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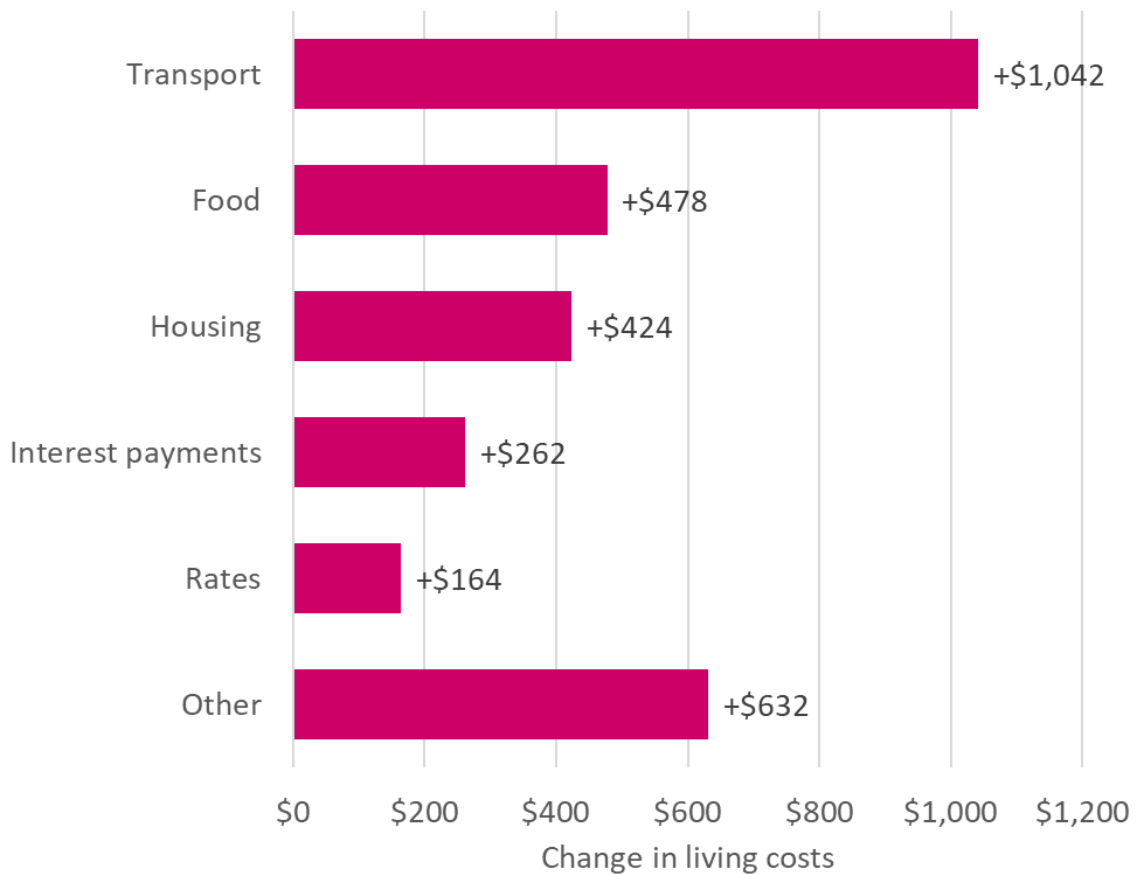
24 March 2022

Introduction

The cost of living has risen by more than \$3,000 for the average New Zealand household over the past year, led by prices of petrol, food, and rents (Figure 1). Analysis of the Household Living Costs Index from Statistics New Zealand shows:

- A third of the increase is due to higher transport costs, mainly due to higher prices at the petrol pump;
- Higher housing costs, mainly due to rents and local rates;
- Increased food prices, especially for fruit and vegetables; and
- Higher interest payments on borrowing.

Figure 1: Estimated increase in living costs year to December 2021

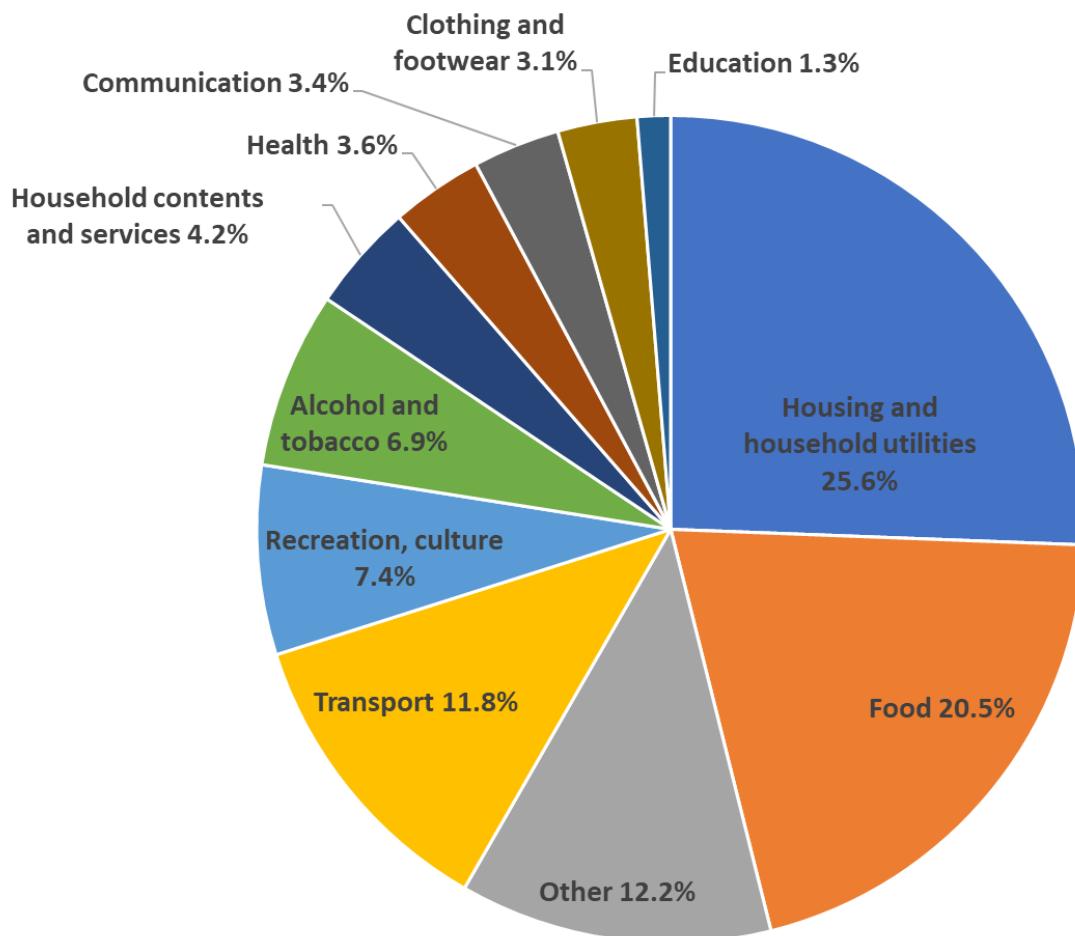


Source: Household Living Costs Price Index, Statistics New Zealand, December 2021 quarter

Behind these aggregated figures lies real hardship especially for those on lower incomes. Rents rose by nearly 10% in the year to September.¹ While the average household spends 12% of their income on rent, for beneficiaries that figure rises to 30%. Those who do not live in a state house – where income-related rents protected them – are likely to be especially affected by rent increases.

It is no surprise that housing and food are driving cost of living pressures. Nearly half of households’ spending is on those two categories (Figure 2). More surprising is that transport makes up only one-eighth of spending but is responsible for one third of cost pressures. This reflects unprecedented increases in petrol and diesel prices over the last 12 months, which we discuss below.

Figure 2: How we spend our money



Source: Statistics NZ Household Living Price Indexes, all households

Wages have not kept up with the rising cost of living. In the year to December 2021, salaries and wages increased 2.6% against general price inflation of 5.9%.² Nominal wage increases raise the effective tax rate by pushing households into higher tax brackets. This is known as bracket creep.

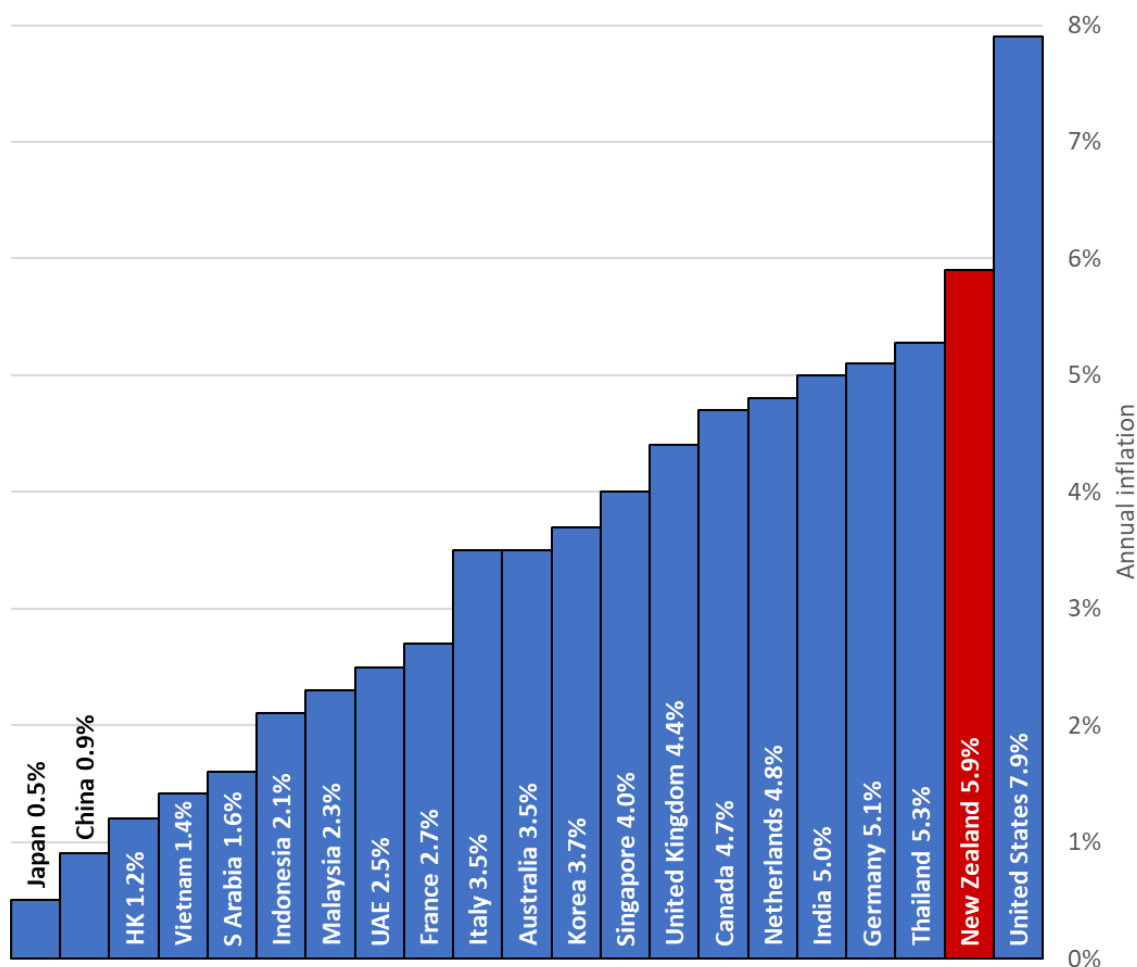
¹ Interest.co.nz (2021), “Average rents up by more than \$70 a week in September year in parts of Auckland, declining in parts of Wellington”, [link](#).

² Statistics New Zealand, “Labour Cost Index,” December 2021, Salary and wage rates.

Why are prices rising?

Prices are rising at the highest rate since 1990.³ This is due to the combination of real supply constraints and increased demand from fiscal and monetary stimulus. That is, too many dollars are chasing too few goods. Although New Zealand avoided the worst of COVID for the first 18 months of the pandemic, this country has the second highest inflation rate among our largest trading partners (Figure 3). While international factors have undoubtedly contributed to inflation around the world, our poor relative performance is arguably the product of domestic policy settings.

Figure 3: Annual CPI change New Zealand vs trading partners⁴



Source: stats.oecd.org

The government out-spent and out-borrowed nearly all other OECD countries in its response to COVID. The Reserve Bank began quantitative easing with its Large Scale Asset Purchases (LSAP) in March 2020. The programme ran until July 2021, long after it had become clear the worst fears of economic fallout from COVID would not be realised. The Reserve Bank will continue to subsidise bank lending via its Funding for Lending Programme until June 2022.⁵ Fiscal policy has also been lavish. Treasury states the government has spent \$74 billion on its COVID response

³ Source: Reserve Bank of New Zealand, M1 price series, [link](#). We emphasise that inflation is monetary and refers to general changes in prices, not relative price changes. As money enters the economy it will induce price changes. This is the Cantillon effect. Separating relative price changes and Cantillon effects is beyond the scope of this note.

⁴ Chart shows New Zealand's top 20 trading partners. Trade data from wits.worldbank.org. Chart displays most recent available monthly or quarterly data for each country as at 18 March 2022.

⁵ <https://www.rbnz.govt.nz/monetary-policy/monetary-policy-tools/funding-for-lending-programme>

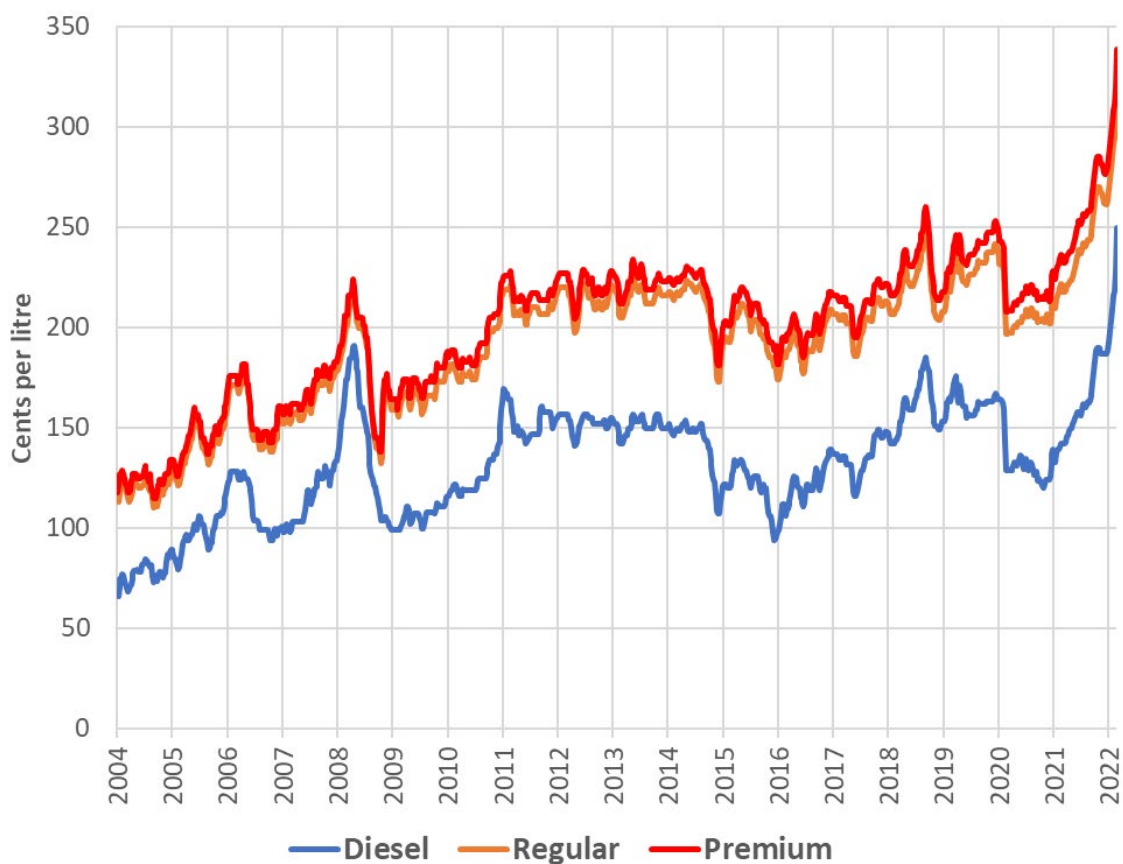
and recovery packages.⁶ The IMF forecasts New Zealand will borrow more through the pandemic relative to GDP than most if not all other OECD countries.⁷

Fuel prices⁸

Before the government reduced petrol excise by 25 cents per litre on 14 March,⁹ prices for diesel, regular and premium petrol all reached historic highs in the week of 11 March (Figure 4). That week saw the most significant 7-day increases in the prices of diesel, regular petrol and premium petrol since weekly tracking began in 2004: diesel rose by 20.9 cents per litre; 91 unleaded petrol by 18.1 cents per litre; and premium 95 unleaded petrol by 18.2 cents per litre.

Motorists are paying about a dollar more for a litre of petrol and diesel than this time last year, the largest one-year price increase since at least 2004. Of the twenty largest one-month increases in petrol prices since 2004, seven have been in the last year (Figure 5); two of those seven increases precede the Ukraine invasion. Diesel prices have doubled since December 2020.

Figure 4: Retail price per litre of diesel and petrol 2004-2022



Source: MBIE

⁶ Treasury (2022), "COVID-19 funding allocation and expenditure," [link](#).

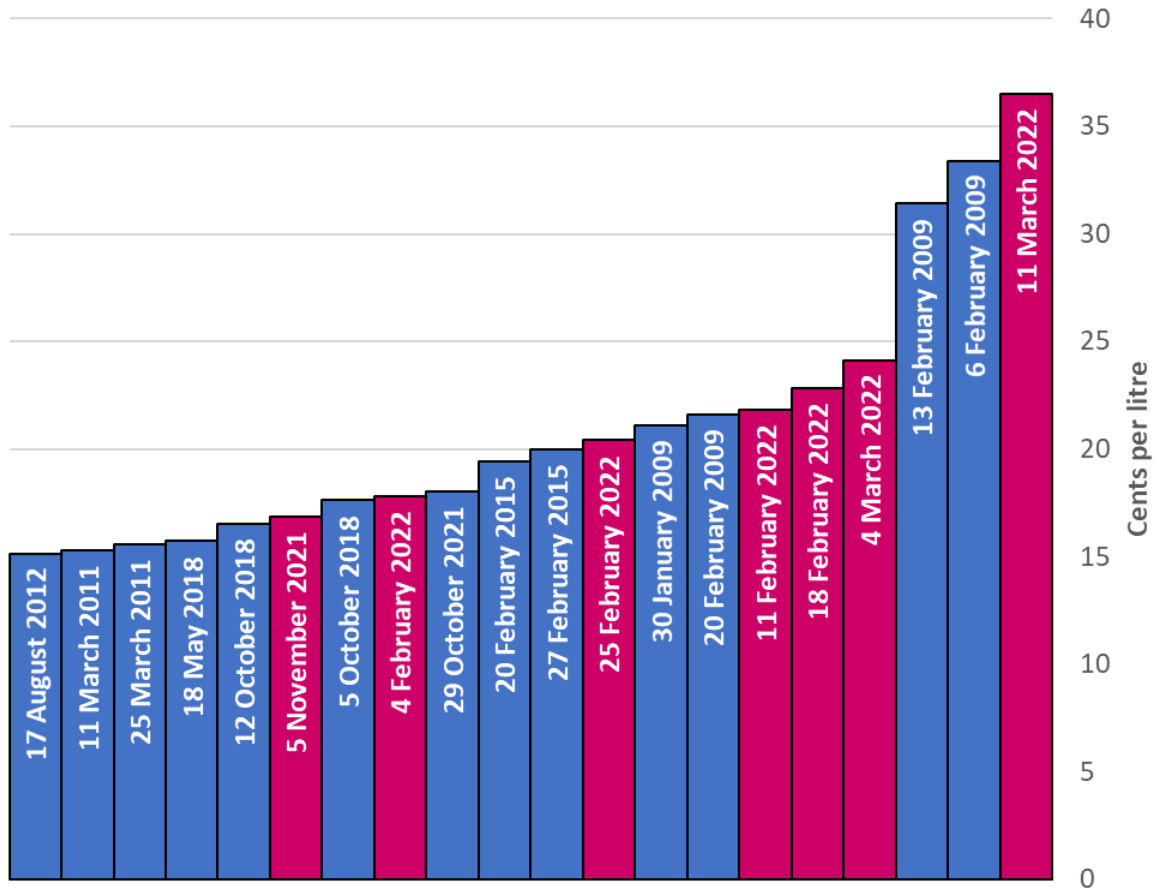
⁷ International Monetary Fund, "Fiscal Monitor, October 2021: Strengthening the Credibility of Public Finances," [link](#). IMF estimates New Zealand will have increased its gross debt by a higher percentage of GDP than any other OECD country by 2024.

⁸ Analysis in this section based on data from the Ministry of Business, Innovation and Employment (MBIE) weekly petrol price monitoring ([link](#)). We follow MBIE's naming conventions: Regular petrol refers to 91 octane petrol, Premium to 95 octane petrol.

⁹ <https://www.beehive.govt.nz/release/government-cuts-25c-litre-fuel-excise-cost-living-relief-package>

Before the government’s decision to temporarily reduce excise, petrol excise and levies added \$0.97 per litre of regular and premium petrol (excluding GST), a record high (Figure 6). Taxes comprise up to 55.6% of the cost of regular (91 unleaded) petrol.¹⁰

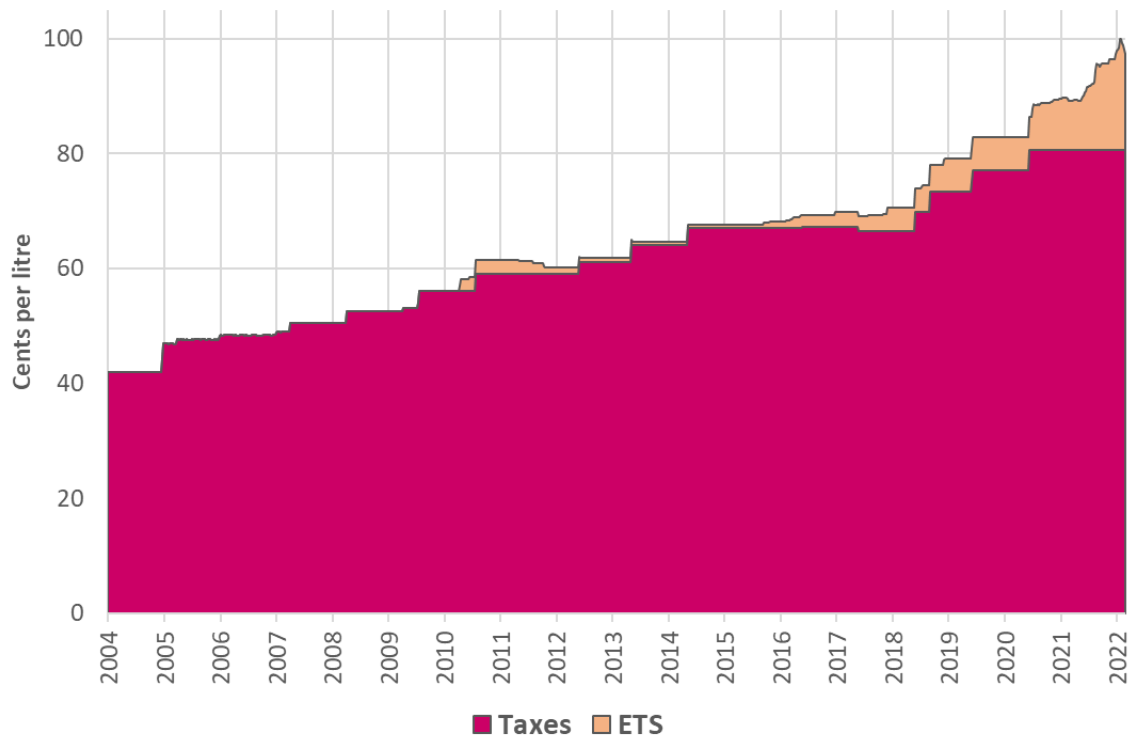
Figure 5: Highest one-month price changes for regular petrol 2004-2018 (red denotes within last 12 months)



Source: MBIE

¹⁰ Taxes include National Land Transport Fund, ACC Levy, Petroleum or Engine Fuel Monitoring Levy, Local Authorities Fuel Tax, and regional taxes on a weighted-average basis. GST is excluded. See [here](#). Taxes made up 55.6% of the price of regular petrol in the week of 25 December 2020. MBIE calculates taxes based on the discounted petrol price. See definitions [here](#). ETS refers to the Emissions Trading Scheme.

Figure 6: Taxes per litre of regular petrol 2004-2022



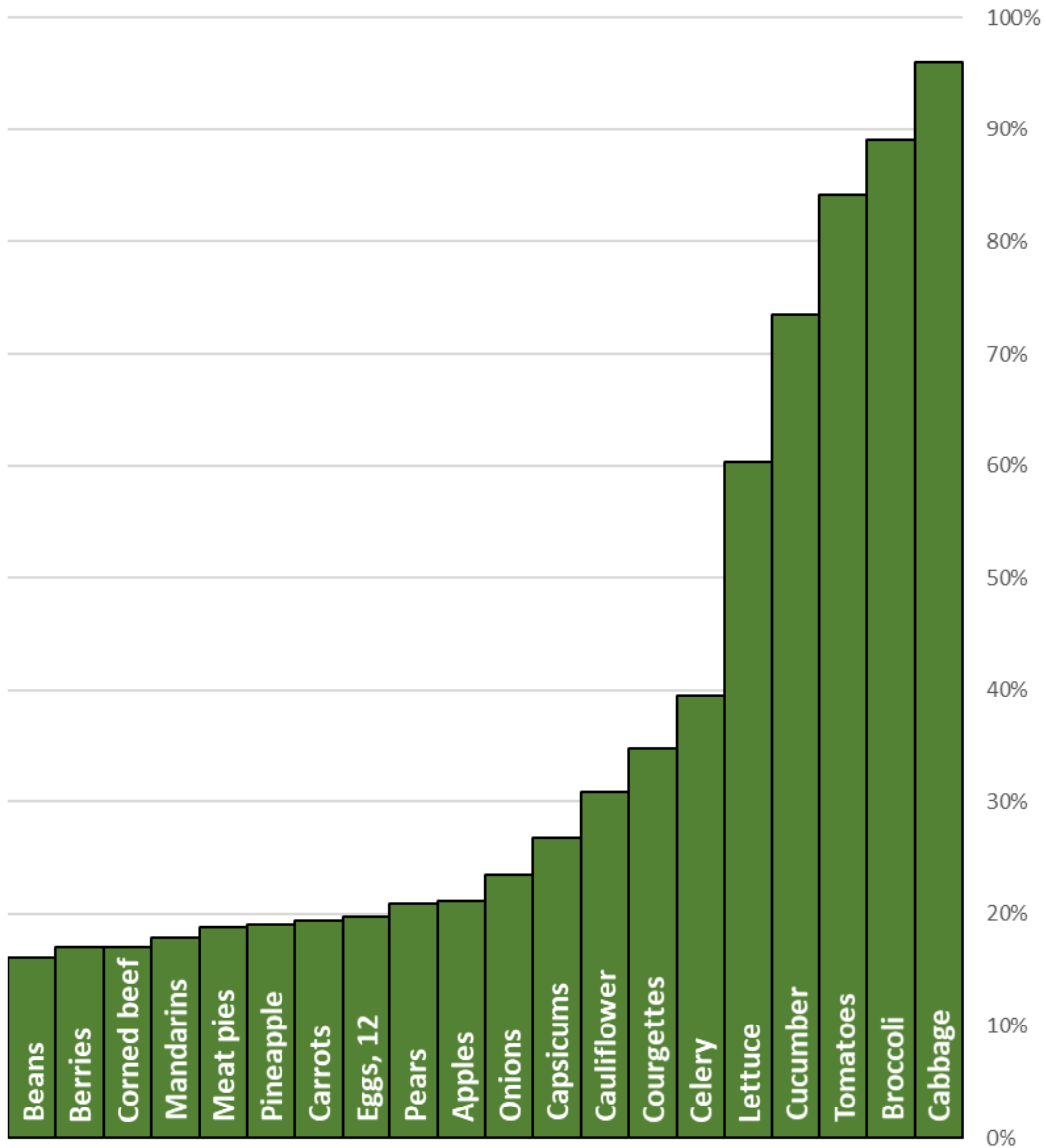
Source: MBIE

Food prices

Perhaps you have felt sticker shock during your visits to the grocery store over the past year. If so, there is a good reason. Food prices rose 6.8% in the year to February, led by a 17% increase in prices for fruit and vegetables. We spend about 21% of our incomes on food – more than any other category except housing, nearly twice as much as transport, and three times more than energy¹¹ – so rising food prices are a problem.

¹¹ Statistics New Zealand, Household living costs, <https://www.stats.govt.nz/information-releases/household-living-costs-price-indexes-december-2021-quarter>

Figure 7: Annual food price increases to Feb 2022 – Top 20¹²



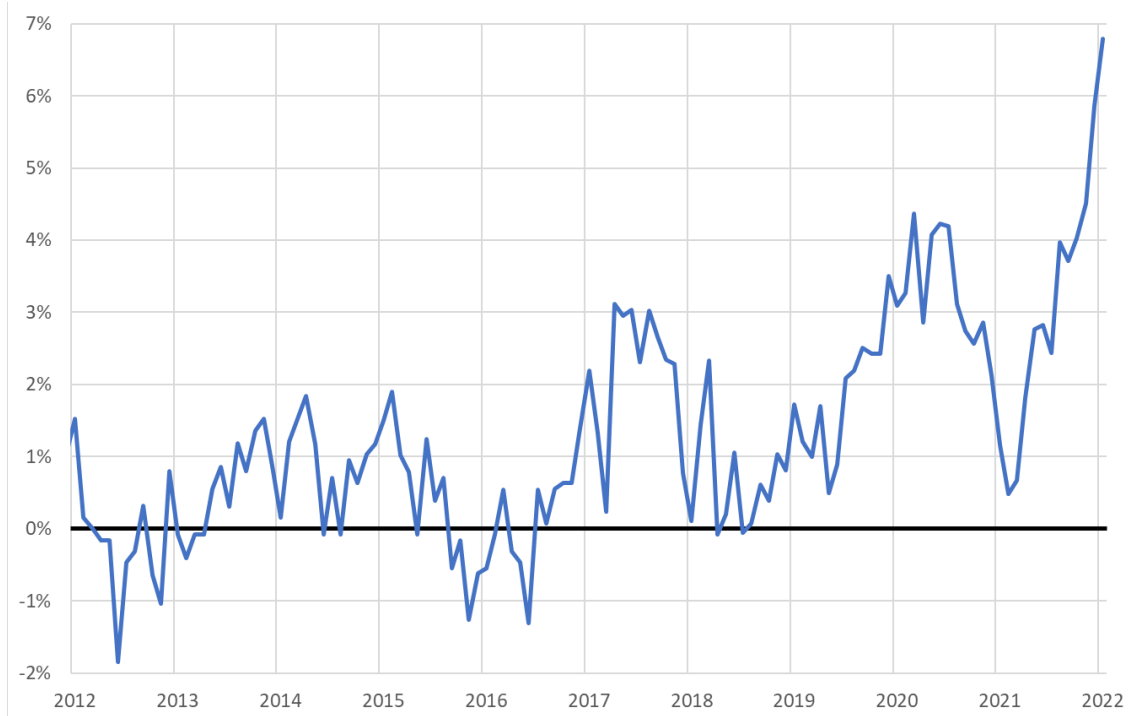
Source: Statistics NZ

Basics are driving food price increases. Prices for vegetables and fruit have risen most over the past 12 months (Figure 7). Statistics New Zealand measures 165 food categories, everything from oranges to chewing gum, yet the top 20 price increases in the last year are noticeably green.¹³ Food prices are rising at their highest rate since the winter of 2011 (Figure 8). Recent price increases are a noticeable departure from longer run trends (Figure 9).

¹² Per 1 kg except for berries (500g), meat pies (6 or 8, whichever is cheapest), and eggs (per dozen),

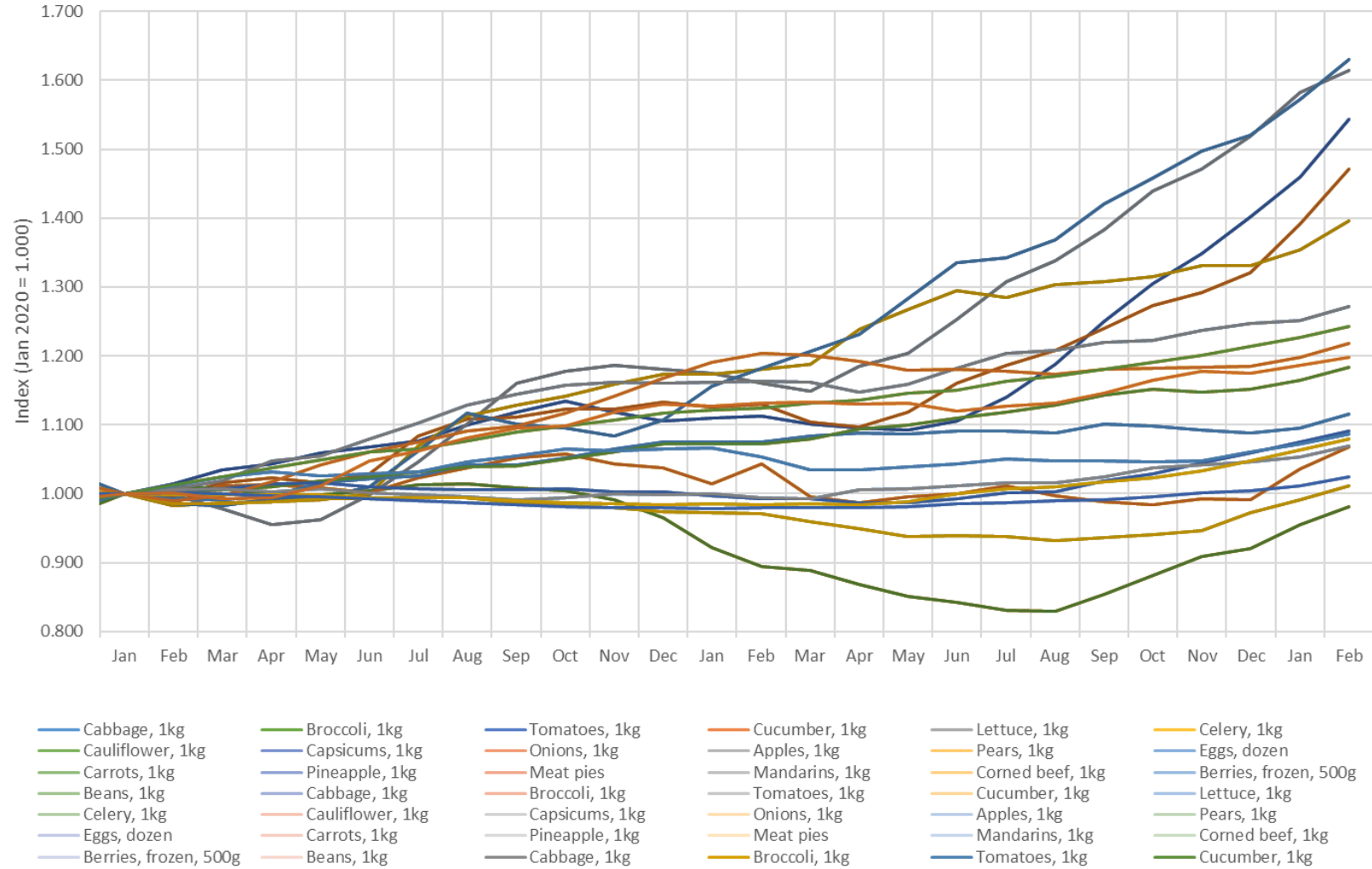
¹³ We checked price increases in other years to confirm this year is exceptional. Other years had a more diverse group of products where price increases were greatest, and the increases were less dramatic.

Figure 8: New Zealand annual increase in food prices 2012-2022



Source: Statistics NZ

Figure 9: Food prices 2008-2022, top 20 annual increase year to Feb 2022, rolling 12-month average, Jan 2020=1.000 (Source: Statistics NZ)



Source: Statistics NZ, Initiative calculations

Conclusion

In the 1970s, the world discovered stagflation, which combined low economic growth with sustained price increases. The experience led to innovations in monetary policy, including central bank independence. The result was three decades of price stability.

Now inflation has returned, and it appears as if the hard-won lessons from past decades must be re-learned. The government has responded to a supply-side crisis with demand-side stimulus. It has overshot, judging from both the relative size of the response and high inflation compared to other countries. Unfortunately, further stimulus is in the pipeline. The Budget in May includes an unprecedented \$6 billion of new spending. Although the Reserve Bank has ended quantitative easing, it appeared to have been slow to raise interest rates in response to rising prices. Since June 2021, inflation expectations for two years out have increased by more (+1.22%) than the Official Cash Rate (+0.75%).¹⁴

The problem with further monetary and fiscal stimulus now that inflation is here, is that it will take a more aggressive interest rate rise and potentially a deeper recession to recover price stability. New Zealand now faces the triple threat of ongoing COVID disruptions, high food, and energy prices due to the war in Ukraine, and rising interest rates with borrowing already at or near record levels.¹⁵ Economic mismanagement has consequences.

¹⁴ Among forecasters, economists, and industry leaders. See Reserve Bank of New Zealand, "Survey of expectations (M14)," [link](#).

¹⁵ Reserve Bank of New Zealand, "Household debt," [link](#).

Appendix

Table 1: Estimated cost of living increases

NZHEC ¹⁶	Item category	Estimated cost increase Dec 2020-Dec 2021
1	Food	\$478.24
1.1	Fruit and vegetables	\$108.59
1.2	Meat, poultry, and fish	\$55.27
1.3	Grocery food	\$175.28
1.4	Non-alcoholic beverages	\$5.53
1.5	Restaurant meals and ready-to-eat food	\$136.42
2	Alcoholic beverages and tobacco	\$66.21
2.1	Alcoholic beverages	\$26.72
2.2	Cigarettes and tobacco	\$41.16
3	Clothing and footwear	\$46.86
3.1	Clothing	\$27.32
3.2	Footwear	\$19.60
4	Housing and household utilities	\$588.02
4.1	Actual rentals for housing	\$342.89
4.3	Property maintenance	\$60.10
4.4	Property rates and related services	\$183.79
4.4.03	Local authority rates and payments	\$164.27
4.5	Household energy	-\$16.91
4.5.01	Electricity	-\$20.57
5	Household contents and services	\$91.32
5.1	Furniture, furnishings, and floor coverings	\$39.89
5.2	Household textiles	-\$1.09
5.3	Household appliances	\$7.58
5.4	Glassware, tableware, and household utensils	-\$3.86
5.5	Tools and equipment for house and garden	\$13.48
5.6	Other household supplies and services	\$33.29
6	Health	\$47.49
6.1	Medical products, appliances, and equipment	-\$8.37
6.2	Out-patient services	\$51.27
6.3	Hospital services	\$4.70
7	Transport	\$1,041.93
7.1	Purchase of vehicles	\$123.71
7.2	Private transport supplies and services	\$810.46
7.2.02	Petrol	\$689.60
7.3	Passenger transport services	\$142.17
8	Communication	-\$28.51
8.1	Postal services	\$1.03
8.2	Telecommunication equipment	-\$9.71
8.3	Telecommunication services	-\$20.87

¹⁶ New Zealand Household Expenditure Classification. [Link](#).

NZHEC¹⁶	Item category	Estimated cost increase Dec 2020-Dec 2021
9	Recreation and culture	\$137.03
9.1	Audio-visual and computing equipment	-\$37.73
9.2	Major recreational and cultural equipment	\$10.29
9.3	Other recreational equipment and supplies	\$134.05
9.4	Recreational and cultural services	\$8.40
9.5	Newspapers, books, and stationery	\$6.00
9.6	Accommodation services	\$21.50
10	Education	\$16.59
10.1	Early childhood education	\$5.29
10.2	Primary and secondary education	\$6.77
10.3	Tertiary and other post school education	\$3.72
10.4	Other educational fees	\$0.00
11	Miscellaneous goods and services	\$254.82
11.1	Personal care	\$61.84
11.3	Personal effects	\$2.33
11.4	Insurance	\$121.80
11.5	Credit services	-\$8.13
11.6	Other miscellaneous services	\$35.76
13.1	Interest payments	\$262.17
A	All groups	\$3,002.18

Source: Statistics New Zealand, Household Living-Cost Price Index, December 2021.

This table estimates the average change in expenditure on each category for all households between December 2020 and December 2021 based on the December 2020 basket. Subcategories do not sum to parent category due to a) rounding and b) some missing subcategories in the source data (this has no effect on parent or overall estimates).

Table 2: Annual price change to Feb 2022 Top 50 (Source: Statistics NZ)

		Feb 2021	Feb 2022	Change
1.	Cabbage, 1kg	\$2.00	\$3.92	+96.0%
2.	Broccoli, 1kg	\$6.30	\$11.91	+89.0%
3.	Tomatoes, 1kg	\$2.54	\$4.68	+84.3%
4.	Cucumber, 1kg	\$5.46	\$9.47	+73.4%
5.	Lettuce, 1kg	\$4.36	\$6.99	+60.3%
6.	Celery, 1kg	\$3.06	\$4.27	+39.5%
7.	Courgettes, 1kg	\$5.60	\$7.55	+34.8%
8.	Cauliflower, 1kg	\$4.87	\$6.37	+30.8%
9.	Capsicums, green, else red, 1kg	\$11.83	\$15.00	+26.8%
10.	Onions, 1kg	\$2.34	\$2.89	+23.5%
11.	Apples, 1kg	\$3.41	\$4.13	+21.1%
12.	Pears, 1kg	\$4.41	\$5.33	+20.9%
13.	Eggs, dozen	\$4.30	\$5.15	+19.8%
14.	Carrots, 1kg	\$2.57	\$3.07	+19.5%
15.	Pineapple, 1kg	\$3.20	\$3.81	+19.1%
16.	Meat pies, chilled, 6 or 8 pack - Cheapest Available	\$6.12	\$7.27	+18.8%
17.	Mandarins, 1kg	\$5.46	\$6.44	+17.9%
18.	Corned beef, fresh, chilled, or frozen, 1kg	\$12.28	\$14.37	+17.0%
19.	Berries, frozen, 500g	\$5.96	\$6.97	+16.9%
20.	Beans, 1kg	\$11.63	\$13.50	+16.1%
21.	Bread - white sliced loaf, 600g	\$1.31	\$1.52	+16.0%
22.	Salad, takeaway, vegetable, 1kg	\$11.33	\$13.13	+15.9%
23.	Grapes, green or red	\$8.85	\$10.19	+15.1%
24.	Chicken nuggets, frozen, 1kg	\$10.19	\$11.65	+14.3%
25.	Two minute noodles, multipack,5	\$2.40	\$2.74	+14.2%
26.	Chicken breast, 1kg	\$12.26	\$13.96	+13.9%
27.	Tomato sauce - canned, 560g	\$2.85	\$3.24	+13.7%
28.	Cheese - mild cheddar (supermarket only), 1kg	\$10.77	\$12.23	+13.6%
29.	Soup, canned, 500g	\$3.62	\$4.11	+13.5%
30.	Pizza, fresh or frozen, with any standard topping, each	\$5.02	\$5.67	+12.9%
31.	Peaches - canned (supermarket only), 410g	\$1.40	\$1.58	+12.9%
32.	Biscuits - chocolate, 200g	\$2.46	\$2.76	+12.2%
33.	Tomatoes, canned, 400g	\$1.33	\$1.49	+12.0%
34.	Bananas, 1kg	\$2.90	\$3.24	+11.7%
35.	Roasting lamb and hogget, fresh, chilled, or frozen, 1kg	\$15.84	\$17.65	+11.4%
36.	Lamb - chops, 1kg	\$17.98	\$20.03	+11.4%
37.	Chicken, cooked, whole, No. 15 - Cheapest Available	\$11.35	\$12.58	+10.8%

		Feb		
	Item	2021	Feb 2022	Change
38.	Oranges, 1kg	\$4.41	\$4.86	+10.2%
39.	Beef - mince, 1kg	\$16.06	\$17.66	+10.0%
40.	Mixed vegetables, frozen, 1kg	\$3.52	\$3.86	+9.7%
41.	Mayonnaise, 380ml	\$2.91	\$3.19	+9.6%
42.	Butter - salted, 500g	\$5.17	\$5.65	+9.3%
43.	Spaghetti - canned, 420g	\$1.74	\$1.90	+9.2%
44.	Dried pasta, spaghetti, or other type, 500g	\$1.97	\$2.15	+9.1%
45.	Fish and chips, One fish/chips	\$7.45	\$8.12	+9.0%
46.	Milk - standard homogenised, 2 litres	\$3.59	\$3.91	+8.9%
47.	Hot chips, hot wedges	\$3.64	\$3.94	+8.2%
48.	Dessert, frozen, 500g	\$6.94	\$7.51	+8.2%
49.	Chicken pieces (excluding breast), boneless or bone in, 1kg	\$7.69	\$8.32	+8.2%
50.	Fresh fish, 1kg	\$35.10	\$37.81	+7.7%

Source: Statistics New Zealand, Food Price Index Selected Monthly Weighted Average Prices for New Zealand (Monthly), to February 2022, via Infoshare.

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