CAMA RBA SHADOW BOARD – COMMENTS

AUGUST 2021

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.

SALLY AULD

No comment.

RENÉE FRY-MCKIBBIN

No comment.

SARAH HUNTER

The deterioration of the COVID situation in Sydney (and spillovers to other regions and states) has materially impacted the near term outlook for the economy. GDP will almost-certainly contract in the September quarter, and given the transmissibility of the delta variant (and the resultant risk of further outbreaks from quarantine) it is likely that significant restrictions will have to remain in place in a number of states until the vaccine rollout is significantly more progressed.

Given the heightened uncertainty, it is appropriate for the RBA to moderate the pace of any monetary tightening it was previously considering. While this implies no change to the cash rate in the near term, the Board should look to delay any further winding back of the QE program.

Over the medium/long term, the encouraging data from the UK, the US and other countries with respect to vaccine efficacy (that is, the breaking of the link between cases of COVID and hospitalisations and adverse outcomes) suggests that once the vaccine rollout has progressed it will be possible to sustainably relax restrictions and reach a ‘new normal’. Assuming fiscal policy settings remain accommodative (including the roll out of disaster payments and grants for businesses), the strength of the recovery in H1 2021 suggests that the economy has the capacity to bounce back strongly, as such my assessment on the outlook for 2023 and beyond is broadly unchanged, although the timing of the recovery is more uncertain given it is now much more contingent on the success of the vaccination program.

MARIANO KULISH

No comment.

GUAY LIM

No comment.

WARWICK MCKIBBIN

The slow speed of vaccine rollout in Australia and the emergence of the delta strain of Covid-19 combined with a worsening global situation means interest rates are likely to remain lower for longer. There will likely be continuing emergence of new strains of the virus in developing countries where Covid-19 remains out of control. The response of worsening health outcomes will dampen economic activity in Australia independently of whether the State government implement lockdowns. The loss of consumer and business confidence implies a need for fiscal and monetary support in Australia for a much more extended period than I had hoped earlier in the year. I would not be surprised to see a W recovery rather than a continuation of the V recovery to date. There is nothing that the RBA can do to offset this outcome apart from maintaining financial stability. It is up to fiscal policy and income support policy for businesses and households to prevent a W-shaped recovery.

JAMES MORLEY

Q2 inflation was just released and the headline number was a 3.8% year-on-year rate. While this is above the RBA's target range of 2-3% and some temporarily higher inflation is welcome to bring the price level back to where it was expected to be prior to the crisis, it is clear that much of this headline number is a temporary spike due to a "base effect" (the CPI was particularly low in 2020Q2 due to the Covid crisis, including measurement issues for prices of goods and services for which exchange was disrupted by the crisis). To see this base effect, note that the CPI suggests prices are only 3.5% higher than they were two years ago in 2019Q2, which corresponds to an annualised inflation rate of only 1.7% over the last two years.

The key for the RBA is that measures of inflation expectations have increased, including a return back up to the (low end of) its 2-3% target range for the break-even 10-year inflation rate of 2.1% in Q1 and sustained at 2.0% in Q2.

Also, the decline in the unemployment rate to 4.9% in June is particularly welcome news, but the economic fallout from the Delta variant is likely to be negative real GDP growth in Q3 and an increase in the unemployment rate. So the RBA's forward guidance to keep the policy rate at 0.1% until at least 2024 remains an appropriate setting.

JEFFREY SHEEN

No comment.