



May News 2016

Current Interest Rates *

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Variable	5.65%
6 Month Fixed	4.75%
1 Year Fixed	4.25%
18 Months Fixed	4.79%
2 Year Fixed	4.19%
3 Year Fixed	4.65%
4 Year Fixed	5.35%
5 Year Fixed	5.35%

* All rates subject to change without notice and not available to all borrowers.

RBNZ Preparing Debt Limits - By Bernard Hickey

Welcome to the May 2016 Edition

The Reserve Bank signalled in May it is considering introducing a new British-style Debt-to-Income (DTI) limit on lending as it grapples with a resurgent housing market and the need to cut interest rates again without pouring more fuel on a hot market.

Governor Graeme Wheeler and his deputy Grant Spencer told a news conference after the release of the Bank's half yearly Financial Stability Report (FSR) on May 11 that they were concerned enough about the revival of house price inflation in Auckland and beyond that they were actively looking at a DTI limit.

They did not indicate any timeframes or potential levels for such a limit, but it was enough to prompt some property industry figures and politicians to warn it would hurt demand in the market, and could hammer first home buyers and new home buyers in particular.

The Bank of England limited DTI lending above 4.5 to no more than 15% of new mortgage lending from October 2014 and the Reserve Bank said in its FSR that almost 60% of property investors and 35% of owner/occupiers in New Zealand had total DTIs of over 5. The Reserve Bank would not say what level it could set its limit at, but a limit of 5 would have a significant impact on investors in particular.

However, Finance Minister Bill English and Prime Minister John Key both said they were open to the idea, although they said they were confident the Reserve Bank would take into account the unintended consequences on first home buyers and on new home building.

Both politically and economically, the Reserve Bank and the Government will be reluctant to discourage new home building in particular and to further penalize first home buyers.

The Reserve Bank is most likely to target rental property investors, as it did with its second round of Loan to Value Ratio (LVR) controls in November last year, and to exempt lending for new home building. However, a new DTI limit may not necessarily target Auckland, as the second round of LVR controls did. Spencer told a select committee after the release of the FSR that he preferred a broad tool that was used across the country, given the 'Halo Effect' of Auckland's boom was spreading to the rest of the country. He also highlighted the role of investors in the continued resurgence through March and April across the country.

Some have said the Reserve Bank could formulate a new DTI tool within three months, but that is less likely given the Bank has yet to make a formal proposal and would need to consult with banks, the Government and others before it launched the tool. A November 30 announcement with the next FSR is more likely.

Meanwhile, the drums are beating for further interest rate reductions because inflation remains below the Reserve Bank's 1-3% target band and the New Zealand dollar remains uncomfortably high. The Reserve Bank held off cutting on April 28, but said "further easing may be required." Financial markets are expecting the Official Cash Rate to be cut again to 2.0% on June 9 and most economists see another cut later in 2016 or early 2017 to 1.75%, particularly if a new DTI tool gives the bank more flexibility to cut more without fuelling the fire in the housing market.

The bottom line:

- Inflation remains weak and deflationary headwinds continue to blow from the rest of the world, pushing down on interest rates.
- The Reserve Bank is expected to cut by a further 50 basis points over the next year starting from June 9. Fixed mortgage rates are falling again.
- The Reserve Bank is considering introducing a Debt to Income multiple limit that could target investors and exempt new builds. It may be announced in November.
- Economic growth is solid at 3% because net migration is at 100-year highs, tourism is booming and construction surges in Auckland and Christchurch are offsetting the dairy slump.
- House price inflation has accelerated across the country since February as the effects of last year's Reserve Bank (LVR version 2) and Government (Bright Line test and new disclosure rules) measures washed out.