Minutes of the September RBA Board Meeting

Patience Required. Warnings Given.

- The RBA's assessment of the global economy remains one of 'close to trend' growth. Concerns were expressed regarding the impact of weaker residential activity in China upon the Chinese financial system. Be alert but not alarmed, China has scope to adjust policy in that area.
- The RBA sounded a warning that additional speculative demand could amplify the property price cycle and increase the potential for property prices to fall later.
- Nothing new was said regarding the currency in the minutes. One imagines that positive comments will be made at next month's meeting regarding this week's decline in the AUD.
- The economy is not without its bright spots. The RBA noted growth in credit, firm housing activity and reasonable levels of business and consumer sentiment. It is also expecting modest growth in non-mining business investment over the course of 2014-15.
- A speech given today by RBA Assistant Governor, Christopher Kent noted that non-mining business investment was potentially being held back by a combination low growth in domestic demand (due in part to low wages growth), the impact of the high exchange rate, a lack of confidence and a lower appetite for risk than in the past.

The minutes of the RBA's September board meeting fleshed out the comments made by the Governor, Glenn Stevens on 2nd September. They added nothing new in terms of foreign exchange analysis, and the 'stability in interest rates' but did note the risks to future growth of further growth in asset prices based on increased leverage.

The RBA's assessment of the global economy remains one of 'close to trend' growth. The US is seen as recovering well while Europe remained weak. Developments in China's residential market were seen as a potential risk to Chinese growth. A further downturn in residential property could disrupt China's financial system although the RBA notes that China has scope to adjust policy in that area.

The RBA board questioned the July labour force figure which reported a sharp rise in the rate of unemployment. They noted the significant measurement issues surround labour market statistic and will no doubt spend time next month discussing the results for August where the unemployment rate fell and 121k jobs were created. This data was released after the RBA meeting.

The RBA noted that with economic growth slightly below trend, a sustained decline in the unemployment rate will be difficult to achieve. One 'positive' outcome from the 'spare capacity' in the labour market was that wage growth is weak. This should ensure inflation remains within the RBA's 2-3% target band – even if the currency were to fall (as it has done this week).

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Assisting global and domestic economic activity is very accommodative monetary policy.

In a section on financial stability, the minutes noted that "additional speculative demand could amplify the property price cycle and increase the potential for property prices to fall later."

The conclusion reached by the board came as no surprise. The market is not expecting the cash rate to rise any time soon.

The two areas where one can sense a degree of frustration within the RBA are the currency and non-mining investment. This week the currency may have begun the depreciation the RBA expected and hoped for. A lower currency will help the economy adjust to the decline in mining investment.

Non-mining business investment has picked up modestly, but the RBA notes that risk aversion has taken hold of both management and shareholders following the global financial crisis. Firms have lifted their holdings of cash and have only recently started to take advantage of historically low borrow costs.

In a speech given today by Christopher Kent, an Assistant RBA Governor, notes that businesses in Australia have a degree of spare capacity but that capacity utilization levels are approaching their long run average.

Holding back investment is a combination low growth in domestic demand (due in part to low wages growth), the impact of the high exchange rate, a lack of confidence and a lower appetite for risk than in the past.

Assistant Governor Kent concluded his speech with the following statement:

"If history is any guide, eventually the period of elevated risk aversion is likely to give way to a concern among businesses, not of losses, but of lost opportunities and a loss of market share."

We look forward to a revival in non-mining business investment.

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