MARKET UPDATES

RBA Update July 2025

The Reserve Bank of Australia (RBA) Monetary Policy Board kept interest rates unchanged at the July meeting, with the cash rate target remaining at 3.85% and the interest rate on Exchange Settlement balances staying at 3.75%.

The decision was a large surprise to market participants and most economists, who expected a 25bps cut in interest rates.

The decision to leave the rates on hold was not unanimous, with Monetary Policy Board members being in favour of keeping rates on hold and three members being against it.

Post-meeting Statement

The post-meeting statement may have sounded slightly hawkish to those market participants who were focused on headline figures over the past month.

Regarding inflation, the RBA Monetary Policy Board highlighted its focus on the quarterly figures, which showed that trimmed mean inflation was at 2.9%. They assessed that the monthly CPI indicator suggests that underlying inflation in Q2 was in line with forecasts, or even 'slightly stronger than expected'. This was despite annual trimmed mean inflation declining to 2.4% in May, which would be somewhat below the most recent RBA projection.

On economic growth, the statement assessed that the national accounts figures confirmed that domestic demand had picked up over the past six months. The Monetary Policy Board acknowledged that there is a risk that the pace of recovery in household consumption could disappoint, but did not mention a downside surprise to GDP growth in Q1 or the renewed decline in GDP per capita in that quarter.

Regarding the labour market, the RBA stressed that labour market conditions remain tight, focusing on low underutilisation rates, as well as the results of business surveys and liaison.

The post-meeting statement again brought attention to the ongoing weakness in productivity, which is putting upward pressure on growth in unit labour costs despite wages growth being off its peak.

The statement also highlighted ongoing uncertainty, both domestic and external, but considers some of the extreme risks around US trade policy to have subsided.

In terms of forward guidance, the Monetary Policy Board stressed twice that it needs more information to confirm if inflation is on track to sustainably reach the mid-point of the target range (2.5%).

The RBA Monetary Policy kept both parts of its mandate in focus in the statement, stressing the importance of maintaining price stability and full employment. The RBA will remain attentive to incoming data and evolving risks.

Press Conference

When explaining the decision, RBA Governor Michele Bullock focused on the following three points.

First, the difference between the Monetary Policy Board Members being in favour of the decision and those against it is about the timing, not 'so much' direction.

Second, the more comprehensive quarterly CPI figures suggest that the underlying inflation has been within the 2-3% target range for only one quarter.

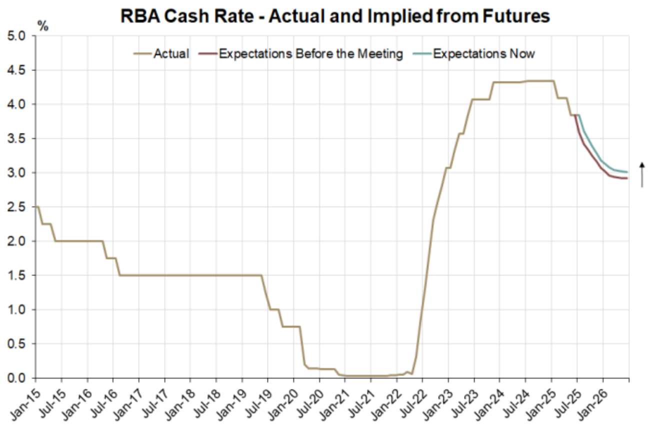
Third, while the monthly figures suggested a further decline in the annual trimmed mean inflation in Q2, there were 'some components' of the report, such as dwelling costs or durables prices, that displayed somewhat stronger growth than the RBA expected.

Market Impact

As the decision to keep the rates on hold was a surprise to market participants, it has triggered:

- a rise in 3-year Commonwealth bond yields from 3.36% to 3.43% at the time of writing,
- a pick-up in 10-year Commonwealth bond yields from 4.23% to 4.27%, and
- a slight appreciation of the Australian dollar, from US$0.6512 to US$0.6535.

The markets continue to almost entirely price in a 25bps rate cut in August, but now expect 64bps of total cuts in the second half of 2025, rather than the 77bps prior to the announcement.



Comment

In our Daily Report this morning, we highlighted that the July monetary policy decision was a closer call than market pricing implied. The RBA appears to be consistent in its focus on the quarterly inflation figures, given the incomplete nature of the monthly CPI indicator. Given this, the Q2 CPI publication on 30 July will be crucial for the interest rate decision in August. With the increasing focus on the mid-point of the target range, a further decline in trimmed mean inflation will most likely be required for a rate cut in August.

08 July 2025