RBA Update February 2025

The Reserve Bank of Australia (RBA) Board decided to cut its policy interest rates by 25bps at its February meeting, taking the cash rate target down to 4.10% and the interest rate on Exchange Settlement balances to 4.00%. The decision was in line with market expectations.

However, the decision was a 'hawkish' cut, with the RBA Board saying explicitly that they will remain cautious about further monetary policy easing.

Post-meeting Statement

The revised post-meeting statement by the RBA Board contained both new hawkish and dovish elements.

The RBA acknowledged that underlying inflation is moderating faster than expected, while private demand remains subdued, and wage pressure has eased.

However, the RBA stressed that upside risks to inflation remain, even if they have eased, and come particularly from the surprisingly strong labour market. The statement continued to underscore that sustainably returning inflation to target remains the RBA's priority.

The RBA again stressed that the inflation outlook remains clouded, citing both domestic and global risks. The major external risks obviously stem from elevated geopolitical and policy uncertainties. Domestically, the RBA highlighted the uncertainty about the persistence of the recent revival in consumer spending, while some labour market indicators have tightened.

The final paragraph containing forward guidance was left unchanged, with further decisions remaining data-dependent.

Statement on Monetary Policy

The RBA has also released its quarterly Statement on Monetary Policy containing updated central projection paths, which since May 2024 have been prepared based on market cash rate forecasts.

While the near-term inflation forecasts were revised down due to a lower starting point, there were upward revisions for 2026. Base effects still mean that headline inflation will be temporarily rise above 3.5% towards the end of 2025. However, trimmed mean inflation is forecast to remain within the target band. Both inflation rates are forecast to be slightly above the mid-point of the target at 2.7% at the end of the forecast horizon in June 2027.

The unemployment rate path has been revised downwards, with the peak now at 4.2% rather than 4.5%.

The GDP growth forecasts were downgraded for the near-term, due to weaker household consumption and business investment outlook, and kept broadly unchanged towards the end of projection horizon.

The Statement included insights from the RBA business liaison, which suggested a rise in hiring and hiring intentions, and that selling price inflation is not expected to ease much further in the coming year.

Press Conference

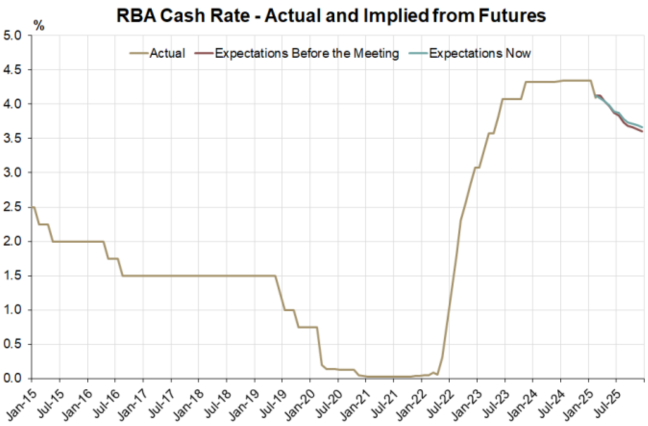
In the press conference, RBA Governor Michele Bullock stressed that the February rate cut was just a removal of the emergency November 2023 hike, with monetary policy intended to remain restrictive.

She added that the decision was a much closer call than implied by market expectations, with arguments both for and against a cut.

Governor Bullock underscored that it will depend on the data if the three cuts for 2025 priced in by the market before the meeting will eventuate. She declined to comment on whether the February cut would be the only one in the cycle.

Market Impact

Governor Bullock's scepticism about market pricing for cash rate cuts did little to alter the market's view. Two more cuts are still largely priced in for the remainder of 2025. However, 3-year Commonwealth bond yields increased to 3.93% from 3.87% just before the decision announcement, while 10-year yield rose to 4.50% from 4.45%. Despite some volatility, the AUD/USD is trading only a little higher at US$0.6352, compared to US$0.6343 before the announcement.



Comment

As emphasised by the RBA Governor today, the February cut decision was not an easy one. While the Q4 inflation reading undershot the November projection, the outlook remains uncertain, and there are still upside risks to inflation, particularly from the still-tight labour market.

The RBA stressed several times today that market expectations regarding future rate cuts were too optimistic. When fed into the RBA model, they implied that inflation would remain above the mid-point of the target range over the medium term. The outlook for RBA policy remains well and truly data dependent.

For the time being, all 'Big Four' banks have announced they will fully pass on the cash rate cut into mortgage costs, effective at the turn of February and March.

18 February 2025