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60 YEARS IMPACT

Research Insights

Is inflation starting to bite financially precarious Australians?

As spending on essential items increases, financially precarious Australians cut non-essential spending.

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Recent changes in spending and expected spending

In the last three years Australians' consumer behaviour has been affected by three distinct events. In 2020, COVID-19 travel restrictions and limitation on social activities reduced spending for transport services and recreational expenditure, with increased time spent at home boosting spending for grocery and home appliances (ABS Monthly spending indicator data).

When the restrictions were progressively lifted in 2021, consumer demand bounced back boosted by strong employment, savings accumulated over 2020 and generous fiscal policies. Although consumption increased, the strong demand was not fully matched by supply, causing a surge in inflation since the end of 2021[1]. The most recent data recorded an annual inflation rate of 7.8%[2], the highest level since 1990. To try to curb inflation the Reserve Bank of Australia (RBA) rose interest rates from a record low 0.1% in May to 3.35% in February 2023, with more hikes expected in the months ahead (RBA statement February 2023).

Growing interest rates impact cost of living pressures as mortgage payments, consumption credit rates and borrowing costs for households, businesses and governments become more expensive.

This Research Insight sheds light on Australians' spending behaviour in times of high inflation, focusing on both those who report struggling to make ends meet or worse (financially precarious) and those who report not struggling to make ends meet (financially comfortable).

The analysis uses data from 2,670 respondents of the Taking the Pulse of the Nation (TTPN) survey, a weekly survey representative of the Australian population that captures how Australians' attitudes and behaviours are shaped by the current social and economic issues. In April and October 2022, TTPN asked all respondents about changes in their current levels of spending compared to the prior year and how they expect their spending will change in the next six months (see Box 1).

BOX 1: MEASUREMENT OF RESPONDENTS' CHANGES IN THE CURRENT LEVEL OF SPENDING AND EXPECTED CHANGES IN SPENDING IN THE NEXT SIX MONTHS

In April and October of 2022, the Taking the Pulse of the Nation (TTPN) survey asked respondents to answer consider total spending and spending on the following 7 items:

Essential items (non-discretionary)

- Groceries and takeaway food
- Electricity, gas and water
- Rent or mortgage
- Transport (fuel, insurance, repairs, public transport, etc.)

Non-essential items (discretionary)

- Dining out in cafes, restaurants, pubs
- Recreation and culture (museums, cinemas, playing sports, gym, clubs, etc.)
- Traveling and holidays

For each item, respondents were asked the following:

- "Compared to this month one year ago, how has your spending today changed, for the following categories?"
- "Compared to your spending TODAY, thinking of your spending 6 months from now, how will your spending change?"

Respondents were offered seven response options for each question: "Increased by a lot", "Increased by a little", "Remained about the same", "Decreased by a little", "Decreased by a lot", "Does not apply", "Do not know".

[1] Tight labour market, supply chain bottlenecks, shortages in key components and materials and logistic disruptions restricted supply and caused a surge in prices. The war in Ukraine and the subsequent ban on Russian oil and gas exacerbated tensions in the energy market and added to inflation.
[2] Australian Bureau of Statistics. (Dec-quarter-2022). Consumer Price Index, Australia.

Key Insights

1 Financial precarity is increasing, particularly among younger cohorts that are more likely to have dependent children

There are signs of increasing financial precarity in Australia. In the six months from April to October 2022 the proportion of Australians reporting being in a financial precarious situation increased from 44.6% to 50.2% (Figure 1). The largest increase occurred among those aged 18-49, the age groups who are most likely to have dependent children (Figure 2).

Figure 1: Reported Financial Precarity in 2022 (%)

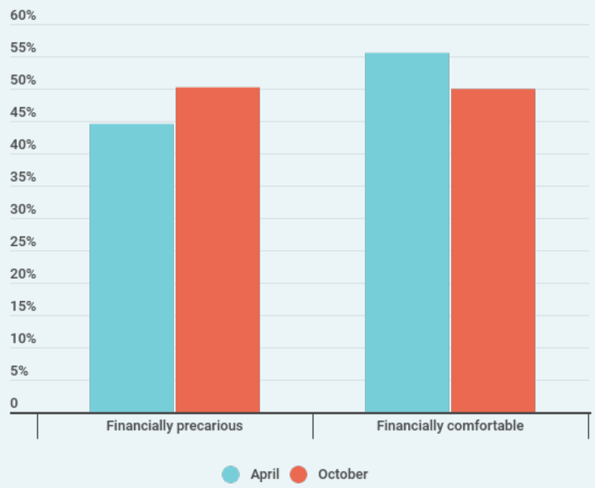
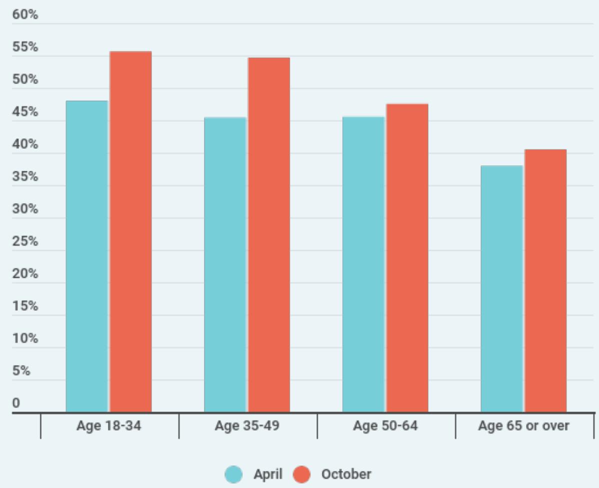


Figure 2: Reported Financial Precarity in 2022 by age (%)



2 Spending on essential items has grown for most Australians. Most of those in a financially precarious situation expect additional increases in essential spending in the months ahead

Table 1 documents that spending on essential items is the major driver for the increases in total spending. In October more than 70% of financially precarious Australians reported an increase in spending for groceries, utilities and transportation costs, with 65% also reporting a rise in rent or mortgage payments. The proportion of financially comfortable Australians who reported an increase on spending on necessities was only marginally lower.

Table 1: Spending on essential items by financial condition (2022)

Spending category	Financially precarious				Financially comfortable			
	Increase (%)		Decrease (%)		Increase (%)		Decrease (%)	
	April	October	April	October	April	October	April	October
Groceries	62.8	72.5	11.0	14.8	53.7	67.3	4.8	7.9
Rent or mortgage	44.5	64.9	3.6	3.5	28.8	55.4	4.6	5.9
Utilities	59.5	76.6	5.1	3.8	44.6	69.5	4.9	4.1
Transportation	67.1	79.5	7.4	4.8	57.4	73.1	5.8	7.9

In October, most Australians expected they would not be able to reduce essential spending in the coming months, but more so for those who report being financially precarious. As shown in Table 2, in October more than 70% of financially precarious Australians expected an increase in spending on utilities and transportation in the next 6 months, 65% expected a rise in spending on grocery and 60% in rent and mortgage payments.

Table 2: Expected spending on essential items in the next 6 months by financial condition (Oct 2022)

Spending category	Financially precarious		Financially comfortable	
	Increase (%)	Decrease (%)	Increase (%)	Decrease (%)
Groceries	65.0	11.9	60.8	6.3
Rent or mortgage	59.8	6.1	50.8	3.8
Utilities	74.0	5.7	66.0	4.1
Transportation	72.4	5.5	63.7	3.8

One possible reason why the financially precarious may report not being able to avoid future inflation is psychological: because it weighs more on their minds, they may be more likely to expect that it will continue. Another possible explanation, which is more worrying, is that financially precarious people have less opportunities to avoid inflation by way of reducing their use, or switching their sources of, essential services.

Financially precarious individuals may live in areas where there are no accessible public transport or lower-cost housing options and/or they may not be able to afford investments such as in insulation or solar panels that could help decrease their power bills.

3 To pay the bills, financially precarious Australians are more likely to cut back on non-essential items

To help offset higher essential spending, a large share of Australians cut back spending on non-essential items. Table 3 documents that those feeling financially precarious were more likely to cut back spending on dining out, holidays and recreational goods and shows that the proportion that reduced their non-essential spending increased from April to October.

Table 3: Spending on non-essential items by financial condition (2022)

Spending category	Financially precarious				Financially comfortable			
	Increase (%)		Decrease (%)		Increase (%)		Decrease (%)	
	April	October	April	October	April	October	April	October
Dining out	31.4	29.9	27.1	44.5	38.6	30.5	14.3	28.3
Recreationals	31.5	25.6	26.2	40.0	35.8	20.1	11.5	23.4
Holidays	36.4	28.3	26.6	45.7	47.0	36.0	14.0	25.7

The proportion of financially precarious Australians that reported a decrease in spending on dining out rose from 27% in April to 44% in October, the share that cut back recreational spending increased from 26% to 40% and the proportion that reduced spending on holidays rose from 27% in April to 46% in October.

Among Australians in a comfortable financial situation, the proportion of those reporting reductions in non-essential spending was relatively lower, but we still note an increase from April to October.

In October 2022 a substantive proportion of financially precarious Australians expected future declines in non-essential spending. Table 4 shows that the proportion that reported they would reduce spending in the next 6 months was 36.3% for dining out, 33.7% for recreational services and 34.2% for holidays.

Table 4: Expected spending on non-essential items in the next 6 months by financial condition (Oct 2022)

Spending category	Financially precarious		Financially comfortable	
	Increase (%)	Decrease (%)	Increase (%)	Decrease (%)
Dining out	27.6	36.3	31.8	21.1
Recreationals	26.8	33.7	26.1	14.6
Holidays	28.1	34.2	37.3	19.0

Policies to protect vulnerable Australians from the effects of high inflation

This study shows that in this period of high inflation, spending on necessities increased for most Australians. Although a large proportion of Australians had the economic resources to deal with inflationary pressures, some of those experiencing financial precarity needed to cut non-essential spending, like restaurant meals and holidays, to help pay for essential items like groceries and energy. As inflation is regressive[3], it is important that the government promotes policies that target those in low incomes who are at potential risk of financial hardship.

There are two main options available to government, the first being to boost social security payments and/or wages. The 5.2% increase in the minimum wage rate in 2022[4] helped low-income Australians deal with cost of living pressures, but a further large increase would be required next July to keep up with the pace of inflation and prevent a decline in real wages. The problem with relying on wage increases, however, is that they are also an important cost of production which exacerbates inflationary pressures. For this reason, instead of relying on wages, increasing targeted payments for essential services, such as rental assistance and/or an energy supplement, may be a better approach.

The second option to alleviate inflationary pressures is to focus on tackling supply-side of essential goods and services. The federal government's intervention in the coal and gas markets is one such approach, but this is only a one-off fix and further interventions of this kind are likely to be politically difficult and economically unsustainable to curb further inflation. Despite price caps, the federal government forecasts that households are likely to face large increases in electricity and gas bills (Federal Budget 2022-23). In response, the government recently announced $3b payments for low- and middle-income households to help meet rising energy costs. While welcome relief, the government should also focus on longer-term access to affordable energy for low-income households.

To better protect financially precarious households from future energy price spikes, more support is needed to help low-income earners reduce their reliance on gas and coal-fired electricity. A recent study finds that low-income households are disproportionately less likely to invest in solar panels, insulating the house or purchase more efficient appliances and cars (Prakash, 2023).

To reduce this gap, the government could offer higher subsidies for solar panels and home insulation to low-income households, renovate social houses to make them more energy efficient and incentivise communities to produce their own electricity from renewable sources. Accompanying any move, it would be important for the federal government to work with states to help fund the training of solar panel installers and insulation specialists to avoid another Home Insulation Program catastrophe[5].

So far, financially precarious Australians have dealt with high inflation by cutting back non-essential spending. What will happen if the price of essential goods keeps rising and their financial situation does not improve? Close monitoring of those at risk of financial hardship is needed to prevent vulnerable Australians becoming homeless or being forced to choose between eating or heating come winter.

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[3] See for example Erosa & Ventura (2012).
[4] In July 2022 the National Minimum Wage rose by 5.2% and employees covered by awards had their wage increased by 4.6%.
[5] To ease the effects of the Global Financial Crisis on the construction industry. the Australian Government introduced the Home Insulation Program (HIP) in February 2009. The HIP, which was giving incentives to insulate properties, was discontinued in 2010 following safety and poor training concerns after the death of four workers.

Further Information

Datasets:

These results have been drawn from Taking the Pulse of the Nation (TTPN), Melbourne Institute's survey. Each wave includes a set of core questions, as well as additional questions that address current and emerging issues facing Australians. The sample is stratified to reflect the Australian adult population in terms of age, gender, and location. The TTPN survey uses a repeated cross-sectional design. This Research Insight has used data from waves 53 (collected between 11th April and 2nd May 2022) and 59 (collected between 3rd and 31st October 2022). The sample used in the analysis contains answers from 2,670 individuals.

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Research Insights produced by the Melbourne Institute provide a clear and practical understanding of contemporary economic and social issues in Australia.

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