

20 October 2022

September Quarter CPI Preview

Ongoing pressures offset by state energy rebates but it is only a temporary reprieve and does not lower core inflation.

- Westpac is forecasting a quite solid 1.1% print in the September quarter lifting the annual pace 0.4ppt to 6.5%. We also raised the peak in annual inflation to 7.7%yr at the December quarter 2022 from the current published forecast of 7.5%.
- The reason for the step down from 1.8%qtr print in Q2 are the significant state energy rebates, particularly in WA and Victoria. Due to these rebates, utility cost are forecast to fall 10.5% subtracting 0.48ppt from the September quarter CPI.
- Without the electricity rebates our CPI forecast would have been 1.8%.
- The Trimmed Mean is forecast to lift 1.5% in September, matching the March and June quarters, taking the annual pace to 5.6%yr from 4.9%yr well up from the March 2021 low of 1.1%yr. Our forecast peak is 5.8%yr in December 2022.
- The ABS provided July and August data for the new Monthly CPI Indicator. While there are issues with converting a monthly series, based on data collected for a quarterly series, to a quarterly series, it does appear to be a helpful guide to the components of the CPI where there are no alternative sources of information. We have used the Indicator to help guide our

fine tuning of components of the September quarter CPI.

- An important note: electricity prices are only measured in the last month of each quarter and so the Monthly CPI Indicator couldn't provide an update on electricity prices. For more information on the Monthly CPI Indicator, and what it does and does not provide in regards to the quarterly CPI, please see ["Australian Monthly CPI Indicator First Release"](#).
- This is a significant issue in September due not just to the reported significant increase in power bills but also the various state government electricity rebates. As shown by WA in 2020 the rebates impact can be significant. Westpac is forecasting electricity prices to fall 17% in the quarter, due to the rebates, then expecting a 40% bounce back in the December quarter. A 17% fall in electricity prices contributes -0.45ppt to the CPI.
- Without the rebates we estimate electricity prices would have lifted a bit more than 8% in the quarter contributing 0.22ppt to the CPI.
- Other key factors in our forecast are: food +2.3%, dwellings +4.0%, household contents & services +2.4%, auto fuel -4.7%, and domestic holidays +10%.

September CPI forecast

Item	Sep 2022 fc		Jun 2022	
	% qtr	contrib	% qtr	contrib
Food	2.3	0.39	2.0	0.34
of which, fruit & vegetables	4.9	0.12	5.8	0.13
Alcohol & tobacco	1.8	0.17	0.8	0.07
of which, tobacco	1.9	0.07	1.0	0.04
Clothing & footwear	-0.2	-0.01	3.5	0.12
Housing	0.4	0.03	2.5	0.58
of which, rents	1.0	0.07	0.7	0.04
of which, house purchases	4.0	0.33	5.6	0.50
of which, utilities	-9.1	-0.48	-0.2	-0.01
H/hold contents & services	2.4	0.22	2.5	0.23
Health	0.3	0.02	0.4	0.03
of which, pharmaceuticals	-0.9	-0.01	-1.1	-0.01
Transportation	-0.5	-0.05	2.3	0.25
of which, car prices	2.1	0.05	1.2	0.04
of which, auto fuel	-4.7	-0.17	4.2	0.14
Communication	-0.2	-0.01	0.1	0.00
Recreation	3.3	0.28	1.4	0.12
of which, audio vis & comp	0.7	0.01	1.2	0.02
of which, holiday travel	9.8	0.21	2.3	0.05
Education	0.0	0.00	0.0	0.00
Financial & insurance services	0.6	0.03	1.1	0.06
CPI: All groups	1.1	-	1.8	-
CPI: All groups % year	6.5	-	6.1	-

Sources: ABS, RBA, Westpac Banking Corporation.

Quarterly CPI forecast vs Monthly Indicator

Item	Sep 22	Jun	Jul	Aug
	Qtr % yr	Mth % yr	Mth % yr	Mth % yr
Food	8.0	6.4	7.8	9.3
of which, meat & seafood	7.6	6.5	7.3	7.3
of which, fruit & vegetables	16.6	9.1	14.5	18.6
Alcohol & tobacco	4.6	2.3	2.8	4.1
of which, Alcohol	3.6	1.4	1.7	3.4
of which, Tobacco	6.4	3.7	4.2	5.2
Clothing & footwear	5.3	1.8	4.0	4.3
Housing	7.5	9.3	9.9	9.5
of which, Rents	2.4	1.6	2.1	2.4
of which, House purchases	21.0	21.0	22.0	20.7
of which, Utilities	-8.0	NA	NA	NA
H/hold contents & services	7.2	6.2	7.3	7.5
Health	2.7	2.5	2.6	2.6
of which, Pharmaceuticals	2.2	NA	NA	NA
Transportation	9.1	16.4	12.3	8.5
of which, car prices	6.2	NA	NA	NA
of which, auto fuel	17.5	43.3	29.2	15.0
Communication	0.3	-0.1	-0.1	1.6
Recreation	7.0	4.9	5.9	3.0
of which, audio/vis & com	2.5	NA	NA	NA
of which, holiday travel	17.4	8.6	14.0	3.5
Education	4.6	4.6	4.6	4.6
Financial & insurance services	3.4	3.3	3.4	3.5
CPI: All groups % year	6.5	6.8	7.0	6.8

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June quarter inflation recap

The June CPI gained 1.8%qtr, splitting the difference between the market median of 1.9% and Westpac's forecast of 1.7%. This increase was the second highest since the introduction of the GST and follows on from a 2.1% increase in the March quarter. The annual pace lifted from 5.1% to 6.1%, the fastest pace since the introduction of the GST and significantly stronger than the mining boom peak of 5.0%yr in 2008. The impact of the unwinding of the HomeBuilder grants was there but the more important story was the shortages of building supplies and labour, heightened freight costs and strong demand on dwelling prices – these factors were also significant for the broader inflationary pulse. This inflationary pulse was captured by 1.5% gain in the trimmed mean while the March quarter trimmed mean was revised from 1.4% to 1.5%. The annual pace of the trimmed mean lifted from 3.7%yr in March to 4.9%yr in June, the fastest pace since September 1991 (using the RBA's historical estimates). The ABS also reported that annual goods inflation was the highest since 1987, due to supply disruptions, rising shipping costs and other global/domestic inflationary factors.

Food prices remain under pressure

Distribution disruptions may have eased somewhat but they remain an additional complexity along with flooding and significant labour shortages which continue to disrupt farm production. While market prices did ease in the month of September it was not enough to full offset earlier gains hence our +4.9% forecast for fruit & vegetables. The Monthly Indicator suggested that price pressures also continued for meat & seafood.

Food forecast is 2.3% contributing 0.39ppt.

Alcohol and tobacco

The tobacco excise rose 1.2% in the month of September so only applied for one of the three months of the quarter. Two thirds of this increase will appear in the December quarter. To August, tobacco in the Monthly Indicator gained 5.2% in the year. Our current forecast is for a 6.4% rise in the year to the Q3. Our Q3 forecast lifts alcohol prices 3.6% in the year, the Monthly Indicator has alcohol prices up 3.4% in the year to August.

Alcohol & tobacco forecast is 1.8% contributing 0.17ppt

Seasonal discounting of clothing & footwear prices

End of financial year sales remain a significant event in Australia so prices for clothing & footwear tend to fall in the September quarter. The introduction of Black Friday sales in November have started to change seasonality in clothing & footwear prices but prices still tend to fall in early Q3. Our 0.2% fall in Q3 has clothing & footwear prices up 5.3% in the year compared to the 4.3%yr at August from the Monthly Indicator.

Clothing & footwear forecast is -0.2% contributing -0.01ppt.

Housing costs have temporary offset via energy rebates

There has been a marked lift in asking rents pointing which will, with time, feed into total average rents in the CPI. The CPI measures all rents paid, not just new contracts, and includes public and defence housing which tend to be more stable. Hence, the volatility in CPI rents is a bit less than half that seen in asking rents. As such we see rents lifting in NSW and Vic adding to the current momentum seen in Qld and WA. In the year to Q3 rents are forecast to be up 2.4%yr compared to the 2.4%yr rise in Monthly Indicator rents to August.

Rents forecast is 1.0% contributing 0.07ppt.

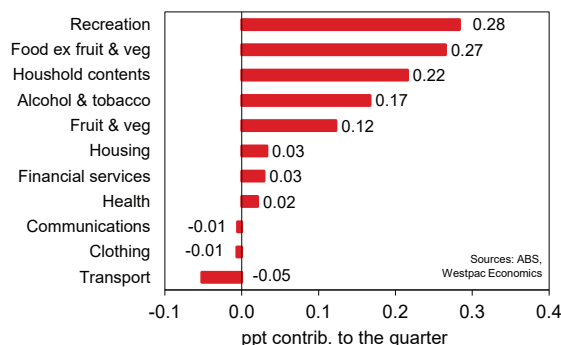
Inflation indicators

		Jun-22	Sep-22	Dec-22	Mar-23	Jun-23
AUD/USD	(index)	0.71	0.68	0.66	0.66	0.67
AUD/USD %yr	(%yr)	-7.2	-7.0	-10.0	-9.4	-6.7
TWI	(index)	62.7	63.3	64.0	64.7	64.6
TWI %yr	(%yr)	-1.3	3.5	4.1	5.8	3.0
Brent US\$bbl	(index)	110	95	86	84	86
Brent %yr	(%yr)	60.3	31.7	9.4	-12.4	-22.0
Output gap t-3	(index)	2.2	1.6	0.9	0.3	-0.1

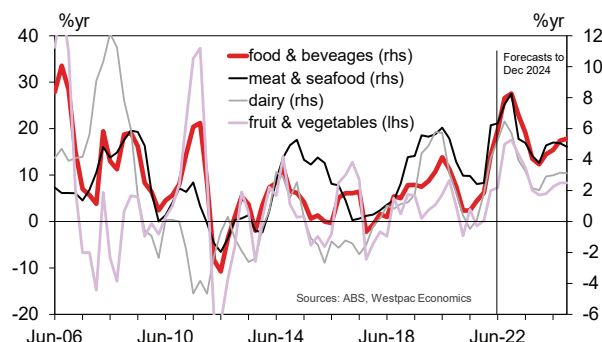
Inflation forecasts

		Sep-22	Dec-22	Mar-23	Jun-23	Sep-23
CPI	(index)	127.5	130.7	131.9	132.9	134.1
	(%qtr)	1.1	2.5	0.9	0.8	0.9
	(%yr)	6.5	7.7	6.5	5.4	5.2
Trimmed mean	(%qtr)	1.5	1.3	0.8	0.7	0.9
	(%yr)	5.6	5.8	5.1	4.4	3.7

Contributions 2022Q3 CPI 1.1%qtr forecast



Food inflation to remain elevated



Through 2021, Commonwealth HomeBuilder grants plus WA and Tasmanian state government grants provided a significant offset for the purchase of a new dwelling, thus suppressing dwelling prices in the CPI as the grants were used. As the use of grant started to fade, this affect was reversed and dwelling prices started to rise more rapidly than underlying prices as prices paid lifted back towards contracted prices. Through the last four quarters, CPI dwelling prices lifted 3.3%, 4.2%, 5.7% and 5.6% in Q3 21, Q4 21, Q1 22 and Q2 22. Underlying dwelling prices before the application of grants increased 3.0%, 3.6%, 4.4% and 5.2%, highlighting how dwelling price lifted more each quarter as less grants were used each quarter and the measured prices moved to be closer to contracted prices.

For the September quarter the Monthly Indicator highlights a surprising moderation in dwelling price inflation. The annual price lifted from 21.0%yr in June to 22.0%yr in July before moderating to 20.7% in August. This led us to moderate our Q3 forecast from 6.4% to 4.0% in the quarter which would have dwelling prices up to 21.0% in the year to the September quarter. We propose this increase would be composed of a 2.6% increase in underlying dwelling prices, a moderation from 5.2% in Q2, and a 1.4ppt contribution from the unwinding grants effect with dwelling prices now in line with contract prices.

Dwelling forecast is 4.0% contributing 0.33ppt.

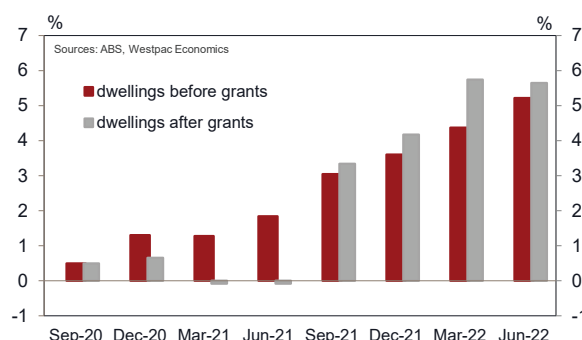
As we covered in our report [“Energy prices driving an outsized price shock”](#) the Australian energy market has been hit by a perfect storm of rising demand, less output from coal fired base load generation plus record high coal and gas prices. There has been a surge in low cost renewable energy but it has not been enough to offset the loss of coal fired generation nor the rise in gas and coal prices plus the demand for further investment in energy storage and distribution. This resulted in a significant increase in the Default Market Offers (DMO) around the country but many states have offset this increase with energy rebates. This increase in DMO, and temporary energy rebates, is set to add significant volatility to our CPI forecast through the September quarter (as the rebates are applied to household bills) and again in the December quarter (as the bills return to normal).

There is a fair bit of variation in how the rebates are applied. In WA and Victoria the grants are open to all local residents. WA is offering a \$400 rebate against an annual average bill of \$1,990. This represents an 80% rebate on a quarterly bill of \$497 before we apply the 5% increase in the DMO. Back in December 2020, when the state government offered a similar rebate in WA, electricity prices fell 67% in Perth. The Victorian rebate is a bit less generous, \$250 compared to a \$1,220 annual bill, which is a 71% rebate against a \$350 quarterly bill. Again, this is before the 5% increase in the DMO.

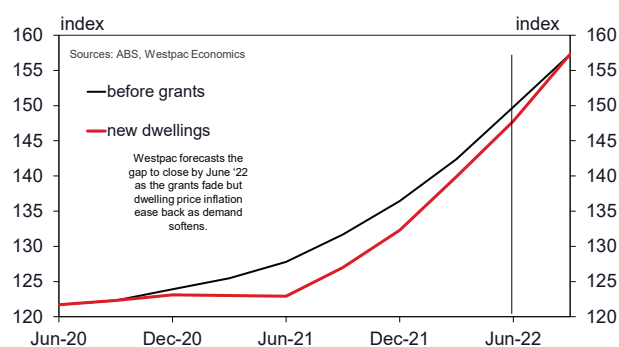
From there it gets a bit more confusing and less generous. In Qld the rebate is \$175 but it is only available to those with social security cards. As such it won't have as dramatic impact on electricity bills. The rebate is worth 47% of the quarterly energy bill but of course the impact will be much less due to it being restricted to those registered for social welfare. The DMO is set to increase by around 11% in Qld.

In NSW the rebate is \$180 which is worth 39% of the \$462 quarterly energy bill. However, it is restricted to first home buyers so its impact will be very limited. The DMO is set to increase by around 12% in NSW in Q3.

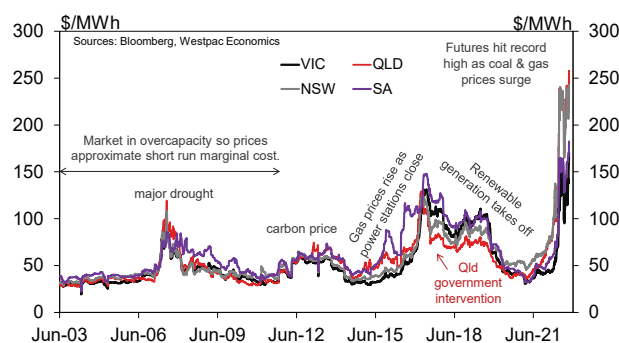
Grants were disinflationary, now inflationary



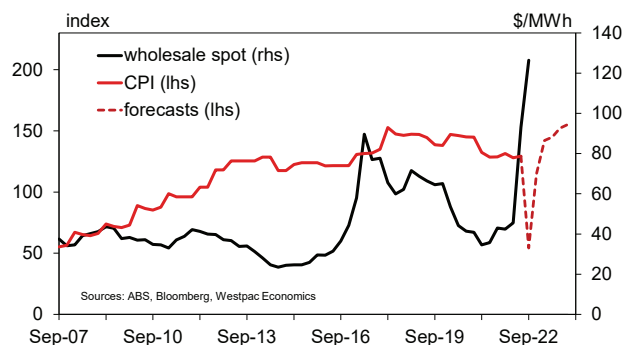
As grants fade dwelling prices lift



Electricity futures



Melbourne - wholesale vs. CPI electricity



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Given different rules around application of state electricity rebates it is tricky to be definitive on just what impact they will have. Nevertheless, as shown by WA in 2020 the rebates impact can be significant. Westpac is forecasting electricity prices to fall 17% in the quarter due to the rebates, then we are expecting a 40% bounce back in the December quarter. A 17% fall in electricity prices contributes -0.45ppt to the CPI.

Without the rebates we estimate electricity prices would have lifted a bit more than 8% in the quarter contributing 0.22ppt to the CPI.

Overall housing forecast is 0.4% contributing 0.03ppt.

Furnishings, household goods & services prices

Price pressures continue to build in domestic & housing services (childcare, hairdressing and other household services). However, the September quarter is also when the end of financial year sales have their largest impact on household goods and appliances. The Monthly Indicator has the annual pace of household good at services at 6.2%yr in June, 7.3%yr in July and 7.5% in August. Our 2.4% forecast for the September quarter will see prices up 7.2% in the year.

Household contents & services forecast is 2.4% contributing 0.22ppt.

PBS starts to offset rising health costs

Pharmaceutical prices are to have their usual seasonal fall as families health expenditure starts to exceed the threshold to qualify for support under the Pharmaceutical Benefit Scheme (PBS). We are forecasting a 0.9% fall in pharmaceuticals but overall health costs are forecast to rise 0.3% to be up 2.7%yr. The monthly indicator has health costs up 2.5%yr in June, 2.6%yr in July and 2.6%yr in August.

Health costs forecast 0.3% contributing 0.02ppt.

Rising fuel and motor vehicles push transport costs

The Ukraine crisis represented a significant shock to global energy markets with crude prices peaking just under US\$125/bbl in early March before prices have stabilised around US\$100/bbl by the end of the month. In the March quarter there was the offsetting temporary halving of the fuel excise (worth 22.2 cents a litre) but there was a rally in crude back up to US\$120/bbl by early June. The temporary cut to the excise ended on the 30th of September so will have a meaningful impact in the December quarter but no impact in the September quarter.

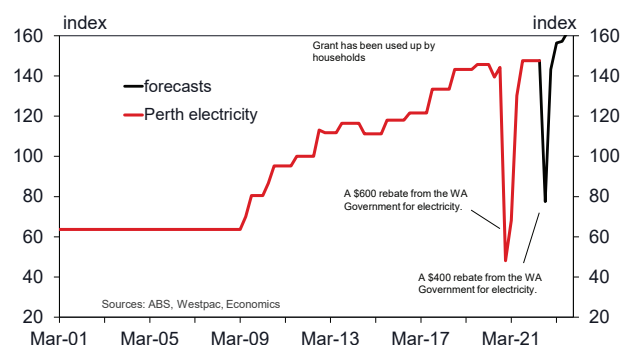
With markets starting to focus on rising interest rates, a stronger US dollar and risks of a recession, crude prices fell back below US\$100/bbl in the September quarter which was reflected in falling pump prices for petrol. While the weaker AUD has boosted Australian petrol prices overall, softer crude prices have seen petrol prices fall in the quarter. Our 4.7% fall in auto fuel prices will still have them up 17.5% in the year which compares Monthly Indicator estimate of 43.3%yr in June, 29.2%yr to July and 15.0%yr to August.

Transport forecast -0.5% contributing -0.05ppt.

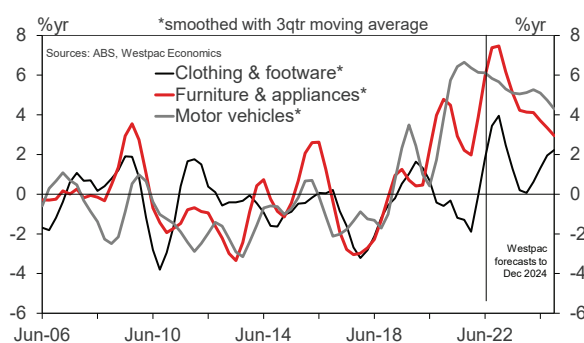
Recreation & culture rebounds from lockdowns

State borders reopened in early 2022 with the international borders doing so a bit later. With no further lockdowns in any capital city, tourism activity has surged for both the domestic and international sectors. We now have the normal price gathering for both domestic and international travel & holidays

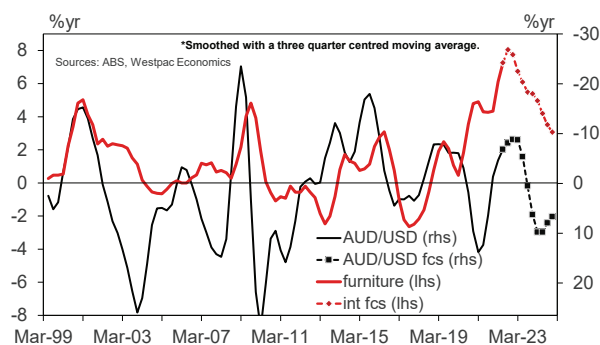
WA electricity rebates return



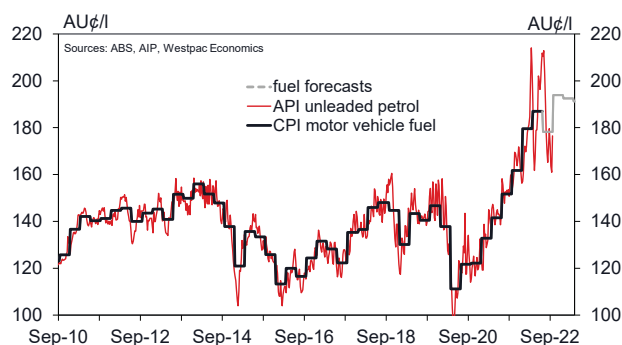
Durable inflation has some strength



Furniture & furnishings vs. the currency*



Weekly bowser price & CPI auto fuel



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following a period where the ABS had imputed price changes for this sector based on the overall CPI. Best air fare data suggests prices surged higher in the September quarter while the average fare pointed to a more modest but still solid gain. We also use the NZ CPI domestic air transport series, adjusted for the exchange rate, as a guide to domestic tourism inflation and it is pointing to an out sized surge in the September quarter. We are forecasting a 10% rise in the quarter.

The weight for international travel is just 0.07% of the CPI reflecting the lack of international travel through the Covid period. As such it has does not have a meaningful impact the CPI but we expect this change through 2022 with the return of international travel. Our forecast for the September quarter is up 4.0%.

All up we see holiday travel prices lifting 9.8% in the quarter to be up 17.4%yr. Compare this to the Monthly Indicator which had holiday prices up 8.6%yr in June, 14.0%yr in July and 3.5%yr in August. For this quarter we have focused on the other indicators, rather than the Monthly Indicator, as we are still waiting for the September update and being a school holiday month a sizable jump in prices is likely.

Recreation & culture forecast is 3.3% contributing 0.28ppt.

Widespread inflationary pressures boosting core inflation

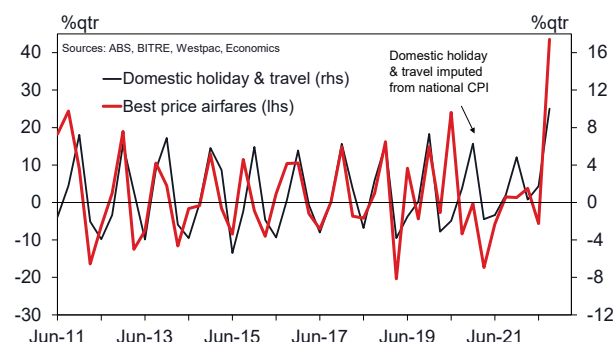
The Trimmed Mean is forecast to rise 1.5% matching the rise in the June and March quarters; the March quarter had been revised from an original estimate of 1.4%.

Recall that the prices that are seasonally adjusted in the core measures and trimmed off the top are; domestic holiday travel & accommodation (10.4%), fruit (10.2%), vegetables (6.2%), new dwelling purchases (4.0%) and tobacco (3.5%). The top of the range that is still in the trimmed mean is between 2.9% and 3.5%. Trimmed off the bottom; electricity (-19.8%), automotive fuel (-4.7%), postal services (-0.4%), footwear for women (-0.1%), footwear for men (-0.1%), garments for infants & children (0.0%), international holiday travel & accommodation (0.0%), garment for women (0.0%), other food products (0.0%), footwear for infants & children (0.0%), audiovisual & computing equipment (0.0%), water & sewerage (0.1%), telecommunication equipment (0.1%) and audio visual & computing (0.2%). The bottom trim starts at a quite high between 0.2% and 0.3%.

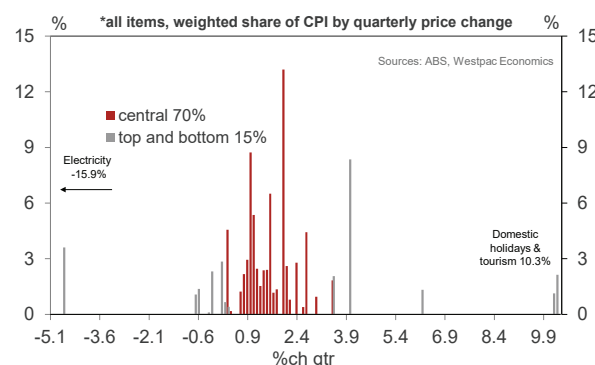
A 1.5% rise in the Trimmed Mean will see the annual pace lift from 4.9%yr to 5.6%yr; the two quarter annualised pace lifts from 6.0%yr to 6.1%yr. Our expectations are that the annual pace of core inflation is likely to peak at around 5.8%yr in the December quarter of 2022, the fastest annual pace since early 1990s.

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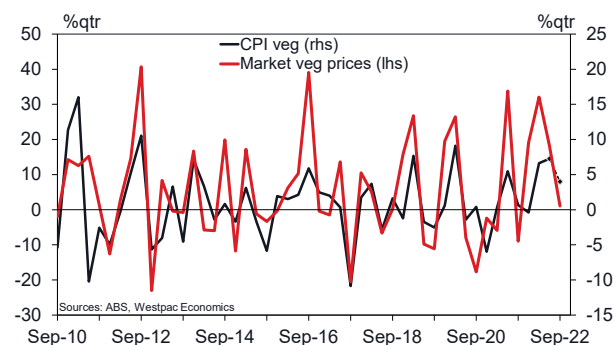
Domestic holidays & travel



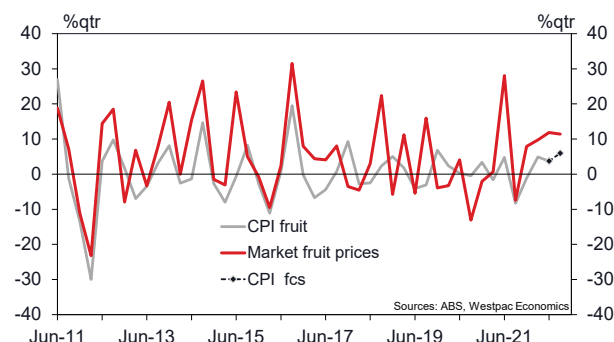
Distribution of seasonally adjusted Q3 CPI fcs



Vegetable prices, wholesale & CPI



Fruit prices, wholesale & CPI



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