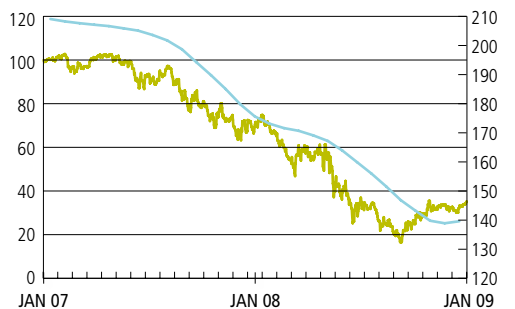


# HOW NEW ZEALAND WEATHERED THE STORM

## US SUBPRIME HOUSING CRISIS

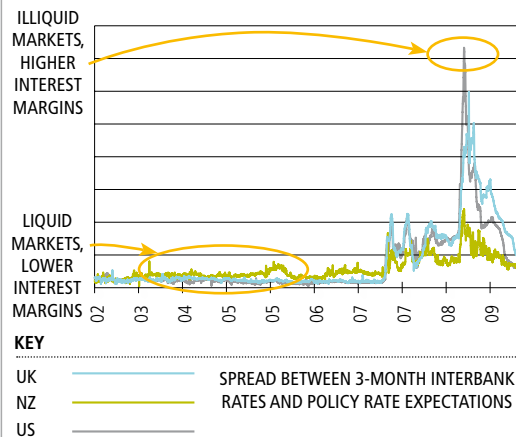


### KEY

US FINANCIAL SHARES DOWN OVER 80% (LHS INDEX) ———  
 US HOUSE PRICES DOWN OVER 30% (RHS INDEX) ———

Subprime housing market collapse spills into sharemarkets. Large investment banks fail. Global banking strains, combined with worsening economic outlook, send property/commodity prices and sharemarkets crashing.

## MONEY MARKETS JAM



ILLIQUID MARKETS, HIGHER INTEREST MARGINS

LIQUID MARKETS, LOWER INTEREST MARGINS

### KEY

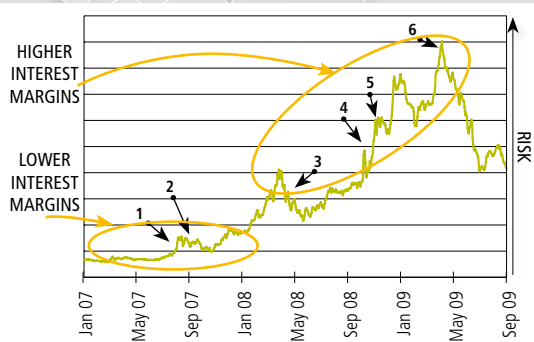
UK ——— SPREAD BETWEEN 3-MONTH INTERBANK RATES AND POLICY RATE EXPECTATIONS  
 NZ ———  
 US ———

Major investors suffer losses, become more wary of risk, uncertain about which institutions to trust and reluctant to lend, resulting in a cash (liquidity) squeeze in short-term money markets.

PRE-2007		2007	
	THE SEEDS	THE CRISIS EMERGES	NORTHERN ROCK COLLAPSES
		April – August	September
INTERNATIONAL	US banks give high-risk loans to people with poor credit histories (subprime). Loans are bundled into portfolios and sold to investors globally.	House prices fall, interest rates rise, people cannot repay mortgages. Subprime lenders collapse. Losses make banks wary of lending to each other. Major central banks inject cash into the banking system and cut interest rates.	Northern Rock fails because of its dependence on wholesale money market funding (80%), leading to a retail depositors' run on the bank. UK Government guarantees Northern Rock deposits.
NEW ZEALAND		RBNZ accepts bank bills/bonds as security for lending to ensure banks have cash.	



### TERM LENDING MARKETS CLOSE

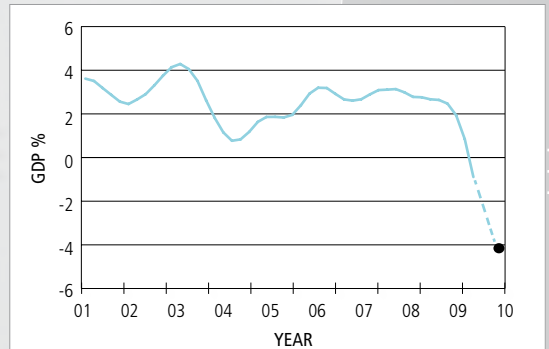


**KEY**

1. Bear Stearns announces major losses for two sub-prime backed hedge funds
2. BNP Paribas sub-prime funds frozen
3. Bear Stearns acquired by JP Morgan with US Fed assistance
4. Lehman Brothers files for bankruptcy
5. US Congress passes Troubled Asset Relief Program (TARP)
6. US sharemarket reaches low and starts subsequent rally

The squeeze spreads to credit for more than one-year lending terms and market interest rates soar.

### FINANCIAL ECONOMIES FALL



Financial market stress hits housing, consumption and production in major financial economies in US and Europe.

## 2008

### CONCERNS DEEPEN

December

Major central banks offer billions of dollars in loans to banks. Bond insurers' credit ratings downgraded.

January – September

Global stock markets' biggest falls since 9/11. US Fed's biggest interest rate cut in 25 years. UK, European banks try raising additional shareholder capital to cover losses.

### EYE OF THE STORM

September

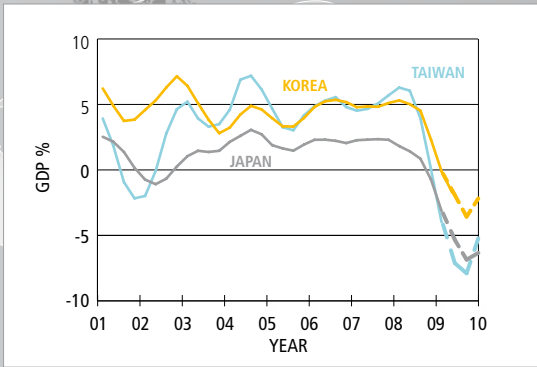
US unemployment 6.1%. Fannie Mae, Freddie Mac rescued by US Government. Lehman Brothers collapses – lack of government intervention shocks world markets.

Bank takeovers and nationalisation in the US, UK, France. US Fed's \$85bn rescue package for biggest insurance company, AIG.

Wide range of liquidity measures announced by RBNZ to ensure banking system has cash. OCR cut to 8%.

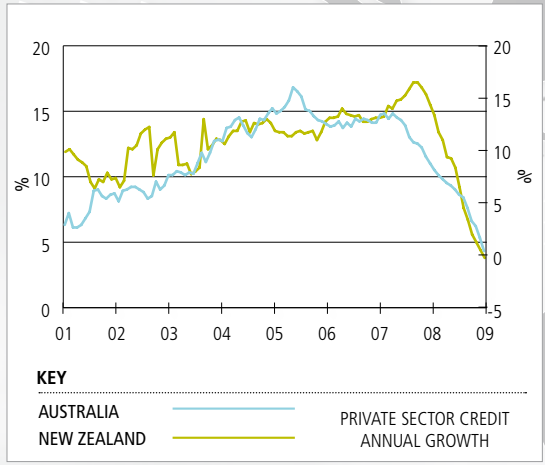
OCR cut to 7.5%.

### MANUFACTURING ECONOMIES PLUMMET



The stress then spreads across the world into East Asian and European manufacturers as their consumer markets shrink.

### CREDIT GROWTH IN AUSTRALASIA



Tighter credit conditions means Australasian banks reduce their lending to business and household sectors. Credit growth in NZ has to date not slowed as much as in some other countries.

### AUTHORITIES STEP UP RESPONSE

October

US House of Representatives rejection of \$700bn Troubled Asset Relief Program (TARP) to buy bad debts from ailing banks sends further shockwaves around the world. Ireland guarantees bank deposits.

UK, US apply quantitative easing measures to stabilise financial systems and encourage lending. US passes \$700bn rescue plan. UK Financial Services Authority increases deposit guarantee. European, UK bank bailouts. Countries around the world guarantee retail deposits, including Australia. Major central banks make emergency interest rate cuts.

Crown Deposit Guarantee Scheme established. RBNZ allows residential mortgage-backed securities as collateral to ensure banks have cash. Retail deposit guarantee scheme launched. OCR cut to 6.5%.

### FROM CRISIS TO RECESSION

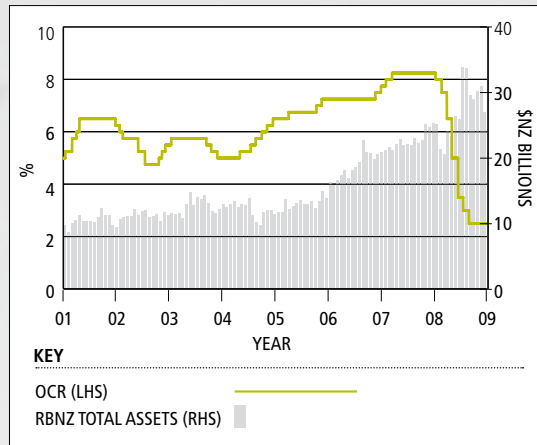
November – December

IMF loans to Ukraine, Iceland. China stimulus package. Eurozone, US in recession. Recovery measures in UK, US, Europe. US plans to help Big Three US car makers. US interest rates cut to 0-0.25%.

Crown Wholesale Guarantee facility launched. RBNZ provides term auction lending facility and allows corporate and asset-backed securities to be eligible for lending to ensure banks have ongoing access to cash. OCR cut to 5%.



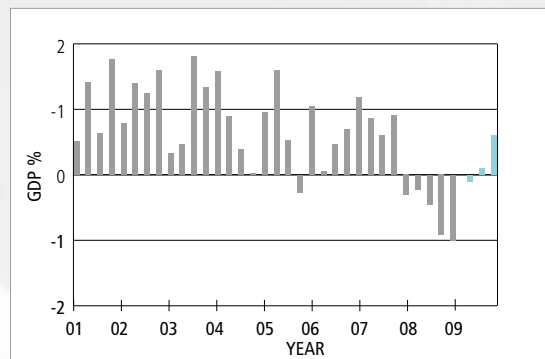
### RBNZ TAKES ACTION



The Reserve Bank cuts the OCR from 8.25% to 2.5%, widens the range of securities that banks can borrow on, expanding its balance sheet significantly.



### NEW ZEALAND ECONOMY CONTRACTS ... BUT FORECAST TO RECOVER



Commodity economies like New Zealand's are initially more sheltered, but a world event of this magnitude had to hit us too.

### 2009

#### UNHAPPY NEW YEAR

January

US jobless rate 7.2%. Chinese exports suffer biggest fall in decade. German stimulus package. UK government loan guarantees for SMEs. UK in recession.

#### SPENDING PACKAGES

February – April

US \$787bn economic stimulus plan signed. G20 agree \$1.1 trillion measures. Total financial sector writedowns forecast at \$4 trillion.

#### MIXED OUTLOOK

May – June

Chrysler files for bankruptcy protection. Ten big US banks fail stress tests, need capital. Carmaker GM bankrupt. UK unemployment 7.1%. Growth forecasts for some countries revised up as indicators stabilise.

Ten of largest US banks say able to repay government (TARP) loans. Japanese economy experiences record decline in first quarter 2009 – minus 14.2% on annualised basis.

Corporate and asset-backed securities eligible to ensure banks have access to cash. OCR cut to 3.5%.

Further cuts to OCR take it to 2.5%.

RBNZ releases prudential policy aimed at reducing dependence on short-term wholesale money market funding.

NZ economy likely to sustain several quarters of economic contraction, but decline is relatively muted compared with other countries.