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ECONOMIC ALERT

MPS — MAY 2019

8 May 2019 | www.bancorptreasury.com

"The Official Cash Rate (OCR) has been reduced to 1.5 percent."

Why …

"The outlook for employment growth is more subdued and capacity pressure is expected to ease slightly in 2019. Consequently, inflationary pressure is projected to rise only slowly."

And …

"Inflation expectations remain well anchored at the mid-point of the target range."

And …

"A lower OCR now is most consistent with achieving our objectives and provides a more balanced outlook for interest rates."

And …

"The Committee was more concerned about a continued slowdown rather than a faster recovery."

In conclusion …

"After discussing the relative benefits of holding the OCR and committing to a downward bias, versus cutting the OCR now so as to establish a more balanced outlook for interest rates, the Committee reached a consensus to cut the OCR to 1.50 percent."

Market Implications

Markets went into today's *Monetary Policy Statement* ("MPS") announcement and Monetary Policy Committee ("MPC") decision with pricing evenly split between no change and an OCR cut. So, half of the market was always going to be happy with today's decision and the other half disappointed.

The New Zealand dollar and local interest rates fell in an immediate adjustment to the lower OCR. However, there was little follow through falls because the forecasts contained in the MPS related to a pre OCR cut scenario.

Comment

The inaugural meeting of the Reserve Bank's MPC decided on a pre-emptive OCR cut. The official Reserve Bank forecasts contained in the MPS, assumed an OCR cut in August or September (the actual forecast has the OCR bottoming out at 1.4% in the March 2020 quarter and slowly rising from the September 2021 quarter).

Clearly today's decision was between *"holding the OCR and committing to a downward bias, versus cutting the OCR now."* The MPC decided, apparently unanimously, to start boldly.

A complication in today's MPS is that the Reserve Bank forecasts pre-date today's OCR cut. When the Reserve Bank's forecasts are adjusted for this cut, there is a strong argument for the OCR to bottom out at 1.50% in the current cycle.

Our main conclusions from today's decision and reasons for it are that a pre-emptive OCR cut was needed *"to establish a more balanced outlook for interest rates"* and that the RBNZ now has a balanced, 'wait and see' stance.

That balanced stance ensured limited falls by the New Zealand dollar and local interest rates today and will ensure heightened anticipation of future Reserve Bank relevant economic data and developments.