

# NEW ZEALAND ECONOMICS DATA REVIEW

## CONSUMERS PRICE INDEX – MARCH 2016 QUARTER

18 April 2016

### CONTRIBUTORS

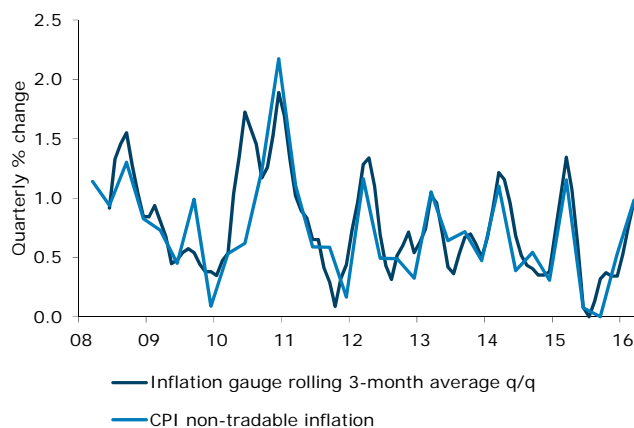
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## A REAL MIXTURE

### KEY POINTS

- **Headline consumer prices rose 0.2% in Q1 (+0.2% sa)**, a touch firmer than the market consensus of a 0.1% rise but in line with the RBNZ's pick. Annual CPI inflation firmed to 0.4%, but was still the sixth consecutive outturn below 1% and 18th successive sub-2% outturn.
- **Tradable prices declined 0.9% q/q (-0.5% sa, -1.2% y/y)**, with a 7.7% fall in petrol prices, a 12% seasonal fall in international airfares and the third consecutive fall for package holiday prices clearly influential. There were also a few more signs that the disinflationary impact of past NZD strength was abating.
- **Non-tradable prices rose 1.0% q/q (+0.4% sa)**, with annual inflation falling to 1.6%. The print was consistent with the signal provided by our Monthly Inflation Gauge, which reaffirms its value as an inflation indicator. Importantly, looking through the details suggest the stronger-than-expected result was not due to one or two surprises, but was more broad-based.
- **Readings from the core CPI measures produced by Statistics NZ were firmer than the headline CPI print.** Our model estimates of the RBNZ Sectoral Factor Model suggest that inflation on this measure is likely to remain "sticky" at around 1½% for Q1.
- **Overall, today's figures are a real mixed bag.** While the data certainly doesn't rule out the RBNZ cutting the OCR again next week, we don't see it as the smoking gun that the market was hoping it would be.
- Our core view is for a further 50bps of OCR cuts over 2016. **We are also wary of the trade-offs a lower OCR will bring given surging asset prices and the return of re-leveraging type behaviour.** This suggests the non-trivial probability we may be at the OCR trough.

FIGURE 1. MONTHLY INFLATION GAUGE AND NON-TRADABLE CPI



Source: ANZ, Statistics NZ

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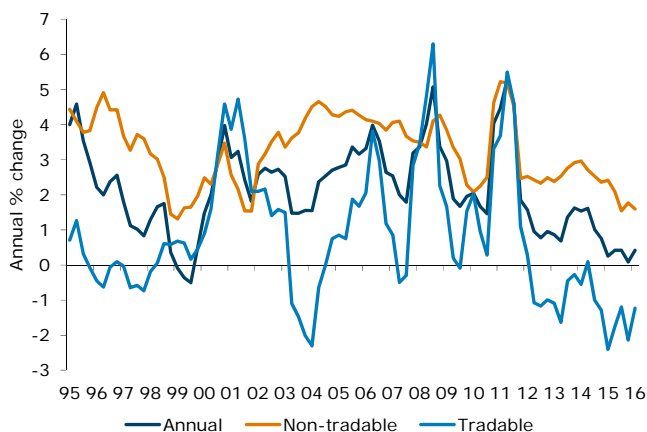
## DATA WRAP

**Headline consumer prices rose 0.2% in Q1 (+0.2% sa),** a touch firmer than the market consensus of a 0.1% rise but in line with the RBNZ's pick. Annual CPI inflation firmed to 0.4%, but was still the sixth consecutive outturn below 1% and 18th successive sub-2% outturn.

	Headline CPI		Tradable		Non-tradable	
	Qtrly % chg	Ann % chg	Qtrly % chg	Ann % chg	Qtrly % chg	Ann % chg
Mar-14	0.3	1.5	-0.7	-0.6	1.1	3.0
Jun-14	0.3	1.6	0.2	0.1	0.4	2.7
Sep-14	0.3	1.0	0.1	-1.0	0.5	2.5
Dec-14	-0.2	0.8	-0.8	-1.3	0.3	2.4
Mar-15	-0.2	0.3	-1.9	-2.4	1.2	2.4
Jun-15	0.4	0.4	0.9	-1.8	0.1	2.1
Sep-15	0.3	0.4	0.7	-1.2	0.0	1.5
Dec-15	-0.5	0.1	-1.8	-2.1	0.5	1.8
<b>Mar-16</b>	<b>0.2</b>	<b>0.4</b>	<b>-0.9</b>	<b>-1.2</b>	<b>1.0</b>	<b>1.6</b>
ANZ	0.1	0.4	-0.8	-1.0	0.8	1.4
Market	0.1	0.4	–	–	–	–
RBNZ	0.2	0.4	–	–	–	–

**Movements for tradable and non-tradable prices were broadly offsetting, reflective of the offsetting shocks hitting the economy** and highlight the difficulties in characterising the current inflation backdrop.

**FIGURE 2. CPI, TRADABLE AND NON-TRADABLE PRICES**



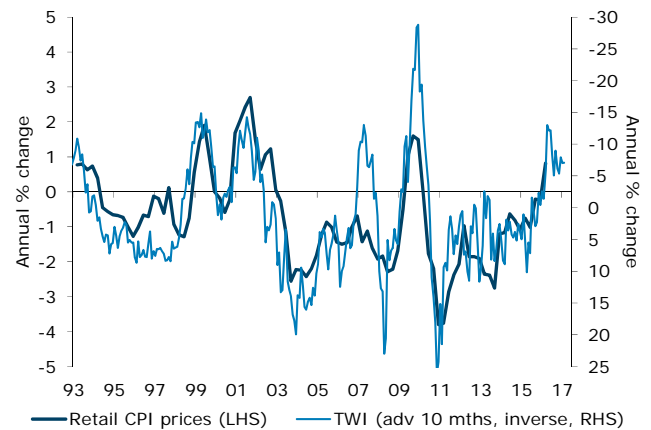
Source: ANZ, Statistics NZ

**Despite seasonal rises for food prices, tradable prices declined 0.9% q/q (-0.5% sa, -1.2% y/y),** The 7.7% fall in petrol prices, a 12% seasonal fall in international airfares and the third consecutive fall for package holiday prices were clearly influential and look to be due to a combination of competitive pressures and the lagged impact of lower oil prices. Lower prices for apparel, medical equipment and

audio visual and computing equipment also helped to hold down tradable prices.

**Despite the soft print for overall tradable prices, the CPI report also provided a few more signs that the disinflationary impact of past NZD strength was abating.** Household contents & services prices rose 1.7% (there were solid rises for textiles, appliances and household utensil prices), motor vehicle prices rose 1.6%, and there were some increases seen in tradable groups that have been recording price falls recently. As Figure 2 suggests, the period of outright retail sector deflation looks to be coming to an end.

**FIGURE 3. RETAIL CPI PRICES AND THE NZD**



Source: ANZ, Statistics NZ

**Non-tradable prices rose 1.0% q/q (+0.4% sa),** with annual inflation falling to 1.6% – a 17 year low. Despite this, the quarterly print was firmer than both our and the RBNZ pick of a 0.8% q/q increase, but was consistent with the signal provided by our Monthly Inflation Gauge. Beyond the housing group, surging accommodation services prices highlight capacity constraints (+4.9% q/q, +4.8% y/y).

**Importantly, looking through the details suggest the stronger-than-expected result was not due to one or two surprises, but was more broad-based.** Government charges featured heavily, with tobacco prices rising 9.4%. Stripping out the impact of government charges and tobacco prices, however, delivered a rising print for quarterly inflation (+0.7% q/q,) with the 1.9% annual print fractionally below the inflation target midpoint.

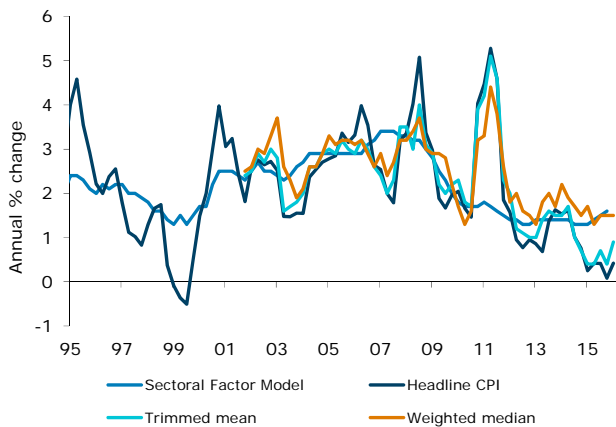
**Pressures from the housing group remained acute,** although the March quarter increases in construction costs (0.8% q/q, and 5.0%y/y) and dwelling rents (0.6% q/q, and 2.3% y/y) were actually a touch softer than we expected. That said, inflation from these sources could step up given firm anecdotes of late. Moreover, the regional splits were consistent with anecdotes, with Auckland having the

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highest annual regional inflation rates for construction and rents (+7.6% y/y and 3.2% y/y respectively).

**Readings from the core CPI measures produced by Statistics NZ were generally firmer.** Prices from the CPI excluding food, fuel and energy prices rose 0.6% q/q (+0.8% y/y), quarterly changes in the 5-15% trimmed means were in a 0.2 to 0.3% range (+0.8% to +0.9% y/y), with a +0.3% q/q change in prices from the 50% weighted median (+1.5%/y/y).

**FIGURE 4. CORE CPI INFLATION MEASURES**



Source: ANZ, Statistics NZ, RBNZ

**Our components based model suggests annual inflation from the RBNZ Sectoral Factor Model is likely to have remained “sticky” at around 1½% in Q1, which followed three consecutive quarterly increases.** In our view outturns from this measure provide a more accurate barometer of underlying inflation trends and suggest that the inflation backdrop is not as soft as the headline numbers suggest. We will find out for sure when the RBNZ publish its estimates at 3pm.

### COMMENT AND ASSESSMENT

In summary, details beneath the surface of today's figures were a little firmer than what we had expected and suggest that many of the factors suppressing inflation are starting to ease. This journey is expected to continue as the effects of past NZD strength wane, which should see annual CPI inflation continuing to modestly edge higher. However, this view critically hinges on commodity prices strengthening, and the local and global outlooks holding together.

Our core view remains for a further 50bps of OCR cuts over 2016, with a low inflation backdrop providing the RBNZ with scope to cushion the economy given the impacts of tighter financial conditions on economic activity. However, **we are**

**wary of the trade-offs a lower OCR will bring given surging asset prices and the return of re-leveraging type behaviour.** In fact, there is a nontrivial probability that we may be at the OCR trough. Non-tradable inflation has firmed now for two consecutive quarters, and some of the traditional drivers for inflation are not as benign as the low headline print suggests.

### IMMEDIATE MARKET REACTION

The CPI result was a fraction above expectations, with the NZD marginally higher following the result. Local yields were also a fraction higher.

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