ANZ Research

Review of the RBNZ April Monetary Policy Review

10 April 2024

Contact

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Confused by acronyms or jargon? See a glossary here.

Keep calm and carry on

- As universally expected, the RBNZ today left the OCR unchanged at 5.5%, with the accompanying commentary very similar to February.
- As in February, "The Committee agreed that interest rates need to remain at a restrictive level for a sustained period".
- We continue to expect that the RBNZ will require considerably more certainty before contemplating cuts. Current upside risks on the tradable inflation front got very little airtime in RBNZ comments, but they do highlight the fact that headline CPI inflation is still a long way from where it needs to be. We continue to expect cuts won't be on the table until 2025.

In brief

As anticipated, the RBNZ today left the Official Cash Rate (OCR) unchanged at 5.5% and kept the tone of the (incredibly short) Policy Assessment extremely similar to that of the February MPS.

The Record of Meeting shows that the Committee discussed a range of upside and downside risks to the inflation outlook, but saw nothing to cause them to deviate from their "watch, worry and wait" stance, with no need nor desire to take a strong stance on when cuts will come at this point.

Key quotes:

- **OCR outlook:** "The Committee agreed that interest rates need to remain at a restrictive level for a sustained period."
- **Labour market:** "Members noted the large decline over recent quarters in the share of firms reporting difficulty in finding labour."
- **Domestic activity:** "The New Zealand economy continues to evolve as anticipated by the Monetary Policy Committee. … Economic growth in New Zealand remains weak."
- **Inflation:** "the Committee is confident that maintaining the OCR at a restrictive level for a sustained period will return consumer price inflation to within the 1 to 3 percent target range this calendar year."
- **Global growth outlook:** "Globally, while there are differences across regions, economic growth remains below trend and is expected to remain subdued."
- **Global central banks:** "most major central banks are cautious about easing monetary policy given the ongoing risk of persistent inflation."
- **Global inflation:** "Aggregate commodity price indices have remained relatively stable despite ongoing geopolitical uncertainties. Oil prices have increased while agricultural commodity prices have generally been weaker."
- **Exchange rate:** no comment.
- **Housing market:** no comment.

Our take

The weakness in demand and activity evident in both the Q4 GDP outturn and the Q1 NZIER QSBO has no doubt reinforced the RBNZ's confidence that domestic inflation is on track to ease meaningfully over coming quarters. The news is less comforting on the global inflation front, with the oil price markedly higher, but that only got the most passing of mentions. If domestic inflation proves stickier than expected and/or there is evidence of flow-through impacts onto broader price pressures and inflation expectations the RBNZ may have a problem, but that's not a problem for today.

Our OCR forecast remains unchanged: we expect domestic inflation will fall a little more slowly than the RBNZ expects and so currently see cuts as a 2025 story.

CPI inflation next week will be closely watched. It's looking like the RBNZ will get yet another upside surprise on domestic inflation (the fourth in a row, but the underlying disinflation trend remains intact). Labour market data on 1 May is arguably actually more important. We expect it to confirm the clear message coming from business surveys – that the labour market is no longer inflationary as strong growth in labour supply meets weakening labour demand.

The RBNZ will also have the Budget high-level numbers in hand for its May Monetary Policy Statement, but awkwardly, won't be able to talk about them, as the Budget is released the following week.

All told, today's Review was a placeholder, as expected. Kudos to the RBNZ for efficiently issuing the shortest Policy Assessment ever seen so we can all get back to watching, worrying and waiting.

Market reaction

Today's Monetary Policy Review came and went without fanfare, with the RBNZ playing with a straight bat. Their view that the economy has evolved broadly as expected and that the outlook for inflation remains as it was in February isn't suggestive of any hurry to change stance, and against the backdrop of a market (particularly offshore participants) that saw the potential for a further dovish tilt, we may see mild upside pressure on short-end rates and the NZD over coming days. However, we wouldn't overplay it. Not only was the policy assessment very short (see below – a mere eight sentences), but the tone was very balanced, and market expectations for cuts had already backed up over recent days.

OCR 5.50% - Official Cash Rate remains unchanged

The Monetary Policy Committee today agreed to leave the Official Cash Rate (OCR) at 5.50 percent.

The New Zealand economy continues to evolve as anticipated by the Monetary Policy Committee. Current consumer price inflation remains above the Committee's 1 to 3 percent target range. A restrictive monetary policy stance remains necessary to further reduce capacity pressures and inflation.

Globally, while there are differences across regions, economic growth remains below trend and is expected to remain subdued. However, most major central banks are cautious about easing monetary policy given the ongoing risk of persistent inflation.

Economic growth in New Zealand remains weak. While some near-term price pressures remain, the Committee is confident that maintaining the OCR at a restrictive level for a sustained period will return consumer price inflation to within the 1 to 3 percent target range this calendar year.

Monetary Policy Committee record of meeting

The Monetary Policy Committee discussed recent developments in the New Zealand and global economies. The Committee agreed that the New Zealand economy has evolved largely as expected since the February Statement. Restrictive monetary policy is contributing to an easing in capacity pressures to ensure inflation returns to target.

Economic growth in most of New Zealand's major trading partners has been below trend. However, this has varied across regions, with stronger activity in the United States compared with the Euro Area and Australia. Economic growth in most major economies is forecast to slow further over 2024. In China, policymakers have announced a similar growth target for this calendar year, which may be difficult to achieve amid ongoing structural challenges.

The Committee noted that in most major economies the better balance between the demand for, and supply of, labour has been reflected in a decline in job vacancies. However, growth in unit labour costs remains elevated. Inflation will continue to be persistent in regions where higher labour costs have not been accompanied by improved productivity or reduced profit margins.

Most major central banks remain cautious about easing monetary policy given the risks of inflation persistence and elevated inflation expectations. Financial market pricing for most central bank policy rates continues to imply some easing later this year, although this has lessened over recent weeks. Participants in global financial markets continue to exhibit strong confidence in the corporate earnings outlook, as reflected in equity prices and credit spreads.

Aggregate commodity price indices have remained relatively stable despite ongoing geopolitical uncertainties. Oil prices have increased while agricultural commodity prices have generally been weaker. The recent spike in global shipping costs, which has partially receded, has yet to be observed in New Zealand merchandise trade data. This timing is consistent with information from discussions with businesses that suggest shipping contracts in New Zealand are typically renegotiated every three to six months.

The Committee discussed domestic economic data released since the February Statement. Gross Domestic Product for the December 2023 quarter was close to expectations and implies a continued easing in capacity pressure in the economy. Some higher frequency indicators suggest a modest recovery in activity in the first quarter of 2024. However, measures of business confidence have declined and firms' own expectations for activity and investment have weakened. Near-term business pricing intentions have declined but remain elevated, in part reflecting an uptick in both realised and expected costs.

The Committee noted that recent monthly Selected Price Indices (SPI) imply some upside risk to the March 2024 quarter Consumers Price Index (CPI). The Committee agreed that there was large monthly variability in the SPI series and noted that recent relative price changes are due mostly to volatile components including fuel, domestic airfares, and overseas accommodation.

The Committee noted the continued strength in net migration, which is supporting aggregate consumer spending and rising dwelling costs. While the rate of net migration has declined from its recent peak, there have been significant upward revisions to recent historical data. Net migration also adds to labour supply in the economy and has helped to alleviate capacity pressures. Members noted the large decline over recent quarters in the share of firms reporting difficulty in finding labour.

The Committee discussed the outlook for fiscal policy and its implications for monetary policy. Based on the most recent published forecasts in the Half-Year Economic and Fiscal Update, and the commitments outlined in the Budget Policy Statement, the Committee noted that government expenditure is indicated to decline as a share of the economy in coming years.

Domestic financial conditions have eased marginally since the February Statement with declines in wholesale interest rates and the New Zealand dollar. There have been modest reductions in retail interest rates. However, these remain consistent with the Committee's restrictive monetary policy stance, with credit growth remaining subdued. The Committee noted that despite a reduction in wholesale funding costs, term deposit rates were little changed reflecting increasing competition for retail deposits.

The Committee discussed whether recent developments in the New Zealand and global economies had implications for when inflation returns to target. Members agreed that there had not been a material change since the February Statement and that monetary policy settings continue to constrain demand broadly as expected. Members agreed that there remains limited tolerance to increase the time to achieve the inflation target while inflation remains outside the target band and while inflation expectations and pricing intentions remain elevated.

The Committee discussed upside risks to the inflation outlook. Members agreed that persistence of services inflation remains a risk and goods price inflation remains elevated. Anticipated near-term increases to local government rates, insurance, and utility costs, could also further slow the decline in headline inflation.

The Committee discussed downside risks to the inflation outlook. Members noted that ongoing restrictive monetary policy in an environment of weak global growth could lead to a more rapid decline in inflation than expected. Business and consumer confidence remain particularly weak which could lead to more unemployment and financial stress than expected. Structural challenges facing the economy in China remain a concern given its importance for the global economy and for New Zealand's trade.

Overall, members agreed that the balance of risks was little changed since the February Statement. Ongoing restrictive monetary policy settings are necessary to reduce inflation, while avoiding unnecessary instability in output, employment, interest rates and the exchange rate.

In discussing the appropriate stance of monetary policy, members agreed they remain confident that monetary policy is restricting demand. A further decline in capacity pressure is expected, supporting an ongoing decline in inflation. The Committee agreed that interest rates need to remain at a restrictive level for a sustained period to ensure annual consumer price inflation returns to the 1 to 3 percent target range. On Wednesday 10 April, the Committee reached a consensus to keep the Official Cash Rate at 5.50 percent.

Attendees

MPC members: Adrian Orr (Chair), Bob Buckle, Carl Hansen, Caroline Saunders, Christian Hawkesby, Karen Silk, Paul Conway

Treasury Observer: Tim Ng

MPC Secretary: David Craigie

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