Review: RBNZ Monetary Policy Statement

28 May 2025

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A 25bp cut delivered; OCR track bottoms at 2.85%

- As expected, the RBNZ cut the Official Cash Rate (OCR) by 25bp to 3.25% today. The decision was reached in a 5:1 vote, with the anonymous dissenter preferring to leave the OCR unchanged. The accompanying OCR track now bottoms out at 2.85% rather than 3.1% as in February, and gradually rises from there to 3.1% by mid-2028, the end of the forecast.
- The tone of the accompanying forecasts and text was balanced. Downside activity risks and upside inflation risks were noted. But overall the RBNZ remains confident the inflation outlook is benign and that they are well placed to respond to developments as they unfold.
- The RBNZ outlined two scenarios related to the global trade situation: inflationary or disinflationary, with the OCR either heading north or south next year as a result, as opposed to staying in a fairly narrow range.
- Short end rates and the Kiwi rose as markets contemplated the gradual decline in the RBNZ's OCR track, which raises the possibility of a pause in the near future.

In brief

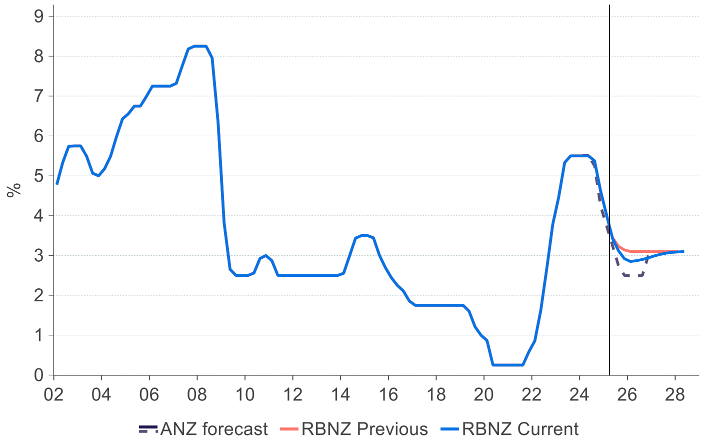
A 25bp cut today was universally expected, so the main interest in the Monetary Policy Statement was always going to be the OCR track and any other signals of intent.

For the hawks: one committee member voted to leave the OCR unchanged.

For the doves: the trough of the RBNZ's OCR projection was lowered – from 3.1% in the February Statement to 2.85%, as we expected. (We are forecasting that the RBNZ will ultimately end up delivering more cuts in order to shore up the domestic economic recovery, but we did not expect the RBNZ to forecast anything close to that today.)

For both the hawks and the doves: given the uncertainty about the impact of global trade spats, trade-related upside and downside scenarios were outlined to help guide the market as to the likely RBNZ response should the data start to tilt one way or the other versus current RBNZ expectations.

Figure 1. OCR forecast



Source: RBNZ, Macrobond, ANZ Research

Key quotes

- **OCR decision:** "The Committee discussed the options of keeping the OCR on hold at 3.50 percent or reducing it to 3.25 percent." "On Wednesday 28 May, the Committee took the decision to vote on the two options. By a majority of 5 votes to 1, the Committee agreed to decrease the OCR by 25 basis points from 3.50 percent to 3.25 percent."

- **OCR outlook:** "Inflation is within the target band, and the Committee is well placed to respond to both domestic and international developments to maintain price stability over the medium term."

- **Domestic activity:** "The New Zealand economy is recovering after a period of contraction. High commodity prices and lower interest rates are supporting overall economic activity."

- **Fiscal policy:** "Domestic fiscal policy is assessed as being broadly neutral from a medium-term inflation perspective, relative to February Statement projections."

- **Inflation outlook:** "Annual CPI inflation is expected to remain in the target band, and converge to the mid-point"…"Non-tradables inflation is expected to continue to decline, consistent with spare productive capacity in the economy. Annual tradables inflation is projected to remain around 1 percent over the medium term, reflecting below average global growth and falling inflation within our trading partners."

- **Inflation expectations:** "Measures of business and household inflation expectations have increased. The Committee discussed whether this increase reflected factors like higher food prices and current reporting on the inflationary effect of tariffs in the US."…"Some Committee members emphasised the risk that these increases reflect a more generalised and persistent increase in inflation expectations."

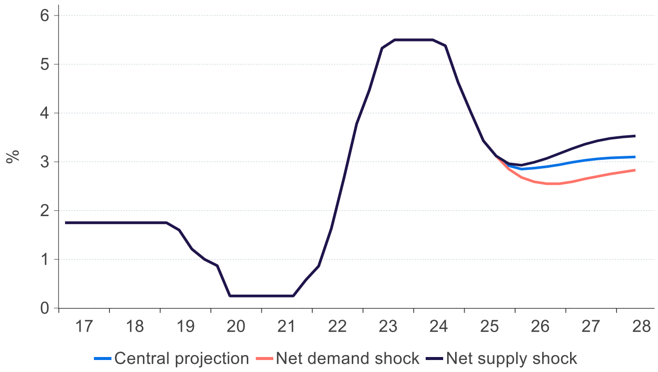
- **Global outlook:** "The Committee noted that projections for global economic activity have weakened since the February Statement, reflecting the shift towards protectionist policies in some major economies."

- **Tariff impacts:** "On balance, the Committee expects the increase in global tariffs to result in less inflationary pressure in the New Zealand economy."…"there is significant uncertainty about this assessment, depending on whether the impact of tariffs proves to be predominantly demand- or supply-side in nature."

That all looks sensible. The economy is recovering, but so far is making fairly hard work of it. New Zealand's commodity prices are doing extremely well, but dark clouds hang over the global outlook. Will they blow away or turn into a storm? With the OCR now well off its peak and closer to neutral the RBNZ doesn't need to pin its colours to any particular mast until the picture is clearer.

Indeed, the RBNZ chose to outline two scenarios related to the global tariff uncertainty: higher imported inflation due to higher global production costs (i.e. a net negative global supply shock), or lower global demand for our exports, along with lower imported inflation (a net negative demand shock). The upshot is that the OCR either rises or falls over 2026 as a result, as opposed to the fairly flat track in the central projection.

Figure 2. RBNZ scenarios



Source: RBNZ, ANZ Research

RBNZ forecasts in brief

The RBNZ's updated outlook is similar to our own. The outlook for GDP growth is much the same as ours, with annual growth lifting to around 3% in mid-2026. Annual CPI inflation is expected to accelerate to 2.7% in Q3 2025 (a little lower and later than our forecast peak of 2.8% in Q2). Underpinning this, the RBNZ is forecasting slightly weaker non-tradable inflation over the remainder of 2025 than we are, but stronger non-tradable inflation in 2026.

Meanwhile, the unemployment rate is expected to peak at 5.2% in Q2 (ANZ also 5.2%) before steadily falling from late 2025, reaching 4.3% by the end of the forecast horizon. Putting it all together, their outlook for the output gap is slightly lower than previously forecast, but follows a similar profile.

See page 7 for charts comparing the RBNZ's latest forecasts against the February MPS and our own forecasts.

Risks

The RBNZ's strategy continues to be to take the OCR close to its estimate of neutral (2.5-3.5%) and reassesses in real time from there – while stressing the conditionality of the outlook on the data flow.

The RBNZ outlined risks on both sides. Higher inflation expectations have caused concern amongst some Committee members (see quotes above). But overall the Committee has parked higher near-term inflation expectations in the "wait and see" basket, as we expected they would, given the "subdued" economic recovery.

Our take

The RBNZ provided few surprises today. With the OCR approaching the neutral zone and enormous uncertainty about the global growth outlook and how that will impact the local economy, there's little to be gained from betting the house on any one particular scenario unfolding.

The market's estimate of how much further easing is required will continue to wax and wane with the data flow. For our part, we are forecasting further 25bp cuts in July, August and October, taking the OCR to a low of 2.5% to shore up the recovery in the face of global headwinds. But as noted in our preview, we didn't expect the RBNZ to feel the need to put that many cards on the table as yet. The domestic data could start to surprise on the upside. Or the global tariff situation could be resolved with less angst than expected, leaving the New Zealand economy to get on with the business of recovery. It's certainly not all downside risks from here, but lacklustre anecdote and data in recent months has seen us conclude a bit more support is warranted.

Meanwhile if downside risks eventuate, the RBNZ is in a good place to respond. Yes, some measures of inflation expectations have lifted recently, but capacity indicators continue to indicate that the output gap is negative and the economy in a disinflationary state. If you're winning the war, there's no need to overreact to minor provocations.

Financial markets

Short-end interest rates and the NZD both edged higher after the 2pm announcement, with the bellwether 2-year swap rate up around 3.5bps to 3.20%, and the Kiwi settling about 10bps higher at around 0.5960 after half an hour. While that may seem surprising given that the RBNZ dropped the low point in their track to 2.85%, matching what the market had priced in, the RBNZ's track falls more gradually. And mathematically, their quarterly track is consistent with 10bp cuts at each of the next four meetings (or 40% odds apiece). Although the RBNZ is always at pains to remind markets not to overinterpret the track, markets still obsess over it, and the more gradual easing profile is suggestive of the possibility of a pause at the next meeting. We also suspect markets were caught slightly on the proverbial back foot by the split vote (one member voted to pause today) and the upturn in the track from mid-2026, even though some analysts – including us – have had eventual hikes pencilled into their forecasts for a while now.

Media release – OCR lowered to 3.25%

The Monetary Policy Committee today voted to lower the OCR by 25 basis points to 3.25 percent.

Annual consumers price index inflation increased to 2.5 percent in the first quarter of 2025. Inflation expectations across firms and households have also risen. However, core inflation is declining and there is spare productive capacity in the economy. These conditions are consistent with inflation returning to the mid-point of the 1 to 3 percent target band over the medium term.

The New Zealand economy is recovering after a period of contraction. High commodity prices and lower interest rates are supporting overall economic activity.

Recent developments in the international economy are expected to reduce global economic growth. Both tariffs and increased policy uncertainty overseas are expected to moderate New Zealand's economic recovery and reduce medium-term inflation pressures. However, there remains considerable uncertainty around these judgements.

Inflation is within the target band, and the Committee is well placed to respond to domestic and international developments to maintain price stability over the medium term.

Summary Record of Meeting – May 2025

Annual consumers price index (CPI) inflation remains within the Monetary Policy Committee's 1 to 3 percent target band. While measures of inflation expectations have increased, core inflation and spare productive capacity in the economy are consistent with inflation returning to the target mid-point over the medium term. Elevated export prices and recent reductions in the OCR are expected to support a modest pace of growth in the New Zealand economy, even as increased global tariffs are expected to slow global economic growth.

Higher global tariffs and policy uncertainty are expected to lower global growth

The Committee noted that projections for global economic activity have weakened since the February Statement, reflecting the shift towards protectionist policies in some major economies. There have been downward revisions to economic growth projections for China and the US, reflecting the scale of tariff increases between these two countries.

The Committee noted that, in addition to the direct effect of higher tariffs, increased policy uncertainty in the international economy is likely to weigh on global investment and consumption. As well as uncertainty about tariff retaliation, it was unclear how countries would respond with fiscal and monetary policies. For example, it is possible that China could respond to weaker economic activity with a sizeable fiscal stimulus. US fiscal policy could place strains on the sustainability of its public debt. More generally, the uncertain trajectory of geoeconomic fragmentation and the decline in the quality of macroeconomic institutional arrangements were likely to result in precautionary behaviour by firms and households. In aggregate, economic growth in New Zealand's main trading partners is expected to remain below potential over 2025.

Headline inflation within New Zealand's trading partner economies has fallen over the past year. Projections for inflation for most of our trading partners have been revised down in recent quarters. The main exception is the US, where higher tariffs are expected to increase inflationary pressure.

The New Zealand economy is starting to recover, after contracting over the middle of 2024

The Committee noted that spare productive capacity remains in the New Zealand economy. This is projected to dissipate over the medium term as the economy recovers. Elevated export commodity prices and lower interest rates are supporting overall economic activity in the New Zealand economy. The Committee noted that the full economic effects of cuts in the OCR since August 2024 are yet to be fully realised.

The Committee discussed conditions in New Zealand's labour market. Nominal wage growth is slowing, while firms report that it is easier to find workers. Employment growth is currently modest but expected to increase from the second half of the year in line with the broader economic recovery.

The announced increase in US tariffs will lower global demand for New Zealand's exports, particularly from Asia, constraining domestic growth. Heightened global policy uncertainty is expected to weigh on business investment and consumption in New Zealand.

On balance, the Committee expects the increase in global tariffs to result in less inflationary pressure in the New Zealand economy. However, as discussed below, there is significant uncertainty about this assessment, depending on whether the impact of tariffs proves to be predominantly demand- or supply-side in nature. The domestic monetary policy response will focus on the medium-term implications for inflation.

Domestic fiscal policy is assessed as being broadly neutral from a medium-term inflation perspective, relative to February Statement projections. The change announced in Budget 2025 enabling businesses to bring forward depreciation allowances is assumed to increase investment activity. However, the inflationary consequences of this policy are assumed to be offset by an announced reduction in government spending.

Annual CPI inflation is expected to remain in the target band, and converge to the mid-point

The Committee discussed domestic inflationary pressure. New Zealand's annual CPI inflation increased to 2.5 percent in the March 2025 quarter, largely in line with previous projections. Most annual core inflation measures continued to decline in the March 2025 quarter, and all are now within the target band for headline CPI inflation.

Annual CPI inflation is projected to increase to 2.7 percent in Q3 2025, then return to near the 2 percent target midpoint from 2026. The near-term increase in headline inflation includes higher food and electricity price inflation.

Non-tradables inflation is expected to continue to decline, consistent with spare productive capacity in the economy. Annual tradables inflation is projected to remain around 1 percent over the medium term, reflecting below average global growth and falling inflation within our trading partners.

The financial system remains stable

The Committee noted that most wholesale interest rates have fallen since the February Statement, resulting in lower mortgage and term deposit rates. The average interest rate on the stock of mortgages is expected to continue to decline in coming quarters as more mortgage holders refix at lower fixed-term interest rates. Close to half the stock of mortgages is due to reprice during the June and September 2025 quarters.

The Committee was briefed on financial system stability. While non-performing loans in the housing and small business sectors have increased in line with the past contraction in the economy, the banking system remains well capitalised and in a strong financial position to support customers. The Committee agreed that there is currently no material trade-off between meeting inflation objectives and maintaining financial system stability.

The Committee was briefed on the status of the Large Scale Asset Purchase programme. The Committee noted there has been increased volatility in domestic wholesale interest rates, reflecting increased global policy uncertainty. Despite this volatility, wholesale interest rate markets continue to function, without impeding monetary policy transmission.

Risks around the economic outlook are heightened

The Committee discussed several key risks around the central projection. Measures of business and household inflation expectations have increased. The Committee discussed whether this increase reflected factors like higher food prices and current reporting on the inflationary effect of tariffs in the US. The projections assume that medium-term inflation expectations remain consistent with the target mid-point. Some Committee members emphasised the risk that these increases reflect a more generalised and persistent increase in inflation expectations.

The Committee discussed the medium-term outlook for import prices. Members noted that a less productive global economy, against a background of deglobalisation, presents an upside risk to the current import price projection.

The Committee noted downside risks to the outlook for export prices. This reflects a weaker global growth outlook and the potential for a quicker international supply response to high prices from global meat and dairy producers.

The Committee noted the risk that large economic policy shifts in overseas economies could lead to additional volatility in financial markets. For example, concerns about US debt sustainability could lead to increased bond yields or declines in global asset prices.

There are alternative scenarios for the domestic outlook

In addition to the uncertain scale and duration of tariff policies, it is unclear how these will transmit to the New Zealand economy. Some members emphasised that the costs of trade could increase more than currently assumed, as global supply chains adapt to trade barriers and geoeconomic fragmentation. This could result in greater domestic medium-term inflationary pressure than in the central projection. Other members emphasised that policy uncertainty could lower global investment, and trade diversion could lower import prices by more than currently assumed. This could, instead, lower medium-term inflationary pressure relative to the central projection.

Two scenarios in the May Statement highlight how the realisation of these risks could affect the outlook for the domestic economy. These scenarios represent just two of many paths the economy may take as higher tariffs and uncertainty transmit through the system. They are intended to broadly highlight the trade-offs and considerations facing the Committee should these risks eventuate.

The Committee noted that, in practice, a broad range of factors contribute to its monetary policy decisions. Its response to any of these risks would depend on economic conditions at the time, the outlook for inflationary pressure, and its secondary objectives of avoiding unnecessary instability in the economy and having regard to financial system stability.

The Committee voted to reduce the OCR to 3.25 percent

The Committee agreed on the projected central path for the OCR.

The Committee discussed the options of keeping the OCR on hold at 3.50 percent or reducing it to 3.25 percent. The case for lowering the OCR to 3.25 percent highlighted that CPI inflation is in the target range and there is significant spare capacity in the economy. Measures of core inflation and wage inflation have continued to decline. In addition, there is a weaker outlook for domestic activity and inflationary pressure relative to the February Statement, because of international developments. Some members also emphasised that non-tradable inflation was currently being boosted by administered prices. Given these factors, a 25 basis point decline in the OCR was seen as consistent with medium-term price stability.

In considering the merits of holding the OCR unchanged at 3.50 percent for this meeting, some members noted that this would allow the Committee to better assess whether increased economic policy uncertainty was having a noticeable impact on household and firm behaviour. An unchanged OCR could also further consolidate inflation expectations around the target mid-point, and guard against the risk of higher-than expected inflation from the supply-side effects of increased tariffs.

On Wednesday 28 May, the Committee took the decision to vote on the two options. By a majority of 5 votes to 1, the Committee agreed to decrease the OCR by 25 basis points from 3.50 percent to 3.25 percent.

Inflation is within the target band, and the Committee is well placed to respond to both domestic and international developments to maintain price stability over the medium term.

Attendees

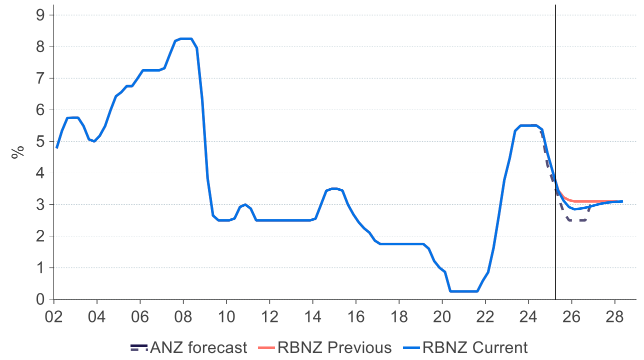
Members of MPC: Christian Hawkesby (Chair), Bob Buckle, Carl Hansen, Karen Silk, Paul Conway, Prasanna Gai

Treasury Observer: Dominick Stephens

MPC Secretary: Adam Richardson

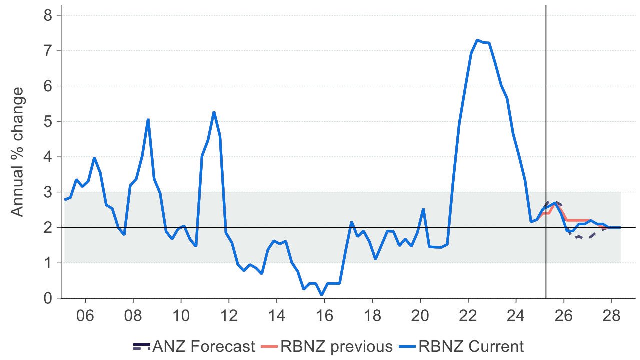
Key forecasts: Relatively minor tweaks to the outlook

The RBNZ's OCR projection dips to 2.85%, lower than previously, but higher than our forecast (we expected as much)



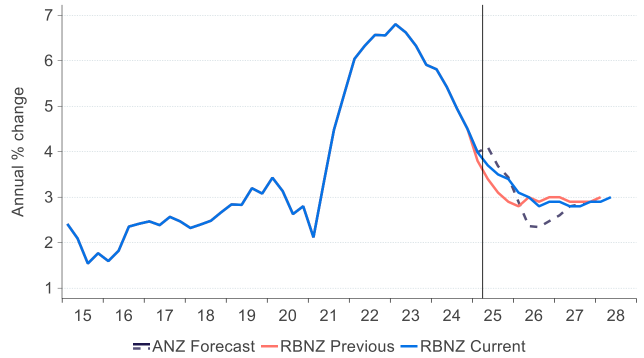
Source: RBNZ, Macrobond, ANZ Research

The CPI inflation outlook is little changed in the near term, but troughs a little lower…



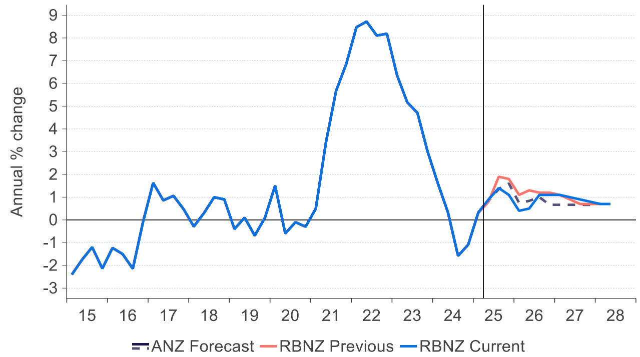
Source: RBNZ, Stats NZ, Macrobond, ANZ Research

…with higher non-tradable inflation in the near term, but slightly lower further out



Source: RBNZ, Stats NZ, Macrobond, ANZ Research

The tradable inflation outlook has had a small downgrade



Source: RBNZ, Stats NZ, Macrobond, ANZ Research

The unemployment rate starts falling a little later than previously

Source: RBNZ, Stats NZ, Macrobond, ANZ Research

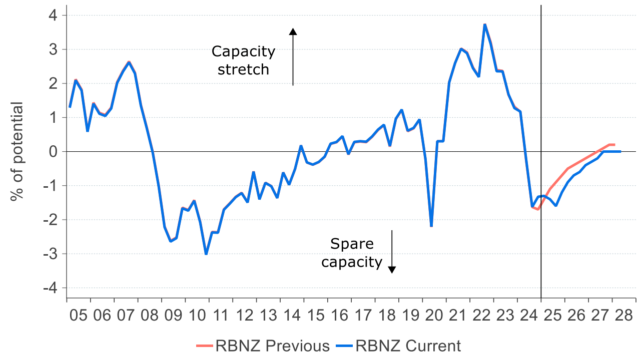
LCI wage growth is weaker in the near term, but stronger from late 2026 onwards

Source: RBNZ, Stats NZ, Macrobond, ANZ Research

The GDP growth outlook is little changed

Source: RBNZ, Stats NZ, Macrobond, ANZ Research

The RBNZ still expects the output gap to remain in disinflationary territory for most of the forecast horizon



Source: RBNZ, Macrobond, ANZ Research

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