



Australian Markets Weekly

A weekly outlook for Australia, key global economies and markets

National
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Bank

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Survival of the fittest: A postcard from Australia's resource-centric North West

The Economist this week carries a topical article on commodities, "Goodbye to all that: a decade of bingeing on raw materials may leave an even longer hangover", outlining the pressure on producers now from declining prices. And that's how it's playing out locally as Australia's bulk commodity and energy producers seek efficiencies in a survival of the fittest.

Having just returned from a visit to the north west of WA – to Karratha and Port Hedland – the pressure is on but activity and exports remains strong. In economic terms, economists call this the net export contribution to GDP, set to continue contributing up to 2 percentage points to GDP, with prospective growth coming from LNG as it takes over from iron ore as the growth driver. (Together with this below postcard from the West, please refer to David deGaris' presentation, [available here](#), to clients and guests in Karratha and Port Hedland.)

In addition to the presentations and meetings in the North West, we first visited clients in Albany in the South of WA, a town centred around local farming, especially wheat. Growing conditions for the current wheat crop have started positively and a pull-back in labour demand from the mines has freed up costs.

Resource exports strong

It would be a big mistake to think that the resources sector is in a moribund state. Nothing could be further from the truth. The unmistakable impression you get from visiting the centrepiece of Australia's iron ore and Liquefied Natural Gas (LNG) production, from the Burrup Peninsula to Port Hedland, is that transport and export activity is frenetic.

The focus on cost reduction after the near completion of new projects is pressuring local business activity. Bulk resource commodity and energy prices are down – world oil prices have just reached the lowest levels since 2009 – and producers are reducing costs to protect margins and profitability.

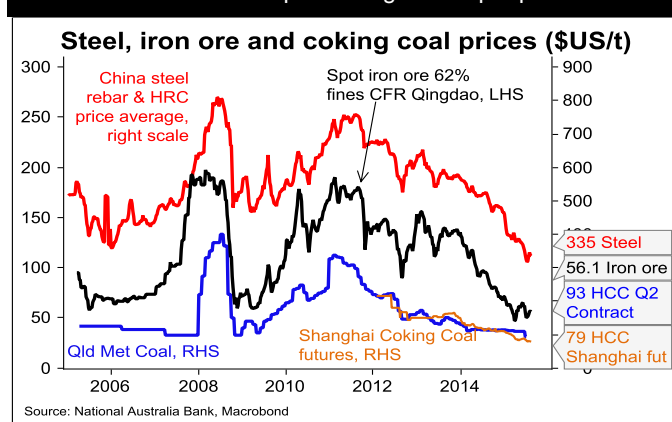
We do note however that while Chinese steel production is struggling, iron ore spot and futures prices have been stable in so far this month, spot iron ore at \$56.1/t on Friday for the 62% Qingdao cif fines price. Dalian futures prices have been similarly stable, also increasing somewhat from early July lows.

Local businesses are competing aggressively. Increased labour availability and lower energy costs are providing some support. The lower Australian dollar will also soften the blow over time and increase the attractiveness of local tourism that offers world-class and unique experiences.



The pace of business activity in the towns and surrounds has undoubtedly slowed. The demand for rental accommodation has fallen back as major projects have been completed and cost efficiencies achieved and still sought. The demand for mining services has contracted, as have the numbers of fly-in, fly-out workers from levels when expansion was at its peak. Property markets have softened, with prices down sharply from their short-lived peaks. Both Karratha and Port Hedland have benefited from increased local building construction in recent years with a somewhat "newer" feel; there is some limited new construction, though with higher vacancies, local property markets are likely to remain soft for now.

Chart 1: China slowdown pressuring steel/input prices



One local property agent reported higher vacancies with more listings in excess of the take up of dwellings, though the take up rate had steadied and picked up a little in the past month. Another mining services client reported the large reductions in contract pricing now "in train" as the large resource companies bear down on costs. Wage rates on offer for mining-related employment have pulled back.

Key markets over the past week

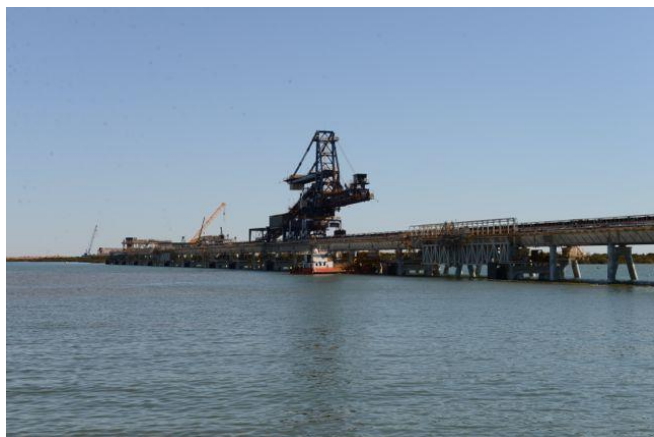
	Last	% chg week		Last	bp / % chg week
AUD	0.7257	-1.6	RBA cash	2.00	0
AUD/CNY	4.64	-1.4	3y sw ap	2.06	-15
AUD/JPY	88.4	-3.6	ASX 200	5,215	-2.6
AUD/EUR	0.638	-3.9	Iron ore	56.1	-1.1
AUD/NZD	1.096	-2.4	WTI oil	40.1	-5.5

Source: Bloomberg

The compression in prices and costs, evident in its impact on the local and State economy, feeds through falling levels of resource-driven labour income and the decline in Australia's terms of trade as export prices wilt. For resource companies, there is some compensation from the cuts to labour and greater competition for work tenders, amplified by declining transport costs as world energy prices reach multi-year lows.

Iron ore expansion mostly complete

The expansion of iron ore production at the mines and the enhancement of transport and delivery infrastructure is now mostly complete. There is likely to be further moderate increases from the major producers, together with shipments from the Roy Hill iron ore project that is expected to commence shipments in coming months. The Roy Hill project has been a complete new iron ore mine including mine development, a railway, rolling stock, offloading facilities for ore near the port, reclaiming the ore from stockpiles, an extensive conveyancing system to the berth, together with construction of new berths and an ore loader.



In the past five years, Australian iron ore shipments will have almost doubled in five years. In 2010, Australia shipped 402mt; once Roy Hill is up at full production of 55mt, total shipments will be within cooe of 800mt. Iron ore exports now account for 21.5% of Australia's volume of goods and services exports, 4.8% of real GDP, on a par with private dwelling investment. In 2014-15, iron ore exports totalled \$54.3bn.

The impact on the economy has not only been material but the pace of development from mine to port has been breathtaking, including mine construction, extraction, crushing and processing, loading at the mine, transport (mostly rail), enhanced "reclaiming" of the ore from port stockpiles, together with conveyor and ship loading facilities.

In July, Port Hedland shipped 35.3mt of iron ore, an average daily shipment rate of over 1.1mt. In late April in a 24 hour period, 11 Cape size vessels shipped 2.028mt. With Cape size vessels carrying in the vicinity of 240,000t, that's an average of 4.7 tankers leaving fully-laden each day. It takes around 22 hours to load one vessel, with a fully-laden vessel having only around 0.3m of clear draught along the shipping channel in and out of the port that has seven metre tides with a uni-directional shipping channel. The largest single shipment was 264,858t in April this year.

Chart 2: Australia takes up more iron ore global share



Port Hedland is used by BHP Billiton and Fortescue, with additional shared loading facilities for junior iron ore and other mining companies. It takes 10-12 trains sets of 150-200 ore rail trucks (each carrying 117t and with four locomotives) to provide enough ore to fill a vessel. There are 17 operational berths for loading, eight are BHP's, five FMG's, four are public/shared berths, while Roy Hill has two new berths constructed. Port Hedland is the largest bulk export port in the world with throughput of 446.9mt in 2014-15 (up 20% pcp). Nearly all exports (98%) are iron ore, the remaining exports being salt and manganese.

Demand for iron ore is likely to be the constraining factor on port throughput for now. Over the medium term a further additional constraint from an operational viewpoint is the Port of Hedland's single lane channel along which all vessels enter and leave the port. To cater for the Cape size ships the channel, 22 nautical miles (45 kilometres) in length, the channel can only cater for one arriving or leaving vessel with skilled pilotage required to avoid vessels being grounded and blocking the channel and thus shutting down the port. This is a key operational risk arguing for further consideration of BHP's "Outer Harbour" development with loading berths outside the Port.

Rio Tinto exports its ore through Dampier and Cape Lambert, close to Karratha, the other main iron ore port. Rio has six iron ore berths at Dampier and another for RTIO Dampier Salt, with Woodside exporting NW Shelf and Pluto LNG gas also from that port.

To this point, while Chinese steel production has stalled this year, Australian exports of iron ore have continued increasing, taking market share from the lower quality, higher cost domestic Chinese ore production. Last week's unofficial Caixin Manufacturing PMI suggested further weakness into August to 47, though it is not known whether steel production was similarly weak. July property prices showed price rises in 31 cities for new residential apartments, slightly more than for the 29 cities where prices fell, a hint that new Chinese property demand may be showing some signs of stabilising.

LNG production now a major growth driver

Australia's North West Shelf project commenced exporting LNG to Japan in 1989. In 2013-14, LNG export volumes totalled 24.18mt, \$13.74bn. LNG exports are 8.4% of goods and services exports, and an estimated 1.6% of GDP. Together with Pluto, that is lifting LNG production and export to around 30mt.

The mega Gorgon project, the three Queensland LNG projects, together with the Prelude Floating LNG project (FLNG, a world first floating LNG), Wheatstone and the Darwin Ichthys project will ultimately add an additional 61.8mt to capacity in future years, a tripling in output and export volumes within this decade. That will contribute a cumulative 3 percentage points to GDP growth.

Still for sale

Finally, for those that may have been following the fortunes of that house in Port Hedland featured on ABC News as having been passed in at auction for \$360,000 after it was bought four years earlier for \$1.3m, it's still on the market.



The week ahead

The data flow starts to pick up again this coming week, with the release of two important quarterly investment partials ahead of June quarter GDP on 2 September. These are Construction Work Done on Wednesday and New Private Capital Expenditure (Capex) with its updated 2015-16 projections on Thursday ahead of Q2 GDP next Wednesday.

There are also remarks from RBA Governor Glenn Stevens at a National Reform Summit on Wednesday that is being hosted jointly by two major Australian newspapers. Given these are remarks, and not a speech per se, and given the proximity of next Tuesday's RBA Board meeting, the Governor may well refrain from any particular monetary policy or other market sensitive commentary. The RBA has just released a Research Discussion Paper this morning at 11.30am titled "Housing Wealth Effects: Cross-sectional Evidence from New Vehicle Registrations". It's a paper that investigates the link between changes in housing wealth at the postcode level and vehicle registrations as a proxy for consumption, the degree of spillover sensitive to income levels.

Internationally, Fed speak will be important with now less than a month until the 17/18 September FOMC meeting. Lockhart speaks Monday, Dudley gives a press conference on Wednesday and the annual Kansas Fed/Jackson Hole symposium begins Thursday and runs through the weekend. Like last year, Yellen is again not slated to attend.

U.S data includes durable goods orders (Wednesday), New Home sales (Tuesday) and the July monthly personal income spending and (more importantly) PCE deflator readings looking like being the highlights. Elsewhere the German IFO survey Tuesday and Japan CPI (Friday) will both be of interest. There's no major data out of China.

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Calendar of Economic Releases

Country	Economic Indicator	Time Period	NAB		Actual	Previous	GMT	AEST
			Forecast	Consensus				
Monday, 24 August 2015								
NZ	RBNZ's Deputy Governor Grant Spencer Speaks						1.30	11.30
US	Chicago Fed Nat Activity Index	Jul				0.1	12.30	22.30
GE	Import Price Index MoM/YoY	Jul		-0.2%/-1.2%		-0.5%/-1.4%	14.00	0.00
US	Fed's Lockhart speaks to Public Pension Funding Forum						19.55	5.55
Tuesday, 25 August 2015								
AU	ANZ Roy Morgan Weekly Consumer Confidence Index	Aug-23				113.2	23.30	9.30
AU	Conf. Board Leading Index MoM	Jun				0.2%	0.00	10.00
CH	Conference Board China July Leading Economic Index						2.00	12.00
NZ	2Yr Inflation Expectation	3Q				1.9%	3.00	13.00
GE	GDP SA QoQ	2Q F		0.4%		0.4%	6.00	16.00
GE	GDP NSA YoY	2Q F		1.6%		1.6%	6.00	16.00
GE	Ifo Business Climate	Aug		107.5		108	8.00	18.00
GE	Ifo Current Assessment	Aug		113.9		113.9	8.00	18.00
GE	Ifo Expectations	Aug		101.9		102.4	8.00	18.00
US	FHFA House Price Index MoM	Jun		0.40%		0.4%	13.00	23.00
US	House Price Purchase Index QoQ	2Q				1.3%	13.00	23.00
US	S&P/CS 20 City MoM/YoY SA	Jun					13.00	23.00
US	Markit US Composite PMI/Services PMI	Aug P		/54.0		55.7/55.7	13.45	23.45
US	New Home Sales / MoM	Jul		511K/6.0%		482K/-6.8%	14.00	0.00
US	Consumer Confidence Index	Aug		93.0			14.00	0.00
US	Richmond Fed Manufact. Index	Aug		9			14.00	0.00
CA	Bank of Canada Deputy Schembri Speaks in Ontario						16.25	2.25
Wednesday, 26 August 2015								
NZ	Trade Balance	Jul	-785m	-600m		-60M	22.45	8.45
JN	PPI Services YoY	Jul		0.4%		0.4%	23.50	9.50
AU	Construction Work Done	2Q	-1.7%	-1.50%		-2.4%	1.30	11.30
AU	Remarks by RBA Governor Glenn Stevens at a National Reform Summit							
CH	Westpac-MNI Consumer Sentiment	Aug				114.5	1.45	11.45
UK	BBA Loans for House Purchase	Jul				44488	8.30	18.30
US	MBA Mortgage Applications	Aug-21					11.00	21.00
US	Durable Goods Orders	Jul		-0.40%		3.4%	12.30	22.30
US	Durables Ex Transportation	Jul		0.20%		0.8%	12.30	22.30
US	Cap Goods Orders Nondef Ex Air	Jul		0.50%		0.9%	12.30	22.30
US	Cap Goods Ship Nondef Ex Air	Jul				-0.1%	12.30	22.30
US	Fed's Dudley speaks at Press Briefing on Local Economy						14.00	0.00
Thursday, 27 August 2015								
JN	Japan Buying Foreign Bonds and Stocks	Aug-21					23.50	9.50
AU	Private Capital Expenditure	2Q	-4.0%	-2.50%		-4.4%	1.30	11.30
EC	M3 Money Supply YoY	Jul				5.0%	8.00	18.00
EC	M3 3-month average	Jul				5.1%	8.00	18.00
US	GDP Annualized QoQ	2Q S		3.2%		2.3%	12.30	22.30
US	Personal Consumption	2Q S		3.1%		2.9%	12.30	22.30
US	GDP Price Index	2Q S		2.0%		2.0%	12.30	22.30
US	Core PCE QoQ	2Q S		1.8%		1.8%	12.30	22.30
US	Initial Jobless Claims	Aug-22					12.30	22.30
US	Continuing Claims	Aug-15					12.30	22.30
US	Bloomberg Consumer Comfort	Aug-23					13.45	23.45
US	Kansas City Fed Hosts Symposium in Jackson Hole, Wyoming							
US	Pending Home Sales MoM	Jul		1.5%		-1.8%	14.00	0.00
US	Kansas City Fed Manf. Activity	Aug				-7	15.00	1.00
Friday, 28 August 2015								
UK	GfK Consumer Confidence	Aug		4		4	23.05	9.05
JN	Jobless Rate	Jul		3.4%		3.4%	23.30	9.30
JN	Job-To-Applicant Ratio	Jul		1.19		1.19	23.30	9.30
JN	Overall Household Spending YoY	Jul		0.5%		-2.0%	23.30	9.30
JN	Natl CPI YoY	Jul		0.2%		0.4%	23.30	9.30
JN	Retail Trade MoM/YoY	Jul		1.10%		0.9%	23.50	9.50
CH	Industrial Profits YoY	Jul				-0.3%	1.30	11.30
UK	GDP QoQ/YoY	2Q P		0.7%/2.6%		0.7%/2.6%	8.30	18.30
UK	Lloyds Business Barometer	Aug					8.30	18.30
EC	Economic Confidence	Aug					9.00	19.00
GE	CPI MoM/YoY	Aug P		0.0%/0.2%		0.2%/0.2%	12.00	22.00
US	Personal Spending	Jul		0.4%		0.2%	12.30	22.30
US	PCE Deflator MoM/YoY	Jul		0.1%/0.3%		0.2%/0.3%	12.30	22.30
US	PCE Core MoM/YoY	Jul		0.1%/1.3%		0.1%/1.3%	12.30	22.30
CA	Industrial Product Price MoM	Jul					12.30	22.30
CA	Raw Materials Price Index MoM	Jul					12.30	22.30
US	U. of Mich. Sentiment	Aug F		93.2		92.9	14.00	0.00
Upcoming Central Bank Interest Rate Announcements								
Australia, RBA		1-Sep	2.00%	2.00%		2.00%		
UK BOE		10-Sep				0.50%		
Japan, BoJ		15-Sep	0.0%-0.1%	0.0%-0.1%		0.0%-0.1%		
Europe ECB		3-Sep				0.05%		
New Zealand, RBNZ		10-Sep	2.75%	2.75%		3.00%		
Canada, BoC		10-Sep				0.50%		
US Federal Reserve		18-Sep				0-0.25%		

GMT: Greenwich Mean Time; AEST: Australian Eastern Standard Time

Forecasts

Economic Forecasts

	Annual % change				Quarterly % change											
	2013	2014	2015	2016	2013			2014				2015				
					Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Australia Forecasts																
Household Consumption	1.7	2.5	2.8	3.1	0.3	0.4	0.8	0.6	0.5	0.7	0.5	0.8	0.5	0.8	0.8	0.7
Underlying Business Investment	-4.5	-6.4	-10.2	-9.6	-4.9	-1.5	0.8	-3.5	-2.4	-0.9	-1.0	-1.5	-4.6	-2.2	-3.5	-3.3
Residential Construction	0.5	7.9	13.7	9.7	-2.7	3.0	0.3	1.3	4.3	1.7	-1.2	3.9	4.7	3.7	4.3	3.1
Underlying Public Spending	0.4	0.8	0.2	1.4	2.7	-0.2	-0.5	1.3	0.3	0.5	-1.4	0.1	0.2	0.4	0.3	0.3
Exports	6.3	6.8	8.0	8.3	0.9	3.7	-0.6	1.7	4.1	-1.6	3.1	1.6	5.0	-1.8	2.4	2.7
Imports	-1.8	-1.6	1.7	0.8	-3.3	2.8	-1.4	-0.5	-2.5	3.1	-1.2	-1.6	3.1	-0.6	0.3	0.2
Net Exports (a)	1.6	1.7	1.3	1.7	0.9	0.1	0.2	0.4	1.4	-0.9	0.9	0.7	0.5	-0.3	0.5	0.6
Inventories (a)	-0.3	0.0	0.2	-0.1	-0.2	0.3	-0.3	-0.2	-0.3	0.9	0.1	-0.7	0.5	0.0	-0.1	-0.1
Domestic Demand - qtr%					-0.1	0.2	0.5	0.2	0.3	0.6	-0.4	0.5	0.0	0.5	0.4	0.3
Dom Demand - ann %	0.5	1.1	1.1	1.6	0.5	0.0	0.6	0.7	1.1	1.5	0.7	1.0	0.8	0.8	1.5	1.3
Real GDP - qtr %					0.3	0.7	0.4	0.8	1.0	0.6	0.3	0.5	0.9	0.6	0.7	0.7
Real GDP - ann %	2.1	2.7	2.6	3.0	2.0	2.1	1.9	2.2	2.9	2.8	2.7	2.4	2.3	2.3	2.7	2.9
CPI headline - qtr %					0.4	0.4	1.2	0.8	0.6	0.5	0.5	0.2	0.2	0.7	0.8	0.9
CPI headline - ann %	2.4	2.5	1.8	3.1	2.5	2.4	2.2	2.7	2.9	3.0	2.3	1.7	1.3	1.5	1.8	2.6
CPI underlying - qtr %					0.5	0.6	0.7	0.9	0.6	0.6	0.4	0.6	0.7	0.5	0.6	0.7
CPI underlying - ann %	2.4	2.5	2.4	2.6	2.4	2.4	2.3	2.7	2.7	2.7	2.5	2.2	2.4	2.3	2.5	2.5
Wages (Pvte WPI - ann %)	2.9	2.5	2.2	2.2	3.1	3.0	2.8	2.5	2.6	2.4	2.4	2.5	2.2	2.2	2.2	2.2
Unemployment Rate (%)	5.7	6.0	6.1	6.1	5.6	5.7	5.7	5.9	5.8	6.0	6.2	6.1	6.2	5.9	6.2	6.2
Terms of trade	-3.8	-7.4	-10.4	-2.0	1.0	-0.3	-1.3	0.4	-1.9	-4.6	-2.9	-1.5	-2.9	-5.6	-0.4	1.2
G&S trade balance, \$Abn	-10.4	-9.2	-26.6	-10.3	-3.0	-2.8	-3.3	-1.3	2.7	-5.1	-4.0	-2.7	-3.7	-9.4	-8.2	-5.3
% of GDP	-0.7	-0.6	-1.6	-0.6	-0.8	-0.7	-0.9	-0.3	0.7	-1.3	-1.0	-0.7	-0.9	-2.3	-2.0	-1.3
Current Account (% GDP)	-3.3	-2.8	-3.4	-2.3	-3.3	-3.4	-3.6	-3.1	-1.9	-3.6	-3.1	-2.5	-2.7	-4.1	-3.8	-3.0

Source: NAB Group Economics; (a) Contributions to GDP growth

Exchange Rate Forecasts

	24-Aug	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16
Majors						
AUD/USD	0.7263	0.72	0.70	0.68	0.69	0.70
NZD/USD	0.6624	0.64	0.62	0.60	0.60	0.61
USD/JPY	121.84	124	125	126	126	127
EUR/USD	1.1374	1.07	1.05	1.03	1.03	1.04
GBP/USD	1.5675	1.53	1.52	1.51	1.51	1.53
USD/CNY	6.3949	6.50	6.55	6.60	6.62	6.65
USD/CAD	1.3220	1.33	1.35	1.37	1.36	1.34

Australian Cross Rates

	24-Aug	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16
AUD/JPY	88.5	89	88	86	87	89
AUD/EUR	0.6386	0.67	0.67	0.66	0.67	0.67
AUD/GBP	0.4633	0.47	0.46	0.45	0.46	0.46
AUD/NZD	1.0965	1.13	1.13	1.13	1.15	1.15
AUD/CNY	4.6446	4.68	4.59	4.49	4.57	4.66
AUD/CAD	0.9602	0.96	0.95	0.93	0.94	0.94
AUD/CHF	0.6882	0.71	0.71	0.71	0.72	0.00

Interest Rate Forecasts

	24-Aug	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16
Aust rates						
RBA Cash rate	2.00	2.00	2.00	2.00	2.00	2.00
3 month bill rate	2.14	2.15	2.15	2.15	2.20	2.40
3 Year Swap Rate	2.06	2.7	2.9	3.2	3.4	3.5
10 Year Swap Rate	2.92	3.8	3.8	4.0	4.1	4.2
Offshore Policy Rates						
US Fed funds	0.25	0.50	0.75	0.75	1.25	1.50
ECB refi rate	0.05	0.05	0.05	0.05	0.05	0.05
BoE repo rate	0.50	0.50	0.50	0.75	1.00	1.25
BoJ overnight call rate	0.08	0.10	0.10	0.10	0.10	0.10
RBNZ OCR	3.00	2.75	2.50	2.50	2.50	2.50
China 1yr lending rate	4.85	4.60	4.60	4.60	4.60	4.60
China Reserve Ratio	18.5	18.0	17.5	17.0	17.0	17.0
10 Year Benchmark Bond Yields						
Australia	2.54	3.0	3.4	3.4	3.4	3.5
United States	2.04	2.50	2.75	2.8	2.8	3.0
Europe/Germany	0.56	0.8	0.9	1.0	1.2	0.0
UK	1.69	2.2	2.2	2.4	2.6	0.0
New Zealand	3.18	3.4	3.5	3.6	3.7	3.9

Sources: NAB Global Markets Research; Bloomberg; ABS

Global GDP

Dec year	2013	2014	2015	2016	20 Yr Avge
Australia	2.1	2.7	2.6	3.0	3.4
US	2.2	2.4	2.3	2.6	2.6
Eurozone	-0.4	0.9	1.4	1.8	1.5
UK	1.7	3.0	2.6	2.4	2.4
Japan	1.6	-0.1	0.9	1.2	0.8
China	7.7	7.4	7.1	6.9	9.2
India	6.4	7.1	7.6	7.6	6.6
New Zealand	2.2	3.3	2.4	2.2	3.0
World	3.3	3.3	3.2	3.3	3.5

Commodity prices (\$US)

	24-Aug	Sep-15	Dec-15	Jun-16	Dec-16
WTI oil	40.06	55	60	65	70
Gold	1162	1150	1100	1060	1060
Iron ore	56	60	61	58	54
Hard cok. coal	112	98	95	93	97
Thermal coal	62	68	68	62	62
Copper	5063	6080	6260	6200	6170
Japan LNG	8.4	11.0	11.0	11.0	11.0

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