

# NEW ZEALAND ECONOMICS

## ANZ MONTHLY INFLATION GAUGE

May 2015

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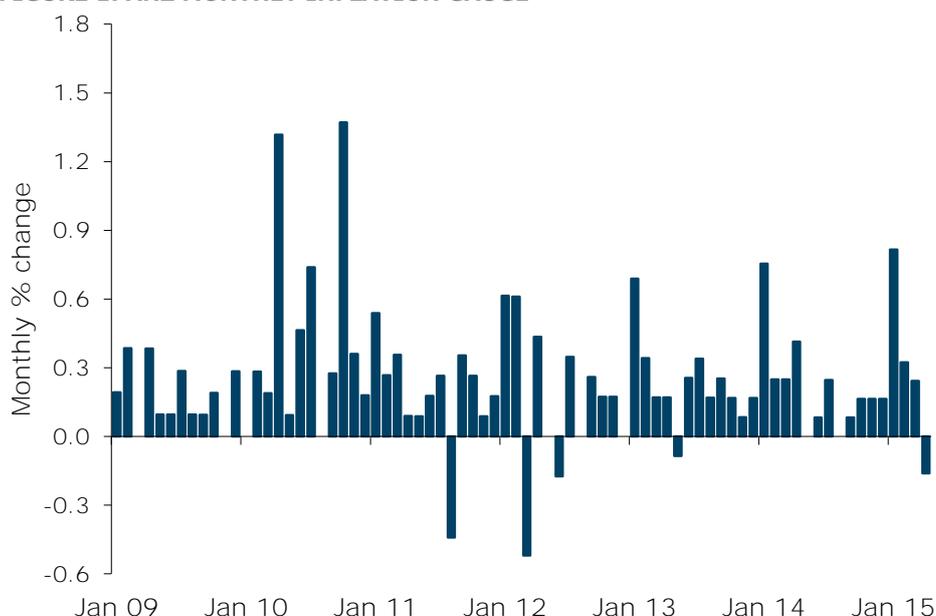
### SUMMARY

- Falls in the housing, miscellaneous goods, and recreation & culture groups contributed to a 0.2% fall in the April Monthly Inflation Gauge. Prices were flat excluding the housing group.
- Prices in the Gauge rose 1.0% in the three months to April. Over this time, pricing pressure remained housing and government charge-centric, with prices outside of these areas up just 0.1% in the three months to April.
- **We've seen enough across our four prongs** (high NZD, dairy income squeeze, inevitability of a prudential response towards housing and continued low core inflation reads) to call the OCR lower.
- We expect the RBNZ to cut by 25bps in June and follow up with another cut in July.
- Monetary policy is more than merely monitoring demand and wage and price setting outcomes; the RBNZ must manage the risk profile around them. Cutting the OCR is a low delta option to manage emerging risks.

### SLEEPING BEAUTY

Measures from our **Monthly Inflation Gauge** provide a **directional signal of broad trends and movements in non-tradable CPI inflation** produced by Statistics New Zealand, but at a monthly frequency. Differences in methodology and coverage mean the Gauge will not exactly mirror the official series. We also produce an Underlying ex housing Gauge that adjusts for indirect taxes and tertiary education fees and removes housing group prices.

**FIGURE 1: ANZ MONTHLY INFLATION GAUGE**



Source: ANZ

**Prices in our Gauge fell 0.2% in April.** Housing was again the major mover, but April actually saw price falls, ending the sequence of sizeable increases. Over the month, price falls were noted for dwelling rents and construction costs, with

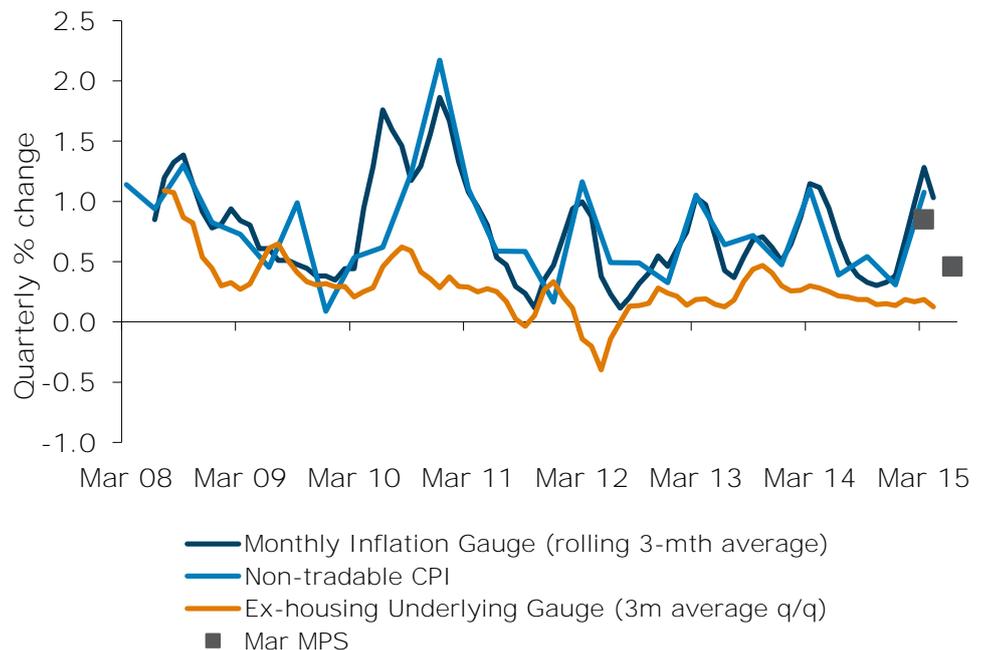
## ANZ MONTHLY INFLATION GAUGE

electricity charges also lower. While rents usually fall in April, what was particularly notable were falls in rents in some Auckland and Canterbury areas despite there being a shortage of dwellings in these regions. Our estimates also suggest pricing pressure is cooling in the construction sector, although it is still early days.

**Prices in the Underlying Ex-housing Gauge were flat for the third consecutive month.** Lower tariffs for hotel and holiday park accommodation offset increases for aquarium admissions, resulting in a fall in recreation & culture group prices. Lower vehicle insurance contributed to lower miscellaneous goods & services prices. There were a few movements elsewhere, with an April increase in GP fees, but these were few and far between. Prices fell in three groups, with an increase in rail passenger transport fees contributing to a solitary rise in the transport group.

**Prices in the Gauge rose 1.0% in the three months to April**, and are moving in a trajectory consistent with the RBNZ's March MPS pick of a 0.5% increase for Q2 non-tradable inflation. **However, price rises outside of government charges and housing were virtually non-existent, with just a 0.1% increase over this period.** What has been notable has been a lack of generalised inflationary pressure despite the economic expansion being well advanced.

**FIGURE 2: MONTHLY INFLATION GAUGE AND NON-TRADABLE CPI**



Source: ANZ, Statistics NZ, RBNZ

**The OCR should be lower.** Demand across the economy is still solid yet the reality is that inflation has failed to show up at the growth party. Core inflation has now been below the 2% target for 21 successive quarters. **That's enough in itself to justify OCR cuts.** The RBNZ has an inflation target not a growth or a housing one. Of course the three are inter-connected but one dominates; one policy instrument (OCR) equals one target (inflation). Any high school student knows you can't solve for two unknowns in one equation.

**However, monetary policy is more than just monitoring the demand side of the economy and wage and price setting outcomes.** That's fine in a perfect world. However, the world is far from that. Uncertainty is pronounced.

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Secular forces collide with cyclical ones. **As if forecasting is not hard enough, there is a risk profile around outcomes to manage as well.**

**The risk profile facing the economy is evolving rapidly;** growth has congregated towards trend and the downside (dairy) is opening up at a time core inflation is closer to 1% than 2%. The RBNZ may ultimately be proven right and the inflationary dragon is merely sleeping. If so the OCR can head back up. However, alternate scenarios are real. It's looking more like Sleeping Beauty than a dozing dragon. **Cutting the OCR is a low delta option to manage emerging economic risks. We see little point waiting until the second half of the year to exercise this optionality.**

	Monthly Inflation Gauge (Index)	Monthly Inflation Gauge (m/m%)	Implied Inflation Gauge (q/q%)	Actual non-tradable CPI (q/q%)
Mar-13	1176	-0.1	1.0	1.1
Apr-13	1178	0.2		
May-13	1177	-0.1		
Jun-13	1180	0.3	0.4	0.6
Jul-13	1184	0.3		
Aug-13	1186	0.2		
Sep-13	1189	0.3	0.7	0.7
Oct-13	1191	0.2		
Nov-13	1192	0.1		
Dec-13	1194	0.2	0.5	0.5
Jan-14	1203	0.8		
Feb-14	1206	0.2		
Mar-14	1209	0.2	1.1	1.1
Apr-14	1214	0.4		
May-14	1214	0.0		
Jun-14	1215	0.1	0.7	0.4
Jul-14	1218	0.2		
Aug-14	1218	0.0		
Sep-14	1219	0.1	0.3	0.5
Oct-14	1221	0.2		
Nov-14	1223	0.2		
Dec-14	1225	0.2	0.4	0.3
Jan-15	1235	0.8		
Feb-15	1239	0.3		
Mar-15	1242	0.2	1.3	1.1
Apr-15	1240	-0.2		

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