Monetary Policy Statement
November 2017
Policy Targets Agreement

This agreement between the Minister of Finance and the Governor of the Reserve Bank of New Zealand (the Bank) is made under section 9 of the Reserve Bank of New Zealand Act 1989 (the Act). The Minister and the Governor agree as follows:

1. Price stability

   a) Under Section 8 of the Act the Reserve Bank is required to conduct monetary policy with the goal of maintaining a stable general level of prices.

   b) The Government’s economic objective is to promote a growing, open and competitive economy as the best means of delivering permanently higher incomes and living standards for New Zealanders. Price stability plays an important part in supporting this objective.

2. Policy target

   a) In pursuing the objective of a stable general level of prices, the Bank shall monitor prices, including asset prices, as measured by a range of price indices. The price stability target will be defined in terms of the All Groups Consumers Price Index (CPI), as published by Statistics New Zealand.

   b) For the purpose of this agreement, the policy target shall be to keep future CPI inflation outcomes between 1 per cent and 3 per cent on average over the medium term, with a focus on keeping future average inflation near the 2 per cent target midpoint.

3. Inflation variations around target

   a) For a variety of reasons, the actual annual rate of CPI inflation will vary around the medium-term trend of inflation, which is the focus of the policy target. Amongst these reasons, there is a range of events whose impact would normally be temporary. Such events include, for example, shifts in the aggregate price level as a result of exceptional movements in the prices of commodities traded in world markets, changes in indirect taxes, significant government policy changes that directly affect prices, or a natural disaster affecting a major part of the economy.

   b) When disturbances of the kind described in clause 3(a) arise, the Bank will respond consistent with meeting its medium-term target.

4. Communication, implementation and accountability

   a) On occasions when the annual rate of inflation is outside the medium-term target range, or when such occasions are projected, the Bank shall explain in Policy Statements made under section 15 of the Act why such outcomes have occurred, or are projected to occur, and what measures it has taken, or proposes to take, to ensure that inflation outcomes remain consistent with the medium-term target.

   b) In pursuing its price stability objective, the Bank shall implement monetary policy in a sustainable, consistent and transparent manner, have regard to the efficiency and soundness of the financial system, and seek to avoid unnecessary instability in output, interest rates and the exchange rate.

   c) The Bank shall be fully accountable for its judgements and actions in implementing monetary policy.

Grant Robertson
Minister of Finance

Grant Spencer
Governor
Reserve Bank of New Zealand

Dated at Wellington this 7th day of November 2017.
Monetary Policy Statement

November 2017


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Chapter 1
Policy assessment

The Reserve Bank today left the Official Cash Rate (OCR) unchanged at 1.75 percent.

Global economic growth continues to improve, although inflation and wage outcomes remain subdued. Commodity prices are relatively stable. Bond yields and credit spreads remain low and equity prices are near record levels. Monetary policy remains easy in the advanced economies but is gradually becoming less stimulatory.

The exchange rate has eased since the August Statement and, if sustained, will increase tradables inflation and promote more balanced growth.

GDP in the June quarter grew broadly in line with expectations, following relative weakness in the previous two quarters. Employment growth has been strong and GDP growth is projected to strengthen, with a weaker outlook for housing and construction offset by accommodative monetary policy, the continued high terms of trade, and increased fiscal stimulus.

The Bank has incorporated preliminary estimates of the impact of new government policies in four areas: new government spending; the KiwiBuild programme; tighter visa requirements; and increases in the minimum wage. The impact of these policies remains very uncertain. House price inflation has moderated due to loan-to-value ratio restrictions, affordability constraints, reduced foreign demand, and a tightening in credit conditions. Low house price inflation is expected to continue, reinforced by new government policies on housing.

Annual CPI inflation was 1.9 percent in September although underlying inflation remains subdued. Non-tradables inflation is moderate but expected to increase gradually as capacity pressures increase. Tradable inflation has increased due to the lower New Zealand dollar and higher oil prices, but is expected to soften in line with projected low global inflation. Overall, CPI inflation is projected to remain near the midpoint of the target range and longer-term inflation expectations are well anchored at 2 percent.

Monetary policy will remain accommodative for a considerable period. Numerous uncertainties remain and policy may need to adjust accordingly.

Grant Spencer
Governor
Chapter 2
Key policy judgements

- CPI inflation is currently near the midpoint of the target range. However, underlying inflationary pressure remains subdued.

- The recent depreciation of the exchange rate will support tradables inflation over the year ahead. Non-tradables inflation is expected to increase gradually over the medium term.

- Monetary policy is expected to remain accommodative. In combination with more expansionary government policies, this will support GDP growth and maintain inflation around the target midpoint over the medium term.

- Inflation expectations remain well anchored around the target midpoint.

While headline inflation is currently near the midpoint of the target range, underlying inflationary pressure in the New Zealand economy remains subdued. Annual CPI inflation was 1.9 percent in the September 2017 quarter, up from 0.4 percent in September 2016 (figure 2.1). The increase in headline inflation over the past year reflects a turnaround in tradables inflation, in part due to increases in fuel and food prices.

Global economic activity continues to strengthen and the growth outlook for New Zealand’s major trading partners has improved. However, measures of core inflation and wage growth remain low in most advanced economies. While central banks in major advanced economies are moving to withdraw monetary stimulus, they are doing so very gradually.

The New Zealand dollar trade-weighted index (TWI) has been relatively strong in recent years, even taking into account the positive outlook for the New Zealand economy and the low level of global interest rates. The TWI has depreciated 4.5 percent since the August Statement.

The depreciation in the TWI will support tradables inflation over the coming year. However, it is assumed continuing low global inflation and limited further rises in commodity prices will result in low tradables inflation in the medium-term.
Persistently low headline inflation over recent years, in large part due to negative tradables inflation, has contributed to weak price-setting behaviour. Domestic businesses appear to be placing more weight on past inflation outcomes than on their expectations of future inflation in their pricing decisions. Although headline inflation has recently lifted, this price-setting dynamic means that past low inflation continues to weigh on current and future inflation.

The relative strength of the New Zealand labour market has contributed to a high level of permanent and long-term arrivals and fewer departures in recent years, contributing to strong population growth. The strong net inflow has moderated recently, but continues to lift demand for housing and other goods and services in New Zealand, albeit by less than in previous cycles. Strong population growth, along with a rise in labour force participation, is contributing significantly to growth in labour supply and potential output. This increase in productive capacity has moderated inflationary pressure.

The New Zealand economy is currently growing at around the same pace as potential output, and the output gap is estimated to be around zero. GDP growth was 2.5 percent in the year to the June 2017 quarter. Growth in the quarter was slightly lower than previously anticipated, having also been weaker than expected in the preceding two quarters. Export volumes increased by more than expected, but this was offset by continuing weakness in construction activity.

Residential investment has been supported over recent years by low interest rates, strong population growth, a shortage of housing, and high house prices. However, growth in residential investment has weakened in each of the past four quarters. Residential construction in Canterbury has fallen from a high level, and elsewhere the sector appears to be approaching capacity limits. Businesses are reporting greater difficulty accessing land, labour, and materials. Also, partly reflecting growing risks in the construction sector, banks have tightened lending standards for residential property development. We expect residential investment to provide less impetus to aggregate growth and capacity pressure over the next year than previously assumed.

Changes to loan-to-value ratio (LVR) restrictions, a tightening in lending standards, and a lift in mortgage rates through the end of 2016 have moderated the demand for housing and slowed house price inflation over the past year. Pressure on affordability, reduced demand from foreign buyers, uncertainty around tax policy, and revised expectations of future capital gains may be further tempering demand at present. It remains uncertain how persistent the slowing in the housing market will be.
Household consumption has strengthened since mid-2016 and has been stronger than expected based on its historical correlation with house price inflation. Aggregate consumption growth is being supported by low interest rates, high terms of trade, and strong population growth. It appears household spending may be less responsive to changes in housing wealth compared to previous cycles.

Fiscal policy is projected to become more expansionary in coming years. Based on Budget 2017, the August Statement included increased fiscal stimulus. With the change of government, changes to fiscal policy and broader economic policy are expected to provide additional stimulus to the economy. What matters for monetary policy is the impact of government policy changes on output and inflation.

We have taken account of four government policy initiatives that we believe are material for the economic cycle and the medium-term outlook for inflationary pressure. These policies are: increased government spending; the Government’s housing programme; changes to requirements for work and study visas; and increases to the minimum wage. At this early stage, with few details available, the future impact of these policy changes remains very uncertain. The way in which government spending and other policy initiatives transmit through the economy will depend heavily on the responses of private households and businesses. Our preliminary working assumptions regarding these policies are outlined in box E in chapter 5.

Given that domestic inflationary pressure remains subdued, it is appropriate for monetary policy to remain accommodative (figure 2.2). In conjunction with more expansionary fiscal policy, the current stance of monetary policy is expected to support growth in the economy. Annual GDP growth is projected to average 3.3 percent over the next two years. This above-trend pace of growth is expected to be strong enough to maintain inflation around the midpoint of the Bank’s target range over the medium term.

The Policy Targets Agreement (PTA) directs the Bank to maintain future inflation in the range of 1 to 3 percent, with a focus on keeping average inflation near the midpoint of this range. The Bank is flexible in its approach to achieving its inflation target, looking through temporary volatility in headline inflation and setting policy in such a manner that it does not generate unnecessary volatility in output, interest rates, and the exchange rate. In the current environment, additional stimulus would risk generating unnecessary volatility in the economy, while a premature tightening would risk undermining growth and could cause headline inflation to settle below the midpoint of the target range.
Survey measures of inflation expectations remain consistent with the Bank’s projections. Longer-term inflation expectations remain well anchored around the target midpoint.

The economic projections, as set out in this Statement, present the Bank’s conditional expectation of monetary policy settings necessary to meet the requirements of the PTA. There is always uncertainty around our projections. At present there is heightened uncertainty regarding the domestic outlook. Our assessment of the outlook and the appropriate stance of monetary policy depend on a range of judgements. The key assumptions and judgements are outlined below. If the assumptions underpinning the projections prove to be inconsistent with incoming data, or if risks to the projections materialise, the outlook for policy will be revised.

Global economic conditions

Global economic conditions are assumed to remain supportive over the projection, with the pace of growth sufficient to see spare capacity absorbed, core inflation increase, and monetary policy become less accommodative. Despite the improved global outlook, we assume global inflation will remain subdued, as the factors underlying recent low inflation persist and further increases in global commodity prices are limited.

Oil prices are assumed to remain relatively stable over the projection. The Dubai oil price is currently around USD 58 per barrel, slightly above our medium-term assumption of USD 55 per barrel. Non-oil import prices are expected to continue to decline relative to world CPI. Whole milk powder prices are assumed to remain stable over the projection, as they are currently close to our medium-term assumption of USD 3,000 per metric tonne.

The New Zealand dollar TWI is assumed to remain around its current level over the projection, with the recent depreciation sustained. We have assumed that the recent fall in the TWI predominantly reflects reduced appetite from offshore investors for New Zealand dollar assets rather than a deterioration in the domestic economic outlook. We expect the depreciation to feed through to higher inflation.

Permanent and long-term arrivals into New Zealand are assumed to continue to decline over the projection, while departures from New Zealand are assumed to gradually increase. What matters for monetary policy is the increase in demand stemming from the net inflow relative to its impact on the productive capacity of the economy. The net inflow in the current cycle has not been associated with the same degree of inflationary pressure as in previous cycles; we assume this continues as the net inflow moderates. Should the composition of arrivals and departures change in such a way that the balance between supply and demand evolves differently, monetary policy may need to respond.

Domestic inflationary pressure

Growth in residential investment has been weaker than expected in recent quarters. There is some uncertainty around the degree to which availability of land, labour, and finance are constraining construction activity. Construction activity has been high in many regions relative to historical experience. We assume the level of residential investment lifts more gradually over the projection than in the August Statement, reflecting capacity constraints and financing pressures. The Government’s housing programme is expected to contribute to the increase in residential investment. If constraints are more binding than assumed, the implications for inflation could vary, depending on the interaction of constraints and underlying demand.
House price inflation has slowed since mid-2016. Although it has lifted slightly in recent months, we assume house price inflation will remain low relative to recent history. We see risks to both sides of this forecast, given uncertainty regarding the effects of excess demand and policy changes that may further dampen investor demand.

Recent strength in household consumption growth is assumed to persist, supported by low interest rates and the high terms of trade. While low house price inflation has a moderating impact on consumption at the margin, the projection assumes households are less responsive to changes in housing wealth than in previous cycles. If households were to be more sensitive to weaker house price inflation, consumption would contribute less to the projected increase in capacity pressure.

In our projections, low past inflation is assumed to have a dampening impact on current and future inflation through weak price-setting behaviour. As headline inflation settles around the target midpoint over the medium term, this dampening influence will gradually dissipate. If businesses adjust their pricing behaviour more quickly in response to stronger CPI inflation or rising wage inflation, inflationary pressure could be stronger than assumed.
Box A

Recent monetary policy decisions

The Bank’s mandate is to set monetary policy to keep future inflation between 1 and 3 percent over the medium term, with a focus on 2 percent. Given this future focus, the Bank must form views about the current state of the economy, how it might evolve in the future and, ultimately, how monetary policy should respond. It is never certain how the economy will evolve. When the economy evolves differently to the Bank’s projections, the Bank seeks to understand why, and what this means for monetary policy. Monetary policy is formulated around a constant process of learning and adapting. This box reviews recent monetary policy decisions, noting how and why the Bank’s views have changed through time and how this influenced policy decisions.

At the beginning of 2014, the New Zealand economy was benefiting from the terms of trade at a 40-year high, fast growth in construction activity and a boost to demand from strong population growth. The Bank’s views of momentum in the domestic economy and anticipated strengthening of inflation suggested the economy no longer required as much monetary stimulus. As such, the Bank signalled an increasing path for the OCR. The OCR was increased by 100 basis points in four steps from 2.5 percent in January 2014 to 3.5 percent in July 2014.

From mid-2014 through to late 2015, the forward path of monetary policy changed markedly as the outlook for inflationary pressure weakened. This was the result of unanticipated changes in global economic conditions and changes in the Bank’s understanding of the domestic economy.

A weakening in the outlook for global economic activity and an increase in supply of key commodities underpinned sharp falls in global commodity prices from mid-2014. The terms of trade declined sharply, in contrast to the Bank’s previous projections of continuing strength. While the New Zealand dollar TWI fell, it remained higher than would be expected given the decline in the terms of trade. Weak import prices and a higher than anticipated exchange rate caused tradables inflation to turn, and remain, negative.

Over the same period, the Bank also observed that non-tradables inflation was not strengthening as expected given its assessment of domestic capacity. In this environment, the Bank began adjusting its policy stance while it sought to investigate the reasons for persistently low domestic inflation. The Bank held the OCR at 3.5 percent from September 2014 and progressively lowered the forward path for the OCR.

The increases in non-tradables inflation observed in earlier quarters were identified as sector-specific, rather than evidence of a broad-based lift in inflationary pressure as initially thought. The Bank revised lower its assessment of capacity pressure, reflecting an evaluation of various alternative measures of the output gap, and recognising the stronger-than-expected growth in the labour supply and potential

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output resulting from increases in both the population and labour force participation.

In addition, the Bank reconsidered the effect of high net arrivals and departures on net demand and inflationary pressure, noting less of an impact than in previous cycles.\(^4\) Analysis also indicated that businesses appeared to be putting more weight on low past inflation in their pricing decisions.\(^5\) Weak pricing behaviour was acting as a drag on future inflation, requiring more stimulus in order to meet the inflation target.

Taking account of these insights, the Bank downgraded its assessment of inflationary pressure, and from June to December 2015 the Bank lowered the OCR by 100 basis points. At the December 2015 Statement, with the OCR at 2.5 percent, the Bank stated that it expected this degree of stimulus would be sufficient to see CPI inflation settle near the midpoint of the target range, but that it would reduce the OCR further if circumstances warranted.

Developments in the first half of 2016 challenged the Bank’s assumption that global economic activity and inflation would strengthen, lifting tradables inflation in New Zealand via higher import prices and a lower exchange rate. Rather, indicators of global economic activity weakened, forecasts of global growth and inflation continued to be revised lower, and the exchange rate remained persistently high. This led the Bank to revise its medium-term view of tradables inflation significantly lower. The effects of this revision on the outlook for inflation and policy were reinforced by the previously mentioned price-setting dynamics, as well as a shift lower in surveyed inflation expectations across all time horizons in the March 2016 quarter (figure A.1). The Bank judged that circumstances warranted further easing, reducing the OCR a further 75 basis points between March and November 2016.

There was little change in the outlook for inflationary pressure at the February 2017 Statement. Accordingly, the Bank held the OCR unchanged at 1.75 percent. Growth appeared to be strengthening as forecast and while housing market activity had slowed, this was expected to be temporary, reflecting tightening of LVR restrictions and disruption due to the Kaikoura earthquakes.

The stance of monetary policy remained stable at the May and August Statements. Through this period, the Bank continued its practice of testing its views against new data and adapting its projections as

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appropriate. Decisions at each point in time reflected a view that developments between Statements, on balance, were neutral for the future direction of monetary policy. Revisions to earlier GDP figures suggested that activity was weaker through the second half of 2016 than previously thought, and had remained weaker than expected in early 2017. The slowing in the housing market was proving more persistent than had been assumed. Offsetting this weakness in terms of the inflation outlook, higher food and fuel prices were boosting headline inflation by more than assumed, while the terms of trade and fiscal stimulus emerged as additional factors expected to support activity. With the OCR at 1.75 percent at the August Statement, the Bank retained the view that monetary policy would remain accommodative for a considerable period (figure A.2).
### Table 2.1
**Key forecast variables**

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Chapter 3
International developments

- Economic activity has continued to improve in most major economies since the August Statement.

- However, global inflationary pressure remains subdued.

- Central banks have been taking steps to gradually normalise monetary policy settings, which include plans to reduce unconventional policy measures.

Momentum in the global economy has continued to increase in recent months. A broad range of economic indicators has shown robust activity in most major economies, and GDP growth has been in line with, or exceeded, policymakers’ expectations.

Since the August Statement, there have been periods of financial market volatility, mostly reflecting elevated geo-political tensions, storm-related disruptions in the United States, and recent regulatory tightening in China’s financial system (figure 3.1). However, these episodes have been short-lived and financial market volatility in general has remained at relatively low levels.

Forecasts of global economic growth for 2017 and 2018 have been revised upwards (figure 3.2), including by the IMF, OECD and Consensus (see box B for a summary of developments in New Zealand’s major trading partners). Improved confidence in the global economic outlook is also reflected in global equity prices, which are near record levels.

Despite the improvement in real economic activity, there has been little sign of inflationary pressure emerging. With the exception of the United Kingdom, headline inflation has tended to surprise on the downside and
Figure 3.1
Financial market volatility

Figure 3.2
Trading-partner GDP growth (annual)

Figure 3.3
Core inflation (annual)

Figure 3.4
Trading-partner inflation (annual)

Note: The VIX index shows the market’s expectation of the 30-day volatility in the S&P500 index. The MOVE (Merrill Lynch Option Volatility Estimate) index shows the implied one-month volatility for United States Treasury bonds.
measures of core inflation remain at relatively low levels (figure 3.3). Forecasts of trading-partner inflation for 2017 and 2018 have been revised lower (figures 3.4). In addition, wage inflation remains subdued in most major economies, even as labour market slack has reduced.

Monetary policy remains accommodative globally, and financial conditions more generally remain supportive of real activity. Despite subdued inflation outcomes, central banks are expected to gradually withdraw monetary policy stimulus. Consistent with this, the Bank of England increased its policy rate to 0.5 percent in November, the Bank of Canada increased its policy rate to 1 percent in September, the Federal Reserve began the process of unwinding its quantitative easing programme in October, and the European Central Bank (ECB) recently announced that it will begin to reduce the volume of asset purchases from January 2018.

There was little financial market reaction to the announcements by the Federal Reserve and the ECB, especially compared with the ‘taper tantrum’ in 2013 when global bond rates increased sharply. This partly reflects that the Federal Reserve’s and the ECB’s plans were signalled to financial markets well in advance, which limited the surprise element. In addition, market participants expect the pace of monetary policy normalisation to be gradual given the current environment of low global price and wage inflation.

There is uncertainty about whether current low inflation reflects transitory or structural factors. Possible structural factors keeping inflationary pressure subdued include: ongoing declines in the cost of information technology and capital goods; increasing competition in the services sector; technological revolution in the oil and gas industry that has dramatically lowered production costs and enabled new sources of supply; wage moderation across advanced economies (see box C); and lower long-term growth expectations reflecting weak productivity growth and population ageing. In turn, these structural factors have tempered expectations of the degree to which interest rates will need to increase over the medium term.

Commodity price movements have been mixed since the August Statement (figure 3.5). Prices of industrial metals have risen, reflecting the improvement in real economic activity in major economies, but agricultural commodity prices have softened. Oil prices have been higher than assumed at the time of the August Statement, reflecting a combination of expectations of higher global demand, prospects of tighter supply from OPEC, and concerns about supply disruption in the Middle East.
The New Zealand dollar TWI has fallen 4.5 percent since the August Statement, with the New Zealand dollar falling against a broad range of trading-partner currencies (figure 3.6). The depreciation of the New Zealand dollar implies slightly higher tradables inflation over the next year.

Box B

Trading-partner developments

United States

The US economy grew at an annual rate of 2.3 percent in the September 2017 quarter. Recent storm-related disruptions are expected to have a transitory effect on economic activity, and growth is expected to increase to 2.4 percent in 2018. Annual core inflation remains subdued at 1.3 percent, as measured by the core personal consumption expenditures (PCE) deflator. While there are some concerns over the persistence of recent low core PCE inflation outturns, the Federal Reserve expects the weakness to be transitory. Based on financial market pricing, the federal funds rate is expected to be increased to 1.25-1.50 percent in December, following the Federal Reserve’s move in October to reduce reinvestment of its balance sheet securities.

Euro area

Economic activity in the euro area has steadily improved over 2017. Annual GDP growth was at an above-trend pace of 2.5 percent in the September quarter. Core inflation has been rising steadily in recent months but remains below target at 1.3 percent. Inflationary pressure is expected to rise during 2018, although the recent appreciation in the euro may dampen inflation in the near term. The ECB remains confident that the pace of economic recovery can be sustained, and has announced an intention to reduce its asset purchases from January 2018.
**Australia**

Economic growth over the first half of 2017 has been weaker than expected. Recent data suggest an improvement in economic conditions, and growth is expected to lift to 2.8 percent in 2018. However, inflation remains below target and wage growth remains low. Employment growth has picked up in recent months, but slack in the labour market remains, with an elevated level of underemployment. The Reserve Bank of Australia has kept its cash rate at 1.5 percent since mid-2016.

**China**

Economic growth has remained stronger than expected over 2017. Activity is being supported by increased spending on infrastructure and property construction, but the high level of debt and rapid credit growth present risks to financial stability. Despite inflation remaining below target, the People’s Bank of China has shifted from an accommodative to a neutral policy stance. At the same time, regulation has been tightened to address financial stability risks. Capital outflows from China have eased and the renminbi has strengthened against the US dollar over 2017.

**Japan**

GDP growth is above trend in Japan and is expected to be 1.6 percent in 2017. There has been broad-based strength across consumption, business investment, and exports. Japan has maintained positive economic growth for six consecutive quarters, the longest economic expansion since 2006. Inflation is still low, with annual core inflation at 0.2 percent. The Bank of Japan is expected to maintain its yield curve targeting framework, targeting the 10-year government bond rate at around 0 percent.

**United Kingdom**

The UK economy has slowed this year, although growth has been better than anticipated. Inflation is above target at 3 percent, in large part reflecting the depreciation of the pound sterling following the Brexit vote. However, inflationary pressure is expected to rise over the medium term, with the unemployment rate currently at a 42-year low. The Bank of England increased its policy rate to 0.5 percent in November from 0.25 percent previously.
Box C

Global price and wage dynamics

Price and wage inflation in advanced economies has been muted in recent years. In many economies, price inflation has surprised on the downside and remains below central banks’ targets. This has occurred in a time of falling unemployment rates and unprecedented monetary policy stimulus by central banks. Typically, low unemployment rates would be associated with high wage growth and inflation more broadly, but this has not yet occurred (figure C.1).

Persistently weak inflationary pressure has raised the issue of whether the Phillips curve – the relationship between labour market slack and inflation – has fundamentally changed following the Global Financial Crisis. While weak labour earnings growth is unusual in light of low unemployment rates (figure C.2), there are a number of factors that help to explain this wage moderation.¹

• Subdued wage growth in advanced economies is consistent with the slowdown in labour productivity growth. Labour productivity will largely influence how much revenue businesses generate, and therefore how much they can pay employees over the long run.²

• There could be more slack in labour markets than headline measures suggest. In some countries, underemployment measures have not fallen by as much as the unemployment rate.

• A more digital and integrated global economy has changed the nature of employment. This may mean that labour market slack spills over between economies. In addition, technology, through greater automation, is adding to the range of competitive forces that may be weighing on overall wage growth.

¹ J. Culling (RBNZ, forthcoming) summarises the recent wage literature, discussing factors limiting wage growth, including: low productivity growth, labour market slack, changing nature of work, fiscal austerity, technological change, globalisation, compositional changes, and declining unionisation.

² The IMF’s recent World Economic Outlook empirically analyses recent wage dynamics in advanced economies. The IMF finds that labour market slack, productivity, and inflation have exerted downward pressure on wages. Furthermore, a common global factor has exerted downward pressure on wages. See IMF (2017), ‘Recent wage dynamics in advanced economies: drivers and implications’ World Economic Outlook, October.
Figure C.2
OECD unemployment and annual earnings growth

Source: OECD.
Chapter 4
Current domestic conditions

• As global growth has improved, New Zealand’s export prices have increased from 2016 lows. Oil prices have also increased and have contributed to higher tradables inflation.

• The New Zealand dollar TWI has depreciated since the August Statement, implying higher tradables inflation over the coming year.

• The pace of GDP growth has increased in recent quarters, but not to the extent expected. The housing market remains subdued and construction activity has slowed.

• Capacity pressure remains limited, despite some tightening in labour market conditions over the past year. Non-tradables inflation and core inflation are below average.

External prices

Global economic growth has improved over the past year, contributing to a lift in New Zealand’s export prices. The prices of the goods New Zealand exports have increased by 12 percent in the year to the June 2017 quarter, with the increase being broad-based across components. Although agricultural commodity prices have softened globally, New Zealand’s export prices have held up (figure 4.1).

The Dubai crude oil price has risen since the August Statement and is around 25 percent higher than a year ago. The increase in oil prices has contributed to a lift in import prices and tradables inflation.

The terms of trade have increased over the past year. The high terms of trade are supporting household and business spending, and spending on imports (figure 4.2).

As described in chapter 3, the New Zealand dollar TWI has depreciated since the August Statement. The TWI is currently at its lowest level since mid-2016 (figure 4.3). The recent depreciation in the TWI is expected to boost tradables inflation over the coming year.
Figure 4.1
Crude oil and ANZ commodity prices
(ANZ commodity prices in world terms)

Source: ANZ Bank, Thomson Reuters.

Figure 4.2
Terms of trade
(s.a.)

Source: Stats NZ.

Figure 4.3
New Zealand dollar TWI

Source: RBNZ.

Figure 4.4
Current account
(annual)

Source: Stats NZ.
A high exchange rate typically leads to a widening in the current account deficit, as exports become less competitive and imports become more attractive. However, New Zealand’s current account has remained broadly stable since 2010 (figure 4.4), despite the high New Zealand dollar. There has been a narrowing in the income deficit, reflecting a reduction in net foreign liabilities as a share of GDP and lower interest rates.¹ This has provided an offset to the fall in the goods and services surplus.

Tradables inflation

Annual tradables inflation has been higher in recent quarters than observed between 2012 and 2016 (figure 4.5). Annual tradables inflation increased to 1 percent in the September 2017 quarter. This increase was driven primarily by higher food and fuel price inflation.

Some of the strength in food and fuel price inflation is expected to fade over the next two quarters. The recent depreciation in the exchange rate is expected to support tradables inflation over the coming year.

Domestic financial conditions

Bank funding costs have eased marginally since the start of the year (figure 4.6). Consistent with the decline in funding costs and a decline in the two-year swap rate, the average two-year mortgage rate has declined in recent months (figure 4.7). Most other mortgage rates have remained relatively stable. Mortgage rates are higher than a year ago across all terms, but remain low relative to history.

Population growth and the housing market

Permanent and long-term (PLT) working-age arrivals to New Zealand have declined since the start of the year (figure 4.8). This reflects lower arrivals of 15-29 year olds. From a geographic perspective, the decline has been driven by fewer arrivals from Asia (figure 4.9). Arrivals from Australia, which typically do not require a visa, moderated slightly. As a result of fewer arrivals and some increase in departures, the net inflow has declined from 5,420 working-age people at the start of 2017 to 4,310 working-age people in September – the lowest number since February 2015. Despite recent falls, the net inflow remains elevated by historical standards and is contributing to above-average population growth.

Housing market activity remains subdued, despite strong population growth and low mortgage rates. Annual house price inflation in Auckland

Note: The data shown are for permanent and long-term working-age arrivals and departures.

Note: The data shown are for permanent and long-term working-age arrivals.
has fallen to -0.6 percent in September 2017, from 15 percent in mid-2016 (figure 4.10). House price inflation in the rest of New Zealand has fallen from a peak of 18 percent in 2016 to 7 percent in September 2017. Monthly nationwide house sales have fallen from a peak of 8,500 in April 2016 to around 5,500 in September 2017.

The slowing in house price inflation over the past year reflects changes to LVR restrictions, tightening in lending standards, and a rise in mortgage rates. Demand for housing may also have been tempered by pressure on affordability, reduced overseas buyer interest, uncertainties around future housing market policies, and revised expectations of future house prices.

**Domestic growth**

Quarterly GDP growth has increased gradually over recent quarters, reflecting continued strength in household spending, a recovery in dairy production and exports, and temporary boosts to tourist spending. Production GDP grew by 0.8 percent in the June 2017 quarter, and near-term indicators of activity suggest similar rates of growth are likely in coming quarters (figure 4.11). Annual GDP growth was 2.5 percent in the June quarter, and is expected to increase to around 3 percent by the end of the year.

Despite recent improvements, GDP growth has been weaker than expected, partly due to a slowing in construction activity. Residential investment has been weaker than expected in the past four quarters (figure 4.12), and annual residential investment growth has declined from 14 percent in the June quarter 2016 to -1.4 percent in the June
quarter 2017 (figure 4.13). The slowing in residential investment was due to a decline in construction activity in Canterbury and slowing growth in Auckland. Surveys and recent business visits suggest that labour shortages and tighter lending standards are limiting growth in construction activity, and cost pressures are high (see box D). Residential investment is expected to remain close to its current level over the second half of 2017.

Non-residential building investment has also weakened, declining by 5.4 percent over the year to June. Commercial construction firms appear to be facing similar constraints as residential developers. Activity is expected to improve over the second half of the year, supported by rebuild work associated with the Kaikoura earthquake, and a large volume of non-residential work that was consented over the past year.

Consumption has been growing at above-average rates in recent quarters (figure 4.14), led by high rates of growth in expenditure on services and durable goods. While house price inflation has slowed, consumption is being supported by high terms of trade, strong population and employment growth, higher consumer confidence, and low interest rates. Consumption growth on a per-capita basis is around average. Electronic card transaction data suggest consumption growth has moderated in the September 2017 quarter.

Visitor arrivals increased during the World Masters Games in April and the Lions rugby tour in June and July (figure 4.15). This provided a boost to services spending. Given the temporary nature of these events, visitor arrivals have fallen, although the recent depreciation of the exchange rate may provide some support in the near term.

Goods exports increased in the June quarter, due to a recovery in dairy-related exports from earlier weakness. Recent unfavourable
weather conditions are expected to weigh on dairy exports over the second half of the year.

**Capacity pressure**

The output gap is estimated to be around zero (figure 4.16). This is below the level expected in previous Statements, mainly due to weaker-than-expected construction activity. The range of estimates for the output gap suggested by our suite of indicators is wide, reflecting uncertainty about the current degree of capacity pressure.

While estimates of the output gap have not increased, conditions in the labour market have continued to tighten. Even with a high participation rate and high population growth, strong employment growth has
meant that the unemployment rate has fallen over the past year. The unemployment rate was 4.6 percent in the September quarter, the lowest level since 2009 (figure 4.17).

The private labour cost index (LCI) increased by 0.7 percent in the September 2017 quarter and by 1.9 percent over the year to September (figure 4.18). Above-average nominal wage growth in the quarter was due to the care and support workers’ pay equity settlement. Abstracting from this, wage growth has remained subdued, in part reflecting the effects of low past inflation.

**Inflation**

Annual CPI inflation was 1.9 percent in the September 2017 quarter, up from 1.7 percent in the June quarter (figure 4.19). The increase in CPI inflation over the past year was due to higher tradables inflation.
Non-tradables inflation remains below average at 2.6 percent, consistent with weak price-setting behaviour and limited capacity pressure. Housing-related components have continued to support non-tradables inflation, along with increases in insurance costs and some administrative prices.

The Bank uses measures of core inflation to abstract from specific price movements and observe the underlying trend in inflation. These measures seek to look through temporary volatility, such as movements in food and energy prices, giving a clearer assessment of inflationary pressure in the economy. Core inflation measures at present suggest subdued domestic inflationary pressure (figure 4.20).

Long-term inflation expectations remain well anchored at 2 percent (figure 4.21), which should be expected, given that annual CPI inflation has averaged 2.1 percent since the 1 to 3 percent target range was introduced in 2002. Short-term inflation expectations have increased from a year ago, consistent with the lift in headline inflation, and are also close to 2 percent.

Stats NZ produces several alternative measures of inflation for consumers, such as the household living-cost price indexes (HLPI) and the private final consumption expenditure deflator. These measures tend to move closely with CPI inflation, although they show different levels of price inflation due, in part, to the weights used for the components (figure 4.22).

The HLPI is designed to measure changes to the cost of living experienced by different household groups, and is calculated using similar methodologies to the CPI. A key methodological difference between the HLPI and the CPI is that the HLPI includes mortgage interest payments for owner-occupied housing, while the CPI does not.
The HLPI shows that lower-income households tend to experience larger price increases than higher-income households (figure 4.23). This largely reflects differences in household expenditure patterns, as lower-income households spend a greater proportion of their total expenditure on items with prices that increase more rapidly than general price inflation, such as rent and household energy.

The consumption deflator is the ratio of the value of consumption and the volume of consumption in GDP. Movements in the consumption deflator can reflect quantity changes along with price changes. The consumption deflator is subject to data revisions, which makes it less suitable for wage indexation and contracts (figure 4.24). In New Zealand, consumption deflator data are released about two months after the CPI.
It is a well-established practice for inflation-targeting central banks to have CPI inflation as their target.\textsuperscript{2} The CPI measures the price of a fixed basket of goods and services purchased by an average household. In New Zealand, the composition of this basket is updated regularly. The CPI is the timeliest measure of living costs in New Zealand, and is not subject to revisions. From a monetary policy perspective, it is important that mortgage interest payments are not included in the inflation measure, as monetary policy directly affects mortgage rates. Given these properties, the CPI is the most appropriate measure for setting monetary policy.


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Box D

Summary of recent business visits

The Bank regularly meets with a range of businesses and organisations to enhance our industry knowledge and understanding of current economic conditions. This helps inform our economic projections. In our most recent round of business visits, we spoke with 20 organisations from Auckland, Wellington, Christchurch, Hamilton, and Rotorua. The majority of these organisations are in the construction and real estate sectors.

Construction activity has eased in recent quarters, although it remains at a high level. Contacts noted that a range of constraints have become more binding, particularly around labour and the availability of finance, while high land prices and other costs have put margins under pressure in the industry. These constraints and cost pressures have resulted in project delays and some cancellations, particularly in Auckland. Firms expect limited increases in construction activity over the coming year.

Housing market activity has weakened over the past year. Contacts cited a range of factors that are contributing to the slowing in the housing market: a tightening of financial conditions; lower capital gain expectations and investor confidence; the tightening in LVR restrictions in late 2016; increases in mortgage rates around the end of 2016; affordability pressures; declines in offshore investor activity; and elevated uncertainty.
Table 4.1

Measures of inflation, inflation expectations, and asset prices

<table>
<thead>
<tr>
<th>Inflation (annual rates)</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mar</td>
<td>Jun</td>
</tr>
<tr>
<td>CPI</td>
<td>0.4</td>
<td>0.4</td>
</tr>
<tr>
<td>CPI non-tradables</td>
<td>1.6</td>
<td>1.8</td>
</tr>
<tr>
<td>CPI tradables</td>
<td>-1.2</td>
<td>-1.5</td>
</tr>
<tr>
<td>Sectoral factor model estimate of core inflation</td>
<td>1.5</td>
<td>1.5</td>
</tr>
<tr>
<td>CPI trimmed mean (30 percent)</td>
<td>1.1</td>
<td>1.2</td>
</tr>
<tr>
<td>CPI weighted median</td>
<td>1.5</td>
<td>1.7</td>
</tr>
<tr>
<td>GDP deflator (expenditure)</td>
<td>0.9</td>
<td>0.2</td>
</tr>
</tbody>
</table>

| Inflation expectations |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
|------------------------| | | | | | | | | | | | | | | |
| ANZ Business Outlook - inflation one year ahead                  | 1.4 | 1.4 | 1.5 | 1.5 | 1.8 | 2.0 | 1.9 | 1.9 |
| (quarterly average to date)                                      |     |     |     |     |     |     |     |     |
| RBNZ Survey of Expectations - inflation two years ahead          | 1.6 | 1.6 | 1.7 | 1.7 | 1.9 | 2.2 | 2.1 | 2.0 |
| AON Hewitt Economists’ Survey - inflation four years ahead       | 2.0 | 1.9 | 2.0 | 2.0 | 2.0 | 2.0 | 1.9 |
| AON Hewitt Economists’ Survey - inflation seven years ahead      | 2.1 | 2.0 | 2.1 | 2.0 | 2.0 | 2.0 | 2.0 |
| Long-run inflation expectations¹                                | 2.0 | 2.0 | 2.1 | 2.0 | 2.0 | 2.0 | 2.0 | 2.0 |

| Asset prices (annual percent changes) |  |  |  |  |  |  |  |  |  |  |  |  |  |  |  |
|--------------------------------------| | | | | | | | | | | | | | | |
| Quarterly house price index (CoreLogic NZ) | 11.6 | 13.9 | 12.6 | 14.0 | 10.9 | 5.1 |
| REINZ Farm Price Index (quarterly average to date) | 4.2 | -2.6 | 4.3 | 4.9 | 4.5 | 5.2 | 9.5 |
| NZX 50 (quarterly average to date) | 9.1 | 18.4 | 26.5 | 15.8 | 12.8 | 7.6 | 6.6 | 16.2 |

¹ Long-run expectations are extracted from a range of surveys using a Nelson-Siegel model. Source: ANZ Bank, Aon Consulting, Consensus Economics, RBNZ estimates.
Chapter 5

The macroeconomic outlook

- Despite the recent increase, tradables inflation is expected to be low over the medium term, reflecting weak global inflationary pressure.
- Stimulatory monetary policy, population growth, and high terms of trade are expected to support GDP growth and a rise in capacity pressure. Domestic demand is also assumed to be supported by more-stimulatory fiscal policy.
- An increase in capacity pressure is expected to generate a sustained rise in non-tradables inflation, keeping CPI inflation near 2 percent over the medium term.

As discussed in chapter 3, the New Zealand dollar TWI has depreciated 4.5 percent since the August Statement. The TWI is assumed to be 73.5 throughout the projection (figure 5.1).

New Zealand’s import prices have increased since 2016, consistent with rises in global commodity prices (figure 5.2). Import prices are expected to be stable in world terms over the medium term, with the Dubai oil price assumed to be around USD 55 per barrel.

Annual tradables inflation is expected to be around its post-2000 average over the next year (figure 5.3). The recent depreciation in the New Zealand dollar is expected to support tradables inflation. Some volatility in tradables inflation is expected over the next year, reflecting movements in fuel and food prices. Over the medium term, persistently low global inflationary pressure (discussed in chapter 3) continues to suppress tradables inflation.

While tradables inflation is projected to fall, we expect a rise in non-tradables inflation to keep CPI inflation around the middle of the target range. Stimulatory monetary policy supports above-trend GDP growth. The associated rise in capacity pressure generates higher non-tradables inflation.
**Figure 5.1**
New Zealand dollar TWI

Source: RBNZ estimates.

**Figure 5.2**
Import prices
*(world terms, s.a.)*

Source: Stats NZ, RBNZ estimates.

**Figure 5.3**
Tradables inflation
*(annual)*

Note: The dashed line represents the post-2000 average of realised annual tradables inflation.

Source: Stats NZ, RBNZ estimates.

**Figure 5.4**
Working-age population growth
*(annual)*

Source: Stats NZ, RBNZ estimates.
Working-age population growth is strong by historical standards, having been supported by high arrivals and low departures. Permanent and long-term arrivals (including returning New Zealand citizens) are assumed to slow over the next three years. Conditions in overseas labour markets are expected to improve relative to New Zealand and the Government is assumed to tighten visa requirements. Lower net inflows are expected to moderate population growth. Nevertheless, the working-age population is projected to increase by 6 percent over the next three years (figure 5.4).

Strong population growth and low mortgage rates are expected to support housing demand. However, these effects are being offset by tight lending conditions and increasing pressures on affordability. As a result, house prices are expected to rise more gradually than in recent years (figure 5.5).
Despite strong underlying demand for new housing, residential investment over the near term is expected to rise at a slower pace than previously assumed (figure 5.6). This reflects constraints relating to the availability of finance, labour shortages, and a lack of land with infrastructure already in place. Residential investment is assumed to be supported by the Government’s housing programme, particularly over the second half of the projection (see box E).

Consumption growth slows over the projection, in part because the impetus from population growth wanes (figure 5.7). Consumption growth is expected to be supported by stimulatory monetary policy, strong population growth, fiscal policy, and high terms of trade (figure 5.8). Subdued housing market activity is projected to provide a modest offset.

High terms of trade and rising capacity pressure are expected to support business investment over the projection (figure 5.9). Domestic demand
is projected to contribute to a strengthening in GDP growth, although pressure on capacity is partly dampened by higher import volumes. Annual GDP growth averages 3.3 percent over the next two years (figure 5.10).

Potential output is expected to grow by 2.8 percent annually over the next two years, driven by continued strong population growth and some recovery in productivity. Above-trend GDP growth has the output gap increasing to 1.1 percent (figure 5.11). Consistent with this rising capacity pressure, the unemployment rate is expected to trend lower to 4.3 percent in 2019. Increasing demand for labour is expected to support underlying wage growth over the coming years. Additionally, the care and support workers’ pay equity settlement and the proposed increases in the minimum wage are expected to boost wage growth over the projection.

The rise in capacity pressure is expected to generate a sustained increase in non-tradables inflation to above-average levels (figure 5.12). This offsets low tradables inflation to see annual CPI inflation settle near 2 percent over the medium term (figure 5.13).

**Scenario analysis**

The projections discussed in this chapter reflect the Bank’s central view of how global and domestic economic conditions might evolve, and how these will affect inflationary pressure in New Zealand. Given this view, the projected path for the OCR is consistent with future average inflation settling near the target midpoint.

The projections and appropriate policy response are conditional on a range of judgements regarding the future path of key variables. As
discussed in chapter 2, there are always uncertainties and risks around these projections. Uncertainty is heightened at present.

The following scenarios illustrate two risks that would have a substantial impact on the projections if they materialised. The two scenarios considered are that:

- global inflationary pressure increases more than expected; and
- domestic capacity pressure is lower than projected, due to weaker growth in consumption and residential investment activity.

**Scenario 1: stronger global inflation**

One of the key judgements underpinning the central projection is that global inflation recovers slowly. This contributes to below-average tradables inflation in the medium term, necessitating an increase in non-tradables inflation to meet the Bank’s inflation target. This scenario assesses the effect on the New Zealand economy if global inflation increases more than expected.

Stronger global inflation would directly boost New Zealand’s import prices (figure 5.14). Higher global inflation would also prompt a faster tightening of global monetary policy than assumed, resulting in a faster narrowing of interest rate differentials and, therefore, a depreciation of the New Zealand dollar TWI (figure 5.15). Both higher import prices and the lower TWI would generate an increase in tradables inflation (figure 5.16).
Without an appropriate monetary policy response, CPI inflation would settle above the midpoint of the target range. In this scenario, the OCR would need to be around 100 basis points higher (figure 5.19), consistent with CPI inflation returning to near 2 percent over the medium term.

**Scenario 2: weaker domestic demand**

The central projection assumes that capacity pressure increases over the medium term, driven in part by growth in consumption and residential investment. However, there is a risk that domestic demand does not pick up to the extent expected. This could occur if consumption and residential investment, counter to our central assumption, weaken in response to weaker house price inflation.

The second scenario assumes that both consumption and residential investment are weaker than in the central projection (figures 5.17...
and 5.18). Low consumption and residential investment imply weaker domestic demand, generating a more gradual rise in capacity pressure and non-tradables inflation. Without an appropriate monetary policy response, headline inflation would settle below the target midpoint over the medium term.

To maintain CPI inflation around the target midpoint, monetary policy would need to be more accommodative. In this scenario, the OCR would need to be lowered by around 100 basis points by the start of 2020 (figure 5.19).

**Policy implications**

It is important to note that the scenarios considered in this chapter represent moderate deviations from the central projection relative to the historical experience. In reality, there are a range of uncertainties relating to the outlook, and combinations of unforeseen developments can influence the economy simultaneously. While some of these developments might be offsetting, deviations from the central projections could be larger than those shown here, leading to a wider range of associated monetary policy responses.
Box E

Key assumptions regarding government policy

There have been significant changes in government policy since the August Statement. In this set of projections, we have incorporated the estimated impacts of four policy areas that are expected to have significant effects on the business cycle. These are:

- government spending initiatives;
- the housing programme (‘KiwiBuild’);
- changes to visa requirements; and
- minimum wage increases.

The working assumptions outlined here are based on what we currently know of government policy given announcements to date. Consistent with the Bank’s standard practice, we have consulted with the Treasury on indicative estimates of policy impacts, and overlaid these with our own assumptions as to the business cycle and behavioural responses. The overall effects of these policies on the economy will depend on how private households and businesses respond. Taken together, the set of assumptions outlined below equates to more fiscal stimulus than incorporated in the August Statement.

Government spending initiatives

Nominal government consumption is assumed to be around 3 percent (or around 0.5 percent of GDP) higher than projected in the August Statement. The overall effects of this higher government consumption are uncertain, depending in part on the reaction of households. Increases in government consumption could be partly offset by a decline in household consumption if households assume increased government expenditure will necessitate higher taxes in the future. The degree of offset can vary with the strength of aggregate demand.

While the effects of tax changes announced in Budget 2017 have been removed from our projections, household consumption is supported by the Government’s Families Package. Taking together the effects of increased government consumption and changes to transfers and allowances, our working assumption is that household consumption is not substantially affected by higher government spending.

Housing programme

The Government has announced an intention to build 100,000 houses in the next decade. Our working assumption is that the programme gradually scales up over time to a pace of 10,000 houses per year by the end of the projection horizon. Given existing pressure on resources in the construction sector, the aggregate boost to construction activity from this policy will depend on how resources are allocated across public and private sector activities. The Government intends to introduce a ‘KiwiBuild visa’ to support the supply of labour to high-need construction-related trades. While accompanying policy initiatives may alleviate capacity constraints to some extent, our working assumption is that around half of the proposed increase will be offset by a reduction in private sector activity.

Changes to visa requirements

The Government has indicated its intention to strengthen requirements for work and student visas, with an estimated effect of reducing annual
arrivals across these visa categories by 20,000-30,000. In light of this proposal, we assume a faster decline in permanent and long-term arrivals in our projections than in August. Changes to visa requirements do not affect arrivals and departures of New Zealand and Australian citizens. We continue to assume only a gradual normalisation of net flows between Australia and New Zealand.

**Minimum wage increases**

The Government has indicated its intention to raise the minimum wage to $20 per hour by 2021, beginning with an initial increase in April 2018. Increases in the minimum wage have a direct impact on labour incomes and wage inflation. It is uncertain how businesses will respond to the increase in minimum wage. The lift in minimum wage may spill over to workers in higher wage brackets, and could impact on businesses’ labour demand and hiring intentions. A higher minimum wage may also encourage workers currently outside of the labour force to enter, increasing labour supply, although labour force participation is already at a record level.

In our projections, we assume the minimum wage rises by equal increments in each of the next four tax years. Allowing for only the direct impact, and accounting for the changes in the minimum wage already implicit in our projections, we assume this lifts annual wage inflation by 0.2 percentage points over the projection. We assume modest effects on labour demand and labour supply over the projection period.2

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### Table 5.1
Composition of real GDP growth
(annual average percent change, seasonally adjusted, unless specified otherwise)

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<td></td>
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<td>Private</td>
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<td>Public authority</td>
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<td>2.5</td>
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<tr>
<td>Total</td>
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<td>2.9</td>
<td>1.7</td>
<td>3.2</td>
<td>3.1</td>
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<td>4.3</td>
<td>3.6</td>
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<tr>
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<td>2.9</td>
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1 Percentage point contribution to the growth rate of GDP.
### Table 5.2
Summary of economic projections
(annual percent change, unless specified otherwise)

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<th>March year</th>
<th>Actuals</th>
<th>Projections</th>
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<td>Export prices (in New Zealand dollars)</td>
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<td>Import prices (in New Zealand dollars)</td>
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<td><strong>Output</strong></td>
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<td>Potential output (annual average % change)</td>
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<td>Output gap (% of potential GDP, year average)</td>
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<td>Current account balance (% of GDP)</td>
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<td>Trading-partner GDP (annual average % change)</td>
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<tr>
<td>Trading-partner CPI (TWI weighted)</td>
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