**Monetary Challenge Report**

It has been decided to keep the Official Cash Rate unchanged at 2.5%.

Overview

 As our team classified and processed the information we gathered, we decided to differentiate between the 3 levels of inflationary pressure, (1) Low (2) Moderate and (3) High. After processing the information we gathered in the table, we appointed each event with the 3 levels of inflationary pressure. In the end our totals were as follows: 29 for hold, 12 for decrease and 2 for an increase. This helped our team to determine and obtain an objective analysis and we have all agreed that the Official Cash Rate (OCR) should remain unchanged at 2.5%.

 Our team of five members have worked together over the last few months to collect information by searching the internet and also observing newspaper articles and viewing the latest current affairs (news). We analysed the collected data by creating three columns – **Hold**, **Decrease** and **Increase.** After analysing and classifying them into three columns we award three grades for the different types of inflationary pressure – High Pressure (3), Moderate Pressure (2) and Low Pressure (1). Together as a team we analysed the collected information and have decided that it is best to keep the OCR at its current point 2.5%. We have all agreed that the Official Cash Rate should remain unchanged at 2.5 per cent based on the information we have collected and examined through keeping in mind the economic relational factors which play a vital role in our countries economy.

Key Outlook:

The key outlook is the developing European Crisis. The Spanish bank bail outs and the Greek Crisis are expected to determine the future of the Official Cash Rate (OCR) decrease. Domestically, New Zealand’s growth (GDP) is sluggish (Dec 2011-1.4%). Unemployment continues to rise at 6.7%, although there has been an increase in the net outflow of migrants to overseas countries. The unemployment rate within New Zealand would have been at high levels if the net outflow of migrants overseas were at a lower rate. Even with a net outflow of migrants, the unemployment rate has risen. Export Commodity Prices have fallen at a swift pace which will lead to those within the agriculture industry to suffer a decrease in income. The exchange rate has dropped by 6 per cent and 3.6 per cent compared to the trade weighted index. Additionally the exchange rate has fallen against the US dollar from 82 cents (US$) when the last official cash rate review was created.

In the other economy of our major trading partners such as Australia, United States, China, Europe and Japan have seen growth figures to be unpleasing. The Reserve Bank of Australia has dropped the OCR by 75 percentage points from 4.25 to 3.5 per cent. The American economy has shown the latest employment figures from USA to show very weak growth. There have only been 69,000 new jobs available within the last month as the unemployment continues to stay at 8.2%. Within China economic growth has decreased with the GDP rate currently at 9.2% forecasted to drop to 8.0% during 2012. Great Britain, France and other European countries are currently struggling with high levels of unemployment and low levels of economic growth. Japan shows levels of unsteady economic growth with minor increases at 1% and slight signs of decreases within the economy.

The effects of high levels of unemployment and poor levels of economic growth affecting our major trading partners will also in turn affect New Zealand’s economy. This is a component of the Aggregate Demand within our countries economy as our trading partners will play a major role on the Net Exports and Imports of New Zealand’s aggregate demand.

Inflationary Outlook:

The current rate of inflation is well within the PTA of its objective of 1 to 3 per cent and it is apparent that it is trending down.

By looking at the above key policy outlook it appears that is it best for the Reserve Bank of New Zealand to decrease the OCR. However, outlined below are some inflationary pressures.

The Christchurch Rebuild, when this process begins at full potential there will be some signs of inflation within the economy. This will result in an injection into the economy as there will be an increase in the availability of jobs for those who are unemployed. An injection of money will be apparent as insurance money is received within the economy and trades people (industry) will be employed. This will lower the levels of unemployment. The House Price Index would also be affected as there will be an increase in the number of rebuilt houses. The Housing Market is showing signs of improvement. Since January 2011 there has been an increase from a minus 1.5% to an increase of 2.7% in December 2011. Retail Sales have significantly increased from previous years on a steady trend. The Household saving ratio from a low minus 9.5% to 0.2%, yet the spending levels are strong which means that there are some inflationary pressures. The graph below shows the House Prices and retail sales:

Conclusion:

There is some inflationary pressure based on the above information which is why our team thinks that we should hold the OCR at 2.5%. However, in the long term from 12-18 months if Europe turns into a major crisis or the New Zealand dollar becomes stronger, then we should consider cutting the OCR to 15 percentage points.