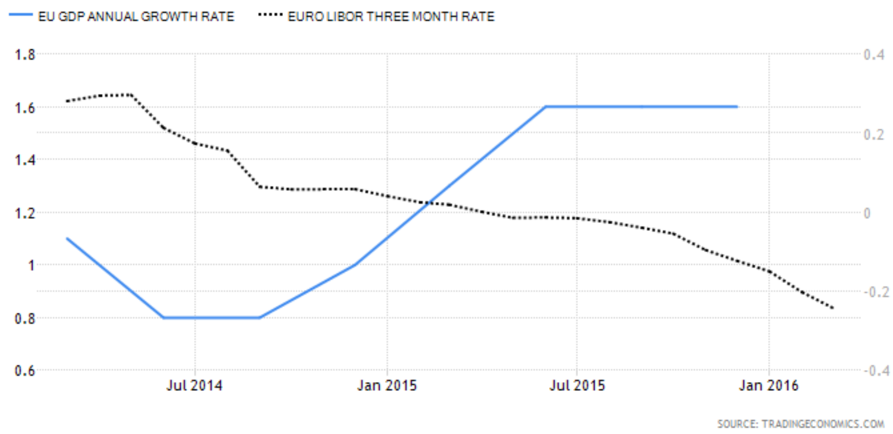
NEGATIVE INTEREST RATES – THEY DIDN'T TEACH THIS AT UNIVERSITY

Negative Interest Rates, I'm pretty certain this concept was never covered in any economic lectures I ever attended. After all who would have thought we would see the day global economies around the world would find themselves in such desperate circumstances that a number of Central Banks would resort to drastic measures in an attempt to stimulate economic growth?

For those who are a little unsure of the concept, a number of Central Banks including the European Central Bank (ECB) and the Bank of Japan (BOJ) have made radical adjustments to their **deposit rates** (the rate at which the financial institutions deposit their surplus reserves with the central bank) **by pushing the rate into negative territory**. Simply put, rather than receive interest for surplus reserves deposited with the central bank, financial institutions instead pay for the privilege. In theory its meant to achieve two things; **First** the cost incentivizes the financial institutions to minimise their surplus reserves held with the central bank by lending to other parties at a better rate (interbank rate) **addressing the issue of liquidity** among banks and non-banks that plagued the financial markets during the Global Financial Crisis. **Second** the interbank rate, determined by supply and demand in the short term cash market among banks and non-bank participants to settle obligations, serves as **the direct "monetary policy transmitter" influencing the lending rate banks charge to the real economy.**



The motivation behind adopting a **negative interest rate policy** is to **drive rates lower on other financial instruments in an attempt to entice businesses and consumers to borrow and spend to stimulate overall economic activity**. However as the above chart reveals, in practice the results aren't always supportive of theory. Despite the radical adjustment, GDP growth in the Eurozone has stalled while Japan, Switzerland and Denmark who have also implemented negative deposit rates are experiencing a slowdown in GDP growth. It leaves many wondering if the experiment fails, what other tools are available to stimulate economic growth. Specifically on our own shores it begs the question, if the RBA was forced to reduce the cash rate will monetary policy prove to be as influential as it has in the past, given the current economic background?

The adverse results we see from the cases above point to a key problem faced by monetary policy, **dealing with unpredictable behaviour.** Central Banks can force rates as low as they choose but **if businesses and consumers are unwilling to borrow and spend, <u>Monetary Policy proves ineffective</u>**. Results so far abroad and at home highlight this is becoming the case, instead looking more like an escalation of **currency wars** rather than a genuine attempt to stimulate economic activity.

Unfortunately Australia is faced with the same dilemma; Rising Debt-to-Income ratios, Declining Wage Growth, Declining Savings Rate and the Anaemic Level of Business and Consumer Confidence are among a number of long existing trends dampening appetite for commercial and housing credit, investment and consumer spending which is beginning to weigh on the performance of the property market and in recent weeks has prompted banks, specifically the ANZ and WBC to increase their provisions for bad debts. These trends point to exhaustion in the capacity of consumers to borrow, creating a **significant roadblock** that will profoundly impact the influence of further loosening in Monetary Policy by the RBA to stimulate economic activity.

While the picture we paint seems bleak enough to make many believe we are staring down the barrel of Financial Armageddon, this is simply not the case. Instead the implication here is a number of trends that have long clouded our economy are now materialising adding another layer of risk that is looking increasingly beyond the control of Monetary Policy, conventional or not. **What this highlights is the significant importance <u>Fiscal Policy</u> now holds in changing the direction of our economy**, **<u>and there is a potential saviour</u>**. The $1.1 Billion National Innovation and Science Agenda (NISA) that will form part of the 2016-2017 Budget, due on the 3rd May, is the very catalyst Australia needs to kick-start the economy. We can only hope Malcolm Turnbull is able to implement the NISA as Prime Minister **far better** than he did the NBN as the Communications Minister. Its feasible then over the short term until the NISA begins to embed itself within the broader economy and we are gifted a few budget surprises, **we will likely remain fixed in the current state of Economic Purgatory**.

<u>DAYLIGHT SAVINGS – ADJUSTMENT TO TRADING HOURS</u>

Daylight Savings has officially concluded in NSW. As a resultfrom today our **office hours will adjust to 7:30am to 4pm (WST)**, while the ASX trading hours will adjust to **8am to 2pm (WST).**

Performance of Key Indices

Equities	*Close*	*Change (M)*	*Change % (M)*
All Ordinaries	5151.8	+203.9	+ 4.12%
S&P/ASX200	5082.8	+201.9	+4.14%
Dow Jones (US)	17685.09	+1168.59	+7.08%
NASDAQ	4869.85	+311.90	+6.84%
S&P500	2059.74	+127.51	+6.60%
FTSE 100 Index	6174.90	+77.81	+1.28%
Nikkei 225 (Japan)	16758.67	+731.91	+4.57%
10-year bond rate (US)	1.77%	+0.00034	+1.96%

Upcoming RBA Events

Reserve Bank Interest Rate Decision–5th April
Minutes of Monetary Policy – 19th April

ABS releases March

Retail Trade (February) – 4th April
Building Approvals (February)–4th April
International Trade in Goods and Services (February) – 5th April
Housing Finance (February) – 11th April
Lending Finance (February) – 13th April
Sales of New Motor Vehicles (March) – 18th April
Consumer Price Index (March) – 27th April

Upcoming US Economic Releases

Employment Situation – 1st April
ISM Manufacturing Index - 1st April
International Trade – 5th April
FOMC Minutes – 6th April
Producer Price Index – 13th April
Retail Sales – 13th April
Consumer Price Index – 14th April
Industrial Production – 15th April
Housing Starts – 19th April
Existing Home Sales – 20th April
New Home Sales – 25th April
Durable Goods Orders – 26th April
FOMC Meeting Announcement – 27th April
GDP – 28th April
Jobless Claims - Weekly Basis