Economics and Markets Research

Australian Forward View

From Risk to Reality

In this issue

- **Our forecasts for growth are largely unchanged following the release of the Q2 national accounts, and we still expect a gradual rise in the unemployment rate.**
- **We now expect Q2 trimmed mean CPI to print at 1.0% qoq amid ongoing cost pressures.**
- **For the RBA, the upside risks to inflation have crystalised and we see them lifting rates at the September meeting, with the risk of a follow up in November.**

The data flow over the past month confirmed that growth has slowed. The national accounts show GDP growth eased from an annualised pace of around 2.9% over H2 2025 to around 1.4% in H1 2026. The decline in business conditions in the NAB Business Survey suggests that growth may have slowed further in Q3. That said, labour market indicators and outcomes have remained resilient.

However, the CPI data point to a stronger than expected outcome for the Q3 trimmed mean (released in late October). Price pressures also remain evident on the input cost side in the business survey and additionally, the rise in oil prices presents a material risk for ongoing cost pass-through.

For the RBA, the extent of inflation pressures mean they will need to recalibrate policy higher, though tighter financial conditions and some signs of slower growth will mean a cautious approach is maintained. We expect a hike in September. A November follow up is a possibility, depending on the activity data over the next two months.

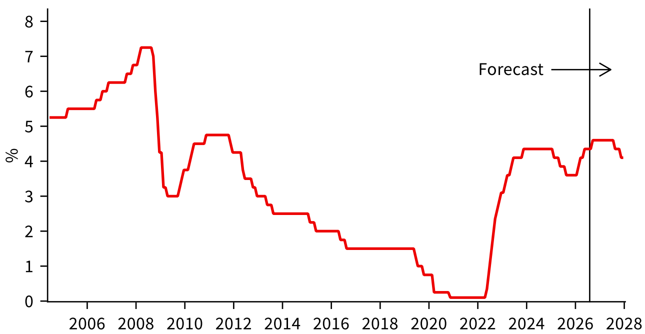
We continue to see below trend growth over 2026 (1.4%) and 2027 (1.6%) before some improvement over 2028 (1.8%). A multi-year period of below trend growth sees an ongoing gradual rise in the unemployment rate – which is now expected to reach around 5% in 2028 before stabilising. On inflation, we still expect a peak this year, and for a gradual cooling in quarterly terms through 2027. This would see underlying inflation reach annualising near the middle of the target band by late 2027.

Uncertainty remains elevated. Ongoing supply disruptions continue to pose a material risk to the economy, while the correction in the housing market poses some additional downside risk to growth. For both growth and inflation, productivity remains a key challenge.

Key Forecasts	2024	2025	2026	2027	2028
Real GDP (b)	1.2	2.6	1.4	1.6	1.8
Employment (a)	2.3	1.5	1.6	1.1	1.3
Unemployment Rate (b)	4.0	4.3	4.5	4.8	5.0
Headline CPI (b)	2.4	3.6	4.2	2.6	2.5
Trimmed Mean CPI (b)	3.2	3.3	3.6	2.8	2.5
RBA Cash Rate Target (b)	4.35	3.60	4.60	4.10	3.60
$US per A$ (b)	0.62	0.67	0.70	0.67	0.70

Source: National Australia Bank
Notes: (a) annual average growth, (b) end-period, shaded area represents NAB forecasts.

RBA Cash Rate Target and NAB Forecast



Source: National Australia Bank; RBA

Authors: Gareth Spence, Taylor Nugent, Jessie Cameron, Michael Hayes, Sally Auld

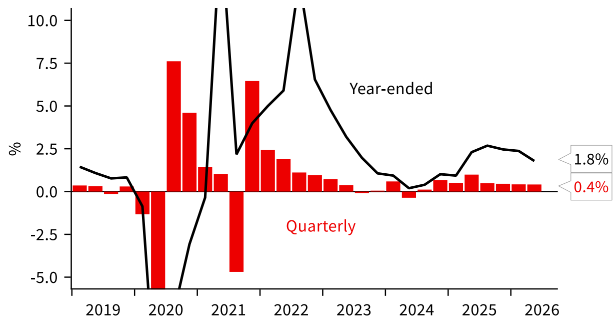
Consumption

Household spending remained solid in Q2 but has moderated from its strong pace last year.

Household consumption rose 0.4% qoq in Q2 to be 1.8% higher over the year. Growth was driven by a 1.4% qoq rise in discretionary spending, largely reflecting a 10.3% qoq jump in vehicle purchases, particularly EVs. While some of this strength may prove temporary, motor vehicle imports remain elevated and wholesalers and retailers continued to build inventories, suggesting expectations of sustained demand. Outside vehicle purchases, discretionary spending growth was broad based.

The increase in discretionary spending more than offset a 0.3% qoq decline in essential spending. Electricity, gas and other fuels spending fell 6.0% qoq because of milder weather conditions, while spending on the operation of vehicles declined 0.6% qoq amid higher fuel prices and free public transport in some states. In contrast, insurance & other financial services spending rose 1.4% qoq.

Real Household Consumption Growth



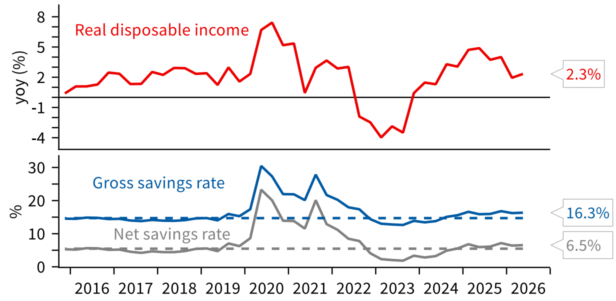
Source: National Australia Bank, Australian Bureau of Statistics, Macrobond

More timely indicators suggest nominal household spending remained resilient into Q3. The ABS Monthly Household Spending Indicator rose 1.1% mom in July and was 7.0% higher over the year, the fastest annual pace since June 2023. Growth was broad-based across both discretionary and essential categories. While our NAB Spend Trend shows spending rose a further 1.1% mom in August, this largely reflected higher fuel spending and there are tentative signs that discretionary spending slowed in the month.

This resilience in spending has occurred despite weak consumer sentiment. While confidence had improved over the previous two months, it fell again in September because of higher fuel prices and expectations of further interest rate rises. Sentiment is around 9% below its level at the start of the year.

Looking ahead, we expect real household consumption growth to slow to 1.5% over 2026, from 2.5% over 2025. This reflects a moderation in real household disposable income growth and, to a lesser extent, softer housing market conditions. However, households have some ability to smooth their consumption by drawing down savings, with balance sheets generally healthy and savings rates a little higher than pre-pandemic levels.

Household Income and Savings



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond
Notes: Dotted line represents the ten-year average to the end of 2019.

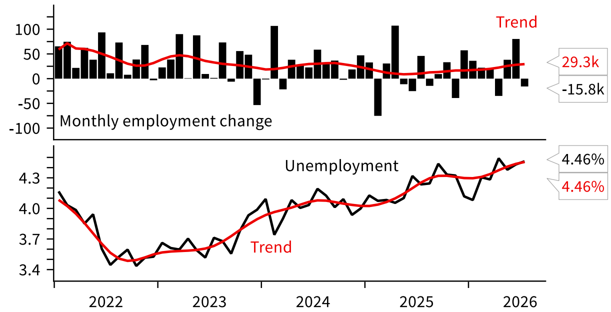
Labour Market

The unemployment rate is expected to continue to gradually trend higher.

Despite monthly volatility, employment growth is trending around +30k per month and the unemployment rate has drifted higher. We expect trend employment growth to slowly ease as activity slows, driving a continued gradual rise in the unemployment rate to around 4.8% by end 2027 and 5% by the end of 2028 where we expect it to peak.

We expect next week's August labour force release to show a rebound in employment growth to around +20k and the unemployment rate to fall to 4.4%.

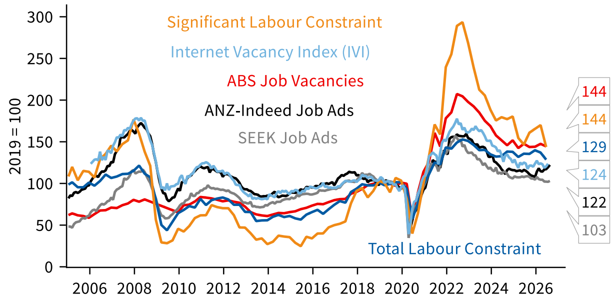
Australian Employment



Source: National Australia Bank, ABS

Measures of job advertising have edged higher in recent months, after signalling mixed but gradual easing since the start of 2026. We continue to expect cooler GDP growth to flow through into softening labour demand, but timely indicators do not yet suggest a sharp shift in labour market conditions is underway.

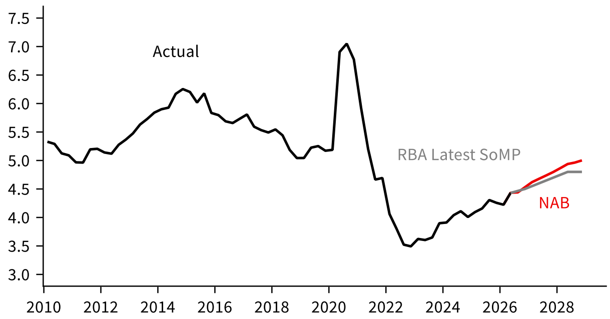
Measures of labour demand



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

We expect to see a relatively steady rise in the unemployment rate peaking near 5% in 2028. This is broadly in line with the RBA's latest SoMP forecast. In July, the unemployment rate came in at 4.5%, in line with the RBA's Q4 forecast.

Unemployment Rate Forecasts



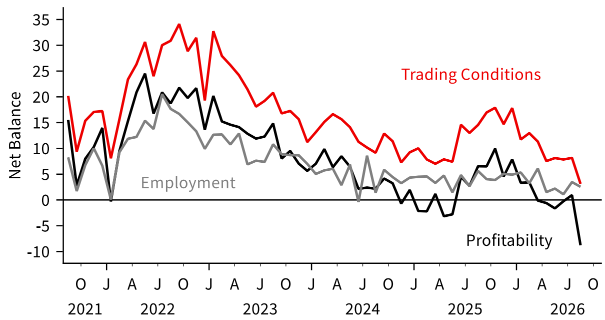
Source: National Australia Bank, RBA

Businesses

Business confidence and conditions weakened in August while the outlook for business investment is soft.

The August NAB business survey saw a broad weakening in activity indicators while cost growth remained elevated. The decline in business conditions was driven by falls across the profitability and trading subcomponents. The fall in profitability mirrors the ongoing larger-than-usual gap between cost and price growth as businesses face elevated margin pressure. Capacity utilisation partially unwound its July spike, though it remained well above its long-run average.

Business Conditions Sub-components, SA

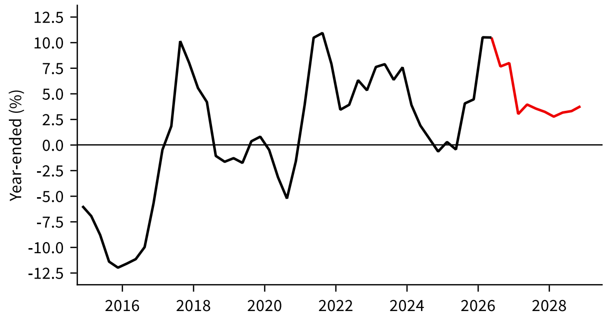


Source: National Australia Bank, National Australia Bank, Macrobond

A key dynamic over the next 6 months will be whether the softer profitability and weak confidence flow through to employment and capex intentions.

Business investment fell 0.5% qoq in Q2 but remained 10.5% higher over the year, with quarterly volatility driven by lumpy data centre investment. Machinery & equipment investment fell sharply because of volatility from data centre equipment but was stronger than expected. This was offset by purchases of aircraft and industrial transport equipment. Meanwhile, there was meaningful growth in non-dwelling construction. Engineering construction was driven by renewables and mining construction, while the ongoing pipeline of projects underway supported new buildings. Business investment remains soft outside of strength in data-centre related activity.

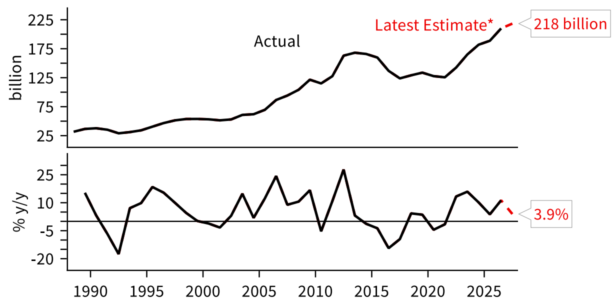
New Business Investment Forecast



Source: National Australia Bank, Australian Bureau of Statistics, Account in-house, Macrobond

The forward-looking element of the ABS' Q2 Capex data released in late August provided a third estimate of nominal business investment intentions for FY26/27. The update implied nominal capex growth of 3.9% for next financial year, up from 0.7% last quarter, but implies only modest growth in real terms. Strength in investment intentions was concentrated in data centre, energy and construction related industries. Despite the improved outlook from last quarter, business intentions are in line with our view that business investment will soften over the forecast period.

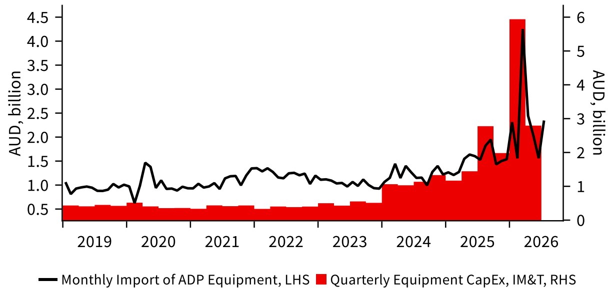
Nominal Capital Expenditure Actuals & Expected (FY)



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond
* Latest estimates are adjusted using their long-run realisation ratio.

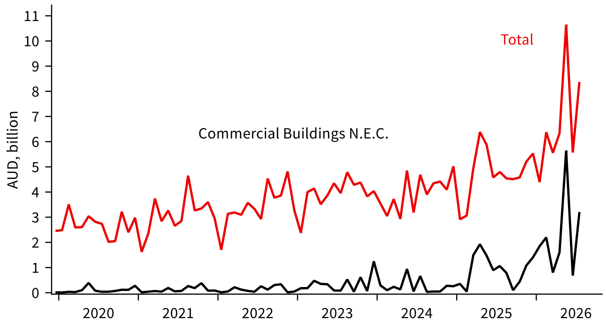
Higher frequency indicators such as the import of goods and building approvals remained softer than they were earlier in the year but do imply some improvement into Q3. ADP equipment imports, which captures the import of chips and other data centre equipment, partially retraced falls seen in Q2. Also seeing improvement in July were private non-dwelling building approvals which saw significant volatility over Q2.

Import of ADP Equipment & Equipment Capex from Information Media & Telecommunication



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

Private Non-Residential Building Approvals



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

We see new business investment slowing to ~3% yoy by 2027 and remaining around that level through the forecast horizon. We expect the quarterly pace to remain volatile but to trend softer as the economy slows more broadly.

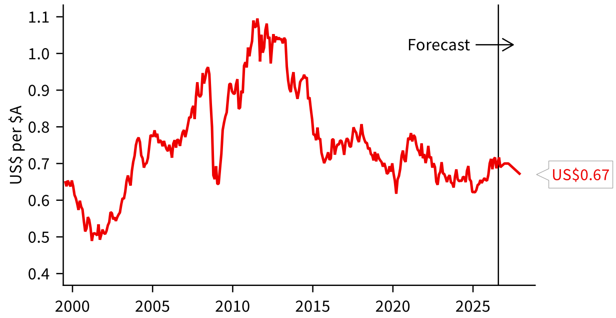
Foreign Exchange

The Australian dollar has appreciated notably since the start of the year.

The AUD/USD and AUD TWI are up 6.6% and 5.9% year to date, respectively. The AUD has been primarily supported by RBA policy tightening and related widening in interest rate differentials. More recently, higher commodity prices have provided additional support, while the continued depreciation in USD/CNY has also been a modest tailwind.

Our NAB FX Strategy team expect AUD/USD to end 2026 around US$0.70c, remaining comfortably within the US$0.6850 to US$0.7280 YTD range. Looking to 2027, NAB FX Strategy forecasts continue to see potential for AUD to move into a lower US$0.65-0.70c range later in the year, consistent with weak domestic economic growth, lower inflation and the commencement of an RBA easing cycle.

AUD/USD



Source: Bloomberg; National Australia Bank

Housing

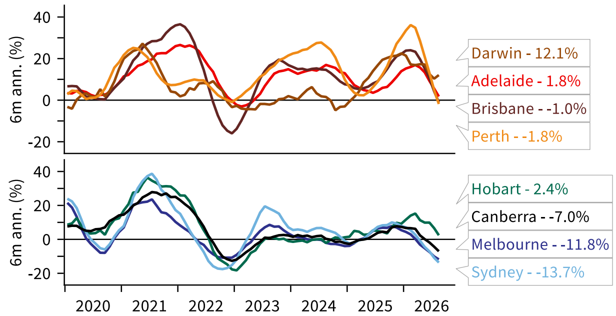
The housing market slowdown continues to broaden.

Dwelling prices across the combined capitals declined by 1.1% in August and are now 4.6% below their March peak. This reflects the combined effects of higher interest rates, deteriorating affordability and weaker sentiment and investor demand following the Federal Budget's tax reforms. While prices have declined for five consecutive months, they remain 1.1% higher than a year ago.

The slowdown has been most pronounced in Sydney and Melbourne, where prices began falling earlier and have since recorded the largest cumulative declines. Indeed, dwelling prices are 7.1% below their February peak in Sydney and 6.5% below their November 2025 peak in Melbourne. By contrast, price declines have only more recently broadened to include the mid-sized capitals, where prices peaked around April and May 2026.

However, the pace of monthly price falls across the mid-sized capitals is approaching those seen in Sydney and Melbourne. In August, dwelling prices fell 1.0% in Brisbane and 0.8% in both Adelaide and Perth, compared with declines of 1.4% in Sydney and 1.1% in Melbourne.

Dwelling Prices Growth - Greater Capital Cities

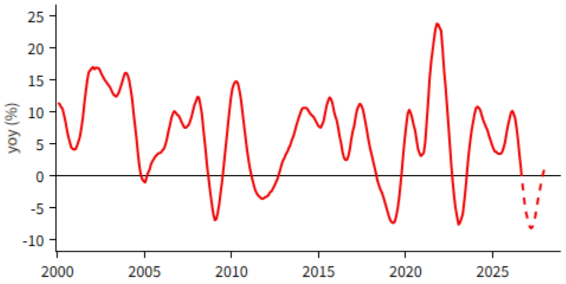


Source: National Australia Bank, Cotality Australia, Macrobond

We now expect dwelling prices to decline by 6% over 2026, compared with our previous forecast of a 5% fall, largely reflecting downward revisions to historical data. Price declines are still expected to be larger in Sydney and Melbourne, where prices are forecast to decline by around 10% over the year. By contrast, prices across the mid-sized capitals are expected to be broadly flat to slightly positive.

We then expect the housing market to stabilise in early 2027 before returning to modest growth in the second half of the year, as the RBA begins its easing cycle.

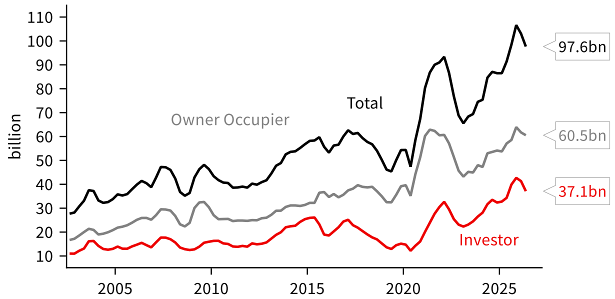
Dwelling Price Forecast - Combined Capitals



Source: Cotality; National Australia Bank
Note: Dotted line reflects NAB forecast.

Rental market conditions remain tight, although some indicators suggest pressure may be easing at the margin. Capital city vacancy rates remain low but have gradually risen to around 1.8%, their highest level since early 2025. Advertised rent growth has also slowed from its peak but remains elevated at 5.3% on a six-month annualised basis.

Value of New Housing Loan Commitments



Source: National Australia Bank, Australian Bureau of Statistics
Notes: Excludes refinancing.

Inflation

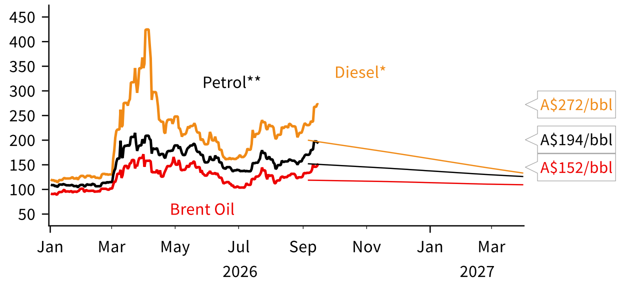
Cost increases are extending too-high inflation.

We had already seen the risk skewed to the high side of the RBA's August SoMP forecast of 0.83% for Q3 trimmed mean inflation. After strong and broad-based inflation evident in the July data, we now expect Q3 trimmed mean inflation of 1.0% qoq.

In the month of July, trimmed mean inflation was 0.5% mom. Seasonal patterns in the monthly data are still unsettled, and the result likely reflects residual seasonality with price increases around the turn of the financial year. We don't expect that monthly pace of growth to persist, but residual seasonality is not reason enough to dismiss the wider pattern of too high and broad-based inflation.

The NAB Business Survey shows cost pressures remain elevated for firms as the consequences of the geopolitical environment continue to echo through and the recent leg higher in oil prices further underscores the extent of cost pressure in the pipeline. Importantly, the disruption to diesel markets has been even more acute than to crude oil, leaving diesel prices especially elevated. Uncertainty about oil market dynamics remains high, the cost shock for now threatens to be more protracted and variable than earlier assumed.

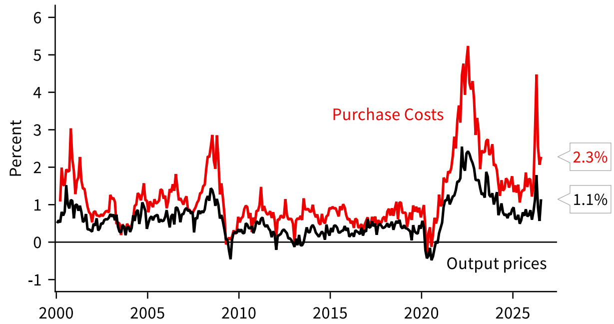
Oil and refined products with RBA assumption



thin line is RBA August SoMP forecast assumption in AUD
*Gasoil 10ppm, **Mogas 95, ***Jet Kerosene
Source: National Australia Bank, Bloomberg

Beyond the direct impact on headline inflation from higher fuel prices, more elevated and more durable cost inflation will in part flow through to end consumer prices and pressure firm margins. Purchase cost rises are sharply outpacing output prices in the NAB Business Survey, and profitability has worsened.

NAB Survey Prices



Source: National Australia Bank

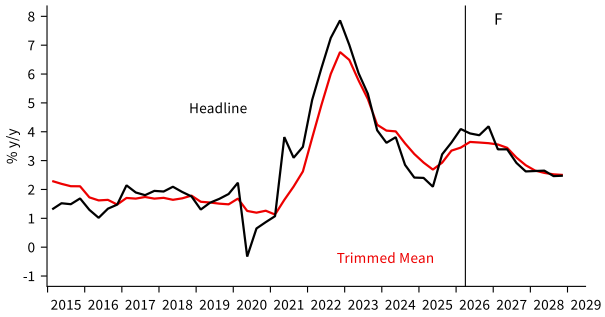
We continue to expect that the combination of tighter monetary policy settings, real income pressures from elevated inflation, and housing market dynamics will together drive growth below trend and leading to a gradual increase in the unemployment rate. As a result, while headline and underlying inflation will remain elevated for now, it is expected to moderate quite sharply next year.

Elevated pipeline inflation pressures and a starting point of a still capacity constrained economy raise the risks that a short-term cost-driven inflation echoes into second round effects that drive a more persistent challenge.

Our forecasts continue to embed an assumption that crude oil prices ease towards $80/bbl by early next year. Prices do not need to fall for inflation (the *change* in prices) to moderate over time, but a more protracted cost challenge is a risk to the outlook. More resilience in the labour market or activity growth than we expect could also forestall the inflation progress we expect to emerge next year, but risks here are not all one way. A sharper rise in the unemployment rate than our baseline would see inflation risks recede more quickly and raise the prospect of a larger cycle.

We expect headline inflation to be 4.2% over 2026 and 2.6% over 2027. We expect trimmed mean of 3.6% over 2026 and 2.8% over 2027, although we see it annualising near the RBA's 2.5% target in the second half of next year.

Inflation and NAB Forecast



Source: National Australia Bank, ABS, RBA

Monetary Policy

We expect the RBA will lift rates at the September meeting, taking the cash rate to 4.6%. There is risk of a follow-up rate hike in November.

While the monthly CPI is volatile, we expect Q3 trimmed mean inflation of 1.0% qoq based on outcomes from the expenditure class level data. If realised, this would be a material upward surprise to the RBA's expectation for 0.8% qoq.

Further, while the RBA held rates at the August meeting in a unanimous vote, the argument for an increase in rates was centred on risks to inflation being skewed to the upside, and that there was little tolerance to see inflation return to target later than envisaged in the forecasts (late 2027). Indeed, the minutes also noted "*several members judged that it was quite possible that the upside risks to the inflation forecast would crystallise, requiring some further tightening*".

In addition, the minutes highlighted a number of sources of upside risk: the Middle East conflict becoming more protracted, widespread cost pressures being passed onto consumer prices, data centre construction proving more inflationary, demand proving more resilient, and weak productivity.

Recent data flow suggests that some of these risks have crystallised. The stronger than expected CPI points to some additional pass-through, oil prices have risen to around US$110/bbl, while the Q2 national accounts showed relatively healthy private sector growth and very weak labour productivity growth.

While the national accounts confirmed that growth had slowed in H1 2026 from the pace seen in H2 2025, this was broadly in line with the RBA staff's forecast. The RBA forecast embodies a period of below trend growth and some spare capacity opening up in the economy in order to bring inflation back to target. Upward revisions to earlier data also mean annual growth was stronger than expected at 2.1% yoy in Q2, suggesting that less capacity may have been building in the interim.

Though volatile, the national accounts also showed ongoing weakness in productivity growth and a reacceleration over the past two quarters in nominal unit labour costs growth in the non-farm sector. Growth in this measure is currently tracking at 3.6% yoy – well above the 2.5% mid-point of the RBA's target band.

The NAB Monthly Business Survey does suggest that growth may have slowed further in Q3, but also highlights the inflation challenges the RBA has seen in its own liaison program, highlighting significant cost pressures for business across both material inputs and labour costs. Capacity utilisation also remains above average despite the slowing in the activity indicators in the survey.

Taking that all together, we see the RBA increasing rates 25bp at the September meeting – that will see policy move more clearly into restrictive territory and be the highest rate since 2011. We also see the risk that the RBA acts again in November, taking the cash rate to 4.85%. One or possibly two rate rises will leave the real cash rate around 1% or a touch higher at end 2026; this outcome would see Australia's real cash rate higher than that in the US, New Zealand, Canada, Japan and a little below that in the UK.

The RBA will remain data dependent and we expect they will maintain their strategy of bringing inflation back towards target while minimising the cycle in the labour market. Tighter policy will depend on both the labour and activity data over the coming months. The RBA do not want to see any economic or labour market softness beyond what is necessary, but the extent of the inflation challenge means they may need to tolerate some undershoot of demand relative to supply.

Key Forecasts

Economic Forecasts	2026 Q1	2026 Q2	2026 Q3	2026 Q4	2027 Q1	2027 Q2	2025	2026	2027	2028
Activity										
Private Consumption	0.4	0.4	0.4	0.3	0.2	0.3	2.5	1.5	1.2	1.4
Dwelling Investment	1.5	1.6	1.6	1.5	1.2	0.9	5.2	6.3	3.2	2.6
Underlying Business Investment	7.5	-1.1	1.0	0.6	1.1	0.0	4.2	8.0	1.7	2.3
Public Final Demand	-0.5	0.2	0.4	0.4	0.4	0.4	2.7	0.5	1.6	1.6
Domestic Final Demand	**0.9**	**0.3**	**0.6**	**0.5**	**0.5**	**0.4**	**3.0**	**2.2**	**1.7**	**1.9**
Inventories (cont.)	-0.1	-0.1	0.0	0.0	0.1	0.0	0.1	-0.2	0.1	0.0
Gross National Expenditure	**0.8**	**0.2**	**0.6**	**0.4**	**0.6**	**0.3**	**3.1**	**2.0**	**1.8**	**1.9**
Net Exports (cont.)	-0.7	0.1	-0.1	0.0	-0.1	0.0	-0.3	-0.8	-0.1	-0.2
Real GDP	**0.3**	**0.4**	**0.4**	**0.3**	**0.5**	**0.3**	**2.6**	**1.4**	**1.6**	**1.8**
Nominal GDP	**0.6**	**0.8**	**0.7**	**0.9**	**1.0**	**0.7**	**6.2**	**3.1**	**3.2**	**3.0**
Labour Market										
Employment (a)	0.6	0.3	0.4	0.4	0.3	0.3	1.1	1.6	1.2	1.4
Unemployment Rate (a)	4.2	4.4	4.4	4.5	4.6	4.7	4.3	4.5	4.8	5.0
Wage Price Index	0.8	0.8	0.8	0.8	0.8	0.8	3.4	3.2	3.2	3.2
Inflation										
Trimmed Mean	0.8	0.8	1.0	0.9	0.8	0.7	3.3	3.6	2.8	2.5
Headline	1.4	0.6	1.3	0.9	0.6	0.6	3.6	4.2	2.6	2.5
Rates and Foreign Exchange										
RBA Cash Rate Target	4.0	4.35	4.60	4.60	4.60	4.60	3.60	4.60	4.10	3.60
$US per A$	0.7	0.69	0.69	0.70	0.70	0.69	0.67	0.70	0.67	0.70

Source: ABS; National Australia Bank
Notes: Data are percentage growth rates over the quarter or year, except where specified otherwise; Shaded area represents NAB forecasts; (a) quarter average.

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