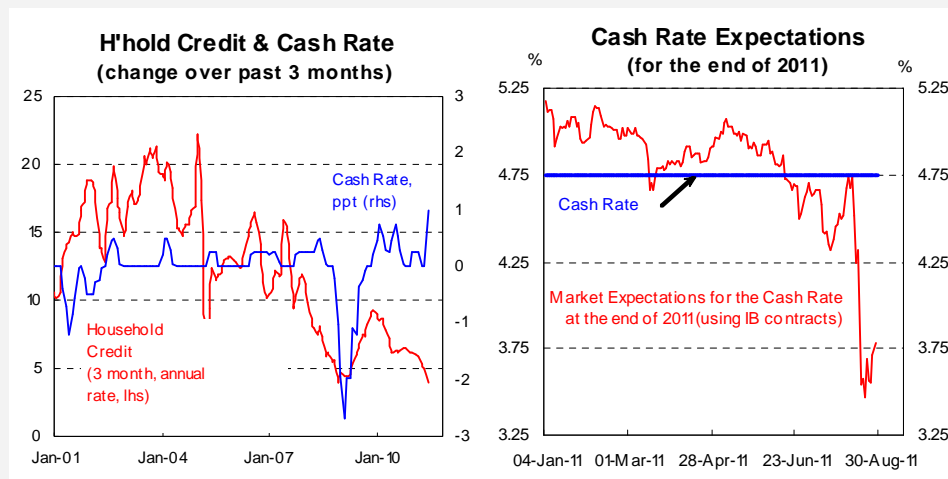


THE CASH RATE OUTLOOK

RBA Minutes – Dovish Undertones

Tuesday, 16 August 2011

- The minutes of the monetary Policy meeting in August largely echoed the more balanced tone in the accompanying statement. However, there were many dovish undertones over the outlook for growth.
- The RBA “considered whether the recent information warranted further policy tightening.” The RBA remains worried about inflation given forecasts pointed to inflation rising above the target range, but is also worried about the outlook for global growth.
- The references to downside risks to the economy and the commentary on the various weak areas domestically suggest a rate cut cannot be ruled out. However, the clear concerns about the inflation outlook are keeping the RBA at bay.
- On balance, we expect the RBA is likely to keep rates on hold for the remainder of this year. However, there are significant downside risks to growth and there is much uncertainty in regards to the debt issues abroad. Thus, there is a growing likelihood of an RBA rate cut, although not as much as what markets are pricing in.



The minutes of the monetary policy meeting in August largely echoed the more balanced tone in the accompanying statement. There remained the usual worries about the multi-speed economy. Further, the RBA “considered whether the recent information warranted further policy tightening.” However, there were many dovish undertones in regards to the outlook for growth.

The RBA remains concerned about the outlook for global growth. It again mentioned the pace of global growth had slowed and global growth was expected to be average, or a bit above, over the next year. However, it also highlighted that “downside risks had become more pronounced” in regards to the sovereign debt issues in Europe and the US.

The RBA also seemed more concerned of the downside risk the instability overseas posed on the domestic economy. Domestically, the main uncertainty for the RBA was the household sector. It talked about the weakness in retail spending and further slowing in housing credit. It highlighted the risk of international developments could have on household spending “as saving could increase further in an environment of uncertainty.”

On employment, the RBA was also less optimistic stating that “the unemployment rate was no

longer falling". In addition, it mentioned that while forward looking indicators pointed to moderate employment growth " staff's liaison with businesses indicated some caution in hiring plans."

Meanwhile, the RBA hinted that financial conditions were quite tight amid slowing credit growth. Indeed, it says that credit growth "was very subdued by historical standards." Credit growth, in particular for business credit, is probably weaker than what the RBA expected.

On the upside, growth in China had remained firm, with the exception of trade data. The terms of trade was now also expected to increase further in the September quarter and decline gradually afterwards.

The RBA remains worried about inflation given forecasts pointed to inflation rising above the target range. The Q2 underlying inflation outcome was also "higher than expected," and said that "there were grounds for concern for the medium term outlook for inflation, given the relatively limited spare capacity in the economy, the widespread increase in cost pressures ... and the relatively low rate of productivity."

Rates Outlook

The references to downside risks to the economy and the commentary on the various weak areas domestically might suggest a rate cut was on the cards. However, the clear concerns about the inflation outlook are keeping the RBA at bay. On balance, we expect the RBA is likely to keep rates on hold for the remainder of this year. However, there are significant downside risks to growth and there is much uncertainty in regards to the debt issues abroad. Thus, there is a growing likelihood of an RBA rate cut, although probably not as much as markets are pricing in (which is about 100bps of cuts by the end of the year).

Janu Chan, Economist
Ph: (02) 9320-5892

Contact Listing

Chief Economist	Besa Deda	dedab@stgeorge.com.au	(02) 9320 5854
Senior Economist	Josephine Heffernan	heffernanj@stgeorge.com.au	(02) 9320 5751
Economist	Janu Chan	chanj@stgeorge.com.au	(02) 9320 5892
State Manager SA	Mark Goldsmith	goldsmithm@banksa.com.au	(08) 8424 5597

The information contained in this report (“the Information”) is provided for, and is only to be used by, persons in Australia. The information may not comply with the laws of another jurisdiction. The Information is general in nature and does not take into account the particular investment objectives or financial situation of any potential reader. It does not constitute, and should not be relied on as, financial or investment advice or recommendations (expressed or implied) and is not an invitation to take up securities or other financial products or services. No decision should be made on the basis of the Information without first seeking expert financial advice. For persons with whom St.George has a contract to supply Information, the supply of the Information is made under that contract and BankSA’s agreed terms of supply apply. BankSA does not represent or guarantee that the Information is accurate or free from errors or omissions and BankSA disclaims any duty of care in relation to the Information and liability for any reliance on investment decisions made using the Information. The Information is subject to change. Terms, conditions and any fees apply to BankSA products and details are available. BankSA or its officers, agents or employees (including persons involved in preparation of the Information) may have financial interests in the markets discussed in the Information. BankSA owns copyright in the information unless otherwise indicated. The Information should not be reproduced, distributed, linked or transmitted without the written consent of BankSA.

Any unauthorised use or dissemination is prohibited.

Neither BankSA Bank - A Division of Westpac Banking Corporation ABN 33 007 457 141 AFSL 233714 ACL 233714, nor any of Westpac's subsidiaries or affiliates shall be liable for the message if altered, changed or falsified.