

RBA – The Balancing Act Continues

- At the RBA's first meeting for the year, the cash rate was left unchanged at 2.0% as widely expected.
- Despite heightened volatility in financial markets, the RBA noted that the global economy is continuing to grow. But it does acknowledge that risks exist and that outcomes remain uncertain.
- The RBA will release its Statement on Monetary Policy on Friday. That may provide details of any downgrade in its outlook for global growth.
- The RBA is permanently engaged in a balancing act, providing support or restraint when needed. As we approach 25 years of continuous economic growth, we expect the RBA will assist in achieving that goal by providing both stability and support via its current accommodative cash rate of 2.00% throughout 2016.

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Despite heightened volatility in financial markets, the RBA noted that the global economy is continuing to grow. The RBA is not hiding from the fact of volatility; it is telling us that, as yet, its impact on real global economic activity is limited. In the face of higher volatility, global monetary policy remains 'remarkably accommodative'. Official interest rates in the US, Europe and Japan remain well below those in Australia. In Germany 10 year bond yields are only 0.35%!

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As a reminder for those who are overly optimistic, the RBA notes that Australia's terms of trade have fallen. This implies reduced incomes in Australia and a drag on economic growth.

While noting the caveats, the governor's statement today provided a relatively upbeat assessment of the Australian economy. It noted the pick-up in credit growth and the slightly above average business sentiment. The decline in mining investment and the search for a lift in non-mining investment remains a vexing issue but one that will pass over time.

The RBA rightly regards its current policy as accommodative and it hints at the positive contribution to activity that flows from the weaker Australian dollar.

If the global economic environment takes a serious turn for the worse, the RBA is in a position to act. But that time is not yet, and in our view, it remains only an outside possibility. The RBA also has the cushion of modest inflation noting that continued low inflation may provide scope for easier policy, should that be appropriate to lend support to demand.

Outlook for Monetary Policy

There was little in today's statement to signal the RBA will look to move interest rates in the near-term. Since it met in December, it has seen the US lift rates, the Japanese adopt negative interest rates and the ECB hint at further stimulus. The RBA looks set to take a steady path.

We hold the view that the current financial market volatility will be contained and is unlikely to precipitate a sharp downturn in real global economic activity. As such, we expect the RBA to remain on hold throughout 2016.

We will be watching closely what happens to US monetary policy with its next meeting in mid-March. A further increase in rates could increase short-term volatility but it would also signal on-going growth in the world's largest economy.

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The one page text of the Governor's Statement can be found at <http://www.rba.gov.au/>

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