

July Monthly Economics and Markets Review

Overview

Domestic economy

Expectations for where the cash rate might trough rose over the month – from 2.87 per cent to 3.02 per cent – as the Bank surprised economists and financial markets by holding rates steady at its July meeting. However, following softer than expected labour market and inflation data, both markets and economists seemed to have gained confidence that this will prove to only be a one-month delay with the cash rate widely anticipated to be lowered in August.

International economy

The US passed a key fiscal bill and signed multiple trade deals while warning of higher tariffs for countries without agreements by 1 August. Meanwhile, the Federal Reserve faces internal and external pressure over interest rate policy, and China's economic data showed slowing GDP and investment growth but stronger industrial output and exports.

Interest rates

Three-year and 10-year Australian Government bond yields rose 14 basis points to 3.39 per cent and 10 basis points to 4.24 per cent respectively in July. The RBA surprising both economist and market expectations by holding rates steady at its July meeting as well as the passing of the 'One Big Beautiful Bill Act', progress on US trade negotiations and solid US labour market data saw rates move higher at the start of the month before a lower-than-expected Q2 CPI had the opposite effect toward the end of the month.

MATURITY	ISSUER	YIELD	1 MONTH BPS CHANGE	1 YEAR BPS CHANGE
3 Year	QTC	3.61	12	-46
	Australian Government	3.39	14	-36
	US Government	3.90	16	-6
5 Year	QTC	3.95	8	-28
	Australian Government	3.60	13	-19
	US Government	3.97	14	14
7 Year	QTC	4.37	4	-11
	Australian Government	3.90	11	-4
	US Government	4.16	14	28
10 Year	QTC	4.91	2	3
	Australian Government	4.24	10	12
	US Government	4.37	13	40

Prices sourced from Macrobond and QTC are correct at the time of publication

AUSTRALIAN DOLLAR CROSSES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
AUD/USD	0.6438	-2.0%	-1.4%
AUD/EUR	0.5625	0.9%	-7.0%
AUD/GBP	0.4864	1.6%	-4.7%
AUD/JPY	96.9063	2.8%	-1.1%

MAJOR CURRENCIES	RATE	1 MONTH % CHANGE	1 YEAR % CHANGE
EUR/USD	1.1444	-2.8%	6.0%
GBP/USD	1.3235	-3.5%	3.5%
USD/JPY	150.52	-4.9%	-0.3%
USD/CNY	7.1769	-0.2%	0.9%

The tables above show yields on bonds issued by the Queensland, Australian and US Governments as well as values for the Australian Dollar against a range of currencies and US Dollar against major currencies. The change in yields and exchange rates over different time periods are also included.

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Domestic economy

SUMMARY:

Expectations for where the cash rate might trough rose over the month – from 2.87 per cent to 3.02 per cent – as the Bank surprised economists and financial markets by holding rates steady at its July meeting. However, following softer than expected labour market and inflation data, both markets and economists seemed to have gained confidence that this will prove to only be a one-month delay with the cash rate widely anticipated to be lowered in August.

REVIEW:

- The RBA kept the cash rate steady at 3.85 per cent at its July meeting against economist and market expectations for a 25-basis point cut.
 - The decision to leave the cash rate unchanged was not unanimous, with six Board members voting for rates to remain on hold and three voting for a change. This is the first time the RBA has published the Board's vote.
 - In the post-meeting commentary, Governor Bullock emphasised that the decision to hold was about timing rather than direction. The Governor added that the Board does not want to fight inflation again and suggested that it wanted to see the Q2 CPI outcome before deciding on rate cuts.
 - The Minutes provided extra detail that while the Board viewed recent data as having been broadly in line with forecasts, some data were considered to have been 'slightly stronger than expected.' Hence, a wait-and-see approach was necessary. Those who voted to keep the rate on hold mentioned that 'lowering the cash rate a third time within the space of four meetings would be unlikely to be consistent with the strategy of easing monetary policy in a cautious and gradual manner to achieve the Board's inflation and full employment objectives'.
- Employment rose 2,000 in June, one-tenth the amount expected. Subdued jobs growth, a higher participation rate and statistical noise (the households rotating into the ABS monthly survey had a higher propensity to be unemployed than those rotating out) were behind a 0.2 percentage point rise in the unemployment rate to 4.3 per cent.
- Headline CPI rose 0.7 per cent in Q2 to be up 2.1 per cent over the year. The annual rate eased from 2.4 per cent in Q1, toward the bottom of the RBA's 2-3 per cent target band and is the lowest since Q1 2021. Trimmed-mean CPI rose 0.6 per cent in Q2 to be 2.7 per cent higher over the year. The annual rate eased from 2.9 per cent in Q1, close to the middle of the RBA's 2-3 per cent target band and is the lowest since Q4 2021. Quarterly growth in these two key measures were both one-tenth below consensus estimates.
- Quarterly growth in other measures of core (market services, weighted median) and domestic (non-tradables, labour market sensitive) related inflation also slowed. Quarterly inflation eased across both goods and services with this softness evident across the CPI basket. For instance, the share of items with quarterly annualised price growth of more than three per cent fell back to its post-2010 average and the share with prices growing by less than two per cent annualised topped 50 per cent for the first time since Q2 2021.
- Consumer confidence edged 0.6 per cent higher in July. There was a divide between those surveyed before the RBA announced its decision to keep rates on hold in July with those surveyed before (after) this more (less) confident.
- The NAB Business Survey suggested an improvement in business conditions (+8 points) and confidence (+3 points) in June. NAB's cost measures were broadly stable in June, with purchase and labour cost growth continuing to outpace growth in final product prices.

WHAT TO WATCH:

With it widely expected that the RBA will lower rates at its meeting in August, attention will now turn to whether a follow-up move might come at either its September, November or December meetings. To that end, getting a cleaner read on the labour market following the softer June read which, at least to some extent, may have been impacted by statistical noise will be important. As will further information on the breadth of disinflationary pressures in the economy. Upcoming monthly CPI reports, but especially the Q3 edition due out in October, will be of particular interest to the central bank.

CHART 1: THE UNEMPLOYMENT RATE LIFTED BY TWO-TENTHS IN JUNE, AGAINST EXPECTATIONS OF NO CHANGE. THIS WAS THE BIGGEST UPSIDE SURPRISE IN MORE THAN A YEAR.

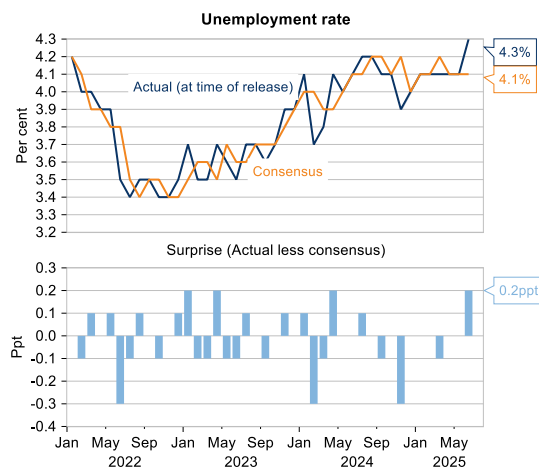


CHART 2: TRIMMED MEAN INFLATION MODERATED IN Q2 WITH THE ANNUAL RATE NOW NOT FAR ABOVE THE MIDDLE OF THE RBA'S TARGET BAND...

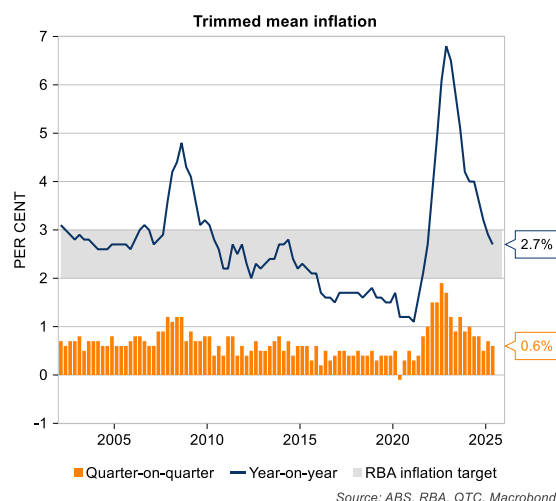
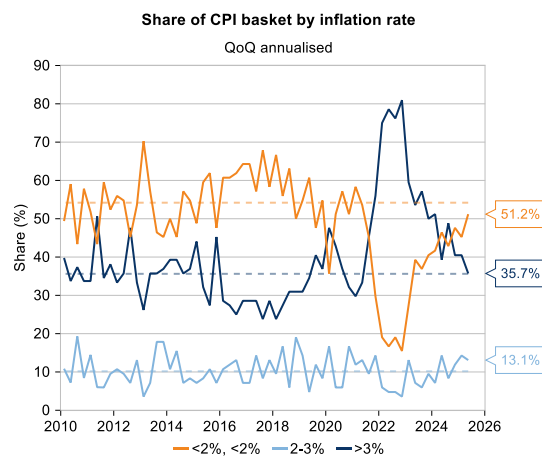


CHART 3: ...WITH THE EASING IN INFLATION EVIDENT ACROSS THE BASKET AS THE SHARE OF ITEMS WITH (QUARTERLY ANNUALISED) PRICE GROWTH OF LESS THAN TWO PER CENT RISING AND ABOVE THREE PER CENT FALLING



International economy

SUMMARY:

The US passed a key fiscal bill and signed multiple trade deals while warning of higher tariffs for countries without agreements by 1 August. Meanwhile, the Federal Reserve faces internal and external pressure over interest rate policy, and China's economic data showed slowing GDP and investment growth but stronger industrial output and exports.

REVIEW:

- The *'One Big Beautiful Bill Act'* was passed. The Congressional Budget Office estimates a net cost to the budget over the next decade of US\$3.4 trillion.
- US trade-related developments included:
 - The US signed trade deals with Japan, South Korea and the EU featuring a 15 per cent tariff on exports to the US along with investments in or purchases from key US sectors as part of the deals. Trade deals were also struck with Indonesia, the Philippines and Vietnam.
 - The Australian Government will lift biosecurity restrictions on US beef originally imposed following an outbreak of 'mad cow' disease in 2019. The decision follows a review by the national agriculture department into steps taken by US authorities to accurately track cattle movements from Canada and Mexico into the US where the animals were slaughtered before being exported. This decision also comes as Australia seeks to negotiate a trade deal with the US and avoid 50 per cent tariffs on steel and aluminium, 200 per cent on pharmaceuticals and 10 per cent on other items.
 - President Trump extended this deadline for higher tariffs to 1 August, while simultaneously sending letters to US trading partners warning of new tariff rates if trade deals are not reached by this date.
 - President Trump plans to shorten the 50-day deadline previously communicated to Russia to agree to a ceasefire with Ukraine to *'about 10 or 12 days.'* If no deal is reached then secondary sanctions (for example, on countries which buy exports such as oil from Russia) could be introduced.
- Focus was on the US Federal Reserve and its Chair Powell:
 - Christopher Waller, a Federal Reserve Governor, echoed his earlier calls for the Fed to cut rates in July. This reflected his view that policy was too restrictive, there are building downside risks to the labour market and that tariffs would temporarily boost the price level but not permanently impact inflation. Waller is one of the candidates considered most likely to replace Fed Chair Powell when his term expires in May. Waller indicated that he would be prepared to serve in this capacity if asked by the President.
 - Kevin Hassett, Head of the National Economic Council, said the Fed has got it wrong on policy and more oversight of the central bank is needed. Kevin Warsh, a former Fed Governor, critiqued the FOMC's inaction on rate cuts. Both Kevins are among the leading candidates to replace Fed Chair Powell.
 - Treasury Secretary Bessent announced plans for an internal review of the Fed, including with respect to its building renovations. He also considers that the Chair Powell should be able to stay in the role till his term expires in May next year (if he wants to).
- In terms of **US** economic data:
 - Core CPI inflation rose 0.2 per cent in June, supported by modest rises in the core goods and services components. The core PCE deflator increased by slightly more than expected in May to be up 2.7 per cent over the year.
 - Non-farm payrolls rose 147,000 in May, above expectations of 106,000. Both the unemployment and underemployment rates fell by one-tenth to 4.1 per cent and 7.7 per cent respectively.
- In **China**, annual real GDP growth slowed from 5.4 per cent to 5.2 per cent in Q2. In the month of June, annual growth in industrial production rose to 6.8 per cent from 5.8 per cent, retail sales growth fell to 4.8 per cent from 6.4 per cent, and fixed investment slowed to the weakest pace since 2021. There were mixed signals on the property market with weaker investment and prices, but stronger starts and completions. Export growth lifted on backlog clearance and export front-loading. Growth in aggregate financing edged up to 8.9 per cent, but RMB loan growth remained at a record low of 7.1 per cent.

WHAT TO WATCH:

How the global economy responds to potential clarity around US trade policy settings will be key to watch in the months ahead as will progress in negotiations with the last big domino to fall, China.

CHART 4: THE *'ONE BIG BEAUTIFUL BILL ACT'* IS SET TO INCREASE THE US BUDGET DEFICIT BY 3.4 TRILLION OVER THE NEXT DECADE

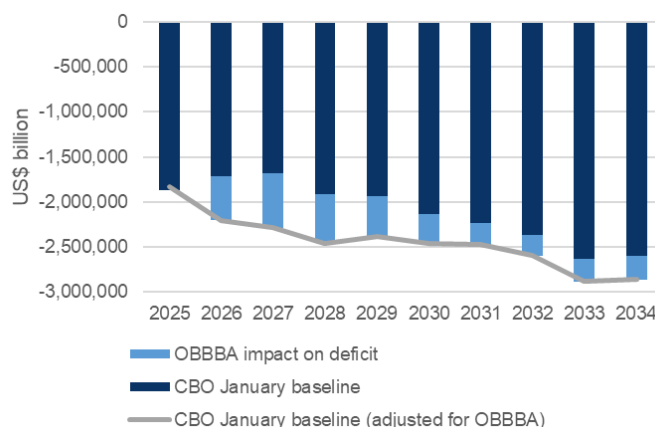


CHART 5: THERE WERE MIXED READINGS ON THE CHINESE ECONOMY IN THE MONTH OF JUNE...

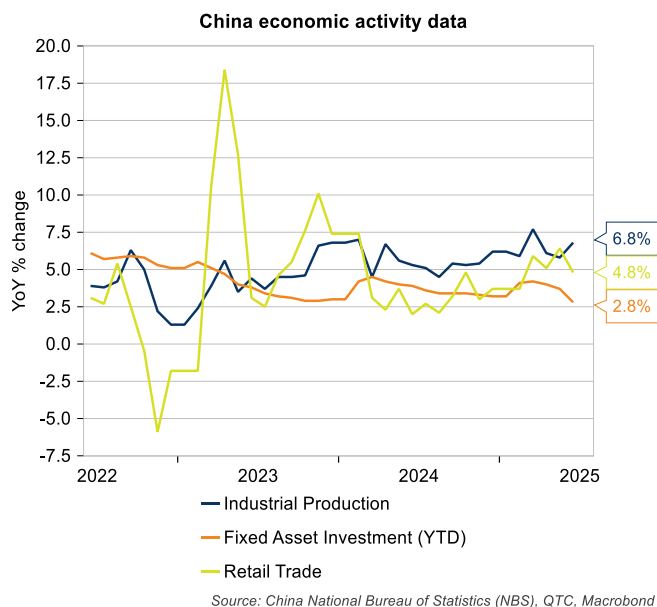


CHART 6: ...WHILE BOTH THE QUARTERLY AND ANNUAL RATES OF GDP GROWTH SLOWED IN Q2

