ANZ Research

Preview: RBNZ Monetary Policy Statement

19 November 2024

Contact

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By halves

- We expect a 50bp cut to 4.25% next week. That would be consistent with RBNZ October messaging, economists' forecasts, and market pricing. Data since the October Monetary Policy Review has been mixed, but no data looks likely to upset the apple cart.
- Beyond this meeting, the data will decide, but with the OCR much closer to neutral, our baseline expectation is that the RBNZ will reduce the pace of easing to standard 25bp cuts, to reach a trough of 3.5% in May.

The view

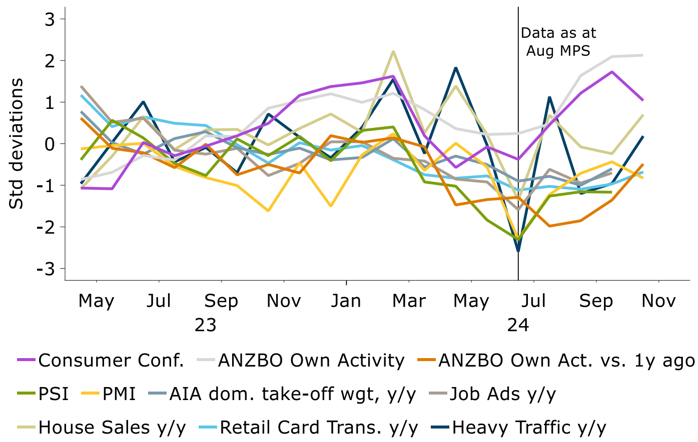
The market is currently pricing a high chance of a 50bp cut, with around a 12% chance of a 75bp cut. That seems fair. A 50bp cut is clearly the path of least resistance, but if there is going to be a surprise, given the RBNZ's confidence regarding the inflation outlook and the unusually long gap until the next meeting, a larger cut does seem likelier than a smaller one.

While we've all learned to put only a small weight on the RBNZ's previous forecasts, it is still useful to look at what the data has delivered relative to those. We publish this in a separate ready reckoner note, but in short:

- Q2 GDP came in a little stronger than the RBNZ's forecast but at -0.2% q/q was certainly not strong. This data was known at the October Review.
- House prices have been slightly weaker, but the recent lift in sales means the RBNZ is unlikely to revise its forecasts down substantially.
- The unemployment rate was lower than the RBNZ forecast in Q3, though it was because of people dropping out of the labour force rather than stronger employment than anticipated. Wage growth was unsurprising.
- Q3 headline CPI was a little weaker than forecast, but it was due to a technical surprise rather than anything economic.

In terms of the higher-frequency data, none are as low as they were in June, the last data point the RBNZ had to hand in August (figure 1). That isn't a problem – the RBNZ is confident that the economy has taken enough medicine – but it doesn't speak to a need for emergency-style cuts.

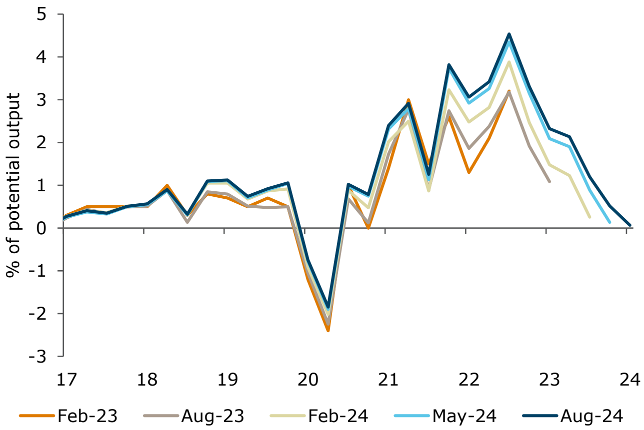
Figure 1. High-frequency activity indicators



Source: Stats NZ, BusinessNZ, AIA, REINZ, Seek NZ, Macrobond, ANZ Research

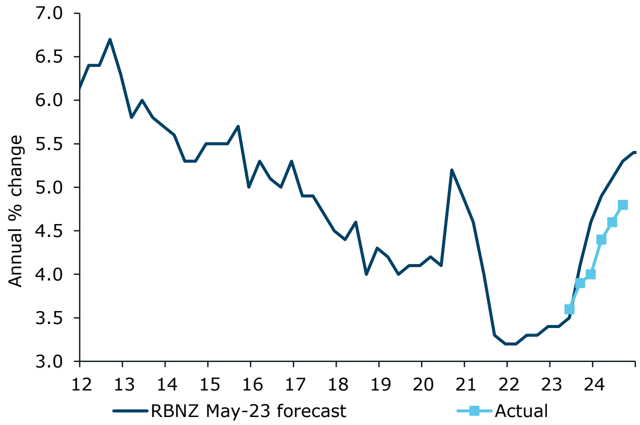
That said, it's always worth bearing in mind that the RBNZ's estimate of the degree of spare capacity in the economy, and thus its room to grow without putting pressure on inflation, is prone to significant revisions (figure 2). And of course their forecasts of such are prone to even more uncertainty. It's therefore important to keep an eye on direct capacity indicators as well as growth. The labour market capacity indicators are very favourable for the RBNZ at present, even with unemployment lower than they expected. Note the latter is not a new story – unemployment has actually been well below where the RBNZ thought it would (need to) be pretty much ever since the RBNZ stopped hiking in May last year (figure 3). That's a *relative* good news story, though of course it doesn't feel like it.

Figure 2. RBNZ output gap estimates (not forecasts)



Source: Stats NZ, RBNZ, ANZ Research

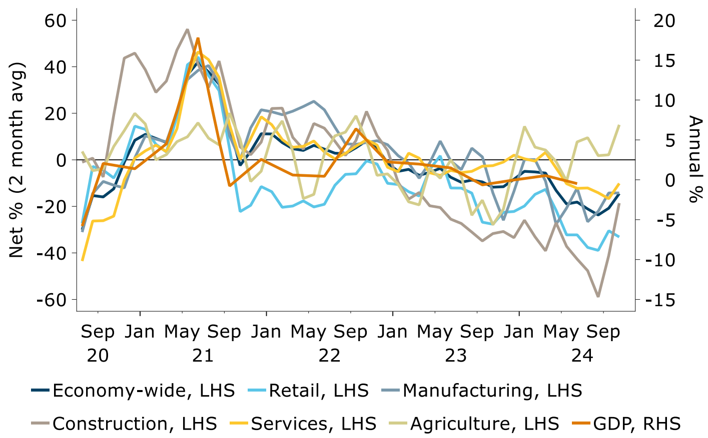
Figure 3. Unemployment rate vs RBNZ May 2023 forecast



Source: Stats NZ, RBNZ, ANZ Research

Our Business Outlook survey suggests that not only are firms' hopes for the future lifting; the dial has started to shift in terms of experienced activity (figure 4). The turnaround has been led by the most rate-sensitive sector that has had the toughest time recently: construction. But the recent lift has been broad-based, with just retail missing out. That means the RBNZ's estimates of the economy's ability to grow without reigniting inflation pressures are going to be pretty important – not a story for today, given the weak starting point, but certainly over the next year, assuming the recovery stays on track.

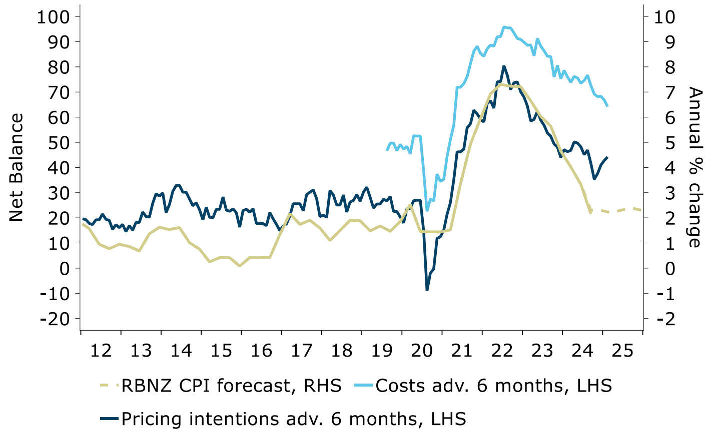
Figure 4. ANZBO Experienced activity by sector



Source: Stats NZ, Macrobond, ANZ Research

What are the direct inflation indicators saying? They're not exactly a slam dunk in the ANZBO survey (figure 5), but the RBNZ's survey of inflation expectations was more encouraging. And the ANZBO survey, firms are saying they expect to offer wage increases of just 2.6% in the next 12 months. Broadly, the RBNZ is likely to continue to be confident that while it'll take some time for domestic inflation to fall back to where it needs to be, they're winning.

Figure 5. ANZBO inflation indicators and RBNZ inflation forecasts

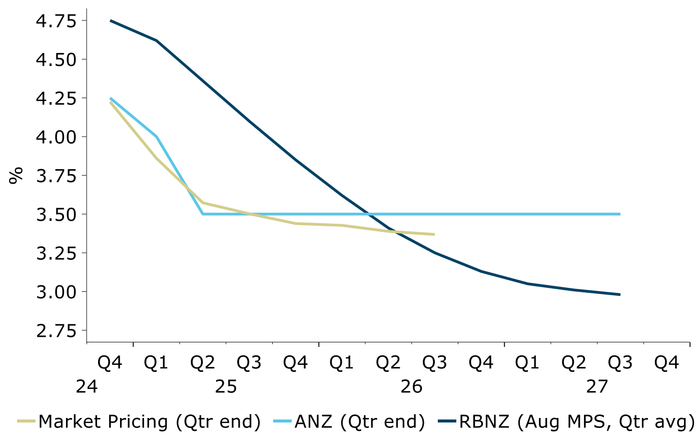


Source: RBNZ, Macrobond, ANZ Research

Pulling it all together

We expect the vibe of the Monetary Policy Statement to be "we got this." The OCR track will have a steeper downhill starting point, given August's track suggested two upcoming 25bp cuts whereas barring a surprise, they will have delivered two 50-pointers. We expect a similar track thereafter with the OCR falling to around 3%, but getting there faster.

Figure 6. OCR forecasts: RBNZ, ANZ, market pricing



Source: RBNZ, ICAP, Bloomberg, Macrobond, ANZ Research

There's no need for the RBNZ to take a strong stance on what happens next. We'd expect them to say that they considered cutting both 25bp and 75bp, and that future moves will be data dependent. We see two-sided risks around our OCR forecast. Yes, the economy is indubitably weak and wage pressures are very modest. But the bottom for growth is in and the vibe is shifting, while domestic inflation is still around 5%, not 3%, even if a few stubborn components account for a good chunk of that gap. Given the usual lags from policy moves to activity and then from activity to inflation it's clearly time to cut, but the appropriate degree of easing remains uncertain and the RBNZ's (and market's) views on that are likely to keep shifting with the data flow. With a 12-week break until the next meeting, it's truer than ever that nothing is set in stone as regards the path ahead.

Markets

Markets are going into this meeting with around -53bp priced in, which is really an acknowledgement by markets that they see 75bp as more likely than 25bp (as do we). Given that pricing, presuming we get a 50bp cut, the decision itself shouldn't cause too much of a stir. However, the market will pay close attention to whether the committee considered 75bp (or 25bp), and that'll be instructive for where market expectations for February and beyond sit after the meeting. If a 75bp cut is discussed but not delivered, that'd likely keep markets open to the idea of February being another 50-pointer, rather than just a 25bp cut.

The RBNZ's OCR track will also be of interest to markets, but its relevance hasn't lasted long after past decisions this year, with traders instead paying closer attention to global moves, and the data pulse. However, a reiteration of the RBNZ's dovish stance has the capacity to change the mood slightly among short-end traders. To be clear, we don't see a strong case for short end rates to move sharply lower, or to fresh lows, but it wouldn't be surprising to see them to drift a little lower, and to continue unwinding what has been a largely offshore markets-driven rise in rates here.

On the FX front, it's difficult to argue that another outsized cut will have a dramatic impact on the Kiwi given that it's already priced in and then some, but if we do see short-end rates drift lower, that has potential to weigh on the Kiwi, especially if US markets continue to question whether the US Federal Reserve may not need to cut by as much as initially thought.

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