MNI RBNZ Preview – August 2022

Meeting Date: Wednesday, 17 August 2022

Statement Release Time: 14:00 NZST/03:00 BST

Press Conference Time: 15:00 NZST/04:00 BST

Link To Statement: https://www.rbnz.govt.nz/monetary-policy/official-cash-rate-decisions

Link To MPS: https://www.rbnz.govt.nz/monetary-policy/monetary-policy-statement

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Central Bank Watch - RBNZ

August 15, 2022

MNI RBNZ Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
CPI (Q)	% y/y	7.3	6.9	↑	5.9	↑					1.29
House Prices	% y/y	9.5	18.8	↓	27.5	↓					-1.49
RBNZ Inflation Exp (Q)	% y/y	3.29	3.27	↑	2.96	↑					1.28
Inflation Breakeven 10Yr	%	3.10	3.12	↓	2.55	↑					1.10
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
ISM	Index	52.7	51.0	↑	52.4	↑					-0.24
GDP (Q)	% y/y	1.2	3.1	↓	-0.2	↑					-0.11
Trade Balance	$mn	-701	-593	↓	-990	↑					-0.23
Exports	$mn	6416	6468	↓	6077	↑					0.66
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Credit Card Sending (Retail)	% m/m	-0.2	7.2	↓	2.7	↓					-0.09
House Sales	% y/y	-36.7	-35.2	↓	-28.6	↓					-1.03
Terms of Trade (Q)	% q/q	0.5	-0.9	↑	0.4	↑					0.08
Commodity Prices	% m/m	-2.2	-1.9	↓	1.0	↓					-0.75
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales (Q)	% q/q	-0.5	8.3	↓	-8.3	↑					-0.24
Consumer Confidence	Index	81.9	84.4	↓	97.7	↓					-0.47
Employment Change (Q)	% q/q	0.0	0.0	→	-0.1	↑					-0.51
Ave Hourly Earnings (Q)	% q/q	2.3	1.9	↑	1.4	↑					1.47
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Equity Market	Index	11801	11884	↓	11889	↓					-0.51
NZ 10-Year Yield	%	3.57	3.65	↓	2.60	↑					0.43
NZ Yield Curve (2s-10s)	bps	5.9	32.8	↓	50.4	↓					-1.76
NZD TWI	Index	72.77	72.43	↑	70.95	↑					-0.78

Note: For quarterly data the 3m ago column will display the previous data point and the 6m ago column will display the data point prior to that.
Source: MNI, Bloomberg

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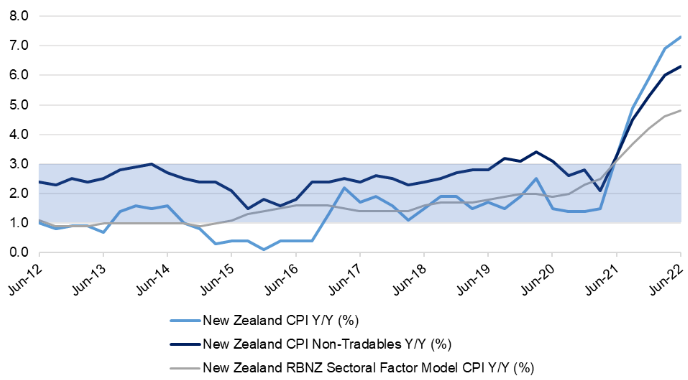
MNI POV (Point Of View): All Eyes On Forward Guidance

Heading into the RBNZ's Monetary Policy Statement this week, virtually all analysts agree that the Committee will raise the Overnight Cash Rate by another 50bp. Inflation is way out of the Reserve Bank's tolerance band and the labour market remains extremely tight, even as headwinds to growth are becoming more evident. We join the consensus call in expecting a half-percentage point move on Wednesday. Barring any surprises on that front (which would take the market off guard indeed), the main highlight of this Monetary Policy Statement will be the Committee's forward guidance, including the updated OCR track.



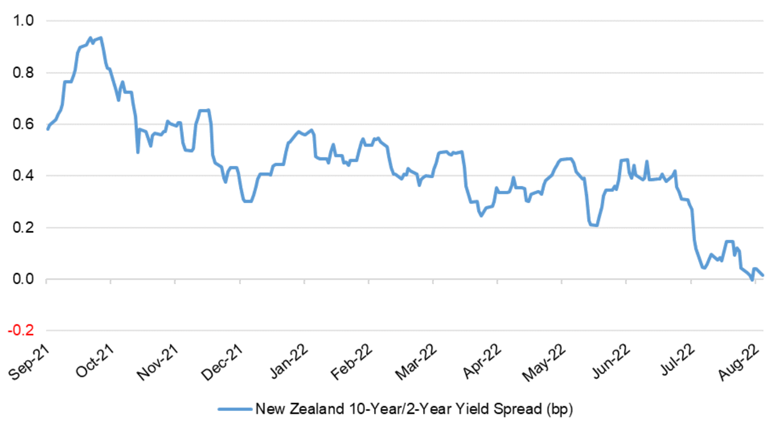
The shaded region represents the RBNZ's inflation target range.

The latest inflation report was, from the RBNZ's perspective, disappointing. Data released just days after the 50bp OCR hike delivered at the July monetary policy review showed that headline price growth accelerated to +7.3% in the second quarter, reaching a 32-year high and exceeding market expectations (+7.1% in a Bloomberg survey) and the RBNZ's own projection from the May MPS (+7.0%). Non-tradable CPI and sectoral factor model inflation also accelerated, signalling that domestically generated price growth was gathering steam.

Extremely tight labour market conditions keep fuelling price pressures. While the unemployment rate surprised in and edged higher amid a slowdown in employment growth and a downtick in participation, it remained near historic lows in Q2. In addition, wage inflation (measured by the Labour Cost Index) accelerated to the fastest pace since late 2008, raising the risk of a wage-price spiral.

On the other hand, recent survey data showed that inflation expectations have eased. The key 2-year out inflation expectations, believed to match the time needed for monetary policy decisions to filter through into the real economy, fell to +3.07% Y/Y from +3.29% in the RBNZ's survey of forecasters, economists and industry leaders. Another poll showed that inflation expectations of New Zealand households stayed broadly unchanged this quarter, while the proportion of respondents expecting higher house prices continued to shrink at a decent pace.

On that last note, the property sector keeps cooling at pace. The latest REINZ House Price Index decreased (on an annual basis) for the first time since mid-2011. In its latest Pain and Gain report, CoreLogic suggested that the market has reached a "turning point" in Q2 as the proportion of properties being sold at a loss edged higher, while average profit on resold houses decreased. In fact, many analysts are calling for a sharper decline in property prices than the 8.1% predicted by the Reserve Bank amid a notable tightening in financial conditions.



Meanwhile, headwinds to growth are intensifying, both domestically and globally. In New Zealand, sentiment among households and firms remains subdued after Q1 GDP report released back in June showed that the economy contracted 0.2% Q/Q. Lingering recession worry was reflected in NZGB yield curve dynamics, with 2-Year/10-Year segment flirting with inversion for the first time since 2015.

Still, we do not think that some green shoots on the inflation front, rapid cooling in the housing market and intensifying growth concerns will be enough to dissuade the MPC from raising the OCR by 50bp this week. Inflation remains well above the target range and acute tightness in the labour market is adding fuel to price growth. Committee members will likely grit their teeth and focus on restoring their inflation-fighting credibility before gradually shifting the emphasis to engineering a soft landing for the economy.

This would be consistent with the Reserve Bank's self-prescribed monetary policy strategy, whereby the Committee prefers taking bolder steps when risks are skewed in one direction to deal with these risks swiftly and return policy settings back to normal. We don't think that macroeconomic trends in New Zealand warrants reducing the pace of policy tightening just yet – with inflation that far from the target and employment still above its maximum sustainable level, taking more heat out of the economy remains a priority.

When this preview is being typed, the OIS strip fully prices a 50bp OCR hike this week and there is broad consensus about the outcome of the meeting. While a 50bp rate hike this week seems is a done deal, the divergence between runaway inflation and slowing growth will force the Committee to perform an increasingly difficult balancing act. Ahead of this meeting, we cannot rule out the dovish risk of early shift in rhetoric to prepare the market for an eventual slowdown in the pace of hikes. By contrast, a strong reaffirmation of exclusive focus on bringing prices under control represents a hawkish risk. In any case, the OCR track and the language of the statement will be closely watched for any tweaks to forward guidance – it will be the sum total of the Committee's forward-looking comments that will set the tone of this MPS.

RBNZ July Monetary Policy Review Announcement

The Monetary Policy Committee today increased the Official Cash Rate (OCR) to 2.50 percent. The Committee agreed it remains appropriate to continue to tighten monetary conditions at pace to maintain price stability and support maximum sustainable employment. The Committee is resolute in its commitment to ensure consumer price inflation returns to within the 1 to 3 percent target range.

The level of global economic activity, combined with the ongoing supply disruptions largely driven by both COVID-19 persistence and the Russian invasion of Ukraine, continue to generate global inflation pressures. Food and energy prices are especially affected by geopolitical tension. However, the pace of global economic growth is slowing. The broad-based tightening in global monetary and financial conditions is acting to reduce spending growth. Asset prices have also declined due to higher interest rates and a weaker earnings outlook.

In New Zealand, domestic spending remains supported by high employment levels, resilient household balance sheets in aggregate, continued fiscal support, and a strong terms of trade. The reduction in COVID-19 health-related restrictions is also enabling increased demand. Labour and resource scarcity are also contributing to upward price pressures which are currently exacerbated by seasonal illness, a resurgence in COVID-19 cases, and a net outflow of labour abroad.

In these circumstances, spending and investment demand continues to outstrip supply capacity, with a broad range of indicators highlighting pervasive inflation pressures. Employment remains above its maximum sustainable level and the Reserve Bank's core inflation measures are around 4 percent. The Committee acknowledged there is a near-term upside risk to consumer price inflation and emerging medium-term downside risks to economic activity.

The Committee agreed to continue to lift the OCR to a level where it is confident consumer price inflation will settle within the target range. The Committee is comfortable that the projected path of the OCR outlined in the recent May Monetary Policy Statement remains broadly consistent with achieving its primary inflation and employment objectives - without causing unnecessary instability in output, interest rates and the exchange rate. Once aggregate supply and demand are more in balance, the OCR can then return to a lower, more neutral, level.

Summary Record of Meeting

The Monetary Policy Committee discussed developments affecting the outlook for inflation and employment in New Zealand. Members agreed that developments were broadly in line with their assessment at the May Monetary Policy Statement. The Committee agreed it remains appropriate to continue to tighten monetary conditions at pace to maintain price stability and support maximum sustainable employment.

The Committee judged that the global economic outlook has continued to weaken, broadly as anticipated. The weaker outlook reflects a tightening of financial conditions, ongoing global supply disruptions, and rising geopolitical tensions. The Russian invasion of Ukraine continues to cause disruption to the supply of oil, gas and food commodities, resulting in continued high prices for food and energy. Ongoing health restrictions are exacerbating supply disruptions, as currently most notable in China.

Globally, many central banks have increased policy rates in response to rising inflationary pressures, to realign economic demand with supply. Members agreed that global inflationary pressures will likely persist in the near-term, as reflected in ongoing high domestic import prices and elevated shipping costs.

Members noted that the New Zealand dollar exchange rate has depreciated since the May Monetary Policy Statement. A moderation in global commodity prices, amid a continued decline in investor risk appetite, and rising central bank policy rates globally have contributed to this depreciation. The Committee noted that the weaker New Zealand dollar is continuing to have an impact on New Zealand dollar import prices.

In New Zealand, GDP contracted modestly in the March 2022 quarter. However, these data remain volatile, with a catch-up in government spending and exports expected. Increased visitors to New Zealand are also supporting hospitality and tourism. Meanwhile, household spending has remained resilient despite a decline in consumer confidence.

Financial conditions have continued to tighten with mortgage rates rising in response to, and in anticipation of, increases to the Official Cash Rate (OCR). Asset prices, including house prices, continue to decline. Members agreed that the increase in mortgage interest rates will assist to bring house prices more in line with sustainable levels. The Committee also agreed that both high food and energy costs and rising mortgage interest rates will lead to more subdued household discretionary spending in coming quarters.

Members noted that while there are near-term upside risks to consumer price inflation, there are also medium-term downside risks to economic activity. Despite these risks, members agreed that capacity pressures remain pervasive. Labour shortages continue to be a major constraint for business activity, as are the ongoing impacts of global supply chain disruptions. A resurgence in COVID-19 cases and a rise in other seasonal illnesses continues to constrain productive capacity in New Zealand. The recent removal of travel restrictions have also enabled a net outflow of labour in the near-term. Members agreed that employment is above its maximum sustainable level, and that rising wage pressure remains an expected outcome. Meanwhile, core inflation measures are around 4 percent.

The Committee discussed the unique shocks the economy is currently facing relative to historical experience. These developments increase the uncertainty about how households and firms will respond to a tightening of monetary policy. The Committee agreed that observing how households and firms are responding to these economic challenges will be important to understanding when monetary policy settings will be sufficient to achieve its remit objectives.

The Committee agreed to maintain its approach of briskly lifting the OCR until it is confident that monetary conditions are sufficient to constrain inflation expectations and bring consumer price inflation to within the target range. The Committee remains broadly comfortable with the projected path of the OCR outlined in the recent May Monetary Policy Statement. Once aggregate supply and demand are more in balance, the OCR can then return to a lower, more neutral, level. The Committee viewed this strategy as consistent with achieving their primary inflation and employment objectives without causing unnecessary instability in output, interest rates and the exchange rate.

On Wednesday 13 July, the Committee reached a consensus to increase the OCR to 2.50 percent.

RBNZ May MPS – Key Forecast Variables

Table 6.1
Key forecast variables

		GDP growth Quarterly	CPI inflation Quarterly	CPI inflation Annual	TWI	OCR
2020	Mar	-1.5	0.8	2.5	70.9	0.9
	Jun	-10.3	-0.5	1.5	69.7	0.3
	Sep	13.9	0.7	1.4	72.0	0.3
	Dec	-0.3	0.5	1.4	72.9	0.3
2021	Mar	1.3	0.8	1.5	74.9	0.3
	Jun	2.5	1.3	3.3	74.7	0.3
	Sep	-3.6	2.2	4.9	74.4	0.3
	Dec	**3.0**	1.4	5.9	74.3	0.6
2022	Mar	**0.7**	**1.8**	**6.9**	**72.6**	**0.9**
	Jun	**1.3**	**1.4**	**7.0**	**71.8**	**1.6**
	Sep	**0.6**	**1.5**	**6.2**	**71.8**	**2.7**
	Dec	**0.5**	**0.8**	**5.5**	**71.8**	**3.4**
2023	Mar	**0.4**	**0.7**	**4.4**	**71.8**	**3.7**
	Jun	**0.2**	**0.6**	**3.5**	**71.8**	**3.9**
	Sep	**0.2**	**0.9**	**3.0**	**71.8**	**3.9**
	Dec	**0.3**	**0.4**	**2.6**	**71.8**	**3.9**
2024	Mar	**0.4**	**0.6**	**2.5**	**71.8**	**3.9**
	Jun	**0.3**	**0.4**	**2.3**	**71.8**	**3.9**
	Sep	**0.2**	**0.8**	**2.2**	**71.8**	**3.8**
	Dec	**0.3**	**0.2**	**2.1**	**71.8**	**3.7**
2025	Mar	**0.2**	**0.5**	**2.0**	**71.8**	**3.6**
	Jun	**0.4**	**0.3**	**1.9**	**71.8**	**3.5**

Source: RBNZ

Sell-Side Analyst Views

ANZ (+50bp)

- It should be a pretty straightforward decision for the RBNZ to deliver another 50bp hike at its Monetary Policy Statement (MPS) this week. On balance, the data flow, while certainly not one-sided, has come in more inflationary than the RBNZ forecast in May. For that reason, one can't rule out a 75bp hike, but this far into the cycle, the RBNZ can deliver the tightening it needs with a 50bp hike, a firm forecast OCR track, and some staunch messaging.
- In the July Monetary Policy Review, the Committee noted that it "remains broadly comfortable" with the May MPS OCR track, which showed the OCR peaking at 3.95%. Adding everything up, there are unders and overs, and considerable uncertainty associated with each. And in the end, the published OCR track is subject to a good deal of judgement as well. But it seems likely that the OCR track is going to be revised higher, and potentially by as much as 50bp.
- Of course, we're forecasting mortgage rates to go up, and CPI inflation to come down, delivering positive real interest rates before long. But it's all contingent on inflation coming down quickly – that's the bit that's doing the work in our forecast. If it doesn't, the OCR will have to keep right on going. Or, in another possible expression of essentially the same risk: the RBNZ may not be in a position to be able to cut the OCR were a negative growth shock to come along (eg to our terms of trade), depending on how quickly inflation falls in that scenario.

ASB (+50bp)

- Like a Rocket Lab launch, the OCR has been shooting up this year. We expect the release of this Wednesday's Monetary Policy Statement to continue that trajectory, with another 50bp Official Cash Rate increase to 3%. That level is likely only just above the 'neutral' OCR, so the OCR is potentially only now getting into contractionary territory. Market pricing is firmly for a 50bp increase: the urgency for an even larger increase is not there.
- The RBNZ's forecasts are likely to again imply the need for the OCR to peak at or slightly higher than the previous 3.9% peak published back in May, and with a slightly swifter flight now to that peak. Inflation pressures remain strong, and the RBNZ will keep wanting to get on top of them quickly. We expect to see similar language as in the last two policy announcements: a "resolute" commitment to getting inflation back in the 1% to 3% target band and continued intent to tighten "at pace". The RBNZ's main regret for now is still not acting swiftly enough, and for the time being the RBNZ will want to prop the interest rate curve up – particularly after recent wholesale rate falls.
- Our forecast for the OCR peak remains 3.75%, with a presumed August 50bp hike followed by 50bp in October and 25bp in November. We acknowledge the peak could prove to be higher, with a particular risk being persistent wage inflation – which is already flashing an early warning that it could exceed the RBNZ's last forecast. Against that, real economic activity over 2022 looks set to be much weaker than the RBNZ assumed in the past. At some point that may flow through to the RBNZ's longer-term outlook for unemployment, wages and – in turn – extent of inflation pressures.

Bank of America (+50bp)

- The RBNZ meets on 17 August and updates its forecast via the quarterly Monetary Policy Statement. We expect the Bank to deliver a 50bp hike to lift the Overnight Cash Rate (OCR) to 3% and reinforce its hawkish stance.
- Domestic inflationary pressures and the de-anchoring of longer term expectations are still a concern. CPI for the June quarter surprised to the upside, with headline inflation now at 32-year highs (7.3%yoy). The Bank's "resolute" commitment to address price pressures and its CPI Sectoral Factor at record levels should pave the way for the OCR to reach a terminal of 4% in November 2022. The Bank's survey of 1-year ahead expectations also show businesses anticipate sticky inflation, higher unemployment and higher rates.

Barclays (+50bp)

- We expect the RBNZ to deliver its fourth straight 50bp hike as it maintains its approach of 'briskly' lifting the OCR. We expect the MPC to signal a slower pace of increases hereafter, as commodity prices come off, and headwinds to growth increase amid already tight financial conditions.

BNZ (+50bp)

- The more things change the more they stay the same. Over the last few weeks (months) we have experienced extreme volatility in financial markets, and data outcomes which have been miles away from expectations. Yet amongst all the noise, once everything is thrown into the mix, the outlook for New Zealand inflation and the labour market is little changed from what the Reserve Bank was looking at when it delivered its July Monetary Policy Review or, for that matter, its May Monetary Policy Statement. On this basis, why would one expect the Reserve Bank to deliver an interest rate message that was significantly different to that of the May MPS? That's how we see it anyway.
- On the price front, the RBNZ's starting point was blown out of the water by a higher than anticipated June CPI. That said, the RBNZ knew this was coming when it warned of the near-term upside risks to inflation in its July MPR. Since then, there have been clear signs this upside surprise will be fully reversed over the following six months. If the RBNZ sees the broader inflationary profile similar to ourselves then the RBNZ's "new" CPI forecast track will be almost identical to its previous published projections.
- With both inflation and labour market settings broadly in line with expectations, we believe the Reserve Bank will hike its cash rate by 50 basis points at its August 17 meeting. That will take the OCR to 3.00%. We believe there is little variation in opinion on this. What is more interesting is what the RBNZ will signal it will do thereafter.
- We still think there is a risk the cash rate does not need to get to 4.0% to achieve the RBNZ's required outcomes but see no reason why the RBNZ would want to change its most recent forecast of 3.95% given the evidence it has received to date. With two meetings, after the August one, before the end of the year, we doubt the RBNZ would want to rule out the possibility of a further 75 basis points of hikes during that period so it will likely signal this, leaving a further 25 points for next year.

Goldman Sachs (+50bp)

- Looking to August, we expect the RBNZ to hike by another 50bp to 3.0% - in line with unanimous consensus among the 15 forecasters (including GS) surveyed by Bloomberg. Since the July meeting, domestic data has been somewhat mixed but fairly strong overall. While the labour market was a touch softer than expected in Q2, this likely reflects labour supply constraints more than slowing demand given strong wage growth. Q2 inflation was stronger than the RBNZ's May MPS forecast at the headline level, although inflation expectations eased somewhat in Q3 and the recent declines in commodity prices should provide some near-term relief for petrol prices. Overall, with the labour market still very tight and wage growth likely to accelerate further over the coming quarters, we expect the RBNZ to deliver on the expectations of a 50bp hike, in line with its May MPS OCR track.
- In terms of the forward guidance, given rates are now meaningfully above the pre-Covid assessment of 'neutral' (around 2%), we expect the RBNZ to remove the language that it will continue to tighten monetary conditions "at pace". Instead, we expect the RBNZ to retain some optionality by signaling that while conditions warrant "further tightening", policy will be more data dependent going forward (e.g. using language similar to the BoE/RBA such as "policy is not on a pre-set path").
- On the macro forecasts, we expect the MPS to largely maintain the OCR track unchanged from May (reaching ~3.5% by end-22 and peaking at ~4% by 2H2023 before gradually falling). There is a risk the RBNZ revises lower its peak OCR projection alongside a downward revision to global tradable inflation given lower commodity prices, although we think such a move at this week's meeting is premature given the still-heightened uncertainty around global supply chains. On growth, we expect the RBNZ to lower its 2022 forecast modestly given the weaker Q1 starting point, but to offset this via slightly stronger growth in 2023.

ING (+50bp)

- The Reserve Bank of New Zealand is likely to hike by another 50bp in August. However, a worsening economic picture and rapidly falling house prices suggest we could see a revision lower in the rate path projections. With the RBNZ increasingly seen as a test case for other central banks, global markets will keep a close eye on any dovish tilt.
- In our view, the risk of a revision lower in the rate projections at the August meeting is elevated. The RBNZ is currently forecasting a terminal rate of around 4.0% by mid-2023, which is starting to look less realistic. We may see 25bp or 50bp being trimmed off the terminal rate projections and/or rate cuts being added sometime in 2023, in what would be a de-facto dovish shift. Alternatively, the Bank may keep rate projections unchanged (at the risk of losing some credibility) to avoid an unwanted impact on inflation expectations. A revision of the rate path later in the year would at that point be quite likely.

J.P. Morgan (+50bp)

- We expect the RBNZ to hike 50bp at this week's meeting to an OCR of 3%, and deliver a broadly hawkish MPS, at least as it regards the rate path. The committee is almost solely focused on inflation at the moment, and is conveying a willingness to hike then cut if required to fast-track the inflation adjustment, ensure "confidence" that inflation will settle in the band, and that a wage-price spiral will be avoided. The nature of policy transmission in New Zealand is such that if the goal is preserving the optics of traction today, the rhetoric cannot give an inch until the inflation descent is assured, so the leadership will attempt to jawbone market rates, which have rallied substantially since mid-year.
- At some point the central bank needs to pivot back to its official framework, which is (as the leadership was highlighting earlier in the pandemic), "forecast targeting". In attempting to speed up the inflation adjustment, policy lags are being downplayed, hence the staff's projected up-down forecast OCR path. With inflation being central to the decision process, we think this week's meeting is too soon for the committee to pivot back to the usual, more forward-looking, assessment. When it does occur, the adjustment will be abrupt. This is almost inevitable under the RBNZ's "least regrets" philosophy, which argues for mitigating tail risks. In such a minimax regret framework, decisions are not particularly anchored to probabilities of different outcomes, and can change quite abruptly even with subtle changes in the underlying profile of risks.
- We expect this transition to occur after the next CPI reading in October, at which point annual inflation will be falling. The backward-looking nature of inflation expectations surveys means lower headline inflation should drag the expectations measures with it. This week's 3Q RBNZ survey displayed the first signs of such an inflection, with the 2Y measure moving back inside the target band, tracing the descent in fuel price inflation. For now though, the RBNZ is focused on 'earning' the decline in expectations and conveying vigilance against a wage/price spiral, even if the data don't suggest that is underway. Wages are growing in line with the long-run relation to the unemployment rate, whereas a true expectations shift would require higher wage inflation for a given level of unemployment.

Kiwibank (+50bp)

- The RBNZ's policy decision, and updated forecasts, will dominate the news wires this week. The RBNZ is widely expected to deliver a 50bps hike, taking the official cash rate to 3%. Although we wouldn't rule out a 75bps move to 3.25%. If the RBNZ wants to get bang for buck, an outsized 75bp move would cause quite the stir in financial markets. We would see short-end wholesale interest rates push higher. And the RBNZ would deliver a nice boost to the currency. A higher Kiwi dollar reduces imported inflation. Despite the risk, we expect the RBNZ to stick to market expectations and deliver a 50bp move.
- We expect the RBNZ to revise their inflation forecasts higher, and deliver some stern wording around the outlook for inflation. The RBNZ will have taken some comfort in the easing of inflation expectations, but inflation expectations remain elevated. The RBNZ want to see actual inflation ease, before they contemplate easing up on their actions.
- We currently expect the RBNZ to hike to 3.5%, and stop. Although the risk is clearly tilted towards a much higher terminal rate of 4%, or above. We believe the RBNZ is getting significant traction in its tightening to date, and confidence in the economy has been hit, hard. We are also wary of the rapidly rising risks of a global recession.

NZIER (+50bp)

- There was a range of views amongst the Shadow Board members on what the Reserve Bank of New Zealand should do with the Official Cash Rate (OCR) over the coming year. However, the majority view was that a 50 basis points OCR increase in the August meeting is warranted, with only two members recommending a different quantum of tightening (25 basis points and 75 basis points each). Shadow Board members highlighted the strong inflation pressures in the New Zealand economy as justification for their recommendation for further tightening over the coming year.
- Regarding where the OCR should be in a year, Shadow Board members' views ranged from 3 percent to 4.25 percent. Inflation is the main concern, with the disagreement centring on the amount of tightening required to bring inflation back to the Reserve Bank's 1 to 3 percent inflation target band. Some members noted the risks of a hard landing for the economy from a sharp rise in interest rates. Signs of slowing in parts of the New Zealand economy highlight the balancing act faced by the Reserve Bank in controlling inflation in the current supply-constrained environment.

TD (+50bp)

- Recent data suggest that the RBNZ's job is not done and near-term risks to inflation should dominate the Bank’s thinking. Updated economic forecasts and the new OCR path will garner market attention.

Westpac (+50bp)

- Both we and the market expect the Reserve Bank to increase the Official Cash Rate by another 50 basis points at the Monetary Policy Statement. That’s been a settled matter for some time – even if the Reserve Bank hadn’t repeated its wording around tightening monetary conditions “at pace” in its July review, the need for a continued strong response to inflation has been all too apparent.
- The bigger question is around what the RBNZ signals for the path ahead. The outlook is becoming more mixed, with activity softening but inflation pressures even stronger than expected. What’s more, financial markets are now trying to front-run the central bank in the other direction, pricing a lower peak in the OCR cycle and a turn to rate cuts as early as August next year.
- With that in mind, we think that the RBNZ will want to keep emphasising its inflation-fighting credentials. Its task requires not just lifting interest rates to a certain level, but holding them there for long enough to do their job of bringing demand back into line. Any softening in the RBNZ’s tone this week could see market interest rates fall even further, which would risk undermining the good work that the RBNZ has done so far.
- We recently lifted our OCR forecast to a peak of 4% by the end of this year, from 3.5% previously. That was broadly in line with the track that the RBNZ published in its May Monetary Policy Statement, although a little more aggressive on the pace. We expect the RBNZ to run with something similar this time, in particular emphasising that interest rates will need to remain high for longer than the market is factoring in.

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