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While the recent increase in the RBNZ's Official Cash Rate will result in a rise in most banks' floating mortgage rates, borrowers are still likely to move to the floating mortgage rate.

Recent RBNZ statistics show that, by volume, around a third of all residential mortgages are at the floating mortgage rate. This is a significant increase from two years ago when only 12% of mortgages were at the floating rate. This trend of borrowers using the floating rate is likely to continue despite today's rise in the OCR, according to Dave Wilson, Investment Strategist at New Zealand Funds Management.

Wilson says previously in New Zealand fixed rate mortgages were lower than floating rate mortgages as New Zealand had a negative yield curve. "That situation is now reversing," Wilson says. "Economically, fixed term mortgage rates offer borrowers certainty and borrowers should expect to pay a premium for this certainty. This means fixed rate mortgages are now likely to remain higher than floating rate mortgages."

New Zealand has been at odds with Australia where most mortgages are at the floating rate. As homeowners move to the floating rate, the efficacy of monetary policy is likely to be more immediate. In the past, it took a number of months for the impact of a higher OCR to affect homeowners. This increased the complexity for the RBNZ in implementing monetary policy.

Wilson also believes property investors and homeowners are likely to face further constraints and costs on borrowing into the future as the Reserve Bank moves to increase the effectiveness of monetary policy on the property market.

On the 1st April, all registered banks were required to seek 65% of their funding from core and stable sources such as consumer deposits or debt instruments with greater than a year to maturity. In 2012, that core ratio will increase to 75%. The average core funding ratio for banks in the past 12 years has been between 55-65%.

This move will put increased pressure on banks to increase their core funding and impose further constraints on property lending. "The Reserve Bank is expecting this move to act as an automatic stabiliser and temper lending in an easy credit environment. This means banks will only be able to increase their balance sheet by increasing core funding."

The combination of increasing interest rates through the official interest rate and implementing stricter prudential policy via the hiked core funding ratios is designed to act in tandem to curb speculative aspects of the housing market.

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