ANZ Research

RBNZ OCR Emergency 75bp Cut

16 March 2020

This is not personal advice. It does not consider your objectives or circumstances. Please refer to the Important Notice.

Contact

Sharon Zollner
Chief Economist
Telephone: +64 9 357 4094
Sharon.Zollner@anz.com

David Croy
Strategist
Telephone: +64 4 576 1022
david.croy@anz.com

RBNZ delivers emergency 75bp OCR cut

- RBNZ delivered an emergency 75bp cut this morning, taking the OCR to 0.25% "for at least the next 12 months".
- The RBNZ indicated that the next step, if required, will be large scale asset purchases rather than further OCR cuts – indeed, the forward guidance explicitly states that the OCR will remain at 0.25%.
- The 25 March meeting has been cancelled.
- We expect a move to unconventional policy as soon as practicable, since more stimulus is very likely to be needed. This clarification should calm the very unsettled bond market, driving the curve lower and flatter.
- The RBNZ has announced that the increase in bank capital requirements will be delayed by 12 months, with further delays possible down the track.
- A very large fiscal package is expected tomorrow. A broad, economy-wide fiscal response is now necessary.

Today the RBNZ cut the OCR 75bps to 0.25% in an out-of-cycle move, an unprecedented step. Immediate and sizeable action was needed, and it brings the RBNZ into the line with the actions of central banks overseas.

We are in uncharted territory economically. Not only exporters but also the domestic economy is experiencing a very significant blow – now amplified by the necessary containment measures that have now been put in place. We are in the midst of an unprecedented synchronised global demand slowdown, with financial market pressures starting to emerge.

The RBNZ said "The Committee also agreed that should further stimulus be required, a Large Scale Asset Purchase programme of New Zealand government bonds would be preferable to further OCR reductions". However, "the Committee agreed that additional tools were not needed at this point."

We think they will be; we expect a move to unconventional policy as soon as practicable. We consider 0.25% to be the effective lower bound for the OCR. In the current environment, the risks of financial market disruption and a credit squeeze are very real; these risks would be exacerbated by zero or negative interest rates and in our view it is just not worth the risk. However, it was actually operational constraints that drove the decision, rather than a strong judgement on where the effective lower bound sits: "Staff also advised that an OCR of 0.25 percent was currently the lower limit, given the operational readiness of the financial system for very low or negative interest rates."

The RBNZ has given unusually specific forward guidance in indicating the OCR would be held at 0.25% for "at least 12 months". Asset purchases are the next cab off the rank. Assistant Governor Christian Hawkesby said the Bank is also ensuring there is sufficient liquidity in the financial system, through regular market operations.

In order to support stimulatory financial conditions and credit provision in particular, the RBNZ will also delay the implementation of its tougher capital requirements for banks by 12 months, to 1 July 2021, and down the track "will consider whether further delays are necessary."

The spotlight is now firmly on fiscal policy to step up to the plate, with a very significant package expected tomorrow. Encouragingly, the RBNZ described the upcoming package as "broad scale". Rather than targeted, sector-specific measures, an economy-wide support package is now required with jobs and business livelihoods hanging in the balance. We're all in this together; no sector of the economy will be left untouched.

Markets

Markets will focus on five key points. First, the OCR is now at its effective lower bound, which is 0.25%. The RBNZ has said that the OCR will "remain at this level", ruling out both hikes and cuts. Second, we have strong forward guidance "for at least the next 12 months". Third, we no longer have a formal timetable for the next decision, with the 25 March meeting scrapped. Anything could happen any time. Fourth, we have crystal clarity that the next step is QE, and it will involve buying NZGBs. Last, we have a 12-month delay to the new capital requirements.

For interest rate markets, beyond the necessary downward adjustment to the entire term structure today that needs to happen on this cut, we expect the threat of QE to drive the NZGB curve lower and flatter, and to see swap spreads widen (in this case, going from negative back to positive as bond yields fall faster than, and through, corresponding swap yields). We see QE as inevitable in the near future and it will work hand in hand with fiscal policy, effectively negating the unhelpful impact further bond issuance would otherwise have had on the bond curve. We expect that QE will be targeted at the very long end of the government bond curve in a bid to lower term rates and restore market functioning. In short, it is pointless cutting the OCR if bond yields are in an uncontrolled upward spiral as they were into the end of last week. Further policy actions from the Fed (who will cut at this week's FOMC meeting, if not earlier) and other central banks will also support longer bonds.

For the NZD – which had already reacted an hour or earlier (the 8am announcement was flagged at 7am) – this is arguably slightly good news, as it takes the RBNZ off the side-lines to firmly midfield, with strong support provided by fiscal policy. Because the majority of NZGBs are held offshore (52.9% of all lines, but much higher proportions of the longer lines), we would expect QE to result in some NZD selling as offshore sellers surrender bonds to the RBNZ – but that's a story for down the track. We also note the RBNZ opined that "the New Zealand dollar exchange rate has also depreciated against our trading partners acting as a partial buffer for export earnings". That's code for "don't expect us to stand in the way of NZD weakness". However, some consistency is required – not all currencies can weaken at the same time and this is a global epidemic/economic slowdown – hence we expect the NZD to be under mild downward pressure as opposed to collapsing.

Important notice

This document is intended for ANZ's Institutional, Markets and Private Banking clients. It should not be forwarded, copied or distributed. The information in this document is general in nature, and does not constitute personal financial product advice or take into account your objectives, financial situation or needs.

This document may be restricted by law in certain jurisdictions. Persons who receive this document must inform themselves about and observe all relevant restrictions.

Disclaimer for all jurisdictions: This document is prepared and distributed in your country/region by either: Australia and New Zealand Banking Group Limited (ABN11 005 357 522) (**ANZ**); or its relevant subsidiary or branch (each, an **Affiliate**), as appropriate or as set out below.

This document is distributed on the basis that it is only for the information of the specified recipient or permitted user of the relevant website (**recipients**).

This document is solely for informational purposes and nothing contained within is intended to be an invitation, solicitation or offer by ANZ to sell, or buy, receive or provide any product or service, or to participate in a particular trading strategy.

Distribution of this document to you is only as may be permissible by the laws of your jurisdiction, and is not directed to or intended for distribution or use by recipients resident or located in jurisdictions where its use or distribution would be contrary to those laws or regulations, or in jurisdictions where ANZ would be subject to additional licensing or registration requirements. Further, the products and services mentioned in this document may not be available in all countries.

ANZ in no way provides any financial, legal, taxation or investment advice to you in connection with any product or service discussed in this document. Before making any investment decision, recipients should seek independent financial, legal, tax and other relevant advice having regard to their particular circumstances.

Whilst care has been taken in the preparation of this document and the information contained within is believed to be accurate, ANZ does not represent or warrant the accuracy or completeness of the information Further, ANZ does not accept any responsibility to inform you of any matter that subsequently comes to its notice, which may affect the accuracy of the information in this document.

Preparation of this document and the opinions expressed in it may involve material elements of subjective judgement and analysis. Unless specifically stated otherwise: they are current on the date of this document and are subject to change without notice; and, all price information is indicative only. Any opinions expressed in this document are subject to change at any time without notice.

ANZ does not guarantee the performance of any product mentioned in this document. All investments entail a risk and may result in both profits and losses. Past performance is not necessarily an indicator of future performance. The products and services described in this document may not be suitable for all investors, and transacting in these products or services may be considered risky.

ANZ expressly disclaims 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 this document to the extent permissible under relevant law. Please note, the contents of this document have not been reviewed by any regulatory body or authority in any jurisdiction.

ANZ and its Affiliates may have an interest in the subject matter of this document. They may receive fees from customers for dealing in the products or services described in this document, and their staff and introducers of business may share in such fees or remuneration that may be influenced by total sales, at all times received and/or apportioned in accordance with local regulatory requirements. Further, they or their customers may have or have had interests or long or short positions in the products or services described in this document, and may at any time make purchases and/or sales in them as principal or agent, as well as act (or have acted) as a market maker in such products. This document is published in accordance with ANZ's policies on conflicts of interest and ANZ maintains appropriate information barriers to control the flow of information between businesses within it and its Affiliates.

Your ANZ point of contact can assist with any questions about this document including for further information on these disclosures of interest.

Country/region specific information: Unless stated otherwise, this document is distributed by Australia and New Zealand Banking Group Limited (**ANZ**).

Australia. ANZ holds an Australian Financial Services licence no. 234527. For a copy of ANZ's Financial Services Guide please click here or request from your ANZ point of contact.

Brazil, Brunei, India, Japan, Kuwait, Malaysia, Switzerland, Taiwan. This document is distributed in each of these jurisdictions by ANZ on a cross-border basis.

European Economic Area (EEA): ***United Kingdom.*** ANZ is authorised in the United Kingdom by the Prudential Regulation Authority (**PRA**) and is subject to regulation by the Financial Conduct Authority (**FCA**) and limited regulation by the PRA. Details about the extent of our regulation by the PRA are available from us on request. This document is distributed in the United Kingdom by Australia and New Zealand Banking Group Limited ANZ solely for the information of persons who would come within the FCA definition of "eligible counterparty" or "professional client". It is not intended for and must not be distributed to any person who would come within the FCA definition of "retail client". Nothing here excludes or restricts any duty or liability to a customer which ANZ may have under the UK Financial Services and Markets Act 2000 or under the regulatory system as defined in the Rules of the Prudential Regulation Authority (**PRA**) and the FCA. ANZ is authorised in the United Kingdom by the PRA and is subject to regulation by the FCA and limited regulation by the PRA. Details about the extent of our regulation by the PRA are available from us on request.

Fiji. For Fiji regulatory purposes, this document and any views and recommendations are not to be deemed as investment advice. Fiji investors must seek licensed professional advice should they wish to make any investment in relation to this document.

Hong Kong. This publication is issued or distributed in Hong Kong by the Hong Kong branch of ANZ, which is registered at the Hong Kong Monetary Authority to conduct Type 1 (dealing in securities), Type 4 (advising on securities) and Type 6 (advising on corporate finance) regulated activities. The contents of this publication have not been reviewed by any regulatory authority in Hong Kong.

India. If this document is received in India, only you (the specified recipient) may print it provided that before doing so, you specify on it your name and place of printing.

Myanmar. This publication is intended to be general and part of ANZ's customer service and marketing activities when implementing its functions as a licensed bank. This publication is not Securities Investment Advice (as that term is defined in the Myanmar Securities Transaction Law 2013).

New Zealand. This document is intended to be of a general nature, does not take into account your financial situation or goals, and is not a personalised adviser service under the Financial Advisers Act 2008 (**FAA**).

Important notice

Oman. ANZ neither has a registered business presence nor a representative office in Oman and does not undertake banking business or provide financial services in Oman. Consequently ANZ is not regulated by either the Central Bank of Oman or Oman's Capital Market Authority. The information contained in this document is for discussion purposes only and neither constitutes an offer of securities in Oman as contemplated by the Commercial Companies Law of Oman (Royal Decree 4/74) or the Capital Market Law of Oman (Royal Decree 80/98), nor does it constitute an offer to sell, or the solicitation of any offer to buy non-Omani securities in Oman as contemplated by Article 139 of the Executive Regulations to the Capital Market Law (issued vide CMA Decision 1/2009). ANZ does not solicit business in Oman and the only circumstances in which ANZ sends information or material describing financial products or financial services to recipients in Oman, is where such information or material has been requested from ANZ and the recipient understands, acknowledges and agrees that this document has not been approved by the CBO, the CMA or any other regulatory body or authority in Oman. ANZ does not market, offer, sell or distribute any financial or investment products or services in Oman and no subscription to any securities, products or financial services may or will be consummated within Oman. Nothing contained in this document is intended to constitute Omani investment, legal, tax, accounting or other professional advice.

People's Republic of China (PRC). This document may be distributed by either ANZ or Australia and New Zealand Bank (China) Company Limited (**ANZ China**). Recipients must comply with all applicable laws and regulations of PRC, including any prohibitions on speculative transactions and CNY/CNH arbitrage trading. If this document is distributed by ANZ or an Affiliate (other than ANZ China), the following statement and the text below is applicable: No action has been taken by ANZ or any affiliate which would permit a public offering of any products or services of such an entity or distribution or re-distribution of this document in the PRC. Accordingly, the products and services of such entities are not being offered or sold within the PRC by means of this document or any other document. This document may not be distributed, re-distributed or published in the PRC, except under circumstances that will result in compliance with any applicable laws and regulations. If and when the material accompanying this document relates to the products and/or services of ANZ China, the following statement and the text below is applicable: This document is distributed by ANZ China in the Mainland of the PRC.

Qatar. This document has not been, and will not be:

- lodged or registered with, or reviewed or approved by, the Qatar Central Bank (**QCB**), the Qatar Financial Centre (**QFC**) Authority, QFC Regulatory Authority or any other authority in the State of Qatar (**Qatar**); or
- authorised or licensed for distribution in Qatar,

and the information contained in this document does not, and is not intended to, constitute a public offer or other invitation in respect of securities in Qatar or the QFC. The financial products or services described in this document have not been, and will not be:

- registered with the QCB, QFC Authority, QFC Regulatory Authority or any other governmental authority in Qatar; or
- authorised or licensed for offering, marketing, issue or sale, directly or indirectly, in Qatar.

Accordingly, the financial products or services described in this document are not being, and will not be, offered, issued or sold in Qatar, and this document is not being, and will not be, distributed in Qatar. The offering, marketing, issue and sale of the financial products or services described in this document and distribution of this document is being made in, and is subject to the laws, regulations and rules of, jurisdictions outside of Qatar and the QFC. Recipients of this document must abide by this restriction and not distribute this document in breach of this restriction. This document is being sent/issued to a limited number of institutional and/or sophisticated investors (i) upon their request and confirmation that they understand the statements above; and (ii) on the condition that it will not be provided to any person other than the original recipient, and is not for general circulation and may not be reproduced or used for any other purpose.

Singapore. This document is distributed in Singapore by the Singapore branch of ANZ solely for the information of "accredited investors", "expert investors" or (as the case may be) "institutional investors" (each term as defined in the Securities and Futures Act Cap. 289 of Singapore). ANZ is licensed in Singapore under the Banking Act Cap. 19 of Singapore and is exempted from holding a financial adviser's licence under Section 23(1)(a) of the Financial Advisers Act Cap. 100 of Singapore.

United Arab Emirates (UAE). This document is distributed in the UAE or the Dubai International Financial Centre (**DIFC**) (as applicable) by ANZ. This document does not, and is not intended to constitute: (a) an offer of securities anywhere in the UAE; (b) the carrying on or engagement in banking, financial and/or investment consultation business in the UAE under the rules and regulations made by the Central Bank of the UAE, the Emirates Securities and Commodities Authority or the UAE Ministry of Economy; (c) an offer of securities within the meaning of the Dubai International Financial Centre Markets Law (DIFCML) No. 12 of 2004; and (d) a financial promotion, as defined under the DIFCML No. 1 of 200. ANZ DIFC Branch is regulated by the Dubai Financial Services Authority (**DFSA**) ANZ DIFC Branch is regulated by the Dubai Financial Services Authority (**DFSA**). The financial products or services described in this document are only available to persons who qualify as "Professional Clients" or "Market Counterparty" in accordance with the provisions of the DFSA rules. In addition, ANZ has a representative office (**ANZ Representative Office**) in Abu Dhabi regulated by the Central Bank of the UAE. The ANZ Representative Office is not permitted by the Central Bank of the UAE to provide any banking services to clients in the UAE.

United States. Except where this is a FX- related document, this document is distributed in the United States by ANZ Securities, Inc. (**ANZ SI**) which is a member of the Financial Regulatory Authority (**FINRA**) (www.finra.org) and registered with the SEC. ANZSI's address is 277 Park Avenue, 31st Floor, New York, NY 10172, USA (Tel: +1 212 801 9160 Fax: +1 212 801 9163). ANZSI accepts responsibility for its content. Information on any securities referred to in this document may be obtained from ANZSI upon request. This document or material is intended for institutional use only – not retail. If you are an institutional customer wishing to effect transactions in any securities referred to in this document you must contact ANZSI, not its affiliates. ANZSI is authorised as a broker-dealer only for institutional customers, not for US Persons (as "US person" is defined in Regulation S under the US Securities Act of 1933, as amended) who are individuals. If you have registered to use this website or have otherwise received this document and are a US Person who is an individual: to avoid loss, you should cease to use this website by unsubscribing or should notify the sender and you should not act on the contents of this document in any way. Non-U.S. analysts: Non-U.S. analysts may not be associated persons of ANZSI and therefore may not be subject to FINRA Rule 2242 restrictions on communications with the subject company, public appearances and trading securities held by the analysts. Where this is an FX-related document, it is distributed in the United States by ANZ's New York Branch, which is also located at 277 Park Avenue, 31st Floor, New York, NY 10172, USA (Tel: +1 212 801 916 0 Fax: +1 212 801 9163).

Vietnam. This document is distributed in Vietnam by ANZ or ANZ Bank (Vietnam) Limited, a subsidiary of ANZ.

This document has been prepared by ANZ Bank New Zealand Limited, Level 26, 23-29 Albert Street, Auckland 1010, New Zealand, Ph 64-9-357 4094, e-mail nzeconomics@anz.com, http://www.anz.co.nz