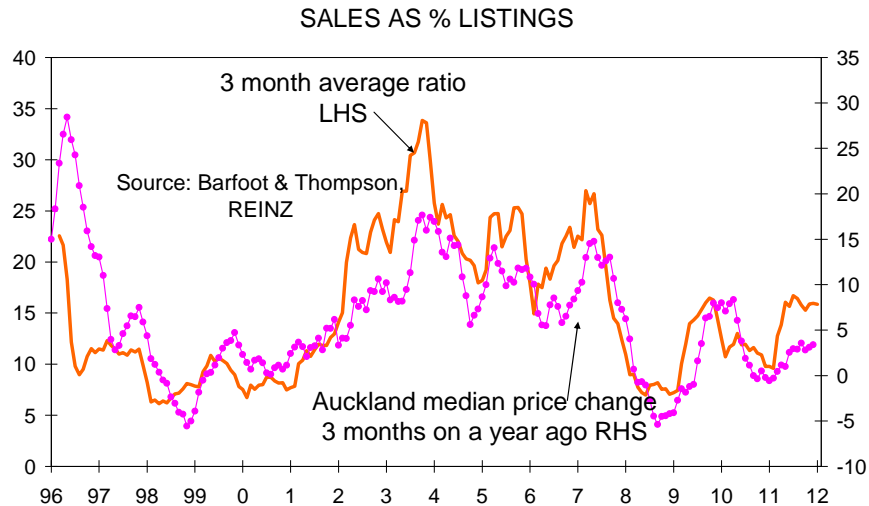
### Monthly Barfoot & Thompson Numbers

Normally in January sales are higher than in December. But this year they fell to 683 for B&T in Auckland from 714 – a decline in rough seasonally adjusted terms of 15%. Given the impact which holidays can have, weather etc. at the turn of the year we are not willing to read too much into the result and will stick with a view for now that sales are improving but at a fairly slow pace.

With regard to availability of stock we saw data last week from [www.realestate.co.nz](http://www.realestate.co.nz) showing a fall in the weeks worth of inventory around the country to just over 36 from 39 six months ago. The change is not large but the trend is downward for this measure, thus giving empirical evidence of the sharp tightening in property availability noted in the NZ Herald’s articles of last week.



Barfoot and Thompson reported total listings of 4,766 at the end of January which was a 19% decline from a year earlier. We like to plot the ratio of sales to listings against the annual change in Auckland dwelling sales prices measured from REINZ data. The orange line implies house price inflation around the 8% level could reasonably be expected soon.



The Barfoots average sale price actually dropped sharply in the month to \$529,000 from \$573,000 in December. But there is almost always a fall in price over this period so we read little into it and note that compared with a year earlier prices were ahead 2.5%. There is mild price growth but nothing strong.

### Migration A Drag

The monthly migration numbers were released this week and they show that in seasonally adjusted terms the country suffered a loss of 520 people in December which when we add in the previous two months gives flows running at an annualised loss recently of near 5,000. That is what the annual flow will probably exceed soon. In calendar 2011 the net migration loss was 1,855 compared with a gain of 10,451 over 2010. The deterioration results from inflows rising 2% but outflows rising nearly 20%, entirely because so many of us have been attracted across the ditch.

The gross outflow to Australia topped 50,000 over 2011 and the net outflow hit a record 36,208 from 20,988 a year ago.

The net population loss will clearly take some of the heat out of the housing market. But as we have noted in various ways since 2004, the key fundamental driving the housing market in NZ is weak construction which is running near four decade lows. That situation does not look like changing soon therefore we can expect to see worsening accommodation shortages, rising rents, and of course rising prices.

### Survey Measures All Rise

Our monthly BNZ-REINZ Residential Market Survey has found rises in all gauges from more first home buyers perceived as being in the market, more people at Open Homes, investors appearing, prices seen as rising, and sellers now being seen as in a stronger position than buyers on average. The results can be found here.

<http://tonyalexander.co.nz/bnz-reinz-survey/>

### Are You Seeing Something We Are Not?

If so, email us at [tony.alexander@bnz.co.nz](mailto:tony.alexander@bnz.co.nz) with Housing Comment in the Subject line and let us know.

# MAJOR OFFSHORE ISSUES

## European Debt

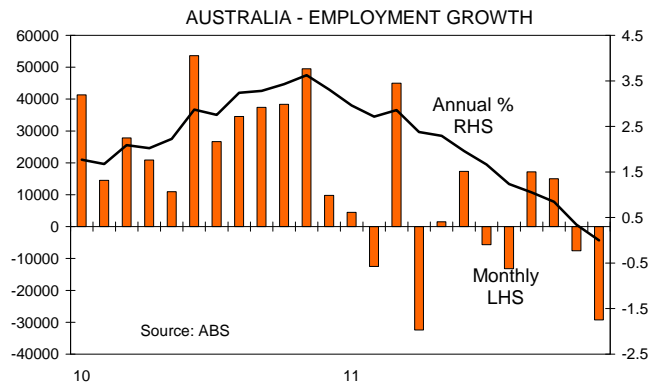
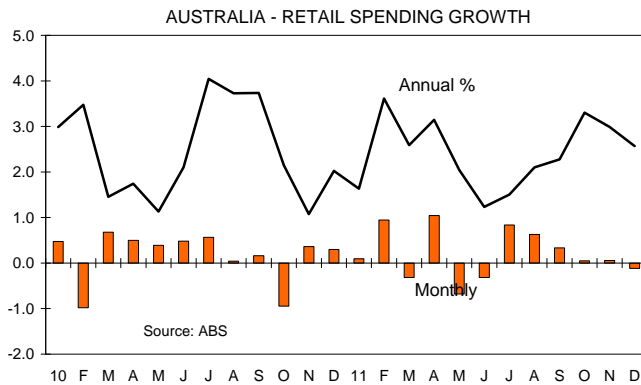
There appears to be a very good chance that the Greeks have decided to make the fiscal and regulatory changes demanded by the European Commission, European Central Bank, and the IMF. If that is the case then a lot of their debt will be written off and Europe will pull back from the brink. But we have been in exactly this position before so there is little reason yet for believing that 2012 will not have the disturbances of 2011 stemming from Europe's multi-year government debt, bank debt, and economic inefficiencies crisis.

## United States Growth

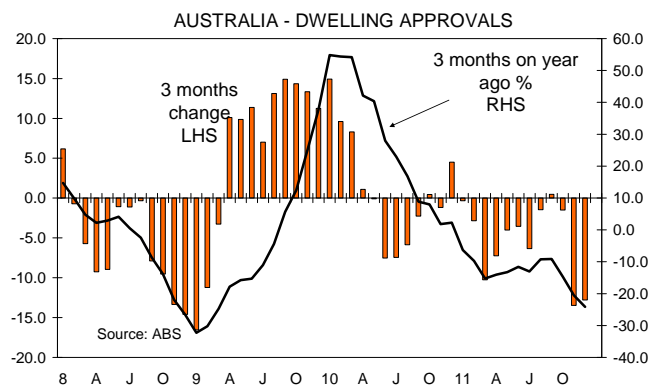
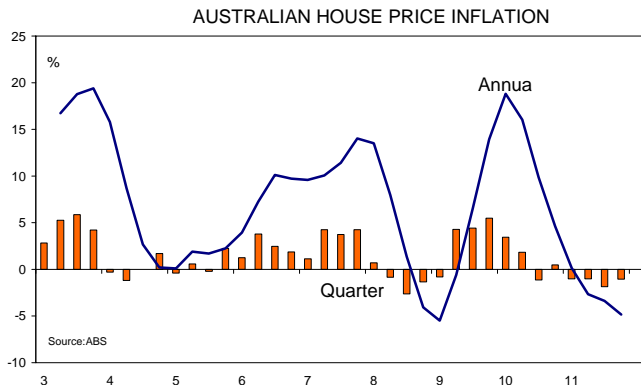
The major piece of data for the week came out of the United States on Friday night in the form of job numbers rising 100,000 more than expected by 243,000 in January and the unemployment rate falling to 8.3% from 8.5%. Given the underlying population growth the fall in the unemployment rate from 9% in September is substantially due to discouraged people leaving the workforce rather than extra strong jobs growth. Nevertheless the result gives credence to an underlying growth story in the United States which saw the Dow Jones Industrials Index rise to a three year high and bond yields jump firmly. Oil prices also bounced up.

## Australian Growth

The RBA surprised 75% of the market this week by leaving their cash rate unchanged at 4.25% rather than cutting it. This in spite of much recent data being weaker than expected. Retail sales for instance fell by 0.1% in December after rising just 0.1% in November and remaining unchanged in October. The employment report released a couple of weeks ago also showed job numbers down 29,000 in December with 0% growth recorded from a year earlier.



Average state capital city house prices fell by 1% in the December quarter after falling 1.9% in the September quarter. They now lie 4.8% down from a year ago. Approvals for the construction of new dwellings also fell 1% in December to make a 10% fall for the December quarter.



## BNZ WEEKLY OVERVIEW

So the bulk of data released recently have been weak. However the RBA made it clear when they cut interest rates in November and December last year that developments offshore were foremost in their mind with the first two paragraphs of each commentary accompanying the rate cut decision focussing on weakness in offshore economies. Recently developments have given some cause for hope hence it appears the RBA feels no further insurance against offshore weakness is warranted. However should things turn sour again offshore there can be little doubt that they would cut again.

### China

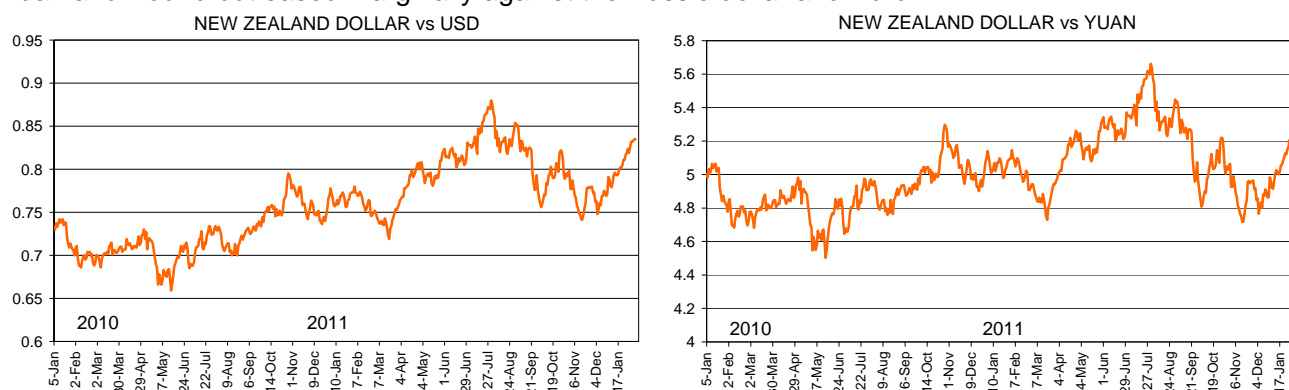
Working on the new publication.

## Exchange Rates

Exchange Rates	This Week	Week ago	4 wks ago	3 Mths ago	Yr ago	10 yr average	
NZD/USD	0.835	0.832	0.779	0.798	0.774	0.67	
NZD/AUD	0.774	0.778	0.763	0.769	0.762	0.85	
NZD/JPY	64.400	63.400	59.800	62.000	63.7	69.6	
NZD/GBP	0.528	0.525	0.505	0.496	0.482	0.388	
NZD/EUR	0.629	0.632	0.614	0.577	0.567	0.52	
NZDCNY	5.259	5.247	4.915	5.065	5.098	4.99	
USD/JPY	77.126	76.202	76.765	77.694	82.300	105.7	
USD/GBP	1.581	1.585	1.543	1.609	1.606	1.72	
USD/EUR	1.328	1.316	1.269	1.383	1.365	1.28	
AUD/USD	1.08	1.07	1.02	1.04	1.02	0.788	
USD/RMB	6.2984	6.306	6.3095	6.3465	6.586	7.56	

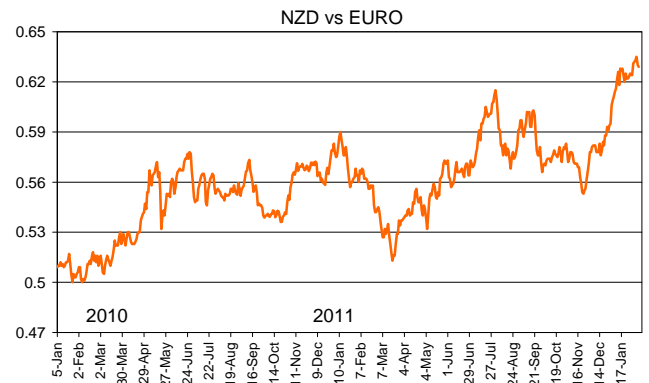
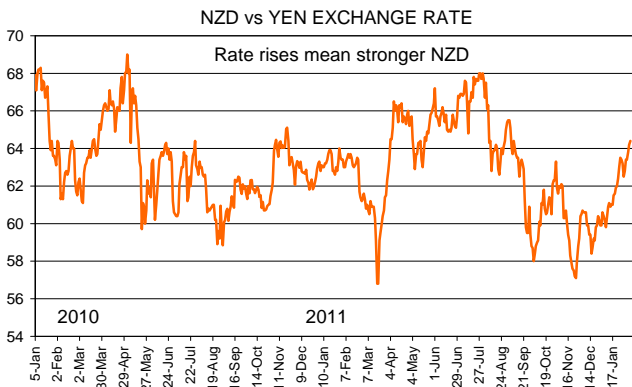
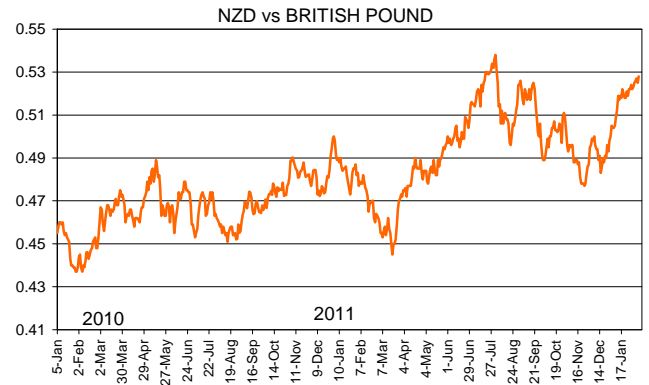
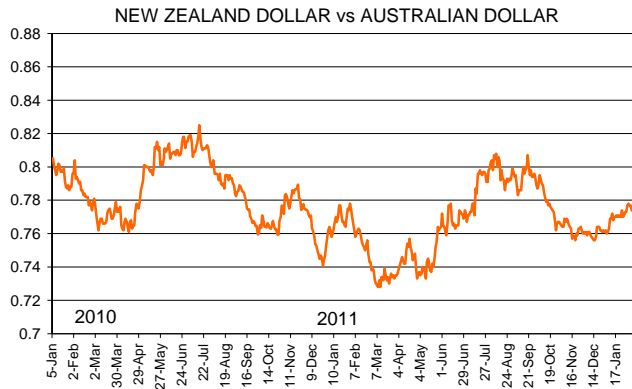
### Kiwi Hits Six Month High

The Kiwi dollar this week has gained slightly from where it was seven days ago against the greenback, Yen, Yuan and Pound but eased marginally against the Aussie dollar and Euro.



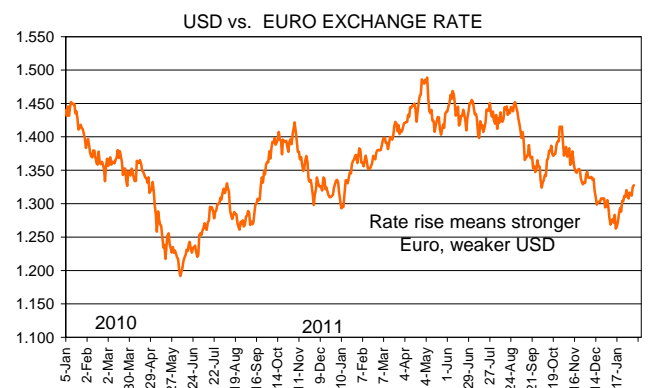
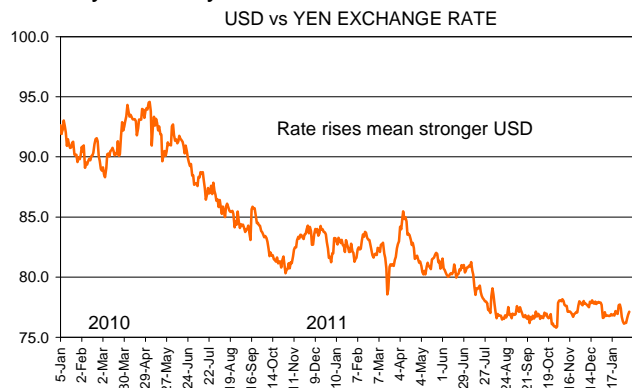
This strength in the NZ dollar stems partly from the Reserve Bank of Australia's decision to leave their cash rate unchanged at 4.25%. The markets had been primed for a 0.25% cut so the steady policy and limited indication of any intention to cut in the future spurred the AUD higher to a six month high against the greenback. The Kiwi dollar rode the coat-tails of the AUD higher while losing slight ground against the Aussie currency. Against the Japanese Yen the NZD has now risen to a half year high while against the British pound it is getting close to rising above the 33 year high of 53.8 reached last August.

# BNZ WEEKLY OVERVIEW



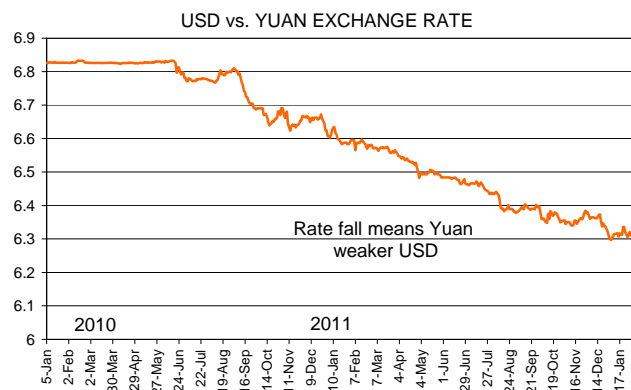
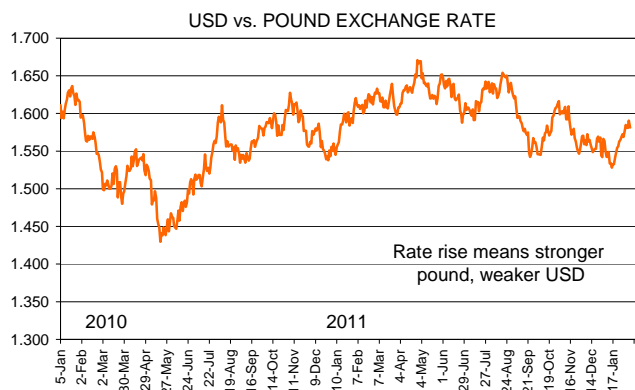
This morning's weaker than expected employment data had little impact on the NZD with attention largely focussed on the ability of the AUD to rise further and developments in Europe. If a restructuring deal is agreed with Greece then the reduction in global risk will add further impetus to the NZD's nine cent gain over the past seven weeks and a movement toward 85 cents would seem likely. If however things go bad in Europe then the NZD would shed some of its recent gains as investors moved away once more from risky assets.

With regard to the greenback there has been broad downward pressure this week against the Euro stemming from rising willingness of investors to embrace risk and sell safe-haven assets like the greenback following the good January employment data, plus some dovish comments from the Federal Reserve Chairman. But the USD has edged up a tad against the Japanese Yen which also ranks as a safe haven currency currently.



Overall though there seems little clear direction in the USD against the Yen and pound, the hint of a trend change against the Euro (stronger Euro) and continuing slow depreciation against the Yuan.

## BNZ WEEKLY OVERVIEW



### Exchange Rate Assumptions

This table contains the latest NAB currency forecasts. In red I indicate where I believe the risk lies for these rates. You are welcome to toss your own coin and generate an equally valid table.

	2011	2012	Risk	2013	Risk
Year end					
NZD/USD	0.77	0.82	Higher	0.77	Higher
NZD/AUD	0.76	0.82		0.81	
NZD/YEN	60.0	66		63	Higher
NZD/GBP	0.50	0.53	Higher	0.50	Higher
NZD/EUR	0.60	0.64	Higher	0.57	Higher
USD/JPY	78	81	Lower	82	Lower
GBP/USD	1.54	1.56	Lower	1.53	Lower
EUR/USD	1.30	1.29	Lower	1.36	Lower
AUD/USD	1.01	1.00	Higher	0.95	Higher

**ECONOMIC DATA**

All %		Latest qtr only	Previous qtr only	Latest year	Year ago	2 Yrs ago
Inflation	RBNZ target is 1% - 3% on average	-0.3%	0.4	1.8	4.0	2.0
GDP growth	Average past 10 years = 2.6%	0.8	0.1	+1.3	1.0	-2.7
Unemployment rate	Average past 10 years = 4.8%	6.3	6.6	.....	6.7	6.9
Jobs growth	Average past 10 years = 1.9%	0.2	0.2	1.6	1.3	-2.2
Current a/c deficit	Average past 10 years = 5.5% of GDP	4.3	3.7	.....	3.5	3.0
Terms of Trade		-0.6	2.4	3.4	17.9	-14.1
Wages Growth	Stats NZ analytical series	1.0	0.8	3.4	3.4	3.7
Retail Sales ex-auto	Average past 9 years = 3.9%.	2.4	1.1	2.1	2.3	-2.5
House Prices	REINZ Stratified Index	1.7	0.5	3.0	0.7	-0.4
Net migration gain	Av. gain past 10 years = 13,900	-1,855	773yr	.....	10,451	22,253
Tourism – an. av grth	10 year average growth = 3.2%. Stats NZ	2.9	1.2	2.9	2.8	-0.0
		Latest year rate	Prev mth year rate	6 mths ago	Year ago	2 yrs ago
Business confidence	BNZ survey	13	3	45	22	37
Consumer confidence	ANZ-Roy Morgan 100=neutral	116	108	109	117	131
Household debt	10 year average growth = 10.3%. RBNZ	1.0	1.1	1.2	1.8	2.9
Dwelling sales	10 year average growth = 2.5%. REINZ	20.9	16.9	14.3	-11.3	15.2
Floating Mort. Rate	(TotalMoney) 10 year average = 7.9%*	5.74	5.74	5.59	6.09	5.59
3 yr fixed hsg rate	10 year average = 7.8%	6.45	6.45	6.99	7.15	7.95

All actual data excluding interest & exchange rates sourced from Statistics NZ.

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**Key Forecasts**

Dec. year		2010	2011	2012	2013
GDP	annual average chg	1.4	1.5 – 2.0	1.5 – 2.2	2.5 – 3.5
CPI	on year ago	4.0	1.8	2.0 – 2.6	2.5 – 2.9
Official Cash rate	end year	3.0	2.5	2.25 – 2.75	3.25 – 4.25
Employment	on year ago	1.3	1.5 – 2.0	1.0 – 1.6	1.5 – 1.9
Unemployment Rate	end year	6.8	6.0 - 6.5	5.5 – 6.0	4.8 – 5.5

\*extrapolated back in time as TotalMoney started in 2007

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