24 March 2026

RBNZ's textbook response to Iranian fallout

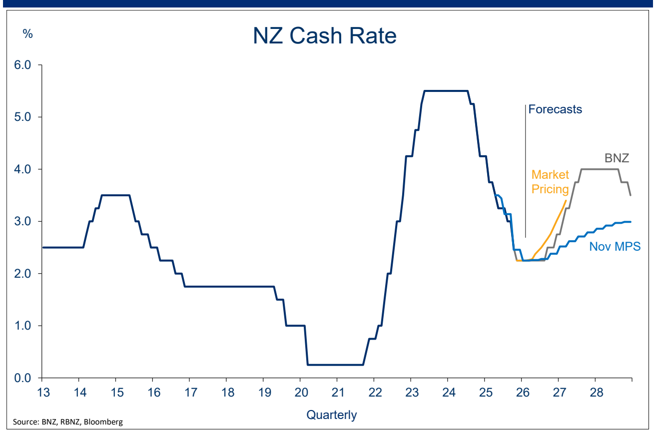
- **RBNZ will not deliver knee jerk reaction**
- **Will look through first round inflation impacts**
- **Effectively rules out April (and maybe May) rate hike**
- **But inflation will linger**
- **Demanding a strong response later this year**

Dr Anna Breman's speech on the impact of the Middle Eastern conflict was one of the most watched in recent history. Financial markets were looking for a clear indication of the Bank's thoughts and what it might mean for monetary policy settings. In contrast, it was our view the new Governor would play a very straight bat. And while the Swedes are not well known for their cricketing prowess, she provided the Black Caps with a very clear lesson as to how that should be done.

For all intents and purposes, Dr Breman's speech was an Eco 101 lecture on how central banks should respond to a major supply shock, in this case an oil crisis. She simply repeated what we have been saying for some time, namely that the central bank can look through the initial shock but will need to respond, eventually, if inflation expectations rise and second round effects indicate some form of elevated inflation permanence.

The first clear message to markets is that it could take months for the central bank to determine that inflation pressures will last for the medium term. This being so, market pricing which, prior to today's speech, indicated a 25% chance of a rate hike in April was given a serve. The RBNZ is not going to provide a knee jerk reaction to the jump in oil prices. It never was but it is now on record as saying so.

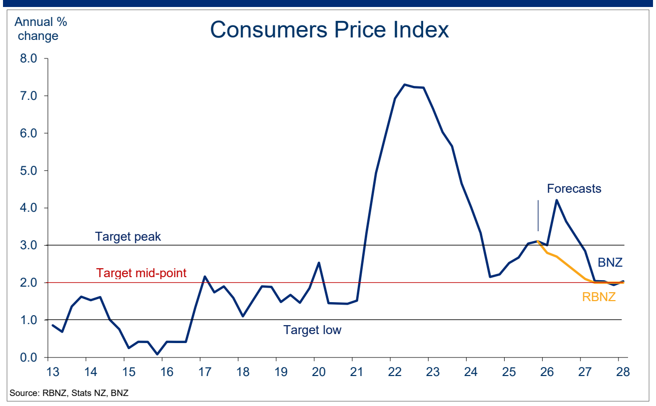
Market overzealous



But that doesn't mean the RBNZ will fail to swing into action later in the piece. Anna Breman is a very traditional central banker. The control of inflation is her focal point. If we've got weak growth but still elevated inflation, getting inflation lower will be her point of focus.

We think it is almost certain inflation expectations will rise. After all they are adaptive. That is, if headline inflation rises so too will inflation expectations. With annual CPI growth set to exceed 4.0% and to then stay outside the target band for all of 2026, it is almost certain inflation expectations will rise to levels that the Reserve Bank will be uncomfortable with.

Inflation expectations bound to rise



Moreover, we believe that second round effects will be elevated. Weak demand suggests it will be more difficult for businesses to pass on increased input costs but the pressure on margins, which was already there, means businesses will have no choice. Sure, the pass through will be less than "normal" but it will be there.

And, lastly, we think the impact of the shock in the Middle East will be enduring. Given the damage that has been done to energy production infrastructure, it is highly unlikely prices of oil and gas will fall to levels seen prior to the start of this conflict. Also, it is expected New Zealand will choose to increase its resilience to such shocks which will come with a cost.

So, we are more convinced than ever that the cash rate will be raised relatively aggressively. We see the process starting in September. This was our view anyway. The circumstances have changed dramatically from demand-driven inflation to supply-driven inflation but it will be inflation all the same, and more so than we had originally expected.

As for the Monetary Policy Review on April 8, we expect something like today’s speech with the addition of greater detail on expected short term inflation and the impact of the crisis on medium term growth.

We do not expect any move in the cash rate in April nor any clear indication as to when rate increases might start.

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