Interest Rate Outlook

Tuesday, 21 June 2016

Bank of Melbourne

Minutes of the June RBA Board Meeting

Another cut? Why?

- **The minutes of the RBA June board meeting, gave few hints regarding the future direction of policy. It was broadly positive on domestic and global economic growth but did note that inflation was expected to remain low for some time.**

- **The board found plenty to be positive about in both the domestic and global economies. Domestically net exports were adding to growth, with a special mention for the growth in service exports which include income from international tourism and international education. The strength of housing demand was noted and construction was expected to remain firm over the next year or so, particularly in the eastern capital cities.**

- **What was missing from the minutes were comments on the risks facing the global economy, apart from concerns over the 'Brexit' vote. There was nothing in these minutes on debt levels in China or the impact of the stronger USD on US export growth. However, the board did note that output in east Asia was growing at a below average pace.**

- **While the RBA expects inflation to remain low for some time, it did point out that some measures of wages were positive. This comment would suggest that the RBA is keeping a very close eye on labour costs and how these might contribute towards higher inflation over time.**

- **Given the minutes of the RBA board meeting, it is not difficult to see why the cash rate was left unchanged. The Australian economy is growing at a reasonable pace, the unemployment rate has fallen, the outlook for business investment may be underestimated by the usual surveys and consumption continues to expand. The global economic environment does not appear threatening and domestic wage growth may have reached its low.**

- **Today's RBA minutes did little to support the view that the RBA will cut rates again. The key to future rate cuts lies in inflation. If inflation moves lower and stays lower for longer than the RBA is currently expecting then a further cut or cuts would make sense. We have a rate cut pencilled in for August as we believe the May rate cut alone will not achieve its aim of lifting inflation in the required time frame.**

The minutes of the RBA June board meeting, gave few hints regarding the future direction of policy. It was broadly positive on domestic and global economic growth but did note that inflation was expected to remain low for some time.

The tone of the minutes reflected the decision to leave the cash rate unchanged.

The board found plenty to be positive about in both the domestic and global economies. Domestically net exports were adding to growth, with a special mention for the growth in service exports which include income from international tourism and international education. The strength of housing demand was noted and construction was expected to remain firm over the next year or so, particularly in the eastern capital cities.

On the consumption front, the board noted that Australian's were still saving at levels well above those seen pre-GFC but, importantly, that the savings rate has fallen over the year. This is supportive of consumption as was the observation that consumers' perceptions of their own finances were still a little above average.

Adding to the positive tone of minutes, the board noted that the ABS survey of businesses may be under estimating business investment intentions. The capital expenditure survey excludes industries such as health and education where assets such as software were becoming increasingly important.

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On the international front, the RBA board 'looked through' the recent weak US payrolls result and noted that its lower unemployment rate and rising wealth had led to stronger growth in consumption and residential investment. On another positive note, the board noted that the level of GDP in the euro area had finally exceeded its pre-GFC peak and that India was growing strongly.

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Outlook for Monetary Policy

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Today's RBA minutes did little to support the view that the RBA will cut rates again. The key to future rate cuts lies in inflation. If inflation moves lower and stays lower for longer than the RBA is currently expecting then a further cut or cuts would make sense. We have a rate cut pencilled in for August as we believe the May rate cut alone will not achieve its aim of lifting inflation in the required time frame.

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