

Australia Watch

RBA review: Not ruling anything in or out

The RBA on hold in March, no April meeting

The Reserve Bank of Australia (RBA) kept rates on hold at 4.35%. As discussed here: [RBA preview: Tone it down](#), the decision to keep rates unchanged was consensus, but the RBA's hawkish guidance was jeopardised by a round of softer data. Monthly inflation was unchanged at 3.4% in January and GDP showed that household spending remains weak (see: [GDP review](#)). The Bank has removed the reference to further tightening, which suggests easing could come earlier than we expect (Feb-25).

Exhibit 1: The evolution of guidance is modestly dovish

As the Bank removes the reference to further increases in interest rates

February	The path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe will depend upon the data and the evolving assessment of risks, and a further increase in interest rates cannot be ruled out.
March	The path of interest rates that will best ensure that inflation returns to target in a reasonable timeframe remains uncertain and the Board is not ruling anything in or out.

Source: RBA

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As we anticipated, the Bank will now pay closer attention to measures of labour market tightness as well as inflation as it tries to preserve employment gains. In the RBA's view, unemployment and the broader underutilisation rate are expected to increase further.

The unemployment rate is now at 4.1% vs the RBA's assumption for 4.2% by June. At the current pace, unemployment is likely to be weaker than the RBA's projections. Data for February will be released on Thursday, and we expect a modest decline in unemployment to 4% driven by a strong 55k jobs and a modest rise in participation to 66.9% from 66.8%. Softer outcomes will be a concern for the RBA and along with softer inflation prints and weak retail spending the case for easing in H2 2024 could strengthen.

Markets: long bias in rates... but wait for jobs, FOMC

It is unsurprising that the RBA, which has been reluctant to raise rates aggressively, would respond to weaker-than-expected domestic data with slightly more dovish communication. The Board's decision to 'not rul[e] anything in or out' is a clear signal that the RBA is mulling its options.

The challenge for trading strategy is the sequence of data with the FOMC and jobs data due on Thursday. While we maintain a long bias, our economist's view that strong jobs growth will depress headline unemployment means that we may get better entry levels. The FOMC's decision could also impact valuations – any de-anchoring of 3 cuts could see cheaper front-end rates in Australia, which moves at a beta to US rates. 2y rates therefore looks cheap but the FOMC meeting and AU jobs report will be key to near-term moves. Richer front-end rates favours near-term weakness in the AUD, although we see tailwinds for the currency from USD depreciation in H2 2024.

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Watch the underlying data

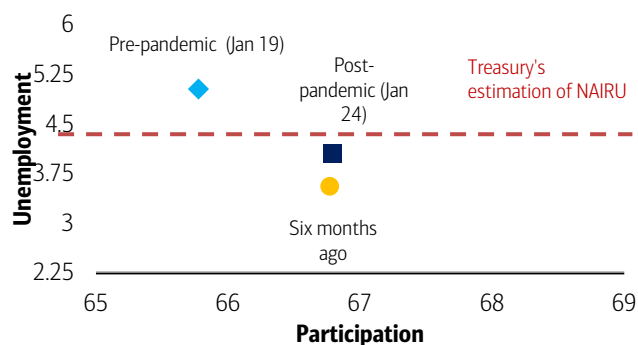
The RBA has historically been reactive to rises in unemployment. In previous cycles, we identified the Bank's guidance was consistently dovish when unemployment increased by around 0.5ppts. At the moment, we could argue unemployment has gone up enough (Exhibit 2) for the RBA to shift to a more dovish stance. Given unemployment remains very low and participation is at record-high (Exhibit 3), we see increased uncertainty around the RBA's reaction function in this low unemployment/above target inflation environment.

There are one-off factors in February that may add volatility to the labour market data, including (1) participation could rebound after people return from leave in January (2) employment growth could be temporarily boosted by one-off spending from Taylor Swift's concerts. Notably, weekly payroll data was consistent with this view. Jobs rose 2% in the month as people return to work after the summer break.

Conversely, the recent slowdown in employment growth from high levels as well as some stabilisation in population growth (RBA forecasts is for the resident population to eased to 2% by June from 2.4%) could offset the rise in participation. The latter means the economy may need fewer job gains to keep unemployment low. We forecast strong jobs growth of 55,000 in February (vs 500 in January) and we see an increase in the participation rate to 66.9% (vs 66.8% prior). This would mean a fall in unemployment to 4% (vs 4.1%) yoy.

Exhibit 2: The labour market remains tight

But unemployment is rising

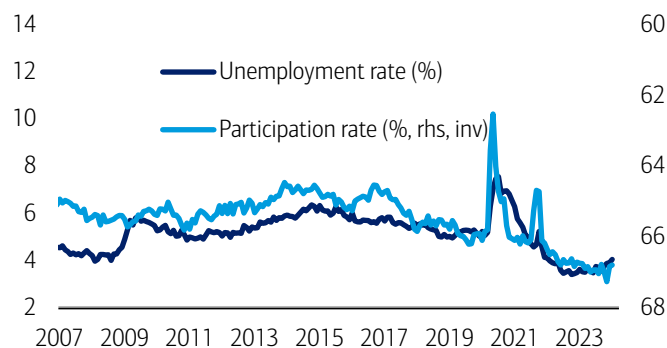


Source: ABS, NAIRU: Non-accelerating inflation rate of unemployment

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Exhibit 3: Unemployment remains very low relative to history

Despite participation rising to a record high



Source: ABS

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Recent changes to the RBA Board, Governor, Board meetings and Statement on Monetary Policy mean the RBA is now willing to share more detail around its forecasts. Assumptions on population growth are available as is forecast for real wages growth, households savings rate and labour productivity (Exhibit 4). These are major changes to increase transparency across how the Bank produces its forecasts. In addition, the RBA has included a forecast for the cash rate that results from an average of consensus economists and market pricing. The latter is below our expectations for rates on hold in 2024 and modest easing to 3.1% by end of 2025 (Exhibit 5).

The March Board meeting was Andrew Hauser's first Board meeting as Deputy Governor so we may see some discussion about the balance sheet as we approach the Term Funding Facility (TFF) maturity (see: [Banks - Australia: Hitting the TFF maturity wall 07 March 2024](#)). We expect any discussion about the pace of balance-sheet rundown to be in the minutes (due on April 2).

Exhibit 4: RBA forecasts

We expect the Bank to place emphasis on underutilisation

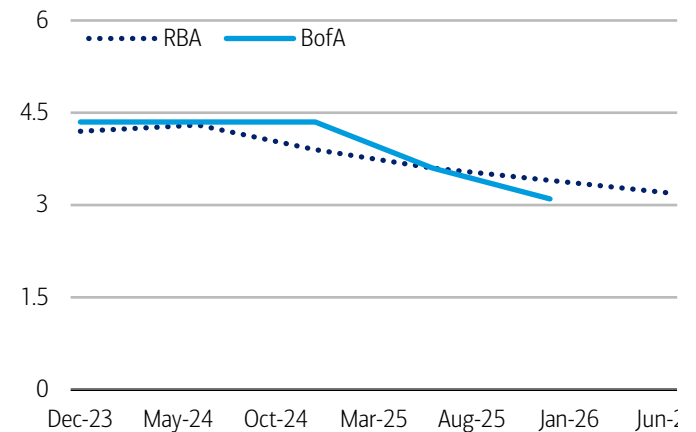
	Dec-23	Jun-24	Dec-24	Jun-25	Dec-25	Jun-26
Unemployment	3.8	4.2	4.3	4.4	4.4	4.4
Estimated resident population	2.4	2	1.6	1.4	1.4	1.4
Hours-based underutilisation rate	5.2	5.8	6	6.2	6.2	6.2
Labour productivity	-0.5	3	1.4	1.1	1.2	1.1
Households savings rate	0.9	1	1.7	2.4	2.7	2.7
Real Wage Price Index	0.1	0.8	0.4	0.5	0.6	0.6

Source: ABS

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Exhibit 5: RBA's assumption for the cash rate

Includes an average of consensus and market pricing for easing



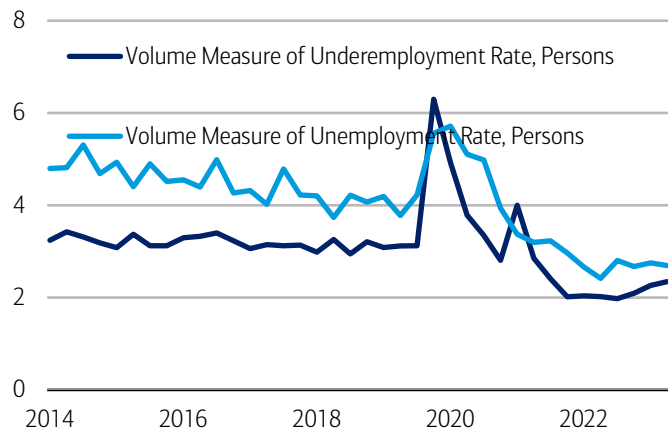
Source: RBA

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In our view, the RBA will focus on broader measures of unemployment, particularly volume-based ones. These measures remove the volatility in the monthly data and provide a better gauge of tightness in the labour market. Hours worked, which have declined 0.5% since last February (in trend terms) could also reflect a softer picture than the unemployment rate. Pre-pandemic, the volume measure of unemployment rate was 3.8% while the latest available data is 2.7%. Note that these measures are quarterly and are only available until December 2023.

Exhibit 6: Broader measures of unemployment

Will be important for the outlook for rates

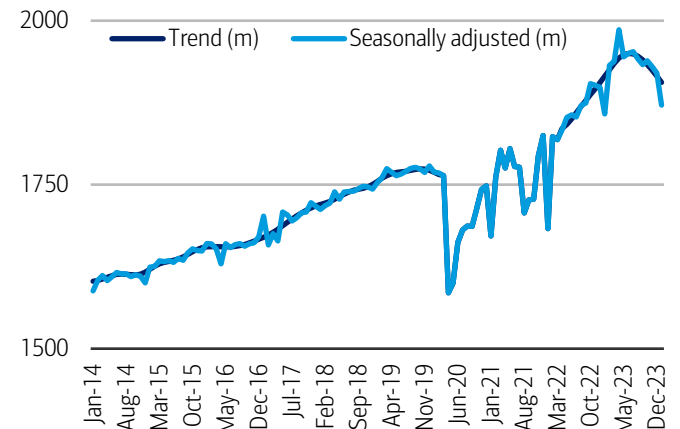


Source: ABS, Macrobond

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Exhibit 7: Hours worked declined

But remain elevated



Source: ABS

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