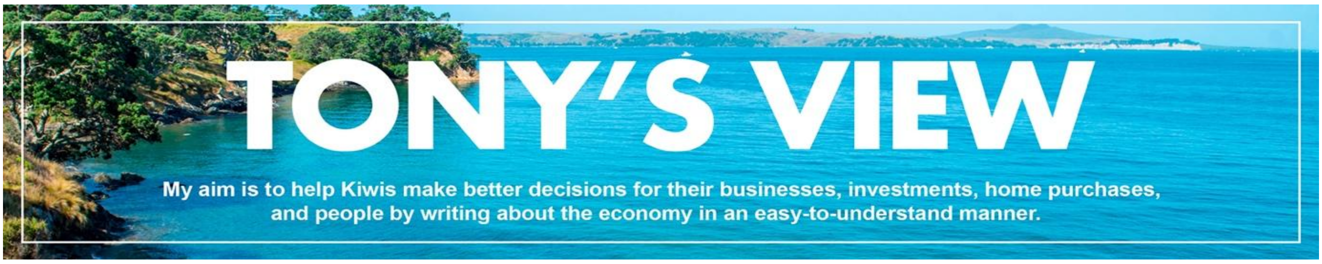

Input to your Strategy for Adapting to Challenges

Feel free to pass on to friends and clients wanting independent economic commentary

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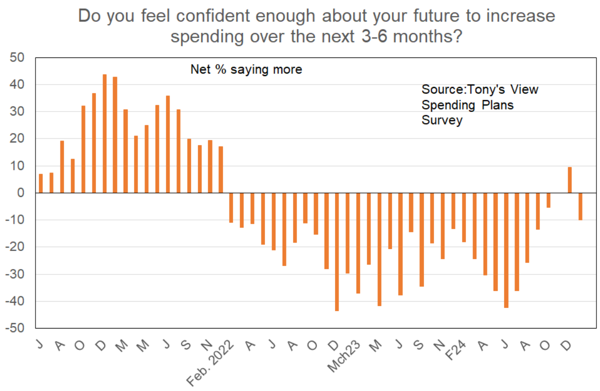
Survey findings

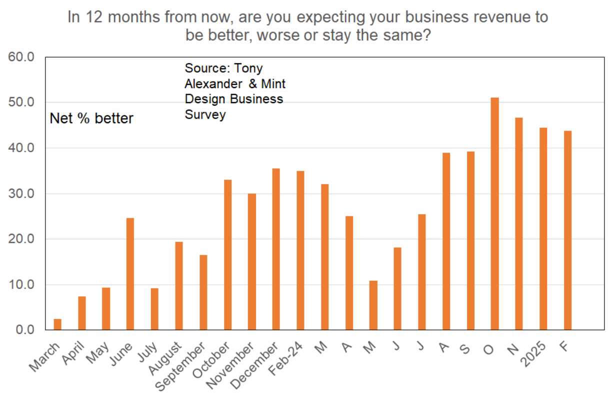
I've completed the five surveys I run each month and here are a few of the main insights I've been able to glean from them.

First, there has been a New Year decline in consumer sentiment and that accords with my view that a reality check is running through the economy. Low interest rates will not immediately bring better times for all. Retailers will need to keep their revenue projections in check for at least the first half of the year and be aware that as the period of "weeding out" extends through this year, cream will rise to the top.

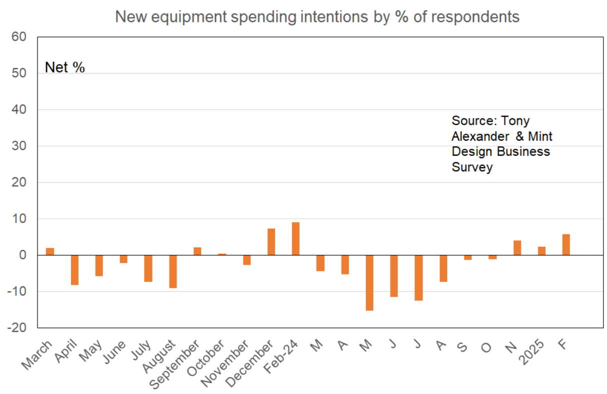


That is, out of the tough conditions of the past three years some survivors will thrive as others less well managed fall to the wayside or get rationalised in some way.

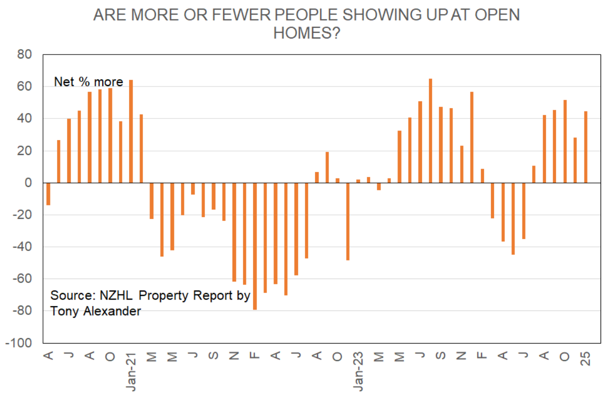
Businesses generally are happy to have survived to 2025 but increasingly are disappointed with the environment they find themselves in, very unhappy with the state of politics and political leadership in the country, and concerned about still rising costs.



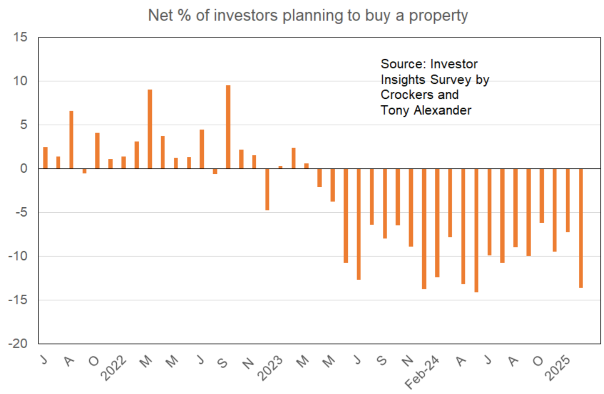
But they are signalling that they plan spending more on plant and machinery and especially technology. So, that is good for the sustainability of the improvement in the economy and the possibility of some better productivity growth. But it's hardly a boom.



Real estate agents are seeing more buyers coming forward. But there are also plenty of sellers and the country is in a very strong buyers' market which is bringing reducing expectations for capital gains.



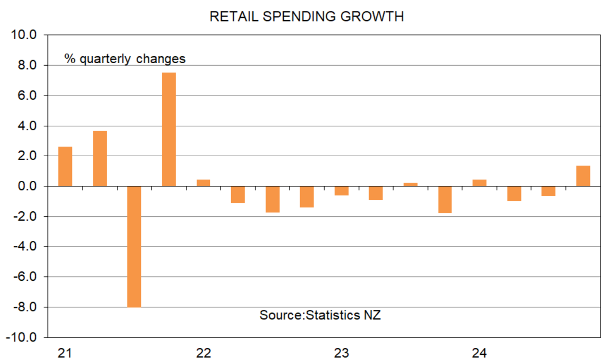
This is occurring even as banks ease their lending rules. For owner occupiers there is a lot of uncertainty about incomes as the unemployment rate rises. For investors there are rapidly rising costs holding many back, and there seems to be no shortage of investors looking to sell.



Basically, the economy is probably on the way back up again, but the growth looks set to be very slow and this housing cycle the capital gains look like being minor.

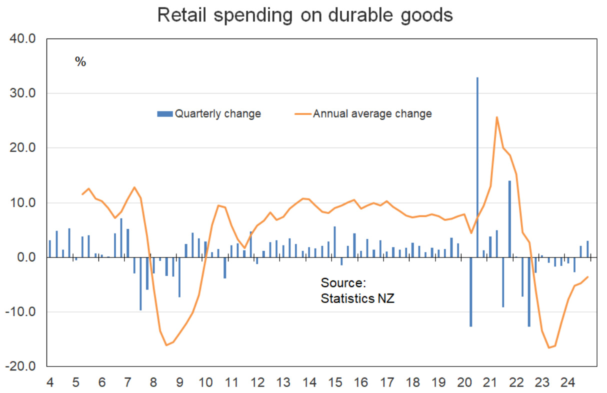
Retail spending grows

There was a small recovery in retail spending in New Zealand during the December quarter. After adjusting for inflation and the usual seasonal factors spending rose by 0.9% after sitting flat in the September quarter and falling 1.2% in the June quarter of last year.

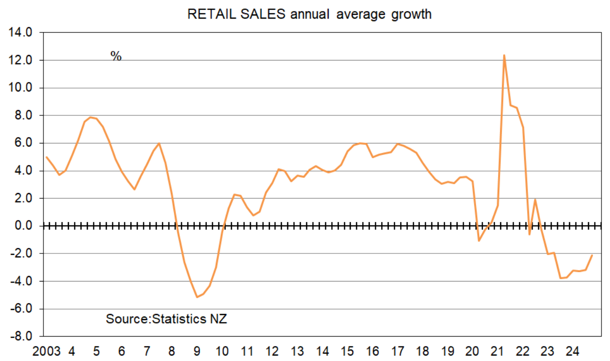


The result was slightly better than expected and the most noteworthy point was a 3% rise in

spending on durable goods following a 2.1% rise in the September quarter.

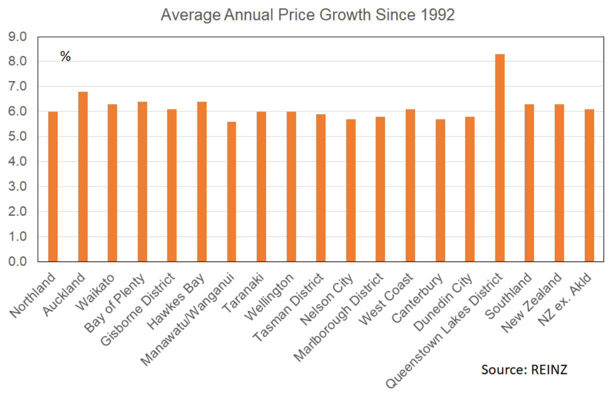


This tells us that there is some solidity to the improvement in household spending. But the rise follows a period of falling sales volumes and much of the improvement is likely simply to be a recovery from lows rather than a shift towards optimism and income-fuelled spending growth.



Long-term house price changes

For your guide, here is a graph showing the average annual increase in prices since 1992 (32 years covered) for all regions around the country. NZ and ex-Auckland NZ outcomes are on the far right.



These are the numbers.

	Average annual rise in prices 1992-24
Northland	6.0%
Auckland	6.8
Waikato	6.3
Bay of Plenty	6.4
Gisborne District	6.1
Hawkes Bay	6.4
Manawatu/Wanganui	5.6
Taranaki	6.0
Wellington	6.0
Tasman District	5.9
Nelson City	5.7
Marlborough District	5.8
West Coast	6.1
Canterbury	5.7
Dunedin City	5.8
Queenstown Lakes District	8.3
Southland	6.3

New Zealand	**6.3**
NZ ex. Akld	6.1

Queenstown's 8.3% reflects lack of land availability plus strong population growth. Canterbury has land available. Auckland has strong population growth but low land availability up until 2016.

If I were a borrower, what would I do?

Banks are concentrating their competition for home mortgage business in the 6 – 24 month terms. There is a three year rate of 5.29% on offer which is good but not as good as the 4.99% rate which lasted for just two weeks.

If I were borrowing currently, I would probably stay floating waiting for the competition to shift back to the three year term and fix at 4.99% or just over 5%.

Most people will probably fix two years and that seems okay. But if that is you then you'd best be aware that your rate will come up for renewal in early-2027 by which time I expect 3-5 year rates to be higher than they are now and monetary policy to be close to tightening again.

It pays to remember that a cyclical recovery in economic activity will drive a cyclical recovery in inflation. That will also drive a cyclical rise in interest rates but because the financial markets are forward looking, we will get wholesale borrowing cost increases well before monetary policy starts tightening.

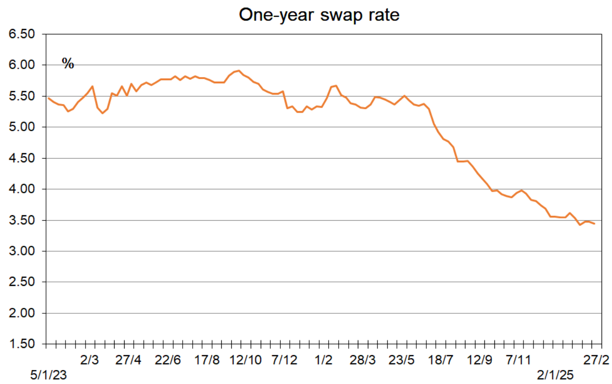
For the moment I feel people have time on their sides to allow some calm decision making. Momentum is downward. But people should not expect a return to low rates of the period 2018-22.

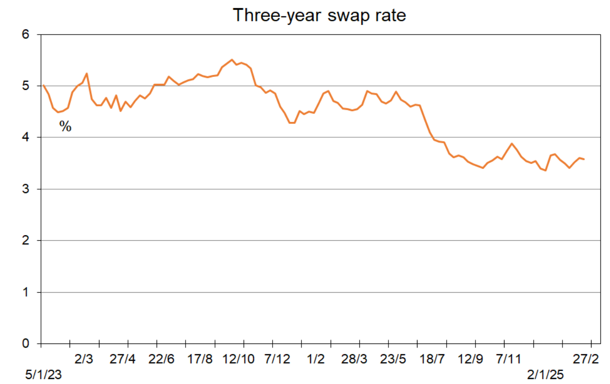
Not only is there upward pressure on inflation to come from the cyclical recovery there are rising electricity prices, soaring council rates (they are monopolies so can be guaranteed to boost prices greatly), climate change-related costs, plus higher global tariffs feeding higher world inflation.

It pays to remember that New Zealand's inflation rate of 2.2% has not been caused by a below average outcome in the inflation we generate here. On average we produce price rises (non-tradeables inflation) of 3.5% and the latest rate is above that at 4.5%.

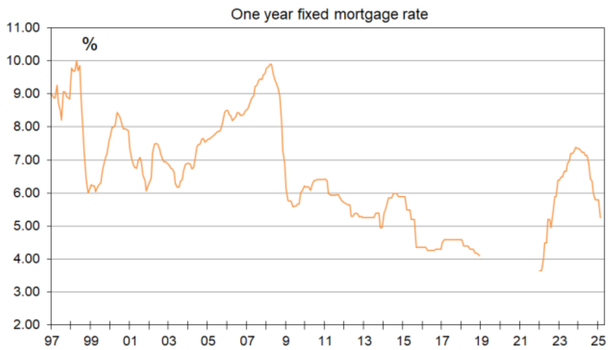
The inflation which arrives from offshore (tradeables) averages 1.4% but is running at -1.1%. It does not seem reasonable to expect that this divergent situation of unusually and below average offshore inflation to continue. The simple absence of it will threaten 3% inflation overall eventually in New Zealand.

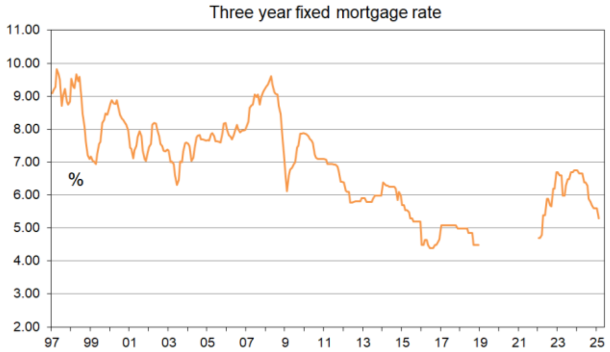
This week wholesale interest rates haven't done anything of great importance. There has been just some mild downward pressure from a bout of weaker than expected data in the United States, most notably two consumer sentiment gauges.

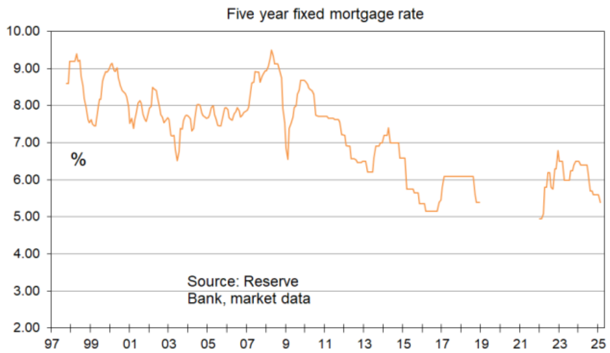




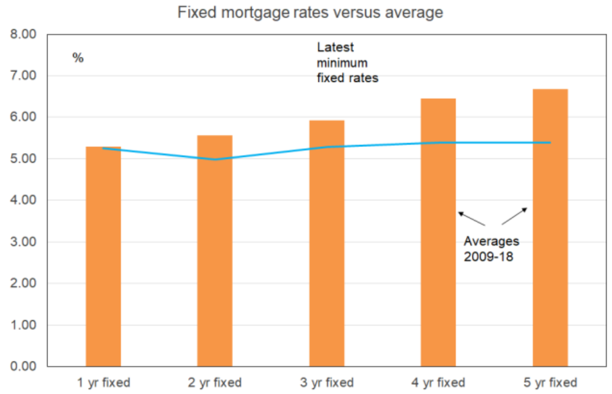
These three graphs show mortgage rates since 1997 excluding the period of deflation worries (2019) and the pandemic.







This graph shows how current rates compare with averages from 2009-19.



To see the interest rates currently charged by major lenders go to www.mortgages.co.nz

Nothing I write here or anywhere else in this publication is intended to be personal advice. You should discuss your financing options with a professional.