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## More questions but fewer answers

- **Uncertainty is elevated and confidence has fallen, but the economy has shown resilience. Spending has held up and business conditions are in positive territory.**
- **Q1 CPI was slightly softer than expected but we see stronger underlying inflation coming through from Q2.**
- **We continue to see growth of 1.5% this year and a marginal improvement next year. The unemployment rate is expected to rise to 4.7%.**

Global uncertainty remains elevated as disruptions to the supply of oil and other key commodities from the Middle East become more prolonged, global inflation pressures grow and the rates backdrop has shifted higher. While the Australian consumer has been relatively insulated from higher fuel prices owing to the reduction in the fuel excise and a fall back in refined product prices, we expect the broad-based cost pressure (as reflected in the NAB Business Survey) to be largely passed through to consumers.

Both business and consumer confidence remain weak, though there is little evidence to date of a significant pull-back in economic activity. That said, the unemployment rate jumped to 4.5% in April and may suggest hesitancy hiring amid elevated uncertainty. Our NAB transactions data point to resilience in consumer spending and while business conditions have eased, they remain in positive territory.

Our forecasts for growth and the labour market are largely unchanged this month, though we have nudged up our Q1 forecast for household consumption to 0.4% qoq (prev. 0.2%). Sensitivity to lower retail fuel prices means our headline inflation profile is now expected to peak slightly lower, though underlying inflation is still expected to peak at 3.9%.

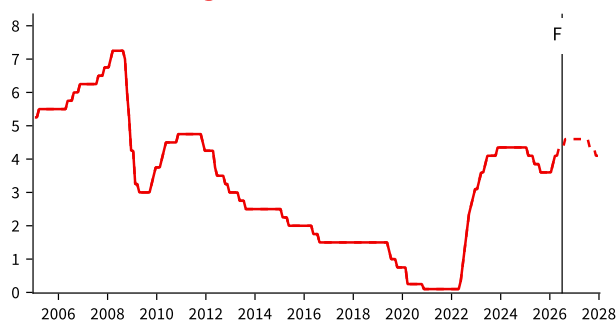
The Federal Budget released last week is expected to have a broadly neutral impact on the economy over 2026-27 and become slightly contractionary over the forward estimates. That is, however, depending on forecasts of expenditure being realised, with 2025-26 having been more stimulatory than initially expected.

Additional cost pressures on the back of higher oil prices comes against a backdrop of already elevated inflation. We see the RBA lifting rates to 4.6% in August and then remaining on hold as incoming data are assessed for the impact of the 100bps of tightening this year and how the impact of the conflict in the Middle East flows through.

Key Forecasts	2024	2025	2026	2027
Real GDP (b)	1.2	2.6	1.5	1.9
Employment (a)	2.4	1.5	1.6	1.2
Unemployment Rate (b)	4.0	4.3	4.5	4.7
Headline CPI (b)	2.4	3.6	4.3	2.3
Trimmed Mean CPI (b)	3.3	3.4	3.7	2.7
RBA Cash Rate Target (b)	4.35	3.60	4.60	4.10
3-year Yield (b)	3.8	4.1	4.5	4.0
\$US per A\$ (b)	0.62	0.67	0.73	0.72

Source: National Australia Bank, Account in-house, Macrobond  
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, Macrobond

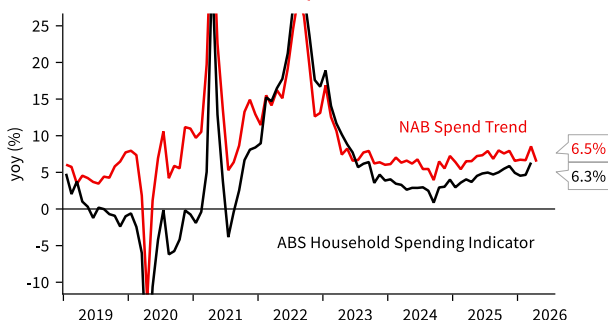
## Consumption

Household spending has remained relatively resilient to date.

The ABS's household spending indicator suggests that real household consumption grew by a solid 0.7% qoq in Q1. This was driven by higher spending on transport, recreation & culture, as well as health. If taken at face value, this would imply some upside risk to our revised 0.4% qoq forecast. However, we place less weight on this signal, as the series has mapped poorly to the national accounts measure of consumption, in part due to coverage and timing differences.

While nominal spending growth has lost some momentum this year and consumer sentiment has fallen by around 10% since March, there are no clear signs of a material pullback in consumption alongside higher global oil prices. Our [NAB Spend Trend](#) shows a 1.1% decline in April however, this partly reflects payback from elevated spending on fuel and food in March. We also saw a sharp decline in travel spending (which also includes refunds on air travel), though it is too early to determine whether this signals a broader slowdown in discretionary spending.

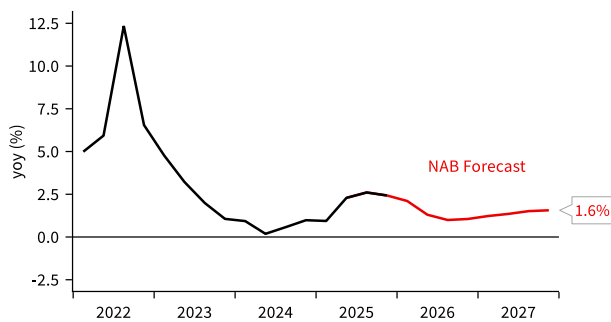
### Nominal Household Consumption Indicators



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

We expect real household consumption growth to slow over 2026 to 1.2% compared to its annual pace of 2.4% over 2025. This reflects a fading of the tailwinds that previously supported real household disposable income growth, higher fuel prices following the end of the fuel excise in June, as well as higher interest rates and a rising unemployment rate. While the Working Australians Tax Offset (WATO) will provide some support to household incomes from mid-2028, the impact is modest, around 0.2% of annual household disposable income.

### Real Household Consumption



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

## Labour Market

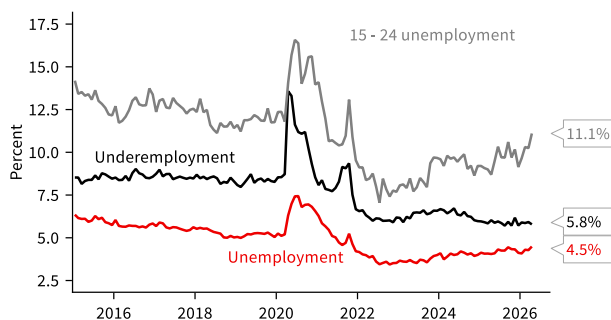
The labour market is expected to weaken as demand softens.

The unemployment rate rose 2 tenths to 4.5% in April. Our forecasts had anticipated a rise in the unemployment rate, but the April jump is sooner and sharper than we expected.

Firms may have pulled back on hiring more sharply than expected in response to very elevated uncertainty. More people remained in unemployment as the job finding rate fell, while hours worked per person rose 0.9% mom as existing staff were used more intensively. It could be the case that hiring recovers should the acute uncertainty facing business decisions recede.

The Easter long weekend occurred within the survey period, which may have further added to usual monthly volatility. On a trend basis the unemployment rate remained at 4.3% and employment was steady at around +22k. Even so, the data highlights the risk that the labour market will prove less resilient than we have been forecasting.

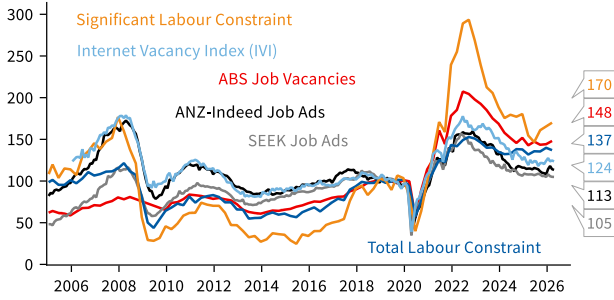
### Australian Unemployment and Underemployment



Source: National Australia Bank, ABS

Forward looking measures of labour demand are consistent with some cooling, but not an abrupt shift. ABS job vacancies rose 2.7% in the three months to February and since then more timely indicators have been mixed. The April business survey saw the employment index reach its lowest level since mid-2024 and both the Seek and Indeed measures of job ads have fallen a little since February.

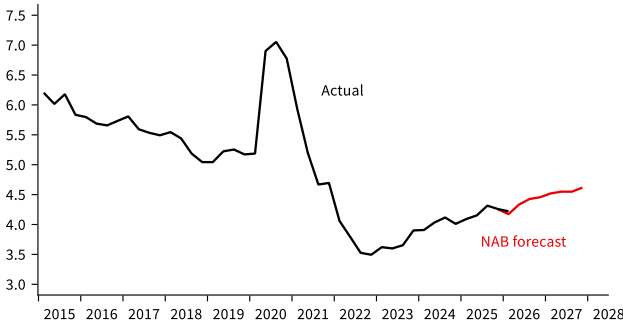
Measures of labour demand



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

Trend unemployment has remained around 4.3% since mid-last year, a level we see as broadly consistent with full employment and not a material source of inflationary pressure. We expect cooler demand to place upward pressure on the unemployment rate, and the April data raises the prospect that could flow through more quickly. We continue to see the unemployment rate rising to around 4.7% by the end of 2027.

Unemployment Rate Forecasts



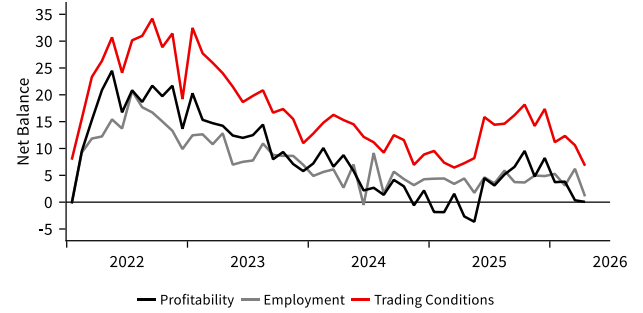
Source: National Australia Bank, RBA

Businesses

The impact of the Middle East conflict and rising interest rates have begun to show up in survey measures of activity.

The [April business survey](#) was the second since the outbreak of the Middle East conflict, with firms reporting higher prices and signs that demand has begun to slow. In the latest survey, the impact of the supply shock, that had previously been constrained primarily within business confidence, became more widespread and was evident in most indicators. Business conditions fell across all three sub-indexes, alongside forward orders, capex and cashflow, all of which declined to be well below their long-run averages. This aligns with our view that demand will begin to slow over the rest of the year.

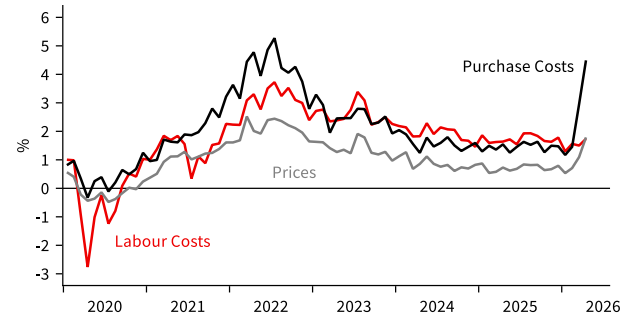
Business Conditions Sub-Components



Source: National Australia Bank, National Australia Bank, Macrobond

Businesses in the survey also reported a spike in input cost growth to 4.5% in quarterly terms, outpacing price growth by a wide margin, suggesting businesses are currently facing growing margin pressure. We expect businesses to pass on much of the supply shock related costs relatively quickly, given the starting point of an economy facing capacity constraints.

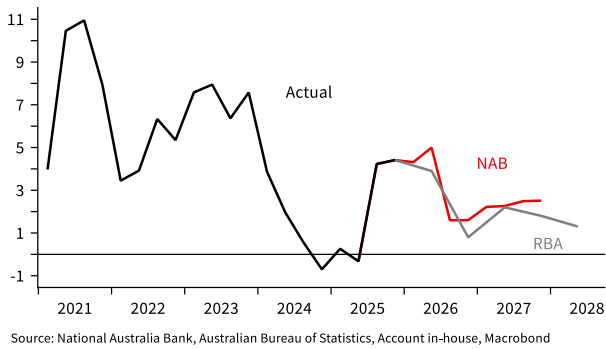
NAB Business Survey, Cost & Prices, Quarterly



Source: National Australia Bank, National Australia Bank, Macrobond

On business investment, next week's Q1 Capex data will provide further insight into the state of business investment prior to the Middle East conflict as well as an updated set of expectations for the last quarter of 2025-26 and the second estimate for 2026-27. While these data will be dated, they will give additional insight into business investment intentions. Previous estimates suggested capex spending would grow ~6.2% over 2025-26 in nominal terms which would then slow to ~1.4% the following year. The latest monthly international trade in goods data and trade price indexes saw ADP imports, which captures much of import heavy data centre equipment, surged in March. While data centres are expected to remain a key story of strong growth, given its relatively small share of spending we expect total underlying business investment growth to slow in the back half of 2026.

**Real Business Investment Forecasts**



**Foreign Exchange**

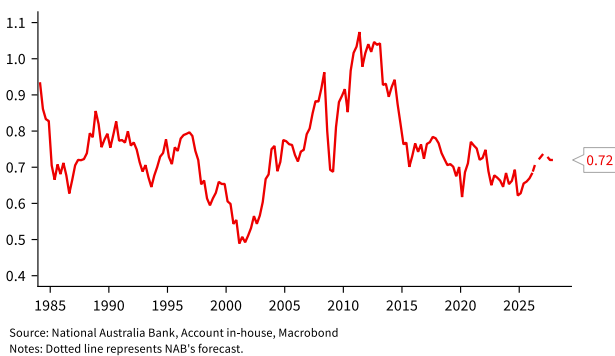
**AUD/USD is still broadly seen trading within a 70 to 75 cent range.**

AUD/USD and the AUD TWI have appreciated by around 6% since the start of the year, supported by a widening interest rate differential and a favourable risk backdrop.

Our [NAB FX Strategists](#) have made no changes to their AUD forecast from their 14 April update. At that time, they lowered the end Q2 AUD/USD forecast by 1 cent to US\$0.71, left the end-2026 forecast unchanged at US\$0.73, and made modest upward revisions to the 2027 profile.

AUD/USD continues to be characterised as a 70 to 75 cent currency, though near-term risks are tilted to the downside. In particular, the limited prospects for a reopening of the Strait of Hormuz in the coming weeks could weigh more heavily on global risk sentiment than has been observed to date.

**\$US per A\$**



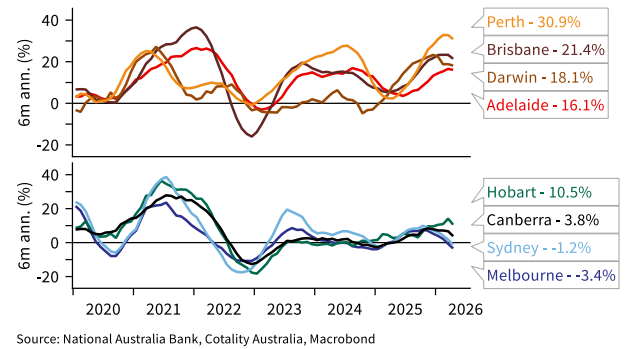
**Housing**

**House price momentum was already slowing prior to the recent tax policy announcements.**

Dwelling price growth eased to 0.3% mom in April, the weakest outcome since early 2025, though prices remain around 10% higher over the year. This moderation is consistent with the 3.8% qoq fall in new housing loan commitments in Q1, following strong growth over 2H25 and a repricing in interest rate expectations.

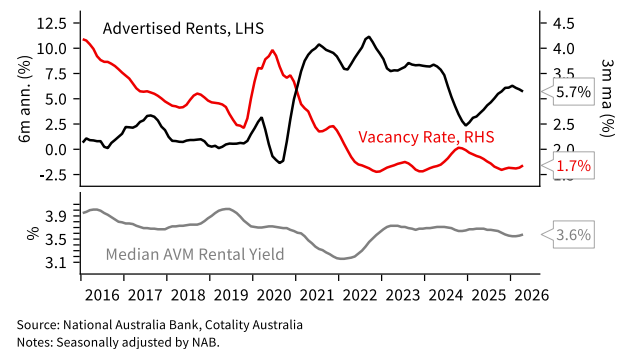
The loss of momentum is more evident in Sydney and Melbourne, where prices fell 0.6% mom in April and, on a three-month annualised basis, declined by 3.7% and 6.0%, respectively. In contrast, mid-sized capitals continue to outperform, supported by stronger population growth and relatively tight labour markets. Median dwelling prices in Brisbane, Perth, and Adelaide are now higher than those in Melbourne, but are still below Sydney.

**Dwelling Prices - Greater Capital Cities**



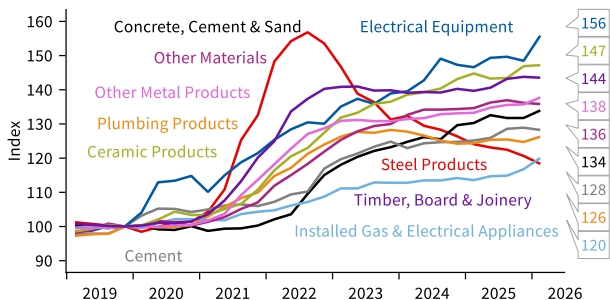
The rental market remains tight, with rental vacancy rates near record lows at 1.7%. Advertised rents growth remains elevated, though has edged lower to 5.7% on a six-month annualised basis in April.

**Advertised Rents and Vacancies**



Both rents and dwelling prices continue to be underpinned by a persistent imbalance between supply and demand. While dwelling starts have lifted since late 2023, led by apartments, they continue to outpace completions. As a result, the pipeline remains elevated at around 235k dwellings under construction, which is about 35% above the pre-pandemic average. At the same time, supply remains constrained by elevated construction costs and capacity limitations, with material input costs still around 40% higher than pre-pandemic levels and likely to face renewed upward pressure from the conflict in the Middle East.

### Construction Input Prices



Source: National Australia Bank, Australian Bureau of Statistics, Macrobond  
Notes: \* Q4 2019 = 100.

The Federal Budget introduced material changes to both capital gains tax and negative gearing, including the removal of negative gearing for established dwellings and a shift to inflation indexation for capital gains. These reforms reduce incentives for leveraged investment in existing housing, particularly high debt / low yield strategies, and are expected to weigh on investor demand and relatedly, credit growth. While exemptions for new builds aim to support additional supply over time, capacity constraints in construction suggest the supply response is likely to be gradual.

Following these announcements, we have revised down our house price growth forecast to 2% in 2026 (from 6% at the beginning of the year) and expect growth of 3% in 2027. These revisions are relatively modest given the underlying supply shortage in the housing market. With house prices only adjusting slightly and rental markets already tight, we expect some upward pressure on rents in the near-term.

## Inflation

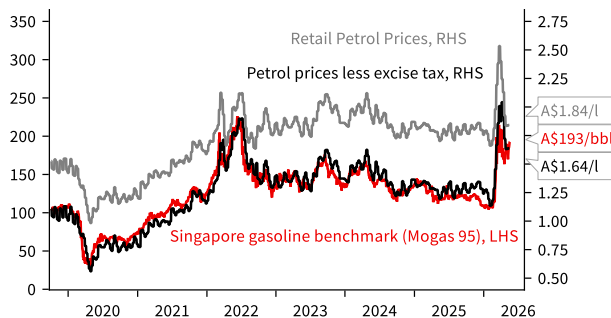
**Inflation remained too high but was improving in Q1. It will get worse before it gets better.**

Q1 trimmed mean was 0.8% qoq and 3.5% yoy. It confirmed that inflation was both too high and broad-based ahead of the Iran shock, but it also suggested that domestic pressures were not driving further acceleration in quarterly terms into early 2026. Absent the Middle East shock, we think the RBA's inflation concerns would have been easing rather than building.

The quarterly trimmed mean outcome was released alongside the March monthly outcome, which reflected the initial impacts of the conflict in the Middle East. CPI rose 4.6% over the year to March driven by the surge in fuel prices, which were 33% higher in March.

Looking forward, the 32c per litre reduction in the fuel excise and a fallback in regional refined benchmarks have driven a decline in fuel prices in April and May. That fallback is sharper than we had assumed and we now expect Q2 headline CPI closer to 4.6%.

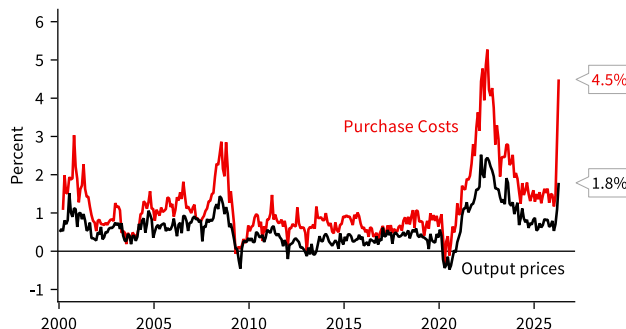
### Fuel prices



Source: National Australia Bank, Bloomberg

However, the cost shock is broader than fuel, and the NAB Business Survey shows businesses have faced a sharp surge in purchase costs. It also suggests that a lot of the pressure is being passed on into end prices. The key question is how much and how broadly this is reflected in measured CPI over coming months, with the first evidence of this to be seen in the April CPI next week.

### NAB Survey Prices

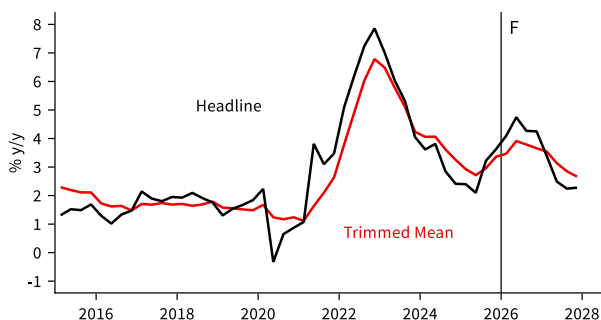


Source: National Australia Bank

We continue to expect quarterly trimmed mean inflation to peak in Q2 at 3.9% and end the year at 3.6%, a cumulative 0.5ppt higher over the course of 2026 due to flow through of the Middle East cost shock.

The magnitude of this shock is outside historical experience. Our forecast anticipates that this will be reflected in rapid and broad-based passthrough to a breadth of consumer prices, but there is significant uncertainty about the magnitude and timing. We also note that while we forecast high quarterly trimmed mean outcomes in the near term, we also expect these underlying measures to show less persistence than would ordinarily be the case. If price rises cascade through explicitly temporary price changes or surcharges, then core inflation is likely to give too strong a signal of underlying inflation momentum.

### Inflation and NAB Forecast



Source: National Australia Bank, ABS, RBA

indicators in the NAB Business Survey. Rates are only modestly restrictive, and inflation is well above target as a starting point. While inflation is expected to peak in Q2 the pace of moderation beyond that will be critical if inflation is to return to around 2.5% as the RBA had forecast by mid-2028.

Risks on inflation are clear, but our central case sees the shock fading and inflation returning to target over time. A peak in rates at 4.6% is in restrictive territory and as a result we continue to pencil in cuts from H2 2027. The timing of this remains uncertain given that rates may not yet have peaked.

## Monetary Policy

**We now expect the RBA to increase the cash rate to 4.6% in August (previously June).**

From there, it is likely that the RBA would pause for a period and assess the impact of the 100bps of tightening delivered this year, which will have taken the cash rate to the highest level since October 2011.

We shifted our call from June to August on the unexpected jump in the unemployment rate to 4.5% in April, which is around 0.3ppts higher than the RBA's Q2 quarter average forecast of 4.2% - and notably above the 4.3% expected at year end. The labour force data can be volatile on a monthly basis and it is possible that the fall in the job finding rate was driven by caution in the business sector amid elevated uncertainty through early April that may well subside.

Nonetheless, this result will support the assessment of the monetary policy board that there is now more "space" to watch and observe the impacts on both inflation and growth that emanate from higher oil prices and elevated uncertainty, given rates are now back in restrictive territory. While most activity indicators show resilience, there are some signs of softening that could feed concerns about the activity outlook. The PMI's for May softened, following the easing in NAB business conditions and forward orders in April, and there has been a significant change in housing market conditions over recent months.

The RBA continues to face a challenging set of circumstances with inflation having risen above target even prior to the unfolding supply shock due to the conflict in the Middle East. While consumers have been somewhat insulated from the impact of petrol and diesel price rises, we expect the magnitude and breadth of pressure on business margins to support CPI in the near term. The immediate impact on activity has also been less than expected. Of note, short term inflation expectations are also elevated, risking that inflation becomes more ingrained.

The Board has sought to minimise any cycle in unemployment and tolerate only a protracted return of inflation to target. The Board looks set to continue that strategy, taking less insurance against elevated inflation risks evident in the RBA staff assessment and cost and price

## Key Forecasts

### Australia forecasts

	% Growth q/q			% Growth y/y		
	Q4-25	Q1-26 (f)	Q2-26 (f)	2025	2026 (f)	2027 (f)
<b>GDP and Components</b>						
Private Consumption	0.3	0.4	0.2	2.4	1.2	1.6
Dwelling Investment	0.6	0.2	0.2	5.5	0.9	2.2
New Business Investment	0.1	-0.2	0.1	4.0	-0.1	1.0
Underlying Public Final Demand	0.9	0.4	0.4	2.4	1.6	1.6
<b>Domestic Demand</b>	<b>0.5</b>	<b>0.4</b>	<b>0.3</b>	<b>2.9</b>	<b>1.5</b>	<b>1.9</b>
Stocks (Cont. to GDP)	0.2	-0.1	0.0	-0.2	-0.1	0.1
<b>Gross National Expenditure</b>						
Exports	1.4	0.4	0.4	5.2	1.5	1.6
Imports	1.8	0.4	0.4	6.7	1.3	1.7
Net Export (Cont. to GDP)	-0.1	0.0	0.0	-0.3	0.1	0.0
<b>Real GDP</b>	<b>0.8</b>	<b>0.3</b>	<b>0.4</b>	<b>2.6</b>	<b>1.5</b>	<b>2.0</b>
Nominal GDP	1.8	0.9	1.3	6.0	4.5	4.1
<b>Labour Market</b>						
Employment	0.2	0.7	0.3	1.1	1.7	1.2
Unemployment Rate (Q-Ave, End of Period)	4.2	4.2	4.3	4.2	4.5	4.7
Wage Price Index (WPI)	0.8	0.8	0.8	3.4	3.2	3.2
<b>Inflation and Rates</b>						
Headline CPI	0.6	1.4	1.4	3.6	4.3	2.3
Trimmed-mean CPI	0.9	0.8	1.1	3.4	3.7	2.7
RBA Cash Rate (End of Period)	3.60	4.10	4.35	3.60	4.60	4.10
10 Year Govt. Bonds (End of Period)	4.76	4.97	5.10	4.76	5.00	4.80
\$A/US cents (End of Period)	0.67	0.68	0.71	0.67	0.73	0.72

Data are percentage growth rates over the quarter or year as noted, except where specified otherwise.

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