Data Snapshot

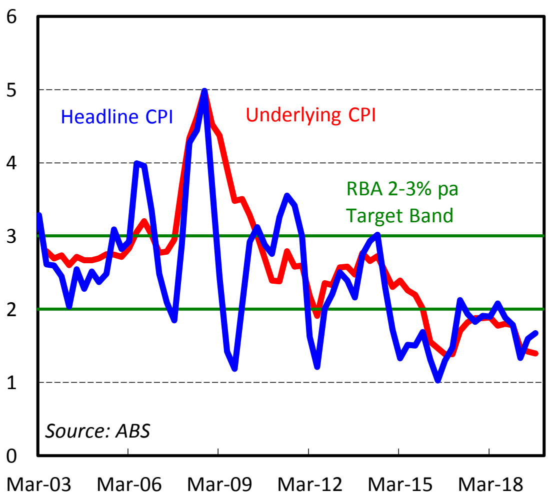
Wednesday, 30 October 2019

Consumer Price Index

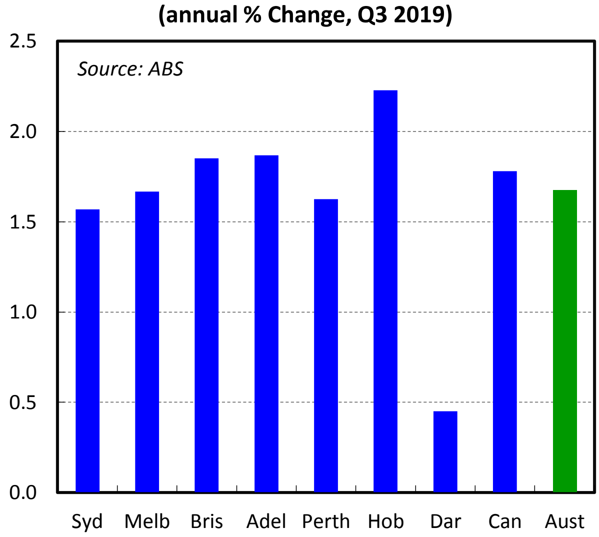
Groundhog Day

- **The Reserve Bank (RBA) must feel like Bill Murray's character, Phil, in the film Groundhog Day. Phil found himself reliving the same day over and over again when he went on location to the small town of Punxsutawney to film a report about their annual groundhog day.**
- **Underlying inflation, using the trimmed mean measure, lifted by 0.4% in the September quarter, the same outcome as the past quarter and the same as every quarter for five of the past six quarters.**
- **The annual rate of growth for underlying inflation also stayed steady in the September quarter at 1.6%. The underlying measure has remained below the RBA's target band of 2-3% per annum for almost 4 years.**
- **The headline measure of inflation rose 0.5% in the September quarter, taking the annual rate from 1.6% in the June quarter to 1.7% in the September quarter. This inflation measure confirms that price growth in the economy is soggy.**
- **Some signs of price pressures in selected areas are evident in the breakdown of today's data. Meat prices have increased due to the drought and some imported goods have seen inflation due to the lower Australian dollar. But these price pressures are limited and not enough to offset the muted and broader-based price pressures elsewhere in the economy.**
- **The latest soft reading means that another rate cut appears locked in and the conversation has now turned towards unconventional monetary policy. We continue to expect the RBA to cut rates once more in February next year but cannot rule out a move in December.**

Consumer Price Index
(annual % change)



Inflation by Capital City
(annual % Change, Q3 2019)



Headline and Underlying CPI

The Reserve Bank (RBA) must feel like Bill Murray's character, Phil, in the film Groundhog Day. Phil found himself reliving the same day over and over again when he went on location to the small town of Punxsutawney to film a report about their annual groundhog day.

Instead of reliving a dreary routine in a small town, the RBA has been in its own loop as it watches inflation consistently miss its target.

The RBA focuses on the underlying inflation measure, trimmed mean, which attempts to look through volatility. The trimmed mean lifted by 0.4% in the September quarter, the same outcome as the past quarter and the same as every quarter for five of the past six quarters (or 1½ years). The result was also in line with consensus expectations.

The annual rate of growth for the trimmed-mean measure also stayed steady in the September quarter at 1.6%. This result takes it to nearly 4 years the underlying measure has stayed under the RBA's target band of 2-3% per annum.

The headline measure of inflation rose 0.5% in the September quarter, taking the annual rate from 1.6% in the June quarter to 1.7% in the September quarter. Again, this inflation measures shows price growth in the economy is soggy.

September quarter, 2019

Headline Consumer Prices	Quarterly % Change
Food and non-alcoholic beverages	0.4
Alcohol and tobacco	2.0
Clothing and footwear	1.5
Housing	0.3
Furnishings, household equipment and services	1.1
Health	-0.2
Transport	-0.3
Communication	-1.1
Recreation and culture	1.5
Education	0.1
Insurance and Financial Services	0.2
Total	**0.5**

Groups Analysis

Among the key eleven categories of the consumer price index, the strongest rise in the quarter was recorded by alcohol & tobacco (up 2.0% and adding 0.2 percentage points).

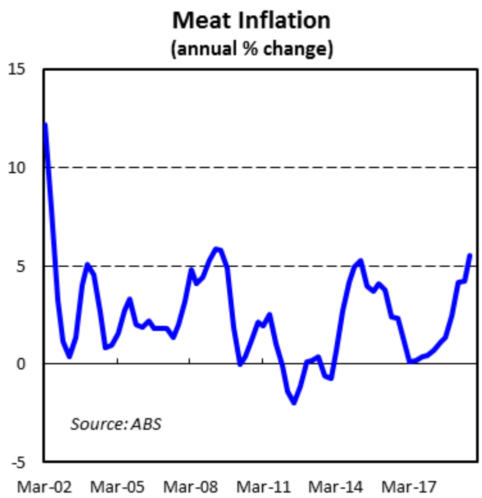
The recreation category was the only other category to contribute 0.2 percentage points in the quarter. This category rose by 1.5% in the quarter, dragged higher by a strong rise in international holiday travel & accommodation (up 6.1% quarter-on-quarter). Flight and accommodation costs typically rise in the September quarter, reflecting the peak seasons in Europe and America for travel.

Within the recreation category, games, toys & hobbies recorded the biggest quarterly decline of 3.1%, which was also the largest decline across all of the sub categories; our kids' demands for more toys are clearly trying to offset this weakness!

Clothing & footwear also showed price growth of 1.5% in the September quarter, boosted by higher prices for footwear. Higher footwear prices might be reflecting the effects of a weaker Australian dollar compared with a few years ago.

The largest decline across the eleven categories was in communication, which was down 1.1% in the quarter. The other categories to record a contraction in prices in the quarter were transportation (-0.3%) and health (-0.2%).

The housing category forms a large component of the CPI. Housing showed price growth of only 0.3% in the September quarter. With further to run in the construction cycle and the housing-price recovery only just begun, we do not expect housing price pressures to add considerably to inflation in the near term.



In annual terms, the strongest rate of price growth was again recorded by alcohol & tobacco at 6.6% and the weakest annual rate was found in communications (-1.1%).

The food category, education and health categories were the other main categories to record growth above 2% at 2.3%, 2.8% and 3.1%, respectively.

The food category highlights some price pressures resulting from the drought; meat prices are substantially higher. Lamb & goat prices recorded a double-digit annual rate for the fourth consecutive quarter.

Tradables and Non-Tradables Inflation

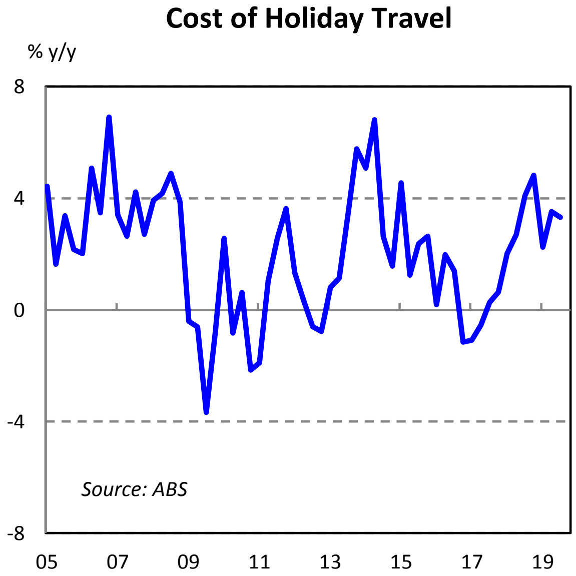
Tradables inflation measures the prices of goods and services that are imported, or those which compete with imported goods, and is heavily influenced by movements in the Australian dollar and other global factors over time.

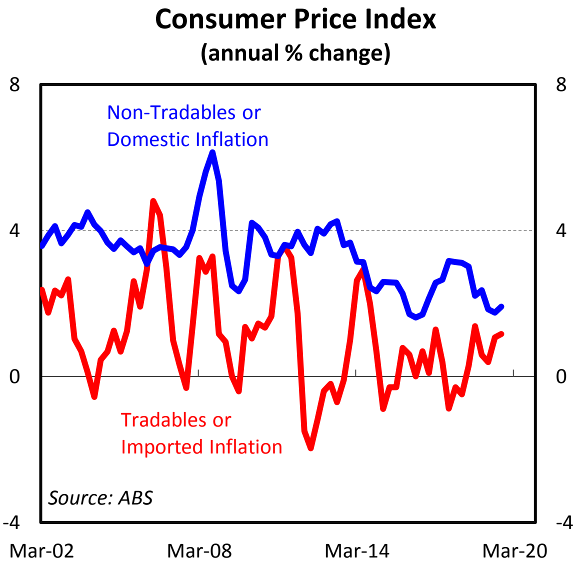
The weak Australian dollar over the quarter led to another strong quarterly increase in tradables inflation. Prices of tradable goods rose 0.9% in the quarter to September, building on a 1.2% increase registered in the June quarter. Driving the segment higher was tobacco prices, which registered a 3.4% rise over the quarter while clothing and footwear prices increased by a further 1.5% following a 1.6% gain in the June quarter. There was also a solid lift in furniture prices, which increased 2.4% over the quarter.

The latest evidence is that a weaker Australian dollar in the September quarter and compared with a few years ago is steadily flowing through to prices. The Australian dollar in trade-weighted terms fell 1.5% over the September quarter. The currency has been in a holding pattern in the second half of the year, but has been trending lower since 2017. It is currently around 12.5% below the high reached in July 2017.

Despite the latest decline in the currency, tradeables inflation remains weak on an annual basis. The tradeable component of inflation was 1.2% higher compared with a year earlier in September compared with a 1.1% rise in June.

Non-tradables inflation is a measure of the price changes of goods that are not subject to international competition. Typically this segment makes a larger contribution to the headline figure and includes items with large household budget expenditure shares, such as utilities and other housing costs. This measure rose 0.4% over the September quarter which was the highest outturn since December 2018. On an annual basis, prices increased 1.9%, boosted by health costs (3.1%) and education fees (2.8%).





Inflation by Capital Cities

Inflation was fairly uniform across capital cities in the September quarter. Boosting prices was the cost of health insurance and an increase in public transport fares.

Sydney and Melbourne both matched the nationwide average over the quarter with an increase of 0.5%. Adelaide and Canberra saw the highest quarterly increase in prices with a 0.7% increase while Darwin recorded the lowest among the capital cities with a 0.3% increase following last quarter's 0.8% jump. Brisbane registered a 0.6% increase and Perth and Hobart prices also rose by the national average of 0.5%.

On an annual basis, all capital cities recorded inflation below 2% except for Hobart which saw a 2.2% rise. Inflation is running at a particularly low annual pace in Darwin (0.5%) due to the soft economic conditions currently prevailing in the Northern Territory.

Outlook

There are few signs the inflation picture is set to change over the coming year. Economic activity will continue to grow at a rate that is below trend (or potential) and the labour market is likely to have ongoing spare capacity.

The breakdown of today's inflation data shows some signs of price pressures in selected areas. Meat prices rose over the quarter due to the drought and some imported goods saw an increase due to a weaker Australian dollar. But these price pressures are limited and not enough to offset the muted and broader-based price pressures elsewhere in the economy. Furthermore, we see limited scope for the Australian dollar to depreciate significantly from current levels.

Whilst the RBA has its eyes firmly on a range of data releases, its guiding "north star" in setting the cash rate remains inflation. Therefore, this latest inflation report adds to the strong case for the

RBA to cut the cash rate again. We see the most likely timing as February next year, but there is some risk the RBA moves sooner (in December).

Another rate cut appears locked in; the discussion has turned to unconventional policies with the cash rate likely to get to or close to the effective lower bound when the RBA cuts the cash rate again. The inflation story adds to the case for more stimulus from the RBA both in terms of a cash rate and/or unconventional monetary policy stimulus on or after the next cash rate.

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