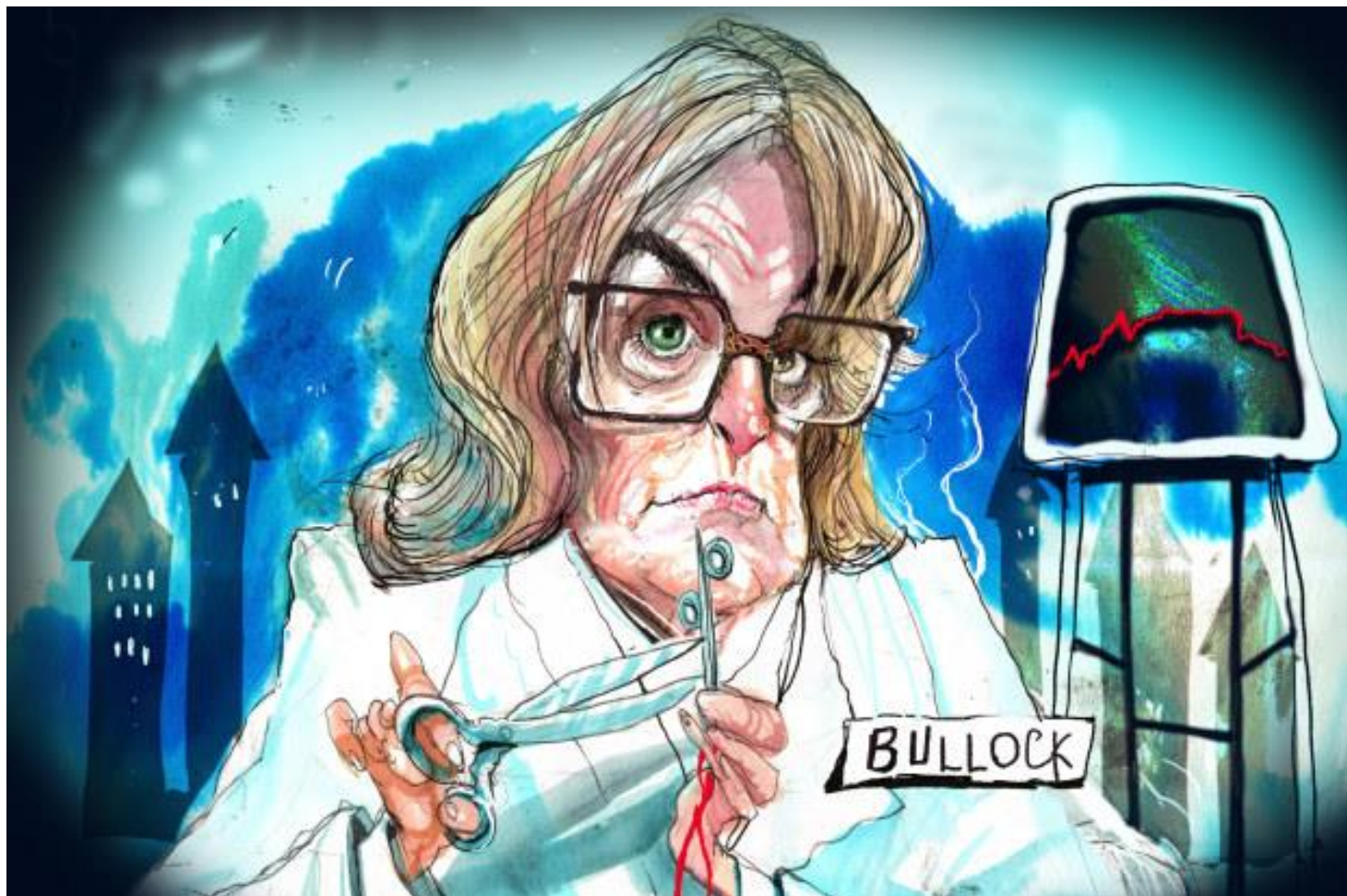


Has the RBA Cut Rates Too Soon?



Has the RBA Cut Rates Too Soon?

BY PAUL MIRON



It has been a very active and interesting start to 2025, with Tuesday's interest rate cut being the main economic news. We believe the right economic decision should have been to hold rates. This is despite the market's overwhelming expectation of a rate cut.

The Australian economy has proven to be remarkably resilient over the course of the 13 interest rate increases since May 2022. More importantly, the economic data is showing green shoots. December 2024 saw an increase of 4.6% in retail sales since December 2023 and the labour market remains strong,² with the

unemployment rate at 4.1% and 44,000 people added to the employment market last month.³

Following the Australian RBA's economic principles, interest rate cuts should only be considered once we have reached two key figures:

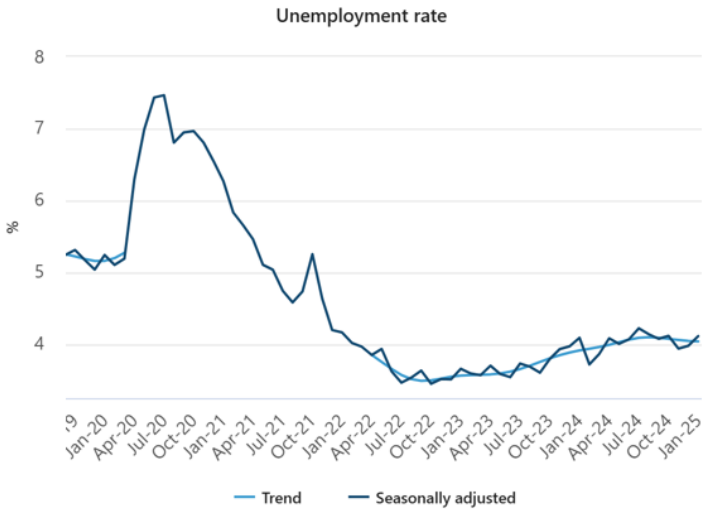
- **Inflation to be between 2% and 3%:** currently, the preferred measurement of inflation by the RBA is 'Trimmed Mean', which is sitting at 3.2%.⁴
- **Non-Accelerating Inflation Rate of Unemployment (NAIRU) of 4.5%:** The unemployment rate is critical as the Treasury's research indicates that the Australian economy is operating past the NAIRU of 4.5%, and excess employment is adding inflationary pressure to the economy. Hence, the RBA would like to see unemployment rise to keep inflationary pressures at bay whilst hoping not to negatively deteriorate GDP.

¹ <https://www.afr.com/policy/economy/why-the-rba-cash-rate-cut-was-a-head-scratcher-20250218-p5ld7o>

² <https://www.abs.gov.au/statistics/industry/retail-and-wholesale-trade/retail-trade-australia/latest-release>

³ <https://www.abs.gov.au/statistics/labour/employment-and-unemployment/labour-force-australia/latest-release>

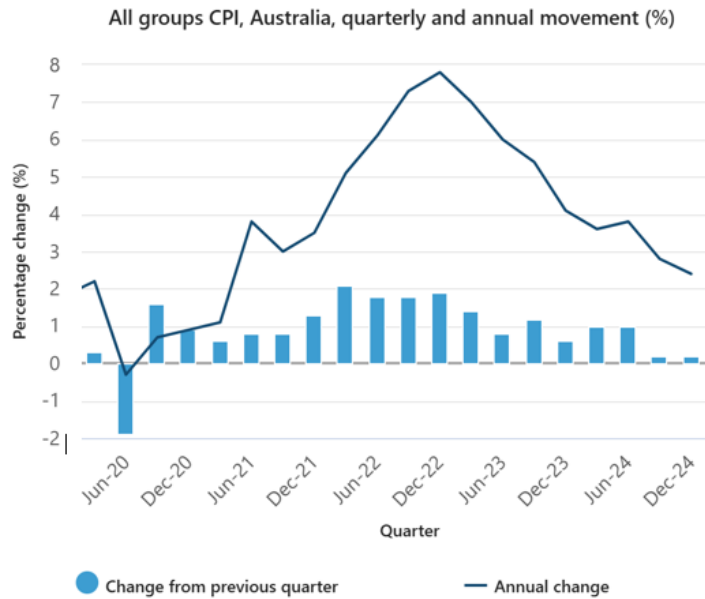
⁴ <https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release#:~:text=CPI%20and%20Trimmed%20mean%20annual%20inflation%20both%20lower&text=This%20quarter%20the%20Trimmed%20mean,cent%20in%20the%20September%20quarter.>



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Michele Bullock's speech in December made it clear that the RBA will not make interest rate decisions on future guidance or forecasting, and this week's interest decision has deviated from this logic.⁶ Furthermore, the RBA Governor's rhetoric was incredibly hawkish in her press conference post the rates announcement this month, overtly implying that the next interest movement could be upward if any forecasted data missed the RBA's expectations. Michelle Bullock was very defensive, calling out the market's future expectation of a series of rate cuts this year as being overly optimistic.

We believe the interest rate call is audacious in light of the evolving trade war and the recent uptick in US inflation that could signal global inflation is sticky and only reinforce the economic argument to hold rates.⁷



⁵ <https://www.abs.gov.au/statistics/labour/employment-and-unemployment/labour-force-australia/latest-release>

⁶ [rba.gov.au/speeches/2024/mc-gov-2024-12-10.html](https://www.rba.gov.au/speeches/2024/mc-gov-2024-12-10.html)

All this leaves one wondering whether, from an outward perspective to the wider community, could the RBA have succumbed to political pressure or been influenced by the overwhelming pressure from financial markets?

It is undoubtedly brave and uncharacteristic of the RBA to commence interest rate cuts before benefitting from economic data that provides the rationale and confidence for cutting rates. We believe that the trigger-happy rate cut is risky, will be very damaging to the RBA's reputation, and could damage confidence in the economy if interest rates need to be reversed; although unlikely, it is still a possibility. There is also a train of thinking that by triggering an early interest rate cut, there will be less focus and pressure on the RBA for rate cuts during the election campaign and can help avoid the perception of influencing the election result.

Time will tell whether this has been the correct decision, but we believe that this is a more precarious decision than the market realises.

Paul has spent the past 25 years in the banking and finance sector, the majority of which has been debt transactions. He co-founded Msquared Capital eight years ago as he identified a widening gap in the market for a trusted private credit fund manager and is passionate about enabling investors to access high-quality mortgage investments secured by real estate.

Paul has been instrumental in the firm's expansion while at all times maintaining a meticulous focus on credit analysis. As the private credit sector has boomed in recent years, Paul has been a vocal advocate for transparency in the sector to ensure investors can understand what they are actually investing in.

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<https://www.theguardian.com/business/live/2025/feb/12/ofwat-thames-water-clean-up-delays-us-inflation-rachel-reeves-bank-bosses-business-live>

⁸ <https://www.abs.gov.au/statistics/economy/price-indexes-and-inflation/consumer-price-index-australia/latest-release>