

Reserve Bank Board Meeting Outcome – August 2010

ECONOMIC ALERT

3 August 2010

KEY POINTS

The RBA Board left the official cash rate at 4.50 per cent at its August 2010 meeting today. The key reasons behind the decision, as outlined in the RBA's related media release, were as follows:

- The global economy has grown at faster than trend over recent months, but the expansion remains uneven. The major advanced economies have seen only modest growth overall, while growth in Asia and Latin America has been very strong. Indicators suggest that growth in China is moderating to a more sustainable pace. In Europe, though output has been improving recently in some major economies, next year's outlook is more uncertain given the budgetary constraints governments face and the pressure on euro area banks. US growth has strengthened in the first half of 2010 though the labour market remains soft and the recovery may be 'lacklustre' in the second half of the year.
- Financial market concerns about European sovereign debt and banks have eased recently but uncertainty around the outlook for global growth remains.
- Global commodity prices have eased from their recent peaks but Australia's key commodity prices remain at very high levels. The terms of trade are approaching their peak of two years ago.
- The high level of the terms of trade is expected to add to incomes and demand, and output growth in Australia over 2010-11 is likely to be about trend, despite diminishing support from past policy stimulus. Consumer spending is rising modestly currently, reflecting households' caution, but most indicators suggest business investment will increase over the coming year.
- Business credit appears to have stabilised, though credit conditions for some sectors remain difficult. Housing credit continues to expand at a solid pace.
- The labour market continues to firm gradually and wages growth has picked up a little. Recent inflation data were in line with the RBA's expectations and underlying inflation remains expected to be in the upper half of the target zone over the next year.
- Current monetary policy is resulting in borrowing rates at around average levels over the past decade. **"With growth likely to be close to trend, inflation close to target and the global outlook remaining somewhat uncertain the Board judged this setting of monetary policy as appropriate."**

Policy implications

- Today's decision by the RBA Board continues its recent position of ongoing assessment of data as it develops. The outcome for the June quarter consumer price index was consistent with Bank forecasts and this, combined with ongoing uncertainty on the international outlook and soft consumer demand is likely to stay the Board's hand in lifting rates further in the immediate future.