CAMA RBA SHADOW BOARD – COMMENTS

JULY 2014

Each CAMA RBA Shadow Board member is 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

Australia's GDP growth was strong in the first quarter, although more timely indicators suggest some loss of momentum recently. New building approvals have fallen while growth in retail sales and housing prices has slowed. Consumer sentiment has remained weak following cuts announced in the Federal budget. Local incomes are also being squeezed by the combination of falling commodity prices and a rising AUD in recent months. With inflation well contained and activity and income growth appearing to have softened in the past couple of months, there is little evidence to suggest that local interest rates will need to rise anytime soon. At the same time, there are still signs that the domestic economy is being supported by low interest rates. Business surveys continue to suggest higher levels of confidence than last year and the labour market is showing signs of gradual improvement. I recommend that the cash rate is left unchanged this month.

MARDI DUNGEY

No comment.

SAUL ESLAKE

No comment.

BOB GREGORY

No radical change either up or down in the economic outcomes just a slow movement. Have been worried about house price increases spreading but this prospect seems to have eased.

GUAY LIM

No comment.

WARWICK MCKIBBIN

In my view current Australian interest rates are too low. The problem is that monetary policy is aimed at stimulating non-mining parts of the economy particularly housing construction. Monetary policy should focus on the growth rate of nominal GDP as a benchmark to guide interest rates. Given the current growth rate of nominal GDP of around 4-5 percent per year, a neutral monetary policy would be a risk adjusted interest rate of at least 4.5 per cent. Allowing for risk adjustment, this suggests the Australian policy rate should be closer to 3 per cent and possibly even 3.5 per cent. The current stance of monetary policy is at risk of increasing demand for assets, which will drive up the price of those assets. Unless there is a supply response, that will lead to pure capital gain and ultimately a bubble which will be costly to clean up. Australia faces a shift in global portfolio preferences towards Australian assets as well ultra-loose monetary policy in major countries that experiences a financial crisis causing a search for robust currencies. This means the usual channel of loose monetary policy through weakening the $A is no longer viable even if it was the goal. The focus on generating economic growth should be on the supply side of the economy through cost reductions (productivity improvements) improving competitiveness. There is not much a central bank can do about this except intellectual leadership in the debate.

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JAMES MORLEY

Inflation expectations remain well anchored, providing scope for the RBA to focus on real and financial conditions.
In light of fragile consumer confidence and fiscal policy uncertainty, the RBA should hold steady until there are clearer indications of improvements in the labour market or there are broad and abnormal increases in credit growth.

JEFFREY SHEEN

Australian output growth is slightly above normal at 3.5%, mostly driven by export volumes in resources. The labour market is showing improvement, with unemployment ticking down to 5.8%, wages growth a modest 2.5%, and labour productivity (in mining and non-mining) back to the pre-crisis average of about 2%. The structural divide between the mining industry and the rest is beginning to dissipate. The real export-weighted index is depreciating a little, largely because relative unit labour costs are falling. Inflation remains benign. The tough fiscal budget proposed by the government is likely to be softened by the Senate, which will reduce its negative short run impact. Confidence as exhibited in asset market prices is strong. Changes in the global economy, as they apply to Australia, are mixed. China's growth rate is slowing marginally, but its demand for our exports remains substantial. Oil prices are rising due to the escalation of hostilities in Iraq, and if these worsen, there could be negative implications for Australian economic activity. This all suggests that, at the margin, the probability of an increase in the cash rate is now higher and the time to wait before that happens is shrinking.