

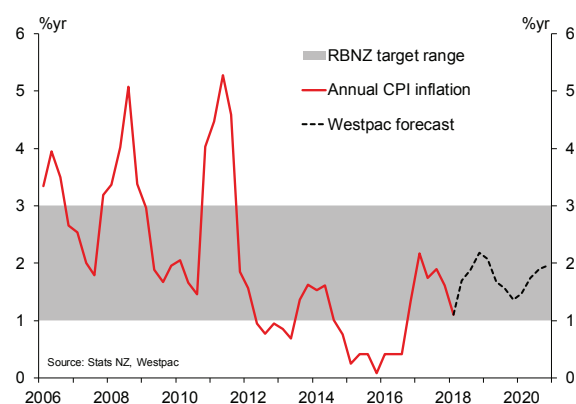
Filling up

June quarter CPI preview: 17 July, 10:45am

12 July 2018

- We expect a 0.6% rise in the Consumer Price Index (CPI) for the June quarter. This would see annual inflation rise to 1.7%.
- The main contributors for the quarter will be higher fuel and food prices. We also expect the lower New Zealand dollar to give a modest lift to import prices.
- Higher fuel prices could lift the inflation rate above 2% by the end of this year. However, we're not confident that this will be sustained into next year.

Annual inflation forecast



For next Tuesday's CPI release, we expect a 0.6% rise in prices for the June quarter. This would see the annual inflation rate rise to 1.7%, after a brief drop to 1.1% in the March quarter.

Our forecast is higher than what the Reserve Bank expected in its May Monetary Policy Statement (0.4% quarterly, 1.5% annual). The difference in forecasts is on the tradables side of the CPI, some of which will reflect the jump in fuel prices late in the quarter.

Fuel prices have played a major role in the gyrations of inflation in recent years, and their influence is likely to linger for a while longer. Given the rise in oil prices to date, plus the planned increases in fuel taxes, we expect annual inflation to reach 2.1% by the end of this year. This would put it above the Reserve Bank's 2% target midpoint for only the second time in seven years. But for this to be sustained into next year, we would need to see a further surge in world oil prices and/or a continued slide in the exchange rate. Home-grown inflation pressures are picking up, but this tends to be a gradual process, and is still some way from the levels that would be consistent with 2% inflation overall.

For the details of next week's release, we expect the biggest positive contributions to come from higher fuel prices and a largely seasonal rise in food prices. The main declines are likely to be in domestic airfares and accommodation, as the peak tourist season comes to an end.

Petrol prices were up 3.5% on average over the June quarter. That's not an unusually large change for this series, but it stands in contrast with the fall in fuel prices this time a year ago. The turnaround in fuel prices accounts for about half of the expected rise in annual inflation from 1.1% to 1.7%.

Higher fuel prices are also starting to affect the cost of air travel, although for this quarter the impact on domestic airfares will be swamped by the usual seasonal decline.

Food prices rose by 0.8% for the quarter, mostly due to a seasonal rise in vegetable prices. There has been a pickup in the cost of eating out since April, possibly stemming from the increase in the minimum wage. But otherwise, food prices have been close to flat over the past year.

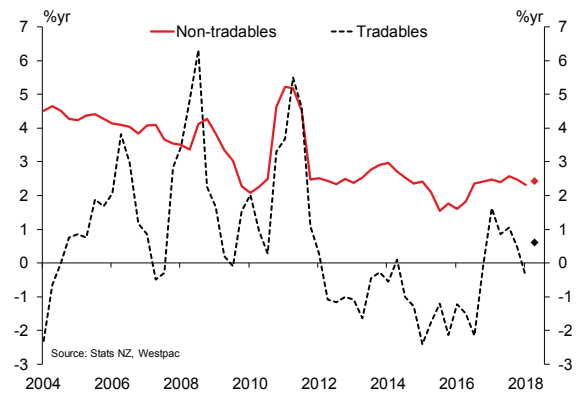
Aside from fuel and food, we expect a modest uptick in tradable goods and services prices. The lower New Zealand dollar over the last year has had little impact on the prices of imported goods to date, but it tends to operate with a lag

of 6-12 months. We expect import prices to rise gradually over the rest of this year.

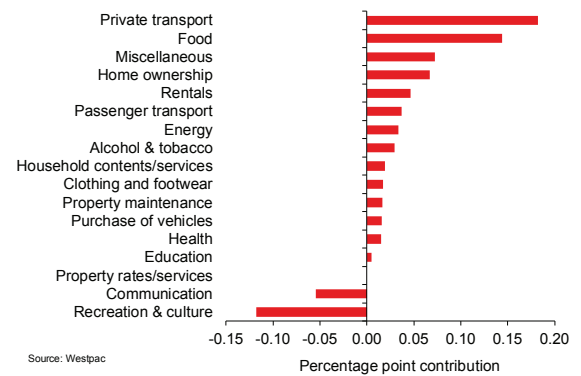
Non-tradables inflation has been picking up gradually for the last couple of years, notwithstanding the impact of Government policies such as the year of free tertiary education that was introduced this year. We expect the annual increase in non-tradables prices to tick up from 2.3% to 2.4%. That said, the housing-related components (rents and new-build homes) are expected to be relatively muted for the quarter.

Michael Gordon
Senior Economist

Inflation components



Contributions to Q2 inflation forecast



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