

Consumer confidence bounces back

Q2 Westpac McDermott Miller Consumer Confidence Index: 119.3

- Consumer confidence rebounded in the June 2010 quarter, reaching its second highest level in 3½ years.
- Consumers' assessment of current conditions drove the increase, the major factor being a sharp increase in perceptions around whether now is a good or bad time to buy major household items.
- The rise in confidence implies stronger consumer spending growth ahead, and supports our view that the RBNZ's tightening cycle has only just begun.

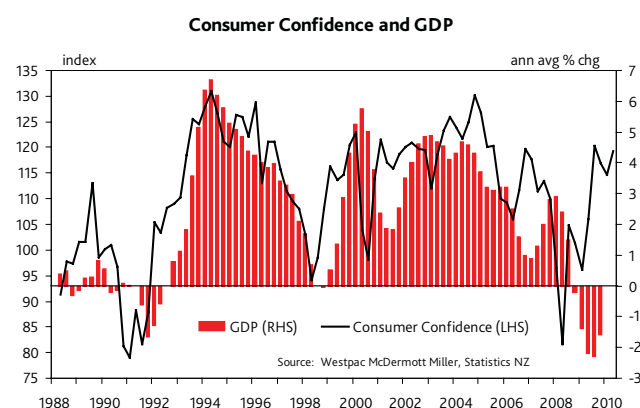
The Westpac McDermott Miller Consumer Confidence Index improved in the June 2010 quarter, rising from 114.7 to 119.3. This is the second highest reading on the Index since the December 2006 quarter and at these levels confidence remains well above the long term average of 111.6. An index number over 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 rebound in confidence is great news for the NZ economy. Consumer spending has been a notable weak spot in the economic recovery since the beginning of the year, with core retail spending being hit particularly hard. However, at these levels, confidence is indicative of a pick up in spending growth through the June quarter.

Other economic news supporting the rise in confidence, and reinforcing our view that consumer spending is set for something of a revival, includes:

- a sharp fall in unemployment;
- a cycle high in business confidence portending further improvements in the labour market;
- the announcement of a near-record payment to dairy farmers from Fonterra for 2011; and
- a \$15bn reduction in income tax over the next four years as announced in the Government's 2010 Budget.

Higher fuel prices and inflation in general, along with rising interest rates and falling house prices, will likely temper the increase in spending. However, overall we expect the pace



Consumer Confidence Indices

	Jun-10	Mar-10	change
Consumer Confidence Index	119.3	114.7	4.6
Present Conditions Index	108.5	99.5	9.0
Future Conditions Index	126.5	124.7	1.8

of spending growth to pick up from Q2 as income grows and the full gamut of tax changes in Budget 2010 improves most households' circumstances.

Survey details

Three of the five component questions increased this quarter. The most influential factor was a sharp improvement in consumers' perceptions of their current purchasing power. A net 31% of respondents say that now is a good time to buy a major household item, up 10 points from the March quarter and the highest reading for this component since the September 2005 quarter. While we expect continued solid discounting by retailers of durable goods is likely playing a part, the imminent increase in GST on 1 October will also be a contributing factor.

Consumers became much less despondent about their personal financial situation this quarter. A net 14% of respondents said they were worse off than a year ago, compared to a net 22% last quarter. This is the least pessimism shown by respondents in two and a half years. And importantly, consumers remain optimistic about the coming year, with a net 16% expecting their

For further information, questions or comments contact Brendan O'Donovan, telephone (04) 470 8250, email brendan_odonovan@westpac.co.nz

For all clients: Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141, incorporated in Australia ("Westpac"). The information contained in this report: does not constitute an offer, or a solicitation of an offer, to subscribe for or purchase any securities or other financial instrument; does not constitute an offer, inducement or solicitation to enter a legally binding contract; and is not to be construed as an indication or prediction of future results. The information is general and preliminary information only and while Westpac has made every effort to ensure that information is free from error, Westpac does not warrant the accuracy, adequacy or completeness of the Information. The Information may contain material provided directly by third parties and while such material is published with necessary permission, Westpac accepts no responsibility for the accuracy or completeness of any such material. In preparing the Information, Westpac has not taken into consideration the financial situation, investment objectives or particular needs of any particular investor and recommends that investors seek independent advice before acting on the Information. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. Except where contrary to law, Westpac intends by this notice to exclude liability for the information. The information is subject to change without notice. Westpac expressly prohibits you from passing on this document to any third party. Westpac Banking Corporation is registered in England as a branch (branch number BR000106) and is authorised and regulated by The Financial Services Authority. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised and regulated by The Financial Services Authority. © 2010 For Australian clients: WARNING - This document is provided to you solely for your own use and in your capacity as a wholesale client of Westpac.

own financial situation to improve over the next 12 months – unchanged from the March quarter.

The upbeat outlook for the economy remained intact this quarter, with a net 16% of respondents saying there will be good economic times in the coming year, up from a net 10% last quarter. Meanwhile, a net 47.6% of respondents still expect good economic times in New Zealand over the next five years, virtually unchanged from March.

By region, the lift in confidence was almost across the board, the exceptions being Gisborne/Hawke's Bay and Canterbury. Particularly sharp increases were registered in Southland, Taranaki/Manawatu/Wanganui, and Otago, likely reflecting the much improved outlook for dairy incomes. Still, on a levels basis confidence remains the highest in the cities, notably Auckland and Wellington.

Consumer Confidence Data

Region	Jun-09	Mar-10	Jun-10
Northland	101.6	107.7	111.4
Auckland	108.6	119.5	126.8
Waikato	98.0	113.0	116.0
Bay of Plenty	103.2	114.0	119.0
Gisborne/Hawke's Bay	106.6	108.5	104.8
Taranaki/Manawatu-Wanganui	109.5	108.2	119.0
Wellington	102.5	118.6	122.6
Nelson-Marlborough/West Coast	105.0	107.7	111.2
Canterbury	109.7	118.0	114.7
Otago	104.6	104.4	114.3
Southland	104.0	103.0	114.6

By age, the rise in confidence was more pronounced among those aged 30 or over, and for those in the middle to upper socio-economic groups. By gender, males (120.1) remain more optimistic than females (114.1).

The financial impact of tax and benefit changes

In the June survey we repeated the additional question we asked last quarter regarding the expected impact of upcoming changes to the tax and benefit system – the difference this quarter being that the tax changes have now been formally announced in Budget 2010.

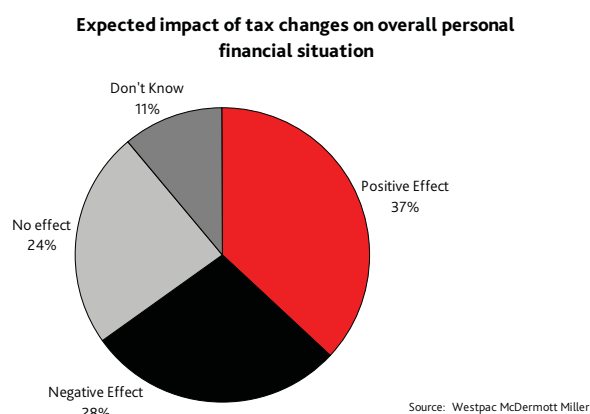
Overall, consumers appear to have been pleasantly surprised by the changes, with the results revealing that 37% of respondents now expect a positive effect (up from 33% in March), 28% expect a negative effect (from 34%), while 24% say they expected no effect (from 22%).

Not surprisingly, respondents in the upper socio-economic category are the most upbeat about the tax changes, with 42% saying they expect the changes to be positive (up from 34% in March), and just 25% expecting them to be negative (down from 32%). The lower socio-economic group remained pessimistic, albeit to a lesser extent than in March, suggesting that the announced changes were not as bad as they has

anticipated. By contrast, the middle socio-economic group appears to be the most disappointed with the tax changes. Just 23% of respondents say they think the changes will be positive. That compares with 32% in the March survey, and 28% in the lower socio-economic group. Still, we note that although fewer in the middle socio-economic group believe the change will be positive, fewer also believe they will be negative with the balance largely falling into the 'no effect' or 'don't know' categories.

By age, people aged 50 or over were still more pessimistic than younger folk about the financial impact of tax and benefit changes, albeit much less so than in the March quarter.

The age and income split from the survey matches our assessment of how the tax changes are likely to affect different groups. Lower income tax is a clear benefit to most people, but more so for high income earners. And our assessment is that the tax changes will temper the rate of house price inflation, which is a boon to the young and a detriment to the old.



Implications

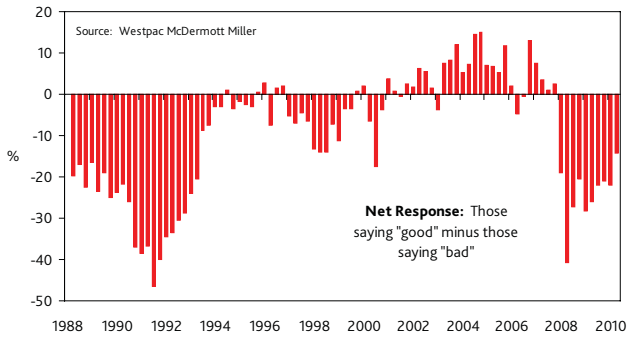
We expect the RBNZ to be somewhat surprised by the strength of today's result. In the June *Monetary Policy Statement (MPS)* the RBNZ stated that they expect the household sector to undertake a period of consolidation, with annual growth in real consumer spending slowing over their forecast horizon. The RBNZ has made a clear assumption that a behavioural shift (away from spending and toward saving) is occurring in the household sector, and will prove reasonably long lasting. Thus, at face value, today's survey results present a clear risk to that view: at current levels, confidence implies stronger spending growth than the RBNZ forecast in the June *MPS*.

That said, at least part of the improvement in confidence this quarter can be put down to upcoming changes in tax policy. That makes it difficult to accurately interpret the implications for monetary policy. Nevertheless, we take heart from the fact that the increase in confidence was reasonably broad-based, with all of the component questions improving or remaining broadly unchanged.

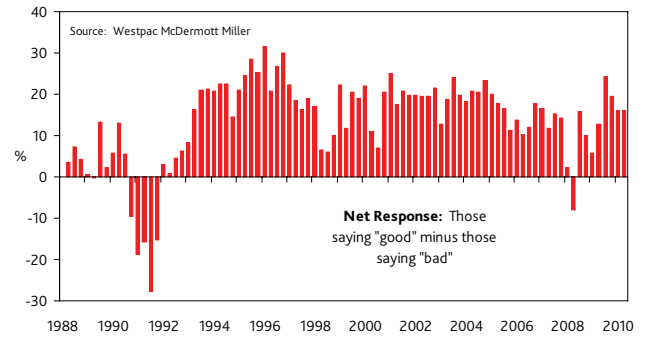
Brendan O'Donovan, Chief Economist, Ph: (64-4) 470 8250

Donna Purdue, Senior Economist, Ph: (64-4) 381 1407

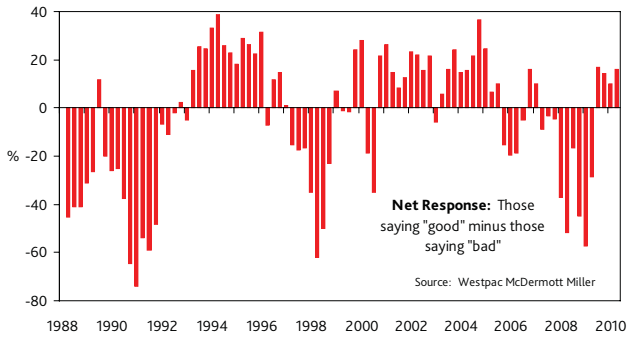
Are you better or worse off financially now than a year ago?



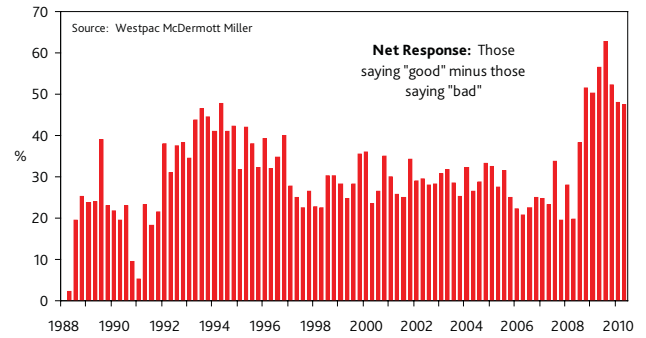
Do you expect to be better or worse off financially this time next year?



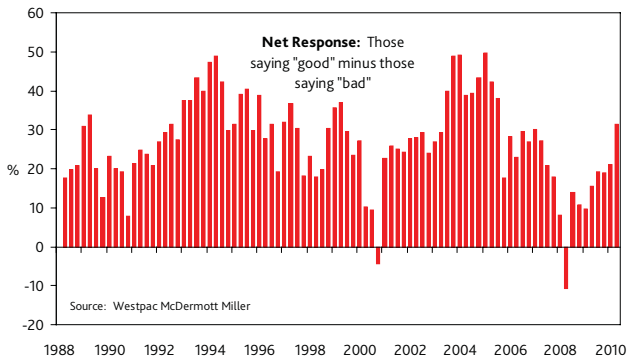
Do you expect good or bad economic times over the next 12 months in NZ?



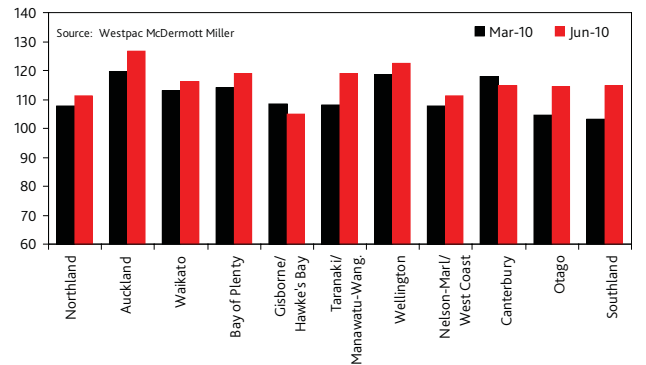
Do you expect good or bad economic times over the next 5 years in NZ?



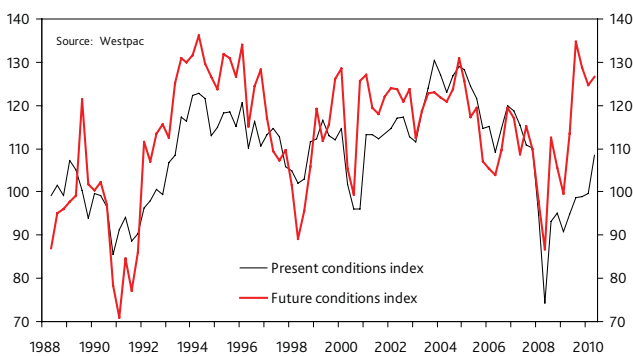
Is this a good or bad time to buy a major household item?



Regional Confidence



Present and Future Conditions Index



Consumer Confidence Data

Quarter	Index
Mar-08	96.5
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