Key Developments[1] & Chart of the week

26 February 2021

The Fed reaffirms its inflation dovishness; but New Zealand takes aim at asset prices

	Outcome	Previous	Comment
US Fed Chair testimony	Reaffirmation of stance		Fed will not hurry to tighten policy
Reserve Bank of New Zealand	A telling change of policy		Asset (housing) prices now a focus
UK average earnings (Dec)	+4.7%	5%	'Underlying' earnings growth at 3% y/y
UK unemployment rate (Dec)	5.1%	+3.7%	Continued weak labour market

Jay Powell testimony

- US Fed Chair Powell emphasised that the Fed will *not* tighten monetary policy "*solely in response to a strong labour market*" (as it has done in the past), but rather will wait until it is clear that *price* inflation has "*moderately*" exceeded 2% "*for some time*".
- The aim is to ensure that "*longer-term inflation expectations* [remain] *well anchored at our 2% goal*" (rather than falling below). With US economy "*a long way from* [the Fed's] *employment and inflation goals*" achieving "*substantial further progress*" will likely "*take some time*".

Reserve Bank of New Zealand

- Perhaps significantly, given its historical role as a pioneer in monetary policymaking, the NZ Government amended the RBNZ's remit, requiring it to take account of asset (housing) prices in both monetary policy and financial stability decisions.[2]

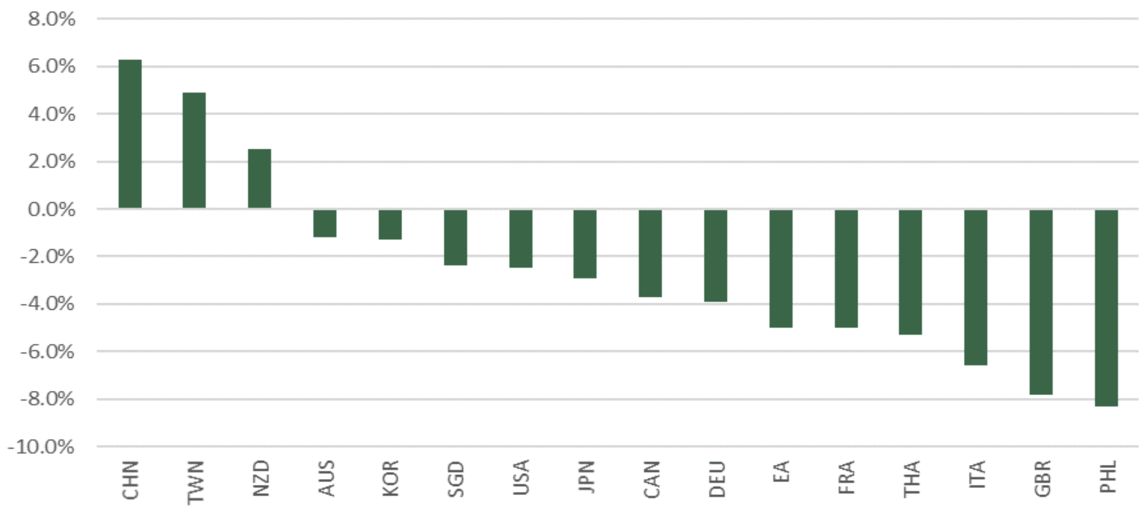
UK labour market data: continued weakness

- UK unemployment has continued to rise, and the employment rate to fall.[3] ONS real-time 'experimental' data suggest that the true slack in the labour market may be even higher.[4] The biggest fall in payroll employees since the pandemic has been in the 18-24 years age group.
- The aggregate earnings figure[5] has grown briskly, but was driven in part by compositional effects – a fall in lower-paid jobs, and postponement of bonuses from earlier in the year.

Bottom line*: While US monetary policy will not be dictated by likely goods and price inflation, New Zealand, with its GDP now above pre-COVID levels, is taking aim at asset prices. A harbinger?*

Chart of the week. **GDP deviation from 2019 peak** (as of Q4 2020).

- Asian economies are recovering fastest, led by the majors. Among the major economies, the service-oriented UK is lagging.



Sources: Llewellyn Consulting and Macrobond
Note: The data for Australia and New Zealand are estimates from respective Treasuries.

[1] *Key Developments* presents what, in our judgement, represent the past week's most important individual data and other developments. These are selected, in an attempt to counteract the risk of Kahneman 'confirmation bias', as those best able to reveal the extent to which the key assumptions and relationships that underpin our *World View* remain valid – or not, as the case may be. Generally we feature hard data rather than forecasts or survey results; but make exceptions in important cases.

This approach is particularly important at present because the shock that has hit economies and markets is both large and novel, twin conditions that typically challenge understanding and lead to unusually large forecasting errors.

[2] This could presage more 'macro-prudential' tightening of mortgage lending following the new limits on high loan-to-value lending imposed earlier this month.

[3] The employment rate is now 1.5 pp lower than it was a year ago.

[4] Early estimates for January 2021 indicate that there were 28.3 million payrolled employees, a fall of 2.5% compared with the same period of the previous year, and a decline of 730,000 people over the 12-month period.

[5] We are watching earning developments keenly, in all major economies. There is concern, in financial markets and beyond, at the risk of inflation as economies recover. Some 'bottleneck' rises are to be expected, and duly reflected in some aggregate price data. But this would become 'true' inflation only if it led to increases in nominal wages, over an above increases in productivity.