

If everyone's feeling the squeeze, where's all this inflation coming from?

Commonwealth Bank · 2026-09-14 · English original

Key points

- Inflation measures how fast prices are rising, not how households are feeling.
- The squeeze isn't even, with older Australians spending more strongly than younger, mortgage-heavy households.
- Rate rises can cool demand, but they can't directly fix every source of inflation.

If everyone is cutting back, why is inflation still high?

It's a question that goes to the heart of Australia's current cost-of-living squeeze.

Households have been dealing with years of higher prices, while mortgage holders have also been hit by three interest rate rises since the start of 2026. Consumer confidence is weak, house prices have fallen and the economy is slowing.

Yet inflation remains stubbornly above the Reserve Bank of Australia's 2% to 3% target range.

RBA Deputy Governor Andrew Hauser acknowledged the frustration in a recent interview with the ABC's 7.30 program .

"People want inflation down. People are furious about inflation. I understand why. It's unfair. It hits people on low incomes. It damages price signals. It makes the job of companies difficult. What they want us to do is our job and bring inflation down," Hauser said.

The latest ABS inflation figures show annual inflation did actually ease from 3.8% in June to 3.5% in July. But trimmed mean inflation, which strips out some of the more volatile price movements to give a better sense of the underlying trend, remained at 3.6%.

So how can inflation still be a problem when so many people feel like they're already cutting back?

What does inflation actually measure?

The first thing to understand is that inflation doesn't measure how much we're buying. It measures how much prices are changing.

It also doesn't tell you how high prices have already become. As the RBA's Hauser said: "When people go to the supermarket every week, they look at the price of the goods they're buying, they compare them to where they were a few years ago and they say, 'Hell, what's going on here?'"

Imagine something that cost \$100 rises to \$110 one year and then \$113 the next. The rate of inflation has slowed considerably, but you're still paying \$13 more than you were before.

So where is the inflation actually coming from?

The short answer is: from several places at once. Some of it is coming from prices Australians can't easily avoid.

Housing was the biggest contributor to inflation in July, rising 5.0% over the year. Somewhat confusingly, the ABS definition of "housing" doesn't include mortgage costs. But among the things it does include, new dwelling construction prices rose 5.7%, rents 3.6% and electricity 6.1%. Other categories that saw gains were food and non-alcoholic beverages, up by 3.2%, while health prices increased 3.8%.

Some of the pressure is also coming from overseas. Higher oil, diesel, fertiliser and other costs linked to the Middle East conflict don't always reach consumers immediately. Businesses can absorb those costs for a while before eventually putting up their own prices and passing them through to customers.

The latest CommBank View says that delayed pass-through of costs is one reason inflation can remain high even as the economy slows. Firms have taken time to pass on higher input costs, meaning some of the impact is only now appearing in inflation.

Then there's a more structural problem: how much the Australian economy can produce.

The RBA's August Statement on Monetary Policy says the economy is still operating with capacity constraints. In other words, demand for some workers, goods and services remains stronger than the economy can comfortably supply without pushing up prices.

Weak productivity makes that harder. If businesses can't produce much more with the workers, equipment and technology they already have, the economy can run into shortages and results in rising costs sooner.

The CommBank view makes a similar point, saying productivity growth remains too low and Australia's supply side is too constrained to allow demand to grow much faster without adding to inflation. At the same time, investment in areas including AI, defence, renewables, transport and housing is competing for workers, capital and materials.

So inflation can keep running even while parts of the economy are clearly slowing.

Are Boomers doing all the spending?

No. But there is a big age divide. It's worth pointing out the label "Boomer" isn't quite right here because the data measures age groups rather than generations. That said, the difference in spending patterns is striking.

CommBank Household Spending Insights data showed spending among Australians aged 65 and over was 10.1% higher in June than a year earlier.

Spending growth among 25 to 34-year-olds was just 4.2%, while 35 to 44 and 45 to 54-year-olds recorded growth of 4.5%.

"Household consumption patterns diverge by age. Shifts in interest rates, inflation and wealth affect age cohorts differently, which can lead to varying rates of spending growth," CommBank Head of Australian Economics Belinda Allen said.

One obvious reason is housing debt. "These groups are more likely to have a mortgage, making them more sensitive to higher interest rates," Allen said of the younger and middle-aged groups.

Someone with a large mortgage feels a rate rise quickly through higher repayments. An older household that owns its home outright doesn't face the same hit, while people with substantial savings can receive more interest income when rates rise.

That doesn't mean older Australians are responsible for inflation, but it helps explain why saying "households are struggling" can hide very different experiences.

If mortgage holders are hurting, who is driving up demand?

Households are only one part of the economy. Businesses are investing, governments are spending and major projects are competing for workers and materials.

Australia's economy grew just 0.4% in the June quarter and 2.1% over the year, according to the latest ABS national accounts. The ABS said households continued to behave cautiously, even though there was increased spending and business investment in some parts of the economy.

CommBank's latest domestic outlook describes the economy as entering a cyclical slowdown, but says the mix of growth is changing.

Private demand is becoming more important, helped by business investment in areas including renewables and data centres. Public investment remains elevated, although it has come off its peak.

Household spending is also proving more resilient than might be expected given higher rates and weaker sentiment, although CommBank expects it to slow further.

So a mortgage holder cutting restaurant meals or putting off a new car matters. But that household isn't the whole economy.

Will more rate rises work?

They can, but not on every source of inflation and not immediately.

The RBA has lifted the cash rate three times this year, taking it to 4.35%. Governor Michele Bullock acknowledged the consequences at the Bank's August monetary policy media conference.

"I know that these increases have been tough for households with mortgages who are also facing high inflation," Bullock said.

Higher rates can't build more houses, lift productivity overnight or bring down the global oil price. What they can do is cool demand.

Mortgage borrowers have less money left after repayments. Borrowing becomes more expensive for businesses. Some investment and purchases get delayed.

Over time, that should reduce competition for limited workers and resources and make it harder for businesses to keep putting prices up as demand slows in the economy.

The RBA says the rate increases already delivered have not yet had their full effect and expects total spending to slow further.

Rates can also help prevent a temporary price shock from spreading through the rest of the economy and keep inflation expectations anchored.

For example, an overseas oil shock might initially push up fuel and freight costs. The RBA becomes more concerned if businesses increasingly pass those costs on, workers seek higher wages to cover

rising prices and people start expecting inflation to remain high.

That's when a temporary shock risks becoming more persistent.

So will the RBA raise rates again?

Hauser said Australia's economy was doing reasonably well on several broad measures, but added: "We have one big problem and that's inflation."

"The question now, frankly, for us is have we done enough or is more needed?" he said. CommBank currently expects one more 0.25 percentage point increase in November, which would take the cash rate to 4.60%, although it says a rise at the RBA's 28 to 29 September meeting is firmly on the table.

The complication is that higher rates don't affect everyone equally and their impact takes time.

That means the RBA has to judge what today's rate rises will do to spending and inflation months from now, rather than simply reacting to how households feel today.

Why doesn't the RBA just keep hiking until inflation is gone?

Because that would come with another cost.

The RBA has two main economic goals alongside maintaining financial stability: keeping inflation under control and supporting full employment.

Much higher rates could bring demand down more quickly, but could also mean weaker growth and more people losing their jobs.

Hauser said the RBA had chosen to take a more gradual path "to preserve as many of the gains to jobs in this country as we could".

That doesn't mean the RBA is comfortable with inflation staying high.

Its latest forecasts have underlying inflation remaining above 3% until around the middle of 2027 before easing to about 2.5% in early 2028.

The balancing act is to slow the economy enough to bring inflation down without slowing it more than necessary.

If inflation falls, will the cost of living fall too?

Usually, no. Lower inflation generally means prices are increasing more slowly. It doesn't mean the level of prices will return to where they were a few years ago.

That's why the supermarket experience Hauser described can linger long after the inflation rate itself has improved.

If something has risen from \$100 to \$120 over several years, getting inflation back to 2.5% doesn't make it cost \$100 again. It means the next price increase should be much smaller.

For living standards, the important shift comes when household incomes can grow faster than prices for a sustained period.

So what's the bottom line?

Australians cutting back and inflation remaining too high aren't contradictory.

The squeeze is landing very differently across households, and many of the prices still rising are for things people can't easily avoid. At the same time, global cost pressures, business and government demand, weak productivity and limits on how much the economy can supply are all playing a role.

Interest rates can cool that demand, but they work slowly and can't directly solve every source of inflation.

What matters most now is whether those pressures fade as the economy slows, or whether inflation remains persistent enough for the RBA to decide that more rate rises are needed.

- Economy
- Explainer
- News

Newsroom

For the latest news and announcements from Commonwealth Bank.

The information presented is an extract of a Global Economic and Markets Research (GEMR) Economic Insights report. GEMR is a business unit of the Commonwealth Bank of Australia ABN 48 123 123 124 AFSL 234945. This extract provides only a summary of the named report. Please use the link provided to access the full report, and view all relevant disclosures, analyst certifications and the independence statement. The named report is not investment research and nor does it purport to make any recommendations. Rather, the named report is for informational purposes only and is not to be relied upon for any investment purposes. This extract has been prepared without taking into account your objectives, financial situation (including your capacity to bear loss), knowledge, experience or needs. It is not to be construed as an act of solicitation, or an offer to buy or sell any financial products, or as a recommendation and/or investment advice. You should not act on the information contained in this extract or named report. To the extent that you choose to make any investment decision after reading this extract and/or named report you should not rely on it but consider its appropriateness and suitability to your own objectives, financial situation and needs, and, if appropriate, seek professional or independent financial advice, including tax and legal advice.

Source: <https://www.commbank.com.au/articles/newsroom/2026/09/if-everyone-is-feeling-the-cost-of-living-crunch-where-is-inflation-coming-from.html>