



## Consumer Price Index (CPI), December quarter (Q4) 2016

Headline consumer inflation inched higher to 1.5% per annum in the December quarter of 2016 (Q4) from 1.3% in Q3, moving closer to the RBA's target band of 2 to 3%. In quarterly growth terms, headline CPI grew by +0.5% which was slower than in Q3 (+0.7%). The main contributors to inflation in Q4 were alcohol and tobacco (+2.8% q/q, +5.9% p.a.), transport (+1.7% q/q, -0.3% p.a.) and food (+0.6% q/q, +1.8% p.a.), which together lifted consumer prices by +0.6% in the quarter.

At +1.5% p.a. in Q4, Australia's headline inflation remains low. Q4 marks over two years (nine quarters) of inflation staying under 2%, the longest such period since 1999. Even so, the Q4 result is the strongest annual rate of inflation since Q4 2015. Inflation may have bottomed out in this cycle as it now seems to be trending back towards the RBA's target band of 2 to 3% p.a. (on average, over the economic cycle).

**Underlying inflation** (the average of the trimmed mean and weighted median measures of inflation, and a less volatile measure than headline CPI) moved slightly higher in annual terms in Q4, at +1.6% p.a. from +1.5% p.a. in Q3. Core inflation remains around the lowest levels recorded since this series commenced in 2003. This suggests that inflation remains structurally weak, despite modest increases in both the headline and core inflation measures in Q4.

These sluggish inflation numbers will allow the RBA to reassess the appropriateness of its current monetary policy. The RBA lowered the cash rate by 25 basis points in August 2016 to an historic low of 1.50%. The RBA decided to leave the cash rate on hold at 1.50% throughout the remainder of 2016 and expects inflation to drift back up into the 2 to 3% p.a. target range during 2017.

**Across the capital cities**, annual inflation in Q4 2016 was slowest in Darwin (which experienced deflation, at -0.4% p.a.) and was equal highest in Sydney and Canberra (both +1.8% p.a.), followed by Brisbane (+1.6% p.a.), Melbourne (+1.5% p.a.), Hobart and Adelaide (both +1.3% p.a.). The eastern capitals are experiencing stronger price growth, as the drivers of economic activity have shifted back to the south-eastern seaboard and away from the mining-oriented states of Western Australia, Northern Territory and Queensland.

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



+0.5%

HEADLINE CPI  
QUARTER GROWTH  
Q4 2016

+1.5%

HEADLINE CPI  
ANNUAL GROWTH  
Q4 2016

Prices for **tradable goods and services** (accounting for around 35% of the CPI basket) fell by -0.1% q/q in Q4 (down from +1.0% q/q in Q3) and were very weak (+0.1%) 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 decrease in tradable prices in Q4 was driven by lower accessories prices (-5.1% q/q, -2.4% p.a.) and lower international travel and accommodation prices (-2.6% q/q, -2.5% p.a.), both of which may reflect movements in the Australian dollar in Q4.

Prices for **non-tradeable goods and services** (accounting for around 65% of the CPI basket) increased in Q4 and drove the increase in headline inflation. Prices for this group increased by +0.8% q/q in Q4 and by +2.1% over the year to Q4. This was a stronger price rise than in Q3 (+0.5% q/q, +1.7% 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 services spending such as housing, healthcare and education.

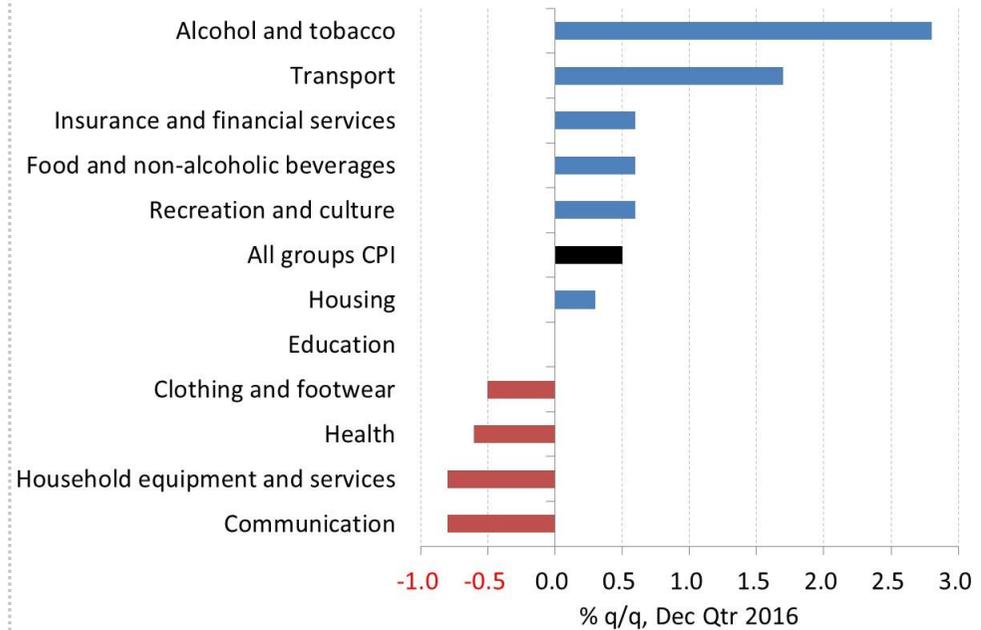
Looking across the categories of goods and services that are included in the CPI 'basket', alcohol and tobacco prices were one of the main drivers of the increase in CPI in Q4 (+2.8% q/q and +5.9%p.a.). Specifically, prices increased for tobacco (+7.4% q/q, +13.2% p.a.) due to an increase in the Federal excise tax on tobacco that came into effect on 1 September 2016.

Transport prices (+1.7% q/q, -0.3% p.a.) also helped drive up prices in Q4, mainly due to automotive fuel prices increasing by 6.7% over the quarter (but -1.1% p.a.). All fuel types experienced price increases in Q4 as higher global oil prices flowed through to fuel prices.

Food prices went up by 0.6% q/q in Q4 and +1.8% p.a. Restaurant meals (+1.1% q/q, +2.4% p.a.), other food products (+5.4% q/q, +0.2% p.a.) and vegetables (+2.5% q/q, +1.6% p.a.) were the main drivers of food price inflation in Q4.

Dampening price growth in Q4 were declines in prices for household equipment and services (-0.8% q/q but +0.6% p.a.) and specifically for furniture, which declined by -1.5% q/q ( but +0.6% p.a.).

Chart 2: Quarterly price rises, Q4 2016



**+0.4%**

CORE CPI,  
QUARTER GROWTH  
Q4 2016

**+1.6%**

CORE CPI,  
ANNUAL GROWTH  
Q4 2016

**Table 1: Key CPI Numbers, December quarter (Q4) 2016**

	Quarterly change (% q/q)	Annual change (% p.a.)
<b>Headline CPI</b>	0.5	1.5
Trimmed mean	0.4	1.6
Weighted median	0.4	1.5
<b>Core CPI</b> <i>(average of trimmed &amp; weighted)</i>	0.4	1.6
Tradable goods and services	-0.1	0.1
Non-tradable goods and services	0.8	2.1
Goods	0.7	1.3
Services	0.4	1.7
<b>Capital cities</b>		
Sydney	0.5	1.8
Melbourne	0.7	1.5
Brisbane	0.5	1.6
Adelaide	0.3	1.3
Perth	0.4	0.4
Hobart	0.8	1.3
Darwin	-0.1	-0.4
Canberra	0.6	1.8

## 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/64.01.o?opendocument#form-banner=LN>

Next CPI release date:

March Quarter (Q1) 2017 due for release on 26 April 2017

## Ai Group Economics and Research Team

<b>Julie Toth</b>	<b>Chief Economist</b>
<b>David Richardson</b>	<b>Senior Economist</b>
<b>Jesse Oliver</b>	<b>Economist</b>
<b>Colleen Dowling</b>	<b>Senior Research Analyst</b>
<b>Elle Spyropoulos</b>	<b>Research Assistant</b>

[economics@aigroup.com.au](mailto:economics@aigroup.com.au)

T: 03 9867 0111