PRO-POL SHADOW RBA BOARD – COMMENTS

MARCH 2012

From March 2012, each Shadow Board member was invited (but not obliged) to provide a personal comment on monetary conditions. Neither the comments nor the probabilities constitute financial advice. The views of the Shadow Board members are not those of CAMA. Any individuals utilizing these comments, or the probabilities, do so at their own risk.

PAUL BLOXHAM

No comment.

MARK CROSBY

No comment.

MARDI DUNGEY

The economy continues to be threatened by the international situation, leading to risk of increased funding costs. Inflationary pressures do not appear to be excessive despite the fall in the overall unemployment rate. Regional differences in economic performance continue to be an issue.

SAUL ESLAKE

No comment.

BOB GREGORY

No comment.

WARWICK MCKIBBIN

The recent wage data suggests that it is likely the RBA will have to consider raising rates in the next 6 months rather than cutting rates again. There continues to be a real chance that a shock from Europe will require a large cut in rates but only when this occurs. The probability of this happening in 2012 is close to 100% but only a slight probability before the next RBA meeting.

JAMES MORLEY

Conditions Still Balanced, Less Risk

The outlook for domestic and international economic conditions remains fairly balanced, with less imminent risk of a large change in direction of the Australian economy than a month ago. Therefore, my recommendation puts the most weight on holding rates steady, but has some weights on incremental raising or lowering. The higher weight on raising continues to reflect the need to return the policy rate its neutral level over the medium term.

Please see this and previous comments at:

http://research.economics.unsw.edu.au/jmorley/Main/Monetary_Policy_Statements.html

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JEFF SHEEN

The Australian economy grew at 2.5% (sa) in 3Q 2011 approaching its normal long run rate of about 3%, with aggregate non-dwelling investment contributing significantly and household consumption growth now nearly back to normal. Productivity growth of GDP per hour is back to being positive and similar to real wage growth. The labour market is showing signs of improvement with employment and participation up and unemployment down to 5.1% in January, which is probably close to the natural rate. All of this suggests the economy is getting close to its long run trend, which is supported by current (trimmed) inflation being inside the RBA's target range.

Therefore, with no downside risks, the cash rate ought to begin soon to return to its medium-run neutral value (between 5% and 6%). With the US economy showing slow but good signs of improvement, the main downside risks now come from:

1. a serious failure of sovereign debt negotiations in Europe, which would affect Australia by further and significantly raising the wholesale funding costs of our banks, as well as leading to the negative wealth effects from a possible collapse in stock markets;

2. a decline in our terms of trade, should China's restrictive policies lead to much lower growth there than at present (though sectors that don't benefit from commodity exports will get relief);

3. a significant rise in energy prices in the event of an escalation of conflict in the Middle East.

The RBA did act late in 2011 to preempt these risks. Since I consider these risks in aggregate to have eased a little, the RBA should not be cutting the cash rate now, leaving plenty of space for a future cut should the worst materialize.

Therefore my recommendation is for most weight on no change in the cash rate in March 2012, with a greater probability weight on a 25 basis point increase than a decrease. Over the next 6-12 months, should the optimistic scenario be realized, I will be recommending a gradual return of the cash rate to its medium-run value.

MARK THIRLWELL

Current cash rate looks broadly appropriate given prevailing domestic conditions, but the global economy remains a source of significant downside risk.