

Submission to the 16th Series Australian Consumer Price Index Review

This paper presents the views of the South Australian Department of Treasury and Finance (DTF) on the review of the CPI being undertaken by the ABS. It does not necessarily represent the views of the Government of South Australia.

Principal Purpose of the CPI

DTF agrees that the principal purpose of the CPI should remain the provision of a general measure of price inflation for the household sector. The conceptual basis for the CPI should remain targeted at producing an official headline measure of household price inflation for the purpose of setting monetary policy. In that context DTF defers to the judgement of the monetary authorities on the following matters covered in this review to the extent that they relate to this principal purpose of the CPI:

- The *acquisitions* approach as the conceptual basis for measuring price inflation faced by households;
- The treatment of expenditure on owner-occupied housing costs;
- The treatment of interest paid by households;
- Evaluation of the deposit and loan facilities index; and
- Commodity classification.

DTF does have an interest, however, in the measurement of changes in prices affecting different groups in the community. The ABS attempts to meet this need through the compilation of the Analytical Living Cost Indexes and the work being done to produce the new Pensioner and Beneficiary Living Cost Index. DTF does not see these living cost indexes as alternatives to the CPI, nor a source of conflict to the relevance of the CPI. Each measure is serving a different purpose but the differences in conceptual basis and appropriate use should be made clear to users.

Compilation Frequency of the CPI

The current quarterly publication of the CPI is adequate for the needs of the DTF. The cost associated with switching to a monthly publication does not appear to be justified by the benefits, and in DTF's view such resources would be better utilised in meeting other statistical needs such as sample sizes for household surveys. Even within the statistical collections relating to prices, any additional resources if available would be better directed to the development of spatial price indexes and expansion of the analytical living cost indexes as discussed below.

Monthly 'flash estimates' between the quarterly measures of CPI are not considered a desirable 'middle ground' either. Unless the current quarterly process was fully replicated on a monthly basis, the quality of monthly estimates may be inferior to the quarterly estimates and potentially a source of greater uncertainty. It would seem that, to the extent that there is a demand for a monthly CPI estimate, that this demand is sufficiently met by the TD-MI inflation gauge.

Maintaining the Relevance of the CPI

A more frequent updating of the weighting regime of the CPI via more frequent HES's would bring Australia in line with ILO recommendations as well as yielding the obvious benefits to the accuracy and relevance of the CPI. Examination of the benefits of more frequent CPI weight updates would be welcome, based on the experiences of other countries and the extent of contemporary shifts in spending patterns not just overall but in respect of population subgroups covered by the ALCIs and PBLCI.

Analytical Series

The ABS' Analytical Living Cost Indexes (ALCI's) are more relevant to State Government policy than the acquisitions based CPI which does not attempt to approximate the purchasing power of incomes and different circumstances faced by specific sectors of the community. The State Government currently provides assistance to certain low and fixed income households in the form of concessions and more broadly through various housing programs. Continued publication of the ALCI's and the work currently being done in relation to the Pensioner and Beneficiary Living Cost Index (PBLCI) is strongly supported. Further disaggregation of the current four ALCI's on the basis of housing tenure may also enhance the usefulness of the indices, particularly to assess whether there are differences between renters and owner occupiers. Longitudinal studies, for example, indicate that those who are persistently poor are predominantly renters. ALCI's available by primary income source *and* by tenure-type would be a useful enhancement if the underlying expenditure weights data were sufficiently robust. In relation to owner occupiers the possibility of using imputed rents as a measure of housing costs should be investigated.

In addition, the ABS applies quality adjustment techniques to measure the "pure" price movements – while this is appropriate in relation to the CPI as a measure of price inflation, in relation to living cost indexes it may not always be appropriate particularly in instances where improvements in the quality of goods and services impose unavoidable costs which may necessitate reduced consumption of other goods and services particularly for households on fixed incomes.

The Average Retail Prices catalogue in its current form is not considered useful. Although it provides some basis for comparison of price levels across the capital cities, the data provided do not provide a sufficiently broad coverage to draw conclusions about overall price movements affecting households, constraining their use in guiding policy. Resources currently devoted to this publication could be better used elsewhere.

Other Issues – Spatial Measures and Geographical Coverage

A spatial price index (SPI) which compares price *levels* between the capitals would be of considerable interest to DTF. Such indices would be useful in highlighting differences in the purchasing power of incomes among the state and territory capitals, particularly in the context of wage negotiations based on interstate comparison benchmarks and State promotional activities. It is considered likely that Adelaide has lower costs of living than other State capitals but in the absence of robust and transparent data which supports this conclusion it is difficult to be definitive (eg to inform the decisions of wage-setting bodies in cases where industrial arbitration is required).

A SPI must include a measure of current housing costs. Housing is one of the largest cost differences between the capitals, and a SPI which does not include this will not yield meaningful results.

While the development of an overall SPI would be the highest priority, SPIs for population sub-groups would be useful if they were feasible and their results proved to be within the statistical limits of reliability. DTF's needs for an SPI mainly relate to the comparative position of employee households between cities. An ability to assess differences between those in different housing tenures may also be useful. Relativities between metropolitan and non-metropolitan price levels would also be of policy interest, although it is recognised that the additional data collection costs would be significant. The Information Paper for the review does raise the issue of collecting non-metropolitan price data as part of the CPI. In DTF's view the benefit of collecting non-metropolitan price information would be more relevant in relation to a SPI than the CPI.

While the ABS may face additional costs in developing a SPI, it would appear likely that the ongoing costs would not be significant given that much of the information would be a by-product of the CPI (and in any case it may not need to be published on a high frequency). If there are any new or diverted resources made available as a result of this CPI review the development of an SPI would be of more value to DTF than any other proposals in the Information Paper such as monthly CPIs,

inclusion of non metropolitan prices or continuation of the Average Retail Prices catalogue.