



WEEKLY ECONOMIC COMMENTARY



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RBNZ creeping towards hikes

It was a big week for policy announcements in the New Zealand economy. On the monetary policy front, the RBNZ kept the OCR on hold at its latest policy meeting, but signalled rate hikes over the coming months. We continue to expect the first hike in September, but a July start could be on the cards depending on the evolution of data. In terms of fiscal policy, the latest Budget included only modest spending increases as the Government tries to ensure its financial position remains on a sustainable path.

Monetary policy tightrope.

As expected, **the RBNZ held the OCR at 2.25%** at its May policy meeting, but it was a close decision. The RBNZ is weighing up how to respond to the complex combination of a sharp oil-related lift in inflation with related downside risks for economic activity. It's not a simple trade-off, and there are genuine uncertainties about how the longer-term inflation outlook will shape up.

Highlighting just how tight that balancing act is, the decision went to a vote with members of the RBNZ's Monetary Policy Committee split down the middle. The three external members of the Committee all voted for a hike, noting that earlier interest rate increases could limit the upside risk for inflation expectations and potentially limit the extent that rates need to rise over the longer term.

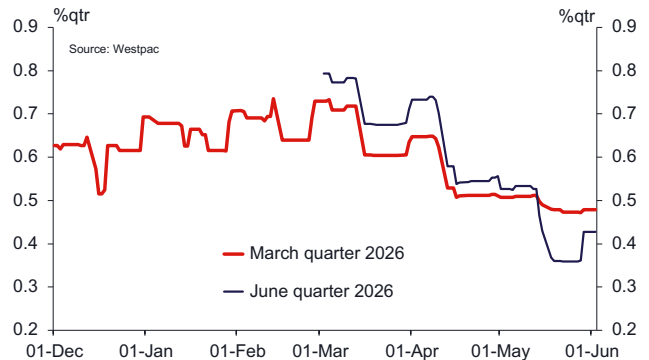
In contrast, all three internal members of the Committee including the Governor voted for a hold. These members highlighted uncertainty around how the inflation outlook was shaping up given the downside risks for activity, along with related questions about the pass through to longer-term wage and price setting behaviour.

In such circumstances, the Governor has the tie-breaking vote, and that saw the OCR left on hold in May.

Key views

	Last 3 months	Next 3 months	Next year
Global economy	→	↘	→
NZ economy	↗	↘	↗
Inflation	→	↑	↗
2 year swap	↑	→	↗
10 year swap	↗	→	↗
NZD/USD	→	→	↗
NZD/AUD	↘	→	↗

Westpac GDP nowcasts

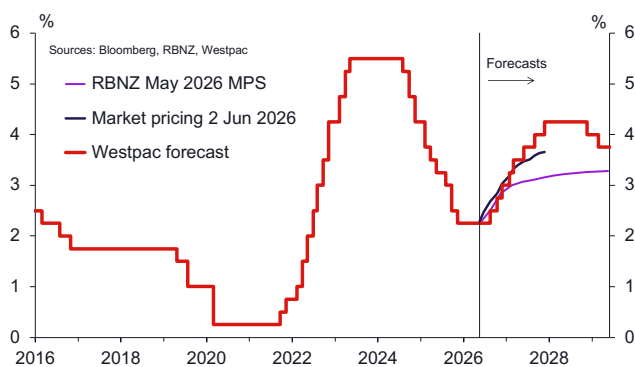


Key data and event outlook

Date	Event
4 Jun 26	Govt accounts for 10 months to April
16 Jun 26	NZ Selected price indexes, May
16 Jun 26	RBA Monetary Policy Decision
17 Jun 26	FOMC meeting (18 Jun NZT)
18 Jun 26	NZ GDP, March quarter
2 Jul 26	Govt accounts for 11 months to May
8 Jul 26	RBNZ OCR Review
14 Jul 26	NZIER QSBO Survey, June quarter
17 Jul 26	NZ Selected price indexes, June
21 Jul 26	NZ CPI, June quarter

But while the OCR was left on hold at the latest meeting, all Committee members agreed that it will likely need to rise over the coming months. That was reflected in the updated OCR profile, with the end of 2026 projection revised up to 2.84% (from 2.38% in the February projections). That's broadly consistent with three rate hikes by the end of this year. The RBNZ also signalled the chance of further rate hikes next year.

Official Cash Rate forecasts



The big question is when OCR increases are likely to begin. We continue to expect 25bp rate hikes in September, October and December. However, an earlier start to the hiking cycle in July is a real possibility, with financial markets almost fully pricing a hike at that time.

Comments from those MPC members who voted for a hold in May have highlighted that the timing of interest rate hikes will be highly dependent on economic conditions over the coming weeks. The RBNZ will be watching economic data closely for signs of pressure on wages and inflation expectations. On this front, the latest confidence surveys for May (released after the RBNZ's meeting) showed modest increases in both household and business confidence after they fell sharply in recent months. At the same time, gauges of inflation expectations and pricing intentions have moderated, but remain at firm levels. Gauges of expected wage growth have also dropped back, and they remain subdued.

Looking to the next few weeks, there will be further updates on confidence and some activity updates, like card spending. However, we won't get meaningful information on inflation and inflation expectations, GDP or wages until just before the September meeting.

To help fill the data void, the RBNZ is also making use of feedback from businesses. Our own talks with businesses in recent weeks have highlighted widespread cost pressures. However, conditions are mixed across the economy. Rural-linked regions and industries are outperforming. In contrast, businesses chasing the discretionary dollar are doing it tough, and that's limiting their pricing power. On the labour front, slack in the jobs market continues to provide a brake on wage growth even as cost of living pressures mount.

The other key factor is the progress of the war and oil prices. This is a fluid situation, and the RBNZ has noted that even when the geopolitical situation improves, any easing in oil and inflation could be gradual. Nonetheless, developments on this front could be an important consideration on both sides of the debate. We certainly see the risk of protracted disruptions stemming from the conflict.

A further consideration is the potential appointment of a new MPC member, expected in June. The successful candidate may come from outside the RBNZ but will become an internal MPC staff member.

Putting this all together, there's a clear case for the OCR to rise over the coming months. Inflation is set to rise to well over 4% this year. That follows an extended period when prices have been rising rapidly. As a result, there is a clear risk of a damaging creep higher in inflation expectations which could extend the lift in inflation beyond the current oil price shock.

However, it's not clear that evidence of such 'second round' inflation pressures will be evident by July. Furthermore, we suspect that some of the RBNZ's concerns about the downside risks for activity will be borne out. As a result, we continue to expect rate hikes will begin in September, but it's a close call between the July and September meetings.

Moving closer to the promised land of fiscal balance.

The other big news last week was the release of **Budget 2026**. This was a relatively austere Budget for an election year. While we did see increased spending in areas like health, transport and education, those increases were relatively modest. Looking ahead, as announced prior to the Budget, the operating allowance for new operating spending in the coming fiscal year has been set at a very tight \$2.1bn a year (albeit up from an even skinnier \$1.3bn in Budget 2025).

Given the deterioration in the near-term economic outlook, the Treasury forecasts an OBEGALx deficit of \$11.4bn (2.4% of GDP) in 2026/27, compared to the \$10.4bn deficit forecast in the HYEFU.

Further ahead, however, a set of relatively 'tax-rich' economic forecasts and restrained spending growth drive a faster improvement in the operating balance compared to the Treasury's previous HYEFU forecasts. Notably, the OBEGALx is projected to return to a surplus of \$2.6bn (0.5% of GDP) in 2028/29, a year earlier than in the HYEFU projections (and a year earlier than we thought). The traditional OBEGAL measure (which doesn't exclude ACC costs) returns to surplus a year later.

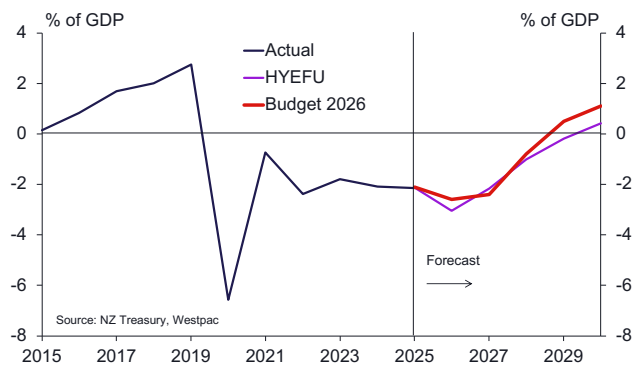
The Budget forecasts of core Crown revenue are higher across every year compared to the HYEFU, reflecting a higher level of nominal GDP and hence a larger tax base in

dollar terms. These revenue forecasts were broadly in line with what we expected.

The robust nominal growth outlook means that the Treasury sees a relatively “revenue rich” outlook from 2028 onwards. This has allowed the Government to bring forward by one year when they anticipate a OBEGALx surplus, with correspondingly lower borrowing requirements. The forecast bond programme in 2026/27 is unchanged and reduced by \$2 billion a year in 2027/28 onwards.

While the Treasury is expecting an improving outlook for the Government’s books, we see a number of risks to this outlook. On expenditure, there will naturally be pressure to spend more in areas like health and aged care. Similarly, we see some downside risk to the Treasury’s forecast for GDP growth, especially given the likelihood that interest rates rise faster than they have assumed.

Operating balance (OBEGALx), % of GDP

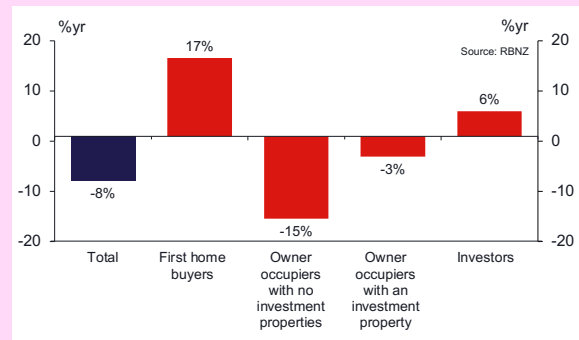


Satish Ranchhod, Senior Economist

Chart of the week.

While house sales are back around average levels, under the surface there have been some notable changes in the make-up of buyers. **Lending to first-home buyers** is up 17% on pre-pandemic levels as buyers have taken advantage of low interest rates and access to low-deposit finance to get their first foot on the ladder. The large number of properties for sale and limited price growth have also made the market more accessible. Investors are also back in the market. However, as we’ve previously discussed, investors now are much more focused on longer-term rental yields, rather than the pursuit of large capital gains that previously characterised the housing New Zealand market. In contrast, lending to existing owner occupiers (i.e. ‘movers,’ who make up the largest share of the property market) remains well down on pre-pandemic levels. In part, that’s because of the sharp price falls in 2022/23 and limited growth more recently. That’s meant that it’s taking longer for owner-occupiers to build their capital, so they’re waiting longer before looking to move.

Housing lending compared to Dec 2019 (pre-pandemic)

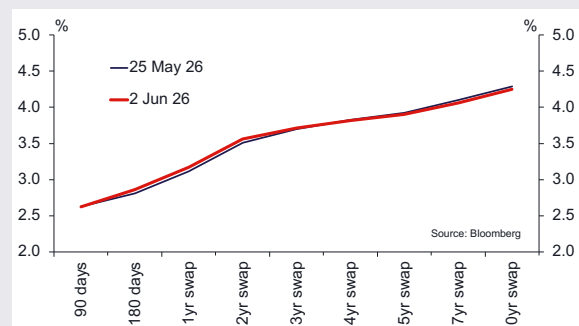


Fixed versus floating for mortgages.

The RBNZ’s May Monetary Policy Statement indicated that the Official Cash Rate is likely to be hiked several times through the latter part of the year. We’re expecting 25bp hikes at the RBNZ’s September, October and December meetings, with the OCR expected to continue rising next year. With the May decision so finely balanced, there is a high chance that the first hike will come at the July meeting, and interest rate markets are priced accordingly.

Fixed-term mortgage rates between two and five years now lie above 5%, but fixing for one of these longer periods still appears attractive as it would insulate borrowers from a trend higher in the OCR over the next couple of years.

NZ interest rates



Global wrap

Middle East.

Last week was again characterised by seemingly gradual progress towards a ceasefire agreement, with conflicting statements as to how close the other side was to making a deal and what had been agreed to. Reports indicate that the deal on the table includes a full resumption of shipping through the Strait of Hormuz within a month; the intent is to allow supply of energy and other goods to resume, alleviating stress on the Iranian and global economy, while negotiations continue over Tehran's nuclear program. President Trump has delayed on agreeing to the deal, and Israel's renewed incursions into Lebanon seem to have been a sticking point for Iran. Crude oil prices ended last week at their lowest level since mid-April, though they picked up again overnight.

Australia.

The April CPI came in slightly below market forecasts, up 0.4% for the month and 4.2% for the year. Volatile, policy-driven components related to travel drove the outcome – the Federal Government's temporary halving of fuel excise and some state governments offering free public transport, while cancelled flights and refunds for holiday travel provided a partial offset. These dynamics were also the main factors behind the 1.1% decline in household spending in April. The passthrough of higher fuel costs has not unfolded as rapidly as we initially feared, but the risk of a larger and faster passthrough in coming months is material.

The highlight for this week will be March quarter GDP on Wednesday. As we **detail in our preview**, we expect a 0.5% increase, slowing from 0.8% in the December quarter. Partial data released last week pointed to strong growth in business investment, particularly for data centres, though some of this will likely 'leak out' again in the form of higher imports.

US.

Consumer-related data was notably soft last week. The second estimate for US GDP was revised down from 2.0% annualised to 1.6%, in large part due to weaker consumption growth. Further, real personal consumption rose just 0.1% in April as wage growth failed to keep pace with inflation. Housing is also clearly under pressure, with S&P/Cotality house prices falling for a second consecutive month (-0.2%, +0.8%/yr), and new home sales down 6.2% in April. The most important release for the week ahead will be the May employment reports, with the market expecting another solid rise in nonfarm payrolls on top of a 155k rise in April. The services ISM for May will also be of interest, following the robust result for the manufacturing ISM, up from 52.7 to 54.0.

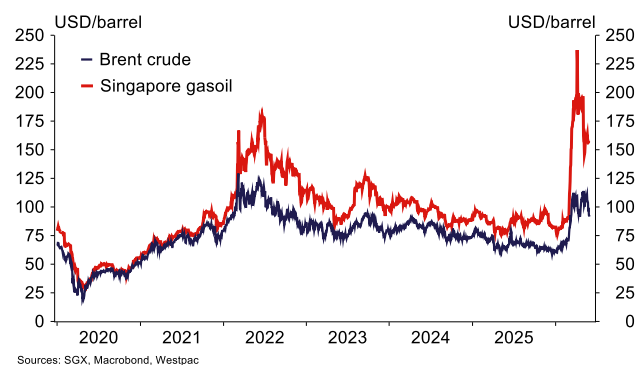
Trading partner real GDP (calendar years)

	Annual average % change			
	2024	2025	2026	2027
Australia	1.0	2.0	1.8	1.2
China	5.0	5.0	4.7	4.6
United States	2.8	2.1	2.0	1.8
Japan	-0.2	1.2	0.6	0.8
East Asia ex China	4.5	4.7	4.3	4.2
India	7.1	7.6	6.5	6.7
Euro Zone	0.9	1.5	0.7	1.1
United Kingdom	1.1	1.4	0.8	1.1
NZ trading partners	3.0	3.2	2.8	2.7
World	3.4	3.4	3.2	3.3

Australian & US interest rate outlook

	29 May	Jun-26	Dec-26	Dec-27
Australia				
Cash	4.35	4.35	4.85	4.85
90 Day BBSW	4.46	4.55	4.90	4.80
3 Year Swap	4.47	4.75	4.70	4.40
3 Year Bond	4.47	4.75	4.70	4.40
10 Year Bond	4.83	5.00	5.05	4.95
10 Year Spread to US (bps)	39	65	60	30
US				
Fed Funds	3.625	3.625	3.625	3.625
US 10 Year Bond	4.44	4.35	4.45	4.65

World oil prices



Australian GDP growth



Financial markets wrap

Foreign exchange.

NZD/USD broke higher last week, following the hawkish RBNZ MPS, reaching 0.5994 – a three-week high. There is potential for this level to be retested during the weeks ahead, and should it break, we would target 0.6050.

The RBNZ MPS gave markets a worthy distraction from the Iran war. It kept the OCR on hold but raised its OCR forecast by more than markets had expected. The US-Iran war also delivered positive news for the NZD, that at least the two sides were negotiating a ceasefire.

This week, there's no major local data or economic event to ruffle the market. In the US, we have monthly payrolls to watch – another solid outturn would be US dollar supportive.

For the quarter ahead, we retain a neutral bias, pending resolution of the Iran war. An escalation would likely cause a break below 0.5700, towards 0.5500, while a positive resolution would likely ignite a rally towards the 0.6100 area.

NZD/AUD broke higher last week following the RBNZ MPS as well as a slightly AU soft CPI update. This bounce could reach 0.8400 during the next few weeks, helped by yield spreads which have been slowly rising in the NZD's favour (the RBA's hiking cycle is maturing, while the RBNZ's has yet to start). Further ahead, though, for H2 we retain a bearish bias, based on expected relative economic performance which should continue to favour the AUD. Australia is likely more resilient than NZ to a prolonged war and oil shock.

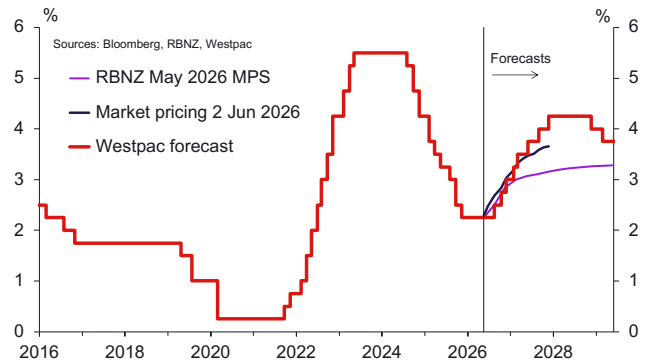
Interest rates.

The NZ 2yr swap rate is expected to remain capped at 3.70% during the weeks ahead. While the RBNZ MPS last week delivered a hawkish surprise for markets, and swap rates did rise in response, offshore yields have been falling as the US-Iran war is expected to de-escalate.

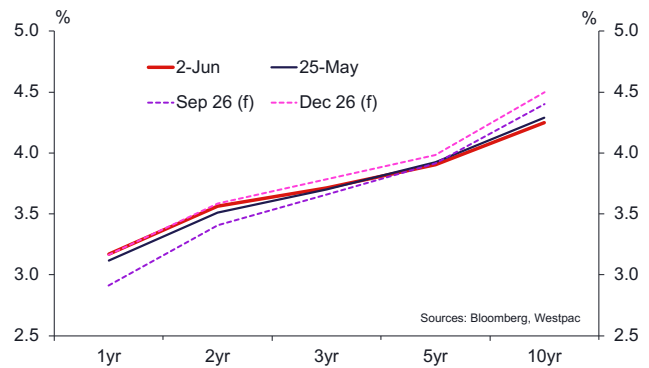
Market pricing for OCR hikes implies 90% chance of a hike in July, with three hikes in total priced by year end – similar to our forecast of hikes in September, October and December.

The yield curve's flattening trend since the peak in late December has resumed following the RBNZ MPS, the 2-10yr swap at 69bp, down from the cycle high of 120bp in December. We expect further flattening during the year ahead as we approach the RBNZ's tightening cycle, the 2-10yr swap potentially to 50bp.

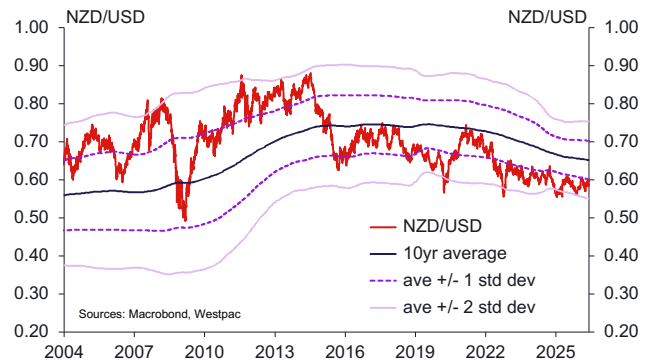
Official Cash Rate forecasts



Swap rates



NZD/USD vs rolling 10yr average



FX recent developments

	Historical data				F'cast
	Spot	3mth range	5yr range	5yr avg	Dec-26
USD	0.595	0.569-0.597	0.553-0.728	0.618	0.62
AUD	0.831	0.816-0.843	0.816-0.971	0.912	0.85
EUR	0.511	0.493-0.511	0.484-0.637	0.561	0.52
GBP	0.443	0.430-0.444	0.426-0.531	0.481	0.45
JPY	94.8	91.0-94.8	74.7-98.6	86.4	95.5

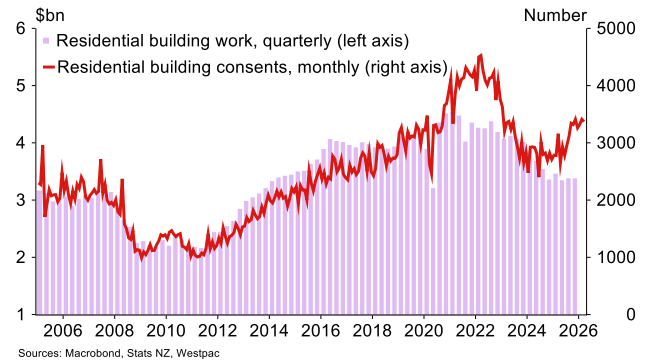
The week ahead

Apr Building Consents

Jun 3, Last: -1.3%, Westpac f/c: -5%

We're forecasting a modest 5% dip in building consents in April. That's related to an expected easing in apartment consents after they took a step higher last month (apartment consents tend to be issued in batches and can be lumpy on a month-to-month basis). Looking at the longer-term trend, residential consent issuance has taken a step higher over the past year. That's encouraging news for the building sector. However, the softening economic outlook and increased economic uncertainty cast doubt on how long that firmness will be sustained. Those headwinds are also expected to be a drag on the amount of non-residential work that's planned.

Residential building and consent numbers



Q1 Building Work Put in Place

Jun 4, Last: -3.1%, Westpac f/c: 1.0%

We're expecting a flattening off in building activity in the March quarter. However, trends remain mixed across sectors. Residential construction has found a base over the past year, and with an uptick in the number of new projects being consented, we expect a moderate 1.5% gain in the March quarter. There's more uncertainty around non-residential building, which has been trending lower for several years now in response to softness in economic conditions and ongoing economic uncertainty. After last quarter's sharp 5% drop, we've assumed a modest 0.5% bounce. Nevertheless, the trend remains downwards.

Real building work put in place

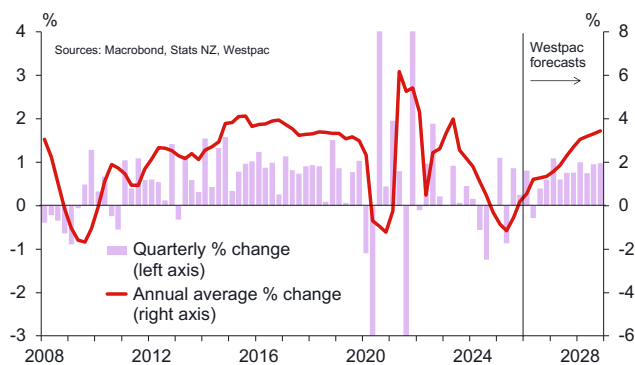


Economic and financial forecasts

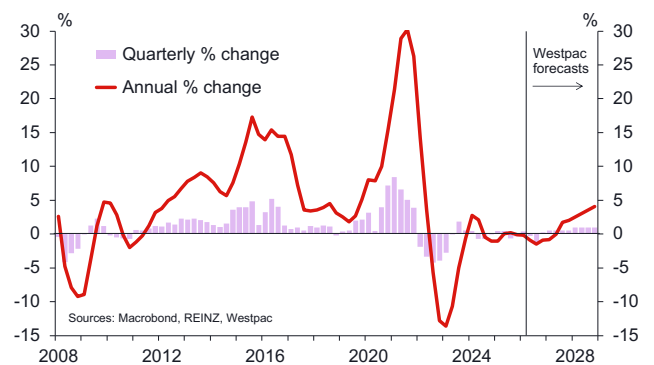
Economic indicators	Quarterly % change				Annual % change			
	Dec-25	Mar-26	Jun-26	Sep-26	2024	2025	2026	2027
GDP (production)	0.2	0.8	-0.3	0.4	-1.6	1.3	1.5	3.2
Consumer price index	0.6	0.9	1.8	1.2	2.2	3.1	4.4	1.6
Employment change	0.5	0.1	0.1	0.1	-1.3	0.2	0.6	2.9
Unemployment rate	5.4	5.3	5.4	5.5	5.1	5.4	5.6	4.9
Labour cost index (all sectors)	0.4	0.5	0.6	0.7	3.3	2.0	2.5	2.3
Current account balance (% of GDP)	-3.7	-3.8	-4.0	-4.1	-4.7	-3.7	-4.1	-4.2
Terms of trade	0.3	-1.9	0.6	2.6	8.9	3.5	1.0	3.3
House price index	-0.4	0.4	-0.3	-1.3	-1.0	-0.1	-0.9	2.0

Financial forecasts	End of quarter				End of year			
	Dec-25	Mar-26	Jun-26	Sep-26	2024	2025	2026	2027
OCR	2.25	2.25	2.25	2.50	4.25	2.25	3.00	4.25
90 day bank bill	2.52	2.51	2.50	2.95	4.45	2.52	3.40	4.45
2 year swap	2.71	3.12	3.75	4.05	3.64	2.71	4.30	4.35
5 year swap	3.27	3.71	4.10	4.30	3.73	3.27	4.35	4.45
10 year bond	4.27	4.54	4.85	4.95	4.50	4.27	5.00	5.10
TWI	66.4	67.2	66.5	66.2	69.5	66.4	69.1	72.7
NZD/USD	0.57	0.59	0.59	0.59	0.59	0.57	0.62	0.67
NZD/AUD	0.87	0.85	0.82	0.82	0.91	0.87	0.85	0.91
NZD/EUR	0.49	0.50	0.50	0.50	0.55	0.49	0.52	0.55
NZD/GBP	0.43	0.44	0.44	0.43	0.46	0.43	0.45	0.48

GDP growth



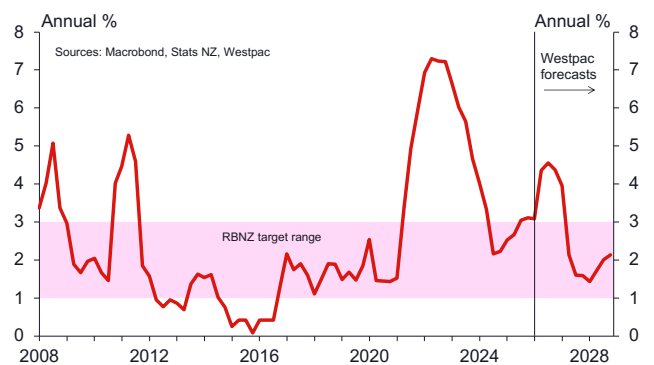
House prices



Unemployment and wage growth



Consumer price inflation



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Tue 02					
Aus	RBA Board Member Speech	-	-	-	Ian Harper speaking at CEDA.
	Q1 Current Account Balance, \$bn	-21.1	-23.5	-24.8	Falling goods trade balance will drive an increase in deficit.
	Q1 Net Exports Contribution, ppt	-0.1	-0.6	-0.6	A surge in data processing equipment imports.
	Q1 Company Profits, %qtr	5.8	0	0.5	Mining profits expected to fall on the back of weaker exports.
	Q1 Inventories, %qtr	-0.1	0.1	-0.1	Imports and demand balance suggest a rundown.
	Apr Dwelling Approvals, %mth	-10.5	-1.5	-1.5	Residual noise around high rise approvals.
Eur	May HICP Inflation, %ann	3	3.3	-	Will be closely watched by the ECB as a June hike is debated.
UK	BoE Speak	-	-	-	Governor Bailey appearing before House of Lords.
US	Apr JOLTS Job Openings, 000s	6866	6890	-	Has seen minor falls in recent months, though remains stable.
	Fedspeak	-	-	-	FOMC members Kashkari and Hammack scheduled to speak.
Wed 03					
NZ	Q1 Terms Of Trade, index	3.7	-1.0	-3.5	Weaker dairy prices in late 2025 flowing through.
	Apr Building Permits, %mth	-1.3	-	-5.0	Trend still firm for now, but expected to soften.
Aus	Q1 GDP, %qtr	0.8	0.5	0.5	The big story in Q1 Accounts will be data centres.
Chn	May RatingDog Services PMI, index	52.6	52.2	-	Competitiveness concerns driving providers to reduce charges.
Eur	Apr PPI, %ann	2.1	-	-	Saw a sharp increase post the US-Iran conflict.
US	Apr Factory Orders, %mth	1.5	4.3	-	Recent strength driven by capital goods.
	May ISM Services, index	53.6	53.7	-	Has cooled in recent months while remaining elevated.
	Jun Federal Reserve's Beige Book	-	-	-	Update on economic conditions across the regions.
World	May S&P Global Services PMI, index	-	-	-	Final estimate for Japan, Europe, UK and US.
Thu 04					
NZ	Q1 Volume of Building Work, %qtr	-3.1	1.5	1.0	Res stabilising. Non-res weak but could see a small bounce.
	May ANZ Commodity Prices, %mth	-0.8	-	0.5	Aluminium up strongly, other prices mixed.
Aus	Apr Goods Trade Balance, \$bn	-1.8	1.6	2.6	Return back to a surplus expected.
	RBA Governor Bullock	-	-	-	Senate testimony with Assist' Governor Kent.
Eur	Apr Retail Sales, %mth	-0.1	-	-	Remains low with consumer confidence having taken a hit.
US	Initial Jobless Claims	215	-	-	Have been relatively stable.
	Fedspeak	-	-	-	FOMC member Daly.
Fri 05					
Aus	RBA Deputy Governor Hauser	-	-	-	Fireside chat at Sky News Economic Summit.
Jpn	Apr Household Spending, %ann	-2.9	-	-	Consumption remains weak despite continued wages growth.
Eur	Q1 GDP, %qtr	0.1	0.1	-	Final estimate.
US	May Nonfarm Payrolls, 000s	115	93	85	Growth likely to continue at a solid pace.
	May Average Hourly Earnings, %mth	0.2	0.3	-	Inflation likely to challenge any real earning growth.
	May Unemployment Rate, %	4.3	4.3	4.3	Has remained stable, although masked by falling participation.

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