

NEW ZEALAND ECONOMICS RBNZ MPS PREVIEW

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CUT AND POLISH

KEY POINTS

- **We expect the RBNZ will cut the OCR by 25bps to 1.75% on Thursday.** This is a view shared by the consensus and market.
- **While the merits of further easing can certainly be debated (there are strong economic reasons for standing pat, reasons for which we have a lot of sympathy), the RBNZ's forward guidance and clear focus on inflation at a time growth has been strong suggests they will follow through.** It was only two weeks ago that Assistant Governor McDermott reinforced that cuts were still a part of the Bank's base case. And let's not forget, if the Bank doesn't move in November, the next scheduled meeting is now not until February.
- **The focus in this Statement will be all about the RBNZ's forward guidance and tone.** Does it cut but signal that it is likely done, shifting to a more neutral stance, or will it retain further easing as its base case? **We doubt it will do either, instead striking somewhat of a middle ground in an attempt to appease financial markets (read: stop too much NZD collateral damage) but not look too out of tune with the economic picture.** In practice, that balancing act is likely to prove difficult. 'Neutral' risks inflaming the currency, while flagging an even lower OCR profile amidst tightening capacity constraints strains credibility.
- **We expect a mild easing bias, as distinct from an explicit one.** All that needs to be done in the key final paragraph is to formally link the outlook more explicitly to the pricing side of the economy in combination with the broader economy. With the domestic economy growing strongly and signs that the inflation cycle is turning (both at a headline but also domestic price level), we'd be surprised if it is still the case that *"the RBNZ's projections and assumptions indicate that further policy easing will be required"*. The labour market is tightening and capacity pressures are building; it's simply taking time to feed into inflation. The currency is still a problem but the terms of trade are looking a lot better and it's hard to argue against a firm currency given the growth picture. Uplifts in oil prices are mathematically helping the inflation profile (and inflation expectations). The wider economic backdrop is making it more difficult to justify additional cuts. There is of course a chance the OCR goes lower again, but the odds are not greater than 50%. It would now likely take something ugly offshore to drive that scenario.
- **To be fair, the market has largely shifted to this view already.** At the time of writing, it was pricing only an additional 4bps of cuts out to the middle of next year. In many ways, this could give the RBNZ a little more comfort that it doesn't have to get creative with its language in order to appease the market. With its views and the market perhaps broadly consistent already, **it can play with a fairly straight bat. Sometimes it pays to keep things nice and simple. The economic facts (an economy growing well above trend and building capacity pressure) speak for themselves.**

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