

# Research Economy Watch

17 June 2025

## Annual CPI inflation to clear 3.0%?

- **Monthly price indices surprise to the upside**
- **And we see emerging upward pressure on oil prices**
- **This portends CPI inflation peaking at 3.1%**
- **Chance of RBNZ July pause rises further**
- **But, eventually, weak economy concerns should dominate**

May month selected price indices are unequivocally hawkish. On balance the monthly data has turned out to be more inflationary than we had expected. This has caused us to revise upwards our Q2 CPI pick to 0.8%, from 0.6% previously. Importantly, this is well above the RBNZ's 0.5% estimate for the quarter.

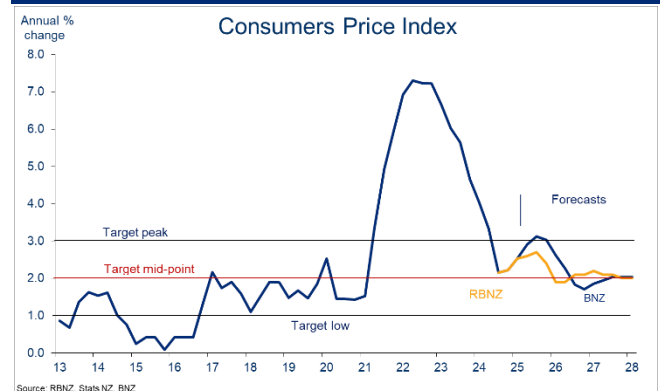
The main contributor to our shift was the reported 4.8% surge in the price of overseas accommodation prepaid in New Zealand. To be frank, it seems somewhat farcical to us that this category even exists in the New Zealand CPI. But it does.

The factors that bother us most were the jumps in the prices of fresh fruit and vegetables, meat and energy costs. Combined the upside surprise from these sources drove most of the rest of the change in our view. These price increases are most bothering because their impact on the real disposable incomes of households is largely unavoidable.

The increase in food prices reflects elevated global commodity prices. As commodity price inflation slows, or even reverses, this should become less of a problem going forward. But energy price increases are still coming thick and fast just in time for the coldest time of the year.

As if all this wasn't bad enough, the Israel-Iran war has resulted in a sharp reversal of recent oil price declines, and they threaten to head even higher yet. This is a completely different environment than that which saw the prices of petrol and diesel fall in the month of May. While domestic market players continue to suggest pump prices should not rise dramatically, unless freight traffic through the Strait of Hormuz is compromised, it still appears likely further cuts in petrol prices are now off the cards. We had further declines built into our inflation forecasts which have now been removed. Unfortunately, this means we have also nudged higher our quarterly CPI track for the second half of the year.

### Inflation trending higher

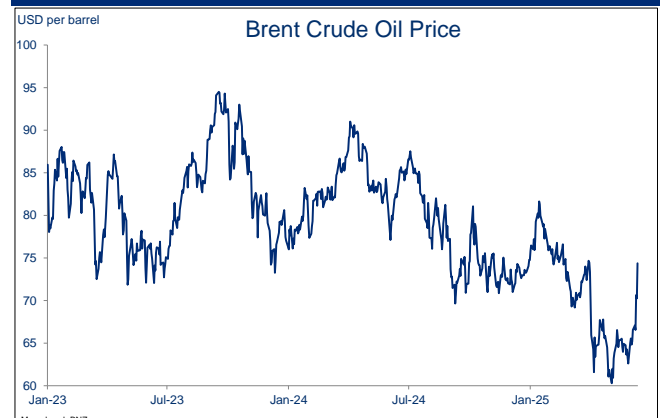


We had warned there was a risk that annual CPI would push through 3.0% sometime this year. We are now formally forecasting that to be the case. We now pick annual inflation to peak at 3.1% in Q3 2025.

That said, we still believe annual inflation will remain relatively well contained over the medium term and should get back towards the mid-point of the RBNZ's target band by Q3 2026. Indeed, we think slowing global demand, ongoing spare capacity in the New Zealand economy, slowing commodity price inflation and the potential reversal of any near-term oil price increases could well see inflation fall below 2.0% for a period of time.

But the current inflationary noise will intensify the RBNZ's headache. In the past the Bank has implied it would look through any short term uptick in prices especially if they were shock-driven.

### An unwelcome spike



But, equally, the Bank was clear, when it released its May Monetary Policy Statement that it was very nervous about rising inflation expectations. And recall that one member of the Committee was sufficiently nervous to vote against the rate cut that was delivered. That Committee member is going to feel no less unnerved this time around, and may well acquire a few friends.

So the chances of the RBNZ holding fast at the July meeting have just taken a leap forward in light of today's data and the evolving global environment.

We were very tempted to change our rate call on the basis of these factors. But we still want to see the July 1 QSBO before making that decision. There is a very real chance that business confidence drops sharply in this survey. If it portends much weaker growth ahead, or an outright end to the expansion, in the manner that the combined PMI and PSI did, then there may well remain solid justification for a July move. Either way we see little reason to change our view that the cash rate will ultimately drop below 3.0%.

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