

The Treasury

Reserve Bank Dual Mandate Change Information Release

February 2024

This document has been proactively released by the Treasury on the Treasury website at <https://www.treasury.govt.nz/publications/information-release/reserve-bank-dual-mandate>.

Information Withheld

Some parts of this information release would not be appropriate to release and, if requested, would be withheld under the Official Information Act 1982 (the Act).

Where this is the case, the relevant sections of the Act that would apply have been identified.

Where information has been withheld, no public interest has been identified that would outweigh the reasons for withholding it.

Key to sections of the Act under which information has been withheld:

- [33] 9(2)(f)(iv) - to maintain the current constitutional conventions protecting the confidentiality of advice tendered by ministers and officials
- [35] 9(2)(g)(ii) - to maintain the effective conduct of public affairs through protecting ministers, members of government organisations, officers and employees from improper pressure or harassment;
- [39] 9(2)(k) - to prevent the disclosure of official information for improper gain or improper advantage

Where information has been withheld, a numbered reference to the applicable section of the Act has been made, as listed above. For example, a [33] appearing where information has been withheld in a release document refers to section 9(2)(f)(iv).

Copyright and Licensing

Cabinet material and advice to Ministers from the Treasury and other public service departments are © **Crown copyright** but are licensed for re-use under **Creative Commons Attribution 4.0 International (CC BY 4.0)** [<https://creativecommons.org/licenses/by/4.0/>].

For material created by other parties, copyright is held by them and they must be consulted on the licensing terms that they apply to their material.

Accessibility

The Treasury can provide an alternate HTML version of this material if requested. Please cite this document's title or PDF file name when you email a request to information@treasury.govt.nz.

Treasury Report: Draft New Monetary Policy Committee Remit and Charter

Date:	Monday 4 December 2023	Report No:	T2023/2038
		File Number:	MC-1-3

Action sought

	Action sought	Deadline
Hon Nicola Willis Minister of Finance	Agree wording for the new Monetary Policy Committee Remit and Charter Sign the attached letter to the Governor of the Reserve Bank	Tuesday 5 December 2023

Contact for telephone discussion (if required)

Name	Position	Telephone	1st Contact
Hamish Dick	Analyst, [39] Macroeconomic and Fiscal Policy	[35]	✓
Simon McLoughlin	Manager, Macroeconomic and Fiscal Policy		
Tim Hampton	Director, Economic System		

Minister's Office actions (if required)

<p>Return the signed report to Treasury.</p> <p>Send the signed letter to the Reserve Bank.</p>

Note any feedback on the quality of the report

Enclosure: Yes (attached)

Treasury Report: Draft New Monetary Policy Committee Remit and Charter

Purpose of Report

1. On 11 December 2023, following Cabinet approval, you will be introducing legislation to remove the “dual mandate” from the Reserve Bank of New Zealand Act 2021 (the Act) [T2023/2001 and T2023/2015 refer]. This will be achieved by removing from the Act the objective that the Reserve Bank of New Zealand (the Reserve Bank) support maximum sustainable employment (MSE) when taking monetary policy decisions.
2. As the current Monetary Policy Committee (MPC) Remit and Charter refer to the objective to support MSE, a new MPC Remit and Charter will be needed upon the passage of this Bill.
3. This report seeks your agreement to the wording of these documents.

New MPC Remit and Charter

4. The MPC Remit issued by you, as Minister of Finance, sets out the operational objectives of monetary policy. The MPC Charter sets out requirements to promote transparency and accountability in connection with the performance of the MPC’s functions, and sets out decision-making procedures.

Legislative requirements

5. Under the Act, you may issue a new MPC Remit at any time (section 122). Before issuing a new MPC Remit, you are required to consult with the Reserve Bank (schedule 3, clause 8).
6. When a new MPC Remit is issued, you and the MPC must consider whether it is necessary or desirable to issue a replacement MPC Charter (section 103). Unlike the Remit, which is issued by you as the Minister, the Charter is agreed and issued by you and the MPC.
7. As the current MPC Charter references the objective to support MSE, we believe it is desirable at this time to agree a new Charter with the MPC, alongside the issuance of a new Remit.
8. Attached to this report are draft versions of a new MPC Remit and Charter. These documents take the existing MPC Remit and Charter as their starting point, and make a small number of focused changes necessary to remove references to the objective to support MSE (as well as a small number of other changes; see section below).
9. The attached MPC Remit and Charter have been drafted so that they are within the scope of the Act both before and after the amendment to remove the MSE objective. This means that the new Remit and Charter can be made before the Bill has passed, ensuring that they come into effect alongside (but not in advance of) the coming into force of the changes to the Act.

Content of new Remit and Charter

10. We recommend that only a few changes are made to the MPC Remit and Charter at this time, given that a comprehensive Remit Review was completed earlier this year.¹ We also value the benefits of broad stability in New Zealand’s monetary policy regime, given the predictability and confidence that policy stability provides to financial markets and the public.
11. If there are other simple changes you intend to make to the MPC Remit and Charter alongside the removal of the objective to support MSE (that do not require more considered advice), we believe that it is better that these are made now than for new documents to be needed again in the near future. However, before considering whether to define the “medium term” more clearly in the MPC Remit and Charter, we recommend that detailed advice is considered on this matter (as set out in the coalition agreement between the National Party and the ACT Party). We are prepared to engage with you on your preferred timing and scope for that advice.
12. The MPC Remit must set out operational objectives for carrying out the function of formulating monetary policy. To give effect to your decision to remove maximum sustainable employment from the Act and to clearly focus the MPC on achieving price stability, we have removed references to maximum sustainable employment in the Remit.
13. Furthermore, the existing MPC Remit also contains the expectation in a “context” section that in pursuing the operational objectives, the MPC should be aware of the broader context in which monetary policy is conducted.
14. Specifically, in the context section, the existing Remit notes that the MPC should seek to understand and communicate material interactions between monetary policy and the Government’s economic objectives, where considered appropriate. This includes the impact on sustainable house prices, explaining how financial risks were considered in choosing the mix of monetary policy tools, seeking to understand material interactions between fiscal and monetary policy and supporting information sharing. These are not requirements that the MPC must take into consideration when setting monetary policy. Rather, they attempt to set the context and an expectation that the MPC will understand and explain these interactions. The MPC Charter contains similar requirements.
15. In their 2023 Remit Review advice, the Reserve Bank recommended that the context section of the MPC Remit should remove references to the Government’s objectives and focus only on the legislative purpose of the Act. The Reserve Bank considered that simplifying the context section would reduce perception risks to the Reserve Bank’s operational independence and would place greater emphasis on the operational objectives. The Reserve Bank also considered that removing such references would support a more enduring MPC Remit. The Reserve Bank viewed other documents – such as the Letter of Expectations and Memorandums of Understanding – as more appropriate avenues to consider these issues through.

¹ Treasury Advice on the 2023 Monetary Policy Committee Remit Review, <https://www.treasury.govt.nz/publications/information-release/treasury-advice-2023-monetary-policy-committee-remit-review-information-release>. Reserve Bank advice, <https://www.rbnz.govt.nz/-/media/project/sites/rbnz/files/monetary-policy/about-monetary-policy/supporting-new-zealands-economic-stability-toitu-te-ohanga.pdf>.

16. We agree that simplifying this context section ensures that the MPC is focused primarily on price stability, which is the intention behind the policy to remove the dual mandate. Our draft attached Remit therefore replaces these detailed context requirements with a generic reference to “the Government’s economic objectives”. We believe it is important to retain some reference to the Government’s economic objectives to support monetary-fiscal coordination and transparency around the effects of policy decisions, as set below (point d).
17. We recommend that the deleted details from the MPC Remit remain in the MPC Charter. These matters sit more naturally in the Charter than in the Remit, as the purpose of the Charter is to set out expectations for MPC decision making processes (whereas the purpose of the Remit is to define the operational objectives for the formulation of monetary policy).
18. The four most significant recommended changes, other than the removal of references to MSE, are:

- a **Employment** – With or without a dual mandate, the impacts of labour market developments remain relevant to monetary policy formulation. We therefore recommend the addition of the word “employment” to section 2(ii) of the MPC Remit:

In pursuing the operational objective, the MPC shall: ii. seek to avoid unnecessary instability in output, employment, interest rates, and the exchange rate.²

This addition reflects the important role that the labour market plays in the implementation of the flexible inflation targeting approach that has been used by the MPC for many years, while maintaining a clear primary focus on the inflation target. Under flexible inflation targeting, the central bank has the primary aim of stabilising inflation in line with the inflation target in the medium term, while having regard to stabilising the real economy in the short term. This addition will require the MPC to explain how it has taken into account volatility in the labour market in its decisions, through the Charter’s requirement that the MPC explain, in each *Monetary Policy Statement*, how it has “sought to meet the requirements of section 2 in the MPC Remit.” This will strengthen incentives to continue to undertake high quality labour market research to better understand labour market dynamics and their relevance for monetary policy.

- b **Sustainable house prices** – It is our view that the reference to sustainable house prices in the MPC Charter is a positive inclusion. As part of the 2023 MPC Remit Review, we noted that the inclusion of the house price sustainability clause in the MPC Remit contributed to an improved understanding of the impacts of monetary policy on the housing market. We have observed that the requirement that the MPC assess its impacts on the objective of sustainable house prices has led to a significant increase in the collective understanding of the impacts of monetary policy on house prices.

If this requirement is to be kept in the Charter, you may wish to provide additional or alternative wording that relates to your Government’s objectives for house prices. Alternatively, you could choose to remove the reference to house prices from the MPC Charter (section 2(b)(iii)), and instead include “house prices” in the MPC Remit alongside output, employment, interest rates and the exchange rate as the variables that the MPC should seek to consider when minimising unnecessary economic instability. Nonetheless, we believe there is a material difference between “instability in” house prices and the “sustainability of” house

² This was the wording of the 2018 Policy Targets Agreement.
T2023/2038 Draft New Monetary Policy Committee Remit and Charter

prices, which you should consider when deciding how and whether this matter might be included in the MPC Remit and/or Charter.

- c **Deviations from target** – We recommend the addition of the underlined text to the MPC Charter (in relation to the requirements of the *Monetary Policy Statement*). This addition reflects the importance of the MPC being able to explain its strategy for returning inflation to target, and therefore supports the prioritisation of price stability.

When inflation outcomes, and/or expected inflation outcomes, are outside of the target range, explain the reasons for this, the timeframe over which inflation is expected to return to the target midpoint and the reasons for that timeframe.

- d **Monetary-fiscal coordination** – We recommend leaving the following sentence in the MPC Remit:

Where appropriate, the MPC should seek to understand and communicate material interactions between monetary policy and the Government's economic objectives.

The retention of this text highlights to the MPC the importance of coordination across different economic policies. Although the MPC is accountable only for monetary policy, we believe it is important to ensure that the impacts of monetary policy are transparent to both monetary and fiscal authorities. Transparency of policy impacts helps mitigate against scenarios where economic policies are developed without regard to one another, and are therefore inadvertently working in different directions (i.e., this text might be seen to mirror the Public Finance Act 1989 requirement that fiscal policy have “regard to the interaction between fiscal policy and monetary policy”).³

Next Steps

19. We seek your direction on these changes and the content of the new MPC Remit and Charter. We are happy to discuss these documents with you in greater detail, should you wish.
20. Once wording for both documents has been agreed, we ask that you sign the attached letter to the Reserve Bank and that this is then sent to the Chairperson and Governor of the Reserve Bank (with the proposed new MPC Remit and Charter attached), so that the Reserve Bank is consulted and so that the MPC may agree changes to the Charter.

³ Section 26G.

Recommended Action

We recommend that you:

- a **note** that, under the Reserve Bank of New Zealand Act 2021, you may issue a new Monetary Policy Committee (MPC) Remit at any time
- b **note** that the Reserve Bank of New Zealand Act 2021 requires that, before issuing a new MPC Remit, you consult with the Reserve Bank of New Zealand
- c **note** that, when issuing a new MPC Remit, you and the MPC must consider whether it is necessary or desirable to issue a replacement MPC Charter
- d **note** that the MPC Charter is a document agreed between you and the MPC, and that you and the MPC may agree to issue a replacement Charter at any time
- e **note** that it is the Treasury's view that both a new MPC Remit and Charter are needed to align with the removal of the "dual mandate" from the Reserve Bank of New Zealand Act 2021 [T2023/2001 and T2023/2015 refer]
- f **agree** to share the attached draft MPC Remit and Charter with the Reserve Bank of New Zealand for consultation and agreement, respectively

Agree / disagree

OR

- g **provide** to the Treasury your intended wording for the new MPC Remit and/or Charter to be shared with the Reserve Bank of New Zealand for consultation and agreement, and
- h **sign** the attached letter to the Chairperson and Governor of the Reserve Bank of New Zealand.

Simon McLoughlin
Manager, Macroeconomic and Fiscal Policy

Hon Nicola Willis
Minister of Finance

_____/_____/_____