



AUSTRALIAN CHAMBER OF
COMMERCE AND INDUSTRY

MEDIA RELEASE

Tuesday, 3 November 2009

Uncertain Recovery Warrants Caution on Rates

Statement by Mr Greg Evans, Director of Economics and Industry Policy

The Reserve Bank's decision to increase the cash rate a further 25 basis points to 3.5 per cent demonstrates increased confidence that the economy is recovering and will return close to trend growth in 2010.

Australian business certainly hope this is the case and would welcome a return to more robust trading conditions in the year ahead. Today's *Commonwealth Bank-ACCI Business Expectations Survey* highlights the pressures on profitability currently faced by business while there is an expectation this will improve.

However, the impact of fiscal policy in the June quarter gives rise to an unusual degree of uncertainty when gauging the underlying performance of the economy.

The second round of cash payments under the *Nation Building and Jobs Plan* appears to have generated a sharp rise in consumer spending in the June quarter. Similarly, the operation of the temporary investment allowance had a significant impact on business investment in that quarter.

The peak impact of both these stimulus measures has now largely passed and there is a real risk that the economy faces renewed challenges in the second half of 2009. Ultimately, determining the underlying health of the economy post-stimulus peak will be a lot easier once the third quarter GDP figures are released in mid-December.

At this stage in the cycle, economic recovery is still more forecast than real. In that environment, there is a good case for the Reserve Bank exercising caution in order to avoid tightening monetary policy too early and by too much. This is especially the case given considerable international uncertainty.

Interest rate increases can have large impacts on business and consumer confidence. Back to back rate hikes in October and November should be sufficient to move monetary policy away from an 'emergency setting' and the prospect of a further increase in December would carry the potential to severely dent consumer sentiment in the lead up to the crucial Christmas trading period.

ACCI believes that continued uncertainty about the economic outlook combined with difficult trading conditions mean there is a good case for deferring any further rise in interest rates until the prospects for recovery are clearer.

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MR 143/09

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