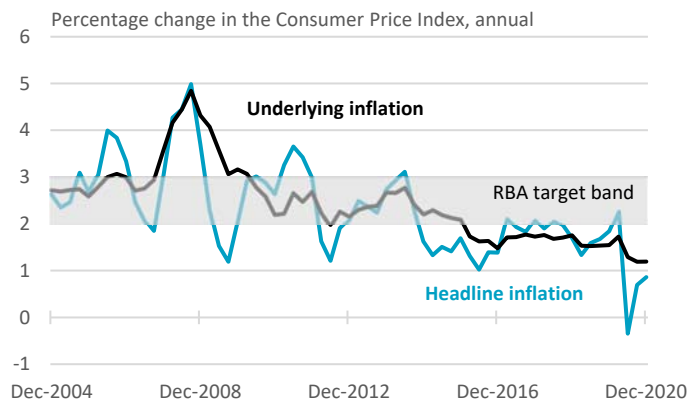


# ASFA Economic Snapshot: week ending 29 January

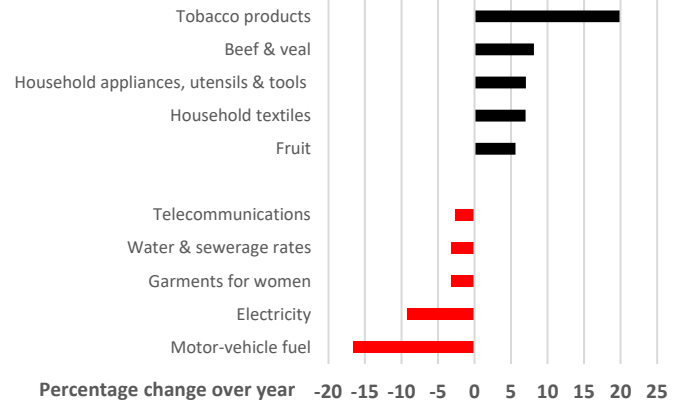
This is a weekly update on the impact of the COVID-19 pandemic on financial and economic conditions, in Australia and globally, and government policy measures to support economic activity and employment.

## Inflation remains low in the December quarter ...



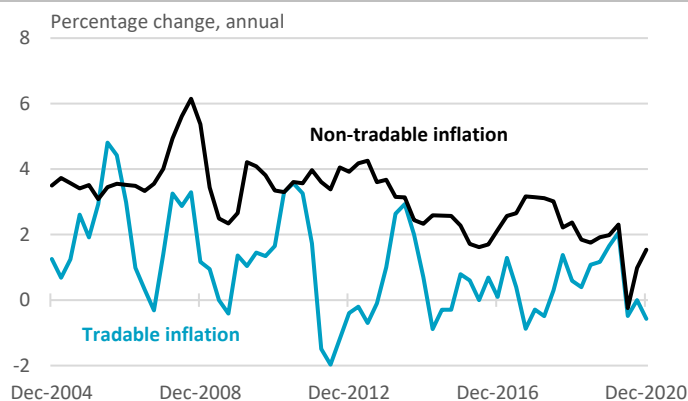
Headline inflation (or growth in Headline CPI) was 0.9% for the year to the December quarter, up from 0.7% for the year to the September quarter. The sharp fluctuation in headline inflation earlier in 2020 largely reflected the introduction and then removal of free childcare. Underlying inflation, which excludes volatile items and is a better indicator of general price pressure, was unchanged (1.2% over the year) and remains well below the RBA's medium-term target band.

## ... with some large price changes during 2020



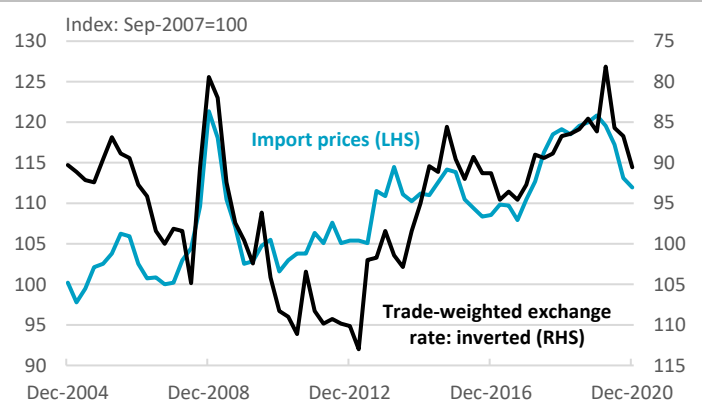
This chart shows the largest price changes in 2020 (among the changes excluded from underlying inflation). Strong demand for household appliances and textiles during the crisis, coupled with shortages, led to price rises. The 20% rise in tobacco prices largely reflected the annual excise-tax hike. Lower demand for vehicle fuel during the crisis led to large price falls, while the fall in electricity prices reflected the impact of the \$600 credit to WA households from the state government.

## Tradable and non-tradable inflation remain low ...



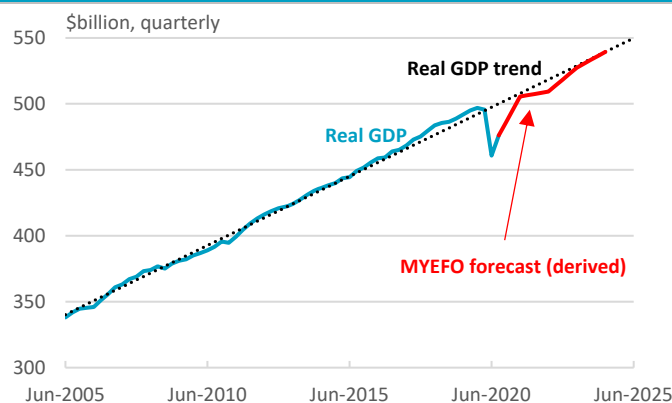
CPI components are designated tradable or non-tradable, depending on the relative influence of international and local factors. Prior to the crisis non-tradable inflation (a measure of domestic price pressure) was about 2%, with the recent fluctuation largely reflecting childcare prices. The recent drop in tradable inflation was driven by the AUD.

## ... with import prices impacted by the exchange rate



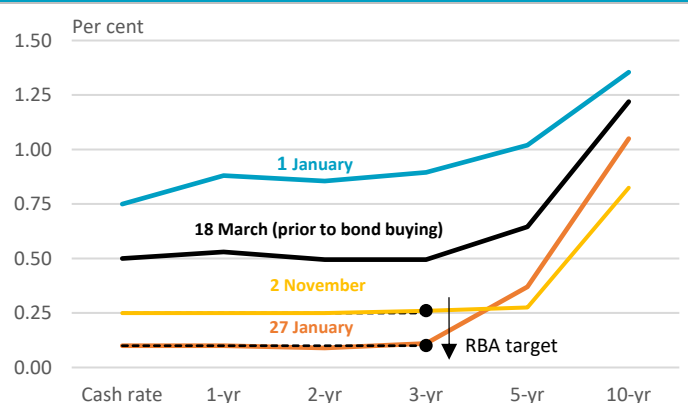
In the short-term, import prices tend to track the exchange rate (the exchange rate is inverted in this chart – falling import prices reflect an appreciating exchange rate). Over the past 12 months, Australia's trade-weighted exchange rate (composed of currencies weighted by trade shares) appreciated by 5%, while import prices fell by 7%.

## Inflationary pressures will remain subdued ...



This chart shows the expected trajectory for real GDP (red), which is derived from the government's MYEFO forecasts. The GDP trend (black) shows an assumed path for GDP in the absence of the crisis and is a measure of potential GDP. The gap between the two lines over the forecast period suggests inflationary pressures will remain subdued.

## ... and the RBA has little policy room



The RBA Board meets next Tuesday for its monthly monetary policy decision. Inflation is below target, while GDP is below potential. However, the RBA has reached the effective limit of traditional policy. It has cut the cash rate to 0.1%, but also reduced rates on government bonds (to about 0.1%) out to 3 years via secondary-market purchases.