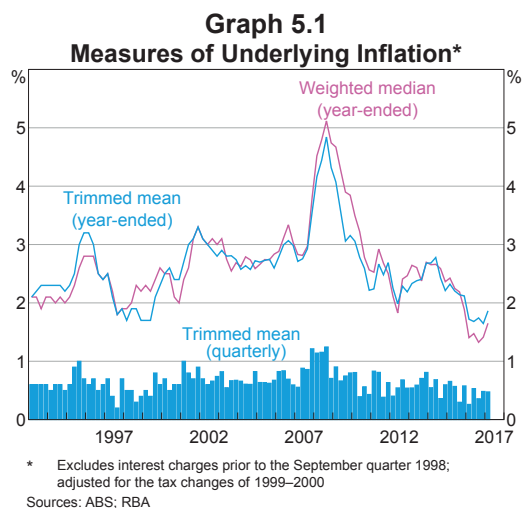


# 5. Inflation

The March quarter inflation data were in line with the forecasts in the February *Statement*. Measures of underlying inflation were steady at around ½ per cent in the quarter, and picked up to 1¾ per cent over the year (Graph 5.1; Table 5.1). Headline inflation was also unchanged in the quarter at 0.5 per cent, and increased to 2.1 per cent over the year (Graph 5.2).

Domestic cost pressures remain subdued. Growth in labour costs has remained low, competitive conditions in the retail sector continue to put downward pressure on consumer prices and rent inflation remains low. Some of this downward pressure has been offset by a pick-up in inflation in fuel and utilities prices and in the cost of new dwelling construction.



An increase in the tobacco excise also boosted headline inflation over the year.

**Table 5.1: Measures of Consumer Price Inflation**  
Per cent

	Quarterly <sup>(a)</sup>		Year-ended <sup>(b)</sup>	
	March quarter 2017	December quarter 2016	March quarter 2017	December quarter 2016
Consumer Price Index	0.5	0.5	2.1	1.5
Seasonally adjusted CPI	0.5	0.5		
– Tradables	0.5	0.0	1.3	0.1
– Tradables (excl volatile items) <sup>(c)</sup>	–0.1	–0.6	–0.9	–0.5
– Non-tradables	0.7	0.8	2.6	2.1
<i>Selected underlying measures</i>				
Trimmed mean	0.5	0.5	1.9	1.6
Weighted median	0.4	0.4	1.7	1.4
CPI excl volatile items <sup>(c)</sup>	0.4	0.3	1.5	1.3

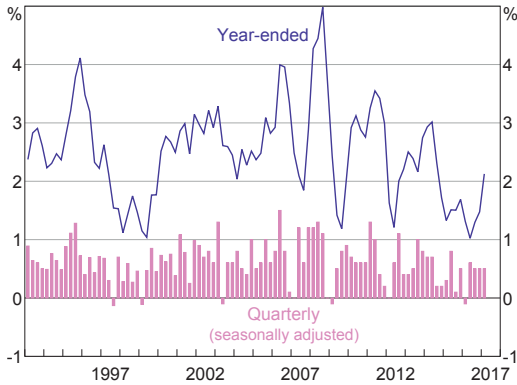
(a) Except for the headline CPI, quarterly changes are based on seasonally adjusted data; those not published by the ABS are calculated by the RBA using seasonal factors published by the ABS

(b) Year-ended changes are based on non-seasonally adjusted data, except for the trimmed mean and weighted median

(c) Volatile items are fruit, vegetables and automotive fuel

Sources: ABS; RBA

**Graph 5.2**  
**Consumer Price Inflation\***

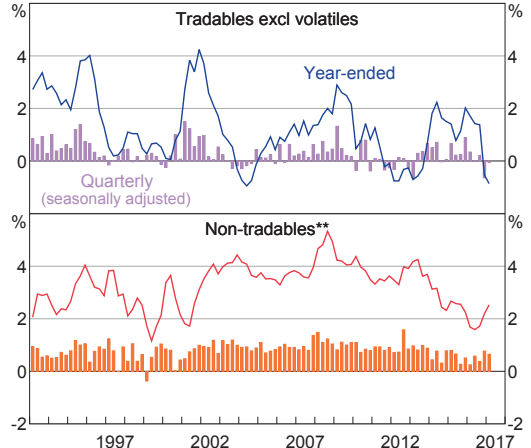


\* Excludes interest charges prior to the September quarter 1998; adjusted for the tax changes of 1999–2000  
Sources: ABS; RBA

Prices of tradable items (excluding volatiles) fell a little in the March quarter to be almost 1 per cent lower over the year (Graph 5.3). The 7 per cent appreciation of the trade-weighted index over the year to the March quarter is likely to have contributed a little to the downward pressure on tradable prices. Inflation in prices for food and clothing & footwear has been low as a result of efforts from both established retail firms and new entrants to gain market share by competing on prices (Graph 5.4). Low growth in labour costs and retail rents has also contributed to weak inflationary pressure. Recent inflation outcomes suggest that some of these competitive forces may be increasing in some retail segments, such as furniture & household appliances. The arrival of further new foreign retailers will be an important influence on final retail prices over the next few years.

Fruit & vegetable prices increased in the March quarter and inflation for these items remains high over the year. There was little impact from Cyclone Debbie in the March quarter CPI because it occurred so late in the quarter. However, the cyclone caused damage to the crops of some specific fruit and vegetables, which will boost their prices in the next couple of quarters.

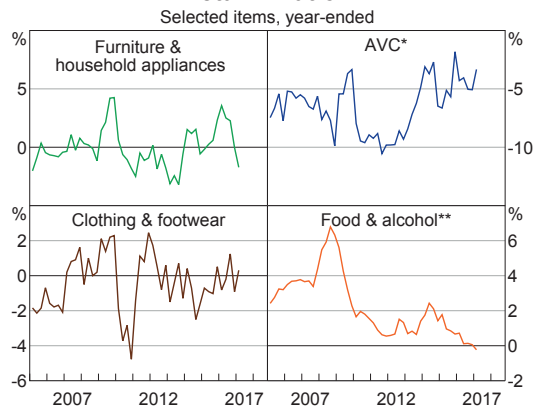
**Graph 5.3**  
**Tradable and Non-tradable Inflation\***



\* Adjusted for the tax changes of 1999–2000  
\*\* Excludes interest charges and deposit & loan facilities  
Sources: ABS; RBA

Prices of tradable items (excluding volatiles) fell a little in the March quarter to be almost 1 per cent lower over the year (Graph 5.3). The 7 per cent appreciation of the trade-weighted index over the year to the March quarter is likely to have contributed a little to the downward pressure on tradable prices.

**Graph 5.4**  
**Retail Inflation**



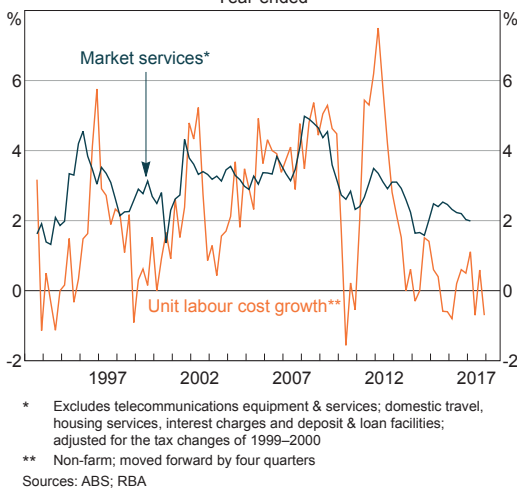
\* Includes audio, visual and computing equipment & services  
\*\* Excludes fruit and vegetables  
Sources: ABS; RBA

Non-tradable inflation was little changed at 0.7 per cent in the quarter and rose to 2.6 per cent over the year. Inflation in this group has been boosted by both higher tobacco and utilities prices over the year.<sup>1</sup> Apart from these components, non-tradable inflation has been

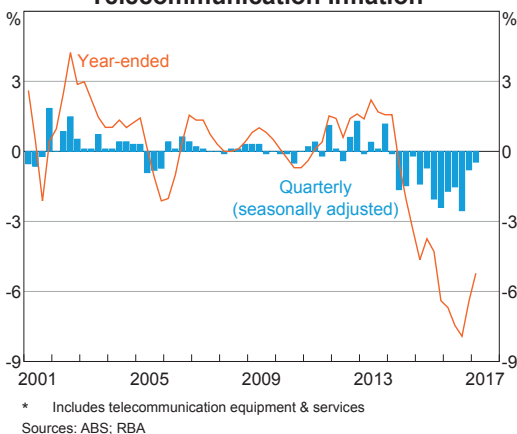
<sup>1</sup> Following an ABS review of the international trade exposure of CPI components, the December quarter 2016 CPI release contained a reclassification of a number of expenditure classes between tradables and non-tradables. The most notable was the reclassification of tobacco from tradable to non-tradable.

relatively subdued. Inflation in market services remains low, consistent with low growth in unit labour costs (Graph 5.5). Technology-driven price declines for telecommunication equipment & services also continues to put downward pressure on non-tradable inflation (Graph 5.6). Declines in prices in this component have subtracted an average of 0.2 percentage points from annual non-tradable inflation since the beginning of 2015. Nevertheless, deflation in this component has slowed over the past two quarters.

**Graph 5.5**  
**Market Services Inflation**  
Year-ended

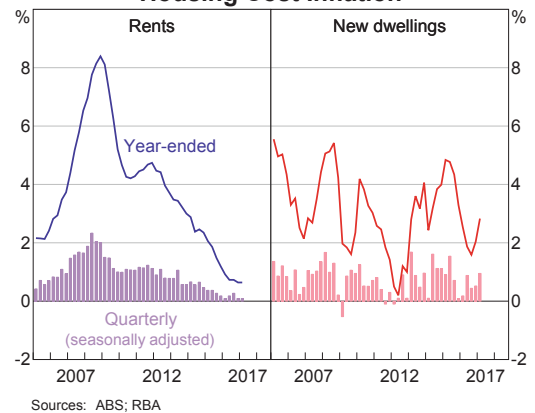


**Graph 5.6**  
**Telecommunication Inflation\***



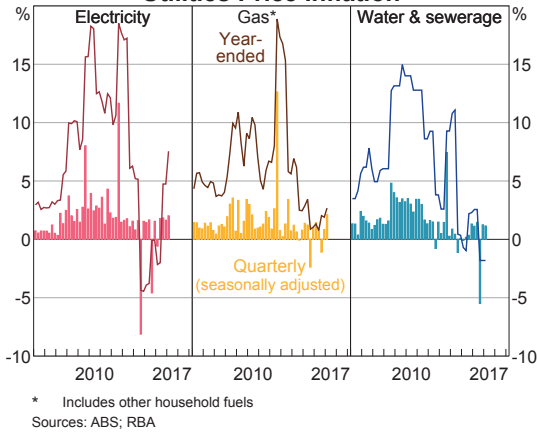
New dwelling cost inflation increased in the March quarter (Graph 5.7). This was a result of higher materials costs; reports of wage pressure in the construction sector are mixed. For the first time, this component now includes the cost of building apartments (as well as detached houses). Inflation in the cost of building apartments has been slightly lower than for detached houses over the past year. Rent inflation remains low, particularly in Perth. The substantial increase in supply of apartments in other cities has contributed to low rental growth, although conditions vary across capital cities, reflecting differences in the amount of new supply, population growth and vacancy rates.

**Graph 5.7**  
**Housing Cost Inflation**



Inflation in utilities prices picked up in the March quarter, and year-ended inflation for these items reached its fastest pace since 2014 (Graph 5.8). Wholesale gas and electricity prices have increased strongly over the past year, largely reflecting an increase in demand for gas for liquefied natural gas production. Furthermore, the recent closure of coal-powered electricity plants will continue to boost electricity prices in the near term. This has started to flow through to retail prices, and will also increase input costs for businesses. Previous Bank estimates suggest that

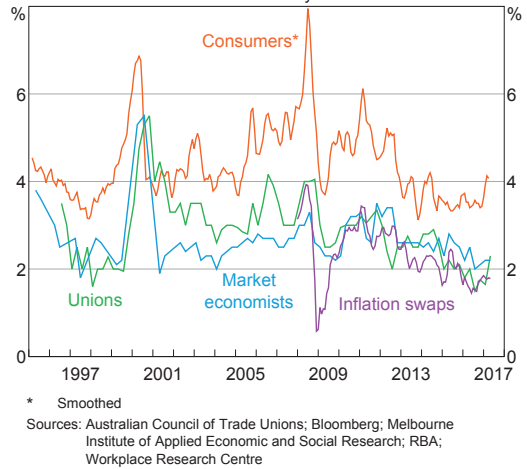
**Graph 5.8**  
**Utilities Price Inflation**



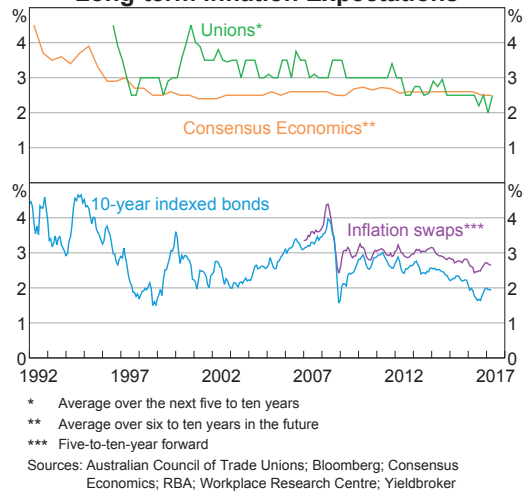
a 10 percentage point increase in utilities price inflation is associated with a 0.3–0.4 percentage point increase in underlying inflation, over and above the direct effects.<sup>2</sup> Excluding utilities, inflation in administered prices slowed in the quarter, partly due to falls in education fees and public transport fares.

Measures of inflation expectations remain low, though most are a bit higher than the lows reached in 2016. Short-term union and consumer expectations have risen in recent months, while other short-term measures have been little changed (Graph 5.9). Long-term survey-based measures of inflation expectations are around 2.5 per cent (Graph 5.10). After increasing over the second half of 2016, financial market measures of inflation expectations have stabilised; both the bond and swap measures remain at higher levels than a year ago. ↘

**Graph 5.9**  
**Short-term Inflation Expectations**  
Over the next year



**Graph 5.10**  
**Long-term Inflation Expectations**



<sup>2</sup> See Plumb M and K Davis (2010), 'Developments in Utilities Prices', *RBA Bulletin*, December, pp 9–17.