

## Regular Inflation in Australia

*Bruce Bradbury  
Social Policy Research Centre  
University of New South Wales*

*26 May 2008*

A recent analysis of the 2007 Australian Election Study concluded that concern about rising prices was a particularly important election issue – more important than rising interest rates.<sup>1</sup> Price rises were a central issue in the Labor campaign (no doubt based on polling information such as this) and the need to curtail inflation has continued to be a constant refrain of the new Treasurer, Wayne Swan.

This concern with prices is something of a puzzle. Over the last 3 years the headline CPI inflation rate has averaged around 3.3 per cent per annum. Though this is slightly above the Reserve Bank's target range, this is still very low by historical standards. One explanation may lie with the exclusion of mortgage interest costs from the CPI. However, this is unlikely to explain the Election Study results, as interest rates were included as a separate question.

Another explanation may lie in the heterogeneity of price changes. The last decade has seen Australian consumers benefit greatly from dramatic falls in the world prices of many manufactured goods – driven by technological developments and the boom in manufacturing in China and India. In recent years these price falls have been accentuated by the appreciation in the Australian dollar. These price falls in tradeable goods have helped offset price rises in other areas.

A key feature of these now-cheaper tradeable goods is that most of them are durable goods – goods that provide services to the household over an extended period of time. This has an important implication for the management of household budgets – the timing of purchase is important for these goods. To take a simple example, most people have a TV in their lounge-room. At some stage, many will want to upgrade to a larger digital TV. The main impact of the reduction in price of digital TVs will be to bring forward the date at which this upgrade is made. Similarly, if a durable good like a TV increases in price, most people can adapt to this by keeping their previous version of that good for a longer period before upgrading. They don't need to stop watching TV to avoid the price increase.

However, with non-durable goods, adaption to higher prices cannot draw on timing in the same way. It is hard to avoid the cost increase associated with a petrol price rise unless you reduce your mobility. Moreover, the price of goods that are consumed regularly is constantly visible, rather than faced only occasionally. Since many tradeable goods are durable goods, we might expect that the price of goods that are regularly consumed has increased faster than overall inflation. How much difference is there?

---

<sup>1</sup> Davis, Mark (2008), 'What made battlers turn the tide', *Sydney Morning Herald*, May 24.

Here, I define 'regular goods' as non-durable goods, minus a few services that are only infrequently purchased and/or whose timing is more discretionary. More specifically, they comprise: food (except restaurant meals), alcohol and tobacco, housing (except repairs), household supplies and services, health, transport fares and running costs, telephone and post, repairs, sport fees, pet fees, education and financial services. The remaining 'irregular goods' include: restaurant meals, clothing and footwear, housing repairs, furniture, appliances, utensils and tools, motor vehicles and parts, electronic equipment, sports equipment, and holidays.

Irregular goods comprise about one quarter of the average household budget in Australia. Since 2005, these prices have grown at an average rate of 0.5 per cent per annum.

The figure below contrasts inflation in the price of the remaining regular goods with the overall CPI. Over the last few years, regular inflation has been consistently higher than the headline CPI. Between June 2005 and March 2008, the average headline inflation rate was 3.3 per cent per annum. For regular goods, the inflation rate was 4.3 per cent.

This gap perhaps explains some of the divergence between the expressed concerns of consumers and the complacency of economists. Though consumers know that their next TV will be much better than their last one for much the same price, they are still struggling to meet their weekly supermarket and petrol station bills.

