

Australian Economic Comment

Q1 core CPI below RBA target – 2nd time in 15yrs

Economics

Australia

Q1 CPI falls 0.2% q/q to 1.3% y/y, below RBA's mid-16 1½% y/y forecast

Headline CPI was -0.2% in Q1 (below consensus for +0.2%), the lowest q/q print in over 7 years, returning the y/y to 1.3%, as it was a year ago. This is below the RBA's mid-16 forecast for 1½% y/y, & below the RBA's 2-3% target for a 6th qtr, the longest 'undershoot' since 1999. Key drivers of the fall were petrol (-10% q/q, -0.3%pts), fruit (-11%, -0.1%pts) & holiday travel (-2%, -0.1%pts), with a largely seasonal fall for clothing (-3%, -0.1%pts). Also contributing were lower than normal seasonal rises in utilities (-0.4% y/y after +0.7%), health (4.6%, was 5.3%) & education prices (3.3%, was 5.5%), with 'flat' housing (rents & construction, 1.7% after 2.2% y/y).

Underlying CPI ¼% q/q, takes y/y to 1.6%, below RBA's 2% mid-16 forecast

Underlying inflation was sharply lower than expected in Q1, with the RBA's statistical measures averaging +0.2% q/q & 1.5% y/y (mkt +0.5% & 1.7%). The trimmed mean was +0.2% (lowest since 1997), with the y/y 1.7% after 2.1%, while the weighted was +0.1%, with the y/y 1.4% after 1.9%. The other key core measure, CPI ex volatiles was 0.3% & 1.7% y/y (after 2.1%). The RBA's underlying inflation (3-core) average eased to 1.6%, below Feb's SoMP mid-16 2% forecast, and the lowest y/y since mid-99.

Implications: RBA now has room to cut...if they need to 'support...demand'

Today's Q1 CPI was materially lower than expected, with underlying inflation below the RBA's 2-3% target for only the 2nd time in 15 years (& the RBA's mid-16 2% forecast). The 1st negative CPI print in 7 years was driven by sharp falls in fuel & fruit. But it also reflected the recently less inflationary trends evolving in areas of new competitive pressure (food, clothing & telecoms), slower gains in regulated prices (utilities, health insurance & property rates) & record low wage growth - as we identified in our recent inflation deep-dive ([Is Australia about to join the low inflation world?](#)). As we wrote, given 3.0% GDP growth & 5.7% unemployment, we doubt a short period of sub-target core CPI is a sufficient condition alone for the RBA to trim. But it certainly lowers the hurdle for further cuts, should the outlook deteriorate. The RBA will need to lower their near-term CPI targets in next month's SoMP...key is how far out they lower them?

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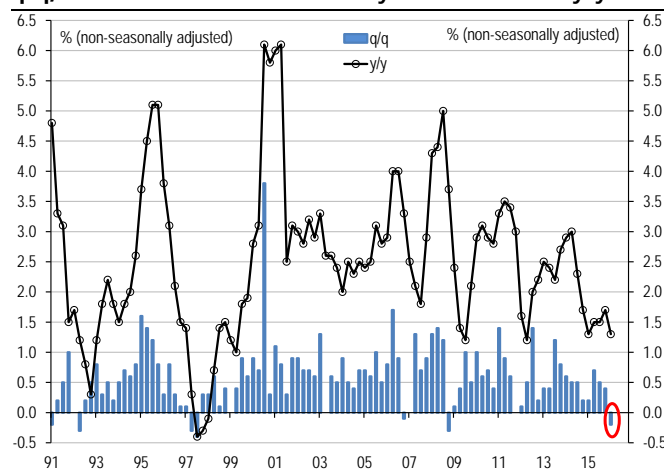
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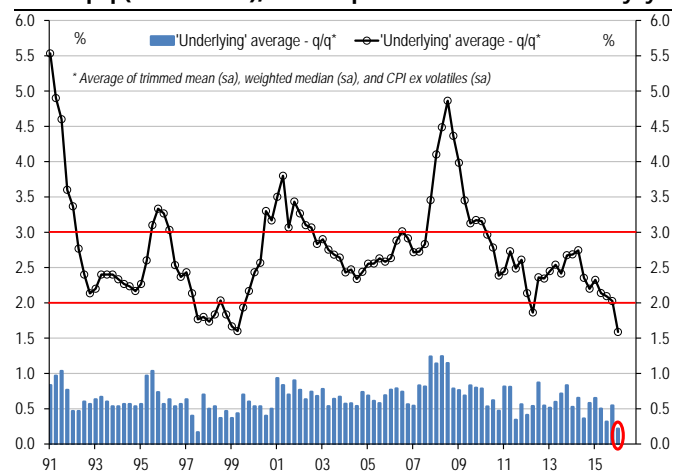
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Figure 1: Q1 headline CPI unexpectedly dropped 0.2% q/q, and moderated back to a ~cycle low of 1.3% y/y



Source: ABS, UBS

Figure 2: Q1 'underlying' rose by an equal record low of 0.2% q/q (after 0.5%), & an equal record low of 1.6% y/y



Source: ABS, RBA, UBS

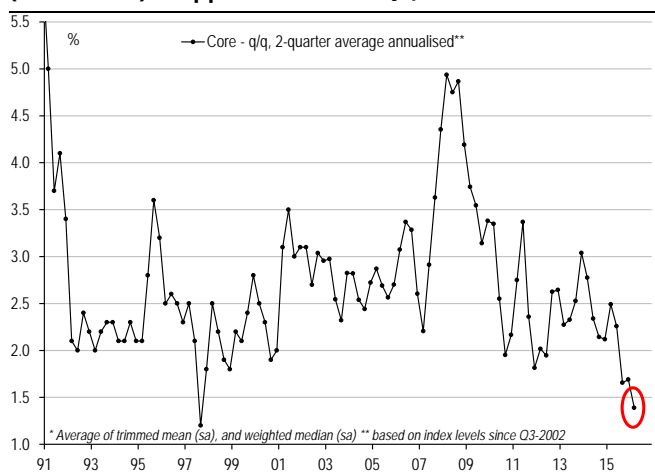
CPI (Q1 2016)

Figure 3: Consumer price index (% change)

	Headline				RBA statistical measures (s.a.)						Ex-volatiles		Underlying**		Tradables		Non-tradables	
	n.s.a.		s.a.		Trimmed mean		Weighted median		Statistical core average		q/q (sa)*	y/y (nsa)	q/q*	y/y	n.s.a.		n.s.a.	
	q/q	y/y	q/q	y/y	q/q	y/y	q/q	y/y	q/q	y/y					q/q	y/y	q/q	y/y
Q1-15	0.2	1.3	0.3	1.3	0.6	2.3	0.6	2.4	0.6	2.3	0.7	2.1	0.7	2.3	-1.2	-0.9	1.0	2.6
Q2-15	0.7	1.5	0.8	1.5	0.6	2.2	0.4	2.3	0.5	2.2	0.5	1.9	0.5	2.1	1.2	-0.3	0.5	2.6
Q3-15	0.5	1.5	0.2	1.5	0.3	2.1	0.3	2.1	0.3	2.1	0.3	2.0	0.3	2.1	0.3	-0.3	0.4	2.6
Q4-15	0.4	1.7	0.4	1.7	0.6	2.1	0.4	1.9	0.5	2.0	0.6	2.1	0.5	2.0	0.5	0.8	0.4	2.3
Q1-16	-0.2	1.3	-0.1	1.3	0.2	1.7	0.1	1.4	0.2	1.5	0.3	1.7	0.2	1.6	-1.4	0.6	0.4	1.7

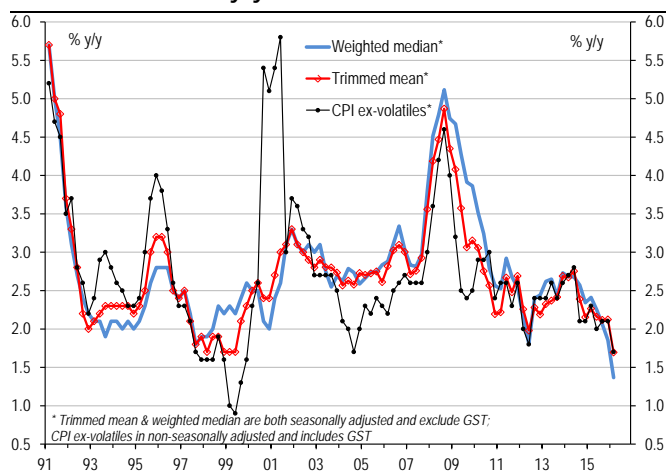
Source: ABS, RBA, UBS * Latest is UBS estimate; ** Average of trimmed mean (sa), weighted median (sa) and ex-volatiles s.a. q/q but ex-volatiles nsa y/y

Figure 4: The 2-quarter average of core CPI q/q (annualised) dropped to 1.4% in Q1, 2nd lowest on record



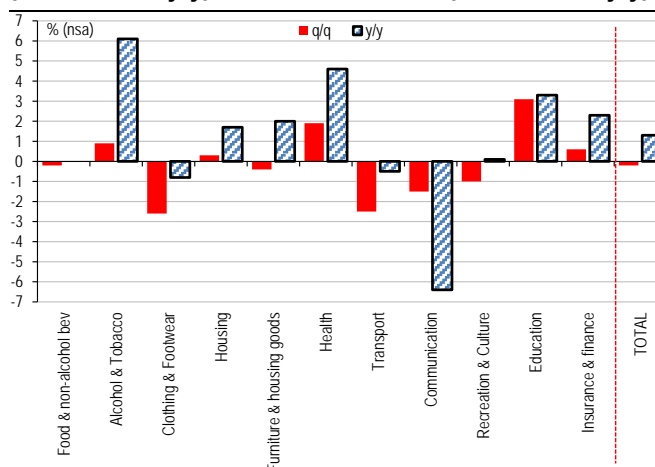
Source: ABS, RBA, UBS

Figure 5: The 3 core CPI measures are all low – ranging from 1.4% to 1.7% y/y



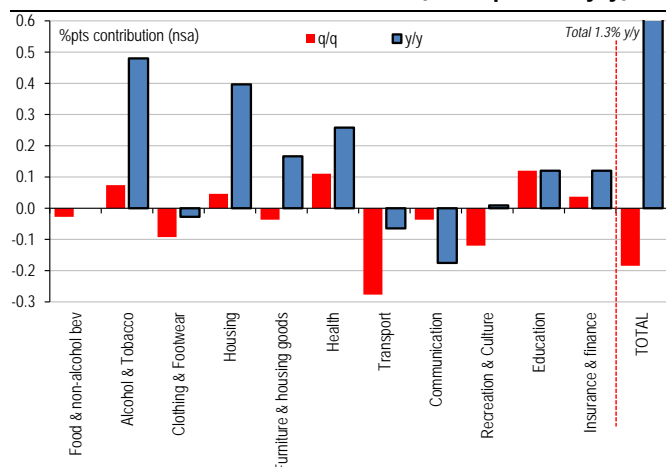
Source: ABS, RBA, UBS

Figure 6: q/q fall led by transport (-2.5%, -0.5% y/y), as fuel slumped (-10.0%, -6.4% y/y); with drops in clothing (-2.6%, -0.8% y/y) and communication (-1.5%, -6.4% y/y)



Source: ABS, UBS

Figure 7: In contribution terms, the largest q/q drag was fuel-driven transport (-0.3pts, -0.1pts y/y); but recreation & culture also subtracted (-0.1pts, flat y/y)



Source: ABS, UBS

Figure 8: 4-quarter average headline CPI still near a 16-year low at 1.5% y/y in Q1, & remains well below 'target'

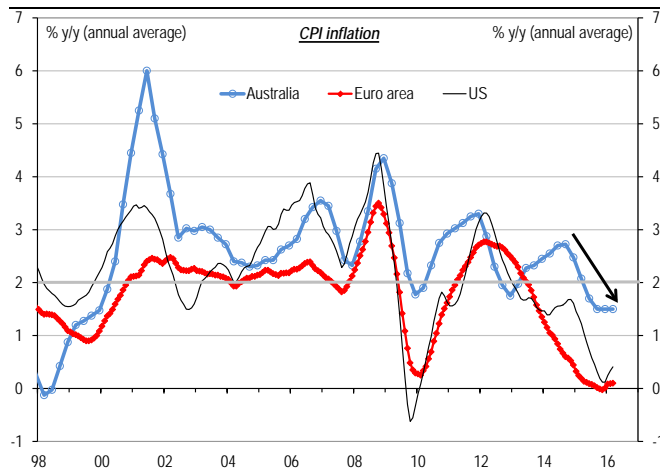


Figure 10: Much lower breadth of q/q inflation in Q1 – with 51 items (out of 87, sa) posting an increase – albeit after a spike in Q4 to the equal highest since 2009

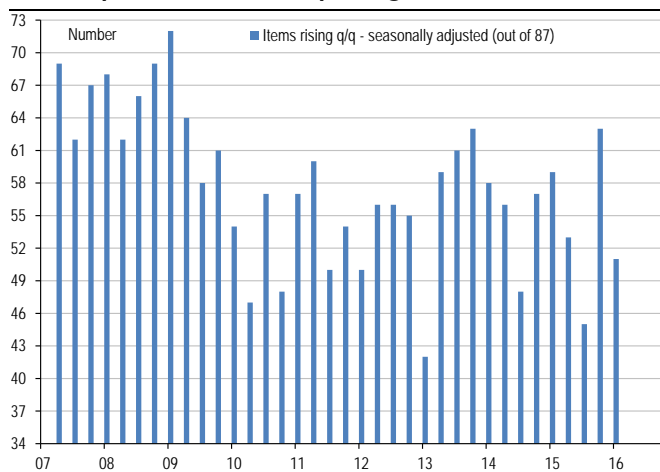
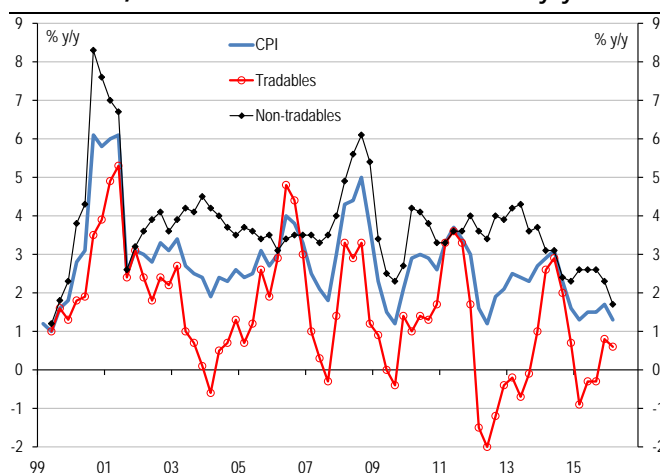


Figure 12: Non-tradables dropped to 1.7% y/y, lowest since 1999; while tradables also eased to 0.6% y/y



Source: ABS, RBA, UBS

Figure 9: Q1 petrol fell 10% q/q & dragged 0.3%pts q/q from CPI – while Q2 to date implies a ~flat trend

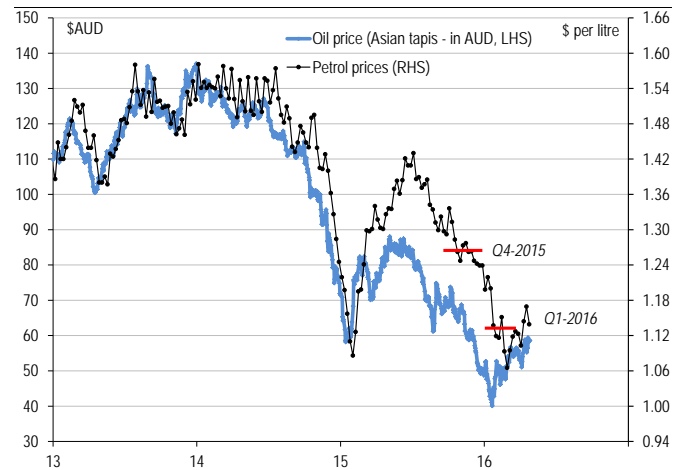


Figure 11: The drop in underlying CPI is consistent with record low wage rates, with low wage growth a likely persistent disinflationary impact over the coming year

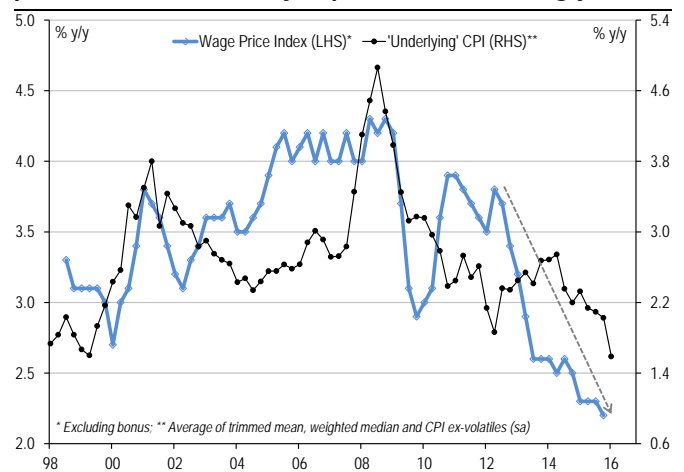


Figure 13: The (very) recent bounce in the AUD suggests tradables inflation may have already peaked

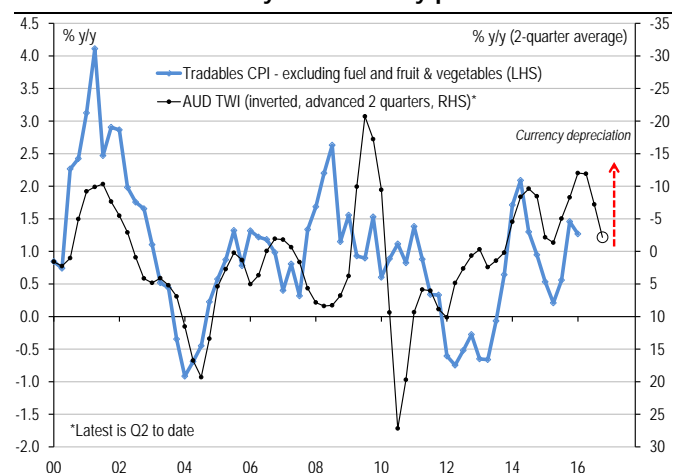


Figure 14: There was a large 10% q/q fall in automotive fuel (-0.3%pts in Q1), with petrol now dragging 0.5%pts from headline CPI over the past 3 quarters

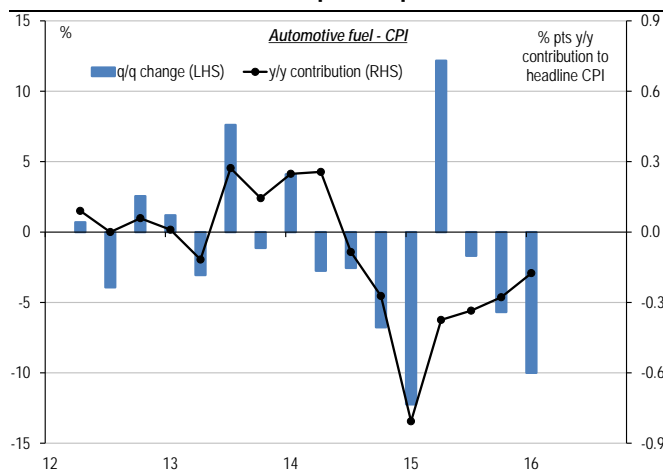


Figure 16: Rents grew just 0.1% q/q in Q1-16, the weakest q/q rise since Q1-94, dragging the y/y to a >20 year low

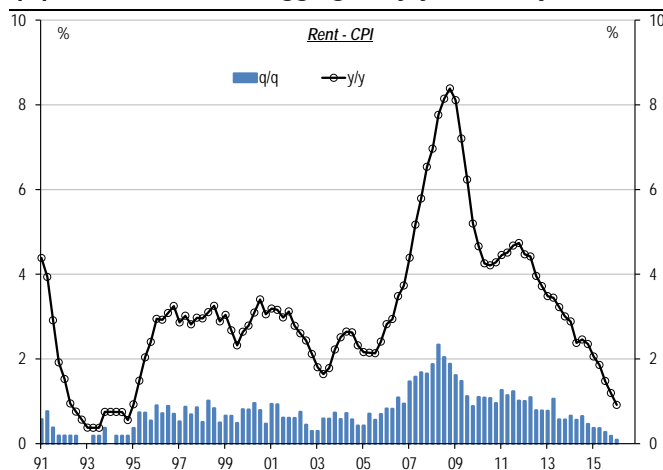
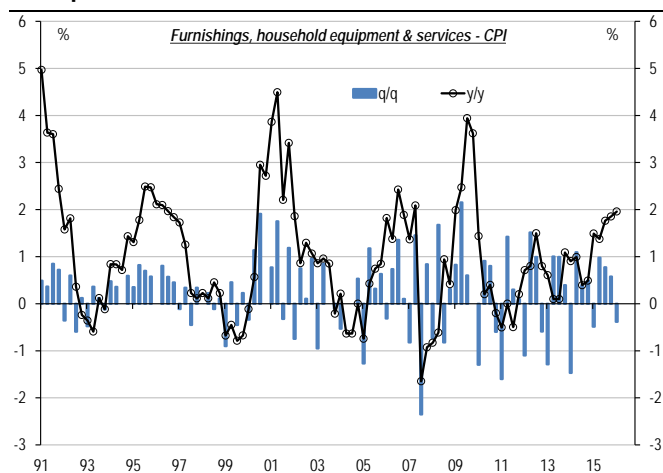


Figure 18: Furnishings, household equipment & services retraced a seasonally modest 0.4% q/q, seeing the y/y tick up to 2%, the fastest since Q4-09



Source: ABS, RBA, UBS

Figure 15: Heightened competition in the grocery sector has seen food inflation moderate to flat

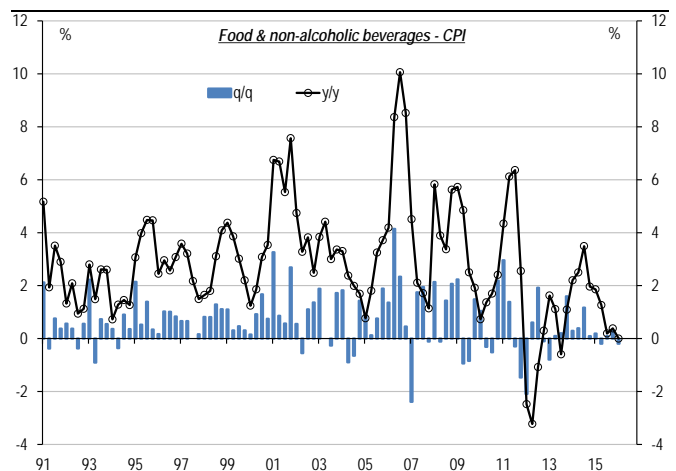


Figure 17: Despite the lower AUD trend, clothing & footwear prices are still falling

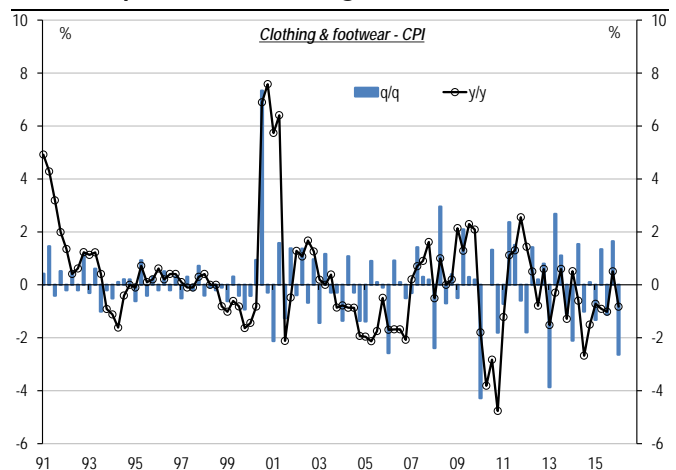


Figure 19: Health inflation rose just 1.9% q/q, the weakest Q1 since 1999, albeit the y/y still remains at a solid 4.6%; while insurance has recovered to 5.2% y/y

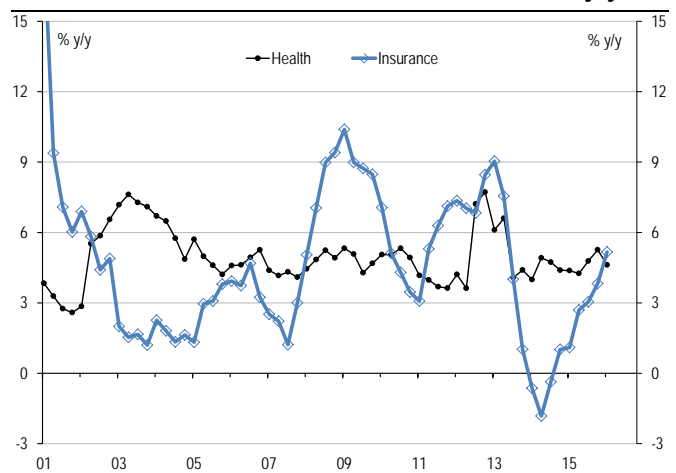


Figure 20: Consumer price index – details (% change, nsa) *

	% q/q		% y/y		%pts q/q		%pts y/y	
	Q4-15	Q1-16	Q4-15	Q1-16	Q4-15	Q1-16	Q4-15	Q1-16
FOOD AND NON-ALCOHOLIC BEVERAGES	0.3	-0.2	0.4	0.0	0.0	0.0	0.1	0.0
- Bread and cereal products	0.4	-0.9	-1.5	-2.0	0.0	0.0	0.0	0.0
- Meat and seafood	1.4	1.2	4.1	3.8	0.0	0.0	0.1	0.1
- Dairy and related products	-1.2	-0.2	-1.5	-2.7	0.0	0.0	0.0	0.0
- Fruit and vegetables	-0.2	-4.3	-3.2	-5.4	0.0	-0.1	-0.1	-0.1
- Other food	0.6	1.2	-0.3	0.2	0.0	0.0	0.0	0.0
- Non-alcoholic beverages	-2.1	1.5	-1.8	-0.7	0.0	0.0	0.0	0.0
- Meals out and take away foods	0.7	0.4	2.1	1.9	0.0	0.0	0.1	0.1
ALCOHOL AND TOBACCO	2.7	0.9	6.0	6.1	0.2	0.1	0.5	0.5
- Alcoholic beverages	-0.4	0.8	1.3	1.5	0.0	0.0	0.1	0.1
- Tobacco	7.4	0.8	13.3	13.3	0.2	0.0	0.4	0.4
CLOTHING AND FOOTWEAR	1.6	-2.6	0.5	-0.8	0.1	-0.1	0.0	0.0
- Garments	0.7	-2.1	-0.1	0.0	0.0	0.0	0.0	0.0
- Footwear	1.8	-3.5	-4.0	-3.8	0.0	0.0	0.0	0.0
- Accessories and clothing services	4.1	-3.5	5.4	-0.8	0.0	0.0	0.0	0.0
HOUSING	0.1	0.3	2.2	1.7	0.0	0.0	0.5	0.4
- Rents	0.2	0.1	1.2	0.9	0.0	0.0	0.1	0.1
- New dwelling purchase of owner occupiers	0.1	0.2	3.3	2.5	0.0	0.0	0.3	0.2
- Other housing	0.3	0.3	3.4	3.5	0.0	0.0	0.1	0.1
- Utilities	-0.3	0.5	0.7	-0.4	0.0	0.0	0.0	0.0
FURNISHINGS, HOUSEHOLD EQUIPMENT & SERVICES	0.6	-0.4	1.9	2.0	0.0	0.0	0.2	0.2
- Furniture and furnishings	1.0	-1.2	2.0	3.8	0.0	0.0	0.0	0.1
- Household textiles	2.2	-4.1	1.7	3.1	0.0	0.0	0.0	0.0
- Household appliances, utensils and tools	0.1	-0.3	2.8	3.2	0.0	0.0	0.0	0.0
- Non-durable household goods	0.4	-0.9	-1.0	-2.0	0.0	0.0	0.0	-0.1
- Domestic and household services	0.4	1.4	4.4	4.1	0.0	0.0	0.1	0.1
HEALTH	-0.4	1.9	5.3	4.6	0.0	0.1	0.3	0.3
- Medical products, appliances and equipment	-1.7	4.3	1.9	1.0	0.0	0.1	0.0	0.0
- Medical, dental and hospital services	0.0	1.3	6.1	5.5	0.0	0.1	0.3	0.3
TRANSPORT	-1.4	-2.5	-1.4	-0.5	-0.1	-0.3	-0.1	-0.1
- Private motoring	-1.4	-2.8	-1.2	-0.6	-0.1	-0.3	-0.1	-0.1
- Urban transport fares	-0.3	0.2	-3.4	0.1	0.0	0.0	0.0	0.0
COMMUNICATION	-2.4	-1.5	-6.3	-6.4	-0.1	0.0	-0.2	-0.2
- Communication	-2.4	-1.5	-6.3	-6.4	-0.1	0.0	-0.2	-0.2
RECREATION AND CULTURE	1.6	-1.0	1.7	0.1	0.2	-0.1	0.2	0.0
- Audio, visual and computing equipment and services	-0.7	-3.5	-1.8	-4.3	0.0	-0.1	0.0	-0.1
- Newspapers, books and stationery	-0.6	1.3	0.7	1.2	0.0	0.0	0.0	0.0
- Holiday travel and accommodation	4.2	-2.0	2.6	0.2	0.2	-0.1	0.1	0.0
- Other recreation, sport and culture	0.4	0.6	2.5	1.6	0.0	0.0	0.1	0.1
EDUCATION	0.0	3.1	5.5	3.3	0.0	0.1	0.2	0.1
- Education	0.0	3.1	5.5	3.3	0.0	0.1	0.2	0.1
INSURANCE AND FINANCIAL SERVICES	0.8	0.6	1.8	2.3	0.0	0.0	0.1	0.1
- Insurance	2.1	1.7	3.8	5.2	0.0	0.0	0.1	0.1
- Financial services	0.3	0.2	0.9	1.0	0.0	0.0	0.0	0.0
CPI – NON-SEASONALLY ADJUSTED	0.4	-0.2	1.7	1.3	0.4	-0.2	1.7	1.3

Source: ABS, UBS * The 11 major groups are in capitals and bold

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