

NEW ZEALAND ECONOMICS RBNZ DEPUTY GOVERNOR SPENCER SPEECH

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SOMETHING IS COMING, JUST NOT YET

KEY POINTS

- RBNZ Deputy Governor Spencer has given a speech titled “Housing risks require a broad policy response” to the New Zealand Institute of Valuers in Wellington.
- It should come as no surprise that the RBNZ is becoming increasingly concerned about broadening housing market strength and the associated increases in credit growth. It has noted this before, but Spencer was explicit that “Evidence from housing cycles in several advanced economies suggests that the longer this continues, the more likely there will be a severe correction.”
- Speculation was that something on the macro-prudential policy front was reasonably imminent. Instead we got a signal that something was around the corner. Little surprise to see the NZD up half a cent. Spencer listed three possibilities:
 1. To adopt a single national LVR limit for investors. It believes such a measure could be introduced by the end of the year.
 2. Introduce a new debt-to-income speed limit. This would need to be agreed with the Minister of Finance under the Memorandum of Understanding, and more consultation with banks is needed.
 3. **Increase bank’s capital requirements.** A review of bank capital requirements is occurring over the coming year.
- **We shouldn’t be overly critical that** nothing concrete was announced today. We all know markets do have tendency to get ahead of themselves and given the complexity of issues facing the housing market it’s better to move slowly and surely than early and lacking sound analysis.
- Elsewhere, there were the usual suspects in the speech. Emerging imbalances are an issue and need to be tackled on a number of fronts. Supply needs to be upped. **On the demand side it’s all about** population and easy credit. The direct reference to easy credit is telling. Obviously a low cost of credit makes debt levels more affordable. And herein lies the rub; taking the OCR even lower will only exacerbate that further and mean more debt and higher imbalances. **So you can’t divorce monetary policy from financial stability.**
- Does this alter odds for an August OCR cut? Certainly Spencer noted that “further reductions in the OCR could pose a risk to financial stability”. **But at the same time he also noted that “the outlook for the CPI inflation will ultimately determine the future path of monetary policy.”**
- New Zealand has a currency problem, but also a housing one. There is no guarantee tweaks to the OCR will fix the former but certainly lower interest rates will exacerbate problems in the later (and excesses are now clearly flowing into inflation so it’s not purely a stability issue). The outlook for the OCR is delicately placed. August still looks a close call to us. Technically we are still calling a cut, but with each passing day of data developments **(despite the high NZD), a lower OCR just doesn’t sit right (unless we see a global accident, which to be fair is not low odds).**

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