Minutes of the July RBA Board Meeting

More Cautious Optimism

- **Those who were expecting a less dovish stance from the RBA were somewhat appeased today. Back on 4 July, the accompanying statement of the RBA's monthly board meeting disappointed markets which were looking for more hawkish commentary. However, today's minutes of the RBA's board meeting in July gave us some further insight into the discussion at the board meeting.**

- **Of focus was a discussion around the neutral cash rate, which the RBA estimates to be around 3.5%. This discussion suggests that the RBA is beginning to lay the groundwork for the normalisation of monetary policy. While this is not suggesting a rate hike is around the corner, it does imply that the RBA is edging further away from thinking about another cut to the cash rate in this cycle. The second point is that once the process of monetary policy normalisation is underway, the RBA views that the cash rate could lift up to 2 percentage points higher from the current level of 1.50%.**

- **The RBA was notably more upbeat regarding the domestic and international economies.**

- **There was extensive discussion on the labour market, which has been a key focus. The RBA recognised the improvement in recent months, but it acknowledged the degree of labour market slack remaining given the high underemployment rate and slow wage growth.**

- **The RBA was still cautious about the growth and inflation outlook, and that "developments in the labour and housing markets continued to warrant careful monitoring."**

- **There continues to be a mixed outlook for the domestic economy given a turning point in the residential construction cycle and weak medium to long-term fundamentals for consumer spending. There is still evidence of spare capacity in the economy which will continue to weigh on the wages and inflation outlook. While today's data signifies yet another step away from a potential rate cut, the RBA is still not ready to consider a rate hike anytime soon.**

Those who were expecting a less dovish stance from the RBA were somewhat appeased today. Back on 4 July, the accompanying statement of the RBA's monthly board meeting disappointed markets which were looking for more hawkish commentary.

However, today's minutes of the RBA's board meeting in July gave us some further insight into the discussion at the board meeting. Of focus was a discussion around the neutral cash rate, which the RBA estimates to be around 3.5%. This discussion suggests two key points – the first is that the RBA is beginning to lay the groundwork for the normalisation of monetary policy (ie. raising official interest rates). While this is not suggesting a rate hike is around the corner, it does imply that the

RBA is edging further away from thinking about another cut to the cash rate in this cycle. The second point is that once the process of monetary policy normalisation is underway, it could see the RBA cash rate up to 2 percentage points higher from the current level of 1.50%.

Commentary on the outlook was much more positive than in previous rhetoric. The RBA was notably more upbeat regarding the domestic and international economies.

It was pointed out that “the improvement in the world economy over the preceding months” was a “welcome development” and that economic growth in some economies had been “a little stronger than expected”. The RBA was positive on developments in China, the US, Europe and Japan.

On the domestic economy, the RBA is continuing to look through the weakness in GDP growth in the March quarter. The RBA also appeared to downplay a potentially weak outcome in the June quarter as well, given that disruptions to coal exports due to cyclone Debbie would affect growth the quarter.

Additionally, the RBA seemed mostly upbeat in various parts of the economy. This includes residential construction, which was expected to be at a “high level over the subsequent year or so”. Non-mining investment was weak in the quarter, but “had been gradually trending up for a number of years”. Fiscal policy was expected to be “more expansionary in 2017-18 than had previously been expected”. The RBA even notes a rise in non-residential building approvals.

There was extensive discussion on the labour market, which has been a key focus. The RBA recognised the improvement in recent months, including the strong growth in employment particularly in full-time work, the trend increase in hours worked, and the decline in the unemployment rate. Nonetheless, the RBA acknowledged the degree of labour market slack remaining given the high underemployment rate and slow wage growth.

That said, the RBA was still cautious about the growth and inflation outlook, and that “developments in the labour and housing markets continued to warrant careful monitoring”. Rate hikes do not seem to be on the agenda in the near-term.

Implications

The RBA is decidedly more upbeat regarding the outlook. Further, the discussion surrounding the neutral cash rate could be interpreted as prep work in the process of normalisation of monetary policy. However there remained some notes of concern in today’s commentary, and the RBA is treating the recent improvement in the domestic labour market with caution.

There continues to be a mixed outlook for the domestic economy given a turning point in the residential construction cycle and weak medium to long-term fundamentals for consumer spending. There is still evidence of spare capacity in the economy which will continue to weigh on the wages and inflation outlook. While today’s data signifies yet another step away from a potential rate cut, the RBA is still not ready to consider a rate hike anytime soon.

Janu Chan, Senior Economist
Ph: 02-8253-0898

Contact Listing

Chief Economist	Senior Economist	Senior Economist
Besa Deda	Josephine Horton	Janu Chan
dedab@bankofmelbourne.com.au	hortonj@bankofmelbourne.com.au	chanj@bankofmelbourne.com.au
(02) 8254 3251	(02) 8253 6696	(02) 8253 0898