Research

Services Landscape

15 September 2025

Turning point taking time

The Performance of Services Index (PSI) slipped back from 48.9 to 47.5 in August. Yes, the three-month moving average for the PSI lifted from 46.9 to 48.0, but it is hardly reason to celebrate. Across the economy, we still believe the general signs of a turning point are there. However, there is a very real risk any ensuing bounce takes longer than currently expected. This means that the balance of risk to our interest rate forecasts (by a slim margin) is that the Official Cash Rate (OCR) may need to go lower than the 2.50% we have forecast.

Further OCR cuts expected

Our forecasts are for two more 25 basis point OCR cuts in October and November. While the two remaining cuts should support the economic recovery, it is important to remember that they are already baked into the cake. This is because the market is also pricing in an OCR low of 2.50%. Any suggestion that these rate cuts will not be delivered would imply a potential increase in lending rates, something we think the Reserve Bank of New Zealand would not be keen on.

Bounce back too optimistic?

We have pencilled in a 0.5% q/q contraction for Q2 GDP released on Thursday. Our estimate was revised down from -0.2% on the back of last week's soft business financial data. While we lowered our Q2 estimate, we also lifted our pick for Q3 (from +0.5% to +0.7%). Looking ahead, the combined PMI and PSI activity indicator (46.4) suggests the pace of our forecast recovery may be too optimistic. Indeed, it would need to jump up to around 53 to be consistent with our year-end GDP forecast.

Off a weak base

For the first two months of Q3, all five PSI sub-components have averaged higher than they did in Q2. We believe the tide in the economy is slowly turning, albeit not in a uniform fashion as indicated by the latest monthly PSI movement. Stepping back from month-to-month volatility, all the PSI sub-components remain well below their long-run average. Despite our forecasts for a modest economic recovery, it will take time before it feels anything close to normal.

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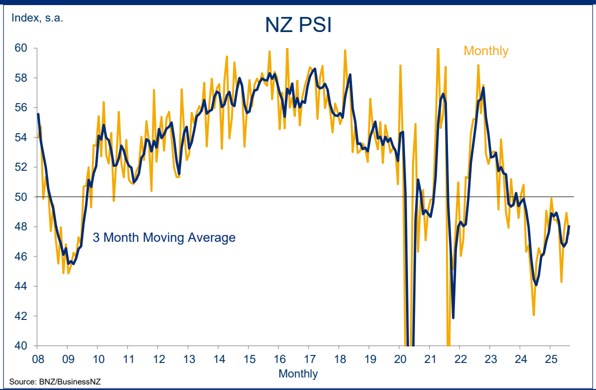
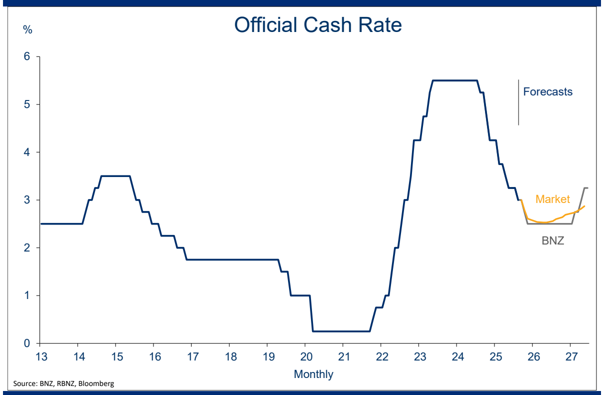
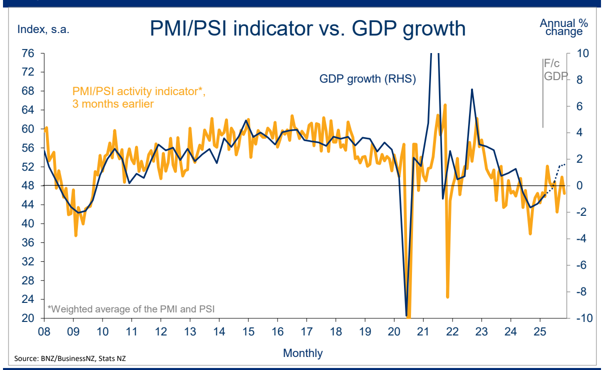
18 months below 50



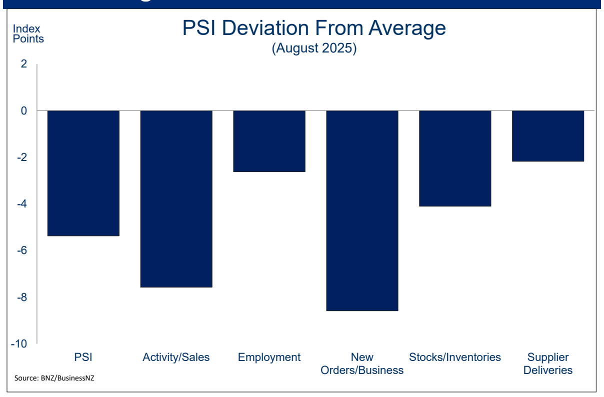
Aligned on 2.50% low



Improvement needed



Below average



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