ANZ Research

March 2024 Quarter CPI Preview

12 April 2024

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Contact

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Something for everyone

The bottom line

- We expect the CPI rose 0.6% q/q in Q1, taking annual inflation from 4.7% y/y to 4.0% y/y, above the RBNZ's February MPS forecast of 0.4% q/q (3.8% y/y).
- We expect non-tradable (domestically driven) inflation rose 1.3% q/q (5.5% y/y), above the RBNZ's forecast of 1.1% q/q (5.3% y/y). Non-tradable inflation has continually printed stronger than the RBNZ has anticipated since the last hike in May last year. However, weakness in activity and the emergence of spare capacity across the economy, particularly in the labour market, should be sufficient for the RBNZ to tolerate near-term strength, given our assessment of a pipeline of domestic disinflation ahead.
- We expect tradable (largely imported) inflation of -0.4% q/q (1.9% y/y), well above the RBNZ's February forecast of -0.8% q/q (1.5% y/y), but still weak as the post-COVID supply-side normalisation continues. However, with renewed inflation risks from rising commodity prices and shipping disruption, disinflation progress must transition to being led by domestic and services inflation.
- The suite of core measures will be crucial for the RBNZ's interpretation of the CPI data. Despite stronger near-term inflation pressures, we expect a meaningful step down in core inflation rates, which should satisfy the RBNZ that the underlying disinflation trend remains intact.
- All up, disinflation progress is occurring more slowly than the RBNZ anticipated, but progress is being made. However, given a potential reemergence of global inflation pressures the RBNZ is likely to remain cautious amidst the uncertainty. Inflation at 4% would still be double the target midpoint, and there is still a risk that inflation stabilises above target. Until the RBNZ has seen concrete evidence that domestic inflation pressures are beaten it likely won't take any chances by easing policy settings too proactively – nor by even suggesting that it might.

Consumers Price Index – March 2024 Quarter

	Prev	ANZ	RBNZ
CPI – q/q	0.5%	**0.6%**	**0.4%**
CPI – y/y	4.7%	**4.0%**	**3.8%**
Tradables - q/q	-0.2%	**-0.4%**	**-0.8%**
Tradables - y/y	3.0%	**1.9%**	**1.5%**
Non-tradables - q/q	1.1%	**1.3%**	**1.1%**
Non-tradables - y/y	5.9%	**5.5%**	**5.3%**

The big picture

We expect the Q1 CPI report to show stronger near-term inflation pressures than the RBNZ had anticipated at the February MPS, though the broader disinflation trend remains intact. Broadly, the divergence across the inflation basket remains, with global (tradable) disinflation still washing through, while domestic-driven (non-tradable) inflation for now remains robust even as the domestic economy itself does not.

The latter is a question of timing and magnitude, certainly not direction. It's clearly heading lower this year. However, the global inflation narrative has shifted in recent months with the re-emergence of inflationary pressures. Global supply-chain disruption, one of the driving forces behind the initial COVID inflation surge, has reemerged, with shipping disruption in the Red Sea (geopolitical risk) and Panama Canal (drought) adding to businesses' cost burden. Meanwhile, commodity prices have risen dramatically, with oil prices up close to 25% since mid-December. While these drivers won't be fully reflected in the Q1 data next week, if sustained, they do create risk that inflation does not return to the RBNZ's target band as soon as Q3, which is likely one of the prerequisites for OCR cuts to be on the table.

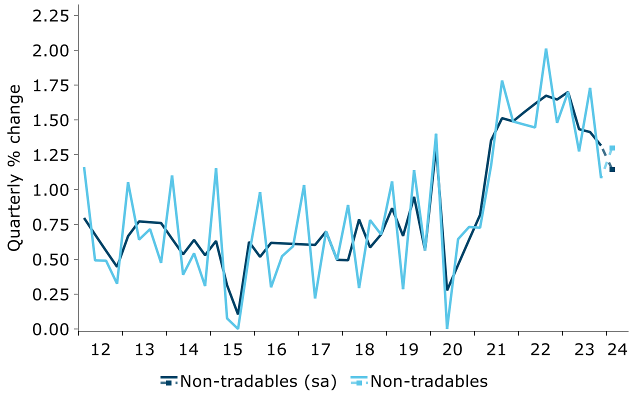
New Zealand is still benefiting from the lagged unwind of global COVID-era supply pressures, with lower goods prices and airfares still yet to be fully reflected in measured inflation. We expect tradable inflation remained weak in Q1, falling 0.4% q/q, though that's a smaller fall than the RBNZ had anticipated. These components are volatile, and we expect the RBNZ will look through any near-term surprises, provided they are transitory and don't spill over into broader prices. But tradable disinflation is likely to wane across the year ahead as the supply-side normalisation runs its course. For the broader disinflation story to remain intact, it will increasingly need to be driven by progress across domestic and services inflation components.

Progress on domestic inflation has occurred, but at a much slower rate than the RBNZ had anticipated, and we expect non-tradable inflation will again surprise the RBNZ to the upside in Q1. While sticky domestic inflation risks remain, particularly across components such as council rates, insurance and rents, stripping out these components highlights monetary policy is having its desired effect. Underlying inflation pressures have eased, inflation expectations have fallen, labour market pressures have faded, and activity has cooled significantly.

The conditions are thus in place for a sustained moderation in domestic inflation, and this is likely to be evident across the suite of core inflation measures in Q1. Across the suite of core measures in next week's release that we focus on (30% trimmed mean, and weighted median, and CPI ex food, fuel and energy), we expect these to step down further to around 4% y/y. This further progress should provide an offset to stronger-than-anticipated near-term inflation pressures for the RBNZ, particularly given that those surprises have largely reflected the more volatile components, rather than broad-based surprising strength.

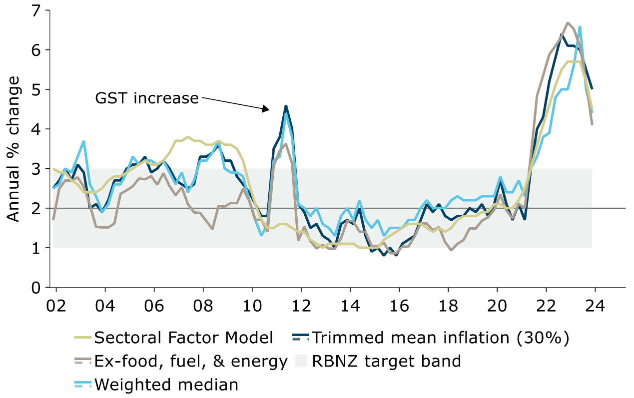
That said, despite the clear progress that has been made, it's simply too early to declare victory. As core and domestic-driven inflation move closer to target, the capacity for the RBNZ to look through shocks will increase, and the certainty about the point at which it will be in a position to cut rates will be much greater. But the RBNZ simply can't be confident enough yet that reality won't get in the way of a good story, with plenty of upside inflation risks still on the table and a starting point that is still a long way from the ultimate destination.

Figure 1. Quarterly non-tradable inflation



Source: Stats NZ, Macrobond, ANZ Research

Figure 2. Core inflation measures



Source: Stats NZ, RBNZ, Macrobond, ANZ Research

The details

Breaking down our forecast for a 0.6% q/q increase in headline inflation:

- **Housing-related costs** are expected to add 0.2%pts to the quarterly headline figure. Within this group:
  - The Rent Price Index rose 1.1% q/q (4.6% y/y) in Q1, adding 0.1%pts to quarterly headline inflation. Given that the CPI measure of rent inflation takes into account tenancies over the past 8-10 years, it is slow to reflect changes. We expect rent price inflation to remain around current levels for the remainder of the year.
  - Construction costs are expected to have lifted 0.7% q/q in Q1, adding 0.1%pts to quarterly headline inflation. Cost pressures in the sector have eased significantly, as disruption to materials supply has unwound. In addition, weakening demand is making it hard for firms to maintain margins, keeping a lid on inflation pressures. Our ANZBO survey highlights that price pressures have tanked in this sector, to be the lowest across the economy.
- **Alcohol and tobacco** are expected to add 0.2%pts to headline inflation, the bulk of which reflects the annual increase in tobacco excise rates.
- **Miscellaneous goods and services** are expected to add 0.1%pts to headline inflation, mostly reflecting continued strength in insurance cost inflation. The influence of monetary policy is fairly limited here. However, the RBNZ will still be concerned about the potential influence on inflation expectations.
- **Recreation and culture** are expected to add 0.2%pts to headline inflation, reflecting strength in accommodation services both here and abroad, tied to the ongoing recovery in tourism-related sectors.
- **Food price inflation** is expected add 0.1%pts to headline inflation. Food price inflation has been softer than is typical in Q1, largely reflecting the normalisation in fresh produce supply capacity after cyclone-related disruption last year. Lower imported food costs are also still flowing through to New Zealand shelves.
- **Transport inflation** is expected to subtract 0.3%pts from quarterly headline inflation, reflecting lower fuel prices in the quarter and the normalisation in international airfares. However, relief at the pump has proven short-lived, with tight supply in global oil markets and a geopolitical risk premium likely to be reflected in Q2 CPI.
- **The remaining 0.1%pts** is a mixed bag of ups and downs across the other components.

The view

We don’t expect the Q1 CPI report to materially shift the dial on monetary policy expectations, with the details likely to have something for both the hawks and the doves. For the doves, falling core inflation will offset the near-term noise, alongside weakening domestic activity and a cooling labour market that’s still flowing through to softer domestic inflation. For the hawks, the potential reemergence of global inflation pressures highlights that a lot of the fall in CPI inflation thus far has been due to factors beyond the RBNZ’s control, as well as the risk that inflation does not return to the target band this year. The outlook remains highly uncertain, and we think the RBNZ’s strategy will be to continue to “watch, worry and wait.”

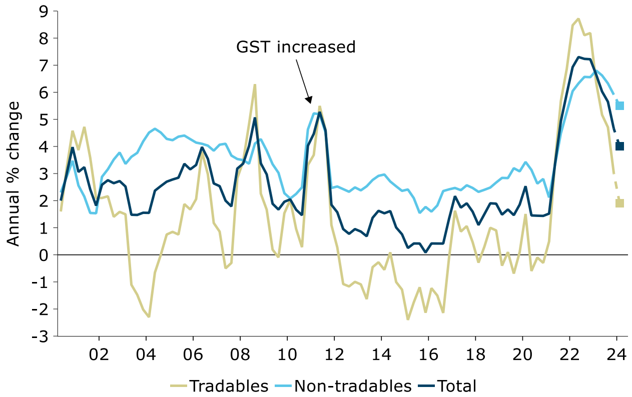
Table 1. ANZ Q1 CPI component-level forecast

	q/q%	%pt cont.
Total	**0.6**	**0.58**
Alcoholic Beverages & Tobacco	2.8	0.24
Housing & Household Utilities	0.6	0.22
Recreation & Culture	1.2	0.19
Miscellaneous Goods & Services	1.4	0.12
Food	0.4	0.09
Education	3.0	0.05
Health	0.5	0.02
Communication	-0.1	0.00
Clothes & Footwear	-0.4	-0.02
Household Contents & Services	-0.6	-0.03
Transport	-1.6	-0.30

■ Quarterly % change ■ Percentage point contribution

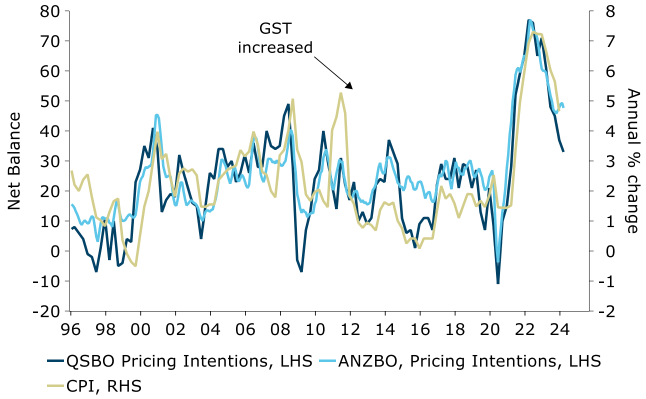
Source: Stats NZ, Macrobond, ANZ Research

Figure 3. CPI inflation measures



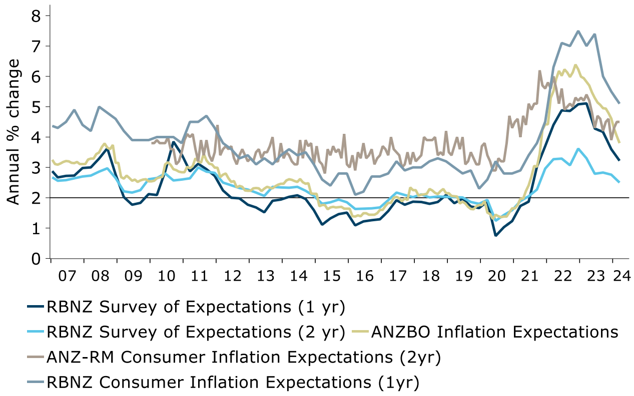
Source: Stats NZ, Macrobond, ANZ Research

Figure 4. Inflation and pricing intentions



Source: NZIER, Stats NZ, Macrobond, ANZ Research

Figure 5. Selected inflation expectations measures



Source: Stats NZ, RBNZ, Macrobond, ANZ Research

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