

Australia: High inflation calls for a re-think on the cash rate profile

We wrote some weeks ago that we were just one bad inflation report away from stripping out our remaining cash rate cut forecast for 2024, and two bad reports from considering a hike. The first of those conditions has now been achieved



3.6 Headline inflation YoY%

April monthly data

Higher than expected

Silver linings are elusive

This was not the inflation report the Reserve Bank of Australia (RBA) would have wanted to see. Was there an element of wishful thinking in the consensus forecast of inflation moderating to 3.4% YoY from 3.5% in March? If so, they will have been disappointed to see inflation not only **not** falling but **rising** to 3.6% YoY.

Last year's 0.67% MoM increase in the April price level should have been a relatively high bar to undershoot. We can't blame base effects for this inflation increase. On a month-on-month basis, the price level rose 0.73% in April 2024. The average monthly increase in the price level over the last three months has been more than 0.5%. Annualised, that puts inflation in the 6% YoY range, a long way from the top of the RBA's 2-3% target. Even on a 6-month-annualised basis, the increase in trend inflation is apparent.

3 and 6m annualised inflation (%)



This looks bad from most angles

This was not just "one of those statistical flukes"

The price level excluding volatile items also rose 0.7% MoM. This was not just "one of those statistical flukes" caused by a big surge in one or two components due to seasonal distortions or supply interruptions. Across the board, inflation components exceeded the 0.25% MoM increase that would be needed to bring inflation to target over the medium term. Only education, finance, communication and housing came in on track on that basis. Rents still grew at 0.5% MoM, though at least they appear to be slowing.

Most other components of the CPI basket experienced price increases well in excess of what is needed to meet the RBA's inflation target.

Rate cuts this year look unlikely

Having said that a bad inflation result would cause us to chop out the remaining rate cut we had pencilled into our forecast for 2024, we will keep to our word. What we do for 2025 remains an open question. For now, we will maintain the 50bp of easing we had been expecting. But we would be dishonest if we did not consider that the risks have shifted to the possibility of some further RBA tightening. For that, we will let the data decide. But we are now only one bad inflation report from

amending our forecasts to include some additional tightening.

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