

Tuesday, 2 March 2021

Reserve Bank Board Meeting RBA Sticking to its Guns

- There was little fresh news out of the meeting today. The Bank reiterated that it does not expect it will lift the cash rate until 2024 at the earliest and left the parameters of the yield curve control and bond purchase programs unchanged.
- There has been speculation amongst investors over recent weeks that the Reserve Bank of Australia (RBA) could increase the cash rate sooner than 2024 but Governor Lowe hosed down any such prospects in his statement.
- The Governor's statement reaffirmed the Bank's commitment to the three-year yield target and quantitative easing program. The statement noted the RBA is prepared to make further adjustments to its purchases in response to market conditions.
- The market reaction was muted overall although suggests investors were after a stronger commitment from the RBA.
- The insertion of the sentence around the importance of "sound lending standards" indicates that housing is on the radar of regulators. It is possible that a review of lending standards could occur down the track.
- The RBA continues to stress that the recovery will be bumpy and uneven. And while prospects for a sustained recovery have improved relative to a few months ago, the outlook remains dependent on the evolution of COVID-19 and significant fiscal and monetary support.

There was little fresh news out of the meeting today. The Bank reiterated that it does not expect it will lift the cash rate until 2024 at the earliest and left the parameters of the yield curve control and bond purchase programs unchanged.

There has been speculation amongst investors over recent weeks that the RBA could increase the cash rate sooner than 2024 but Governor Lowe hosed down any such prospects in his statement. It reaffirmed the cash rate will not be increased until inflation is sustainably within the 2% to 3% per annum target range. The RBA still expects this won't happen until at least 2024.

In order for this to occur, wage growth will need to increase significantly. And this doesn't look to be happening any time soon. There needs to be a sustained and significant decline in the unemployment rate to generate wage growth. In addition, there are a number of structural headwinds to wage growth including globalisation and technological change, and limited bargaining power of organised labour.

The insertion of the sentence around the importance of "sound lending standards" indicates that housing is on the radar of regulators. If the housing market were to show signs of overheating, we

expect this could be handled with macroprudential policy, not by hiking interest rates. It is possible that a review of lending standards could occur down the track.

Markets were looking to the RBA for their thoughts on yield curve control and quantitative easing given the recent volatility in the bond market. The Governor's statement reinforced the Bank's commitment to the three-year yield target. It also noted that recent unscheduled bond purchases, under the bond purchase program, were a bring-forward of weekly purchases (not additional stimulus) in order to smooth the functioning of the market. The statement noted the RBA is prepared to make further adjustments to its purchases in response to market conditions.

The Bank reaffirmed that price pressures are expected to remain subdued. The statement flags that inflation is expected to rise temporarily due to the reversal of some COVID-related price cuts.

The market reaction was muted overall although suggests investors were after a stronger commitment from the RBA. The yield on 10-year Australian government bonds spiked 7 basis points. The 3-year yield also popped 2 basis points higher, touching 0.14%, before retracing. The RBA's efforts to keep borrowing costs low in the face of the economic recovery, and market expectations for an increase in inflation, will no doubt remain in focus going forward.

The RBA continues to stress that the recovery will be bumpy and uneven. And while prospects for a sustained recovery have improved relative to a few months ago, the outlook remains dependent on the evolution of COVID-19 and significant fiscal and monetary support.

Matthew Bunny, Economist

Ph: 02-8254-0023

Contact Listing

Chief Economist

Besa Deda
dedab@banksa.com.au
(02) 8254 3251

Senior Economist

Hans Kunnen
hans.kunnen@banksa.com.au
(02) 8254 1316

Economist

Matthew Bunny
matthew.bunny@banksa.com.au
(02) 8254 0023

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 BankSA 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 unauthorized use or dissemination is prohibited. Neither BankSA- 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.