NZ September quarter 2025 inflation review: Crunchy outside, soft core.

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NZ inflation: Crunchy outside, soft core.

- New Zealand consumer prices rose 1.0% in the September quarter. That saw the annual inflation rate rising to 3.0%, up from 2.7% in the year to June.
- The result was in line with our expectations (+1% qtr / +3.0%yr) and close to the RBNZ's August MPS forecast (+0.9%qtr / +3.0%yr).
- While the headline inflation rate has pushed higher, underlying inflation pressures are contained.

What was behind the September quarter rise in prices?

- The rise in inflation prices was mainly related to volatile categories, like food, or regulated prices like council rates.
- However, Inflation in parts of the economy that are more responsive to interest rates has been lower.
- The September quarter saw muted price rises in a range of discretionary spending areas like household durables, consistent with the continued softness in retail spending.
- There has also been particular softness in housing costs, with very muted gains in building costs and housing rents.

Core inflation

- Measures of core inflation have drifted back towards or inside the RBNZ's 1% to 3% target band in recent months.
- However, they are generally flattening off at levels above 2%, rather than at low levels.

NZ inflation: Crunchy outside, soft core (continued)

Non-tradables

- The domestically oriented non-tradables group rose 1.1% over the quarter. That saw annual non-tradables inflation slowing to 3.5%, down from 3.7% last quarter and the lowest level since 2021.
- Domestic inflation is still lingering above historic averages due to the continued large increases in administered prices, like council rates.
- However, excluding central and local government charges, the more market oriented components of non-tradables have been subdued, rising 2.6% over the past year. That reflects the softness in economic activity, and related muted growth in wages and service sector prices.

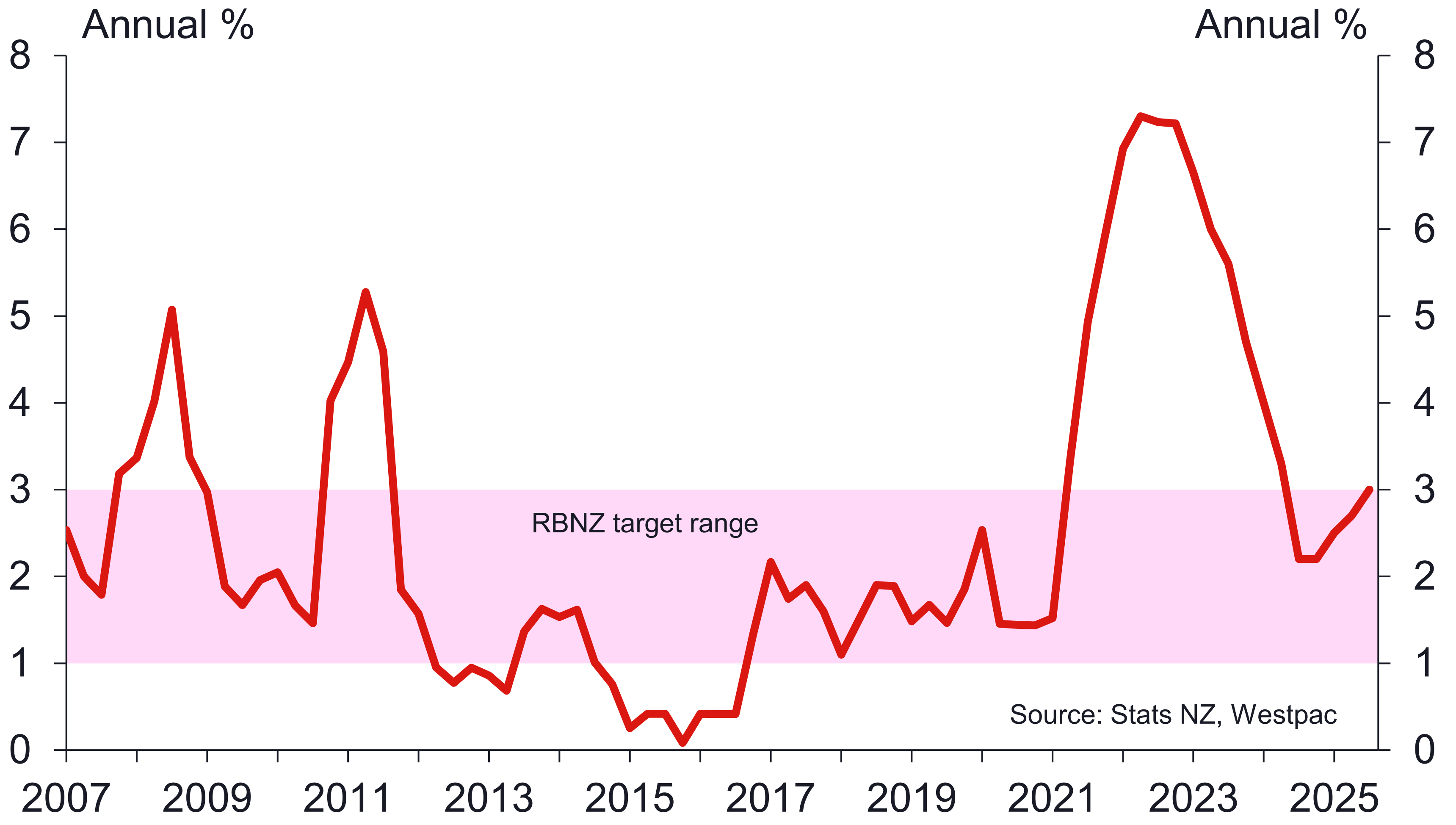
Tradables

- On the imported front, tradables prices rose by 0.8% for the September quarter. That saw annual tradables inflation rising to 2.2%.
- Tradables inflation is likely to drop back from its current highs as food price inflation eases. Even so, tradables inflation isn't likely to be as low as it was in recent years. That's important as it will limit the downside for overall inflation over 2026.

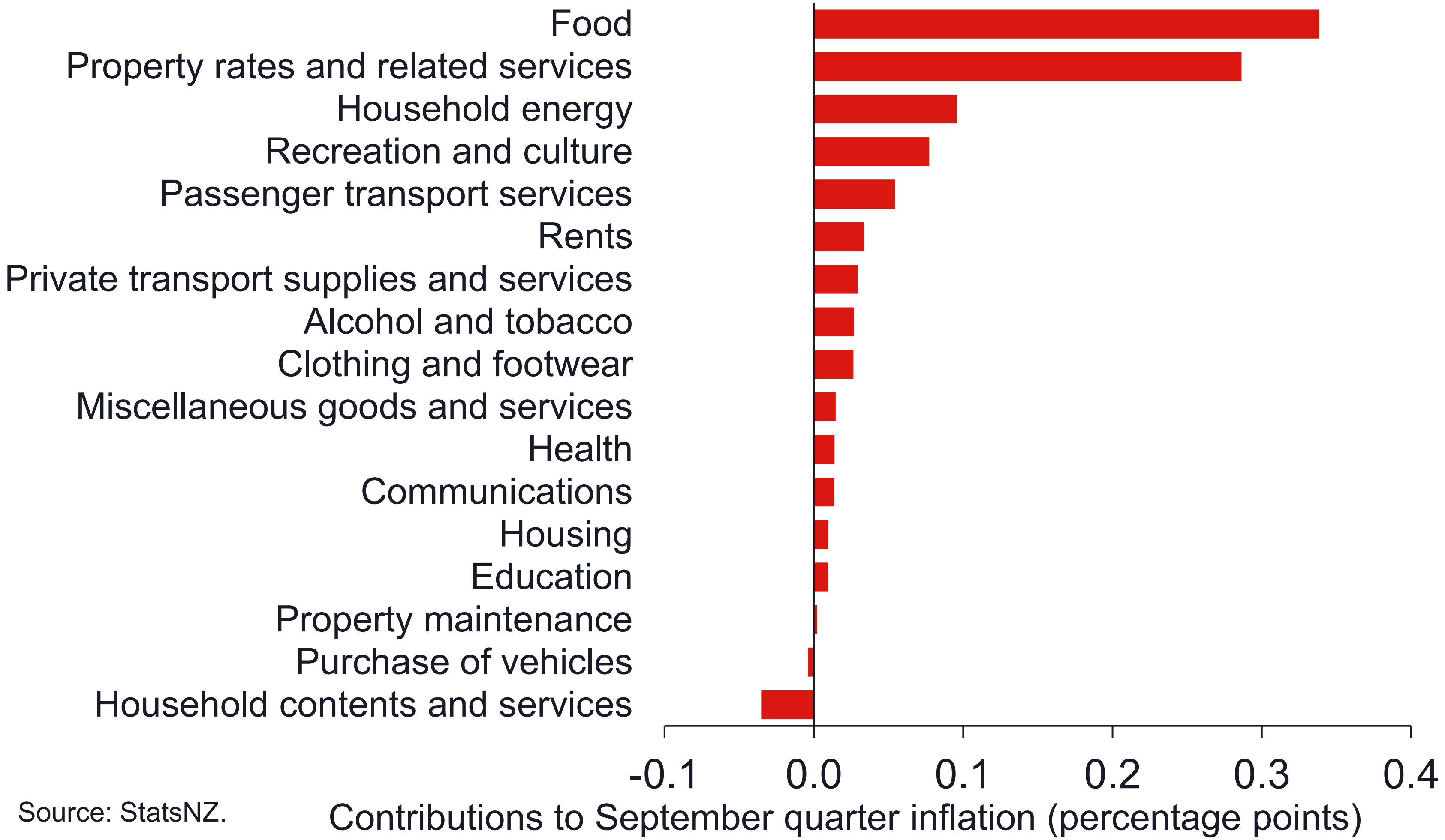
Takeouts for the RBNZ

- For the RBNZ, there was little in the September quarter prices update that would prompt it to change its projection for a moderation in inflation back inside the target band over the year ahead (the reasons we expect inflation will drop back are discussed later in this pack).
- Much of the recent rise in inflation is likely to be temporary (for example, food prices).
- At the same time, prices in discretionary spending areas or areas that are responsive to interest rates remains low.

Annual inflation lifted 3.0% in the September quarter, close to RBNZ and market forecasts.

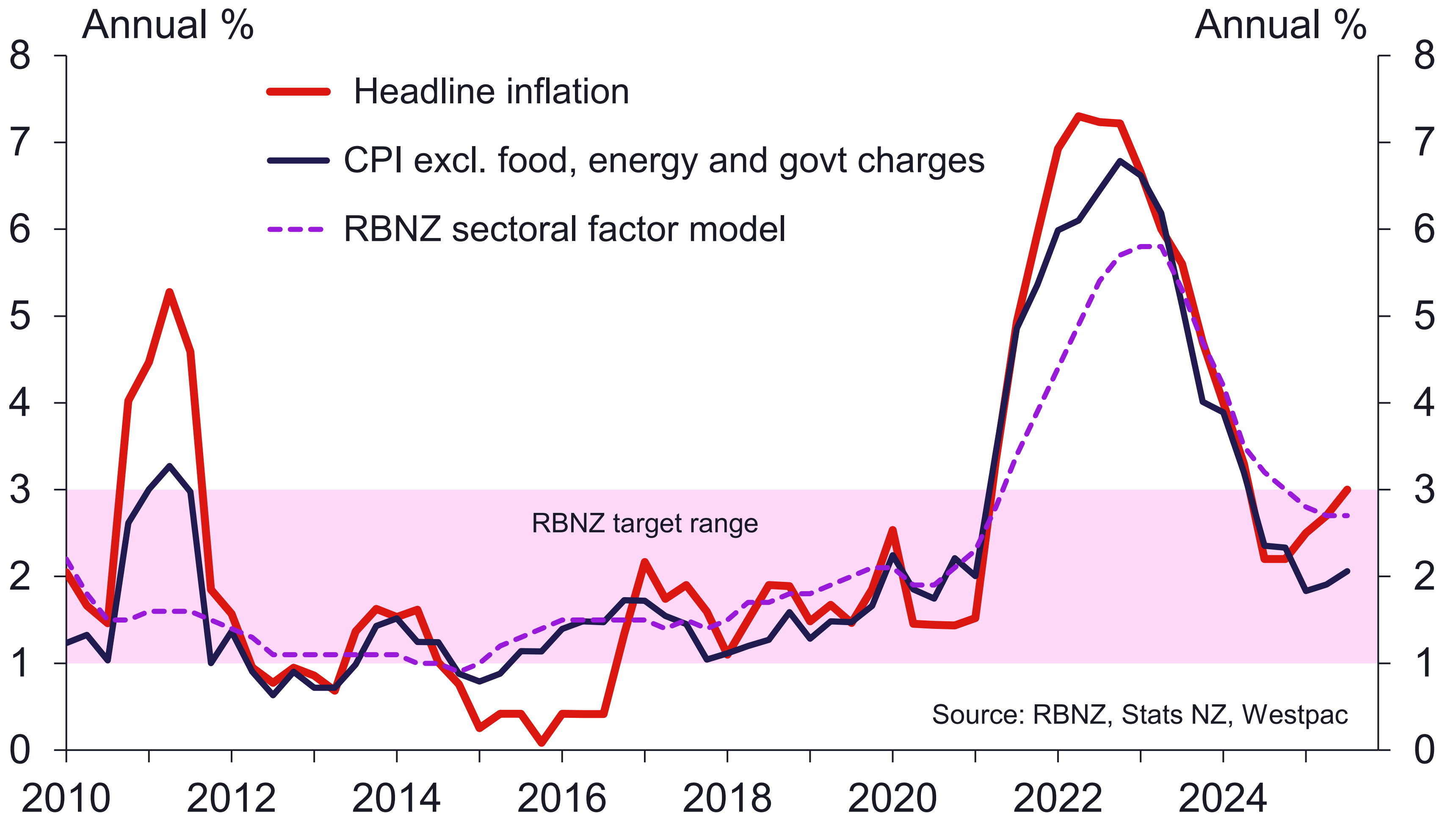


While food and local council rates have picked up, price pressures in other parts of the economy have been softer.



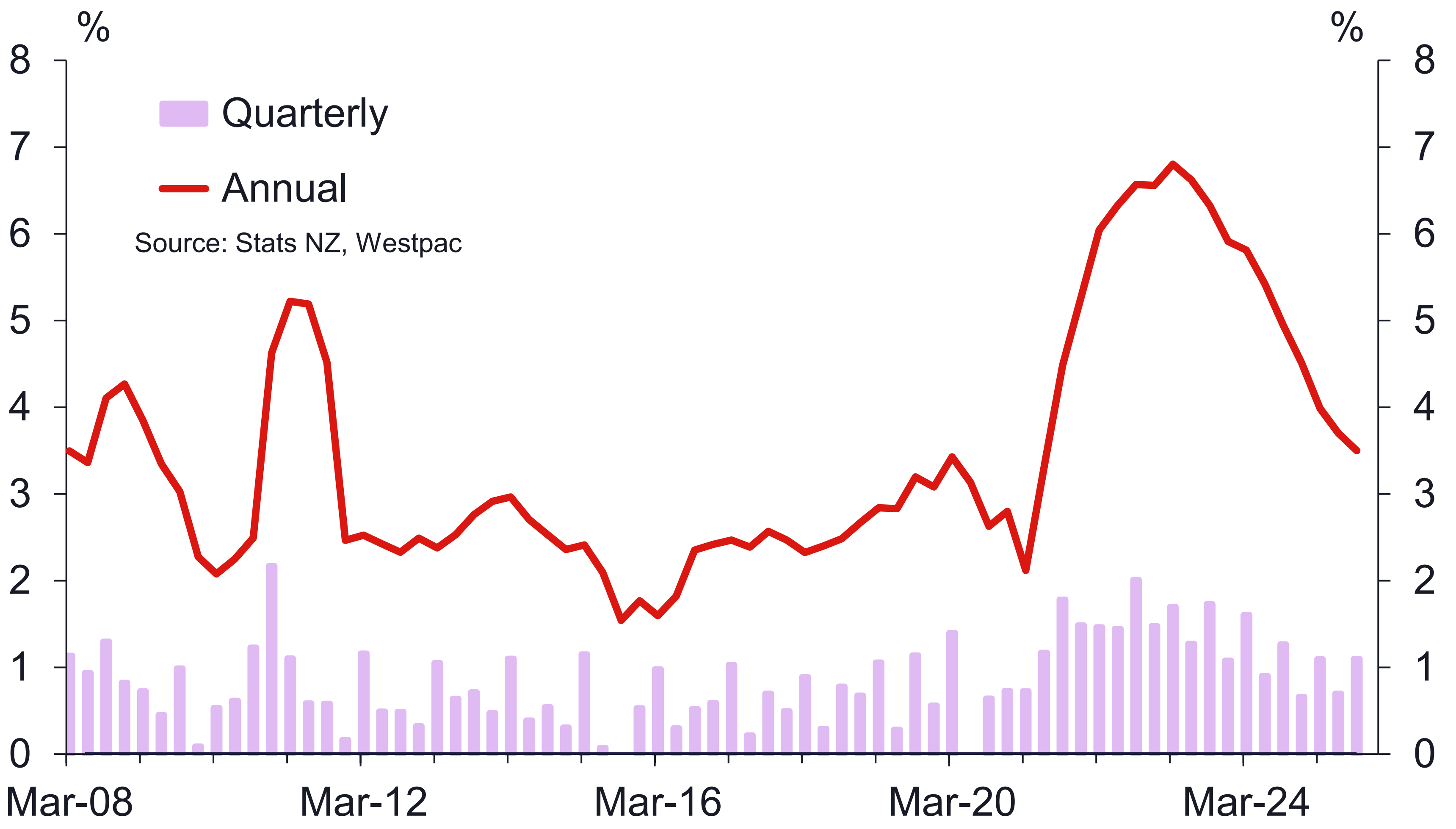
Source: StatsNZ.

Under the surface, core inflation has remained contained, but is lingering above 2%.

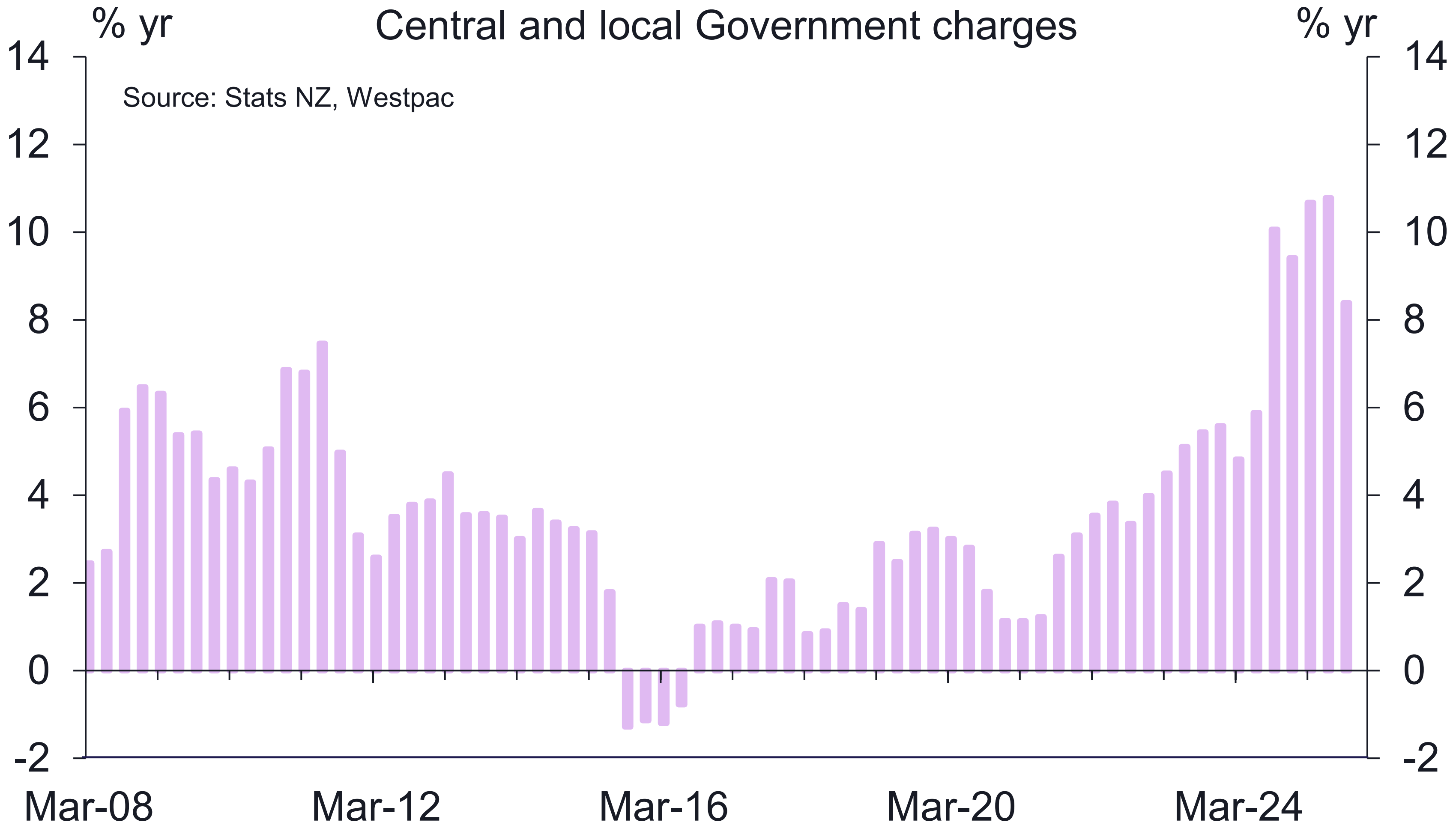


Non-tradables inflation

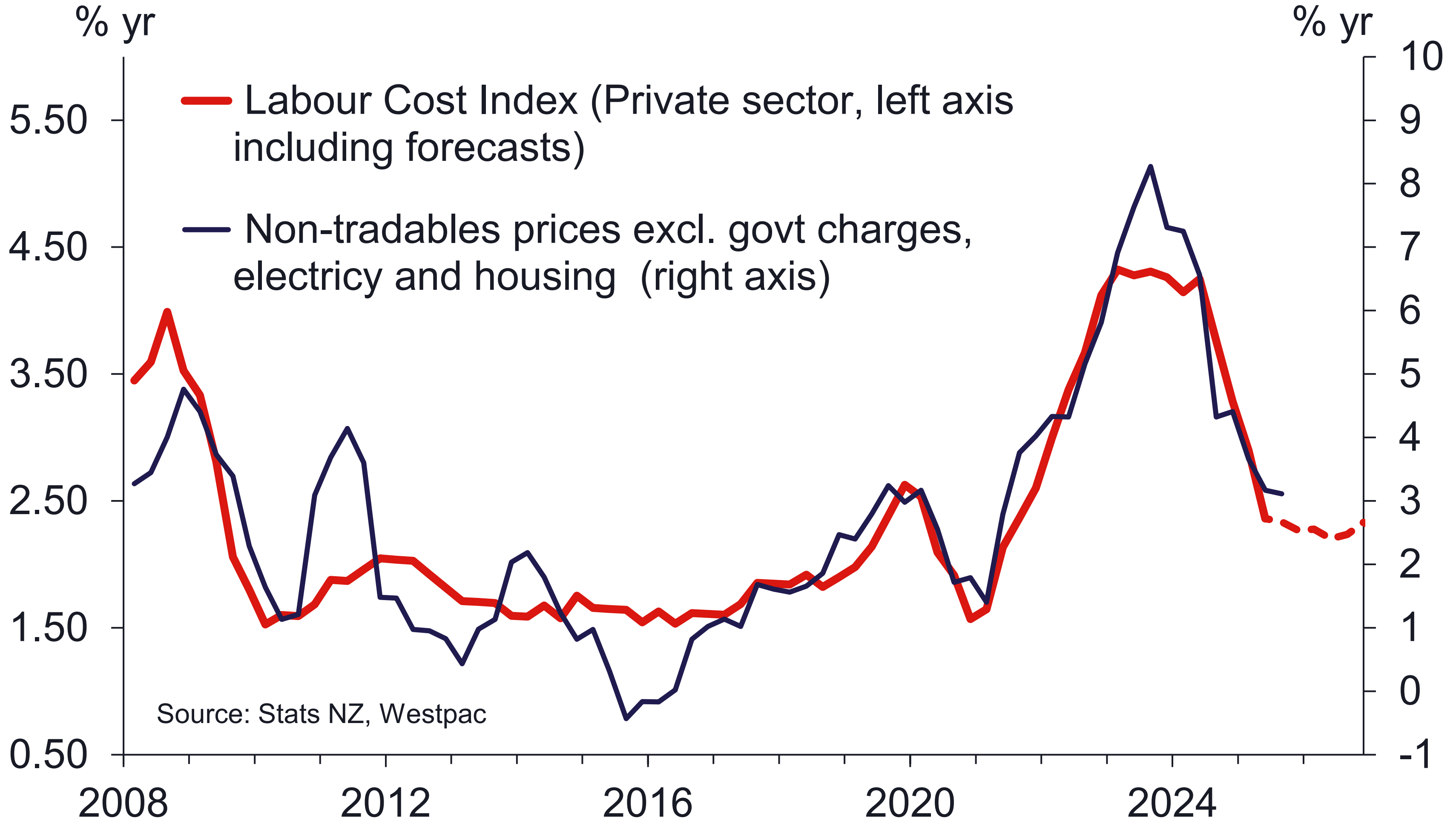
Domestic (non-tradables) inflation has cooled.



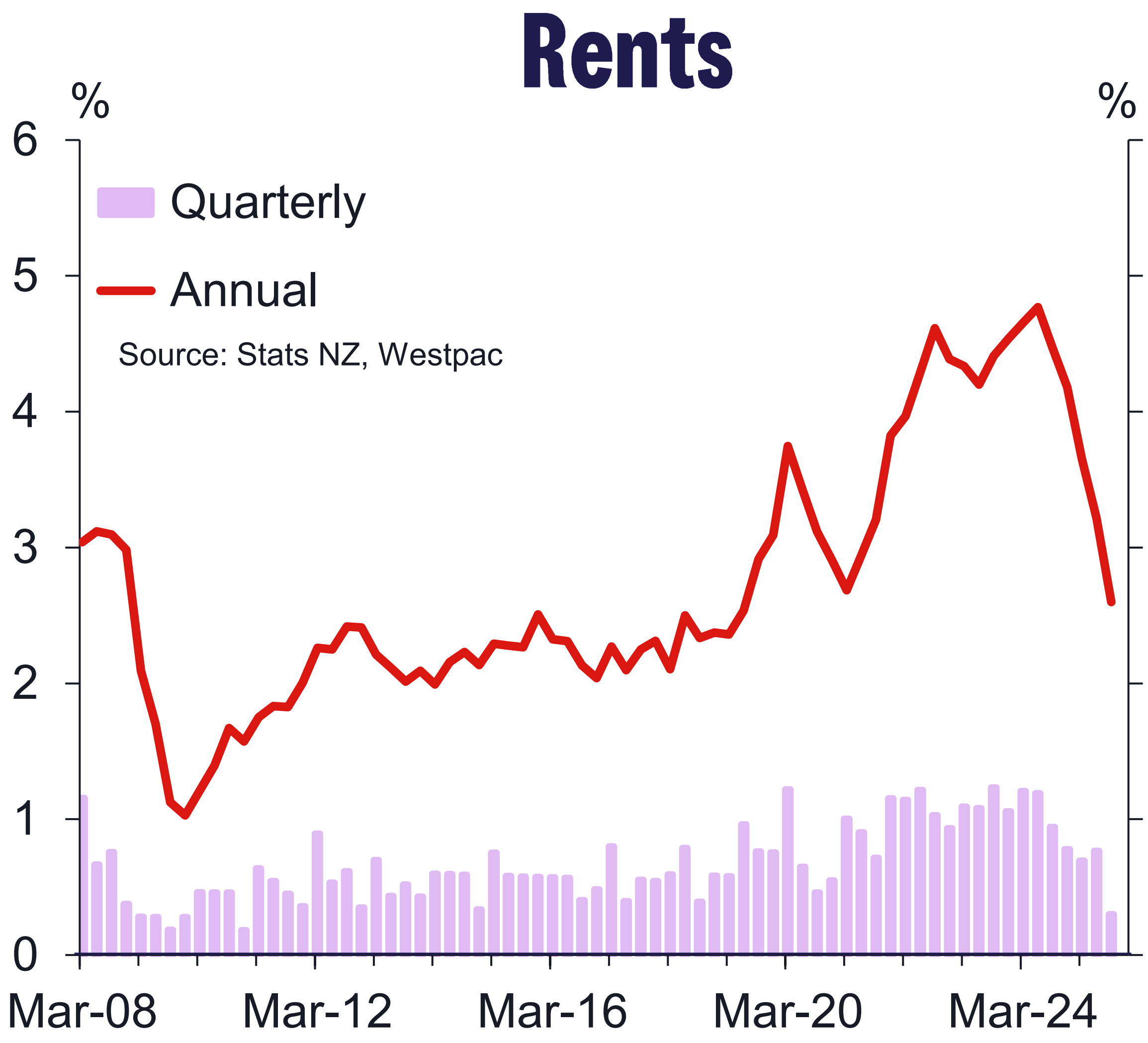
Large and ongoing increases in government charges are limiting the fall in total non-tradables...

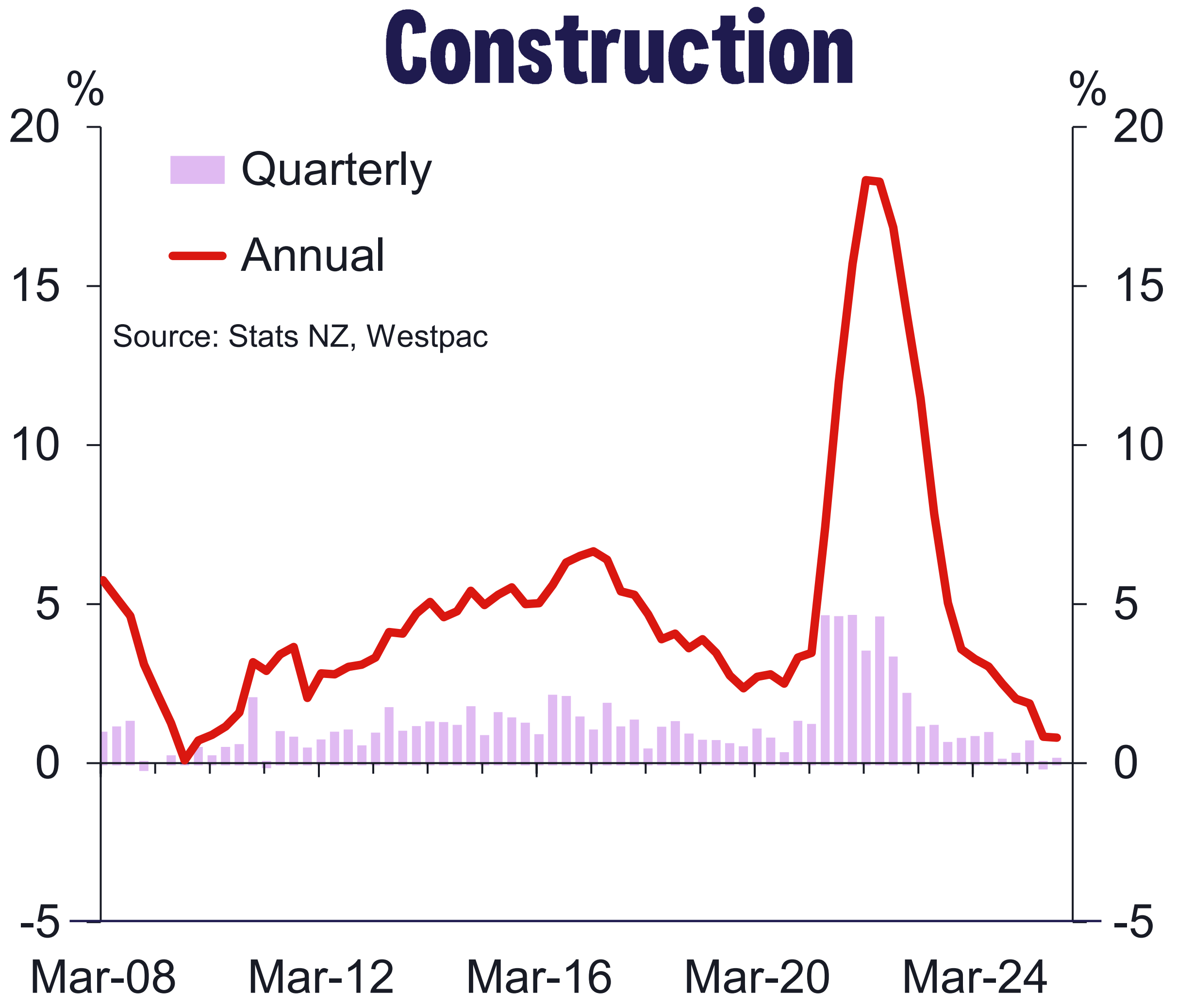


..but outside of government changes, domestic inflation has softened as activity and the labour market have cooled...



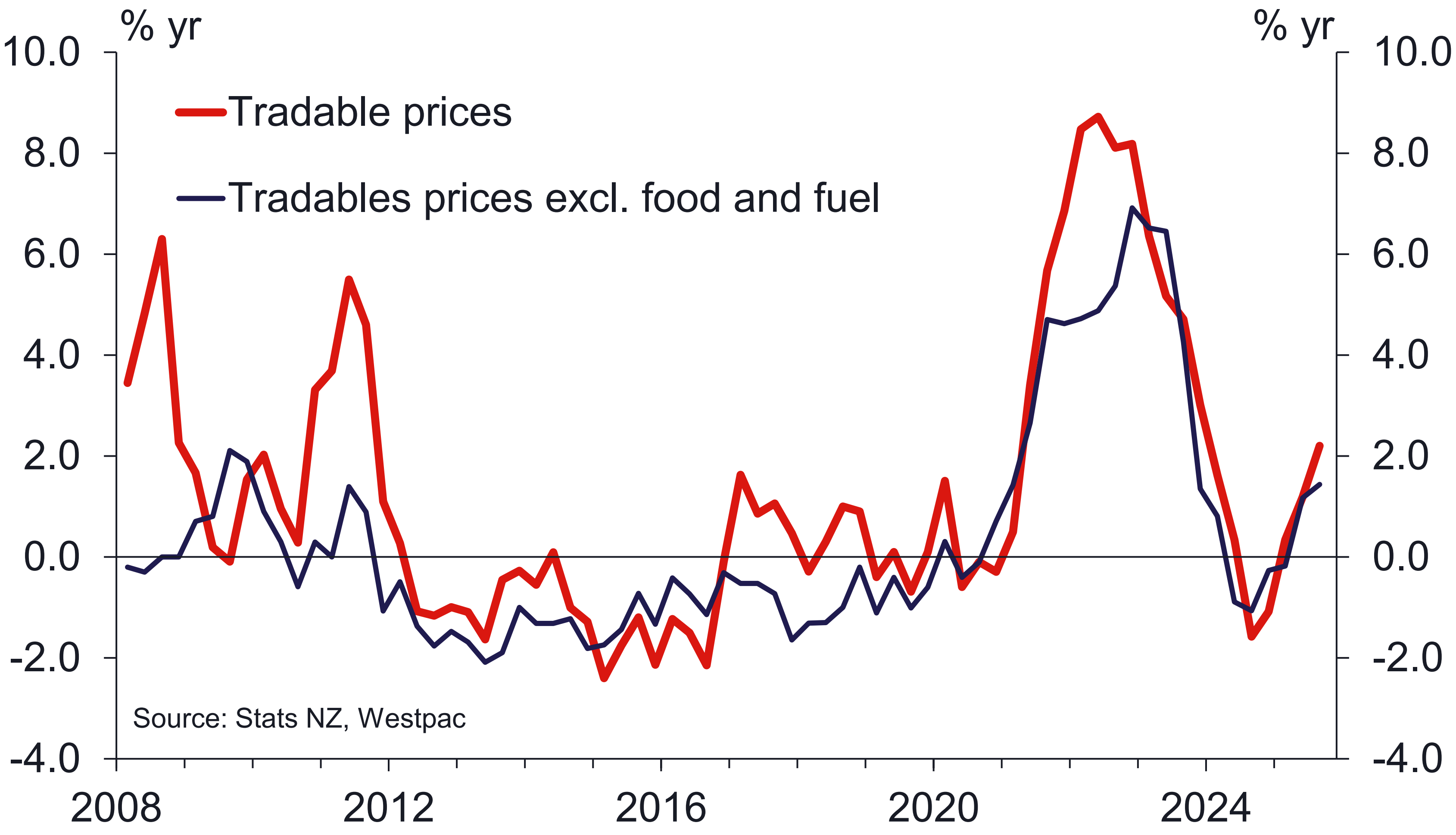
...with particularly softness in housing costs.



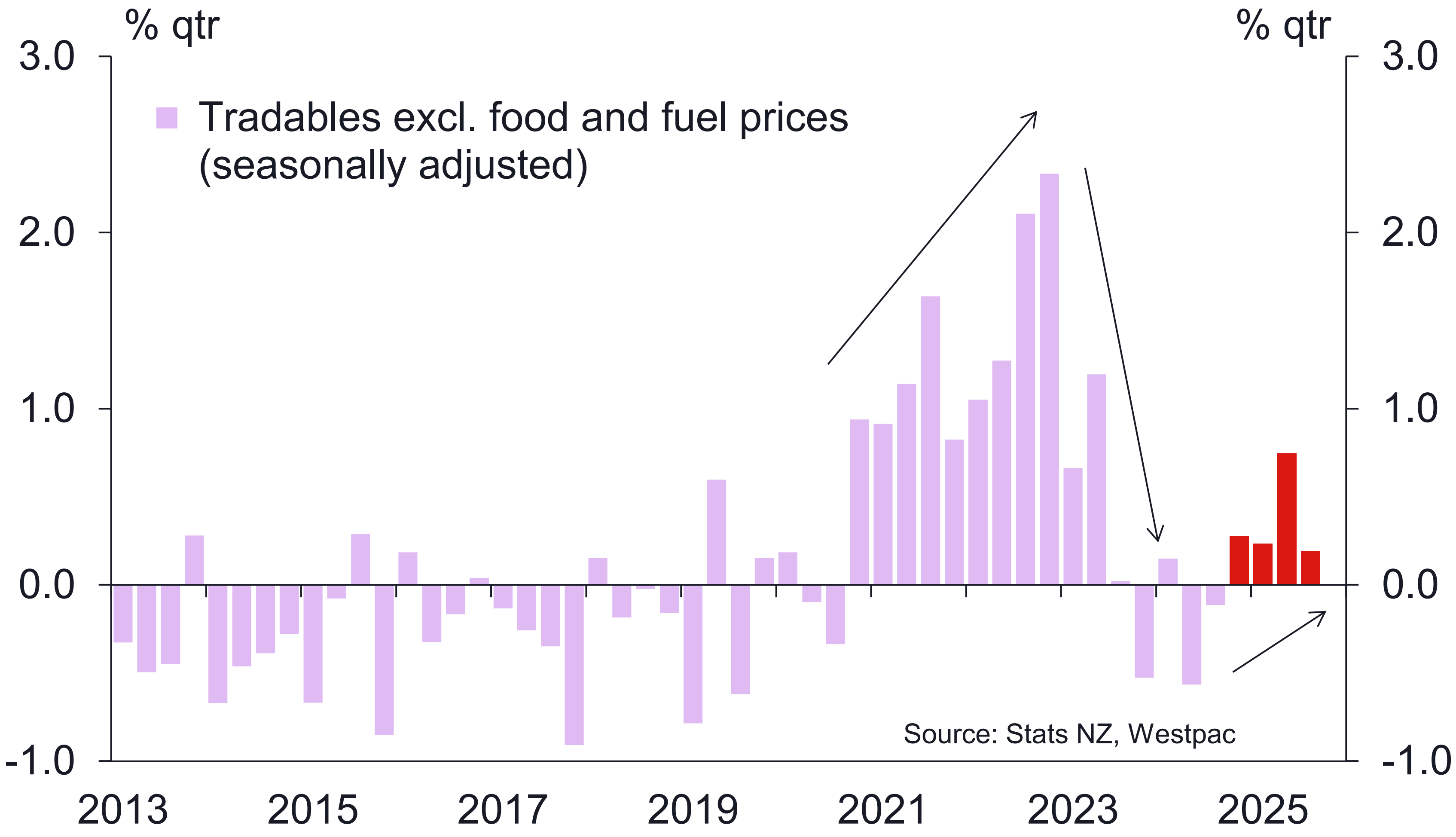


Tradables inflation

Food prices have pushed tradables higher, but the pick up in imported inflation has been more general.



We don’t expect high rates of tradables inflation, but equally it won’t have the dampening impact on inflation that it did last year.



Outlook and the RBNZ

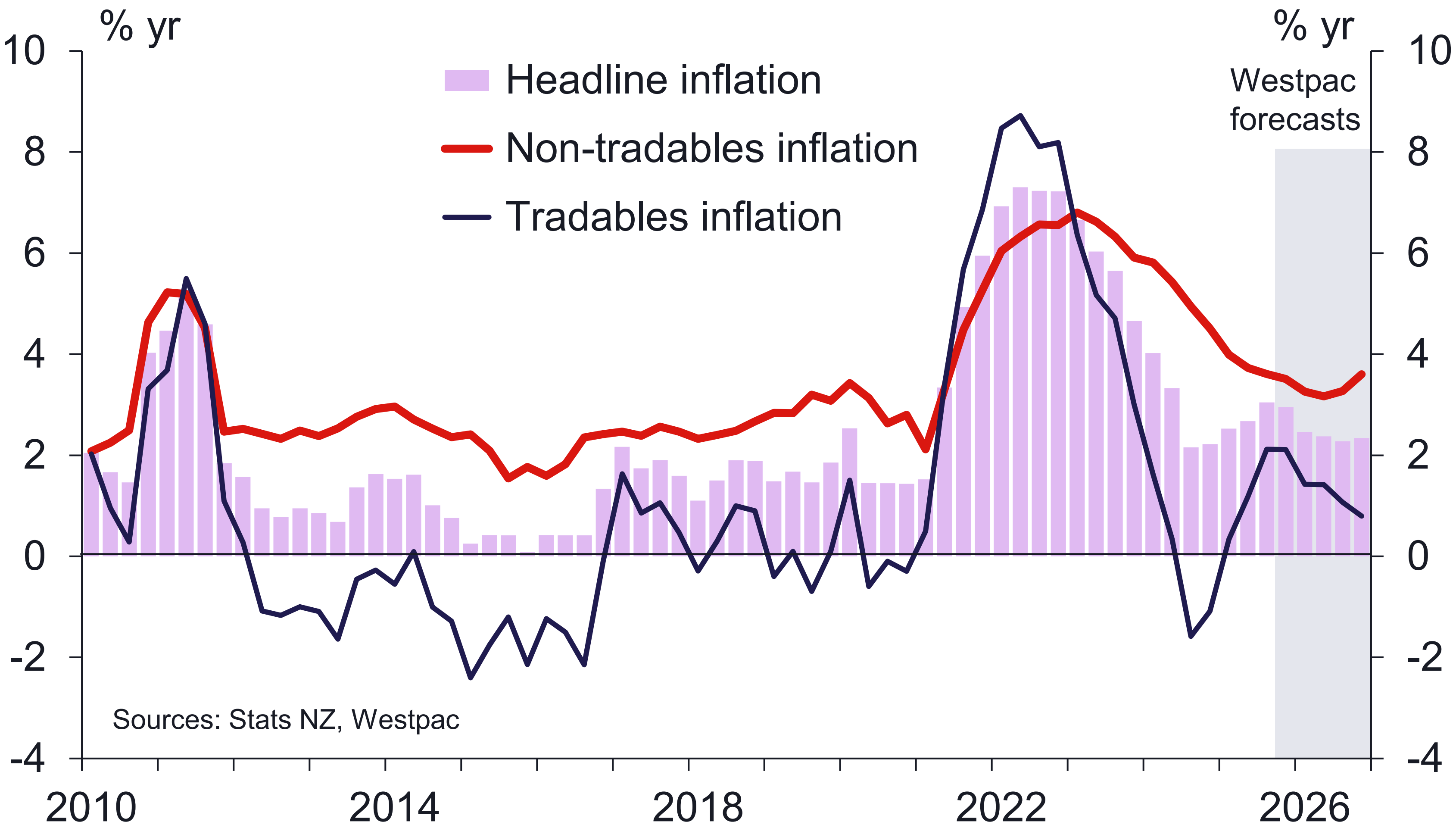
Why do we expect inflation to ease over 2026?

- The current rise in inflation is expected to be temporary. We expect inflation will return comfortably inside the RBNZ's target band next year.
- Much of the recent rise in inflation is due to higher food prices, with particularly large increases for items like milk and butter. While food prices are likely to continue rising, further increases are likely to be a lot more modest (for instance, we might see butter prices increase, but we're not likely to see another 30% rise as we did over the past year). In fact, over the past month we saw falls in a number of categories.
- There have also been some large increases in administered prices, most notably electricity. Again, while we'll get further price rises, they're likely to be more modest than those seen over the past couple of months.
- On the more cyclical components, the softness in rents and construction costs is notable. Neither of those groups will remain at their current lows forever, but a significant turnaround over the coming year looks doubtful.
- A recovery in home building is still someway off, with the pipeline of new projects flat and house price growth very muted. Those conditions aren't supportive of a large pickup in building or significant price rises over the coming year.
- In the case of rents, we might see some lift from the current very low levels, but there's been a big increase in supply at the same time as population growth has fallen. That's limiting the upside for rents over the year ahead.
- Looking at demand and prices more generally, as a nation we're continuing to operate with a sizeable amount of excess capacity, with related softness in retail spending.
- The pass through of interest rate reductions has been gradual to date. But large numbers of borrowers are now rolling on to lower mortgage rates, and that will boost disposable incomes over the next 6 to 12 months. Over time, that will also boost demand and inflation pressures, but that's a lift from subdued levels.

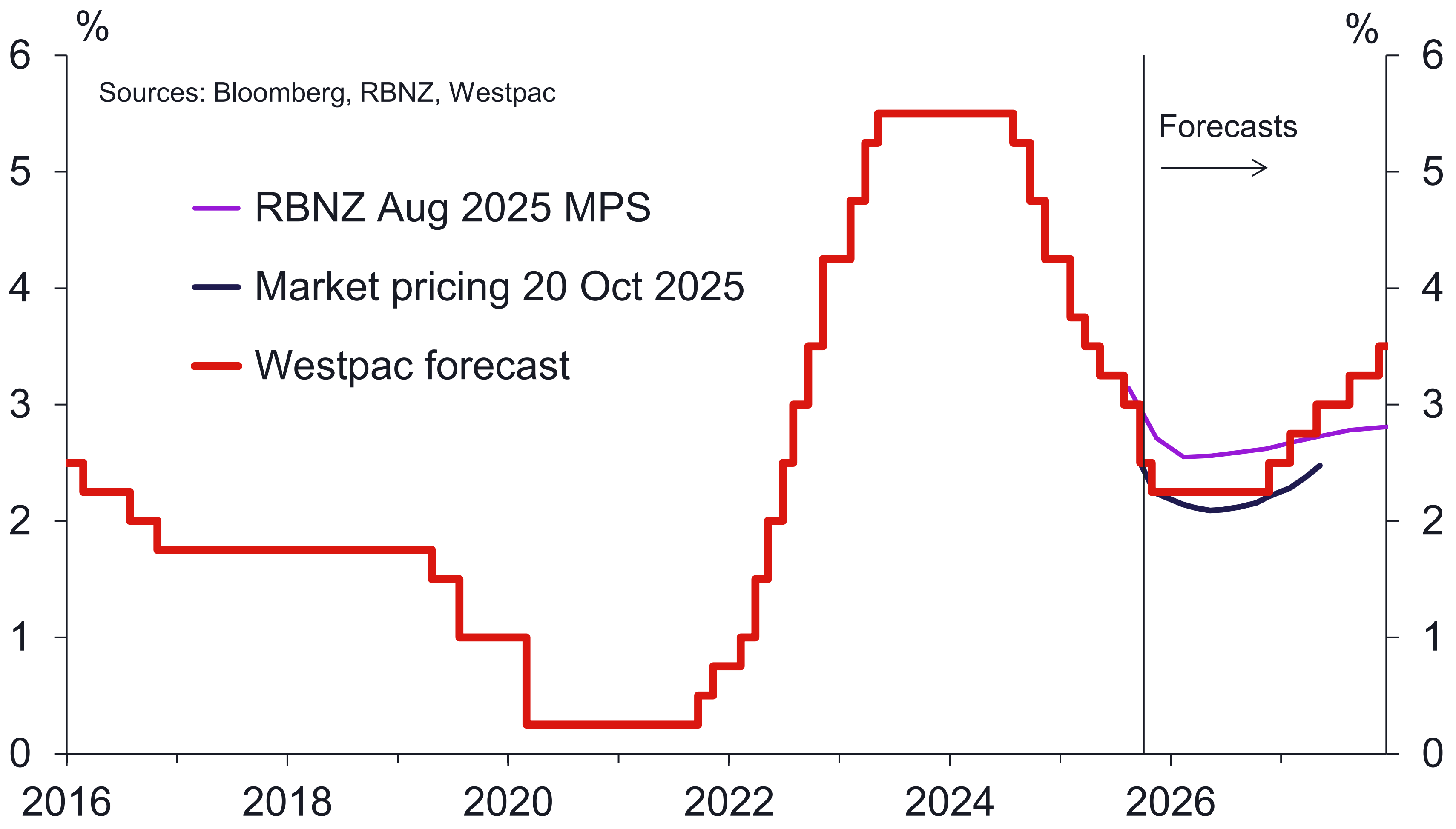
What next for the RBNZ?

- The RBNZ has been forecasting that inflation will return to more modest levels, and we think that there was nothing in the September quarter prices update that would have changed its mind.
- To the extent that the CPI confirms that we have seen the peak in inflation, it seems possible that even 3% inflation won't hold back further easing while the economy remains weak.
- We suspect the RBNZ will be tossing up between a final cut in 2025 of either 25 or 50 basis points.
- A risk the RBNZ will have in mind is that the rise in inflation close to 3% will lead to increasing inflation expectations. However, a lack of economic momentum, a still weak labour market and significant excess capacity are likely to be of greater importance. Businesses have noted pressures on operating costs, but soft demand means they haven't been able to pass that through to output prices. Similarly wage growth remains muted.
- We understand why markets are pricing some chance of a 50bp cut in November, and we assess the chance of a 50bp cut as lying in the 30-35% range.
- The next key event to watch ahead of the RBNZ's November policy meeting will be the September quarter labour market update on 5 November.

Inflation to ease back in 2026

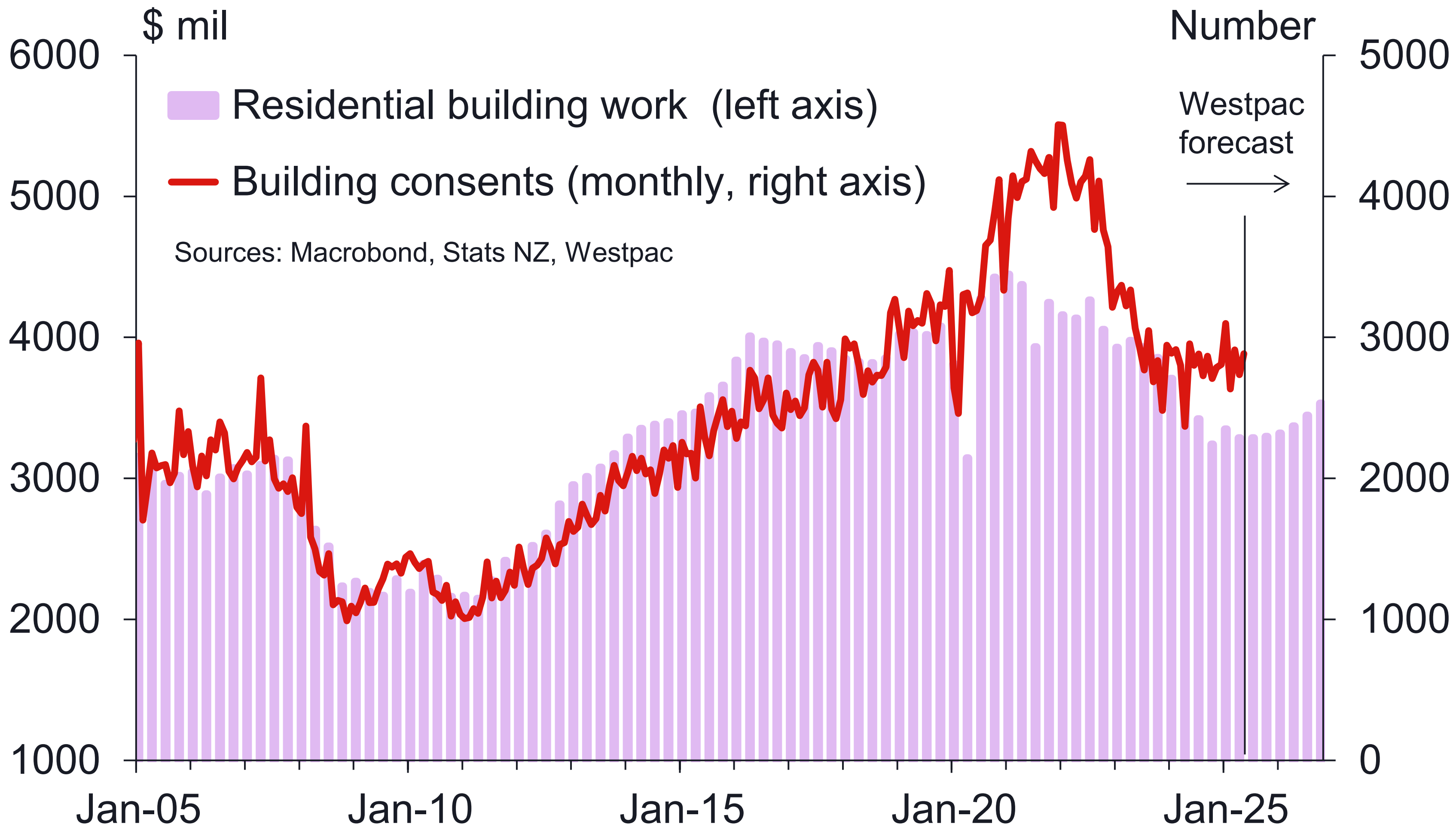


Official Cash Rate forecasts



The risk higher prices boost inflation expectations is a concern for the RBNZ, but soft demand means that firms are struggling to pass on price rises.

A near-term turn around in the housing market and home building looks unlikely, and that's keeping housing inflation low.



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