MOODY'S
INVESTORS SERVICE

CREDIT ANALYSIS

New Zealand

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New Zealand

	FOREIGN CURRENCY	LOCAL CURRENCY
Government Bond Rating	Aaa-Stable	Aaa-Stable
Country Ceiling	Aaa-Stable	Aaa
Bank Deposit Ceiling	Aaa-Stable	Aaa

Moody's sovereign rating list

Rating Rationale and Outlook

New Zealand's Aaa ratings are based on the country's high economic strength, very high institutional and government financial strength, and very low susceptibility to event risk. New Zealand's flexible and market-oriented economic policies have supported economic performance that has become stronger and less subject to external shocks, although the recent global financial crisis did affect the country and government finance. Per capita income is at the low end of the Aaa range, and the relatively small scale of the economy is also a factor considered in assessing economic strength. Institutional strength is very high, as measured by governance, rule of law, and transparency. In addition, Moody's believes that the government, of whichever party, will maintain a policy of low debt and fiscal soundness.

The rating outlook is stable, anchored by the government's low debt relative to most other Aaa-rated countries and Moody's belief that New Zealand will continue with fiscal and monetary discipline and market-oriented policies.

After the Crisis: A Weak Rebound

Factor 1 – Economic Strength: High

		VERY HIGH	HIGH	MODERATE	LOW	VERY LOW	
New Zealand	+		■				-

New Zealand's economic strength is classified by Moody's as high, which is lower than the "very high" classification of other Aaa-rated countries. Reasons for the somewhat lower economic strength include the relatively small size of the economy, its dependence on agricultural commodities for a substantial portion of economic activity and exports, and lower-than-average per capita income compared to other advanced economies.

The economy suffered one of the longest recessions among advanced economies in the recent past, with negative quarterly GDP during five consecutive quarters through the first quarter of 2009. The recession was not the deepest, however, with the year ending in March 2009 showing negative growth of 1.0% and the figures for the first two quarters of 2010 turning positive. During those two years, fixed investment showed a steep decline, both in the residential and non-residential sectors, while government spending supported growth as stimulus measures were implemented. In real terms, exports, after declining in 2009, showed a revival in 2010, as high commodity prices and demand from Asia and Australia remained strong. Imports declined fairly steeply in real terms, and, thus, net exports also helped prevent New Zealand's downturn from being as steep as in many other advanced economies.

After the turn of the century, New Zealand's real GDP rose at an average annual rate of 3.3% through 2007, a solid growth rate for an advanced economy. High commodity prices during some of the period, combined with strong growth in Australia and China, contributed to acceleration in growth compared to the record of the previous two decades.

Going forward, however, it is likely that growth will be more subdued. As in some other countries, household leverage had reached a fairly high level prior to the recent crisis, and less willingness to take on additional debt may limit the growth of household spending. The government also faces the prospect of an extended period of fiscal consolidation after the ending of economic stimulus. Thus, although exports may provide some underpinning of growth, and business investment should revive, growth rates are likely to be lower than during the years leading up to the global financial crisis. The Reserve Bank forecasts rates in the 2-3% range for the coming few years, although the budget produced in May is somewhat more optimistic, with GDP growth averaging 3.0% in the coming four years.

Growth in the 2-3% range going forward is unlikely to change New Zealand's position in terms of economic strength relative to other Aaa-rated countries. Thus, a categorization of the country's economic strength as "high" continues to seem appropriate.

Strong Institutions Support Aaa Rating

Factor 2 – Institutional Strength: Very High

		VERY HIGH	HIGH	MODERATE	LOW	VERY LOW	
New Zealand	+	■					-

New Zealand's strong institutional framework is an important factor supporting the Aaa rating. Although the recent crisis has tested the fiscal policy framework, it has been responsible for maintaining government debt at relatively low levels over the past two decades.

Under the Fiscal Responsibility Act of 1994, the government must clearly lay out its short-term fiscal intentions and long-term fiscal objectives, subject to the principles of responsible fiscal management specified in the act. These principles include keeping government debt at "prudent" levels and maintaining, on average, a balanced budget. The global crisis tested this framework, and government debt is set to rise over the next few years. However, the framework means that the government has had to spell out a path for reversing the upward debt trajectory and returning to a prudent level.

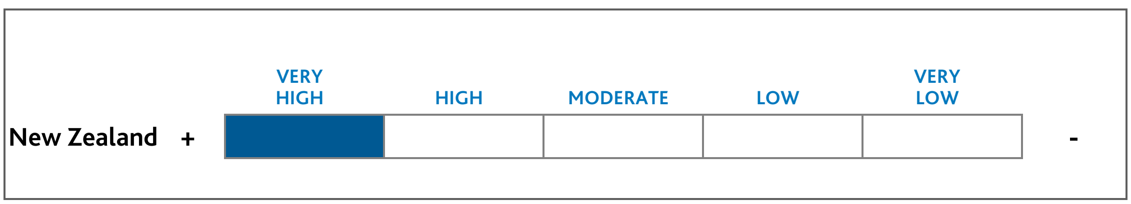
The Reserve Bank of New Zealand is another pillar of institutional strength. Given formal independence in 1989 (although its policy goals are set with the agreement of the Minister of Finance), it was the first central bank to adopt formal inflation targeting. This provides the economy with an important element of stability, although, on average, interest rates in New Zealand tend to be higher than in some other advanced economies.

Political Consensus on Fiscal Matters

After three terms of a Labor-dominated government, the National Party formed the government following elections in late 2008. Three other small parties support the government. In general, there is considerable continuity in policies from one government to the next, particularly when it comes to the maintenance of sound public finances. The government followed through with its electoral promise of tax cuts, but the financial crisis and recession have reduced fiscal flexibility. The next elections must be held by late 2011.

Government Finances: Long Path to Recovery

Factor 3 – Government Financial Strength: Very High



During the years prior to the recent global financial crisis, New Zealand's government finances showed steady improvement, the result of continuous primary budget surpluses. The ratio of general government debt (including not just the central government but other levels of government and certain government agencies) to GDP fell from 40% in 1999 to 26% in 2008, while the ratio of debt to general government revenue dropped from 96% to 58%. Debt affordability also improved, with the ratio of interest payments to government revenue declining from 5.3% to a low of 2.9% in 2007. As a result of these improvements, which placed New Zealand on the strong side compared to a number of the largest Aaa-rated governments, the country was in a relatively good position to deal with the effects of the crisis.

However, the economic downturn and its effects on government finances altered the fiscal and debt dynamics. An extended period of deficits is now forecast by the government, leading to several years of rising debt ratios before they begin to come down again. Nonetheless, the levels projected—and the reversibility of the trajectory after several years—are still within a range easily compatible with New Zealand's Aaa rating.

After falling 3.8% in the fiscal year ended June 30, 2009, central government (core crown) revenues in the most recent fiscal year are now estimated to have declined by a further 5.2%, the result of the slow economy but also of tax cuts. At 29.6% of GDP, revenues will be the lowest in recent history in relation to the size of the economy. Furthermore, the budget forecasts show them remaining near that level in the following four years.

Expenditures as a proportion of GDP rose sharply in the FY 2008-2009, reaching 34.7% of GDP after averaging 30.8% during the previous decade; they remained near that level in the following year. This ratio is forecast to decline very gradually in the coming four years, thus reducing the budget deficit.

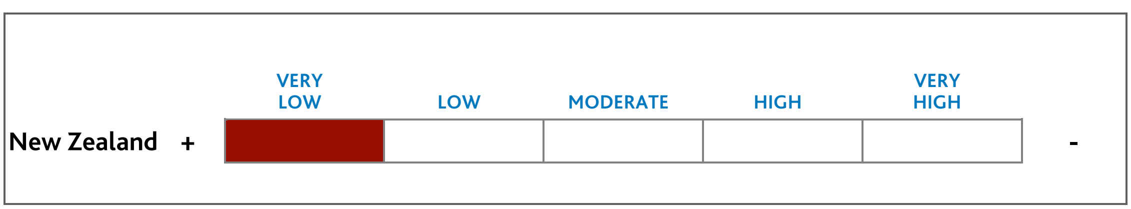
The government now expects to return to an operating surplus in 2016. As a result, debt will rise through 2015. Gross central government debt, which the previous government had targeted to be in the range of 20% of GDP, had fallen to 17.2% in 2008. It rose abruptly to 23.5% in 2009 and is estimated to have reached 28.4% at the end of the most recent fiscal year. Continuing deficits indicate that this ratio will rise to the 32-33% range during the 2011-14 period before beginning to decline. The recent call on the government deposit guarantee and expenditure related to the Canterbury earthquake may result in a somewhat higher ratio, although not very much higher.

The new government in 2009 changed its primary fiscal target to net debt (excluding the assets of New Zealand Superannuation). The Fiscal Strategy Report presented at the time of the current year's budget indicates that the government will ensure that this measure remains below 40% and will eventually come back to under 20%. The ratio had declined from around 30% to a low of 5.6% in the decade through 2008. It has since risen to an estimated 14.1% at present and is expected to peak at 27.4% in 2015 before beginning to decline.

From the point of view of public finances, one difference between the two major parties is National's less adverse view of privatization. However, they have said that they will not privatize public companies during this term and only include privatization in the next election platform. In any case, the amount of possible assets for privatization is not massive.

Despite External Financing Requirement, Low Vulnerability

Factor 4 – Susceptibility to Event Risk: Very Low



New Zealand's major vulnerability is its dependence on foreign capital inflows, with the country running fairly large current account deficits for a long period of time. As a result, the negative net international investment position is one of the largest of any advanced country, equivalent to about

100% of GDP. According to the Reserve Bank, net external debt (excluding equity) was 84% of GDP at the end of 2009, of which two thirds represented the foreign liabilities of the banking system.

During a period at the beginning of the global financial crisis, there was some question as to whether banks in New Zealand (the largest of which are subsidiaries of Australian banks) could access external financing. Some of their funding comes from their Australian parents, but they also borrow directly in the international market. In the end, the New Zealand government instituted a guarantee program for bank wholesale funding, and there was no significant disruption in the bank funding market. The wholesale guarantee scheme ended in April 2010.

The performance of New Zealand's external finances during the recent global financial crisis demonstrates that, even in times of global financial stress, its financial vulnerability remains very low. Access to finance remains strong, despite problems in the European sovereign sphere. New Zealand's banks had only a very short period at the height of the financial crisis when there was any question of market access. As a result, Moody's does not consider event risk from external financial factors to be significant for the rating.

Retail Deposit Guarantees

In addition to the wholesale guarantee scheme, the government implemented a retail deposit guarantee, which is still in place through the end of 2011. This seems unlikely to be required for the major banks, covering roughly 80% of the assets, as these banks are both strong in their own right and also are subsidiaries of highly rated Australian banks. Some finance companies have failed, however, triggering usage of the deposit guarantee. The largest of these was the recent failure of the country's biggest finance company. The government announced that it would compensate all depositors. The net loss to the government, after recovery of assets of the company, is estimated to be well under 1% of GDP. Thus, while this will increase marginally government debt levels, the magnitude in relation to overall debt levels is not significant. Any further calls on the retail deposit scheme are likely to be very small.

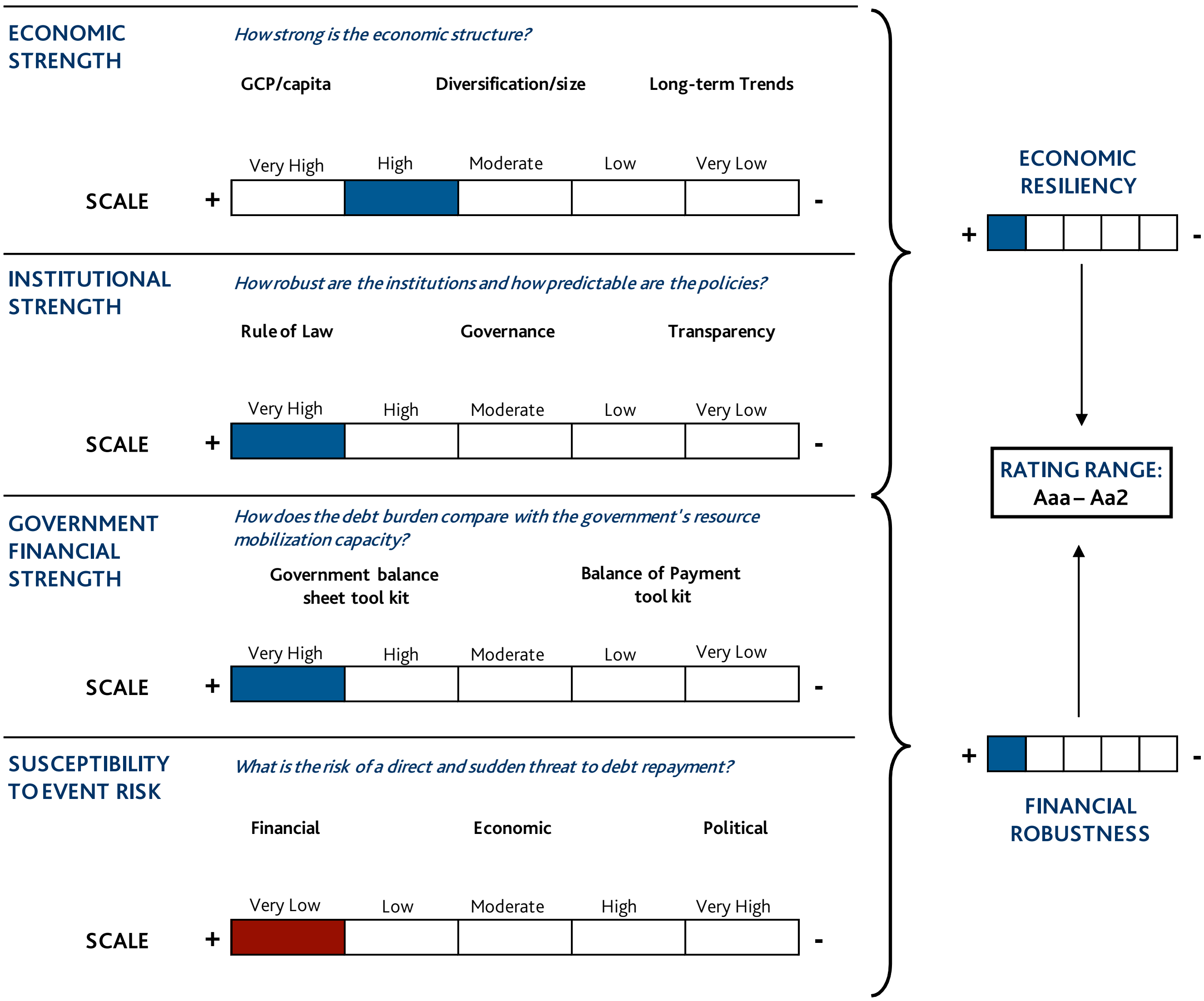
Vulnerability to Earthquakes

Another potential vulnerability that came to the fore once again in September 2010 is the susceptibility to earthquakes. A major earthquake struck Christchurch, the country's second largest city, causing an estimated NZD 4.5 billion in damage. As earthquakes have been relatively frequent in the past, the government established an Earthquake Commission at the end of World War II, amending the original act in 1993. The commission has more than enough financial assets to deal with claims (up to $120,000 per policyholder) from even a fairly large earthquake, such as the one in Christchurch. Private insurance covers a considerable part of the remaining damage to residential and commercial properties. Thus, the government's actual outlays resulting from such a natural disaster are limited, related to infrastructure rebuilding and compensation to workers who become unemployed. Overall, the direct budgetary impact is unlikely to be of a magnitude that would cause rating concerns.

Rating History

	FOREIGN CURRENCY CEILINGS				GOVERNMENT BONDS		OUTLOOK	DATE
	BONDS & NOTES		BANK DEPOSIT		FOREIGN CURRENCY	LOCAL CURRENCY		
	LONG-TERM	SHORT-TERM	LONG-TERM	SHORT-TERM				
Rating Raised	Aaa	--	Aaa	--	Aaa	--	Stable	October-02
Rating Lowered	Aa2	--	Aa2	--	Aa2	--	--	September-98
Review for Downgrade	Aa1	--	Aa1	--	Aa1	--	--	June-98
Outlook Changed	--	--	--	--	--	--	Negative	January-98
Outlook Changed	--	--	--	--	--	--	Stable	March-97
Rating Raised	Aa1	--	Aa1	--	Aa1	--	--	February-96
Review for Upgrade	Aa2	--	Aa2	--	Aa2	--	--	January-96
Rating Assigned	--	--	--	--	--	Aaa	--	October-95
Rating Raised	Aa2	--	Aa2	--	Aa2	--	--	March-94
Review for Upgrade	--	--	--	--	Aa3	--	--	February-94
Rating Lowered	Aa3	--	Aa3	--	Aa3	--	--	August-86
Rating Assigned	Aa	--	Aa	--	--	--	--	April-85
Rating Lowered	--	--	--	--	Aa	--	--	October-84
Rating Assigned	--	P-1	--	P-1	--	--	--	May-79
Rating Raised	--	--	--	--	Aaa	--	--	June-77
Rating Raised	--	--	--	--	Aa	--	--	July-75
Rating Assigned	--	--	--	--	Baa	--	--	July-65

Sovereign Rating Mechanics : New Zealand



Annual Statistics

New Zealand

	2003	2004	2005	2006	2007	2008	2009	2010F	2011F
Economic Structure and Performance									
Nominal GDP (US$ Bil.) [1]	85.4	101.9	110.7	110.3	137.4	116.4	127.2	143.9	149.6
Population (Million)	4.0	4.1	4.1	4.2	4.2	4.3	4.3	4.4	4.4
GDP per capita (US$)	21,202	24,926	26,783	26,362	32,502	27,268	29,481	33,024	33,976
GDP per capita (PPP basis, US$)	23,124	24,105	24,718	25,946	27,336	27,029	--	--	--
Nominal GDP (% change, local currency) [1]	6.8	8.5	5.6	5.0	7.6	1.3	2.2	7.3	6.3
Real GDP (% change)	4.0	3.5	3.3	2.3	2.8	-1.3	0.5	2.1	2.2
Inflation (CPI, % change Dec/Dec)	1.5	2.7	3.2	2.6	3.2	3.4	2.0	3.8	2.4
Unemployment rate (%)	4.8	4.0	3.8	3.8	3.7	4.2	6.2	6.2	5.6
Gross Investment/GDP [1]	23.6	24.5	24.7	23.2	23.9	22.2	19.0	20.5	22.5
Gross Domestic Savings/GDP	23.8	23.8	22.5	21.7	23.0	20.9	20.4	20.9	21.8
Nominal Exports of G&S (% change US$ basis) [1]	18.7	17.7	3.9	4.2	23.6	-7.6	-2.4	14.2	5.3
Nominal Imports of G&S (% change US$ basis) [1]	24.8	21.7	9.8	1.1	21.5	-6.9	-10.6	18.3	9.7
Real Exports of G&S	2.3	6.2	-0.5	1.7	3.8	-1.4	0.0	4.3	5.6
Real Imports of G&S	8.4	15.9	5.4	-2.5	8.9	1.9	-14.9	14.7	9.0
Net exports of G&S/GDP [1]	0.3	-0.7	-2.3	-1.4	-0.9	-1.2	1.3	0.4	-0.8
Openness of the Economy [1] [2]	57.9	58.1	57.1	58.8	57.8	63.3	54.1	55.5	57.5
Government Effectiveness [3]	2.0	2.1	1.9	1.9	1.9	1.8	--	--	--
Government Finance									
Gen. Gov. Revenue/GDP	41.6	41.4	43.0	45.0	44.1	42.6	41.2	40.9	40.8
Gen. Gov. Expenditures/GDP	37.8	37.5	38.5	39.9	40.1	42.2	44.7	45.2	44.5
Gen. Gov. Financial Balance/GDP	3.8	3.9	4.5	5.1	4.0	0.4	-3.5	-4.3	-3.7
Gen. Gov. Primary Balance/GDP	5.5	5.4	6.0	6.6	5.3	1.7	-2.2	-3.1	-2.2
Gen. Gov. Debt (US$ Bil.)	24.69	28.17	30.08	28.68	33.81	37.45	41.33	57.51	65.87
Gen. Gov. Debt/GDP	31.0	28.3	27.0	26.7	25.8	29.1	35.0	40.3	44.4
Gen. Gov. Debt/Gen. Gov. Revenue	74.6	68.3	62.7	59.3	58.6	68.3	85.0	98.6	108.8
Gen. Gov. Int. Pymt/Gen. Gov. Revenue	4.1	3.6	3.3	3.2	3.0	3.2	3.2	2.9	3.7
External Payments and Debt									
Nominal Exchange Rate (local currency per US$, Dec)	1.5	1.4	1.5	1.4	1.3	1.7	1.4	1.4	1.4
Real Effective Exchange Rates (% change)	17.0	7.2	5.1	-7.8	7.7	-8.0	-5.1	--	--
Realtive Unit Labor Costs (1995 = 100)	81.2	90.1	100.0	97.4	106.0	100.6	93.2	--	--
Current Account Balance (US$ Bil)	-3.45	-6.17	-9.23	-9.12	-10.54	-11.24	-3.69	-3.75	-5.00
Current Account Balance/GDP	-4.2	-6.2	-8.3	-8.5	-8.0	-8.7	-2.9	-2.6	-3.4
Net Foreign Direct Investment/GDP	1.1	2.8	2.7	4.2	-0.2	4.1	0.7	1.5	2.0
Net Int'l Investment Position/GDP [4]	-84.8	-86.3	-79.3	-92.3	-88.4	-73.0	-102	--	--
Official Forex Reserves (US$ Bil.)	5.41	6.44	8.69	13.92	17.12	10.86	13.98	17.00	15.00

Notes:

[1] Fiscal years beginning April 1

[2] Sum of Exports and Imports of Goods and Services/GDP

[3] Composite index with values from -2.5 to 2.5: higher values suggest greater maturity responsiveness of government institutions

[4] Series break 2000

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