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Reserve Bank has room to cut rates again - IMF

By Colin Brinsden, Economics Correspondent | May 06, 2009

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FINANCIAL conditions in Australia have room for improvement and the Reserve Bank (RBA) has "considerable" room to cut interest rates again, the International Monetary Fund (IMF) says.

The RBA left its cash rate unchanged at a 49-year low of 3.0 per cent yesterday after its monthly board meeting, saying "monetary policy has been eased significantly".

It has cut rates by 425 basis points since September, but they remain by far the highest among the world's advanced economies.

Outlining its reasoning for the rate decision, RBA governor Glenn Stevens said there were "signs of stabilisation" in the global economy and a pick-up in activity in China.

But the IMF warns the global crisis has hit Australia's Asian neighbours hard, and it may take some time before the region's economies recover.

In its latest Regional Economic Outlook for Asia and the Pacific released today in Singapore, the IMF says "forceful" monetary and fiscal policies will need to be sustained through 2010. It also warns that Asia will need to lift domestic demand rather than depend on export growth as consumption in advanced countries may remain weak for years to come.

"The spillovers from the global crisis have impacted Asia with unexpected speed and force," the IMF said.

"The downswing has been even larger than in other regions, and sharper than at the epicentre of the global crisis."

As in its global economic outlook issued last month, it expects Australian economic growth to contract by 1.4 per cent on average during 2009, before returning to modest positive growth of 0.6 per cent in 2010.

It expects the recovery will start towards the end of the year, due to its "strong policy response, healthy financial sectors, and exchange rate depreciation".

It says although credit growth is slowing in Australia, financial conditions have "loosened markedly" because of the sharp cut in official interest rates since September 2008 and lending rates have come down faster than expected.

"The positive contribution of financial conditions to growth could be about 0.25 percentage points," it said.

"Australia's financial conditions have further scope for improvement going forward given the considerable monetary policy space."

On the region more widely, the IMF says external shocks and stresses will make it difficult for the region to recover. "As long as exports remain depressed, private investment will remain low," it said.

Consumption will be hampered by growing unemployment as firms retrench workers in order to restore profitability.

"So, a sustained recovery will need to await an improvement in the global economy, which the IMF does

not expect before the middle of 2010."

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