MNI RBNZ Preview – November 2020

Meeting Dates: Wednesday, 11 November

Statement Release Time: 14:00 NZST/01:00 GMT

Link To Statement: https://www.rbnz.govt.nz/monetary-policy/official-cash-rate-decisions

Link To MPS: https://www.rbnz.govt.nz/monetary-policy/monetary-policy-statement

Press Conference: 15:00 NZST/02:00 GMT

Link To Live Stream Of Press Conference: https://www.rbnz.govt.nz/research-and-publications/webcasts

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Central Bank Watch - RBNZ

MNI RBNZ Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
CPI (Q)	% y/y	1.4	1.5	↓	2.5	↓					-0.93
House Prices	% y/y	7.1	7.7	↓	5.3	↑					0.44
RBNZ Inflation Exp (Q)	% y/y	1.43	1.24	↑	1.93	↓					-1.21
Inflation Breakeven 10Yr	%	0.72	0.47	↑	0.70	↑					0.46
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
ISM	Index	54.0	56.3	↓	38.1	↑					0.61
GDP (Q)	% m/m	-12.4	-0.1	↓	1.8	↓					-2.42
Trade Balance	% m/m	-1017	473	↓	726	↓					-1.86
Exports	K	4005	5082	↓	5815	↓					-1.73
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Credit Card Sending (Retail)	bps	8.8	4.7	↑	-49.2	↑					0.33
House Sales	Index	37.1	10.9	↑	-1.0	↑					0.96
Terms of Trade (Q)	$bn	2.5	-0.6	↑	2.7	↓					0.94
Commodity Prices	K	1.9	2.9	↓	-1.1	↑					1.05
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales (Q)	% m/m	-14.6	-1.2	↓	0.4	↓					-4.56
Consumer Confidence	Index	108.7	104.3	↑	84.8	↑					1.07
Employment Change (Q)	K	-0.8	-0.3	↓	1.1	↓					-1.62
Ave Hourly Earnings (Q)	% y/y	1.4	0.4	↑	1.4	→					1.08
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Equity Market	Index	12635	11728	↑	10532	↑					1.02
NZ 10-Year Yield	%	0.59	0.73	↓	0.84	↓					-1.02
NZ Yield Curve (2s-10s)	bps	52.5	46.3	↑	71.0	↓					-0.66
NZD TWI	Index	72.71	72.47	↑	69.24	↑					0.52

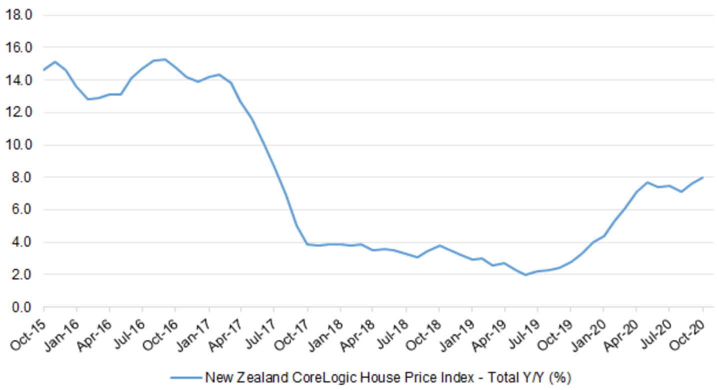
Note: For quarterly data the 3m ago column will display the previous data point and the 6m ago column will display the data point prior to that.
Source: MNI, Bloomberg

MNI POV (Point Of View): Expanding The Toolkit

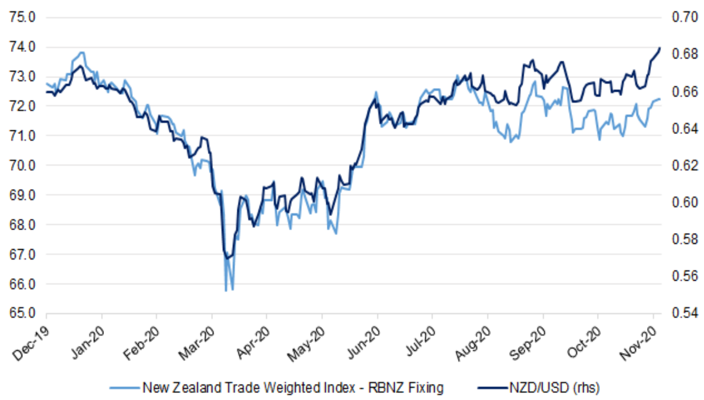
The RBNZ set the scene for the launch of a Funding for Lending Programme (FLP) by the turn of the year. With main policy parameters widely expected to stay unchanged, the details of the new tool will take centre stage. Elsewhere, it will be more about rhetoric than policy. Given the RBNZ's explicit commitment to a "least regrets" approach, we should hear a reiteration of readiness to add stimulus if needed to sustain economic recovery, despite what has been a string of generally positive data signals.

The picture painted by the economic data released since the last Monetary Policy Review reflects a relatively healthy performance of New Zealand's economy, relative to the difficult and highly uncertain conditions. Unemployment crept higher to 5.3% in Q3, but that uptick fell in line with market expectations and was significantly more modest than the 7.0% forecast by the RBNZ. Admittedly, consumer price inflation proved somewhat more sluggish than projected, but the RBNZ's preferred metric of core inflation (sectoral factor model) remained unchanged, while the impressive pace of the rebound in house prices has taken virtually everyone by surprise.

In fact, the scale of house price inflation has been so large that it has become a source of worry and the MPC may address this concern on Wednesday. CoreLogic House Price Index is now rising at its fastest pace since mid-2017, while REINZ House Price Index sits at a record high. Worth noting that the RBNZ sees house prices as one of the chief monetary policy transmission channels and per its forecasting models, such an overshoot bodes well for consumption and hence broader economic outlook. On the other hand, there is mounting concern over an inflating housing market bubble and in a recent speech to an INFINZ conference, RBNZ Governor Orr noted that policymakers are "looking at" the possibility of re-introducing loan to value ratio (LVR) lifted in May.



A sense of worry over rallying house prices has been clearly communicated by the government too. In the lead-up to Wednesday's decision, Prime Minister Ardern told reporters that domestic housing market is "under [upward] pressure". Elsewhere, Finance Minister Robertson revealed that he brought forward his meeting with RBNZ Governor Orr and deflected reporters' questions on whether he intended to argue for the re-introduction of LVRs. In addition, affordable housing remains one of the core – and unfulfilled – pledges of the Labour Government. This is not to insinuate any attempts at undermining the central bank's independence, but the combination of ongoing, open dialogue between fiscal and monetary authorities with mutual concern over elevated house prices may prompt the MPC to at least express its lack of comfort and gesture towards potential macroprudential measures.



Whereas the RBNZ would certainly prefer to see a lower exchange rate, the NZD does not seem to be out of line with fundamentals. Although NZD/USD has been printing fresh multi-month highs recently, its move has been underpinned by USD weakness vs. a basket of currencies. These include AUD and CNY, the two largest contributors (with a combined weight of ~42%) to the RBNZ's Trade Weighted Index. Accordingly, in TWI terms, the NZD has traded sideways and close to the forecast included in the August MPS. That being said, it would be reasonable for the RBNZ to refrain from ruling out foreign asset purchases. Suggesting that this option remains on the table would allow the MPC to place a bumper ahead of the NZD ahead of the three-month hiatus before the next monetary policy meeting.

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The case for lowering the OCR or boosting the LSAP programme is weak. There would be little benefit for the RBNZ in breaking the promise to keep the OCR at 0.25% through March 2020. Meanwhile, relatively upbeat performance of domestic economy has allowed national coffers to allow excessive depletion. The Treasury's most recent financial statements, covering the three months through September 31, revealed that the tax take topped forecasts, while expenses were smaller than projected owing to the lower than expected take-up of the Wage Subsidy Scheme – a function of labour market performance. The condition of the government's books reduces the need to increase borrowing and thus for the RBNZ to boost asset purchases, especially with the current size of the LSAP.

In the absence of changes to the OCR and LSAP parameters, the highlight of this MPS will be the publication of details of the upcoming FLP. At the last Monetary Policy Review, policymakers expressed preference for launching the programme by the year-end and directed staff to make appropriate preparations. The MPS will be a perfect occasion to disclose the exact date when it is going to be rolled out. Aforementioned concern with the pace of house price inflation could see policymakers tailor the FLP to promote lending to businesses rather than the general public, which could further fuel the booming housing market. A targeted FLP could come in the form of either a hard constraint on access to the facility or conditionality attached to the amount of funding available under the scheme. Although simplicity of design could initially translate into larger take-up and prove more effective, there is a chance that the FLP will come in a more targeted form.

All in all, Wednesday's MPS should boil down to the presentation of the design and details of the FLP, any hints regarding the proximity of negative interest rates and, perhaps, commentary on the house price conundrum. New Zealand's booming housing market may (but does not have to) result in the implementation of a more business-targeted form of FLP. Other than that, MPC members have all reasons to leave policy settings unchanged. Despite occasional hiccups, the performance of New Zealand's economy has been solid, though of course in relative terms. Persistently difficult conditions, highly uncertain outlook and the RBNZ's "least regrets" approach will likely result in rhetoric underscoring the Bank's readiness to add stimulus if needed.

RBNZ September Interim Monetary Policy Review

The Monetary Policy Committee agreed to continue with the Large Scale Asset Purchase (LSAP) Programme up to $100 billion. This action is necessary to further lower household and business borrowing rates in order to achieve the Committee's inflation and employment remit. The Official Cash Rate (OCR) is being held at 0.25 percent in accordance with the guidance issued on 16 March.

Reflecting the possible need for further monetary stimulus, the Committee noted the progress being made on the Bank's ability to deploy additional monetary instruments. The instruments include a Funding for Lending Programme (FLP), a negative OCR, and purchases of foreign assets. The Committee agreed that these instruments can be mutually supportive in bolstering economic activity. Members also agreed that the alternative instruments can be deployed independently, and noted that the FLP would be ready before the end of this calendar year.

Economic information available since the August *Monetary Policy Statement*, both international and domestic, has confirmed the level of economic activity remains significantly below that experienced prior to the COVID-19 economic disruption. The ongoing virus-led activity restrictions – most notably in Auckland – had also continued to dampen economic activity, and business and consumer confidence.

Any significant change in the global and domestic economic outlook remain dependent on the containment of the virus, which is highly uncertain. International border restrictions will continue to significantly curtail migration and tourism, and lead to the activity outlook being uneven across industries and regions. Commodity prices for New Zealand's exports remain robust, but this has been partly offset by the New Zealand dollar exchange rate moderating the return to local export producers.

Ongoing support for domestic economic activity is being provided through significant government spending on business assistance and household income support. This will be accompanied by a rising level of government investment. However, the removal of temporary support policies has commenced. For example, the Wage Subsidy scheme is now closed to new entrants.

In line with the weak underlying international and domestic economic conditions, the Committee expects a rise in unemployment and an increase in firm closures, as resource reallocation continues. Members agreed that monetary policy will need to provide significant economic support for a long time to come to meet the inflation and employment remit, and promote financial stability. They also agreed they are prepared to provide additional stimulus.

Summary record of meeting

The Monetary Policy Committee discussed international and domestic economic and financial market developments. The Committee noted that global economic activity had increased in recent months as social restrictions in some regions had eased, and that the consensus outlook was for a partial recovery in the level of economic activity. Members agreed that the balance of risks to the global economic outlook remained to the downside. The Committee noted that cases of COVID-19 were growing and social restrictions were being reintroduced in some regions of the world, including some areas where the virus had previously appeared to have been reasonably well contained. Members noted that while global monetary and fiscal easing has supported financial and economic conditions, there was a risk that the recent recovery in international activity could stall or reverse if policy stimulus was withdrawn prematurely.

The Committee noted that the August outbreak of COVID-19 in New Zealand appeared to now be contained. Restrictions imposed to contain the virus had constrained economic activity, but were being relaxed. Some members observed that the outbreak had dented confidence, as firms and households are wary of a future outbreak with a subsequent reduction in activity and spending.

The Committee noted the historically unprecedented contraction in economic activity in the June quarter, as measured by the national accounts. The size of the contraction had been smaller than earlier expectations. The Committee noted that some more timely measures of activity had recovered quickly following the easing of restrictions after the initial lockdown, but had dipped again as restrictions were re-introduced, particularly in Auckland. The Committee agreed that the pandemic and associated travel restrictions could have a significant long-term negative impact on the economy, with lower potential growth as resources were gradually redeployed within and between industries. Some members noted that it is also harder to estimate what the maximum sustainable level of employment is under these conditions.

The Committee discussed the recent strength in the housing market. House prices had risen over recent months, in contrast to the Reserve Bank's baseline scenario which had assumed a decline. Some members noted that economic activity in New Zealand has historically been closely correlated with changes in household wealth, and that a stronger housing market may indicate a stronger recovery in consumer spending and residential construction if sustained. However, other members noted that low population growth and rising unemployment are expected to constrain further house price increases.

Members agreed that the outlook for inflation and employment remained subdued. Members discussed the balance of risks, and agreed that they remained to the downside. There is substantial uncertainty about the future spread of COVID-19 both domestically and globally, and how economic, health, and social activity will adapt.

The Committee discussed the effects of monetary policy easing measures taken so far. Members agreed that the reductions in the OCR, forward guidance, and Large Scale Asset Purchase (LSAP) programme had contributed to lower wholesale, household, and business interest rates, and had kept the exchange rate lower than otherwise. Members noted that the expansion and front-loading of the LSAP programme after the August *Statement* had contributed to lower government bond yields. They also noted that market participants now believed that it was likely the OCR would be reduced below zero next year, and that this had also contributed to lower wholesale interest rates. The Committee expected lenders to continue to pass through these reductions in wholesale rates to household and business borrowing rates over time.

The Committee reaffirmed that a Funding for Lending Programme (FLP), a lower or negative OCR, purchases of foreign assets, and interest rate swaps remain under consideration. The Committee maintained its view as expressed in the August *Statement* that a package of an FLP and a lower or negative OCR could provide an effective way to deliver additional monetary stimulus.

The Committee discussed the sequencing of deployment of the components of the package. Members noted staff advice that deploying an FLP before the forward guidance period for holding the OCR ends could provide additional stimulus to the economy sooner. Having an FLP in place earlier would provide certainty to financial institutions planning their funding needs, and speed up the transmission of the programme by allowing banks to replace funding as it matures over time.

The Committee agreed that providing term funding at rates near the OCR via an FLP would lower the financial system's funding costs, and therefore borrowing costs for firms and households, and support the availability of credit to the economy. The effectiveness of the programme would be influenced by the degree to which financial institutions passed on their funding cost declines to their customers. Members agreed that they preferred to launch an FLP before the end of 2020.

The Committee noted that the banking system is on track to be operationally prepared for negative interest rates by year end. Members agreed with the previous assessment that a lower OCR would be complementary to its other monetary policy tools, and that it was prepared to lower the OCR to provide additional stimulus if required.

The Committee endorsed staff advice to continue front-loading purchases under the LSAP programme, while maintaining flexibility to adjust purchases as market conditions dictate.

The Committee discussed the appropriate settings for monetary policy. It agreed that further monetary stimulus may be needed in order to achieve its remit objectives. The Committee agreed that a severe and prolonged economic downturn would make it difficult to achieve its inflation and employment objectives, and at the same time would pose a material risk to financial stability. Providing sufficient monetary stimulus would therefore both help achieve the Committee's remit objectives, and promote financial stability.

On Wednesday 23 September, the Committee reached a consensus to:

- hold the OCR at 0.25 percent, in accordance with the guidance issued on 16 March;
- maintain the existing LSAP programme of a maximum of $100b by June 2022; and
- direct the Bank to prepare to have an FLP ready to deploy before the end of this calendar year. Details on the design of the programme would be agreed and published ahead of deployment.

RBNZ August Monetary Policy Statement – Key Variables Under The Baseline Scenario

Key baseline scenario variables

		GDP growth Quarterly	CPI inflation Quarterly	CPI inflation Annual	TWI	OCR
2018	Mar	0.7	0.5	1.1	74.9	1.8
	Jun	1.0	0.4	1.5	73.7	1.8
	Sep	0.5	0.9	1.9	72.4	1.8
	Dec	1.0	0.1	1.9	73.4	1.8
2019	Mar	0.4	0.1	1.5	74.0	1.8
	Jun	0.1	0.6	1.7	72.6	1.6
	Sep	0.8	0.7	1.5	72.0	1.2
	Dec	0.5	0.5	1.9	71.3	1.0
2020	Mar	-1.6	0.8	2.5	70.9	0.9
	Jun	**-14.3**	-0.5	1.5	69.7	0.3
	Sep	**12.2**	**1.1**	**1.8**	**72.3**	**0.3**
	Dec	**1.9**	**0.0**	**1.3**	**72.2**	**0.3**
2021	Mar	**0.4**	**-0.2**	**0.4**	**72.2**	**0.3**
	Jun	**1.2**	**0.1**	**1.0**	**72.2**	
	Sep	**0.9**	**0.4**	**0.3**	**72.2**	
	Dec	**0.5**	**0.0**	**0.3**	**72.2**	
2022	Mar	**1.8**	**0.3**	**0.8**	**72.2**	
	Jun	**0.7**	**0.2**	**0.9**	**72.2**	
	Sep	**0.4**	**0.6**	**1.0**	**72.2**	
	Dec	**0.8**	**0.2**	**1.2**	**72.2**	
2023	Mar	**0.4**	**0.6**	**1.5**	**72.1**	
	Jun	**0.5**	**0.5**	**1.8**	**72.1**	
	Sep	**0.4**	**0.7**	**2.0**	**72.1**	

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Analyst Views - Summary

- The RBNZ is expected to leave its OCR and LSAP settings unchanged.
- The main focus will fall on the details of the Funding for Lending Programme (FLP), expected to be announced at the upcoming MPS and rolled out by the turn of the year.
- Forecasts of the size of the FLP in those among those of the following sell-side previews which mention a specific figure vary between NZ$10bn and NZ$50bn, with most guesses falling around NZ$30bn.
- It is likely that policymakers will take note of the unexpected pace of increase in house prices.
- Forward guidance will receive scrutiny, with eyes on any hints on the future OCR track in the light of existing pledge not to change the main policy rate until March 2021.

Sell-Side Analyst Views

ANZ

- The focus of next week's Monetary Policy Statement will be the upcoming Funding for Lending (FLP) programme, including design details and deployment date. We expect the programme to have relatively few strings attached in order to facilitate take-up, and to be priced at or near the OCR. Our best guess is that the programme might be $30-50bn in size. We do not expect any changes to the OCR or the LSAP (QE) programme. The market will also be looking for further comments on the likelihood of a negative OCR and to see if the OCR forecast track is extended beyond the end of existing forward guidance (ie Q1 2021).
- We expect the RBNZ to continue to dodge extending the forecasts until the February MPS, as it is very likely to be misconstrued as either a firm commitment to, or a ruling out of, a negative OCR. We expect the RBNZ to reaffirm its forward guidance that the OCR will not be lowered before mid-March. Nonetheless, on balance we still think that a negative OCR is more likely than not, given the balance of risks.
- As regards to the economic forecasts and the tone of the document, there were strong hints in the Governor's recent public comments that they will not be putting a great deal of weight on the more positive recent data flow, but rather remain firmly focused on the medium-term and the sub-par outlook for both inflation and employment. However, one forecast they will definitely have to revise up is house prices. The subject of macroprudential mortgage restrictions is likely to come up in the press conference.
- The market will be keenly interested in the size of the LSAP program. We do not expect a change, with the focus rather on the FLP. Our central scenario is that the LSAP remains at $100m through until 30 June 2022. If there is a tweak, the risks are tilted towards a larger programme with an extended end date.
- Finally, the market will be interested in any comments about the possibility of foreign asset purchases. We do not expect such purchases to ever actually happen, but there's no advantage to the RBNZ in ruling it out. The small size of the NZGB market has always been a limiting factor for QE, and the exchange rate matters for New Zealand more than it does elsewhere. Keeping this option on the table will not only underscore the Bank's erstwhile commitment to do what it takes, but it will get noticed by FX markets.

ASB

- Most of focus in the November Monetary Policy Statement (MPS) will be the release of key design elements on the Funding for Lending Programme (FLP), which looks set to be launched before the end of the year. Its size and design will have a key bearing on its take-up and effectiveness in lowering borrowing costs and stimulating the economy. We expect the FLP to be operational before the end of the year, to be sizeable (in the region of $30bn), longer-term (3-5 years), offer attractive rates to banks (possibly a floating rate capped at current OCR) and to offer sweeteners to entice more take-up for business/SME lending. We also expect the FLP will include features that will make it effective to operate in a negative OCR environment.
- Elsewhere, we don't expect the RBNZ to markedly shift the tone from recent policy announcements, with the Bank to maintain its broad policy parameters. It will likely hold the OCR at 0.25% and reaffirm the March 16 guidance (on hold until March 2021) and will maintain its $100bn Large Scale Asset Purchase (LSAP) package. The published projections are expected to adhere to recent RBNZ practice and not publish the OCR beyond the March 2021 quarter (0.25%). Moreover, we expect the RBNZ to signal the intent to increase policy accommodation and keep other policy options on the table, including pushing the OCR below zero after the period of forward guidance expires. The message for banks will be: be prepared.

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- We also expect the RBNZ to downplay potential (short-term) upside risks to the outlook, but to focus on more (predominantly downside) medium-term risks. The NZ economy and labour market have held up much better than expected, the domestic economy has shown signs of life, the housing market is going gangbusters, and sentiment measures are well above early 2020 lows. However, uncertainty is still pronounced and with fiscal tailwinds set to abate this improvement could easily stall. The global outlook is tenuous with COVID-19 headwinds arguably getting stronger. NZ's border restrictions may have helped contain the spread of the virus here but will pose more of an economic headwind going forward.
- Our current view is that the RBNZ will move the OCR below zero in April, although the timing and extent of OCR moves will depend on the effectiveness in the FLP in supporting the economy, the impact and duration of COVID-19 and the path of the NZ and global economies, all of which remain highly uncertain.

Barclays

- We expect the RBNZ to maintain its cash rate at 0.25% and the LSAP programme at NZD100bn. We also think the bank is likely to deploy the Funding for Lending program (term lending for banks at near OCR levels) at this meeting, before taking the OCR negative in April 2021.

BNZ

- In addition to rates, we have another suite of possible policy measures to ponder any or all of which could be drawn upon in the 11 November Monetary Policy Statement. At the top of the list for the upcoming MPS are details on the Funding for Lending Programme, an update on the Large Scale Asset Programme and any information that the RBNZ might provide on how it might respond to surging house prices.
- Whatever the detail of the MPS, it's best to think of the overarching message the Reserve Bank will want to deliver. In our view that message is likely to be along the lines of: more near-term stimulus will be announced on the day with a clear indication that even more will be required before all is said and done. This will be leveraged off the RBNZ reiterating its message that the achievement of its employment and inflation targets seem beyond reach without further monetary policy assistance.
- In addition, we think the Bank will down play the recent positive developments that we have seen domestically and point, instead, to the medium term risks that remain so pervasive - in particular, the immediate negative impact of the economic restrictions being re-imposed around the globe.
- Indeed, the big news in the November statement will be the detail and introduction date of the Funding for Lending Programme (FLP). This programme will see the RBNZ lending to banks at an interest rate at, or very near to, the cash rate.
- Finally, it will be interesting to see if the RBNZ says anything about the current strength in the housing market. The Bank sees the wealth effect, via rising house prices, being key to the transmission of monetary policy but it is doubtful it will be comfortable with the current pace of house price inflation. The price increases so far will not be enough to deter it from its central course of action but don't be surprised if the Bank fires a warning shot across the bows of the market.

Citi

- The RBNZ is likely to leave the OCR unchanged at 0.25% at its monetary policy meeting on November 11, while introducing the FLP in preparation for negative interest rates next year. We believe the overall message will remain dovish, and, though it's not likely, a rate cut to 0.1% at this week's meeting cannot be ruled out completely.
- With the USD weakening overall currently, we do not expect the RBNZ's dovish stance to lead directly to NZD depreciation. We think NZDUSD can continue to rise towards its 2019 high of around 0.69 in the near term. However, given that the RBNZ retains room for further easing while the RBA has now exhausted its options, our belief is that the rise in NZD will be limited compared with AUD in the medium term.

Goldman Sachs

- Looking to the November meeting, we expect the OCR (0.25%) and LSAP size (NZ$100bn through mid-2022) to remain unchanged. However, we do expect the RBNZ to announce the details around a 'Funding for Lending Programme' (FLP) which provides term funding to banks. As a base case, we expect the programme to extend c.NZ$30bn of funding (~10% of GDP and total credit outstanding) at the prevailing OCR with a term of around 2-3 years. Such a programme would help support bank interest margins, allow a further reduction in retail interest rates over time and aid the transmission of monetary policy – similar to the RBA's TFF and the ECB's TLTROs.

- On the macro forecasts, we expect the key change to be on the unemployment rate, given the 3Q unemployment rate was 170bp below the RBNZ's August forecast and domestic restrictions have largely been removed at this point. We will also be watching closely on the RBNZ's assumptions around a vaccine and the reopening of international borders. Given the macro risks remain skewed to the downside for now, we expect the RBNZ to maintain a very dovish tone overall and continue to highlight the risks of further easing being introduced – including the use of negative policy rates. However, given our more optimistic views around a vaccine and the growth recovery, our base case remains that the OCR will ultimately remain on hold in 2021 although we acknowledge it is a very close call (GSe: 45% probability of negative rates in 2Q2021).

ING

- The Reserve Bank of New Zealand has a solid easing bias in place and will likely deploy the pre-announced Funding for Lending Programme next week to support the banking sector through cheap loans. We don't expect a cut at this meeting and markets are also not pricing any rate adjustment. The key driver of the market reaction is going to be the language used by Governor Orr around the prospect of negative rates in the coming months. Unless there is a clear timing provided or an even more explicit pledge to cut rates further, a reiteration of the same rhetoric we saw recently by the RBNZ (that the negative rates under serious consideration) should not shock a market that is largely pricing in NIRP in 2021.

J.P. Morgan

- The RBNZ is broadly expected to leave the OCR on hold at next week's meeting, but to ease via the new bank funding for lending (FFL) scheme flagged at previous meetings. It announced plans for the scheme in August as part of a policy package including a negative OCR. Since that meeting, the RBNZ has been conducting many public, town-hall-style speeches to get the public comfortable with negative rates.
- The pricing of the FFL facility will be important as it relates to the specifics for negative rates, and funding spreads. The package flagged in August "includes a negative OCR sup- ported by funding retail banks directly at near-OCR." As the package approach suggests, the measures are interrelated. The point of FFL, and indeed tiering, is to keep banks profitable despite having to hold NZ$100bn of reserves at a negative OCR, which would otherwise eliminate the entire return on their assets, and constrain credit creation.
- The language so far suggests that while the facility will be markedly cheaper than current market or deposit funding, its cost will not be as low as the OCR. We continue to think it is politically unpalatable for the RBNZ to fund banks at a negative rate, and the decision to bring forward the FFL suggests a hope that take-up can occur at 0.25%, before the OCR goes negative. We continue to forecast a 50bp cut to the OCR in April.

Kiwibank

- The fragility of the NZ economy remains the number one concern for policymakers. More needs to be done to stimulate the economy in the recovery. This week the RBNZ is due to release its November Monetary Policy Statement. The RBNZ is expected to deliver a funding for lending programme (FLP), to enable banks to lower lending rates further. The RBNZ is unlikely to stop there. We think that the RBNZ will follow through on their quest to go negative next year.
- Whilst an expected announcement of a Funding for Lending program will attract the headlines, from a currency perspective, the market's focus will be on the RBNZ's setup for negative rates in 2021 – if and when? Given what we know and what has been voiced by various RBNZ officials in recent months - a commitment and belief of negative rate effectiveness, we are electing a "play the man/team" rather than a second-guessing approach. This should likely mean that the RBNZ will want to show a dovish enough stance to ensure a rally in currency (and a sell-off in rates) is negated and thus sees a risk of a NZ Dollar decline from Wednesday afternoon.

NZIER

- We are continuing to seek our Shadow Board members' views on whether the Official Cash Rate (OCR) should be negative and if the Reserve Bank should expand its quantitative easing (QE).
- Board members once again saw a reduced need for a negative OCR and further QE over the coming year. The expected implementation of a Funding for Lending programme (FLP) by the Reserve Bank was highlighted by some Board members as an influence on their view about the need for further stimulus. The Reserve Bank has indicated it was likely to implement the programme to offer secure long-term funding at

low interest rates to banks by the end of this year. The aim of the FLP was to reduce borrowing costs for households and businesses in order to encourage them to borrow and invest.

- Shadow Board members continue to highlight the challenges facing New Zealand as it navigates the post-COVID recovery. However, members generally remain sceptical about the effectiveness of a negative OCR to stimulate the economy.

TD Securities

- The NZ economy has held up better than RBNZ f/c's – Q3 u/e 5.3% well below 7% in the Aug MPS and house prices are booming, +10% y/y, vs RBNZ -7% y/y Aug MPS. As such, statement is likely to be less dovish. Stronger economy -> less RBNZ issuance -> need to slow QE purchases cements RBNZ introducing a Funding for Lending Program (FLP) next wk, ~NZ$10-$15b to take slack off QE.

Westpac

- The situation facing the Reserve Bank has changed. The economy has proven far more resilient to Covid-19 than anticipated. The unemployment rate is only 5.3%, not 7% as the RBNZ anticipated. And most importantly, house price inflation will be around 9% this year, whereas the RBNZ was forecasting -7% as recently as August. A sixteen percentage point surprise on the level of house prices is unprecedented, and absolutely must cause the RBNZ to lift its assessment of medium-term inflation and employment.
- Consequently, we anticipate a change in tone from the RBNZ. The RBNZ will still emphasise the downside risks facing the economy. But whereas back in August the RBNZ said that more monetary stimulus was needed, we think that the RBNZ will now say that it intends to provide stimulus for an extended period. The RBNZ will say it needs to keep its foot on the accelerator for a long period, rather than saying it needs to press down harder.
- Consistent with this change of tone, we expect that the RBNZ will lift its Unconstrained OCR forecast. In the past, the RBNZ estimated that monetary stimulus equivalent to an OCR of -2.4% would be required. We expect that the new Unconstrained OCR forecast will be about -1.8%. That is more moderate, but it is still a massive monetary stimulus, for a very long period.
- The medium-term outlook may be looking better for the RBNZ, but it still faces two big conundrums. We think that the solution will be to gradually switch the tools for providing monetary stimulus. We expect the RBNZ will introduce a business-oriented Funding for Lending Programme next week and will cut the OCR below zero next year, while simultaneously slowing the pace of bond purchases under the Long Term Asset Purchase Programme (LSAP).
- Next week is about monetary policy, not financial stability. Therefore there will be no announcement about the reintroduction of loan-to-value restrictions on mortgage lending (LVRs). But there might be hints, because the RBNZ will be very keen to ward off accusations that it is fuelling a housing bubble. We expect that the RBNZ will actually reintroduce LVRs next year. The new LVRs will be effective from 1 May, although they will be announced earlier than that.

MNI Policy Team Insights

MNI PREVIEW: RBNZ To Stand Pat, Boost Lending Facilities

By Lachlan Colquhoun

The Reserve Bank of New Zealand meets Wednesday and is expected to leave its Official Cash Rate unchanged at a record low 0.25%, holding back from a move towards negative rates at this meeting.

The bank said in March that the OCR would remain at 0.25% for "at least a year" and it has asked commercial banks to be ready for negative rates by the end of 2020, with expectations a move into negative rates will likely come in Q1 2021.

The RBNZ is likely to leave the level of quantitative easing unchanged at NZD100 billion, but announce a funding for lending program (FLP), which could be as large as NZD50 billion, around 15% of GDP.

--FUNDING FOR LENDING

In September, the RBNZ repeated its guidance on the OCR but introduced the concept of the FLP, designed to offer low-cost, secured, long-term funding to banks by the end of this calendar year to help commercial banks lower thir rates to customers .

"Having an FLP in place earlier would provide certainty to financial institutions planning their funding needs, and speed up the transmission of the program by allowing banks to replace funding as it matures over time," the RBNZ September statement said.

The RBNZ is also offering low cost funding to banks through a Term Lending Facility (TLF), under which funds are lent to commercial banks at the OCR, but only NZD42 million has been lent to the end of September.

The TLF is slated to run until February 2021. Details on how the TLF differs from the new FLP are expected on Wednesday.

The other pillar of RBNZ policy has been its Large-Scale Asset Purchase (LSAP) of Quantitative Easing, which has committed the bank to purchasing NZD100 billion in NZ Government and some local government debt through June 2022, with the current term giving policymakers more than enough bond buying power for now.