Data Snapshot

Tuesday, 21 October 2014

Bank of Melbourne

# Minutes of the October RBA Board Meeting

## 'Steady as she goes and avoid the rocks'

- The RBA's assessment of the global economy had flashes of weakness but remained positive. Weakness in Europe and a softer Chinese property market were noted along with better business investment in the United States.
- Warnings about property prices were not made in the minutes but be assured, the RBA and APRA are watching closely.
- Historically slow wage growth and a soft labour market may sit behind the modest growth in retail spending. In the June quarter, spending rose more rapidly than income indicating that savings had declined.
- The RBA appeared to welcome the decline in the AUD but, given the decline in commodity prices, still seems to expect further weakness in the months ahead.
- The economy has a range of bright spots. Credit growth, dwelling investment and a steady rise in exports are underpinning economic activity. Consumption is growing, forward looking labour market indicators have improved and the weaker AUD will assist competitiveness.
- Still expecting a rate cut? The RBA's liaison with businesses suggested that the cost and availability of finance were not restraining business investment. Given this, a further rate cut would not be expected to spark a lift in investment.

The minutes of the RBA's October board meeting expanded upon the comments made by the Governor, Glenn Stevens on 7th October. Gone were the warnings on property prices but the minutes made it clear that the RBA is working with APRA on ensuring strong lending standards would be maintained.

The board's assessment of global economic conditions sounded a number 'warnings'. Weaker economic conditions in Europe had led to an 'unexpected' decline in the Eurozone's official interest rates. All is not well in Europe. China's softer property market was noted. This may have contributed to weaker iron ore prices and the lower AUD. In its view, the RBA believes that China has the policy tools to maintain growth at its target rate of a little above 7.0%.

The minutes sounded upbeat on the US with business investment lifting and job growth showing progress. Given very accommodative monetary policy around the globe, global growth is expected to expand on trend.

Considerations on the domestic economy were mostly positive. Exports have grown, dwelling investment is firm and consumption is growing. Wage growth is at historically low levels but while this is good for inflation, it does little to spur consumption. To this end, growth in consumption over the June quarter was assisted by a decline in the savings ratio.

Restraint in non-resources private business investment appears to be giving the RBA board a degree of frustration. They imply that a lack of 'animal spirits' lies behind the hesitancy to invest given the accommodative stance of monetary policy. It is this view that strongly suggests that the RBA has no intention of further reducing its cash rate.

Exchange rate volatility was discussed but the bottom line remains that the AUD is relatively high by historical standards. This is holding back the exchange rate's role in achieving a rebalancing of growth in Australia.

The RBA expects that the current setting of monetary policy will support demand as will the lower AUD. It notes that financial markets have priced in no change in the cash rate for the next 12 months. We believe it may come a little earlier given growth in the US economy and expected growth out of China. The travails of Europe are a shadow over global growth but in our view, steady reform and easy monetary conditions should see them rise off the floor in due course.

The RBA has presented a case for 'Steady as she goes and avoid the rocks'. Europe is likely to see more weak economic numbers and Chinese statistics will occasionally be unsettling. Markets may be volatile.

In the short term, the cash rate is most likely to remain on hold. The AUD seems set for a little more weakness (and volatility) and the economy will continue to expand modestly. In the current circumstances, this is not a bad outcome while we wait for 'animal spirits' to stir.

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The Detail

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