

Research Economy Watch

14 November 2023

Downside Risk To Q4 CPI Forecast

- **New monthly price series released**
- **We see downside risk to our Q4 CPI forecast**
- **Annual inflation may fall further below RBNZ view**
- **Supporting our view that the RBNZ is on hold**

Today's selected price indexes from Stats NZ – including some new indicators – point to downside risk to our Q4 CPI forecast which sits at 0.7% q/q and 4.9% y/y.

To start with, food prices fell 0.9% in October, which was a bit more than the small drop we had pencilled in for the month. Importantly, the undershoot to our priors was not in volatile fruit and vegetable prices (that didn't fall as much as we thought they might), but rather spread across the other categories. This suggests October's downside surprise might not unwind over coming months (relative to our forecasts for November and December). If so, this, alone, would lower Q4 CPI by 0.1ppt relative to our current view.

Rents rose 0.4% m/m in October. This matched our priors and thus does not change our thinking for this component for Q4 CPI.

Then there were the new series released today. These implied downside risk to our forecasts for the relevant components for Q4 CPI.

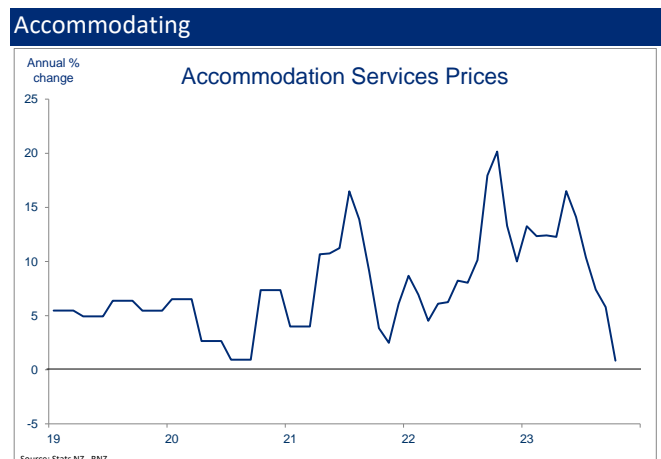
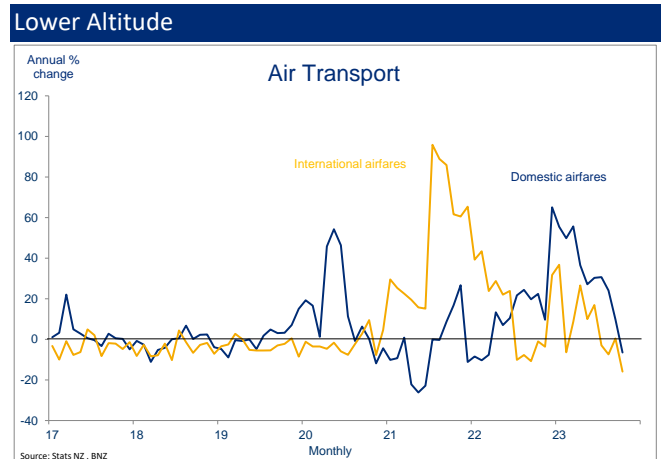
For example, the potential price drop we have long talked about in airfares looks to be coming through with October's figures suggesting a bit more of a drop than we have pencilled in for Q4 overall. Domestic airfares were down 9.4% m/m in October and international airfares fell 7.5% m/m. These prices are down 6.5% and 15.8% on a year ago respectively. Combined, and assuming some bounce through November and December, could see airfares reduce our current Q4 CPI forecast by around 0.2ppt.

Accommodation prices were up a mere 0.8% y/y in October, also suggesting some downside risk to our current Q4 estimates.

Bucking the trend was alcohol and tobacco prices. Combined these rose 1.3% m/m, to be up 8.3% y/y which is tracking ahead of what we currently have built in for Q4. This was driven by the cigarettes and tobacco section. It is unusual for price gains in this component at this time of year. Larger price changes usually occur at the start of the year, often coinciding with changes in excise tax. On its

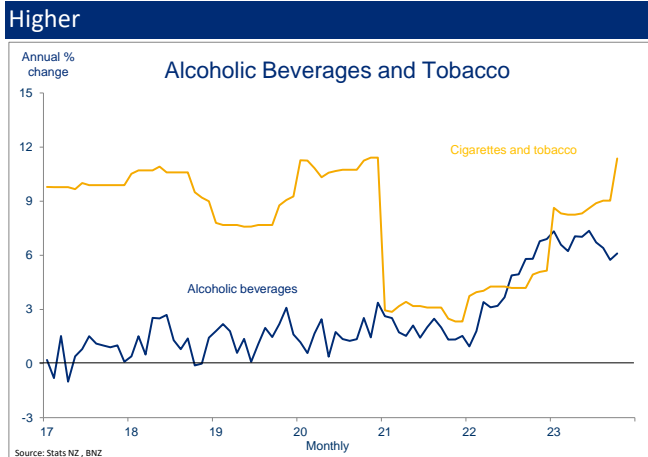
own, if it is sustained, it would add around 0.1ppt to our Q4 CPI estimate.

Monthly petrol and diesel price indexes were also released as part of today's data. At face value, they looked a little stronger than we have factored in. However, in contrast to all the other monthly series released today, the petrol data will be adjusted (by discounts) before entering the quarterly CPI.



Bringing it altogether, today's data suggest downside risk to our current Q4 CPI view in the order of 0.2 to 0.3ppts.

Of course, whether that is what transpires will depend on what happens to these various prices in November and December, as well as other CPI component prices not covered in today's selected prices monthly release.



It will take time to fully assess the new series for such things as typical seasonality, especially post Covid, across the various component detail. In any case, we are wary of drawing firm conclusions from monthly data (and even

more so from new data series). But we think it is worth highlighting the current risk around our Q4 CPI estimate.

We are not revising down our Q4 CPI pick today, pending further analysis, but it is fair to say it has been put on notice by today's augmented array of monthly price indexes.

We note that the RBNZ's prior (August MPS) CPI forecast had annual inflation at 5.2% in Q4. This was prior to Q3 CPI printing below the Bank's expectations. Today's monthly numbers suggest that annual CPI inflation in Q4 is at risk of pushing further below the Bank's prior forecasts.

All of this supports our view that the RBNZ is done with its hiking cycle. Of course, monetary policy is about much more than just the next quarter's CPI. But the potential starting point and near-term direction for inflation is important to consider. We will provide our full preview of the November MPS next week.

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