Harbour Navigator

New Governor arrives as inflation falls outside target.

16 October 2012 | ContactUs@harbourasset.co.nz +64 4 460 8309

The NZ CPI rose by +0.3% in the September quarter, to be only +0.8% higher than a year earlier. This was below market expectations, and leaves annual inflation at a decade-low and just below the bottom of the RBNZ's 1 to 3% target range.

So does this mean that the RBNZ should ' think the unthinkable' and cut its Official Cash Rate from its record low of 2.5%?

While current inflation is below the bottom of the target range, the real job of the RBNZ will be to judge inflation pressures going forward, and how they expect inflation to get back to target over the next 12 to 18 months.

Most economists argue that the RBNZ should not cut interest rates from these levels. They highlight that non-tradeable inflation at 2.3% is roughly in the middle of the target. This is just another way of saying that our current low inflation can mostly be put down to the unusual high NZ dollar. They also point to the Canterbury rebuild and buoyancy in the Auckland housing market fuelling domestically generated inflation on the horizon.

However, it is also true the inflation outlook looks much less troublesome than it did earlier in the year, and there is a chance that inflation stays stubbornly low. The last two weak inflation outturns should keep the inflation expectations of local households and businesses well anchored. Importantly, in recent weeks the leading indicators of economic activity have also tended to point to a weak Q3 GDP number ahead. Furthermore, with foreign central banks loosening policy, there is a good chance that the NZ dollar remains at elevated levels for some time yet, keeping tradeable inflation low.

In our view, it has genuinely become a 50/50 call whether the RBNZ cuts rates over the next six months. It certainly makes for a very interesting start to the job for new Governor Graeme Wheeler at the Reserve Banks' Official Cash Rate (OCR) review next week.

IMPORTANT NOTICE AND DISCLAIMER

The Harbour Navigator is provided for general information purposes only. The information is given in good faith and has been prepared from published information and other sources believed to be reliable, accurate and complete at the time of preparation but its accuracy and completeness is not guaranteed. Information and any analysis, opinions or views contained herein reflect a judgement at the date of publication and are subject to change without notice. To the extent that any such information, analysis, opinions or views constitute advice, they do not take into account any person's particular financial situation or goals and, accordingly, do not constitute personalised advice under the Financial Advisers Act 2008, nor do they constitute advice of a legal, tax, accounting or other nature to any persons. Investment in funds managed by Harbour Asset Management Limited can only be made using the Investment Statement, which should be read carefully before an investment decision is made. The price, value and income derived from investments may fluctuate in that values can go down as well as up and investors may get back less than originally invested. Where an investment is denominated in a foreign currency, changes in rates of exchange may have an adverse effect on the value, price or income of the investment. Reference to taxation or the impact of taxation does not constitute tax advice. The rules on and bases of taxation can change. The value of any tax reliefs will depend on your circumstances. You should consult your tax adviser in order to understand the impact of investment decisions on your tax position. No person guarantees repayment of any capital or payment of any returns on capital invested in the funds. Actual performance will be affected by fund charges. Past performance is not indicative of future results, and no representation or warranty, express or implied, is made regarding future performance. To the maximum extent permitted by law, no liability or responsibility is accepted for any loss or damage, direct or consequential, arising from or in connection with this presentation or its contents. Actual performance of investments managed by Harbour Asset Management Limited will be affected by management charges. No person guarantees the performance of funds managed by Harbour Asset Management Limited.