

The Rural Loan Report

May 2016



Benchmark Interest Rates (%)*	Current	Month ago	Year ago	10-year Average	Outlook**
Official Cash Rate	2.25	2.25	3.50	4.06	↘
90-day bank bill	2.40	2.33	3.62	4.30	↘
1-year Swap Rates	2.30	2.24	3.56	4.42	↘
3-year Swap Rates	2.35	2.32	3.55	4.76	↘
5-year Swap Rates	2.55	2.56	3.67	5.00	↘

*Rates current as at 29 April 2016

**Outlook is over the next 6 months

Key points

- All rates remain very low, despite the unchanged Official Cash Rate last month.
- However, we expect the Reserve Bank will be pressed to cut rates over coming months.
- In turn, we expect floating and short-term interest rates to fall, while long-term rates will at least stay low, if not fall.

ASB expects the RBNZ to cut the OCR by 50bps

The Reserve Bank (RBNZ) is in no immediate hurry to cut the Official Cash Rate (OCR). Indeed, the RBNZ kept the OCR unchanged at 2.25% last month, while still hinting at a cut later this year, stating “further policy easing may be required.”

Following the “on-hold” 28 April announcement, **short-term rates have nudged higher, but rates generally remain very low.** For example, all the benchmark rates sit over a percent lower than the same time a year ago and remain well down on their 10-year averages.

However, we expect the RBNZ to be pressed into action soon. **Our view is that the RBNZ will cut the OCR by 50bps this year to 1.75%.**

In particular, **we expect still low inflation, reinforced by a resilient NZ dollar, to drive the move lower.** With NZ interest rates relatively high by international standards, international investors still favour the NZD. Indeed, rates in our closest neighbour, Australia, have just been cut and could fall further over coming months.

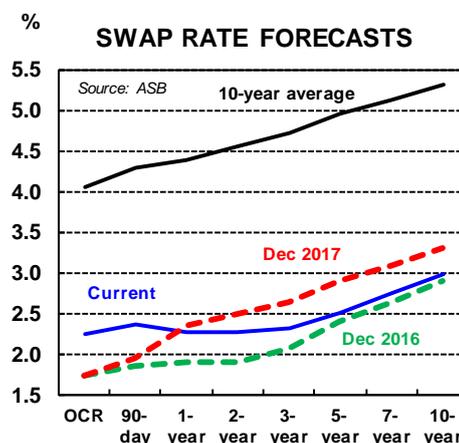
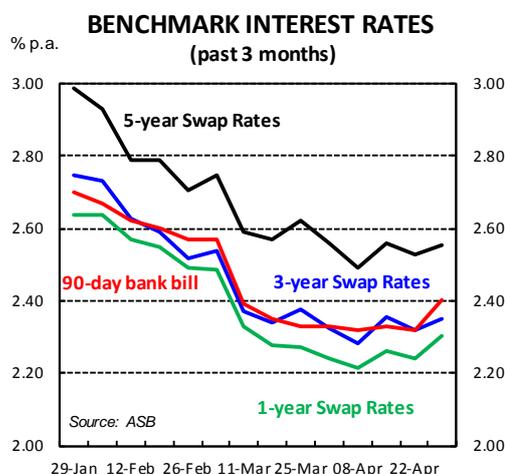
While the re-heating Auckland housing market complicates the interest rate picture, the RBNZ has other tools to counter that strength. As a result, **we expect the RBNZ to announce additional home lending restrictions as well, and for these measures to provide the necessary room for the OCR to head lower.**

Interest Rates Outlook

If the RBNZ cuts the OCR, **we expect the floating rates and very short-term fixed rates to fall over the next six months.** Although, with banks paying more for their offshore funding recently, the floating rate falls, for example, may be less than the usual one-for-one.

Longer-term rates are also likely to fall over the year, but not by as much. With offshore interest rates also important for NZ’s long-term rates, any moves higher by the US Federal Reserve may partially offset RBNZ cuts.

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



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