4. Inflation

Inflation declined in the March quarter, although it remains high and broadly based. The easing in global upstream cost pressures has started to flow through to domestic goods prices and this is expected to continue in the year ahead. Market services inflation remains high and rent inflation has picked up further in response to the tight conditions in the rental market. Measures of short-term inflation expectations have continued to decline in recent months but remain high, consistent with the high inflation environment. Most measures of medium- and long-term inflation expectations remain consistent with the inflation target.

The December quarter outcomes for wages and broader measures of labour costs suggest that the strong September quarter outcomes had to some extent overstated the underlying momentum in labour cost growth. Nonetheless, labour cost growth over 2022 was the highest it had been in over a decade, driven by the tight labour market, high inflation and the Fair Work Commission's (FWC) decision on minimum and award wages. With productivity growth very weak over 2022, growth in unit labour costs was around multi-decade highs. Timely indicators suggest that wages growth was solid in the March quarter of 2023. Firms in the Bank's liaison program report that their wages growth has stabilised at around 4 per cent, but that they expect growth to moderate in the year ahead. Market economists and union officials expect wages growth to peak around 3¾ to 4 per cent over the year ahead and to then moderate over the following year.

Inflation eased in the March quarter

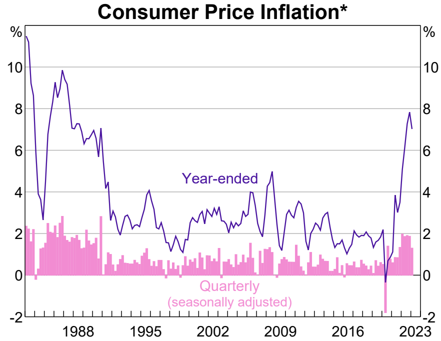
The Consumer Price Index (CPI) increased by 1.3 per cent in the March quarter (in seasonally adjusted terms) and by 7 per cent over the year, down from a peak of 7.8 per cent in the December quarter. Nonetheless, inflation remains around its highest level since 1990 (Graph 4.1; Table 4.1).

High inflation continues to be broadly based. A wide range of items have contributed to the strong inflation outcomes over the past year (Graph 4.2). The share of the CPI basket growing faster than 3 per cent in annualised terms declined in the March quarter but remains high (Graph 4.3).

Measures of underlying inflation (which remove the effect of irregular or temporary price changes) also eased in the March quarter but remain high. Trimmed mean inflation was 1.2 per cent in the quarter (in seasonally adjusted terms) and 6.6 per cent over the year,

Graph 4.1

Consumer Price Inflation*



* Excludes interest charges prior to the September quarter of 1998; adjusted for the tax changes of 1999–2000.

Sources: ABS; RBA

Table 4.1: Measures of Consumer Price Inflation

Per cent

	Quarterly(a)		Year-ended(b)	
	March quarter 2023	December quarter 2022	March quarter 2023	December quarter 2022
Consumer Price Index	1.4	1.9	7.0	7.8
Seasonally adjusted CPI	1.3	1.9	–	–
– Tradables	0.6	1.9	6.1	8.7
– Tradables (excl. volatile items)(c)	0.8	2.4	6.7	8.1
– Non-tradables	1.7	1.9	7.5	7.4
Selected underlying measures				
Trimmed mean	1.2	1.7	6.6	6.9
Weighted median	1.2	1.6	5.8	5.6
CPI excl. volatile items(c)	1.4	2.1	7.3	7.6

(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

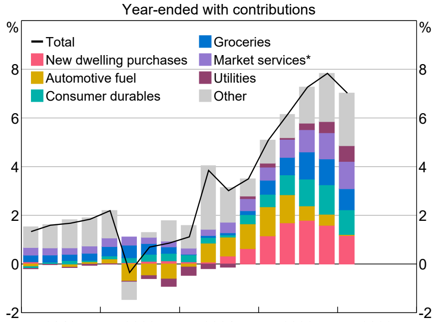
down from a peak of 6.9 per cent in the December quarter of 2022 (Graph 4.4; Table 4.1).

Fuel prices declined in the March quarter

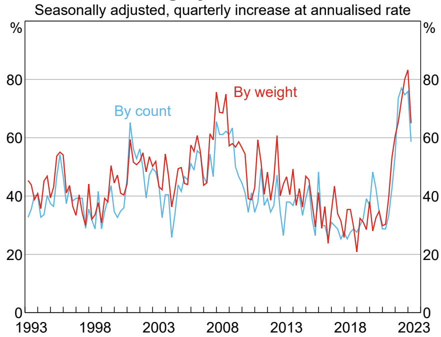
Fuel prices declined a little in the March quarter, largely reflecting price declines for diesel fuel. Fuel prices are little changed compared with a year ago and are well below the peaks reached following Russia's invasion of Ukraine in March 2022 (Graph 4.5). So far, fuel prices are higher in the June quarter than the average levels observed in the March quarter.

Goods price inflation has slowed in response to the easing in upstream cost pressures

The easing in global upstream cost pressures has contributed to slower inflation for new dwellings, groceries and many consumer



* Excludes domestic travel and telecommunications.
Sources: ABS; RBA



* Adjusted for the tax changes of 1999–2000.
Sources: ABS; RBA

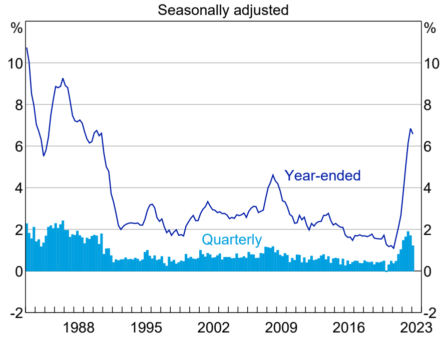
durable items. Global supply chain conditions have returned to around pre-pandemic norms and cost pressures for international freight, materials and some imported goods have eased significantly. This easing in international costs has been partially offset by increased domestic costs, particularly from energy, wages and logistics. Nonetheless, lower input cost growth has started to affect prices paid by consumers and is expected to lead to a further slowing in goods inflation in the period ahead, consistent with the experience overseas.

New dwelling cost inflation eased further to around 1 per cent in the March quarter, well below the quarterly outcomes of around 5 per cent observed in the first half of 2022.

Graph 4.4

Trimmed Mean Inflation*

Seasonally adjusted



* Excludes interest charges prior to the September quarter of 1998 and deposit & loan facilities; adjusted for the tax changes of 1999–2000.

Sources: ABS; RBA

Prices were around 13 per cent higher over the year, down from a peak of 21 per cent in September 2022. The easing in new dwelling inflation reflects improvements in the supply of building materials and weaker demand following the rise in interest rates. However, trade costs due to labour shortages remain a source of upward pressure for some builders. Prices for building materials increased by 1.6 per cent in the March quarter and 11 per cent over the year, which is slower than the pace of increases seen over 2022 (Graph 4.6).

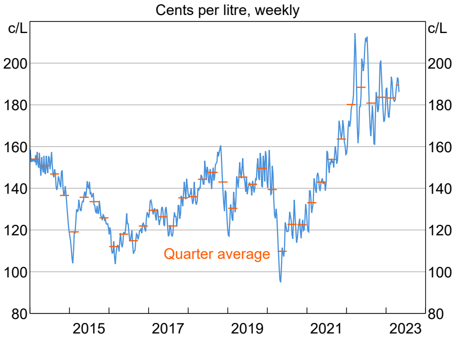
Consumer durables inflation eased in the March quarter to be 6 per cent over the year (down from 7 per cent in the December quarter) (Graph 4.7). Prices declined or remained little changed for a number of components – such as clothing and footwear, household appliances, textiles and furniture – due to increased post-Christmas discounting activity (Graph 4.8). However, price increases remained strong for audio, visual and computing equipment, as well as for some other items such as motor vehicles. Notably, the decline in wholesale LCD panel prices that has flowed through to retail prices of TVs and other audio-visual equipment in other advanced economies has yet to occur in Australia.

Grocery prices (excluding fruit and vegetables) increased by around 1 per cent in the quarter –

Graph 4.5

Unleaded Petrol Prices

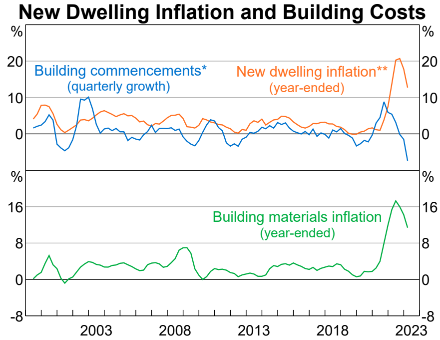
Cents per litre, weekly



Sources: Australian Institute of Petroleum; RBA

Graph 4.6

New Dwelling Inflation and Building Costs



* Six-quarter average lagged by one quarter.

** Adjusted for the tax changes of 1999–2000.

Sources: ABS; RBA

the slowest rate since 2021 – and were 9 per cent higher over the year (Graph 4.7). Supermarkets continue to pass through supplier cost increases, although the pace of these increases has moderated lately. Grocery inflation eased for most food categories in the quarter, particularly for meat and seafood (Graph 4.9). Liaison suggests that grocery prices are likely to increase further in the near term, but at a slower pace than seen over the past year. Prices of fruit and vegetables were broadly unchanged in the quarter.

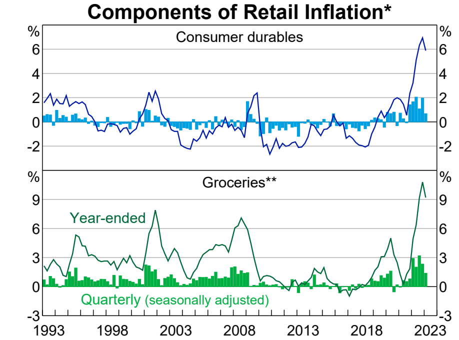
Services inflation remains strong

Input cost pressures and strong demand continued to contribute to large price increases for many services. Market services inflation – which covers a little more than one-fifth of the CPI basket – was 1.6 per cent in the March quarter and around 8 per cent over the year (Graph 4.10). This was the strongest outcome since 1990 and annual inflation remained strong across most items. The prices of these services are generally among the most sensitive to domestic labour costs, although increases in non-labour costs such as materials and transport have been an important factor driving higher prices for some of these services in recent quarters (in particular, for cafes and restaurants).

Outcomes differed in the quarter across different types of market services. Prices for insurance and financial services increased strongly in the March

Graph 4.7

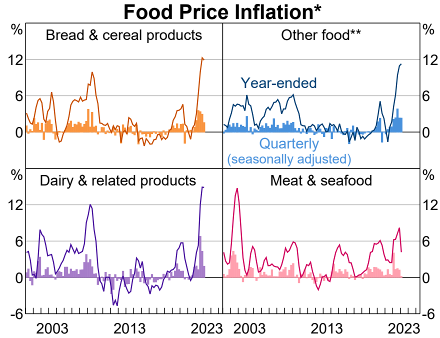
Components of Retail Inflation*



* Adjusted for the tax changes of 1999–2000.
** Excludes fruit & vegetables.
Sources: ABS; RBA

Graph 4.9

Food Price Inflation*

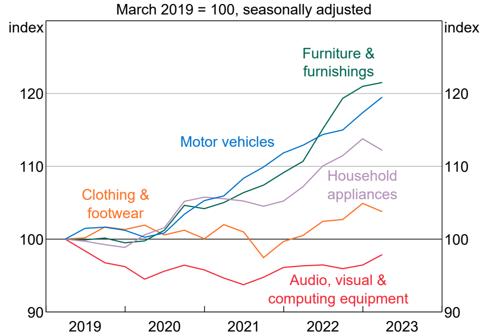


* Adjusted for the tax changes of 1999–2000.
** Includes products such as eggs, jams, oils, snacks, etc.
Sources: ABS; RBA

Graph 4.8

Consumer Durables Prices

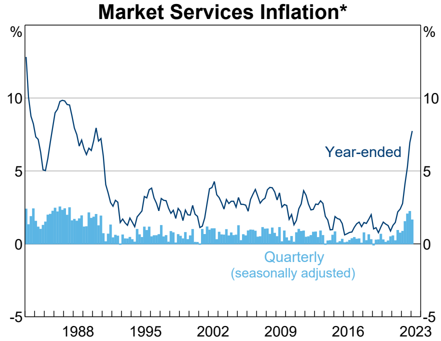
March 2019 = 100, seasonally adjusted



Sources: ABS; RBA

Graph 4.10

Market Services Inflation*



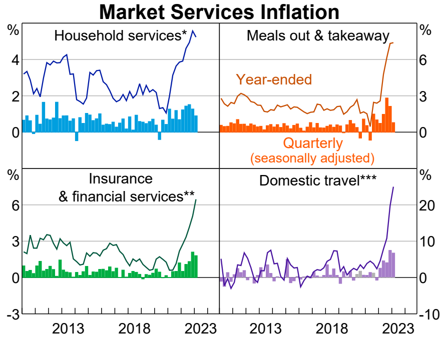
* Adjusted for the tax changes of 1999–2000.
Sources: ABS; RBA

quarter and over the year, reflecting higher insurance premiums due to increased claims arising from natural disasters (Graph 4.11). Meals out and takeaway inflation eased in quarterly terms, following strong increases in recent quarters. Domestic holiday travel and accommodation inflation remained strong in the quarter, reflecting robust demand; however, prices for international holiday travel and accommodation declined due to lower airfare prices.

Rents increased by 1.6 per cent in the March quarter and by 5 per cent over the year, reflecting tight rental market conditions across the country (Graph 4.12). The indexation of private rent assistance partly offset a larger increase in underlying prices. In the absence of this offset, rents would have increased by 1.8 per cent – stronger than the previous quarterly outcome. In monthly terms, rent inflation was fairly stable throughout the quarter at 0.7 per cent (excluding the effect of rent assistance in March), though this was stronger than the outcomes seen over the second half of 2022. Rents were strong across all cities, with particularly large increases in Brisbane and Perth. Strong current rental market conditions across the country, as reflected in high advertised rents and historically low vacancy rates, are expected to contribute to a further pick-up in CPI rent growth in the year ahead.

Graph 4.11

Market Services Inflation



* Includes home cleaning, vehicle repairs, hairdressing, veterinary services, sports and leisure services.
** Excludes deposit & loans to June quarter of 2011.
*** Imputed using headline CPI in the June and September quarters of 2020 and September quarter of 2021.
Sources: ABS; RBA

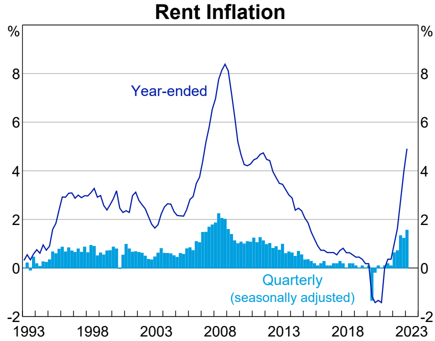
Gas prices rose strongly due to higher wholesale costs

Gas prices increased by 12 per cent in the March quarter, due to the pass-through of higher wholesale costs; prices were 26 per cent higher over the year – the largest annual increase on record (Graph 4.13). Prices increased in all capital cities but were largest in Melbourne over the quarter (23 per cent). Electricity prices increased by 2½ per cent in the quarter due to the continued unwinding of rebates in Queensland, Western Australia and Tasmania. Electricity prices were 15½ per cent higher over the year – the highest rate of increase since 2013. Electricity and gas prices are expected to increase further over the second half of this year as retail prices catch up to wholesale costs; however, the size of these increases are expected to be smaller than was anticipated prior to the announcement of the Australian Government's Energy Price Relief Plan (see Chapter 5: Economic Outlook).

In the CPI basket, 'administered prices' are (at least partly) regulated or relate to goods and services for which the public sector is a significant provider. They include categories such as health, education and child care, as well as utilities. Inflation for administered prices (excluding utilities) picked up to around

Graph 4.12

Rent Inflation



Sources: ABS; RBA

4½ per cent over the year to the March quarter. Prices for medical and hospital services increased by 3½ per cent in the quarter due to higher private health insurance premiums and increases in non-hospital medical services (Graph 4.14). Prices for education increased strongly in the quarter, due to the indexation of tertiary course fees to inflation, the final cohort of students transitioning to higher fees as a result of the job-ready graduate scheme introduced in 2021, and higher wages growth contributing to increases in school fees. State government fee relief programs in New South Wales, Victoria and Queensland more than offset underlying increases in prices for pre-school and primary education. Childcare prices increased by 2.4 per cent in the quarter, reflecting the pass-through of higher labour costs; however, prices remained flat compared with a year ago due to the effects of the increase in the subsidy rate in 2022 for families with more than one child.

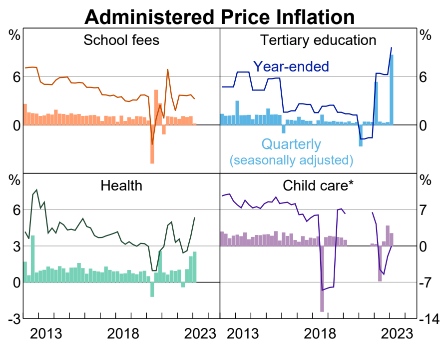
The monthly CPI indicator points to easing inflationary pressures

The ABS released the monthly CPI indicator for the month of March alongside the regular quarterly CPI release. The monthly CPI indicator points to inflationary pressures easing, with the year-ended rate slowing through the quarter (to 6.3 per cent in March, down from a peak of 8.4 per cent in December 2022) (Graph 4.15). The measure excluding volatile items also eased through the quarter (to 6.9 per cent in March, down from a peak of 8.3 per cent in December). The easing in the monthly CPI indicator over January to March was largely driven by disinflation in prices for many goods and holiday travel and accommodation – as was the case for the quarterly CPI.

Short-term inflation expectations have eased further, and longer term inflation expectations are mostly consistent with the inflation target

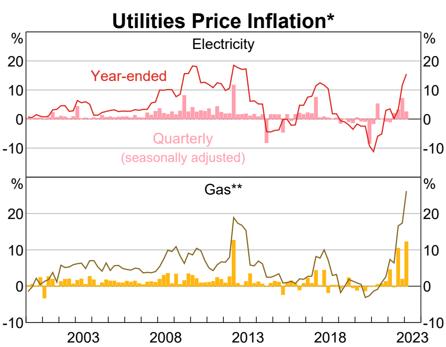
Measures of short-term inflation expectations have continued to decline from their

Graph 4.14



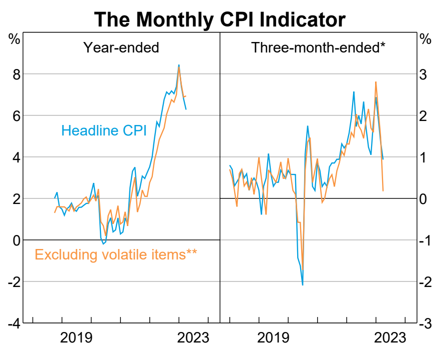
* Excludes volatile periods from June 2020 to September 2021 caused by the government's free child care policy.
Sources: ABS; RBA

Graph 4.13



* Adjusted for the tax changes of 1999–2000.
** Includes other household fuels.
Sources: ABS; RBA

Graph 4.15

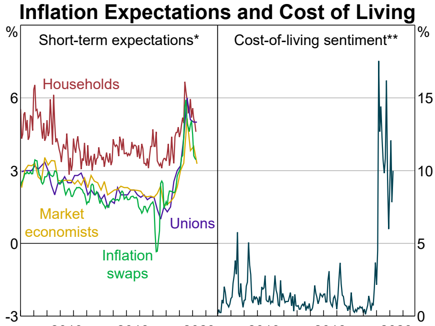


* Headline CPI is seasonally adjusted.
** Volatile items are automotive fuel and fruit & vegetables.
Sources: ABS; RBA

mid-2022 peaks but remain above the Bank's inflation target, consistent with the high inflation environment (Graph 4.16). The share of households expecting inflation to be greater than 10 per cent over the year ahead has declined over recent quarters; however, the share of households that expect inflation to be above 6 per cent over the coming year remains considerably higher than prior to the pick-up in inflation in mid-2021 (Graph 4.17). Most medium- and long-term measures remain consistent with the inflation target (Graph 4.18).

Graph 4.16

Inflation Expectations and Cost of Living

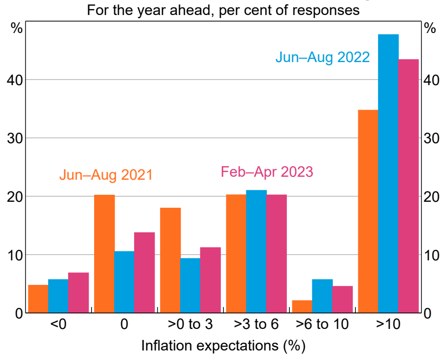


* Over the next year.
** Percentage of financial news articles mentioning 'cost of living'.
Sources: Australian Council of Trade Unions; Bloomberg; Dow Jones Factiva; Melbourne Institute; RBA; Workplace Research Centre

Graph 4.17

Distribution of Households' Inflation Expectations

For the year ahead, per cent of responses



Sources: Melbourne Institute; RBA

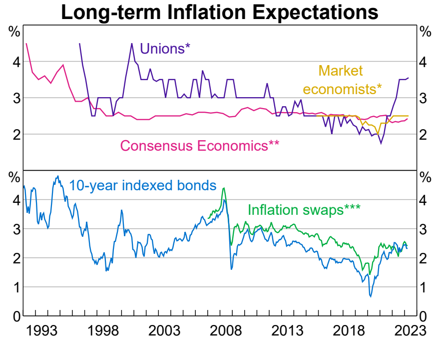
Wages growth was solid in the December quarter …

The Wage Price Index (WPI) grew by 0.8 per cent in the December quarter and 3.3 per cent in year-ended terms (Graph 4.19). This was the highest rate of year-ended wages growth since 2013, reflecting tightness in the labour market and high inflation outcomes. Wages in the private sector grew by 0.8 per cent in the quarter; although this was a solid increase, it was lower than the large increase in the September quarter that was boosted by the implementation of the FWC's award and minimum wage increases. Over the year to December, wages in the private sector grew by 3.6 per cent. By contrast, public sector wage growth continued to weigh on aggregate outcomes, increasing by 2.5 per cent over the year.

In the private sector, the average size of increases (for those jobs that received an increase in the quarter) remained around the highest rate in over a decade at around 4 per cent (Graph 4.20). This was partly driven by the delayed implementation of wage increases for awards in hospitality, tourism and aviation jobs announced by the FWC in 2022, with most of these jobs receiving a 4.6 per cent wage increase. Wages in accommodation and food

Graph 4.18

Long-term Inflation Expectations



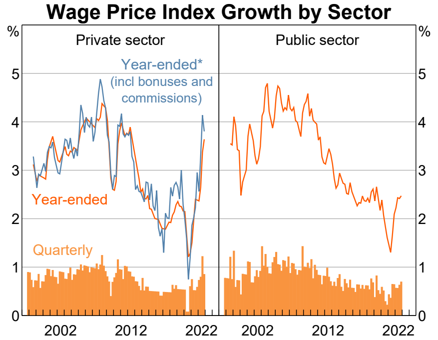
* Average over the next 5–10 years.
** Average over 6–10 years in the future.
*** 5-years to 10-years forward.
Sources: Australian Council of Trade Unions; Bloomberg; Consensus Economics; RBA; Workplace Research Centre; Yieldbroker

services recorded the largest increase in wages across industries in the quarter, reflecting the high proportion of jobs in this industry either on awards or that are covered by enterprise agreements or individual arrangements linked to the award wage increase. Lower skill jobs experienced stronger wages growth in the December quarter than higher skill jobs, consistent with the prevalence of award wage reliance in these jobs (Graph 4.21).

Broader measures of labour costs remained strong in the December quarter. Despite a slight slowing in the quarter, measures of wages that include bonuses continued to grow faster than base wages over the year, consistent with reports that employers have been using bonuses to attract or retain staff amid the tight labour market and to compensate for cost-of-living pressures. Compensation of employees – the broadest measure of economy-wide labour costs, which also includes headcount and hours worked – rose by 10 per cent over the year, its fastest pace in over a decade (Graph 4.22), largely driven by the private sector. Average earnings per hour declined in the quarter, although this measure continues to be affected by volatility in average hours worked. With productivity growth very weak over 2022, growth in unit labour costs was around multi-decade highs.

Graph 4.19

Wage Price Index Growth by Sector



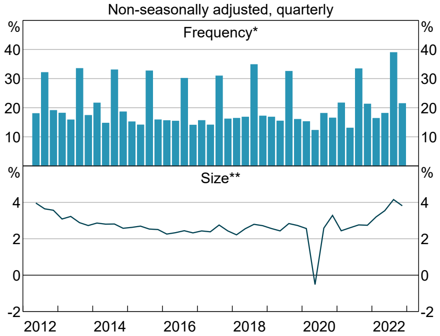
* Non-seasonally adjusted.

Source: ABS

Graph 4.20

Wage Changes in the Private Sector

Non-seasonally adjusted, quarterly



* Share of jobs that experienced a wage change in the quarter.

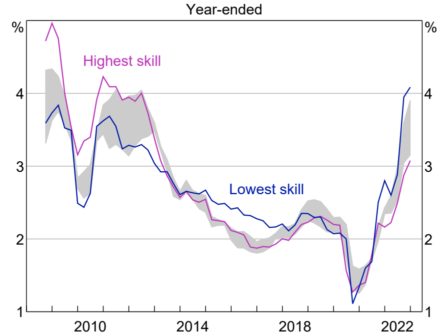
** Average percentage wage change, conditional on a wage change having occurred in the quarter.

Sources: ABS; RBA

Graph 4.21

Wages Growth by Skill Level*

Year-ended



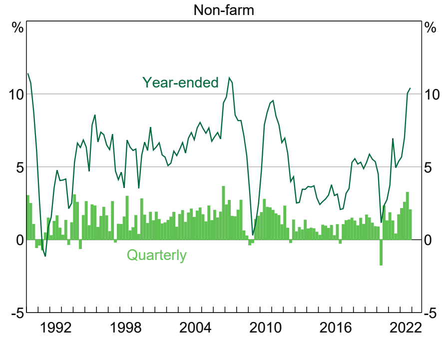
* The 'highest' and 'lowest' skill categories are ABS occupational skill levels 1 and 5 respectively; grey range denotes wages growth for skill levels 2–4.

Sources: ABS; RBA

Graph 4.22

Compensation of Employees Growth

Non-farm



Source: ABS

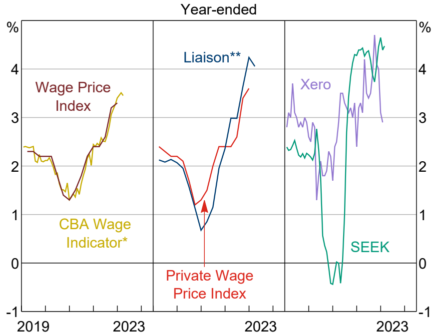
… and this is expected to continue over coming quarters

Timely indicators suggest that wages growth was solid in the March quarter, though there appears to be less upward momentum than a few months ago. Firms in the Bank's liaison program report their wages growth has stabilised at around 4 per cent, but they expect growth to moderate in the year ahead (Graph 4.23). Market economists and union officials expect wages growth to be around 3¾ to 4 per cent over the year ahead and to then moderate over the following year (Graph 4.24).

Graph 4.23

Timely Measures of Wages Growth

Year-ended



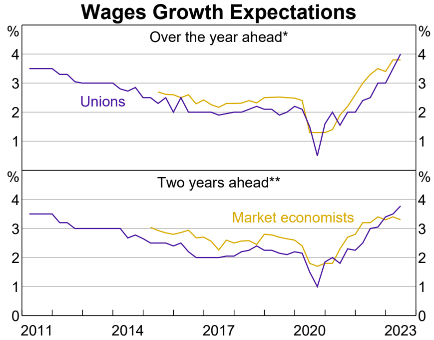
* Changes in base wages based on a sample of CBA retail banking transactions.

** Private sector; trimmed mean; rescaled to have the same mean as the private Wage Price Index.

Sources: ABS; CBA; RBA; SEEK; Xero Small Business Insights

Graph 4.24

Wages Growth Expectations



* The current calendar year for union expectations.

** The next calendar year for union expectations.

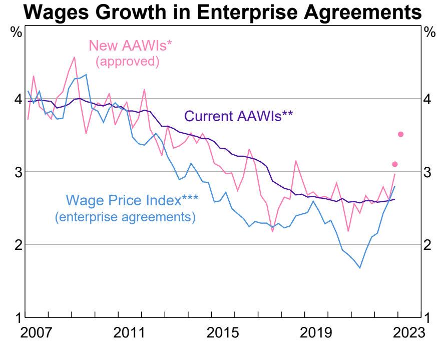
Sources: Australian Council of Trade Unions; RBA; Workplace Research Centre

Wages growth in enterprise agreements is expected to pick up further over coming quarters. Wages growth in newly lodged enterprise agreements increased to 3.5 per cent in the March quarter, though the number of employees covered by new agreements was lower than average (Graph 4.25). This series has tended to report slightly stronger wages growth than the data on *approved* new enterprise agreements, which likely reflects timing mismatches for some agreements. Firms in the Bank's liaison program generally expect wage growth outcomes in new enterprise agreements to be higher than current or expired agreements. Recent changes to the wage policies of a number of state governments and the Australian Government are also expected to support wages growth as they flow through to enterprise agreements in the public sector. For example, Victoria recently increased the public sector wage cap to 3 per cent for new enterprise agreements, and the NSW Government has indicated that it intends to offer larger public sector wage increases than is provided for under the existing wage cap.

Increases to award and minimum wages in coming quarters should further support wages growth. In February 2023, the FWC approved an

Graph 4.25

Wages Growth in Enterprise Agreements



* Quantifiable average annualised wage increases (AAWIs) in new FWC-approved and federally registered enterprise agreements; dots represent AAWIs in enterprise agreements submitted but not yet approved.

** AAWIs in the total stock of nominally current, FWC-approved and federally registered enterprise agreements.

*** Year-ended growth; excludes bonuses and commissions.

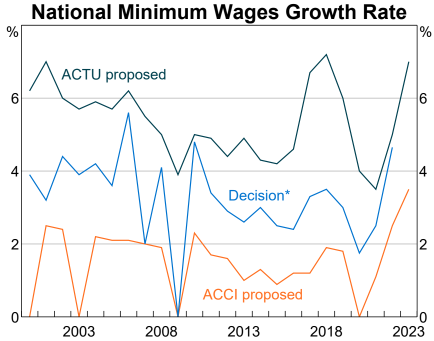
Sources: ABS; Department of Employment and Workplace Relations; FWC; RBA interim 15 per cent increase to modern award minimum wages for direct care workers and some other staff in the aged care sector; this will take effect from 30 June 2023. The FWC is considering whether further increases are warranted and whether to extend this interim increase to other workers in the sector. More broadly, the FWC will decide on the increases to award and minimum wages in coming months as part of its Annual Wage Review. In making its decision, the FWC is required to consider a range of factors, including the performance and competitiveness of the national economy, gender equality and the relative living standards and needs of low-paid workers. It also considers submissions from interested parties. The Australian Council of Trade Unions (ACTU) proposed a 7 per cent increase, while the Australian Chamber of Commerce and Industry (ACCI) proposed a 3.5 per cent increase (Graph 4.26).

Real incomes declined further in the December quarter

Real (inflation-adjusted) labour income declined further in the December quarter as labour income increased by less than consumer prices. Real wages declined by around 4 per cent over the year. The declines have been smaller for lower wage earners; nominal wages growth has been strongest for this group, due in part to the FWC award wage decision, while the rise in inflation has been broadly based across the income distribution and household types. Administrative employment data also suggests that lower income workers experienced relatively stronger earnings growth than higher income workers in the year to the December quarter of 2022. Across all quintiles, nominal employment income growth has been stronger than base wages growth, which likely reflects increases in hours worked, especially for those on lower incomes, switching to higher paid jobs and promotions, as well as additional payments such as overtime or cost-of-living bonuses (Graph 4.27). The increase in the cost of living has been broadly based across different household types, however, those on lower incomes typically have the most constrained budgets as they spend a greater proportion on essential items and have lower financial buffers (Graph 4.28). Furthermore, the experience of individual households varies widely and some workers who have remained in the same job and maintained the same hours will have seen their real incomes decline significantly.

Graph 4.26

National Minimum Wages Growth Rate



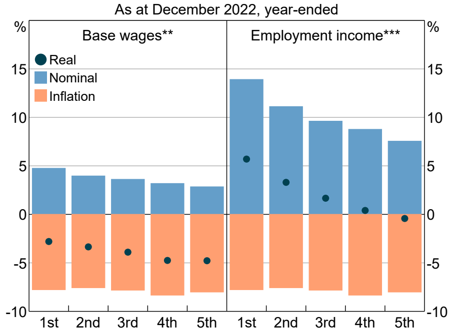
* The operative date for the 2020 decision was delayed for most award-reliant employees and for some award-reliant employees in 2021 and 2022.

Sources: ACCI; ACTU; AFPC; AIRC; FWC

Graph 4.27

Growth in Real Earnings by Quintile*

As at December 2022, year-ended



* Inflation quintiles constructed by income levels.

** Total hourly rates of pay, excluding bonuses and commissions; quintiles constructed using hourly wage rates in the previous period.

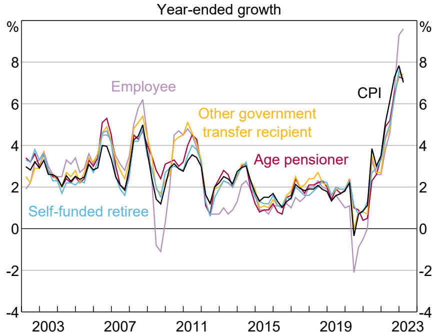
*** Single Touch Payroll employment income per worker for those with a 2019/20 tax return; percentiles constructed using employment income in the current period; estimates are based on the percentile at the mid-point of each group; administrative data on incomes are not necessarily directly comparable to published aggregate estimates.

Sources: ABS; ATO; RBA

Graph 4.28

Selected Living Cost Indexes by Household Type*

Year-ended growth



* The living cost indexes include mortgage interest payments (which are not included in the CPI) but exclude the construction costs of new dwellings (which are included in the CPI); other financial and insurance items also differ between the indexes.

Source: ABS