

Australia Economic Watch

RBA review: The reluctant hiker's last raise?

One more hike, just in case

The RBA delivered a 25bps hike to 4.35% today after four consecutive pauses. The case to hike was stronger than the case to pause at this meeting as “inflation is proving more persistent than expected a few months ago”. While the RBA retains its option to hike open, we see this hike as an insurance hike to reinforce the hawkish stance, but we don't expect any further tightening this year or in 2024. See note: [Australia Economic Watch: RBA preview: Should I hike, or should I hold? 01 November 2023](#)

The Bank remains data dependent: “Whether further tightening of monetary policy is required to ensure that inflation returns to target in a reasonable timeframe will depend upon the data and the evolving assessment of risks”. We see more upside risk to unemployment versus inflation, so we do not expect further tightening at this point.

How long can the RBA retain a hawkish bias?

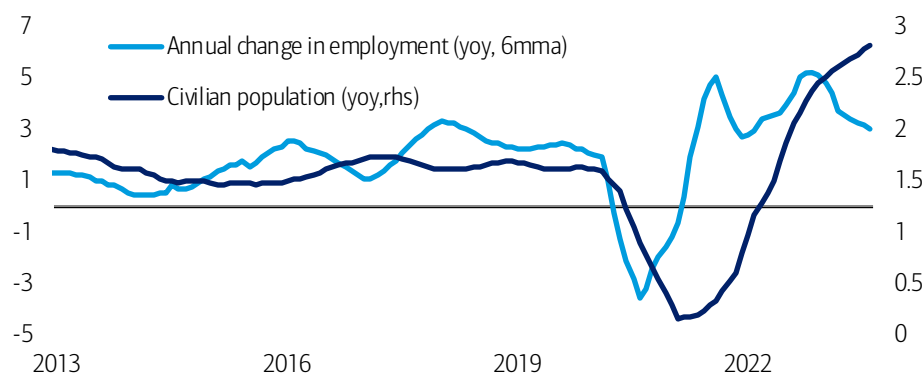
The RBA's strong hawkish stance means policy is more likely to be tightened than eased as inflation remains above target at 5.4%yoy. However, demand has continued to slow, and the labour market is no longer tightening. Population growth is now above pre-pandemic levels while employment growth has peaked. Further tightening means the probability of a hard landing will increase. The RBA now expects a slightly lower unemployment rate than before and inflation to reach the top of the target in late 2025.

Close paid November RBA at target

The RBA's decision to raise rates lifts November OIS to our target of 4.32% (entry 4.24%, stop 4.2%) and we close the trade recommendation. Given ambiguity around RBA communication and signs of a potential inflection point in offshore data, we recommend trading tactically and see Dec/Feb trading within 5-15bps. We also like paying terminal at around 10-12bps and receiving at around 30bps.

Exhibit 1: Population growth is rising while employment growth is slowing

Reflecting early signs of increased spare capacity



Source: ABS

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Economics
Australasia

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Minor changes to forecasts

As we had expected, the RBA's Board judged an increase in interest rates was warranted today to be more assured that inflation would return to target in a reasonable timeframe. See note: [Asia Economic Weekly: Australia – RBA's time to tighten 03 November 2023](#).

Ahead of the Statement on Monetary Policy due on Friday, the RBA highlighted modest changes to their forecasts for inflation and the unemployment rate. These changes seem to increase flexibility around reaching the inflation target. CPI is now expected to be around 3.5% by the end of 2024 and at the top of the range by the end of 2025 versus previous assumption for inflation to reach the mid-point of the target by late-2025.

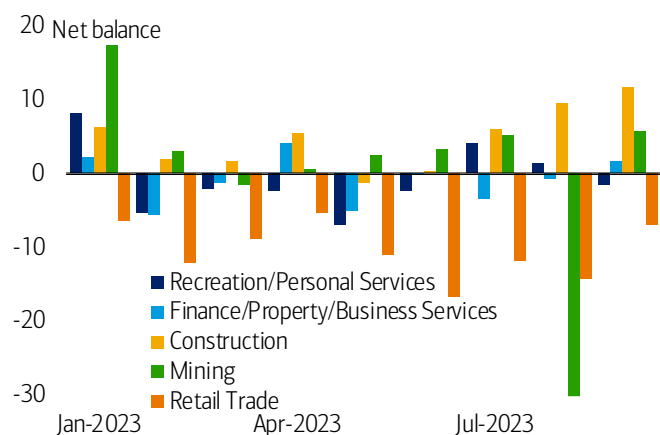
For unemployment, the RBA now expects a more gradual increase to 4.25% from 4.5% by year end. While spending has picked up ahead of the Christmas period, the retail sector's outlook for the next 12 months is pessimistic (Exhibit 2).

Ahead of the December Board meeting, the RBA will receive several economic releases and speeches will step up (Exhibit 3). Wages prices data will be in focus as it will reflect public sector rises from July 1 along with increases in the health and education sectors. Leading indicators for wages suggest private sector increases have peaked. In the RBA's view, wages growth remains consistent with the inflation target.

Labour market data for October will be important as well as monthly CPI. Leading indicators for the labour market have softened with job vacancies down 3% in the month. Headline monthly CPI will likely be pushed higher by energy prices but rent relief will likely weigh on rental inflation.

Exhibit 2: Business confidence across industries

Services and retail softened of late, mining and construction improved



Source: NAB, Macrobond

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Exhibit 3: Upcoming releases

Rump up of RBA communication ahead of the December meeting

10-Nov	RBA Statement on Monetary Policy
15-Nov	Wage Price Index (3Q)
16-Nov	Labour force data for October
21-Nov	RBA's Bullock Panel
21-Nov	RBA Minutes (Nov)
22-Nov	RBA's Bullock speech
28-Nov	Retail Sales (Oct)
29-Nov	Construction Work done (3Q)
29-Nov	Monthly CPI (Oct)
30-Nov	Private sector credit (Oct)
4-Dec	Business indicators (3Q)
5-Dec	Net Exports of GDP (3Q)
5-Dec	RBA decision (Dec)

Source: RBA, Bloomberg, BoFA Global Research

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No appetite for active QT

The Board did not mention quantitative tightening (QT). Our baseline scenario now assumes the RBA does not commence active bond sales in the foreseeable future and instead relies on maturities (without reinvestments) to reduce its balance sheet. A more aggressive form of balance-sheet normalisation is still plausible, but the RBA has declined several opportunities to indicate potential asset sales and active QT is now a risk scenario rather than our base case.

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