Interest Rate Outlook

Tuesday, 3 October 2017

Bank of Melbourne

RBA Still Erring on the Side of Caution

- **The Reserve Bank (RBA) left the cash rate unchanged at 1.50% at its board meeting today, as widely expected.**
- **Given the lack of new developments over the past month, there were no major surprises in the accompanying statement.**
- **A key change however, was the RBA's more upbeat view on non-mining business investment, noting that "there have been more consistent signs that non-mining business investment is picking up". The RBA also highlighted that "a large pipeline of infrastructure investment" was "also supporting the outlook".**
- **The RBA remains of the view that economic growth would "gradually pick up" over the coming year.**
- **In regards to the labour market, the RBA somewhat downplayed the recent strength. The RBA recognised that employment had "continued to grow strongly over recent months" but that the unemployment rate was "expected to decline only gradually over the next couple of years", hinting that the RBA is still recognising that spare capacity remains in the labour market.**
- **The fact that wage growth will remain low for some time, the recent appreciation in the Australian dollar and the high rate of household indebtedness continued to be highlighted as concerns for the RBA.**
- **Today's statement suggests a Reserve Bank remaining content to leave rates unchanged for some time. While the RBA is becoming increasingly more positive on the domestic outlook, there are a range of factors that remain a concern or the RBA. We continue to expect the RBA to leave the cash rate on hold at 1.50% this year and into next year.**

The Reserve Bank (RBA) left the cash rate unchanged at 1.50% at its board meeting today, as widely expected.

Given the lack of new developments over the past month, there were no major surprises in the accompanying statement.

A key change was the RBA's more upbeat view on non-mining business investment, noting that "there have been more consistent signs that non-mining business investment is picking up" and that "a consolidation of this trend would be a welcome development". The RBA also highlighted that "a large pipeline of infrastructure investment" was "also supporting the outlook".

We were also able to obtain the RBA's response to the most recent data on economic growth and the labour market.

On the GDP release, the RBA noted that the 0.8% quarterly growth in the June quarter was consistent with the expectations that economic growth would “gradually pick up” over the coming year.

In regards to the labour market, the RBA somewhat downplayed the recent strength. It noted that employment had “continued to grow strongly over recent months” and that it had been “accompanied by a rise in labour force participation”. Nonetheless, the RBA added that the unemployment rate was “expected to decline only gradually over the next couple of years”, hinting that the RBA is still recognising the spare capacity that remains in the labour market.

Some of the other concerns facing the RBA were still apparent in today’s Statement.

The fact that wage growth was likely to remain low for some time, the recent appreciation in the Australian dollar and the high rate of household indebtedness continued to be highlighted as concerns by the RBA.

Indeed, the RBA notes that “growth in household debt has been outpacing the slow growth in household incomes for sometime”, implying that household debt was still increasing as a proportion of incomes.

Outlook and Implications

Today’s statement suggests a Reserve Bank remaining content to leave rates unchanged for some time. While the RBA is becoming increasingly more positive on the domestic outlook, particularly with regards to non-mining business investment, there are a range of factors that remain a concern or the RBA. Spare capacity in the labour market, low wage growth combined with high household debt levels remain at the top of mind. In addition, the RBA continues to desire a lower currency. We expect the RBA to remain on hold at 1.50% this year and into 2018.

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