Economic Alert

MONETARY POLICY STATEMENT — FEBRUARY 2024

Wednesday, 28 February 2024

"The Monetary Policy Committee today agreed to hold the Official Cash Rate (OCR) at 5.50 percent."

But don't expect rate cuts anytime soon:

"A sustained decline in capacity pressures in the New Zealand economy is required to ensure that headline inflation returns to the 1.0%-3.0% target. The OCR needs to remain at a restrictive level for a sustained period of time to ensure this occurs."

The good news is:

"The New Zealand economy has evolved broadly as anticipated by the Committee. Core inflation and most measures of inflation expectations have declined, and the risks to the inflation outlook have become more balanced."

However, there was a hook:

"Headline inflation remains above the 1.0%-3.0% target band, limiting the Committee's ability to tolerate upside inflation surprises."

And a warning:

"Heightened geopolitical and climate conditions remain a risk for inflation. The recent rise in global shipping costs is one manifestation of these risks. The Committee remains alert to these relative cost pressures and will act to limit spillovers into general inflation if necessary."

Globally:

"Internationally, global economic growth remains below trend and is expected to slow further during 2024. This subdued environment will support a further moderation in New Zealand's import price inflation."

To conclude:

"The Committee agreed that interest rates need to remain at a restrictive level for a sustained period of time, to ensure annual consumer price inflation returns to the 1.0%-3.0% target range."

Comment:

While there had been some debate regarding the possibility of further rate hikes, the Committee ultimately decided the domestic economy is slowing sufficiently to leave the OCR at 5.50%.

The statement still maintained warnings that the battle with inflation is far from over, but the warnings weren't as hawkish as in previous statements, giving one the distinct impression that the peak of the hiking cycle is now in place. Simply put, the statement reflected a 'dovish hold'!

To some extent, we can take comfort that the Committee has aligned itself with its international peers emphasising that while inflation is falling, risks remain, and rate cuts shouldn't be contemplated until inflation is back within its target range (which in NZs case is projected to happen in Q3 2024 when CPI will reach 2.6%). Well … that's the take for now, but we've still to hear what the Governor says at the post-meeting press conference and in various speeches in the coming days…

Market Implications:

One of the most interesting facts of the statement was that the RBNZ lowered their peak OCR projection from 5.69% to 5.60%, a tiny 9bps decrease since November, but as I type this 30 minutes after the release, it is surprising to see the reaction from fixed income markets, with the swaps curve 20bps-25bps lower. No doubt swap traders believe that we have seen the peak, but surely the view of one economist couldn't have contributed to such over extension?

The NZD also sold off, in the region of -0.65 to -0.75%, with the sell-off in NZD/JPY the most noticeable, but ultimately all we have really seen is that most of the NZD-related pairs have adjusted back into the lower quartile of their recent ranges.

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