Preview: RBNZ Monetary Policy Review

1 October 2025

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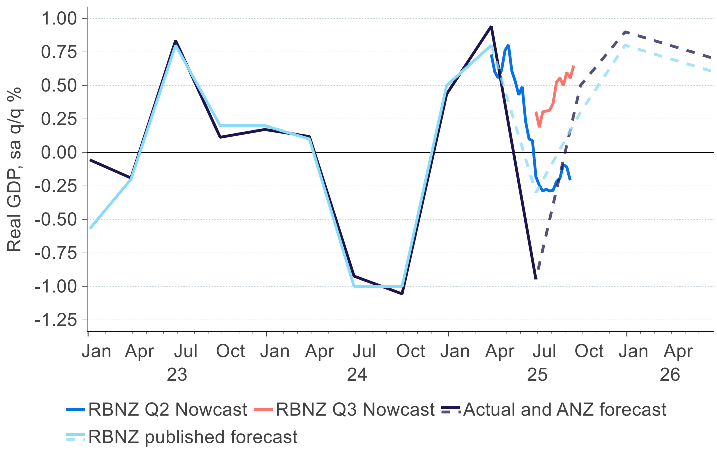
A 25bp cut provides the most optionality

- **We expect the RBNZ to cut the OCR 25bp to 2.75% next week**, with dovish messaging that leaves open the option of a 50bp cut in November and thereby prevents monetary conditions tightening on the day.
- There are also good arguments for frontloading easing; we'd put 35% odds on a 50bp cut.
- The NZIER's Quarterly Survey of Business Opinion on Tuesday could move the dial if it suggests a markedly greater degree of spare capacity.

Markets are currently pricing in a cut with certainty, and are now just debating how big it will be, with a roughly a 70% chance of a 25bp cut and a 30% chance of a 50bp cut. Economists are also split. We already laid out the arguments for 25bp and for 50bp in a note shortly after the GDP data, so we won't repeat them all here. The economics could justify either choice. Given that, we think the deciding factor will be strategy. A 25bp cut with plenty of dovish messaging around it reduces the risk of needing to change direction abruptly down the track, and it leaves maximum options open. The trade-off, monetary conditions not being quite as easy over the next six weeks as a 50bp cut would deliver, is likely to be judged acceptable. The RBNZ isn't currently forecasting CPI inflation to go under the midpoint of the target band at any stage, so there is a buffer to the downside, whereas the fact is, inflation is going to be around the top of the band over the next couple of reads – a bygone, in monetary policy terms, but still a bit awkward.

Since the RBNZ's appropriate August pivot to focus on downside risks, the data has been mixed but overall fairly lacklustre, with the big surprise being a 0.9% q/q fall in GDP in Q2, versus the RBNZ's expectation of a 0.3% drop. Since then, the signs are pointing to a better Q3 – though that's not saying a great deal. A fair amount of climbing is needed to even get to the top of the hole we're currently in. At this stage the RBNZ's Nowcast model is suggesting a little upside risk to the RBNZ's published forecast for Q3, but nothing as large as Q2's downside surprise. But at least it currently has a clear upward trend, whereas Q2 estimates generally got lower and lower as the release approached.

Figure 1. GDP and RBNZ Kiwi-GDP Nowcast



Source: RBNZ, Stats NZ, Macrobond, ANZ Research

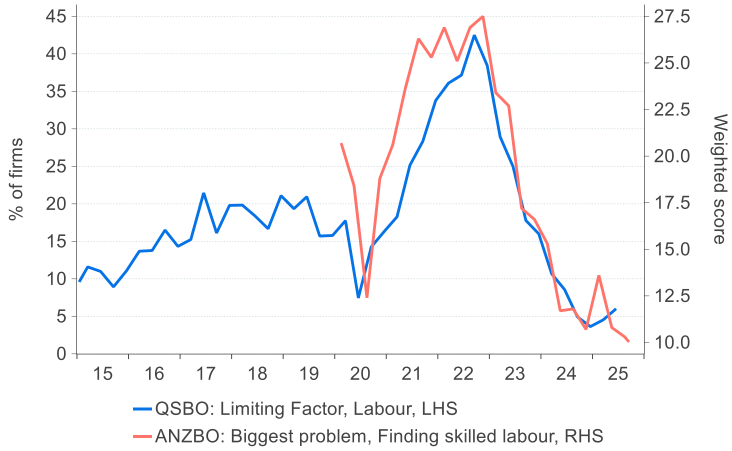
Option value is the main reason we've stuck with our call for a 25bp cut next month despite the large GDP miss. But another important consideration is that the RBNZ no longer treats GDP as the "truth" about where the economy has just been. One therefore has to be careful assuming they'll allow the surprise in the GDP to drive large changes in their view. Indeed, a desire to use a broader suite of economic data to assess the state of the economy drove the GDP Kiwi-GDP Nowcast project. GDP revisions have been enormous in recent years, changing the whole economic story at times. And currently, quirky (read: unreliable) seasonal adjustment is a known problem, as the COVID-19 volatility has confused the algorithms.

From the RBNZ's paper this week looking at long-run forecasting performance:

> "GDP data typically take several years to stabilise, which supports our practice of putting more weight on labour market and business survey data to estimate the contemporaneous output gap (the difference between output and the economy's potential output)."

In the context of that comment, the QSBO the day before the MPR will be important. Key indicators to watch are difficulty finding skilled labour, and labour and capacity as limiting factors. Our Business Outlook survey suggests we could see a further easing in labour as a limiting factor in Q3 (figure 2), which would be consistent with the unexpected activity weakness in Q2.

Figure 2. ANZBO and QSBO labour tightness measures



Source: NZIER, Macrobond, ANZ Research

Beyond the OCR decision at this meeting is the question of where the OCR will end up before it inevitably changes direction once again. The market is currently forecasting a trough of 2.26%, i.e. three more 25bp cuts rather than our and the RBNZ's forecast of two. We certainly agree that the risks are tilted towards an OCR that low, or even lower if the recovery disappoints. We are sceptical of the assumption in the RBNZ's model that lowering the OCR to neutral is sufficient to bring about sufficient economic momentum to close a negative output gap. But we're also wary of taking estimates of the output gap at face value, given how dramatically they can be revised over time. And who knows what the neutral OCR is anyway? It is best to be humble about our ability to estimate either of those things in real time, and prepare to be surprised one way or the other. To their credit, the RBNZ tends to be very upfront about that uncertainty.

If we are right that the RBNZ will deliver only 25bp in October and again in November, then when we weigh up the odds of the OCR going below 2.5% from there, we have to contend with the simple fact that February is a very long time away. By then, activity data will be on a firmer footing, and CPI inflation will likely be higher (we are forecasting 3.0% in Q3 and 2.9% in Q4, versus 2.7% today). And the NZD seems to be running out of puff recently, potentially representing some upside risk to tradeable inflation.

If, by February, activity is lifting and inflation is higher, then even if the RBNZ believes the negative output gap is closing only slowly, the temptation to “wait and see” could be strong. That would mean a 2.5% OCR for a longer time as opposed to a lower OCR trough for a shorter time – different paths to the same goal.

Markets

As at this morning, markets are going into this meeting with a 25bp cut fully priced and 28% odds of a 50bp cut. As such, the decision itself will matter, but so too will the tone. Our base case is a dovish 25bp cut, with no mention of caution around neutral or some pre-determined end to the easing cycle, and an acknowledgement that policy may need to go into stimulatory territory – and possibly at a faster pace if the economic vibe doesn’t improve by November. We think that approach gives the RBNZ the most tactical optionality: the Committee can always deliver a larger cut in November, and as long as they flag that possibility, markets will react accordingly. We’d expect that to deliver lower short-end swap rates on the day, as markets contemplate the possibility of a bigger cut to backstop the recovery over the three-month gap over summer until February, and then the data will decide from there.

We’d likely see a bigger downside move on the day on a 50bp cut, as markets move to price in greater odds of a follow-up 50bp cut in November. But the complicating factor, and the 64-billion-dollar question, would then be: once the dust settles, would markets then start pricing in hikes over 2026, on the presumption that a 2% OCR should guarantee a recovery? We think they might. Markets are already pricing in small odds of hikes after May 2026, and it wouldn’t take much to bring those expectations forward, possibly undermining the intended effect of a bigger cut. All up, we think the RBNZ will decide a dovish 25bp cut is the ’safer’ option both economically and strategically.

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