

Monetary Policy On Hold In New Zealand

- The Reserve Bank of New Zealand maintained the Official Cash Rate at 1.0% against expectations for a 25 basis point cut.
- The door was left open for further monetary stimulus should economic developments necessitate it.

The Reserve Bank of New Zealand (RBNZ) kept the Official Cash Rate unchanged at 1.0% today, against our and consensus expectations. The benchmark interest rate was cut twice this year, by 25 basis points in May and by 50 bps in August (chart 1). The Monetary Policy Committee (MPC) maintained a dovish tone today, noting that the risks to the economy were tilted to the downside while highlighting its readiness to add further monetary stimulus if needed.

The RBNZ's communications revealed that the MPC had discussed cutting the policy rate by 25 bps to 0.75%; nevertheless, it reached a consensus to stay on hold, as policymakers assessed that economic conditions since the August rate cut had not weakened to the extent that would have warranted further stimulus at this time. The decision reflects the RBNZ's monetary policy framework that includes an employment objective to complement the central bank's inflation-targeting policy approach; indeed, the MPC noted that employment in New Zealand remains close to its maximum sustainable level—despite some softening in Q3—and that inflation—1.5% y/y in Q3—is within the 1–3% target range.

Monetary authorities assess that New Zealand's economic growth is set to remain subdued over the coming quarters on the back of weak global trade growth combined with elevated uncertainty and its adverse impact on confidence; the RBNZ's projections show the country's real GDP growth slowing to 2.1% y/y in 2020 from an estimated 2.7% gain in 2019. Nevertheless, the policymakers expect the stimulatory monetary setting and increased public spending to provide some counterbalancing support to domestic demand in 2020. The central bank foresees employment growth remaining subdued in 2019 before recovering over the course of 2020.

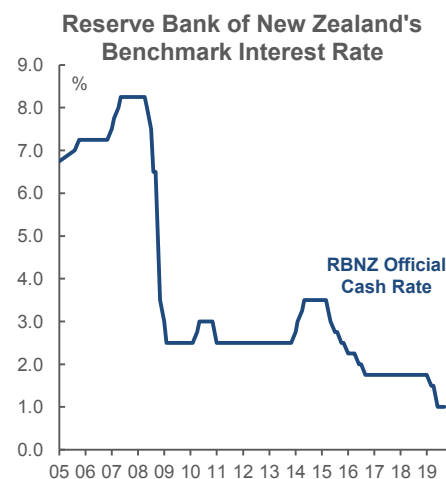
New Zealand's inflationary pressures will likely remain soft; the RBNZ projects consumer price inflation to average slightly below 2% y/y—the midpoint of the central bank's target range—over the next two years. Indeed, demand-driven price gains are set to remain contained considering the RBNZ's expectation of weaker annual wage inflation over the next year.

Against the soft economic growth prospects and an anchored inflation outlook, the MPC noted that accommodative monetary policy conditions remain necessary. The RBNZ's economic projections show the Official Cash Rate at 0.9% through 2020; accordingly, we assess that further modest easing may need to materialize for the economy to evolve as the central bank expects, particularly given persistent downside risks. The RBNZ's next monetary policy decision is scheduled for February 12, 2020.

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Chart 1



Sources: Scotiabank Economics, Bloomberg.

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