Macro-prudential policy

Slides for RFI Roundtables

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Outline

- Macro-prudential policy objectives
- Policy instruments
- Implementation
- Governance and accountability
- Points raised in the Reserve Bank’s public consultation

Objectives

- Macro-prudential policy aims to promote financial stability by:

  - *building additional resilience in the financial system during periods of rapid credit growth and rising leverage or abundant liquidity; and*

  - *dampening excessive growth in credit and asset prices.*

Policy instruments

System-wide tools	**Core funding ratio** Greater use of stable funding e.g. deposits, long-term wholesale funding	**Counter-cyclical capital buffer** Extra capital required against total lending book
Targeted tools	**Sectoral capital requirements** Extra capital required against lending to risky sector(s) e.g. housing, commercial property, agriculture	**Housing loan-to-value restrictions** Option 1 - outright caps  Option 2 - speed limits 

Implementation

- Tools used temporarily to manage extremes of credit cycle
- Tools need to be used early enough to build buffers/lean against cycle
- Could be a single tool or a mix of tools
- Instruments are not monetary policy tools
  - But likely to support the Official Cash Rate
- All tools have costs and risks as well as benefits
  - efficiency, disintermediation and avoidance

Governance and accountability

- Memorandum of Understanding between Governor and Minister of Finance
- Consultation with Minister ahead of decision
- Final decisions would rest with Reserve Bank
- Financial Stability Report – will be key accountability document

Submissions (1)

- Submissions generally supportive of proposed objectives but a few asked …
  - Could the tools be used more actively to assist other policy goals e.g. monetary policy, exchange rate management, housing affordability?
  - Is existing prudential regulation not sufficient?

- RBNZ Response:
  - Macro-prudential tools may assist monetary policy but not as powerful as OCR
  - Tools intended to bolster existing prudential regulation during extremes in credit and asset price cycles

Submissions (2)

- Much of the focus was on LVR restrictions:
  - Concern about 1st home buyers, SMEs, Christchurch rebuild, Welcome Home Loans
  - Could LVRs be applied with regionally or with exemptions?
  - Risks of disintermediation were noted

- RBNZ response:
  - Policy focus is on high-risk borrowing –1st home buyers are a big driver of Auckland market
  - Exemptions or regional use poses practical difficulties:
    - But there is a government policy case for exempting Welcome Home Loans
  - Disintermediation risks need to be carefully monitored
    - Might still need to contemplate extension beyond the banks

Submissions (3)

- Feedback on effectiveness of tools
  - LVRs likely to be better for dampening credit cycle but costly (eg in terms of fairness, disintermediation)
    - Costs would be mitigated under "speed limit" approach
  - Other macro-prudential tools:
    - banks might simply opt to run down existing funding or capital buffers if these exceed the requirement
    - impact on lending/pricing will depending on market conditions and competition considerations

- RBNZ response:
  - Market conditions and state of banks' balance sheets will be part of instrument choice/calibration decision
  - Capital and funding tools may be more effective in building resilience than dampening credit cycle
  - Instrument choice will balance effectiveness and cost/risk considerations

Submissions (4)

- Clarity sought on the risk indicators used to guide macro-prudential policy
- Mixed views on proposed notice periods
- A few submitters proposed other tools
  - *eg debt service ratios*

- RBNZ response:
  - We will continue to publish guidance on our macro-prudential indicators
  - Notice periods balance need to be timely and avoid pre-emptive borrowing behaviour
  - Other instruments may be considered in future

Next Steps

- Enhancing data collection
  - *Loan-to-value ratios*

- Banking Supervision Handbook
  - *Instrument preparedness*
  - *Operational details of tools*
  - *Consultation with industry*

End