



The global economy and the Fiji dollar

David de Garis
Senior Treasury Economist

Fiji, February 2005

*economics@***ANZ**

Today's talk

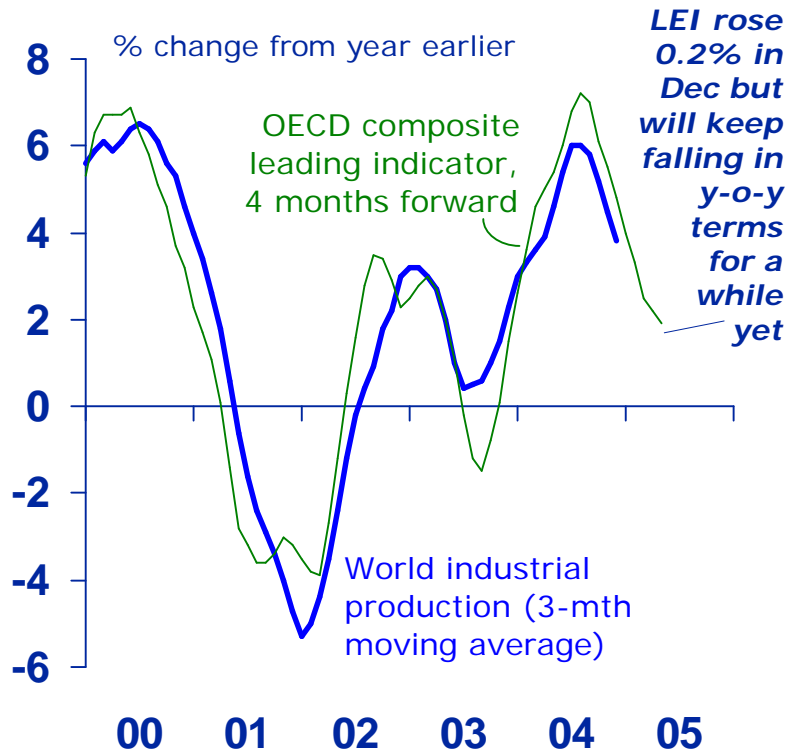
- The global economy
- Outlook for major currencies and interest rates
- Australia and New Zealand: two Fiji major trading partners
- Outlook for the Fiji dollar

Today's talk

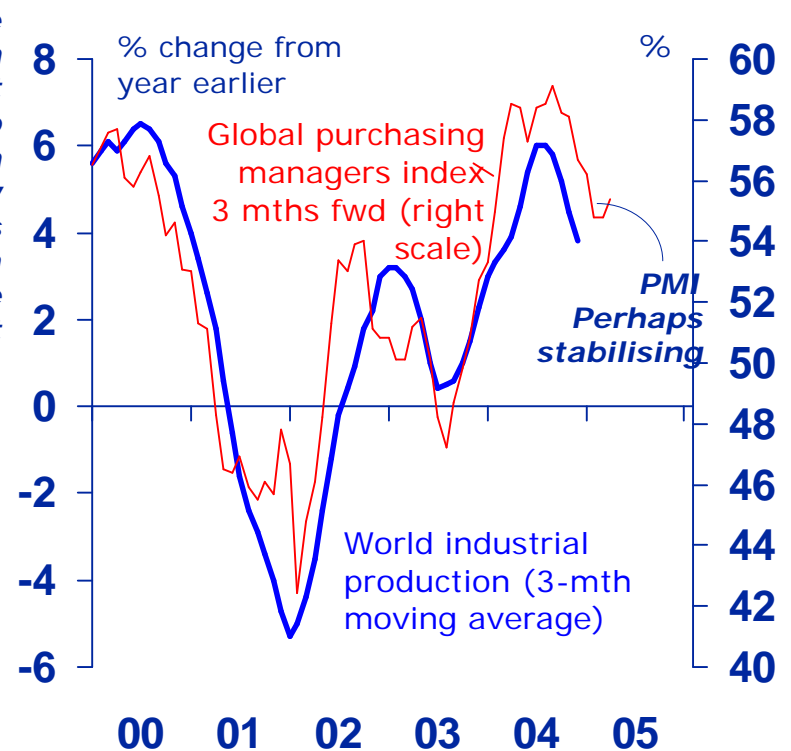
- The global economy
- Outlook for major currencies and interest rates
- Australia and New Zealand: two Fiji major trading partners
- Outlook for the Fiji dollar

Global growth peaked in Q3 2004

World IP and the OECD leading indicator



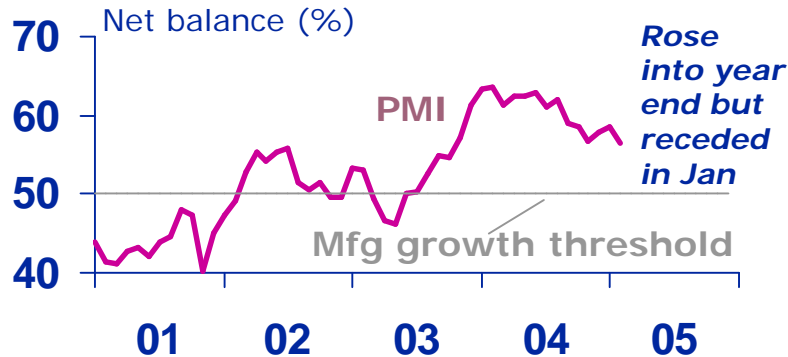
World IP and purchasing manager sentiment



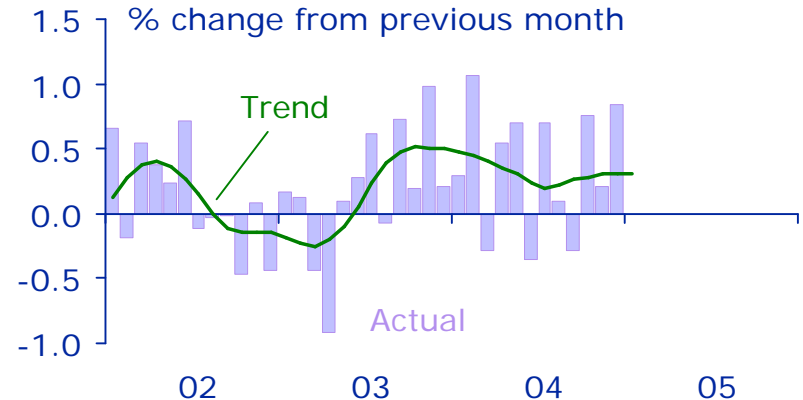
Note: 'IP' is industrial production. The global PMI is constructed from PMIs for the US, Euro area, Japan, UK, Canada, Australia, HK & Singapore. Sources: OECD; Datastream; Economics@ANZ.

The US economy ended 2004 with reasonable growth momentum

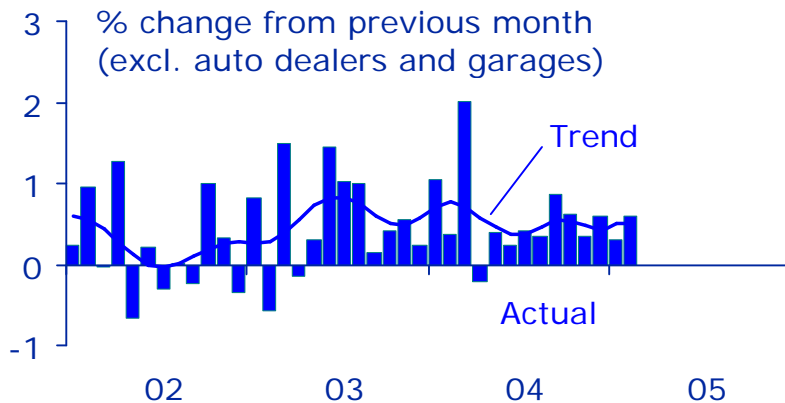
Purchasing managers' (ISM) index



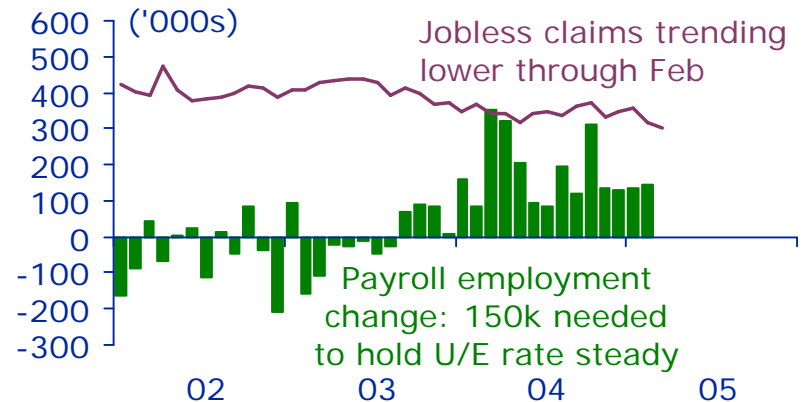
Industrial production



Retail sales



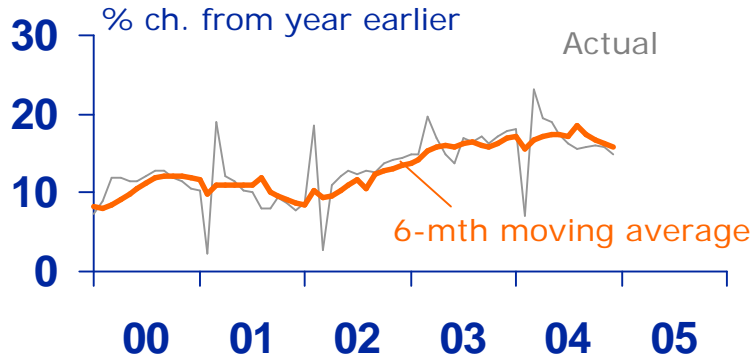
Non-farm employment



Sources: Institute of Supply Management; US Commerce Department; Federal Reserve; Bureau of Labor Statistics.

China's economy has slowed a bit, and lower inflation removes some pressure for higher rates

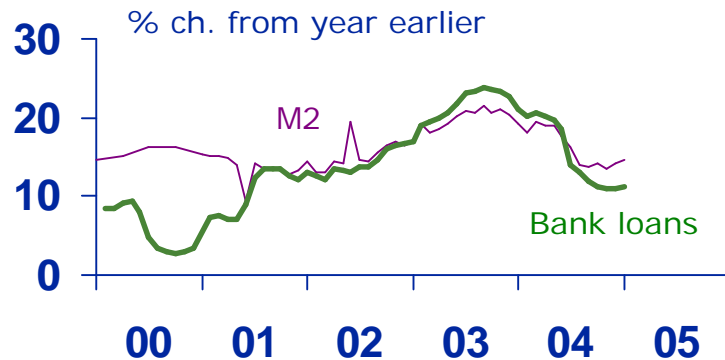
Industrial production



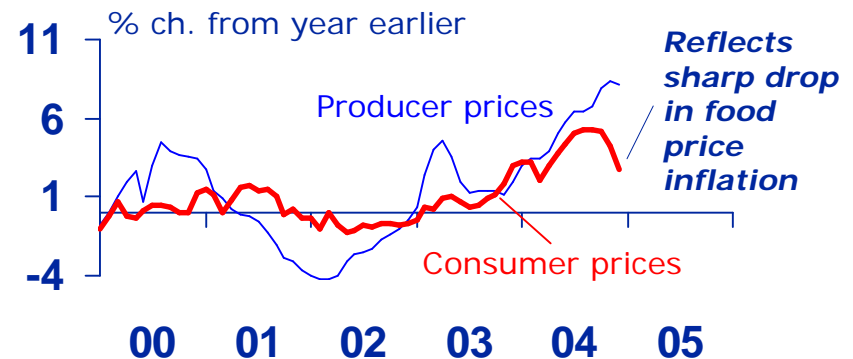
Retail sales



Money supply and bank lending



Producer and consumer prices



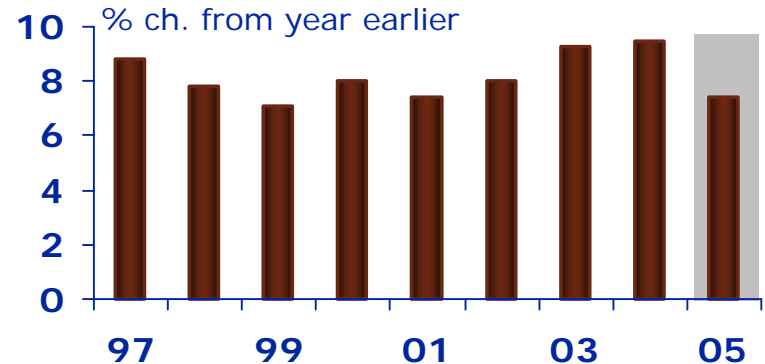
Sources: China National Statistics Bureau;
People's Bank of China.

Global growth outlook – more uncertainty than a year ago

United States: the mainstay



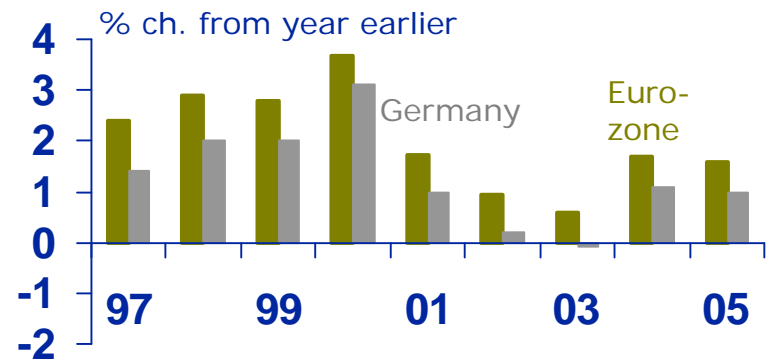
China the powerhouse: slowing not stopping!



Japan: structural improvement?

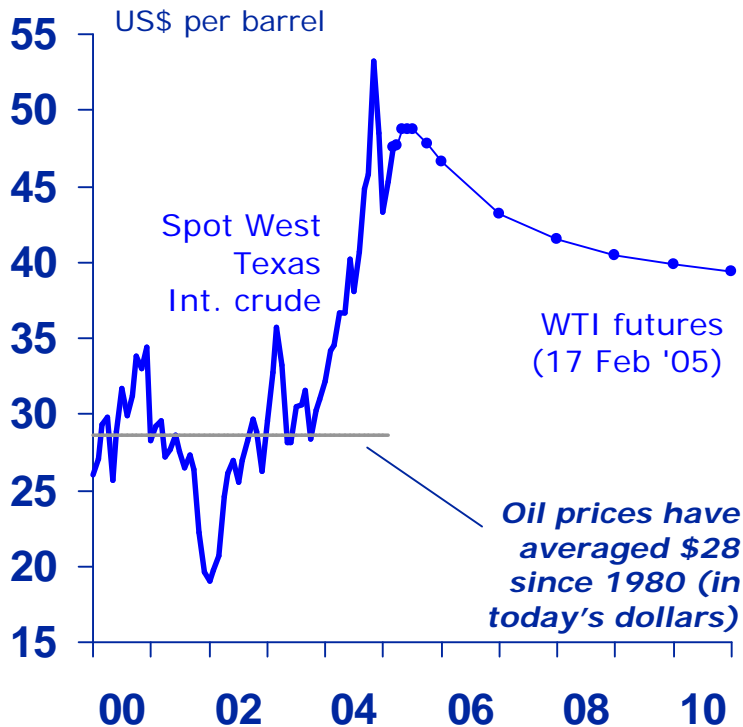


Europe: lagging



Oil prices and surrounding geopolitics remains a “thorn in the side” of the global economy

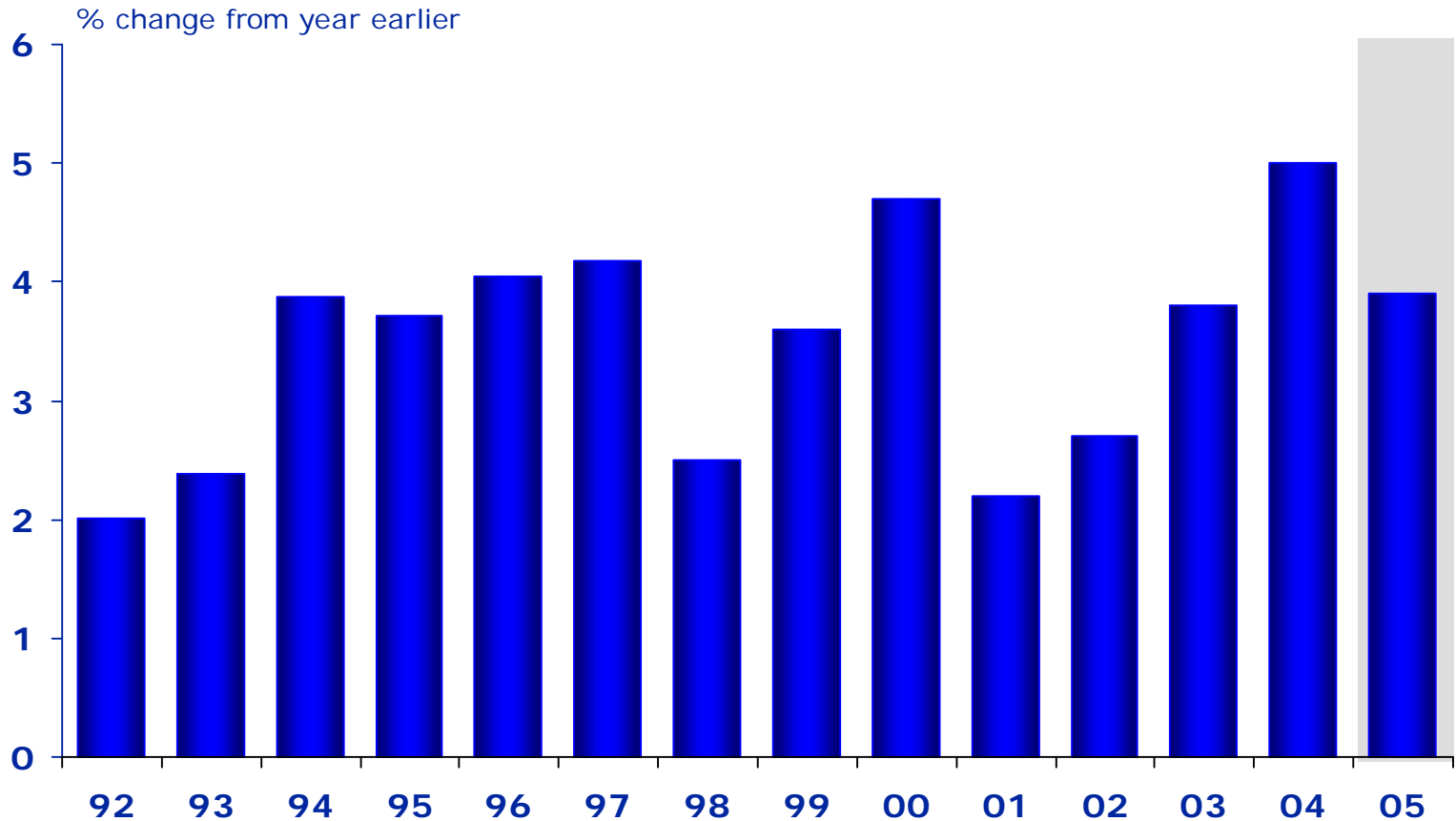
Crude oil prices



- ANZ expects oil to average \$45 this year
 - which would encompass some pull-back
 - OPEC is now defending \$40 as a base
- Politics and oil are an ugly mix
 - Iraq, the Middle East and political instability in some oil producing economies is keeping the market on edge
 - OPEC is meeting demand which is holding up. OPEC is closer to capacity limits but supply disruption cannot be ignored
 - the \$9 average rise in oil prices this year has already cut 0.5% off world growth this year

Last year started strongly but then growth eased

World growth outlook



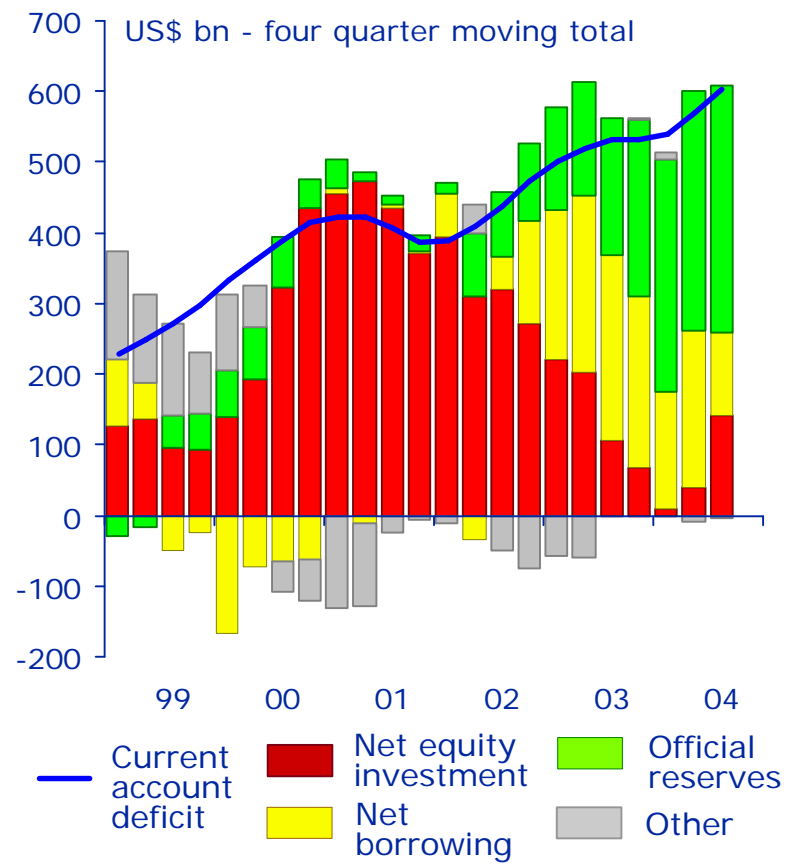
Sources: OECD; IMF; Economics@ANZ.

Today's talk

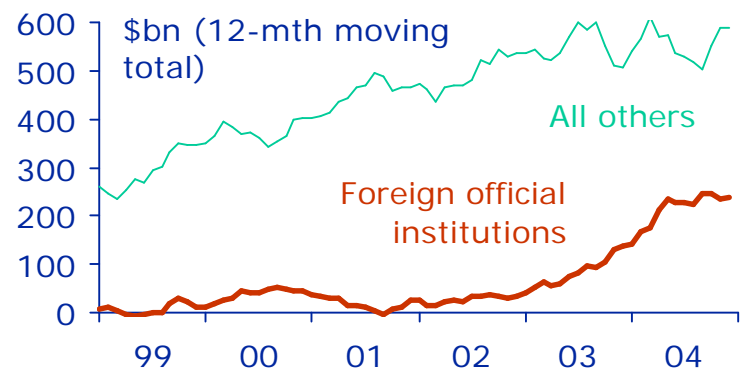
- The global economy
- Outlook for major currencies and interest rates
- Australia and New Zealand: two Fiji major trading partners
- Outlook for the Fiji dollar

The number one currency market issue: the US current account deficit

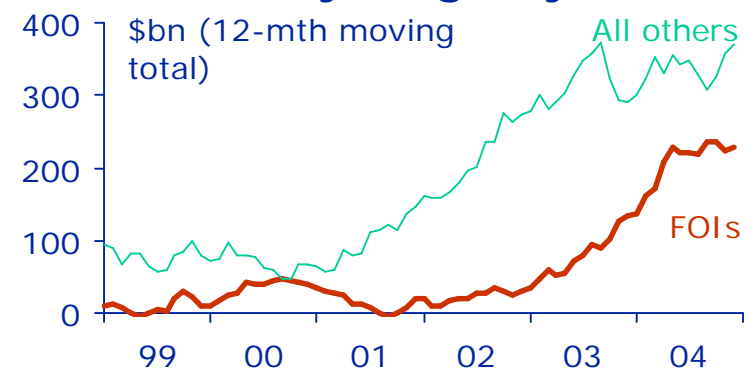
US current account deficit and its financing



Net foreign purchases of US bonds and stocks



Net foreign purchases of Treasury & agency bonds

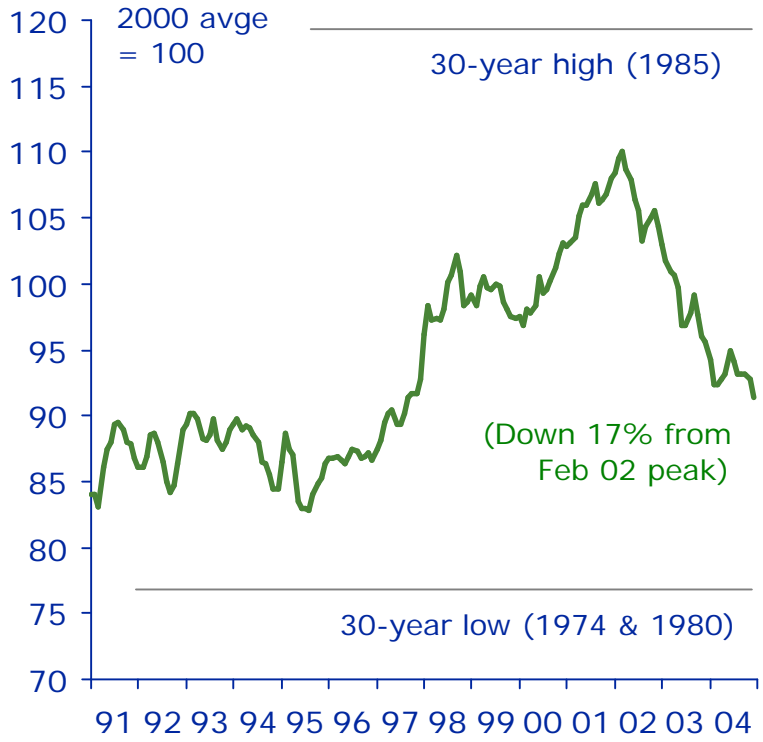


Note: 'equity investment' includes corporate bonds.
 Sources: US Bureau of Economic Analysis; Department of the Treasury.

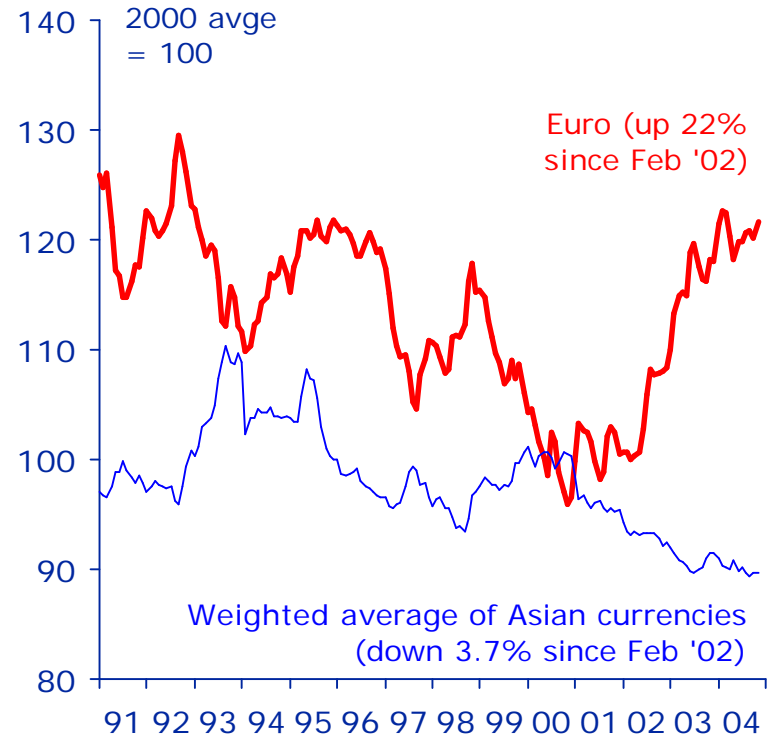
The US dollar has already fallen significantly, if unevenly

Real effective exchange rates

US dollar



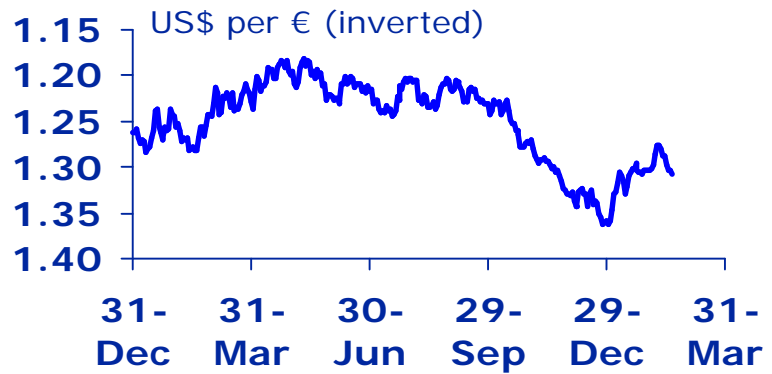
Other currencies



Sources: JP Morgan; Economics@ANZ. Asian currencies are JPY, CNY, KRW, TWD, HKD, THB, MYR, SGD, IDR, PHP and INR, weighted by 2002 GDP at market exchange rates.

The US\$ has had a mixed opening against 'major floating currencies' so far in 2005 ...

EUR/USD



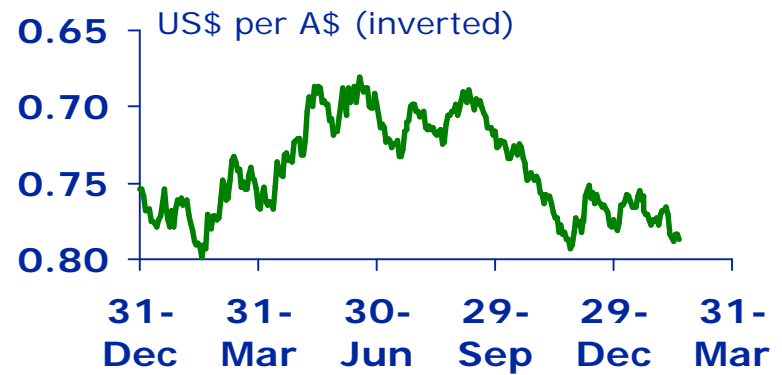
USD/JPY



GBP/USD



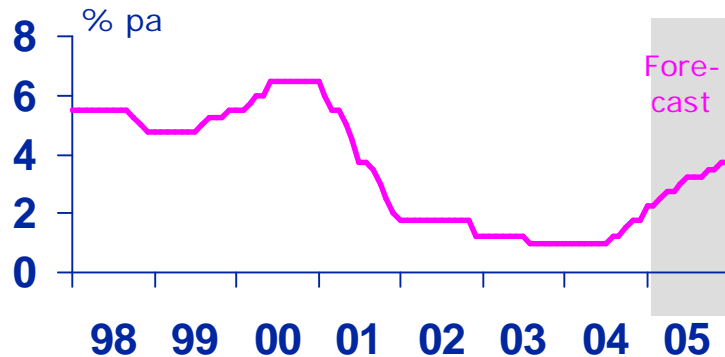
AUD/USD



Note: charts show daily data from 31 Dec 2003 onwards.
Source: Reuters.

The Federal Reserve will keep nudging rates to "neutral" ($= > 3\%$) but on a "measured" basis

US fed funds rate



- **Chairman Greenspan's Feb '05 semi-annual testimony**
 - the economy has entered 2005 at a reasonably good pace
 - Inflation is low even with "accommodative" monetary policy
- **Inflation not (yet?) a threshold policy driver for the Federal Reserve**
 - No doubt there are upstream commodity price pressures from oil, metals etc
 - And a lower US\$ could have produced more consumer inflation
 - The Fed expects 1.5-1.75% for PCE inflation over 2005

The Fed's preferred inflation measure



Sources: US Federal Reserve; Datastream.

Outlook for the US\$

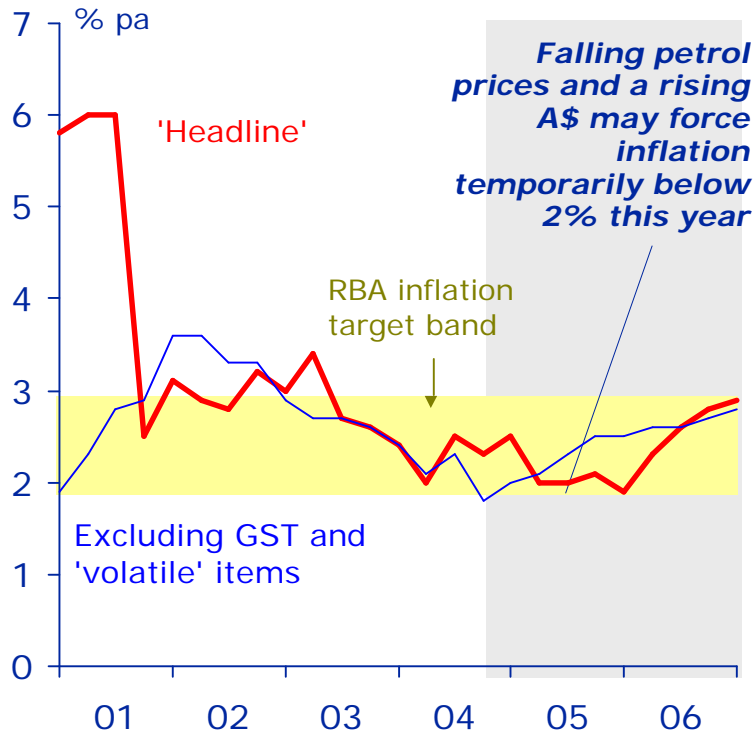
- No doubt, the US economy, after China remains the global economy's major growth spur and probably destination of choice
- The US budget deficit has appeared on the US Administration's radar with promises to halve the deficit by 2009 and accelerate economic and social security reforms
- US interest rates are becoming attractive (2.5% cf ECB 2%; Japan 0%; UK 4.75%; Australia 5.25%; NZ 6.5%)
- We would not rule out one last phase of US\$ decline, but we are approaching the end game of its demise; if it does decline further, a EUR/USD of 1.35-1.40 would likely be the Euro's peak; USD/JPY of 100-103 and up to 2 for the GBP

Today's talk

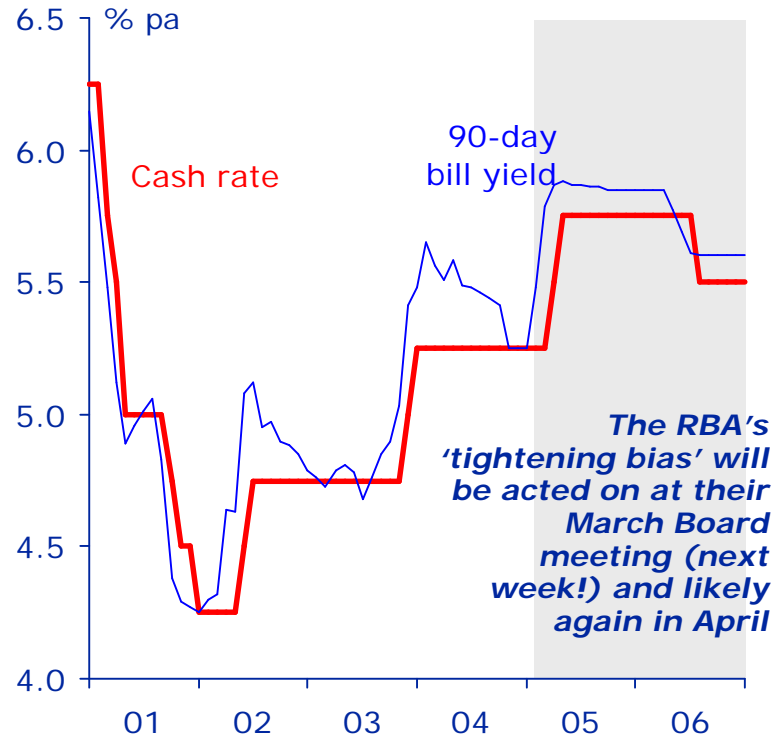
- The global economy
- Outlook for major currencies and interest rates
- **Australia and New Zealand: two Fiji major trading partners**
- Outlook for the Fiji dollar

The RBA has recently signalled that rates could rise over the next few months

Inflation



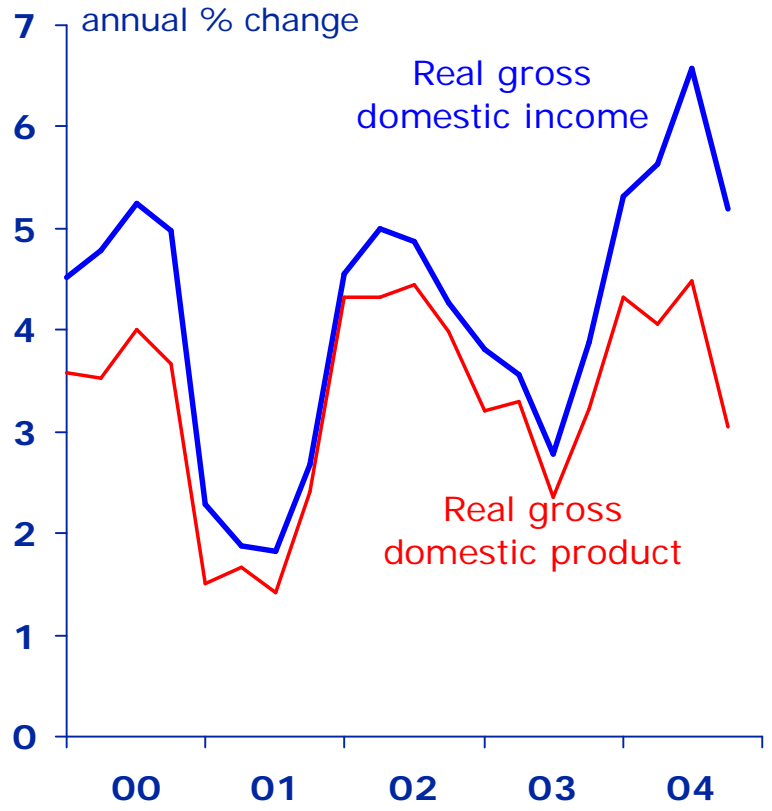
Interest rates



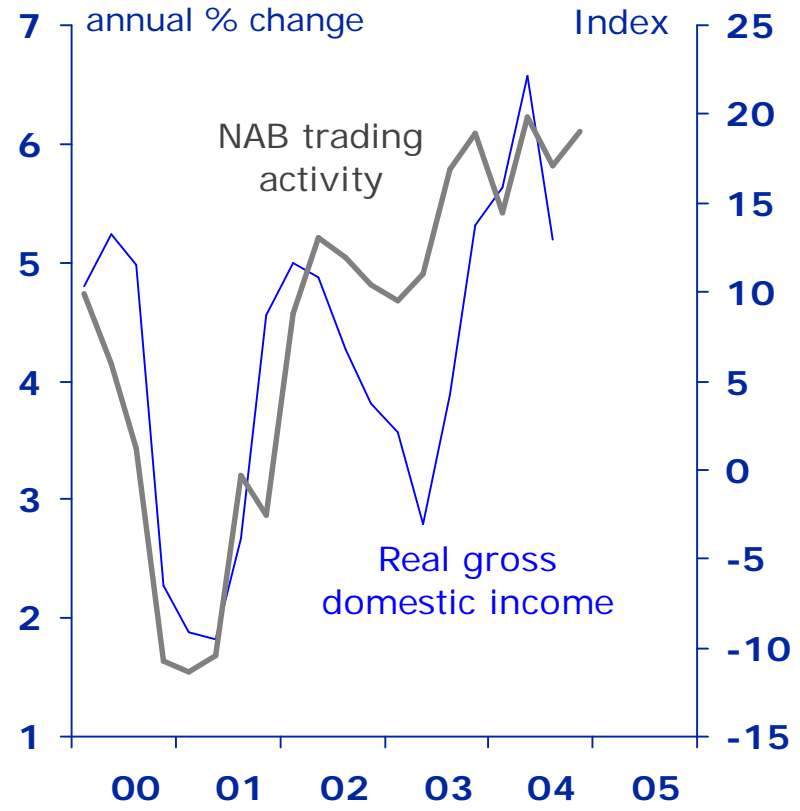
Sources: ABS; RBA; Economics@ANZ.

The RBA thinks the Australian economy is stronger than official figures

Economic growth



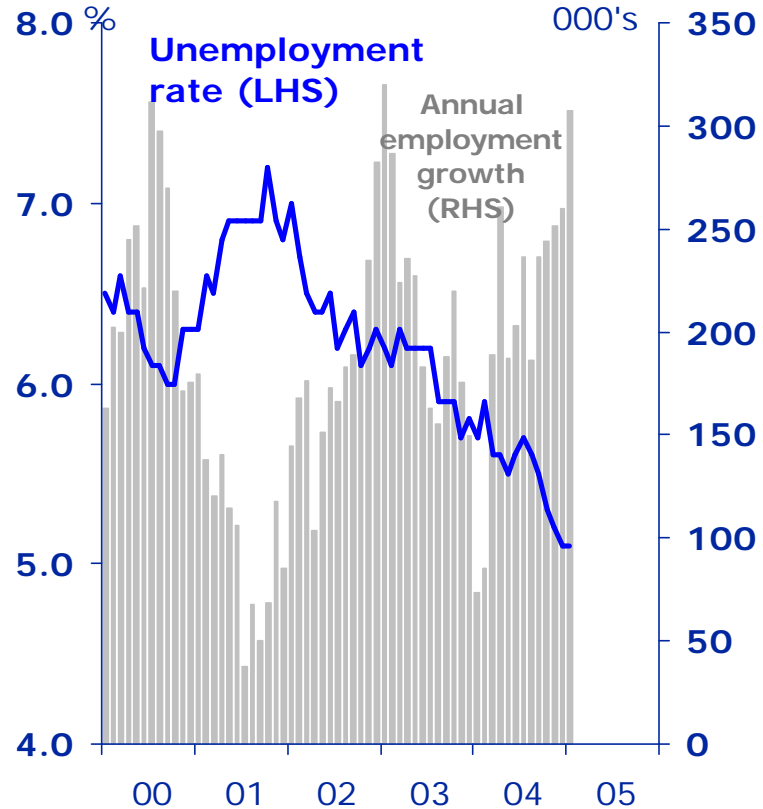
Growth and NAB survey



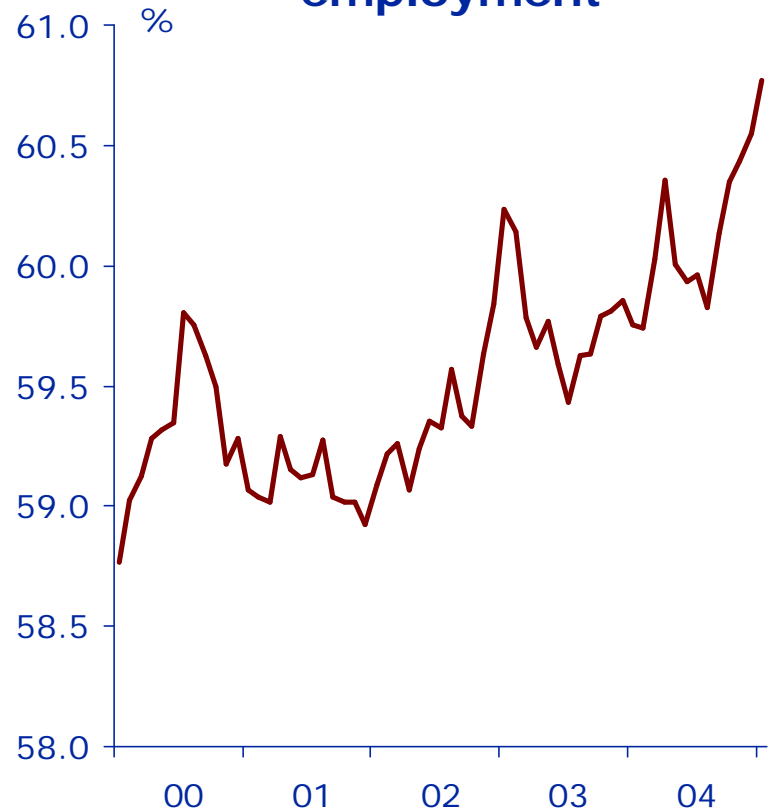
Sources: ABS; NAB

The labour market is very strong, with many businesses reporting acute skills shortages

Employment



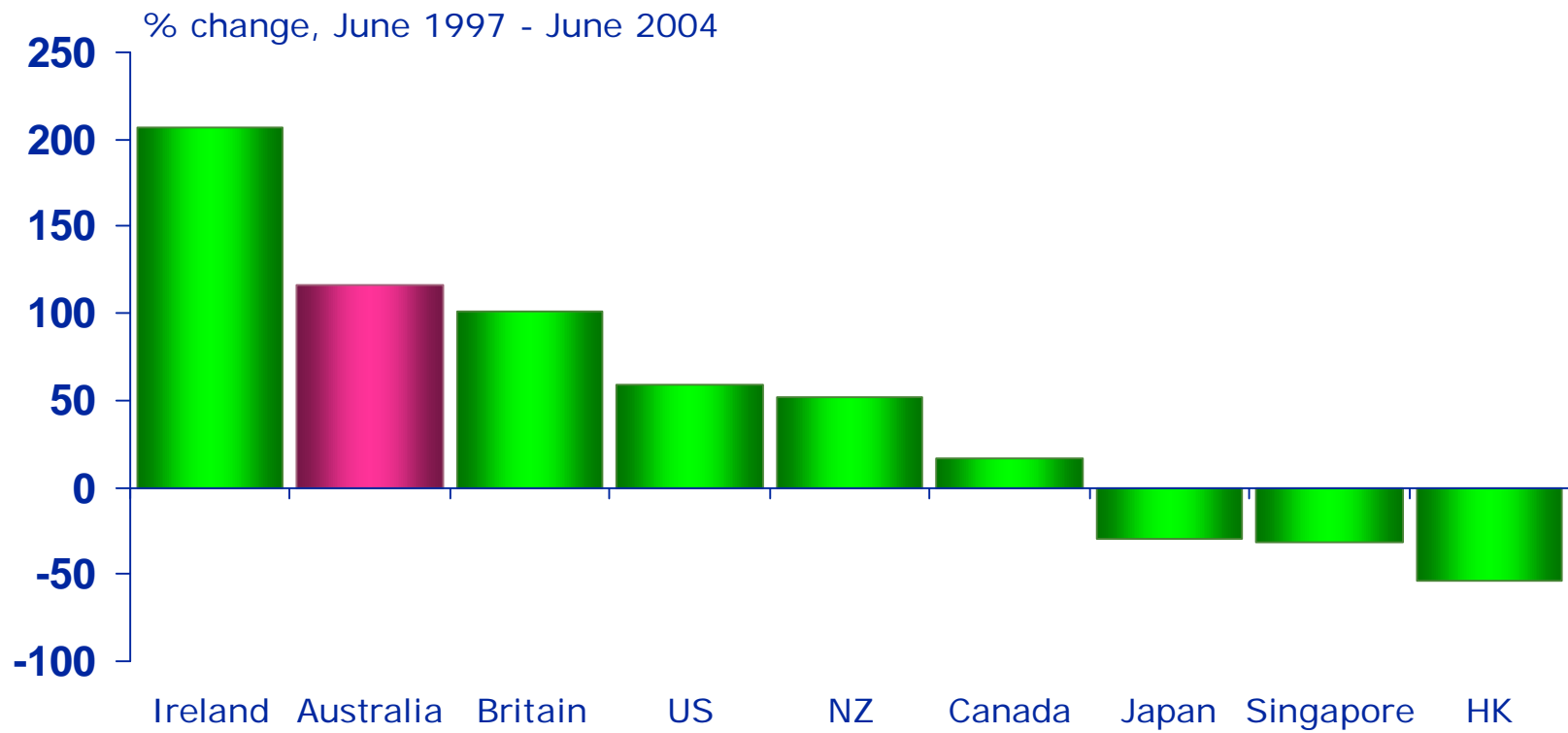
Proportion of population in employment



Sources: ABS

Australian house prices rose faster than almost anywhere else in the world from 1997 to 2004

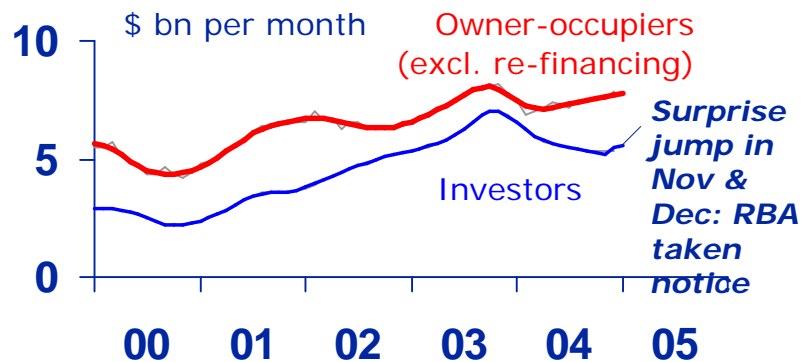
Increases in house prices selected Anglo-Saxon and Asian economies



Sources: national statistical agencies and real estate institutes; Datastream; Economics@ANZ

Housing sector leading indicators stabilising

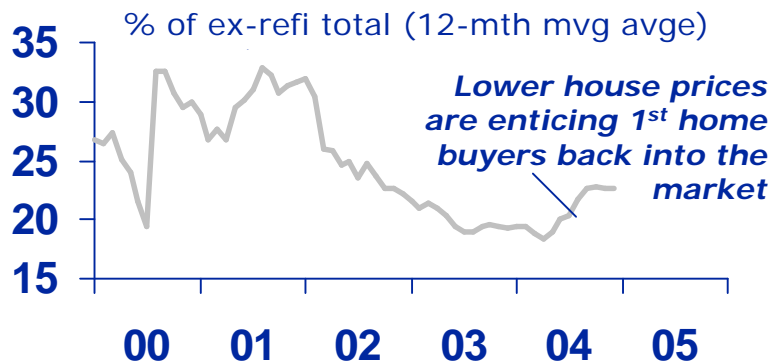
Housing finance commitments



Residential building approvals



1st home buyer finance



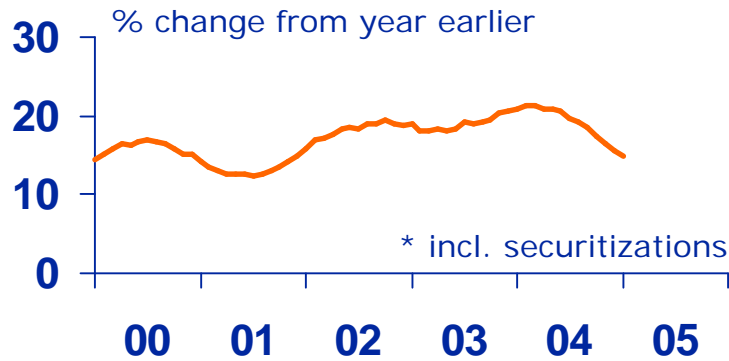
Home-buying sentiment



Sources: ABS; Westpac/Melbourne Institute; Economics@ANZ.

Financial intermediaries' lending growth showing signs of stabilising

Housing credit*



Business credit



Other personal credit



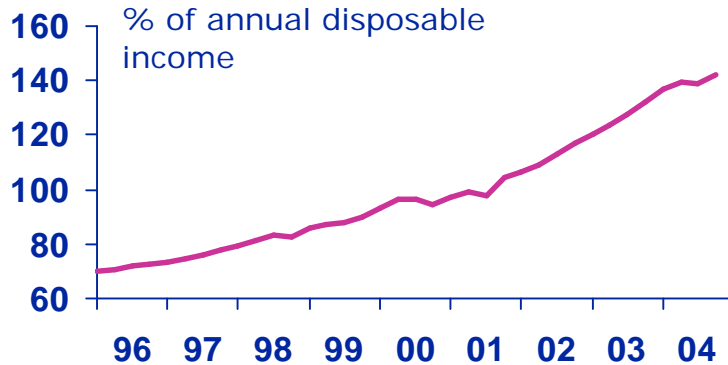
Total credit



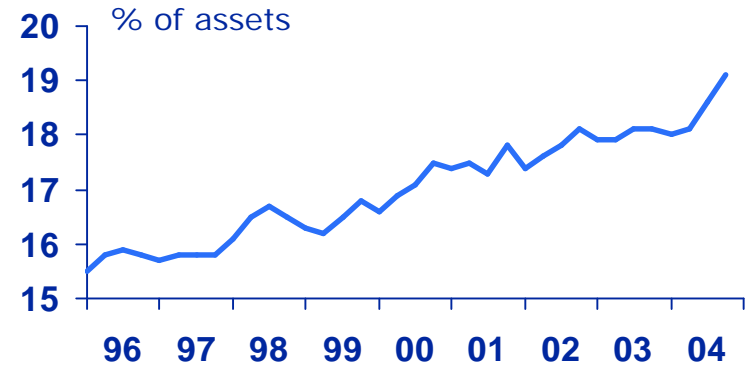
Source: Reserve Bank of Australia

Household debt and debt servicing are being closely watched by the RBA

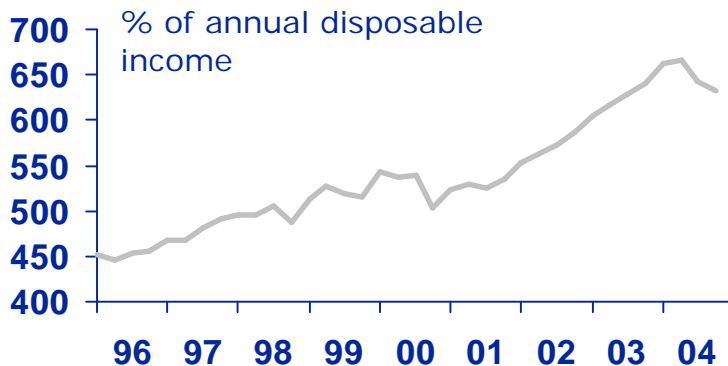
Household debt to income



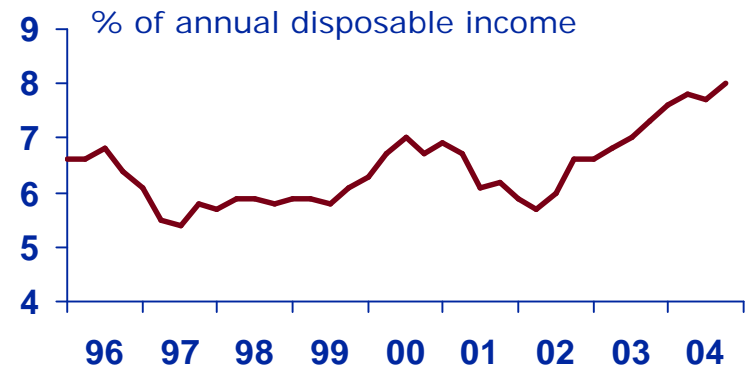
Household debt to assets



Household net worth to income



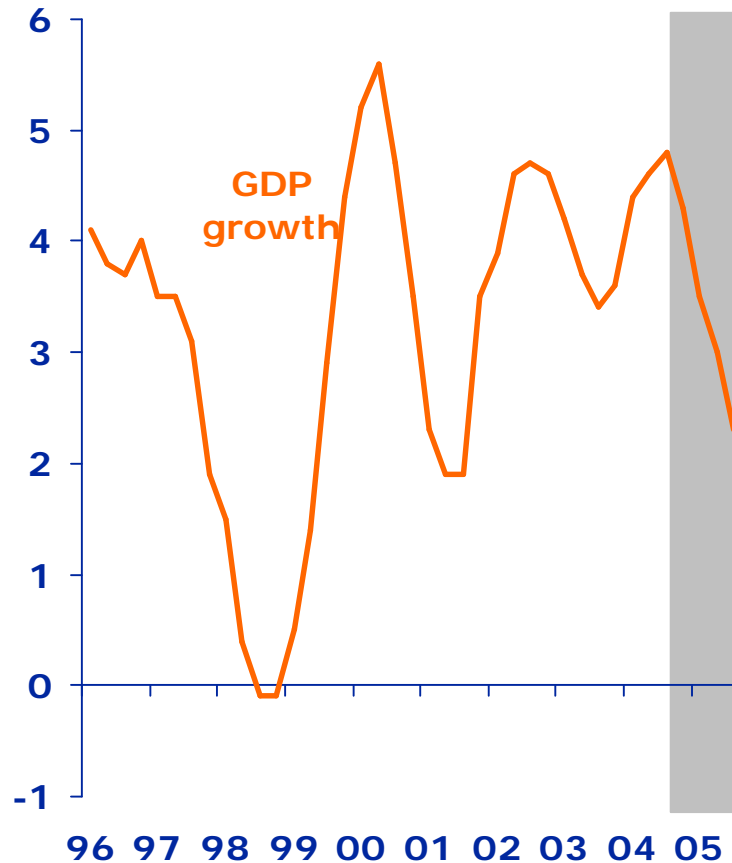
Household interest paid to income



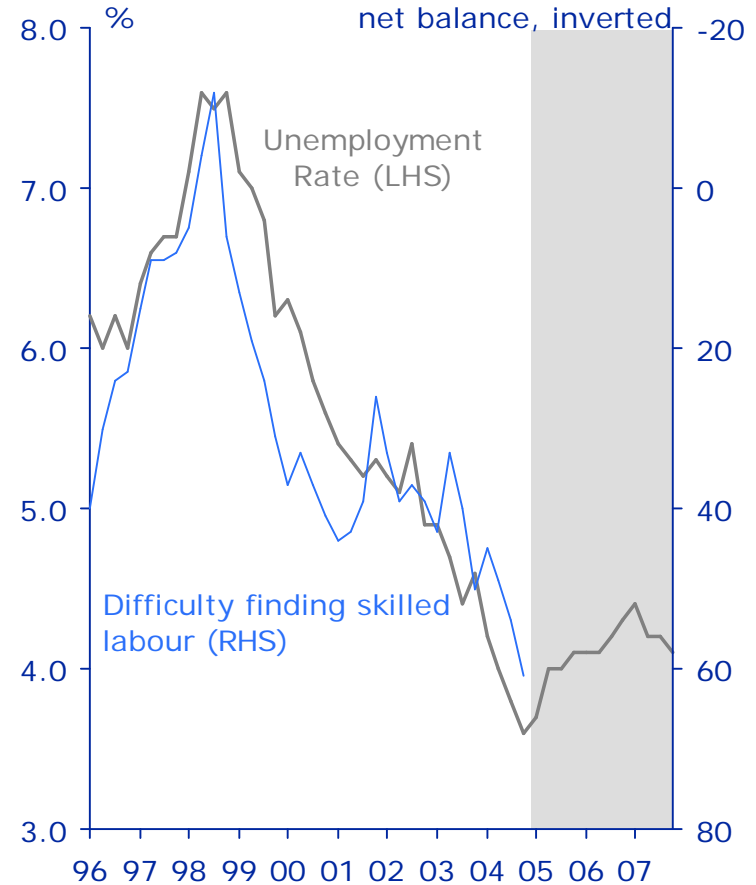
Sources: Reserve Bank of Australia; ABS;
Economics@ANZ estimates.

NZ economy: slowdown still not arriving!

Economic growth



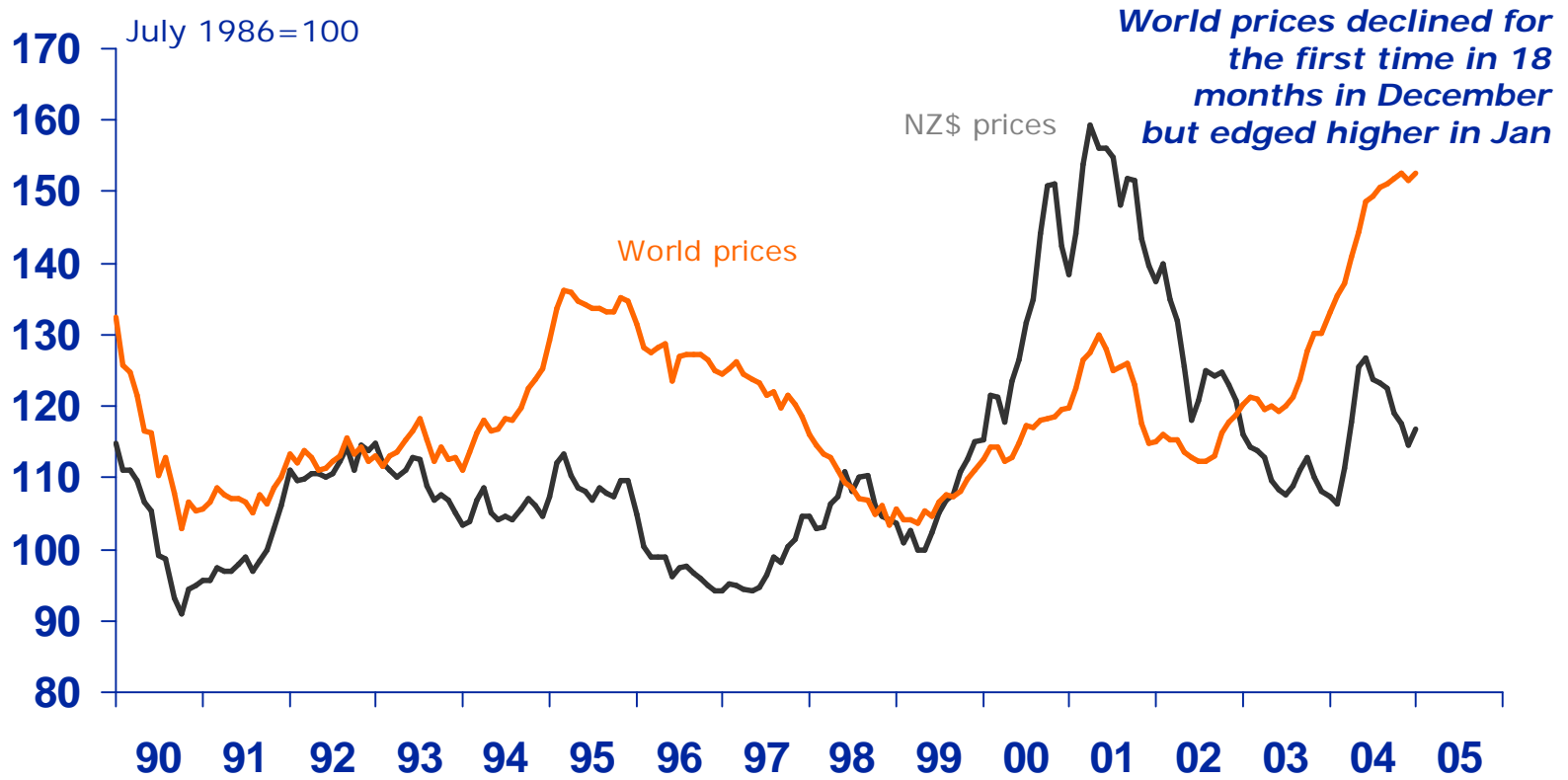
Unemployment rate and demand for skilled labour



Sources: ANZ National Bank, Statistics NZ

World commodity prices for NZ's key commodity exports still strong

ANZ commodity price index

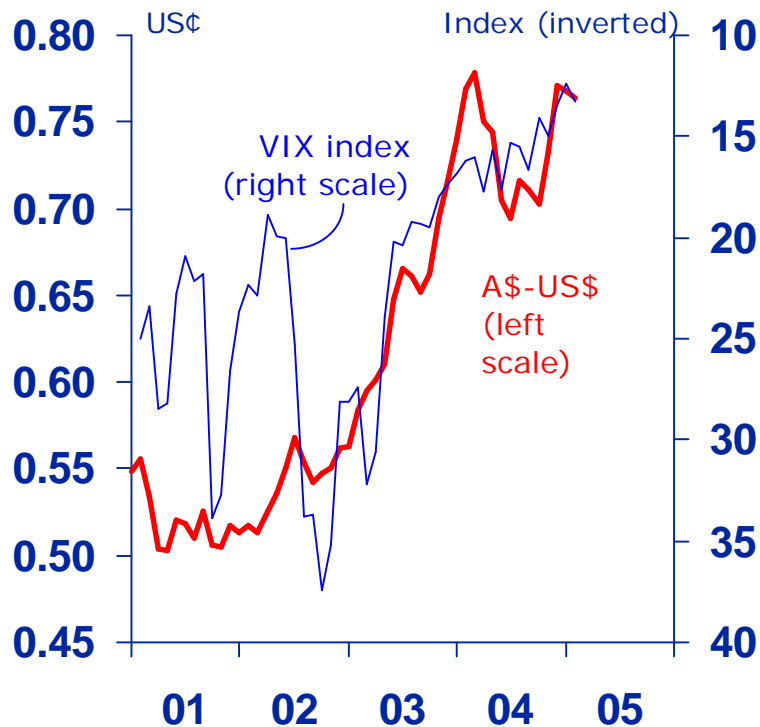


Sources: ANZ National Bank

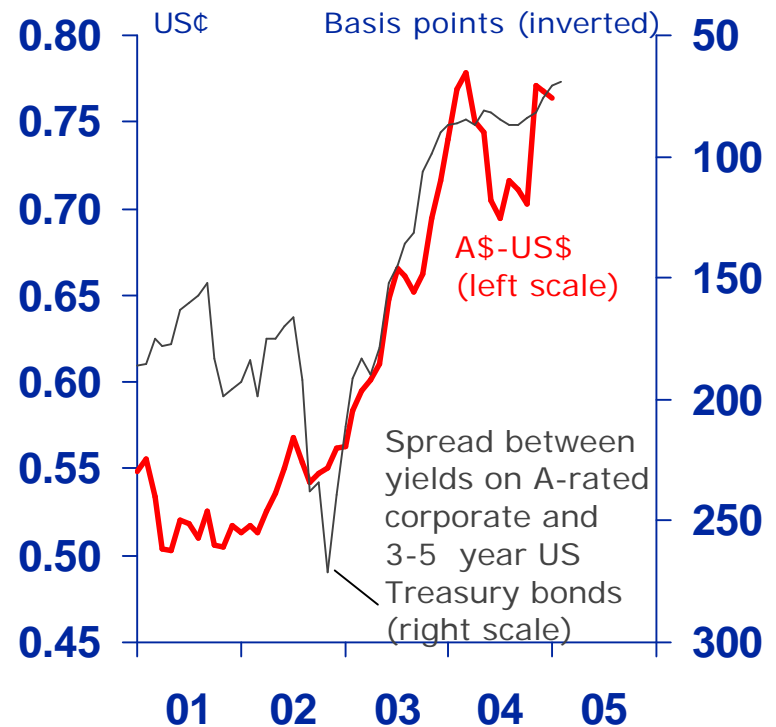
Any increase in 'risk aversion' on the part of global investors would also weaken the A\$

Measures of investor risk aversion and the A\$

Equity market volatility



Credit market spreads

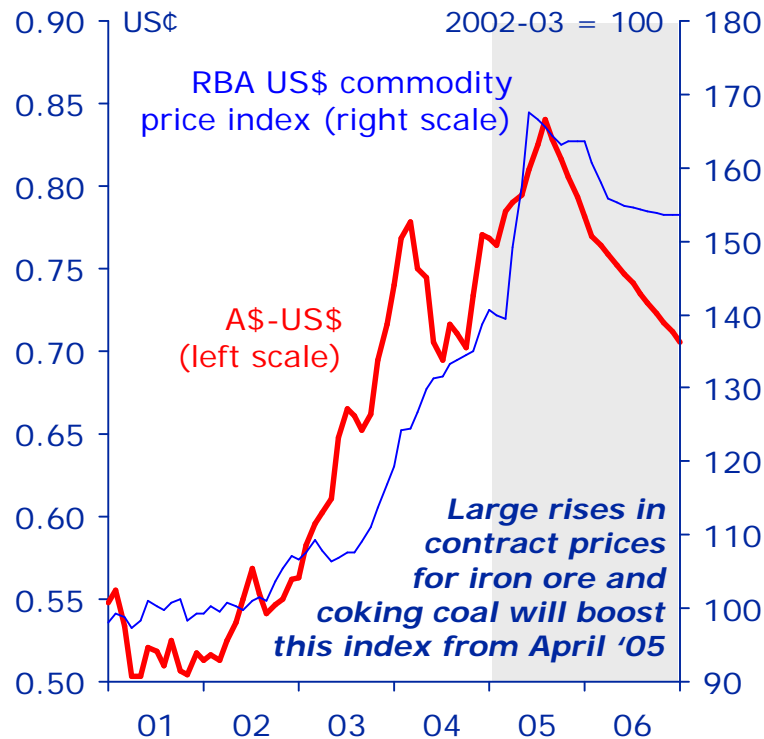


Note: The VIX index is a measure of US stock market volatility based on prices of options on S&P500 futures.
Sources: Datastream; Economics@ANZ.

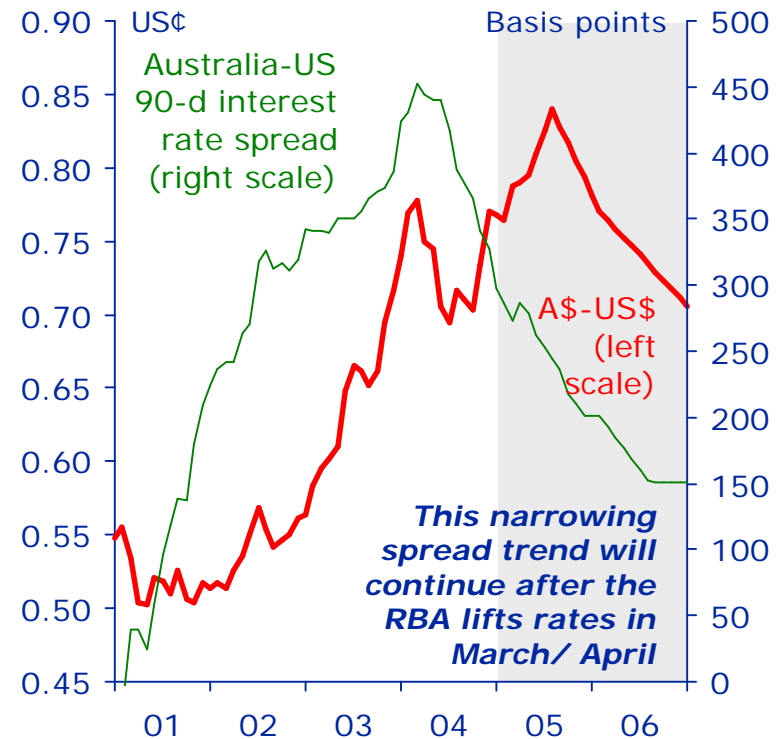
Slower world growth and a narrowing rate spread to cap the A\$'s rise

Traditional 'fundamentals' and the A\$

Commodity prices



Interest rate spreads



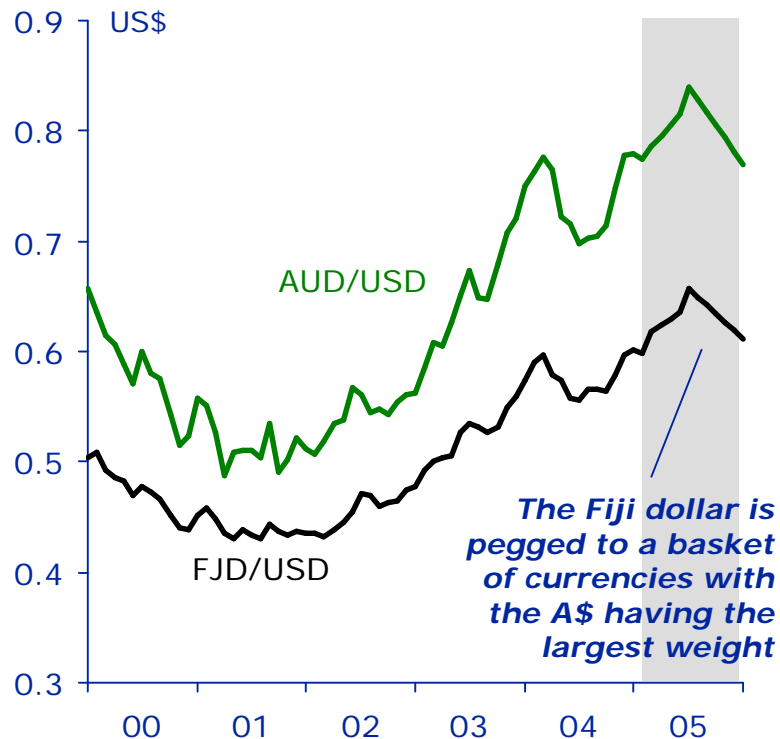
Sources: Datastream; Economics@ANZ.

Today's talk

- The global economy
- Outlook for major currencies and interest rates
- Australia and New Zealand: two Fiji major trading partners
- Outlook for the Fiji dollar

Outlook for the Fiji dollar (FJD)

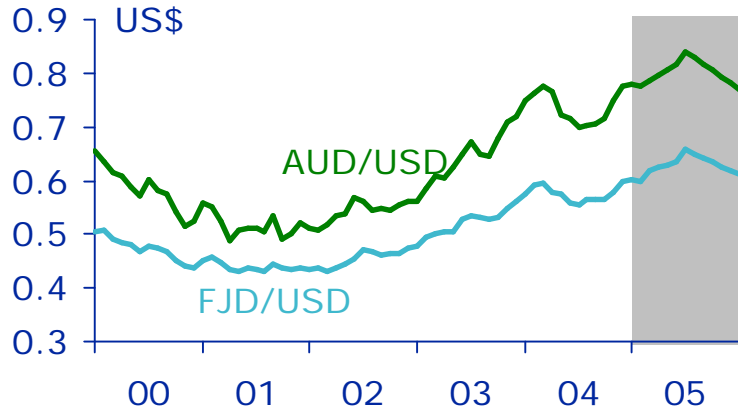
Exchange rates: AUD & FJD



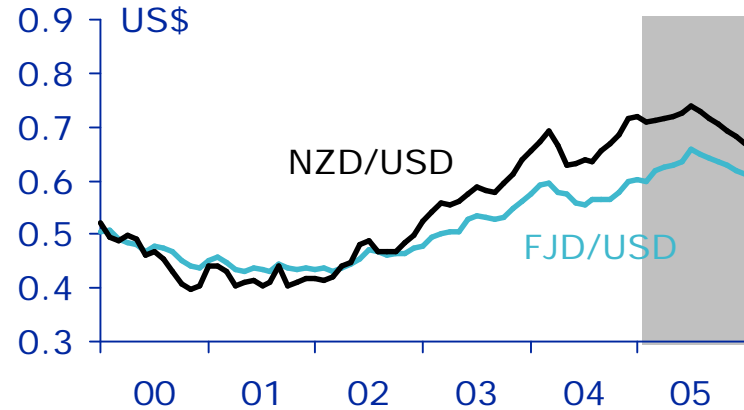
- **ANZ expectation of the A\$/US\$ breaching 0.80 in this half is coming to pass**
 - In part from a soft US\$, but now:
 - Expectations of A\$ rate rises and booming commodity prices also large A\$ positives
- **The Fiji dollar is pegged to a basket of currencies with the A\$/US\$ the main key**
 - assuming a broadly unchanged FJD “effective” trade-weighted rate, on the above forecasts the FJD/USD could reach a peak of 0.65-0.66 by mid year
 - With the FJD/AUD easing from 0.77 to 0.75 by mid year as the A\$ peak ...
 - ... before FJD/AUD recovering as the A\$ falls later in 2005

Fiji dollar cross rates

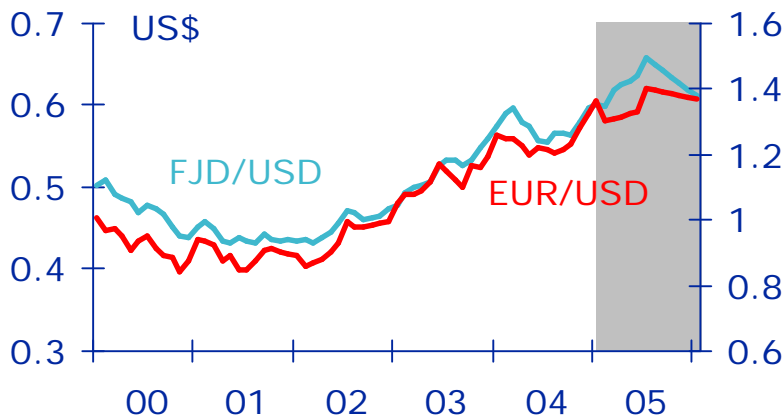
FJ\$ vs A\$



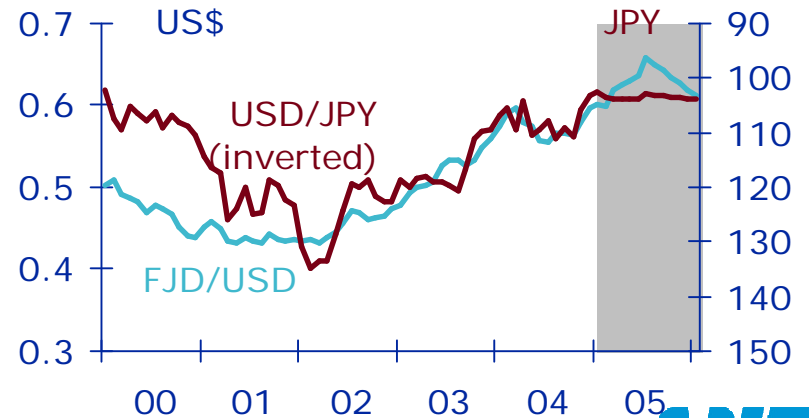
FJ\$ vs NZ\$



FJ\$ vs EUR



FJ\$ vs JPY



Key FJD-related FX rates & drivers

	Dec 2004*	Jun 2005	Dec 2005	Dec 2006
US Fed funds rate (% pa)	2.25	3.25	3.75	4.00
€ - US\$	1.36	1.40	1.37	1.26
US\$ - ¥	103	103	104	101
A\$ - US\$	0.78	0.84	0.77	0.70
RBA cash rate (% pa)	5.25	5.75	5.75	5.50
Australian 10-year bond yield (% pa)	5.33	5.50	5.30	5.10
RBNZ cash rate	6.50	6.50	6.25	6.00
FJD – US\$	0.60	0.63	0.60	0.56
FJD – A\$	0.77	0.75	0.78	0.80
FJD – NZ\$	0.84	0.85	0.89	0.94
FJD - €	0.44	0.45	0.44	0.45
FJD - ¥	61.7	65.1	62.1	55.9

* actual

Summary

- Prepare for some slowing in the global economy
 - Watch oil prices; uncertainty in Europe and Japan
- The Fed is lifting rates gradually to around 3-4%
- The US\$ has already declined significantly
 - Perhaps one “final phase” of US\$ decline but not enduring
- Australian and New Zealand economic growth will struggle
 - Two RBA rate rises are in the pipeline; maybe one from RBNZ
- Spot FJD/USD is now appreciating with the A\$; this rise could continue further (a “final US\$ decline phase”) but then follow the A\$ down
 - Under current arrangements with a managed FJD basket

The global economy and the Fiji dollar

David de Garis
Senior Treasury Economist

Fiji, February 2005