ANZ Research

September 2019 Quarter CPI Preview

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Falling short

- We expect headline CPI rose 0.7% q/q in the September quarter, with annual inflation ticking back down to 1.5% from 1.7%. Non-tradable inflation is expected to print at a solid 0.9% q/q, with tradable inflation up a more modest 0.4% q/q.
- While we expect headline inflation to fall further from the 2% target midpoint in Q3, the RBNZ may find a glimmer of hope from the rise in domestic (non-tradable) inflation to 3% y/y that we're expecting. That said, the RBNZ's focus will remain on the slowing economy, which we expect will see inflation continue to fall short over the next year.

Key points

September quarter CPI figures are released next Wednesday (16 October).

We expect headline CPI inflation will print at 0.7% q/q, with annual inflation dipping to 1.5% from 1.7%. This is higher than the RBNZ's August MPS pick of 1.3%, driven by higher food prices and expected strength in domestic inflation.

Non-tradable inflation is expected to post a solid 0.9% q/q rise, above the RBNZ's August expectation for a 0.7% q/q rise. Our pick would see annual non-tradable inflation rise to 3.0%. The solid print is led by strength in housing-related prices. Core inflation has stabilised over the past year, and we expect it to continue to track broadly sideways in Q3.

We expect tradable inflation to print at 0.4% q/q, with food prices rising and petrol prices largely flat in the quarter. This would see annual tradable inflation dip to -0.4% from 0.1% y/y.

There are a few factors driving the 0.7% q/q print this quarter:

- **Property rates, rents and construction costs continue to support domestic inflation.** Property rates rose about 3% in the quarter according to our Monthly Inflation Gauge, a typical September quarter lift. Rental prices rose 0.8% q/q, and construction costs are expected to increase a solid 1.2% q/q. The household and household utilities group is expected to boost CPI inflation by 0.3%pts.
- **A surprise lift in food prices provides a boost.** Food prices rose 1.3% q/q in the quarter, with strong increases in meat prices and moderate rises in other subgroups. Together, these contribute 0.25%pt.
- **Higher road user charges offset a fall in international airfares.** Within the transport group, international airfares are expected to post a 4% seasonal decline, while other transport services prices were boosted 8% by a hike in road user charges. Overall, we've pencilled in a 0.1% q/q rise for the transport group.
- **A seasonal rise in accommodation services and domestic airfares supports non-tradable prices.** We're picking accommodation services to have risen 3% q/q, and domestic airfares to be up 2% q/q. Together these contribute 0.1%pts.

On the whole, we see the risks to our 0.7% q/q Q3 CPI forecast as slightly skewed to the upside. In particular, non-tradable inflation could be stronger than expected, based on the signals from our Monthly Inflation Gauge. However, persistent weakness in tradable prices could continue, despite the weaker NZD.

Consumers Price Index – September 2019 Quarter

	Expected	Prev
CPI – q/q	0.7%	0.6%
CPI – y/y	1.5%	1.7%
Tradable - q/q	0.4%	0.9%
Tradable - y/y	-0.4%	0.1%
Non-tradable - q/q	0.9%	0.3%
Non-tradable - y/y	3.0%	2.8%

While we expect headline inflation to fall further from the 2% target midpoint in Q3, the RBNZ may find a glimmer of hope from the rise in non-tradable inflation towards 3% y/y we're expecting. Movements in non-tradable inflation are more persistent than tradable inflation, and therefore more important for monetary policy. That said, the RBNZ's focus will likely remain on the slowing economy, which we expect will see inflation continue to fall short over the next year.

Taking much signal from this CPI print would be navigating by looking in the rear-view mirror. Inflation is a lagging indicator, and recent strength reflects previous stretch in the economy. For the RBNZ, a stronger-than-expected non-tradable inflation print would be unlikely to sway the Committee from a November cut, or the possibility of more cuts into 2020.

With annual GDP growth down to a 6-year low of 2.1% y/y last quarter, and growth set to remain subdued, it looks like more slack will open up in the economy. More slack means less price pressures ahead, something that the RBNZ will be acutely concerned about, given that inflation expectations are already low.

And the outlook for domestic inflationary pressure is getting weaker by the day. Business surveys now confirm that capacity pressures have eased, with a lack of demand increasingly becoming a constraint for firms, with many businesses now expecting to lay off staff after years of reported labour shortages. On top of that, cost pressures are moderating and pricing intentions have slumped.

All up, inflation is likely to continue to fall short of 2% and potential underlying strength in Q3's inflation print won't be enough to comfort the RBNZ. We expect annual non-tradable inflation to slow over 2020, with headline inflation to remain below 2% out to the end of 2021. The RBNZ needs GDP growth to accelerate to achieve a sustained lift in inflation to 2%, and that is looking increasingly unlikely to occur. We're expecting a 25bp cut in November, and further cuts in February and May to take the OCR to 0.25%.

Table 1. ANZ Q2 CPI component-level forecast

Groups	q/q%	%pt cont.
Food	1.3	0.25
Alcoholic beverages and tobacco	0.1	0.01
Clothing and footwear	0.0	0.00
Housing and household utilities	1.1	0.28
Household contents and services	0.6	0.03
Health	0.5	0.02
Transport	0.1	0.01
Communication	-1.1	-0.03
Recreation and culture	1.1	0.10
Education	0.1	0.00
Miscellaneous goods and services	0.9	0.07
Total	**0.7**	**0.7**

Figure 1. Selected core inflation measures

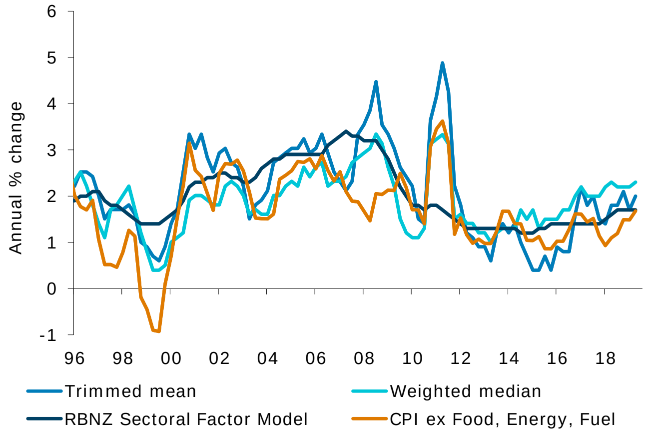


Figure 2. Headline, tradables & non-tradables inflation

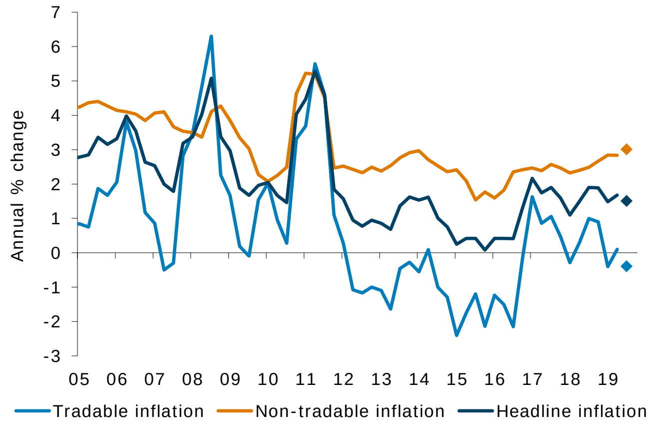
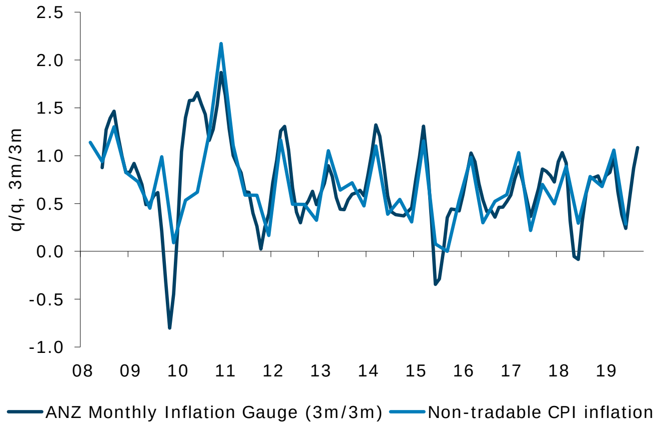


Figure 3. ANZ Inflation Gauge & non-tradables inflation



Source: Statistics NZ, RBNZ, ANZ Research

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