



# New Zealand's CPI still contained

A close call, but another hike likely

**New Zealand's inflation has remained surprisingly contained, with today's Q2 CPI lower than the market expected. The CPI rose by +1.6% y-o-y in Q2 (market had +1.8%), so remains in the lower half of the RBNZ's 1-3% target band. There were some signs in the print that the effect of the downward pressure from the high NZD is starting to wear off, with tradables prices up +0.1% y-o-y, the highest reading in over two years. But, non-tradables inflation was surprisingly contained, falling to +2.7% y-o-y. A recent step down in some indicators of local conditions will also give the RBNZ pause for thought, although these indicators still imply above-trend growth. It's a closer call than we thought, but given the RBNZ's recent rhetoric, we still expect them lift rates by a further 25bps next week.**

## Facts

- Headline CPI increased by +0.3% q-o-q to be +1.6% higher y-o-y (market had +0.4% q-o-q and +1.8% y-o-y; HSBC had +0.6% q-o-q and +2.0% y-o-y).
- Non-tradable inflation slowed a little to +2.7% y-o-y, down from +3.0% y-o-y in Q1. Tradable inflation rose to +0.1% y-o-y, from -0.6% in Q1.
- The key measures of core inflation remained generally contained, with the trimmed mean running at +1.6% y-o-y, up from +1.5% y-o-y in Q1. Weighted median inflation rose to +2.2% y-o-y, up from +1.7% in Q1, although it has been surprisingly volatile recently.

## Implications

New Zealand is currently enjoying a great ride. The economy is booming, with GDP well above trend and inflation remains well contained. On the Q1 print, GDP rose by +3.8% y-o-y with timely indicators suggesting that this pace probably continued into Q2. Adding further icing to the cake, today's CPI numbers suggested that booming growth is yet to show up in price pressures. The Q2 CPI print showed inflation running at a very comfortable +1.6% y-o-y, lower than the market expected, and in the lower half of the RBNZ's target band.

In response to the booming economy, the RBNZ has been forward-looking in its approach and has already lifted its cash rate by 75bp this year, the first central bank in the developed world to do so. And it appears to be working. The previously overheating housing market has eased back a bit in the past couple of months. Survey indicators of business conditions, which had travelled at levels suggesting GDP growth of 4-5%, have stepped back in recent months, although they still remain in economic boom territory.

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The RBNZ would be pleasantly surprised by today's CPI result. Low inflation and strong growth are what central bankers dream about. The composition of the CPI print is also reassuring. Domestically produced, non-tradables, inflation eased back a bit, to +2.7% y-o-y, which is comforting, albeit somewhat surprising. Although tradables inflation is lifting, it is still modest and the NZD remains very high, so the downward pressure on imported prices will probably continue for a bit longer yet.

But being ever-cautious, the RBNZ has already been sending strong signals in its public statements that it is determined to stay ahead of any possible inflation break-out. And by any standard, timely indicators suggest that the New Zealand economy is still booming. With this previous forward-guidance from the RBNZ in mind, we suspect they will err on the side of caution and lift the cash rate by a further +25bps to 3.50% next week. That said, with inflation contained and an election due in September, we then expect them to be on hold for at least a few months.

# Disclosure appendix

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