

# RESERVE BANK OF NEW ZEALAND SURVEY OF EXPECTATIONS

*The first Reserve Bank of New Zealand survey of expectations is introduced, together with the first results from the June 1987 quarter survey.*

## Introduction

During a period of rapid economic change more attention has been placed on the operation of markets. This has emphasised the crucial role that expectations play in influencing actions of economic agents. A lack of expectations data on macroeconomic variables has inhibited our understanding of New Zealand markets in the past and this lack provided the stimulus to initiating a regular survey to directly measure key decision-makers' expectations. The RBNZ quarterly survey of financial expectations is a new survey which has as its primary aim the establishment of a database for use in monitoring economic developments and for future economic research.

This article discusses the establishment of the survey, aspects of methodology and design, and briefly discusses the highlights of the June quarter survey.

## The Need for an Expectations Survey

While both the widespread usage of econometric methods and the higher level of economic awareness overall have changed the demand for data, shifts in economic theory have also altered the nature of the data requirements. The survey of market expectations is a response to developments in economic thought that have taken place in recent years. This period has seen an increasing recognition of the importance of expectations of macroeconomic variables held by agents in the economy and of their impact on the determination of actual outcomes in the economy. Expectations feature in a wide range of theoretical economic models and consideration of private sector expectations is now a generally accepted part of policy analysis. This is not to say that our understanding of the influence of expectations and of the formation of expectations is precise. Having access to a consistent expectations data series over time, however, should assist in this regard.

## Existing Surveys

A number of expectations surveys have been conducted overseas. The best known survey series on general price expectations is the Livingston data series for the United States, a series which has been extensively used in economic analysis. There are also a number of series based on business opinion surveys in which businessmen are asked for the expected change in the price of their own products. Many of these surveys have been running for a long period of time and have extensive samples.

New Zealand already has a number of business surveys. Perhaps the best known is the New Zealand Institute of Economic Research Quarterly Survey of Business Opinion (QSBO). The QSBO has a wide coverage and a long history of data. The National Bank carries out a survey of business opinion among its customers covering mainly activity-related measures such as sales but also including a question on inflation and wage expectations. The Manufacturers' Association conducts a quarterly survey of manufacturers while the Agricultural Economics Research Unit at Lincoln conducts an annual survey of farmers.

The Reserve Bank of New Zealand Survey of Expectations is unlike any survey currently operating in New Zealand for several reasons. Whereas many surveys are seeking information on past outcomes (i.e. historical statistics), this survey is asking for perceptions of events yet to occur. Also the survey focusses on economy-wide variables of interest rather than seeking opinions regarding respondents' own particular activities. Furthermore, while some existing surveys do cover expectations of selected economic variables, none covers a wide range of variables in a systematic manner, and none obtains the same range of quantitative replies as does the Reserve Bank survey.

## Methodology

The RBNZ Expectations Survey obtains key decisionmakers' expectations of major monetary and real economic variables. Respondents were included in the survey on the basis of their likely influence on the path of the relevant economic variables themselves, and in particular, their likely influence on financial variables. Accordingly both large corporates and small but 'significant' financial service companies are included in the survey.

Because of the relatively small sizes of the various business sectors to be covered there was no scope for selecting the sample randomly as is done for example with household surveys. Instead the sample is determined judgmentally and is to remain fixed, apart from normal turnover of respondents. As such the survey sample can be described as a panel.

The population or frame for the survey was those agents whose actions as a whole have significant influence on the outcome of the variables of interest. The subjective criteria of significance and influence were quantified, initially, by first identifying organisations through such measures as turnover statistics for manufacturers and deposit and loan size for financial institutions. Inevitably, even using these statistics as guides, there were firms and organisations that did not fit the criteria but were judged to have a significant influence in a particular market and were therefore included. Further, the identification of the appropriate person(s) within respondent organisations allowed for some qualitative selection.

To the extent to which it is feasible to make a distinction, respondents are grouped into four main categories relating to activity. These are financial, manufacturing, agricultural and labour. In addition, an 'others' group is included to cover respondents such as economic commentators and advisers who do not directly make decisions that influence actual economic outcomes but who may have a significant influence on the formation of expectations in the other groups.

At least initially, this sectoral breakdown will not be reported in the results.

### The Questionnaire

The survey is orientated towards expectations of financial and monetary variables and is comprised of five primary sections — Monetary Conditions, Prices, Interest Rates, Exchange Rates and Others. The Others section includes questions on real activity, balance of payments, fiscal deficit, prevailing weekly wages and unemployment.

At the expense of possibly deterring some respondents from particular questions, it was decided (after experience with the results of a pilot survey) to express most questions in quantitative terms. Respondents all receive the same questionnaire and as it was anticipated that only those with direct interests in particular variables would be able to answer related questions a cannot answer box was provided with every question. Respondents were urged to use this box when no firm expectation was held. No information was provided on the

past trends or values of the surveyed variables, in an effort to avoid potentially biasing answers towards a central point.

The survey questionnaire consists of sixteen questions, most of which have more than one part to them. Copies of the questionnaire format are available on request from the Bank, as are copies of the detailed results for each quarter. (A small charge may be made.)

### Summary of the June 1987 Quarter's Survey Results

Present monetary conditions are seen as tight but are expected to ease slightly by September 1987.

Over 80 per cent of respondents perceived present monetary conditions to be tight, while more than 50 per cent expect monetary conditions to ease by September 1987. Expectations were a little more divided over the change in monetary conditions expected by March 1988 but by and large, no change or some easing was expected. (Refer Figure 1.)

Slower M3 money supply growth is expected by March 1988 at 12.7 per cent per annum.

After strong money supply growth in the December quarter of 1986, respondents expect annual growth to fall to 16.5 per cent by June 1987 and fall further to 12.7 per cent in the year to March 1988.<sup>1</sup>

Annual CPI inflation is expected to be 9.8 per cent by March 1988.

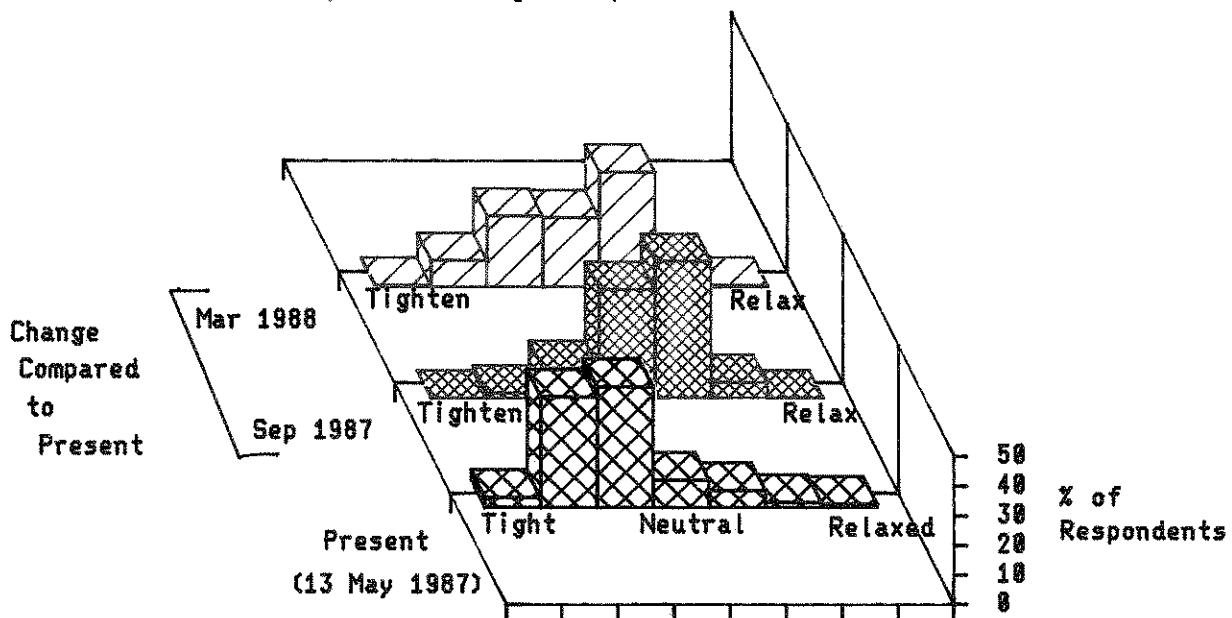
The expectation of the annual percentage change in the consumers price index for the year to March 1988 is 9.8 per cent, falling to 8.1 per cent for the year to March 1989.

Quarterly percentage changes of 2.3 and 2.2 are expected for the June and September quarters respectively, although 50 per cent of respondents expect the September quarter to be 2 per cent or less. The expected profile is shown in Figure 2.

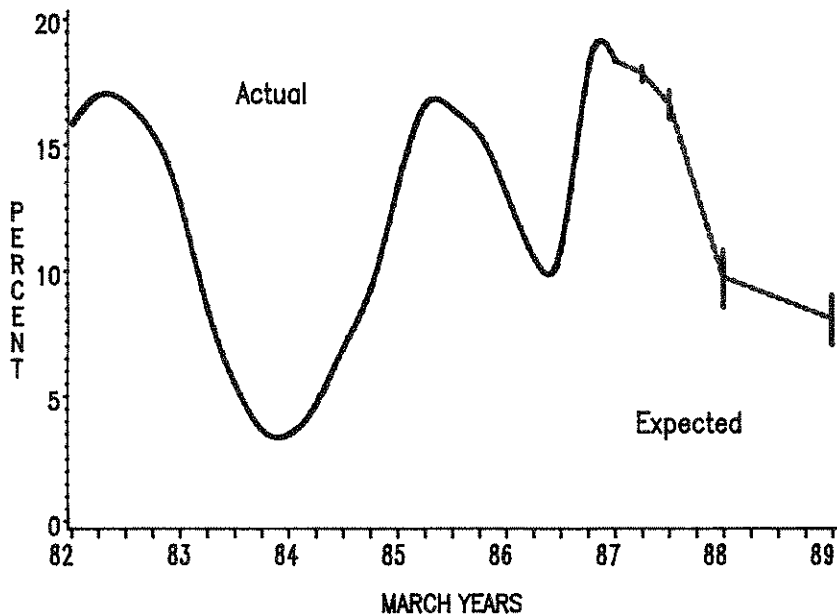
<sup>1</sup> The numbers used in the text will refer to the mean expectation unless otherwise stated.

Figure 1

Current Perception of Monetary Conditions and Expected Change Compared to the Present



**Figure 2**  
Actual And Surveyed Expectations Of The  
Annual Percentage Change In The Consumers Price Index



1 25% of expectations fell above and below the band shown.

Long term interest rates are expected to fall to 14.7 per cent by the end of March 1988 and the yield curve is expected to flatten over the same period.

The 5-year government security market yield is expected to decline to 16.4 per cent by the end of June 1987 and to fall further to 14.7 per cent by the end of March 1988. At the shorter end of the yield curve, 90 day prime commercial market yields are expected to fall to 21 per cent by the end of June 1987 and 17.8 per cent by the end of March 1988. The closing of the yield gap (i.e. the difference between long term and short term interest rates) resulting from these respective 5 year and 90 day yield expectations is shown in figure 3.

The exchange rate is expected to fall by 2.4 per cent over the year to March 1988.

The Reserve Bank Trade Weighted Index (a measure of the general movement in exchange rates) is expected to fall by 1.4 per cent over the September quarter and to fall by 2.4 per cent for the year to March 1988

(refer Figure 4). With respect to the individual cross rates, the New Zealand dollar is expected to depreciate against all the major currencies surveyed with the smallest depreciation expected against the Australian dollar.

Real Gross Domestic Product is thought to have fallen in the March 1987 quarter.

Real GDP is thought to have fallen 0.4 per cent in the March 1987 quarter, but is then expected to remain constant in the June 1987 quarter.

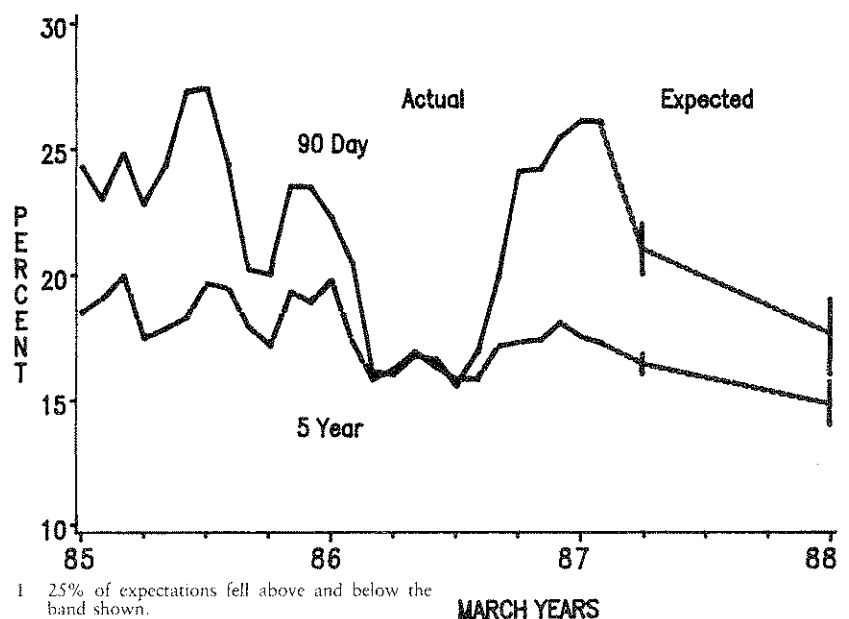
The current account balance is expected to improve over the year to March 1988.

A deficit of \$2.1 billion is expected for the External Balance of Payments on Current Account for the year to June 1987. The deficit is then expected to improve to \$1.8 billion for the year to June 1988. The expected profile is shown in Figure 5.

The Government Budget Deficit is expected to decline in the year to March 1989.

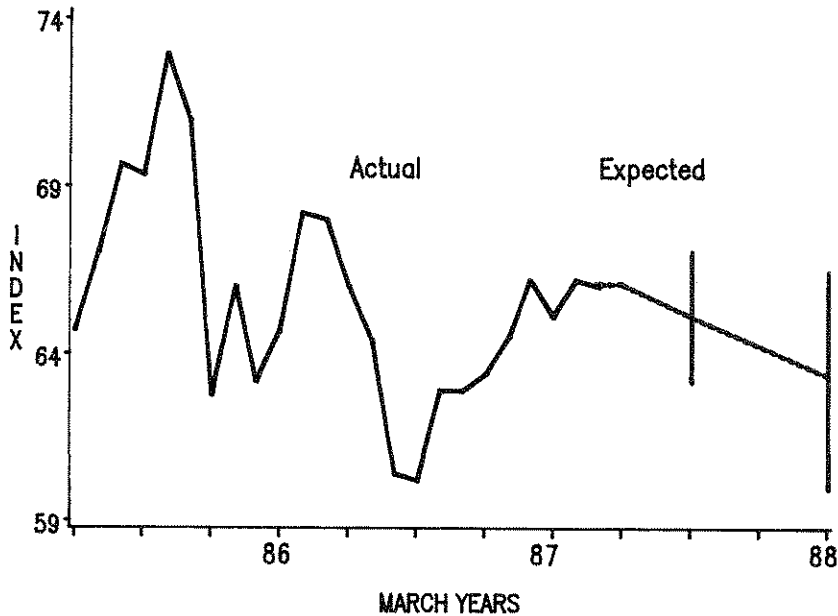
For the current financial year (to March 1988) the Table 2 Budget

**Figure 3**  
Actual And Surveyed Expectations Of 90 Day  
Commercial Bill And Five Year Government Stock Interest Rates



1 25% of expectations fell above and below the band shown.

**Figure 4**  
Actual And Surveyed Expectations Of The  
RBNZ Trade Weighted Exchange Rate Index



- 1 25% of expectations fell above and below the band shown.
- 2 End of September index is based on estimated index of 66.0 at the end of June (equal to the 1st June value of the index).

Deficit is expected to be \$2.0 billion, with a subsequent reduction to \$1.8 billion expected for the financial year to March 1989.

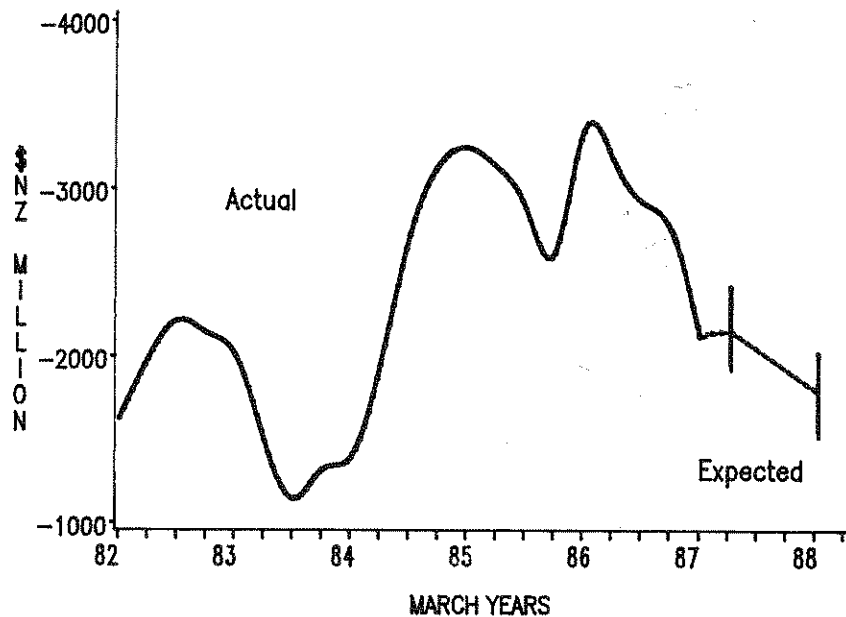
Wage rates are expected to rise by 8.8 per cent for the year to March 1988.

The annual per cent change in the prevailing weekly wage rates index for the year to March 1988 is expected to be 8.8 per cent.

Unemployment levels are expected to worsen over the year to March 1988.

By June 1987 the number of unemployed persons registered with the Labour Department (excluding special work schemes and vacation workers) is expected to be 81,100. This total is expected to increase to 84,400 by March 1988. (The range of responses to this question suggests that respondents are still unclear as to the precise definition of unemployment being used. Therefore these results should be treated with caution.

**Figure 5**  
Actual And Surveyed Expectations Of The  
Annual Current Account Balance



- 1 25% of expectations fell above and below the band shown.