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ECONOMIC ALERT

OCR — JUNE 2020

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“The Monetary Policy Committee agreed to continue with the Large Scale Asset Purchase (LSAP) programme aimed at keeping interest rates low for the foreseeable future. The LSAP quantum remains set at NZD60 billion.”

And ...

“The Official Cash Rate (OCR) is being held at 0.25 percent in accordance with the guidance issued on 16 March.”

Why ...

“The severe global economic disruption caused by the COVID-19 pandemic is persisting, leading to lower economic activity, employment, and inflation abroad and in New Zealand. The negative economic impact on New Zealand is exacerbated by the required international border restrictions ...

As ...

“New Zealand has contained the spread of COVID-19 locally for now, enabling a relaxation of social restrictions and an earlier resumption of domestic economic activity than assumed in our May “Monetary Policy Statement.” The Government’s intended fiscal stimulus, announced in its May Budget, was also slightly larger than we assumed. These outcomes give cause for some confidence, but significant economic challenges remain.”

However ...

“The Monetary Policy Committee is prepared to provide additional stimulus as necessary. As well as potentially expanding the LSAP programme, the Committee continues to prepare for the use of additional monetary policy tools as needed.”

In conclusion ...

“As outlined in our May Statement, the balance of economic risks remains to the downside. The LSAP programme aims to continue to reduce the cost of borrowing. Retail interest rates have declined with lower wholesale borrowing costs. It remains in the best long-term interests of the banking sector to promptly maximise the effectiveness of our LSAP programme.”

Market Implications ...

The Reserve Bank of New Zealand (“RBNZ”) held the Official cash rate (OCR) at 0.25% and maintained its Large Scale Asset Purchase (LSAP) programme, or Quantitative Easing by any other name, at NZD60 billion.

The RBNZ maintained the dovish nature of its commentary, reiterating that the balance of economic risks remains to the downside, with the RBNZ remaining prepared to provide additional stimulus as required. The committee members discussed the pros and cons of expanding the LSAP programme, noting that any expansion would need to be driven by the economic outlook and that any change would have to be of a sufficient magnitude to make a meaningful difference.

It was also noted that RBNZ staff are working towards ensuring a broader range of monetary policy tools that could be deployed in the coming months, including a term lending facility, reductions in the OCR, and foreign asset purchases (requiring the

sale of NZD), as well as reassessing the appropriate quantum of the current LSAP.

This language unnerved the New Zealand dollar, and it retraced from its pre-announced rate of 0.6500 against the USD to a low of 0.6450. It is now consolidating at the 0.6485 level.

Since the announcement we have seen the swaps curve steepen, with short-term rates unchanged and the longer end firming. The 10 year NZ IRS is now at 0.795%.

Comment

While the RBNZ’s statement highlighted New Zealand’s successful containment of COVID-19 and recognised the increased fiscal stimulus, it nevertheless continued its pessimistic tone regarding both the domestic and global economy.