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# 1 Policy assessment

The Reserve Bank has decided to leave the Official Cash Rate unchanged at 5.0 per cent. However, in saying that, small increases in the OCR may be required over the year ahead to ensure that inflation remains comfortably within the target range over the medium term. New Zealand's economy has continued to perform well in 2003, although growth has been seated in the domestic economy rather than the export sector, where earnings are under pressure from the rising NZ dollar. New Zealand's current account deficit is again building and some key asset prices appear to be moving beyond their sustainable level. The strong activity, especially in housing and construction, spurred by rapid population growth and high consumer confidence, has produced quite intense inflation pressures in parts of the domestic economy.

Despite the domestic inflation pressures, CPI inflation has fallen over the past year largely due to falling import prices. Although the immediate outlook for the exchange rate is uncertain, the sharp falls in import prices seem unlikely to be sustained. CPI inflation is therefore expected to lift over the next year or so, driven by underlying domestic inflation pressure. Slower population growth and the flow-on effects of weaker export activity will help to limit inflation pressures, although a modest increase in the OCR may be required to keep inflation comfortably within the Bank's inflation target as defined in the Policy Targets Agreement.

As always this assessment is subject to change as new economic data emerge. We will pay close attention to the path of the domestic economy, which has proven more robust over 2003 than we expected. We will also be closely monitoring the path of the New Zealand dollar, with a particular focus on what it means for the export sector and the medium-term path of inflation.



Alan Bollard  
Governor