

# The Rural Loan Report

February 2015



Benchmark Interest Rates	Current	Month ago	Year ago	10-year Average	Outlook*
Official Cash Rate	3.50	3.50	2.50	4.55	→
90-day bank bill	3.64	3.67	2.93	4.82	→
1-year Swap Rates	3.60	3.74	3.50	4.94	↘
3-year Swap Rates	3.62	3.79	4.21	5.23	↘
5-year Swap Rates	3.67	3.82	4.62	5.43	↘

\* Rates current as at 16 February 2015

\*\*Outlook is over the next 6 months

## Key points

- We expect the Reserve Bank to be on hold for the foreseeable future.
- Also at the moment, gaining some certainty by locking in a medium- or long-term rate is inexpensive.
- Meanwhile, rates could potentially head marginally lower this year before rising in 2016.
- All up, we are in for lengthy period of low interest rates.

## Reserve Bank: interest rates could go “up or down”

The Reserve Bank (RBNZ) has shifted to a neutral stance. In its January announcement, it raised the possibility that the next move in the Official Cash Rate (OCR) could be “up or down.”

A key development in this regard has been the dramatic plunge in oil prices. With the resulting dive in local petrol prices, the RBNZ now expects headline inflation to remain below its target band (1%-3%) through 2015 and take longer to return to the middle of the band.

Prior to the announcement, we moved in to a view that the RBNZ would stay on the interest rate sidelines foreseeable future i.e. over 2015 and 2016. Around that view, we see the risks to the OCR as skewed more up than down over the longer term. However, markets have – very understandably – continued to price in the chance of OCR cuts in the short term, given easing policy by a large number of central banks globally.

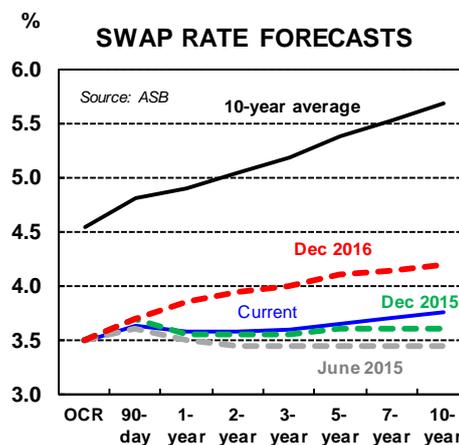
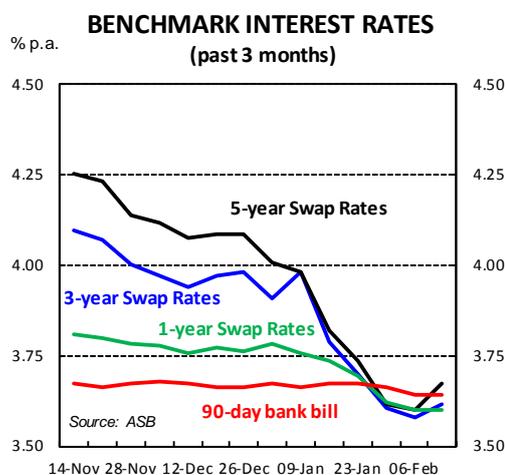
Those moves have seen long-term interest rates slide. Over the last month, 3-year swap rates, for example, have fallen a touch under 20 basis points.

## Interest Rates Outlook

Over the next six months, we expect short-term rates to largely tread water as the RBNZ stays on hold. However, the risks appear skewed to a cut in the OCR, with a low tolerance for further weak inflation data and some concerns around economic momentum in China.

Longer-term rates are being pulled in opposite directions, but, on balance, we expect a marginal fall over the next six months. Low or falling global rates such as those in Australia and Europe are keeping the downward pressure on longer-term NZ rates, while the RBNZ remaining on hold is having a similar effect. However, pulling NZ rates the other way is a potential lift in rates by the US Federal Reserve as the US economy continues to improve. At this stage, we judge the former will dominate the latter in the short term.

All up, by historical standards we are in for a lengthy period of low interest rates.



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