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Central Bank Outlook

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New Zealand: Rates Unchanged, Extended Policy Pause

As was universally expected, the Reserve Bank of New Zealand decided to leave the Official Cash Rate (OCR) unchanged at 2.50% following its meeting in September, after similar decisions in its eleven previous meetings, all following the 50 bp rate cut in March 2011 in response to the earthquake.

Growth Projections Revised Higher, Inflation Contained

The accompanying statement by Governor Bollard began by noting that the domestic economic outlook remained broadly consistent with that described in the June monetary policy statement, with *modest growth still expected over the next few years as housing market activity (including the expected repair and reconstruction efforts in Canterbury) offsets fiscal consolidation and the high exchange rate*. However, the outlook for a number of the nation's trading partners was noted to have remained weak, with several Eurozone economies noted to be in recession and Chinese growth seen to have slowed. The risk of a significant deterioration in the Eurozone, meanwhile, was still seen to have persisted. More specifically, updated forecasts in the latest (September) Monetary Policy Statement show GDP growth slowing clearly from the 1.1% Q/Q jump in Q1 to 0.4% in the second quarter, before then gradually picking up again to peak around mid-2013 at 0.8% and finally settling back to around 0.4% by the end of 2014.

In regard to inflation, *the underlying annual rate was noted to have moved below 2%, but was still projected to settle near the mid-point of the Bank's target range of 1-3% over the medium-term*. This is reflected in updated projections showing headline inflation rising from the 1.0% Y/Y outcome in Q1 to 2.1% by mid-2013 and then hovering at or below 2% until Q2 2014.

DE View: In what is Governor Bollard's last meeting, he described the latest Monetary Policy Statement as "reassuringly boring" because the economy was "stable", with medium-term inflation well within the zone and growth forecasts actually slightly upgraded from June. The Governor further noted that the RBNZ was in a "reasonably sweet position with regards to monetary policy setting" with the option either to raise or cut the OCR going forward. However, the actual 90-day rate forecasts provided in the Statement largely reflected the stable economic outlook in showing only a very gradual increase in rates, hitting 3% only by Q2 2014 (revised lower from June). *All of which clearly implies that an extended policy pause is the most probable outcome going forward*. On a separate note, incoming Governor Graeme Wheeler will take his position on 26 September.