

# New Zealand Economic Watch

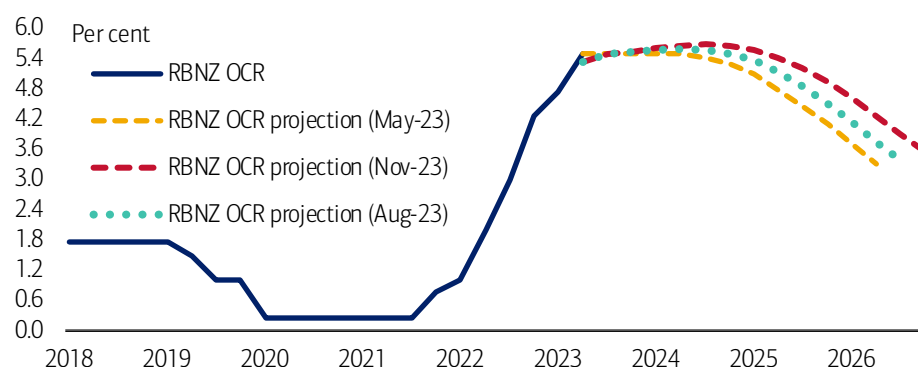
## RBNZ review: hawks emerge again

### The RBNZ keeps rates unchanged at 5.5%

The RBNZ kept the official cash rate (OCR) unchanged at 5.5% as widely expected. However, guidance, including changes to the bank's forecasts and the OCR track, were more hawkish than we had anticipated (Exhibit 1). While the Bank is confident that high rates are restricting spending and reducing inflation, the progress is slower than expected. In their view, "inflation remains too high and inflationary pressures continue to emerge". The OCR track now reflects even higher rates than in August, but economic data has continued to slow to reflect traction from restrictive policy.

#### Exhibit 1: OCR track moves higher

To strengthen hawkish guidance



Source: RBNZ

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### We still think cuts are likely

The RBNZ discussed the possibility of the need for further tightening but concluded that interest rates are already restrictive, and it is appropriate to wait for further economic data to "observe the speed and extent of easing in capacity pressures in the economy". The RBNZ believes impact from hikes on CPI is most evident around eight quarters after the tightening cycle. Notably, while the Bank has upgraded its estimation of neutral rate to 2.5% from 2.25%, policy is still restrictive, in their view. We think there are several downside risks ahead for New Zealand (see: [New Zealand Economic Watch: RBNZ preview: Last hold of 2023, cuts next? 27 November 2023](#)). The labour market is clearly weaker, and interest rate-exposed sectors of the economy are showing traction from policy.

### Strategy: Fade the sell-off in AUDNZD

The double whammy of weaker-than-expected Australian CPI and a hawkish RBNZ have supported a move down in AUDNZD. The AUD is trading more than 90 pips cheaper vs NZD on the day and now looks attractive on a strategic basis. Our economist expects the policy-rate differential between the RBA and RBNZ to tighten from +115bps to -60bps. We like to pay 2y AU swaps vs NZ but we prefer to express this view in FX by going long AUDNZD. Risk: weaker data in Australia or further RBNZ rate increases.

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## Risks are tilted to the downside

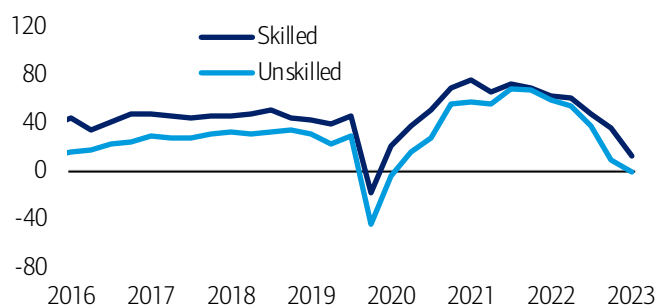
Population growth has eased supply constraints, but its effects on aggregate demand mean the economy was stronger than the RBNZ expected in the first half of 2023. This is now reflected in upgrades to the Bank's forecasts for growth (Exhibit 6). A more resilient economy means inflation could move back to target at a lower pace than previously expected. We think the RBNZ is on track to meet target in mid-2024.

Leading indicators suggest the outlook for employment is fading, with job advertisements falling to below pre-COVID-19 levels and employers reporting less difficulty finding labour (Exhibit 2). The underutilisation rate and unemployment rate both increased in the September 2023 quarter (Exhibit 3) and inflation expectations declined, but longer-term measures are steady (Exhibit 5).

The RBNZ also highlighted the new government's spending plans as an upside risk to aggregate demand. While total government spending as a share of potential GDP is still forecast to decline, the RBNZ now expects a material increase in government investment over the medium term, linked to infrastructure requirements.

### Exhibit 2: Difficulty in finding labour

Labour supply has eased significantly

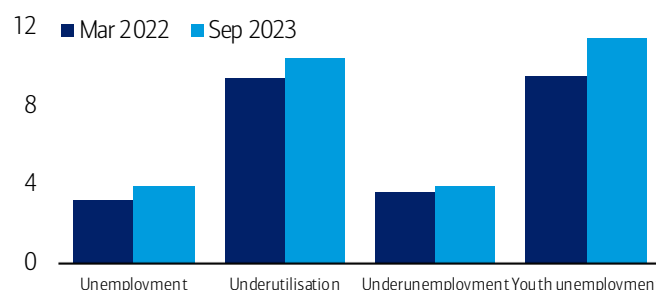


Source: QSO, RBNZ

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### Exhibit 3: Broader unemployment rises

Reflecting traction from tighter policy

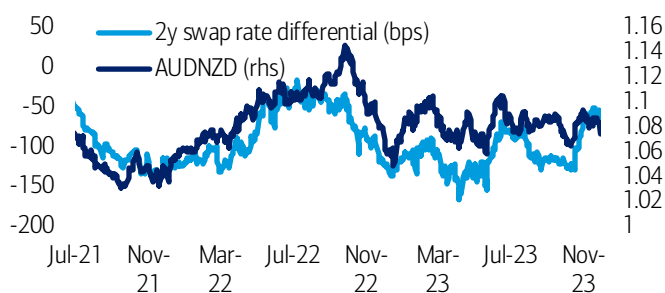


Source: StatsNZ

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### Exhibit 4: AUDNZD closely correlated with rate differentials

We recommend fading the cheapening of AUDNZD

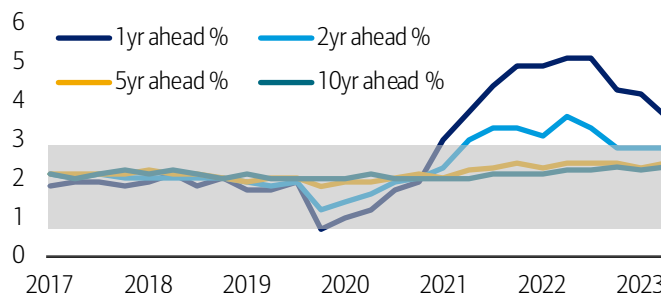


Source: BofA Global Research, Bloomberg

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### Exhibit 5: Business inflation expectations

Long-term measures rise slightly



Source: RBNZ

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### Exhibit 6: Changes to RBNZ's forecasts

November vs August

	Jun-23	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26	Dec-26
GDP (production, %yoy)	1.8	1.1	0.8	1.6	2.3	3.1	3.3	3.0
Aug-23 MPS	1.2	0.0	0.2	1.6	2.4	3.1	3.1	
CPI (%yoy)	6.0	5.0	3.7	2.5	2.2	2.0	2.0	2.0
Aug-23 MPS	6.0	5.2	3.9	2.4	2.2	2.0	2.0	
Unemployment Rate (%)	3.6	4.2	4.9	5.1	5.2	5.0	4.9	4.8
Aug-23 MPS	3.6	4.4	5.1	5.3	5.3	5.1	5.0	
Official Cash Rate	5.50	5.50	5.67	5.66	5.42	4.95	4.25	3.55
Aug-23 MPS	5.33	5.54	5.59	5.50	5.12	4.51	3.76	

Source: RBNZ

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