Preview: RBNZ Monetary Policy Review

1 July 2025

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Tough call

- **It's a *very* close-run thing after the dovish QSBO, but on balance we think the RBNZ will keep the OCR unchanged at 3.25% next week.** From there, we are now forecasting a cautious pace of cutting with 25bp cuts in August and November, with a third 25bp cut in February to 2.50% best interpreted as a placeholder for global headwinds, particularly confidence impacts.

- The RBNZ made it clear in May that their next decision would be data dependent. Subsequent data has clearly suggested a meaningful loss in economic momentum, while near-term CPI signals have been mixed: the Selected Price Indexes have suggested upside compared to the RBNZ's forecast, but the QSBO suggested downside. **We see the net dataflow since May as dovish, easily justifying a cut next week. Indeed, we think the RBNZ should cut.** However, on balance we think the Committee will decide it is prudent and low-cost to wait for more data on inflation – and inflation expectations – before cutting in August. But the decision is far from simple and at ~20% **we think the market is very much underestimating the chance of a cut next week. We'd put the odds at 40%+.** There's likely to be a range of opinions in the Committee, and much to-ing and fro-ing, if our own deliberations are anything to go by!

- We're calling 75bp of cuts in total whereas the May MPS implied only -40bp, and we acknowledge the risks around our call are currently tilted towards less and/or slower easing. Domestically, we expect consumption and non-tradable inflation to persistently undershoot the RBNZ's May forecasts, but even if that's correct, this may take considerable time to become evident. And we have explicitly built in 25bp of easing on global headwinds, and these are very uncertain.

The May Monetary Policy Statement (MPS) OCR track implied a cut in either July or August, but the market perceived comments by Acting Governor Hawkesby at the time to be "hawkish" and has since that time consistently put only around 20% odds on a cut next week, even as the data has delivered unders and overs. As is often the case, we suspect the market heard a clearer message re the next decision than the RBNZ probably thought it delivered. In our view, the Committee will view this as a clean-slate decision where they left all their options open.

Let's summarise the data since the May MPS.

Near-term inflation indicators – mixed: Selected Price Indexes (SPIs) for May were in the ballpark of our Q2 CPI forecast of 0.6% q/q (2.8% y/y), but they suggested upside risk to the RBNZ's May MPS non-tradable forecast of +0.7% q/q (ANZ: 1.0% q/q). Countering this, direct pricing indicators in today's QSBO suggested downside risk to the near-term CPI outlook. The SPIs are observed prices, so have to take precedence when forecasting, but the QSBO suggested the bounce in CPI will be short-lived, and that's really important.

Activity indicators – net dovish: At face value, GDP growth of 0.8% q/q in Q1 (RBNZ: 0.4% q/q) looked like the nail in the coffin of a cut. However, there are downward revisions either side. Q4 2024 was revised down 0.2%pts (to 0.5% q/q), and we recently revised down our Q2 2025 forecasts by 0.3%pts (from 0.4% q/q to 0.1%) based on soft timelier activity data including the PSI, PMI, retail card spending, and ANZBO past activity. And then today, QSBO experienced domestic trading activity was very soft and at face value suggests a *negative* quarter for GDP in Q2. It'll certainly hit the RBNZ's new real-time GDP indicator hard.

Housing – dovish: We recently revised down our (REINZ) house price forecast from 4.5% to 2.5% this year. The RBNZ in May forecast a 3.5% lift (CoreLogic).

Labour market – dovish: Monthly filled jobs suggest downside risk to our forecast of 0.1% q/q employment growth in Q2 (RBNZ 0.2%). QSBO experienced employment was more neutral.

Bits and bobs: The NZD trade-weighted index is 69.9 versus an RBNZ assumption of 69.0. That would typically be worth at least 10bp off an OCR track ready reckoner, if sustained. Dairy prices are falling, but this was expected, and we don't have any specific RBNZ forecasts to compare it against.

If the RBNZ was in May truly on the fence re cutting in July (as their published OCR track implied), and is data dependent, then they'd cut next week, based on that set of data. And we'd put 40%, even 45%, odds on that. But the fly in the ointment is lingering concerns that inflation could be more persistent than forecast. The previous decision was forced to a vote – and if one Committee member disagreed with cutting the OCR to 3.25%, they presumably aren't going to be keen to cut it to 3% at this stage. Will the rest of the Committee feel confident enough that a cut is the right thing to again overrule them, in that instance?

It seems fair to assume that the dissenter was one of the Committee members concerned about "a more generalised and persistent increase in inflation expectations". We haven't had a great deal of data on that front since May, at least not the measures the RBNZ focuses on. Household inflation expectations two years ahead have risen to a two-year high of 4.9%, likely impacted by food price inflation of 4.4% y/y, while 1-year-ahead business expectations in our ANZBO survey have been steady at 2.5-2.7% since November. By the time of the 20 August MPS, the RBNZ will have its own Survey of Expectations (7 August), and its new Tara-ā-Umanga Business Expectations Survey (18 August). At that release the RBNZ is going to start reporting the weighted median, in addition to the weighted mean. The former has been much better behaved. From the May MPS:

> "Mean inflation expectations from the BES at 5- and 10-years ahead are materially higher than those for 1- and 2-years ahead, and those from SOE respondents. This reflects a materially higher share of firms reporting very high inflation expectations (e.g. 10 percent or higher) at these terms. In contrast, weighted median inflation expectations from the BES were 2.5 percent across all horizons in the June 2025 quarter."

There is information in the fact that a few more people don't expect inflation targeting to survive for the long haul, but it's unusual to allow those responses to affect the reported central tendency of expectations. In our view, inflation expectations as relevant to price-setting decisions are indeed well-anchored, and this will become evident before long. Accordingly, we expect the RBNZ will cut the OCR in August once this data – and importantly, Q2 CPI – is in the bag (assuming they don't cut next week).

Turning points are messy, and our own OCR call is no less data dependent than the RBNZ's. But for now, the OCR track that is consistent with our macro forecasts versus the RBNZ is one of cautious cuts as it gradually becomes clear that risks have tilted towards medium-term inflation being too low, rather than too high. We see both consumption and non-tradable inflation undershooting RBNZ forecasts over the second half of the year, and therefore have a follow-up cut in November after another pause in October.

The third 25bp cut in February is best interpreted as a placeholder for global headwinds. While market turmoil has subsided dramatically as markets take a glass-half-full view, there is plenty of water to flow under the bridge – a fair bit of it this month as the 90-day tariff pause expires. We don't have sufficient confidence that "she'll be right" to take that cut out of our forecasts at this juncture, but we freely describe it as pencilled in.

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