

# RBNZ speech on potential impacts of oil shock

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## Reassurance

- The RBNZ Governor Breman struck a reassuring tone today in a speech about the potential impacts on the New Zealand economy of the Middle East oil shock. It's early days, and "wait and see" was very much the tone.
- Market pricing has moved dramatically in recent times to price three hikes this year. The Governor noted that monetary policy would only have to respond with a higher OCR than otherwise if medium-term inflation or inflation expectations threaten to move away from the 2% midpoint.
- Our own take is along the same lines. We have recently [upgraded our CPI forecast](#), [downgraded our GDP forecast](#), and like the RBNZ are watching for the [potentially offsetting impacts on medium term inflation](#) via upside risks to inflation expectations but downside risks to economic slack.
- The 2-year swap fell around 5bp following the speech.

## Wait and see

As context for the speech, it's important to note that the New Zealand rates market has moved sharply in recent days and weeks, which has tightened monetary conditions considerably. Before market open today, almost 90bp of hiking was priced this year, versus just 25bp after the February Monetary Policy Statement.

Figure 1. Wholesale swap rates



Source: Bloomberg, Macrobond, ANZ Research

Given illiquidity and volatility we'd certainly caution against reading pricing as a literal reflection of expectations of how the RBNZ will respond, but whatever the driver, it's a sharp move, and looks unwarranted in a fundamentals sense. Accordingly, in a [speech](#) today Governor Breman did what she could to calm the waters by reminding listeners about how central banks react to negative supply shocks such as this, providing reassurance that there will be no knee-jerk hawkish response to the inevitable near-term spike in inflation.

## Key quotes

### Let's not overreact:

- “We should try to avoid reacting too early to near-term inflation pressures that monetary policy can do little about – or reacting too late if above-target inflation becomes embedded in the economy.”
- “The picture changes if this disruption is longer lasting... or if there is a greater risk of heightened oil and other import prices feeding into higher inflation expectations and inflationary wage- and price-setting behaviour.”
- “Tightening monetary policy in response to a short-lived disruption would only dampen growth without materially improving near-term inflation outcomes.”

### The economic starting point is not strong:

- “The New Zealand economy continues to operate below capacity.”
- “Household and business balance sheets are also more fragile, with less scope to absorb significant price increases.” As a result “It may be harder for businesses to increase prices, and it could be less likely that short-term price pressures... become embedded.”
- “We may see somewhat weaker economic growth in 2026”
- “Rising uncertainty tends to weigh on business investment and household spending.”
- “Higher wholesale interest rates and lower equity prices are already tightening global financial conditions.”

### At the same time, the RBNZ needs to remain alert to inflation risks:

- “We could still see higher inflation over the medium term.”
- “We will be looking closely at second round impacts, such as price- and wage-setting behaviour.”
- “The best contribution monetary policy can make... is to deliver low and stable inflation.”
- “If there are effects on medium-term inflation or inflation expectations, the appropriate policy response could be to increase interest rates to prevent these second round effects. We would need tighter monetary policy to make sure inflation expectations remained well-anchored at 2 percent, and that inflation remains within our target band of 1 to 3 percent over the medium term.”

### A reminder about the appropriate role of fiscal policy, with an eye to the lessons of the COVID era:

- “Fiscal policy, not monetary policy, is best placed to provide targeted support to households.”
- “Targeted responses [must be] timely and temporary, to avoid sustained upward pressure to inflation.”

### And reassurance that financial stability is not an issue:

- “...there is a risk that global financial stability risks could emerge and affect the cost and availability of funding for New Zealand banks. However, recent stress testing suggests that banks are resilient with strong capital and liquidity buffers, and are well-placed to weather severe geopolitical shocks.”

## Our take

The Governor's comments today are very much in line with our own thinking. There are a number of ways this could play out, and wait and see is the appropriate response. The RBNZ will need to constantly reassess and rebalance the risks of inflation pressures becoming embedded with the risk of causing unnecessary economic pain in what is already a difficult situation. We continue to forecast that the first OCR hike will come in December, but we cannot emphasise enough that uncertainty is the only certainty at present.

## **Market reaction**

Markets went into this hoping for a composed message highlighting the importance of not jumping to conclusions, and that it will take time to assess the impact of the conflict, and that's what we got. Not surprisingly, short-end interest rates fell after the speech was released, with the 2-year swap down around 5bp to 3.56%. That's a reasonable reaction, but against the backdrop of volatility and lower global interest rates overnight and earlier this morning ahead of the speech, it is difficult to precisely disentangle the impact of Governor Breman's comments from global moves.

Consistent with the oil-shock playbook, Breman noted that "a short-lived disruption and a temporary increase in petrol prices can – and should – be looked through from a monetary policy perspective if it is unlikely to have an impact on medium-term inflation", reiterating that the inflation target is forward-looking. Obviously, if the conflict becomes protracted, it may well be appropriate to tighten policy, but as Breman noted, the Bank's task will be all about "balancing higher near-term inflation and potentially higher inflation expectations against a weaker growth outlook". We think her calm and considered messaging should be reassuring for markets. However, in this environment, ongoing volatility can be expected.

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