

# Economic Alert

MONETARY POLICY STATEMENT – NOVEMBER 2020

Wednesday 11 November, 2020

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## Key Points:

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"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 Large Scale Asset Purchase ("LSAP") programme of a maximum of \$100b by June 2022; and
- direct the Bank to implement a Funding for Lending Programme ("FLP") in early December 2020."

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## How will the RBNZ implement the FLP?

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"We plan to implement the FLP in early December. Details of operations, including terms and conditions, will be made available in coming weeks."

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## What to expect if the FLP is effective?

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"The key success metric of the FLP will be whether it results in declines in funding costs and encourages recent declines in these costs to be passed through to lower household and business borrowing costs."

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## Design features of the FLP:

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"Cost: OCR

Size of programme: Initial allocation of 4% of each eligible participant's total loans and advances to New Zealand households, private non-financial businesses, and non-profit institutions serving households 'eligible loans'. A conditional additional allocation of 2% of eligible loans will then be made available, for a total size of 6% of eligible loans.

Term of lending: 3 years, with a floating interest rate.

Eligible collateral: High-quality collateral – e.g. New Zealand government bonds, Kauri bonds, and Internal Residential Mortgage Backed Securities (I-RMBS).

*Incentive mechanism: The additional allocation discussed above can only be accessed when participants increase their provision of credit to the economy. The FLP provides 50 cents of funding for every \$1 increase in their stock of eligible loans."*

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## Market Implications:

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While the statement didn't contain any surprises, the tone wasn't dovish enough to halt the momentum of the NZD or fixed income markets. In fact, the NZD is continuing its relentless grind higher and, against the USD, it has retraced to levels not seen since March 2019.

It should be noted that the RBNZ's projections assume the NZD TWI will remain around the 72.00 level, and it has traded in a 71.00-73.00 range since the beginning of June, but the underlying strength of the NZD has seen the TWI rally to 73.20.

Interest rate markets, too, saw the statement as not dovish enough, sending swap rates 5-8 basis points higher across the curve following the announcement, building on the upward moves seen in this week.

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## Comment:

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Given there was no adjustment to the OCR rate, nor the LSAP, the markets focus was on the FLP programme and, to be fair, there were no surprises here either. The central bank estimates the FLP programme will provide around NZD28 billion of funding, very much at the low end of market expectations.

In saying this, the RBNZ reaffirmed that the FLP, a lower or negative OCR, purchases of foreign assets, and interest rate swaps still remain under consideration, however, Mr Orr did add that it is "too early to tell" if a negative OCR is needed, which has done nothing to quell the rise in interest rates and the NZD today. As a result, the banks have been quick to back away from their calls for a negative OCR.



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