WEEKLY ECONOMIC COMMENTARY

10 Aug 2026 | **Westpac Economics Team** | **westpac.co.nz/economics** | economics@westpac.co.nz

Plenty of slack in the labour market

The economy appears to have weathered the Iran war fairly well but has not emerged totally unscathed. Labour market data last week confirms significant excess capacity remains, which is helping to restrain inflation pressures. Nevertheless, inflation remains too high and wage pressures appear sticky, raising questions on how easy it will be to bring inflation back to 2%. The RBNZ will likely need to do more than they currently say to achieve that. Markets seem to agree with that assessment even though the sequencing of OCR hikes beyond September seems murky.

It's been a rough few months for the economy. A recovery in economic activity had taken hold from the September quarter of 2025 and delivered three above-trend quarters (averaged) until the Iran war stepped in and interrupted progress. The war saw a reduction in consumer and business sentiment, as well as consumer spending, along with increased volatility. Heightened uncertainty associated with the energy supply situation reasonably saw consumers and businesses retreat into their shells while the shooting was going on.

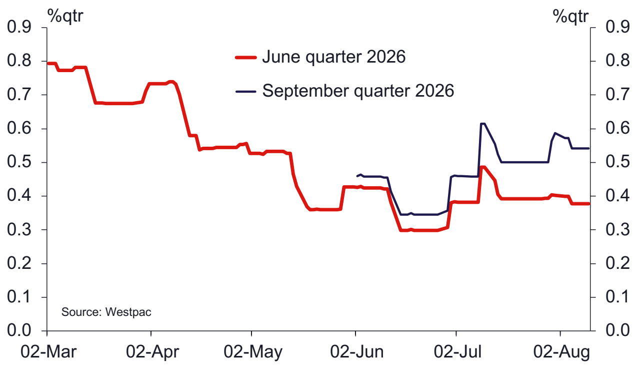
We can now see that GDP Nowcasts and high-frequency activity indicators are consistent with a flat to negative June quarter growth outcome. Nevertheless, this is a better performance than was feared early in the war when the risks of very high fuel costs and potential supply disruptions were in prospect. Early indicators for September quarter growth look noticeably stronger than the June quarter and suggest a return to growth.

Whether that September quarter growth is above trend remains to be seen. Uncertainty remains high as we go into the sixth month of the Iran war. The Strait of Hormuz remains effectively closed and the entry of the Yemen Houthis into the fray is interrupting alternative Red Sea

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

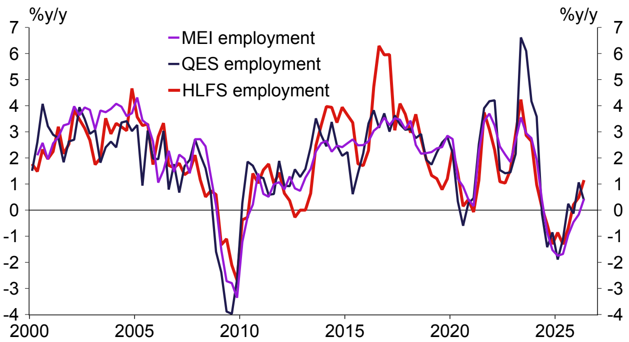
Date	Event
11 Aug 26	RBA Monetary Policy Decision
17 Aug 26	NZ Selected price indexes, July
2 Sep 26	RBNZ OCR Review & Monetary Policy Statement
16 Sep 26	FOMC meeting (17 Sep NZT)
17 Sep 26	NZ GDP, June quarter
18 Sep 26	NZ Selected price indexes, August
29 Sep 26	NZ Govt Pre-election Economic & Fiscal Update
29 Sep 26	RBA Monetary Policy Decision
6 Oct 26	NZIER QSBO Survey, September quarter
8 Oct 26 (tbc)	Pre-Election Economic & Fiscal Update

supply routes. Deals are purportedly on the table, but at the time of writing the shooting continues and oil prices are moving up into the mid US $80s again.

Recent strength in consumer and business confidence seems fragile and its sustainability will be heavily dependent on whether some kind of Middle East stability can be found. And as noted, prospects there remain very murky. The Government announced last week an extension to the fuel relief package that was initially implemented in March to assist lower income households. Technically, the threshold to withdraw the scheme had been met. But rising fuel costs and high uncertainty meant it was pragmatic for the government to maintain the support for now.

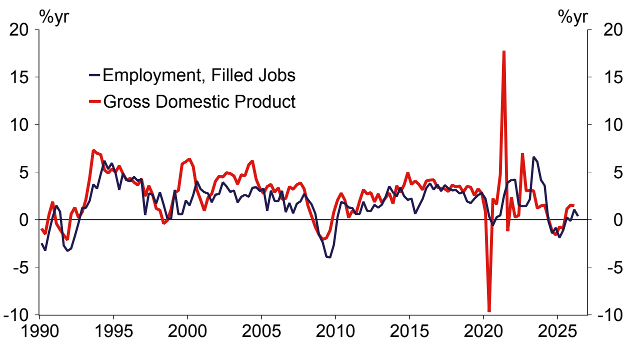
Last week's data confirmed that significant slack remains in the labour market. The key signal came from the unemployment rate which rose more than expected to a new cycle high of 5.6%. The RBNZ will likely put the most weight on this observation when determining how much downward pressure excess capacity is exerting on inflation at its still very elevated level.

NZ employment measures



Sources: Macrobond, Stats NZ, Westpac

NZ annual GDP growth versus filled jobs growth

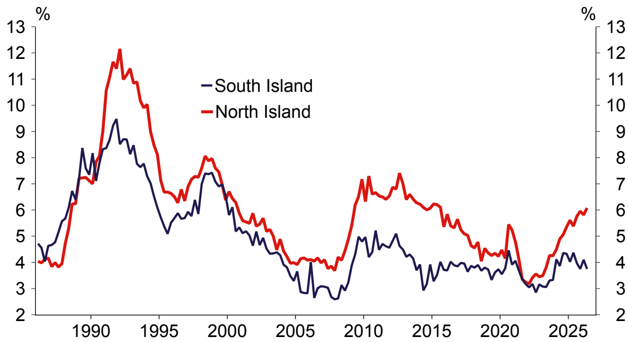


Sources: Macrobond, Stats NZ, Westpac

Interestingly though, the details of the labour market report were messy, and not uniformly consistent with a weak economy view. The official measure of household employment growth and labour force participation surpassed expectations – albeit possibly exaggerated by survey sample error given what we see in other employment measures – continuing a trend seen for a few quarters now. At face value, slack was created through a rise in labour supply that stronger than expected labour demand could not overcome. That's not fundamentally a weak economic story. Employment growth is firmly positive in a 0.4-1.2% y/y range which is consistent with the lift in GDP growth seen since the middle of last year.

We see significant diversity in labour market performance around the country. The South Island, which is more heavily driven by the strong agricultural and tourism sectors, saw a falling unemployment rate which is close to the 10-year average. At the same time the more heavily service-sector dominated North Island urban centres were weak and unemployment is almost 2 standard deviations above the 10-year average. Population growth trends likely reflect these divergent performances.

Unemployment rate – North vs South Island, s.a.



Sources: Macrobond, Stats NZ, Westpac

Interestingly, wage growth slightly surpassed expectations and looks sticky at 3.1% on an unadjusted Labour Cost Index (LCI) basis. The headline productivity-adjusted LCI growth rate of 2% – less than half of its pandemic peak – is consistent with achieving 2% inflation over the medium term, but as yet labour market slack seems not to have led to sub-2% wage growth. This raises questions on the future direction of wage growth given elevated inflation expectations and reduced labour market slack as the economy further recovers. Firms report a rising proportion of wage demands that reflect cost of living pressures. This tells us the public has noticed elevated inflation and sees it as sufficiently persistent to warrant including in the wage bargaining process. This could be a headwind for the RBNZ to overcome if it hopes to return inflation to 2% in any reasonable timeframe.

Last week the RBNZ Governor commented to the press on policy and the economy. She understandably reiterated her goal of returning inflation to 2%. However, the strategy to achieve this is unclear as the policy strategy at this point is limited to "taking away a little bit of the stimulus". The RBNZ's forecasts are for the OCR to return to their view of long-term neutral levels as opposed to restrictive levels. Hence, it's unclear how this strategy will push core inflation down from the current

2.5-3% level to 2% as the economy recovers. Disinflation may or may not happen within a reasonable timeframe and could easily be knocked off course by future inflation shocks (for example El Niño driven food price risks).

In all likelihood, more work will be required in time. Historically this has been the behaviour of the RBNZ. Early in the cycle, forecasts often indicate a modest tightening cycle that is scaled up as the cycle progresses. Hence, we remain comfortable with the idea the OCR reaches 4% sometime in 2027.

In the immediate period though, the observation of increased labour market slack asks questions of the cadence of OCR increases to end 2026. A tightening in September remains a strong possibility as we currently forecast. The elevated headline inflation outlook also strongly points to a September OCR increase. However, the case for an October hike remains unclear given the unemployment rate has lifted by more than the RBNZ forecast in May. The MPC can reach an end year OCR of 3% without an October move. We really don't have enough clarity on the MPC's strategy to be sure how meetings beyond September will progress.

There has been a shift away from providing forward guidance in central banks globally. Both the US and Australian central bank governors have shied away from such guidance recently. It's important though for the policy reaction function and strategy to be clear. Doubts have emerged in the US recently about the Federal Reserve's reaction function and strategy to return inflation to 2%. These doubts have impacted on long-term interest rates and some measures of policy credibility. We think it will be important that the RBNZ doesn't also slip into the same trap. Hence at some point the RBNZ should clarify how exactly inflation will be returned to target. Hope is not a strategy, but raising the OCR to restrictive levels is a credible approach. The RBNZ will need ultimately to move away from the "removing stimulus" line and be upfront on the path ahead for the OCR through 2027. Perhaps we will hear more in the September Monetary Policy Statement.

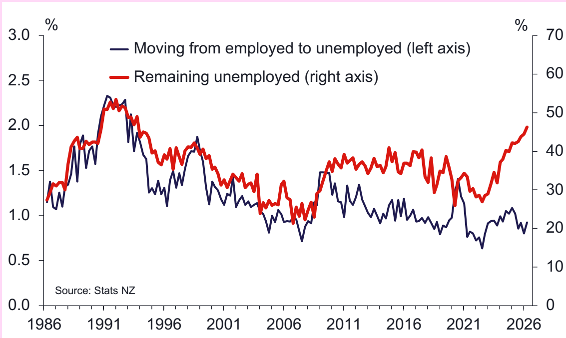
Lastly, the election campaign period is now upon us, and the race looks very close. While for much of the year the polls have pointed to a right-leaning coalition being returned to power with NZ First being the kingmaker, the situation is now changing. The Opportunity Party is gaining ground and increasingly looks likely to breach the key 5% threshold. These developments have shifted the calculus and made a left-leaning coalition more likely and has positioned Opportunity as the deciding factor. Hence political uncertainty in on the rise and the future policy mix is in flux. Watch this space!

Kelly Eckhold, Chief Economist

Chart of the week.

The June quarter HLFS showed that the jobs market remains a 'low-fire, low-hire' environment. As the economy slowed through 2024-25, businesses looked to hold on to workers to the extent that they could, wary of the severe skill shortages that had emerged in previous years. This potentially dampened the peak in the unemployment rate through the downturn. The flipside, however, is that businesses are not returning to hiring again in the way that they might otherwise as the economy picks up steam again. The result is that for those who find themselves out of work, it's been increasingly difficult to get back in. This has been even more challenging for school leavers looking to break into the workforce for the first time.

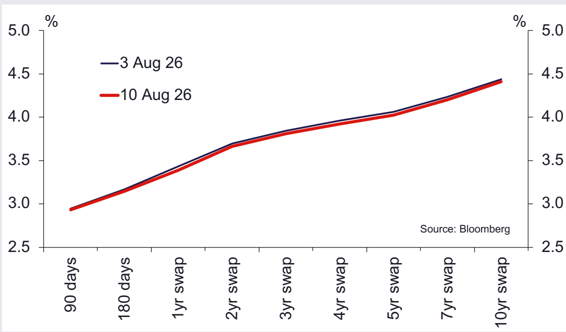
Labour force transition rates



Fixed versus floating for mortgages.

The RBNZ lifted the OCR to 2.5% at its July meeting and signalled the likelihood of further rate hikes over the coming months (dependent on the strength of economic data). We're expecting 25bp hikes at the RBNZ's September and December meetings, with the OCR expected to continue rising next year. 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 conflict.

Brent crude traded around US$79 to $84/bbl last week. A deal between Iran and Oman allowing for the opening of the Strait of Hormuz to commercial shipping is reportedly in the final stages of drafting. However, Iran has cautioned that such an agreement would be dependent on the US meeting its demands (including compensation and the lifting of sanctions) and that this would not result in an immediate reopening of the Strait.

US.

The July non-farm payrolls report was weaker than expected, with jobs numbers falling 27k, well below market expectations for a rise of 80k. While much of the decline was related to government jobs, private sector jobs growth was softer than expected. Previous months were also revised down and average hourly earnings undershot expectations. Despite that softness, a continued fall in the participation rate saw the unemployment rate drop to 4.1% (from 4.2% previously). In other news, business conditions were mixed in July. The ISM manufacturing gauge continued to strengthen, with increases in orders and production, along with a lift in employment. However, service sector conditions cooled with notable softness in the labour market. Against that mixed outlook, factory orders fell 0.3% in June (below expectations). The highlights of this week's calendar are the July CPI report (Wednesday) and updates on retail sales and consumer confidence (both out on Friday).

Asia-Pacific.

In Australia, nationwide house prices dropped another 0.7% in July, following declines of 0.5% and 0.7% in May and June respectively. Prices have been weighed down by restrictive monetary policy, weak homebuyer sentiment following recent tax changes and broader economic uncertainty. In the household sector, nominal spending rose 0.8%mth in June, with spending up 6% over the past year. While much of that rise was due to higher prices, discretionary spending was firmer than non discretionary categories, pointing to resilience in spending appetites. The RBA meets on Tuesday. The Board is expected to leave the cash rate on hold but retain a hawkish stance.

In China, the RatingDog manufacturing PMI fell 0.8pts to 50.9 in July, its weakest reading in four months. July saw falls in both production and new orders. There was also softness in the services PMI, which fell to 50.4 in July (its lowest reading since September 2024), driven by weakness in domestic new orders. Against that backdrop, both PPI and CPI were softer than expected in July.

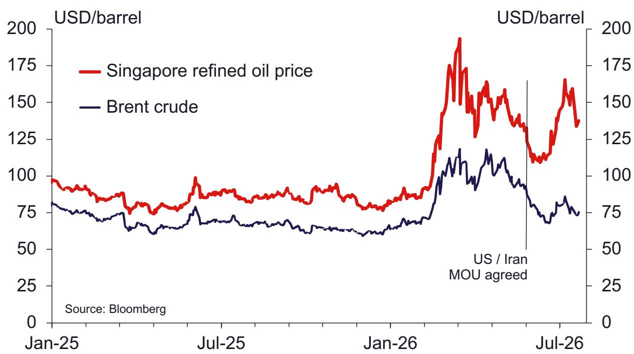
Trading partner real GDP (calendar years)

	Annual average % change			
	2025	2026	2027	2028
Australia	2.0	1.5	1.3	2.2
China	5.0	4.7	4.6	4.4
United States	2.1	2.0	1.8	1.9
Japan	1.1	0.6	0.8	0.9
East Asia ex China	4.7	4.8	4.2	4.2
India	7.6	6.7	6.7	6.6
Euro Zone	1.5	0.2	1.1	1.5
United Kingdom	1.4	1.1	1.1	1.5
NZ trading partners	3.2	2.8	2.7	2.9
World	3.4	3.2	3.3	3.3

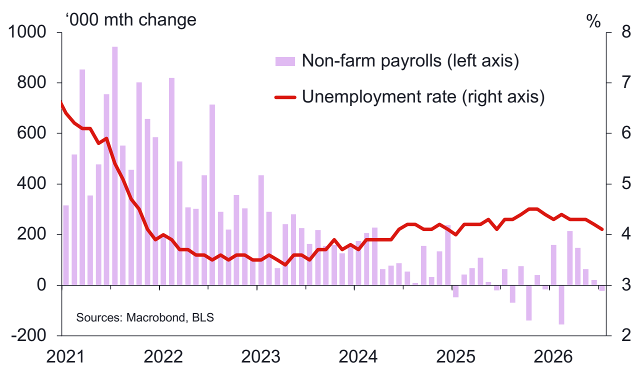
Australian & US interest rate outlook

	7 Aug	Dec-26	Dec-27	Dec-28
Australia				
Cash	4.35	4.35	3.85	3.60
90 Day BBSW	4.51	4.45	3.75	3.70
3 Year Swap	4.54	4.45	4.10	3.90
3 Year Bond	4.54	4.45	4.10	3.90
10 Year Bond	5.02	4.85	4.65	4.65
10 Year Spread to US (bps)	34	25	0	-20
US				
Fed Funds	3.625	3.625	3.625	3.625
US 10 Year Bond	4.68	4.60	4.65	4.85

Oil prices



US nonfarm payrolls and unemployment rate



Financial markets wrap

Foreign exchange.

NZD/USD is threatening to break above the week-old range of 0.5860-0.5910. Should it do so, nearby targets are minor resistance at 0.5930 and major resistance at 0.6000.

Much will hinge on the US CPI data on Wed. The NZ calendar is low-key, apart from RBNZ inflation expectations (Thu), with the next major event being the RBNZ MPS on 2 September.

Looking further ahead, NZ-US yield spreads have preserved most of July's OCR hike-related gains and are expected to extend higher during the quarter ahead given RBNZ vs Fed expectations. That should lend support to NZD/USD.

For the quarter ahead, we retain a neutral bias, pending an enduring resolution of the Iran war. A positive outcome could lift the NZD above the 0.6000 area, while a full-scale war could cause a decline to 0.5600.

NZD/AUD's rebound, helped by the RBNZ's July hike, has stalled in the 0.8320-0.8400 area, with further consolidation likely until fresh event surprises. On that score, the RBA decision tomorrow will be important for its guidance update, as will Governor Bullock's testimony on Friday.

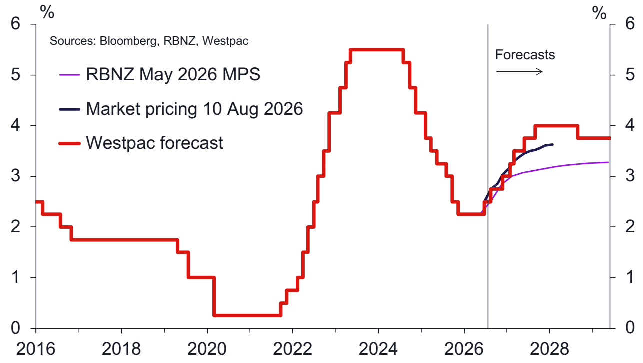
Interest rates.

The 2yr swap rate continues to consolidate inside the month-old range of 3.60%-3.80%, after making a cycle high of 3.81% in July. We expect that range to hold for the month ahead given the paucity of major NZ data ahead of the RBNZ MPS (2 Sep). The RBNZ's inflation expectations survey on Thursday will be worth watching though.

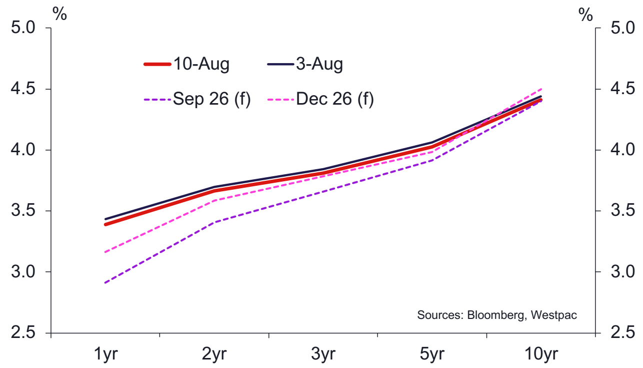
OIS pricing remains firm at a 90-95% chance of a hike in September, but the chances of another in October have been trimmed to 50% (from 65% two weeks ago), with a total of two hikes by December. OIS pricing predicts an OCR of 3.50% in a year's time, lower than our economists (who forecast hikes in September and December, an OCR of 3.75% in a year's time, and a peak of 4.0%).

The yield curve's flattening trend since the peak in late December remains stalled awaiting fresh RBNZ guidance, the 2-10yr swap at 75bp (vs a 67bp cycle low). We expect the RBNZ's tightening cycle to bear-flatten the curve further during the year ahead, but in the meantime, steepening in US and AU curves will spillover to NZ such that the 2-10yr could rise to the 80bp-90bp area.

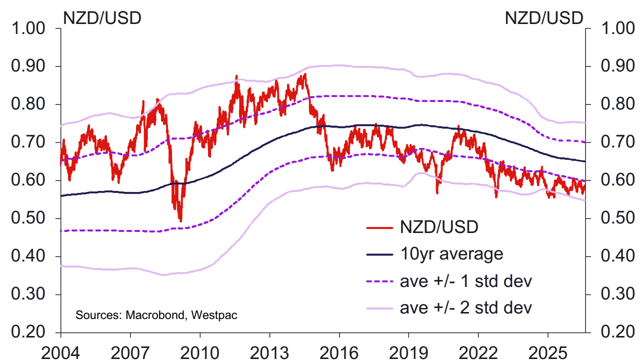
Official Cash Rate forecasts



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	0.590	0.563-0.596	0.553-0.720	0.614	0.60
AUD	0.835	0.816-0.837	0.816-0.971	0.908	0.84
EUR	0.510	0.495-0.513	0.484-0.637	0.558	0.51
GBP	0.437	0.425-0.442	0.425-0.531	0.478	0.44
JPY	93.1	91.1-95.3	74.7-98.6	87.0	96.0

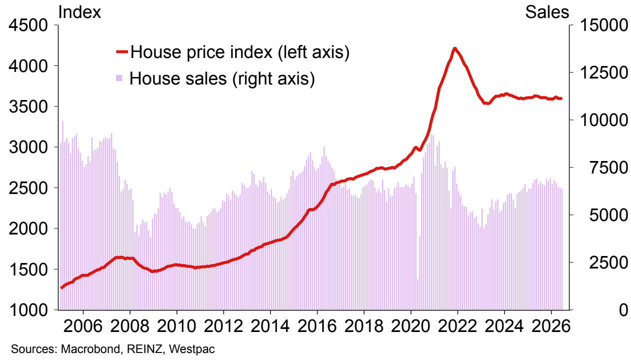
The week ahead

Jul REINZ House Sales & Prices

Aug 13, Sales, Last: –2.9%yr; Prices, Last: –0.8%yr

The housing market softened further in June. House sales were down around 1% in seasonally adjusted terms, adding to a cumulative 9% fall since the start of the year. The REINZ house price index fell by 0.3% for the month and was down 0.8% on a year ago. Fixed-term mortgage rates have risen since the start of this year, in anticipation of the next RBNZ tightening cycle (which is now in motion). We expect that higher interest rates will continue to weigh on the housing market, leaning against any improvement in incomes as the economy gets back on its feet.

REINZ house prices and sales

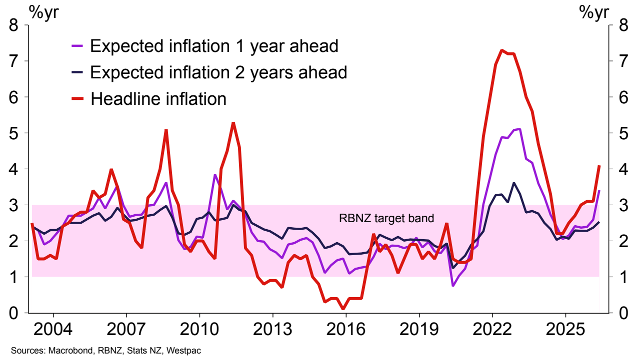


Q3 RBNZ Survey of Inflation Expectations

Aug 13, Inflation two years ahead last: 2.53%

Inflation expectations are a key focus for the RBNZ right now, with concerns that the oil-related rise in inflation will result in a broader and more enduring lift in pricing behaviour. Expectations already took a step higher in the Q2 survey. Since then, we've seen large swings in oil prices, while overall inflation has risen back up to 4.1%. We're expecting that the Q3 survey will show another rise in inflation expectations at the closely watched one- and two-year ahead horizons. However, expectations at longer horizons (five and ten years ahead) are likely to be more stable given the start of the RBNZ's tightening cycle.

RBNZ Survey of Expectations

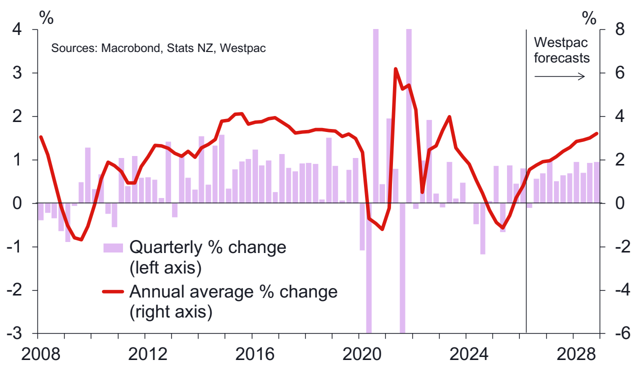


Economic and financial forecasts

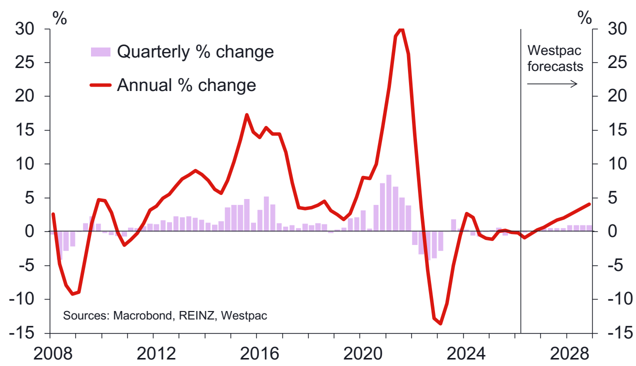
Economic indicators	Quarterly % change				Annual % change			
	Mar-26	Jun-26	Sep-26	Dec-26	2024	2025	2026	2027
GDP (production)	0.8	-0.1	0.6	0.7	-1.6	1.5	2.0	2.9
Consumer price index	0.9	1.5	0.7	0.4	2.2	3.1	3.5	1.9
Employment change	0.1	0.1	0.3	0.6	-1.3	0.2	1.2	2.5
Unemployment rate	5.4	5.6	5.5	5.4	5.1	5.4	5.4	4.9
Labour cost index (all sectors)	0.5	0.6	0.7	0.6	3.3	2.0	2.4	2.4
Current account balance (% of GDP)	-3.6	-3.7	-3.9	-3.9	-4.7	-3.6	-3.9	-3.9
Terms of trade	-1.6	1.4	0.9	-0.1	8.9	3.4	0.6	3.9
House price index	0.1	-0.1	0.0	0.2	-1.0	-0.1	0.3	2.0

Financial forecasts	End of quarter				End of year			
	Mar-26	Jun-26	Sep-26	Dec-26	2024	2025	2026	2027
OCR	2.25	2.25	2.75	3.00	4.25	2.25	3.00	4.00
90 day bank bill	2.51	2.63	3.00	3.40	4.45	2.52	3.40	4.20
2 year swap	3.12	3.47	3.70	3.95	3.64	2.71	3.95	4.20
5 year swap	3.71	3.88	3.95	4.15	3.73	3.27	4.15	4.40
10 year bond	4.54	4.61	4.65	4.65	4.50	4.27	4.65	5.05
TWI	67.2	66.5	67.0	67.6	69.5	66.4	67.6	72.2
NZD/USD	0.59	0.58	0.59	0.60	0.59	0.57	0.60	0.66
NZD/AUD	0.85	0.82	0.83	0.84	0.91	0.87	0.84	0.90
NZD/EUR	0.50	0.50	0.51	0.51	0.55	0.49	0.51	0.55
NZD/GBP	0.44	0.44	0.44	0.44	0.46	0.43	0.44	0.47

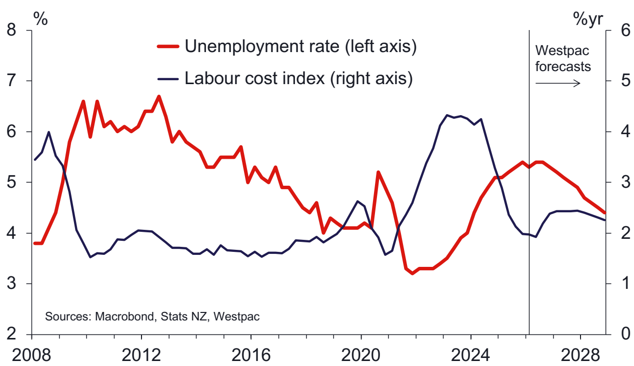
GDP growth



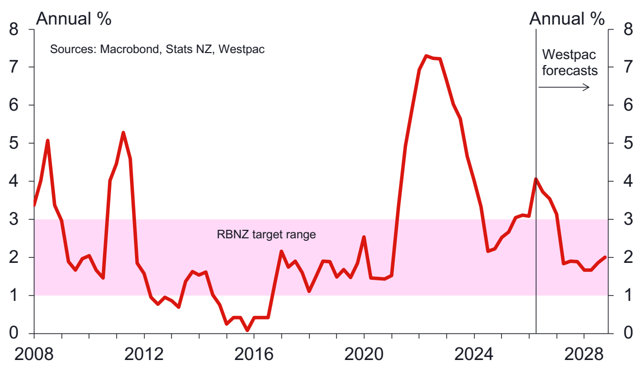
House prices



Unemployment and wage growth



Consumer price inflation



Data calendar

		Last	Market median	Westpac forecast	Risk/Comment
Mon 10					
Jpn	Jun Current Account Balance, ¥bn	3968	1514	–	Weakness in net direct investment likely to narrow surplus.
	BoJ Summary of Opinions	–	–	–	Minutes from the July meeting.
Eur	Aug Sentix Investor Confidence, index	–3.1	–2.9	–	Confidence recovery faces ongoing uncertainty.
Tue 11					
Aus	Jul NAB Business Conditions, index	3	–	–	Conditions sluggish, confidence fragile.
	RBA Policy Decision	4.35	4.35	4.35	'Hawkish' hold is expected; updated forecasts also in focus.
US	Jul NFIB Small Business Optimism, index	97.4	97.3	–	Small firms remain cautious on demand and costs.
	Jul Existing Home Sales, %mth	–2.4	–1.0	–	Affordability pressures continue to curb turnover.
Wed 12					
US	Jul CPI, %mth	–0.4	0.1	0.2	Markets watching for second-round risks.
Thu 13					
NZ	Jul REINZ House Prices, %yr	–0.8	–	–	Buyer enthusiasm dampened by rising mortgage rates...
	Jul REINZ House Sales, %yr	–2.9	–	–	... and an ample supply of homes on the market.
	Q3 RBNZ 2Yr Inflation Expectations, %ann	2.5	–	–	Likely to lift again, consistent with the lift in actual inflation.
Aus	RBA Assistant Governor (Fin Mkts)	–	–	–	Kent, fireside chat.
Eur	Jun Industrial Production, %mth	–0.2	0.2	–	Manufacturing activity continues to underperform.
UK	Q2 GDP, %ann	0.6	0.4	–	Growth momentum relatively firm, probably not for long.
US	Initial Jobless Claims	199	203	–	Still at relatively low levels.
	Jul PPI, %mth	–0.3	0.2	–	Upstream price pressures contained despite oil prices.
	Fedspeak	–	–	–	Hammack, Barkin.
Fri 14					
NZ	Jul Manufacturing PMI, index	59.7	–	–	Oil fluctuations continuing to impact trading conditions.
	Jun Net Migration, no.	1860	–	–	Balance turning more positive as outflow of NZers slows.
Aus	RBA Governor Bullock	–	–	–	Testimony before House of Representatives.
	Q2 Housing Finance Approvals, %qtr	–3.8	–4.0	–6.0	Larger decline anticipated given interest rate rises, uncertain...
	Q2 Owner-Occupier Approvals, %qtr	–4.3	–	–3.5	... near-term economic outlook and a sharp pull-back in...
	Q2 Investor Approvals, %qtr	–3.0	–	–9.7	... investor activity following the Budget's tax policy changes.
Chn	Q2 Current Account Balance, US$bn	184.3	–	–	Trade's strength a saving grace amid sluggish domestic growth.
Eur	Q2 GDP, %qtr	0.4	0.4	–	Second estimate to provide more colour.
	Jun Trade Balance, €bn	–5.0	–	–	Surplus with US shrinking, deficit with China growing.
US	Jul Retail Sales, %mth	0.2	0.2	–	Consumer spending slowed to a below-trend pace ...
	Aug Uni. Of Michigan Sentiment, index	55.2	54.1	–	... record-low consumer sentiment skews risks to downside.
	Jun Business Inventories, %mth	0.3	–	–	Inventory accumulation has picked up in recent months.

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