Economic Insights

CommSec

"Performing well": Rates locked at record lows

Reserve Bank Board meeting

- **The Reserve Bank has left the cash rate at a record low of 1.50 per cent for the 28th straight month (26th meeting). The last rate change was a quarter percent rate cut on August 2, 2016.**

What changed since the last meeting?

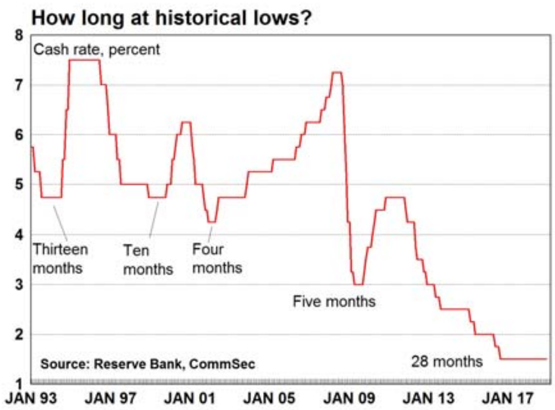
- The US and China have declared a truce in their tariff war.
- The wage price index rose 2.3 per cent over the past year – the fastest growth in 3½ years.
- The Australian jobless rate remains at a 6-year low at 5.0 per cent.
- The Australian dollar has lifted to the US73-74 cent range.
- There has been the biggest upgrade to business investment plans in 19 years.
- Annual credit growth stands at 4.6 per cent – just above the slowest rate recorded in 4½ years.
- The rolling annual budget deficit has fallen to $2.3 billion or less than 0.2 per cent of GDP.
- Petrol prices have fallen 26 cents a litre over the past five weeks.
- OPEC oil ministers prepare to meet on December 6 and discuss output cuts.
- National home prices fell by 0.7 per cent in September to stand 4.1 per cent lower on the year.
- Construction work done is at record highs across three states.
- Company profits stand at record highs, up 13.2 per cent in the year to September.
- Building approvals fell 1.5 per cent in October to be down 13.4 per cent on the year.

The assessment

- The Reserve Bank hasn't made major changes to its commentary. But the Bank has indicated that the US-China tariff war has led to some slowing of global trade. On the Australian economy, there have been no major changes in commentary: it is *"performing well".* Clearly, from the Reserve Bank viewpoint, the fall in home prices is almost wholly a Sydney-Melbourne phenomenon. But curiously, the RBA notes *"some lenders having a reduced appetite to lend."* The lift in wage growth is seen as a *"welcome development".* The RBA has presided over an economy with strong growth, low inflation, record low interest rates and near-full employment. Remarkable.

Perspectives on interest rates

- The Reserve Bank has left the cash rate at 1.50 per cent. The previous move was a rate cut in August 2016 (25 basis points). There have now been 12 rate cuts since November 2011, with the Reserve Bank cutting rates from 4.75 per cent to 1.50 per cent.
- The Reserve Bank had previously lifted rates seven times from October 2009 to November 2010 – a total of 1.75 percentage points, from 3.00 per cent to 4.75 per cent.



What are the implications of today's decision?

- The job market remains the area to watch. If rates were to rise in the next year to would be because the tight job market was pushing up wages and prices. The Reserve Bank will always act on rates pre-emptively.

Craig James, Chief Economist
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Comparing the two most recent statements

- The statement from the November 2018 meeting is on the left; the statement from today’s December 2018 meeting is on the right. Emphasis has been added to highlight key points in the wording in the statements.

Media Release

No: 2018-27
Date: 6 November 2018

Statement by Philip Lowe, Governor: Monetary Policy Decision

At its meeting today, the Board decided to leave the cash rate unchanged at 1.50 per cent.

The global economic expansion is continuing. A number of advanced economies are growing at an above-trend rate and unemployment rates are low. Growth in China has slowed a little, with the authorities easing policy while continuing to pay close attention to the risks in the financial sector. Globally, inflation remains low, although it has increased due to both higher oil prices and some lift in wages growth. A further pick-up in inflation is expected given the tight labour markets and, in the United States, the sizeable fiscal stimulus. One ongoing uncertainty regarding the global outlook stems from the direction of international trade policy in the United States.

Financial conditions in the advanced economies remain expansionary but have tightened somewhat recently. Equity prices have declined and yields on government bonds in some economies have increased, although they remain low. There has also been a broad-based appreciation of the US dollar this year. In Australia, money-market interest rates have declined recently, after increasing earlier in the year. Standard variable mortgage rates are a little higher than a few months ago and the rates charged to new borrowers for housing are generally lower than for outstanding loans.

The Australian economy is performing well. Over the past year, GDP increased by 3.4 per cent and the unemployment rate declined to 5 per cent, the lowest in six years. The forecasts for economic growth in 2018 and 2019 have been revised up a little. The central scenario is for GDP growth to average around 3½ per cent over these two years, before slowing in 2020 due to slower growth in exports of resources. Business conditions are positive and non-mining business investment is expected to increase. Higher levels of public infrastructure investment are also supporting the economy, as is growth in resource exports. One continuing source of uncertainty is the outlook for household consumption. Growth in household income remains low, debt levels are high and some asset prices have declined. The drought has led to difficult conditions in parts of the farm sector.

Australia's terms of trade have increased over the past couple of years and have been stronger than earlier expected. This has helped boost national income. While the terms of trade are expected to decline over time, they are likely to stay at a relatively high level. The Australian dollar remains within the range that it has been in over the past two years on a trade-weighted basis, although it is currently in the lower part of that range.

The outlook for the labour market remains positive. With the economy growing above trend, a further reduction in the unemployment rate is expected to around 4¾ per cent in 2020. The vacancy rate is high and there are reports of skills shortages in some areas. Wages growth remains low, although it has picked up a little. The improvement in the economy should see some further lift in wages growth over time, although this is still expected to be a gradual process.

Inflation remains low and stable. Over the past year, CPI inflation was 1.9 per cent and, in underlying terms, inflation was 1¾ per cent. These outcomes were in line with the Bank's expectations and were influenced by declines in some administered prices due to changes in government policies. Inflation is expected to pick up over the next couple of years, with the pick-up likely to be gradual. The central scenario is for inflation to be 2¼ per cent in 2019 and a bit higher in the following year.

Conditions in the Sydney and Melbourne housing markets have continued to ease and nationwide measures of rent inflation remain low. Growth in credit extended to owner-occupiers has eased but remains robust, while demand by investors has slowed noticeably as the dynamics of the housing market have changed. Credit conditions are tighter than they have been for some time, although mortgage rates remain low and there is strong competition for borrowers of high credit quality.

The low level of interest rates is continuing to support the Australian economy. Further progress in reducing unemployment and having inflation return to target is expected, although this progress is likely to be gradual. Taking account of the available information, the Board judged that holding the stance of monetary policy unchanged at this meeting would be consistent with sustainable growth in the economy and achieving the inflation target over time.

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Media Release

No: 2018-31
Date: 4 December 2018

Statement by Philip Lowe, Governor: Monetary Policy Decision

At its meeting today, the Board decided to leave the cash rate unchanged at 1.50 per cent.

The global economic expansion is continuing and unemployment rates in most advanced economies are low. **There are, however, some signs of a slowdown in global trade, partly stemming from ongoing trade tensions.** Growth in China has slowed a little, with the authorities easing policy while continuing to pay close attention to the risks in the financial sector. Globally, inflation remains low, although it has increased due to the earlier lift in oil prices and faster wages growth. A further pick-up in core inflation is expected given the tight labour markets and, in the United States, the sizeable fiscal stimulus.

Financial conditions in the advanced economies remain expansionary but have tightened somewhat. Equity prices have declined and credit spreads have moved a little higher. There has also been a broad-based appreciation of the US dollar this year. In Australia, money-market interest rates have declined, after increasing earlier in the year. Standard variable mortgage rates are a little higher than a few months ago and the rates charged to new borrowers for housing are generally lower than for outstanding loans.

The Australian economy is performing well. The central scenario is for GDP growth to average around 3½ per cent over this year and next, before slowing in 2020 due to slower growth in exports of resources. Business conditions are positive and non-mining business investment is expected to increase. Higher levels of public infrastructure investment are also supporting the economy, as is growth in resource exports. One continuing source of uncertainty is the outlook for household consumption. Growth in household income remains low, debt levels are high and some asset prices have declined. The drought has led to difficult conditions in parts of the farm sector.

Australia's terms of trade have increased over the past couple of years and have been stronger than earlier expected. This has helped boost national income. Most commodity prices have, however, declined recently, with **oil prices falling significantly.** The Australian dollar remains within the range that it has been in over the past two years on a trade-weighted basis.

The outlook for the labour market remains positive. The unemployment rate is 5 per cent, the lowest in six years. With the economy expected to continue to grow above trend, a further reduction in the unemployment rate is likely. The vacancy rate is high and there are reports of skills shortages in some areas. **The stronger labour market has led to some pick-up in wages growth, which is a welcome development.** The improvement in the economy should see some further lift in wages growth over time, although this is still expected to be a gradual process.

Inflation remains low and stable. Over the past year, CPI inflation was 1.9 per cent and in underlying terms inflation was 1¾ per cent. Inflation is expected to pick up over the next couple of years, with the pick-up likely to be gradual. The central scenario is for inflation to be 2¼ per cent in 2019 and a bit higher in the following year.

Conditions in the Sydney and Melbourne housing markets have continued to ease and nationwide measures of rent inflation remain low. Credit conditions for some borrowers are tighter than they have been for some time, **with some lenders having a reduced appetite to lend.** The demand for credit by investors in the housing market has slowed noticeably as the dynamics of the housing market have changed. **Growth in credit extended to owner-occupiers has eased to an annualised pace of 5–6 per cent**. Mortgage rates remain low, with competition strongest for borrowers of high credit quality.

The low level of interest rates is continuing to support the Australian economy. Further progress in reducing unemployment and having inflation return to target is expected, although this progress is likely to be gradual. Taking account of the available information, the Board judged that holding the stance of monetary policy unchanged at this meeting would be consistent with sustainable growth in the economy and achieving the inflation target over time.