

PERFORMANCE OF SERVICES INDEX



BusinessNZ 

Service sector still struggling in tough economic conditions

The Bank of New Zealand - Business NZ Performance of Services Index is a monthly survey of the services sector providing an early indicator of activity levels. A PSI reading above 50 points indicates services activity is expanding; below 50 indicates it is contracting.

Bank of New Zealand - Business NZ PSI for October 2008

- The Bank of New Zealand - Business NZ Performance of Service Index (PSI) remains in contraction, with the October result (48.7) the seventh consecutive time in which the overall sector has contracted. On a positive note, the October result was 1.8 points higher than September, but 9.7 points down from the same month in 2007.
- Only two of the five diffusion indices that make up the PSI exhibited contraction during October. However, these two involved the key indices of *activity/sales* (46.8) and *employment* (47.1), which dragged the overall index down. *New orders/business* (50.0) recovered from its minor contraction in September to show no change for the current month, while *deliveries* (50.2) also recovered from September. *Stocks/inventories* (52.0) experienced a minor drop, but still in expansion.
- Activity by region continued to show a similar pattern to previous months. The *Northern* region (48.4) improved slightly, with its highest result since May. The *Central* region (55.4) recovered to levels experienced in August, and has shown the strongest growth of any region over the last four months. In the South Island, the *Canterbury/Westland* region (52.3) continued to build on its September result, while the *Otago/Southland* region (37.7) remained entrenched with a value below 40.
- The various service sectors continued to be almost all in contraction mode during October, with only *health & community services* (53.9) and *property & business services* (50.2) in positive territory. Encouragingly, *wholesale trade* (49.6), *accommodation, cafes & restaurants* (49.7) and *transport & storage* (49.9) all were close to the level of no change for the month. *Retail trade* (46.6) improved slightly on September, although still remained in contraction for the seventh consecutive month.
- Three of the four firms by employment size experienced contraction during October. Large firms (101+ workers) experienced the lowest level of activity (47.4), followed by micro firms (1-10 workers) (48.0). Medium-large firms (51-100 workers) (48.3) improved on the previous month, while small-medium firms (11-50 workers) (50.1) was largely in a state of no change for October after five consecutive months in contraction.
- The proportion of negative comments from respondents during October stood at 62.4%, exactly the same as that received in September. However, there was a distinct difference comparing activity with the same time last year for positive and negative comments. Unlike last month when the average was the same, activity for those with negative comments (3.8*) worsened significantly, while for positive comments there was a strong improvement (2.3).

HIGHLIGHTS

- **The overall level of activity for the service sector remained in contraction for the seventh consecutive month.**
- **Both activity/sales (46.8) and employment (47.1) improved on September, but remained in contraction.**
- **The Central region continued to lead regional activity, while Otago/Southland remained weak.**
- **The proportion of negative comments from respondents was unchanged at 62.4%.**

Next Bank of New Zealand - Business NZ PSI: December 15 2008

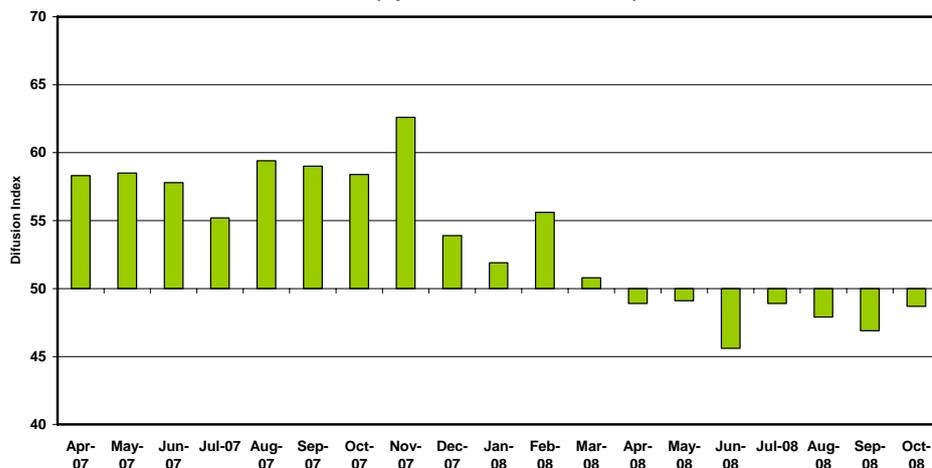
SPONSOR STATEMENT

Bank of New Zealand Ltd is delighted to be associated with the Performance of Services Index (PSI) and Business NZ. This association brings together the significant experience of leading business advocacy body Business NZ, and business finance specialist BNZ. We look forward to continuing our association with Business NZ and associated regional organisations, and to playing our part in the ongoing development of the New Zealand services sector.

Bank of New Zealand (www.bnz.co.nz)

*Respondents are asked for a score from 1-5, where 1= large rise and 5= large fall.

Bank of New Zealand - Business NZ Performance of Services Index Time Series (April 2007 - October 2008)



PSI time series tables

National Indexes	Oct 2007	Jun 2008	Jul 2008	Aug 2008	Sep 2008	Oct 2008
Bank of New Zealand - Business NZ PSI	58.4	45.6	48.9	47.9	46.9	48.7
Activity/Sales	58.7	44.9	47.9	41.2	43.9	46.8
Employment	52.2	41.8	47.5	48.1	45.8	47.1
New Orders/Business	66.0	51.4	52.7	50.2	49.4	50.0
Stocks/Inventories	56.7	46.6	46.7	53.2	53.0	52.0
Supplier Deliveries	57.0	42.7	48.2	51.3	45.6	50.2

Regional Indexes	Oct 2007	Jun 2008	Jul 2008	Aug 2008	Sep 2008	Oct 2008
Bank of New Zealand - Business NZ PSI	58.4	45.6	48.9	47.9	46.9	48.7
Northern	60.4	43.9	48.2	47.3	46.5	48.4
Central	54.7	47.9	54.9	55.4	52.7	55.4
Canterbury/Westland	59.6	51.1	51.1	47.7	50.9	52.3
Otago/Southland	55.3	36.1	40.4	39.3	37.0	37.7

PARTICIPANTS

Business NZ gratefully acknowledges the participation of the following associations in contributing to the PSI:

- Employers & Manufacturers Association (Northern)
- Employers & Manufacturers Association (Central)
- Canterbury Employers' Chamber of Commerce
- Otago Southland Employers Association
- Hospitality Association of New Zealand
- New Zealand Retailers Association
- Tourism Industry Association New Zealand

Disinflation an Economic Stabiliser

- Inflation is dying
- Led by slumping commodity prices
- Interest rates will be slashed further
- The currency will drift lower
- The pain before the gain

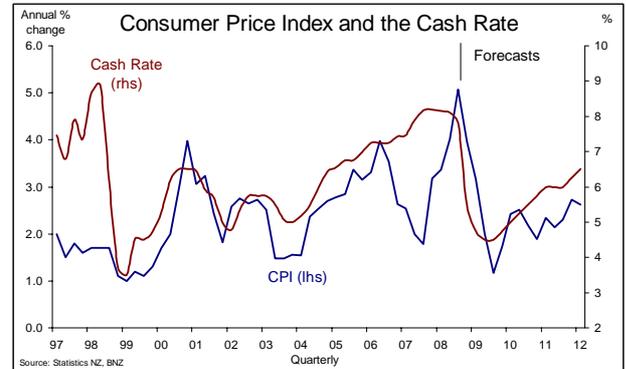
Things are very tough out there at the moment and few businesses are escaping the fact that the economy is now in the midst of what we believe to be the fourth quarter of the current recession. Moreover, there is more pain to come yet with the next leg of the downturn likely led by a sharp contraction in investment activity and a significant increase in the unemployment rate.

While this is a far from inspiring environment, the good news is that the economy's automatic stabilisers are swinging into action. These will not only provide some short term relief but will also start the wheels turning that will eventually see an end to this downturn.

Foremost amongst the adjustments that inevitably take place when the economy slows is the death of inflation. At least in this regard, this cycle looks to be no different to all the others. As domestic demand softens, spare capacity in the economy begins to appear and inflationary pressures fall. From a New Zealand Inc perspective we are only just seeing the first signs of this with non-tradables inflation still fairly lofty and only expected to fall gradually.

However, where the big disinflationary pulse is coming from is the demise of demand globally and the ensuing drop in commodity prices. Global growth forecasts are being slashed by the day. At the beginning of the year the consensus was that global growth of 3.4% would be reported for calendar 2009. At the time this was a small improvement on what was then expected for 2008. By September the expectation for calendar 2009 had fallen to 2.5%. Then the fun really began with the forecast being slashed to 1.9% in October and to a paltry 1.1% in November. On this basis, it looks like the global environment is much worse than what accosted us in the major downturn of 1991/92 and rather more like what was seen in 1982.

Consistent with this, commodity prices of all types are in freefall. Most notable for the world, and us, has been the drop in oil prices. Dubai Crude, the oil New Zealand



uses, has slumped from USD140 a barrel in mid July to just USD48 now. This has had a massive impact on New Zealand pump prices resulting in 91 Octane dropping from 218.9c/l early in July to 154.9 now.

Consequently, this has resulted in a massive shift in expectations for total CPI inflation at home. Annual inflation peaked at 5.1% in the third quarter and we reckon it will be just 1.2% by this time next year. The reduction in inflation will soon start to haul back wage increases too.

Accordingly, the Reserve Bank has been given the green light to lower its cash rate aggressively. It's already gone from 8.25% to 6.50% and we see it dropping another 2.0% over the next few months. This, in turn, is resulting in a sharp drop in the exchange rate, with more to come.

Ultimately, these developments will eventually set the scene for an economic rebound particularly when the effects are compounded by substantial easing in fiscal policy. Even as things stand, most of the aforementioned events should come as an immediate welcome relief to businesses.

This aside, it's way too early to pop the champagne corks. To start with, the resolution of our current demand weakness is still some way off meaning that businesses will continue to face faltering sales for some time to come. Moreover, while the falling NZD is great news for exporters it's a substantial impost for importers and retailers who will not be able to pass on the full burden of the exchange rate to their customers.

stephen_toplis@bnz.co.nz

Contact Details

Bank of New Zealand Research



Stephen Toplis
Head of Research
+(64 4) 474 6905

Craig Ebert
Senior Markets Economist
+(64 4) 474 6799

Mark Walton
Markets Economist
+(64 4) 474 6923

Danica Hampton
Currency Strategist
+(64 4) 472 4767

Main Offices

Wellington
1 Willis Street
PO Box 2392
Wellington
New Zealand
Phone: +(64 4) 474 6145
FI: 0800 283 269
Fax: +(64 4) 474 6266

Auckland
125 Queen Street
PO Box 2139
Auckland
New Zealand
Phone: +(64 9) 976 5762
Toll Free: 0800 081 167

Christchurch
129 Hereford Street
PO Box 1461
Christchurch
New Zealand
Phone: +(64 3) 353 2219
Toll Free: 0800 854 854

NAB/nabCapital Research



Peter Jolly
Head of Research
+(61 2) 9295 1199

Alan Oster
Group Chief Economist
+(61 3) 8641 3464

Rob Henderson
Chief Economist, Markets
+(61 2) 9237 1836

John Kyriakopoulos
Currency Strategist
+(61 2) 9237 1903

Contact Phone Numbers

Wellington
Foreign Exchange +800 642 222
Fixed Income/Derivatives +800 283 269

Sydney
Foreign Exchange +800 9295 1100
Fixed Income/Derivatives +(61 2) 9295 1166

London
Foreign Exchange +800 333 00 333
Fixed Income/Derivatives +(44 20) 7796 4761

New York
Foreign Exchange +1800 125 602
Fixed Income/Derivatives +1877 377 5480

Hong Kong
Foreign Exchange +(85 2) 2526 5891
Fixed Income/Derivatives +(85 2) 2526 5891

24 HOUR FOREIGN EXCHANGE SERVICE

Phone Toll Free 6am to 10pm NZT – Wellington Office
0800 739 707 10pm to 6am NZT – London Office – Olivia Core

ANALYST DISCLAIMER: The person or persons named as the author(s) of this report hereby certify that the views expressed in the research report accurately reflect their personal views about the subject securities and issuers and other subject matters discussed. No part of their compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in the research report. Research analysts responsible for this report receive compensation based upon, among other factors, the overall profitability of the Markets Division which is part of nabCapital a division of National Australia Bank Limited, a member of the National Australia Bank Group ("NAB"). The views of the author(s) do not necessarily reflect the views of NAB and are subject to change without notice. NAB may receive fees for banking services provided to an issuer of securities mentioned in this report. NAB, its affiliates and their respective officers, and employees, including persons involved in the preparation or issuance of this report (subject to the policies of the National), may also from time to time maintain a long or short position in, or purchase or sell a position in, hold or act as advisors, brokers or commercial bankers in relation to the securities (or related securities and financial instruments), of companies mentioned in this report. NAB or its affiliates may engage in these transactions in a manner that is inconsistent with or contrary to any recommendations made in this report.

NEW ZEALAND DISCLAIMER: This publication has been provided for general information only. Although every effort has been made to ensure this publication is accurate the contents should not be relied upon or used as a basis for entering into any products described in this publication. Bank of New Zealand strongly recommends readers seek independent legal/financial advice prior to acting in relation to any of the matters discussed in this publication. Neither the Bank of New Zealand nor any person involved in this publication accepts any liability for any loss or damage whatsoever may directly or indirectly result from any advice, opinion, information, representation or omission, whether negligent or otherwise, contained in this publication.

US DISCLAIMER: This information has been prepared by National Australia Bank Limited or one of its affiliates or subsidiaries ("NAB"). If it is distributed in the United States, such distribution is by nabCapital Securities, LLC which accepts responsibility for its contents. Any U.S. person receiving this information wishes further information or desires to effect transactions in the securities described herein should call or write to nabCapital Securities, LLC, 28th Floor, 245 Park Avenue, New York, NY 10167 (or call (877) 377-5480). The information contained herein has been obtained from, and any opinions herein are based upon, sources believed to be reliable and no guarantees, representations or warranties are made as to its accuracy, completeness or suitability for any purpose. Any opinions or estimates expressed in this information is our current opinion as of the date of this report and is subject to change without notice. The principals of nabCapital Securities, LLC or NAB may have a long or short position or may transact in the securities referred to herein or hold or transact derivative instruments, including options, warrants or rights with securities, or may act as a market maker in the securities discussed herein and may sell such securities to or buy from customers on a principal basis. This material is not intended as an offer or solicitation for the purchase or sale of the securities described herein or for any other action. It is intended for the information of clients only and is not for publication in the press or elsewhere.

