New Zealand Institute of Economic Research (Inc)
Media release

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Lockdown divides *Shadow Board's* views on tightening

The Shadow Board has become divided over its views on what should happen with monetary policy at the October *Monetary Policy Review*. This is due to the ongoing lockdown in Auckland to contain the COVID-19 community outbreak and heightened uncertainty over the economic outlook.

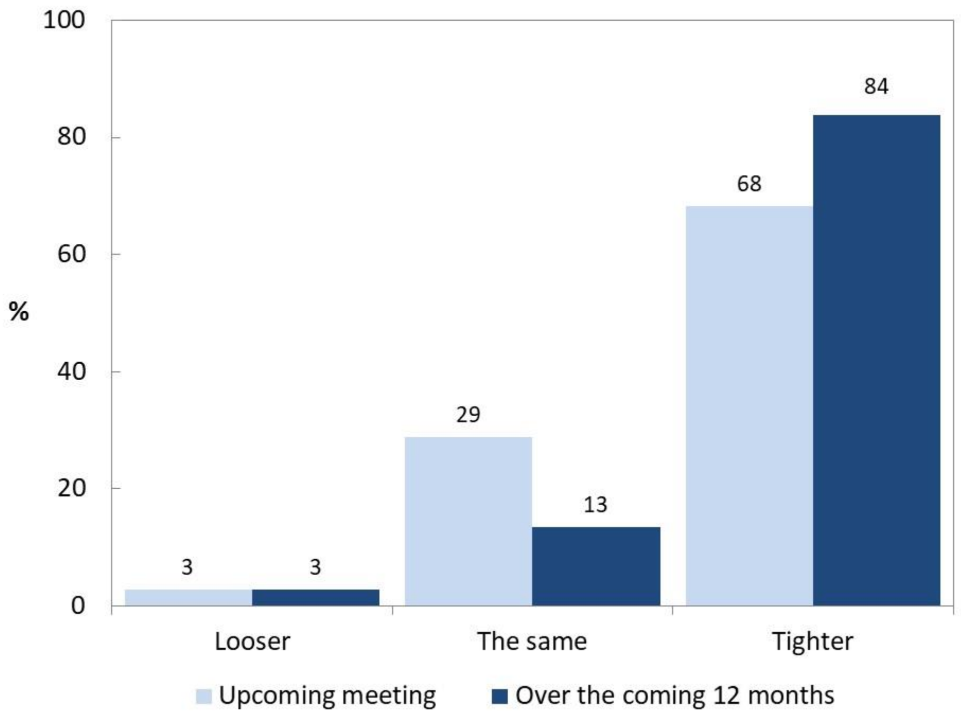
Shadow Board members in the business community highlighted the negative impact of the latest lockdown on businesses, with small to medium businesses hit particularly hard. This led to some Shadow Board members calling for monetary policy to be left unchanged at the upcoming meeting.

In contrast, other Shadow Board members continued to see tightening of monetary policy as appropriate given the intense inflation pressures in the New Zealand economy. These inflation pressures reflect both strong demand and acute supply pressures. Besides the increase in broader inflation pressures, some Shadow Board members also highlighted the surge in asset prices that have resulted from monetary policy being too loose.

Overall, while the views of the Shadow Board favour a tightening in monetary policy, there was a more cautious tone relative to August. How the latest COVID-19 community outbreak evolves, and beyond that, the Government's plans for the relaxation of restrictions will be a key influence on the economic and inflation outlook in New Zealand.

Figure 1 Reduced calls for tightening as lockdown hurts businesses

% strength of policy preference on stance RBNZ should take



Source: NZIER *Monetary Policy Shadow Board*

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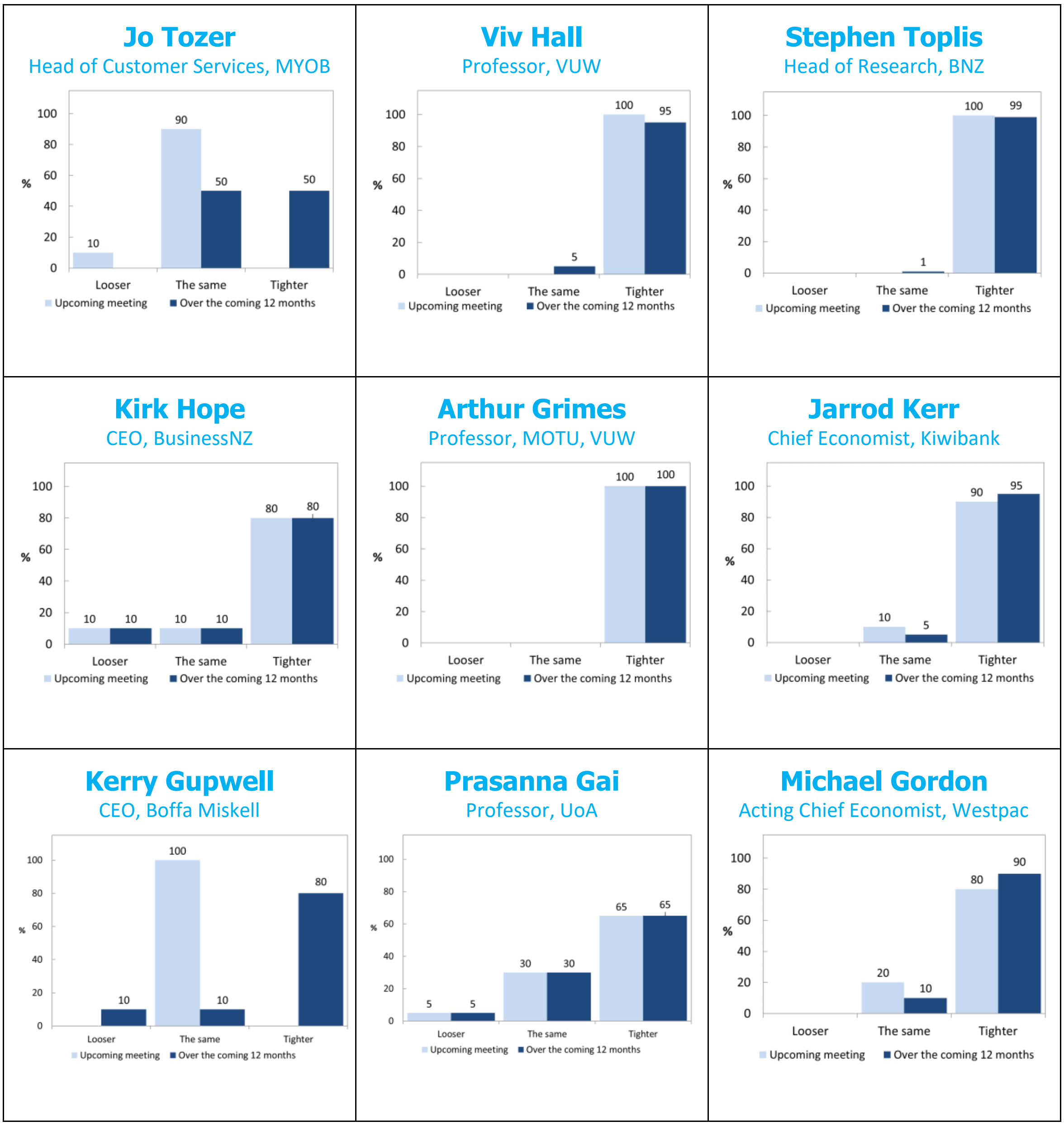
Figure 2 Individual participants' recommended rate settings – 29 September 2021



Source: NZIER *Monetary Policy Shadow Board*

Table 1 Participant comments

Participant comments are optional.

Stephen Toplis	There is no excuse not to raise interest rates in New Zealand. All targets have been met and, probably, breached. They will also stay that way. It's not appropriate for the RBNZ to start buying bonds back yet, so it's all up to the OCR. Least regrets mean the cash rate needs to be substantially higher.
Viv Hall	Inflation pressures continue to become more persistent, there remains the risk of even further asset price inflation, and the contribution of monetary conditions towards supporting maximum sustainable employment has been more than sufficient. Progressive OCR increases are now required, starting with an immediate increase of 25 bp.
Kirk Hope	Despite significant uncertainty over the current tail of Covid cases and potentially ongoing impact on output which make decision-making risky, the Reserve Bank has little choice but to move on interest rate rises now given the continued significant rise in inflationary expectations. Markets have basically already priced in at least a 25 basis points rise. Current rising inflationary pressures are not necessarily a short-term NZ phenomenon but are a significant international issue with transportation delays and shortages developing for a wide range of input and raw materials, as evidenced by the latest JP Morgan Global Performance of Manufacturing (PMI) responses over a range of countries. Inflationary pressures are likely to persist well into next year until borders are fully reopened (including for labour) and supply chains completely restored. The risk of not moving now on interest rate rises now is that the Reserve Bank may have to go much harder next year.
Jarrod Kerr	This will be another awkward decision, given Auckland is likely to still be in lockdown level 3. A 'considered' hike of 25bp to 0.5% is most justified. But the explanation needs to respect the pains that the largest city is going through. As our strategy evolves from elimination with vaccinations to vaccinated and living with it, the economy has shown enough momentum to justify pulling back on emergency levels of stimulus.
Jo Tozer	New Zealand's SME sector has borne the brunt of the latest COVID-19 Delta lockdown and ongoing restrictions. For many, revenue has fallen sharply, projects or sales have been delayed and work for this quarter will have been significantly disrupted. Even prior to the lockdown, our MYOB SME Snapshot showed more than a quarter of SMEs had less work in the pipeline for the quarter, and this has been followed by significant hits to cashflow. Aggregated and anonymised data of MYOB online customers showed overall cash deposits from EFTPOS card payments fell to -72.6% below a pre-COVID baseline in the second week of the latest lockdown – and that's just week two of many. In this immediate term given the current environment, increases to interest rates by the RBNZ would only put further pressure on local businesses who are already struggling. Looking ahead, while we would hope to see a similar effect as that following last year's lockdown, with a strong return to growth in the SME economy, there is a nervousness from businesses about the impact of Delta on consumer behaviour. Provided however (and this uncertainty continues to weigh the most on SME confidence), that the Delta outbreak can be controlled with the relaxing of restrictions long-term and increasing vaccine coverage, there is hope that the higher levels of SME economic confidence and growing revenue streams we saw prior to the lockdown, will return. This could see pressure on the RBNZ to again consider taking action to reduce inflation.

Kerry Gupwell	The latest lockdown has required the Government to provide additional support in terms of wage subsidies etc. How long can this yoyo-ing in and out of lockdowns go on? While recent labour market figures and inflation rate were clear signs that we needed a tightening in monetary policy, including an increase in the OCR, Delta complicated things, so there should be no change to the current settings for the moment. It's all about the vaccine rollout now.
Arthur Grimes	The Reserve Bank is way behind the curve when it comes to inflation. They have caused a hugely destructive rise in house prices and must now start to make amends by raising rates. A sell-down of some of their massive bondholdings is also warranted. This tightening applies even more firmly in the coming year.
Michael Gordon	Domestic conditions clearly warrant a move away from ultra-low interest rates. As I noted in August, the main reason for caution is around the Delta variant. While the current outbreak appears to be coming under control, Covid restrictions will remain a risk over the coming months, as our vaccination rate is still a long way from providing effective levels of protection.
Prasanna Gai	No comment.

About the NZIER *Monetary Policy Shadow Board*

NZIER's *Monetary Policy Shadow Board* is independent of the Reserve Bank of New Zealand. Individuals' views are their own, not those of their respective organisations. The next *Shadow Board* release will be Monday 22 November 2021, ahead of the RBNZ's *Monetary Policy Statement*. Past releases are available from the NZIER website: www.nzier.org.nz

Shadow Board participants put a percentage preference on each policy action. Combined, the average of these preferences forms a *Shadow Board* view ahead of each monetary policy decision.

The NZIER *Monetary Policy Shadow Board* aims to:

- encourage informed debate on each interest rate decision
- help inform how a Board structure might operate
- explore how Board members could use probabilities to express uncertainty.