

Consumer Price Index (CPI), September quarter (Q3) 2016

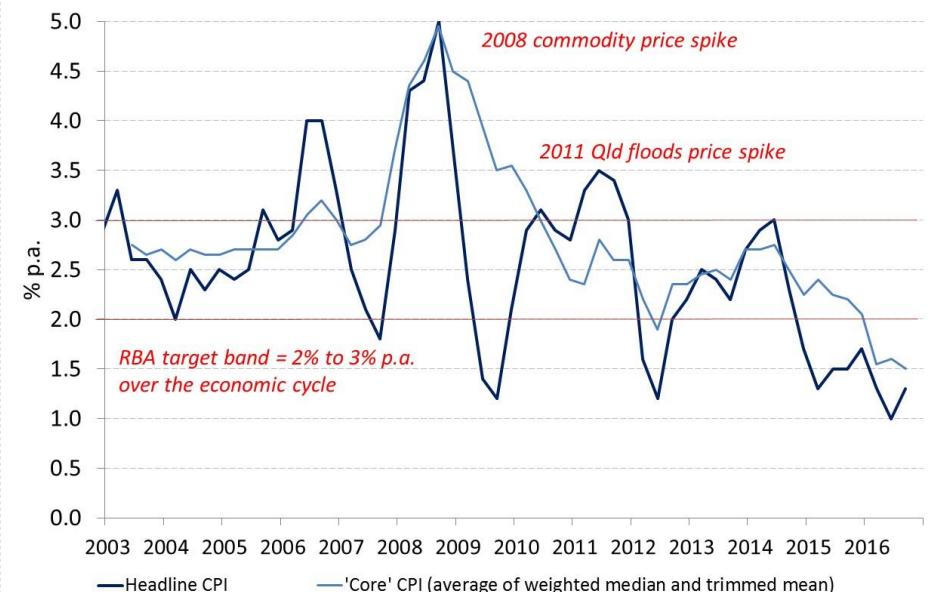
Headline annual consumer inflation picked up to 1.3% p.a. in the September quarter of 2016 (Q3), moving closer towards the RBA's target band of 2 to 3%. In quarterly growth terms, headline CPI grew by +0.7%, after more sluggish growth in Q2 (+0.4%) and no growth in Q1 (0.0% upwardly revised from -0.2% previously). The main contributors to inflation in Q3 were food & beverages (+1.7% q/q., +1.5% p.a.) and housing (+1.0% q/q, +1.8% p.a.), both of which account for large shares of the consumer 'basket' of spending on goods and services.

At +1.3% p.a. in Q3, Australia's **headline inflation** is still very low. This was the same headline inflation as in Q1 2016 and Q1 2015. Headline inflation has now been below the RBA's target band of 2 to 3% p.a. (on average, over the economic cycle) for the past two years, or eight consecutive quarters. This is the longest period that CPI annual growth has stayed below 2% since 1999.

Underlying inflation (the average of the trimmed mean and weighted median measures of inflation, and a less volatile measure than headline CPI) moved lower in annual terms in Q3, at +1.5% p.a. and down from (an upwardly revised) +1.6% p.a. in Q2. Q3 2016 marks the lowest level of underlying inflation in the current relevant CPI data series, which commenced in 2003. This suggests that inflation is still structurally weak, despite an increase in headline inflation.

This protracted period of low inflation will allow further scope for monetary easing (lowering the cash rate) by the RBA if it considers this necessary. The RBA lowered the cash rate by 25 basis points in early August to 1.5% after the release of very weak inflation data for Q2. The RBA may consider lowering the cash rate further in coming months, after considering a range of factors in its decisions (including the labour market and balance sheets across the economy). The RBA has said it expects inflation to pick and eventually return to the 2 to 3% target range. The Q3 inflation results are broadly in line with the RBA's expectations.

Chart 1: CPI p.a., headline & core



+0.7%

HEADLINE CPI,
QUARTER GROWTH

+1.3%

HEADLINE CPI,
ANNUAL GROWTH

Across the capital cities, annual inflation in Q3 2016 was slowest in Darwin (0.0% p.a.) and highest in Sydney (+1.7% p.a.), Brisbane (+1.5% p.a.), Canberra (+1.4% p.a.) and Melbourne (+1.4% p.a.). The eastern capitals have generally experienced stronger price growth, while other capitals have had softer inflation in 2016. This reflects stronger economic performance in the eastern states and particularly in NSW and Victoria in 2016, with weaker growth and a build-up of spare capacity in the formerly booming mining states.

Prices for **tradable goods and services** (accounting for around 40% of the CPI basket) lifted by 1.0% q/q in Q3 (up from +0.6% q/q in Q2), and headed slightly higher (+0.7%) in annual terms. Prices for tradable goods and services are largely determined globally and are affected by movements in the exchange rate and commodity prices (agricultural as well as resources). The increase in tradable prices in Q3 was driven by higher fruit prices (+19.5% q/q, +4.4% p.a.).

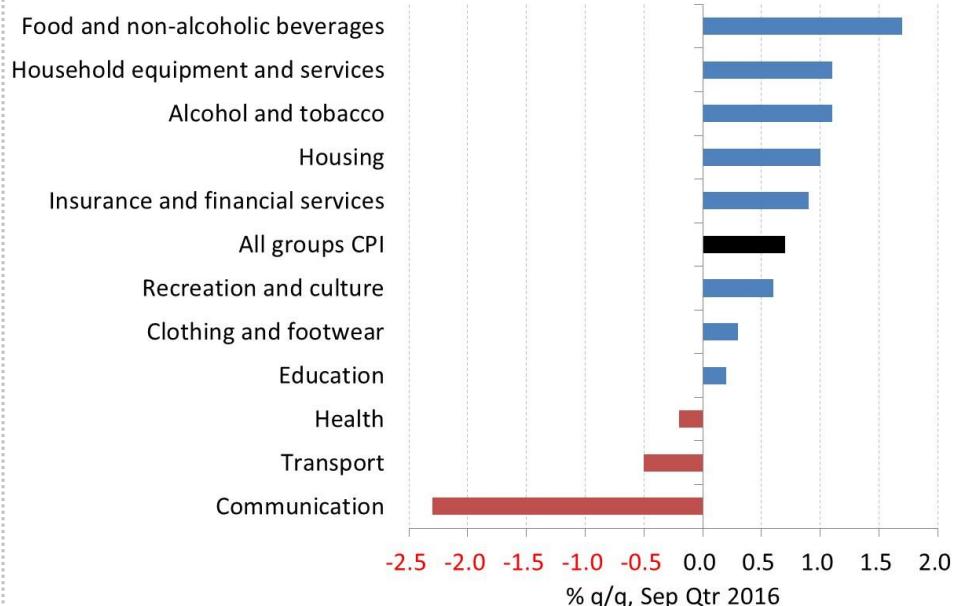
Prices for **non-tradeable goods and services** (accounting for around 60% of the CPI basket) increased more modestly, at +0.5% q/q and +1.7% p.a. In annual growth terms, this was slightly stronger than in the June quarter (+1.6% p.a.). Prices for non-tradeable goods and services are largely determined locally by labour, rent and other local costs. They include large categories of consumer spending such as housing, healthcare and education. Non-tradeable price increases in Q3 were strongest in electricity prices (+5.4% q/q, +4.7% p.a.).

Muddying the inflation story somewhat for Q3, a number of non-tradable goods have now been re-classified as tradable (mostly food and beverages products), while some goods have been classified as non-tradable that were previously classified as tradable (including spirits, tobacco, and pharmaceutical products). This reclassification may help to explain some of the divergence in growth between tradables and non-tradables inflation; quarterly growth in tradables prices outstripped growth in non-tradables in Q3, which was the reverse of the historical pattern of non-tradables inflation typically outperforming tradables inflation.

Looking across the categories of goods and services that are included in the CPI 'basket', food and beverages was the main driver of increases in CPI in Q3 (+1.7% q/q and +1.5% p.a.). Specifically, prices for fruit (+19.5% q/q, +4.4% p.a.) and vegetables (+5.9% q/q, +11.9% p.a.). This spike in fruit prices was mainly driven by adverse weather conditions including flooding in parts of the country, impacting some food producing regions and restricting supply.

Housing prices also added upward pressure to the CPI in Q3 (+1.0% q/q, +1.8% p.a.). In particular, electricity prices (+5.4% q/q, +4.7% p.a.) increased due to a jump in wholesale electricity price in the eastern and southern states (notably south Australia). Property rates and charges also added to housing costs (+4.0% q/q, +4.0% p.a.) due to a rise in new dwelling purchases by owner occupiers.

Chart 2: Quarterly price rises, Q3 2016



Key numbers: Australian core CPI, September quarter 2016

+0.4%

CORE CPI,
QUARTER GROWTH

+1.5%

CORE CPI,
ANNUAL GROWTH

Table 1: Key CPI Numbers, September quarter (Q3) 2016

	Quarterly change (% q/q)		Annual change (% p.a.)	
	Sep-16	Jun-16	Sep-16	Jun-16
Headline CPI	0.7	0.4	1.3	1.0
Trimmed mean	0.4	0.5	1.7	1.7
Weighted median	0.3	0.5	1.3	1.5
Core CPI <i>(average of trimmed & weighted)</i>	0.4	0.5	1.5	1.6
Tradable goods and services	1.0	0.6	0.7	0.0
Non-tradable goods and services	0.5	0.4	1.7	1.6
Goods	0.8	0.6	1.0	0.3
Services	0.5	0.3	1.8	2.0
Capital cities				
Sydney	1.0	0.6	1.7	0.9
Melbourne	0.5	0.4	1.4	1.4
Brisbane	0.6	0.5	1.5	1.5
Adelaide	0.8	0.5	1.2	0.7
Perth	0.4	0.3	0.5	0.5
Hobart	0.7	0.0	1.3	1.2
Darwin	0.4	0.3	0.0	0.0
Canberra	0.8	0.2	1.4	0.8

What is the CPI?

The Consumer Price Index (CPI) measures changes in the price of a 'basket' of goods and services which account for a high proportion of expenditure by metropolitan households. CPI data is collected by the Australian Bureau of Statistics (ABS) and released each quarter in January, April, July and October.

Headline CPI is the most commonly referenced CPI figure. It is not adjusted for the seasonality of volatile movements in prices.

Underlying CPI (or Core CPI) is a less volatile measure, as it removes the effects of items that tend to fluctuate frequently in price. Core CPI is the average of the trimmed mean CPI and the weighted mean CPI.

For more information from the ABS, or for information from the ABS on how to use the CPI in contracts, see:

<http://www.abs.gov.au/AUSSTATS/abs@.nsf/mf/6401.0?opendocument#from-banner=LN>

Next CPI release date:

December Quarter (Q4) 2016 due for release on 25 January 2017

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