

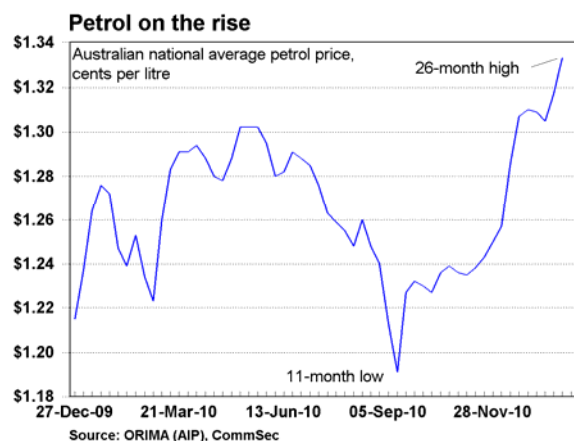
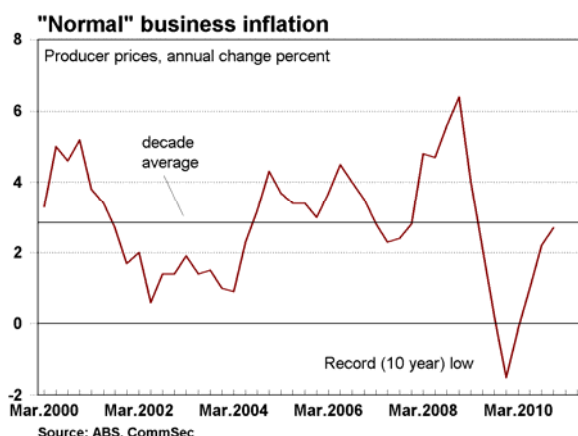
# Petrol pain; Tame business inflation

## Producer price index; Weekly petrol price

- The broad measure of business inflation – the producer price index (PPI) – rose by just 0.1 per cent in the December quarter, well below expectations for an increase of 0.5 per cent. Compared with a year ago, producer prices were up by 2.7 per cent.
- Inflation was narrowly based, and largely driven by price increases for building materials and agricultural products like flowers and poultry. The rising Australian dollar resulted in prices of imported goods falling by 4.4 per cent in the December quarter to be 2.4 per cent lower over the year.
- Motorists need to prepare for higher petrol prices. The terminal gate or wholesale price of petrol leapt by almost 2 cents a litre last week to 26-month highs. CommSec expects petrol prices to rise 3 cents a litre over the coming fortnight.

### What does it all mean?

- The latest business inflation result certainly surprised on the lower side of expectations. Business inflation was pretty much non-existent and more importantly narrowly based in the December quarter. And if consumer prices are similarly restrained, then Reserve Bank policymakers will be able to stay on the interest rate sidelines well into the June quarter.
- As we have highlighted on many an occasion, the market is underestimating the impact that the higher Australian dollar is having on imported inflation. Prices on imported goods fell by 4.4 per cent in the December quarter. In fact in annualised terms imported prices have been falling for 15 months – effectively offsetting domestic inflationary pressures. And given that the Aussie is expected to remain near parity in coming months, imported inflation will continue to be tame.
- On the domestic front, contributing most to the inflation story was a rise in the prices of agricultural products like flowers, and poultry, while building construction and accommodation services also rose. With the pickup in mining, infrastructure and home building it is understandable why costs have been rising, albeit modestly.
- The ultimate concern is where prices go from here. CommSec anticipates a 0.8 per cent lift in the underlying measure of consumer price index for the December quarter, with the annual growth rate rising from 2.5 per cent to 2.7 per cent



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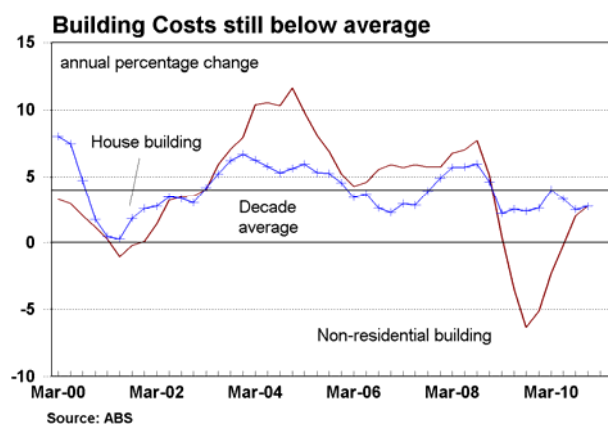
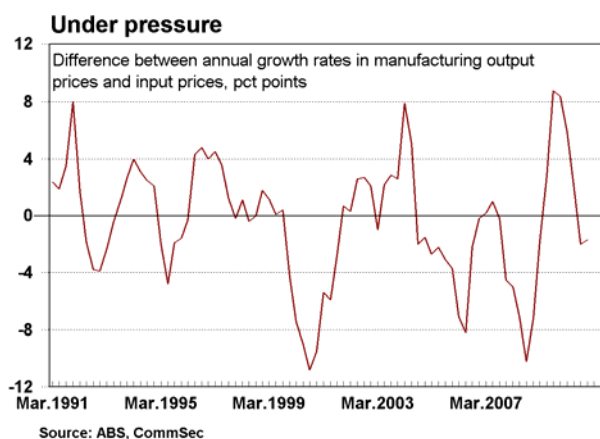
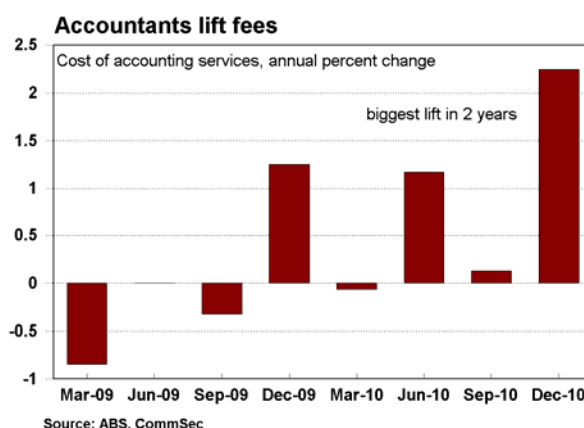
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- In the longer term, the rebuilding in Queensland has potential to add further pressure to an already tight labour market, resulting in wage pressures in the back end of 2011. Similarly, the Aussie dollar is expected to ease over the second half of 2011 as the US economy strengthens, ensuring that the offset from imported prices is likely to minimise.
- Importantly manufacturing margins have continued to contract in recent quarters. The cautious consumer and business environment has resulted in businesses having to absorb costs while the strength of the Australian dollar will also result in domestic manufacturers becoming even less competitive, adding further downward pressure on profitability.
- Motorists need to prepare for higher petrol prices over the next fortnight. The wholesale price of petrol leapt by almost two cents a litre last week and more than likely the higher cost will be passed through to motorists over the next 7-10 days.
- Not only has the wholesale price continued to rise but even on the world stage the Singapore unleaded price has risen in the past week and is now holding at 27-month highs. Unfortunately for motorists the fall in the Australian dollar over the past week is likely to compound the price rise at the pump.

## What do the figures show?

### Producer prices:

- **Final stage producer prices** rose by just 0.1 per cent in the December quarter, well below expectations for a rise of 0.5 per cent. Producer prices were up 2.7 per cent on a year ago.
- Prices of **domestically produced** goods and services rose by 0.7 per cent to stand 3.5 per cent higher than a year ago. And prices of **imported goods and services** fell by 4.4 per cent to be 2.4 per cent down on a year ago.
- The ABS reported that final stage prices were driven by “*risers in the prices received for other agriculture (+18.3 per cent), building construction (+0.8 per cent) and accommodation (+8.6 per cent) and partly offset by falls in the prices received for industrial machinery and equipment manufacturing (-3.2 per cent) and electronic equipment and appliance manufacturing (-7.1 per cent)*”.
- **Consumer good** prices rose by 0.1 per cent in the quarter while **capital good** prices rose by 0.1 per cent. Over the year, prices of consumer goods rose by 3.7 per cent, while capital goods rose 2.1 per cent.
- **Prices of intermediate goods** were unchanged in the quarter to stand 3.3 per cent higher over the year. **Preliminary stage materials** rose by 0.1 per cent in the quarter to be 3.8 per cent higher than a year ago.
- Prices of building materials rose by 0.6 per cent in the December quarter and were up 2.4 per cent on a year earlier.
- Charges for parking services rose 7.7 per cent over the December quarter to be 19.7 per cent higher than a year ago.
- Real estate agent fees rose by 0.1 per cent in the December quarter – marking the slowest growth in 15 months,



to be 8.2 per cent higher than a year ago.

- **Manufacturing output prices** rose by 0.4 per cent in the December quarter, above the 0.2 per cent lift in **manufacturing input** prices. Over the year, prices of outputs rose by 3.8 per cent, below the 5.5 per cent rise in input prices.

#### **Petrol prices:**

- According to the Australian Institute of Petroleum, the national average Australian price of unleaded petrol rose by 1.6 cents per litre to 133.3 cents a litre in the week to January 23. The metropolitan price rose by 1.9 c/l to 133.5 c/l, while the regional average price rose by 1.0 c/l to 132.9 c/l.
- Petrol prices across states in the past week were: Sydney (up 2.7 cents to 134.4 c/l), Melbourne (up 2.6 cents to 133.5 c/l), Brisbane (down 0.4 cents to 131.3 c/l), Adelaide (up 2.0 cents to 133.0 c/l), Perth (up 1.6 cents to 133.8 c/l), Darwin (up 0.5 cents to 135.9 c/l), Canberra (down 0.9 cents to 133.2 c/l) and Hobart (up 1.6 cents to 136.5 c/l).
- The national average wholesale (terminal gate) price hit a 26-month high of 127.0 cents a litre today. Over the past week the terminal gate price has risen by almost 2 cents a litre. Just over three months ago (October 1) the terminal gate price stood at an 11-month low of 111.6c/l.
- Last week, the key Singapore unleaded petrol price rose by US\$1.58 (1.5 per cent) to US\$106.60 a barrel. And in Australian dollar terms the Singapore gasoline price rose by \$2.40 (2.6 per cent) over the week to \$108.10 a barrel.

#### **What is the importance of the economic data?**

- The Bureau of Statistics releases a range of measures on **producer prices** each quarter all contained in the one publication. Indexes cover manufacturing, mining, construction, transport and property and business services. Overall producer price measures are divided into components reflecting the stage of processing - final, intermediate and preliminary (raw) commodities. There are also separate producer price components for domestic and imported goods.
- The producer price figures are important in flagging price pressures at an early stage. If business costs are rising, the risk is that these will be passed on in terms of higher prices of final consumer goods. The Consumer Price Index is regarded as the key gauge of economy-wide inflation.
- **Weekly figures on petrol prices** are compiled by ORIMA Research on behalf of the Australian Institute of Petroleum. National average retail prices are calculated as the weighted average of each State/Territory's metropolitan and non-metropolitan retail petrol prices, with the weights based on the number of registered petrol vehicles in each of these regions.

#### **What are the implications for interest rates and investors?**

- The one thing that is clear from the latest producer price data is that business inflation is well contained apart from a few categories. Reserve Bank policymakers are unlikely to be alarmed. The strength of the Australian dollar will support a low inflation environment, while at the same time slowing activity in an array of sectors will put further downward pressure on prices. CommSec expects a 0.7 per cent lift in the consumer price index, with the annual growth rate rising from 2.8 per cent to 3.0 per cent.

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