11/2023

Monetary Policy SNAPSHOTS

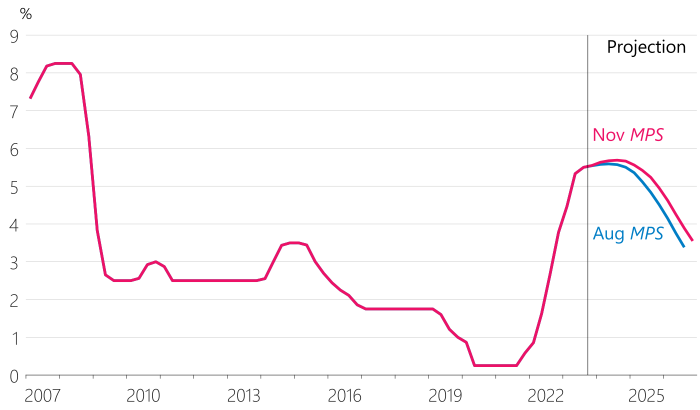
Monetary policy to remain restrictive

The Monetary Policy Committee today agreed to maintain the Official Cash Rate at 5.50 percent.

Figure 1

Official Cash Rate (OCR)

(quarterly average)

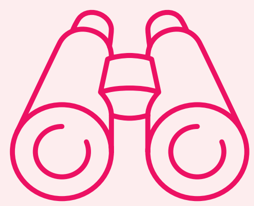


Source: RBNZ estimates.

Demand is declining, but economic activity remains elevated

Resources have been freed up in the economy

High levels of immigration and ongoing government investment are supporting economic activity



Maintaining high interest rates will help to achieve our inflation and employment objectives

Latest key statistics

- Annual economic growth: 1.8 percent (Q2 2023)
- Annual inflation: 5.6 percent (Q3 2023)
- Unemployment rate: 3.9 percent (Q3 2023)

Interest rates are restricting spending in the economy and consumer price inflation is declining, as is necessary to meet the Committee's *Remit*. However, inflation remains too high, and the Committee remains wary of ongoing inflationary pressures.

Demand is declining, but economic activity remains elevated

- Annual growth in economic activity has continued to slow. Recent data suggest the overall level of demand in the economy is in line with our outlook for subdued economic growth over the coming year. There is now a better balance between overall demand and the economy's ability to sustainably supply goods and services.
- High interest rates are still reducing the amount that some households can spend, as repayments for those with housing loans increase when they re-fix their mortgages. High interest rates also encourage those who can to save more, and reduces households' and businesses' ability to borrow. This lowers spending today.
- House prices have increased slightly in recent months, after bottoming out at levels well below their late-2021 peak. More net immigration into New Zealand adds to the number of people that require housing. This extra demand creates upwards pressure on rents and prices for existing housing, as the supply of housing is slow to respond.
- High interest rates, lower house prices and high construction costs have made it less appealing for developers to build houses. The number of building consents has decreased over the past year, pointing to a slowdown in residential building activity.
- Businesses' investment intentions over the next year remain low due to high interest rates and weaker global growth. Globally, economic activity has also continued to slow, reducing both inflationary pressures and also demand for New Zealand's goods exports.

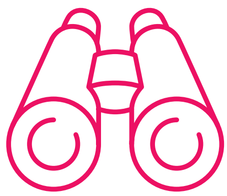
Resources have been freed up in the economy

- The bottlenecks in global supply chains have eased considerably over the past year. Global shipping and freight costs have returned to around pre-COVID-19 levels. Similarly, global commodity prices – in particular for oil and food – have fallen from their early-2022 peaks. Combined, these have helped to ease some costs faced by businesses.
- Labour shortages in New Zealand have been easing compared to this time last year. Labour supply has been increasing as net immigration adds substantially to New Zealand's labour force. High labour force participation of New Zealanders has also added to labour supply. Job ads have continued to fall as businesses have filled vacant roles. High interest rates are reducing demand and therefore businesses' intentions to hire.

High levels of immigration and ongoing government investment are supporting economic activity

- Demand in the economy is reducing overall, and the ability of the economy to sustainably supply goods and services has increased. However, several factors continue to support steady economic activity, despite high interest rates.
- Annual net immigration as a share of population is at its highest since the 1870s, some of which may be catching up for the years when the border was closed. The overall effect of immigration on inflation is uncertain, as immigrants help ease labour shortages but also create more demand in the economy.
- Government investment is expected to increase, reflecting the ongoing repair and rebuild work in the aftermath of severe weather events at the start of 2023. The impact of government investment on economic activity will be spread out over many years.
- Government consumption has remained high to help support the economy through the COVID-19 pandemic. Government consumption is expected to decline on an inflation-adjusted basis, but remain elevated compared to history. The outlook for government policy is uncertain, given that a new Government has just been formed.

Maintaining high interest rates will help to achieve our inflation and employment objectives



- Easing demand and increasing supply have led to lower inflation in New Zealand. Annual consumer price inflation eased to 5.6 percent in the September 2023 quarter. Declines in annual headline inflation have been led by continued falls in imported inflation, especially for food and petrol. Domestically-generated inflation is falling more slowly.
- Although decreasing, inflation remains too high. Most measures of inflation expectations and core inflation have declined in the last three months but remain elevated. This indicates that underlying inflationary pressure is starting to ease, though it may take some time to return to the mid-point of the Monetary Policy Committee's 1 to 3 percent target range.
- New Zealand's labour market remains tight but labour shortages are easing. The unemployment rate increased from 3.6 to 3.9 percent in the September 2023 quarter. While most indicators of labour market pressure have eased a lot, ongoing actual and expected wage growth are still supporting inflationary pressures.
- The New Zealand economy has shown some resilience, compared to what was expected in the August *Statement*. Interest rates remain restrictive at their current level based on our understanding of the state of the economy. However, high interest rates need to be maintained, and may need to increase further, to meet our inflation and employment objectives.