

Wages are not to blame for rising inflation

Analysis of the National Accounts and Reserve Bank data and forecasts confirms rising wages are not causing renewed inflation increases.

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February 2026

INTRODUCTION

The start of 2026 has marked a return to rising inflation. After a period of inflation mostly within or only marginally above the Reserve Bank's (RBA's) target band, inflation is back. The most recent consumer price index (CPI) figure showed inflation spiked to 3.8%. Even more worrying, the RBA's latest Statement on Monetary Policy forecast inflation peaking at 4.2% in the middle of 2026 and not returning to below 3% until the June quarter of 2027.

As was the case in 2022 and 2023 when the RBA increased interest rates in response to rising inflation, much debate has centred on the cause of this recent inflation spike. In those years, the Australia Institute played a central role in bringing to public attention the role that increased profits played in inflation.¹ That analysis, which was ultimately supported by the Organisation of Economic Cooperation and Development (OECD) and other international organisations, to some extent inspired the Fells Review into retail and company pricing that made similar conclusions.

Once again, using National Accounts data together with the RBA's own forecasts shows that, as was the case in 2022 and 2023, wages growth is not causing the increased inflation in the past 6 months, nor for that forecast over the next year. As a result, the

¹ Stanford et al (2023) "Profit-Price Inflation: Theory, International Evidence, and Policy Implications"
<https://australiainstitute.org.au/report/profit-price-inflation-theory-international-evidence-and-policy-implications/>

RBA’s decision in February to raise the cash rate from 3.6% to 3.85% involves a misreading of the factors driving the current rise in inflation.

The RBA raises interest rates to reduce household spending and, in turn, increase unemployment in the desire to then reduce wage growth. However, analysis of wage, inflation and productivity data during 2025 and the RBA’s forecasts for 2026 and beyond reveals that rising wages have not been the driver of the recent rise in inflation. More significantly, the RBA’s own forecasts over the next 2 years imply that wages will have a progressively smaller impact on rising prices.

While raising interest rates is the standard response to increased inflation, this briefing note reveals that, as was the case in 2021-23, rising inflation is not due to workers receiving higher wages. Their wage growth is not driving excessive household consumption nor requiring businesses to raise prices above inflation levels to cover labour costs. The data is clear that the cause of the spike in inflation lies elsewhere, and further rate rises will only serve to hurt workers who have been wrongly blamed for inflation.

WAGES ARE NOT DRIVING INFLATION

The Reserve Bank’s February 2026 *Statement on Monetary Policy* forecasts a wide range of economic indicators, including wages and prices out to June 2028.² These forecasts provide valuable information for calculating the drivers of inflation.

Importantly, the RBA expects annual wages growth to fall from 3.4% in the December 2025 half, to 3.1% in the June 2026 half, despite the RBA also expecting consumer prices to surge from 3.6% to 4.2%. This alone is enough to highlight that wages cannot be the cause of the inflation increases.

Table 1: RBA forecasts used to decompose the wage and non-wage share of CPI (%)

	Jun-25	Dec-25	Jun-26	Dec-26	Jun-27	Dec-27	Jun-28
Wage price index	3.4	3.4	3.1	3.1	3.1	3.1	3.0
Consumer price index	2.1	3.6	4.2	3.6	2.9	2.7	2.6
Labour productivity	0.1	0.7	0.6	0.6	0.6	0.7	0.7

Sources: RBA (2026)

Note: Forecasts are for rolling annual, 12-month, periods.

While the RBA does not publish a table that shows the ‘decomposition’ (or breakdown) of the role of wages and non-wage factors in driving inflation, it is possible to use the

² RBA (2026) *Statement on Monetary Policy – February 2026*, <https://www.rba.gov.au/publications/smp/2026/feb/>

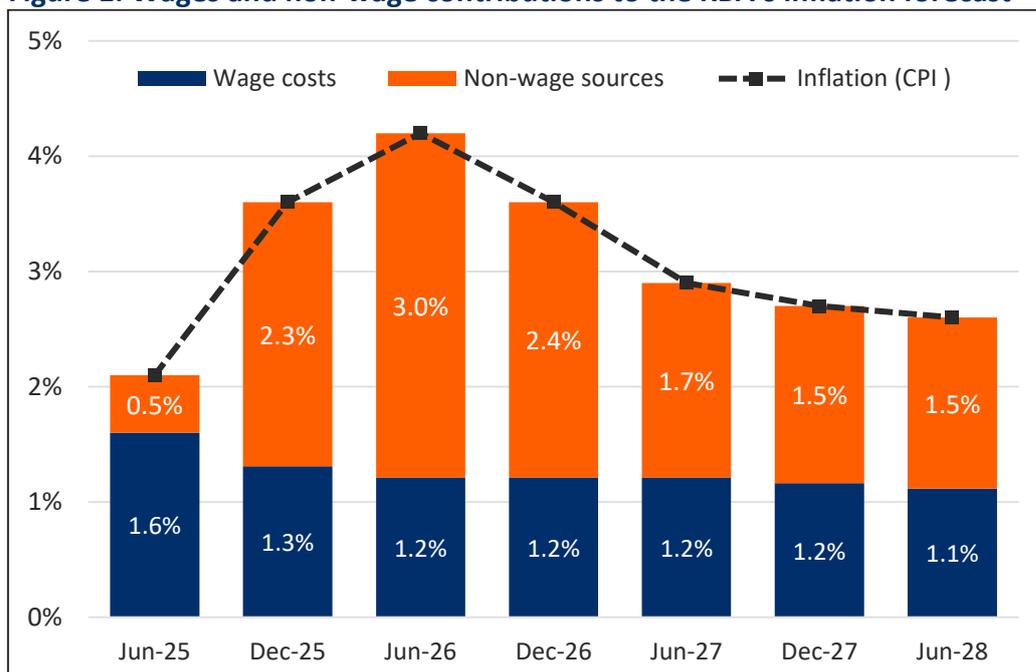
RBA’s forecasts, combined with data from the ABS *National Accounts* publication, to calculate the contribution of wage and non-wage factors to inflation.³

Essentially, GDP can be broken down into two parts: wages and other employee incomes, such as superannuation; and non-wage income such as company profits, the incomes of small businesses, and taxes less subsidies on production. To calculate the impact of wages on inflation, we have incorporated the RBA’s forecasts for productivity growth. We have then weighted the impact by using the share of wages in the domestic economy (48.5%).

Given these factors, it is clear that the RBA is implicitly forecasting that the increase in inflation over the next 12 months is due to a huge increase in non-wage income.

Figure 1 shows the breakdown of the RBA’s inflation forecast into contributions from wage and non-wage income. According to the RBA, over the first half of 2026, the surge in annual inflation is entirely due to a corresponding increase in non-wage incomes, most likely profits. Indeed, the RBA expects the contribution of wage growth to inflation to decline over the next two and half years.

Figure 1: Wages and non-wage contributions to the RBA’s inflation forecast



Sources: Analysis of RBA (2026) and ABS (2025)

Note: Figures from June 2026 onwards are for rolling annual, 12-month, periods based on RBA forecasts.

³ ABS (2024) *Australian System of National Accounts*, <https://www.abs.gov.au/statistics/economy/national-accounts/australian-system-national-accounts/>

For the 12 months to December 2025, inflation of 3.6% was comprised of a wage component of 1.3 percentage points and a non-wage component of 2.3 percentage points. This was a major change from the previous period, 12-months to June 2025, where the wages component accounted for 1.6 percentage points, and non-wage sources accounted for just 0.5 percentage points.

Just as significantly, the RBA now forecasts inflation to peak in June 2026 at 4.2% annually, but it also forecasts wages to contribute a reduced amount of 1.2 percentage points, while the non-wage contribution jumps to 3 percentage points.

The jump in non-wage contributions coupled with the decline in the contribution of wages marks out the folly of the RBA decision to raise interest rates to slow wage growth. Not only is wage growth forecast to have a declining impact on prices over the next two years, but the recent inflation increases, which the RBA's is now reacting to, according to the RBA's own figures was not caused by wage growth.

As the RBA does not forecast profit growth we are unable to assert definitively the main drivers of the non-wage components. However, the RBA itself in the February Statement on Monetary Policy noted that retailers have in the past year been able "to increase prices by more than might be expected given changes in the prices of imported consumer goods". Future data from the national accounts will enable greater insight of the precise non-wage drivers of inflation.

Put simply however, according to the RBA, wage costs explain only a small and shrinking part of the RBA's forecast increase in inflation over this coming year. The majority of the RBA's expected increase in the CPI is due to pressures from non-wage sources of income, in particular, the profit share of national income.

METHOD

It is possible to calculate the wage share of the RBA's projected CPI figure by converting their estimate of nominal wage growth into 'unit wage costs' using the RBA forecasts and the ABS's estimate of the share of nominal GDP attributable to wage costs. For example, for the year to June 2026 we know the following from Table 1:

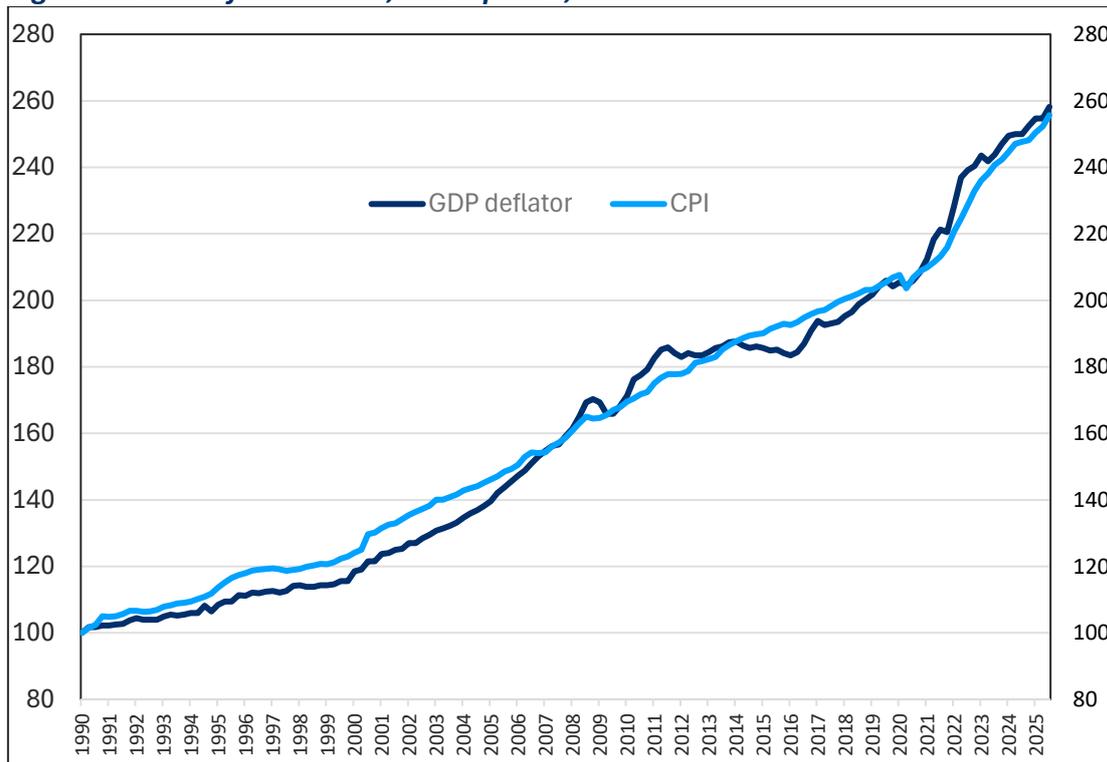
- The RBA expects nominal wages will increase 3.1%.
- The RBA expects productivity will increase 0.6%.
- The RBA forecast for nominal wage growth and productivity growth means the RBA expects wage costs will increase 2.5% per unit of output.

- But while the RBA expects wage costs per unit of output will increase by 2.5% we know from the ABS data that wage costs account for only 48.5% of GDP as measured from the income side.
- This means that the implied RBA forecast is that growth in unit wage costs will increase nominal GDP by for 1.2% (2.5% x 48.5%).
- Given that the RBA forecasts the CPI to increase by 4.2% over the same period and given that only 1.2% of that increase is expected to come from higher unit wage costs, then the remaining 3% of the RBA's forecast inflation must be due to non-wage factors.

TECHNICAL MATTERS

Ideally, rather than the CPI, we would use the GDP deflator to be consistent with the income components of GDP. However, the RBA does not provide forecasts for the GDP deflator. Fortunately, as Figure 2 shows, the GDP deflator and the CPI are highly correlated with a correlation coefficient of 99.6 over the period 1990 to 2025.

Figure 2: GDP deflator vs CPI, index points, March 1990=100



Sources: ABS (2025) & ABS (2026) *Consumer Price Index, Australia*,
<https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release>

Our estimates are conservative, and more conservative the further out we look. That is, because we use a fixed wages (compensation of employees) share of GDP to work out unit labour costs. We use the figure for 2024-25 whereas the RBA forecasts suggest the wages share of GDP will further contract the further into the future we go.

The non-wages share of GDP at factor cost includes:

- Gross operating surplus, which is a broad measure of company profits before deducting interest, tax, and depreciation, (68.4%).
- Mixed incomes, which are basically unincorporated businesses (mostly small businesses), (12.8%).
- Taxes less subsidies on production, (18.9%).
- An error term (-1%).

CONCLUSION

Every period of rising inflation is accompanied by an attempt to find something or someone to blame for the increased price growth. Unfortunately, because the most common and generally first response to inflation is to raise interest rates, this means that workers and their wages are reflexively the ones not only to be blamed for inflation, but also who are expected to shoulder the burden of solving it. Even worse, given the burden of higher rates falls more acutely on recent home buyers, the pain of rate rises more greatly affects those who are younger and on lower incomes than those who were likely to have taken out loans more than 10 or 15 years ago.

The RBA raises interest rates in order to slow household spending and also raise borrowing costs – especially for small businesses – such that businesses will either reduce hours or cut back on employees. This, in turn, will inevitably reduce the pressure on employers to offer higher wages in order to retain or attract workers.

However, this briefing note has found that the RBA's own figures and forecasts show that wage growth has not caused, nor are they expected to drive, the current increased levels of inflation.

The RBA's forecasts in the February Statement on Monetary Policy imply that wages will have a reduced impact on the level of inflation over the next 12 months, and that the spike in inflation forecast to happen in the year to June 2026 is entirely due to non-wage factors such as company and business profits.

In 2022 and 2023, workers were forced to shoulder the blame of inflation despite research by The Australia Institute, which was confirmed by the OECD and others, that found profits were the main driver of inflation.

Once again, workers are being hit with higher interest rates in order to reduce wages despite, once again, workers and their wages not being the cause of rising inflation.

