

# Term Deposit Report

03 December 2021

## Interest rates have risen but so has inflation

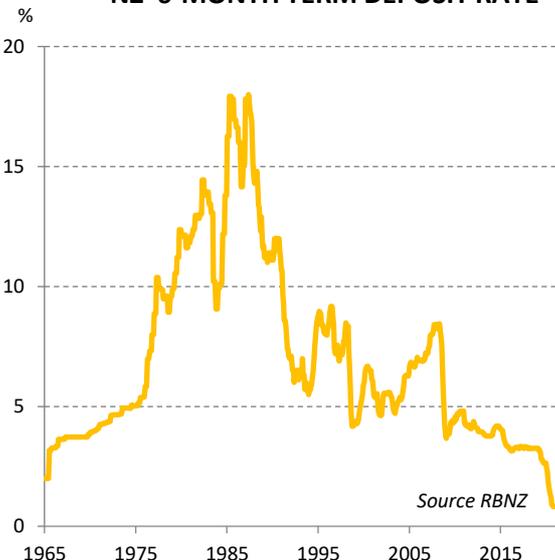
During the pandemic, term deposit rates dipped to the lowest level on record going back to the 1960s. But we have turned a corner in 2021. Term deposit interest rates have lifted off their lows over the year, including several increases over recent months. The RBNZ delivered its first Official Cash Rate increase in over seven years in October and followed up with another hike in November. More OCR increases are forecast for 2022, and this is priced into longer term interest rates in New Zealand, including term deposits. Despite the increase we have seen this year, rates on offer are still very low and are expected to remain below historical averages over the coming years. ASB's term deposit interest rates are [tabled here](#), and selected rates and their recent changes are shown below.

Term Deposit Rates	90-days	6 months	9 months	1 Year	2 years	3 years	4 years	5 years
10-year ave	2.53	3.17	3.22	3.28	3.50	3.66	3.82	3.96
Low	0.35	0.80	0.75	0.75	0.80	0.90	1.00	1.00
<b>Dec-21</b>	<b>0.50</b>	<b>1.30</b>	<b>1.45</b>	<b>1.65</b>	<b>2.25</b>	<b>2.60</b>	<b>2.80</b>	<b>3.00</b>
2021 increase	0.15	0.50	0.70	0.90	1.45	1.70	1.80	2.00

### Some important considerations are:

- **Over the course of 2021 term deposit rates have been lifting off their all-time lows but returns from term deposits are still expected to remain low relative to historical averages over the years ahead.**
- **Inflation has been low but is rising sharply and could well erode all the return from term deposits.** Consumer price (CPI) inflation over the past 10 years has generally been significantly below the 2% mid-point of the Reserve Bank of New Zealand's 1-3% target range. That has changed this year. CPI inflation has spiked above that target over 2021 and is expected to run at between 2-3% p.a. over the coming years.
- Related to the rising inflation situation and the economic recovery in the wake of the COVID-19 pandemic, the RBNZ lifted the Official Cash Rate in October and November. Further increases are expected. **We also expect to see some more increases in term deposit rates over the years ahead, but do not expect rates to return to the higher levels seen over the past 10-20 years.**
- **Making sure you are paying the right tax rate is important, and it's easy to check ASB has the right tax rate details for you.**
- **Higher returns are possible** through focusing on longer-term investments and diversification into different assets with different risk profiles.
- It's always important that investors make sure investments suit their personal needs - **talking with an advisor can be a good idea.**
- **Safety of savings is important** – at times like these, savers want to know their money is secure.

NZ 6-MONTH TERM DEPOSIT RATE



## Snapshot and Outlook

Even though we have seen a lift off the record lows over the past year, our view is that interest rates for most term deposits are going to stay historically low for several years, rather than return to the higher levels we have seen over the past 10-20 years

At the time of writing, ASB's term deposit interest rates for amounts over \$5,000 are largely between 0.5% and 1.45% for terms between 90 days and 9 months, and between 1.65% and 3.00% for terms between 1 and 5 years. Over the past 10 years, term deposit interest rates have averaged between 1 to 2% higher than the current rates available for the various terms.

For the popular term deposit rates – short terms up to 1 year – a key influence is what the RBNZ does with the Official Cash Rate (OCR). The RBNZ adjusts the OCR to help it achieve its price stability (inflation) and employment objectives. The RBNZ has a 1-3% target range for inflation and would like it to be around 2% per annum on average. Similarly, it would like employment to be as close as possible to its maximum sustainable level. Consumer price inflation (CPI) averaged around 1.3% per annum over 2015-2020 but is now on the rise. Annual CPI inflation has printed above 4%, and we expect inflation to average above 2% p.a. over the next five years. Moreover, the labour market is tight, with acute labour shortages. As a result of the stronger inflation outlook, limited spare capacity and strength of the local economy, the RBNZ delivered its first OCR increase in over seven years in October. The RBNZ delivered a follow up increase in November. We think the RBNZ will lift the OCR several more times over the next year: read more on ASB's thoughts of the RBNZ's recent rate increases [here](#).

Despite the ongoing challenges of the pandemic, the New Zealand economic recovery is progressing, and that's a key reason why we have seen long-term interest rates in the economy lift off the record lows recorded over the past year.

Increases in the OCR should help lift shorter-term deposit rates, which are still very low. These rates should continue to go up, but not to the levels we have observed in the past, given we expect the OCR to peak at a historically-low 2.00%. In summary, based on our OCR forecasts and outlook for the economy, we expect further increases in term deposit rates over the year ahead, but also expect rates to remain below the longer-term averages tabled at the top of this report.

## Some issues for consideration

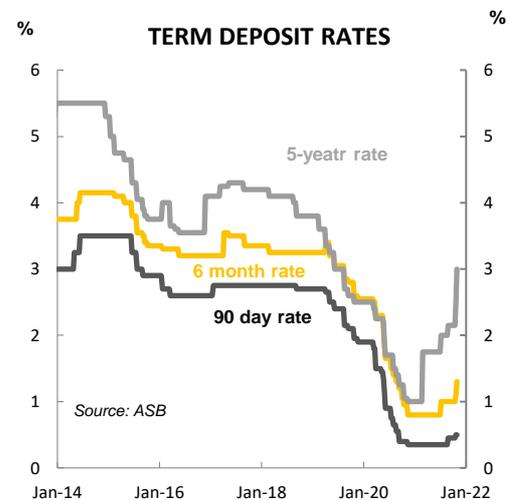
For savers, these expectations of historically-low term deposit rates have major implications. We acknowledge that people are rightly concerned about the significant income drop caused by the lower interest rates available today compared to earlier years.

## Access to your money

Short-term interest rates are expected to remain low, but rates for longer terms have started to lift, so investors can get a higher return by investing for longer terms. However, with term deposits, funds are locked in, and only accessible in limited circumstances. This is an important consideration for investors, particularly when weighing up longer terms ([more here](#)). In other words, savers need to weigh up their personal circumstances and need for flexibility when considering what term is best for them.

## Inflation

Inflation has been low until recently, but it's still there, eroding the real value of investment returns, including term deposit interest. In fact, despite the recent increases, many term deposit rates are still below what we expect CPI inflation to average over our forecasts for the corresponding periods. (we expect inflation to average above 2% over our forecast horizon). In other words, after taking expected inflation into account, there's not much return from locking money away for several years, which adds to the current challenge of generating income from term deposits.



## Safety of your money

When financial markets are volatile like they have been at times during the COVID-19 pandemic, many investors become understandably concerned about the safety of their savings. For term deposit customers, it is important to know that ASB is strongly capitalised and maintains a very conservative (high) level of liquidity. This enables us to safely withstand extended periods of market disruption and uncertainty like we have just been through. ASB's credit ratings reflect the independent opinion of three international rating agencies about the capability and willingness of ASB to repay its debts (which includes term deposits). ASB is rated on an international scale as 'strong to very strong'. The RBNZ's website has information about credit ratings [here](#).

## Check you are on the right track

It's worth thinking hard about the timeframe to invest for because the increase in return you can get for making a longer time commitment can make a difference. For example, the current interest rate on a twelve-month term deposit is 1.15% higher than the three-month rate (1.65% vs. 0.5%).

ASB's term deposit interest rates are [tabled here](#). Higher returns are possible through longer-term investments and diversification into different assets with different risk profiles. But you need to be sure those investments suit your needs. Talking to an [ASB advisor](#) could help.

## Check you are paying the correct tax rate

You should ensure your Resident Withholding Tax (RWT) rate is correct for your level of taxable income. Selecting a rate that is too low may mean you have an end of year tax liability. Selecting a rate that is too high may mean you are paying too much tax. If you are paying too much RWT, you may get a refund at the end of the year from the IRD after assessment of your total taxable income for the year. You can find out more [on our website](#).

You can also update your tax rate online using FastNet Classic ([find out more here](#)). If you are a non-New Zealand tax resident, the default rate will be the withholding tax rate for your indicated country of tax residence.

## Should you be in a term deposit or a term fund?

An ASB Term Fund is an alternative to a term deposit and may provide a better after-tax return than a term deposit offering the same rate, term, and fees. Tax on your returns is capped at a maximum rate of 28%, so an ASB Term Fund may be worth considering if you're on a higher income tax rate. [Find out more here](#).

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