

CONFIDENTIAL
MEMORANDUM

26 January 2009

THE MINISTER OF FINANCE

Cc: Hon. Prime Minister
Deputy Prime Minister
Members of the CBS Board
CEO, Foreign Affairs and Trade
CEO, Commerce, Industry and Labour

EXCHANGE RATES DEVELOPMENTS IN
DECEMBER 2008

A. OVERVIEW

The **US dollar** was less aggressive in December as ‘talks’ of bailing out automakers in the US helped revive confidence in the equity markets, while reducing the need for safe haven currencies like the Greenback. Economic fundamentals in the US remain bleak and in an effort to revive the economy, the Fed slashed its 1.0 percent Federal funds rate by 75 basis points to 0.25 percent.

The **Yen**, likewise, gained much ground over the month as weak global economic statistics continued to weaken equity market performances and risk appetite, while increasing demand for safe currencies like the Yen. Economic statistics out of Japan were also weak and this led the BOJ to cut its official interest rate from 0.3 to 0.1 percent.

The **Euro** was weak earlier in the month but it turned around completely by the end of December having gained much support from the Greenback’s decline coupled with some positive movements in the equity markets. The ECB lowered its repo rate by 75 basis points to 2.5 percent.

The **Australian dollar**, likewise, started the month modest but with bouts of recovering equity markets, higher commodity prices coupled with the US dollar’s decline, the AUD was able to pull itself up. The RBA slashed its cash rate by 100 basis points, from 5.25 to 4.25 percent.

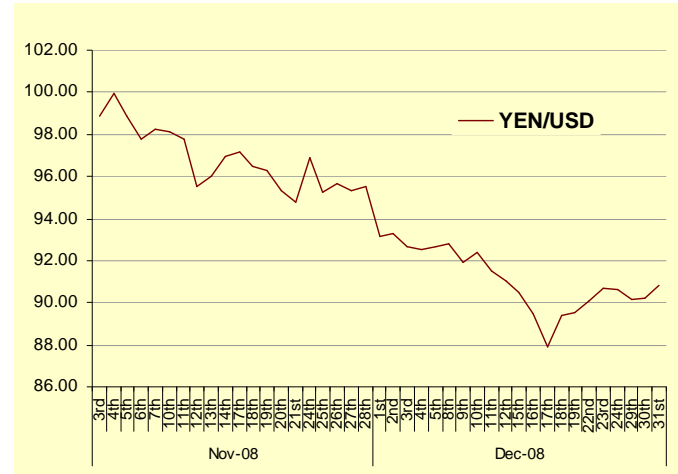
The **New Zealand dollar** also weakened over the month as a result of the equity markets’ volatile movements but the US dollar’s decline, high commodity prices coupled with periods of recovery in the equity markets helped lift the Kiwi. The RBNZ also slashed its OCR by 150 basis points from 6.5 to 5.0 percent.

In December 2008, the **Tala** strengthened against the **USD** but it weakened against the **NZD**, **AUD** and the **EURO**. The Tala also fell against the **YEN** and the **FJD**.

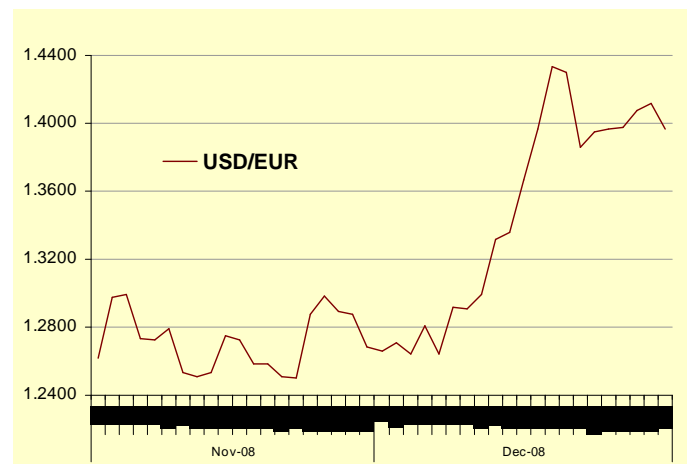
B. CURRENCY WATCH

The *US dollar* was fairly strong in early December as equity markets volatility continued amid fears of a deepening global slowdown, which led investors to seek safety in risk-free US dollar assets. Despite efforts by Central banks across the globe to stem the economic slump by lowering their key interest rates, weak economic statistics out of the US continued to dominate the equity markets' movements. The dollar's steady rise was later stalled by talks of an imminent bailout deal for US carmakers. As expected, equity markets received a boost from such news and it consequently led to a decline in demand for safe haven currencies. The Greenback fell further after the Fed slashed its Fed funds rate from 1.0 percent to 0.25 percent. However, it rebounded on the market's view that the US dollar's decline was too big to sustain. The BOJ rate cut also helped support the US dollar. Gains to the currency were reversed after conflict in Israel also raised fears that the geopolitical conflict with Gaza may disrupt the supply of crude oil to the US. The Greenback finally closed the month on a weak note compared to the previous month.

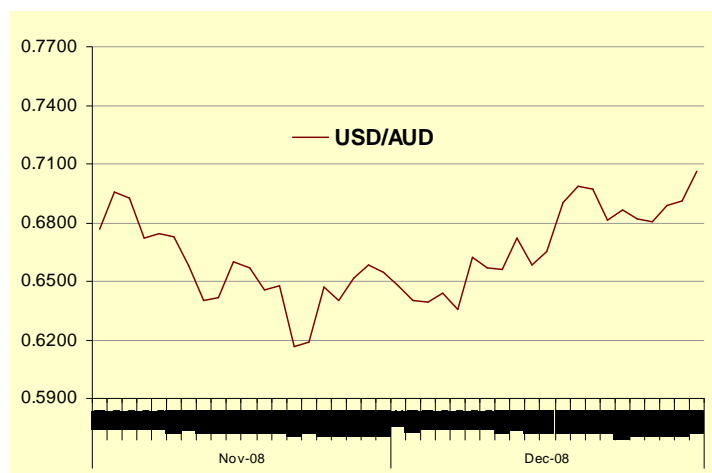
The *Japanese Yen* opened the month at Yen93.17 and like the Greenback, it gained support from the ongoing volatility in equity markets, which prompted investors to unwind their risky carry trades in favor of risk-free or 'safe' currencies like the Yen and the US dollar. The Yen's trade was mostly directed by the equity markets, which at the time were still fairly unstable and thus contributed to investors being highly risk averse. The Yen continued to strengthen to Yen91 until talks of a plan to bail out automakers in the US sparked a rally in global equity markets and weakened the Yen back to Yen92. Nevertheless, the Yen steadily climbed the ladder to Yen89 until eventually it peaked at Yen87.88 after the Fed slashed its interest rate, making it the lowest yielding currency among the industrialized nations. The Yen fell to Yen89 after the GDP report showed the Japanese economy shrank in the September quarter by an annualized rate of 1.8 percent. The BOJ rate cut from 0.3 percent to 0.1 percent weakened the currency further to Yen90. Despite being weaker, the Yen was still relatively stronger compared to earlier in the month. The Yen closed the month at Yen90.84.



The *Euro* opened the month at US\$1.2662, slightly weaker from the previous month as the Greenback persisted higher on demand for safe haven currencies. The Euro was see-sawing between US\$1.26 and US\$1.27 as it sought to find steady ground against the resilient US dollar. The Euro rose to US\$1.2812 after the ECB lowered its official interest rate from 3.25 percent to 2.5 percent to boost growth, but gains were brief as the stronger Greenback pressured it down to US\$1.2638. The Euro rebounded to US\$1.2919 after bailout talks for US automakers boosted stocks and the ensuing global equity market rally revived investors' appetite for risk. The Euro steadily rose to US\$1.3357 and then to US\$1.3968 and finally peaked at US\$1.4337 after the Fed rate cut to near zero percent. The Euro came off its highs after currency traders reversed their bets on the view that the US dollar's decline was overdone and this saw the Euro weaken back to US\$1.39. Fresh declines in the Greenback following tensions in the middle-East saw the Euro recover to US\$1.41 before closing the month at US\$1.3966.



The *Australian dollar* opened the month slightly weaker from the previous month but it was well supported at US\$0.6478 after the RBA reduced its cash rate to 4.24 percent in a bid to head off the impact of slower world economic growth on an already slowing Australian economy. The strengthening of the Greenback amid ongoing volatility in the global equity markets saw the Aussie currency trade down to US\$0.6397. It then rose to US\$0.6621 following a strong rally in world stock markets, which was set off by talks of a bailout plan for the US automakers. The Aussie unit held steady near US\$0.66 for a short time as equity markets stabilized and commodity prices rose. The Aussie dollar hiked further up to US\$0.69 following the Fed's 75 basis points rate cut but it gave up some of its gains and was set back to US\$0.68 as the Greenback rebounded on the markets' self-correction of a US dollar sell-off that was speculated to be overdone. Renewed weakness in the US dollar amid tensions in the Middle-East supported the Australian dollar until it closed the month at US\$0.7062.



The *New Zealand dollar* opened the month at US\$0.5363. It steadily fell to US\$0.5274 on weak domestic data coupled with the strengthening of the Greenback amid ongoing volatility in global equity markets. The Kiwi was tugged lower to US\$0.5258 by more weak US data, which fuelled investors' fear of a deepening global slowdown and accelerated investors' flight out of risky carry trades. The Kiwi showed little reaction to the RBNZ's 150 basis points OCR reduction to 5.0 percent. The NZ dollar then recovered to US\$0.5443 as bailout plans for the US carmakers gave a boost to equity markets across the globe. The Kiwi strengthened further to US\$0.55 and finally to US\$0.57 after the Fed reduced its key interest rate to almost zero percent. The currency continued to

capitalize on the Greenback's decline following the rate cut so that it climbed as high as US\$0.59 before it fell back to US\$0.57 on a rebound in the US dollar. In the lead up to the Christmas holidays trading in the Kiwi was quiet and so it held steady at US\$0.57 before closing the month slightly stronger at US\$0.5856 as the Greenback fell due to fears that the conflicts in the Mid-East may disrupt crude oil supply.

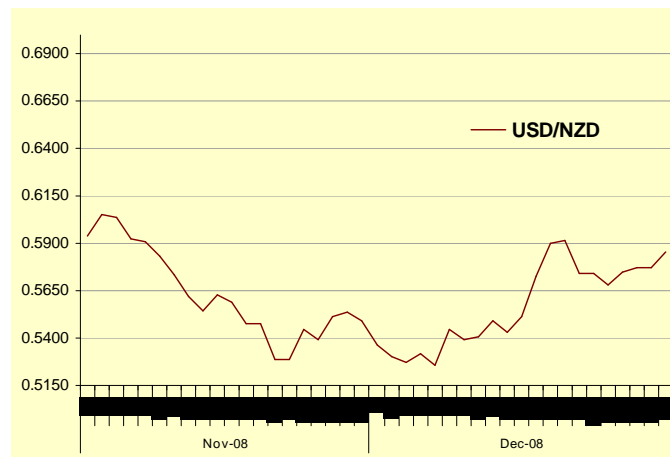


Table 1 shows the movements of the currencies in our currency basket against the US dollar at end December 2008, compared to the previous month and December 2007.

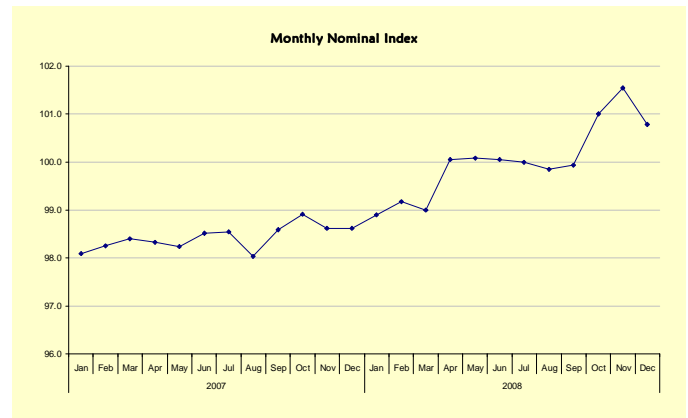
Table 1					
USD per other currencies (end period)					
	Movement of other currencies against the USD				
	(+) appreciation / (-) depreciation				
	Dec-07	Nov-08	Dec-08	Dec-07	Nov-08
				(%)	(%)
USD/NZD	0.7643	0.5490	0.5856	-23.38	6.67
USD/AUD	0.8752	0.6546	0.7062	-19.31	7.88
YEN/USD	111.51	95.56	90.85	18.53	4.93
USD/EUR	1.4581	1.2685	1.3966	-4.22	10.10
USD/FJD	0.6422	0.5469	0.5691	-11.38	4.06

At end December 2008, the Greenback weakened against all the currencies in the basket when compared to the previous month. The US dollar also weakened against the FJD and the YEN from the previous month.

C. EFFECT ON THE TALA

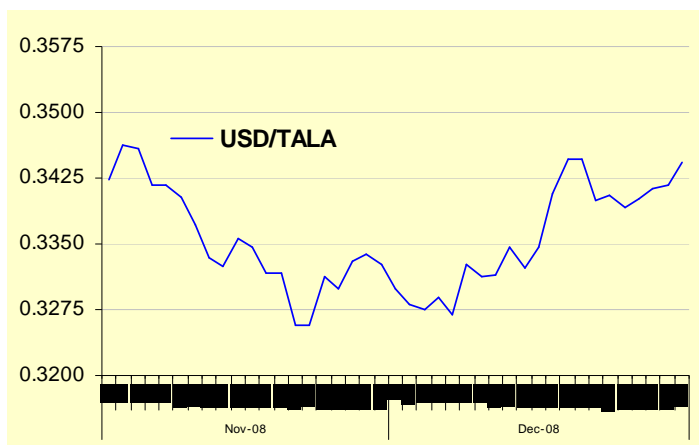
Compared to end December 2007 and the previous month, Table 2 shows the movement of the Tala at end December 2008 against the currencies in our currency basket as well as its movement against the FJD and the YEN.

Table 2					
Tala per foreign currencies (end period)					
	Dec-07	Nov-08	Dec-08	Movement of the Tala	
				(+ appreciation / (-) depreciation	
				Dec-07 (%)	Nov-08 (%)
TALA/USD	2.5580	3.0061	2.9043	-13.54	3.39
TALA/NZD	1.9549	1.6504	1.7007	13.00	-3.05
TALA/AUD	2.2387	1.9677	2.0509	8.39	-4.23
TALA/EUR	3.7298	3.8133	4.0561	-8.75	-6.37
TALA/FJD	1.6427	1.6439	1.6528	-0.62	-0.54
YEN/TALA	43.593	31.7869	31.2798	-28.25	-1.60
Nominal Index	98.62	101.54	100.79	2.20	-0.74



At end December 2008, the Tala strengthened against the USD but it weakened against the NZD, AUD and the EURO from the previous month. The Tala also fell against the YEN and the FJD when compared to the previous month.

In terms of the *Nominal Index*, the Tala depreciated by 0.74 percent at end December 2008 from the previous month. (See Table 2)

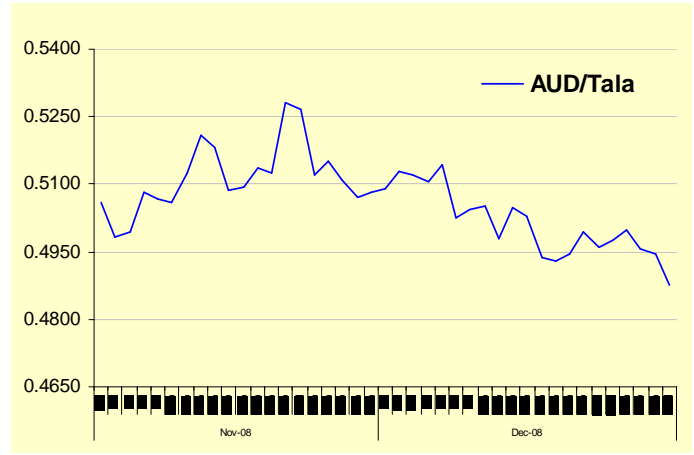
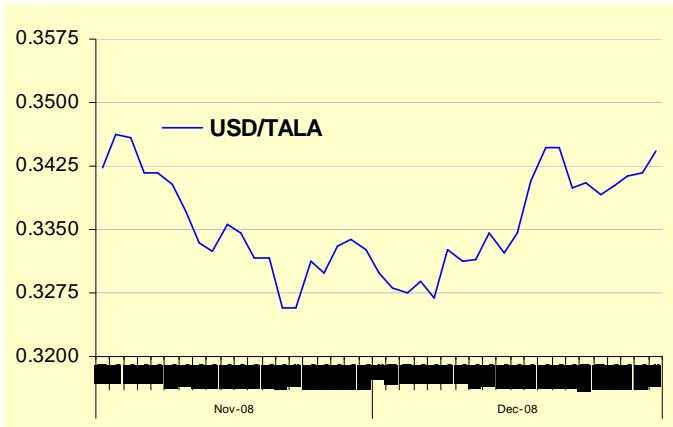


The Tala opened the month at US\$0.3298, slightly weaker from the previous month's close. The Tala was at US\$0.32 in the first week although it was somewhat volatile. The second week saw the Tala strengthen to levels above US\$0.33 as the New Zealand, Australian and Euro currencies strengthened against the Greenback. In the latter weeks of the month, the Tala was mostly trading at levels above US\$0.34 during when the Greenback was mostly weak. The Tala closed the month at US\$0.3443.

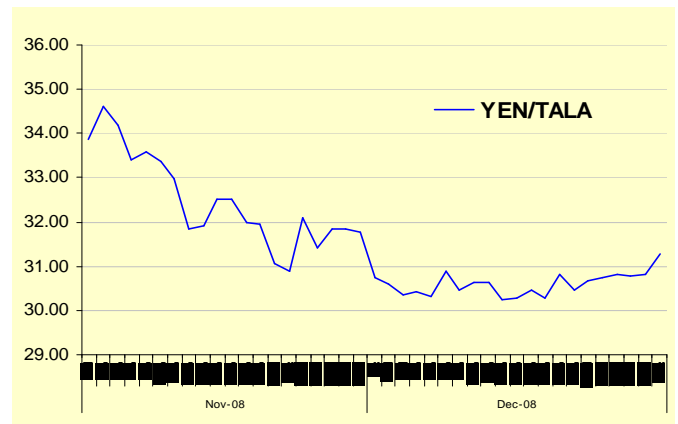
**Leasi P T Scanlan
Governor**

TALA GRAPHS

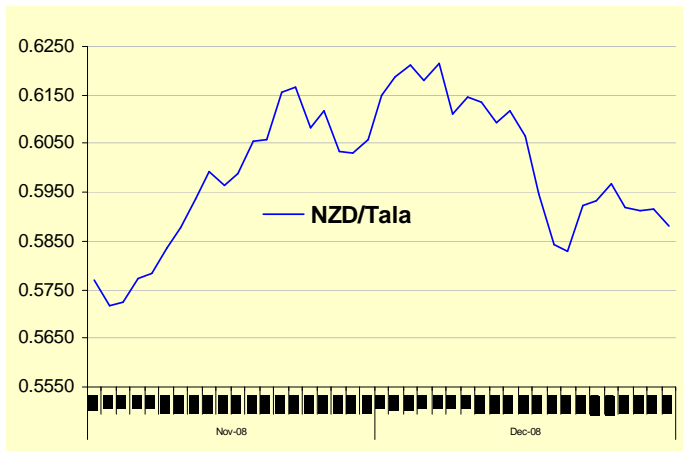
USD/TALA



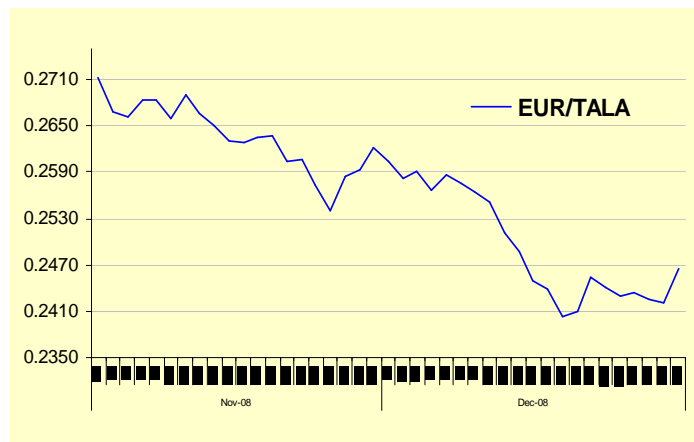
YEN/TALA



NZD/TALA



EUR/TALA



AUD/TALA

FJD/TALA

