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## Inflation tanks but not the time to slash interest rates says NZIER Shadow Board

Despite inflation falling below 1 percent, NZIER’s *Monetary Policy Shadow Board* recommends the Reserve Bank leaves the Official Cash Rate at 3.50 percent on Thursday.

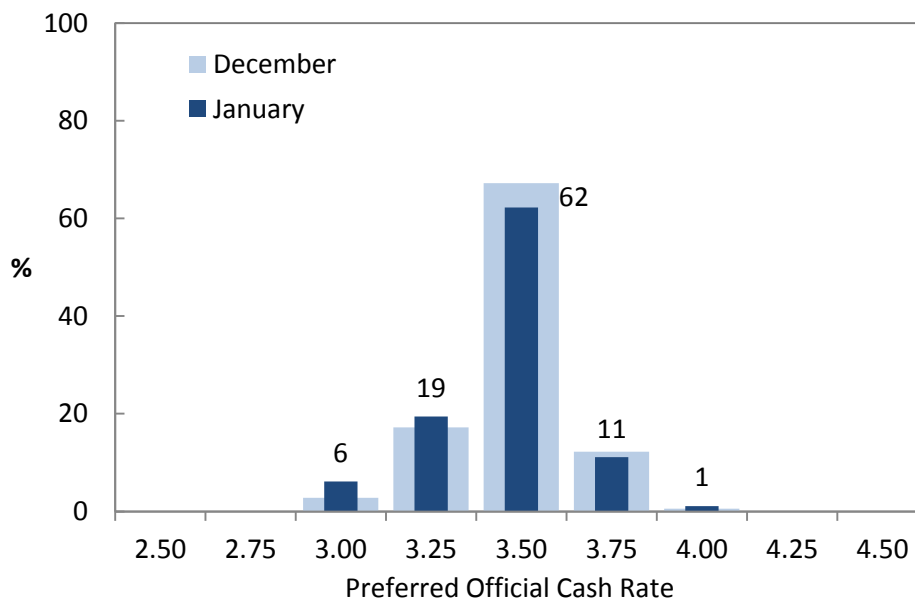
“Many indicators continue to point to a strong economy and Auckland’s house prices have reignited,” said Dr Kirdan Lees, Principal Economist at NZIER. “Notwithstanding the drop in inflation, on balance the *Shadow Board* recommends leaving interest rates where they are – now is not the time to unwind last year’s interest rate hikes.”

Domestic indicators, such as NZIER’s *Quarterly Survey of Business Opinion*, point to strong economic growth of 3-3.5% continuing from the end of 2014 to the start of 2015. Meanwhile Auckland city’s median house price rocketed up 13.2 percent last year, boosted by strong migration. These factors favour higher interest rates.

But the price of oil has slumped taking annual inflation from 1 percent in September to 0.8 percent in December. Inflation pressures are also extremely muted right throughout the economy – it’s simply hard to find businesses that can pass on price increases to consumers. Dairy price falls and drought conditions will also dampen economic activity in 2015. These conditions lean towards lower interest rates, as some *Shadow Board* participants prefer.

Weighing up the competing pressures, Figure 1 shows most of the *Shadow Board* are comfortable leaving interest rates on hold. Figure 2 and Table 1 show individuals’ views and comments. The *Shadow Board*’s average recommended interest rate is slight lower at 3.46 percent – down only a little since December.

**Figure 1 NZIER’s Shadow Board recommends leaving interest rates at 3.50 percent**



Source: NZIER *Monetary Policy Shadow Board*

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**Figure 2 Individual responses – 23 January 2015**



Source: NZIER Monetary Policy Shadow Board

## Table 1 Participant comments – 23 January 2015

Participant comments are always optional and can be limited to 60 words.

<b>Cameron Bagrie</b>	The RBNZ has an inflation target and not a growth or a housing one. Non-tradable inflationary pressures are receding rather than accelerating. There looks to be material structural forces at work. The OCR is higher than it needs to be. They won't be cutting but the tightening bias needs to disappear.
<b>Scott Gardiner</b>	Concerns loom on the horizon for SMEs with many sectors at top of business cycle – and headwinds about to arrive with prices flowing through to cash flow challenge for key sectors.
<b>Arthur Grimes</b>	Goods markets are showing approximately zero inflation while some asset markets are still showing some upward pressure. This complicates monetary policy rate-setting but, on balance, a wait-and-see approach to the interest rate level is warranted with no precipitate changes required in either direction.
<b>Dominick Stephens</b>	No comment.
<b>Phil O'Reilly</b>	No comment.
<b>Viv Hall</b>	The RBNZ can look through temporary exceptional movements in the prices of commodities traded in world markets, and recent substantial falls in global oil prices cannot yet be declared sustained in nature. More pertinent to this OCR call is that NZ's domestic aggregate demand is strong and projected to remain healthy. So, no current case for OCR cuts (or increases).
<b>Stephen Toplis</b>	There are a lot of balls in the air at the moment. The major risks to inflation still lie to the upside as activity runs above potential and the housing market reheats but, at the same time, downside risks from global issues, weak dairy prices and a prospective drought are very real.
<b>Dave Taylor</b>	Always thought the RBNZ pushed too hard too fast. With the current conditions there is a case to redress.
<b>Prasanna Gai</b>	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 Wednesday, 11 March 2015, ahead of the RBNZ's March *Monetary Policy Statement*. Past releases are available from the NZIER website: [nzier.org.nz](http://nzier.org.nz)

Shadow Board participants share out 100 points across possible interest rates to indicate what they believe is the most appropriate Official Cash Rate setting for the economy. Combined, these scores form a Shadow Board view ahead of each monetary policy decision.

Participants show where they think interest rates should be, not what they believe will happen.

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.