

# New Zealand Fixed Income Monthly June 2023

Yield curve among factors underscoring low probability of rate hikes

By Ian Bellew, Senior Fixed Income Manager  
12 July 2023

## Further interest rate moves unlikely ahead of October general election

The Reserve Bank of New Zealand (RBNZ) indicated in its latest Monetary Policy Statement in May that the current interest rate hiking cycle is by and large complete, with the Official Cash Rate (OCR) having peaked at its current level of 5.5%. The central bank also signalled that it is unlikely to cut the OCR in the near future, stating its intention to keep interest rates at a restrictive level for some time in order to keep inflation under control. In addition, New Zealand has a general election scheduled for 14 October 2023, further reducing the likelihood of near-term moves in the OCR. Given that central banks generally avoid acting in ways that may be seen as political, we believe further action on rates is unlikely between now and October unless a major shock occurs in the economy. Although the race between New Zealand's two main political parties (the Labour Party and the New Zealand National Party) is currently difficult to call, we also believe that the election's impact on the economy (and, by extension, bond markets) is likely to be evolutionary rather than revolutionary regardless of its result.

## New Zealand's current yield curve consistent with pause in monetary policy

New Zealand's current bond yield curve also illustrates the diminished prospect of further rate hikes in the future. Although yield curves typically slope upwards at the back end given the higher risk assumed with longer term securities, New Zealand's yield curve is currently inverted, with shorter term bonds at the front end offering higher yields than longer dated bonds at the back end. This reflects expectations that New Zealand's interest rates will decline rather than rise in the future. In the current situation, we believe that the front end of the curve presents a less complicated prospect for the market than the long end. For example, a high-quality short-term asset with a yield of approximately 6% or higher may provide a certain level of reassurance regardless of whether the RBNZ unexpectedly hikes the OCR by another 25 basis points in six or nine months' time. At the same time, some investors may also be looking for opportunities at the longer end of the curve given the possibility of interest rates falling in the future.

## Increases seen in central and local government bond issuance

Although bond issuance has been scarce overall in the past month, the weekly amount of government bond issuance was recently increased from New Zealand dollar (NZD) 400 million to NZD 500 million. The government has also announced the syndication of a new 2033 maturity bond, most of which is likely to be placed offshore. In addition, the New Zealand Local Government Funding Authority, a collective funding vehicle for local government authorities, is ramping up bond issuance from its historical level of about NZD 3 billion per year to over NZD 4 billion per year going forward.

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