

Businesses see China and the US as key influences on NZD

- The ASB Institutional Kiwi Dollar Barometer tracks exporters', and importers' and importer/exporters' exposures to foreign exchange risk, through surveying businesses with annual turnover of at least NZ\$1 million. The Barometer also surveys businesses' expectations for the NZD/USD and businesses' hedging plans for managing foreign exchange risk, as well as special questions on topical issues in the FX markets.
- Businesses see China and the US as having the most influence on the NZD/USD over the coming year. Exporters were more likely to name the economic development of China as key, while importers were more likely to name the US as having the most influence on the NZD.
- Interest rate differentials and safe-haven investment flows were seen as the key drivers of the current strength in the NZD/USD.

Most influential regions for NZD

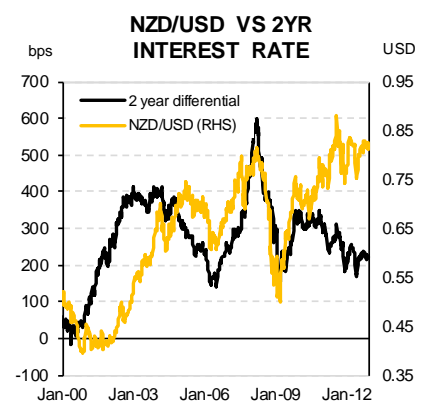
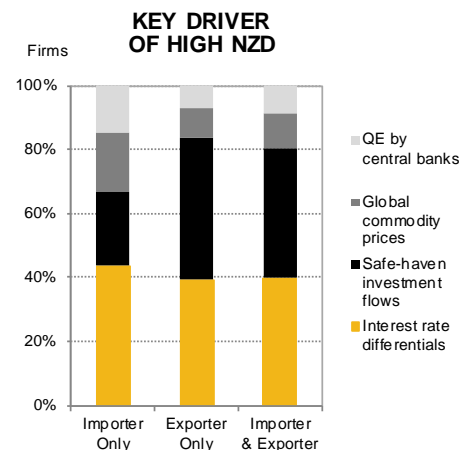
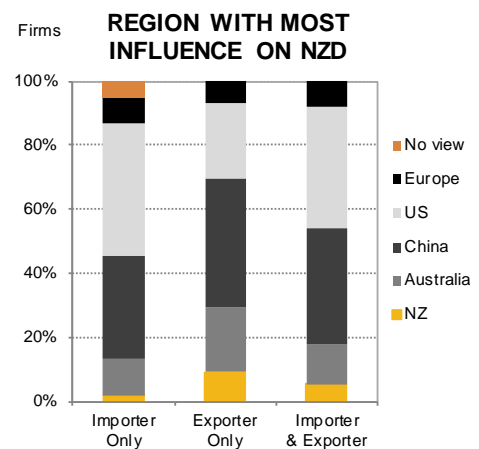
The ASB Institutional Kiwi Dollar Barometer indicates businesses see China and the US as the regions with the most influence on the NZD/USD over the next twelve months. Exporters were more likely to name China as being the key influence for the NZD, while importers were more likely to name the US as key.

- Of all the businesses surveyed, 35.6% see China as the key region. The US follows close behind with 35.3% of businesses naming this region as a key influence on the NZD/USD.
- Just over 40% of exporters saw China as the region having the most influence on the NZD over the coming year. Of the other regions, the US and Australia were also seen as fairly influential for the NZD, with just over 23% and 20% of exporters picking these regions respectively.
- Importers were more likely to see the US as a key influence on the NZD, with just over 41% picking this region. China was also seen as very influential for the NZD, with just over 32% of importers naming this region as key. A small proportion of importers picked Australia and Europe as the regions having a key influence on the NZD (just over 11% and 8% respectively).

Key drivers of strong NZD

Interest rate differentials (41%) and safe-haven investment flows (34%) were seen as the key factors behind the current strength in the NZD/USD. While interest rate differentials were seen as the most important factor across all types of businesses, a higher proportion of exporters, relative to importers, named safe-haven investment flows as the key driver.

- Amongst exporters, just over 44% of businesses see safe-haven investment flows as the key driver of the NZD, with interest rate differentials coming a close second with just over 39% of businesses naming it as the biggest factor.
- Just over 43% of importers saw interest rate differentials as the biggest factor behind the current strength in the NZD. Beyond that, importers were roughly split between safe-haven investment flows (23%), global commodity prices (19%) and quantitative easing by the major central banks (15%) as the key factor driving the current strength in the NZD.



Interest rate differentials tend to become more important for the direction of currencies in times of low market volatility. While NZ interest rates have generally fallen over the past year, these moves generally reflect the decline in interest rates offshore. NZ interest rates remain high relative to those in the major economies. In particular, the Federal Reserve has indicated US interest rates are likely to remain extremely low through 2015.

The substantial proportion of businesses which see safe-haven investment flows as a key driver of the current strength in the NZD is surprising. Typically, the USD and JPY are perceived as the safe-haven currencies: a deterioration in market sentiment tends to see demand for the USD and the JPY increase, with the NZD depreciating accordingly. It may be the case businesses see the NZ economy as relatively stable in light of the uncertainty in many of the major economies recently, and hence now perceive NZ as a safe haven for global investors.

We link higher global commodity prices to the sustained strength in the NZD over the last seven years. However, in the survey respondents put a relatively small weight on this influence. Even fewer respondents regarded quantitative easing as the biggest influence on the NZD, notwithstanding the recent media debate after the US embarked on its third round of QE. We consider the influence of QE on the NZD as being at the margin – yet another reminder of NZ’s relatively healthy fundamentals.

FX forwards most common form of FX transaction

Businesses were asked what proportions of FX transactions were allocated to spot, forwards and options. Results were similar across exporters and importers, with all businesses surveyed allocating on average just over 65% of their FX transactions to FX forwards. Larger businesses tended to allocate a greater proportion of their FX transactions to FX forwards.

- Businesses with annual turnover of over \$150 million on average use FX forwards for just over 81% of their FX transactions. A small proportion of FX transactions were allocated to FX options (14%) and spot (5%).
- The use of FX forwards was much less common amongst small- and medium-sized businesses. Amongst businesses with annual turnover of between \$1 to 30 million, 49% of FX transactions were done through spot, while 47% were done through FX forwards.

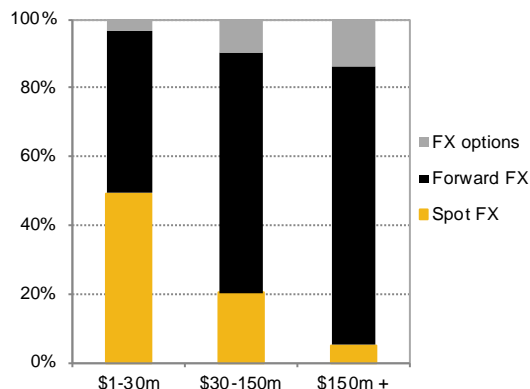
These results indicate larger businesses make much greater use of forwards and options to manage their foreign exchange risk. There is scope for small and medium sized businesses to make more use of these tools to manage their business risks.

Businesses expect NZD to peak in June 2013

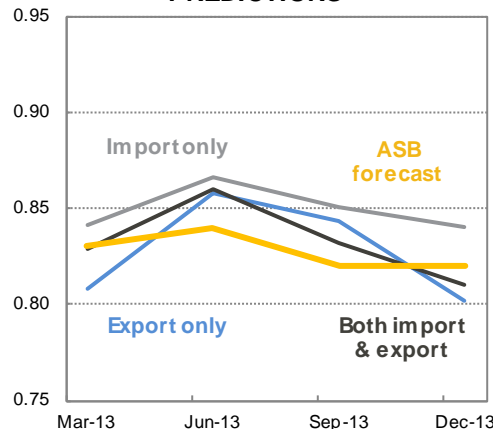
Businesses’ expectations of the NZD/USD have risen in recent quarters, such that they are now reasonably close to ASB Economics’ forecasts. Importers continue to have higher NZD expectations relative to exporters. On average, businesses across all business types expect the NZD/USD to peak in June next year at 86.2 cents.

- Exporters, on average, expect the NZD/USD to peak at 85.8 cents in June 2013, before easing to 80.2 cents by the end of next year.
- Although importers also expect the NZD/USD to peak in June 2013, on average they expect a slightly higher peak of 86.6 cents. Importers expect the NZD/USD to ease from there by a milder amount, to reach 84.0 cents by the end of next year.

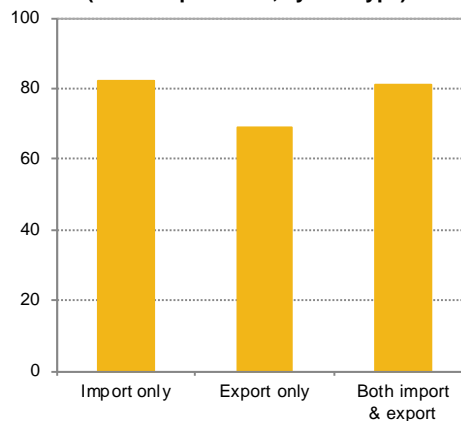
FX TRANSACTIONS ALLOCATED
(proportion of transactions)



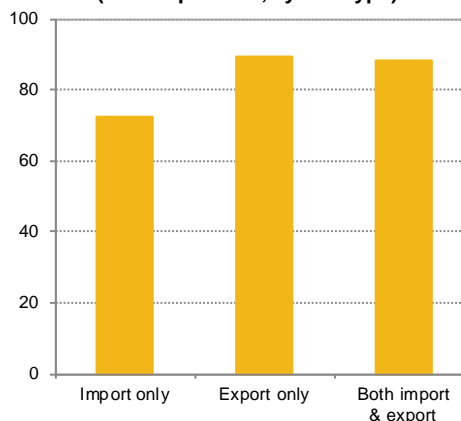
NZD BAROMETER PREDICTIONS



PLANS TO HEDGE
(% of respondents, by firm type)



AVERAGE HEDGES
(% of exposures, by firm type)



ASB Economics also expect the NZD/USD to peak in June 2013, but at a lower peak of 84 cents. Beyond that, ASB Economics expect the NZD to gradually ease to 82 cents by the end of next year, as economic activity in the major economies starts to pick up.

Managing currency risk

Hedging currency exposure is a way of managing possible future adverse changes in the currency. The proportion of businesses intending to hedge their foreign exchange exposures continues to increase, suggesting NZ businesses are becoming more engaged with managing their foreign exchange risk.

A smaller proportion (just under 69%) of exporters indicated they intend to hedge their FX exposures (relative to 82% of importers), but those exporters that did expect to hedge a larger proportion of their exposures (89%), relative to the proportion of FX exposures expected to be hedged by importers (73%).

This pattern is in line with that found in the latest Australian Dollar Barometer, with a lower proportion of Australian exporters planning to hedge their FX exposures (57.7% of exporters and 81.9% of importers) but those that do on average planning to hedge a greater proportion of their FX exposures (85.2% for hedging exporters and 76.4% for hedging importers). However, NZ businesses appear to hedge to a greater extent.

The NZ Dollar Barometer also finds the larger the business, the greater the average proportion of FX exposure that is hedged. This may reflect the fact larger businesses tend to have more formal hedging policies in place which set the proportion of FX exposure required to be hedged.

Key “take-outs” from the ASB Institutional Kiwi Dollar Barometer

The Kiwi Dollar Barometer indicates businesses see China and the US as the regions that will have the most influence on the NZD/USD over the coming year. Exporters were more likely to name China as the region with the most influence on the NZD, while importers were more likely to name the US as key.

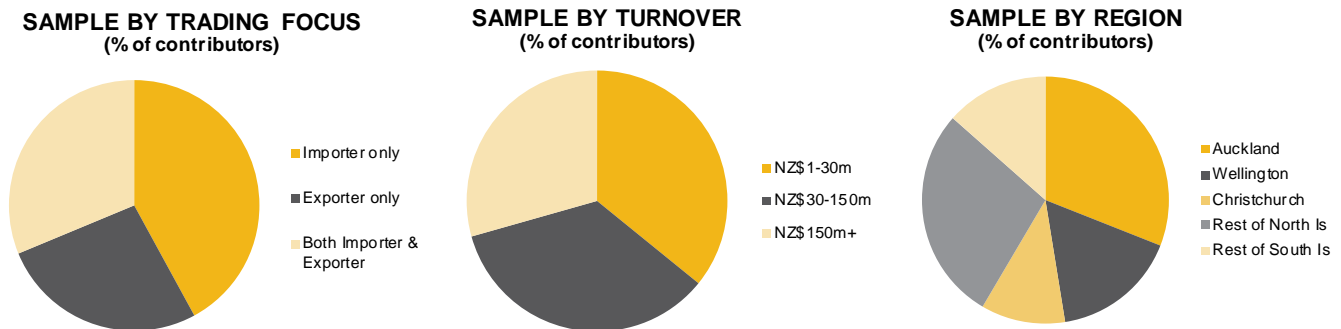
Meanwhile, interest rate differentials and safe-haven investment flows were seen as the key drivers of the current strength in the NZD/USD. Market participants tend to focus on interest rate differentials in times of low market volatility, and NZ's relatively high interest rates have supported demand for the NZD in recent years. The substantial proportion of respondents picking safe-haven investment flows as the biggest influence on the NZD is more surprising, given the USD and JPY are typically seen as the safe-haven currencies. These results suggest businesses regard NZ as a good place to invest in given the stability of the NZ economy relative to many of the major economies recently. Despite a lot of debate recently about the influence of quantitative easing on the NZD, few respondents saw it as the key factor behind the NZD's strength.

Of the businesses surveyed, the majority of FX transactions were done through FX forwards. This was particularly the case amongst large companies, with just over 81% of their FX transactions allocated to FX forwards. The use of FX forwards was less prevalent amongst small businesses, with just under half of their FX transactions done through spot FX. This suggests scope for smaller-sized businesses to make more use of FX forwards and options to manage their foreign exchange risks.

About the Kiwi Dollar Barometer

The ASB Institutional Kiwi Dollar Barometer will be prepared every three months based on a survey conducted by East & Partners. East & Partners is a market research and advisory firm.

For the December 2012 edition of the ASB Kiwi Dollar Barometer, East & Partners interviewed 371 businesses turning over at least NZ\$1 million per year. The interviews were conducted between 22nd October to 5th November. Businesses were asked a range of questions about their exposure to and views about the NZD. The charts below provide information on the survey sample.



The specific questions asked were:

1. What approximate NZD/USD exchange rate do you expect to see by:
 - end-March 2013
 - end-June 2013
 - end-September 2013
 - end December 2013
2. What percentage of your FX exposures are you planning to hedge in the next 3 months?
3. By what percentage are you expecting your foreign currency exposure to change over the next 3 months?
4. What do you see as the biggest single factor behind the current NZD/USD strength?
 - Interest rate differentials
 - Global commodity prices
 - Quantitative easing by the major central banks
 - Safe-haven investment flows
 - Other
5. Which region's development do you consider will have the most influence on the NZD/USD over the next twelve months?
 - New Zealand
 - Australia
 - China
 - United States
 - Europe
6. What proportion of FX transactions are you currently allocating to each of the following?
 - Spot
 - Forwards
 - Options

Chief Economist	Nick Tuffley	nick.tuffley@asb.co.nz	(649) 301 5659	(649) 302 0992
Senior Economist	Jane Turner	jane.turner@asb.co.nz	(649) 301 5660	
Economist	Christina Leung	christina.leung@asb.co.nz	(649) 301 5661	
Economist	Daniel Smith	daniel.smith@asb.co.nz	(649) 301 5853	

<https://reports.asb.co.nz/index.html>

ASB Economics

Level 9, 135 Albert Street, Auckland

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