Economic Alert

MONETARY POLICY REVIEW — OCTOBER 2022

Wednesday 5 October, 2022

"The Monetary Policy Committee today increased the Official Cash Rate (OCR) to 3.50 percent from 3.00 percent."

Because:

"It remains appropriate to continue to tighten monetary conditions at pace to maintain price stability and contribute to maximum sustainable employment. Core consumer price inflation is too high and labour resources are scarce."

With more to come:

"Committee members agreed that monetary conditions needed to continue to tighten until they are confident there is sufficient restraint on spending to bring inflation back within its 1-3 percent per annum target range."

But there are risks internationally:

"Global sovereign bond yields have increased significantly. Simultaneous and fast-paced monetary tightening in multiple countries was increasing downside risks to global growth. Large movements in wholesale interest rates and exchange rates were causing a deterioration in financial market liquidity, which can exacerbate market volatility."

While there will be further pain domestically:

"Household balance sheets are resilient despite the recent declines in house prices. Household debt servicing costs were rising and had further to increase on average as more fixed-rate mortgages are reset at higher interest rates."

And we could have gone further ...

"The Committee considered whether to increase the OCR by 50 or 75 basis points at this meeting. Some members highlighted that a larger increase in the OCR now would reduce the likelihood of a higher peak in the OCR being required. Other members emphasised the degree of policy tightening delivered to date."

Comment:

In undertaking its 5th consecutive 50bps hike, the RBNZ has taken a different approach than its Australian cousin, remaining hawkish. There is no doubt that the biggest issue for Mr. Orr and his team is that *"productive capacity is still being constrained by labour shortages and wage pressures are heightened"* while *"spending continues to outstrip the capacity to supply goods and services."*

Simply put, *"core consumer price inflation is too high"*, labour resources are *"scarce"*, global price pressures remain *"heightened"*, employment remains *"high"*, while core inflation *"has risen and persist(s)."*

This Governor is sticking to his guns and there are more hikes to come.

Market Implications:

Following the release of the statement, and the continuation of the central bank's prior rhetoric, the NZD surged strongly across the board as did swap rates. Despite unanimous market expectations for a 50bps hike, the stronger kiwi suggests perhaps the statement was more hawkish than expected. The NZD rose 30-60 points across the board however, the interest rate markets are less convinced. Swaps initially saw a 5-7 bp jump following the statement, however have since retraced the whole move and then some.

The question remains how much more the RBNZ will do, but if this statement is anything to go by, another 50bps in November is a given.