

Falling dairy prices to prompt OCR cuts

OCR cut predictions have taken a big step up following the latest fall in dairy prices.

Thursday, July 2nd 2015 by Miriam Bell

Last night's GlobalDairyTrade auction delivered more bad news for the dairy sector with prices falling by 5.9%.

The fall was just the latest in a long series, but it took dairy prices to a new low and put paid to hope that prices might stabilise.

In the wake of the news, economists have been predicting the Reserve Bank will up the rate of its OCR cuts over the rest of 2015.

ASB chief economist Nick Tuffley said the RBNZ is likely to cut the OCR three times before the end of the year – with the first cut coming in July. “We think the RBNZ will cut to 2.5% by the end of the year.” Tuffley said the prediction was not just because of the latest fall in dairy prices.

It is also because dairy prices will now take longer to recover and because business sentiment surveys are indicating reduced confidence.

The market has been pricing in cuts, he continued. “So if the OCR does fall further - to say 2.75% - then there is still scope for short term fixed rates to move a bit lower.”

Tuffley noted that this scenario could further fuel the housing market and, in turn, macro-prudential concerns.

ANZ chief economist Cameron Bagrie agreed that more OCR cuts were in the winds.

He said the latest fall in dairy prices definitely skewed the risk profile to the RBNZ further easing the OCR.

“There will definitely be a cut in July. And we are picking another two by the end of the year.”

New Zealand's economy is experiencing a softening in momentum, he said.

“So, at a time of low inflation pressures and a shifting risk profile, we are seeing the RBNZ embark on a modest easing cycle.”

Bagrie also thought that, as the market has been pricing in about 50/60 basis cuts, if the RBNZ does make those cuts, there could be further falls in one year fixed rates.

Meanwhile, Westpac chief economist Dominick Stephens has been predicting that the RBNZ will cut the OCR further in both July and September.

In his view, interest rates are likely to remain under downwards pressure for some time.

HSBC chief economist Paul Bloxham has taken a slightly different view.

He has predicted the RBNZ will react to the growing pressure and cut the OCR to 3.0% in July.

“However, after that, we expect the RBNZ to hold steady and for a rising trend in inflation to keep them comfortably on hold at 3.00%.”