

20 July 2023

June Quarter CPI Preview

Power rebates holding down inflation while goods prices continue to rise.

- Westpac is forecasting a 1.1% rise in the June quarter taking the annual pace down 0.7ppt to 6.3%yr from 7.0%yr. We believe that December was the peak for annual inflation in this cycle and the pace is expected to continue to moderate from here.
- The biggest reason for a further step down from the 1.9%qtr print in Q1, and the 1.4% print in Q4, is the moderation in housing costs from a 1.9% rise in March to a 0.9% rise in June, with the contribution falling 0.24ppt to 0.22ppt.
- The moderation in housing inflation is due to state government rebates driving down electricity prices in the quarter. The contribution from utilities falls from 0.22ppt in March to -0.05ppt in June. This more than offsets the acceleration in rent inflation.
- There is also the usual seasonal moderation in health costs as families cross the expenditure threshold for the Pharmaceuticals Benefits Scheme. The contribution from health falls from 0.24ppt in March to 0.04ppt in June.
- March also saw the usual annual increase in education prices which contributed 0.25ppt to the CPI. This increase won't occur again until the March quarter of 2024.
- The Trimmed Mean is forecast to lift 1.1% in June, a moderation from the gains in March (1.2%), December (1.7%) and September (1.9%). The annual pace for the Trimmed Mean is set to moderate from 6.6%yr to 6.0%yr. We see the 6.9%yr pace in December 2022 as the peak in that measure in core inflation.
- The Monthly CPI Indicator is turning out to be a very helpful guide to the components of the CPI and we have used the data from the April and May surveys to fine tune our forecasts.
- Despite the additional information provided by the Monthly CPI Indicator, there are still many significant unknowns we have to estimate.
- Overall, the June quarter CPI is set to confirm that inflationary pressures peaked in late 2022 and continues to moderate as we move through 2023. However, it will also continue to highlight that core inflation remains significantly above the top of the RBA's target band and is not likely to return to being within the band any time soon.

June Quarter CPI forecast

| Item | June 2023 f/c | | Mar 2023 | |
|---|---------------|---------|----------|---------|
| | % qtr | contrib | % qtr | contrib |
| Food | 1.8 | 0.31 | 1.6 | 0.27 |
| of which, fruit & vegetables | 2.8 | 0.07 | 2.4 | 0.06 |
| Alcohol & tobacco | 1.3 | 0.11 | 1.1 | 0.10 |
| of which, tobacco | 1.3 | 0.05 | 0.5 | 0.02 |
| Clothing & footwear | 2.0 | 0.07 | -2.6 | -0.09 |
| Housing | 0.9 | 0.22 | 1.9 | 0.46 |
| of which, rents | 2.4 | 0.14 | 1.6 | 0.09 |
| of which, house purchases | 1.2 | 0.11 | 1.2 | 0.11 |
| of which, utilities | -1.2 | -0.05 | 5.2 | 0.22 |
| H/hold contents & services | 2.4 | 0.22 | -0.5 | -0.04 |
| Health | 0.7 | 0.04 | 3.8 | 0.24 |
| of which, pharmaceuticals | -1.1 | -0.01 | 4.5 | 0.05 |
| Transportation | 0.7 | 0.08 | 0.6 | 0.07 |
| of which, car prices | 1.0 | 0.03 | 1.8 | 0.06 |
| of which, auto fuel | 0.5 | 0.02 | -0.8 | -0.03 |
| Communication | 0.6 | 0.01 | 0.1 | 0.00 |
| Recreation | -0.4 | -0.03 | 0.2 | 0.02 |
| of which, audio vis & comp | 0.4 | 0.01 | 1.1 | 0.02 |
| of which, holiday travel | -2.0 | -0.04 | -0.7 | -0.02 |
| Education | 0.0 | 0.00 | 5.3 | 0.25 |
| Financial & insurance services | 2.5 | 0.14 | 1.9 | 0.11 |
| CPI: All groups | 1.1 | - | 1.4 | - |
| CPI: All groups % year | 6.3 | - | 7.0 | - |

Sources: ABS, RBA, Westpac Banking Corporation.

Quarterly CPI forecast vs Monthly Indicator

| Item | June 23 | Apr | May | Jun |
|---|-----------|-----------|-----------|---------------|
| | Qtr % qtr | Mth % mth | Mth % mth | Mth f/c % mth |
| Food | 1.8 | 0.2 | 1.0 | 0.6 |
| of which, bread & cereals | 3.5 | 1.7 | 1.7 | 0.1 |
| of which, meat & seafood | 0.8 | 0.2 | 0.4 | 0.2 |
| of which, dairy & related prod. | 0.9 | 0.2 | -0.2 | 0.8 |
| of which, fruit & vegetables | 2.8 | -0.7 | 1.4 | 2.2 |
| of which, food products nec | 1.0 | 0.4 | -0.2 | 0.9 |
| of which, non-alcohol bev, | 3.1 | 2.0 | -0.1 | 1.1 |
| Alcohol & tobacco | 1.3 | 0.1 | 0.1 | 1.1 |
| of which, Alcohol | 1.3 | -0.1 | 0.1 | 1.3 |
| of which, Tobacco | 1.3 | 0.7 | -0.2 | 0.8 |
| Clothing & footwear | 2.1 | 1.9 | -1.9 | 2.1 |
| of which, Garments | 4.1 | 3.9 | -3.2 | 3.4 |
| Housing | 0.9 | 0.3 | 0.3 | 0.3 |
| of which, Rents | 2.4 | 0.8 | 0.8 | 0.8 |
| of which, House purchases | 1.2 | 0.5 | 0.4 | 0.3 |
| of which, Electricity | -2.0 | -0.9 | -0.8 | -0.3 |
| H/hold contents & services | 2.4 | 1.5 | 0.3 | 0.7 |
| Health | 0.7 | 0.1 | 0.0 | 0.5 |
| Transportation | 0.7 | 0.9 | -2.0 | 2.2 |
| of which, auto fuel | 0.5 | 2.9 | -6.7 | 6.4 |
| Communication | 0.5 | -0.7 | 0.8 | 0.5 |
| Recreation | -0.4 | 2.8 | -4.4 | 2.7 |
| of which, holiday travel | -2.0 | 7.2 | -11.3 | 9.8 |
| Education | 0.0 | 0.0 | 0.0 | 0.0 |
| Financial & insurance services | 2.5 | 0.0 | 1.1 | 1.3 |
| CPI: All groups %qtr/%mth | 1.1 | 0.8 | -0.4 | 1.0 |

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March quarter inflation recap

The March quarter CPI rose 1.4% as per the Westpac forecast (market median was 1.3%); the Trimmed Mean was softer than expected lifting 1.2% vs. Westpac's 1.4% forecast. Annual inflation eased back to 7.0%yr from 7.8%yr which was the fastest pace since March 1990. It is increasingly clear that the December quarter 2022 was the peak in current inflationary cycle. Trimmed Mean inflation eased back to 6.6%yr from 6.9%yr in December, the fastest pace since December 1988 and above the RBA's earlier forecast peak of 6.5%yr. However, just like headline inflation, it appears that core inflationary pressures peaked at the end of 2022.

The more modest rise in the Trimmed Mean highlighted a disinflationary force, particularly for goods, that is greater than we had thought. While services inflation is holding up, and is likely to prevent inflation falling back within the band in 2023 (and even in 2024 as per our current forecasts), it is not enough to prevent goods disinflation taking the annual pace of headline inflation close to the top of the band by the first half of 2024.

The most significant contributors to the March quarter rise were medical & hospital services (+4.2%), tertiary education (+9.7%), gas & other household fuels (+14.3%) and domestic holiday travel & accommodation (+4.7%). Partially offsetting the rise was international holiday travel & accommodation (-8.2%), as some destinations entered their off-peak seasons following significant rises in recent quarters. Also discounting by retailers resulted in falls across furniture (-4.6%), major & small appliances (-3.8%) and clothing (-3.2%).

Food inflation is steady

The CPI Monthly Indicator provides a detailed breakdown of many of the components in food, giving us with the best leading indicator of food prices we have to date. This data includes estimates for restaurants and take away food which are only surveyed once each quarter. Bread & cereals are experiencing the strongest growth (3.5%qtr) followed by non-alcohol beverages (3.1%qtr) with fruit & vegetables not far behind (2.8%qtr),

Food forecast is 1.8% contributing 0.31ppt.

Alcohol & tobacco step up

The data to May was on the soft side, with a reported fall in tobacco prices in the month of May, making an allowance for a recovery in prices in June based on a slightly stronger than usual seasonal margin recovery.

Alcohol & tobacco forecast is 1.3% contributing 0.11ppt

Seasonal recovery in clothing & footwear

A number of components within clothing & footwear are only surveyed once a quarter, and that occurs in the first month the quarter. So we have a lot of the data already for this group. We only have to estimate the month of June for men and women's garments.

Clothing & footwear forecast is 2.0% contributing 0.07ppt.

Housing costs moderating as electricity prices fall

Rental costs continue to tick along at 0.8% per month, and we expect this to occur again in June. Dwelling purchase price inflation continues to moderate, rising 0.5% in April, 0.4% in May and we are looking for a 0.3% rise in June.

Rents forecast is 2.4% contributing 0.14ppt.

Dwellings forecast is 1.2% contributing 0.11ppt.

Quarterly CPI forecast vs Monthly Indicator

| | June 23 | Apr | May | Jun |
|---|------------|------------|-------------|------------|
| | Qtr | Mth | Mth | Mth fc |
| Item | % yr | % yr | % yr | % yr |
| Food | 7.7 | 7.9 | 7.9 | 7.7 |
| of which, bread & cereals | 12.2 | 11.4 | 12.8 | 11.5 |
| of which, meat & seafood | 4.2 | 4.4 | 3.8 | 3.9 |
| of which, dairy & related prod. | 14.4 | 14.5 | 15.1 | 15.1 |
| of which, fruit & vegetables | 2.0 | 3.5 | 2.7 | 2.1 |
| of which, food products nec | 11.2 | 11.7 | 11.5 | 11.1 |
| of which, non-alcohol bev, | 9.5 | 9.7 | 9.2 | 10.2 |
| Alcohol & tobacco | 5.0 | 4.8 | 4.7 | 5.9 |
| of which, Alcohol | 5.3 | 5.1 | 5.0 | 6.6 |
| of which, Tobacco | 4.4 | 4.3 | 4.1 | 4.8 |
| Clothing & footwear | 1.8 | 2.0 | -0.4 | 3.2 |
| of which, Garments | 2.9 | 3.5 | -0.6 | 5.3 |
| Housing | 8.2 | 8.9 | 8.4 | 7.7 |
| of which, Rents | 6.6 | 6.1 | 6.3 | 7.2 |
| of which, House purchases | 8.0 | 9.2 | 8.3 | 6.7 |
| of which, Electricity | 13.2 | 15.2 | 14.1 | 10.8 |
| H/hold contents & services | 6.6 | 6.3 | 6.0 | 7.0 |
| Health | 5.7 | 4.7 | 4.7 | 5.6 |
| Transportation | 2.7 | 7.1 | 0.8 | 0.3 |
| of which, auto fuel | -2.5 | 9.5 | -8.0 | -8.4 |
| Communication | 1.6 | 0.2 | 1.1 | 2.2 |
| Recreation | 6.6 | 6.4 | 3.5 | 4.7 |
| of which, holiday travel | 12.2 | 11.9 | 7.3 | 11.7 |
| Education | 5.4 | 5.5 | 5.5 | 5.5 |
| Financial & insurance services | 8.0 | 6.7 | 7.8 | 8.0 |
| CPI: All groups %qtr/%mth | 6.3 | 6.8 | 5.6 | 5.8 |

Inflation indicators

| | | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 |
|----------------|---------|--------|--------|--------|--------|--------|
| AUD/USD | (index) | 0.68 | 0.67 | 0.68 | 0.69 | 0.70 |
| AUD/USD %yr | (%yr) | -5.5 | -6.4 | 0.1 | 4.9 | 2.8 |
| TWI | (index) | 61.4 | 60.4 | 62.2 | 61.7 | 62.6 |
| TWI %yr | (%yr) | 0.3 | -3.6 | -0.8 | 0.1 | 2.0 |
| Brent US\$bbl | (index) | 82 | 78 | 77 | 76 | 81 |
| Brent %yr | (%yr) | -14.2 | -29.3 | -19.8 | -13.0 | -1.2 |
| Output gap t-3 | (index) | 0.31 | -0.13 | -0.40 | -0.48 | -0.57 |

Inflation forecasts

| | | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 |
|--------------|---------|--------|--------|--------|--------|--------|
| CPI | (index) | 132.6 | 134.1 | 135.3 | 136.4 | 137.6 |
| | (%qtr) | 1.4 | 1.1 | 0.9 | 0.8 | 0.9 |
| | (%yr) | 7.0 | 6.3 | 5.4 | 4.3 | 3.8 |
| Trimmed mean | (%qtr) | 1.2 | 1.1 | 0.8 | 0.9 | 0.8 |
| | (%yr) | 6.6 | 6.0 | 4.9 | 4.1 | 3.7 |

As we covered in our earlier report “[Energy prices driving an out-sized 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. Low cost renewable energy production has surged but it has not been enough to fully 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.

The surprise in the last two Monthly CPI Indicators has been the reported fall in electricity prices. This would be due to the various state rebates kicking in and this resulted in electricity falling 0.9% in April then down a further 0.8% in May. We have pencilled in a smaller 0.3% fall in June but clearly there is a risk the fall could be larger. The recently announced increase in the DMO will be applied from July and so will impact on the September quarter CPI, not the June quarter. Gas & other household fuels are not surveyed until the last month of the quarter so we don't have any guide on this series.

Utilities forecast is -1.2% contributing -0.05ppt.

Overall housing forecast is 0.9% contributing 0.22ppt.

Furnishings, household goods & services

As with clothing, a large share of this group is surveyed only once in a quarter, and again, it is during in the first month of each quarter; thus we have quite a good lead on this group. We need to make a June estimate for non-durable household products as they are surveyed monthly and while we have the quarterly estimates for hairdressing and other household services, the critical child care group is surveyed in the last month of the quarter – this has the potential to be a real wild card over the next few quarters as we are hit by the contrasting forecast of rising costs vs. increasing subsidies.

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

The reset to PBS will see the usual Q1 surge in health costs

Pharmaceutical prices should experience their usual seasonal fall in prices as families health expenditure on health crosses the threshold to qualify for support under the Pharmaceutical Benefit Scheme (PBS). However, most of this group is only surveyed in the last month of the quarter so the Monthly CPI does not provide us with any guidance.

Health costs forecast 0.7% contributing 0.04ppt.

Bounce in fuel prices underpinning transport inflation

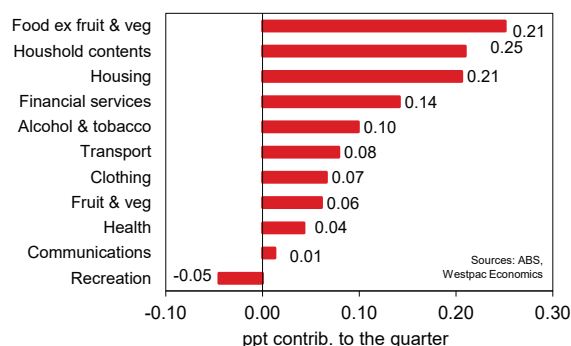
We have the Monthly CPI Indicator fuel prices for April and May, to which we can add the reported pump fuel prices, which suggest auto fuel gained 0.5% in the June quarter. Many other components of this group are only surveyed in the mid-month of the quarter so we have good guidance here. However, motor vehicles are surveyed in the last month of the quarter so we are sure just has strong the recent inflationary trend was in June.

Transport forecast 0.7% contributing 0.08ppt.

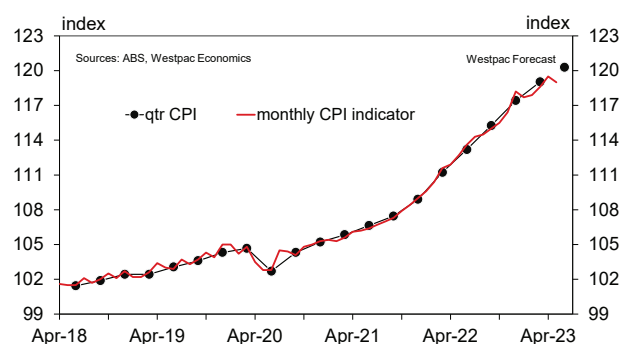
Recreation & culture rebounds from lock-downs

The Monthly CPI provides data on holiday travel with prices surging in April (domestic 6.1% international 8.6%) to then collapse in May (domestic -15.5% international -4.7%) and we are forecasting a modest recovery in prices in June. We have quarterly estimates for some of the series while books,

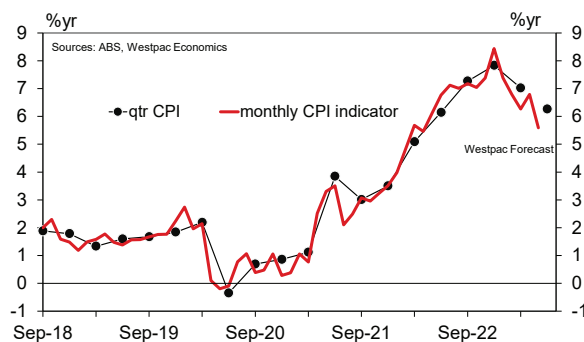
Contributions 2023Q2 CPI 1.1%qtr print



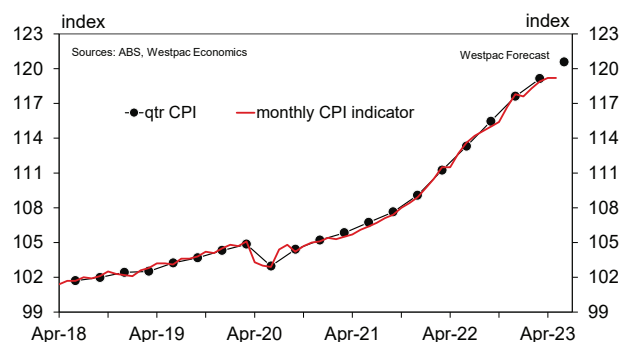
CPI Monthly Indicator vs. qtr CPI



CPI Monthly Indicator vs. qtr CPI



Comparing seasonally adjusted prices



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newspapers and veterinary services are surveyed in the last month of the quarter. We need to make a June estimate for the monthly data we have on audiovisual & computing equipment and pets & related products.

Recreation & culture forecast is -0.4% contributing -0.03ppt.

Inflationary pressures are moderating

The Trimmed Mean is forecast to rise 1.1%, moderating from the 1.2% gain in March, 1.7% in the December quarter and 1.9% in the September quarter (likely to be the peak in quarterly pace this cycle). The annual pace is set to ease from 6.6%yr to 6.0%yr with the two-quarter annualised pace easing from 5.9%yr to 4.6%yr.

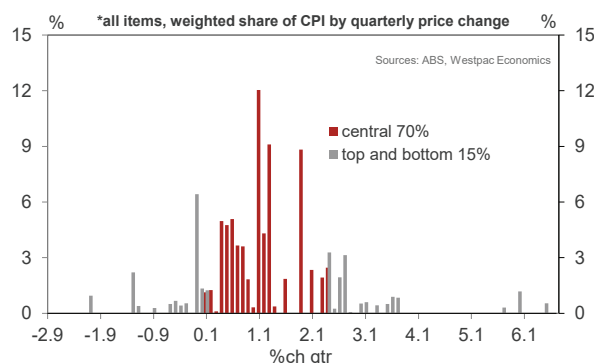
The ABS clearly has put a lot of work into estimating a trimmed mean series from the Monthly Indicator that can provide a more useful guide of this measure of core inflation in the quarterly CPI. As you can see in the chart over, the estimated annual growth rate for the Monthly Trimmed Mean now more closely aligns with the estimates from the quarterly CPI. The Monthly Trimmed Mean has core inflation peaking at 7.2% in December 2022 before moderating to 6.5% in March then down to 6.1% in May.

Recall that the prices that are seasonally adjusted in the core measures and the largest 15% by weighted change are trimmed off the top and bottom. Trimmed off the top are; household textiles (6.9%), bread (6.5%), insurance (5.9%), garments for children (5.7%), childcare (3.6%), waters & soft drinks (3.5%), other food products (3.5%), poultry (3.3%), cakes & biscuits (3.0%), eggs (3.0%), fish & other seafood (3.0%), infants footwear (2.7%), ice-cream (2.7%), take away & fast foods (2.7%), spirits (2.6%), books (2.6%), motor vehicle spare parts (2.5%), coffee, tea & cocoa (2.5%), rents (2.4%). The top of the range Trimmed Mean estimate is 2.4%.

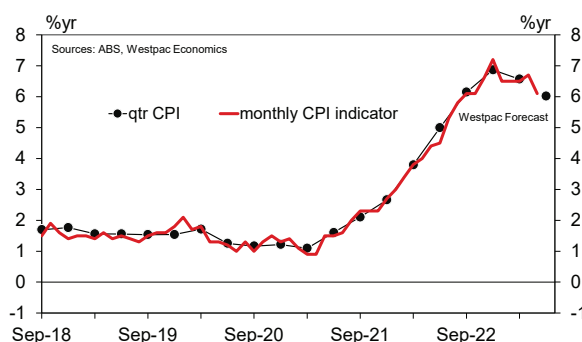
Trimmed off the bottom are; accessories (-2.2%), men's footwear (-2.2%), international travel (-1.3%), glassware, tableware & utensils (-1.3%), household appliances (-1.3%), women's footwear (-1.0%), beef & veal (-0.7%), other household services (-0.5%), milk (-0.5%), pets (-0.4%), audiovisual & computing equipment (-0.2%), sports & camping equipment (-0.2%), medical & hospital services (-0.1%), small electrical appliances (-0.1%), pharmaceuticals (-0.1%), electricity (0.0%). The bottom Trimmed Mean estimate is 0.0%.

Justin Smirk, Senior Economist, ph (61-2) 8254 9336

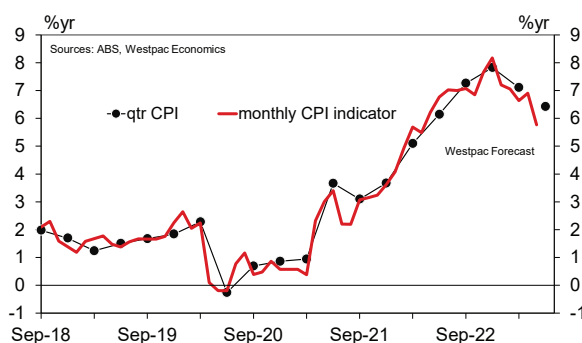
Distribution of seasonally adjusted Q2 CPI fcs



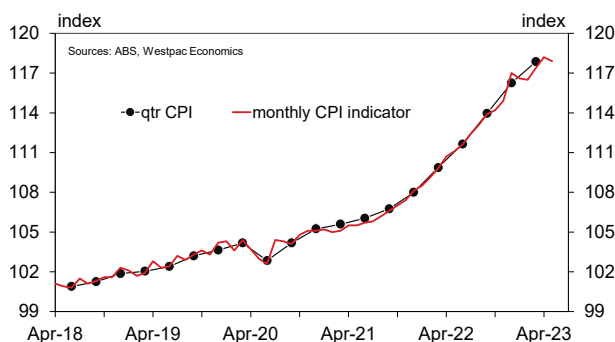
Annual inflation trimmed mean measures



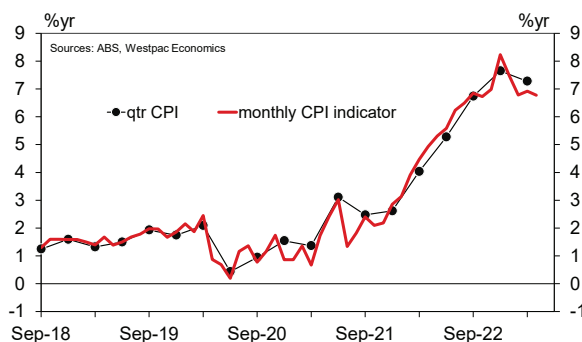
Annual inflation seasonally adjusted measures



Comparing excluding volatile prices



Annual inflation excluding volatile measures



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- II. physical separation of various Business/Support Units;
- III. Strict and well defined wall/cell crossing procedures;
- IV. a “need to know” policy;
- V. documented and well defined procedures for dealing with conflicts of interest;
- VI. reasonable steps by Compliance to ensure that the Chinese Wall/Cell arrangements remain effective and that such arrangements are adequately monitored.

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