

Tuesday, 18 July 2017

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 dedab@stgeorge.com.au (02) 8254 3251	Josephine Horton hortonj@stgeorge.com.au (02) 8253 6696	Janu Chan chanj@stgeorge.com.au (02) 8253 0898

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.