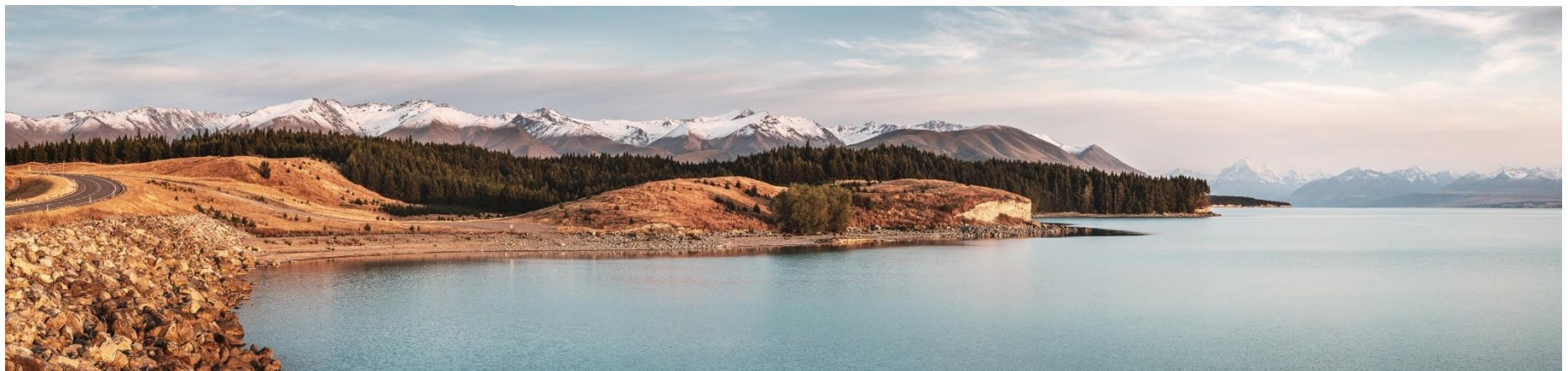


SALT

New Zealand Chartbook

Bevan Graham, Economist

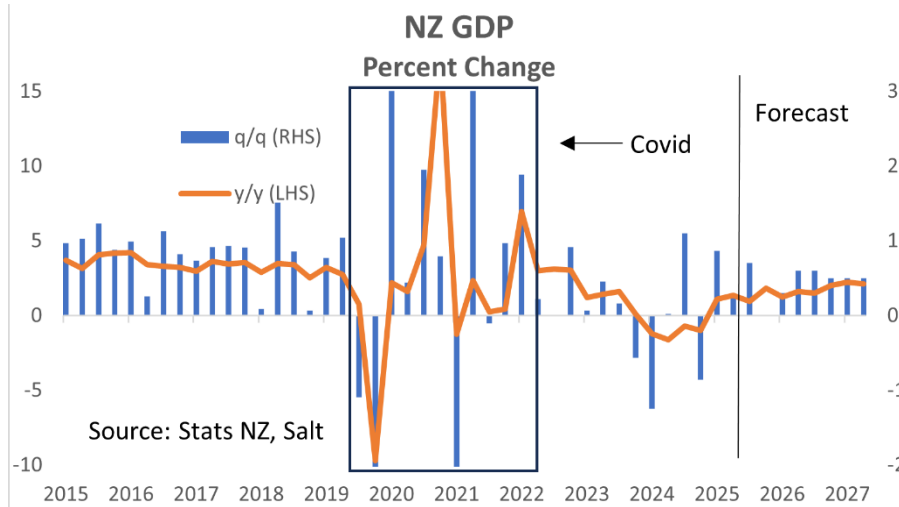
May 2026



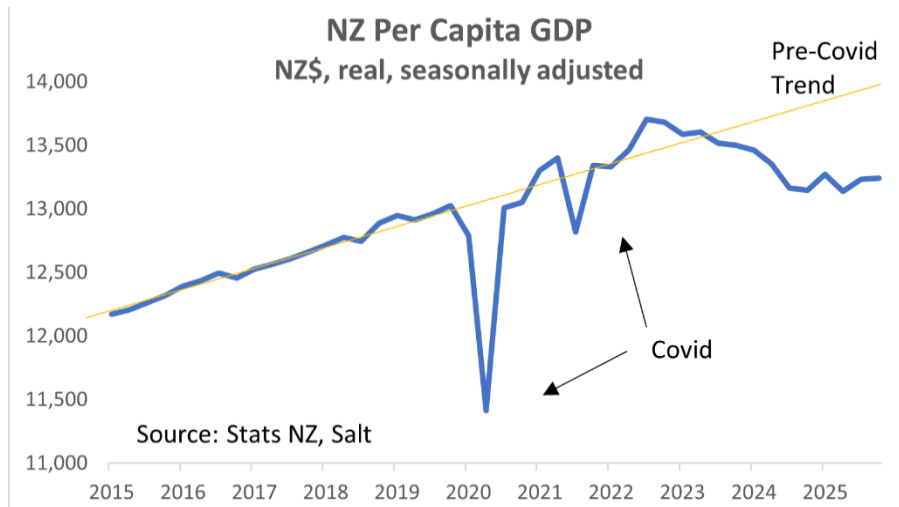
Highlights

- **The New Zealand economy has recently been slowly recovering from a prolonged recession.**
- **The onset of the war in Iran has delivered a stagflationary shock to the recovery. Growth will suffer on the back of higher fuel prices, while headline inflation will move sharply higher in the near-term.**
- **Inflation was already at the top end of the target band as the war started. We see headline inflation breaching 4% in the June quarter of this year. The monetary policy response will be determined by the extent of second-round inflation impacts which will take some time to show through.**
- **In the meantime, we expect the RBNZ to start removing current stimulatory monetary conditions in September this year, but there is a high degree of uncertainty around the view. Much depends on how the war plays out from here.**
- **The labour market was beginning to show early signs of improvement with modest employment growth and a tick down in the unemployment rate in the March quarter. However, employment intentions moved sharply lower following the start of the war, so the labour market is not completely out of the woods yet.**
- **Market attention is starting to focus on the Budget later in May. Fiscal consolidation is proving challenging as demonstrated by the recent downgrade to the outlook to our Sovereign credit rating by Moody's.**

The stagflationary implications of the war in Iran

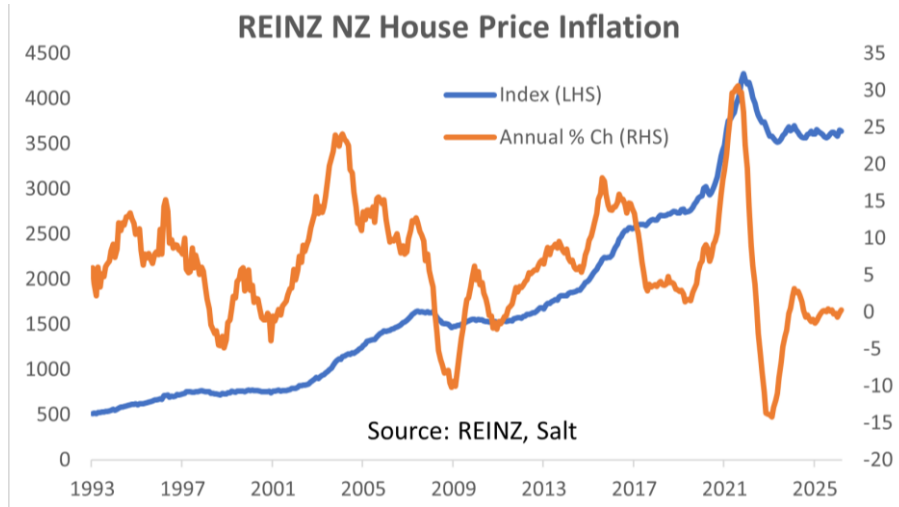


Prior to the war, the economy was meeting our expectations of a slow, grinding recovery. Quarterly growth numbers were proving exceptionally volatile but annual growth of 1.3% in the year to December was probably an accurate reflection of the pace of the recovery. Sharply higher oil prices will provide a new unwelcome challenge with a real risk of a return to contraction in the period ahead.

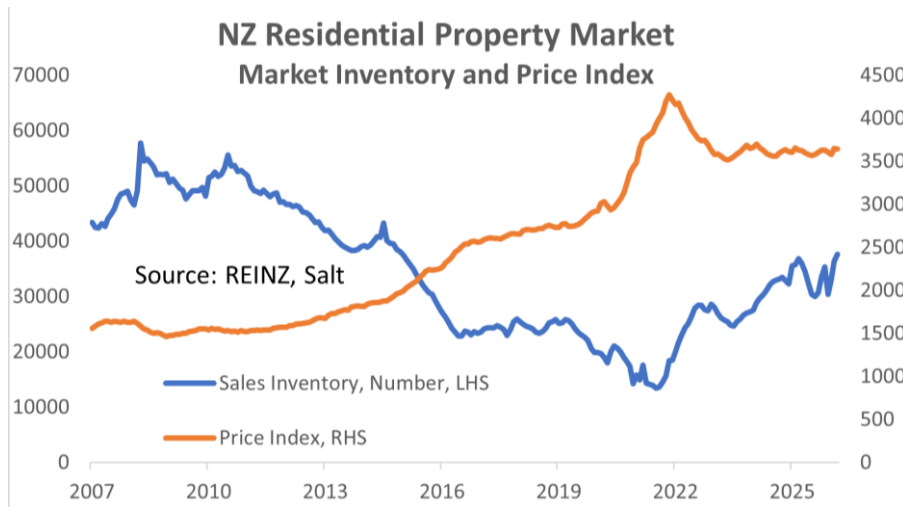


Such has been the subdued nature of the recovery that per-capita growth has only stabilised following a significant decline during the recession. The December 2025 level was still over 3% below the peak in 2022, though to be fair that was boosted by the recovery from Covid. Still, per-capita GDP remains well below the trend it was on prior to the pandemic.

No tailwind from house price inflation...

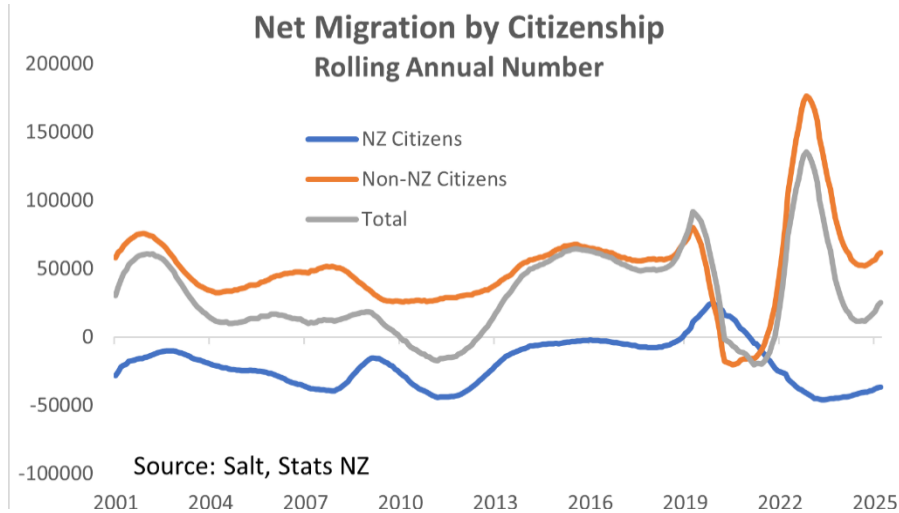


House price inflation has been a traditional tailwind to economic growth as households benefit from the wealth effect of higher prices. However, house prices remain soft in the early months of 2026, reflecting the ongoing impact of a host of cyclical and structural factors. The annual rate of change currently stands at +0.3% in the year to March. The key question now is the extent to which the Iran war impacts activity.

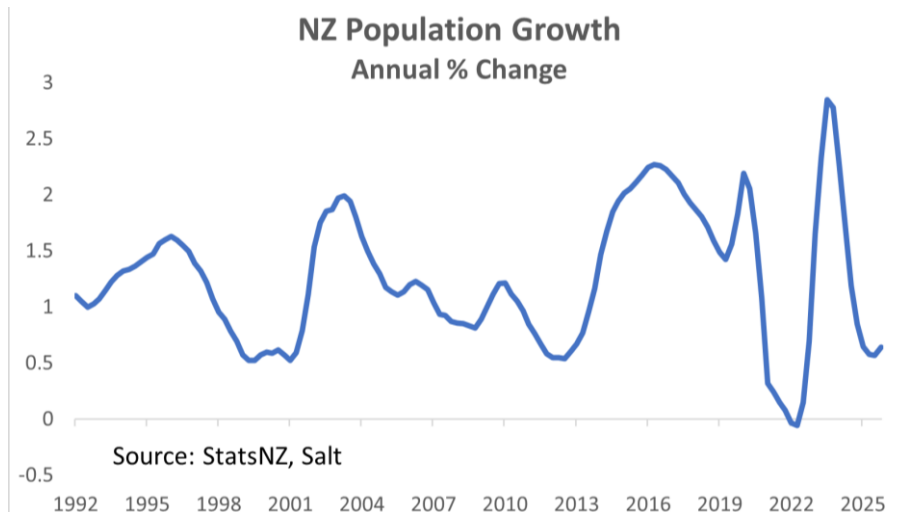


One of the key constraining factors is the level of inventory which remains at decade highs. Lower population growth, still high interest rates relative to the last cycle, too high vendor price expectations, the ageing population and public policy initiatives that have boosted housing supply and land availability are key factors that are expected to keep house price inflation in check in the period ahead.

Net inward migration recovering more quickly than anticipated

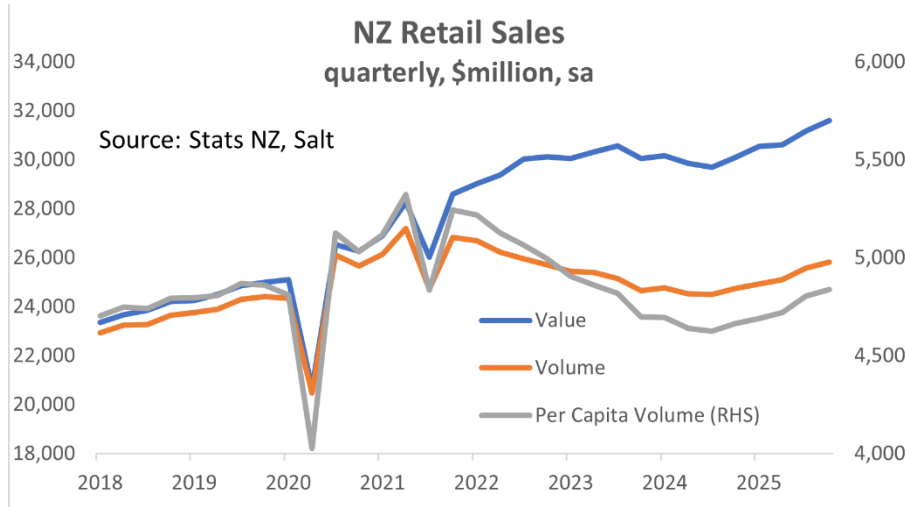


Net migration has clearly turned the corner, with a net inflow of +25,100 people in the year to February. That reflects a net outflow of -36,400 NZ citizens offset by a net inflow of +61,600 non-NZ citizens. The recovery has been sharper than I expected, with net inflows rising from a low of +11,500 in the year to last August and now moving back toward the long-run average of around +30,000 per annum.

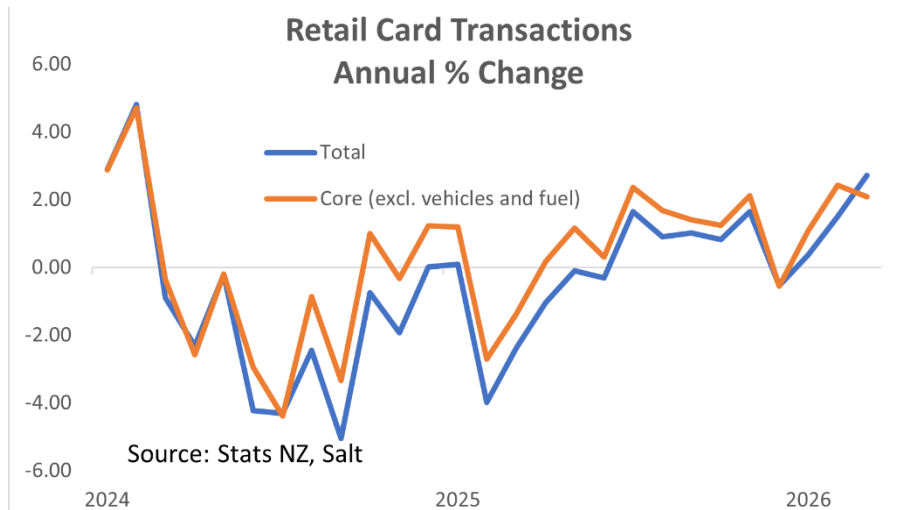


As net migration has turned around, so too has population growth. The stronger population backdrop should support headline GDP growth at a time when the economy has been struggling. But don't confuse population growth with productivity growth. While New Zealand absolutely needs skilled migrants choosing to ply their trade here, migration-led growth does little for living standards if it is not accompanied by stronger productivity and capital investment.

Retail spending recovering slowly

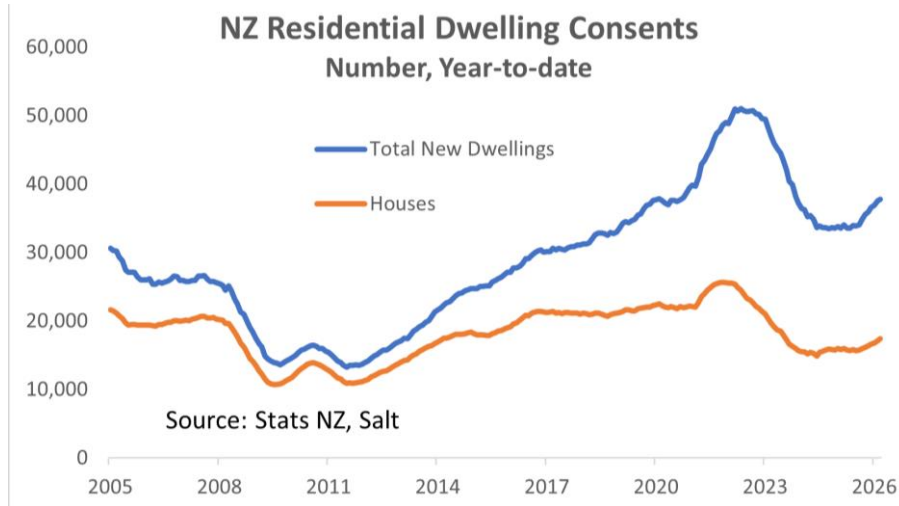


NZ retail sales were stronger than expected in the December quarter with the volumes of sales up +0.9% over the 3-month period and +4.4% over the year. Also good to see per-capita sales continuing their recovery, up +3.7% over the year to December. We expect sales rose again in the March quarter (see more timely card transaction data below), but beyond that it's about the impact of the higher fuel prices.

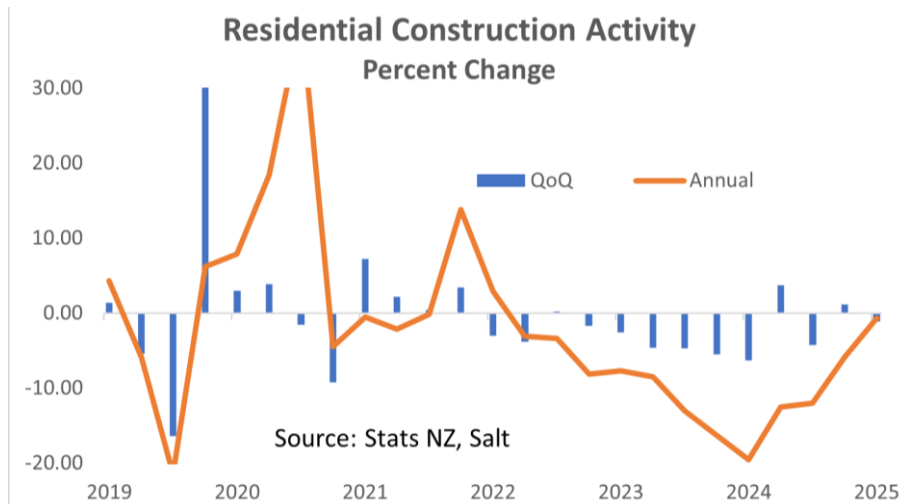


Electronic card transactions rose 0.7% in the March month, driven (pun intended) by a 17% increase in spending on fuel. Core sales (excluding fuel and motor vehicles) held up better than expected, falling only -0.1% in the month. That said, the biggest drag was in discretionary spending items such as hospitality and apparel. But it's early days. An extended period of higher fuel prices will create a bigger headwind for core spending in the period ahead.

Residential construction turning the corner

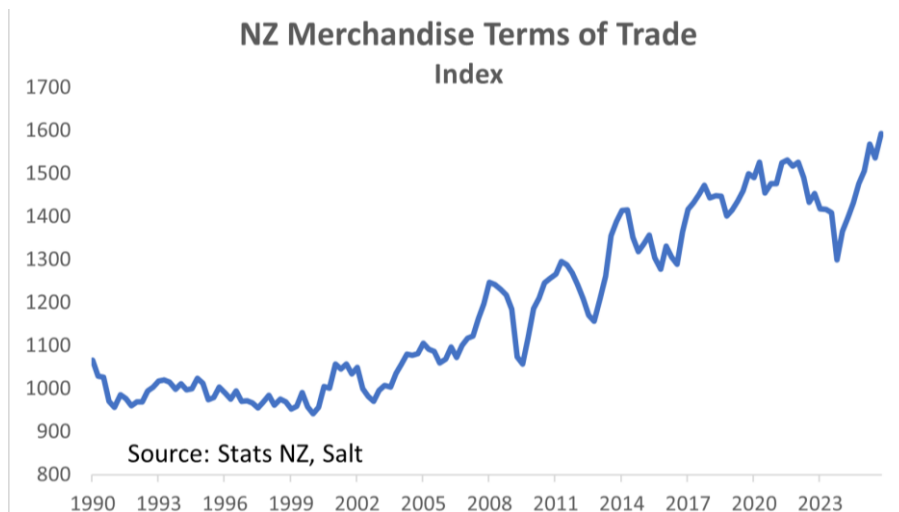


New Dwelling consents fell sharply over 2023 and 2024 before stabilising through 2025. A recovery is underway with 37,800 permits issued for the year to March 2026, a level not seen since mid-2020. This recovery is likely built on lower interest rates, stable house prices and, more recently, a recovery in net migration.

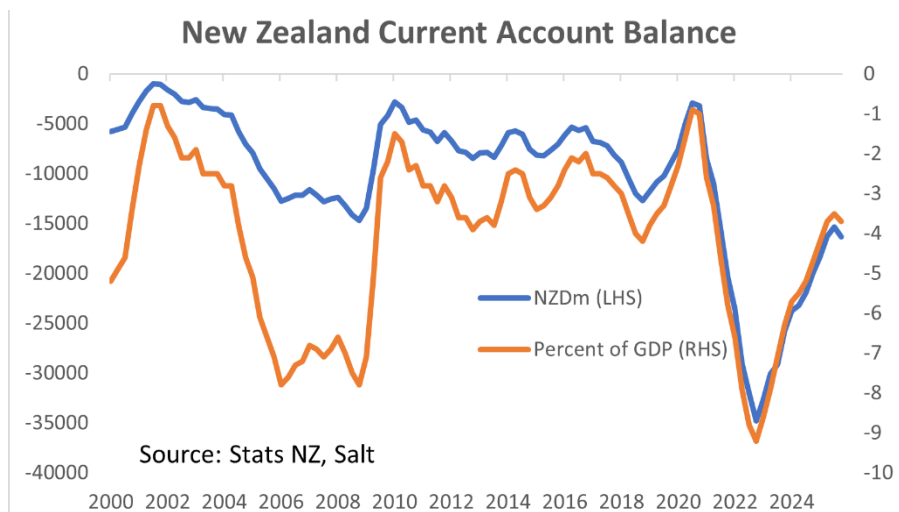


Of course, a permit is just an intention to build. Actually residential construction activity is lagging the recovery in permits. Residential building work put in place stabilised over the later part of 2025, though the annual rate of growth is only back to zero. Look for a recovery to emerge in the second half of the year, though uncertainty created by the war may yet dent any renewed confidence.

Terms of trade will be hit by higher oil prices

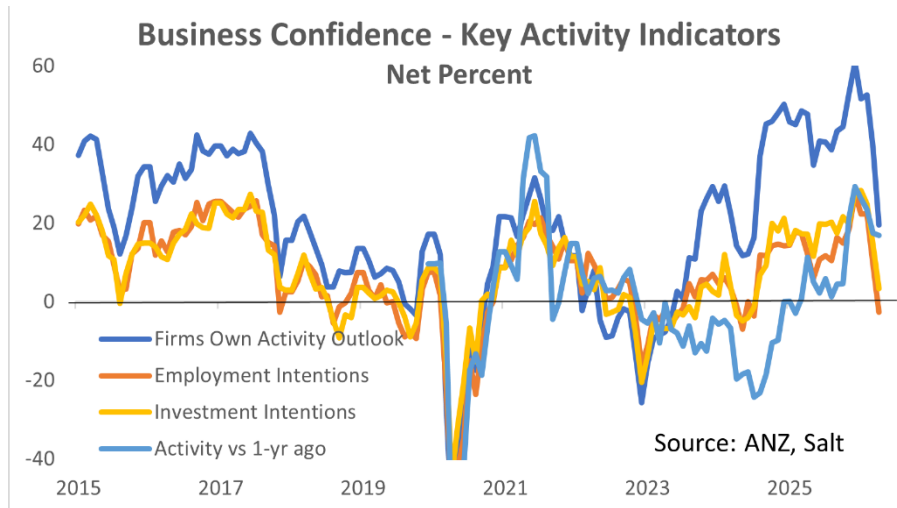


NZ's Terms of Trade index moved back to a record high at the end of 2025. Higher prices for our key export commodities has been a key support for the economy, particularly in the regional centers, as other historical supports have been absent. The terms of trade will likely take a hit in the next quarter from higher import (fuel) prices.

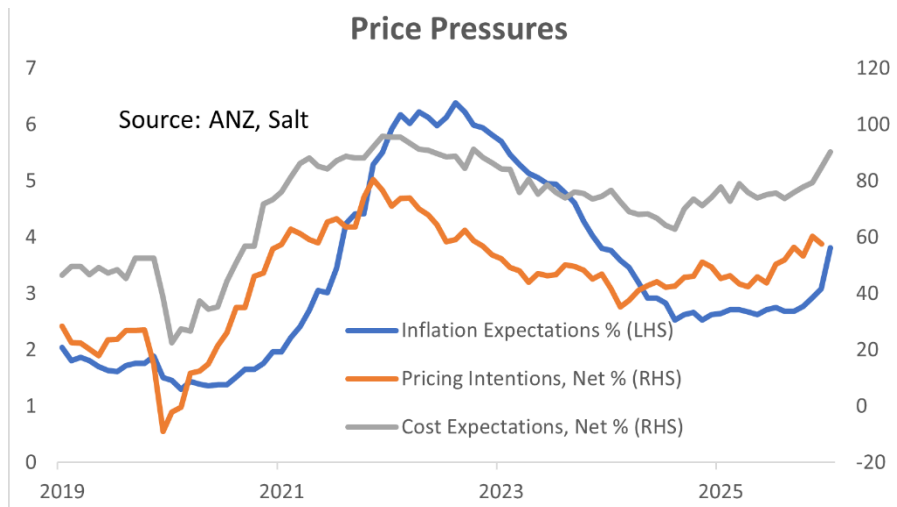


The improved terms of trade has been a key contributor to the impressive improvement in our current account position which bottomed out at -9.2% of GDP at the end of 2022 and stood, after a modest deterioration, at -3.7% at the end of 2025. We were already expecting a deterioration through 2026 as the emerging recovery drew in more imports, but this will now be exacerbated by the higher fuel prices.

Business confidence takes a hit from the war

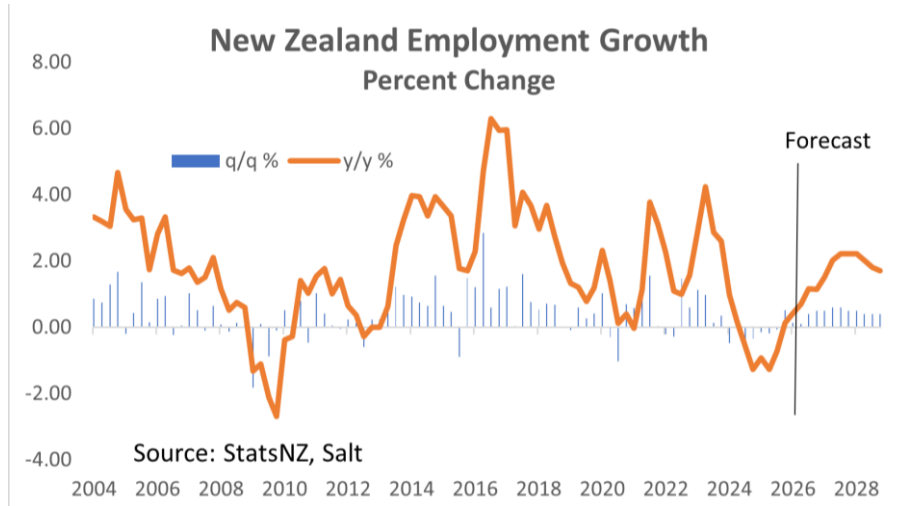


The April ANZBO survey showed the expected weakness across the key activity indicators. Firms' expectations of their own activity outlook fell from +39.3 to +19.6 over the month, while intentions relating to employment and investment were also sharply lower in the face of the uncertainty created by the war in Iran.

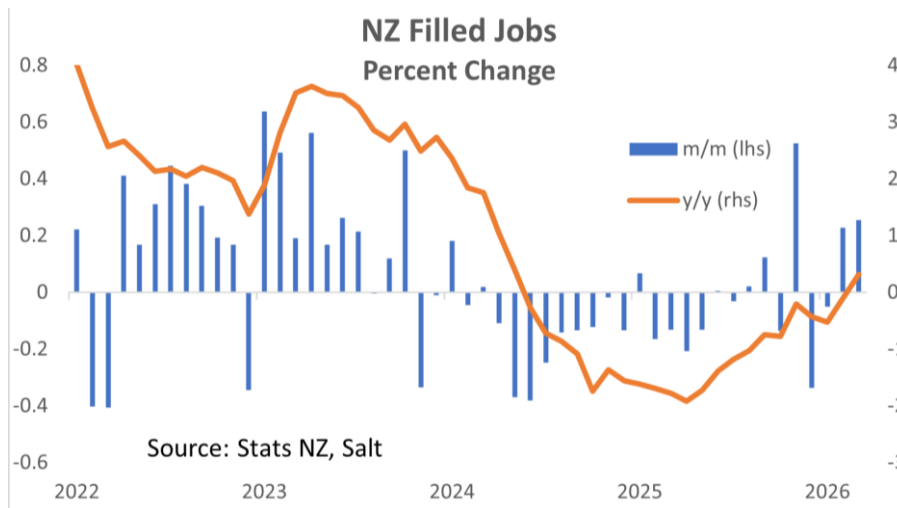


The survey also showed rising cost expectations, but in a potential bright spot for the RBNZ, pricing intentions fell back a bit, although from already lofty levels. The circle of higher costs and lower pricing intentions gets squared by a sharp fall in profit expectations which fell from +20 to -13 over the month. Challenges abound.

Employment conditions looking a little brighter

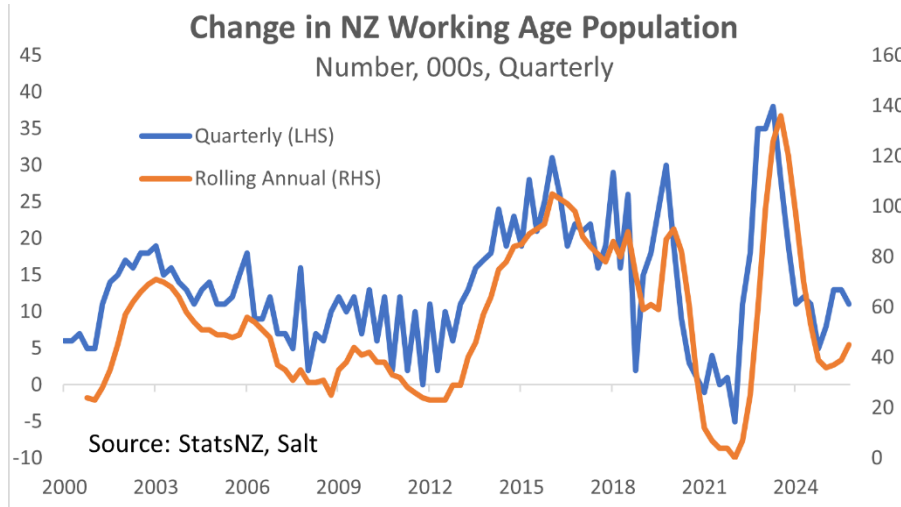


Employment expanded by a modest +0.2% in the March quarter to be up +0.4% on year ago levels. The slow rate of improvement is consistent with the generally constrained recovery in the economy generally, particularly in what is typically a lagging indicator. We expect an ongoing slow recovery, though weaker employment intentions due to the war in Iran will have near-term implications.

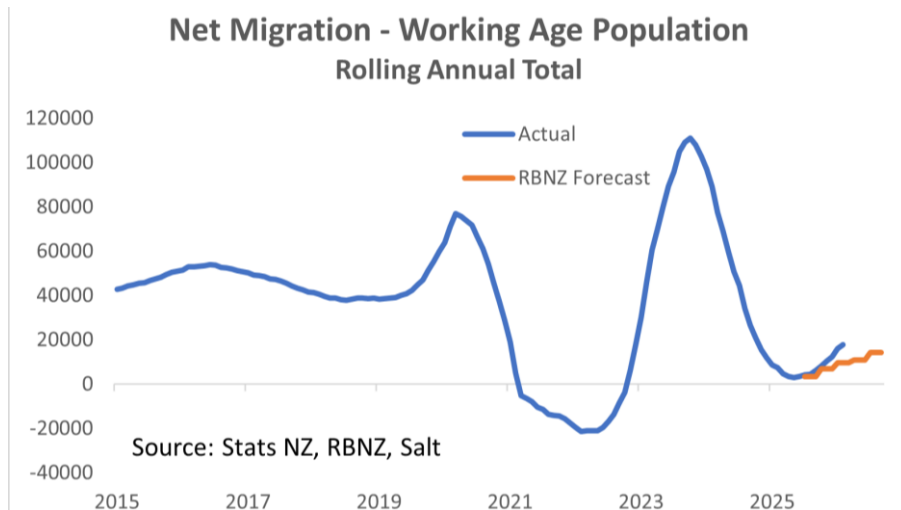


The more frequent monthly filled jobs data, sourced from the IRD, will be the first indications we will get of any renewed weakness in employment.

Labour market supply recovering with higher net migration

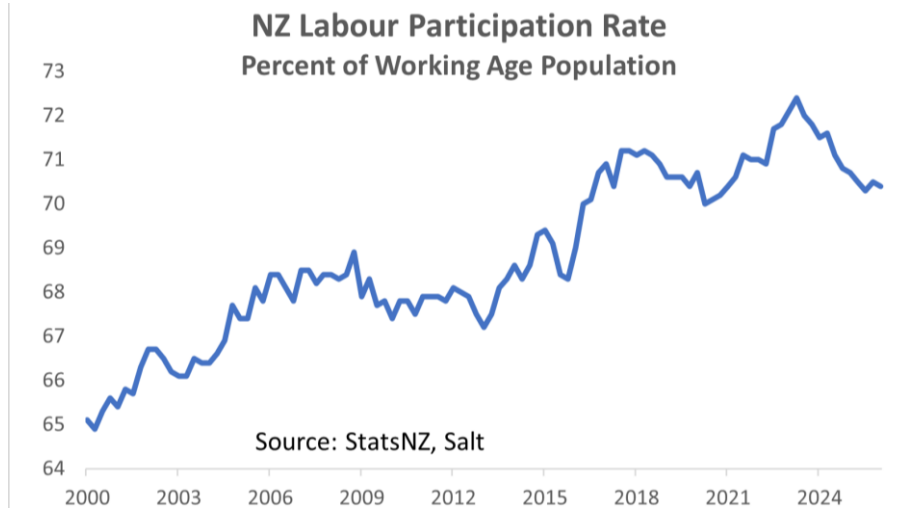


Growth in the working age population is recovering, driven by the recent increase in net inward migration. A growing working age population will ease any emerging labour shortages, will tend to suppress wage growth and, in an environment of only modest employment growth, will keep the unemployment rate more elevated than might otherwise be the case.

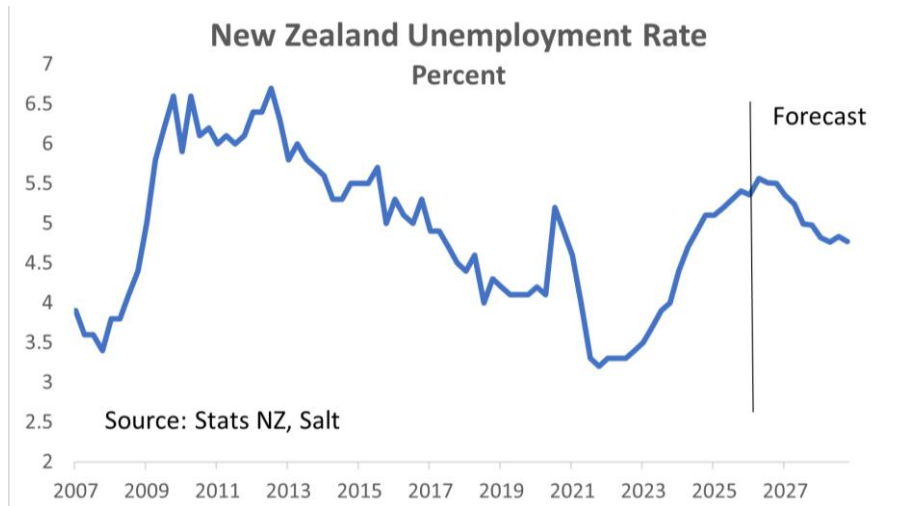


The recent turnaround in net migration is running ahead of RBNZ projections. As well as the direct labour market implications mentioned above, a faster turnaround in net migration will tend to boost the RBNZ's assessment of potential growth in the economy, in other words the rate of growth the economy can sustain without generating excess inflation.

Unemployment rate at risk of further near-term increase

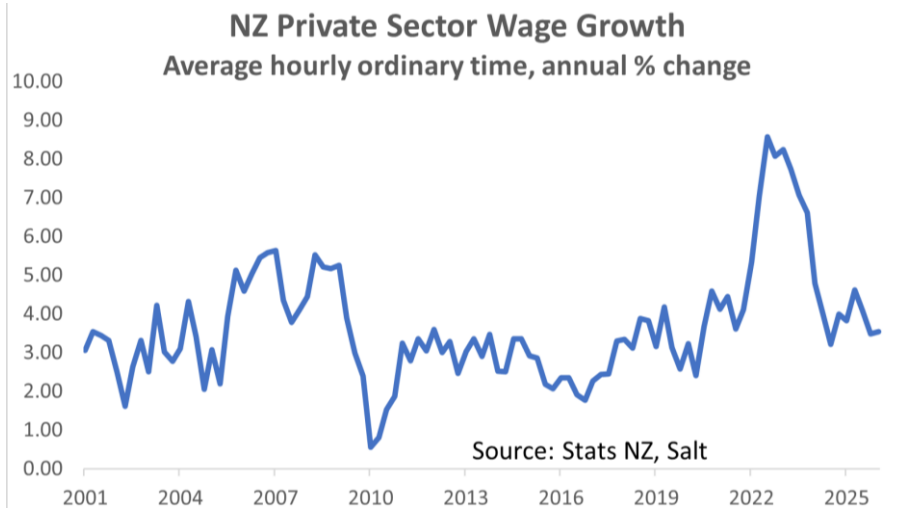


Labour market supply isn't just determined by the working age population but also the participation rate, the proportion of the working age population that is either in or actively seeking work. During tough economic times people can become discouraged at the prospect of finding work and drop out of the labour market. We expect this will head higher again as the recovery strengthens.

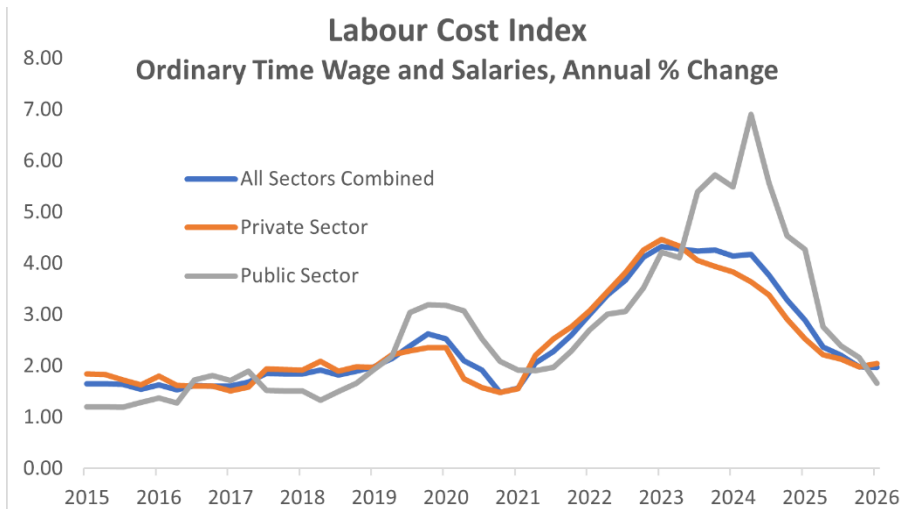


The unemployment rate stood at 5.3% in March 2026, down slightly from the 5.4% recorded in December last year. Absent the war we would have expected a continued modest improvement, however there is now a risk the unemployment rate heads higher in the near term given the collapse in employment intentions in the recent business surveys.

Wage growth moderating

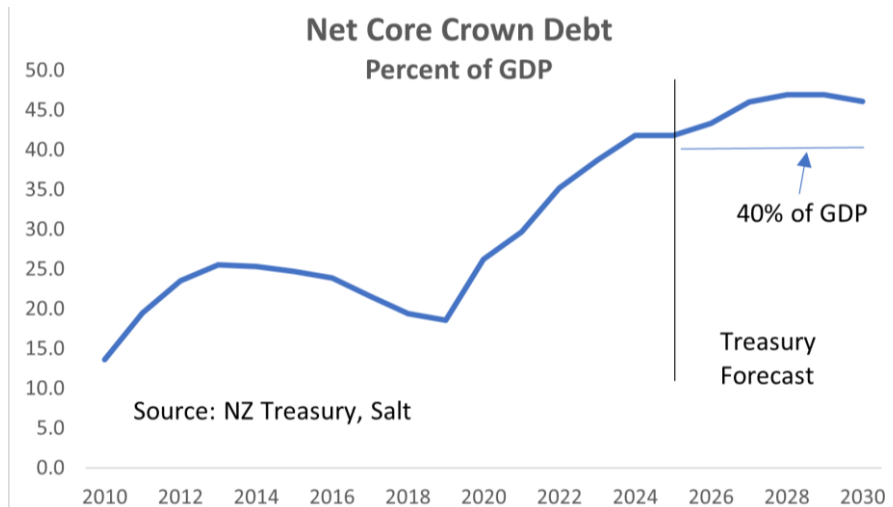
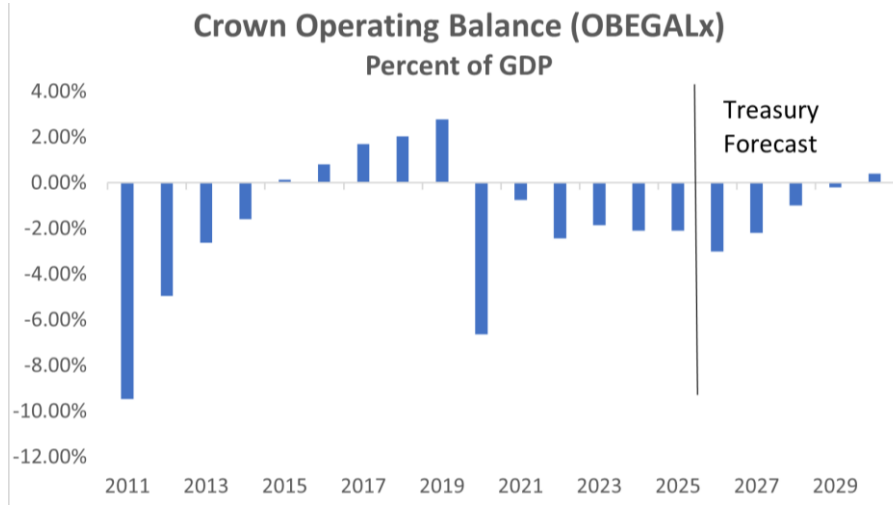


Wage growth in the Quarterly Employment Survey does not adjust for any change in the composition of the workforce. That's why we think of this data as the pace of growth in total wage income across the whole economy, rather than the rate of change in individual wage rates. At 3.5% growth in the year to March, wage income is only running slightly ahead of inflation of 3.1% over the same period.



The Labour Cost Index is the more reliable measure of wage inflation. The key measure for the RBNZ is for the private sector as it is the measure they can most influence. From a peak of 4.5% this has now fallen to 2.0% as at March 2026, the level consistent with 2% inflation. If there is any surprise for us in this data it is that it has not been even weaker given the rise in the unemployment rate.

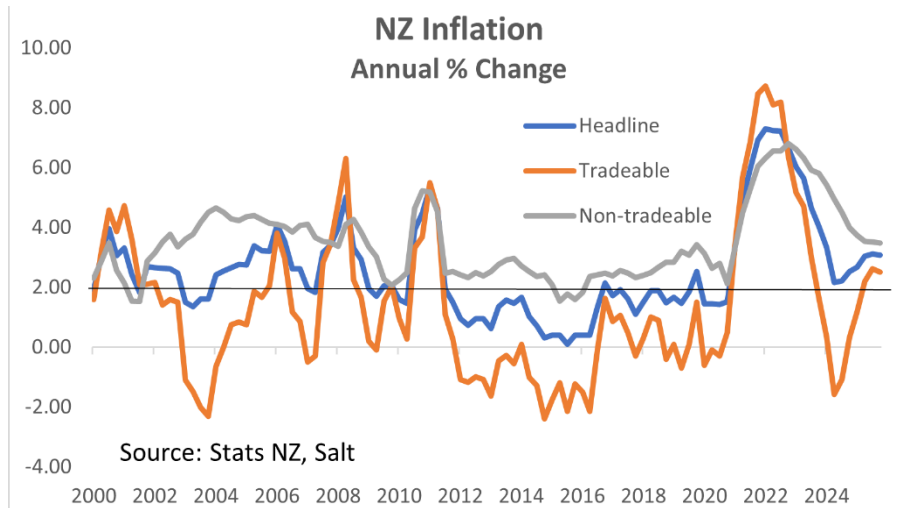
Fiscal position is challenging



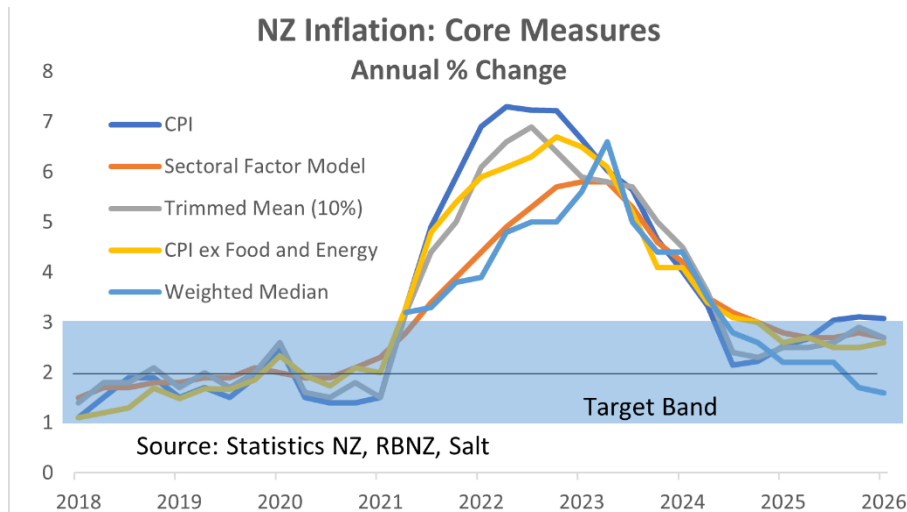
It's the 2026 Budget on Thursday May 28th. Added attention has been brought to the fiscal consolidation process by the recent credit rating downgrade by Moody's. While affirming our Aaa credit rating, the agency shifted its outlook to "negative" because of the risks posed by global economic and geopolitical uncertainty. We expect the Budget to show the return to surplus has been pushed further out.

Ongoing revisions to the fiscal position has seen upward revisions to net debt as a percentage of GDP which is currently expected to peak at 46.9% of GDP in 2029. The Government remains committed to its 40% target for net Crown debt, which we fully support. It is essential we restore a buffer for whatever the next crisis is that gets thrown at us.

Back to the top of the band before the war

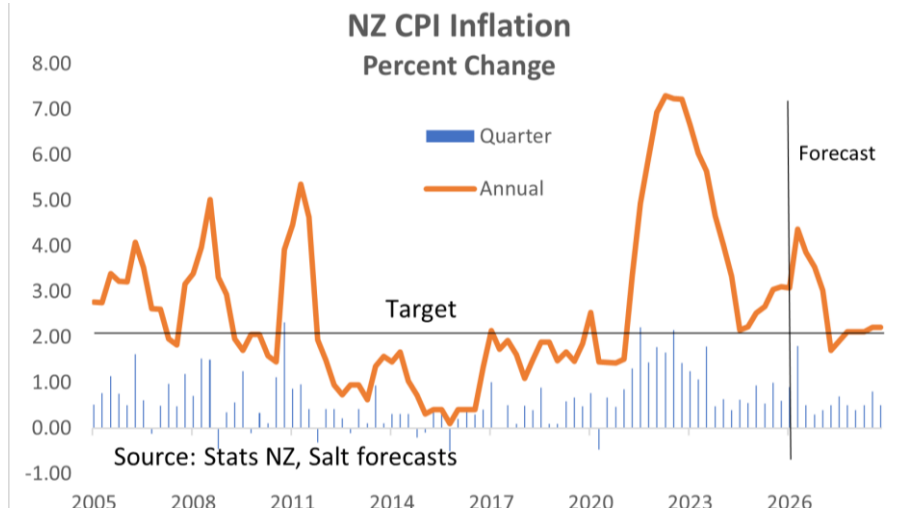


March quarter CPI came in a bit stronger than expected, rising +0.9% q/q and 3.1% y/y. The annual rate is unchanged for the year to December vs expectations of a modest decline. In terms of the impact of the war, petrol prices were up 3.5% but it's too early to see any significant second round effects – that is the critical part of the story in determining the monetary policy response.

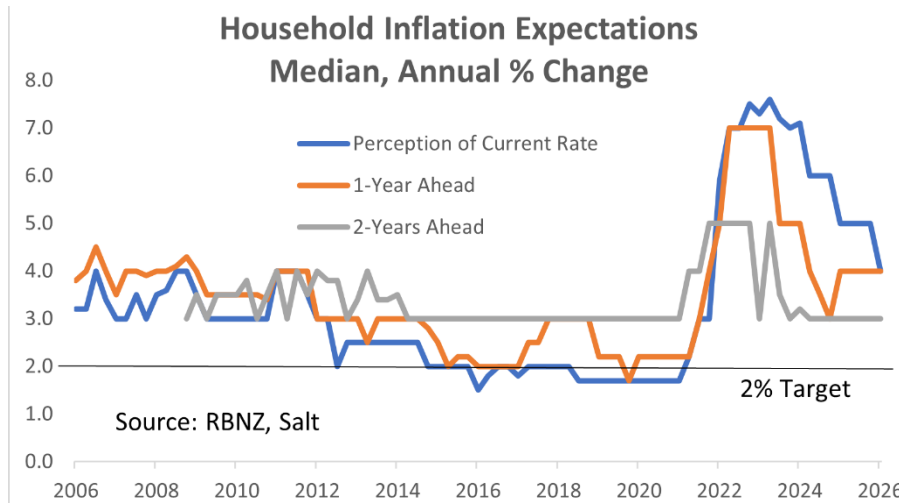


The key measures of core inflation are within the band though most remain in the top-half and some have started to rise again. And, of course, this is before we see any sign of second-round effects from higher fuel prices. The next move in interest rate is up - it's just a question of when.

Ouch!

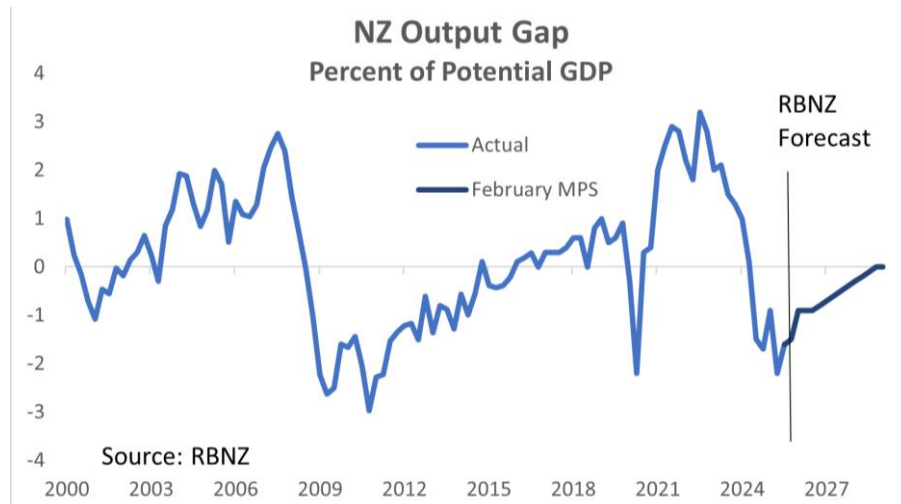
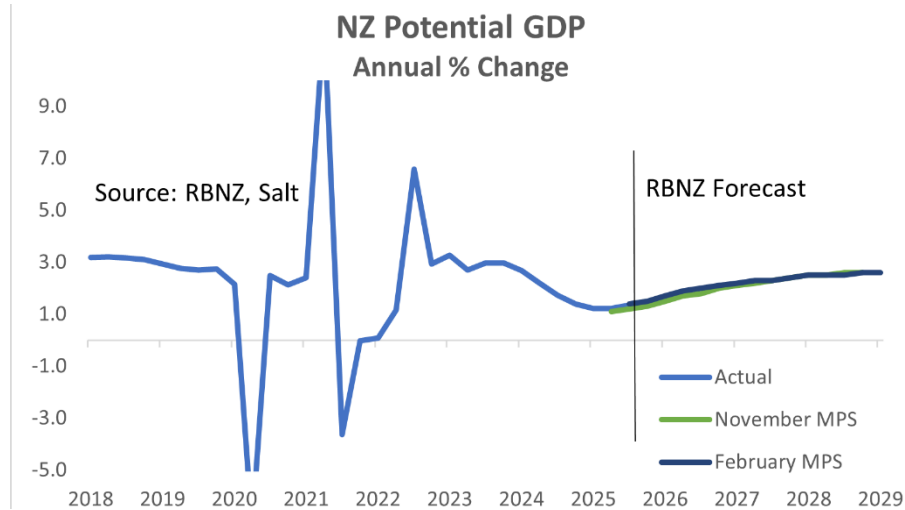


Only a small part of the recent fuel price increases came through in the March quarter data, the bulk will come through in June. That has us expecting headline CPI to hit 4.4% in the year to June. That assumes oil prices remain around the US\$100-110 per barrel through the quarter.



The RBNZ had already signaled close attention to household inflation expectations before the war as inflation headed back to top of the target band. Watching how expectations evolve over the next few months will be a key part of their assessment of the risk of second round effects feeding through into wages.

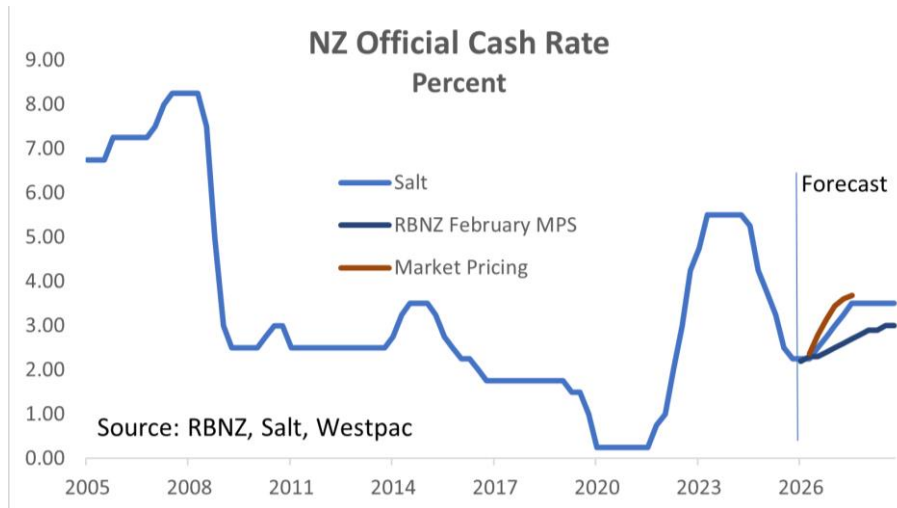
This isn't Covid 2.0



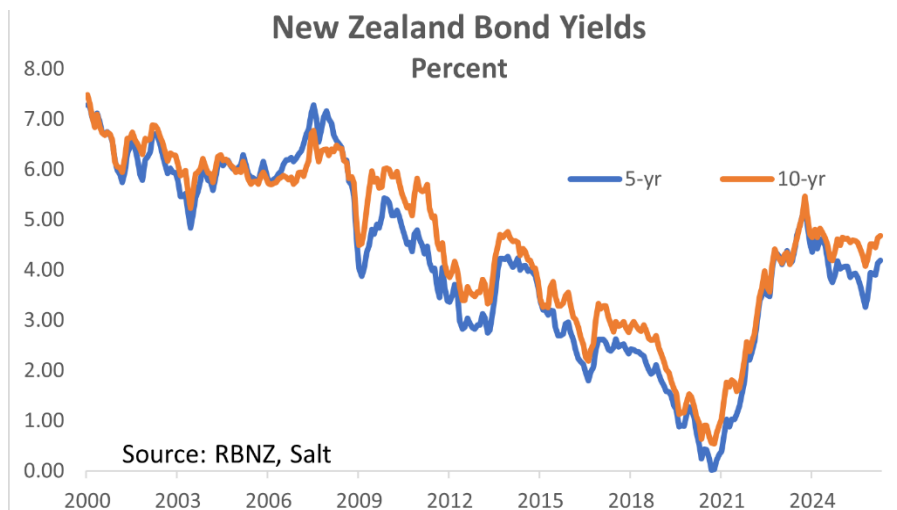
Critical to the outlook for inflation and monetary policy is how fast the economy can grow while achieving low and stable inflation, or its potential growth rate. This is a function of factors such as growth in the working age population and productivity. The RBNZ estimates our potential growth rate is currently around 1.5%, rising to 2.6% over time. The 1.5% isn't flash but the 2.6% is optimistic.

The monetary policy outlook will in large part be shaped by the extent of second round inflation impacts. But this is not a repeat of Covid. At the outbreak of the pandemic the economy was growing in excess of its potential and the unemployment rate was around 4%. Today the economy is in the early stages of recovery and there is a lot of spare capacity with the unemployment rate over 5%. That will help limit second round inflation impacts.

It's not a question of "if" to hike, but "when"

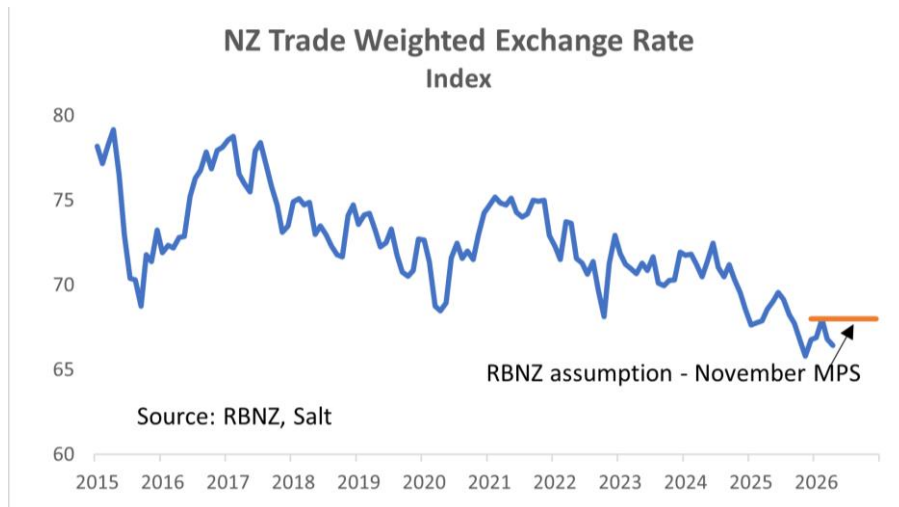
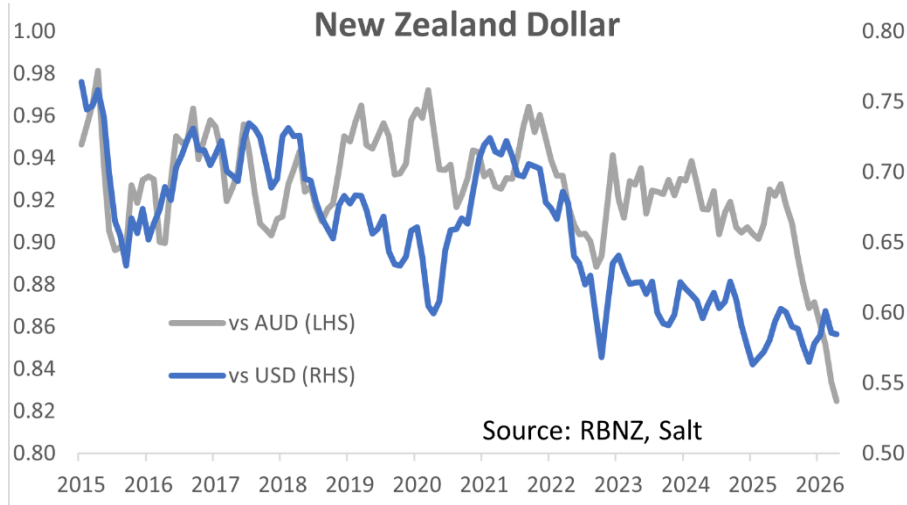


With the RBNZ cutting interest rates below neutral and thus into stimulatory territory, it was only a matter of time before they needed to start hiking again. The stagflationary shock from higher fuel prices has muddied the waters. Assuming the conflict is resolved soon, we expect the RBNZ to start hiking the OCR from September this year, up to the top end of our estimated 3.0-3.5% range for the neutral rate.



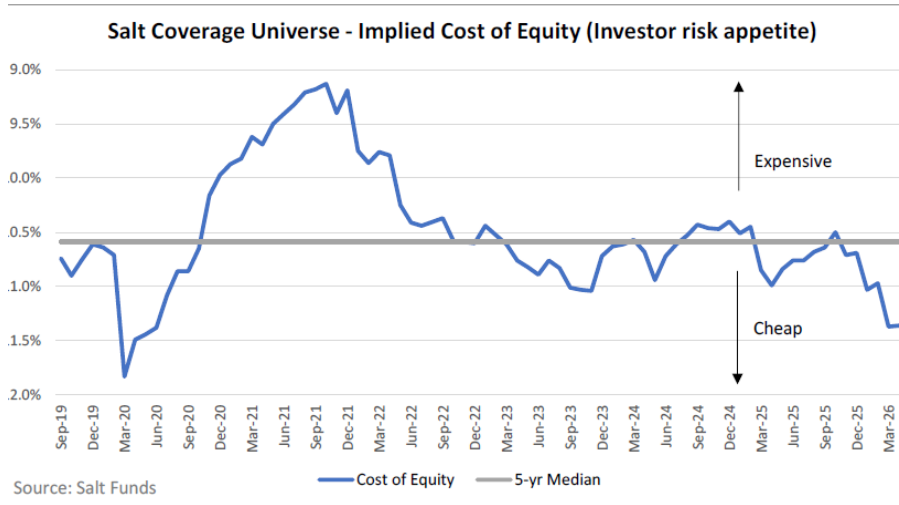
Yields have headed higher again around the world as bond markets have focused on the inflationary impulse from higher fuel prices. Underlying this, concerns about fiscal sustainability persist. Here at the home the focus is on the Budget in May which will be presented in the aftermath of the recent downgrade to the fiscal outlook by the Moody's rating agency.

Big move for the NZD vs. AUD



Despite the considerable geopolitical turmoil associated with the Iran war, the NZD has remained broadly stable against the US dollar. That resilience may seem surprising given the NZD’s traditional “risk-sensitive” characteristics, but it likely reflects a combination of still-solid global risk appetite and markets taking the view that the economic and inflation implications of the conflict are global rather than uniquely negative for New Zealand. The NZD/AUD is a different story with the weakness being driven by relative monetary policy stories with the RBA hiking and the RBNZ on hold, at least for now. What matters most for the RBNZ is how the NZD moves on a trade weighted basis. The TWI is currently a bit below the level assumed in the most recent set of MPS projections from November.

Share valuations around fair value



We view current pricing of the Salt stock coverage universe as cheap relative to its 5-year average, with New Zealand equities priced around a 7% discount to Australian equities based on bottom-up DCF valuation methodology. Equities have derated through CY26 on Iran-war driven negative earnings risk. Spiking fuel costs and declining consumer sentiment are expected to apply downward pressure to short-term earnings of cyclical stocks in particular. The key question for investors currently is the duration of the war and its residual impact on the macro recovery that had gradually gained momentum in New Zealand through late CY25 & into early CY26

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