

### Consumers Price Index: September 2008 quarter

#### Key points

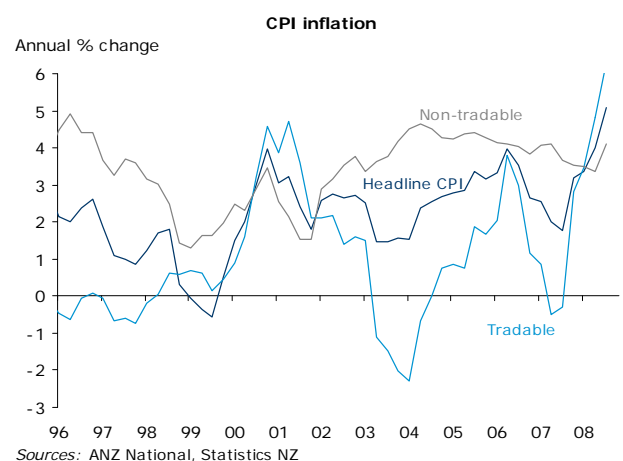
- > **Headline inflation hits 5.1 percent and underlying inflation still elevated. But a peak has been reached.**
- > **No clear sign yet that slowing domestic demand is curbing domestic inflation pressure, though we continue to expect the inflation outlook to improve.**
- > **Today's CPI data will not get in the way of an aggressive easing by the RBNZ this Thursday. But still lingering inflation pressure, if it continues to persist, may slow the pace of future easings.**

#### Assessment

The CPI rose by 1.5 percent in the September quarter, taking the annual headline rate to 5.1 percent. The increase was in line with market expectations, although stronger than ours and the RBNZ's forecast of 1.3 percent. It follows an increase of 1.6 percent in the June quarter and takes annual inflation to the highest rate since the June 1990 quarter. Food prices (up 3.7 percent) made the largest contribution to the quarterly increase (0.6ppts), followed by a 0.3ppt contribution from petrol. These increases are not at all surprising given the surges seen in global commodity prices. Wet weather conditions were also blamed for increases in fruit and vegetable prices over the quarter. Government related charges also helped push the CPI higher. Local authority rates rose 4.7 percent, vehicle licensing fees rose 16.1 percent and there was the usual annual alcohol tax adjustment. Statistics NZ also reported that a recent amendment to the Building Act (2004) (which came into force on 1 July), whereby buildings are required to be more energy efficient, may have played some part in the strong 1.3 percent increase in construction prices in the quarter. Together, central and local government charges rose 2.7 percent – the largest quarterly increase since September 2003.

**We were again surprised by a lack of retail discounting.** While some sectors showed signs of the discounting that we had expected, such as audio-visual equipment falling 5.3 percent, others did not. This was particularly the case for the household contents and services group. Household appliances rose 1.6 percent, glassware rose 1.8 percent and outdoor garden tools rose 1.2 percent. This leaves us a little puzzled given the anecdotes that we were hearing. Perhaps there is more price decreases to flow through into the December quarter.

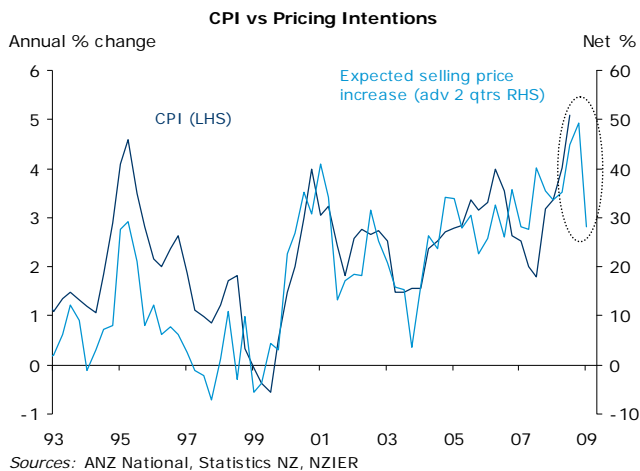
	Headline CPI		Tradable		Non-tradable	
	Qtrly % chg	Ann % chg	Qtrly % chg	Ann % chg	Qtrly % chg	Ann % chg
Jun-06	1.5	4.0	2.3	3.8	1.0	4.1
Sep-06	0.7	3.5	0.3	3.0	1.0	4.0
Dec-06	-0.2	2.6	-1.3	1.2	0.8	3.8
Mar-07	0.5	2.5	-0.4	0.9	1.2	4.1
Jun-07	1.0	2.0	0.9	-0.5	1.1	4.1
Sep-07	0.5	1.8	0.5	-0.3	0.6	3.7
Dec-07	1.2	3.2	1.8	2.8	0.7	3.5
Mar-08	0.7	3.4	0.2	3.4	1.1	3.5
Jun-08	1.6	4.0	2.3	4.8	0.9	3.4
<b>Sep-08</b>	<b>1.5</b>	<b>5.1</b>	<b>1.9</b>	<b>6.3</b>	<b>1.3</b>	<b>4.1</b>
<b>ANZ</b>	<b>1.3</b>	<b>4.9</b>	<b>1.4</b>	<b>5.8</b>	<b>1.2</b>	<b>4.0</b>
<b>RBNZ</b>	<b>1.3</b>	<b>4.9</b>	<b>1.6</b>	<b>5.9</b>	<b>1.1</b>	<b>3.9</b>
<b>Market</b>	<b>1.5</b>	<b>5.1</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>



**Underlying inflation remains elevated.** Non-tradable inflation rose by 1.3 percent in the quarter, taking the annual rate to 4.1 percent. The housing group again made a solid contribution here, but even excluding this, non-tradable ex housing still rose a robust 1.1 percent, indicating broad-based strength. After being reasonably subdued over the past few quarters, services prices rose 1.6 percent. Looking at other core measures, the trimmed mean rose 1.3 percent and the

weighted median rose 1.0 percent, both higher than the previous quarter's reading. Inflation, excluding food, fuel and energy rose 0.8 percent in the quarter and 2.1 percent for the year, up from 1.5 percent in the June quarter. Whatever core measure is looked at, the direction is the same. As yet, there are no clear signs that slowing (or contracting) domestic demand is curbing domestic inflation pressures. This could be due to the usual lags involved, or it could also be businesses "trying it on" given the margin pressures faced.

**Looking forward, the inflation outlook has improved.** Petrol prices have fallen 13c/ltr since last Friday, and if they remain unchanged for the rest of the quarter, will shave 0.7ppt of December quarter headline CPI. Recent business surveys have shown firms' pricing intentions have begun to fall and capacity pressures are also easing. The medium-term outlook for inflation has improved, given the global backdrop and also a sharp turn in the domestic economy and labour market. In this regard, we believe the September quarter marked the peak in annual inflation. However, domestic inflation pressure may yet prove to be sticky in the near-term, particularly given that there is a certain structural aspect to it (e.g. local authority rates and electricity charges etc).



## Implications

**While we do not view today's data as getting in the way of an aggressive easing by the RBNZ this Thursday, the Bank will remain wary over still strong underlying inflation pressure.** The medium-term inflation outlook may have improved, but the elevated core inflation readings will have disappointed the RBNZ. And while inflation is not the predominant policy concern at the moment, with offshore developments and a still very weak domestic economy taking precedence, persistent domestic inflation pressures may yet slow the pace of future easings.

CPI Components	Quarterly % change	%-point contrib.	Annual % change
Food	3.7	0.7	9.5
Alcohol and Tobacco	1.3	0.1	2.6
Clothing and Footwear	-0.4	0.0	-0.3
Housing and Household Utilities	1.4	0.3	4.7
Household Contents and Services	0.8	0.0	0.4
Health	1.4	0.1	3.2
Transport	2.0	0.3	11.3
Communication	-1.1	0.0	-1.2
Recreation and Culture	0.8	0.1	0.1
Education	0.1	0.0	3.7
Miscellaneous Goods and Services	0.5	0.0	2.2
<b>All Groups</b>	<b>1.5</b>	<b>1.6</b>	<b>5.1</b>
<b>Tradables</b>	<b>1.9</b>	<b>0.9</b>	<b>6.3</b>
<b>Non-tradables</b>	<b>1.3</b>	<b>0.7</b>	<b>4.1</b>
<b>Trimmed Mean</b>	<b>1.3</b>		<b>4.2</b>
<b>Weighted Median</b>	<b>1.0</b>		<b>3.7</b>

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The Bank (in respect of itself and its principal officers) makes the following investment broker disclosure to you pursuant to section 41G of the Securities Markets Act 1988.

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