

September 2022 Quarter CPI Preview

13 October 2022



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Past the peak?

The bottom line

- We expect annual CPI inflation eased to 6.6% in Q3, down from 7.3% in Q2 and a touch stronger than the RBNZ's August MPS forecast of 6.4%.
- The bulk of the decline in headline inflation is expected to come from a sharp drop in petrol prices. While that's absolutely welcome, the fact that there's unlikely to be any sign of a broad-based easing in underlying inflation pressures means monetary policy makers can take only limited comfort from the headline fall.
- We're forecasting that annual non-tradables (ie domestic) inflation stayed high at 6.3%, and that measures of core inflation remained too strong (even if they could ease a touch from recent highs).
- All up, next week's inflation report is unlikely to contain the evidence needed to convince the RBNZ that underlying inflation has turned the corner. Unless there's a step change in the outlook, we see the RBNZ [on track to lift the OCR](#) to a peak of 4.75% in May 2023.

The view

September quarter CPI inflation figures are released next Tuesday (18 October), and it's looking very likely that headline CPI inflation declined. We're forecasting that consumer prices rose 1.6% q/q (6.6% y/y) in Q3, decelerating from Q2's 1.7% q/q (7.3% y/y) lift. The bulk of the decline in inflation is expected to come from a drop in petrol prices. While that's good news for squeezed consumers, it's less comforting for the RBNZ than an equivalent but broader-based fall in inflation would be. We anticipate that annual tradables (ie imported) inflation eased to 6.8% in Q3 (8.7% previously), while annual non-tradables (ie more domestically oriented) inflation is expected to remain high at 6.3%. In short, we're unlikely to see significant evidence of domestic inflation pressures starting to ease in next week's data. Some core inflation measures may well dip from recent highs, but not enough to provide much comfort for the RBNZ, who remain firmly focussed on upside inflation risks.

Breaking down the expected 1.6% q/q rise in headline CPI in the September quarter:

- **Food prices** have surged in recent months, with the Stats NZ Food Price Index posting an 8.3% lift in the 12 months to September. Russia's invasion of Ukraine (the 'breadbasket of Europe') has driven some of the increase in global food prices over 2022, but adverse weather events and surging domestic costs have been doing their part to push up local food prices as well. The 3.6% increase in food prices in the three months to September is expected to add 0.7ppts to the headline figure.
- **Housing-related costs** are expected to add 0.6ppts to the headline figure. Within this group, the Rent Price Index rose 1.1% q/q (4.1% y/y) in Q3. That's expected to add 0.1ppts to headline inflation. Annual council rates increases are estimated to have added another 0.2ppts.

Consumers Price Index – September 2022 Quarter

	Prev	ANZ	RBNZ
CPI – q/q	1.7%	1.6%	1.4%
CPI – y/y	7.3%	6.6%	6.4%
Tradable – q/q	1.9%	1.0%	0.7%
Tradable – y/y	8.7%	6.8%	6.5%
Non-tradable – q/q	1.4%	1.8%	1.8%
Non-tradable – y/y	6.3%	6.3%	6.3%

Construction costs are expected to have lifted 3.5% q/q, adding 0.3ppts to overall inflation. However, construction costs are a source of considerable uncertainty in the forecast. The steep drop in house prices (and sales) in recent months would usually be associated with a sharp slowdown in construction cost inflation (albeit with a roughly six-month lag). But house prices have been declining since the end of last year, and there's been precious little sign of any decline in cost inflation yet. In the Q3 QSBO, reported average costs amongst construction firms actually rose relative to Q2. And with residential dwelling consents remaining elevated in Q3, resource pressure in the construction sector may be slow to abate. Nonetheless, we do expect it to ease in coming quarters as the [slowing housing market](#) and rising interest rates take their toll.

- **Recreation & culture** is expected to add 0.2ppts to headline inflation, reflecting a range of broad-based price increases across audio-visual and computing equipment, accommodation services, recreational and cultural services, and recreational equipment and supplies.
- **Transport costs** are the only group in the CPI that are expected to subtract from overall inflation, weighed down by an estimated 8.1% q/q decline in petrol prices. The drop in petrol alone is expected to chop 0.3ppts off the quarterly headline CPI inflation print. The relief from lower petrol prices may not last long, unfortunately. Global oil stocks are relatively low, OPEC+ has agreed on further cuts to oil production, and US shale oil production is likely to remain weak, despite the still-elevated price of crude oil. ANZ forecasts that we could see crude oil prices back above USD110/barrel by the end of the year. Add in NZD weakness against the USD, and petrol prices could climb significantly before the year is out.
- **The final 0.4ppts** consist of price rises across all the other CPI groups, reflecting the broad-based nature of the current inflation surge.

Uncertainty about the inflation outlook remains high, and there are significant upside and downside risks. On the downside:

- Global shipping costs have fallen steeply in recent months, and measures of delivery times have improved rapidly too. If this flows through to a faster-than-expected slowdown in tradables (ie imported) inflation, then headline inflation could fall away much faster than currently anticipated.
- Construction costs could also ease faster than expected, which would help to take some of the heat out of domestic inflation. But with non-tradables inflation remaining broad based, a drop in construction cost inflation is necessary, but not sufficient, for the RBNZ to be confident that they've broken the back of core inflation.

On the upside, domestic labour market and capacity pressure indicators are holding up remarkably well:

- The economy was still adding new jobs [at a steady clip](#) in the three months to August 2022, and
- Measures of labour market stretch and employment intentions [remained extremely robust](#) in the latest QSBO.

A persistently stretched labour market adds to the risk of domestic inflation pressures remaining stubbornly high, requiring the RBNZ to continue hiking into the face of a pronounced housing downturn.

The details of next week's inflation data will be key for the RBNZ. If we see headline inflation ease, but domestic inflation pressures remaining intense (our forecast), that shouldn't do much to change their hawkish stance. However, if we see a fall in CPI inflation accompanied by a significant reduction in a broad range of CPI groups (ie not just petrol prices), that could be the evidence the RBNZ needs to ease back on the pace (and eventual level) of OCR hikes. However, given the strong starting point for core inflation pressures, we think the hurdle will be very high for next week's data to deter the RBNZ from delivering a sixth consecutive 50bp rate hike at the November MPS. Q3's labour market report on 2 November will be key ahead of the RBNZ's next decision. Should we continue to see widespread surges in labour cost inflation, the bar for a change in tack from the RBNZ will be raised higher still.

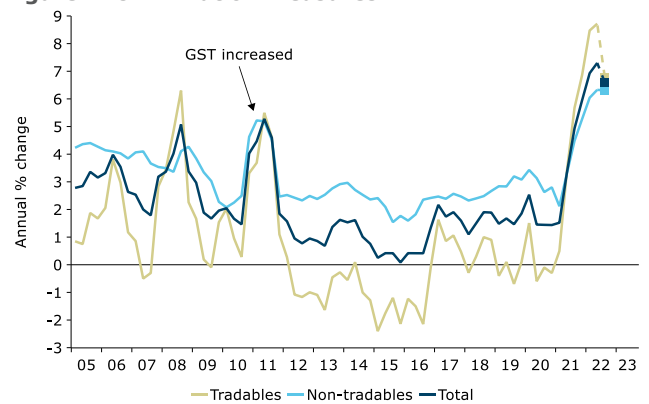
Table 1. ANZ Q3 CPI component-level forecast

	-3	-2	-1	0	1	2	3	4	q/q%	%pt cont.
Total									1.6	1.54
Food									3.6	0.75
Housing & Household Utilities									1.9	0.63
Recreation & Culture									1.9	0.18
Miscellaneous Goods & Services									1.0	0.09
Household Contents & Services									1.9	0.09
Alcoholic Beverages & Tobacco									0.4	0.04
Health									0.7	0.03
Education									0.7	0.01
Communication									0.5	0.01
Clothes & Footwear									0.1	0.00
Transport									-2.2	-0.30

■ Quarterly % change ■ Percentage point contribution

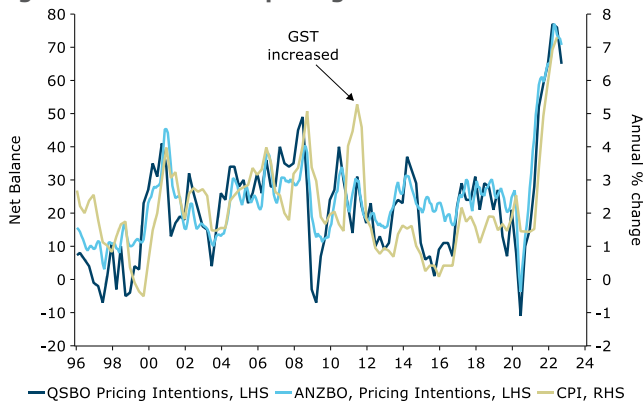
Source: Stats NZ, Macrobond, ANZ Research

Figure 1. CPI inflation measures



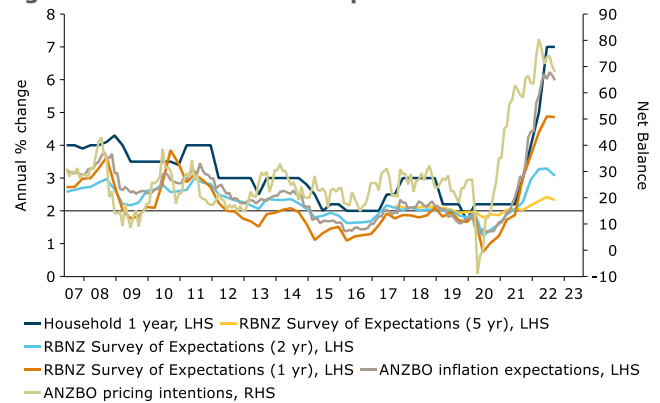
Source: Stats NZ, Macrobond, ANZ Research

Figure 2. Inflation and pricing intentions



Source: NZIER, Stats NZ, Macrobond, ANZ Research

Figure 3. Selected inflation expectations measures



Source: Stats NZ, ANZ, RBNZ, Macrobond, ANZ Research



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