mni

All Signal, No Noise

MARKET ANALYSIS

MNI RBNZ Review – May 2023

Meeting Date: Wednesday, 24 May 2023

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

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

CONTENTS

Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

MNI POV (Point Of View): RBNZ Moves To Neutral

The RBNZ hiked rates 25bp to 5.5%, as generally projected, but the tone of the statement was significantly more dovish than expected. The forecasted peak in the OCR remains at 5.5%, thus the central bank appears to have reached its terminal rate and so has shifted to a neutral stance from its tightening bias. The discussion also shifted down a step to whether to hike 25bp or pause. In the vote that followed 5 chose the hike and 2 a pause. The statement focused on the slowing impact of restrictive policy and the transmission lags rather than upside risks to inflation. It now looks highly likely that the RBNZ will be on hold at its July 12 meeting.

The RBNZ felt that neither hiking 25bp nor pausing would be destabilising but Governor Orr said that it was a very difficult decision. The final decision was about having the “increased confidence” that enough had been done to contain inflation and that “25bp was there”. Orr stated that the bank is pleased that it is “getting on top of inflation” and that demand is slowing towards supply, which is what needed to happen. Thus, there was no mention that further tightening is required, consistent with its forecasts, just that policy will need to “remain at a restrictive level for the foreseeable future” in order to meet the inflation target. While its stance has moved to neutral, any near-term easing expectations have been quashed.

Governor Orr stated that in the central bank’s charter a “vote” is a tool available to the Committee to make decisions. The May meeting was the first time this option has been used and how members voted will be kept confidential. But Orr made it clear that the Committee as a whole stood by the decision and that they were in “broad agreement” on the monetary policy outlook even if not on the OCR itself.

The summary of the meeting stated that “the usual lags of monetary policy transmission mean that the full effects of past OCR increases will still take some time to occur”. So, while the 2023 OCR forecasts have been revised up, the peak remains at 5.5% with the first easing in H2 2024, the time when inflation is projected to be below the top of the target band. Rate cuts are now expected to be faster than assumed in February from H2 2025 with Q4 now at 4.1% from 4.3%.

The Committee also didn’t seem concerned by the near-term fiscal expansion or the increase in immigration. It noted that “overall, fiscal policy will be contractionary” over the forecast period even if it adds to demand over 2023/24. The RBNZ was pleased that migration was taking some of the heat out of the labour market due to the increase in labour supply and believed that the risks to activity and inflation were “mixed” as the population surge was likely temporary. It noted that while the labour market remains very tight, there are indicators pointing to pressures easing helped by the increased supply of labour. But it did revise down its unemployment rate expectations across the forecast horizon.

CPI inflation forecasts have been revised down in 2023 to 4.9% in Q4 while Q4 2024 is almost unchanged at 2.5%, thus signalling that the RBNZ isn’t concerned about the inflationary impact from rebuilding. 2025 is unchanged with inflation close to the bottom of the band. The meeting summary observed that “short-term price pressure from recent severe weather events appears to have been less than initially assumed”. It noted that while business’ inflation expectations are lower, households’ are higher, which it thinks is due to past inflation and could be adding to the “persistence of domestic inflationary pressure”.

Restrictive policy is driving a slowdown in demand across sectors, but spending will need to ease further to return inflation to target. Unlike the Treasury’s estimates, the 2023 recession is still in the RBNZ’ forecast but is shallower and could be avoided altogether if the usual forecasting error is considered. 2024 growth has been revised up helped by rebuilding. The bank estimated that recovery from the extreme weather events will add about 1.5% to GDP over several years.

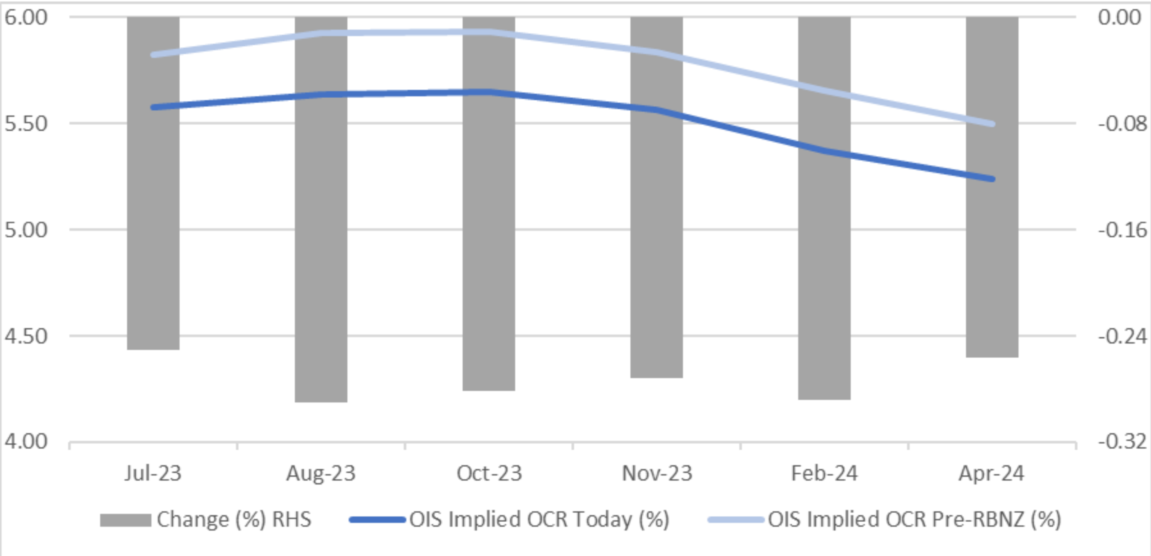
With the RBNZ leaving the expected peak in the OCR at 5.5%, the shift to neutral and the clearly more dovish tone of the statement, it appears that the RBNZ is done and that they will watch for the full effects of the 525bp of tightening this cycle to be fully felt. Thus, a large upside surprise to inflation, inflation expectations or the labour market is probably required for the Committee to raise rates further. With elections in October, the last window for a move would be the August 16 meeting, which would not only have updated information on CPI, GDP, employment/wages and inflation expectations but would also have a revised set of forecasts. If that data continues the recent “moderating” trend though, then tightening is most likely over this cycle. But don’t expect rate cuts in 2023 either.

RBNZ Dated OIS Pricing

RBNZ dated OIS pricing has shunted 25-29bp softer across meetings after the RBNZ lifted the OCR by 25bp to 5.50%, as expected, but surprised the market by signalling that the current level is likely to be the peak.

- The statement released by the RBNZ primarily focused on the impact of restrictive policies and acknowledged the presence of transmission lags. Notably, the Committee appeared unconcerned about the near-term fiscal expansion and the rise in immigration.
- Prior to the announcement, the market had priced 37bp of tightening for yesterday meeting and an expected terminal rate of 5.93%. The expected terminal rate is currently 5.66%.
- Based on the current scenario, it appears increasingly likely that the RBNZ will keep rates unchanged at its upcoming meeting on July 12. The market attaches a 70% chance of that outcome occurring.
- Despite the RBNZ's expectation that "interest rates will need to remain at a restrictive level for the foreseeable future, to ensure consumer price inflation returns to the 1 to 3% target range...", the market has priced 40bp of easing by April 2024.

Figure 1: RBNZ Dated OIS: Today Vs. Pre-RBNZ



Source: MNI – Market News / Bloomberg

RBNZ May Monetary Policy Assessment

The Monetary Policy Committee today voted to raise the Official Cash Rate (OCR) from 5.25% to 5.50%.

The Committee agreed the level of interest rates is constraining spending and inflation pressure. The OCR will need to remain at a restrictive level for the foreseeable future, to ensure that consumer price inflation returns to the 1-3% annual target range, while supporting maximum sustainable employment.

Global economic growth remains weak and inflation pressures are easing. This follows a period of significant monetary policy tightening by central banks internationally. International supply-chain constraints have also eased following a period of disruption, and shipping costs have declined. The weaker global growth has led to lower export prices for New Zealand's goods.

In New Zealand, inflation is expected to continue to decline from its peak and with it measures of inflation expectations. However, core inflation pressures will remain until capacity constraints ease further. While employment is above its maximum sustainable level, there are now signs of labour shortages easing and vacancies declining.

Consumer spending growth has eased and residential construction activity has declined, while house prices have returned to more sustainable levels. More generally, businesses are reporting slower demand for their goods and services, and weak investment intentions. Businesses report that a lack of demand, rather than labour shortages, is now the main constraint on activity.

There has been a return of net inward migration since international borders reopened. The Committee expects the pace of immigration to ease back toward pre-COVID-19 trend levels over coming quarters. While immigration has assisted to ease labour shortages, its net impact on overall spending is uncertain. The recent recovery in tourism spending, to around three-quarters of its preCOVID-19 trend level, is also supporting demand.

The repair and rebuild facing significant regions of the North Island – due to the recent severe weather events – will support economic activity, in particular the horizontal construction sector. The timing of this predominantly government investment will be spread over several years. Broader government spending is anticipated to decline in inflation adjusted terms and in proportion to GDP.

The Committee is confident that with interest rates remaining at a restrictive level for some time, consumer price inflation will return to within its target range of 1-3% per annum, while supporting maximum sustainable employment.

See full RBNZ statement here.

RBNZ May MPS – Key Forecast Variables

Key forecast variables

		GDP growth Quarterly	CPI inflation Quarterly	CPI inflation Annual	Unemployment rate	TWI	OCR
2021	Mar	2.0	0.8	1.5	4.6	74.9	0.3
	Jun	2.1	1.3	3.3	4.0	74.7	0.3
	Sep	-4.1	2.2	4.9	3.3	74.4	0.3
	Dec	3.5	1.4	5.9	3.2	74.3	0.6
2022	Mar	-0.5	1.8	6.9	3.2	72.6	0.9
	Jun	1.6	1.7	7.3	3.3	72.1	1.6
	Sep	1.7	2.2	7.2	3.3	70.6	2.7
	Dec	-0.6	1.4	7.2	3.4	70.8	3.8
2023	Mar	**0.3**	1.2	6.7	3.4	71.3	4.5
	Jun	**-0.2**	**1.1**	**6.1**	**3.5**	**71.5**	**5.3**
	Sep	**-0.1**	**1.8**	**5.7**	**4.1**	**71.5**	**5.5**
	Dec	**0.0**	**0.6**	**4.9**	**4.6**	**71.5**	**5.5**
2024	Mar	**0.2**	**0.6**	**4.3**	**4.9**	**71.5**	**5.5**
	Jun	**0.3**	**0.6**	**3.7**	**5.1**	**71.5**	**5.5**
	Sep	**0.4**	**0.9**	**2.7**	**5.3**	**71.5**	**5.4**
	Dec	**0.4**	**0.4**	**2.5**	**5.4**	**71.5**	**5.3**
2025	Mar	**0.6**	**0.5**	**2.3**	**5.4**	**71.5**	**5.1**
	Jun	**0.7**	**0.5**	**2.2**	**5.4**	**71.5**	**4.8**
	Sep	**0.8**	**0.7**	**2.0**	**5.4**	**71.5**	**4.5**
	Dec	**0.7**	**0.4**	**2.0**	**5.3**	**71.5**	**4.1**
2026	Mar	**0.6**	**0.5**	**2.0**	**5.2**	**71.5**	**3.7**
	Jun	**0.6**	**0.5**	**2.0**	**5.2**	**71.5**	**3.3**

Source: RBNZ

RBNZ Watch: Lower GDP Surprise, Higher OCR Working

By Daniel O'Leary

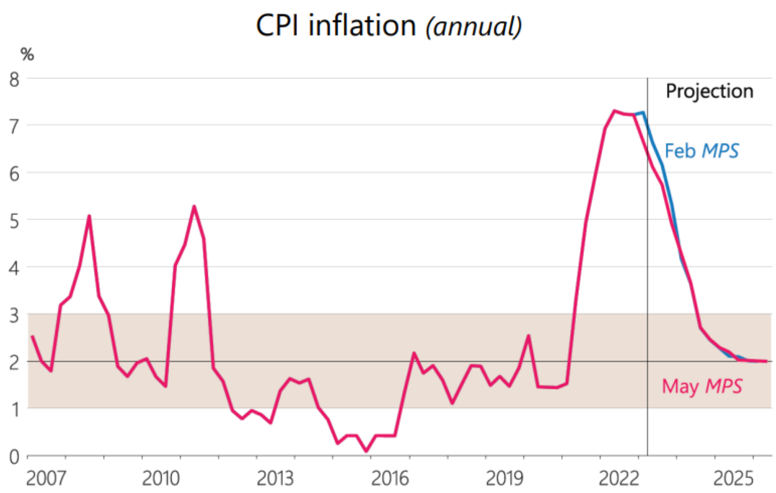
(MNI) Sydney - New Zealand will likely experience a recession, despite the Treasury's recent forecasts to the contrary, illustrating that the interest-rate sensitive parts of the economy are starting to slow, according to Reserve Bank of New Zealand officials.

At a press conference following the Reserve's decision to hike the Official Cash Rate 25bp to 5.5%, Chief Economist Paul Conway said the RBNZ expected the economy to record two consecutive quarters of negative GDP, with Q2 declining 0.1-0.2%, following 0.3% growth over Q1. “So definitely a soft patch in terms of GDP,” he noted. “That's a little bit south of the Treasury's projections, but by the same token, our projections have inflation coming back into the [1-3%] band more quickly.”

The RBNZ reverted to a smaller 25bp rise to meet its expected peak Official Cash Rate today (see: MNI BRIEF: RBNZ Hikes OCR To 5.5% "Peak," Rates Restrictive), decelerating from the 50-75bp moves seen since February 2022. The Reserve noted in its release and accompanying quarterly Monetary Policy Statement that higher rates had begun to slow the economy and reduce inflation.

"It's quite nice to see some of the things we were hoping would already be here, actually be here," noted Governor Adrian Orr at the press event, pointing to the lower GDP and decline in inflation. "All of the indicators suggest the interest sensitive parts of the New Zealand economy are yielding, slowing and inflation pressures coming out."

The MPS also showed the Reserve's peak OCR forecast remained unchanged, however, the central bank now expects the rate to fall faster than its February assumption. The Bank noted demand and inflation had slowed faster than expected, however, its forecasted return of CPI to 2% by 2025 was unchanged (see chart below).



LABOUR, IMMIGRATION & FISCAL POLICY

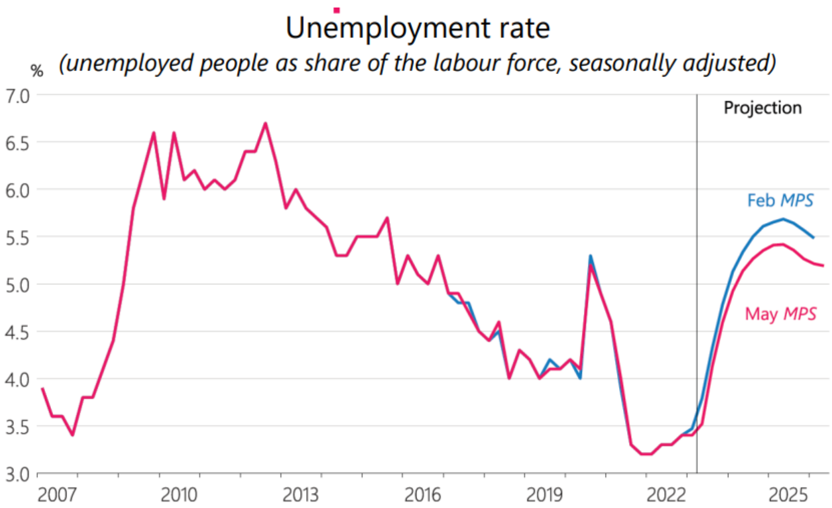
Leading into the decision, ex-staffers and commentators noted labour, immigration and government spending would be key to understanding the Reserve's strategy (see: MNI RBNZ WATCH: Hike Expected as Key Inflation Inputs Sticky).

On immigration, the RBNZ noted views among board members were mixed. Pent up domestic demand had likely driven price strength, and high net migration levels could help loosen the tight labour market, the Board noted.

At the press conference, Orr explained immigration will trend downwards to pre-Covid levels. Although “still a strong number, around 35,000 per annum, but the big surge has happened and is already behind us,” he added.

"Given the level of aggregate spending and dividing it by even more people who are actually in the country shows just how restrained consumer spending has been."

The RBNZ board also noted employment had risen above its maximum sustainable level, despite the high level of immigration. Orr explained data suggested labour conditions had improved and a shortage of manpower was no longer constraining activity. "The number one problem is actually demand," he added.



The Governor said spending found in the most recent government budget would likely not be a major source of inflation and would reduce over the next few years. "Government consumption… is declining as a proportion of GDP," he commented. "It's come from a very high level of Covid support and it's come off significantly and that is where we get the contractionary impact of fiscal policy on overall aggregate demand."

In its statement, the board noted, while fiscal policy will be contractionary on demand, it will be less so than assumed in February.

FUTURE FACTORS

The Board said it would monitor household spending growth and continued moderation in global inflationary pressure.

The board will next review the OCR on July 12.

Sell-Side Analyst Views

ANZ: As was widely expected, the RBNZ lifted the Official Cash Rate (OCR) 25bp to 5.50% today. However, overall the tone and OCR forecast was not nearly as hawkish as analysts or the market was expecting.

- The RBNZ's OCR forecast is practically identical to that in the February Monetary Policy Statement (MPS). It peaks at 5.5%, suggesting the RBNZ thinks (hopes?) they're done. As before, cuts are pencilled in for the second half of 2024.
- The RBNZ noted that the Committee considered a pause or a 25bp hike, whereas the market and analysts believed they would be weighing up 25bp vs 50bp. It is notable that for the first time, the RBNZ reported that they held a vote, with the decision to hike winning 5-2 over a pause.
- The RBNZ played down migration, noting its impacts are "uncertain". On fiscal policy it noted that it would be "less contractionary" than appeared the case in February." This is a pretty mild take on things, in our view.
- We see the risks as balanced around our forecast peak OCR of 5.75%, but there is clearly a risk that the RBNZ takes longer to get there than our forecast (another 25bp hike in July). We'll be watching labour market and housing data closely – as will the RBNZ.
- The RBNZ's economic forecasts were little changed from February, with a few offsetting changes.

ASB: The RBNZ surprised all and sundry by lifting the OCR 25bp and signalling it has most likely done enough to contain inflation. Expectations were spread over a 25bp vs. 50bp for this meeting, and for an eventual peak of 5.75% - 6% (we had expected a 50bp OCR hike today and a 5.75% OCR peak). Rather than a choice between 25bp and 50bp, the RBNZ debated between pausing and lifting the OCR .by 25bp, with the vote 5-2 in favour of an increase.

- The RBNZ's relatively mild takes on recent key events made all the difference. The near-term inflationary impact of the weather events is now deemed to be milder than the RBNZ's initial take back in February, representing a marked shift from its April view. The inflationary impact of the Budget was also downplayed. At this point the RBNZ is uncertain what the inflationary impact of migration will be, but it appears they are prepared to allow for a relatively greater impact on the supply side of the economy (in favour of dampening inflation) than historical norms.
- The general tone of the Statement points to the RBNZ being comfortable that it has done enough to get on top of inflation, particularly as there is still a lagged impact of past monetary tightening yet to come through. We think the RBNZ is now done (our pre-Budget view!), though inflation pressures will still need to continue to ease in line with expectations for the RBNZ to truly be comfortable.

BNZ: According to the RBNZ, the tightening cycle is now complete following its decision today to increase the cash rate by 25 basis points to 5.5%. We thought the RBNZ had little option but to raise rates again today, especially given its surprise 50 basis point hike back in April. And so it did.

- It appears the RBNZ integrated much of the fiscal easing that was confirmed in the Budget into its April decision, especially the spending associated with the floods.
- One thing is for sure, the tenor of today's MPS has helped depoliticise the Bank's actions. Not only in its rhetoric but also because there is no talk of moving rates in either direction between now and the election.
- It believes the deflationary impact on wage growth from migration outweighs the inflationary impact emanating from the increase in demand.
- In addition, the Bank largely overlooks the jump in employment in Q1 but, instead, highlights the lower-than-expected increase in same-job wage inflation.
- Overall, the Reserve Bank focusses intensely on the things that are generating a less inflationary environment. In addition to the above it talks of - Weak global growth - Easing international inflationary pressures - Reduced supply chain constraints - Lower export prices - Lower-than-anticipated inflation - The weak Q4 GDP starting point and - The negative impact on spending from negative wealth effects.
- The Monetary Policy Committee is now "confident" inflation will return to within its target band. Upside risks are noted but certainly not stressed. While dovish, there is a clear message that the RBNZ does not expect interest rates to fall any time soon. According to the Bank's modelled cash rate track, it would appear the first rate cut is not expected to happen until the fourth quarter of 2024. And, once rate cuts start they will gather substantial momentum such that by June 2026 we can expect a cash rate of just 3.25%.
- Prior to today's statement we were forecasting the first rate cut to be much earlier than this. We maintain this view in expecting a first cut in May 2024. The balance of risk is that the reduction starts even earlier.

Note that this was the first time the Monetary Policy Committee has published a split vote. The intent, for now at least, is very much to keep rates where they are for a long time. We have lopped that one last hike off our interest rate track. The risk of a shift to 5.75% is not zero but it is now looking very slim.

CIBC: The RBNZ lifted the Official Cash Rate by 25 bps to 5.50% and forecast rates to remain on hold until Q3 2024. This outcome is in line with our forecast but was unexpected by the market which had 36 bps priced for this meeting and a further 32 bps priced by August. The Bank noted that the current level of interest rates is constraining spending and inflationary pressures and that interest rates will need to remain at contractionary levels. The record of the meeting noted that the RBNZ considered either a pause or a final 25 bps hike at this meeting, but ultimately decided to hike in order to maintain their guidance and increase confidence that inflation will fall back to the midpoint of the target band.

- The MPS skewed relatively dovish as it emphasized the progress made on inflation expectations, the easing in the labour market, and the impact that waning global demand will have on exports. The Bank did however condition their pause on a continued moderation in inflation, inflation expectations, and a further slowing in household spending growth. Moving forward, focus is likely to shift to the timing of the first cut, rather than the possibility of further hikes, given the dovishness of the MPS.
- The forecast explained that increased spending on investment, post-cyclone, will likely be offset by declining government consumption.
- The MPS contained a special topic which explained that inflation expectations are currently more sensitive to recent inflation than in the past. Should this behaviour continue, the forecast for the first rate cut (currently Q3 2024) could be brought forward, as there was some concern that expectations would only exhibit this relationship on the upside.
- We expect upside risks to the policy rate from here to be low given the RBNZ's dovishness and the direction of forward looking indicators. We are currently calling for the first RBNZ cut in Q2 2023, which is one quarter sooner than the RBNZ's forecast. Should the sensitivity of inflation expectations to recent inflation persist, we believe that the RBNZ will move up their forecast for the first rate cut, thus we will be monitoring this dynamic closely moving forward.

Citi: The RBNZ deserted the hawks today by raising the OCR by +25bps to 5.5%, while also signalling the end of its tightening cycle by keeping the OCR track unchanged at 5.5%. The outlook for inflation was lowered across the forecast horizon. Meanwhile, we still believe that the Bank remains too bullish on near-term growth prospects. Consequently, we expect the first RBNZ rate cut to occur in Q1 2024, as opposed to the Bank's OCR projection which has rate cuts starting by year-end 2024.

- For the first time we can recall, the MPC decision to increase the OCR was not unanimous. Five members voted to increase the OCR by 25bps while two members disagreed. Given that the options up for discussion were either a 25bp increase or no change, we can infer that the two dissenters voted to keep the OCR unchanged at 5.25%. This outcome suggests that the policy stance of the MPC as a whole was more dovish than expected when compared to previous decisions where the decision to hike has been unanimous. Note that there was no suggestion that these members preferred to cut the OCR and in fact the MPC decided that the OCR needs to remain at a restrictive level for the foreseeable future. Guidance from the MPS has the OCR at 5.50% until June 2024, which suggests the committee wants to keep financial conditions tighter for longer than the market expects.
- The RBNZ has decided that short-term price pressure from Cyclone Gabrielle and flooding across the North Island will be less than previously expected. Importantly, the Bank sees recovery efforts adding about 1.5% to GDP over a number of years. In our view, spreading out the additional demand boost from reconstruction over a longer time frame will dampen inflationary concerns. Furthermore, while the Budget was seen as expansionary in FY24, over the next few years fiscal policy is actually expected to be contractionary on demand.

Goldman Sachs: The RBNZ lifted the Official Cash Rate (OCR) by 25bp to 5.50% today. This outcome was in line with GS/Bloomberg consensus expectations, although pre-meeting financial markets were pricing-in +38bp of hikes today and a cumulative +64bp of hikes by October. The overall tone of the meeting was surprisingly dovish. The Monetary Policy Committee (MPC) voted 5-2 in favour of a 25bp hike, with the two dissenting votes in favour of a pause. The RBNZ's OCR tracker and post-meeting press conference guided fairly firmly to a 5.5% terminal rate for the OCR.

- The RBNZ stressed that a recent easing in demand and labour shortages had increased its confidence that inflation would fall to target under current policy settings. While we were surprised by the RBNZ's sanguine assessment of the inflationary pulse from the recent Budget (post-disaster rebuild and strong migration) –

and comfort with tentative evidence of a positive inflection in the housing market – the RBNZ appears to have repositioned itself to be far less proactive to inflation risks from these sources.

- Looking ahead, following today's dovish RBNZ meeting and weaker retail sales print, we now expect the RBNZ to keep the OCR at its current 5.50% level (prior: +25bp to 5.75% in July) until a gradual easing cycle commences alongside the US Fed in 2Q2024 (prior: 1Q2024).

J.P. Morgan: The RBNZ hiked the cash rate 25bp today as we and consensus expected to 5.5%, but less than market pricing of +37bp.

- The MPS forecasts and commentary today reflected the policy transmission in train, which marks an important dovish shift. The staff MPS forecasts for terminal didn't rise, which taken at face value suggests the cycle is over. The committee's debate was between +25bp and no change, the first time this cycle that the holding option was considered. It was also the first time the committee held and reported an official vote (5-2), rather than agreeing a consensus.
- Having long conveyed doubts about how much tightening will prove enough, the concluding guidance in the statement now describes the committee as "confident that with interest rates remaining at a restrictive level for some time, consumer price inflation will return to within its target range...".
- Though still counselling that rates will be restrictive for the foreseeable future, the RBNZ has already opened the door to cuts via the bowed shape of its forecasts. Starting in 3Q24 (as it was in the last forecast round), the staff's OCR track forecasts a cumulative 220bp of cuts over the medium-term.
- The committee also now has more confidence that mortgage transmission is going to do further work in maintaining tight financial conditions.
- While the Budget last week stoked fears of hawkish implications, the RBNZ's forecasts had already embedded a decent reconstruction impulse in February. In the Q&A, Governor Orr argued that government spending is falling as a share of GDP through the forecast period, which was deemed enough for the Budget to be broadly consistent with the RBNZ's stance.
- Our forecasts imply one more 25bp hike next meeting, then 100bp of cuts into next year. Given the decision framework has been in flux we hold the former forecast for now, though if the activity data continue their current path the OCR will likely be on hold next meeting.

Kiwibank: The RBNZ hiked the cash rate by 25bps today. The 12th consecutive hike brings the cash rate to 5.50% which remains our forecasted peak. Importantly, the RBNZ lowered their OCR track from late 2024 and into 2025, factoring in deeper rate cuts.

- The commentary was much more dovish than expected, with a virtually unchanged inflation outlook despite the surge in net migration. Today signalled the peak in the tightening cycle, the next move is likely to be a cut, but not for a while yet.
- Inflation has peaked and therefore wholesale interest have also likely peaked. We have pencilled in a rate cutting cycle commencing in early 2024. Our main message has been to expect lower lending rates into 2024. Today's statement supported our view.

Rabobank: The RBNZ today increased the OCR by a further 25bps to 5.5% and signalled that this is expected to be the peak in the policy rate for this cycle. This is consistent with Rabobank's forecast of a 25bp hike today to end the cycle.

- The 25bps lift was widely anticipated by markets, but a number of local banks had increased their prediction of the terminal cash rate in recent days, following the delivery of what was perceived to be an expansionary budget last week and a large uptick in net inward migration in the first quarter of the year. These higher expectations for the path of the OCR were reflected in the futures market, which had a peak OCR of 5.93% priced into the curve as of yesterday, and a decent probability of a 50bps hike today. Those additional rate hikes have now been rapidly priced out of the futures curve following the publication of the RBNZ's decision today.
- Interestingly, this was the first decision by the RBNZ's Monetary Policy Committee that had to be put to a vote. The vote was between +25bps or no change, with the hike carrying through on a 5- 2 split. RBNZ Governor Orr noted in his press conference that there was a broad consensus among MPC members that the OCR needed to reach 5.5%, and that the only disagreement was around the timing of getting to that level.
- Despite the expected growth in Q1, the RBNZ still expects a recession later in the year. Of particular note in the Monetary Policy Statement was a comment from the RBNZ that firms are now reporting that lack of forward orders, rather than labour supply constraints, are now the major impediment to increasing output.

Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

This is the first time since mid-2021 that labour constraints was not nominated as the biggest issue facing firms.
- It is our view that the next movement in the OCR is likely to be a cut that we expect to arrive at the April 2024 meeting.

RBC: The RBNZ hiked rates 25bp today to 5.50% in a split decision, with 2 dissenting votes calling for no change. This is the first time the decision has been reached via vote rather than consensus following the bank's change in 2019 from the Governor alone determining policy to a formal collective process.
- Given the smaller hike, dissenting votes, the vote was between 0 and 25bp (rather than 25 or 50bp) and a raft of statement & press conference comments indicating that the RBNZ was increasingly confident that inflation will ease and return to target, today has seen a rather dovish turn from the RBNZ, at least relative to market expectations. In addition, the published OCR forecast track has not changed in the near term versus the February MPS, but we note that from 2H 2024 the track has been tweaked 34bp lower.
- Softening aggregate demand and progress on inflation appear to be the key motivators for the RBNZ deciding not to take a more hawkish stance today. The 1Q inflation and GDP reports were broadly softer than the RBNZ expected, and the Governor noted in the press conference that people were indeed “cooling their jets”. He also noted that the interest-rate sensitive parts of the economy were (“pleasingly”) responding to hikes. Given the effects past rate hikes are yet to be fully felt, and with about ¼ of low fixed rate mortgages yet to reset to higher rates, the RBNZ appears to think that the consumer has now begun to show enough restraint. The statement also notes that “Businesses report that a lack of demand, rather than labour shortages, is now the main constraint on activity”.
- Perhaps the biggest surprise for markets was the response from the RBNZ to last week's stimulatory NZ Government budget. The Governor noted on a number of occasions in the press conference that fiscal policy was “contractionary”.
- This meeting gives us some comfort that the RBNZ has probably reached terminal. Risks are still skewed to further hikes, but the hurdle looks high and data will need to surprise to the upside. We expect the RBNZ to begin easing in Q4 with two cuts leaving the OCR at 5% by end-23, and 3.50% by end-24. We note this is a much more dovish outlook than the RBNZ, with Governor Orr pushing back on speculative questions around the timing of first cuts in the press conference and broadly reiterating the statement language that “interest rates will need to remain at a restrictive level for the foreseeable future”.

TD Securities: The RBNZ hiked 25bps as expected by consensus, taking the OCR to 5.50% vs our forecast for a 50bps hike. Of most interest was the Bank's forward guidance. The Bank sent an unequivocal message that it does not expect to hike the OCR further.
- Aside from the Bank looking past the surge in net migration and increased near-term fiscal stimulus, the Statement and the Minutes of the meeting were littered with downside risks. In particular signs of slowing demand, inflation already easing and the lags in monetary policy helping do the work for the Bank in driving inflation lower.
- The RBNZ has set a very high bar to hike again. It has dismissed net migration, fiscal stimulus and green shoots in housing, essentially leaving CPI data driving the Bank's response function. We doubt Q2 CPI on its own will prompt the Bank to hike, and a hike late into the year is unlikely. As such, we now expect the RBNZ to firmly remain on hold at 5.50%.

Westpac: The Reserve Bank delivered the expected 25 basis point increase in the OCR, taking it up to 5.50%.
- The Reserve Bank strongly signalled that the peak in the OCR is in, but easing remains a long way off – towards the end of 2024.
- We continue to see significant upside risks to the Reserve Bank's growth and inflation outlook from the migration surge and government spending. We see the OCR rising 25 points at the August meeting as these risks become clearer to the Reserve Bank.
- August is pretty much the last stop on the line before the election period starts in earnest. By then, data on house prices and migration will be available that can either confirm or refute the Reserve Bank's current view. Similarly, the June quarter labour market report will be available. Hence, we now see the RBNZ on hold in July, but anticipate an increase in the OCR of 25 points to 5.75 percent at the August Monetary Policy Statement.
- The case for a further move in the OCR to 6 percent could become clearer to the RBNZ after the election in October. By then we expect that the housing market and migration pressures will be showing up strongly and non-tradables inflation will be looking quite sticky.