

Input to your Strategy for Adapting to Challenges

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ISSN: 2703-2825

23 October 2025

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Employment will turn

In my five monthly surveys I ask a range of questions aimed at allowing myself and others to get a feel for how some key things may be changing. The prices measure from my real estate agent survey for instance gives a good reading on what average house prices are doing around the country ahead of the eventual release of “official” data.

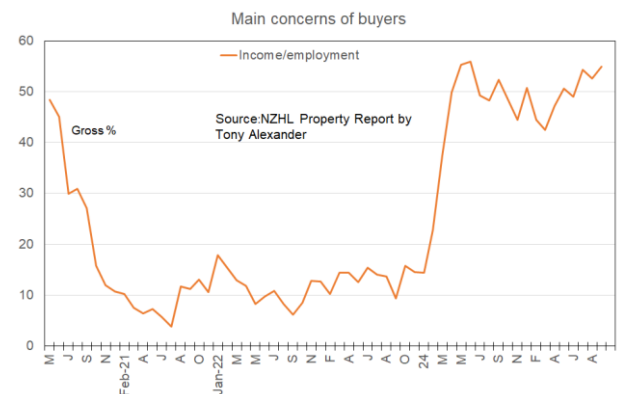
We can also gain early insight into shifts in the willingness of consumers to spend and that is very important because typically in a modern economy some 65% of spending is undertaken by households.

I also can get a broad feel for how the labour market is tracking and that is important because it looks like it is the lack of feelings of job security which is holding back some elements of the housing market.


If the labour market indicators I gather start to turn upward overall, then that would be useful information for someone contemplating likely changes in house prices but more especially the degree to which preparations should be made for higher consumer spending.

So, what do the bloody entrails hint at once thrown on the ground in front of us?


First, people do not feel secure in their jobs as yet. A gross 55% of real estate agents three weeks ago said that buyers are worried about their jobs. This is near the record high of 56% reached in June last year and up from 42% in March.




We also gain some insight into job security feelings from my Spending Plans Survey. Offsetting the net proportion of people saying they will spend more against those saying less for reasons of expecting more work time, the latest result is -3%. This is down from -2% in September




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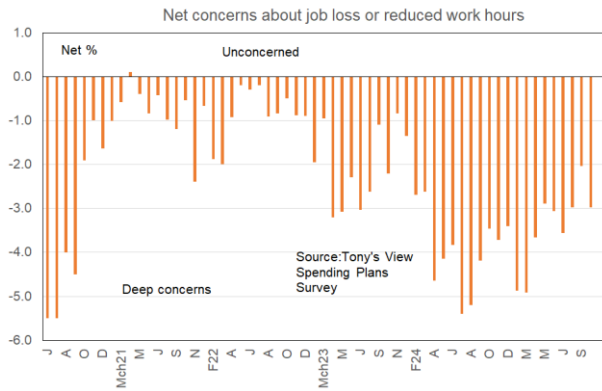
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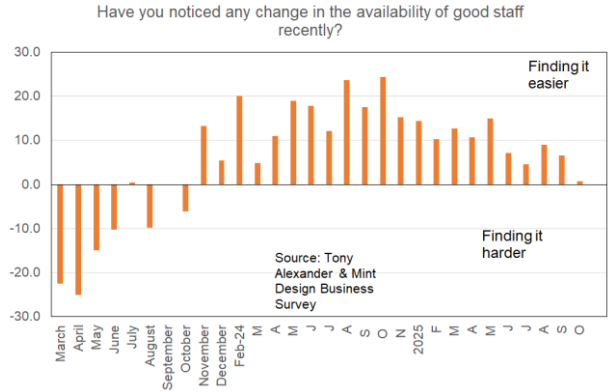
and not yet all that different from most results since the start of 2024 when job security disappeared – as seen in the real estate agent survey above.



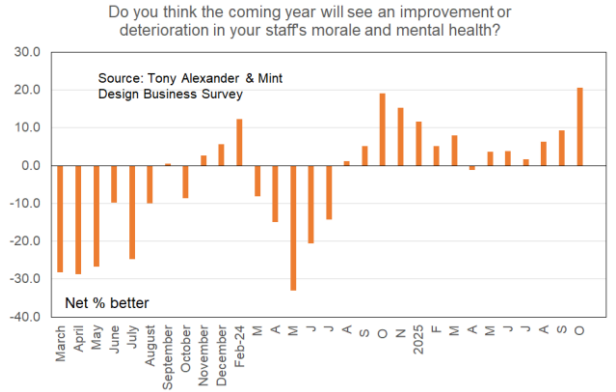
Second, are there signs that businesses may however be thinking more seriously about hiring? Yes, according to my survey of businesses although the measures are at low levels and have only recently turned. Solidity is not there yet.

Businesses are less and less finding it easy to get the staff they want. They do not perceive that on average they can throw an ad out there and then pick and choose amongst the wonderfully skilled and motivated applicants.

This is shown in the following graph by the latest observation falling almost to a net zero when businesses are asked how easy people are to find.



A strong net 21% of businesses reckon that their staff are going to feel a lot happier in a year's time. That is, they feel their actions and the likely improvement in the economy will work to improve feelings of job security and happiness – as illustrated by the jump up in the measure I gather shown in the next graph.



Businesses are beginning to make preparations for hiring more people with more indicating that they intend lifting spending on recruitment. This is shown as the upward trend in the following graph of the net proportion of businesses planning higher expenditure in this area.

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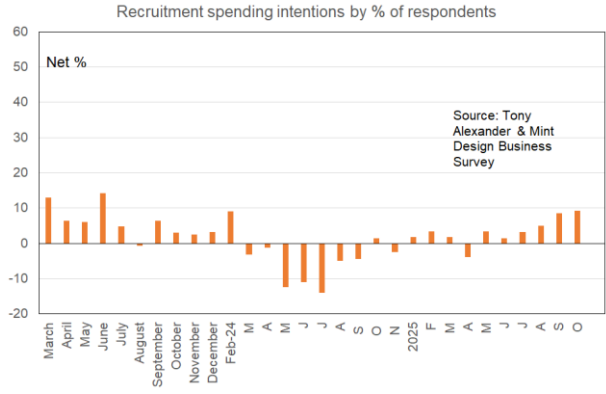
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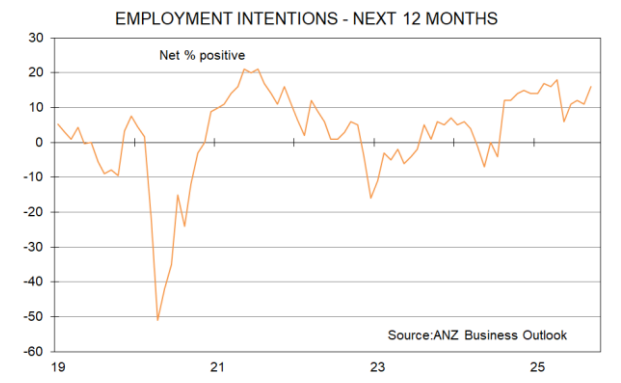
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We are almost certainly past the weakest period for the New Zealand labour market. Improvement lies ahead and forward-thinking businesses will already have shed excess and less productive staff and should be well into the next phase of sorting out what types of people to source when their willingness to back better growth expectations lifts a tad further.

I reckon we'll see this transition in my surveys well before it gets picked up elsewhere – although keep a close eye on the ANZ Business Outlook survey. Their employment intentions measure has been trending up since June although it has yet to regain the level seen in April.



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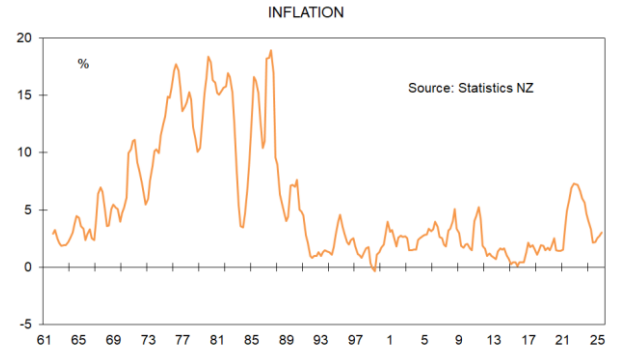
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It is impossible to know when that transition on average from believing in an upturn to actively preparing for it will occur. But the chances are good that the better businesses will be actively recruiting even while the media continue to focus on the tail-end Charlies of companies laying off staff only now having probably been up the creek without a decent paddle for years.

Inflation accelerates

On Monday we learnt that the annual inflation rate in New Zealand accelerated to 3% in the September quarter from 2.7% in the June quarter and 2.2% a year earlier.



This is an unusually high rate of inflation when we consider that over the year to June the economy shrank by 1.1% and the unemployment rate rose

from 4.7% to 5.2%. Are the various underlying measures which we economists tend to look at to try and see what is happening away from special factors looking any better? Only to a limited extent.

If we focus just on the non-tradeables part of the CPI over which the Reserve Bank's influence on the economy can in turn have some influence, we see inflation at 3.5%. This is down from 4.9% a year ago and equal to the long-term average. In that regard it is good and bad.

Good in that this rate has appreciably fallen – bad in that the weak state of the economy and plentiful spare capacity have only been able to produce average and not below average non-tradeables inflation. That is concerning.



If we focus on the measure which excludes the sometimes volatile energy elements, then the annual rate is 2.5% from 3.1% a year ago. This is good, but again not as good as one would want considering the shrinkage in the economy.

There is a lot of faith on the part of the Reserve Bank and many analysts that the inflation rate will now fall as the pace of growth in the economy accelerates. It probably will. However, a lot of reliance is placed on measures showing a strong freeing up of capacity in the economy – meaning restraint on inflation even as growth lifts.

The problem here is that some measures are already tightening up. For instance, a year ago in the NZIER's Quarterly Survey of Business Opinion a net 26% of businesses said that it was easy to find skilled labour. That proportion has now fallen to just 10%. The proportion saying unskilled people are easy to find has decreased from 57% to 31%.

As noted above, there are signs that the labour market is tightening up early in the economic recovery cycle. Add in compressed margins and indications from businesses of above average pricing plans and we get some high risks attached to the view that accelerating economic growth will produce falling inflation and a settling of such in the middle of the target band.

We should add in also the likely upward turning of the house price cycle over summer, a mild inflation boost from the recent weakening of the NZ dollar, and probably easing of fiscal policy as we get through election year.



The outlook for inflation comfortably falling and settling low as growth accelerates 4% is risky and that means relying on short-term financing rates staying low for the next few years is well against the odds.

If I were a borrower, what would I do?

Wholesale bank borrowing costs have edged slightly lower again this past week. The one year swap rate for instance has decreased to near 2.37% from 2.41% last week, and 2.8% six weeks ago. The three year rate is near 2.6% from 2.67% last week and 3% six weeks back.

Rate declines mainly reflect some further easing of rates in the United States as investors grow wary at the margin of the ability of the US sharemarket to maintain its high levels and switch to other assets such as gold and US treasuries.

Local data in New Zealand have been thin on the ground this week with just the September quarter inflation number attracting attention. The increase of 1% for the quarter and 3% for the year met expectations by and large.

Scope for further declines in wholesale rates looks fairly limited – but we have all said that before many times over recent months and still the Reserve Bank have kept easing and US rates have crept lower.

For borrowers who actively manage their interest rate risk the issue is one of how long to keep punting that rates will fall further. But even then, once a consensus is formed that rates are at their lows for the cycle, the debate will still be afoot regarding when to shift from cheap short-term rates to more expensive medium to long-term

rates which will give some insulation when rate risks and movements shift to the upside – as always eventually happens.

It is impossible to know when the medium to long-term rates properly commence their cyclical march upward. That means it comes down to one's degree of risk aversion. I am quite risk averse and that means I would personally be happy to fix five years at 4.99% currently and both pay more than fixing short and run the risk that the five year rate falls slightly further.

Most people however will fix short and take the immediate cash outflow candy. The effectiveness of monetary policy depends on myopic borrower behaviour.

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