

Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Budget Estimates – 2–4 June 2009

Question: bet 143

Topic: Printing money/Risk for inflation

Hansard Page: Written

Senator BUSHBY asked:

1. To what purposes is the practice of printing extra money and putting it into circulation generally used by sovereign governments as an economic tool?
2. What circumstances would lead to a sovereign government undertaking this practice?
3. What are the potential benefits of this practice – depending on the economic circumstances being faced in a nation's economy at the time?
4. What are the potential negative consequences?
5. Are you aware of any developed nations using printing money as a tool at present or since the global economic downturn started?
6. Which nations? To what extent are they employing this practice?
7. Do you consider there are any inflationary risks arising out of the employment of this tool in these nations?
8. Has Australia increased the amount of money in circulation in our economy by printing and releasing into the economy more than it would otherwise have done in the past 12 months?
9. What risk is there to Australia's economy from other nations printing extra money? If there was an inflationary effect in the US for example, could this flow through to Australia?

Answer:

These questions relate to the conduct of monetary policy.

The *Statement on the Conduct of Monetary Policy* states that: 'The Government recognises the independence of the Bank and its responsibility for monetary policy matters and intends to respect the Bank's independence as provided by statute.'

The *Statement* also notes that 'both the Reserve Bank and the Government agree on the objective of keeping consumer price inflation between 2 and 3 per cent, on average, over the cycle.'

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To the extent that international developments are relevant for the inflation outlook in Australia then they would be taken into account by the RBA in forming its view on the appropriate monetary policy settings.

The principal policy tool the RBA employs to conduct monetary policy is to set the official cash rate.

Central banks of many other advanced economies generally set monetary policy in a similar way to the RBA, in that they target a specific interest rate. However, as the target rate approaches zero, other approaches – broadly under the umbrella of quantitative easing – have been employed.

The potential benefit of undertaking quantitative easing is that it allows further support to be provided to aggregate demand even when the central bank's target rate approaches zero.

As the level of the official cash rate in Australia remains well above zero the RBA has not needed to employ quantitative easing measures.

M3 and Broad Money are measures of money in circulation in the economy. The monthly movements in these measures of the money supply are set out in the table below. For both measures, the monthly average increases in 2008-09 (up to May 2009) have been slightly lower than in the previous two financial years.

Monthly Changes in the Money Supply - M3 and Broad Money								
2006/2007	M3	Broad Money	2007/2008	M3	Broad Money	2008/2009	M3	Broad Money
Jul	0.8	0.5	Jul	1.3	0.9	Jul	2.3	1.7
Aug	1.1	1.1	Aug	2.1	2.1	Aug	1.2	0.7
Sep	0.7	1.2	Sep	1.4	0.1	Sep	1.3	1.2
Oct	1.4	0.9	Oct	3.0	2.8	Oct	1.1	0.9
Nov	0.6	0.7	Nov	2.6	1.9	Nov	1.4	1.0
Dec	1.1	0.8	Dec	0.9	1.0	Dec	0.2	-0.2
Jan	1.0	1.1	Jan	1.3	1.1	Jan	1.3	1.8
Feb	1.7	1.2	Feb	0.6	0.6	Feb	1.4	1.2
Mar	1.7	1.2	Mar	1.4	1.0	Mar	0.3	0.9
Apr	1.3	1.1	Apr	0.7	0.5	Apr	1.1	0.7
May	1.2	1.1	May	0.7	0.9	May	1.2	0.8
Jun	2.4	2.4	Jun	0.8	0.6			
Average	1.3	1.1	Average	1.4	1.1	Average	1.2	1.0

Source: Reserve Bank of Australia

Note: All series are seasonally adjusted. Growth rates are adjusted for series breaks.

Since the start of the global economic downturn central banks in some economies - for example the US, UK, Japan and European Monetary Union - have undertaken different forms of quantitative easing. However, the International Monetary Fund in the July 2009 *World Economic Outlook* has projected consumer prices for the Advanced economies to rise by 0.1 and 0.9 per cent for 2009 and 2010.

These issues were also discussed in detail in a May 2009 speech on 'Global monetary developments' by RBA Deputy Governor Ric Battellino.