

# Wealth Management Adviser

Summer 2009

Issue 39

## Easy as she goes

Despite the bombardment of suggestions of an economic recovery in the US, look past the media hype and a different picture emerges.

Banks continue to be closed at an alarming rate, particularly those highly exposed to the weak housing and commercial real estate sectors. A second wave of residential mortgage delinquencies' is forecast for early next year as many ARM mortgages are due to start resetting, and the Governments money printing presses (quantitative easing) continue to work overtime as the US endeavours to solve a significant debt crisis with considerably more debt - increasing the amount of money the nation owes to levels never seen before.

### US banking woes continue

US regulators recently closed down nine more banks taking the total for 2009 to a staggering 124, compared to 25 in 2008 and 3 in 2007. The Federal Deposit Insurance Corporation's (FDIC) list of problem institutions grew from 305 in Q1, 2009 to 416 in Q2. This is the highest since the savings and loan crisis back in 1994.

### It didn't work for Japan so will it work for the US?

So here we have the US Government attempting to stimulate the economy, it didn't work back in 1998 for the Japanese, so what makes the US think it'll work for them now? The Japanese governments' aim was to throw enough money at the problem so that growth would return and by the year 2000 the government could achieve its fiscal deficit reduction

targets. Eleven years on, countless packages later and the news really doesn't look very different - neither do Japanese Government Bond Yields.

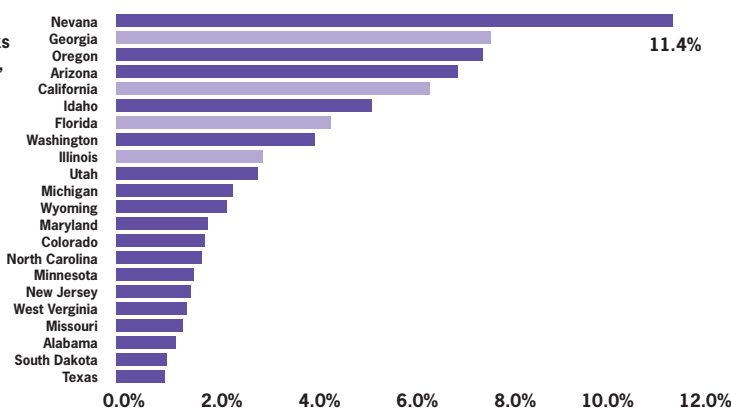
### The credit bubble bursts

Not unlike many Kiwi consumers, the US consumer has simply been living on credit far too long. Now that the credit bubble has burst, US politicians continue to print money in the hope of encouraging the US consumer to spend their way out of this crisis.

The US now has significantly more debt than just five years ago, it has the highest unemployment rate seen since the early 1980's, GDP growth has only just turned positive and corporate America is making much less money than it was two - three years ago, all of which leads to a significant reduction in tax revenue for the Government. So less tax revenue at a time when less people are earning and when there was an election pledge not to increase taxes for middle income earners. Increasing taxes for the "wealthy" may help bridge the gap for a while but it

continued overleaf...

Fig 1: US banking failures - % of banks failed in each state, 2007 till today



Source: Triple T Consulting and the FDIC

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is not a long-term solution. Wealthy people tend to have a lot of resources available to reduce tax burdens. So the effect of the Global Financial Crisis (GFC) still has some way to go in our view.

Whilst generally New Zealand lenders (predominantly banks) have used much better underwriting standards for residential loans, unemployment still has the potential to impact our rate of mortgage sales here. Fortunately most New Zealand homeowners are managing to retain their properties and some recent reports suggest that the rate of mortgage sales may have peaked; however that position could shift if people continue to lose jobs. With 2.1 million Kiwis working, our unemployment levels in New Zealand have increased to 6.5% as of Q3 2009, last seen back in Q1 2000.

### All is not lost

One of the leading indicators of global economic activity is the Baltic Dry Index, which we have spoken about before. Essentially this index is a measure of shipping freight capacity and utilisation for dry goods and commodities around the world. The index has shown a good level of pick-up in activity from its very low point almost 12 months ago, back to levels consistent with late-2003, 2004 and mid-2007.

A lot of this activity has been heading to the emerging economies and Asia. As inventories have been depleted new orders have now begun to build up again to meet the demand of the many infrastructure programmes. Asia-bound shipments of iron ore from Port Hedland have chalked up fresh records of more than 14 million tonnes in each of the past three months, according to figures published recently.

A currency strategist at Westpac, Jonathan Cavenagh, said it was clear the slump had made only a slight indent on the transformation of China and India into developed economies. "The industrialisation of India and China is still going to continue. The global financial crisis may have slowed it down a touch in 2008 ... but really it's just gone from strength to strength since then."

This bodes well for the Australian

dollar, the world's strongest-performing currency in recent months.

In another sign of the return to better times, Westpac recently reported that 77 ships were queued up outside the Queensland coal port of Dalrymple Bay, where the waiting times are at near record highs.

### And in New Zealand, migration data positive again

In a country with a population base of just 4.3 million, changes in immigration trends can have a profound effect on supply and demand imbalances, particularly in the labour and housing markets.

October immigration data saw another five year annual high, with a net yearly gain in permanent migrants of 18,560. A major influence on this number was that 15,600 fewer Kiwi's left our shores to move overseas in the past year.

Short term visitor arrivals were up 7.7% compared with the same time last year - Australians made up the majority with a 22% increase. The tourism sector is the country's second largest industry, and as such the strength of the Australian economy has some direct lower beta impact upon New Zealand.

The ever reducing opportunities in the UK and Europe have had a positive impact on New Zealand. Our migration numbers are evidencing a return of offshore Kiwi's and continuing migrant growth from Asia. This is having the dual effect of boosting demand for housing (both rental and sub \$1million buying), and weakening the hand of the average worker in wage negotiations.

Expectations are that this situation will not necessarily be long lasting, but for now it is giving the RBNZ comfort that labour shortages will not spark a break out in inflation. Given the strength of the Australian economy and the huge development projects being unleashed in W.A. the Kiwi labour pool will undoubtedly be tapped by Australian employers as their economy continues to expand in 2010/11.

### Where to for the Kiwi investor?

For the Kiwi investor looking for portfolio growth at better than bank deposit rates, we continue to recommend

good diversification and exposure to both Australasian and International equity markets - the last eight months have produced strong returns. From an Australasian point of view our preference continues to be weighted in favour of Australia. Internationally we remain biased towards the developing economies versus the developed economies, a view we have had for most of this year. New positions taken in early 2009 in economies such as Brazil, Russia, India and China (BRIC) have performed very well against those in the more traditional economies, despite the strength of the kiwi dollar.



A disclosure statement is available on request, free of charge. If you require further information on any of these topics please contact:

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