

New Zealand Fixed Income Monthly January 2025

Interest rates seen dropping further amid weak activity and external uncertainty

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Activity continues to struggle amid weak consumer spending

Although the arrival of a new year has brought some optimism after a tough 2024, economic activity continues to flounder in New Zealand. Official data released in December 2024¹ showed that the country's GDP declined by 1.0% on-quarter in the September 2024 quarter. Furthermore, separate official data released in November 2024² showed that seasonally adjusted retail sales were down 0.1% on-quarter in the same period, suggesting that consumers remain reluctant to spend. Given that figures released by the Reserve Bank of New Zealand (RBNZ) in January³ showed that the amount of new residential mortgage lending with floating interest rates surged to New Zealand Dollar (NZD) 3.579 billion in November 2024 (almost half of that month's total of NZD 7.556 billion), many mortgage holders may be waiting for future cuts to the Official Cash Rate (OCR). In turn, companies may refrain from increasing expenditure until they can expect to see satisfactory returns from their investments. We feel that a rebound in consumer confidence will be needed for a substantial turnaround in business investment.

Downward trajectory in interest rates seen continuing

When the RBNZ reduced the OCR by 50 basis points to its current level of 4.25% in November 2024, it mentioned the possibility of a further cut early in 2025. The RBNZ's next interest rate decision is due on 19 February, and many market observers expect to see a reduction comparable to the one seen in November. Paul Conway, the RBNZ's Chief Economist, commented in a speech in January⁴ that the central bank estimates New Zealand's long-term neutral interest rate (the level that neither stimulates nor restrains the economy) at between 2.5% and 3.5%. Considering this, there still appears to be a long way for the OCR to fall from its current level. At the same time, we believe that further rate cuts are likely to become smaller as the easing cycle moves towards its end point. There may also be pauses in the cycle along the way. In our view, this highlights the need to continue monitoring how the economic data develop.

Trump's second administration among key uncertainties in 2025

There is also significant amount of global uncertainty that analysts may not have factored into their forecasts at this stage. The key example is Donald Trump's second administration in the US. Furthermore, although the US economy is widely expected to achieve a soft landing, the risk of a turnaround remains. China's current economic weakness is also a factor to consider in 2025.

¹ <https://www.stats.govt.nz/information-releases/gross-domestic-product-september-2024-quarter/>

² <https://www.stats.govt.nz/information-releases/retail-trade-survey-september-2024-quarter/>

³ <https://www.rbnz.govt.nz/statistics/series/lending-and-monetary/new-lending-fully-secured-by-residential-mortgage>

⁴ <https://www.rbnz.govt.nz/hub/news/2025/01/beyond-the-cycle>

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