

# Australia Economic Watch

## RBA review: A surprising pause

### The RBA pauses again at 4.1% and highlights risks

The Reserve Bank of Australia held rates unchanged at 4.1% for the second consecutive month. We had expected one more hike to address high persistent inflation and a very tight labour market, but guidance suggests uncertainties around the outlook and weaker consumer spending has weighed more on today's decision.

The Bank believes "higher interest rates are working to establish a more sustainable balance between supply and demand in the economy and will continue to do so". Some evidence of traction from high rates along with uncertainty surrounding the economic outlook pushed the Board to hold interest rates steady this month.

Notably, in the RBA's view, recent data are consistent with inflation returning to the inflation target range over the forecast horizon and with output and employment continuing to grow. We do not expect further hikes at this stage but see risk for a further hike in November as 3Q inflation data will be strong. Softer than expected CPI outcomes in 2Q seemed to have allowed the Bank to remain focused on growth and employment while ensuring the inflation target can be reached over time.

However, the RBA highlights risks to the inflation outlook. In the short-term, 3Q CPI will be strong due to a spike in electricity prices, rent inflation, seasonals and communication rises. Beyond 3Q, risk is for services price inflation proving more persistent than expected, as it has been the case overseas.

On the downside, the outlook for household consumption is also an ongoing source of uncertainty for the Bank. Cost-of-living pressures and higher interest rates were evident in 1Q GDP data, and we will get an update for 2Q GDP just after the September Board meeting, which would be Phil Lowe's last as the Governor.

### Forecast changes suggest a soft landing

The RBA will publish a Statement on Monetary Policy on Friday along with a new round of forecasts. The central forecast is for CPI inflation to continue to decline, to be around 3.25% by the end of 2024 and to be back within the 2-3% target range in late 2025. The current assumption is for inflation to reach 3% in June-2025.

As for the economy, below-trend growth is expected to continue for a while. Household consumption growth is weak, as is dwelling investment. The central forecast is for GDP growth of around 1.75% over (from 1.5%) 2024 and a little above 2% over the following year. The unemployment rate is expected to rise gradually from its current rate to 4.5% (unchanged) by the end of next year. These minor changes to the Bank's forecasts suggest some comfort around the current inflation pulse and the level of growth that supports an unemployment rate below 5%. These forecasts would represent an ideal soft-landing for the RBA as the strong labour market would continue to support aggregate demand. Indeed, there seems to be more patience on returning inflation back to target.

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## Traction from high rates and soft landings

A surprise pause relative to consensus and our expectations means the RBA has found some comfort on the economic data and the need to address inflation pressures is now less urgent as high rates gain traction and global prices ease. See: [Australia Economic Watch: CPI review: Softer but persistent 26 July 2023](#).

The RBA will provide an update to their forecast and views in the Statement on Monetary Policy due for release on Friday. The RBA now expects slightly better growth outcome and a modest delay in reaching the inflation target (Exhibit 1) We provide our best guess for the overall forecast changes in the table and highlight the published numbers ahead of release in yellow.

### Exhibit 1: SMP Forecasts update

Our best guess. Focus on inflation

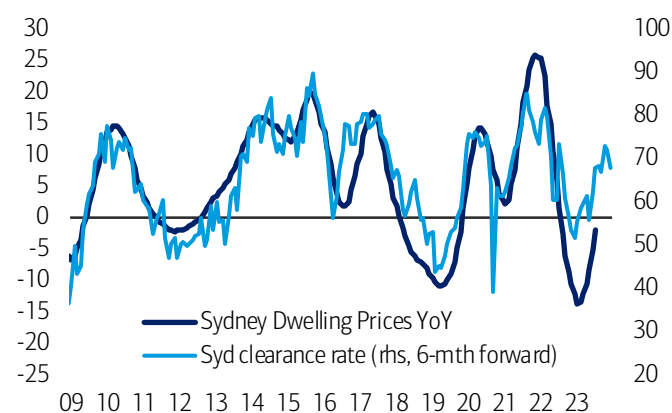
	Jun 2023	Dec 2023	June 2024	Dec 2024	Jun 2025	Dec 2025
<b>Year-Ended %</b>						
GDP	1.50	1.00	1.75	1.75	1.75	2.25
May-23	1.75	1.25	1.50	1.75	2.00	-
<b>Unemployment</b>	3.50	3.75	4.00	4.50	4.50	4.50
May-23	3.50	4.00	4.25	4.50	4.50	-
<b>CPI</b>	6.00	4.25	3.25	3.25	3.00	2.75
May-23	6.25	4.50	3.50	3.25	3.00	-
<b>Underlying CPI (Trimmed Mean)</b>	5.90	4.50	3.50	3.25	3.00	2.75
May-23	6.00	4.00	3.25	3.00	3.00	-
<b>Wages</b>	3.7	3.50	3.25	3.00	2.75	2.75
May-23	3.75	4.0	3.3	3.1	2.9	-

Source: RBA

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### Exhibit 2: House prices are picking up

As the RBA reaches the end of the hiking cycle



Source: CoreLogic

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Focus may shift to financial stability as we approach the end of the hiking cycle. House prices recorded the fifth consecutive month of increase by growing 0.7% in July. The increase was broad-based though the monthly pace of growth in Sydney housing has declined as the number of listings rises. Leading indicators of activity suggest house prices will continue to rise in the next six month (Exhibit 2), but at a slower pace than during the previous cycle, in our view. The national rental index increased by 0.6% in July, the 35<sup>th</sup> consecutive month of increases.

Most importantly for the inflation outlook, rent prices increased by 0.6% and this marks the 35<sup>th</sup> consecutive rise. The strongest rental conditions seen across the unit sector, where rents were up 2.9% over the three months to July nationally, compared with a 1.9% rise in house rents. The RBA has noted rent inflation, for which inflation was typically quite persistent is still too high.

## Beyond August

Monthly inflation data for July will be the first gauge for price pressures in 3Q. This is due for release on Aug 31<sup>st</sup>. Also, an update to wages growth will be out on Aug 15 for 2Q and should reflect public sector rises. Monthly labour force, confidence measures, house prices and credit growth will be closely watched as well as some partial data for 2Q GDP due for release on Sep 6.

We expect another pause in September, but an upside surprise to inflation in 3Q could trigger another hike in November, provided the labour market remains in good shape and economic growth does not decline faster than expected. While the tone in the RBA's Statement is dovish as current conditions are mixed, they highlight significant uncertainty the outlook for inflation.

**Exhibit 3: Upcoming releases**

Wages, Monthly CPI and Labour force ahead of the September meeting

<b>4-Aug</b>	<b>RBA Statement on Monetary Policy (Aug)</b>	<b>3-Oct</b>	<b>RBA Cash Rate decision (Oct)</b>
15-Aug	RBA Minutes (Aug)	17-Oct	RBA Minutes (Oct)
<b>15-Aug</b>	<b>Wages (2Q)</b>	<b>19-Oct</b>	<b>Employment (Sep)</b>
<b>17-Aug</b>	<b>Employment (Jul)</b>	<b>25-Oct</b>	<b>Quarterly CPI (3Q)</b>
28-Aug	Retail Sales (Jul)	25-Oct	Monthly CPI (Aug)
30-Aug	Monthly CPI (Jul)	30-Oct	Retail Sales (Sep)
<b>5-Sep</b>	<b>RBA Cash Rate decision (Sep)</b>	<b>7-Nov</b>	<b>RBA Cash Rate decision (Nov)</b>
<b>6-Sep</b>	<b>GDP (2Q)</b>	<b>15-Nov</b>	<b>Wages (3Q)</b>
19-Sep	RBA Minutes (Sep)	<b>16-Nov</b>	<b>Employment (Oct)</b>
27-Sep	Monthly CPI (Aug)	21-Nov	RBA Minutes (Nov)
28-Sep	Retail Sales (Aug)		

Source: ABS

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