

5. Price and Wage Developments

Recent Developments in Inflation

Consumer price inflation eased noticeably in the March quarter. In part this was due to the sharp fall in fruit prices from the high levels that followed the floods and Cyclone Yasi a year ago, but it also reflected a broad-based easing in non-tradables and tradables inflation. In seasonally adjusted terms the consumer price index (CPI) fell by 0.2 per cent in the March quarter, to be 1.6 per cent higher over the year (Table 5.1, Graph 5.1). The various measures indicate underlying inflation was around ¼ per cent in the March quarter and between 2–2¼ per cent over the year (Graph 5.2). The recent run of quarterly data, while somewhat volatile, suggest that the momentum in underlying inflation has eased since the first half of 2011.

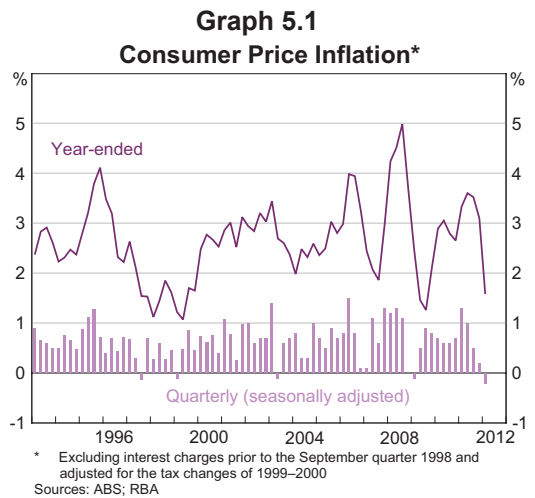


Table 5.1: Measures of Consumer Price Inflation
Per cent

	Quarterly ^(a)		Year-ended ^(b)	
	December quarter 2011	March quarter 2012	December quarter 2011	March quarter 2012
CPI	0.0	0.1	3.1	1.6
Seasonally adjusted CPI	0.2	-0.2	3.1	1.6
- Tradables	-1.0	-1.6	1.8	-1.5
- Tradables (excl food, fuel and tobacco)	-0.6	-0.9	-1.1	-1.7
- Non-tradables ^(c)	1.0	0.7	3.6	3.5
<i>Selected underlying measures</i>				
Trimmed mean	0.7	0.3	2.6	2.2
Weighted median	0.6	0.4	2.5	2.1
CPI excl volatile items ^{(c), (d)}	0.5	0.2	2.3	2.0

(a) Except for the headline CPI, quarterly changes are based on seasonally adjusted data

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

(c) Excludes deposit and loan facilities to June 2011

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

Sources: ABS; RBA

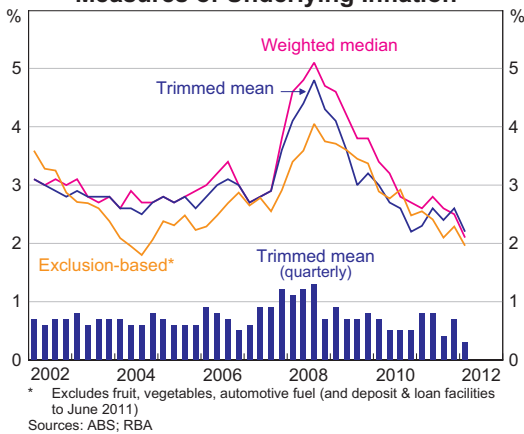
There was a modest easing in the quarterly pace of non-tradables inflation in the March quarter following relatively strong inflation in the December quarter. In seasonally adjusted terms, non-tradables prices rose by 0.7 per cent in the March quarter to be 3.5 per cent higher over the year (Graph 5.3). Although there were larger-than-usual increases in some administered prices, such as urban transport fares and secondary education fees, and quite strong rises in rents and financial services prices, these increases were partly offset by falls in the prices of domestic travel & accommodation and new dwellings. Liaison contacts in the residential

construction industry are reporting that pricing for new building work remains subdued as customers are reluctant to commit to purchases. Inflation in a broad range of other market services also slowed in the quarter.

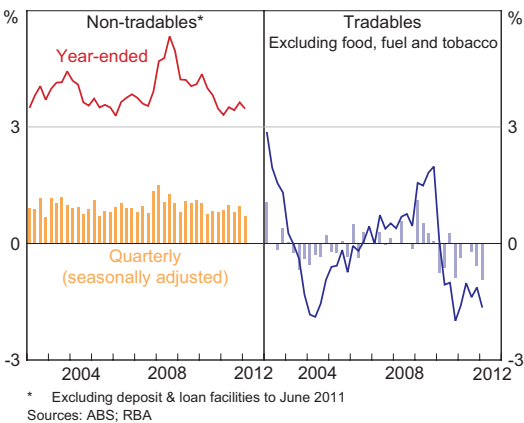
Tradables prices fell sharply in the March quarter, following a relatively large decline in the December quarter. Excluding food, fuel and tobacco, tradables prices declined by 0.9 per cent in the quarter to be 1.7 per cent lower over the year. The fall in the quarter was driven by large declines in the prices of audio visual & computing equipment and overseas travel & accommodation. There were also broad-based declines in the quarter across a range of consumer durables prices, including clothing, motor vehicles and furniture. The fall in durables prices over the past year was greater than implied by the historical relationship with the exchange rate, which is little changed from its level in early 2011. This suggests that there has been some compression of margins for these goods (Graph 5.4).

The decline in banana prices, following the recovery in supplies from the disruptions in early 2011, drove a further fall in food prices in the March quarter, with fruit prices falling by 26 per cent. Excluding fruit and vegetable prices, food price inflation remains subdued with prices rising by 1 per cent over the year

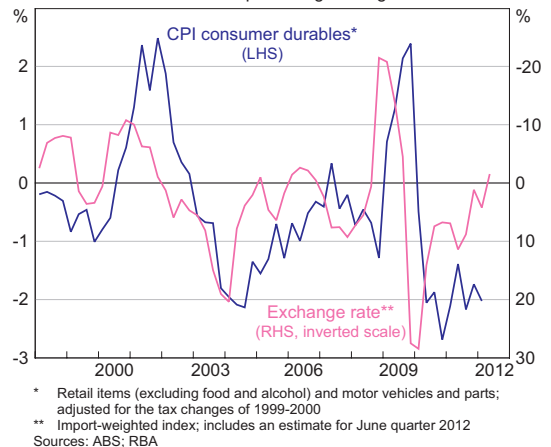
Graph 5.2
Measures of Underlying Inflation



Graph 5.3
Consumer Price Inflation

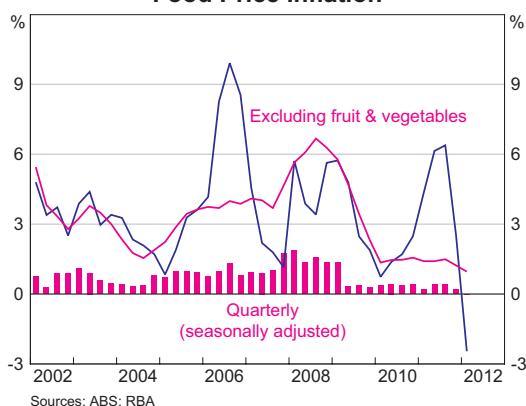


Graph 5.4
Consumer Prices and the Exchange Rate
Year-ended percentage change



(Graph 5.5). There has been relatively soft inflation in most grocery food items over recent years. This continued in the March quarter with prices falling in a range of grocery food categories including meat & seafood and some cereal-based items.

**Graph 5.5
Food Price Inflation**



Costs

The pace of aggregate wage growth appears to have moderated slightly over 2011. Private sector wage growth was little changed over 2011 despite soft momentum in employment growth. The private sector wage price index increased by 1 per cent in the December quarter, to be 3.8 per cent higher over the year (Graph 5.6). However, business surveys and the Bank's liaison with firms suggest a slight easing in private sector wage pressures in the March quarter (Graph 5.7). This is consistent with firms generally reporting that they are not experiencing significant difficulty finding suitable labour, except for in some mining-related industries and occupations.

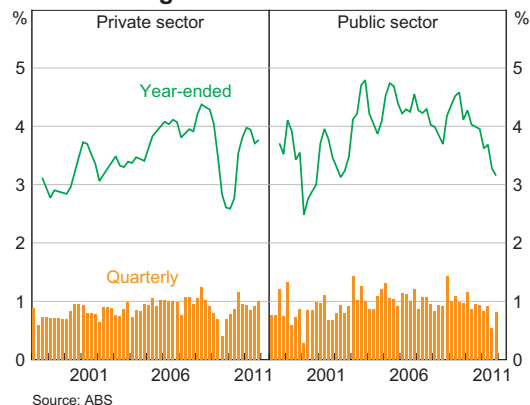
Public sector wage growth was relatively subdued over 2011. Although delays in the finalisation of new public sector enterprise agreements have likely overstated the extent of the slowdown in public sector wage growth, there is some genuine downward pressure on wage growth in the sector.

Data from the national accounts indicate that growth in unit labour costs – the average cost of labour per unit of output – has eased somewhat from the spike

in early 2011, owing to some recovery in labour productivity growth (Graph 5.8). Nonetheless, the growth of unit labour costs, as measured, remained relatively high over 2011. The national accounts measure of average hourly earnings grew by around 5¼ per cent over the year, partly reflecting strong average earnings growth in Western Australia.

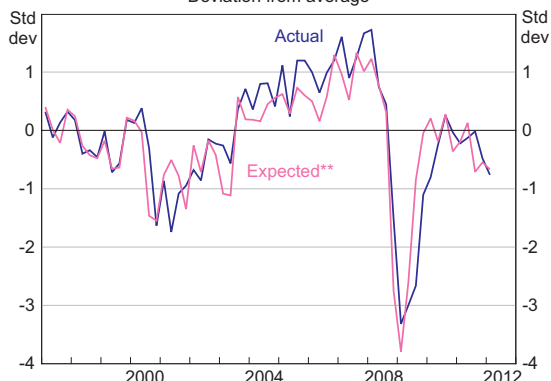
ABS data on industrial disputes – which capture stop-work meetings, strikes and employer-initiated lockouts – suggest that the number of disputes picked up slightly in the December quarter, although the number of working days lost nevertheless fell in the quarter. In 2011, there were 192 disputes, down from

**Graph 5.6
Wage Price Index Growth**



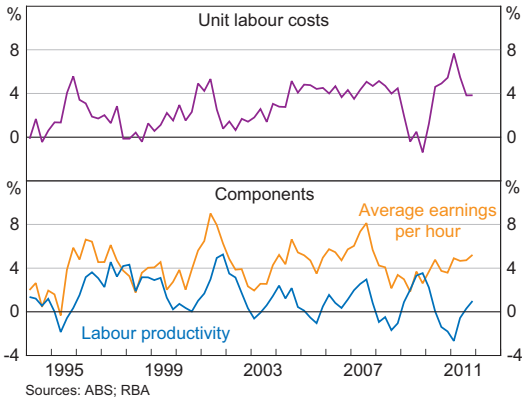
Source: ABS

**Graph 5.7
Surveys of Business Labour Costs***
Deviation from average



* Weighted average of data from various business surveys since 1994, with weights calculated by the RBA using the principal component method
** Expectation for following quarter
Sources: ACCI; NAB; RBA; Sensis

Graph 5.8
Unit Labour Costs Growth
Year-ended, non-farm



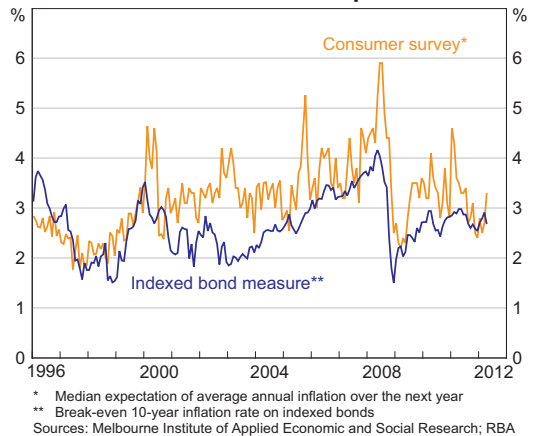
227 disputes in 2010. Working days lost picked up in 2011, compared with the low level in the previous few years, although days lost remained low relative to history.

Producer price data suggest that upstream price pressures eased further in the March quarter. Final-stage producer prices (excluding oil) fell slightly in the quarter, following a modest rise in the December quarter, to be 1.2 per cent higher over the year. The decline in the quarter was driven by falls in import and fruit prices. Abstracting from the large fall in fruit prices, final-stage domestic prices rose modestly, held down by further weakness in output price inflation for construction and manufacturing. Import prices fell at all stages of production, largely due to the small appreciation of the exchange rate in the quarter.

Inflation Expectations

Most measures of inflation expectations remain consistent with the Bank's target. Financial market expectations of inflation fell a little following the release of the March quarter inflation data after rising earlier in the year (Graph 5.9). Market economists and union officials have also revised down their forecasts for inflation over 2012 and 2013, with both groups expecting inflation to be around the middle of the target range over 2013 (Table 5.2). In contrast, the somewhat volatile measure of consumer inflation expectations for the year ahead rose to 3.3 per cent in April, although the survey took place before the release of the inflation data. Survey measures suggest that business expectations for near-term selling price inflation remain below average. ↕

Graph 5.9
Indicators of Inflation Expectations



* Median expectation of average annual inflation over the next year
** Break-even 10-year inflation rate on indexed bonds
Sources: Melbourne Institute of Applied Economic and Social Research; RBA

Table 5.2: Median Inflation Expectations^(a)
Per cent

	Year to December 2012			Year to December 2013	
	November 2011	February 2012	May 2012	February 2012	May 2012
Market economists	2.9	2.5	2.2	2.7	2.6
Union officials	3.4	3.0	2.3	3.0	2.5

(a) Excluding carbon price

Sources: RBA; Workplace Research Centre