



Source: Reserve Bank of New Zealand

20 August 2025

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Governor

Transcript

Christian Hawkesby:

Kia ora koutou katoa, nau mai, haere mai. Welcome. Welcome. We are here to discuss this, the August Monetary Policy Statement. Just checking you're in the right room and on the right channel. Joined as usual with the Assistant Governor Karen Silk, Chief Economist Paul Conway and our other members of the Monetary Policy Committee here in the front row. Professor Prasanna Gai, Carl Hansen. And I'd particularly like to acknowledge Professor Bob Buckle whose term on the MPC finishes after this meeting. So one of the originals back from April, 2019. Bob, it's been an absolute honour working with you through that. So to today's decision, the Monetary Policy Committee voted to reduce the Official Cash Rate by 25 basis points to 3%. Annual consumer price inflation is currently at the top of our 1 to 3% target range. However, with spare capacity in the economy and declining domestic inflation pressure, headline inflation is expected to return to around 2% by the middle of next year.

New Zealand's economy. Economic recovery stalled in the second quarter of this year. Spending by households and businesses has been constrained by heightened global policy uncertainty, falling employment, higher prices for some essentials and declining house prices. Looking forward, there are upside and downside risks to the economic outlook. Cautious behaviour by households and businesses could further dampen economic growth. Alternatively, the economic recovery could accelerate as the full effects of interest rate reductions flow through the economy. Further data on the speed of New Zealand's economic recovery will determine our next steps from here. If medium term inflation pressures continue to ease as expected there is scope to reduce the official cash rate further. Thank you. I will open it up to questions. Just a reminder, there is a lot going on at the Reserve Bank across many fronts including some significant organisational changes. We are here today to discuss the Monetary Policy Statement and so would welcome your questions on the decision and the outlook for the economy. Thank you. And if you just direct your questions to me, I can share them around the team as appropriate.



Media questions

Media:

Thanks. Matthew Brock from Bloomberg, you've obviously lowered your OCR forward track. Could you confirm for us that the final two meetings of this year you would consider them to be live with the potential for the OCR to fall to 2.5% by the end of this year?

Christian Hawkesby:

So every decision of the monetary policy committee is always live and no decisions have been made for future dates at this point. It's true. We have revised down significantly our official cash rate projection in the document that's largely around the news about the starting point for the economy for New Zealand. So that stalling of growth that we've observed through Q2, that's meant that there's more spare capacity for longer than previously and that's meant we can have interest rates lower to support the economy and get the right amount of domestic inflation pressure. That projection is troughs at around two point a half percent by the end of this year and so that would be consistent with further cuts through the course of this year. Whether we end up going faster or slower than that will be determined by developments over that period.

Media:

And just in terms of the dates for these sorts of decisions, the finance minister has said that she would quite like you to introduce an additional policy meeting over the summer. I'm wondering whether that's something you are giving consideration to and whether if you do intend to do that it could come as soon as this summer.

Christian Hawkesby:

So we always like to have 12 months of our meeting dates in the public domain in that enables OIS contracts to be priced meeting to meeting sufficiently far out into the future. So we currently have 12 months of dates out there that includes over this summer period. Of course we always have the ability to have an emergency meeting outside that schedule if we wish. We are currently working on the plan for the next 12 month period and we're looking to release that over the next month or so.



Media:

Well, let me try again. Have you taken on board what the finance minister has said? Is it an option that you are looking at for adding an extra rate decision?

Christian Hawkesby:

We are conscious of the gap in meetings between November and February and particularly the one that we experienced earlier this year. Our meeting schedules have to be determined by the availability of data and that's what we really work off. What is the schedule of data ahead of us for our projections? What is the key data that needs to go into that process? We are getting more frequent data. We've got a monthly CPI coming up in the future and we hope to have more of other types of frequent data. So that's what will drive our schedule. We are conscious that it is wide over that summer break and we are looking at ways that we can narrow that while it's still being driven by data availability. I'd also note that, I mean not having a meeting in January is not unusual internationally. So the RBA used to meet 11 times a year and not meet in January. They now meet 8 times in the year and don't meet in January either and that's also dictated by data availability.

Media:

Tom Pullar-Strecker from The Post. It looks as though two members of the committee voted for a larger cut this time, but there was also some discussion around keeping the rates on hold. Can you just give us a flavour of I guess the range of views at the meeting and was this a factious decision? I mean this seems to be a more divided decision if I'm correct than any other that the Reserve Bank has held on this.

Christian Hawkesby:

We've never had a 4-2 vote before. That is true. So as always we follow the process in terms of we in accordance with our charter. Our charter asks us to try and seek consensus and the processes designed that way to work on building up a common understanding of the data, the analysis, the outlook from here where there was a strong consensus was around the central path for the official cash rate. There was comfort that that could be lowered significantly to acknowledge the data flow that we've seen since May where there was the range of views was around the risks around that outlook. So we had some members emphasising the downside risk. There's always uncertainty and a range of outcomes around our central projection. We had some members emphasising the downside risks, other members



emphasising the upside and others seeing the risks as balanced and so I think that's a key outcome and it illustrates the uncertainty that we are in at the moment.

The argument for a more modest cut, no cut or a more modest cut was around the fact that yes, we've seen economic activity stall in Q2, but that could be temporary, that could bounce back and we are already seeing some indicators from July quite healthy. Also a consciousness that inflation is near the top of the range and so there's a risk that inflation expectations ratchet up and make our job harder. On the downside, the risk is really around the slowdown in QT to being more persistent and really needing more of a jolt and more aggressive action from us to write the economy.

Media:

The bank has signalled the possibility that inflation could breach 3% in this statement. I mean should we sort of regard this as confirmation that the change of mandate for the Reserve Bank to focus solely on inflation hasn't had too much of a difference in terms of the way that you view these decisions?

Christian Hawkesby:

I'd really emphasise quite strongly that the mandate is to set interest rates today to achieve our inflation target in the medium term. So we know that our actions today can't affect inflation measures right now, but they can have a strong effect in the medium term. And so we're always looking out at that horizon and I think our actions today illustrate that focus because we have this consciousness that there is a 50-50 chance that we do go over 3% in the near term, but an acknowledgement that we have little impact on that, but we have a strong impact on where inflation will be over that medium term and with inflation pressures abating, our job is to keep focused on that horizon.

Media:

Jenée Tibshraeny from the Herald, just a question about timings in terms of the appointment of a permanent governor and also Professor Bob Buckle's replacement, it's two roles that'll be up in the air and are you able to provide us a bit more information about when those changes will take place?



Christian Hawkesby:

So those appointments are both in the hands of our Board and the Minister of Finance, so I'm not the spokesperson on either of those appointments. I know in the case of the MPC appointment we're on track to have Bob's replacement for October, so we will look to make that appointment before that time.

Media:

Sure. Does that, I mean uncertainty has been a big theme for a long time now, but does the fact that there's quite a bit of change underway at the committee, does that add another layer of uncertainty on top of the existing uncertainty, which is I guess reflected the different views held by the members of the committee?

Christian Hawkesby:

I would actually come to the opposite conclusion, which is we've had a lot of over 6 and a half years we've had the natural turnover that you would have on a committee where these terms are 3 to 5 years long and I'll be the last standing original from April 2019. We've had new members come in and the committee roll on and that's the power of the process that we have, which is very much driven around the analytical capabilities of our staff supporting a group of decision makers. So I have a very strong degree of confidence that whoever's in these roles in 12 months time will be very well supported in achieving our mandate.

Media:

Sure. Just finally, I didn't want to give the impression that Christian, you might not be on the Committee in the future. Are you able to tell us whether it's a job that you'd like for full term?

Christian Hawkesby:

I did manage to find time to dust off my CV and throw it in the mix and I'll leave it at that.

Media:

Hi, Jenny Ruth from Good Returns and Just the Business. Your projections put the OCR now bottoming at 2.3, sorry, 2.5, sorry. Is that, has your view of where neutral is changed at all?



Christian Hawkesby:

I'm going to give myself a break from talking and pass this over to Paul who I know will speak to that with wisdom.

Paul Conway:

Thanks Governor. No, we know Jenny, we have not changed our view on where neutral is. So the OCR, it's clearly not restrictive anymore. We're sort of in that zone of neutral, but you can't be too sort of mechanistic about these things. You can't say the economy's in a bit of a hole, therefore the OCR is restrictive. We're sort of layering on the sort of uncertainty shock from tariffs and global economic policy uncertainty, which explains the whole. So yeah, we are around that neutral sort of period and I made a speech on this a while ago. We sort of feel our way as much as else without getting too mechanistic about whether the OCR is a 10th of a point above or below neutral. It's what effect are we having on the economy. It's sort of more to the fore now.

Christian Hawkesby:

Yeah, that's right. I'd just add that concept of neutral and where it is is a very helpful one when you're at 5.5% or when you're at half a percent, but when you are in and around it and within that range of uncertainty it's less a focus for the committee. The committee's more focused on what are we learning about the economy and how it is responding and what it's going through.

Media:

I just looked up the dates for the central bank meeting in Jackson Hole and seeing you here, does that mean you're not going this year?

Christian Hawkesby:

I thought I'd prioritise showing up to this press conference over taking a flight to Jackson Hole, although Karen tells me it's, or Karen and Paul have both been there. Actually, yes, and this is one of the things we need to when it comes to a meeting schedule, these are the things that we need to navigate the data key international meetings and how we find our way there. This time around the regular Jackson Hole's been scheduled a week differently than normal and that's one of the reasons we are not there.



Media:

Thank you. My name's Zane Small, I'm with Stuff and 3 News. The Minister of Finance just spoke in parliament saying that the government's disciplined spending has given the Reserve Bank room to reduce the Official Cash Rate. I'm just curious how much that is the case.

Christian Hawkesby:

We mentioned in our record of meeting that we do, we did discuss the fiscal outlook. It is one where government spending as a proportion of all activity is falling through our projection period. So in that sense it's part of reducing inflation pressures that's also consistent with what we had in May because we don't have any new information since the May budget.

Media:

So it does help.

Christian Hawkesby:

Yes.

Media:

Okay, thank you. And just to follow up, you mentioned that there are downside risks to economic growth with the behaviour of households and businesses perhaps being a bit more cautious. How much does that play into your decisions and have you noticed that there has been a significant change in the behaviour of households and businesses and their spending habits?

Christian Hawkesby:

Well, what we have noticed is that economic activity in Q2 was considerably weaker than we expected. We knew that we had the liberation day 2nd of April announcements around tariffs internationally and that there was a lot of uncertainty and a lot of anxiety about how that could play out and how that could escalate. We've ended up in avoiding the worst case scenario. There hasn't been the escalation that there could have been and some of those measures of global policy uncertainty have actually been falling more recently. But despite that, there has been this cautiousness in businesses and consumers and it has lingered longer



than we had anticipated and so that's some of the thinking around whether those sectors have just become too cautious and need a bit more of a lift than we had expected.

Paul Conway:

I think the other interesting factor there is around house prices. Normally we'd expect house prices to be increasing a bit more at this point in the cycle, but we are not expecting them to increase a great deal over the coming 18 months also. And when you look at household consumption, it's very highly correlated with changes in what's going on in the housing market. So there's a bit of an open question there. Can the New Zealand economy grow without that sort of wealth effect coming through the house health?

Karen Silk:

But one of the key things that we also need to consider is that the 250 basis point cuts that we've now done, we've probably seen 50% of that transmit through. So there's another 50% still to go. So there's certainly more stimulation still to come that will support freeing up of disposable income at a household level and eventually feed into house prices and residential construction as a consequence of that as well.

Paul Conway:

So we do see growth going forward. We've got a negative number in there for Q2, a small positive for Q3 and then back into reasonable growth from the end of this year.

Karen Silk:

Yeah.

Media:

Lucy from Reuters, Paul, just on that, does that mean that you think the worst is over and things are going to improve from here?

Paul Conway:

Yes.



Karen Silk:

Yeah.

Paul Conway:

Yeah, if you look at our forecasts, the Q2 is the trough in terms of GDP growth. So yeah, we're now in Q3, so yeah.

Media:

And following on from Jenny's question, if we're around neutral at the moment, where do you see two point a half percent? Is that stimulatory? Is that where we are getting into stimulus kind of territory and you there's a possibility you might go below 2 and a half. What would need to happen for you to be tipped into going lower?

Christian Hawkesby:

I'll just repeat that. There's a very wide range of uncertainty around where neutral is and that it's not a concept that we're focusing on at the moment. Given that we're close to that zone, what will determine the outlook from here is how the data and information plays out and if we are seeing businesses and consumers persisting in this cautious behaviour and needing more support, that might be something that prompts more action from us. Alternatively, if we come out the other end of that zone and into Q3 and economic activity picks up, then that's the flip side for us.

Paul Conway:

Can I just add to that the fact, as Karen was saying, the fact that we've cut from 5.5 to 3%, that 250 basis points of easing, which takes us from clearly restrictive to around neutral that will support economic growth. It's not like we sort of magically get into a new zone and the economy takes off on us or anything like that. So we do see the economy growing from here and low interest rates a big part of the reason why.

Media:

Yeah, two of you voted to cut by 50 basis points. Any chance you want to tell us who wanted to cut by 50 basis points?



Christian Hawkesby:

We don't disclose the votes. Members are able to out themselves if they wish, but we haven't had any indication this time around.

Media:

They don't want to out themselves. And last question, Christian has dusted off his CV, Paul, Karen, have either of you dusted off your CVs?

Paul Conway:

No, I have not dusted off my CV. I'm very happy being Chief Economist.

Karen Silk:

I don't don't feel the need.

Media:

Fair enough.

Paul Conway:

My job is big enough. Thank you very much.

Media:

Richard Harmon, Politic. Earlier this year the bank published a study on the pass through rate of interest rate of OCR changes on a sector by sector basis. Are you able to give us some indication of which sectors you would expect to see the impact of today's decision appear in?

Christian Hawkesby:

Paul, would you like to speak to that?



Paul Conway:

Yeah, I'll have a crack at that. So one of the obviously export prices have been very high in the New Zealand economy recently, so sort of outward looking sectors, the ag sector have been a source of growth, whereas those more inward looking parts of the economy have been lagging. So we've got quite a mixed picture as the governor was saying, it's a multi-speed economy at the moment, which isn't unusual. So going forward we would expect lower interest rates to show up in things like investment and residential investment and consumption and on an industry by industry basis what industries are leaning into those parts of the economy and that would be retail, et cetera, et cetera. So yeah, we are seeing monetary policy is working, it is passing through, it's affecting mortgage rates and deposit rates and it is showing up on the real side. Growth was pretty pretty reasonable end of last year and the beginning of this year we've hit a bit of a jutter bar as we say in this country.

A key issue for the Monetary Policy Committee is how long is that going to persist? We think we will get through it because of lower interest rates and we will see that in things like residential investment and consumption, which is a huge part of this economy.

Karen Silk:

The other thing is it's not just interest rates that will drive the outcomes in some of those sectors. Paul's certainly talking about the ones that are more interest rate sensitive. There's no doubt about that. But if you think about housing, housing in Auckland population growth is a significant impact as well on what's happening with housing in the Auckland region. So low net working age immigration is very low. So that is having its own impact in particular where we've got an economy that has focused on increasing supply at the same time. So there's lots of different factors that fit into these things and monetary policy is only one of them.

Paul Conway:

It's super interesting at the moment because the housing market, we're not seeing house prices increase, as Karen was saying, maybe we're seeing it more on the supply side. So increases in demand will lead to more residential investment that could be part of low interest rates, part of low population growth, population growth is very low and house prices and population growth have been key drivers of economic growth in this economy for decades. So it really gets us back to the issue of productivity growth. If we want to get growth going forward in the long run, then it's about improving productivity in this economy and monetary



policy is not the instrument for that. We're about controlling demand to keep inflation low and stable. There's only so much we can do.

Media:

Giles Beckford from Radio New Zealand. A lot of discussion about your faith in the transmission of lower rates and that. Have you paused and thought back as to why the transmission to date of 250 basis points has been so weak and so slow?

Karen Silk:

Yeah, we have been definitely looking at that and in fact a whole section on that in the monetary policy statement this time around, there's a couple of things that we would probably call out. The first of those is consumer behaviour itself and if we think about what's actually happening in terms of re-fixing mortgage rates, people have opted to stay in shorter terms, so on demand or up to six months at much higher rates in the belief that they would come lower before they started to move out. So as that happens, it means your transmission is actually slower than you would anticipate That's changing. So what we are now seeing is households move to refix for longer terms at much lower rates and that's why we see the average stock rate coming down over the next 12 months. So if we saw it peak at 6.4, it's probably running around about 5.6 now and it'll be in 12 months time, slightly below five.

So there's that aspect of it coming through. The second aspect to it is in terms of disposable income in what we'd say lower household or slowing household income profile is what's happening with some of the more essential items that a household needs to continue to pay for. So what's happening with electricity prices, what's happening with rates, what's happening with food prices? So you're getting a little bit more contraction there. So money is going from discretionary spending into maintaining what they would regard as essential requirements that they need to do. So there's a little bit of that going on as well.

Media:

Does that make you have pause for thought about whether you need to tweak the mechanisms, whether you need to tweak your communication in order to perhaps get better, more immediate effect of the decisions that you take notwithstanding that it takes you nine months, 12 months for that to flow through?



Christian Hawkesby:

What I'd emphasize is that we've known for a long time that monetary policy lags along in variable and monetary policy works through different channels and different times and different speeds. When I started in this role 2019, interest rates were low and people were talking about they're not effective. You're pushing on a string, you won't get any increase in economic activity and we've learned that when you do move to those extremes, you do have an impact on the economy. We've felt it at the top and we've felt it at the bottom. It's just that there's a lot of uncertainty about how quickly these things will work through. I think that's what gives us the confidence that monetary policy, when we say monetary policy works, we say that interest rates lower or higher do have an impact and you've just got to have a confidence that will work its way through. The challenge is there will be other things that go on along the way.

Media:

Exactly.

Christian Hawkesby:

And that's where we need to constantly readjust and recalibrate about whether we've done enough or whether we need to do more and particularly in the zone that we're in at the moment where we've done a lot in a rapid period, now we start feeling our way.

Karen Silk:

Look, a great example was Q4, end of Q4 last year, Q1 this year where we were seeing consumption up, investment up. We then got hit with, it's an uncertainty shock is what I would call happened at the beginning of Q2 and you saw saw that kind of external impact contract and pull that back. Now we're looking for it to, as that starts to wane that we believe that monetary policy, the continuing transmission that we're seeing will continue to have the impact that we were starting to see over the end of last year and into the early part of this year.

Media:

I could ask just one more, which is what's your message to lenders, banks and your message to households rather than just something more than have faith it will work?



Karen Silk:

You might want to answer Christian, but the first thing I would say is that from a lender's perspective, there is no constraint in terms of their ability to continue to lend its credit demand that is weak at the moment and that's why you are seeing a bit more competition in those mortgage rates in particular occur in terms of households. Look, honestly, you will start to see this flow through and part of that is dependent on some of their behaviour as well and what decisions they choose to make, but we are anticipating that that recovery is going to pick up to the later part of this year and we'll see growth going into next year. That's our central projection and that's the one that we have faith in.

Christian Hawkesby:

I mean another key message for both households and businesses is that they can have confidence that inflation's going to remain low and stable into the future and they should base their decisions on being in that environment.

Media:

Kia ora, Mandy He from interest.co.nz. I'm just wanting to return back to that cautiousness cautious behaviour for businesses and recent comments from Simon Bridges as the Auckland business Chamber of Commerce head boss. Just wondering if you think any fiscal stimulus is needed for places like Auckland and Wellington?

Christian Hawkesby:

That's really a question for the Minister of Finance. I mean what we focus on is what we can do with monetary policy and we acknowledge that at the moment it feels like a two speed economy. What we'd emphasize is that it's always a multi-speed economy. There's always different sectors, industry regions feeling, feeling different depending on the environment that we're in. So it's not unusual that we're in a multi-speed economy, but it is very pronounced at the moment between Auckland and Wellington and the rest of the country.

Media:

Tracy Withers from Bloomberg. Do you feel that the pause in July had a negative impact on confidence and sentiment and maybe has prolonged this downturn?



Christian Hawkesby:

That's not my assessment. I think we always make our decisions based on the information that we have available at the time. In July, we did talk about our openness to lower interest rates and that was something that we made clear in July. There was some evidence that things were cooling there. We showed an openness to be responsive to that. As we got more information and now we've followed through on that and more today.

Media:

There was a lot of expectation, 3% may have been the bottom point of the cycle. Now you're leaning towards virtually 2.5%. That's quite a shift in 3 months.

Christian Hawkesby:

And that reflects our assessment of how much spare capacity there is in the economy. The fact that as the data through Q2 has panned out, it's given us more a firmer assessment that the economy actually contracted through that period and we don't need such a large negative output gap so much to be a capacity to achieve our mandate. That doesn't need to be the case. And so we need lower interest rates to close that gap.

Paul Conway:

We've learned a lot since the May statement at the time or the hold was in July and we sort of said we need more information on the economic slowdown, how persistent inflation is going to be at the top end of the band there and how tariffs and how uncertainty is going to sort of percolate and flow through the economy. And obviously we don't have all the answers on all of that, but we've definitely pushed our knowledge frontier out on many of those issues. Hence the more assertive approach in this MPS compared to the last.

Media:

The market seems to have taken this statement as being very doveish and the dollars fallen quite a lot against the US. I think maybe 70 points. Is that a reaction that you are comfortable with?



Christian Hawkesby:

Yes, it's a reaction we're comfortable with and a reaction that we anticipated given our actions. It's one of the ways that illustrate that even by moving 25 basis points, but the signalling power of the vote and of the OCR track means that actual conditions and markets can start moving for us in terms of providing that additional easing in monetary conditions. Any further questions? No. Great, great. Well, we'll wrap it up there and we'll be back in November and hopefully introducing Bob Buckle's replacement. So we will see you then. October. We'll be here in November.