

Inflation and Cost of Living

Using data from the Household Income and Basic Amenities Survey (HIS/BA) and the Household Expenditure Survey (HES)¹ for 2009 and 2014; as well as the disaggregated state-level Consumer Price Index (CPI) data, this article analyses the cost of living for different groups of households in Malaysia. The HIS/BA is conducted every two to three years to collect statistics pertaining to the pattern of income distribution of the Malaysian households. The HES is conducted once every five years to collect comprehensive information on the level and pattern of consumption expenditure of households.

Differences between CPI inflation and the cost of living

The inflation rate, as measured by the change in the CPI, reflects the average rate of increase in the price of a basket of goods and services. The CPI is constructed by assuming that there is a single basket of goods and services which represents the consumption basket of all households in the country². Prices of goods and services that are used to construct the CPI are the average prices collected from retail outlets across the country. Thus, the CPI captures the average increase in prices with the assumption of homogeneity of spending patterns across households and holding the quantity and quality of the goods and services in the consumption basket as constant.

As the CPI reflects average prices in the economy, it provides a good measure of the changes in the overall price level of goods and services in the economy. As such, it is a relevant and useful indicator for the conduct of macroeconomic policies, such as monetary policy, that aims to affect the broader economy. The cost of living, on the other hand, refers to the amount of expenditure on goods and services incurred by households, including their financial obligations, to maintain a certain standard of living.

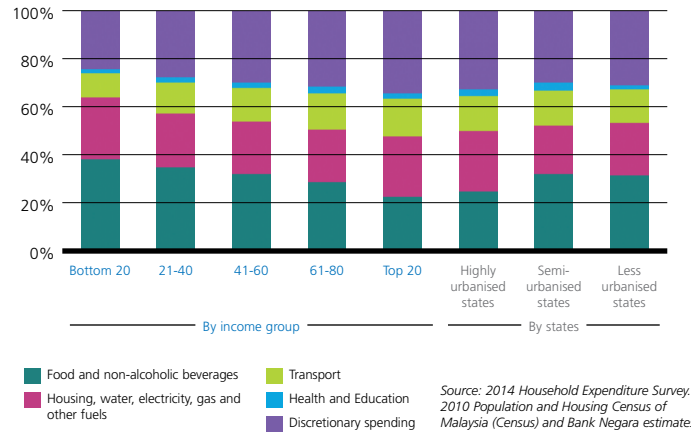
This spending or cost of living is determined by both household spending patterns and the prices faced by households. Spending patterns differ across households as the patterns are primarily influenced by household income, demography, family structure and area of residence. Price changes faced by households, in turn, vary by geographical factors.

As the CPI masks the heterogeneity in household spending patterns and the variations in price changes of goods and services faced by households, the inflation rate is considered as an approximation of the rate of increase in the cost of living.

Cost of living using household surveys and disaggregated CPI data

Chart 1 shows the differences in spending patterns across different income groups for households in Malaysia based on the most recent HES survey. The lower income groups allocate more of their expenditure on food and less for transport, healthcare, education and

Chart 1: Household Consumption Basket by Income Groups and States



that growth in expenditure was not only driven by higher prices, but also by an increase in the volume of consumption of goods and services. The strong growth in expenditure was observed across all income groups (Chart 2). Aggregate discretionary spending, in particular, rose strongly by 9.0% (Chart 4), contributed mainly by higher spending on restaurants and hotels, recreational services and communication (Chart 5).

The growth in aggregate expenditure was accompanied by an increase in aggregate household income, which increased by a CAGR of 8.8% during the same period. On average, the level of income exceeded the level of expenditure

for all income groups, allowing households to save a portion of their income (Chart 3). However, a more detailed analysis of the disaggregated data from the 2014 HIS/BA and 2014 HES reveals the following:

- **Disavver households.** There are households, mainly from the lower income groups, that spend more than their income.
- **The bottom 40% of households⁵.** Financial obligations of these households, including loan repayments, have registered relatively strong growth. Consequently, these households, who only have a relatively small amount of savings⁶, are vulnerable to both income and price shocks.
- **Households earning fixed incomes, including pensioners.** While aggregate income grew at an average of 8.8%, there are segments of the total population who experienced a much lower or no income growth. The analysis has shown that the inflation rates experienced by households vary due to differences in spending patterns and price changes. In particular, households in the lower income groups living in highly urbanised states experienced higher inflation. At the aggregated level, the rise in

Chart 2: Growth in Average Household Income and Expenditure*

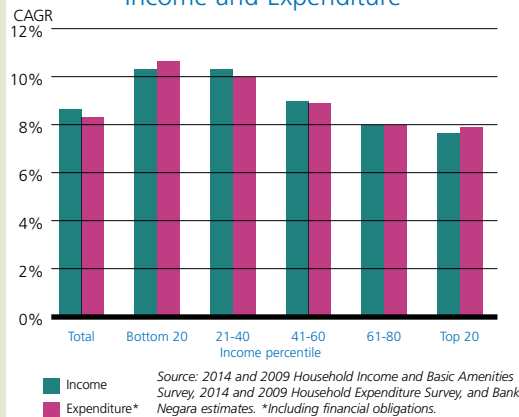
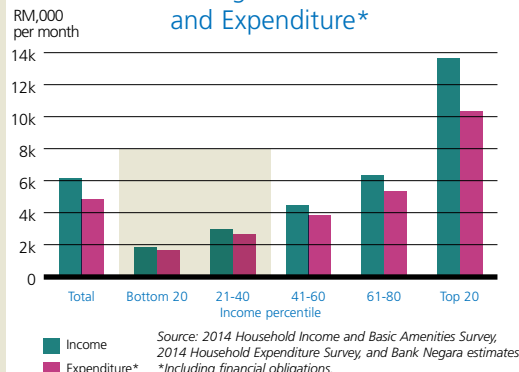


Chart 3: Average Household Income and Expenditure*



REHDA President assumes Chairmanship of BIPC

The Building Industry Presidents' Council (BIPC) is an industry body formed to be a pro-active platform of Presidents of Institutions in

the building industry. Its members comprise 7 permanent member organisations namely REHDA Malaysia, Pertubuhan Akitek Malaysia (PAM), Master Builders Association Malaysia (MBAM), The Institution of Engineer, Malaysia (IEM), Association of Consulting Engineers Malaysia (ACEM), Royal Institution of Surveyors Malaysia (RISM) and Malaysian Institute of Planners (MIP). BIPC selects its Chairman on a yearly basis, amongst the current Presidents of permanent member organisations based on a rotation system for no more than two terms of the calendar year that is 1 January to 31 December.

At the last BIPC meeting on 15 February 2017 at Wisma REHDA, the BIPC Chairmanship was officially handed over to REHDA from PAM for a term of one year. REHDA took the opportunity to update the BIPC members on pertinent industry matters including the proposed amendments to the Housing Development (Control and Licensing) Act, Water Services Industry Act 2006 as well as the imposition of IBS by CIDB based on projects of above 50,000 sqm. Current challenges and issues faced by the respective BIPC members were also discussed such as, among others, proposed implementation of steel scaffolding, recent requirement by BOMBA on insulated fire-rated door for lifts and standard living quarters for construction workers.

(L-R): Datuk S. Sivanyanam (REHDA Vice President), Datuk Seri FD Iskandar (REHDA President), Ar S. Thirlogachandran (PAM Honorary Treasurer) and Ir Tiah Oon Ling (REHDA Secretary General).

Chart 4: Growth in Average Household Expenditure by Type

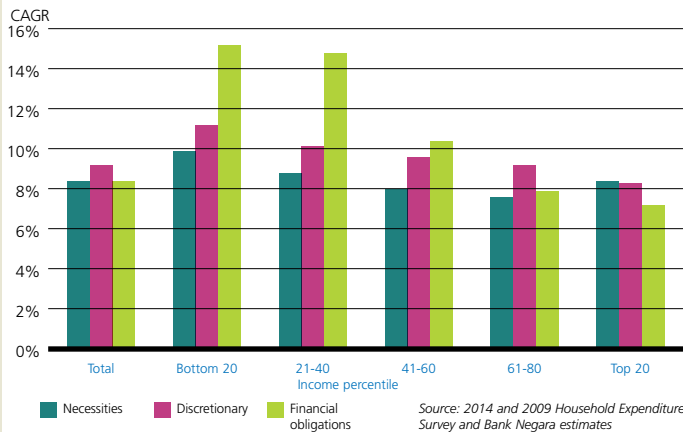
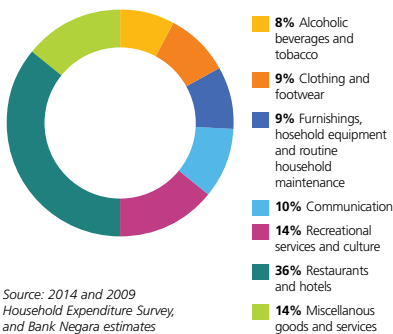


Chart 5: Contribution to Growth in Discretionary Spending



the cost of living, on average, has been accompanied by a commensurate increase in income. At a disaggregated level, however, analysis of both income and expenditure data shows that there are segments of the society that are vulnerable to the increase in the cost of living, and these are households who dissaved; the bottom 40% of households; and households earning fixed incomes.

- Both the HIS/BA and the HES are carried out using a personal interview approach, covering urban and rural areas for all states. The surveys are carried out by probability sampling that represents all households in Malaysia.
- The composition of goods and services in the CPI basket and their respective weights are determined based on the aggregate household expenditure patterns obtained from a nationwide expenditure survey. In Malaysia, the CPI basket is revised every five years based on the Household Expenditure Survey as per international practice. The latest CPI weights, based on the 2014 survey, were released in January 2016.
- Highly urbanised states are states that register urbanisation levels of above 70%. The level of urbanisation is computed in the 2010 Population and Housing Census of Malaysia (Census 2010). These states include Kuala Lumpur, Selangor and Putrajaya, Pulau Pinang, Melaka and Johor. The less urbanised states are states that register urbanisation levels of below 55%. These states include Sabah, Sarawak, Pahang and Kelantan.
- Financial obligations include transfer payments such as contribution to the Employees Provident Fund (EPF) and income tax payments; as well as the repayment of loans.
- The bottom 40% of households are households which fall under the bottom 40% of the nation's income distribution, which is below RM3,649 based on the 2014 HIS/BA.
- About 28% of the bottom 40% of households do not save on a monthly basis, while 11% of them save RM100 or less a month.

Conclusion

In addressing the issue of the rising cost of living, the policy approach must be multi-dimensional, including measures to address the challenges of urbanisation such as housing and connectivity, improving financial education and awareness, and enhancing productivity and income. Of importance, greater efforts would need to be directed at increasing the productivity level of Malaysians through the adoption of modern technology and increasing the skills of workers through access to better education and training. This would enable Malaysians to move up the value chain towards higher value-added jobs to achieve higher income and hence, afford a higher standard of living.

