NAB MONETARY POLICY UPDATE 16 SEPTEMBER 2022
50BP RATE RISE NOW LIKELY IN OCT; 3.10% CASH RATE BY END-22
NAB Economics

Key points

- In light of recent data and the RBA Governor's statement this morning, we now see a fifth consecutive 50bp rate increase in October (previously 25bps). We continue to expect a 25bp rise in November taking the cash rate to 3.10%, which we see as a mildly contractionary policy setting.
- We still expect the RBA to pause the hiking cycle after November to assess the impact of rate hikes taken across 2022 and the evolution of inflation, the labour market, and the economy. We continue to expect GDP growth to slow in 2023 as higher rates weigh on consumers.

Strong data and concern about inflation expectations

Recent data has continued to show elevated price pressures and resilient consumption. The NAB Business Survey suggests business conditions remained elevated through August and price measures in the survey point to another very strong inflation print in Q3.

The labour market also remains very tight with unemployment around 3.5% in recent months. As noted in this week's *Forward View*, we expect wage growth to pick up to 3.2% by the end of 2022 and 3.4% in 2023, putting some upward pressure on core prices even as global shocks to goods and oil prices show signs of easing.

Further, in today's statement to the Parliament's Standing Committee on Economics Governor Lowe explicitly noted that "the general inflation psychology appears to be shifting; it is easier for firms to put their prices up and the public is more accepting of this". To us this is a significant shift and suggests an increased concern that more needs to be done to keep inflation expectations anchored.

RBA not yet ready to step down the pace of rate rises

Since July, our view has been that the RBA would slow the pace of rate rises in October to 25bp, before pausing after the November meeting. However, in light of recent data and the Governor's statement, we are now of the view that when the Board debates the decision in November, it will conclude that the balance of inflation risks argues against a step down in the pace of rate rises.

We therefore expect a fifth consecutive 50bp rate increase in October, taking the cash rate to 2.85%. We then expect a step down to occur with a 25bp rise in November taking the cash rate to 3.10% by year-end. We still expect the RBA to pause the hiking cycle after November to assess the impact of rate hikes taken across 2022 and the evolution of inflation, the labour market, and the economy.

Outlook remains uncertain

A 25bp increase remains a live possibility for the October meeting with the Governor signalling the Board would debate a 25bp or 50bp rise and indicating that the higher rates rise, the stronger the case for a step down. Regardless, we see a 3.10% rate at year-end as likely with the potential for a rise in December.

Our updated profile will see the RBA having raised rates some 300bps over 7-8 months. Still, there remain some upside risks to this profile. We expect a very strong Q3 core CPI print and expect headline inflation to only peak in Q4, which will continue to put pressure on the RBA.

That said, we continue to expect GDP growth to slow in 2023 as higher interest rates weigh on consumers, though these effects are lagged and the strength of the labour market and savings buffers will continue to provide some additional support to households. How consumption holds up as the recent interest rate rises begin to flow through to mortgage payments remains a key source of uncertainty with risks in either direction for growth and for interest rates.

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