

Economic Bulletin.

14 April 2021



Biding their time – RBNZ Monetary Policy Review, April 2021.

- The Reserve Bank left monetary policy settings unchanged, as expected.
- The bottom line was almost identical to the February review.
- The RBNZ is waiting until it is confident about a sustained lift in inflation before it starts to withdraw stimulus.
- The key word is ‘sustained’ – inflation will jump higher this year, but due to factors that are seen as temporary.
- The global environment remains uncertain, and the domestic economy has cooled as the absence of overseas tourists has been felt more keenly.
- The RBNZ will wait and watch the impact of the Government’s recent housing policy announcement.
- Our view remains that the OCR will stay unchanged until 2025.

Michael Gordon, Acting Chief Economist

+64 9 336 5670

The Reserve Bank kept all of its policy settings unchanged at today’s Monetary Policy Review, with the Official Cash Rate remaining at 0.25% and no changes in large-scale bond purchases or the Funding for Lending Programme for bank. While this was the first occasion since the RBNZ was freed from its self-imposed commitment to not change the OCR for 12 months, there was little prospect of a change this time. The RBNZ believes that it has already put a substantial amount of monetary stimulus in place, and is now prepared to let it run its course.

As we noted in our forecast update last week, we expect the OCR to remain unchanged until early 2025. That’s in keeping with the sorts of timelines that overseas central banks will be looking at, as they try to navigate through this uncertain environment. However, it remains somewhat out of step with global financial markets, where a rebound in inflation still tends to dominate their thinking.

Details.

The bottom line of the RBNZ’s statement was more or less identical to the February review:

The Committee agreed to maintain its current stimulatory monetary settings until it is confident that consumer price inflation will be sustained at the 2 percent per annum target midpoint, and that employment is at or above its maximum sustainable level. Meeting these requirements will necessitate considerable time and patience. The Committee agreed that it was prepared to lower the OCR if required.

In terms of inflation, the key word is ‘sustained’. The RBNZ knows that annual inflation is set to jump higher in the near term, to around 2.5% or more by the June quarter. Global supply chain disruptions and soaring shipping costs are putting upward pressure on a range of imported goods prices,



and oil prices are sharply higher compared to where they were in mid-2020 at the depths of the Covid crisis.

But these pressures are likely to fade as the shipping industry restores capacity, and oil prices won't repeat that same rate of growth. We expect that by 2022 annual inflation will be back in the lower half of the RBNZ's target range.

For a sustained rise in inflation, we'd need to see rising prices feeding back into inflation expectations and wage-setting. And the domestic economy isn't quite strong enough to support that yet. The initial resurgence as the country was released from lockdown has since cooled a little, and the absence of overseas tourists has been felt more keenly over the summer months. Unemployment is still above pre-Covid levels, and a full recovery awaits on a reopening of the international borders.

We're probably actually past the worst in terms of the tourism impact. In normal times, the flow of people into the country peaks early in the year, and turns to a net outflow by March. But because of the publication lag, the data over the next couple of months is likely to remain on the softer side.

The confirmation of a trans-Tasman travel bubble from 19 April is great news for local tourism operators, and those hoping to see friends and family for the first time in over a year. But as the RBNZ correctly points out, the net impact on the economy will depend on the two-way nature of this travel. In 2019 our net tourism earnings with Australia were about \$500m, or 0.15% of GDP. Even a complete restoration of these flows would have only a marginal impact on GDP growth this year.

The housing market didn't feature much in the RBNZ's statement, despite the developments on this front since February. First, the Minister of Finance has added housing as a consideration to the RBNZ's remit. On the monetary policy side, it's a fairly weak change – the RBNZ is required to assess how its decisions affect the Government's wider housing affordability goals, but it doesn't have to respond to house prices in any way. The RBNZ concluded that monetary stimulus has played a role in lifting house prices, but that it was one among a host of factors. It also noted that the distributional impacts of low mortgage rates are ambiguous.

The incorporation of housing into the RBNZ's financial stability remit is potentially more significant. The Minister of Finance had asked the RBNZ for information on the role of high debt-to-income and interest-only mortgages (presumably with an eye towards restrictions on these). The RBNZ noted that it has prepared some preliminary material, which will feature in next month's *Financial Stability Report*.

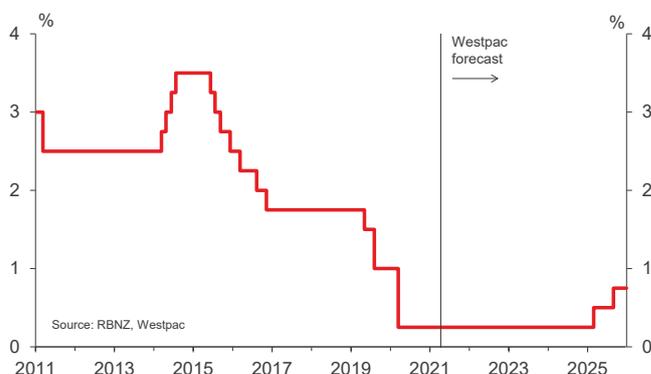
The bigger development was the Government's announcement of changes to the tax treatment of property investors. We think this will be quite effective in dampening investor demand (and likely making restrictions on high debt-to-income lending redundant). However, the RBNZ took a more circumspect approach, noting that the impact "will take time to be observed". The RBNZ was already forecasting an abrupt slowdown in house price growth from the second half

of this year, so the Government's policy announcement plays into that view nicely.

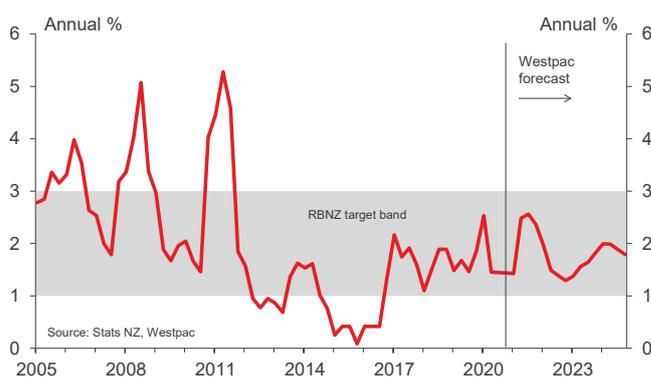
The RBNZ ended by reiterating that it is prepared to take the OCR lower, even below zero, if conditions warrant. The RBNZ's attitude towards a negative OCR has been in stark contrast to some of its peers such as the Reserve Bank of Australia and the US Federal Reserve – it has long listed a negative OCR as one of its favoured options for 'unconventional' monetary easing, and has worked to establish that banks' systems are prepared to handle it.

That said, the case for going negative has diminished since last year as the economic outlook has improved. We suspect that taking the OCR negative would require evidence of a sudden shift down in domestic activity. If the outlook is more towards a slow pace of recovery, then keeping the existing stimulus measures in place for longer may be more appropriate.

Westpac OCR forecast



Consumer price inflation forecast



Contact the Westpac economics team.

Michael Gordon, Acting Chief Economist

+64 9 336 5670

Satish Ranchhod, Senior Economist

+64 9 336 5668

Nathan Penny, Senior Agri Economist

+64 9 348 9114

Paul Clark, Industry Economist

+64 9 336 5656

Gregorius Steven, Economist

+64 21 713 363

Any questions email:

economics@westpac.co.nz

Past performance is not a reliable indicator of future performance. The forecasts given in this document are predictive in character. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Disclaimer.

Things you should know

Westpac Institutional Bank is a division of Westpac Banking Corporation ABN 33 007 457 141 ("Westpac").

Disclaimer

This material contains general commentary, and market colour. The material does not constitute investment advice. Certain types of transactions, including those involving futures, options and high yield securities give rise to substantial risk and are not suitable for all investors. We recommend that you seek your own independent legal or financial advice before proceeding with any investment decision. This information has been prepared without taking account of your objectives, financial situation or needs. This material may contain material provided by third parties. While such material is published with the necessary permission none of Westpac or its related entities accepts any responsibility for the accuracy or completeness of any such material. Although we have made every effort to ensure the information is free from error, none of Westpac or its related entities warrants the accuracy, adequacy or completeness of the information, or otherwise endorses it in any way. Except where contrary to law, Westpac and its related entities intend by this notice to exclude liability for the information. The information is subject to change without notice and none of Westpac or its related entities is under any obligation to update the information or correct any inaccuracy which may become apparent at a later date. The information contained in this material does not constitute an offer, a solicitation of an offer, or an inducement to subscribe for, purchase or sell any financial instrument or to enter a legally binding contract. Past performance is not a reliable indicator of future performance. Whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The ultimate outcomes may differ substantially from these forecasts.

Country disclosures

Australia: Westpac holds an Australian Financial Services Licence (No. 233714). This material is provided to you solely for your own use and in your capacity as a wholesale client of Westpac.

New Zealand: In New Zealand, Westpac Institutional Bank refers to the brand under which products and services are provided by either Westpac or Westpac New Zealand Limited ("WNZL"). Any product or service made available by WNZL does not represent an offer from Westpac or any of its subsidiaries (other than WNZL). Neither Westpac nor its other subsidiaries guarantee or otherwise support the performance of WNZL in respect of any such product. The current disclosure statements for the New Zealand branch of Westpac and WNZL can be obtained at the internet address www.westpac.co.nz. For further information please refer to the Product Disclosure Statement (available from your Relationship Manager) for any product for which a Product Disclosure Statement is required, or applicable customer agreement.

China, Hong Kong, Singapore and India: This material has been prepared and issued for distribution in Singapore to institutional investors, accredited investors and expert investors (as defined in the applicable Singapore laws and regulations) only. Recipients in Singapore of this material should contact Westpac Singapore Branch in respect of any matters arising from, or in connection with, this material. Westpac Singapore Branch holds a wholesale banking licence and is subject to supervision by the Monetary Authority of Singapore. Westpac Hong Kong Branch holds a banking licence and is subject to supervision by the Hong Kong Monetary Authority. Westpac Hong Kong branch also holds a license issued by the Hong Kong Securities and Futures Commission (SFC) for Type 1 and Type 4 regulated activities. This material is intended only to "professional investors" as defined in the Securities and Futures Ordinance and any rules made under that Ordinance. Westpac Shanghai and Beijing Branches hold banking licenses and are subject to supervision by the China Banking and Insurance Regulatory Commission (CBIRC). Westpac Mumbai Branch holds a banking license from Reserve Bank of India (RBI) and subject to regulation and supervision by the RBI.

UK: The contents of this communication, which have been prepared by and are the sole responsibility of Westpac Banking Corporation London and Westpac Europe Limited. Westpac (a) has its principal place of business in the United Kingdom at Camomile Court, 23 Camomile Street, London EC3A 7LL, and is registered at Cardiff in the UK (as Branch No. BR00106), and (b) authorised and regulated by the Australian Prudential Regulation Authority in Australia. Westpac is authorised in the United Kingdom by the Prudential Regulation Authority. Westpac is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. Details about the extent of our regulation by the Prudential Regulation Authority are available from us on request. Westpac Europe Limited is a company registered in England (number 05660023) and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.

This communication is being made only to and is directed at (a) persons who have professional experience in matters relating to investments who fall within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "Order") or (b) high net worth entities, and other persons to whom it may otherwise lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (all such persons together being referred to as "relevant persons"). Any person who is not a relevant person should not act or rely on this communication or any of its contents. The investments to which this communication relates are only available to and any invitation, offer or agreement to subscribe, purchase or otherwise acquire such investments will be engaged in only with, relevant persons. Any person who is not a relevant person should not act or rely upon this communication or any of its contents. In the same way, the information contained in this communication is intended for "eligible counterparties" and "professional clients" as defined by the rules of the Financial Conduct Authority and is not intended for "retail clients". With this in mind, Westpac expressly prohibits you from passing on the information in this communication to any third party. In particular this communication and, in each case, any copies thereof may not be taken, transmitted or distributed,

directly or indirectly into any restricted jurisdiction. This communication is made in compliance with the Market Abuse Regulation (Regulation(EU) 596/2014).

Investment Recommendations Disclosure

The material may contain investment recommendations, including information recommending an investment strategy. Reasonable steps have been taken to ensure that the material is presented in a clear, accurate and objective manner. Investment Recommendations for Financial Instruments covered by MAR are made in compliance with Article 20 MAR. Westpac does not apply MAR Investment Recommendation requirements to Spot Foreign Exchange which is out of scope for MAR.

Unless otherwise indicated, there are no planned updates to this Investment Recommendation at the time of publication. Westpac has no obligation to update, modify or amend this Investment Recommendation or to notify the recipients of this Investment Recommendation should any information, including opinion, forecast or estimate set out in this Investment Recommendation change or subsequently become inaccurate.

Westpac will from time to time dispose of and acquire financial instruments of companies covered in this Investment Recommendation as principal and act as a market maker or liquidity provider in such financial instruments.

Westpac does not have any proprietary positions in equity shares of issuers that are the subject of an investment recommendation.

Westpac may have provided investment banking services to the issuer in the course of the past 12 months.

Westpac does not permit any issuer to see or comment on any investment recommendation prior to its completion and distribution.

Individuals who produce investment recommendations are not permitted to undertake any transactions in any financial instruments or derivatives in relation to the issuers covered by the investment recommendations they produce.

Westpac has implemented policies and procedures, which are designed to ensure conflicts of interests are managed consistently and appropriately, and to treat clients fairly.

The following arrangements have been adopted for the avoidance and prevention of conflicts of interests associated with the provision of investment recommendations.

- (i) Chinese Wall/Cell arrangements;
- (ii) physical separation of various Business/Support Units;
- (iii) and well defined wall/cell crossing procedures;
- (iv) a "need to know" policy;
- (v) documented and well defined procedures for dealing with conflicts of interest;
- (vi) steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

U.S: Westpac operates in the United States of America as a federally licensed branch, regulated by the Office of the Comptroller of the Currency. Westpac is also registered with the US Commodity Futures Trading Commission ("CFTC") as a Swap Dealer, but is neither registered as, or affiliated with, a Futures Commission Merchant registered with the US CFTC. Westpac Capital Markets, LLC ("WCM"), a wholly-owned subsidiary of Westpac, is a broker-dealer registered under the U.S. Securities Exchange Act of 1934 ("the Exchange Act") and member of the Financial Industry Regulatory Authority ("FINRA"). This communication is provided for distribution to U.S. institutional investors in reliance on the exemption from registration provided by Rule 15a-6 under the Exchange Act and is not subject to all of the independence and disclosure standards applicable to debt research reports prepared for retail investors in the United States. WCM is the U.S. distributor of this communication and accepts responsibility for the contents of this communication. All disclaimers set out with respect to Westpac apply equally to WCM. If you would like to speak to someone regarding any security mentioned herein, please contact WCM on +1 212 389 1269. All disclaimers set out with respect to Westpac apply equally to WCM.

Investing in any non-U.S. securities or related financial instruments mentioned in this communication may present certain risks. The securities of non-U.S. issuers may not be registered with, or be subject to the regulations of, the SEC in the United States. Information on such non-U.S. securities or related financial instruments may be limited. Non-U.S. companies may not be subject to audit and reporting standards and regulatory requirements comparable to those in effect in the United States. The value of any investment or income from any securities or related derivative instruments denominated in a currency other than U.S. dollars is subject to exchange rate fluctuations that may have a positive or adverse effect on the value of or income from such securities or related derivative instruments.

The author of this communication is employed by Westpac and is not registered or qualified as a research analyst, representative, or associated person under the rules of FINRA, any other U.S. self-regulatory organisation, or the laws, rules or regulations of any State. Unless otherwise specifically stated, the views expressed herein are solely those of the author and may differ from the information, views or analysis expressed by Westpac and/or its affiliates.