

NAB Monetary Policy Update 10 April 2025



A fast return to neutral and additional support

NAB Economics

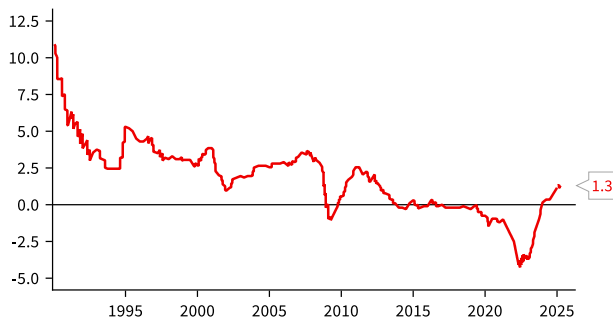
Key points

- We now see the RBA easing more quickly through mid-2025 taking the cash rate to 2.6% by February.
- We expect the RBA to cut by 50bps in May, followed by 25bps in July, August, November and February.
- Headwinds from the global environment have intensified, but error bounds around our forecast are large given uncertainty remains exceptionally elevated.
- We have slightly revised up our unemployment rate in the near term, and shaved growth for 2025 but ultimately expect a larger policy response is required to keep activity on track.

RBA to ease more quickly, take policy modestly accommodative

Much has changed since the RBA Board last met in early April. Risks to both global and domestic growth have shifted to the downside. Against this backdrop, a restrictive policy stance in Australia is no longer appropriate, in our view. At present, the real cash rate in Australia (based on our 1Q CPI forecast for trimmed mean inflation) is well over 1%. As Chart 1 shows, this looks elevated relative to recent history.

Real Cash Rate (%)



Source: National Australia Bank, Macrobond

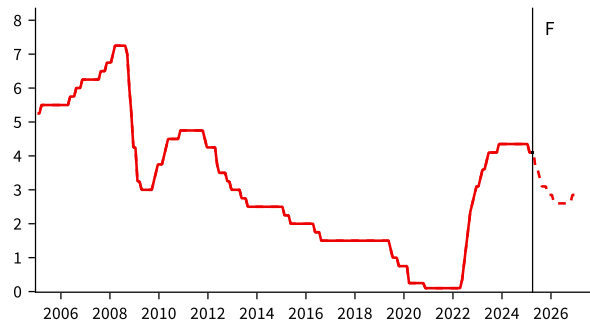
Accordingly, we now expect the RBA to cut the cash rate by 50bps at the May meeting (19th-20th) with follow up cuts of 25bps at each of the July and August meetings. In our view that shifts the cash rate back to a neutral stance more quickly than we

had previously expected and leaves the RBA with a more appropriate policy stance.

Our call for a 50bp easing in May reflects the fact that with the real cash rate of 1.3% and policy currently restrictive, the RBA needs to play catch up. With longer periods between RBA Board meetings now a feature of the RBA calendar, some flexibility on the policy front has been lost, especially when developments are moving fast.

Once the cash rate reaches a level more consistent with a neutral policy setting, we then expect the RBA to pause for a few months before taking the cash rate into modestly accommodative territory. We expect a further 25bp easing at each of the November and February meetings, taking the cash rate to a new cyclical low of 2.6% (Chart 2).

RBA Cash Rate Target (%)



Source: National Australia Bank, Reserve Bank of Australia, Account in-house, Macrobond

Prior to the developments over the past week, we did not view inflation as a barrier to gradually easing policy towards our long-held view of neutral (at a little above 3%), in order to sustain healthy outcomes in the labour market. While we assess that the labour market is not currently a source of inflationary pressure, the RBA has been cautious in their assessment of spare capacity in the labour market and has noted that it would require further evidence to be comfortable the outlook is consistent with sustaining inflation at target.

A weaker global backdrop and the impacts of weaker consumer and business confidence have now shifted the distribution of risks away from a tighter labour market and towards the risk of a rise in the unemployment rate.

On inflation, we have been more optimistic than the RBA's Feb SMP forecasts with respect to ongoing progress through early/mid 2025. The meaningful disinflation in the largely weighted housing components and further progress over early 2025 on market services inflation has delivered a more benign inflation outlook. The depreciation in the AUD places some near-term upward pressure on imported goods inflation which has been benign over the past year.

However, we see the net impact of weaker global growth and the implications of tariffs on our trading partners in Asia as ultimately disinflationary for Australia. Unlike many other central banks, we do not expect the RBA will be constrained by inflation and thus will move proactively to support growth and the labour market.

We have tweaked our forecasts for GDP growth and the unemployment rate. We now see GDP growth of 2.0% over 2025 (was ~2¼%) and see the unemployment rate peaking slightly higher at around 4.4% before edging back down to around 4¼% at end 2026. That is, we see the support from

meaningfully lower interest rates as mitigating a larger impact on both growth and inflation.

Though we expect the direct impact of tariffs on Australia to be small (with the US a relatively small goods trading partner), we are not immune from the indirect impacts. For Australia we see the key impact on activity being driven by three channels: first, consumer and business confidence; second, potential national income and wealth impacts from weaker commodity prices; and third, volatility in financial markets. Managing the risks associated with each of these channels argues for a shift to a more pre-emptive policy response by the RBA.

We would also note that the situation remains quite fluid at present; hence there are large bands of uncertainty to our modal forecasts. Should the likely tariff regime in the US settle at a less severe outcome, then the RBA may have scope to consider a more gradual policy adjustment. But for now, we think the distribution of risks to both growth and inflation in Australia have shifted such that the central bank is required to act with some sense of urgency.

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