International Commentary — August 14, 2025

Reserve Bank of Australia Cuts Rates, Signals a Steady Easing Bias

Summary

- The Reserve Bank of Australia (RBA) delivered a widely expected 25 bps rate cut at this week's monetary policy meeting, lowering the Cash Rate to 3.60%, marking its third rate cut this year. The decision was unanimous and the accompanying statement struck a neutral tone, though perhaps leaning slightly dovish on the margin. The central bank remains on a steady easing path, without signaling any particular urgency regarding adjustments to its policy stance.
- The RBA downgraded its GDP growth outlook due to persistently weak productivity, while inflation and unemployment forecasts were left broadly unchanged. Governor Michelle Bullock reiterated that Australia's shallower hiking cycle means it may not need to cut rates as deeply as other advanced economies.
- Recent labor market and wage data, in our view, support the RBA's cautious stance. July's jobs report showed a strong rise in full-time employment and a drop in underemployment, while Q2 wage growth unexpectedly held steady at 3.4% year-over-year.
- Uncertainties surrounding weak productivity and the dynamics of elevated labor costs remain an important area of focus for the RBA. Against this backdrop, we think that the central bank is likely to wait for confirming evidence of improving productivity and moderating wages before contemplating a faster pace of monetary easing. With those improving productivity and costs likely to reveal themselves only gradually over time, we view a continued quarterly cadence of rate cuts as more probable. As a result, **our base case remains for further 25 bps cuts in November and February, bringing the Cash Rate to 3.10% by early 2026,** with risks tilted slightly toward an even slower pace of easing.

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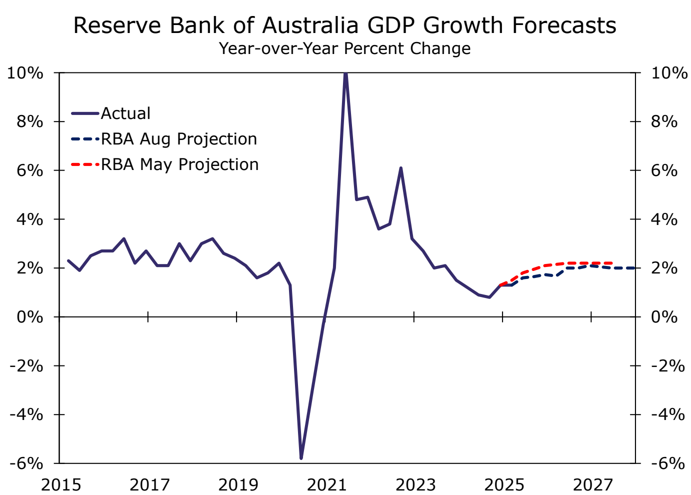
Reserve Bank of Australia Cuts Rates, Signals a Steady Easing Bias

In a widely anticipated move, the Reserve Bank of Australia (RBA) delivered a 25 bps rate cut at this week's monetary policy meeting, lowering the Cash Rate to 3.60%. This marks the third rate cut of this year. Unlike the July meeting, which saw a split decision to hold rates steady—a surprise to many market participants—this week's outcome was unanimous. Meanwhile, the accompanying statement struck a neutral overall tone though, if pressed to characterize it, we would say it leaned slightly dovish on the margin.

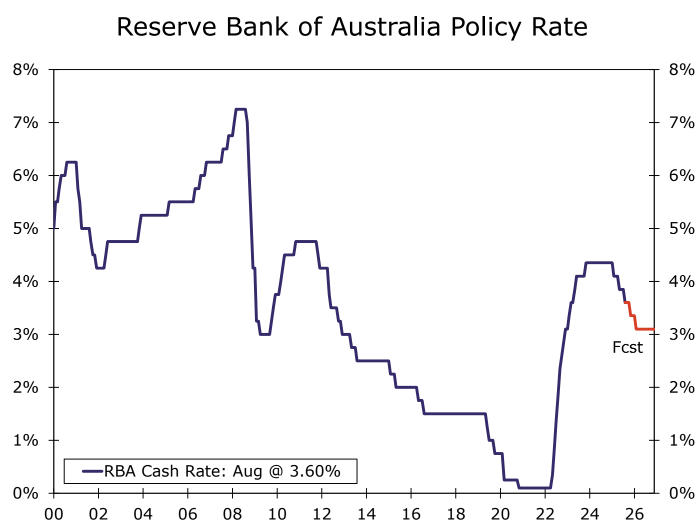
Given the widely expected nature of the rate cut, market attention quickly shifted to the RBA's updated economic projections within the release of its Statement on Monetary Policy (SoMP). The SoMP provided deeper insights into the RBA's thinking and revealed several notable developments:

- The most significant revision came in the form of downgraded GDP growth projections. The RBA attributed this to a weaker outlook for productivity growth, stating that "consistently weaker-than-expected productivity growth has led us to revise down our productivity assumption." This adjustment affects the entire forecast horizon and reflects a more cautious stance on Australia's medium-term growth prospects.
- On inflation, the RBA noted that underlying inflation continues to ease toward the midpoint of its 2–3% target range and is expected to remain sustainably around that level. This was reflected in the unchanged inflation forecasts, with the newly added projection for Q4 2027 placing trimmed mean inflation at 2.5%.
- On employment, they acknowledged that labor market conditions have softened slightly in recent months, though they maintained that conditions remain "a little tight". While subtle, this is a shift from the previous characterization of conditions as remaining "tight." Importantly, unemployment forecasts were left unchanged, implying no expected rise in the jobless rate.
- On the external front, the RBA acknowledged that global growth may come in below previous projections. However, it also noted that there is now greater clarity around the scope and scale of U.S. tariffs and the policy responses from other countries which reduces the likelihood of more extreme outcomes.

Importantly, the RBA indicated that the reduced growth projection largely reflected the weaker outlook for productivity and thus potential GDP growth, which it now views as close to 2%, but that it did not substantially alter its assessment of the economy's demand-supply balance. As a result the RBA's outlook for inflation and the unemployment rate were essentially unchanged, and the more subdued growth forecast has in our view few implications for the immediate path of monetary policy ahead.



Source: Reserve Bank of Australia, Bloomberg Finance L.P. and Wells Fargo Economics



Source: Bloomberg Finance L.P. and Wells Fargo Economics

The RBA also highlighted risks to the outlook that were both dovish and hawkish in nature. On the dovish side, they noted that due to weak demand, “some businesses continue to report difficulty passing on cost increases.” Additionally, they added that the “slower-than-expected consumption growth could weigh on aggregate demand and lead to a more pronounced easing in the labor market.” The central bank also suggested global trade concerns were likely to weigh on Australian inflation. On the hawkish side, the RBA flagged that “there may be more excess demand in the economy than judged.” If labor market conditions are indeed tighter than originally forecast, it could lead to stronger wage growth. In turn, “rising real incomes and household wealth could prompt higher consumption and lower savings, adding upward pressure on inflation.” This would then see inflation settle above the midpoint of the target range.

During the post-meeting press conference, Governor Michelle Bullock noted that a couple more rate cuts would be necessary to achieve the RBA’s current forecasts and maintain inflation within the 2–3% target range. This broadly matches the revised economic projections, which are predicated on the Cash Rate declining further from its current level to a trough of 2.9% in Q4 2026, lower than the RBA’s previous 3.20% assumption.

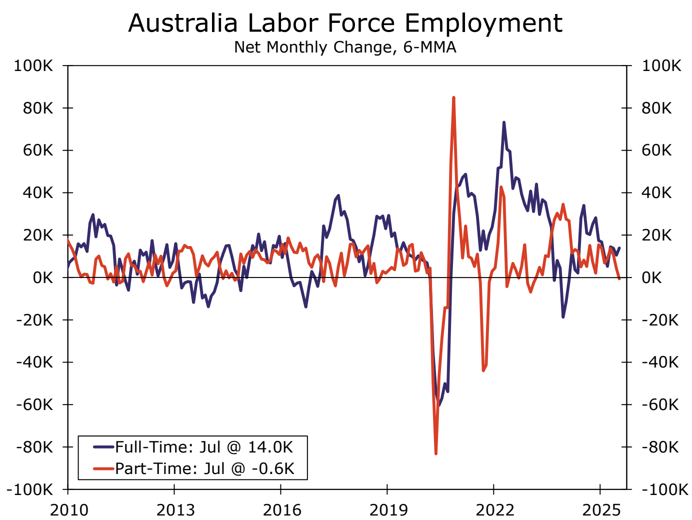
The Smaller They Rise, The Shallower They Fall

For us, the key takeaway from the RBA’s latest monetary policy announcement is that while the central bank remains on a steady easing path, it is not signaling any perceptible urgency regarding its monetary policy moves. We view the approach as continuing to be data-dependent, and expect rate cuts to continue to follow a cadence of 25 bps per quarter. In that sense, the focus remains on timing rather than direction of rate moves. Governor Bullock has repeatedly emphasized that Australia’s relatively shallower hiking cycle compared to other advanced economies means it may not need to cut rates as deeply. In her words, “because we didn’t take rates as high as some other countries, it may be that we don’t need to reduce rates as much either.” While the central bank's forecasts imply that the Cash Rate will need to fall modestly below current levels to support the convergence of inflation and employment to their respective targets on a sustained basis, the RBA remains cautious, letting incoming data guide its policy decisions.

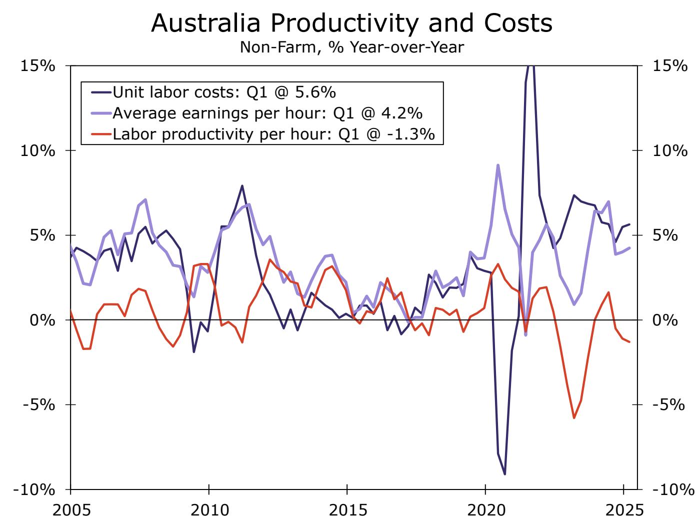
Moreover, we view the latest round of data releases as consistent with the RBA’s gradual approach to easing. The July jobs report reinforces the view that labor market conditions remain relatively tight, and are loosening at only a measured pace—supporting the central bank’s cautious stance. Employment rose by 24.5K, driven entirely by a surge in full-time jobs, which increased by 60.5K, while part-time positions declined by 35.9K. The unemployment rate fell to 4.2% in July, down from 4.3% in June, suggesting that last month’s uptick may have been more noise than a signal of genuine softening. The underemployment rate also edged lower to 5.9%, its lowest level in nearly two decades, perhaps indicating that labor market conditions remain reasonably tight as more workers secure the type of employment they prefer. In our view, the July figures do not present a compelling case for urgent action; instead, they reinforce the appropriateness of the RBA’s current quarterly cadence. If anything, the strength in full-time employment and the decline in underemployment will likely increase the RBA’s inclination to proceed cautiously and remain data-dependent, as it has throughout this cycle. When the RBA chose to hold rates steady in July—a decision that surprised both us and market participants—it did so before the release of the softer-than-expected June labor data, which led to some criticism and second-guessing. The July release, however, strengthens the rationale behind that decision and underscores the value of waiting for more complete data before adjusting policy.

We also viewed this week's wage data as consistent with a continued gradual pace of easing from the RBA. Growth in the Q2 Wage Price Index unexpectedly held steady at 3.4% year-over-year, in contrast to expectations for a slight deceleration to 3.3%. Within the details, private sector wage growth actually ticked higher to 3.4%, while growth in government sector wages remained elevated at 3.7%. Australia's wage and compensation trends are likely to be a particular focus for the central bank in the months and quarters ahead, especially in the context of productivity and cost issues that were highlighted by the RBA in its updated economic projections. The uncertainties surrounding the future path of productivity and cost dynamics offer another important reason, in our view, for the central bank to take a careful and calibrated approach as it considers future monetary easing. The latest available data, for Q1-2025, highlight a poor productivity performance over the past year, with labor productivity down 1.3% year-over-year. With average earnings per hour rising 4.2%, unit labor costs were up some 5.6% over the past year, representing an elevated pace of unit labor cost growth by historical standards. To be sure, the RBA anticipates a modest improvement in productivity in the years ahead (albeit less than previously), while also expecting wage growth to decelerate, bringing unit labor cost pressures more in line with its inflation target. That said, we suspect the RBA would prefer to see confirming evidence of improving productivity and decelerating wages before quickening the pace of monetary easing, making a more aggressive rate-cutting cycle unlikely for the time being.

Altogether, the RBA's "as expected" rate cut, the broadly neutral message from its accompanying guidance and economic projections and the incoming data flow, are strongly supportive of the central bank continuing with a measured pace of monetary easing. **Against this backdrop, our base case remains for further 25 bps policy rate cuts from the RBA at its November and February announcement, for the policy rate to reach a low of 3.10% by early next year.** We view the risks around the RBA's policy outlook as broadly balanced though, if anything, perhaps slightly tilted to an even slower pace of monetary easing. We also believe the RBA's gradual rate cut approach, when juxtaposed with our outlook for more regular Federal Reserve monetary easing and a slowing U.S. economy, could be supportive of further Australian dollar upside through the balance of 2025.



Source: Bloomberg Finance L.P. and Wells Fargo Economics



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