

# Harbour Navigator

## Labour's mainstream monetary policy proposals

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Yesterday, Labour Party finance spokesperson Grant Robertson announced “**Labour’s modern approach to monetary policy**”, outlining their proposals to amend the objective and governance of the Reserve Bank of New Zealand (RBNZ). We would contend that “mainstream” should be added to this title. If anything, these suggestions would bring the RBNZ into line with global practice. And Labour aren’t the only ones considering this issue; there are already signs that the National Party are considering governance changes that would challenge the RBNZ Governor’s sole decision making role.

While inflation targeting has been considered sacrosanct in New Zealand for the past 25 years, there is a history of opposition political parties proposing tweaks at the margins. Some have been implemented; like the change in the inflation target range. Others never saw the light of day; like David Parker’s radical 2014 Labour proposal to add targeting the current account deficit, and giving the RBNZ the ability to move KiwiSaver contribution rates to hit the target.

There are two elements of Grant Robertson’s current proposal:

### 1. Objective:

While keeping the 1-3% inflation target, the RBNZ would be given a dual mandate of also targeting full employment.

This would bring New Zealand into line with other regimes such as that in the United States. Indeed, it would represent a convergence between the US and New Zealand models from both directions. The US Federal Reserve has long had a dual mandate, but only in recent years quantified 2% as its inflation target. New Zealand has had a specific numerical inflation target for longer than any other central bank, and would add full employment without this concept being quantified.

In our view, the addition of full employment to the mandate would not materially change the way the RBNZ operates in practice. Employment is already a key consideration when thinking about capacity pressures, and therefore inflation pressure.

Grant Robertson understands that putting full employment in the RBNZ’s mandate does not magically make it happen. However, in our view there could be political mileage in emphasising that the RBNZ’s objectives are aligned with Labour’s broader economic priorities.

## 2. Governance:

The second element of the proposal is moving away from the current decision making structure, where the Governor alone is accountable for Official Cash Rate (OCR) decisions.

The current structure is, to a large extent, a function of history. When inflation targeting was first introduced, the challenge was getting inflation down from the highs of the 1970s and 1980s. This required a highly independent, highly incentivised public servant to deliver on this new and difficult task. However, now that inflation expectations are more comfortably anchored around the RBNZ's inflation target, the environment today is much different.

Graeme Wheeler has already acknowledged this point and introduced a more conventional decision making structure by forming an informal Governors Committee (made up of four internal Governors) that votes on OCR decisions.

Grant Robertson's proposal would take this a step further by adding three external members and a Treasury observer, with minutes published. There are some details that remain open to debate: the balance of internals and externals; who makes the appointments; the independence of externals; their access to internal resources; the type of relevant expertise. These issues may bore the average person on the street, but nevertheless are important governance considerations.

The broader point is that removing the current sole decision-maker structure would bring the RBNZ into the global mainstream; there is no other central bank globally with such a singular concentration of power. In recent years, it appears to us that the main argument against changing the governance structure has been that it would require new legislation to be passed, opening up the government to debate on other aspects of the legislation.

It may transpire that changes to the RBNZ's governance are on the way, whichever party is in power after the General Election this year. As Minister of Finance, Steven Joyce, appears much more open to exploring these issues than his predecessor, Bill English. It was reported on the weekend that Steven Joyce had commissioned former State Services Commissioner, Iain Rennie, to undertake preparatory work on the RBNZ's governance and committee decision making structures.

Rather than radical changes, we see these types of governance changes as enhancements on the margins to a framework that will continue to be centred on price stability.

For investors and analysts, the only difference may be a little less focus on the Governor of the RBNZ, and a greater need to understand the other decision makers around the table.

***Harbour Asset Management***

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