Data Snapshot

Tuesday, 4 June 2013

Bank of Melbourne

Cash Rate unchanged at 2.75%

- The Reserve Bank of Australia (RBA) left the cash rate unchanged at 2.75% at its meeting today as widely expected.
- The commentary gave the impression that the RBA is bit more confident that the low interest rate settings are doing its job. The Board "judged that the easier financial conditions now in place will contribute to a strengthening of growth over time, consistent with achieving the inflation target".
- However, the RBA has maintained its easing bias and continued to keep open the possibility for another rate cut. Monetary policy remained appropriate "for the time being". Further, the RBA continued to state that "the inflation outlook, as currently assessed, may provide some scope for further easing, should that be required to support demand."
- The RBA remains concerned about the level of the Australian dollar, and that it "remains high", despite falling sharply over a short period of time. We expect the Australian dollar will be a key factor in coming RBA decisions.
- We remain comfortable with our view that the RBA will remain on hold at its next meeting in July and in coming months. However, we still recognise the possibility of another depending on upcoming developments. The impact of earlier interest rate cuts on the domestic economy and the path of the Australian dollar will warrant close watching.

Below is the Governor's statement interspersed with our views.

RBA Statement: At its meeting today, the Board decided to leave the cash rate unchanged at 2.75 per cent.

Information becoming available since the previous meeting is consistent with global growth running a bit below average this year, with reasonable prospects of a pick-up next year. Commodity prices have declined from their peaks but, overall, remain at high levels by historical standards. Inflation has generally moderated over recent months and monetary policy has been eased further in a number of countries.

Our view: The outlook on the global economy is largely unchanged, but there is now "reasonable prospects" of a pickup in global growth next year.

RBA Statement: Financial conditions internationally are very accommodative. Despite the recent rise in sovereign bond yields, funding conditions for sovereigns, well-rated corporates and most financial institutions remain very favourable.

Our view: Global interest rates remain very low by historical standards, and should continue to *provide stimulus in time.*

RBA Statement: In Australia, growth over the past year has been a bit below trend. The outlook published by the Bank last month is for a similar performance in the near term and recent data are consistent with this. The unemployment rate has edged higher over the past year and growth in labour costs has moderated. Inflation has been consistent with the medium-term target and is expected to remain so over the next one to two years.

Our view: We continue to expect growth just a bit below 3 percent for 2013, which is close to the RBA's forecasts. We also continue to expect the labour force to continue to add jobs, but not strong enough to prevent the unemployment rate from rising to around 6 percent. The near-term outlook for below trend growth, soft employment and low inflation will continue to give the RBA room to cut rates if necessary.

There was a notable omission of the commentary on resource investment approaching a peak, and scope for other areas of the economy to pick up. It is possible that the RBA is a bit more confident that this is will occur. While recent data provides some tentative evidence of this, we believe that there remains some uncertainty about the strength this recovery in non-mining sectors.

RBA Statement: The easing in monetary policy over the past 18 months has supported interest-sensitive areas of spending and has been reflected in portfolio shifts by savers and higher asset values. Further effects can be expected over time. The pace of borrowing has thus far remained relatively subdued, though recently there have been some signs of increased demand for finance by households. The exchange rate has depreciated since the previous Board meeting, although, as the Board has noted for some time, it remains high considering the decline in export prices that has taken place over the past year and a half.

Our view: The RBA has been encouraged by the pickup in demand for home lending, providing evidence that low interest rates are having the desired impact, although soft growth in credit will keep the possibility of another rate cut alive. The commentary surrounding the Australian dollar would suggest that the RBA is still a little concerned about its current level despite falling sharply over a short period of time. We expect the Australian dollar will be a key factor in coming RBA decisions.

RBA Statement: At today's meeting the Board judged that the easier financial conditions now in place will contribute to a strengthening of growth over time, consistent with achieving the inflation target. It decided that the stance of monetary policy remained appropriate for the time being. The Board also judged that the inflation outlook, as currently assessed, may provide some scope for further easing, should that be required to support demand.

Our view: The first sentence alone would suggest that the RBA is a bit more comfortable that the low interest rates settings are doing its job. The use of "consistent with achieving the inflation target", would suggest that the RBA expects growth to strengthen sufficiently. However, the last two sentences indicate that the easing bias remains for the RBA and it continues to leave the door open for a rate cut. We would agree that low interest rates are working, but we continue to have some doubts about the strength of the recovery and the outlook for business investment.

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