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focus

Interest Rates Cut Again

The Reserve Bank of New Zealand (RBNZ) has delivered another 50 bps interest rate cut, bringing the Official Cash Rate (OCR) down to 3.75%. This latest reduction is part of an ongoing effort to revive economic activity amid softening inflation and sluggish growth. Further cuts are expected, with the OCR likely to finish the year closer to 3%, impacting businesses, investors, and everyday savers.

FORSYTH BARR

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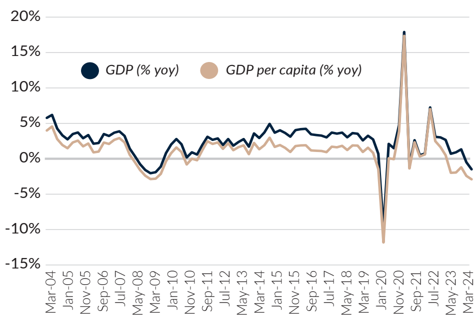
Room to move

New Zealand is experiencing one of its worst economic downturns since the 1990s, with a prolonged slump, creating tough conditions for households and businesses. This has been partly due to high interest rates, which were necessary to combat post-pandemic inflation pressure.

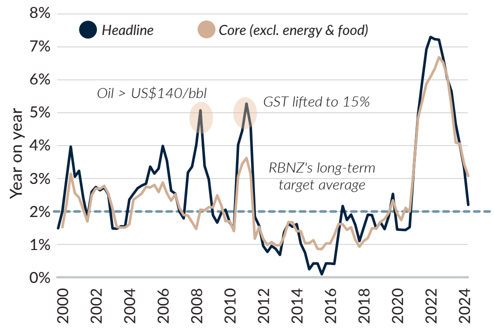
NEW ZEALAND GDP AND GDP PER CAPITA (% YOY)



Source: StatisticsNZ, Forsyth Barr analysis

The RBNZ's primary mandate is to manage inflation, not economic growth. With inflation—the rate at which prices rise—finally under control, the RBNZ is cutting interest rates swiftly to encourage borrowing and spending. Additional rate cuts, likely in 25 bp increments, are anticipated over the coming months. The RBNZ's latest forecast suggests the OCR will bottom out at around 3% to 3.25% by the end of 2025, accelerating its previously projected timeline.

NEW ZEALAND INFLATION (% YOY)



Source: StatisticsNZ, Forsyth Barr analysis

However, challenges remain. The New Zealand dollar has weakened over the past three months, and oil prices have risen—both of which could drive up costs for imported goods in the coming months. Despite these risks, the RBNZ expects these pressures to be temporary and remains confident that inflation will stabilise around 2% over the next few years.

The central bank is also cautiously optimistic about the outlook for economic growth. While some early indicators suggest improving business activity, there is yet to be a convincing upward trend. The first half of 2025 is likely to remain a muddle-through period for the economy, with recovery slow and tepid. Conditions should start to improve as we head into the second half of 2025.

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A small island nation

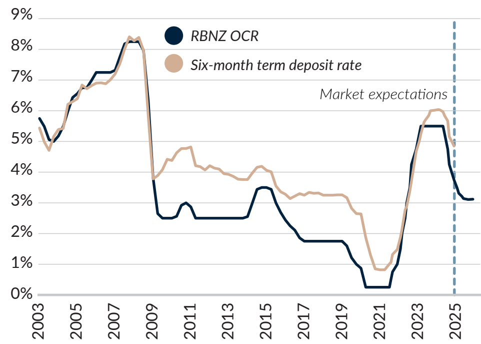
New Zealand's economy is heavily influenced by global events. While global growth is slowing, New Zealand's major exports have performed well over the past year, providing some support to the domestic economy. As a result, regional areas have been more resilient than major urban centres. However, increasing global trade tensions—particularly those driven by US President Trump's tariff policies—pose a risk to international trade and New Zealand's export sector.

China remains New Zealand's largest trading partner, but its economy is struggling with weak demand and ongoing issues in the property market. A further slowdown in China, particularly if exacerbated by a trade war with the US, could negatively impact New Zealand's exports and broader business environment. The US is now New Zealand's second-largest export market. While the country is unlikely to be a major focus for Trump, broad-based tariffs could still harm New Zealand's trade prospects.

Double-edged sword

After a couple of years of elevated interest rates, the RBNZ's rate cuts will provide much-needed relief for borrowers and should help stimulate economic activity. However, savers and fixed-income investors may need to adjust their strategies in a lower-rate environment to ensure they continue meeting their financial goals.

RBNZ OCR AND SIX-MONTH TERM DEPOSIT RATE



Source: RBNZ, Forsyth Barr analysis

What's next for NZ Inc.?

While the RBNZ has outlined a plan for further rate cuts, uncertainties remain. If economic conditions deteriorate, the bank may need to cut rates more aggressively. Additionally, global trade issues—such as new tariffs or economic instability in key markets—could create further challenges.

Conversely, although inflation appears to be under control, unexpected price surges could force the RBNZ to adjust its approach. Ultimately, how the economy responds in the coming year will determine the central bank's next moves.

If at any time you want to discuss investment options and opportunities, your Forsyth Barr Investment Adviser is available to provide you advice and assistance.

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