

# New Zealand Fixed Income Monthly March 2025

With inflation seemingly defeated, attention is shifting to factors such as tariffs

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## RBNZ appears to have defeated inflation, albeit at a cost

In a key development for New Zealand's fixed income market, official figures suggest that the Reserve Bank of New Zealand (RBNZ) has won its fight against inflation. New Zealand's consumers price index (CPI) stood at an annual rate of 2.2% for the second straight quarter in the three-month period up to December 2024<sup>1</sup>, keeping the figure within the RBNZ's medium-term policy target range of 1-3% per annum. We feel that the victory has come at a cost, however, given the significant impact interest rate rises have had on consumers and businesses. One example of this is official data showing that the total value of seasonally adjusted retail sales decreased by 1.4% quarter-on-quarter (QoQ) and 0.5% QoQ in the three-month periods ending in June 2024 and September 2024, before edging up by 1.4% in the December 2024 quarter<sup>2</sup>. However, the RBNZ has been making deep and rapid cuts to New Zealand's Official Cash Rate (OCR) since August 2024. This means that, in terms of monetary policy, the area of focus should now shift from the likely extent of further reductions to the length of time the OCR will stay at the "neutral" level at which interest rates are thought to be neither inflationary nor deflationary for the economy.

## New Zealand's growing bond issuance not excessive in relation to other markets

One example of a number of domestic forces with the potential to impact the fixed income market this year is the ever-increasing amount of government bonds New Zealand is issuing. Over the past four years, the New Zealand Treasury has consistently increased its planned amount of bond issuance. Although this may have created an impression of ballooning debt and contributed to higher yields, we feel that New Zealand's debt is not excessive in relative terms. In the US, for example, deficit levels are roughly twice those of New Zealand's. Furthermore, deficit levels in the UK and Europe are broadly similar to New Zealand's. In addition, these deficits look likely to increase going forward given growing pressure for Europe to spend a greater percentage of its aggregate GDP on defence. While it is true that New Zealand faces a similar need to increase defence spending, in our view the situation is not as urgent for the country given its relative distance from the war in Ukraine.

## Tariff impact on inflation to be more muted than assumed

Perhaps the most significant development for the fixed income market in terms of news headlines is the impact of US tariffs. We believe that while tariffs can have an inflationary impact, the effect is likely to be more muted than commonly assumed. This is due to factors such as the gap between imported costs and retail prices as well as the challenges that companies can face when trying to hike prices, such as lost sales. Therefore, we believe that that tariffs will have a larger impact on global growth and company profitability than on inflation.

<sup>1</sup> <https://www.stats.govt.nz/indicators/consumers-price-index-cpi/>

<sup>2</sup> <https://www.stats.govt.nz/information-releases/retail-trade-survey-december-2024-quarter/>

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