



Risky business

Are New Zealand businesses showing evidence of changes in investment behaviour and risk appetite?

Business investment plays a vital role in shaping the economy

When firms invest in new equipment, buildings, technology, and innovation, they increase the economy's ability to produce more goods and services. This helps lift productivity, supports job creation, and drives long-term growth in living standards. Strong and confident business investment also signals that firms are willing to take risks, explore new markets, and adopt emerging technologies.

In New Zealand, business investment has not always kept pace with the broader economy. Even during periods of steady growth and low borrowing costs, firms have sometimes chosen to hold back on new projects.

Since the Global Financial Crisis (GFC), the capital-to-labour ratio has plateaued, meaning the amount of capital available to workers has remained relatively unchanged. There has been some improvement in this ratio post-COVID-19, but it's too early to say whether this marks a change in trend or a one-off.

This raises an important question: have businesses become more cautious about investment?

The potential for businesses' risk appetites to change over time matters for New Zealand's future prosperity: a lower appetite for risk among firms can slow the renewal of capital

and delay innovation, limiting opportunities for productivity gains and higher wages.

If firms are facing greater uncertainty or structural change, investing less may be a rational response. But if weaker investment persists, it can slow capital renewal¹ and innovation, which tends to reduce productivity and hold back wage growth over time.

Understanding the drivers of changing investment behaviour helps policymakers and business leaders make better decisions about how to support sustainable, long-term economic growth in New Zealand.

What drives firm investment?

Several theories try to explain what drives firms' investment behaviour. The most prominent of these are theories on the influence of aggregate demand described by the accelerator model, the effect of economic uncertainty on investment timing, and the role of financial conditions as captured by Tobin's q (Ratcliffe and Tong 2021).

- **Aggregate demand (accelerator model)**
The accelerator model suggests that investment is primarily driven by changes in output or demand. When gross domestic product (GDP) or production grows, firms need more capital to meet higher demand, leading to increased investment. Expected future demand and

¹ 'Capital renewal' means replacing, upgrading, or modernising the assets a business uses to operate.

past profitability influence firms' expectations and, in turn, their willingness to expand capacity.

- **Economic uncertainty**
In times of heightened uncertainty, firms may choose to delay investment because capital projects are costly to reverse. The 'wait-and-see' behaviour reflects the idea that investment is like purchasing an option; it has value precisely because it can be deferred until uncertainty is reduced. Higher uncertainty, therefore, tends to suppress investment even when other conditions are favourable.
- **Financial conditions (Tobin's q theory)**
Tobin's q proposes that firm investment depends on the ratio of the market value of capital to its replacement cost. When the market values a firm's existing capital more highly than the cost of acquiring new capital ($q > 1$), firms have an incentive to invest. In this framework, investment is driven by financial conditions and the firm's ability to raise funds at a favourable cost.

Firms' investment intentions are weighted more towards expected profitability

The NZIER Quarterly Survey of Business Opinion (QSBO) provides insight into firms' investment expectations over time. Figure 1 shows firms' economy-wide investment expectations over the next 12 months for each quarter, alongside their profitability over the last 3 months and their expected profitability over the next 3 months.

Investment expectations appear cyclical and tied to global events, dropping sharply during the GFC in 2008–2009 and again around 2020 due to the COVID-19 pandemic and pandemic restrictions.

Figure 1 shows that firms are generally more optimistic about their profitability than what they actually experience. Even when firms have experienced lower than expected profitability for some time, they tend to remain optimistic.

QSBO data show that expected profitability over the next 3 months tends to move closely with profitability in the past 3 months.

Expected investment also moves with profitability, but less tightly, particularly for buildings. This suggests that recent trading conditions are more closely reflected in short-term profitability expectations than in firms' investment plans.

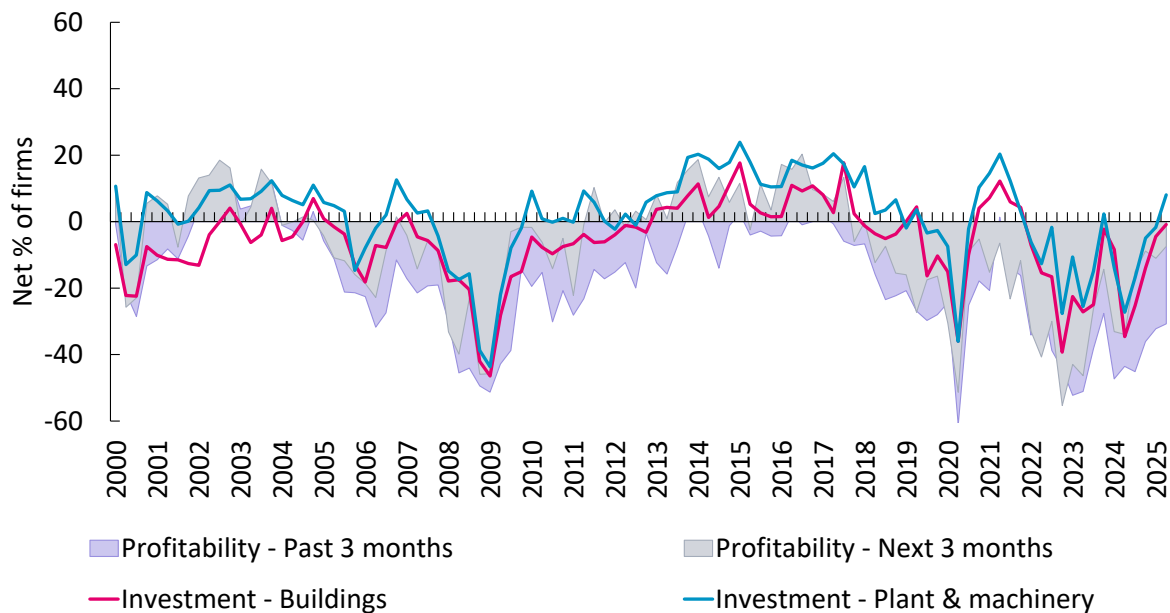
Firms seem to be more cautious in recent times

Since 2018, total industry current assets have increased as a share of total assets at a pace of around 0.6 percentage points each year, according to the Stats NZ *Annual Enterprise Survey* (AES) (2025). Current assets, which include cash and other assets expected to be converted to cash within 12 months (such as receivables and inventories), have grown from 27 percent of total assets across all industries in 2018 to 31 percent in 2024.

A rising share of current assets may be consistent with greater financial caution, though this interpretation should be treated with care, as the increase may also reflect inventory accumulation, receivables growth, or nominal valuation effects rather than an intentional shift away from long-term investment.

Higher current assets may partly reflect slower inventory turnover or increased trade credit provision, noting that AES financial data are reported in current prices. To the extent that the shift is behavioural, it may reflect firms' responses to economic uncertainty, higher interest rates, and tighter credit conditions.

Figure 1 Economy-wide profitability in the past and next 3 months and expected investment over the next 12 months



Source: NZIER QSBO

Investment in fixed tangible assets, such as buildings, machinery, and equipment, has grown at a steadier pace. This divergence implies that while firms are expanding their asset bases overall, they seem to be prioritising liquidity and short-term stability over long-term capital expansion. Businesses may be delaying major fixed investment until economic conditions stabilise.

The financial ratios from the Stats NZ survey point to an increase in reported firm liquidity over the past decade. Both the current and quick ratios, which measure businesses' capacity to meet short-term liabilities, have risen over the past five years.

The current ratio measures current assets relative to current liabilities, while the quick ratio excludes inventories from current assets to provide a more conservative indicator of short-term liquidity.

For all industries combined, these ratios historically sat around their 2020 levels of 77 percent and 69 percent, respectively, increasing to 81 percent and 74 percent in 2024 (i.e. current assets equal to 0.77 of current liabilities in 2020, rising to 0.81 in 2024).

While this represents a modest upward trend, it may reflect valuation effects, shifts in industry composition, or precautionary cash-holding following recent shocks, rather than a uniform or structural improvement in underlying liquidity across firms.

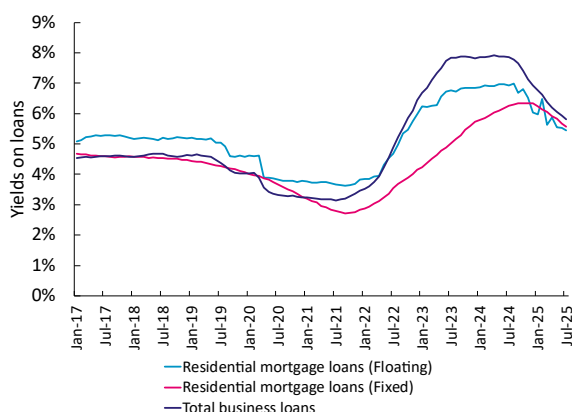
At the same time, return on equity (ROE) has stayed relatively constant, increasing from 10 percent in 2020 to 14 percent in 2022 and going back down to 12 percent in 2024. This suggests that firms have built up liquid reserves and short-term assets, without an obvious deterioration in aggregate profitability. However, ROE reflects multiple influences, including leverage and compositional change among other factors.

Increased borrowing costs have made it harder for businesses to take on debt for investment...

The total yield on business loans increased to nearly eight percent in 2023–2024, the highest in over a decade, while mortgage rates rose more moderately. This indicates that the effective interest burden on firms increased faster and more sharply than in other sectors.

Yields on business loans had previously been in line with those on residential fixed mortgage loans until around February 2021, when they increased sharply, even surpassing yields on floating residential mortgage loans. Although business loan yields have eased since peaking at 7.9 percent in April 2024, they were still some way off pre-COVID-19 levels (Figure 2) as of July 2025.

Figure 2 Banks' loan yields as a percent of loan values



Source: RBNZ (2025b)

...and so have tighter credit conditions

The RBNZ *Credit Conditions Survey (2025a)* provides insight into how financing constraints have influenced business investment behaviour. Since 2022, both the cost of borrowing and the availability of credit have tightened significantly, reflecting the impact of higher interest rates and more cautious lending standards.

Loan demand fell sharply through 2022 and 2023, overlapping with the period of peak borrowing costs. At the same time, credit availability weakened, particularly for commercial property and corporate loans, where banks reported reduced lending appetite and stricter terms.

These trends indicate that firms were facing not only higher financing costs but also reduced access to credit, potentially compounding the effect on their willingness and ability to invest.

The tightening of credit conditions since 2022 could have suppressed firms' risk appetite, especially among smaller and more leveraged firms that rely on external financing. Larger corporates, with stronger balance sheets, appear better able to absorb the higher cost of capital, as reflected in more resilient credit availability for institutional loans.

What does this imply for firm investment?

Survey evidence, balance sheet indicators, and financing conditions point to a more cautious investment environment for firms in recent years. While firms have maintained profitability on average, they appear to have increased their preference for liquidity and balance sheet resilience amid elevated uncertainty and higher borrowing costs.

This pattern is consistent with a 'wait-and-see' approach to investment, where preserving optionality is prioritised over committing to long-lived capital. Importantly, this behaviour may reflect rational risk management rather than a deterioration in firm fundamentals.

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