Research

Economy Watch

15 August 2025

Q3 inflation still lining up 3%

- **Monthly indicators point to higher inflation**
- **But no higher than we assumed**
- **We maintain our 0.9% q/q, 3.0% y/y Q3 CPI pick**
- **RBNZ still expected to cut OCR next week**
- **Higher priced essentials squeezing household incomes**

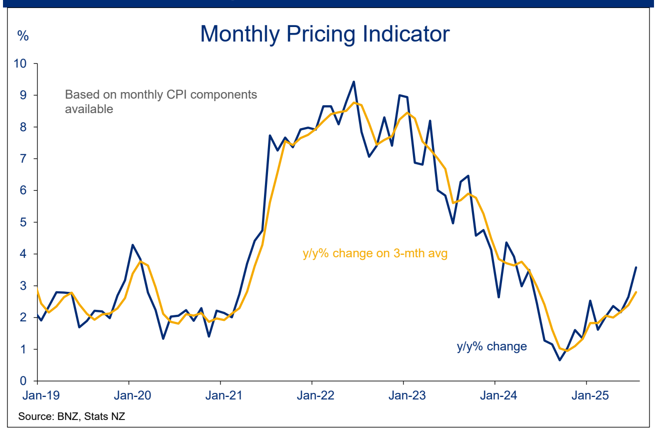
The main interest in today's July Selected Price Indexes was to see what they suggested for our thoughts on Q3 CPI and related influence on household disposable incomes.

On balance, the monthly indicators came in close to expectations so nothing to alter our view of the world. We have no reason to alter our Q3 CPI pick that remains at +0.9% q/q.

Of course, Q3 CPI inflation also depends on the remain 53%+ of the index not covered by the monthly prices.

Our Q3 CPI view remains a tick above the RBNZ's May MPS estimate of 0.8% q/q. However, the Bank already acknowledged in July that it expected higher near-term inflation (in Q2 and Q3) so we don't see anything here to prevent the OCR being lowered by 25 bps next week. But if higher inflation were to show signs of sticking around, it would be more problematic for the RBNZ. Policy is focused on medium term inflation.

Inflation indicator higher into Q3



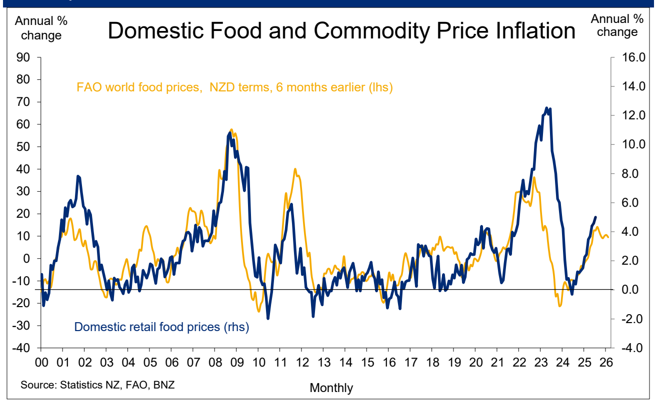
Many monthly components were close to our expectations, with a balance of unders and overs in some of the more volatile components like airfares.

Prices for many essential items continue to rise firmly. Food and energy prices are two important components in this category.

Food prices rose 0.7% m/m, to be up 5.0% on a year ago. While close to our priors, the annual change is still a significant rise in the single biggest component of households' budgets.

Many factors influence food prices. Two are the influences from offshore prices and movements in the NZD. Some recent easing in offshore food price inflation, as measured by the UN FAO food price index in NZ dollars, suggests some downward influence on domestic food price inflation from this source heading into 2026, given the usual lags.

Food prices rise 5%



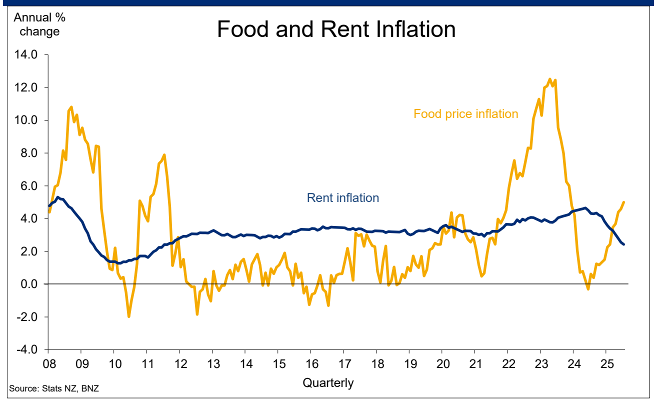
Electricity prices pushed another up another 1.0% m/m, taking its annual gain to around 11%. Gas prices are about 14% higher than a year ago. Both suggest household energy prices in Q3 will be a touch higher than we had factored in.

More of the household purse will be directed to groceries and energy. Higher prices are eroding purchasing power of incomes and inhibiting people's ability to spend on other things. This is a key reason why we remain cautious on the pace of pickup in real household spending ahead.

Fuel prices also rose in July, with petrol up 1.2% m/m and diesel up 2.3% m/m. However, indications are that prices have eased again in early August. And despite the push up in July, fuel prices remain below year earlier levels with petrol down 3.7% y/y and diesel 7.2%. These were close to our expectations.

Rent inflation was also close to our expectations and remains on a softening trend. The 0.1% m/m rent increase sees annual inflation slow to 2.4%. It was 4.3% a year ago. We think annual rent inflation will continue easing.

Different directions



Airfares were their usual volatile selves in July but less than expected domestic airfares and stronger than expected international airfares netted to about square compared to our priors.

Domestic accommodation prices were down 4.4% on a year ago, likely reflecting, in part, low occupancy rates in some areas. Conversely, overseas accommodation prepaid in NZ pushed another 2.0% higher in the month taking its annual inflation to 20.5% y/y. We remain perplexed as to why this component is included, but it is notable that this might well be the peak in its annual inflation rate with upcoming prior year monthly comparators looking difficult to match.

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