

### RBNZ April OCR Review

#### Key points

- > A 50 basis point cut, door open to more and rates to stay low until late 2010.
- > The RBNZ's actions and comments today were about as dovish as you can get.
- > We concur with the broad spirit of the RBNZ's views, and their wariness towards economic prospects, both in terms of the trough and prospects for recovery.
- > We have pencilled in a more modest 25bp cut for June, but believe that the ultimate endgame for the OCR will be partly dependent on what sort of adjustment we see in the currency over the coming months.

#### Assessment

The RBNZ delivered a clear message today in cutting the OCR by 50 basis points, flagging the potential for more, and also committing to keeping rates low until late 2010. In so far as central bank communication is concerned, today's message is clear cut: if you are a borrower, don't panic and rush to fix.

**The statements accompanying the decision (reproduced in full at the end of this note) are so stark they speak for themselves. It is worthy of full reproduction, and resonates very closely with our core views.**

*"Overall, developments since March point to lower medium-term inflation", which points to Plan B for the RBNZ in using the 50 basis points of ammunition it kept up its sleeve in the March Monetary Policy Statement. That is, an endgame for the OCR of around 2 percent as opposed to the previously flagged 2.5 percent.*

The RBNZ note that there has been an **"unwarranted** tightening in financial conditions via both higher long-term interest rates and a stronger exchange rate than expected." In this environment it is appropriate to use monetary policy more aggressively.

On the outlook for growth, the RBNZ appears to have downgraded their March Monetary Policy Statement view of a strong H2 recovery, stating that *"the scale of the global financial crisis and domestic adjustments underway are such that it is likely to be **some time** before economic activity returns to robust and healthy levels."* The Bank now foresees an elongated recovery, which will be reflected in downward revised growth forecasts in their upcoming June MPS.

The key paragraph was the last one, where the Governor said **"We expect to keep the OCR at or**

**below the current level through until the latter part of 2010. The OCR could still move modestly lower over the coming quarters."**

This is a step further from his April 1 statement when he said *"we are projecting interest rates to remain at relatively low levels for an extended period."* With the medium-term inflation outlook very favourable and the economy still weak, with any recovery tepid at best, the RBNZ felt a need to provide more policy stimulus and importantly, keep conditions stimulatory for a long time.

The sentence about keeping rates low until the latter part of next year is a leaf out of recent offshore central bank communications of late. The Bank of Canada and Sweden's Riksbank also committed to keeping their policy rates low until the end of Q2 2010 and early 2011 respectively. But the big difference is that the RBNZ did not put any conditionality around their policy outlook commitment, feeling sufficiently comfortable that inflation will be tamed for some time. In this respect, today's statement is as dovish as you can get.

The Governor is open to further cuts to the OCR in the coming quarters, and we expect another 25bp cut in June. In our view, the ultimate endgame for the OCR will be dependent on what sort of adjustment we see in the currency over the coming months. In terms of data releases we see the March quarter employment (or unemployment) report as strongly validating a further OCR move in June. Beyond that close attention will need to be paid to leading indicators. If the influential NZIER Quarterly Survey of Business Opinion (due early July) follows the lead of yesterday's National Bank Business Outlook survey and recovers (off historical lows), a pause and 2.25 percent trough is likely.

In the post-decision press conference, the Governor made some interesting comments of note:

On the reason behind the specific statement: *"we have been firmer"* in our words and we are *"trying to avoid the premature expectations of recovery"* that have been seen elsewhere, which could *"ultimately prove damaging"*.

On how the recovery won't feel like a recovery: the economy *"will recover off this trough"*, but *"it's a very low trough"* by historical standards. Most forecasters like us are pencilling in a recovery in H2 2009 (in part reflecting the base effect following six successive quarterly falls in GDP). But with the unemployment rate continuing to rise, the key message will be one of grumpy and patchy growth. The rebalancing process for the economy away from debt-fuelled spending centric growth towards the earning sector (i.e. exports) will take time, and still remains partly dependent on the global environment.

On what happened in March: *"we were a little scared"* of some of the *"euphoria"* in the housing market, with some people thinking it was *"happy days"*.

Bollard on the rates outlook: *"we certainly haven't set a floor"* in interest rates, a change from sentiment expressed March.

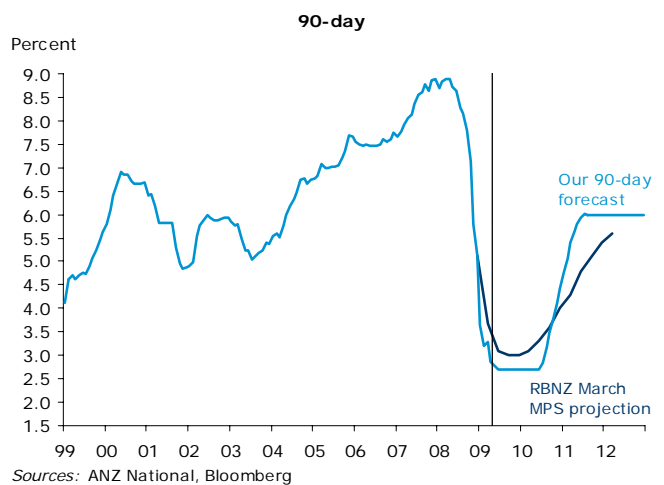
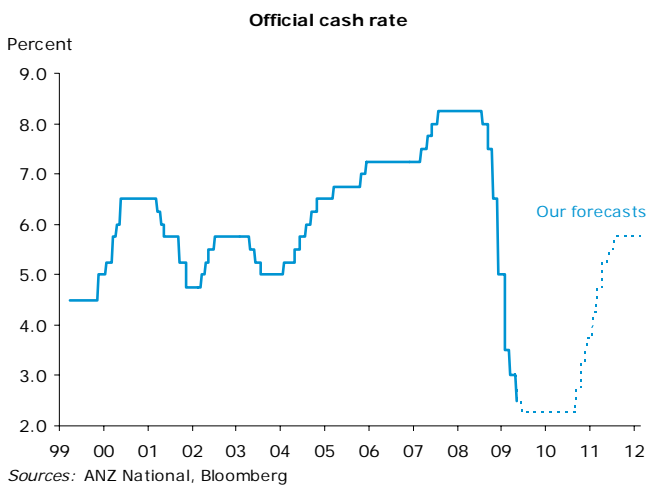
One RBNZ official at the press conference also commented that there *"is potentially not the rush to jump into long term rates at this stage"*.

### Implications

**In our view, today's assessment and commentary is about as clear as central bank communication could possibly be.** Policy is attempting to remove the temptation for the market (via pricing in rate hikes in 2010) to preempt the recovery. Term wholesale rates should be lower. It's a timely reminder that the NZD is not a one way ticket higher, and equally a signal to borrowers not to panic. Get used to a positive sloped yield curve, and target favourable short-term rates as opposed to rushing in to fix.

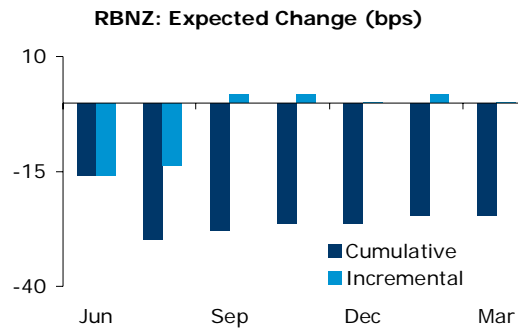
Unsurprisingly, rates rallied hard initially by between 19 and 28bps, with the curve steepening (though there has been some retracements by midday). We expect rates to rally further as the full ramifications of today's decision sinks in. We look for the 2-year swap yield to head towards sub-3 percent and for the curve to continue steepening. The NZD fell a cent against the USD and the AUD, and the kiwi should remain heavy.

**In terms of our key forecasts, we see little reason for alteration at this stage.** A further 25 basis point cut seems inevitable but we are coy about leaps beyond that. Our core forecasts already assumed rates would remain on hold until Q3/Q4 2010. In terms of the currency, we continue to expect the NZD to remain under pressure, but with the AUD being supported, it may well be that the NZD/AUD becomes the key release valve that a lower NZD on a TWI basis is expressed.



## Latest OCR market pricing

New Zealand Current Rate	Rate	Change from current
Jun 09	2.34	-0.16
Jul 09	2.20	-0.30
Sep 09	2.22	-0.28
Oct 09	2.24	-0.26
Dec 09	2.24	-0.26
Jan 10	2.25	-0.25
Mar 10	2.25	-0.25



Source: ANZ National, Bloomberg

## Full text of the OCR Review

The Reserve Bank today reduced the Official Cash Rate (OCR) by 50 basis points to 2.5 percent.

Reserve Bank Governor Alan Bollard said: "Overall, developments since March point to lower medium-term inflation than previously projected. The main factors behind this are weaker global growth, and an unwarranted tightening in financial conditions via both higher long-term interest rates and a stronger exchange rate than expected.

"Global financial markets have showed some tentative signs of stabilisation since the March Monetary Policy Statement and governments in the major economies are continuing to make progress in resolving their banking system difficulties. However, a large amount still needs to be done and sentiment remains fragile. Negative feedback from the global recession could also still adversely affect financial institutions.

"The world economy deteriorated further than expected in the first quarter of 2009. While monetary and fiscal policy responses in many countries have been substantial and there are some signs of stabilisation in some countries, we still expect the adverse economic forces generated by the crisis to remain dominant throughout 2009. The timing and extent of global recovery remain highly uncertain.

"While the New Zealand economy has not experienced the same extreme falls in economic activity as seen in a number of our trading partners, it remains weak. Business sentiment is low, investment has been curtailed and employment reduced.

"We expect the large decline in the OCR over the past year to pass through to more borrowers over coming quarters as existing fixed-rate mortgages come up for re-pricing. This, together with the stimulus from fiscal policy, will act to support the New Zealand economy and eventually see activity trough and pick up thereafter. However, the scale of the global financial crisis and domestic adjustments underway are such that it is likely to be some time before economic activity returns to robust and healthy levels.

"We consider it appropriate to provide further policy stimulus to the economy. We expect to keep the OCR at or below the current level through until the latter part of 2010. The OCR could still move modestly lower over the coming quarters."

## NEW ZEALAND DISCLOSURE INFORMATION

The Bank (in respect of itself and its principal officers) makes the following investment adviser disclosure to you pursuant to section 41A of the Securities Markets Act 1988.

The Bank (in respect of itself and its principal officers) makes the following investment broker disclosure to you pursuant to section 41G of the Securities Markets Act 1988.

### Qualifications, experience and professional standing

#### Experience

The Bank is a registered bank and, through its staff, is experienced in providing investment advice about its own securities and, where applicable, the securities of other issuers. The Bank has been selling securities, and providing investment advice on those securities, to customers as a core part of its business for many years, drawing on the extensive research undertaken by the Bank and its related companies and the skills of specialised staff employed by the Bank. The Bank is represented on many bank, finance and investment related organisations and keeps abreast of relevant issues by running seminars and workshops for relevant staff and having its investment adviser staff attend external seminars where appropriate. The Bank subscribes to relevant industry publications and, where appropriate, its investment advisers will monitor the financial markets.

#### Relevant professional body

The Bank is a member of the following professional bodies relevant to the provision of investment advice:

- New Zealand Bankers Association;
- Associate Member of Investment Savings & Insurance Association of NZ;
- Financial Markets Operations Association; and
- Institute of Finance Professionals.

#### Professional indemnity insurance

The Bank (and its subsidiaries), through its ultimate parent company Australia and New Zealand Banking Group Limited, has professional indemnity insurance which covers its activities including those of investment advisers it employs.

This insurance covers issues (including 'prior acts') arising from staff fraud, electronic crime, documentary fraud and physical loss of property. The scope of the insurance also extends to third party civil claims, including those for negligence. The level of cover is of an amount commensurate with the size and scale of the Bank.

The insurer is ANZcover Insurance Pty Limited.

#### Dispute resolution facilities

The Bank has a process in place for resolving disputes. Should a problem arise, you can contact any branch of the Bank for more information on the Bank's procedures or refer to any of the Bank's websites.

Unresolved complaints may ultimately be referred to the Banking Ombudsman, whose contact address is PO Box 10-573, Wellington.

#### Criminal convictions

In the five years before the relevant investment advice is given none of the Bank (in its capacity as an investment adviser and where applicable an investment broker) or any principal officer of the Bank has been:

- Convicted of an offence under the Securities Markets Act 1988, or the Securities Act 1978 or of a crime involving dishonesty (as defined in section 2(1) of the Crimes Act 1961);
- A principal officer of a body corporate when that body corporate committed any of the offences or crimes involving dishonesty as described above;
- Adjudicated bankrupt;
- Prohibited by an Act or by a court from taking part in the management of a company or a business;
- Subject of an adverse finding by a court in any proceeding that has been taken against them in their professional capacity;

- Expelled from or has been prohibited from being a member of a professional body; or
- Placed in statutory management or receivership.

#### Fees

At the time of providing this disclosure statement it is not practicable to provide accurate disclosure of the fees payable for all securities that may be advised on. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

#### Other interests and relationships

When a security is sold by the Bank, the Bank may receive a commission, either from the issuer of a security or from an associated person of the Bank. Whether that commission is received and, if received, its value depends on the security sold. At the time of providing this disclosure statement it is not practicable to provide a detailed list of each security that may be advised on, the name of the issuer of that security and the rate of the commission received by the Bank. However, this information will be disclosed to you should you seek advice from one of the Bank's investment advisers on a specific investment.

In addition to the interest that the Bank has in products of which it is the issuer, the Bank, or an associated person of the Bank, has the following interests or relationships that a reasonable person would find reasonably likely to influence the Bank in providing the investment advice on the securities listed below:

- ANZ Investment Services (New Zealand) Limited (ANZIS), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. ANZIS may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- UDC Finance Limited (UDC), as a wholly owned subsidiary of the Bank, is an associated person of the Bank. UDC may receive remuneration from a third party relating to a security sold by the Investment Adviser.
- The Bank has a joint venture relationship with ING (NZ) Holdings Limited (ING). ING and its related companies may receive remuneration from a third party relating to a security sold by the Investment Adviser.

#### Securities about which investment advice is given

The Bank provides investment advice on the following types of securities:

- Debt securities including term and call deposits, government stock, local authority stock, State-Owned Enterprise bonds, Kiwi bonds and corporate bonds and notes;
- Equity securities such as listed and unlisted shares;
- New Zealand and overseas unit trusts;
- Share in a limited partnership;
- Superannuation schemes and bonds;
- Group investment funds;
- Life insurance products;
- Derivative products including interest rate and currency forward rate contracts and options; and
- Other forms of security, such as participatory securities.

## PROCEDURES FOR DEALING WITH INVESTMENT MONEY OR INVESTMENT PROPERTY

If you wish to pay investment money to the Bank you can do this in several ways such as by:

- Providing cash;
- Providing a cheque payable to the relevant product or service provider and crossed 'not transferable'; or
- Making an automatic payment or payment through another electronic delivery mechanism operated by the Bank.

Investment property (other than money) may be delivered to the Bank by lodging the relevant property (for example, share certificates) with any branch of the Bank offering a safe custody service, or by posting (using registered post) the documents or other property to a branch of the Bank, identifying your name, account number and investment purpose.

Any investment money lodged with the Bank for the purchase of securities offered by the Bank, its subsidiaries or any third

parties will be deposited in accordance with your instructions, to your nominated account or investment. Such money will be held by the Bank according to usual banking terms and conditions applying to that account or the particular terms and conditions relating to the investment and will not be held by the Bank on trust unless explicitly accepted by the Bank on those terms. Any investment money or property accepted by the Bank on trust will be so held until disbursed in accordance with your instructions. Any investment property lodged with the Bank will be held by the Bank as bailee according to the Bank's standard terms and conditions for holding your property.

#### **Record Keeping**

The Bank will keep adequate records of the deposit of investment moneys or property and all withdrawals and dealings with such money or property, using the account/investment number allocated to your investment. You may have access to those records upon request.

#### **Auditing**

The Bank's systems and operations are internally audited on a regular basis. The financial statements of the Bank and its subsidiaries are audited annually by KPMG. However, this does not involve an external audit of the receipt, holding and disbursement of the money and other property.

#### **Use of Money and Property**

Money or property held by the Bank for a specific purpose communicated to the Bank (e.g. the purchase of an interest in a security) may not be used by the Bank for its own purposes and will be applied for your stated purpose. No member of the Bank's staff may use any money or property deposited with the Bank, for their own purposes or for the benefit of any other person. In the absence of such instructions, money deposited with the Bank may be used by the Bank for its own purposes, provided it repays the money to you upon demand (or where applicable, on maturity), together with interest, where payable.

#### **NEW ZEALAND DISCLAIMER**

The Bank does not provide investment advice tailored to an investor's personal circumstances. It is the investor's responsibility to understand the nature of the security subscribed for, and the risks associated with that security. To the maximum extent permitted by law, the Bank excludes liability for, and shall not be responsible for, any loss suffered by the investor resulting from the Bank's investment advice.

Each security (including the principal, interest or other returns of any security) the subject of investment advice given to the investor by the Bank or otherwise, is not guaranteed, secured or underwritten in any way by the Bank or any associated or related party except to the extent expressly agreed in the terms of the relevant security.

This document is provided for informational purposes only and does not constitute an offer to sell or solicitation to buy any security or other financial instrument. No part of this document can be reproduced, altered, transmitted to, copied to or distributed to any other person without the prior express permission of the Bank.

This document is a necessarily brief and general summary of the subjects covered and does not constitute advice. You should obtain professional advice before acting on the basis of

This document has been prepared by ANZ National Bank Limited.

ANZ (part of ANZ National Bank Limited), Level 7, 1 Victoria Street, Wellington 6011, New Zealand Phone 64-4-802 2000 Fax 64-4-496 8639 <http://www.anz.co.nz> e-mail [ecnmcs@anz.com](mailto:ecnmcs@anz.com)

any opinions or information contained in it. The information contained in this document is given in good faith, has been derived from sources perceived by it to be reliable and accurate and the Bank shall not be obliged to update any such information after the date of this document. Neither the Bank nor any other person involved in the preparation of this document accepts any liability for any opinions or information (including the accuracy or completeness thereof) contained in it, or for any consequences flowing from its use.

#### **UNITED STATES DISCLAIMER**

This document is being distributed in the United States by ANZ Securities, Inc. ("ANZ S") (an affiliated company of Australia and New Zealand Banking Group Limited ("ANZBG") and the Bank), which accepts responsibility for its content. Further information on any securities referred to herein may be obtained from ANZ S upon request. Any US person(s) receiving this document and wishing to effect transactions in any fixed income securities referred to herein should contact ANZ S 1177 Avenue of the Americas, New York, NY 10036 USA, Tel: 1-212-801-9160, Fax: 1-212-801-9163, not its affiliates.

This document is issued on the basis that it is only for the information of the particular person to whom it is provided. This document may not be reproduced, distributed or published by any recipient for any purpose. This document does not take into account your personal needs and financial circumstances. Under no circumstances is this document to be used or considered as an offer to sell, or a solicitation of an offer to buy.

In addition, from time to time ANZBG, the Bank, ANZ S, their affiliated companies, or their respective associates and employees may have an interest in any financial products (as defined by the Australian Corporations Act 2001), securities or other investments, directly or indirectly the subject of this document (and may receive commissions or other remuneration in relation to the sale of such financial products, securities or other investments), or may perform services for, or solicit business from, any company the subject of this document. If you have been referred to ANZBG, the Bank, ANZ S or their affiliated companies by any person, that person may receive a benefit in respect of any transactions effected on your behalf, details of which will be available upon request.

The information herein has been obtained from, and any opinions herein are based upon, sources believed reliable. The views expressed in this document accurately reflect the author's personal views, including those about any and all of the securities and issuers referred to herein. The author however makes no representation as to its accuracy or completeness and the information should not be relied upon as such. All opinions and estimates herein reflect the author's judgement on the date of this document and are subject to change without notice. No part of the author's compensation was, is or will be directly or indirectly related to specific recommendations or views expressed in this document. ANZBG, the Bank, ANZ S, their affiliated companies, their respective directors, officers, and employees disclaim any responsibility, and shall not be liable, for any loss, damage, claim, liability, proceedings, cost or expense ("Liability") arising directly or indirectly (and whether in tort (including negligence), contract, equity or otherwise) out of or in connection with the contents of and/or any omissions from this communication except where a Liability is made non-excludable by legislation.