

NEW ZEALAND ECONOMICS

CONSUMERS PRICE INDEX – 2016Q4

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REUNITING THE BAND

BOTTOM LINE

- Headline inflation was stronger than expected in Q4, and surprises appeared reasonably broad-based. Importantly, there are clear signs that underlying inflation pressures are continuing to lift off lows (with some core measures now back at 2%), and this is something we expect to continue, albeit gradually, going forward.
- While stronger inflation has threatened before, only for it to prove to be a head-fake, and deflationary factors here and abroad still persist, the number of 'traditional' inflation drivers that are pointing in the same direction (output gap, labour market, inflation expectations, and the global inflation cycle) is becoming hard to ignore.
- It speaks to an inevitability about the OCR not staying at these levels indefinitely, although we still feel the RBNZ has (for now) time on its side.

KEY RESULTS

- **Headline CPI inflation was 0.4% q/q in Q4, above consensus expectations (0.3%).** And as a result of base effects, annual inflation rose to 1.3% y/y, marking the end of eight consecutive quarters below the bottom of the RBNZ's target band. Tradable prices rose 0.3% q/q (-0.1% y/y), while non-tradable prices rose 0.6% q/q (2.4% y/y).
- **As expected, petrol prices made a large positive contribution** (and are a key reason for the bounce in annual inflation – as is the case around the world). A 4.1% q/q lift contributed 0.2%pts to the quarterly CPI result. If petrol prices hold at current levels for the rest of the March quarter, a similar contribution is likely in Q1.
- **The housing group, once again, also recorded a decent lift** (0.6% q/q). Implied construction costs rose 1.4% q/q, and while that is a softer pace than seen in Q2 and Q3, annual inflation in this category lifted to 6.5% – the highest since 2005. There is nothing new in this and it is expected to remain a theme for some time yet, given capacity strains in the construction sector. Rent and property maintenance inflation was broadly stable.
- **Lower food prices (which typically fall in Q4) provided some offset**, again as expected. Prices fell 1.2% q/q (a 0.2%pt drag).
- **The impact of persistent deflationary forces is also still evident, although perhaps not as much as expected.** Tradable-ex-fuels prices fell 0.3% q/q, with some durable-type goods (furniture and floor coverings, appliances, audio visual equipment etc) reversing – at least partially – their surprising lifts in Q3. This was partially offset by gains in new and used car prices and a seasonal lift in international airfares (11% q/q). Nevertheless, the elevated NZD, strong retail competition and the ongoing impact of technology look set to continue to have an influence over elements of the domestic inflation process for some time yet.

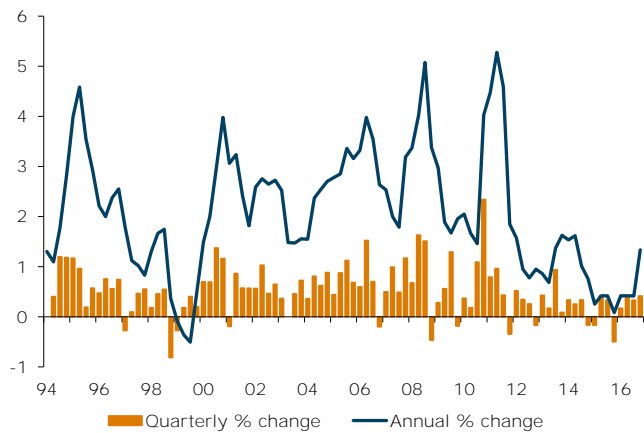
DATA SUMMARY

	% qtr	% ann
Headline CPI	0.4%	1.3%
Tradable	0.3%	-0.1%
Non-tradable	0.6%	2.4%

CPI 2016Q4

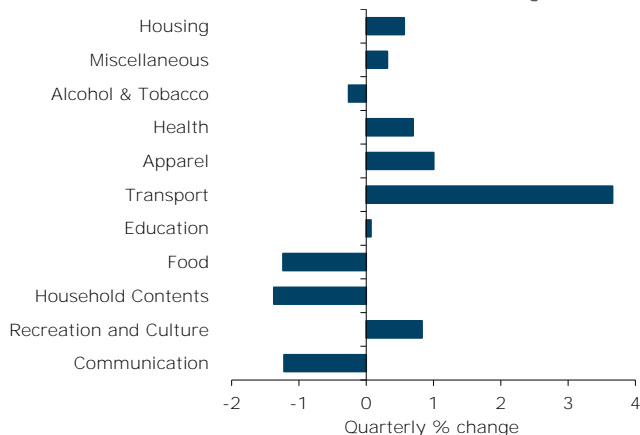
- That said, there are clear signs of emerging price pressures.** Non-tradable inflation ex government charges and tobacco rose 0.8% q/q, to be up 2.4% y/y. That is the strongest annual inflation in this measure since q4 2013. In seasonally adjusted terms, headline inflation rose 0.7% q/q, the strongest quarterly lift since Q3 2013. Core measures such as the weighted median and trimmed mean continue to increase and are closer – or at – the target midpoint (at 2.0% and 1.6% respectively). The CPI ex food, energy and fuel rose to 1.6% y/y, the highest since Q1 2014.
- Our distribution analysis shows that 43% of the CPI basket recorded annual price growth above 2%,** which is the highest proportion in close to five years. We expect this theme of stronger and broader underlying pressures to develop further over the course of 2017. It is all consistent with an economy that is not only growing strongly, but increasingly hitting capacity and resource pressures.

FIGURE 1. HEADLINE CPI INFLATION



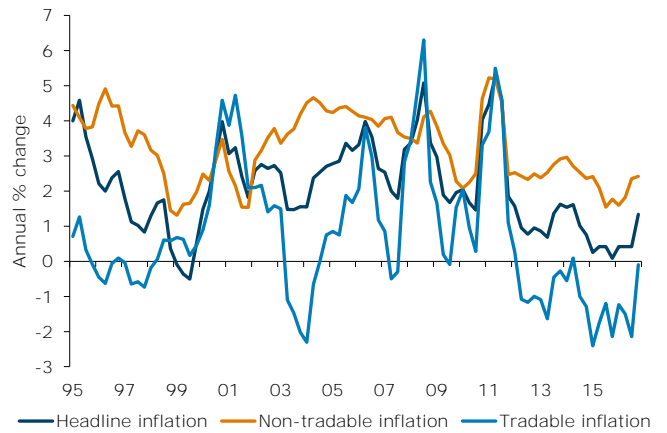
Source: ANZ, Statistics NZ

FIGURE 2. CPI GROUPS – DECEMBER 2016 QUARTER



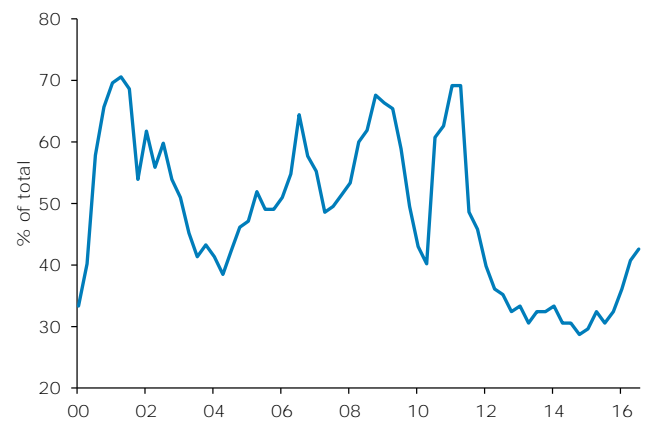
Source: ANZ, Statistics NZ

FIGURE 3. CPI INFLATION COMPONENTS



Source: ANZ, Statistics NZ

FIGURE 4. PROPORTION OF CPI BASKET WITH ANNUAL INFLATION ABOVE 2%



Source: ANZ, Statistics NZ

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