Reserve Bank
of New Zealand
Te Pūtea Matua

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Financial Stability Report SNAPSHOTS

Financial system well placed to support economic recovery despite uncertainty and risks.

Ongoing challenges from COVID-19 are affecting many businesses and making the future hard to plan for. Stretched house prices and climate change also present risks to financial stability. However, banks’ capital levels have risen, making them more resilient to potential losses and well positioned to meet upcoming higher capital requirements.

The financial system remains sound and financial institutions have increased their resilience.

The economy has recovered well but the current outbreak continues to create uncertainty.

Housing market momentum has continued, with recent buyers more vulnerable to a fall in house prices.

Understanding and managing climate-related risks is necessary for financial stability.

The financial system remains sound and financial institutions have increased their resilience.

- The global economy continues to face challenges from the COVID-19 pandemic and the economic outlook remains uncertain. Despite this, New Zealand's financial system has been resilient and continues to support households and businesses as they manage their way through the pandemic.
- Banks have built robust liquidity positions and increased their capital ratios, meaning that they are well placed to absorb the near-term impacts of the current COVID-19 outbreak, and to meet upcoming higher requirements coming as a result of the Capital Review. Our 2021 stress test of New Zealand's five largest banks highlighted increased resilience to a severe but plausible economic downturn.

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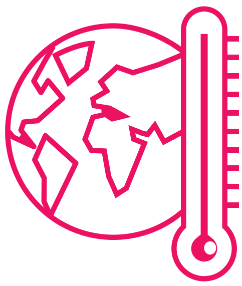
- Economic activity in New Zealand was back to strong levels prior to the August lockdown, with households and businesses experiencing a significant recovery in economic conditions, supported by fiscal and monetary policy.
- However, restrictions brought in to contain the recent Delta outbreak are presenting economic challenges, particularly for the Auckland region. The global economy also continues to face challenges with ongoing supply chain issues creating additional costs for businesses here and abroad and contributing to higher inflation. Resulting higher interest rates could prove to be a headwind to asset prices. Transitioning to 'living with COVID-19' in the community could affect consumer preferences and behaviours, and the viability of some businesses may be challenged.

Housing market momentum has continued, with recent buyers more vulnerable to a fall in house prices.

- The household sector has endured the pandemic quite well so far, supported by a resilient labour market. However, continued strong demand for housing is creating price pressure, resulting in recent buyers borrowing more relative to their income.
- Loan-to-value ratio restrictions have been further tightened to lean against financial stability risks resulting from the housing market. We will soon consult on forms of debt servicing restrictions which would further bolster households' resilience and broader financial stability.

Understanding and managing climate-related risks is necessary for financial stability.



- Climate change presents both long-term risks and opportunities to financial institutions. The physical impacts of climate change are already becoming more common, which means increasing claims for insurers and greater risk to properties that banks use to secure their lending, among many other impacts.
- Understanding and managing climate-related risks is necessary to support ongoing financial stability. Our actions to support this were recently published in a climate change report. Our 2021 stress test programme is considering the impacts of droughts and other extreme weather events on banks and insurers. We are undertaking further analysis of the impacts of climate change to understand the extent of these risks.