

Under the pump

March quarter CPI preview: 20 April, 10:45am

- We estimate that the Consumer Price Index (CPI) fell by 0.3% over the March quarter, taking the annual inflation rate down to 0.2%.
- A sharp drop in fuel prices is largely responsible for the slowdown in annual inflation.
- However, wider inflation pressures are likely to have remained subdued, reflecting low wage growth and the still-high New Zealand dollar.

Next Wednesday’s CPI release will be dominated by the steep fall in fuel prices, which began late last year and really kicked into gear over the New Year period. We expect a 0.3% drop in the CPI over the March quarter, which would take annual inflation down from 0.8% to 0.2%. This would be the slowest pace since 1999, when annual inflation briefly dipped below zero.

We estimate that petrol pump prices were down 11% on average over the quarter (and diesel prices were down 17%). The drop in fuel prices equates to a 0.6 percentage point fall in the CPI – that is, it accounts for all the slowdown in annual inflation that we’re expecting.

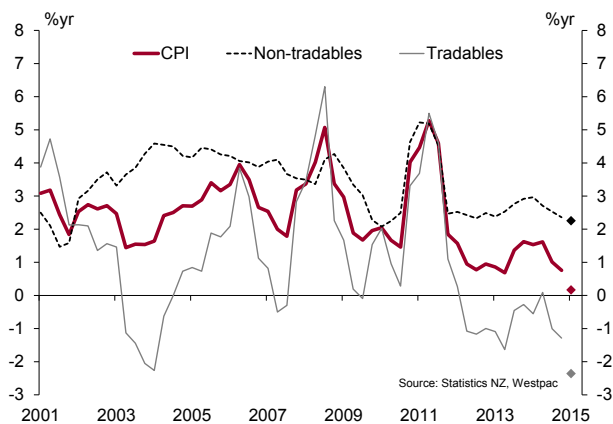
Beyond the plunge in fuel prices, our forecast for the March quarter reflects the usual mishmash of seasonal influences. On the plus side, we have another 10% hike in tobacco excise duty, annual increases in education fees, and a seasonal rise in food prices. These will be partly offset by seasonal declines in overseas airfares and package holidays.

The broader picture remains one of subdued inflation despite a rapidly growing economy. The New Zealand dollar has played a significant part in this: while it’s fallen about 10% against the US dollar over the last year, it was little changed on a trade-weighted basis. As a result, it’s likely that the currency continued to have a depressing effect on tradable goods prices through to the March quarter. Meanwhile, price inflation for non-tradable goods and services has been slowing recently, aside from an acceleration in new home prices as the building industry has hit capacity constraints.

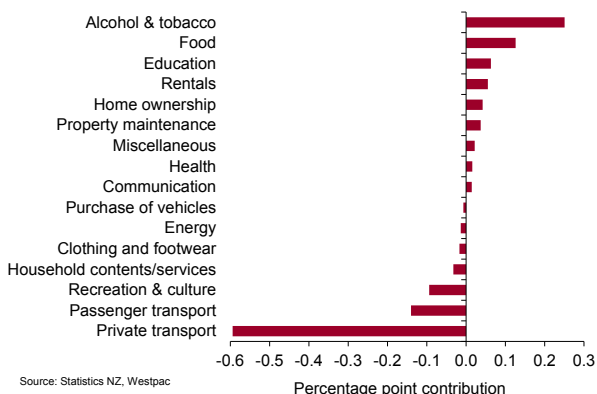
The Reserve Bank has said that it doesn’t intend to respond to the direct impact of a one-off fall in fuel prices. But it is concerned that the persistently below-target inflation of recent years could become embedded in wage- and price-setting behaviour, making it more difficult to return to the 2% target midpoint. In that respect, the non-tradables component of next week’s release will be of most interest. There are already signs of low nominal wage growth and slower price increases for labour-intensive services in particular.

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CPI inflation



Forecast contributions to quarterly inflation



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