The Forward View Australia: July 2025

Coming in for landing in a heavy cross wind

NAB Economics

Overview

- Our activity, labour market and inflation forecasts are unchanged this month.
- Growth is expected to return to trend over the next 18 months, with unemployment remaining low and inflation settling at 2.5%.
- A more cautious RBA means we now see cuts in August, November and February, for a terminal rate of 3.1%.
- Global factors remain a risk to the activity and labour market outlook, though there is little evidence of an impact so far in domestic data.

Domestic data flow over the past month has continued recent themes. The April and May Monthly CPI Indicator suggests little incremental progress on disinflation this quarter, pointing to a quarterly outcome slightly stronger than we (and the RBA) had expected. That said, inflation will continue to moderate in annual terms. Labour market data suggest that labour demand remains resilient, and the unemployment rate remains low. The labour market data had been challenging our forecasts that the unemployment rate would gradually increase, but the increase in June supports our view that the labour market has cooled over the past 12 months.

Activity data has been mixed. Measures of household spending point to another weak quarter of household consumption growth but have shown an improving trend through the quarter. NAB Business survey data showed a spike in conditions, confidence and capacity utilisation in June, and the quarterly survey showed an uptick in investment intentions, while also pointing to ongoing resilience in labour demand.

Our outlook for the economy is unchanged. We expect another year of below trend growth, but for GDP growth to accelerate to around trend over 2026. We expect the unemployment rate to drift up modestly, peaking at 4.4% in late 2025. Despite the small upside surprise to inflation in the quarter, we still expect inflation to settle around 2.5% in H2 2025.

However, despite the elevated global risks to activity (and the likelihood that additional US tariffs would be disinflationary for Australia) the RBA continues to focus on the domestic data flow. We see the RBA remaining cautious, cutting with a quarterly cadence, taking the cash rate to 3.1% by early 2026.

We see the risks around our rate track as broadly balanced. That said, the uncertain global backdrop sees a risk of faster and deeper cuts, although the domestic data suggests that the economy has remained resilient to date

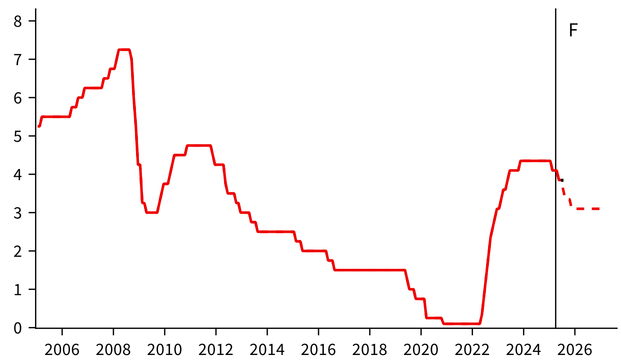
Contents

Key Economic Forecasts

	2023	2024	2025(f)	2026(f)
Domestic Demand (a)	2.9	1.9	1.8	2.2
Real GDP (annual ave)	**2.1**	**1.0**	**1.5**	**2.2**
Real GDP (year-ended)	**1.5**	**1.3**	**1.7**	**2.2**
Employment (a)	3.4	2.4	2.2	1.7
Unemployment Rate (b)	3.9	4.0	4.4	4.2
Headline CPI (b)	4.1	2.4	2.9	2.8
Trimmed-mean CPI (b)	4.2	3.3	2.6	2.5
RBA Cash Rate (b)	4.35	4.35	3.10	3.10
$A/US cents (b)	0.68	0.62	0.70	0.73

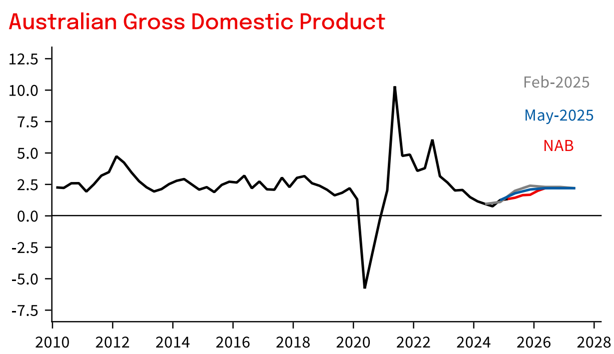
(a) annual average growth, (b) end-period

Chart 1: RBA Cash rate forecast



Source: National Australia Bank, RBA, Macrobond

Chart 2: GDP forecasts



Source: National Australia Bank, ABS, RBA

18 July 2025 | Authors: Taylor Nugent, Gareth Spence, Gerard Burg

Consumption

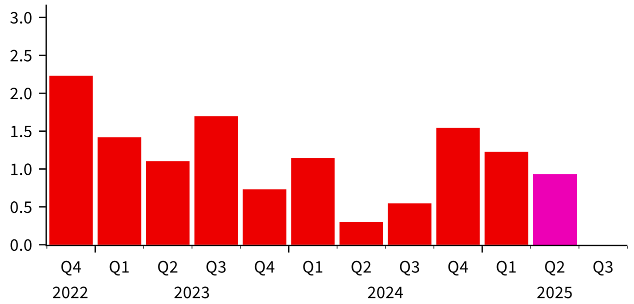
An ongoing recovery in household consumption growth remains key to the outlook for overall GDP growth, though it appears household spending growth has recovered more slowly than expected in early 2025.

Partial data for household spending in Q2 have been mixed. The ABS's monthly household spending indicator (MHSI) saw a solid 0.9% mom rise in May, following a flat outcome in April. The soon-to-be-defunct ABS retail sales release (which covers a much smaller proportion of household spending) saw a weaker 0.2% rise mom.

Updates on both measures for the month of June, including price adjusted volumes, will be released in early August. While these are only partial indicators of household consumption (as measured in the national accounts), they will give further insights into the underlying pace of growth in Q2, following a weaker than expected outcome in Q1.

The NAB Data Insights measure of household spending points to a solid 0.9% mom rise in June. This, in combination with MHSI data for the first two months of the quarter, points to a 0.9% quarter average increase in household spending in nominal terms.

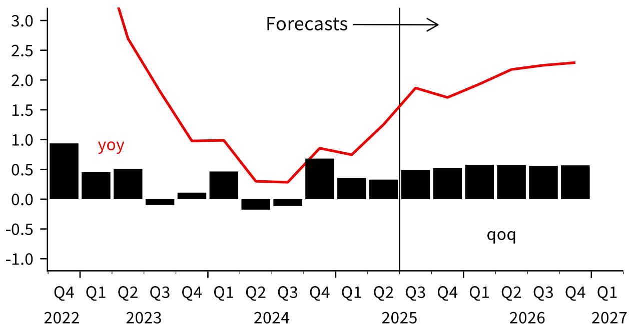
Monthly Household Spending Indicator (Quarter average, %)



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond

In real terms, this implies a rise of around 0.2-0.3% qoq for household consumption in Q2. We continue to see consumption growth recovering further in H2 2025, with the quarterly pace picking up to 0.5-0.6% qoq for an increase of 1.7% yoy over 2025. This would be slightly softer than the RBA's current May SoMP forecast of 1.9% yoy, but notably below the February staff forecasts of 2.1% yoy.

NAB Consumption Growth Forecasts (%)



Source: National Australia Bank, Account in-house

The key dynamics at play will continue to be households' decisions to spend or save against a backdrop of recovering real income growth. While disposable income growth has improved over the past three quarters, households have continued to also restore savings rates. In other words, households appear to have rundown savings rates over recent years in the face of pressures on purchasing power and this is now being reversed.

Slowing population growth will also continue to be a drag on spending growth, with the balance between the recovery at the individual household level easing population growth likely to see some bumpiness in overall activity.

Labour market

The labour market remains close to balance.

The unemployment rate rose to 4.3% in June after a period of stability at just over 4%. Employment rose 2k in the month following a fall of a similar magnitude last month, with trend employment growth now closer to 20k per month than the 30k per month through early 2025.

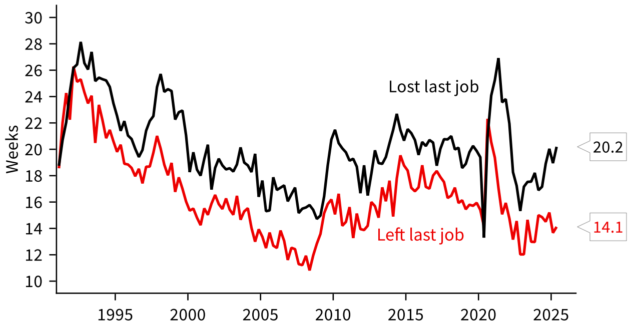
We wouldn't overinterpret this result as a rapid cooling in the labour market, though this month's result supports the assessment, based on a range of indicators, that the labour market had shown some gradual cooling which was not reflected in the stable unemployment rate.

In trend terms, the unemployment rate has remained low and the underemployment rate, has fallen back from its levels a year ago, our assessment remains that the labour market is near balance. Similar to recent dynamics in the US, the current labour market is characterised by lower numbers of quits and hires than would be expected based on headline indicators like the unemployment rate alone.

For those people who are unemployed, rates of finding a job remain only a little higher than they were in the soft pre-pandemic labour market. Unemployed people who lost their last job have been unemployed for an average of 20 weeks, around levels seen in 2019.

The current labour market is not proving particularly wage-inflationary, and wages growth in those parts of the labour force that tend to be most exposed to cyclical conditions has been gradually cooling, even as broader wages growth has been supported by slower moving collective agreements and by administered pay increases delivered by the Fair Work Commission. We expect wages growth measured by the WPI to slow toward 3% over the next 12 months.

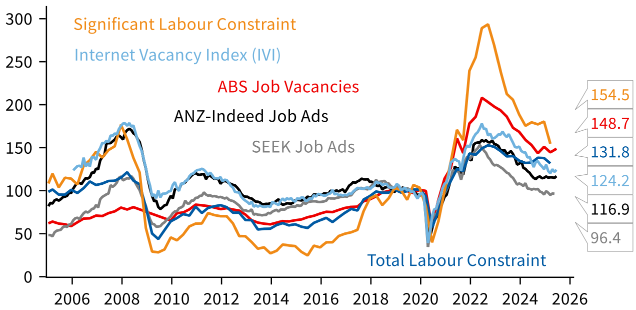
Average duration of unemployment



Source: National Australia Bank, ABS

Earlier cooling in forward indicators of labour demand has steadied over the past 12 months, but there is little to suggest re-tightening. Job ads on a range of measures have been flat to modestly lower in 2025 so far, and some measures of recruitment difficulty have eased. The share of businesses reporting availability of suitable labour as a significant constraint on output has fallen further over the past 2 quarters.

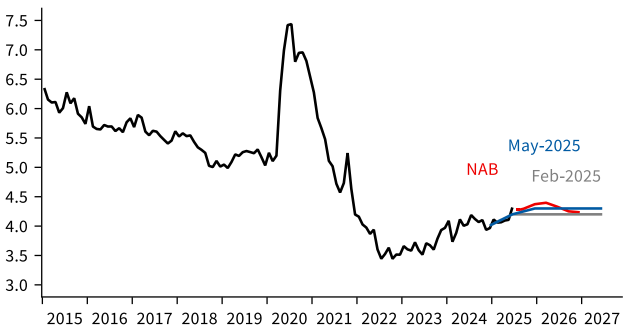
Measures of labour demand



Source: National Australia Bank, Australian Bureau of Statistics, ANZ-Indeed, SEEK Australia, National Australia Bank, Jobs & Skills Australia, Macrobond

We continue to assess that the risks to the labour market are skewed to the downside given continued profitability pressures faced by businesses and a weaker demand backdrop. We forecast the unemployment rate will rise to 4.4% by the end of 2025 and settle around 4¼% longer term.

RBA Unemployment Rate Forecasts



Source: National Australia Bank, RBA

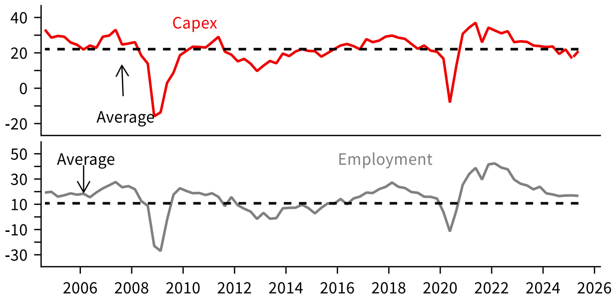
Businesses

Business confidence and conditions spiked in June, an encouraging sign that the trend lower in profitability and trading conditions in early 2025 may be reversing.

Conditions in wholesale, retail and manufacturing remain weakest in trend terms, while the services sector is strongest. Of note, is the trend improvement in construction over the past year or so. The improvement in conditions and rise in capacity utilisation, if sustained, will be key to firms maintaining labour demand and investment intentions going forward.

Interestingly, despite the persistence of weak confidence and conditions through early 2025, the NAB Quarterly Survey showed an uptick in 12-month investment intentions which are now back around average. 12-month employment intentions were broadly steady at an above average level. This suggests that fears over global trade and growth amid elevated uncertainty have not been amplified domestically yet.

NAB Survey 12m capex and employment intentions (Net Bal.)



Source: National Australia Bank, Macrobond

Respondents report that the most significant drivers of confidence are wage costs, margins and federal government politics (amid the proximity to the election). Pressures from a tight labour market continue to fade but remain the 4th largest factor impacting confidence.

Input cost pressures continue to track at a higher rate than pre pandemic. Though both labour and purchase costs have eased from their peaks, there has been little further easing through H1 2025. Output price growth on the other hand appears to have normalised, pressuring margins and profitability. Indeed, the margins question in the quarterly survey weakened further in Q2.

Foreign exchange

Our Australian dollar forecasts are unchanged, and we expect the AUD/USD to end the year around US70c before drifting higher over 2026.

The Australian dollar has edged up by just under 1% over the last month and has traded around US65.5c in recent days. On a trade weighted basis, the Australian dollar has risen by a similar amount over the month. Since January, it is up 1.5% below the 5.5% in increase in the AUD/USD.

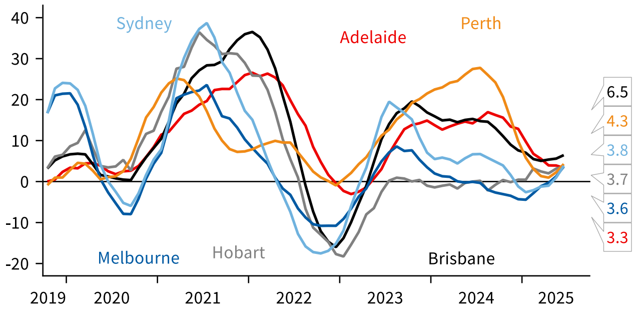
Housing

House price growth is stabilising, as Sydney and Melbourne return to the pack.

According to Cotality (formerly CoreLogic) data, the 8-Capital City dwelling price index rose by 0.6% mom in June, continuing the relatively robust monthly growth trends evident since February (excluding softness in April). The index rose by 2.7% yoy, showing signs of stabilising following the steep slowdown in growth across the second half of 2024 and into 2025.

Month-on-month growth trends for mainland capital cities have converged since the start of the year – as price growth in Sydney and Melbourne has recovered from comparatively weak rates.

CoreLogic Hedonic Dwelling Price Growth by Capital City (6-month-ended Annualised,%)

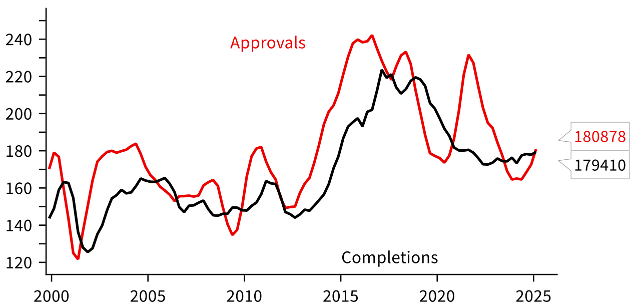


Source: National Australia Bank, CoreLogic Australia, Macrobond, Account in-house

In rental markets, vacancy rates remain low by historical standards – just above 1.5% nationally (compared with around 2% at the end of 2024) – with local markets particularly tight in Adelaide and Perth. Despite this tightness, growth in hedonic rents has slowed in recent months – down to 0.3% mom in June – albeit rents climbed rapidly between late 2020 and mid-2024.

Despite the strength of both dwelling prices and rents post-pandemic, housing completions remain well below pre-pandemic levels. Completions fell 4% in the quarter and are up a more modest 4% yoy. In rolling annual terms, completions continue to hover around 180k per year. There are currently 220k dwellings under construction.

Dwelling Approvals and Completions (Rolling annual, 000s)



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond

Building activity has remained constrained by a range of factors, including supply of labour and costs of building materials. That said, the ABS reports that the cost of inputs into the housing construction industry fell by 0.1% qoq in Q1 2025 – the first decline since Q1 2012. Overall, the index remains 35% above the level in March 2020.

That said, commencements rose 12% in Q1 and are up 17% over the year, at a rate of 50k per quarter. Commencements are now 25% off their low in late 2023 and a little above their 2019 levels, but remain relatively low.

Following two months of steep month-on-month declines, dwelling approvals rose relatively strongly in May (up by 3.2%). On a trend basis, dwelling approvals moved higher across 2024 before stabilising well below the peaks of early 2021.

Inflation

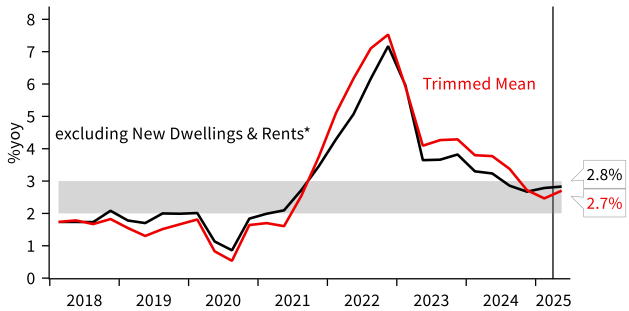
Inflation cooled sharply in Australia from mid 2024 and is now within the RBA's 2-3% band on most measures, but the extent of recent disinflation in Australia is less pronounced than at face value. The RBA noted in May that recent monthly outcomes have come in "at the margin, slightly stronger than expected." That caution is not unfounded.

Electricity subsidies in the second half of 2024 subtracted more than 0.5ppt from CPI. The underlying trimmed mean measure does a reasonable job of abstracting from that, but most of the cooling in that measure reflected shelter categories.

On a six-month annualised basis, trimmed mean inflation fell 0.9ppt to 2.5% between Q3 2024 and Q1 2025. When New Dwellings and Rents are excluded, this measure fell just 0.1ppt to 2.8% over the same period.

We do not look for much further disinflation from shelter categories, and indeed a surprise pickup in New Dwelling purchase costs in April leaves the risk to the high side of the RBA's May 0.6% qoq forecast for Q2 trimmed mean. (See CPI Preview – underlying inflation near target).

Trimmed Mean Inflation and Shelter (6m annualised)



*Calculated by NAB using EC level data and a reweighted basket that excludes New Dwellings & Rents
Source: National Australia Bank, ABS

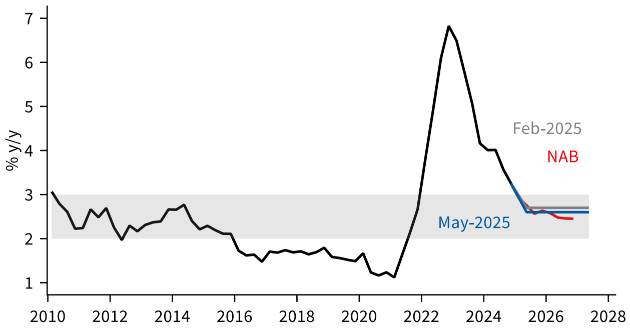
Even so, the economic backdrop is consistent with inflation sustaining around the midpoint of the RBA's target looking forward.

Encouragingly, components of inflation including many services prices that the RBA tends to look at as an indicator of domestic inflationary pressures have been benign and are expected to remain so.

A recent uptick in food and grocery prices is not expected to be sustained, with global food commodity prices stabilising recently and some increased discounting among major supermarkets is evident. Elsewhere, durable goods prices are set to support Q2 inflation, reflecting the earlier depreciation of the Australian dollar feeding through into strengthening input prices. Those earlier pressures will fade, and we continue to think that on balance the disruptions from higher US tariffs will have a net disinflation impact for Australia, especially for finished consumer goods.

Beyond the component level drivers, our broader macro assessment is that the economy is near balance, and a modest pick up in growth towards trend means it will stay there, consistent with inflation sustaining near target. To the downside, a more material headwind from global growth could see spare capacity open up and inflation move below the midpoint of the RBA's target. Conversely, a risk is that weak productivity growth and supply constraints across housing mean that even modest growth drives inflation pressures that keep the RBA cautious.

Trimmed Mean Inflation Forecasts



Source: National Australia Bank, ABS, RBA

Monetary Policy

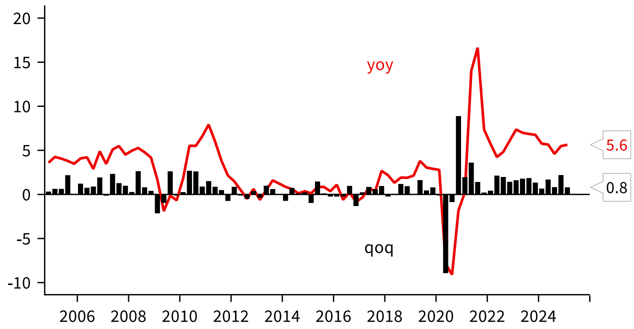
We now see the RBA lowering rates further in August, November and February, taking the cash rate to 3.1% by early 2026.

The RBA surprised markets and most economists by holding the cash rate unchanged in July. The RBA's assessment of the recent data flow since the May SoMP was in line with our own at the time. The CPI for Q2 is likely to surprise slightly to the upside, unemployment was tracking (Before June data) slightly below their forecast and, at the margin household spending data point to a slightly softer outcome than forecast in the May SoMP.

However, the RBA looks to be moving more cautiously than we had expected because of the uncertainty around not just the demand side of the economy but also the supply side. The unemployment rate had remained low, and the post meeting statement highlighted ongoing concerns about weak productivity growth and the sustainability of high unit labour costs growth.

That said, the RBA clearly expects to ease further, moving away from restrictive settings to support an ongoing recovery in growth (particularly in the private sector) and to maintain a healthy labour market. Indeed, in the post meeting press conference, Governor Bullock framed the decision to hold as "*looking for further evidence that the Bank's forecasts are on track*" and that the discussion between board members was about 't*iming not direction of rates*'.

Non-farm Nominal Unit Labour Costs Growth (%)



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond

The Governor highlighted the key pieces of information ahead of the 11-12th August board meeting included the jobs data for June (released yesterday) and the full quarterly CPI for Q2. While one month's move in the labour force survey should not be overinterpreted, the June data saw a rise in the unemployment rate, broke the stability in the unemployment rate over earlier months, and indicated that trend employment growth may be slowing. On inflation, our forecast for the Q2 CPI is slightly stronger than the RBA had expected in May, but still broadly in line with their expectation and will see the annual rate in the trimmed mean ease further towards target at 2.7% yoy.

Beyond that, our assessment remains that the RBA will need to continue to normalise interest rates in order to support a pickup in growth towards trend. We don't see the labour market as a source of inflation pressure at present. We see inflation settling around 2.5% in H2 2025, meaning inflation is not expected to constrain the RBA from becoming more forward looking and focusing on sustaining low unemployment.

A further downward shock to global growth remains the largest source of downside risk, in our view, that could see a faster and deeper cutting cycle, taking the cash rate meaningfully into accommodative territory. Slower global growth, amplified by a weakening in consumer and business confidence as well as weaker commodity prices, could weigh on both domestic growth and labour demand. However, the RBA remains well placed to respond to a shock of this nature given we do not expect such a shock to be inflationary – unlike the US where higher tariffs will drive up the domestic price level.

The key upside risk to our expected rate track continues to be a cautious RBA combined with a tight starting point for the labour market, particularly as private sector growth is expected to pick up. Though we currently see the labour market as close to balance, a retightening in labour market conditions and reacceleration in wage growth (amid soft productivity growth) could see a shallower cutting cycle than we expect.

Key Forecasts Tables

Australia forecasts table

	% Growth q/q			% Growth y/y		
	Q4-24	**Q1-25 (f)**	**Q2-25 (f)**	**2024**	**2025 (f)**	**2026 (f)**
GDP and Components						
Private Consumption	0.7	0.4	0.3	0.9	1.7	2.3
Dwelling Investment	0.7	2.6	0.9	3.5	5.0	1.8
Underlying Business Investment	-1.6	-0.7	1.1	-3.8	1.7	2.9
Underlying Public Final Demand	0.6	-0.4	1.0	5.3	1.5	1.6
Domestic Demand	**0.7**	**0.2**	**0.4**	**2.2**	**1.7**	**2.3**
Stocks (Cont. to GDP)	0.3	0.2	-0.1	0.1	-0.1	0.1
Gross National Expenditure	**0.7**	**0.3**	**0.3**	**2.3**	**1.9**	**2.3**
Exports	0.1	-0.8	0.4	1.3	0.6	1.9
Imports	0.7	-0.4	0.3	6.4	1.0	2.0
Net Export (Cont. to GDP)	-0.1	-0.1	0.1	-1.1	-0.1	0.0
Real GDP	**0.6**	**0.2**	**0.3**	**1.3**	**1.7**	**2.2**
Nominal GDP	1.5	1.4	0.6	3.7	4.4	4.6
Labour Market						
Employment	0.6	0.4	0.7	2.4	1.7	1.9
Unemployment Rate (Q-Ave, End of Period)	4.0	4.1	4.2	4.0	4.4	4.2
Wage Price Index (WPI)	0.7	0.9	0.9	3.2	3.5	3.2
Inflation and Rates						
Headline CPI	0.2	0.9	0.7	2.4	2.9	2.8
Trimmed-mean CPI	0.5	0.7	0.7	3.3	2.6	2.5
RBA Cash Rate (End of Period)	4.35	4.10	3.85	4.35	3.10	3.10
10 Year Govt. Bonds (End of Period)	4.48	4.38	4.35	4.48	4.25	4.05
$A/US cents (End of Period)	0.62	0.63	0.66	0.62	0.70	0.73

Data are percentage growth rates over the quarter or year as noted, except where specified otherwise.

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