Economic outlook

Reserve Bank of New Zealand
May 2020
Disclaimer:

This presentation represents the view of the Monetary Policy Committee, not of any individual member.
The Monetary Policy Statement at a glance

• The Reserve Bank’s Monetary Policy Statement (MPS) provides a quarterly picture of the New Zealand economy and where we think it is heading next.

• It sets out how the Bank has implemented monetary policy and how it plans to do so in the next five years.
Overview

• The spread of COVID-19 and related containment measures have had an unprecedented impact on economic activity globally
• The extent and persistence of this decline is very uncertain
• Fiscal policy is providing significant support to the economy
• Considerable monetary stimulus is needed to complement fiscal policy, we have reduced the OCR to 0.25% and implemented a Large Scale Asset Purchase programme
Impacts of COVID-19 on the New Zealand economy
COVID-19 containment measures have significantly reduced economic activity

GDP by industry during alert levels 3 and 4
(as % of pre-COVID level)

Source: RBNZ estimates. Note: This figure shows output by industry as a share of its pre-COVID level. A value of 100 percent means that the industry is producing the same as it normally would. A lower value indicates output has fallen because of the closure of non-essential businesses or reduced productivity.
Border restrictions have hit tourism and education sectors particularly hard

Overseas arrivals
(7-day moving average)

Source: Customs NZ. Note: This chart includes all arrivals to New Zealand on commercial air services, except those travelling on New Zealand passports. The data will include New Zealand residents arriving on non-New Zealand passports.
Household spending is set to decline as wage growth slows and unemployment rises.

Consumption and Electronic Card Spending

*(annual)*

Nominal private consumption + exports of travel services

Source: Stats NZ, RBNZ estimates.
Lower incomes and greater uncertainty leads firms to scale back investment plans

Source: ANZ. Note: ANZBO investment intentions measures the net percentage of firms that report an increase or decrease in intended investment.
The economic downturn is reducing demand for labour

Unemployment rate and job seeker support recipients

(share of labour force)

Source: Stats NZ, Ministry of Social Development.
Labour market slack is emerging and employment is expected to remain below MSE for some time
Inflationary pressures fall over 2020

Inflation expectations

Source: Stats NZ, RBNZ estimates.
International economy and financial markets
Growth slows for New Zealand’s main trading partners in 2020

Trading partner growth and IMF forecasts (annual)

Source: Haver Analytics, IMF.
In response to COVID-19, Governments announce large fiscal stimulus packages...

Fiscal support
/share of GDP/

Source: IMF. Note: Figures relate to COVID-19 relief and recovery measures announced as at 30 April 2020 and does not consider when the spending occurs.
... And central banks are engaging in substantial monetary policy easing, with many having reduced policy rates

Central bank policy rates

Source: Bloomberg.
Scenario analysis helps to set policy

• Given the unparalleled current environment, the economic outlook is very uncertain.

• Current estimates of the appropriate monetary policy stance are imprecise.

• We outline three scenarios to demonstrate some possible paths the economy could take.
  • Baseline scenario
  • Longer lockdown scenario
  • Slower recovery scenario
# Key forecast assumptions in the May *Statement*

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<thead>
<tr>
<th>New Zealand GDP falls in 2020 and growth remains subdued for some time</th>
<th>Global growth also declines in 2020, suppressing global inflation</th>
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<tr>
<td>Labour market to soften considerably</td>
<td>Inflation to fall relative to target</td>
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All scenarios indicate a sharp decline in economic activity...

GDP

(s.a.)

Source: Stats NZ, RBNZ estimates. Note: The series has been rebased to equal 100 in 2019 Q4
...causing employment to drop substantially...

Unemployment rates

Source: Stats NZ, RBNZ estimates.
..alongside a sharp temporary dip in inflation

Source: Stats NZ, RBNZ estimates.
Considerable monetary stimulus is needed to meet our objectives over the medium term.

Unconstrained Official Cash Rate

Source: RBNZ estimates. Note: Quarterly average.
Policy responses to date

- Fiscal policy is providing considerable support to households and business. Since early March, the Government has announced more than $20 billion in fiscal support and has provisioned for significantly more.

- OCR was cut 75bp to 0.25 percent in March and is intended to stay at this level for at least a year.

- A Large Scale Asset Purchase (LSAP) programme also began in March, and has been expanded up to $60 billion of central and local government bonds over 12 months.
Fiscal spending cushions the economic impact of COVID-19 and supports a faster recovery.

COVID-19 fiscal package
(as at 6 May)

- Wage subsidy $12.0b
- Tax relief $5.9b
- Income support $2.8b
- Health $0.6b
- Other $1.6b

Source: RBNZ estimates.
Note: These indicative estimates are derived from information outlined in Government press releases. Our projections incorporate a further $30 b fiscal spending spread over the projection period.
LSAPs support the Monetary Policy Committee’s employment and inflation objectives through three main channels:

- Lowering interest rates throughout the economy
- Lowering the New Zealand dollar exchange rate
- Increasing inflation expectations
The LSAP programme has successfully lowered interest rates on government bonds

Interest rates on New Zealand Government bonds

Source: Bloomberg.
Interest rate market have stabilised

Stabilisation of benchmark yield curves

Dysfunctional markets (26 March)  Functional markets (4 May)

Source: Bloomberg.
Local Government Funding Agency (LGFA) bond purchases have improved monetary policy transmission

Source: Bloomberg, RBNZ.
However, we have not yet seen full pass through to retail rates

Mortgage rates

Source: interest.co.nz, RBNZ estimates. Note: The rates shown for each term are the average of the latest rates on offer from ANZ, ASB, BNZ, and Westpac.
Summary

• The spread of COVID-19 and related containment measures have had an unprecedented impact on economic activity globally

• The extent and persistence of this decline is very uncertain

• Fiscal policy is providing significant support to the economy

• Considerable monetary stimulus is needed to complement fiscal policy, we have reduced the OCR to 0.25% and implemented a Large Scale Asset Purchase programme

• The Monetary Policy Committee stand ready to act further if needed
Thank you
Extra slides
Unemployment in New Zealand’s key trading partners is forecast to rise

Trading partner unemployment rates and IMF forecasts (s.a.)

Source: Haver Analytics, IMF.
We’re working closely with the whole of Government and industry to keep our financial system stable ensuring foreign exchange, debt and money markets are operating efficiently and at low cost. We’re keeping cash-flow moving around the economy - between banks, firms, households, and the Government.

We’ve got a broad range of initiatives in place to respond to COVID-19

Monetary policy: we’re keeping interest rates low to build confidence and enable cheaper lending for businesses and households
- We’ve lowered the Official Cash Rate to 0.25% and are committed to keeping it there for the next year.
- We’re keeping long-term interest rates down by buying $30bn of government bonds and $3 billion of Local Government Funding Agency (LGFA) debt in the secondary market over a 12 month period. This takes the total size of the Large Scale Asset Purchases programme to $33 billion over 12 months.

Financial Stability: we’re ‘banking the banks’ to maximise their access to cash and keep the economy stable
- We’re ensuring banks can access enough cash to keep lending long-term at low interest rates (ESAS tiers, Term Auction Facilities and Term Lending Facility) and we’re providing additional channels for banks to keep funding corporate clients (Corporate Open Market Operations).
- We’ve also removed mortgage loan-to-value ratio (LVR) restrictions for the next 12 months. This is to ensure LVR restrictions don’t have an undue impact on borrowers or lenders as part of the mortgage deferral scheme implemented in response to the COVID-19 pandemic. It will help banks support their customers and removes a potential obstacle to the flow of credit in the economy, helping to soften the downturn and maintain financial stability.

Meeting the needs for access to cash: we’re making sure there’s plenty of cash and it’s safe to use
- Cash is well distributed to ensure people can access it all around New Zealand.
- We’re monitoring and working closely with cash system players to ensure a stable supply.

We’re working with the Government to support households and businesses
- We’ve helped roll out the Government mortgage payment deferrals and business finance guarantee scheme. To help banks and other regulated firms focus on supporting households and businesses, we’ve deferred some regulatory initiatives, including the planned increases in bank capital requirements, and we’re allowing firms some delays in their reporting and disclosure.

The Government is also supporting households and businesses directly.
- Helping people maintain cash flow and connection to employment through income support, redeployment and wage subsidies.
- Ensuring viable and important businesses – big and small – can bridge through the difficulties ahead, through financial support and regulatory tax changes.

More information on Reserve Bank initiatives at www.rbnz.govt.nz/covid-19
More information on Government financial support at www.covid19.govt.nz