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Reserve Bank: Money printing didn't cause inflation to soar; \$11 billion cost to the Crown was offset by benefits

**Jenée Tibshraeny**

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The Reserve Bank is pouring cold water on the narrative its Covid-era money printing programme caused sky-high inflation and ended up costing the Government billions of dollars.

The bank has published new research that concludes its controversial \$55 billion Large-Scale Asset Purchase (LSAP) programme didn't "meaningfully" contribute to above-target inflation after the pandemic.

The Reserve Bank's modelling suggests the annual inflation rate would only have been about 0.5 percentage points lower in 2020/21 had it not embarked on its LSAP programme. In the years after, the inflation rate would've been the same as it was.

Speaking to the *Herald*, Reserve Bank chief economist Paul Conway said the conclusion largely stemmed from the fact the programme lowered longer-term interest rates.

The main effect of this was it kept the New Zealand dollar low. This made New Zealand exports relatively attractive on the world stage and boosted the economy.

Official Cash Rate (OCR) cuts also boosted the economy – but in a different way.

They influenced shorter-term interest rates, which had a more direct bearing on retail rates. With households and businesses spending less on interest, they were able to spend more elsewhere in the economy, lifting economic demand.

Conway said it was difficult to isolate the impact of a single tool the Monetary Policy Committee used at a time the Reserve Bank and Government were throwing a lot at the economy to keep it buoyed.

He also recognised the collective response caused prices to soar.

However, he cautioned against people assuming money printing was largely to blame for the economy overheating.

Conway said the Reserve Bank preferred using the OCR to keep prices stable, as LSAP programmes could be costly.

The Covid-era programme is estimated to have directly cost the Crown nearly \$11b.

This is basically because the New Zealand Government Bonds the bank created money to buy in 2020 and 2021 plummeted in value once interest rates rose. The bank is crystallising its losses as it sells the bonds it bought, and is receiving regular indemnity payments from Treasury to keep its books in the black.

The Reserve Bank has always argued losses to the Crown were well worth it, as the LSAP programme helped stimulate the economy, which enabled the Government to receive more tax revenue than would otherwise have been the case. It also lowered the Government's interest costs.

The Reserve Bank's latest modelling put some numbers to this assertion. It found the direct financial benefit of the LSAP programme to the Crown broadly offset the \$11b cost.

Defending the programme in 2022, Reserve Bank Governor at the time Adrian Orr said the benefits were worth "a multiple" of the direct costs.

While the Reserve Bank didn't use such strong language in its latest research, Conway said it was hard to quantify the benefits that stemmed from the programme soothing dysfunction in the bond market at the onset of the pandemic.

Investors were initially panicked by the amount of debt the Government was issuing to pay for its response. The Reserve Bank's intervention in the bond market calmed their jitters and helped the lower OCR flow through the economy.

The Reserve Bank's research is topical, as the United States' Treasury Secretary Scott Bessent this month took aim at the Federal Reserve for printing money, otherwise known as quantitative easing.

Bessent accused the central bank (whose experience with LSAPs predates Covid) of "mission creep" and said it should have a simpler toolkit.

Looking ahead, Conway said LSAP programmes could again be used if the market was dysfunctional, there was a major crisis, or the OCR had reached its effective lower bound (this could be at a level below zero as, unlike in 2020, banks are now able to operationalise a negative OCR).

"While the OCR is our preferred tool, we need to keep LSAPs in the toolbox for use in targeted interventions," he said.

The Reserve Bank noted its balance sheet didn't expand by as much as that of many of its peers, which also bought assets to stimulate their economies in response to the pandemic.

However, it noted the Government spent much more (relative to the size of the economy) than other governments.

Conway said it was important for the Government and Reserve Bank to work alongside each other, while maintaining their independence, during crises.

"This means sharing perspectives on the crisis in real time, understanding each other's policy reaction functions and the likely economic impacts of different stabilisation policies. Crucially, working alongside each other does not mean joint decision-making," he said.

The Reserve Bank's research built on a [major review](#) of its monetary policymaking it completed in 2022.

Its new research didn't delve into the widely criticised Funding for Lending Programme, which it also used in response to the pandemic.

This programme involved the Reserve Bank creating \$19b and lending it to banks at the OCR.

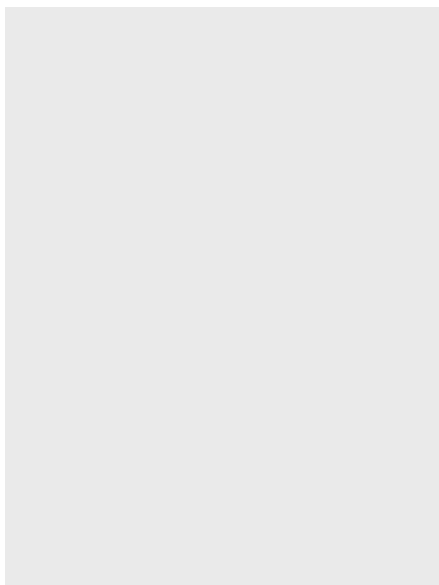
The Reserve Bank estimates its Funding for Lending and LSAP programmes were equivalent to it cutting the OCR by 90 basis points.

Jenée Tibshraeny is the *Herald's* Wellington Business Editor, based in the Parliamentary press gallery. She specialises in government and Reserve Bank policymaking, economics and banking.

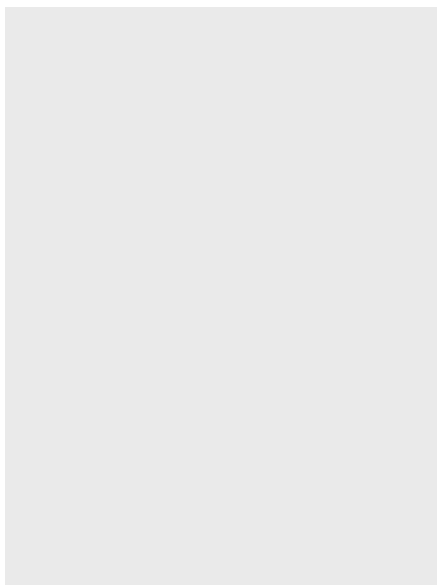
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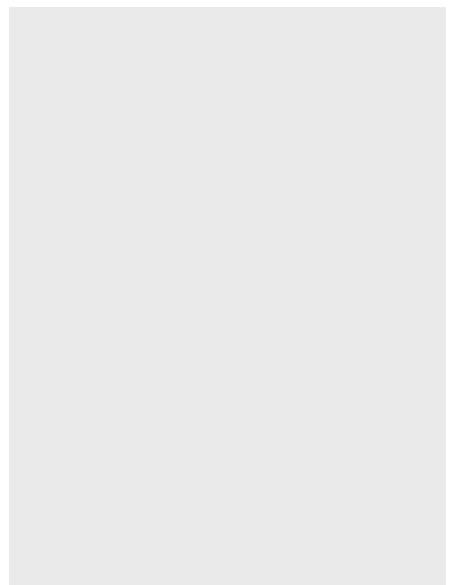
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