mni

All Signal, No Noise

MARKET ANALYSIS

MNI RBNZ Review – September 2020

Meeting Date: Wednesday, 23 September 2020

Link To Announcement: https://www.rbnz.govt.nz/news/2020/09/prolonged-monetary-support-necessary

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Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

MNI POV (Point Of View): Unpacking The Package

As expected, the RBNZ refrained from any major policy moves at its interim Monetary Policy Review on Wednesday, leaving the OCR and LSAP settings unchanged. The reiteration of the central bank's commitment to its existing forward guidance disappointed some doves, but it was not breaking news. Comments surrounding the exchange rate were uninspiring and roughly repeated communique from the August MPS.

While leaving the size and duration of its LSAP programme unchanged, the MPC endorsed front-loading asset purchases but also reduced their pace, lowering weekly purchase targets to NZ$1.16bn of NZGBs (previously NZ$1.35bn) and NZ$40mn of LGFA bonds (previously NZ$50mn). The decision to moderate the pace of operations was purely reactive, as it came in the wake of the reduction of bond issuance announced by the government.

The central bank retained its dovish bias, flagging readiness to add stimulus if needed amid a highly uncertain outlook and with the balance of risks tilted to the downside. Policymakers tipped hat to an above-forecast GDP print for the second quarter, but stressed that the economic contraction was historically unprecedented. While lack of any greater enthusiasm about the reading may have disappointed some hawks, it was hard to expect a warm reception of the worst recession in history.

The highlight of the RBNZ's announcement was further colour around alternative monetary policy tools under consideration and their sequencing. The MPC had previously suggested that its next tool of preference would be a "package" of a negative OCR and a Funding for Lending Programme (FLP). On Wednesday, policymakers reaffirmed that these tools remain on its menu, alongside foreign assets purchases, but noted that the "alternative instruments can be deployed independently". In addition, the MPC expressed a clear preference for the deployment of an FLP before the year-end and noted that the scheme could be ready by then. Since the turn of the year marks the deadline set for lenders to prepare operationally for negative interest rates, the deployment of an FLP at the November MPS without cutting the OCR is highly likely.

Between the lines, the announcement strongly suggested that the bank is committed to keeping its promise to leave the OCR on hold until mid-March. Much of the discussion of the sequencing of alternative policy tools implied so – from outlining the benefits of deploying an FLP *before* going negative to noting that an FLP *would* be ready by year-end, while the banking system is *on track* to be prepared for negative interest rates by then. For what it's worth, the MPC seemed to not only refrain from altering its forward guidance, but also subtly downplay suggestions to the contrary.

The ramifications of the RBNZ's sequencing strategy are twofold. On one hand, an early deployment of an FLP would better prepare the banking system for a negative interest rate environment, freeing the MPC from certain second thoughts when they choose to go negative. On the other hand, an FLP would by itself provide some additional stimulus, slightly diminishing the urgency to deploy a negative OCR. The decision to set the scene for sequencing the two is rational and enhances the RBNZ's optionality with regards to the timing of negative interest rates after its forward guidance period.

That being said, the MPC made it explicit that it still views the pair of its most preferred additional tools as a package in functional terms. The arduous task of helping New Zealand recover from the current downturn will require action further down the line and at this stage the deployment of negative interest rates, perhaps as soon as in April 2021, looks like all but a done deal.

Wednesday's Monetary Policy Review was expected to be a fairly low-key event. Although the main policy settings remained unchanged, the MPC took the opportunity to reaffirm commitment to its forward guidance and talk us through its thinking on alternative policy tools under preparation. It didn't disclose any details on the design of its FLP, but pledged to unveil them before deploying the programme, which points to an important thing to look out for going forward.

RBNZ September Monetary Policy Review Announcement:

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.

Sell-Side Analyst Views

ANZ

- As expected, the RBNZ left the OCR unchanged at 0.25% and the QE program unchanged at a cap of $100bn today. The RBNZ reiterated again that "The Official Cash Rate (OCR) is being held at 0.25% in accordance with the guidance issued on 16 March." Strictly speaking this isn't a promise to not change its mind, of course, but it's a reminder of their commitment that strongly suggests they do indeed intend to stick to it, as we expected. Further reinforcing the point, the Summary of Meeting also said that "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."
- In our FAQ on a negative OCR and FLP yesterday we noted that introducing a bank Funding for Lending Programme (FLP) before a negative OCR might well be a strategy the RBNZ could choose to pursue. The RBNZ declared that an FLP "would be ready before the end of this calendar year", and that while complementary, an FLP and a negative OCR "can be deployed independently". Indeed, the Summary of Meeting noted that an FLP before the end of the year was "preferred". This sequencing makes sense, if the two policies are not to be introduced simultaneously. A negative OCR without a FLP could be highly detrimental to credit supply, but introducing a FLP even before the OCR is moved should provide banks with certainty that deposit rates can safely be cut further, paving the way for lower lending rates as well.
- The RBNZ has seen little in the data since the August MPS to convince it that it doesn't need to have its foot flat to the floor. "In line with the weak underlying international and domestic economic conditions, the Committee expects a rise in unemployment and an increase in firm closures." The renewed COVID-19 restrictions also warranted a mention, as did the fact that fiscal support has started to roll off. The NZD was mentioned in the context of being a partial offset to New Zealand's "robust" commodity prices.
- The RBNZ stopped short of promising a negative OCR, saying rather that they "are prepared to provide additional stimulus". But it's pretty clear which way the wind is blowing. We continue to expect that the RBNZ will cut the OCR 50bp in April to -0.25%, with risks skewed to another cut after a pause to check that things are panning out as hoped.
- The RBNZ reiterated that "the outlook for inflation and employment remained subdued." With the impact of the current QE programme set to start to wane next year, and yet a commitment to leave the OCR on hold until March (with mid-April being the first scheduled meeting after that date), the RBNZ will therefore be looking for ways to deliver stimulus quickly.
- With regard to the LSAP, we saw a $200m reduction in the pace of purchases scheduled for next week. While that was a reduction, it was a lesser reduction than the $400m reduction in issuance next week. The pace of next week's LSAP purchases of NZGBs is almost twice the rate of issuance, and the delta of next week's QE is almost 2.5x that of issuance ($1114k vs $448k). The fact that the tactical approach to purchases will continue to be aggressive gives scope for more purchases at the longer end of the curve. That in turn speaks to continued vigilance and pressure on the curve to flatten.

ASB

- There was much in the September MPR assessment that was little changed on the August MPS. For one, current policy settings were retained, with the RBNZ holding the OCR steady at 0.25% and maintaining the size of its Large Scale Asset Purchase Programme (LSAP) at $100 billion. Moreover, it stuck to its forward guidance to leave the OCR on hold at 0.25% until early next year.
- Second, the RBNZ assessment of the economic outlook was sombre. The RBNZ remains concerned over the global outlook, and the risks of the recovery stalling. While there were a few glimmers of positivity, the policy assessment pointed to subdued levels of economic activity, with the Summary Record of Meeting citing the "unprecedented contraction" in Q2 economic activity and the potentially longer-lasting headwinds posed by COVID. Fiscal policy support measures had been effective in cushioning the economy, but with the income support measures rolling off, fiscal tailwinds were receding.
- Third, the RBNZ view is that monetary policy will need to provide significant economic support for a considerable period. International border restrictions are likely to significantly curtail migration and tourism, and lead to the activity outlook being uneven across industries and regions. The weak global backdrop and soft domestic conditions will likely result in rising NZ unemployment and firm closures. The RBNZ reiterated that the economic outlook remained highly uncertain and dependent on the course of the virus. However, the balance of risks remained skewed to the downside, with the MPC concerned that a severe and prolonged economic downturn would make it difficult to achieve its inflation and employment objectives. We concur.

- Fourth, the RBNZ maintained the same additional options for providing policy stimulus. These included the same 'Big 3' that were cited in August, including a Funding for Lending Programme (FLP), a negative OCR, and purchases of foreign assets. The policy assessment also reiterated that these instruments would be mutually supportive in bolstering economic activity.
- What was different this time around, however, was the comments on the progress being made on the Bank's ability to deploy additional monetary instruments. First, the RBNZ was explicit in noting that these alternative instruments could be deployed independently, rather than as a package of measures. Second, it was noted that the FLP would be ready before the end of this calendar year, an explicit signal to banks to get things ready now. It seems the RBNZ has done a lot more thinking on policy implementation, including the sequencing of additional monetary instruments.
- The intention to implement FLP before year-end may mean it is ready to implement the scheme at the November 11th Monetary Policy statement release. But if the scheme is not ready by then, it is still likely the RBNZ would want to get it implemented before Christmas rather than waiting until next year. It was helpful that the RBNZ has pledged to provide details on the design of the programme prior to them being deployed. However, to get more bang for its policy buck, the sooner these details are provided the better. As we noted recently, the RBNZ will need to get the design details right to ensure the scheme maximises its effectiveness. We still expect the RBNZ will cut the OCR in early 2021 and have pencilled in an April OCR cut. In our view, risks to the economic outlook are still tilted to the downside and the RBNZ will want to provide as much stimulus as possible to support the economy that it going through a severe downturn.

Barclays

- The RBNZ left policy settings unchanged earlier today, but provided more clarity on its next steps. The MPC acknowledged progress on the RBNZ's ability to deploy additional monetary instruments and indicated that a Funding for Lending Programme (FLP), a negative overnight cash rate (OCR), purchases of foreign assets, and interest rate swaps remain in consideration. Details on their sequencing indicate that the FLP could come first as it should be ready before year end with a negative OCR next, given its guidance from 16 March, if additional stimulus is required. The bank maintained the LSAP programme with a maximum of NZD100bn by June 2022 and held the OCR steady at 0.25%.
- Today's outcome had no dovish surprises, but reinforced markets bullish expectations, in our view. Comments by key RBNZ officials had helped fuel expectations of a negative OCR, and yields on up to-5y NZGBs were below zero. Markets were perhaps assigning a non-zero chance to another 'dovish' surprise, especially after RBA comments earlier this week and the Fed's shift to flexible average inflation targeting. Markets were already positioned for more easing, with Feb RBNZ OIS at 0.1%, April OIS at -0.1% and 1y ahead RBNZ OIS at -0.19%. Front-end rates are little changed, but the IRS and NZGB curves bull flattened as markets extended duration and sentiment was boosted by hints about a possible FLP.
- advance. Our economists now expect the FLP to be announced in November and the RBNZ to lower the OCR to -0.25% in April 2021. The RBNZ April meeting OIS is underpriced relative to our revised OCR forecasts, and there is some optionality in the November meeting OIS, especially if the RBNZ chooses to ignore its March 2020 guidance and lower the OCR to or near 0%. The Funding for Lending Programme, depending on its overall size and duration, should reduce funding needs and help swaps outperform NZGBs.

BNZ

- Recently, the RBNZ seems to have developed the habit of throwing in a wee curve ball to keep markets on their toes. Today was no different. While the vast majority of the wording in the Reserve Bank's Monetary Policy Review was bang on our expectations, the decision to make the Funding for Lending Programme available by the end of the year was a bit of a surprise.
- A surprise, it may be, but we can see the rationale. In short, the RBNZ thinks this might help lower the cost of funds for the banking sector in advance of any move to negative interest rates. In so doing, the Bank would not only achieve its objective of pushing lending rates lower but it could do so in a way which might allow it to keep its cash rate at 0.25% until April 2021, as previously indicated. Importantly, the Bank noted that while the instruments available to it are "mutually supportive" they "can be deployed independently" reinforcing the fact that while the Funding for Lending programme is ultimately intended to be accompanied by negative interest rates it need not be the case at the time of initial implementation. With this in mind, it is notable that the RBNZ reiterated its interest rate intention in saying "The Official Cash Rate (OCR) is being held at 0.25 percent in accordance with the guidance issued on 16 March".

- At this stage, we see no reason to change our view that the move to negative interest rates will not occur until April. We expect this to be restated at the Bank's November MPS. However, we would not be surprised if the Bank's forward guidance, which currently only runs to the February 2021 meeting, might be extended to reveal the expected nature of the interest rate track through calendar 2021.
- We would also expect the Bank to provide detail of its Funding for Lending Programme at the November meeting Some in the market will have been disappointed the RBNZ wasn't more dovish today but we think the RBNZ can achieve what it wants without needing to be so. Could the Bank bring forward its negative shift to February? Yes, most definitely, particularly if downside risks to the economy evolve. We would still put the probability of a February cut at around 20% but we think today's announcement, at the margin, actually decreases the likelihood of February compared to April.
- Concurrently, the RBNZ today announced it would reduce its LSAP purchases as from next week. This should not be seen as signaling a change in policy, as such, but, rather, is in response to NZDM announcing a reduced debt programme and a lower rate of debt issuance. Importantly, the RBNZ reiterated its commitment to continue with the Large Scale Asset Purchase Programme up to $100 billion. That said, it seems to us there will be a moderation in RBNZ bond purchases as negative interest rates are introduced.

Goldman Sachs

- The RBNZ maintained its policy settings unchanged today as expected, including the 0.25% OCR, forward guidance of unchanged OCR until at least March 2021 and a NZ$100bn Large Scale Asset Purchase (LSAP) programme. The attending statement also maintained a very dovish tone as we expected, with the RBNZ noting "the progress being made on the Bank's ability to deploy additional monetary instruments" and that it is "prepared to provide additional stimulus".
- The decision statement was dovish in an absolute sense as we expected. The RBNZ continued to highlight "the possible need for further monetary stimulus" and the progress being made on the Bank's ability to deploy additional monetary instruments, including a Funding for Lending Programme (FLP), a negative OCR, and purchases of foreign assets.
- Importantly, the Minutes flagged that a 'Funding For Lending' programme (FLP) is likely before the end of 2020 and, as a result, we now expect an ~NZ$30bn programme (~10% of GDP and total credit outstanding) to be delivered at the November meeting, with significant uncertainty around the specific parameters of the programme (our base case is a fixed rate programme of 0.25% for 3 years). We note an FLP would help lower funding costs for banks, assistant the pass-through to retail interest rates while also providing explicit incentives for banks to lend (similar to the RBA's Term Lending Facility).
- With regard to further rate cuts however, while the RBNZ reiterated the possibility of a negative OCR today's characterization signalled somewhat less urgency in the near-term (the Committee "was prepared to lower the OCR to provide additional stimulus if required"). Our base case remains for an unchanged OCR over the medium term given our above-consensus growth forecast and more positive vaccine views - although we acknowledge the clear risk of a rate cut in 1H2021 (45% probability).

J.P. Morgan

- The RBNZ left the OCR unchanged at 0.25% today, and affirmed the NZ$100bn QE program. They maintained the guidance that the OCR would stay unchanged until March next year. However, there was an explicit commitment to the previously-flagged funding for lending program (FLP) for banks, which staff are now advising "can be deployed independently", and will be ready before the end of this calendar year.
- This separation between the FLP and the timing of a possible OCR cut to lower/negative rates was described straightforwardly in the minutes as providing "additional stimulus to the economy sooner", given the constraint that banks can't yet process a negative OCR.
- Interestingly the funding facility pricing is still referenced to be "near the OCR", an intriguing detail which in our view suggests a wedge will be set initially, or will arise over time if the OCR is cut afterward. We have favoured flatteners within the basket of negative OCR trades assuming FLP would be set above OCR, and because the effective rate on reserves will end up higher than the OCR via a likely tiering regime too. The separation in time, in doing the FLP first, adds a further leg to that story. We also think the FLP is fairly likely to be a 5Y facility, longer than the RBA's equivalent (the 3Y rolling TFF), as the RBNZ's narrower existing facilities supporting government-sponsored business loans have just been extended to that tenor. We are received 3Y3Y NZD/USD cross-currency which should also benefit from today's commitment to launching a funding facility.

- On the policy rate itself, we have been expecting the RBNZ to break its guidance, given that has not been serving any helpful purpose. But now even the Finance Minister is being seconded to deliver the RBNZ's party line (see last week's comments), so officials seem very committed to finishing what they started. The commitment to not touching the OCR until March, despite negative being feasible by year-end, has always been mysterious, and remains so given the stitch in time argument driving the FLP this year somehow doesn't apply. Regardless, by the time we get to early next year, the cost/benefit of moving a couple of months early vs the loss of face from reneging on the guidance becomes unfavourable. We push out our call for a cut from November to April, at which point negative is feasible (-0.25%). With the reserve base likely to grow to over NZ$100bn, we continue to think the majority of reserves will earn a tiering rate above a negative OCR, initially in the 0 to +0.25% range. Of course the risk will remain to earlier action rather than a cut beyond April, as soon as negative is feasible.

Kiwibank

- The RBNZ left the OCR unchanged at 25bps. And the LSAP programme was left at $100b, as expected. In a positive development, the RB spoke of unpacking previously packaged tools – as we suggested in Monday's report "Unpacking and then repacking a packaged deal." 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. We couldn't agree more. Way to go!
- The RBNZ has made it increasingly clear that more policy stimulus will be needed to meet its dual mandate. While the economy has already bounced out of the June quarter hole, we have yet to experience the full force of the pandemic on the economy. The global situation has deteriorated, and NZ's unemployment rate is likely to rise. Future policy stimulus includes both a negative cash rate (NIRP) and a bank funding for lending programme (FLP). Doing more, much more, is the so-called path of least regret.
- We've taken some comfort in the RB potentially pulling the leavers on these polices separately. We have continually noted that it would be better to focus on the FLP now, and consider NIRP later. The bank FLP is the next best tool in the shed, and we will get the FLP before year-end. We expect the FLP to be started in November.
- Further policy action will lower retail interest rates, adding fuel to a fiery housing market. We had been surprised by the fervour of the housing market straight out of lockdown. Moreover, Auckland's level 3 lockdown caused little disruption in August. Sales activity across NZ are at levels last seen five years ago, and house price growth has accelerated. Record low mortgage rates and the removal of LVR restrictions explain much of the renewed activity. But the ongoing shortage of housing is playing a role too. As evident in the record low levels of listed property.

Westpac

- Today the Reserve Bank announced that it is developing a Funding for Lending Programme (FLP) that will be ready to deploy before the end of this year. Consequently, we are now forecasting that an FLP will be announced at the Monetary Policy Statement on 11 November.
- The FLP will cause a reduction in retail mortgage rates, term deposit rates and business lending and deposit rates, at the time it is introduced. The main impact of this will be to further stimulate asset prices, particularly the housing market. In turn, higher asset prices will stimulate consumer spending and therefore boost inflation and employment. The secondary impact of the FLP will be to suppress the exchange rate, which also tends to boost inflation and employment.
- Today's press release from the RBNZ was incredibly downbeat. There was very little acknowledgement that the economy has exceeded expectations, and at least some members of the Monetary Policy Committee doubted the durability of the housing market upturn.
- The outlook is highly uncertain, but we think that the risks are to the upside of the RBNZ's dour economic expectation, particularly on house prices. Despite that, we agree with the RBNZ's assessment that "further monetary stimulus may be needed". In fact, we would go further – massive monetary stimulus is required to prevent inflation from lingering too low. Therefore, we support the RBNZ's move to introduce an FLP this year, and we continue to expect that the RBNZ will reduce the OCR to -0.5% in April next year.

MNI Policy Team Insights

MNI REVIEW: RBNZ Policy On Hold; Further Options Progressing

By Lachlan Colquhoun

SYDNEY (MNI) - The Reserve Bank of New Zealand left monetary policy unchanged Wednesday, but signaled that more policy easing was possible, including negative interest rates, a funding facility for commercial banks and the purchase of foreign assets.

The Monetary Policy Committee kept rates on hold at a record low 0.25% and affirmed the NZ$100 billion program to buy NZ Government securities, saying prolonged monetary support was still necessary.

The committee also discussed possible future policy measures, such as a Funding for Lending Programme (FLP), a negative OCR, and purchases of foreign assets and interest rate swaps, saying progress hade been made on the ability to deploy such policies if needed.

A funding for lending program "would be ready before the end of this calendar year", the RBNZ said, and was a logical first step before lowering rates further.

"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 statement published alongside the policy decision said.

The RBNZ also noted market expectations for zero interest rates this year, and that this had already contributed to lower wholesale interest rates.

The banking system, the RBNZ statement said, "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 statement said.

No timetable was given for foreign asset purchases, although again the RBNZ said progress had been made to the future deployment if needed..

While NZ had opened the economy after the pandemic disruptions, it remained weak and more stimulus was required, the bank said.