

The evolution of Policy Targets Agreements

This paper summarises the changes made to the Policy Targets Agreements (PTAs) since the Reserve Bank of New Zealand Act 1989 came into force in early 1990. The main points made in the paper are summarised here.

- The PTA is a key element in the New Zealand monetary policy framework. It is the means by which the Minister of Finance/Treasurer and the Governor of the Reserve Bank agree on the specification and measurement of price stability. The PTA forms an important element in the monetary policy transparency and accountability processes.
- Changes to the PTA can only be made with the mutual agreement of the Minister of Finance/Treasurer and Governor. Both must satisfy themselves that any changes made to the PTA are consistent with the price stability objective, as laid out in the Act. However, the Act makes provision for the Government to override the price stability objective and to require the Reserve Bank to conduct monetary policy for other purposes.
- Although price stability could be achieved through a number of alternative mechanisms, all the PTAs to date have been based on explicit inflation targeting.
- There have been six PTAs since the Act came into force. The current PTA was signed in December 1999.
- Although there have been a number of changes to the PTAs in the last decade, most have been relatively minor in nature. The core features have remained essentially the same, particularly the concept of the inflation target and the “caveats” enabling the Bank to allow inflation to move temporarily outside the inflation target band in certain circumstances.
- The most important changes made to the PTA have been:
 - the change from requiring a re-negotiation of the PTA where price shocks appear to threaten the price stability objective, to a “caveat” approach requiring the Bank to identify price shocks and to state its intended approach to bring inflation back within the target band, made in December 1990;
 - the lengthening of the period for achieving inflation within the (original) 0 to 2 per cent target band, made in December 1990;
 - the widening of the inflation target band to 0 to 3 per cent, effected in December 1996; and
 - making explicit the requirement for the Bank to seek to avoid unnecessary instability in output, interest rates and the exchange rate in the pursuit of price stability, which was introduced in December 1999.

Introduction

1. This paper should be read in the context of the Reserve Bank’s submission to the Review of the Operation of Monetary Policy and is one of a number of background

papers supporting that submission. It summarises the main changes made to the Policy Targets Agreements (PTAs) since the Reserve Bank of New Zealand Act 1989 (1989 Act) was enacted.

2. Attached to the paper is an [appendix](#) summarising in greater detail the main changes made to successive PTAs.

Background

3. Section 9 of the 1989 Act requires the Minister of Finance/Treasurer, in agreement with the Governor of the Reserve Bank, to fix policy targets for the Bank to carry out its primary function of conducting monetary policy to achieve and maintain stability in the general level of prices. The PTA must be agreed between the Minister of Finance/Treasurer and Governor before the appointment or reappointment of the Governor and applies for the term of the Governor. The Act requires the PTA to be tabled in Parliament, and is therefore a public document. It can be changed or replaced at any time by mutual agreement between the Minister of Finance/Treasurer and Governor. Under the Act, the Governor is required to ensure that the actions taken by the Bank in implementing monetary policy are consistent with the policy targets specified in the PTA.
4. The Act empowers the Government to direct the Reserve Bank to conduct monetary policy for a purpose other than price stability. The direction is effected by Order in Council and may apply for a period not exceeding 12 months, although it can be renewed by the promulgation of a further Order in Council. The direction must be tabled in Parliament and publicly disclosed. In giving a direction to the Bank, the Minister is required to set a new PTA for the duration of the Order in Council.
5. The PTA forms an integral part of the New Zealand monetary policy framework. While the 1989 Act sets out the overall objective of monetary policy as being the achievement and maintenance of price stability, the PTA is the mechanism by which this objective is made operational. It should be noted that the Act is silent on the matter of how price stability is to be operationalised. In principle, any number of alternative mechanisms could be specified in the PTA to deliver the price stability outcome, including, for example, nominal GDP targeting, monetary targeting, using the exchange rate as a nominal anchor or having a price level target. From the outset, however, it was decided that the most appropriate mechanism for delivering price stability in New Zealand would be inflation targeting, and this approach has been adopted in every PTA since the Act came into force in early 1990.
6. In effect, the PTA represents a contract between the Minister of Finance/Treasurer and the Governor of the Reserve Bank, and forms a central element of the Bank's mandate and accountability. The Act and PTA framework were created in the context of the public sector reforms made in the mid 1980s, which stressed the importance of specifying clear policy objectives, assigning responsibility and the necessary authority for meeting the objectives, and providing clear lines of accountability. In this context, the monetary policy framework has four key elements.
 - Clear specification of public policy objectives. The overall objective is price stability (as set out in the 1989 Act) and the specific objective is maintaining CPI inflation within the specified target band (as set out in the PTA).

- Clear allocation of responsibility and authority for meeting the objectives. The power to formulate and implement monetary policy is vested in the Governor of the Reserve Bank.
 - Robust transparency arrangements, so that performance can be monitored. This is achieved principally through the Bank's obligation to publish a *Monetary Policy Statement* not less frequently than every six months.
 - Accountability mechanisms to strengthen the incentives for performance. There are a number of mechanisms in place for this purpose. An important one is the Bank's Board of Directors, which has responsibility for monitoring the Governor's performance, effectively as agent for the Minister of Finance/Treasurer. In addition, one of the grounds for removing the Governor from office is where the Minister of Finance/Treasurer is satisfied that the Governor's performance in ensuring that the Bank achieves the inflation target has been inadequate.
7. Changes to the PTA can be initiated by either party. Over the years since 1990, most of the changes to the PTA have been initiated by successive Governments. The changes have occurred either as a result of a change in Government or the reappointment of the Governor. In each case, before agreeing to the proposed changes, both the Treasurer and the Governor must be satisfied that the changes are consistent with the price stability objective (unless the PTA is entered into in the context of the override provision being activated).
 8. It is desirable that PTAs are seen as enduring documents and are not subject to frequent changes. For this reason, we have expressed regret that changes made to PTAs have been as frequent as they have been. However, it is also desirable that the Government of the day shares in the ownership of the monetary policy framework and the price stability objective. In that regard, we have taken the view that there is some merit in a new PTA being entered into upon the formation of a new Government.
 9. The first PTA was signed on 2 March 1990, shortly after the 1989 Act came into force. Since then, the PTA has been changed five times, with the current PTA coming into effect on 16 December 1999. The core features of the PTA have not changed significantly over the last decade. In particular, the inflation targeting concept, the "caveats" to the maintenance of inflation within the target band, and the accountability structures have all remained essentially unchanged. Most of the changes have been relatively minor in nature, although there have been a small number of more significant changes. And there has been some broadening in the tone and reduction in the degree of specificity of the PTA. This reflects a move away from what was probably an excessively precise approach to accountability for staying in the inflation target in the mid 1990s to a situation today where a somewhat less rigid approach is taken to the Bank's accountability for keeping inflation within the target band.
 10. The most important changes have been:
 - in December 1990, when the original PTA requirement to re-negotiate the PTA as a result of a price shock affecting the Bank's ability to achieve the inflation target was replaced with a requirement for the Bank to indicate the effect of the price shock and to set out its approach to bringing inflation back within the target band;

- in December 1990, when the period for achieving the 0 to 2 per cent inflation target was extended by 12 months to the year ended 31 December 1993;
- in December 1996, when the inflation target was widened to 0 to 3 per cent; and
- in December 1999, when a modified clause was included in the PTA to make explicit the requirement that the Bank should seek to avoid unnecessary instability in output, interest rates and the exchange rate in the pursuit of price stability.

Evolution of PTAs – 1990 to 2000

11. As noted above, the first PTA was signed in March 1990 between the then Minister of Finance, the Hon David Caygill, and Dr Brash. It specified the inflation target as 0 to 2 per cent, to be achieved by the year to 31 December 1992. The target was to be measured using the All Groups CPI. However, in recognition that this index included the purchase price of dwellings and credit finance costs, and was therefore an inappropriate measure of inflation for monetary policy purposes, the PTA required the Bank to calculate an alternative measure of inflation. In the initial stages of inflation targeting under the 1989 Act, the alternative measure of inflation, as calculated by the Reserve Bank, was the CPI adjusted for housing costs and finance credit costs (the Housing-Adjusted Price Index, or HAPI).
12. In recognition that one-off price shocks could result in the inflation rate moving outside the target band, and that monetary policy should not seek to offset the immediate price effect of these shocks, the PTA specified a number of “caveats” to the achievement of the 0 to 2 per cent goal. It provided for the PTA to be re-negotiated where achievement of the inflation target was threatened by any of the following events:
 - a divergence of at least 0.5 per cent between the annual CPI inflation rate and the Bank’s alternative measure of inflation (HAPI);
 - a change in GST or other indirect taxes;
 - a significant change in the terms of trade; or
 - any other crisis situation (eg a disease-induced fall in livestock numbers).
13. The enactment of the 1989 Act and introduction of the first PTA did not result in any immediate changes to the focus and implementation of monetary policy in the early 1990s, given that, by mid 1988, the Bank was already directing monetary policy at reducing inflation to the 0 to 2 per cent target. More generally, since 1984, the Bank had been directing monetary policy solely at reducing the inflation rate. The enactment of the 1989 Act and promulgation of the first PTA therefore represented a continuation of the approach to monetary policy that had been evolving in the latter half of the 1980s. However, the Act and PTA sharpened the clarity of monetary policy objectives and provided a stronger basis for promoting public understanding of monetary policy and lowering inflationary expectations. By entrenching price stability as a statutory goal, and encapsulating an inflation target in the PTA, the new framework also reduced the scope for the government or the Bank to surreptitiously back away from the disinflationary process and medium-term goal of price stability.
14. In December 1990, after the election of a new Government, a new PTA was entered into between the Minister of Finance, the Hon Ruth Richardson, and Dr Brash. It simplified the PTA, removing elements of the former PTA that had merely duplicated provisions in the Act, and introduced two main changes from the original PTA.

15. First, it extended by one year the time for achieving the inflation target band, to 31 December 1993, in line with the new Government's election pledge and the Bank's desire to ease the transition costs associated with the disinflationary process (particularly in relation to facilitating adjustment in the real exchange rate). The change was made at a time when the inflation rate was still significantly above the target band and before it had become apparent that inflationary pressures were subsiding more quickly than had earlier been thought likely.
16. Second, it removed the need for the PTA to be re-negotiated in the event of a price shock. This change was initiated by the Bank as a way of simplifying the PTA and reducing the need for potentially frequent future changes to the PTA that might have arisen under the original formulation. Under the new PTA, in the event of a price shock, the Bank was required to explain in the *Monetary Policy Statement* the effect of the price shock on the CPI and on the likely achievement of the target inflation band, and to set out the measures being taken to return inflation to the target band. The price shock events referred to in the PTA were much the same as in the original PTA, although a new one was added to the list – changes in government or local authority levies.
17. In accordance with the original requirement to bring inflation down to the target band of 0 to 2 per cent by December 1992, the Bank had announced in its April 1990 *Monetary Policy Statement* some interim indicative ranges for inflation to ease the transition to price stability. The indicative ranges were 3 to 5 per cent for the year to December 1990 and 1.5 to 3.5 per cent for the year to December 1991. When the time horizon for achieving the 0 to 2 per cent target was extended to December 1993, the Bank announced in February 1991 a somewhat slower track for reducing inflation, with indicative ranges of 2.5 to 4.5 per cent for the year to December 1991 and an indicative range of 1.5 to 3.5 per cent in the year to December 1992. The interim indicative ranges reflected the Bank's desire to achieve a progressive reduction in inflation to the 0 to 2 per cent target band, in the belief that a sharp process of disinflation could impose significant costs on the economy. Publication of the interim indicative ranges also provided additional internal disciplines to assist the Bank in its monetary policy decisions over this period.
18. Given the role of the caveats in the PTA, the Bank began to calculate an inflation measure that came to be known as "underlying inflation", to adjust for the effects of interest rates, housing costs and one-off price shocks. The underlying measure of inflation was released by the Bank each time the quarterly CPI was published by Statistics New Zealand, and the Bank based its monetary policy decisions on the trend in the underlying measure of inflation rather than the so-called headline rate. In the early 1990s, for example, adjustments were made to the CPI to exclude the impact of changes in interest rates and the effect of changes in government charges. In doing this, the Bank demonstrated that it was disregarding the immediate effect on the CPI of these one-off influences, and instead, focusing monetary policy on the medium term trend in inflation – ie on the underlying rate of inflation. However, as became increasingly apparent in later years, the calculation of underlying inflation posed difficulties in determining which items to include or exclude. This sometimes resulted in arbitrary demarcations for determining when items would be included or excluded for the purpose of calculating underlying inflation and tended to result in spurious accuracy. These issues are discussed later in this paper.

19. A new PTA was issued in December 1992, signed by the Hon Ruth Richardson and Dr Brash, when the Minister announced Dr Brash's appointment for a second term. Most of the changes were of a minor, administrative, nature and the basic structure was very similar to the previous PTA. The main change was the replacement of the former requirement to *achieve* inflation within the target band by December 1993, with an obligation to *maintain* inflation within the target band. This reflected the fact that the inflation target had been met by December 1991 and maintained throughout 1992.
20. The new PTA was structured to apply for the remainder of the Governor's first term of office (which was due to expire on 31 August 1993) and for his next term of office.
21. A new PTA was issued in December 1996, replacing the one dated December 1992. The new PTA was initiated as a result of the formation of the National/New Zealand First Coalition Government in December 1996, and was signed by the Rt Hon Bill (now Sir William) Birch, Minister of Finance, on behalf of the Rt Hon Winston Peters (Treasurer-elect), and Dr Brash. The PTA introduced two main changes.
 - First, it widened the inflation target band to 0 to 3 per cent, reflecting the new Government's preference for a somewhat wider inflation target.
 - Second, it modified the statement of the overall monetary policy objective in order to give greater emphasis to the Bank formulating and implementing monetary policy "... with the intention of maintaining a stable general level of prices, *so that monetary policy can make its maximum contribution to sustainable economic growth, employment and development opportunities within the New Zealand economy.*" (New words italicised.)

Both changes were at the initiative of the incoming Government.

22. The widening of the inflation target was acceptable to the Governor because the wider band was seen as still being consistent with the overall price stability objective and because he felt that it would not materially affect the credibility of the monetary policy framework or adversely affect inflation expectations (which, by the mid 1990s, had become more strongly anchored). Although the widening of the band did not result in any significant change to the Bank's approach to monetary policy, it did enable a somewhat greater degree of variability in the inflation rate and therefore assisted in reducing the constraints associated with the narrower inflation band.
23. The new wording in the PTA, explicitly linking monetary policy with economic growth, employment and development, reflected the new Government's desire for a clearer and more visible statement that price stability is the best contribution that monetary policy can make to economic growth and employment, and not simply an end in itself.
24. The new wording linking monetary policy to broader economic objectives presented no difficulty for the Bank, given that the Bank had, from the time that the 1989 Act was enacted, espoused the view that, over the long haul, monetary policy can most effectively contribute to broader economic objectives, such as encouraging economic growth, by focusing on maintaining price stability. Consistent with the arguments run in numerous speeches and publications from the Bank, the new wording in the PTA emphasised this linkage more explicitly than in earlier PTAs and did not imply a broader set of objectives for monetary policy.

25. A new PTA was issued in December 1997, signed by the Treasurer, the Rt Hon Winston Peters, and Dr Brash on Dr Brash's re-appointment for a third term. The PTA was drafted to apply for the remainder of the Governor's term of office (scheduled to expire on 31 August 1998) and for his next term of office (commencing on 1 September 1998 and due to expire on 31 August 2003).
26. Although the fundamental features of the preceding PTA were not materially altered, the new PTA introduced quite a substantial number of generally minor changes. In some respects, the new PTA was drafted in broader language and a somewhat softer, less prescriptive tone than its predecessors. The changes included the following.
- It specified that the 0 to 3 per cent inflation target would be measured using the CPIX measure of inflation (the new CPI measure excluding credit services, issued by Statistics New Zealand). As discussed below, the adoption of CPIX as the official measure of inflation for PTA purposes enabled the Bank to discontinue publication of the underlying measure of inflation.
 - The PTA dropped the previous wording requiring the Bank to be "... fully accountable for its handling of the price effects [of supply shocks] and, in particular, for any movements outside the 0 to 3 per cent band", and replaced it with a somewhat more generalised statement of the Bank's accountability: "The Bank shall constantly and diligently strive to meet the policy target established by this agreement" and "The Bank shall be fully accountable for its judgements and actions in implementing monetary policy".
 - It also introduced a somewhat more open form of wording on the nature of the possible price shocks, with a stronger suggestion that the examples of shocks specified are illustrative rather than exhaustive.
27. The introduction of CPIX as the official measure of inflation for PTA purposes helped the Bank abandon the calculation of an underlying measure of inflation, given that most of the difference between headline inflation and underlying inflation was usually the result of changes in interest rates. The decision to discontinue publication of an underlying measure of inflation also reflected the difficulties associated with calculating underlying inflation – difficulties that had become more apparent as the decade progressed. In particular, the calculation and publication of an underlying measure of inflation was seen as problematic for a number of reasons.
- From the outset, the Bank was concerned that, despite its efforts to make the calculation of the underlying inflation rate objective and transparent, some commentators might cast doubt on the credibility of the calculation. In particular, we were aware of the potential for an argument to be made that the Bank might manipulate the calculation of the underlying rate of inflation and thereby impede the government's and market's ability to assess the Bank's performance in meeting the inflation target.
 - At times, the Bank faced considerable difficulty in accurately determining the impact of a price shock on the CPI. For example, there were difficulties in differentiating between the effect on the CPI of a price shock that was purely a result of something of a one-off nature (such as an increase in international oil prices or a change in government policy directly affecting the prices of domestic goods or services) and the effect of underlying inflationary pressures. This sometimes led to calculations of

spurious accuracy and had the potential to undermine the credibility of the Bank's calculations of underlying inflation. That said, no credible commentator did accuse the Bank of manipulating the underlying inflation calculations.

- The calculation of the underlying inflation rate was subject to a number of difficult judgements, not least being a determination of what events would constitute “significant” price shocks. (Successive PTAs referred to the need for the Bank to disregard the immediate effect of “significant” price shocks, but, understandably, did not provide guidance on what might constitute “significant” for this purpose.) In order to provide a degree of objectivity to the determination of what might constitute a significant price shock, the Bank adopted some “rules” for determining which items would be included and which would be excluded from the calculation of underlying inflation. These rules were necessarily arbitrary and at times resulted in some odd inclusions in, and exclusions from, the measure of underlying inflation.
 - The close attention paid to the underlying inflation rate, and the intensive efforts made to determine an appropriate measure of underlying inflation, occupied considerable time on the part of senior Bank staff. At times, the decisions as to which items should be included in, and which excluded from, the calculation of underlying inflation had the potential to distract the Bank from looking at the broader picture.
28. Eventually, the Bank concluded that these difficulties outweighed the benefits of calculating and publishing an underlying measure of inflation. The regular publication by Statistics New Zealand of CPIX provided the opportunity to discontinue the publication of underlying inflation. However, this did not alter the Bank's approach to monetary policy. In particular, the Bank continued to disregard the immediate effect of temporary price shocks, such as those referenced in the PTA, and focused monetary policy on keeping inflation within the 0 to 3 per cent band over the medium term, even although there would be times when measured inflation would fall outside the band. Although *Monetary Policy Statements* from 1998 onwards did not include references to underlying inflation (other than in reference to earlier periods), the Bank was still obliged to explain inflation outcomes where these fell outside the target band. Accordingly, where appropriate, the Bank's *Monetary Policy Statements* included estimates of price shock effects on the CPIX measure of inflation.
29. The current PTA was signed in December 1999 between the Hon Michael Cullen, Treasurer, and Dr Brash, upon the formation of the new Labour/Alliance Government. The new PTA replaced the previous one, but retained most of the structure and wording, with two main changes.
- The modification of clause 4(c), stating that: “*In pursuing its price stability objective, the Bank shall implement monetary policy in a sustainable, consistent and transparent manner and shall seek to avoid unnecessary instability in output, interest rates and the exchange rate.*” (New wording is highlighted in italics.)
 - It specified that the 0 to 3 per cent inflation target should be measured by the All Groups CPI (and not the CPIX), reflecting the fact that Statistics New Zealand calculated the standard CPI in a manner that excluded section prices and interest costs from the September quarter 1999.
30. The modified clause 4(c) was made at the initiative of the incoming Government and reflected its desire to ensure that the maintenance of price stability did not create an

excessive degree of variability in economic growth, employment, interest rates or the exchange rate.

31. We have viewed the modification of clause 4(c) as largely confirming the approach that the Bank has taken to monetary policy since the inception of formalised inflation targeting. Over that period, the Bank has been mindful of the short term effects that monetary policy can have on the real economy, exchange rates and interest rates. In that regard, throughout the last 10 years of formalised inflation targeting, the Bank has adopted a number of measures in an attempt to avoid unnecessary instability in output and financial market prices. These issues are discussed in the paper dealing with clause 4(c) – [*“Inflation targeting in principle and in practice”*](#).

Appendix

Principal features of, and changes to, successive Policy Targets Agreements

This appendix sets out the main features and changes made to successive Policy Targets Agreements (PTAs) since the first PTA was signed on 2 March 1990.

There have been six PTAs (including the current one) since the Reserve Bank of New Zealand Act came into force on 1 February 1990. The PTAs were as follows:

- PTA dated 2 March 1990, between the Hon David Caygill (Minister of Finance) and Dr Brash;
- PTA dated 19 December 1990, between the Hon Ruth Richardson (Minister of Finance) and Dr Brash;
- PTA dated 16 December 1992, between the Hon Ruth Richardson (Minister of Finance) and Dr Brash;
- PTA dated 10 December 1996, between the Rt Hon William Birch (Minister of Finance, on behalf of the Rt Hon Winston Peters, Treasurer-elect) and Dr Brash;
- PTA dated 15 December 1997, between the Rt Hon Winston Peters (Treasurer) and Dr Brash; and
- PTA dated 16 December 1999, between the Hon Michael Cullen (Treasurer) and Dr Brash.

The principal features of, and changes to, each PTA are summarised below.

PTA dated 2 March 1990

Key features were as follows.

- The PTA specified the 0 to 2 per cent inflation target (measured using the CPI), to be achieved by the year ending 31 December 1992 and then maintained thereafter.
- The PTA required the Bank to monitor price movements using a range of price indices.
- In recognition of the deficiencies in the CPI as a measure for inflation target purposes (such as the inclusion of the purchase price of dwellings and mortgage finance costs), the PTA required the Bank to calculate an alternative measure of inflation so as to enable an assessment to be made of the impact of investment-related housing costs on the CPI. It stated that the Reserve Bank's measure of CPI inflation would calculate housing costs based on imputed house rentals.
- The PTA would cease to have effect if a section 12 Order in Council was promulgated, and a new PTA would be issued within 30 days of the Order coming into force.
- The inflation target could be re-negotiated on the occurrence of any of the following events.

- The Governor could choose to re-negotiate the PTA if there was likely to be a divergence of at least 0.5 per cent between the annual CPI inflation rate and the Bank's measure of inflation in 1992 or 1993.
 - Any change in GST or other indirect taxes would trigger a re-negotiation of the inflation target if the change was expected to materially affect inflation rates in 1992 or 1993. (Direct effects of the tax changes would be accommodated, but there would be no accommodation of second round effects.) A new PTA would be set within 30 days of advice on the inflation effects of the change being given to the Minister.
 - A significant change in the terms of trade would require a re-negotiation of the PTA if the change was likely to have a significant impact on the inflation rate in 1992 or 1993. A new PTA would be set within 30 days of advice of the inflation effects of a change in the terms of trade being given to the Minister.
 - Any other crisis situation would trigger a new PTA if it could be expected to have a significant effect on inflation.
- The PTA required the Bank to take into account the effects of its actions on the efficiency and soundness of the financial system and to advise the Minister where the Bank believed its actions might have a material effect on the financial system (in which case the PTA might be re-negotiated).
 - It required the Bank to consult with any party where the actions of that party might have an adverse effect on the achievement of the inflation target, might increase the economic or social costs of achieving the inflation target, or might prejudice the soundness or efficiency of the financial system.
 - If the institutional structure of the financial sector changed in such a way as to hinder the Bank's ability to implement monetary policy, the Bank was required to advise the Minister and the PTA might be subject to re-negotiation.

PTA dated 19 December 1990

This PTA replaced the preceding one and introduced several substantial changes. The main changes were:

- an extension of the time horizon for achieving 0 to 2 per cent CPI inflation to the year ending 31 December 1993;
- removal of the need to re-negotiate the PTA in the event of any of the caveated shocks occurring, but with an explanation required in the *MPS*;
- simplification of the PTA (eg removal of unnecessary duplication of provisions in the Act); and
- specification of a new price shock event, being changes in government or local authority levies.

The key features of the PTA were that:

- it specified the inflation target as 0 to 2 per cent inflation on a CPI basis, to be achieved by the year ending 31 December 1993;
- it required the Bank to monitor inflation using a range of price indices;

- it required the Bank to publish each quarter its housing-adjusted CPI (HAPI);
- it noted that the Bank would generally react to changes in relative prices (induced by external shocks, government policy changes or a natural crisis) in a manner that prevented general inflationary pressures from emerging;
- the principal shocks were identified as significant changes in the terms of trade, a change in GST or other indirect tax rates, a crisis such as a natural disaster or disease-induced fall in livestock numbers, a significant price level impact arising from changes to government or local authority levies, or a significant divergence between CPI and HAPI inflation rates;
- the PTA required the Bank to be accountable for its handling of the price effects of these shocks. It required the Bank to publish in the *MPS* its estimate of any such shock and its impact on the inflation target, and detail the measures being taken by the Bank to ensure that the inflation effects of the shock were temporary;
- it required the Bank to inform the Minister if changes in policy instruments available to the Bank were likely to impede the effective conduct of monetary policy (in which case a new PTA could be renegotiated);
- it required the Bank to implement monetary policy in a sustainable, consistent and transparent manner; and
- it required each *MPS* to contain a statement of how the Bank proposed to formulate and implement monetary policy and required it to contain a projected path for inflation (for the years until the inflation target was achieved).

PTA dated 16 December 1992

This PTA replaced the preceding one, but was very closely modelled on it, with few significant changes.

- The PTA was signed on the re-appointment of the Governor, so that the PTA would apply for the remainder of the existing term (due to expire on 31 August 1993) and for the term commencing on 1 September 1993.
- It contained a wording change to reflect the fact that the 0 to 2 per cent target had been achieved (and hence, it focused on maintaining price stability within the target band).
- The requirement for the Bank to publish the HAPI was removed.
- The caveat referring to differences between the CPI and HAPI inflation rates was replaced with one that referred to a movement in interest rates that causes a significant divergence between the change in the CPI and the change in the CPI excluding the interest costs component.

PTA dated 10 December 1996

This replaced the preceding PTA, was closely modelled on it, but introduced two significant changes.

- The inflation target was widened to 0 to 3 per cent.

- The overall objective of price stability was embellished with the following wording “... the Bank shall formulate and implement monetary policy with the intention of maintaining a stable general level of prices, *so that monetary policy can make its maximum contribution to sustainable economic growth, employment and development opportunities within the New Zealand economy*”. (New wording in italics.)

No changes were made to the caveats or to other features of the PTA.

PTA dated 15 December 1997

This replaced the preceding PTA with the following main changes.

- It was worded so as to apply for the remainder of the Governor’s then existing term of office (due to expire on 31 August 1998) and the next term (due to commence on 1 September 1998), being signed at the time of the Governor’s re-appointment.
- It specified that the inflation target of 0 to 3 per cent would be measured by the CPI excluding credit services (CPIX).
- It made provision for the Treasurer and Governor to use an alternative index of consumer price inflation following the implementation of the changes to the calculation of consumer prices proposed by the Government Statistician to take effect during 1999.
- It contained different wording in relation to caveated shocks. Wording changes of note in this PTA are set out below.
 - It noted that a range of events could have a significant temporary effect on inflation and could “... mask the underlying trend in prices which is the proper focus of monetary policy”. (This wording was somewhat different from that in earlier PTAs and more specifically drew attention to the focus of monetary policy being on the underlying trend in prices - ie more explicitly suggesting that the Reserve Bank should “look through” temporary price shocks.)
 - It noted that price shocks could include exceptional movements in international commodity prices, changes in indirect taxes, significant government policy changes that directly affect prices, or a natural disaster. The wording was somewhat more suggestive than in previous PTAs that the list of examples was not exhaustive – ie the examples cited were merely illustrative.
- It contained modified wording on accountability: “The Bank shall constantly and diligently strive to meet the policy target established by this agreement.” and “The Bank shall be fully accountable for its judgements and actions in implementing monetary policy.”
- It dropped the earlier wording requiring the Bank to be “... fully accountable for its handling of the price effects [of economic shocks], and, in particular, for any movements outside the 0 to 3 per cent band”. And it introduced some modified wording: “It is acknowledged that, on occasions, there will be inflation outcomes outside the target range.” It retained wording to require the Bank to explain any breach of the target band and to explain the actions to be taken to bring inflation back within the band.

- It dropped the clause in earlier PTAs relating to the scope to re-negotiate the PTA in the event that the Bank formed the view that changes in the availability of monetary policy instruments might impede the conduct of monetary policy.

PTA dated 16 December 1999

This replaced the preceding PTA. The wording and format of the preceding PTA were largely retained, but two main modifications were made.

- It introduced a new clause (clause 4(c)): *“In pursuing its price stability objective, the Bank shall implement monetary policy in a sustainable, consistent and transparent manner and shall seek to avoid unnecessary instability in output, interest rates and the exchange rate.* The new wording is marked in italics.
- The 0 to 3 per cent inflation target was specified in terms of the All Groups CPI (not CPIX), to reflect the new structure of the CPI as calculated by Statistics New Zealand. It noted that, until the June quarter 2000, 12 monthly increases in the CPI would be calculated by comparing the new CPI series with the old CPI series, adjusted by removing the impact of changes in interest rates and section prices.