

Pre-Christmas rate cut to stir shoppers

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Official interest rates are tipped to be slashed before Christmas as the worst global financial crisis in decades stirs fears about a possible recession in Australia next year.

All 18 economists surveyed by AAP expect the Reserve Bank of Australia to cut interest rates next Tuesday.

Eleven expect the cash rate to be slashed by a 75 basis points, following the RBA's December 2 monthly board meeting. Five economists tip a 100-basis point reduction.

Investors, though, are predicting an even bigger cut. There's an 83% chance the RBA will lops its key cash rate by 1.25 percentage points to 4% when its board meets, according to Credit Suisse today.

If the majority of economists are right, however, the cash rate will drop from 5.25%, to 4.5% for the first time since June 2002, after a 75 basis points cut in November.

Repayments on an average \$250,000 home loan would fall by 7% to \$1,662 a month, from \$1,790, if lenders reduced their standard variable mortgage rates by 75 basis points in December, in line with an RBA move of that size.

Rates have not been below this level since the RBA began publishing its overnight cash rate target in 1990.

TD Securities senior strategist Joshua Williamson said the RBA would have to slash rates by 1 percentage point to minimise the risk of Australia sinking into recession.

"The worsening in global conditions and the fact...Australia is more likely to enter a recession means monetary policy needs to be taken to an accommodating level very quickly," he said.

AMP Capital Investors chief economist Shane Oliver said the RBA would cut rates by 75 basis points, and keep cutting until the cash rate hit 3% by mid-2009, a level last seen in March 1960.

"The economic threat to Australian growth from the global slump is the biggest seen in the post-war era," Dr Oliver said.

"We have a situation in the advanced world where all three major economies - Europe, Japan and the US - will be in recession next year."

Consumers

Citigroup managing director of economics Stephen Halmarick said the RBA would lower rates by one percentage point in December to restore consumer confidence, amid a slump in global share markets.

"Their biggest concern is falling confidence will feed through to consumers bunkering down and not spending, so they need to offset that through lower rates," he said.

More interest rate cuts are expected in the March and June quarters, with even the most conservative forecasters expecting a 4% cash rate by the middle of next year, which would take rates to the lowest level since October 1972.

Three economists see the cash rate hitting 3%, or lower, in the June quarter.

However, ICAP senior economist Adam Carr said the RBA was more likely to cut rates by a smaller 50 basis points in December, as it anticipated a recovery in consumer spending early next year.

"Early next year, consumers will borrow again and home affordability will never be better," Mr Carr said, adding rates would fall to 4.5% by mid-year before being raised again in late 2009.

ANZ economist Riki Polygenis said upbeat Australian business investment plans for 2008/09 made a 75 basis point rate cut more likely.

"Despite the highly uncertain environment, corporate Australia is still planning to spend," she said, referring to figures in the Australian Bureau of Statistics' capital expenditure data for the September quarter released this week.

An economist with financial markets research group 4CAST, Mick Turner, said an upcoming "nasty" decline in Australia's terms of trade, the ratio of export to import prices, would make the RBA slash rates by 100 basis points in December, and keep cutting until the cash rate hit a record low of 2.5% by the end of June 2009.

AAP