Reserve Bank of New Zealand
Te Pūtea Matua

Monetary Policy Statement.

September 2026

Policy assessment.
The Monetary Policy Committee today reached consensus to increase the OCR by 25 basis points to 2.75 percent.

Inflation increased to 4.1 percent in the June quarter because of higher fuel prices arising from the conflict in the Middle East. Core inflation, expected wage growth, and inflation expectations remain consistent with inflation returning to the 1 to 3 percent target band by mid-2027 and the 2 percent target mid-point later next year.

After lacklustre growth in the June quarter, New Zealand's economic recovery has most likely resumed but remains uneven. Resilient demand from New Zealand's trading partners and strong export prices are supporting income growth and investment in export-exposed sectors and regional New Zealand. In contrast, weak income growth, job insecurity, and flat house prices continue to weigh on household spending and residential investment, particularly in Auckland and Wellington.

The recovery is expected to strengthen and broaden. The Committee expects New Zealand's export sector to remain resilient and household spending to gradually increase. Conditions in the labour market should improve as the recovery gathers pace. Purchasing power will increase as inflation returns to the 2 percent target mid-point.

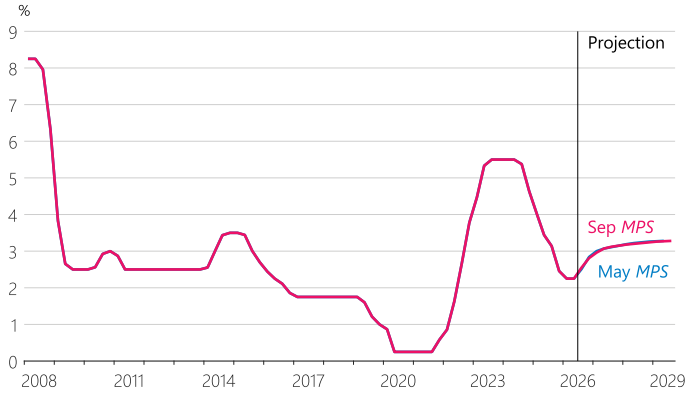
The global economy is facing significant risks that could affect commodity prices and demand for exports. New Zealand's economic recovery could be stronger or weaker than expected and price pressures could generate more persistent inflation. The Committee remains vigilant and will respond as necessary to ensure inflation returns sustainably to the 2 percent target mid-point over the medium term.

The Committee judges that gradually removing monetary stimulus is appropriate to return inflation to the 2 percent target mid-point while supporting growth and employment. This decision reduces the risk that the OCR needs to increase by more later. Future policy decisions will depend on the Committee's judgement of the balance of risks to medium-term inflation.

Anna Breman

Anna Breman
Governor

Figure i.1
Official Cash Rate (OCR)
(quarterly average)



Source: RBNZ estimates.

Monetary Policy Framework

The Monetary Policy Committee operates and makes decisions under the Monetary Policy Framework that comprises the following key components:

- the *Remit*;
- the *Charter*;
- the *Code of Conduct*; and
- the monetary policy strategy.

The corresponding documents to these components and additional information can be accessed on our website under the Monetary Policy Framework.

Report and supporting notes published at:

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The projections were finalised on 26 August 2026. The Official Cash Rate (OCR) projection incorporates an outlook for monetary policy that is consistent with the MPC's monetary policy assessment, which was finalised on 2 September 2026.

Chapter 01

Summary record of meeting

Abel Tasman National Park. Photo: Zhongchen Song

Chapter 1.
Summary record of meeting

Annual consumers price index inflation is above the Monetary Policy Committee's 1 to 3 percent target range. Inflation increased to 4.1 percent in the June 2026 quarter, largely driven by higher fuel and related prices due to the Middle East conflict. The Committee is setting monetary policy to return inflation to 2 percent by late 2027. Economic activity is expected to strengthen and broaden.

Inflation is forecast to fall to 2 percent by late 2027

The Committee expects inflation to remain elevated this year before returning to the target band by mid-2027 and reaching the 2 percent mid-point later next year. Excluding vehicle fuels, annual CPI inflation decreased to 2.9 percent in the June quarter. Most measures of core inflation are within the 1 to 3 percent target band.

As the effects of higher fuel prices drop out of the annual CPI calculation, spare capacity and the gradual removal of monetary stimulus are expected to support inflation returning to the 2 percent target mid-point.

Forward-looking indicators of inflation and spare capacity are consistent with achieving the medium-term target. Longer-term inflation expectations remain near 2 percent, while most measures of one- and two-year-ahead inflation expectations have fallen since May. Expected wage growth is consistent with returning inflation to 2 percent.

Trading partner inflation has increased and export prices remain resilient

High and volatile energy and petrochemical-derived product prices have increased inflation in many of New Zealand's trading partners, increasing import prices. Global supply chains, refining capacity, and trade flows remain disrupted.

Despite recent geopolitical events, economic growth in New Zealand's trading partners has remained resilient and the outlook has improved. Continued demand and supply-side constraints in global food markets have resulted in elevated prices for New Zealand's commodity exports. This is partly offsetting higher import prices, and New Zealand's terms of trade are projected to resume their long-run upward trend.

New Zealand's economic recovery is resuming and expected to broaden

The Committee assessed that growth was lacklustre in the second quarter of 2026. The economic recovery is expected to have resumed in the third quarter, while remaining uneven across sectors and regions.

The Committee noted that economic conditions remain favourable for households and businesses exposed to the export sector, contributing to a recovery in business investment. Resilient trading-partner demand and strong export prices are supporting activity in the South Island and some North Island regions.

The Committee assessed that positive spillovers from the export sector into the broader economy have been limited. Households and businesses more exposed to the domestic economy continue to face challenging conditions.

Employment growth has not been sufficient to fully absorb new entrants into the labour market and unemployment is elevated, particularly in Auckland and Wellington and for youth and the long-term unemployed. Some households are moving to regions with stronger labour markets as part of this economic adjustment.

In some regions, job insecurity and falling real house prices may be contributing to precautionary behaviour. Household saving rates have increased and consumption growth remains weak. Strong growth in dwelling consents has not yet translated into residential construction nationwide.

Household consumption growth is expected to gradually strengthen. The labour market is expected to slowly improve, with employment growing and unemployment falling as the economy recovers. A pick up in real income growth and a modest recovery in house prices supported by past and current monetary stimulus is expected to strengthen household balance sheets, consumer confidence and spending. Improvements in the terms of trade from next year will also support national income growth over the forecast period.

On balance, the Committee assesses that spare capacity remains in the economy, particularly in the labour market. Looking forward, strength in the external sector and the effects of accommodative monetary policy will continue to support and broaden the recovery, absorbing spare capacity over the medium term.

Financial conditions have tightened in recent months

Domestic financial conditions have tightened. Higher wholesale interest rates have led to a comparable increase in bank mortgage and business lending rates and a small appreciation in the exchange rate, partly reflecting expectations of future OCR increases.

The Committee noted a more limited pass through of higher wholesale interest rates to term deposit rates, which is lowering the cost of new funding for banks. A greater pass through to deposit rates would be more consistent with the desired stance and transmission of monetary policy.

Members agreed that domestic financial stability continues to pose no material trade-off to its inflation objective.

Risks to global and domestic economic growth

The Committee discussed risks to the global outlook. There are significant risks to financial stability from the serviceability of public and private debt and ongoing fiscal deficits. Geopolitical instability also continues to present considerable risks. Uncertainties remain about the sustainability of various asset valuations, including for AI-related investments.

El Niño weather conditions do not necessarily imply that New Zealand will experience a drought. However, adverse global and local weather events can impact supply, posing upside risk to commodity and food prices. Although risks to the global economy remain heightened, the Committee expects global economic conditions to remain favourable for New Zealand's export-facing businesses over the medium term.

Members discussed risks to New Zealand's economic recovery. Consumption growth could be subdued if employment and house price growth remain weak, or if precautionary behaviour persists. If this were to occur, the recovery could be weaker and current unevenness could continue. Alternatively, consumption growth could be stronger and absorb spare capacity faster than currently anticipated.

Members highlighted that the real economy is showing signs of adjusting to a range of structural changes, but transitions can be slow and contribute to divergences across sectors and regions. It was noted that monetary policy cannot influence the ultimate path of these real adjustments.

The Committee remains vigilant to inflation risks

The outlook for medium-term inflationary pressures depends on price-setting behaviour and the speed with which spare capacity in the economy is absorbed. Recent elevated inflation is expected to continue to impact price setting, keeping inflation more persistent than otherwise.

Hayley Gourley, Karen Silk, Prasanna Gai and Anna Breman saw upside risks to inflation relative to the central projection. These members observed that more persistence in energy and petrochemical prices could raise near-term inflation risks, impact price-setting behaviour, and lead to more sticky inflation over the medium term. Price setting can be a front-loaded process, meaning businesses could raise domestic prices more than import costs warrant. They also noted that high administered price inflation could continue. These factors increase the risk that monetary policy needs to lean against broader inflation pressures.

Paul Conway and Carl Hansen saw risks to inflation as balanced. These members shared concerns that high inflation could become embedded through price-setting behaviour. But weighed against this, they saw activity risks as skewed to the downside and noted that these could weigh on inflation. They highlighted the potential effects of weak house prices and precautionary behaviour, weakening growth in household spending.

All members agreed that downside risks to activity were significant and that the recovery could remain uneven. They also noted growth in activity may not flow through into additional employment as expected, particularly if businesses are relatively more focused on efficiency and technology investment in the short run.

Gradually removing monetary stimulus remains appropriate

The Committee discussed the monetary conditions required to return inflation sustainably to the 2 percent target mid-point.

When considering the policy response at this meeting, there was a clear consensus across the Committee. All members agreed that gradually removing monetary stimulus is consistent with achieving the medium-term inflation target, conditional on the outlook.

Members reflected on the potential trade-offs associated with a faster or slower monetary policy response. The Committee judged that its response balances containing inflationary pressures against the risk of holding the OCR and then having to raise it faster and to a higher level later.

All members agreed that the central projection for the OCR is appropriate. Conditional on the central economic outlook, members judged that the OCR may need to increase further. The Committee assessed that its monetary policy stance would guard against the effects of the oil price shock leading to persistently elevated price-setting behaviour, while supporting growth and employment.

However, the future OCR path is not pre-determined. The Committee's response to data is not mechanical, as it depends on its assessment of various factors that impact inflation. Currently, indicators of medium-term inflation are consistent with inflation returning to target.

The Committee decided by consensus to increase the OCR by 25 basis points to 2.75 percent

The Committee judged that increasing the OCR to 2.75 percent is appropriate to sustainably return inflation to the 2 percent target mid-point while avoiding unnecessary instability in output, employment, interest rates, and the exchange rate.

Future policy will depend on the Committee's judgement of the balance of risks to medium-term inflation. This approach allows the Committee to observe and assess the effects of reduced monetary stimulus.

On Wednesday 2 September, the Committee decided by consensus to increase the OCR by 25 basis points to 2.75 percent.

Attendees:

MPC members:

Anna Breman (Chairperson), Carl Hansen, Hayley Gourley, Karen Silk, Paul Conway, Prasanna Gai

Treasury Observer:

Struan Little

MPC Secretary:

Liz Kendall

Chapter 02

Economic assessment and monetary policy outlook

Tararua Ranges. Photo: Trent Lockyer

Chapter 2.
Economic assessment and monetary policy outlook

Key points

Inflation has increased, reflecting higher fuel prices due to the Middle East conflict. Annual consumers price index (CPI) inflation increased to 4.1 percent in the year to the June 2026 quarter, above the Monetary Policy Committee's 1 to 3 percent target range for inflation over the medium term. Annual CPI inflation excluding vehicle fuels decreased to 2.9 percent in the June 2026 quarter. The state of the conflict has been highly changeable, causing volatility in oil prices. Further volatility could materially affect the near-term inflation outlook.

The Middle East conflict has delayed the recovery in economic activity, but growth has likely resumed in the September 2026 quarter. Higher prices for fuel and other products affected by the conflict are reducing household disposable incomes. Lower real incomes, elevated uncertainty, and declining house prices are reducing domestic spending and growth. Economic growth was likely around zero in the June 2026 quarter. The unemployment rate has increased further, as growth in labour supply has exceeded growth in labour demand. However, the strong performance of a range of New Zealand's major exporting industries is supporting economic activity. GDP growth had been increasing prior to the conflict, and there were signs that spare capacity in the economy was beginning to be absorbed. Growth is estimated to have resumed in the September 2026 quarter and is projected to recover further as cost pressures ease and uncertainty declines.

Inflation is expected to return to target next year. Conditional on our central forecast for global oil prices, we project that inflation has peaked. There is significant spare capacity in the domestic economy. Most measures of core inflation, which attempt to look through volatility, remain within the target range, albeit above the 2 percent target mid-point. Almost all measures of inflation expectations declined in the September 2026 quarter, and longer-term inflation expectations remain near but slightly above 2 percent. Inflation is projected to return within the target range in the June 2027 quarter, as the initial increase in fuel prices drops out of the annual calculation, and to near the 2 percent target mid-point in late 2027.

Nevertheless, inflationary pressure has increased since the onset of the conflict. Firms' non-labour costs have increased materially over recent years, and the Middle East conflict is contributing to further cost pressures. While oil prices have declined from their peaks in March, they are likely to remain higher than before the conflict over the medium term. Significant spare capacity in the domestic economy is limiting firms' ability to pass on higher costs and dampening growth in labour costs. However, if spare capacity in the economy is absorbed quickly, this could delay the return of underlying inflation, and ultimately headline inflation, to the 2 percent target mid-point.

Gradual removal of monetary stimulus will support the return of inflation to the 2 percent target mid-point over the medium term. A higher OCR will lean against inflationary pressures, enabling a sustainable economic recovery while ensuring that higher near-term inflation does not become embedded in price- and wage-setting behaviour. Conditional on the central economic outlook, we project that the OCR may need to increase further. The outlook for monetary policy will evolve in response to the economic outlook over time.

Economic assessment

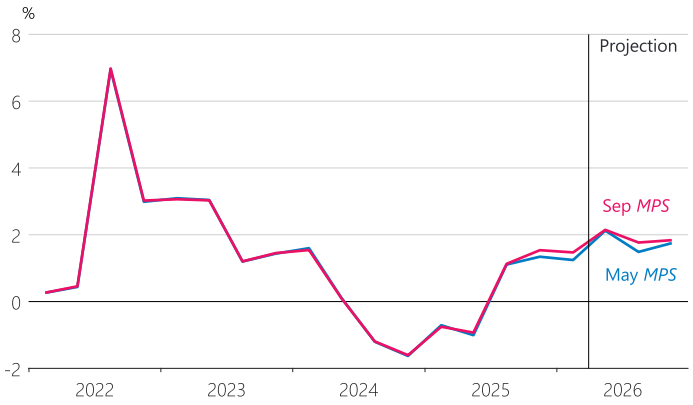
GDP growth was increasing prior to the Middle East conflict

Real production GDP increased by 1.5 percent in the year to the March 2026 quarter, slightly stronger than expected at the time of the May *Statement* (figure 2.1). Growth was supported by continued expansions in services and primary industries, while construction activity continued to contract. Lower interest rates were supporting a recovery in domestic demand, while growth in overseas demand was supporting activity in the tourism and primary sectors. There were signs that increasing economic growth was translating to some reduction in spare capacity in the March 2026 quarter (see chapter 4.2 of the May 2026 *Statement*).

Figure 2.1

Production GDP growth

(annual)

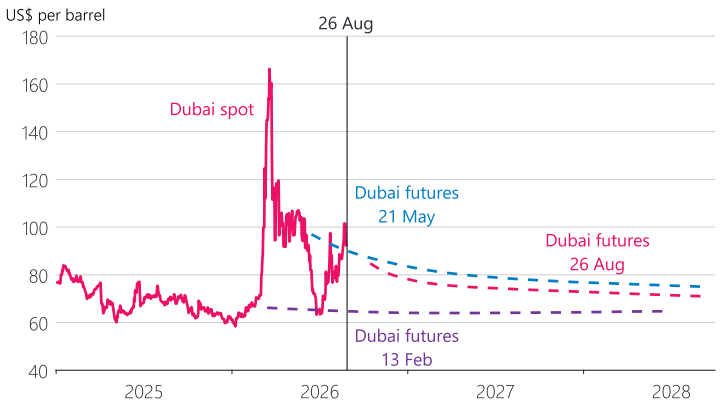


Source: Stats NZ, RBNZ estimates.

Figure 2.2

Dubai oil prices

(daily)



Source: Bloomberg, LSEG.

The Middle East conflict has disrupted global markets for energy and other products

International oil prices are materially higher than at the start of 2026, reflecting past, current, and expected ongoing disruptions to oil supply (figure 2.2). The outbreak of conflict in the Middle East in late February and the subsequent closure of the Strait of Hormuz led to a sharp increase in global prices for energy products, including oil. Prices for other petrochemical products, such as plastics and fertilisers, also increased. Global oil and related prices have been volatile, reflecting developments in the conflict and other factors (see chapter 3). At present, oil prices are materially lower than their peaks in March, and slightly lower than assumed in the May *Statement*, but higher than their levels in late June and early July. Refining margins have also increased since late June and remain well above pre-conflict levels, contributing to higher prices for refined fuels like petrol, diesel, and jet fuel.

Futures pricing is consistent with oil prices easing slightly over coming months, but remaining above pre-conflict levels over the medium term. The conflict has caused damage to oil production facilities and decreased global inventories. Global strategic oil reserves have been drawn down, and the need to rebuild reserves may support prices for some time. The outlook for the Middle East conflict and future oil supply is highly uncertain. Outcomes could diverge significantly from futures pricing over time, with material implications for growth and inflation in New Zealand (see box A in the May 2026 *Statement*).

Global inflation has increased, while global growth has been resilient

Growth in New Zealand's trading partners has been resilient in the face of the Middle East conflict (figure 2.3). Annual GDP growth in our trading partners increased from 3.2 percent in the December 2025 quarter to 3.5 percent in the March 2026 quarter. While lower real incomes and higher uncertainty are dampening demand in many of our trading partners, strong AI-related investment demand and fiscal policy responses have supported growth in some economies. GDP growth has been very strong in developed Asian economies, driven by strong growth in exports of AI-related products. Consensus forecasts for trading-partner GDP growth in 2026 were revised down following the start of the Middle East conflict, but have since retraced this decline.

Trading-partner inflation has increased, reflecting higher global energy prices. Annual CPI inflation in our trading partners increased from 2.2 percent in the March 2026 quarter to 2.7 percent in the June 2026 quarter. Consensus forecasts for annual trading-partner inflation have been revised from 2 percent in 2026 and 2027 at the start of this year, to 2.7 percent and 2.2 percent respectively (figure 2.4). Measures of core inflation have been broadly stable across trading partners, but prices for many goods and services are likely to face upward pressure as higher energy costs are passed through global supply chains.

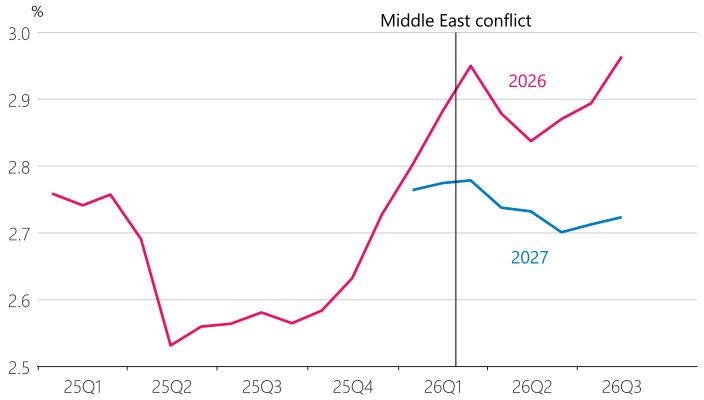
New Zealand's terms of trade have deteriorated

Higher prices for imported fuel, and to a lesser extent other goods, are weighing on New Zealand's terms of trade (figure 2.5). In addition to higher fuel costs, New Zealand businesses are facing higher prices for fertiliser, petrochemicals, and petrochemical-derived products such as plastics. More generally, higher inflation in New Zealand's trading partners is expected to contribute to higher prices for a wide range of goods and services that New Zealand imports. If the depreciation in the New Zealand dollar exchange rate since the start of the conflict is sustained, this will also contribute to higher prices for imports in New Zealand dollar terms.

Figure 2.3

Consensus forecasts for global GDP growth

(annual, weighted by New Zealand trade)



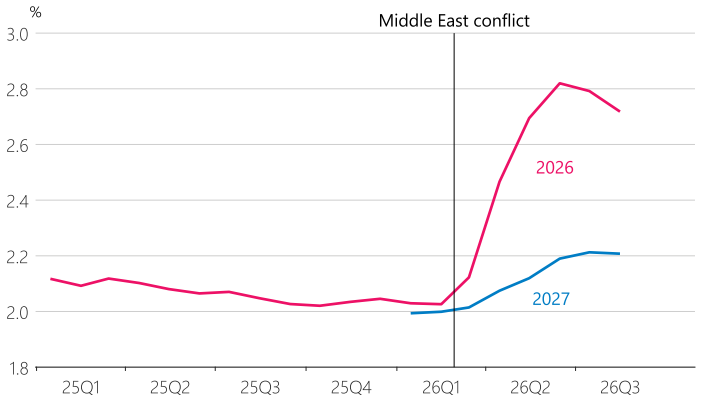
Source: Stats NZ, Haver Analytics, Bloomberg, RBNZ estimates.

Note: Global GDP growth is based on 16 of New Zealand's largest trading partners. 2026 shows forecasters' prediction made in each quarter for annual GDP growth in the year to December 2026. 2027 shows forecasters' prediction made in each quarter for annual GDP growth in the year to December 2027.

Figure 2.4

Consensus forecasts for global CPI inflation

(annual, weighted by New Zealand trade)



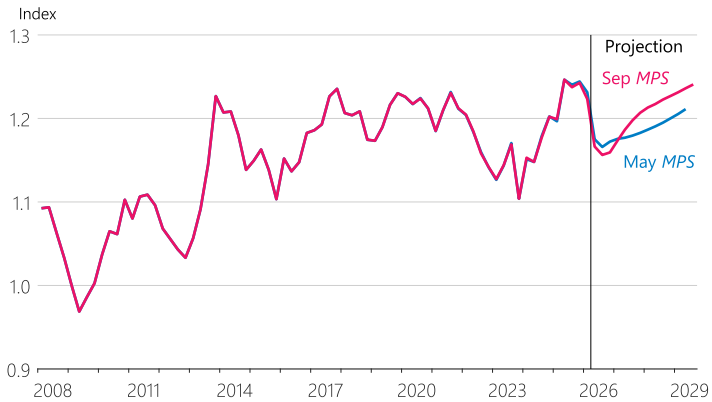
Source: Stats NZ, Haver Analytics, Bloomberg, RBNZ estimates.

Note: Global CPI inflation is based on 17 of New Zealand's largest trading partners. 2026 shows forecasters' prediction made in each quarter for annual inflation in the year to December 2026. 2027 shows forecasters' prediction made in each quarter for annual inflation in the year to December 2027.

Figure 2.5

New Zealand terms of trade

(quarterly average)



Source: Stats NZ, RBNZ estimates.

Prices for some of New Zealand's key commodity exports have been elevated. High global commodity prices for meat, dairy, and aluminium have supported New Zealand exporter incomes, although international dairy auction prices have declined over recent months. Weaker global demand and higher global supply for some products may put downward pressure on New Zealand's export prices over the medium term. However, higher fertiliser and feed prices may provide some support to dairy and meat prices, and the weaker New Zealand dollar is supporting exporter revenues.

The terms of trade are assumed to improve over the medium term. Compared to the May *Statement*, our assumption for import prices is lower over the medium term, reflecting a lower outlook for oil prices, which reduces upward pressure on other import prices. This results in a faster improvement in the terms of trade, particularly over 2027.

Financial conditions have tightened since the Middle East conflict began

Interest rates in advanced economies have increased since the Middle East conflict began. Market expectations for policy rates have shifted materially higher in advanced economies since February. The Reserve Bank of Australia and the European Central Bank have increased policy interest rates since the conflict began, although in Australia this mostly reflects domestic inflationary pressure persisting from prior to the Middle East conflict. Financial market pricing indicates that the US Federal Reserve, the Reserve Bank of Australia, the European Central Bank, the Bank of England, and the Bank of Canada are expected to increase their policy rates over coming months. Interest rates on long-term government bonds have continued to increase since the May *Statement*.

New Zealand interest rates have also increased since the conflict. Compared to just prior to the conflict, market pricing for the OCR has shifted higher by around 35 basis points to be around 3 percent by the end of 2026. Longer-term interest rates, such as those on New Zealand government bonds, have also increased, consistent with global increases. Retail lending and deposit rates have also increased since the conflict began (see chapter 3). The New Zealand dollar has depreciated on a trade-weighted basis since the conflict, although it is at a similar level to the time of the May *Statement*. This depreciation is consistent with changes in interest rate differentials, with New Zealand interest rates increasing by less than US interest rates at most terms since the start of the conflict.

The conflict is materially affecting inflation and growth in New Zealand

The Middle East conflict is affecting inflationary pressure in New Zealand through a range of trade, financial market, and uncertainty channels (see chapter 4.1 of the May 2026 *Statement*). We classify the effects of the conflict on inflation into four broad categories:

- first-round direct effects,
- first-round indirect effects,
- second-round demand effects, and
- second-round price effects (see chapter 4.1).

The effect of the Middle East conflict on medium-term inflationary pressure depends on the balance between inflationary second-round price effects and disinflationary second-round demand effects.

First-round direct and indirect effects are contributing to higher inflation

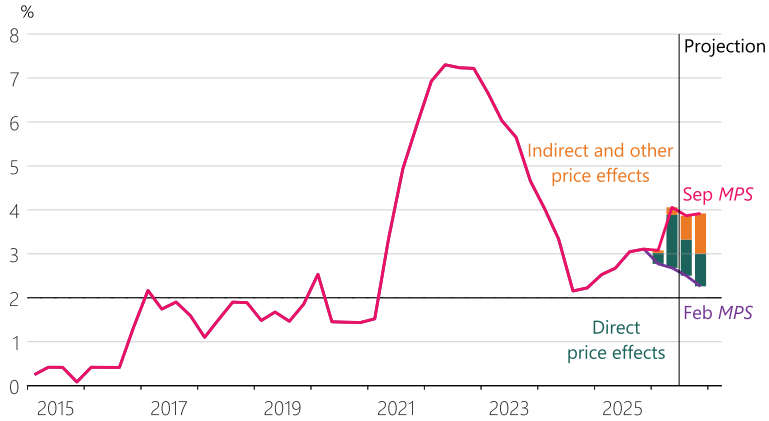
The Middle East conflict has resulted in higher CPI inflation in New Zealand. Annual CPI inflation increased to 4.1 percent in the June 2026 quarter from 3.1 percent in the March 2026 quarter, reflecting the direct contribution of higher petrol and diesel prices (figure 2.6). In contrast, annual CPI inflation excluding vehicle fuels decreased to 2.9 percent in the June 2026 quarter from 3.2 percent in the March 2026 quarter. Annual CPI inflation is expected to fall slightly in the second half of 2026. The direct contribution of higher petrol and diesel prices is expected to reduce, reflecting lower global oil prices. However, this is partially offset by increasing contributions from indirect effects as higher costs for fuel and other affected inputs are passed on to other consumer prices. Relative to the May *Statement*, inflation was slightly lower than expected in the June 2026 quarter and is projected to be slightly lower over the rest of 2026, reflecting smaller direct effects due to lower fuel prices.

Tradables inflation increased in the June 2026 quarter because of higher retail fuel prices. Annual tradables inflation increased to 4.9 percent in the June 2026 quarter from 2.5 percent in the March 2026 quarter (figure 2.7). Tradables inflation excluding fuel declined to 2.1 percent in the June 2026 quarter from 2.7 percent in the March 2026 quarter. Annual tradables inflation is assumed to fall in the September 2026 quarter, as fuel prices have declined from their peaks. In contrast, annual tradables inflation excluding fuel is assumed to increase over the remainder of the year, as significant indirect effects increase other tradables prices, including international travel and food. The depreciation in the New Zealand dollar exchange rate over the past two years is also increasing import costs, contributing to higher tradables inflation than otherwise.

Figure 2.6

CPI inflation contributions

(annual)

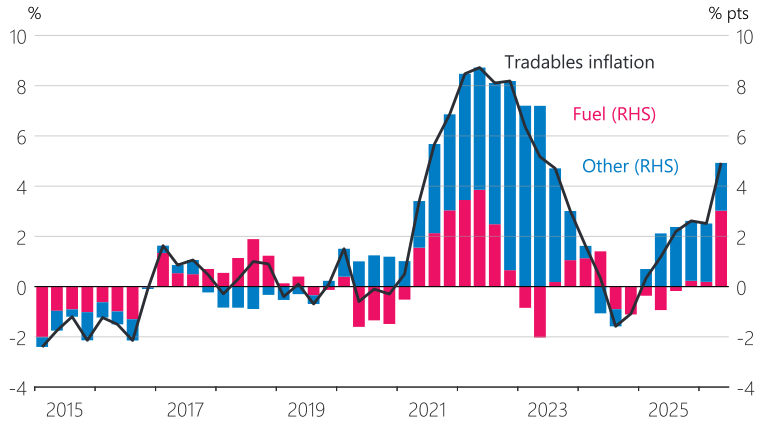


Source: Stats NZ, RBNZ estimates.

Figure 2.7

Tradables inflation contributions

(annual)



Source: Stats NZ, RBNZ estimates.

We expect annual non-tradables inflation to increase slightly in the second half of 2026 due to indirect effects from the Middle East conflict. Annual non-tradables inflation declined to 3.4 percent in the June 2026 quarter, as expected in the May *Statement*. Elevated non-tradables inflation mostly reflects high administered price and energy inflation.[1] Annual non-tradables inflation is expected to increase slightly over the second half of this year, due to the indirect effect of higher fuel prices on items such as domestic airfares, road transport, and house construction.

The Middle East conflict is slowing the economic recovery

Higher fuel prices and uncertainty are dampening household spending. Higher fuel prices are reducing real household disposable incomes. While some households are maintaining spending by drawing on savings, others are cutting back on fuel and other spending. Higher uncertainty and higher long-term interest rates following the conflict are dampening house prices, reducing household wealth and therefore spending. How household consumption evolves over the medium term is a key uncertainty underlying our economic projections (see chapter 4.2). Residential investment is also likely to recover more slowly as a result of the Middle East conflict, as higher input costs for diesel and other materials, lower house prices, and increased uncertainty reduce the incentive to build.

Strong growth in export volumes is supporting economic activity. Service export volumes have grown strongly over the past year, increasing 15.6 percent in the year to the March 2026 quarter. This reflects strong growth in the tourism sector, and in a broad range of other services exports. Our projections assume a modest decline in service export volumes in the short term as a result of the Middle East conflict disrupting travel and increasing international airfares, but this is highly uncertain. Monthly merchandise trade data suggest that goods export volumes grew strongly in the June 2026 quarter, consistent with strong production of dairy, meat, horticulture, and other export products. The strong performance of many exporting sectors has also supported a recovery in business investment, although high uncertainty may cause some firms to delay or cancel investment plans.

The current El Niño weather pattern is likely to develop into one of the strongest in recent history over coming months. This increases the risk of dry conditions in parts of New Zealand, which could affect agricultural production, although weather outcomes are uncertain and are influenced by many factors (see box A).

1 Administered prices are based on the 'central and local government charges' series produced by Stats NZ. It incorporates a wide range of prices set or heavily influenced by central or local government. Stats NZ updated the methodology for the 'central and local government charges' series in the March 2026 quarter to better reflect current government charges, most notably removing electricity prices. Stats NZ currently publishes both the old series and the updated series.

Box A
El Niño, droughts, and the New Zealand economy

El Niño is a climate phenomenon characterised by unusually warm sea surface temperatures in parts of the Pacific. Earth Sciences New Zealand has confirmed the recent emergence of El Niño conditions. Through the coming spring and summer, the north and east of New Zealand are expected to be drier than usual, while some southern and western parts of the South Island are expected be wetter than normal. The association of El Niño with dry weather conditions in the northern and eastern parts of the country has raised concerns about an increased risk of drought.

The historical relationship between El Niño conditions and drought in New Zealand is weak. Figure A.1 shows the Southern Oscillation Index (SOI) with a timeline of droughts of varying severity in New Zealand. The SOI measures the air pressure difference between Tahiti and Darwin, Australia. Sustained periods of negative values for the SOI coincide with warmer-than-usual ocean waters across the eastern Pacific, typical of an El Niño episode. On the other hand, a prolonged positive phase of the SOI indicates the La Niña climatic pattern. Importantly, the SOI has historically been a poor predictor of drought in New Zealand. While the severe 1997–98 drought coincided with a strong El Niño episode, other major droughts occurred during La Niña conditions or when the SOI was neutral.

Evidence on the overall impact of El Niño on economic growth and inflation in New Zealand is inconclusive.[2] There is also no strong empirical evidence that El Niño conditions are consistently associated with droughts in New Zealand, or any other identifiable indirect effects through weather conditions in other affected countries.

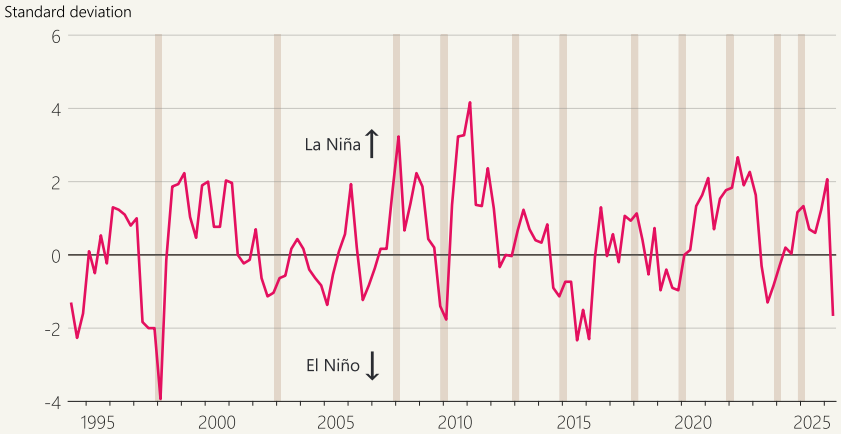
Droughts tend to decrease economic activity and increase prices. Forthcoming Reserve Bank research by Chipeniuk, Jacob and Turnip (2026) examines the transmission of drought shocks in New Zealand, building on earlier work on effects of weather shocks.[3] The study finds that a drought shock, represented by an increase in soil dryness, pushes down economic activity temporarily and lifts some consumer prices. A drought acts as an adverse supply shock, reducing production and increasing prices of affected goods.

To the extent that El Niño may increase the likelihood of a drought in parts of New Zealand, it may increase the risk of higher inflation and weaker economic growth. However, this link has been difficult to establish empirically. The Reserve Bank will continue to monitor weather conditions as El Niño develops.

Figure A.1

Droughts in New Zealand and the Southern Oscillation Index

(quarterly average, deviation from seasonal norm)



Source: National Centers for Environmental Information, National Oceanic and Atmospheric Administration, Local and central government agencies, RBNZ estimates.

Note: The vertical bars highlight summers identified as drought periods by local or central government agencies.

2 See Bloor and Matheson (2010) and Cashin et al. (2017).

3 See Kamber et al. (2013), Drying out: Investigating the economic effects of drought in New Zealand; and Buckle et al. (2007).

We assume that the level of GDP was unchanged in the June 2026 quarter. Most timely indicators of economic growth weakened in the June 2026 quarter, including the Performance of Manufacturing and Performance of Services indices (PMI and PSI), real electronic card transactions, traffic volumes, and house sales. The Reserve Bank's GDP nowcasting model, Kiwi-GDP, incorporates information from these data and a broad range of other indicators. It suggests that GDP growth was about 0.2 percent in the June 2026 quarter.

We expect the economic recovery to have resumed in the September 2026 quarter. While still elevated, retail fuel prices have fallen materially from their peaks in the June 2026 quarter. Most timely indicators of economic activity, including the PMI and the PSI, point to stronger growth over the months of June and July, although these data may not capture the effects of higher retail fuel prices since late July. Measures of business and consumer confidence have recovered their initial falls following the start of the conflict. We forecast GDP to grow 0.5 percent in the September 2026 quarter. Kiwi-GDP currently forecasts a stronger growth rate, but is estimated on limited data at this stage in the quarter.

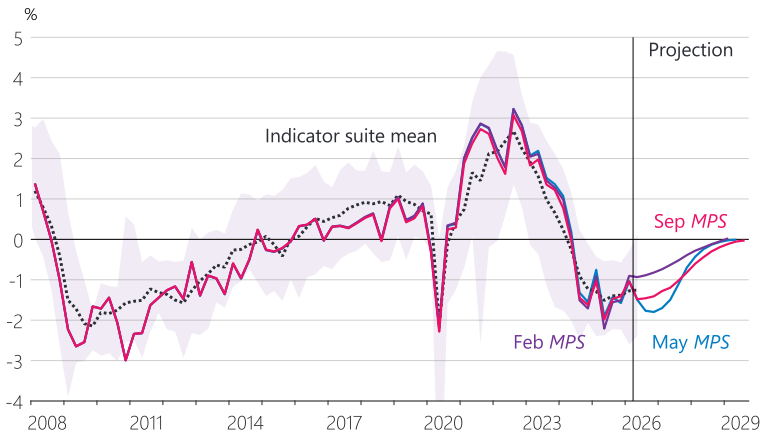
There is significant spare capacity in the domestic economy

We expect spare capacity in the economy to linger over the coming year (figure 2.8). The Middle East conflict has delayed the economic recovery, which will result in spare capacity in the economy lingering for longer than otherwise. We expect the output gap to average -1.4 percent over 2026, compared to -1.5 percent in 2025. The output gap is forecast to be less negative this year compared to the May *Statement,* consistent with lower oil and fuel prices than assumed in May. The output gap is projected to recover from next year as the economic recovery builds, supported by lower inflation, stronger real income growth, and reducing uncertainty.

Figure 2.8

Output gap and indicator suite

(share of potential GDP)



Source: NZIER, MBIE, Stats NZ, RBNZ estimates.

Note: The shaded area shows the range of values of indicators in the suite.

The New Zealand economy's potential growth rate remains low, but is increasing. Over recent years, slow population growth, low investment, and weak productivity growth have all contributed to low potential output growth. This constrains the rate at which the economy can grow without contributing to inflationary pressure. We estimate that annual potential growth has increased to 1.7 percent in 2026 from 1.1 percent in 2025, and will continue to gradually increase over the medium term. This reflects a gradual increase in net immigration, a cyclical recovery in investment, and an assumption that total factor productivity growth increases towards its average in the years prior to the COVID-19 pandemic.

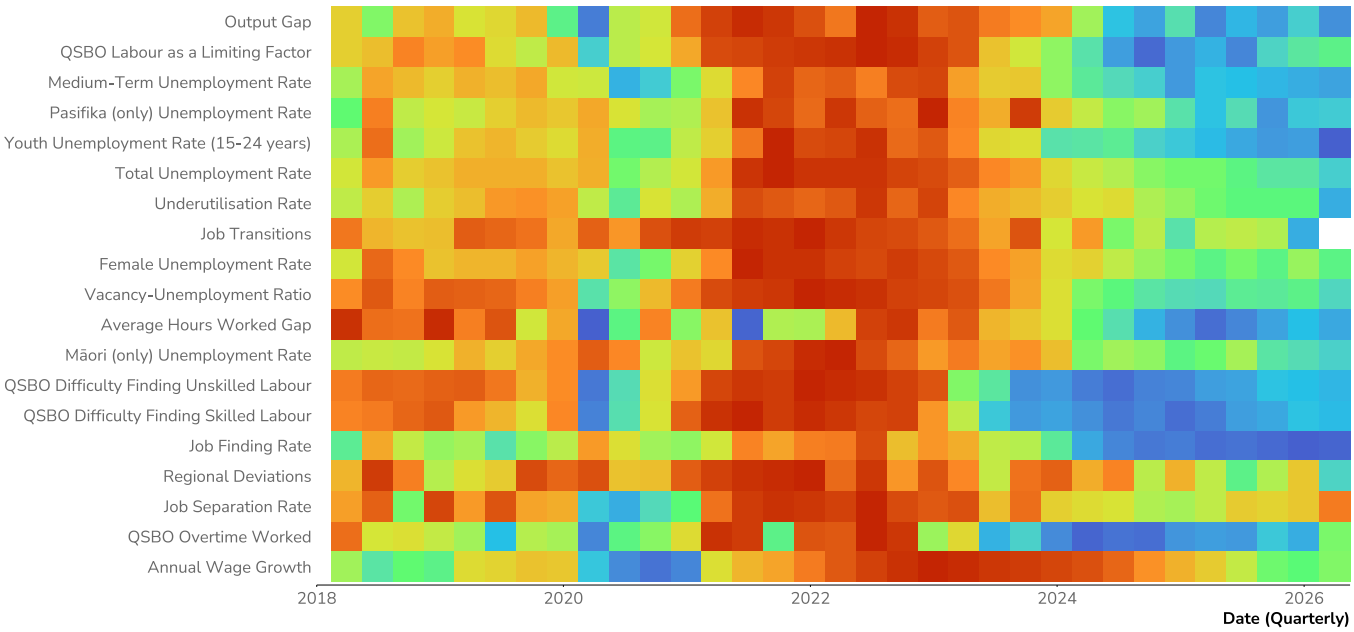
Spare capacity in the labour market has increased further. Spare capacity in the labour market increased further in the June 2026 quarter, with the unemployment rate increasing to 5.6 percent. Most measures of labour market tightness remain at levels consistent with substantial spare capacity (figure 2.9). Over the past year, labour demand has been increasing as economic activity has recovered, but employment growth has been insufficient to absorb growth in the supply of labour. While employment grew by 1.2 percent in the year to the June 2026 quarter, the labour force grew by 1.6 percent over the same period, reflecting both population growth and a higher labour force participation rate. Total hours worked declined slightly in the June 2026 quarter after several quarters of strong growth, consistent with slower economic growth dampening labour demand in the quarter.

The share of workers moving from unemployment to employment remains historically low. While the share of workers becoming unemployed is relatively low (the job separation rate), the very low share of unemployed people finding employment (the job finding rate) is contributing to higher youth unemployment and longer spells of unemployment. The unemployment rate for people aged 15 to 24 years has increased to a similar level to following the Global Financial Crisis, while the share of the labour force unemployed for a year or longer is around its highest levels since 2000. The ratio of job vacancies to unemployment remains low, at around half of its pre-COVID-19 level. In contrast, some other indicators of labour market spare capacity have begun to tighten, with firms in the Quarterly Survey of Business Opinion reporting that labour is becoming a bigger constraint on production, and that skilled labour is becoming more difficult to find.

Figure 2.9

Labour market indicators

Fill colour shows the standardised value for each variable compared to the weakest, median & strongest since 2000.



Sorted by rank correlation with output gap, top (highest) to bottom (lowest).

Source: Stats NZ, NZIER, MBIE, RBNZ estimates.

Note: See Ball (2024), Assessing and communicating labour market indicators of inflationary pressure.

Unemployment rates are higher in the North Island than in the South Island (figure 2.10). Labour market conditions have been stronger in the South Island, consistent with larger exposure to strong-performing export industries.

We project spare capacity in the labour market to be absorbed as the economic recovery resumes. Increasing GDP growth is assumed to contribute to stronger employment growth and lower unemployment, although the unemployment rate is projected to remain above 5 percent until 2028 (figure 2.11).

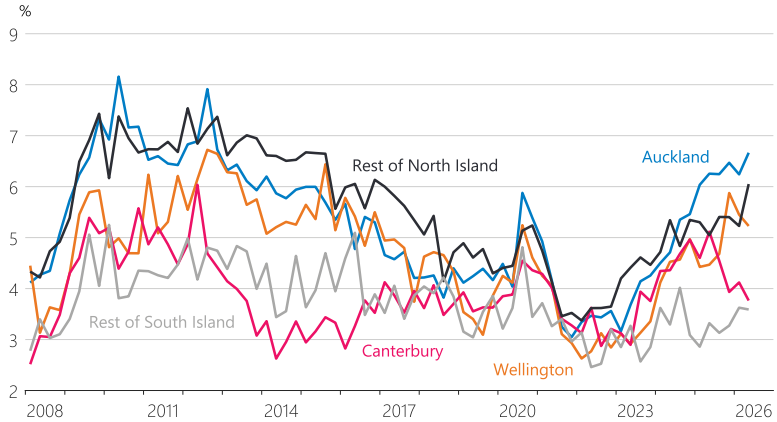
Spare capacity will moderate second-round price effects

Spare capacity in the labour market is limiting wage growth. Nominal wage inflation has declined as the labour market has weakened (figure 2.12). Annual private sector wage inflation was 2.0 percent in the June 2026 quarter, consistent with underlying inflation converging to the 2 percent target mid-point over the medium term. Annual public sector wage growth has been declining and was 1.7 percent in the June quarter. Higher CPI inflation means that real wages are falling (see chapter 4.2). Some workers will attempt to bargain for higher wages in response to higher inflation. However, significant spare capacity in the labour market and squeezed business margins due to the Middle East conflict are limiting workers' bargaining power. Consistent with this, firms' expectations of wage growth have remained broadly stable. Wage inflation is projected to be slightly higher in the near term compared to the May *Statement*, reflecting slightly stronger wage inflation than projected in the June 2026 quarter.

Figure 2.10

Unemployment rate by region

(unemployed people as a share of the labour force, seasonally adjusted)

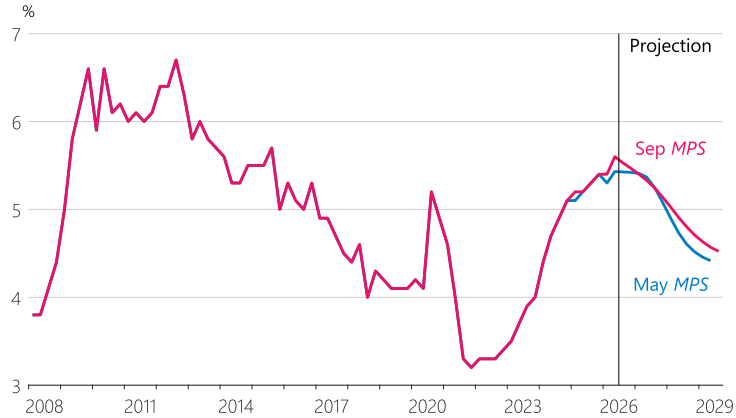


Source: Stats NZ, RBNZ estimates.

Figure 2.11

Unemployment rate

(unemployed people as a share of the labour force, seasonally adjusted)

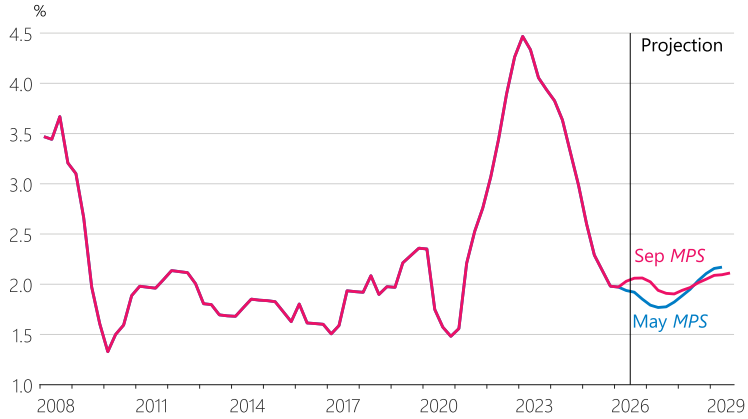


Source: Stats NZ, RBNZ estimates.

Figure 2.12

Private sector LCI wage inflation

(annual)



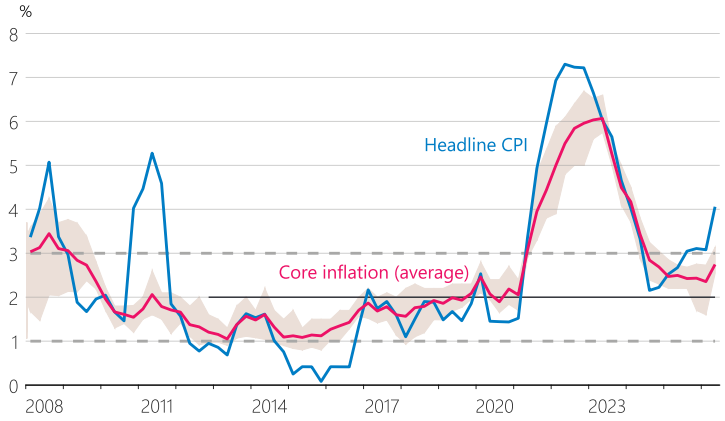
Source: Stats NZ, RBNZ estimates.

Measures of core inflation are above the 2 percent target mid-point, but all except one remain within the target range (figure 2.13). Movements in the five main core measures we monitor were more variable than usual in the June 2026 quarter, likely due to differences in how effectively they strip out the direct impact of higher fuel inflation (see chapter 4.1). Factor model and weighted median inflation increased relatively sharply in the quarter, while trimmed mean inflation increased slightly. In contrast, sectoral factor model inflation was unchanged, and CPI excluding food and energy inflation decreased slightly. While some core inflation measures likely overstate underlying inflation at present, all measures remain above the 2 percent target mid-point, indicating lingering inflationary pressure in the economy. Significant spare capacity and low growth in labour costs are reducing inflationary pressure, while still-elevated price-setting behaviour and high growth in non-labour costs are contributing to inflationary pressure (figure 2.14).

Figure 2.13

Headline and core inflation measures

(annual)

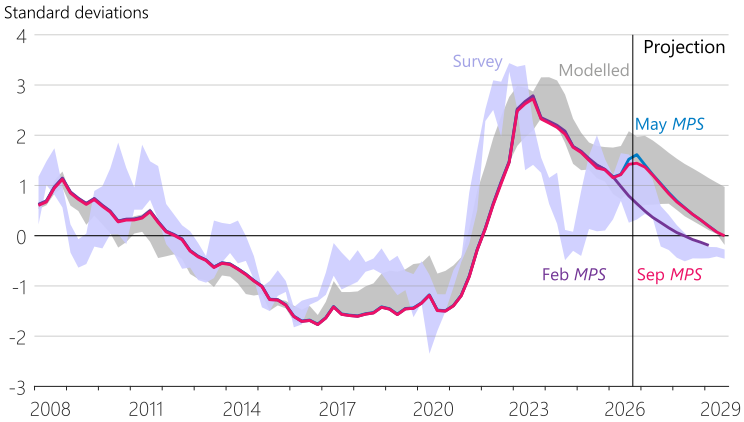


Source: Stats NZ, RBNZ estimates.

Note: The dashed lines represent the MPC's 1 to 3 percent target range for inflation over the medium term. The shaded area shows the range of core inflation measures. The core inflation measures include the sectoral factor model, factor model, trimmed mean (30%), weighted median, and CPI excluding food and energy.

Figure 2.14

Price-setting behaviour



Source: RBNZ estimates.

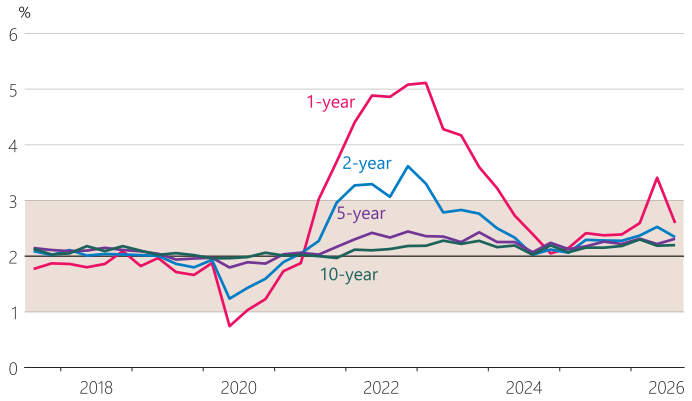
Note: Measures have been standardised over history to make them comparable given differences in historical averages and degrees of variability between measures. The vertical axis shows how many standard deviations away from its historical average each measure is, where zero indicates the historical average. The shaded areas show the range of modelled and survey measures. Modelled measures include adaptive measures of the form used in NZSIM with varying sensitivities to recent inflation, and a measure based on the simple average of headline inflation over the past 3 years. Survey measures include 1- and 2-year ahead inflation expectations from the Survey of Expectations, and 1-year ahead inflation expectations from the Household Expectations Survey. See chapter 4.1 in the August 2024 *Statement* for further discussion.

Business and professional forecaster expectations for inflation over the next one and two years decreased in the September 2026 quarter, following increases in the June 2026 quarter (figures 2.15 and 2.16). Longer-term measures of inflation expectations continued to be broadly stable. Household expectations for inflation reversed most of their increase last quarter at the two- and five-year horizons, but remained elevated for one-year ahead (figure 2.17). Inflation expectations remain at least slightly elevated relative to the 2 percent target mid-point across households, businesses, and professional forecasters, and across horizons.

Figure 2.15

Inflation expectations of professional forecasters and business leaders

(annual, years ahead)



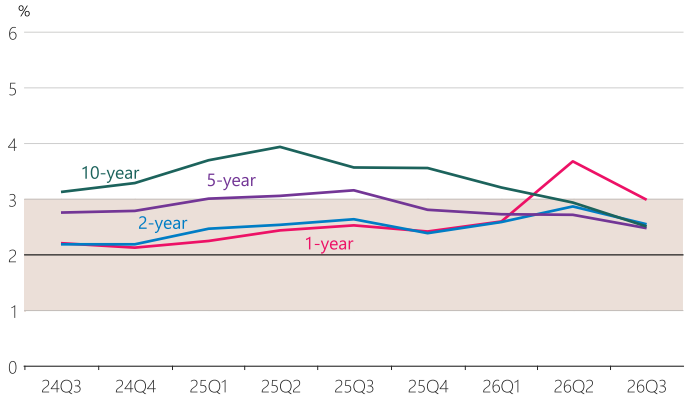
Source: RBNZ *Survey of Expectations*.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 2.16

Inflation expectations of businesses

(annual, years ahead)



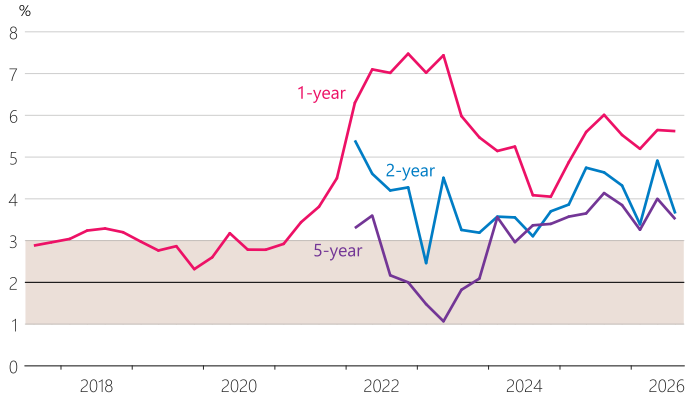
Source: RBNZ *Tara-ā-Umanga – Business Expectations Survey*.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 2.17

Inflation expectations of households

(annual, years ahead)



Source: RBNZ *Tara-ā-Whare – Household Expectations Survey*.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Inflation is projected to return to the target mid-point in 2027

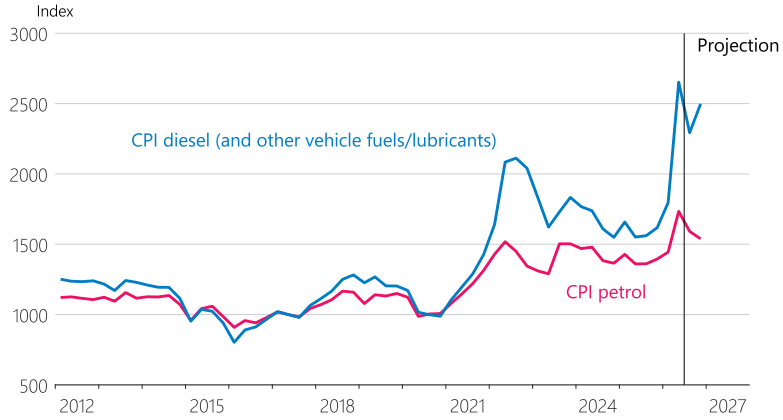
Retail fuel prices are projected to decline but remain higher than before the conflict. Retail petrol prices are projected to continue to decline over the second half of 2026, with diesel prices remaining elevated, in line with futures market pricing for refined fuels (figure 2.18). Retail fuel prices are expected to remain materially higher than before the Middle East conflict, particularly for diesel. Indirect price effects from the conflict are likely to depend mostly on diesel and jet fuel prices, which are relatively higher compared to pre-conflict levels than petrol prices.

Annual CPI inflation will fall when the initial increase in fuel prices drops out of the annual calculation. Even if fuel prices were to remain around current levels, annual inflation would fall once the June 2026 quarter increase drops out of the calculation. CPI inflation was 1.5 percent in the June 2026 quarter on a quarterly seasonally adjusted basis. We forecast that seasonally adjusted quarterly inflation will be higher than 0.5 percent until early 2027, before settling close to 0.5 percent over the remainder of the projection period.

Annual CPI inflation is projected to return to the 2 percent target mid-point next year (figure 2.19). Annual non-tradables inflation is forecast to decline from the second half of 2027 as the indirect effects of the Middle East conflict on non-tradables inflation fade. Spare capacity in the economy will continue to limit wage inflation and the extent to which costs can be passed on to prices. Tradables inflation is assumed to return to around historical average rates once fuel price increases drop out of the annual calculation.

Figure 2.18

CPI vehicle fuel prices

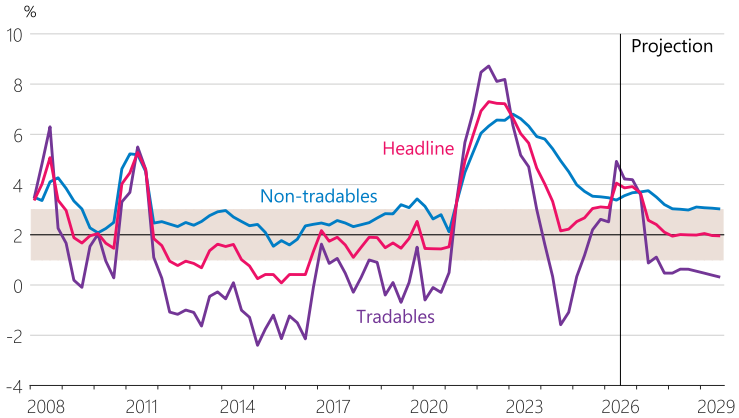


Source: Stats NZ, RBNZ estimates.

Figure 2.19

Headline, tradables, and non-tradables inflation

(annual)



Source: Stats NZ, RBNZ estimates.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Monetary policy outlook

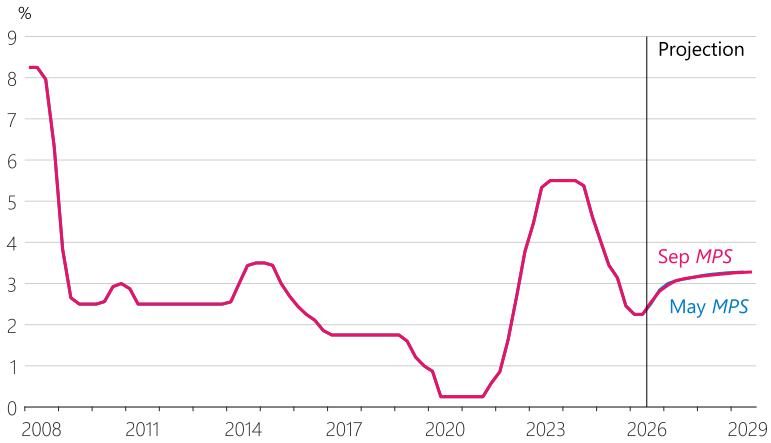
Conditional on the central economic outlook, we project that the OCR will increase further to ensure that inflation settles sustainably near the 2 percent target mid-point in the medium term (figure 2.20). A higher OCR will lean against inflationary pressures, enabling a sustainable economic recovery while ensuring that higher near-term inflation does not become embedded in price- and wage-setting behaviour. Consistent with the MPC's *Remit*, the projected path for the OCR returns inflation to 2 percent sustainably in the medium term, avoiding unnecessary instability in the economy (see box B).

The outlook for the OCR is similar to the May *Statement*. Global fuel prices have fallen faster than assumed in the May *Statement*, resulting in slightly less inflationary pressure in the very near term. Over the medium term, the path of the OCR will depend on price-setting behaviour and the speed at which spare capacity in the economy is absorbed.

Figure 2.20

OCR

(quarterly average)



Source: RBNZ estimates.

Box B
How should monetary policy respond to an oil supply shock based on the MPC's *Remit*?

The *Remit* embodies a 'flexible inflation targeting' approach. This approach recognises the importance of controlling inflation over time. It also acknowledges that monetary policy is limited in its ability to offset short-run volatility in inflation without resulting in high variability in interest rates and the economy, which reduce economic wellbeing. Flexible inflation targeting is the prevailing monetary policy framework across advanced economies globally. Although there have been changes to the degree and nature of flexibility over time, it has been the general framework for monetary policy in New Zealand since the first *Policy Targets Agreement* was signed in 1990.[4]

Tightening monetary policy to offset the first-round direct effects of an unanticipated adverse supply shock, such as a sharp increase in international oil prices, would not be consistent with the *Remit*. Three elements of the *Remit* reinforce this:

1. **The inflation target range is for future inflation over the medium term, not current inflation.** 'Medium term' is not defined in the *Remit*, because the exact time horizon at which it is desirable to return inflation to target varies based on economic circumstances. The Reserve Bank has historically interpreted the medium term to be the second half of its three-year forecast horizon.[5] By this time, initial direct effects of changes in oil prices will have mechanically dropped out of annual inflation calculations.
2. **The medium-term orientation is reinforced by instructing the MPC to '...discount disturbances to inflation that are expected to be temporary in a manner consistent with meeting the medium-term target.'** Again, the initial direct effects of an unanticipated oil price increase will mechanically drop out of annual inflation calculations after a year, and so should be discounted. This clause emphasises that the focus should instead be on any persistent effects that will affect inflation over the medium term.
3. **In pursuing its medium-term inflation target, the *Remit* requires the MPC to seek to avoid unnecessary instability in other economic variables.** This requirement applies to instability in output, employment, interest rates, and the exchange rate, reinforcing the flexible, medium-term nature of the inflation target.[6] It recognises that because monetary policy has its peak effect on inflation with a considerable lag, attempting to minimise short-run deviations of inflation from target would result in high variability in other economic variables, particularly in the face of supply shocks.

The MPC must respond to anticipated second-round effects of supply shocks. These *Remit* requirements do not mean that the MPC should not or will not adjust monetary policy settings in response to supply shocks. Supply shocks may place upward or downward pressure on medium-term inflation. This depends on their size, duration, breadth, and on their relative second-round price and demand effects. The MPC has increased the OCR sooner than projected prior to the Middle East conflict, in part reflecting their assessment that tightening sooner would lean against the risk of sustained inflationary pressure due to second-round price effects.

4 See the Reserve Bank's Monetary Policy Handbook and 2023 Advice on changes to the Monetary Policy Committee's Remit and Charter for more discussion.

5 See Bollard (2008), Flexibility and the limits to inflation targeting.

6 See Hunt (2004), Interpreting clause 4(b) of the *Policy Targets Agreement*: avoiding unnecessary instability in output, interest rates and the exchange rate.

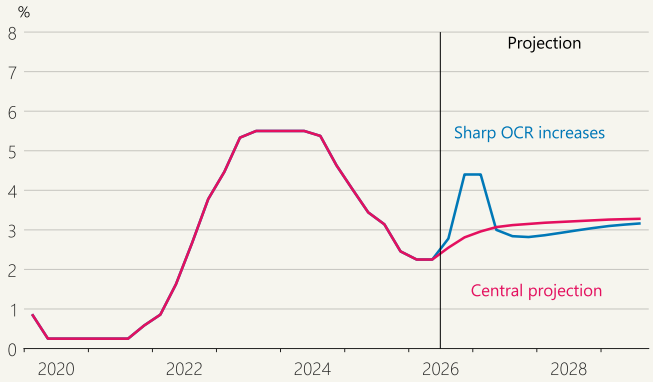
The MPC is setting monetary policy so that inflation returns sustainably to the 2 percent target mid-point. In our central projection, conditional on oil futures market pricing, annual CPI inflation declines to near 2 percent in the December 2027 quarter. While monetary policy settings can influence inflation at this horizon, the return to 2 percent also reflects the initial increase in fuel prices dropping out of the annual calculation and making a negative contribution to inflation as fuel prices decrease. A higher OCR helps to ensure that inflation settles sustainably at 2 percent, even as the anticipated negative contribution from lower fuel prices fades over the medium term. The MPC is focused on ensuring inflation returns to 2 percent at the time horizon at which monetary policy has its largest impact, and therefore achieving its inflation target while avoiding unnecessary instability in interest rates and the economy.

Bringing inflation back into the target range more quickly would require a sharp increase in the OCR, create unnecessary instability, and result in inflation undershooting 2 percent in the middle of the projection period. Figures B.1 to B.4 show a scenario where the MPC increases the OCR quickly, in order to return annual CPI inflation to within the 1 to 3 percent target range by the March 2027 quarter. Because monetary policy has only a small influence on inflation at this time horizon, the OCR must increase sharply, peaking at around 4.5 percent. If oil prices evolve as projected, inflation falls well below 2 percent in the middle of 2027, as higher fuel prices drop out of the annual calculation. The output gap declines further to almost -3 percent, and the unemployment rate increases to 5.9 percent. The OCR must be reduced rapidly over 2027 to return inflation to 2 percent, resulting in further instability in the economy.

Figure B.1

OCR

(quarterly average)

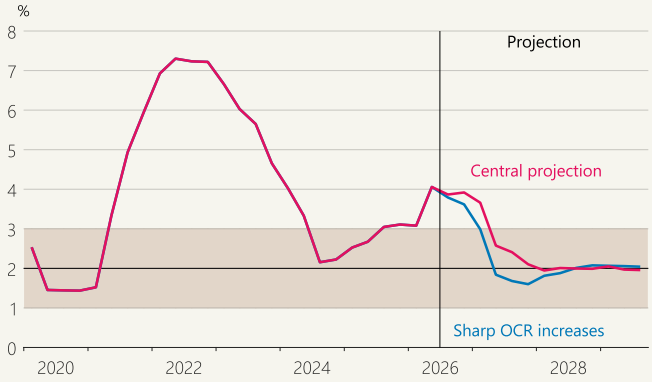


Source: RBNZ estimates.

Figure B.2

CPI inflation

(annual)



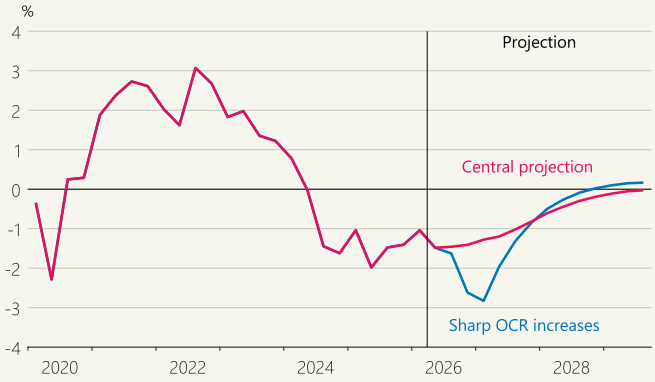
Source: Stats NZ, RBNZ estimates.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure B.3

Output gap

(share of potential)

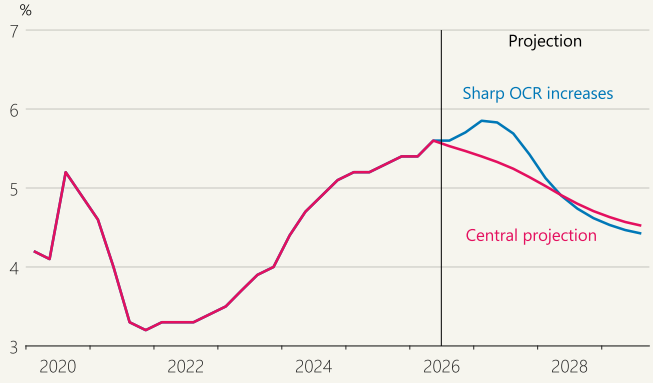


Source: Stats NZ, RBNZ estimates.

Figure B.4

Unemployment rate

(unemployed people as a share of the labour force, seasonally adjusted)



Source: Stats NZ, RBNZ estimates.

Chapter 03

Global economy and financial markets

Cape Reinga. Photo: Elvis Ludvich

Chapter 3.
Global economy and financial markets

Key points

Global growth has been resilient, supported by AI-related investment. New Zealand's trading-partner growth was strong in the March 2026 quarter, and the outlook has been revised slightly higher since the May *Statement*. This has been supported by AI-related investment, and demand for semiconductors and advanced electronics, boosting exports from developed Asian economies. Higher energy prices have been weighing on the global economy, but timely indicators of economic activity have rebounded since the early stages of the Middle East conflict.

Inflation developments across New Zealand's trading partners have been mixed. Headline inflation remains higher than before the Middle East conflict. However, core inflation rates have not yet shown a material rise among our key trading partners.

Higher energy prices remain a key risk to the global outlook. Crude oil prices are lower than at the time of the May *Statement* but are higher than before start of the Middle East conflict. Refined fuel prices and natural gas prices remain elevated, reflecting ongoing disruption to energy supply chains.

Central banks remain focused on the inflation risks from higher energy prices. Policy rate expectations are above pre-conflict levels across major advanced economies.

Global financial markets have remained broadly resilient. Equity prices have continued to increase, supported by earnings from companies exposed to AI-related investment. Government bond yields are higher than at the time of the May *Statement*, while the US dollar is broadly flat.

Domestic financial conditions have tightened since the Middle East conflict, and are tighter than at the time of the May *Statement*. Financial market participants expect the OCR to increase to around 3 percent by the end of 2026. Higher wholesale rates are being passed through to higher mortgage rates at terms between 6 months and 2 years. Six-month and 1-year term deposit rates have increased by less than equivalent-term wholesale interest rates, contributing to lower-than-otherwise bank funding costs.

Global economic conditions

Trading-partner growth has been resilient, supported by AI investment

Annual New Zealand trade-weighted global growth increased from 3.2 percent in the December 2025 quarter to 3.5 percent in the March 2026 quarter (figure 3.1). Growth was supported by AI-related investment and strong demand for semiconductors and advanced electronics. This has boosted activity in developed Asian economies closely integrated into global technology supply chains. Annual trading-partner growth is now expected to be 3.0 percent in 2026, up from 2.8 percent at the time of the May *Statement*. Although higher energy costs have weighed on the growth outlook in some economies, particularly developed markets outside Asia, this has been more than offset by stronger growth expectations in developed Asian economies. Growth is expected to slow to 2.7 percent in 2027, little changed from the May *Statement*.

Timely indicators of economic activity have recovered from earlier weakness. The global composite Purchasing Managers' Index is now little changed since the beginning of 2026, after falling following the outbreak of the Middle East conflict. Services activity has recovered from earlier declines, while manufacturing activity has continued to expand. Developed market economies have generally been more resilient than emerging market economies, reflecting stronger AI-related manufacturing demand and relatively smaller real household income losses from higher energy prices. In China, monthly economic indicators highlight a continued slowdown in the domestic economy which is being broadly offset by a strong external sector.

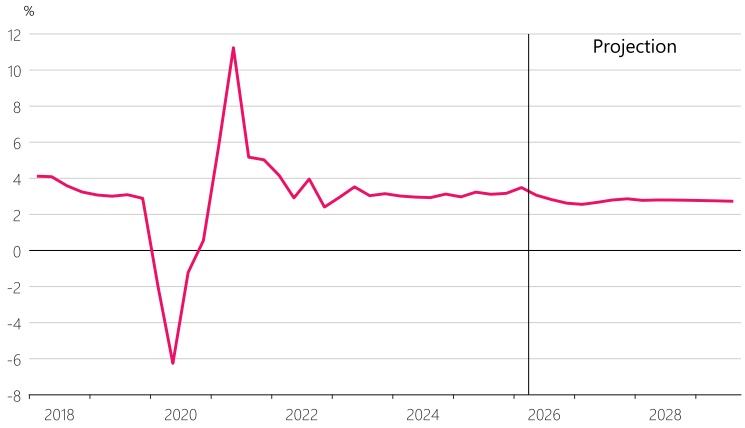
Global inflation has increased, though core inflation remains contained

The conflict in the Middle East and higher energy prices have lifted global inflation. New Zealand trade-weighted CPI inflation has increased from 2.1 percent in the December 2025 quarter to 2.7 percent in the June 2026 quarter, where it is broadly expected to remain over coming quarters (figure 3.2). In 2027, annual inflation is expected to be 2.2 percent, up from 2.0 percent before the Middle East conflict but little changed from the May *Statement*.

Figure 3.1

Trading-partner GDP growth

(annual)



Source: Stats NZ, Haver Analytics, Consensus Economics, Bloomberg, RBNZ estimates.

Note: The trading-partner aggregate is based on 16 of New Zealand's largest trading partners.

Figure 3.2

Trading-partner inflation

(annual)

Source: Stats NZ, Haver Analytics, Consensus Economics, Bloomberg, RBNZ estimates.

Note: The trading-partner aggregate is based on 17 of New Zealand's largest trading partners.

Measures of core inflation among our key trading partners have been contained. This suggests that higher energy prices are not leading to broad-based indirect or second-round price effects, so far. This could change over coming quarters as firms face higher input costs related to energy prices, which could be passed on to consumers. Sharp rises in the price of some electronic components are also increasingly feeding through to broader price increases for consumer electronics products.

Commodity prices remain elevated relative to pre-conflict levels

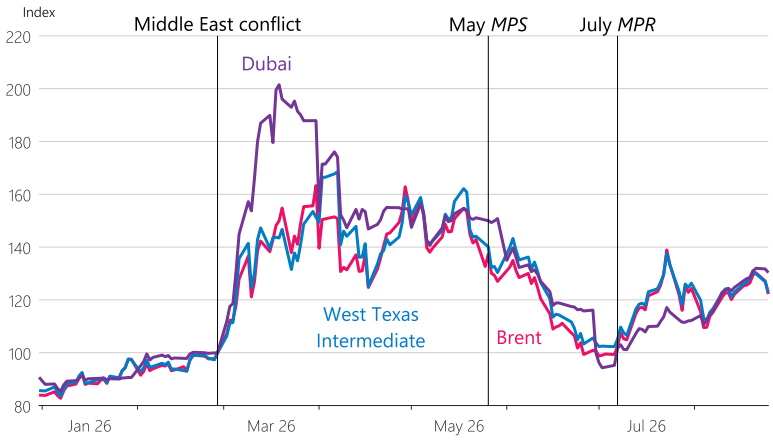
High energy and other commodity prices may increase medium-term inflation pressures. Dubai crude oil prices, the most relevant benchmark for New Zealand and many trading partners, are lower than at the time of the May *Statement* but have increased since the July Monetary Policy Review (figure 3.3). The gap has continued to widen between crude oil prices and the prices of refined products derived from it, such as diesel, gasoline, and jet fuel. This is because refinery capacity, inventories, and trade flows remain more constrained than crude oil supply. This is putting upward pressure on fuel prices paid by consumers and businesses. European and Asian natural gas prices have also continued to increase, reflecting renewed disruption to gas supply chains. Outside of energy markets, industrial metal prices remain above pre-conflict levels, supported by demand for copper and other metals used in AI-related infrastructure (figure 3.4). These developments, together with higher semiconductor prices starting to feed through to broader consumer prices for electronics, could eventually pass through to core inflation.

Global agricultural commodity prices have risen by around 15 percent since the start of the conflict. The price of urea, a nitrogen fertiliser, has returned to around pre-conflict level. Phosphate fertiliser prices remain elevated, reflecting disruption to sulphur exports from the Middle East. Higher fuel and fertiliser prices can raise farmers' production costs, adding pressure to food supply and prices. There are also concerns about how a strong El Niño event may affect agricultural production.

Figure 3.3

Selected oil futures prices

(1-month futures)

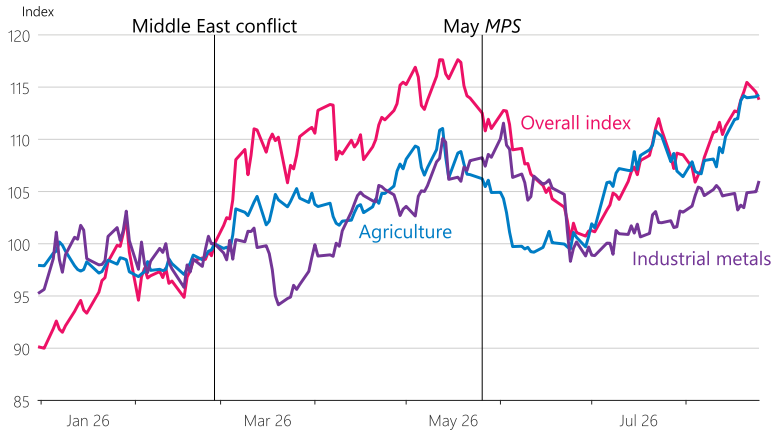


Source: Bloomberg.

Note: Brent refers to the main European crude oil benchmark, WTI (West Texas Intermediate) the main US benchmark, and Dubai the main benchmark for crude oil exports to Asia.

Figure 3.4

Selected commodity prices



Source: Bloomberg.

Note: The overall index is the Bloomberg Commodity Index, a diversified futures-based measure of prices across energy, metals, and agricultural commodities.

Global financial conditions

Policy rate expectations remain above pre-conflict levels

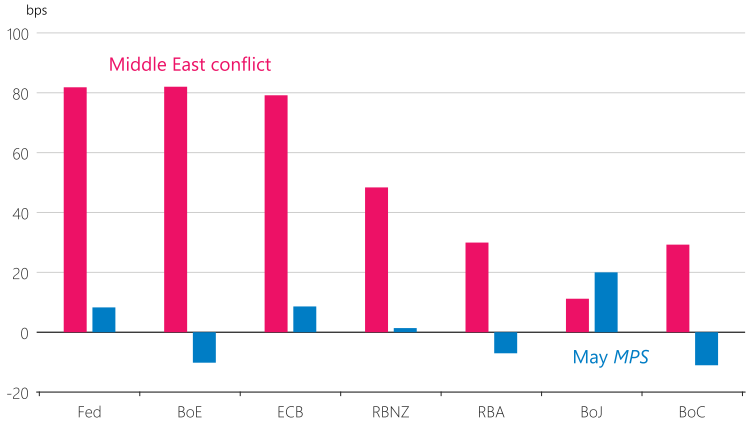
Financial market participants' expectations for central bank policy rates are higher than before the Middle East conflict began. Market-implied expectations for policy rates at the end of 2026 are around 80 basis points above their pre-conflict levels in the US, the UK, and the euro area, and around 10 to 30 basis points higher in Australia, Japan, and Canada (figure 3.5). The Reserve Bank of Australia and the European Central Bank have already raised policy interest rates since the conflict began, although in Australia this mostly reflects domestic inflationary pressure. Major central banks have noted that there is limited evidence of second-round price effects so far, but that the risk of these could increase if energy prices remain elevated.

Longer-term government bond yields have increased modestly

Government bond yields are higher than at the time of the May *Statement*. Two-year sovereign bond yields have increased between 5 and 30 basis points across several advanced economies, reflecting market expectations that policy rates will remain higher than before the Middle East conflict. Ten-year government bond yields are between 15 and 30 basis points higher (figure 3.6). The rise in longer-term yields has partly reflected higher term premia, or the additional compensation investors require to hold longer-term bonds. This has occurred even as longer-term market-based inflation expectations have remained stable.

Figure 3.5

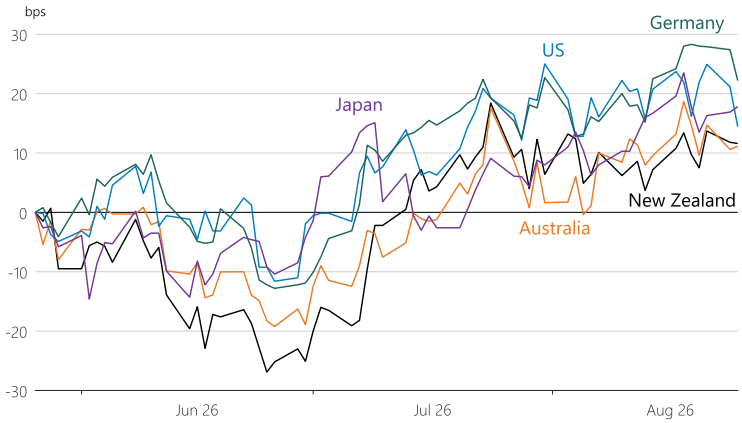
Change in market-implied policy rate expectations for the end of 2026



Source: Bloomberg.

Figure 3.6

Change in 10-year government bond yields since the May *Statement*

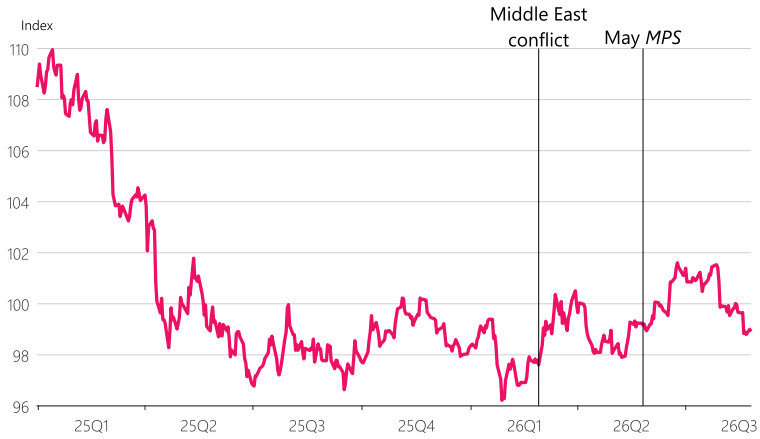


Source: Bloomberg.

Exchange rate movements have reflected differences in monetary policy expectations

The US dollar is broadly flat since the May *Statement*. The US dollar index, which measures the value of the US dollar against a basket of six major currencies, is unchanged compared to at the time of the May *Statement,* and is around 3 percent above its low point at the end of January (figure 3.7). Movements since the May *Statement* have reflected financial market pricing for US interest rates relative to other major economies.

Figure 3.7
US dollar index

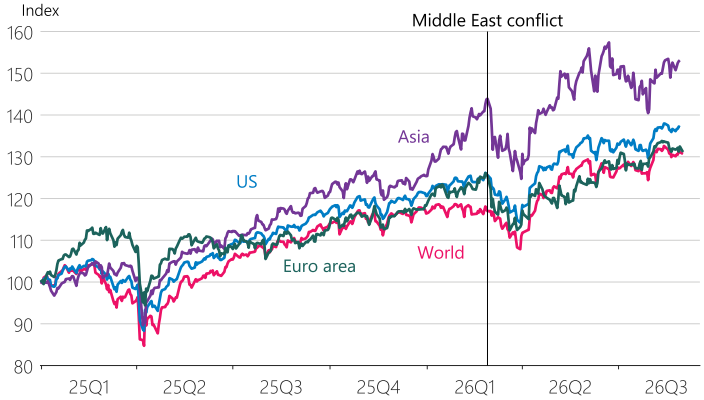


Source: Bloomberg.

Global equity markets have risen, led by AI-exposed sectors

Global equity prices have continued to rise despite elevated uncertainty. Since the onset of the Middle East conflict, global equities have increased by around 10 percent, supported by stronger earnings expectations and continued demand for AI-related hardware and services (figure 3.8). However, recent volatility in some Asian semiconductor stocks highlights that equity markets remain sensitive to changes in expectations for AI-related profitability.

Figure 3.8
Global equity indices



Source: Bloomberg.

Note: Daily closing values of headline equity price indices in local currency terms. Indices are S&P 500 (US), MSCI All Country World Index (World), MSCI Asia (Asia), Euro Stoxx 50 (Euro area).

Domestic financial conditions

Wholesale interest rates have increased

Domestic financial conditions have tightened since the May *Statement*. Oil prices have had a significant influence on New Zealand wholesale interest rates in 2026. Periods of escalating tension between the US and Iran have caused oil prices to increase. This has increased near-term inflation and heightened the risk of second-round price effects, putting upward pressure on inflation expectations, resulting in market participants raising their expectations for central bank policy rates. Domestic wholesale interest rates decreased after the US-Iran Memorandum of Understanding in June, before increasing over July as tensions rose again. Domestic factors have also contributed to higher New Zealand interest rates, including the 25 basis point OCR increase in July.

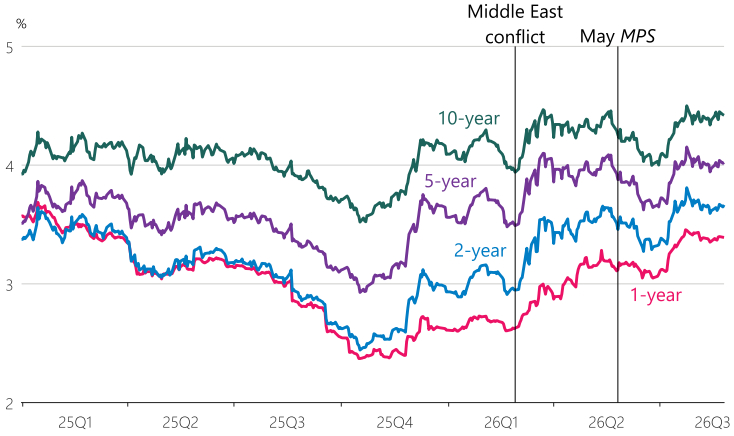
New Zealand swap rates have increased since the May *Statement*. Shorter tenor rates have increased by around 25 basis points and longer tenor rates by around 15 basis points (figure 3.9). Market pricing for the level of the OCR in 2026 is slightly higher over the near term and slightly lower over 2027 than just before the May *Statement*. Market pricing implies the OCR is expected to increase to around 3 percent by the end of 2026 (figure 3.10).

The New Zealand dollar has appreciated since the May *Statement*

The New Zealand dollar trade-weighted index has appreciated by around 1.4 percent since the May *Statement* (figure 3.11). This primarily reflects an increase in New Zealand interest rates compared to those of its trading partners over this period. The increase in the OCR in July and some stronger domestic data releases have contributed to relatively higher New Zealand interest rates since the May *Statement*. However, the New Zealand dollar trade-weighted index remains lower than before the Middle East conflict.

Figure 3.9

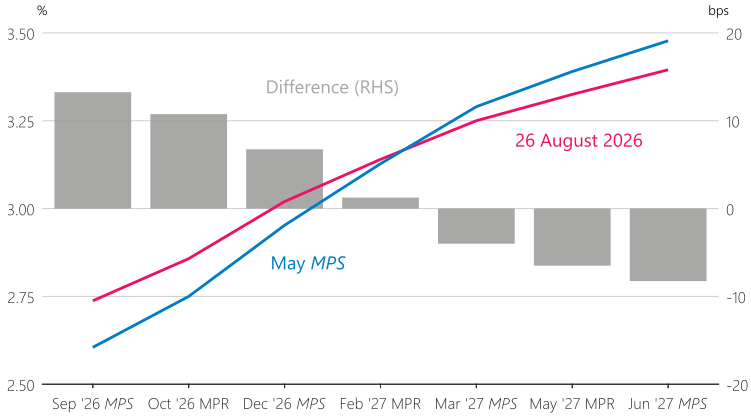
New Zealand swap rates



Source: Bloomberg.

Figure 3.10

Financial market participants' expectations for the OCR



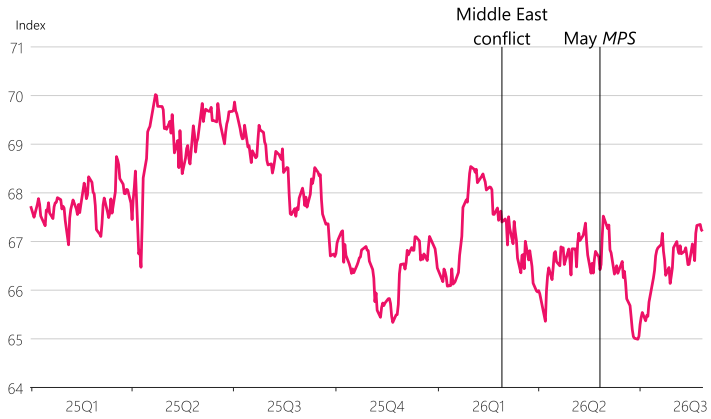
Source: Bloomberg.

Note: The blue line shows expectations for the OCR immediately before the May *Statement*. Each data point represents market expectations of the level of the OCR at a given point in the future, as measured by overnight indexed swap pricing.

Figure 3.11

NZ dollar trade-weighted index

(nominal)



Source: RBNZ.

Higher wholesale interest rates have been passed through to mortgage rates

Mortgage rates at the 6-month to 2-year tenors have risen by 20 to 30 basis points (figure 3.12). Since the May *Statement*, the spread between the 2-year mortgage rate and the 2-year interest rate swap rate is broadly unchanged, indicating that higher wholesale interest rates have passed through to bank lending rates.

The average yield on the total stock of mortgage lending is little changed in recent months (figure 3.13). Mortgage holders have, on average, been refixing at similar rates to those they were previously paying. However, the increase in new mortgage rates this year means that the average yield on mortgage lending is likely to increase in coming months.

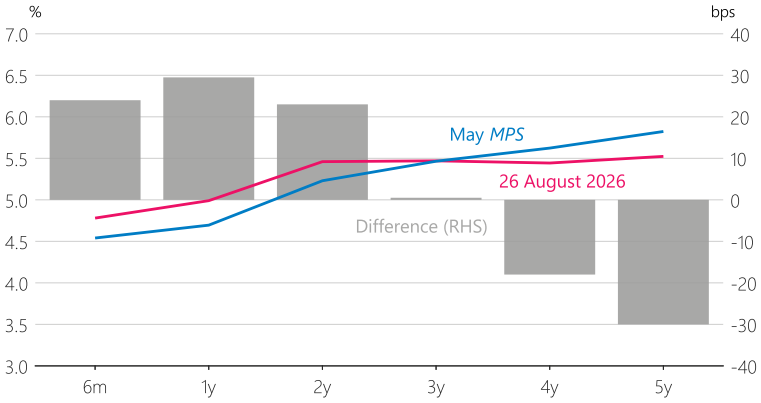
Since the May *Statement*, the difference between term deposit rates and wholesale rates has decreased. Term deposit rates have either increased by less than wholesale rates, or have fallen. For example, the difference between the 6-month term deposit rate and the 6-month wholesale interest rate has fallen by around 35 basis points since the May *Statement*, and around 75 basis points from its October 2025 peak (figure 3.14). That said, there are some signs banks are starting to pass through higher wholesale rates to depositors, as banks have recently increased the 6-month term deposit rate, which has been largely unchanged since late 2025.

Our estimate of the weighted average cost of new bank funding relative to wholesale rates has decreased since the May *Statement*. This is primarily because the difference between deposit rates and wholesale rates has decreased. Banks' cost of raising new wholesale funding relative to equivalent term wholesale rates has also remained low. At the margin, a reduction in the weighted average cost of new bank funding means financial conditions have tightened slightly less than would otherwise have been the case. For example, it may reduce the pace at which banks pass on higher wholesale rates to lending rates.

Figure 3.12

New Zealand mortgage rates

(terms in years)

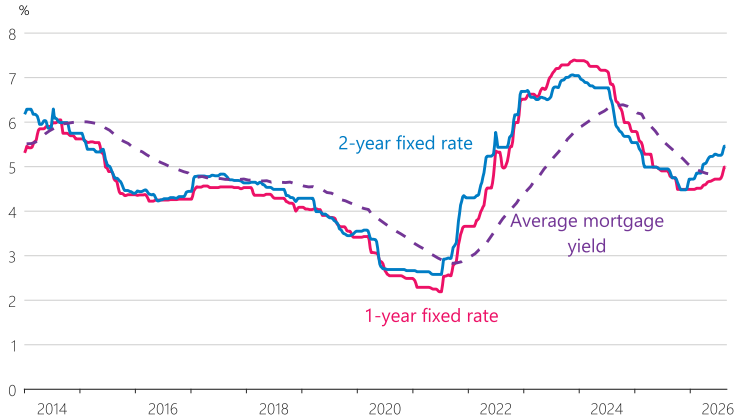


Source: interest.co.nz.

Note: The 6-month to 3-year rates are the average advertised fixed mortgage rates offered by ANZ, ASB, BNZ, and Westpac for loans with a loan-to-value ratio below 80%. The 4- and 5-year rates are the equivalent averages for ASB, BNZ, and Westpac. May *Statement* rates are those advertised on the Friday before the May OCR decision.

Figure 3.13

Mortgage rates



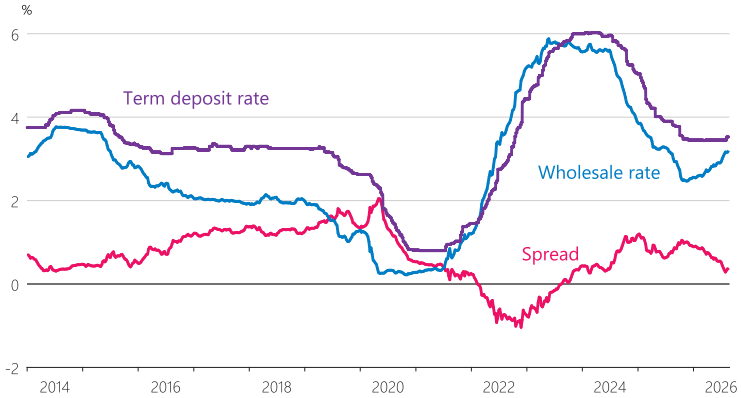
Source: interest.co.nz, RBNZ.

Note: The average mortgage yield is the monthly yield on the total stock of residential mortgages for registered banks. The other rates are the average of the advertised fixed-term rates on offer from ANZ, ASB, BNZ, and Westpac for mortgages with a loan-to-value ratio of less than 80%.

Figure 3.14

Spread of term deposit rate to wholesale rate

(6-month)



Source: Bloomberg, interest.co.nz.

Note: The wholesale interest rate is the 6-month Bank Bill Benchmark Rate (BKBM).

Chapter 04

Special topics

Richmond Hut. Photo: James Hancock

Chapter 4.
Special topics

Before the publication of each *Statement*, Reserve Bank staff provide analyses of some topical issues to the Monetary Policy Committee.

Topics for the September *Statement* included:

1. The effect of the Middle East conflict on inflation
2. Recent developments and the outlook for household consumption

Special topics in the past 12 months

Topic	Date/publication
How will the Middle East conflict affect the New Zealand economy?	May 2026 *Statement* (Chapter 4)
How much spare capacity is there in the New Zealand economy?	May 2026 *Statement* (Chapter 4)
Recent developments in inflation and the outlook for key drivers	February 2026 *Statement* (Chapter 4)
How are high commodity prices affecting the New Zealand economy?	November 2025 *Statement* (Chapter 4)
A closer look at our measures of labour market spare capacity	November 2025 *Statement* (Chapter 4)
Household sector developments and outlook	August 2025 *Statement* (Chapter 4)
Assessing developments in inflation expectations	August 2025 *Statement* (Chapter 4)

1 The effect of the Middle East conflict on inflation

Summary

- **The MPC is focused on the outlook for medium-term inflation, as directed by its *Remit*.** The effects of the Middle East conflict on medium-term inflation will depend on how second-round demand and price effects net out. Monetary policy cannot prevent the first-round effects of higher oil prices on inflation. However, it can prevent an increase in the price of oil from becoming embedded in price- and wage-setting behaviour.
- **Annual CPI inflation increased to 4.1 percent in the June 2026 quarter, largely reflecting the direct effects of higher fuel prices due to the Middle East conflict.** Inflation is expected to remain elevated over the rest of 2026. Increasing contributions from indirect effects will partially offset diminishing contributions from direct effects.
- **A range of indicators can be used to help assess second-round price effects, including core inflation, inflation and wage expectations, firms' pricing intentions, and wage inflation.** At this stage, inflationary pressure appears to be evolving broadly as expected in the May *Statement*.
- **The outlook remains sensitive to developments in global fuel prices.** Further volatility in oil markets could lead to different inflation outcomes.

Oil shocks can have first- and second-round effects on the economy

Higher oil prices affect inflation through several channels, and at different speeds. We decompose the effects of the conflict on the economy into four broad categories (see chapter 4.1 of the May 2026 *Statement*):

- **First-round direct effects** describe the immediate impact of changes in global refined fuel prices on petrol and diesel prices in the CPI.
- **First-round indirect effects** describe changes in the prices of other goods and services in the CPI that use directly affected goods as inputs.
- **Second-round demand effects** describe how reduced real household and business spending increases spare capacity, dampening inflationary pressure.
- **Second-round price effects** describe the way in which higher prices in the near term propagate through the economy over the medium term via price- and wage-setting behaviour. Second-round price effects also include the medium-term impact of generalised global inflationary pressure and a weaker New Zealand dollar on import costs and domestic prices.

The MPC's focus is on medium-term inflationary pressure. First-round effects impact the outlook for inflation in the near term, over which monetary policy has little influence (see box B, chapter 2). The effect of the Middle East conflict on medium-term inflationary pressure depends on the balance between inflationary second-round price effects, and disinflationary second-round demand effects.

First-round price effects are contributing significantly to inflation in 2026

Annual headline inflation increased to 4.1 percent in the June 2026 quarter. First-round direct effects contributed less to inflation than forecast in the May *Statement*, as fuel prices fell more quickly than assumed over the latter half of the June quarter. The direct effect of higher fuel prices contributed 0.9 percentage points to quarterly CPI inflation in the June 2026 quarter.

While indirect price effects are difficult to isolate, we estimate that aggregate indirect price effects in the June 2026 quarter were small. Cost pressures associated with the conflict, including for diesel and plastics, contributed to price increases for new home construction and property maintenance. Higher synthetic material costs may have contributed to higher prices for clothing and footwear. We estimate that first-round indirect effects contributed about 0.1 percentage points to CPI inflation in the June 2026 quarter.

Indirect effects are expected to increase over the remainder of 2026. Even if fuel prices decline as assumed, we expect that indirect effects will strengthen over the remainder of the year. This is because firms may initially absorb higher costs into margins, passing higher costs on to customers over time. Indirect effects are assumed to contribute 0.3 percentage points to quarterly CPI inflation in the September 2026 quarter, and 0.5 percentage points in the December 2026 quarter.

We look at a range of indicators to assess second-round price effects

To assess second-round effects and medium-term inflationary pressures, we monitor a range of indicators, including core inflation, inflation and wage expectations, firms' pricing intentions, and wage inflation. These can help us assess whether inflation is becoming more broad-based and persistent.

Core inflation has increased, likely reflecting first-round effects

Measures of core inflation attempt to look through volatility to identify persistent and generalised inflation. The Reserve Bank monitors a range of different core inflation measures, which take different approaches to removing volatility from CPI inflation.

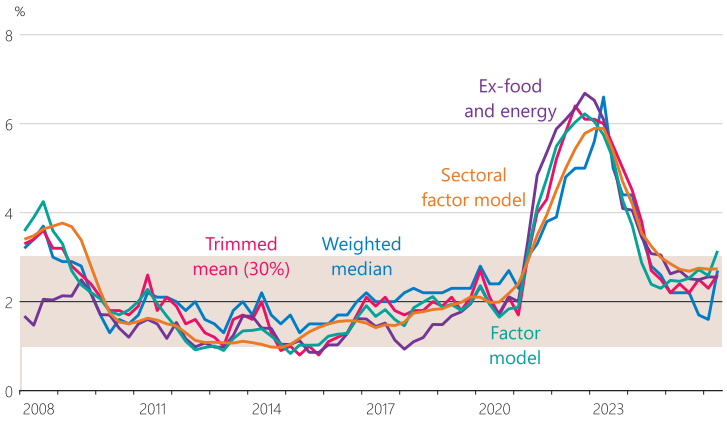
Most measures of core inflation increased in the June 2026 quarter (figure 4.1). The increases across core inflation measures are broadly consistent with what we would expect for an oil supply shock of the size experienced since the conflict began. Historically, core inflation measures have not perfectly removed the first round-effects of oil supply shocks. Internal Reserve Bank modelling suggests that most measures of core inflation tend to increase following an oil supply shock, before fully reversing over time.

If the increase in core inflation becomes materially larger, broader across measures, or more persistent, this could indicate stronger second-round price effects than we assume.

Figure 4.1

Measures of core inflation

(annual)



Source: Stats NZ, RBNZ estimates.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Inflation expectations have eased since the May *Statement*

Inflation expectations can play an important role in shaping how inflation will evolve, as they influence how businesses set their prices and approach wage negotiations. The Reserve Bank surveys households, businesses, and professional forecasters to understand their inflation expectations over different time horizons. Near-term inflation expectations tend to move closely with headline inflation. Medium- and long-term inflation expectations are more stable, and can provide signals about whether higher inflation is expected to persist and the credibility of the MPC's inflation target.

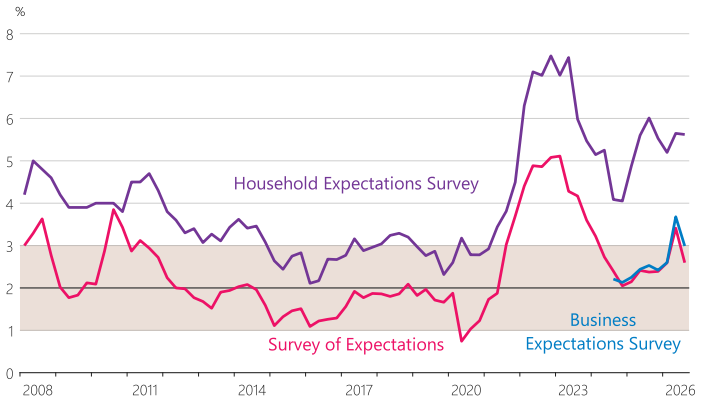
One-year ahead inflation expectations rose sharply in the June 2026 quarter, but have eased to varying degrees in the September 2026 quarter (figure 4.2). These movements have been somewhat larger and more volatile than the typical relationship with inflation outcomes would imply. When forming near-term expectations, respondents have likely been reacting to the highly visible and sharp changes in fuel prices since the conflict began.

Two-year ahead expectations of professional forecasters and business leaders decreased to 2.3 percent in the September quarter from 2.5 percent in the June quarter. Expectations are close to pre-conflict levels and well below historical peaks (figure 4.3). These survey results suggest little evidence that oil shock inflation pressures have become embedded in respondents' expectations beyond one year ahead. The oil shock does not appear to have added to longer-term inflation expectations, although they remain slightly above 2 percent. A material or prolonged increase in medium-term expectations would provide a stronger signal of second-round effects and inflation persistence.

Figure 4.2

1-year ahead inflation expectations

(annual)



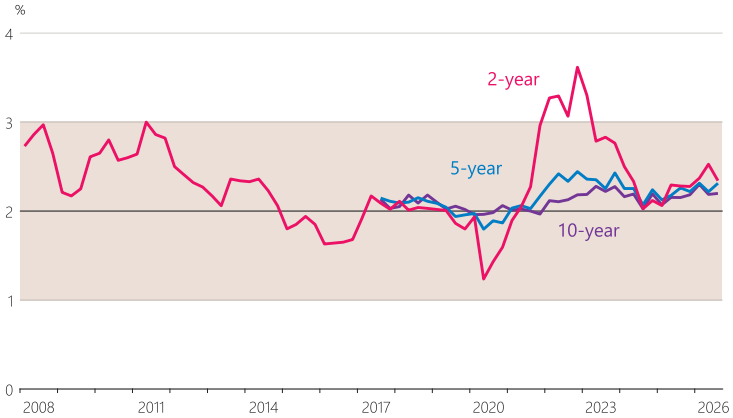
Source: RBNZ.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 4.3

Inflation expectations of professional forecasters and business leaders

(annual, years ahead)



Source: RBNZ *Survey of Expectations*.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Wage pressures remain subdued due to significant spare capacity in the labour market

Developments in wage inflation can be a signal of the extent to which inflation is broadening. However, in New Zealand wage-setting is generally infrequent, with most businesses reviewing and setting wages annually. Any effect of the Middle East conflict on wages is likely to emerge slowly.

Annual LCI wage inflation (private sector, all salary and wage rates) remained at 2 percent in the June 2026 quarter (figure 4.4). This is a level consistent with CPI inflation returning to 2 percent over time Other measures of wage growth remain subdued.

We expect wage inflation to remain modest due to significant spare capacity in the labour market. While some workers will attempt to bargain for higher wages in response to higher inflation, bargaining power is reduced by squeezed profit margins and a weak labour market. If wage inflation increases over the coming year, this could signal that inflationary pressures are larger and more broad-based.

Firms and professional forecasters expect wage growth to remain subdued. Surveys of businesses' and professional forecasters' expectations of one- and two-year ahead wage growth have remained broadly unchanged since the conflict began. If wage growth expectations increase, this could be a sign that higher near-term inflation is beginning to contribute to broader inflationary pressure.

The inflation outlook remains sensitive to developments in global fuel prices

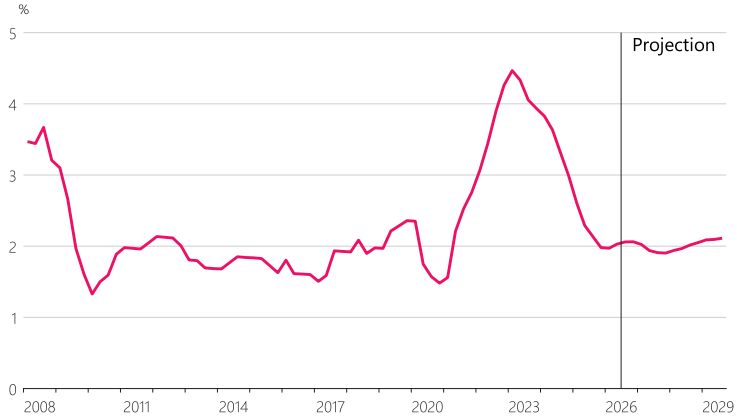
The evolution of the conflict in the Middle East remains highly uncertain, as do its implications for global crude and refined oil markets (see box A in the May 2026 *Statement*). Our near-term projections for CPI inflation have been revised at each meeting since the start of the conflict in response to changes in fuel prices (figure 4.5). Further volatility in oil prices could result in materially different direct and indirect effects on New Zealand CPI inflation than assumed in the central projection.

Over the medium term, monetary policy may need to respond differently if oil prices evolve differently or have larger or more persistent effects on price-setting behaviour. The MPC will continue to monitor indicators of core inflation, inflation and wage expectations, firms' pricing intentions, and wage inflation when assessing the outlook for medium-term inflation pressures.

Figure 4.4

Private sector LCI wage inflation

(annual)

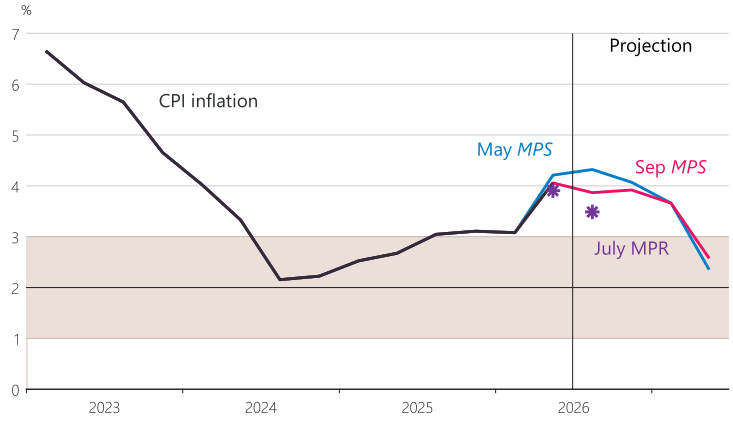


Source: Stats NZ, RBNZ estimates.

Figure 4.5

Evolution of CPI inflation projections

(annual)



Source: Stats NZ, RBNZ estimates.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

2 Recent developments and the outlook for household consumption

Summary

- **Over the last year, household consumption growth remained subdued despite lower nominal and real interest rates.** Annual consumption growth was 0.8 percent in the year to the March 2026 quarter.
- **Weak real income growth, declining real household wealth, subdued population growth, and increased saving have dampened household consumption.** High inflation has eroded households' purchasing power. House prices have continued to fall, constraining growth in household wealth, while weak labour market conditions have limited labour income growth and encouraged some households to save a larger share of their incomes.
- **Consumption growth is projected to increase as inflation falls, real house prices begin to rise, and real labour income growth increases.** Labour market conditions are projected to strengthen as economic growth recovers. Increasing wealth and higher income growth are assumed to more than offset the dampening effect of higher interest rates on consumption.

Consumption has increased more slowly than expected

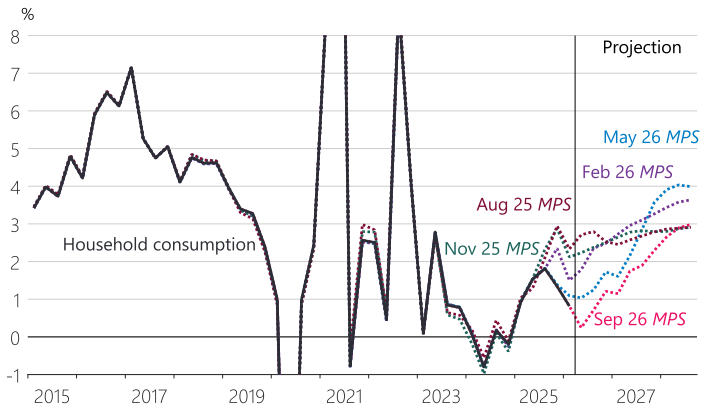
Household consumption accounts for about 55 percent of nominal GDP and is an important channel through which monetary policy affects domestic demand and inflation. Although overall GDP growth has been broadly in line with our forecasts over the past year, consumption has expanded more slowly than expected (figure 4.6).

Annual household consumption growth was 0.8 percent in the March 2026 quarter, compared with 2.3 percent projected in the August 2025 *Statement*. Over the past year, spending on services and non-durable goods has been broadly flat, while durable consumption has continued to increase, but at a slower pace than previously. The weakness in household consumption contrasts with stronger export activity and a recovery in business investment in recent quarters, supported by high commodity prices and resilient demand in New Zealand's trading partners.

Figure 4.6

Household consumption growth

(annual)



Source: Stats NZ, RBNZ estimates.

Key drivers of consumption growth have been weak in recent years

Lower interest rates have supported spending over the past year, but increases in the OCR from mid-2026 will reduce this support over time. Real interest rates have declined considerably in recent years, supporting household demand. The average interest rate on the total stock of mortgage lending fell as fixed-rate borrowers rolled onto lower rates, reducing household debt-servicing costs towards pre-COVID-19 shares of income (see figure 3.13 in chapter 3). The boost to household disposable incomes from lower mortgage costs has been partly offset by lower returns on deposits.

More recently, mortgage rates have increased, reflecting higher wholesale interest rates. Higher advertised rates affect new borrowing and saving decisions, and housing demand. The average rate paid on the stock of mortgage lending will increase gradually as existing borrowers refix, affecting household cash flows. Real interest rates are projected to increase further as inflation declines. This means that interest rates will provide less support to household consumption over time.

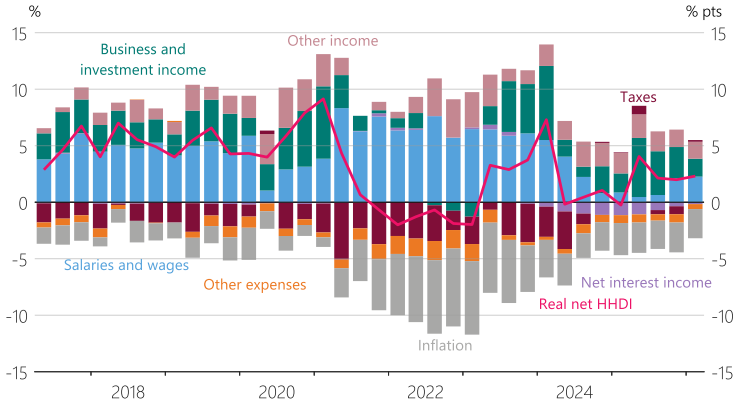
Real household income growth has been weak, reflecting soft labour market conditions. Real household disposable income includes income from wages, salaries, and self-employment as well as other sources like pensions and investment returns, deflated by the CPI. Real household income growth has increased slightly since 2024 but remains low relative to pre-COVID history (figure 4.7). Nominal wage growth remains subdued, and higher inflation resulted in negative real wage growth in the June 2026 quarter (figure 4.8). While total salary and wage income growth has increased, reflecting growth in employment and hours worked since late last year, but remains low. Elevated inflation continues to reduce real income growth.

Nominal wage growth is expected to remain around current moderate levels over the medium term, while increasing economic growth is assumed to boost employment growth. Real labour income growth is expected to strengthen from 2027 as inflation declines and nominal labour income growth increases.

Figure 4.7

Real household disposable income decomposition

(annual)



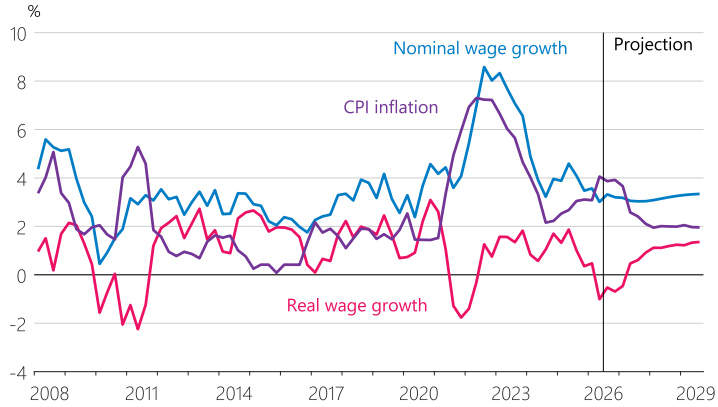
Source: Stats NZ, RBNZ estimates.

Note: For illustrative purposes, compared to the categories reported by Stats NZ we have recategorised interest payments on rental properties into net interest income instead of business income. Net HHDI represents net household disposable income.

Figure 4.8

Average hourly wage growth

(annual)



Source: Stats NZ, RBNZ estimates.

Note: Nominal and real wage growth are based on Quarterly Employment Survey average hourly earnings, which is a better measure of the average hourly wage received by households than the Labour Cost Index.

The household savings rate has increased as consumption has grown more slowly than household income (figure 4.9). This suggests households remain cautious about spending, reflecting uncertainty about job prospects, low consumer confidence, and declining real wealth.

Declining real household wealth has weighed on consumption. Housing is the largest component of household assets, and declining real house prices are reducing household wealth. Unlike in some previous periods of monetary policy easing, lower interest rates have not been accompanied by rising housing wealth, contributing to the slow recovery in household consumption (figure 4.10). While the value of other assets has been growing, this has been insufficient to offset the decline in real housing wealth.

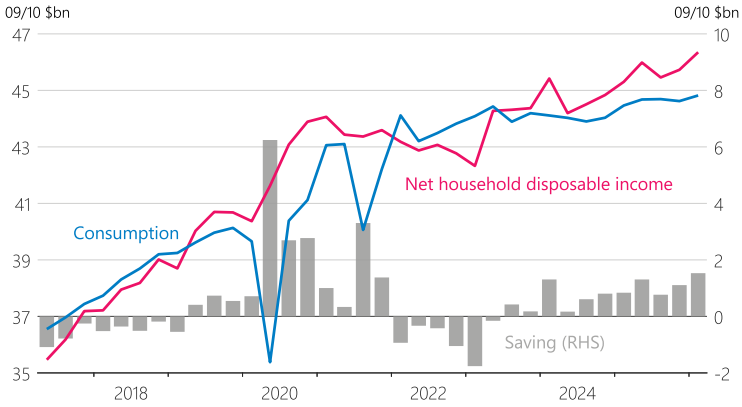
Real house prices are projected to decline slightly in the near term before increasing modestly over the medium term. The Middle East conflict has resulted in higher uncertainty, weaker purchasing power, and a higher interest rate outlook, weighing on house prices. We assume that real house prices increase modestly from mid-2027, broadly in line with household incomes over the remainder of the projection period. Rising real house prices are expected to support household wealth and consumption.

Population growth remains subdued compared to recent years. Population growth has increased slightly as net immigration has recovered. The working-age population grew by 1.3 percent in the year to the June 2026 quarter, and is projected to remain around this level over the medium term. This is broadly in line with longer-run historical averages but below rates immediately before COVID-19. If population growth increases or decreases, this would influence aggregate consumption growth over our forecast horizon.

Figure 4.9

Household sector real net disposable income, consumption, and saving

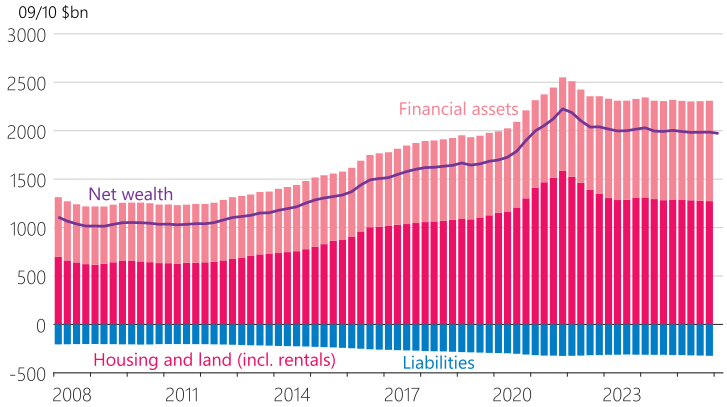
(seasonally adjusted)



Source: Stats NZ, RBNZ estimates.

Figure 4.10

Real household wealth



Source: Stats NZ, RBNZ estimates.

Note: Compared to the categories reported by Stats NZ, we have recategorised the implied value of rental property from equity in unincorporated businesses to housing and land, and the value of loans on rental properties from equity in unincorporated business to loans. Components of net wealth are not available for the March 2026 quarter.

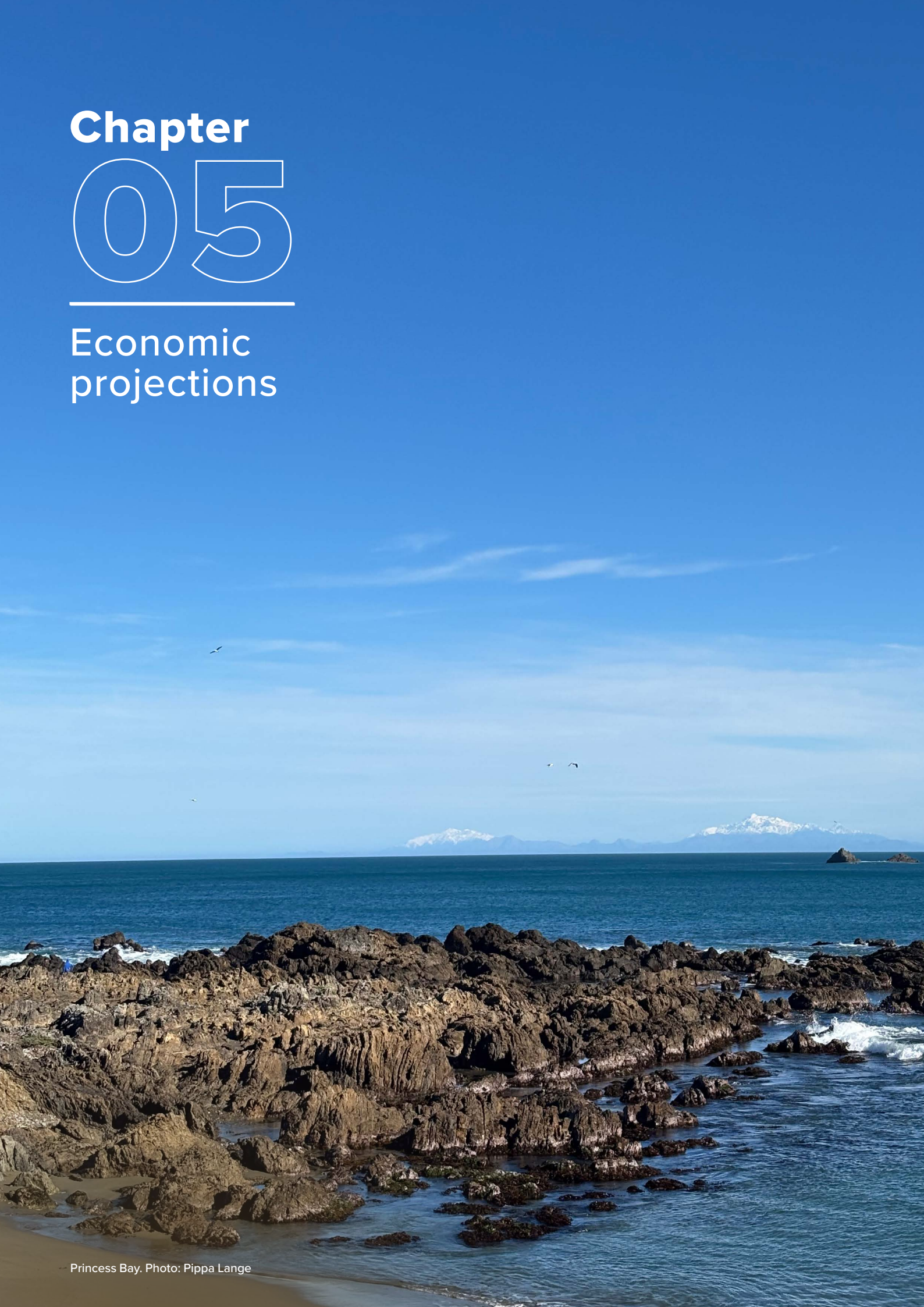
Consumption growth is projected to increase over time

Consumption growth is projected to strengthen from the end of 2027 and increase further over the medium term, supporting the closing of the output gap. Stronger real labour income growth and a gradual recovery in real house prices are expected to support consumption, as the support from low interest rates is gradually reduced.

Our projection for stronger consumption growth is conditional on strengthening labour market conditions, a recovery in purchasing power, and improving household wealth. If income growth is weaker than projected, then household spending could recover more slowly, and spare capacity could persist for longer. Conversely, households may become more willing to spend and reduce precautionary savings once they see signs of momentum building in the labour and housing markets, resulting in faster consumption growth than projected.

Chapter 05

Economic projections



Princess Bay. Photo: Pippa Lange

Chapter 5.
Economic projections

This chapter summarises the central economic projections that the MPC considered when making their policy assessment. The projections were finalised on 26 August 2026.

Inflation was above the target range in the June 2026 quarter due to the direct effects of higher fuel prices. Annual CPI inflation was 4.1 percent, of which fuel contributed 1.2 percentage points.

Indirect price effects are expected to make a larger contribution to CPI inflation in the second half of 2026, as some businesses pass on higher fuel costs. Higher costs for fuel, plastics, fertilisers, and other petroleum-based products are expected to spill over into other prices over the rest of 2026, such as air and road transport, food, and construction. Indirect price increases are forecast to contribute 0.9 percentage points to annual CPI inflation by the December 2026 quarter.

Second-round price effects may add to medium-term inflationary pressure. Higher import prices and a lower exchange rate feed directly into costs, and the initial increase in inflation may result in firms and households adjusting their price- and wage-setting behaviour (figure 5.8). These dynamics make inflation more persistent, adding to inflationary pressure over the medium term. However, these are partly offset by second-round demand effects, which reduce inflationary pressure.

A recovery in demand was under way before the oil shock, and economic activity is beginning to expand again. Timely indicators suggest that the level of economic activity was broadly unchanged in the June 2026 quarter. However, a range of indicators suggest economic activity is increasing again in the September 2026 quarter. We assume the output gap is -1.5 percent of potential GDP in the September 2026 quarter, about 0.3 percentage points higher than assumed in the May *Statement*.

The labour market has remained weak, but is expected to recover as activity grows. The unemployment rate rose to 5.6 percent in the June 2026 quarter, as growth in the labour force outpaced growth in employment. We expect the unemployment rate to decrease gradually as the output gap recovers. Same-job wage growth has decreased to a level consistent with headline inflation near the target mid-point. Wage growth is expected to remain around current levels as elevated unemployment and compressed business margins limit workers' bargaining power.

We project the OCR will increase gradually over the next two years to about 3.2 percent (figure 5.6). The OCR increases to lean against medium-term inflationary pressures, allowing economic activity to grow sustainably while preventing higher near-term inflation from embedding in price- and wage-setting behaviour. This projection represents what we believe is the most likely path for the economy, conditional on our key economic assumptions (table 5.1). However, this is only one of many possible paths. Global developments and the evolution of the domestic economy are likely to be different to our central assumptions.

Table 5.1
Key projection assumptions

Economic growth and capacity pressure	
GDP	• Production GDP increased 0.8 percent in the March 2026 quarter (figure 5.5). Consistent with timely indicators, we assume GDP growth was flat in the June 2026 quarter, and will be 0.5 percent in the September 2026 quarter. • We assume second-round demand effects from the Middle East conflict caused June 2026 quarter GDP to be about 0.6 percent lower than otherwise, due to higher fuel prices, lower real incomes, and greater uncertainty. • GDP growth is seasonally adjusted but has a remaining predictable seasonal pattern. This residual seasonality is assumed to reduce GDP growth by 0.2 percentage points in the June 2026 quarter, and have no effect on the September 2026 quarter. We have not accounted for residual seasonality in quarters from September 2026 onward. • Although the level of GDP in the March 2026 quarter was close to our May 2026 *Statement* forecast, the activity mix has been different. Exports, business investment, and government consumption have been higher than expected, but this has been offset by lower-than-expected private consumption and higher imports.
Domestic capacity pressures	• The output gap is estimated to have declined to -1.5 percent of potential GDP in the June 2026 quarter. We project that the output gap narrows to -0.8 percentage points by the end of 2027 and closes in 2029. • We assume that the negative second-round demand effects in late 2026 and early 2027 will be smaller than in the May *Statement*, in proportion to the decrease in oil futures pricing since the May *Statement*.
Consumption	• We project consumption growth to increase gradually, as the effects of the oil shock fade, real house prices begin to rise, and real labour income growth increases (see chapter 4.2). • Nominal house prices are projected to decrease slightly in 2026. A large stock of housing available for sale, higher borrowing costs, and low real income growth have limited households' ability and willingness to bid up house prices. From mid-2027, house prices are projected to increase only gradually as income growth recovers.
Business investment	• Business investment has decreased significantly over the past three years, as spare capacity reduced firms' incentive to invest in new capital. Business investment grew strongly in the March 2026 quarter, but increased spare capacity and uncertainty from the Middle East conflict are assumed to delay further recovery. • Business investment is projected to increase later in the projection as activity increases and spare capacity reduces.
Residential investment	• Residential investment is expected to increase over 2026, but by less than the recent large increase in new dwelling consents would typically imply. • The Middle East conflict has increased construction costs via higher diesel and materials prices. It has also increased uncertainty and reduced real income, weighing on house prices. Higher interest rates are also expected to dampen residential investment activity. • Over the medium term, higher net immigration and housing supply policy changes are expected to support an increase in construction activity.

Government	• We assume that real government expenditure (consumption and investment) declines over the middle of 2026, before remaining broadly flat over the medium term. As domestic activity grows, government expenditure declines as a share of potential GDP. • Total government expenditure is assumed to be consistent with fiscal forecasts in the *Budget Economic and Fiscal Update* 2026, updated for a stronger-than-expected starting point in the March 2026 quarter GDP data.
Export volumes	• Services export volumes have been growing strongly, and were about 16 percent higher in the March 2026 quarter than in the March 2025 quarter. They are expected to remain high over the June 2026 quarter, consistent with high tourist numbers and overseas card spending. • We assume second-round demand effects reduce tourism spending over the second half of 2026, because the Middle East conflict has increased prices and reduced the availability of flights to New Zealand. Services exports are projected to increase as a share of potential GDP over the medium term. • Goods export volumes are estimated to have grown strongly in the June 2026 quarter, based on strong merchandise trade, livestock slaughter, and milk production data. We assume this substantial increase partly reflects timing effects, leading to a decline in the September 2026 quarter. • Goods export volumes are projected to grow at a slower rate than potential GDP over the medium term, consistent with recent declines in real goods export prices.
Global factors	
Export prices	• Export prices, in real foreign currency terms, are assumed to remain at about their current level over the medium term. • We assume no effects from El Niño in these projections. Reserve Bank research finds that droughts push down economic activity and lift some consumer prices. However, while El Niño is associated with drier weather conditions in some parts of New Zealand, El Niño does not have a consistent relationship with drought conditions (see box A, chapter 2).
Import prices	• Dubai crude oil prices peaked 40 percent higher than their pre-conflict level at US$93 per barrel on average in the June 2026 quarter and are assumed to average US$85 per barrel in the September quarter, about 30 percent above pre-conflict levels (figure 5.7). We assume crude prices remain about 15 percent above pre-conflict levels by the end of the projection. Our oil price assumption is based on oil futures prices, adjusted for risk using a term structure model. • Refined fuel spreads are assumed to decline over the coming year. • Non-oil import prices are assumed to increase in the near term, as global firms face higher costs for energy, fertiliser, petrochemical-derived products, and shipping. Non-oil import prices then decline in real terms over the medium term, but more slowly than oil, as it takes time for the oil price increase to transmit to other prices.
Global interest rates and exchange rate	• Based on market pricing, the outlook for global policy interest rates is slightly higher than our May *Statement* assumption. All else equal, higher global interest rates put downward pressure on the New Zealand dollar, which adds to inflationary pressure in New Zealand. • The New Zealand dollar trade-weighted index (TWI) is assumed to remain at 66.9 through the projection.

Labour market	
Employment and wages	• The unemployment rate increased to 5.6 percent in the June 2026 quarter and is forecast to remain elevated at 5.5 percent at the end of 2026 (figure 5.3). Second-round demand effects from the Middle East conflict dampen growth and slow the rate of hiring (relative to population growth) in the near term. We expect the unemployment rate to decrease towards the end of the projection, in line with the recovering output gap. • Same-job (LCI) wage growth remains at a level consistent with headline inflation near the target mid-point (figure 5.2). The relatively high unemployment rate and compressed business margins reduce workers' bargaining power. We assume that wage inflation increases slightly over the medium term as labour market conditions strengthen. • Real wages received by households, as measured by average hourly earnings from the Quarterly Employment Survey less CPI inflation, are forecast to decrease this year due to the sharp fuel-driven increase in inflation. Real wage growth is assumed to resume at about 1 percent in 2027, before increasing gradually over the medium term as CPI inflation declines and nominal wage growth lifts slightly.
Migration	• Net working-age immigration increased to about 4,400 in the June 2026 quarter. We assume net working-age immigration rises gradually to 6,800 per quarter in the medium term.

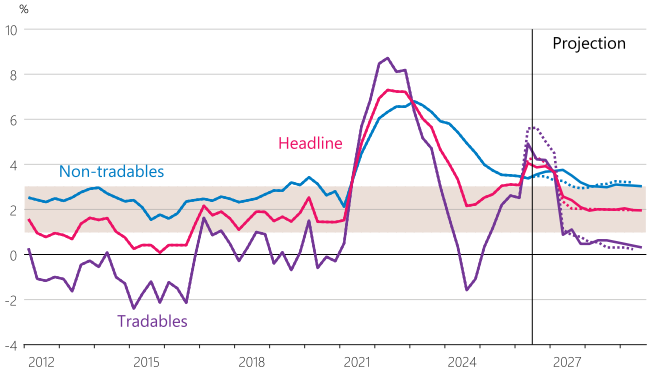
Inflation	
Headline CPI inflation	• Annual CPI inflation is forecast to decrease to 3.9 percent in the September 2026 quarter (figure 5.1). By the December 2026 quarter, direct effects from the higher oil prices are expected to contribute 0.7 percentage points to annual CPI inflation, and indirect effects are expected to contribute 0.9 percentage points. • Annual CPI inflation is forecast to return to near the 2 percent target mid-point in the December 2027 quarter. The negative output gap continues to put downward pressure on inflation, as price-setting behaviour adapts to a low-inflation environment, and administered and tradables inflation normalise. • The average of our core inflation measures increased from 2.4 to 2.7 percent in the June 2026 quarter. The increase was concentrated in measures that are more sensitive to oil supply shocks (see chapter 4.1).
Non-tradables	• Annual non-tradables inflation is projected to increase slightly over the coming year. Spare capacity is continuing to put downward pressure on non-tradables inflation. However, this is offset over the coming year by inflationary pressure from indirect price increases, including for domestic airfares, road transport, and house construction. • Given these assumptions, non-tradables inflation declines to 3.0 percent by the start of 2028.
Tradables	• Annual tradables inflation is assumed to have peaked at 4.9 percent in the June 2026 quarter, in response to the significant increase in oil prices. Annual tradables inflation is forecast to remain elevated in the near term, at 4.2 percent in the September and December quarters, as a declining direct contribution from fuel prices is partially offset by an increasing contribution from indirect price effects for items including food and international airfares. • Tradables inflation then rapidly declines in 2027 as the June 2026 quarter fuel price increase falls out of the annual percentage change calculation.

Economic projections charts

Figure 5.1

Inflation components

(annual)



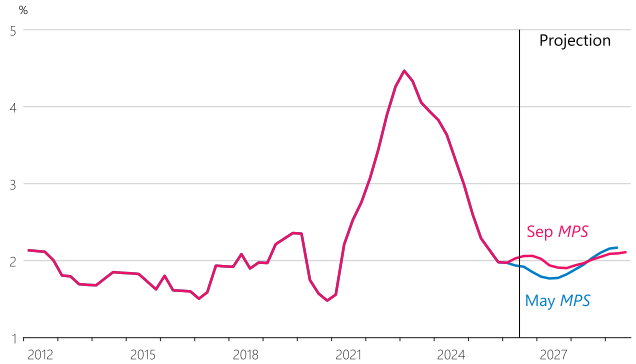
Source: Stats NZ, RBNZ estimates.

Note: Dotted lines show the projections from the May *Statement*. The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 5.2

Private sector LCI wage inflation

(annual)

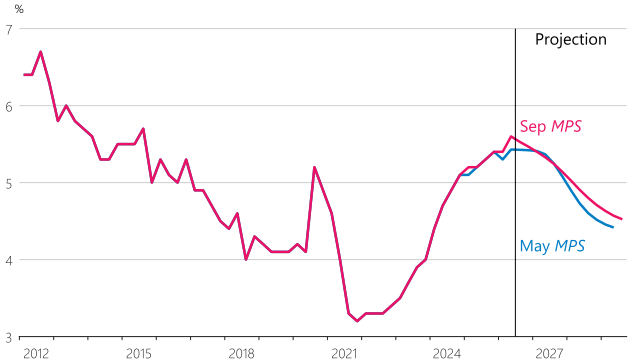


Source: Stats NZ, RBNZ estimates.

Figure 5.3

Unemployment rate

(unemployed people as a share of the labour force, seasonally adjusted)

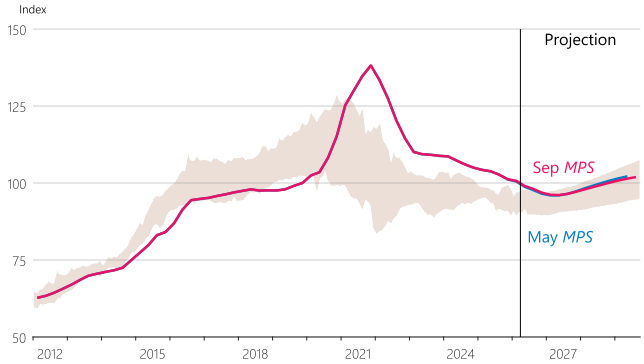


Source: Stats NZ, RBNZ estimates.

Figure 5.4

Real house prices and sustainable indicators

(index)



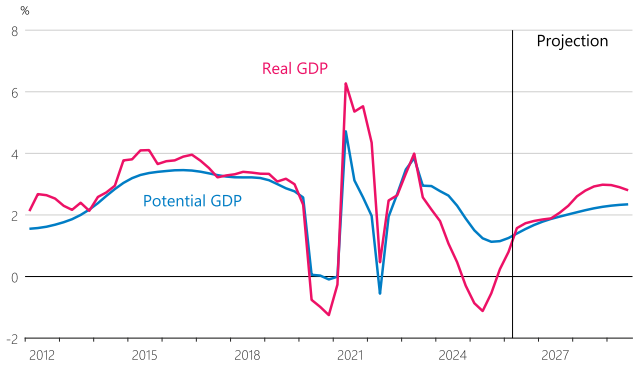
Source: Cotality, RBNZ estimates.

Note: See Brunton (2021), Measures for assessing the sustainability of house prices in New Zealand. The shaded area shows the range of indicators. This may be revised from time to time as certain assumptions change, such as neutral interest rates. The indicator range has been projected in line with our projections for wages and population growth. The projection assumes the neutral interest rate remains at its current level.

Figure 5.5

Production GDP growth

(annual average)

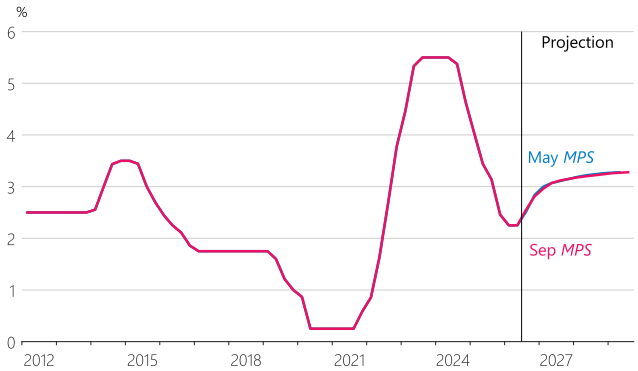


Source: Stats NZ, RBNZ estimates.

Figure 5.6

OCR

(quarterly average)



Source: RBNZ estimates.

Figure 5.7

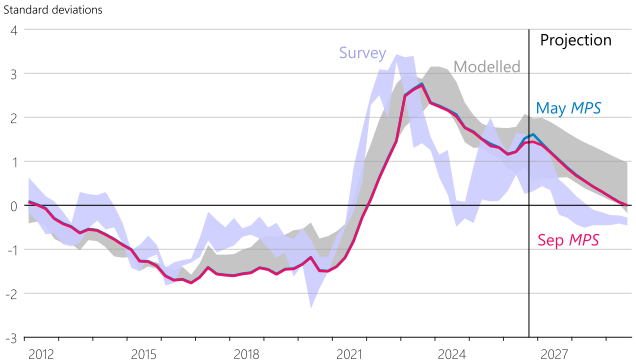
Dubai oil price

(quarterly average)

Source: LSEG, RBNZ estimates.

Figure 5.8

Price-setting behaviour



Source: RBNZ estimates.

Note: Measures have been standardised over history to make them comparable given differences in historical averages and degrees of variability between measures. The vertical axis shows how many standard deviations away from its historical average each measure is, where zero indicates the historical average. The shaded areas show the range of modelled and survey measures. Modelled measures include adaptive measures of the form used in NZSIM with varying sensitivities to recent inflation, and a measure based on the simple average of headline inflation over the past 3 years. Survey measures include 1- and 2-year ahead inflation expectations from the Survey of Expectations, and 1-year ahead inflation expectations from the Household Expectations Survey. See Kendall & Sing (2025), How well do different measures of price-setting behaviour explain non-tradables inflation?.

Chapter 06

Appendices

Wellington. Photo: Katie Taylor

Chapter 6.
Appendices

Appendix 1: Statistical tables

Table 6.1
Key forecast variables

		GDP growth Quarterly	CPI inflation Quarterly	CPI inflation Annual	Unemployment rate	TWI	OCR
2024	Mar	0.0	0.6	4.0	4.4	71.6	5.5
	Jun	-0.5	0.4	3.3	4.7	71.4	5.5
	Sep	-1.2	0.6	2.2	4.9	70.9	5.4
	Dec	0.1	0.5	2.2	5.1	69.5	4.6
2025	Mar	0.9	0.9	2.5	5.2	67.8	4.0
	Jun	-0.7	0.5	2.7	5.2	69.1	3.4
	Sep	0.9	1.0	3.0	5.3	68.4	3.1
	Dec	0.5	0.6	3.1	5.4	66.4	2.5
2026	Mar	0.8	0.9	3.1	5.4	67.2	2.3
	Jun	**0.0**	1.5	4.1	5.6	66.5	2.3
	Sep	**0.5**	**0.8**	**3.9**	**5.5**	**66.7**	**2.6**
	Dec	**0.5**	**0.7**	**3.9**	**5.5**	**66.9**	**2.8**
2027	Mar	**0.6**	**0.7**	**3.7**	**5.4**	**66.9**	**3.0**
	Jun	**0.6**	**0.4**	**2.6**	**5.3**	**66.9**	**3.1**
	Sep	**0.7**	**0.6**	**2.4**	**5.2**	**66.9**	**3.1**
	Dec	**0.8**	**0.4**	**2.1**	**5.1**	**66.9**	**3.2**
2028	Mar	**0.8**	**0.5**	**1.9**	**5.0**	**66.9**	**3.2**
	Jun	**0.7**	**0.5**	**2.0**	**4.9**	**66.9**	**3.2**
	Sep	**0.7**	**0.6**	**2.0**	**4.8**	**66.9**	**3.2**
	Dec	**0.7**	**0.3**	**2.0**	**4.7**	**66.9**	**3.2**
2029	Mar	**0.7**	**0.6**	**2.0**	**4.6**	**66.9**	**3.3**
	Jun	**0.6**	**0.4**	**2.0**	**4.6**	**66.9**	**3.3**
	Sep	**0.6**	**0.6**	**2.0**	**4.5**	**66.9**	**3.3**

Table 6.2

Measures of inflation and inflation expectations

	2024	2025				2026		
	Dec	Mar	Jun	Sep	Dec	Mar	Jun	Sep
Inflation (annual rates)								
CPI	2.2	2.5	2.7	3.0	3.1	3.1	4.1	
CPI non-tradables	4.5	4.0	3.7	3.5	3.5	3.5	3.4	
CPI tradables	-1.1	0.3	1.2	2.2	2.6	2.5	4.9	
Sectoral factor model estimate of core inflation	3.0	2.9	2.7	2.7	2.8	2.7	2.7	
CPI trimmed mean (30% measure)	2.5	2.2	2.4	2.2	2.5	2.3	2.6	
CPI weighted median	2.6	2.2	2.2	2.2	1.7	1.6	2.7	
GDP deflator (expenditure)	5.4	4.2	4.0	2.8	3.1	2.7		
Inflation expectations RBNZ Survey of Expectations Tara-ā-Pūkenga (SOE)								
1 year ahead	2.0	2.1	2.4	2.4	2.4	2.6	3.4	2.6
2 years ahead	2.1	2.1	2.3	2.3	2.3	2.4	2.5	2.3
5 years ahead	2.2	2.1	2.2	2.3	2.2	2.3	2.2	2.3
10 years ahead	2.2	2.1	2.2	2.2	2.2	2.3	2.2	2.2
Inflation expectations RBNZ Business Expectations Survey Tara-ā-Umanga (BES)								
1 year ahead	2.1	2.3	2.4	2.5	2.4	2.6	3.7	3.0
2 years ahead	2.2	2.5	2.5	2.6	2.4	2.6	2.9	2.6
5 years ahead	2.8	3.0	3.1	3.2	2.8	2.7	2.7	2.5
10 years ahead	3.3	3.7	3.9	3.6	3.6	3.2	2.9	2.5
Inflation expectations RBNZ Household Expectations Survey Tara-ā-Whare (HES)								
1 year ahead	4.1	4.9	5.6	6.0	5.5	5.2	5.6	5.6
2 years ahead	3.7	3.9	4.7	4.6	4.3	3.4	4.9	3.6
5 years ahead	3.4	3.6	3.7	4.1	3.8	3.3	4.0	3.5

Table 6.3

Measures of labour market conditions

(seasonally adjusted, changes expressed in annual percent terms, unless specified otherwise)

	2024	2025				2026	
	Dec	Mar	Jun	Sep	Dec	Mar	Jun
Household Labour Force Survey							
Unemployment rate	5.1	5.2	5.2	5.3	5.4	5.4	5.6
Underutilisation rate	12.2	12.4	12.8	12.9	12.9	12.9	13.8
Labour force participation rate	70.8	70.7	70.5	70.3	70.5	70.4	70.7
Employment rate (% of working-age population)	67.2	67.1	66.8	66.6	66.7	66.7	66.7
Employment growth	-1.3	-0.9	-1.3	-0.7	0.2	0.5	1.1
Average weekly hours worked	33.1	32.9	32.8	33.1	33.3	33.5	33.3
Number unemployed (thousand people)	155	156	158	160	165	164	171
Number employed (million people)	2.88	2.88	2.87	2.87	2.89	2.89	2.91
Labour force (million people)	3.04	3.03	3.03	3.03	3.05	3.06	3.08
Extended labour force (million people)	3.13	3.14	3.14	3.14	3.16	3.16	3.19
Working-age population (million people, age 15+ years)	4.28	4.29	4.30	4.31	4.33	4.34	4.35
Quarterly Employment Survey — QES							
Filled jobs growth	-0.9	-1.9	-1.1	0.2	-0.1	1.1	0.4
Average hourly earnings growth (private sector, ordinary time)	4.0	3.9	4.6	4.1	3.5	3.6	3.0
Other data sources							
Labour cost index growth, adjusted (private sector, ordinary and overtime)	3.0	2.6	2.3	2.1	2.0	2.0	2.0
Labour cost index growth, unadjusted (private sector, ordinary time)	3.9	3.7	3.5	3.3	3.3	3.2	3.2
Estimated net working-age immigration (thousands, quarterly)	-0.3	0.7	1.7	1.3	2.0	3.7	4.4
Change in all vacancies index*	-27.2	-21.7	-7.6	3.5	6.4	11.8	6.7

Note: The all vacancies index is produced by MBIE as part of the monthly Jobs Online report, which shows changes in job vacancies advertised by businesses on internet job boards. The unadjusted labour cost index (LCI) is an analytical index that reflects quality change in addition to price change (whereas the official LCI measures price changes only). For definitions of underutilisation, the extended labour force, and related concepts, see Statistics New Zealand (2016), Introducing underutilisation in the labour market.

* The all vacancies index is a non-seasonally adjusted series.

Table 6.4

Composition of real GDP growth

(annual average percent change, seasonally adjusted, March years, unless specified otherwise)

	Actuals								Projection		
March year	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**
Final consumption expenditure											
Private	4.5	2.5	0.3	6.0	3.2	1.1	0.0	1.4	**0.8**	**2.2**	**2.9**
Public authority	3.1	5.5	7.0	8.0	2.6	1.1	-1.3	3.9	**-0.5**	**-0.6**	**0.1**
Total	**4.2**	**3.2**	**1.8**	**6.5**	**3.1**	**1.1**	**-0.3**	**2.0**	**0.5**	**1.5**	**2.3**
Gross fixed capital formation											
Residential	0.1	2.7	2.1	3.0	-1.3	-4.8	-12.7	-3.8	**6.7**	**13.2**	**8.2**
Other	7.0	3.0	-2.2	10.6	5.3	0.1	-2.7	0.7	**2.8**	**4.9**	**5.5**
Total	**5.2**	**2.9**	**-1.2**	**8.6**	**3.7**	**-1.1**	**-4.9**	**-0.2**	**3.6**	**6.6**	**6.1**
Final domestic expenditure	4.4	3.1	1.1	7.0	3.2	0.6	-1.4	1.5	**1.2**	**2.6**	**3.2**
Stockbuilding*	-0.2	-0.2	-0.3	0.6	0.3	-1.4	0.4	0.3	**0.2**	**0.0**	**0.0**
Gross national expenditure	**4.3**	**2.8**	**-0.1**	**8.2**	**3.8**	**-0.8**	**-1.0**	**2.0**	**1.5**	**2.6**	**3.1**
Exports of goods and services	3.3	0.2	-17.9	2.5	5.6	8.3	3.3	3.3	**5.9**	**1.4**	**3.2**
Imports of goods and services	4.7	1.3	-15.7	16.8	4.2	-1.3	1.4	5.4	**3.4**	**2.0**	**4.0**
Expenditure on GDP	**3.8**	**2.5**	**0.2**	**4.4**	**4.0**	**1.5**	**-0.7**	**1.3**	**2.0**	**2.5**	**2.9**
GDP (production)	3.3	2.3	-0.3	4.3	3.3	1.8	-0.9	0.8	**1.9**	**2.6**	**3.0**
GDP (production, March qtr to March qtr)	3.4	0.8	4.7	0.3	3.1	1.5	-0.8	1.5	**1.7**	**2.9**	**2.8**

* Percentage point contribution to the growth rate of GDP.

Table 6.5

Summary of economic projections

(annual percent change, March years, unless specified otherwise)

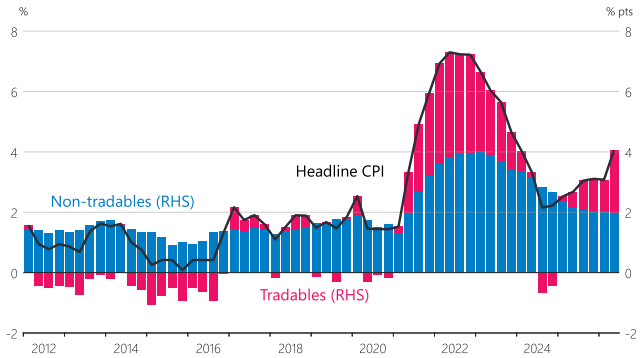
	Actuals								Projection		
March year	**2019**	**2020**	**2021**	**2022**	**2023**	**2024**	**2025**	**2026**	**2027**	**2028**	**2029**
Price measures											
CPI	1.5	2.5	1.5	6.9	6.7	4.0	2.5	3.1	**3.7**	**1.9**	**2.0**
Labour costs	2.0	2.4	1.6	3.1	4.5	3.8	2.6	2.0	**2.0**	**1.9**	**2.1**
Export prices (in New Zealand dollars)	1.2	6.8	-6.1	20.6	1.0	-2.2	10.9	0.8	**2.2**	**1.8**	**2.2**
Import prices (in New Zealand dollars)	4.1	2.3	-2.9	18.6	7.9	-4.4	6.6	-1.2	**6.6**	**-1.6**	**0.7**
Monetary conditions											
OCR (year average)	1.8	1.2	0.3	0.5	3.1	5.5	4.9	2.8	**2.6**	**3.1**	**3.2**
TWI (year average)	73.4	71.7	72.4	74.0	71.2	71.0	69.9	67.8	**66.7**	**66.9**	**66.9**
Output											
GDP (production, annual average % change)	3.3	2.3	-0.3	4.3	3.3	1.8	-0.9	0.8	**1.9**	**2.6**	**3.0**
Potential output (annual average % change)	3.1	2.6	0.0	2.0	3.5	2.8	1.5	1.3	**1.8**	**2.1**	**2.3**
Output gap (% of potential GDP, year average)	0.6	0.4	0.0	2.4	2.3	1.3	-1.0	-1.5	**-1.4**	**-0.9**	**-0.3**
Labour market											
Total employment (seasonally adjusted)	1.3	2.4	0.0	2.3	2.9	1.0	-0.9	0.5	**1.8**	**2.3**	**2.2**
Unemployment rate (March qtr, seasonally adjusted)	4.2	4.2	4.6	3.3	3.5	4.4	5.2	5.4	**5.4**	**5.0**	**4.6**
Trend labour productivity	0.8	0.9	1.0	0.9	0.6	0.5	0.5	0.4	**0.3**	**0.3**	**0.4**
Key balances											
Current account balance (% of GDP)	-3.9	-2.4	-2.5	-6.5	-8.3	-5.7	-4.3	-3.7	**-4.6**	**-3.9**	**-3.6**
Terms of trade (SNA measure, annual average % change)	-2.1	2.1	-0.5	0.4	-5.1	-0.9	3.4	4.7	**-5.9**	**3.2**	**2.0**
Household saving rate (% of disposable income)	-1.1	1.3	7.5	2.5	-2.2	1.0	1.5	2.1	**2.5**	**1.1**	**0.0**
World economy											
Trading-partner GDP (annual average % change)	3.5	1.7	-0.3	6.3	3.1	3.2	3.0	3.3	**2.8**	**2.8**	**2.8**
Trading-partner CPI (TWI-weighted)	1.4	2.5	0.9	4.1	4.8	2.2	1.8	2.2	**2.6**	**2.1**	**2.1**

Appendix 2: Chart pack

Figure 6.1

Composition of CPI inflation

(annual)

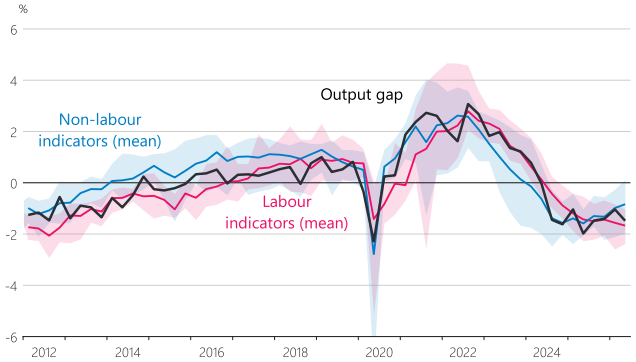


Source: Stats NZ.

Figure 6.2

Output gap and output gap indicators

(share of potential)



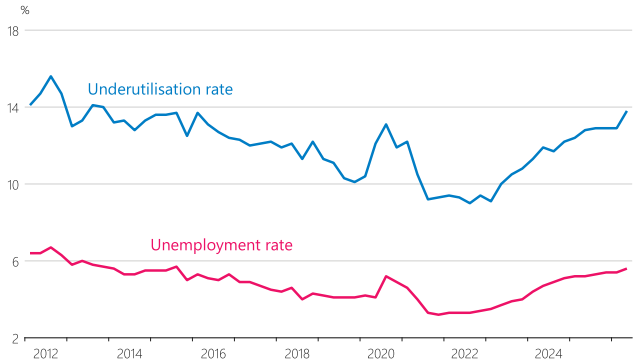
Source: NZIER, MBIE, Stats NZ, RBNZ estimates.

Note: The output gap indicators based on information from labour market surveys are shown separately from the other indicators. For each group of indicators, the shaded area shows the range of values and the line shows the mean value. The output gap estimate in the final quarter is based on our near-term GDP estimate.

Figure 6.3

Unemployment and underutilisation rates

(seasonally adjusted)

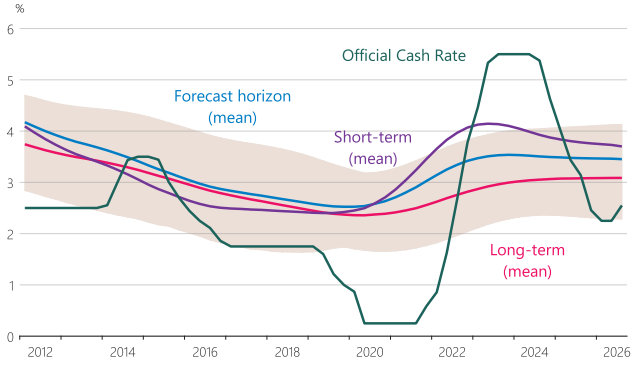


Source: Stats NZ.

Figure 6.4

OCR and nominal neutral OCR indicator suite

(quarterly average)



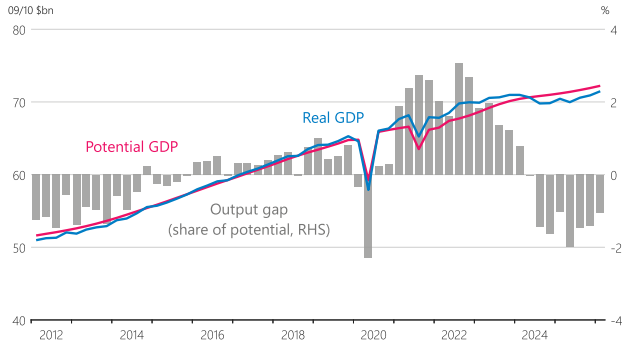
Source: RBNZ estimates.

Note: The shaded area indicates the range between the maximum and minimum values from our suite of long-run nominal neutral OCR indicators. See Castaing et al. (2024), Estimates of New Zealand's nominal neutral interest rate.

Figure 6.5

GDP and potential GDP

(seasonally adjusted)

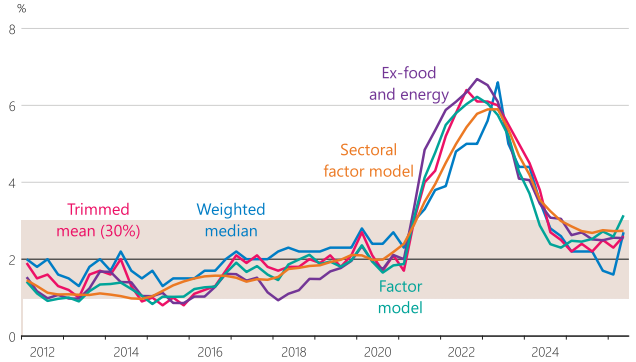


Source: Stats NZ, RBNZ estimates.

Figure 6.6

Measures of core inflation

(annual)



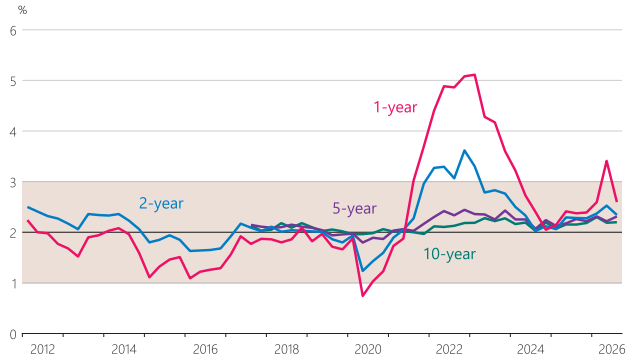
Source: Stats NZ, RBNZ estimates.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 6.7

Inflation expectations

(annual, years ahead)



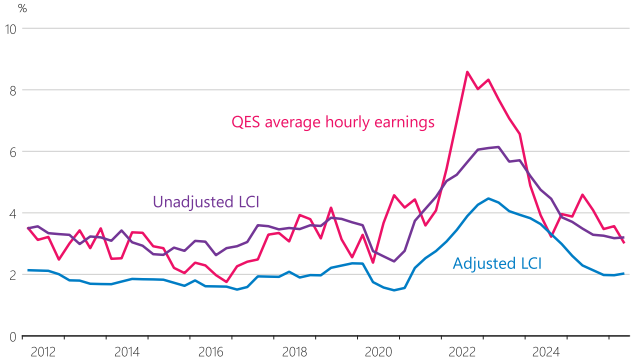
Source: RBNZ *Survey of Expectations*.

Note: The shaded area represents the MPC's 1 to 3 percent target range for annual CPI inflation over the medium term.

Figure 6.8

Private sector wage growth

(annual)

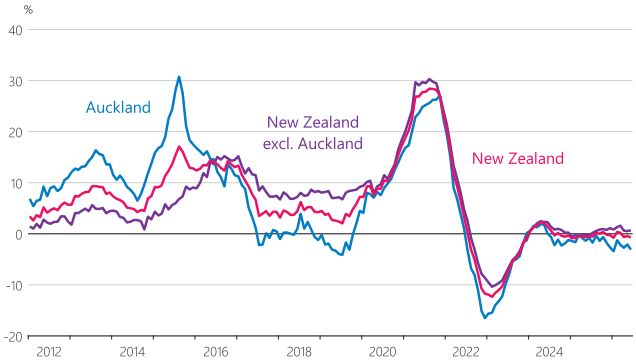


Source: Stats NZ.

Figure 6.9

House price inflation

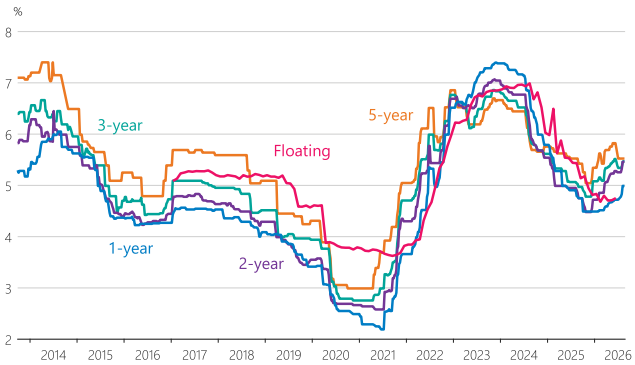
(annual)



Source: REINZ.

Figure 6.10

Mortgage interest rates



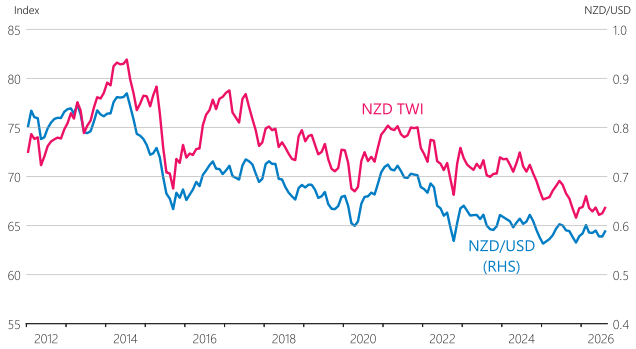
Source: interest.co.nz, RBNZ estimates.

Note: The rates shown for the fixed terms are the average of the advertised rates from ANZ, ASB, BNZ, and Westpac, shown as weekly data. The floating rate represents the monthly yield on floating housing debt from the RBNZ *Income Statement* survey.

Figure 6.11

New Zealand dollar exchange rates

(monthly average)

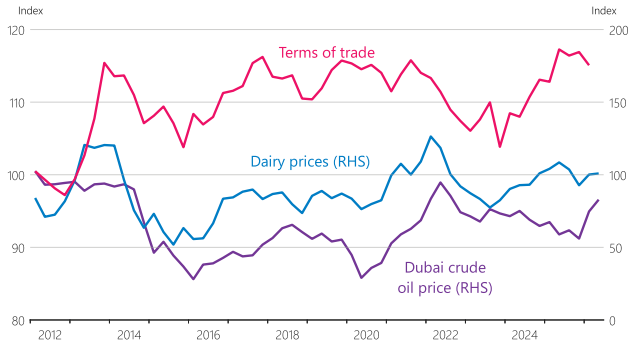


Source: NZFMA, RBNZ.

Figure 6.12

Terms of trade, dairy, and oil price indices

(index = 100 in the September 2008 quarter, quarterly average)



Source: Stats NZ, Global Dairy Trade, LSEG, RBNZ estimates.

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