SOME REFLECTIONS ON INFLATION, ECONOMIC GROWTH, AND ON MONETARY AND FISCAL POLICY

PRESENTATION TO THE ACT BRANCH
OF THE ECONOMIC SOCIETY OF AUSTRALIA

PARLIAMENT HOUSE, CANBERRA
11TH AUGUST 2022

SAUL ESLAKE

CORINNA ECONOMIC ADVISORY
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Economist

'Welcome to my website ...
I'm an independent economist, speaker, company director and Vice-Chancellor's Fellow at the University of Tasmania'

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Welcome to my website. Here you'll find a bit about me and my work as an economist. My most recent articles, talks and presentations can be found here, while there is a more complete archive, organized by topics, here. There's also a guide to upcoming events and appearances. Other links below will take you to things that other people are saying, either about me or about topics in which I also have an interest.

Some of the material on this site is free – especially if it's also been published elsewhere. However some of it, especially the more contemporary material, is only available to subscribers. If you'd like to become a subscriber, please do so here. I also offer professional services (writing, speaking, advisory etc.) through my own consultancy business, Corinna Economic Advisory.

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THE AUSTRALIAN ECONOMY THIS WEEK

What's new?

THE AUSTRALIAN ECONOMY THIS WEEK – 5TH AUGUST 2022

- As expected, the Reserve Bank rais
cumulative increase since the first i
second half of 1994, when the RBA
- The RBA now expects the annual 'h
December quarter 2023 and 3% by
also lowered its forecasts for econo
- The upward revisions to the RBA's ir
RBA's cash rate – although markets
- The volume of retail sales rose 1.4%
spend large amounts on a broad ra
the end of June) two increases in in
and interest rates
- Residential property prices across A
having fallen by 5.6% and 3.6% ove
- Housing finance commitments fell 4
down 6.4% and 7.8% from their resp
- Residential building approvals fell 0
by historical standards (slides 41-42
- Australia's surplus on international t
largely due to a (likely one-off) spu
much to increases in the value of c
- The numbers of new and active Co
health officials to suggest that Austr
- Next week's calendar is fairly light
Melbourne Institute consumer confi

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THE WORLD ECONOMY THIS WEEK

What's new?

THE WORLD ECONOMY THIS WEEK – 8TH AUGUST 2022

- US non-farm payrolls increased by a larger-than-expected 528K (0.3%) in July, while the unemployment rate fell 0.1 pc pt to 3.5%, matching the pre-pandemic lows in January-February 2020, which were in turn the lowest since 1969 (slide 48): note, however, that (as it has done since February) the household survey showed a smaller gain in employment of only 179K (0.1%) – and that the household survey has historically been better at picking 'turning points' in employment than the (larger, and thus usually regarded as more reliable) payrolls survey
- Financial markets interpreted the larger-than-expected increase in US payroll employment as increasing the prospect of a third successive 75 basis point increase in the fed funds rate at next month's FOMC meeting, reversing what had previously been growing expectations that future increases would be smaller (slides 59, 36 and 38)
- Global supply-chain pressures appear to be easing, as indicated by the decline in the New York Fed's index of global supply chain pressures in July to its lowest level since January 2021, and the now 36% decline in container shipping costs since they peaked last September (slide 24)
- Consistent with that, 'upstream' price pressures, as indicated by the 'prices paid' components of the US ISM indexes fell in July to their lowest levels since August 2020 for manufacturing, and since February 2021 for services businesses (slide 54); the manufacturing ISM also points to some easing in supply-chain disruptions (slide 55)
- The US goods and services trade deficit narrowed by US\$5.3bn to \$79.6bn in June, the smallest deficit since December last year, driven by increases of 1.3% and 0.6%, in the volume and average price, respectively of US exports, and falls of 0.4% and 0.1% in the volume and price of imports (slide 56)
- The Bank of England raised its bank rate by 50 basis points, to 1.75%, at last week's Monetary Policy Committee meeting, the largest increase since February 1995: the Bank now expects the UK's 'headline' inflation rate to peak at 13% in Q4 this year, and the UK economy to enter a recession in Q4 entailing a 2¼% contraction in real GDP over five quarters (slide 68)
- China's merchandise trade surplus widened another US\$3.3bn to a new record \$101.3bn in July, with exports up 0.5% in July and by 17.8% from a year earlier, whereas imports fell 0.7% in July and were only 2.3% above the year-earlier level (slide 75)
- Indonesia's real GDP expanded by 5.4% in Q2 from a year earlier, driven by strong growth in household consumption and exports (slide 90)
- The Reserve Bank of India lifted its policy rates by a larger-than-expected 50 basis points, the third consecutive increase, and also raised banks' cash reserve requirement ratio by 50bp (slide 109)
- Employment in Canada fell another 0.2% in July, but the unemployment rate remained unchanged at a 52-year low of 4.9% (slide 112)
- The Reserve Bank of Australia raised its cash rate another 50 bp, to 1.85%, bringing the cumulative increase over the past four months to 175 bp, the fastest increase since the second half of 1994 (slides 111 and 113)
- Banco Central do Brasil lifted its Selic rate another 50bp, to 13¾% (making for a cumulative increase of 11½ pc pts since March last year), but appeared to suggest that the tightening cycle may be approaching its peak (slides 116-117)
- US July CPI is the most important item on this week's calendar but there's also Q2 GDP for the UK, the Philippines, Taiwan, Malaysia, HK & Singapore, while the Bank of Thailand is likely to lift rates for the first time since the pandemic (slide 125)

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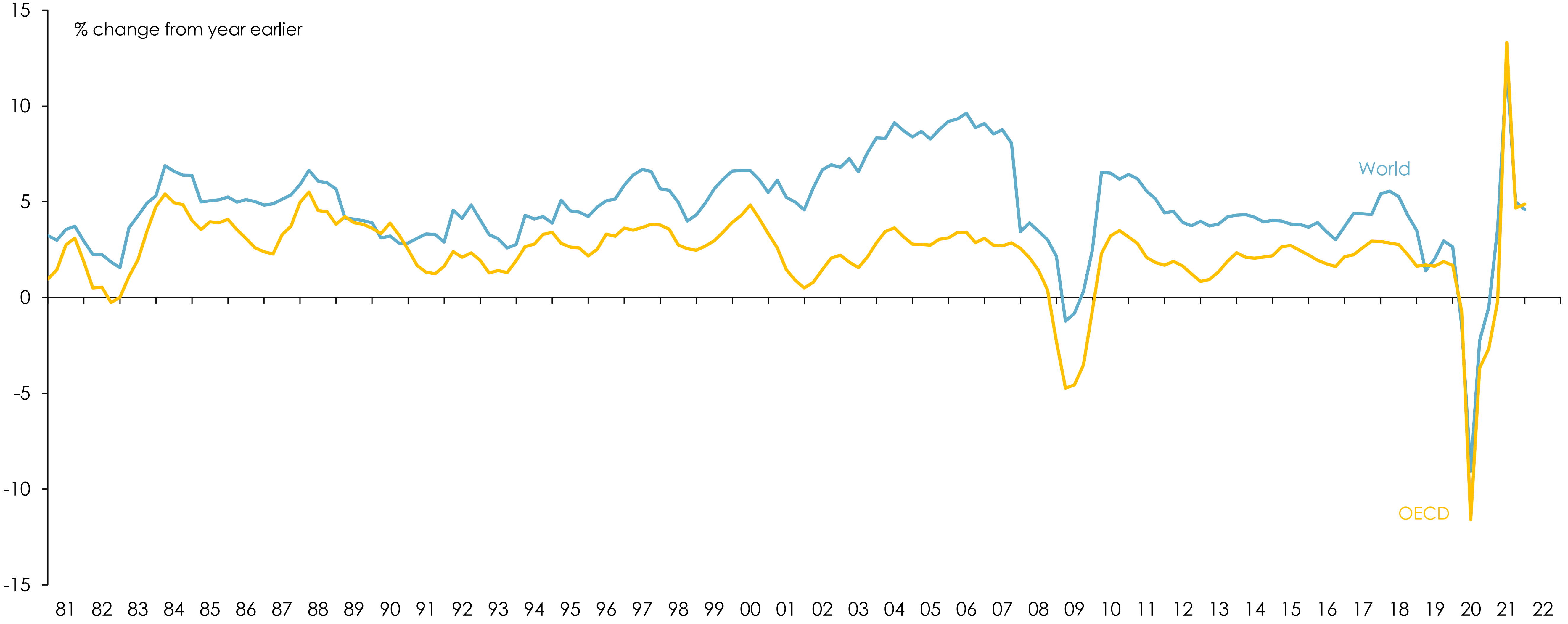
Covid-19 threw the world economy into its deepest recession since the 1930s, from which it has recovered quite quickly over the past 18 months

World and OECD area real GDP growth



Note: Estimates of global GDP growth compiled by Corinna using data for 100 countries accounting for 94% of 2019 world GDP as measured by the IMF, weighted in accordance with each country's share of global GDP at purchasing power parities in 2019; excludes constituents of the former USSR before 1993, the former Czechoslovakia before 1995, and the former Yugoslavia before 1998. *Sources:* national statistical agencies and central banks; Eurostat; OECD; IMF; Corinna.

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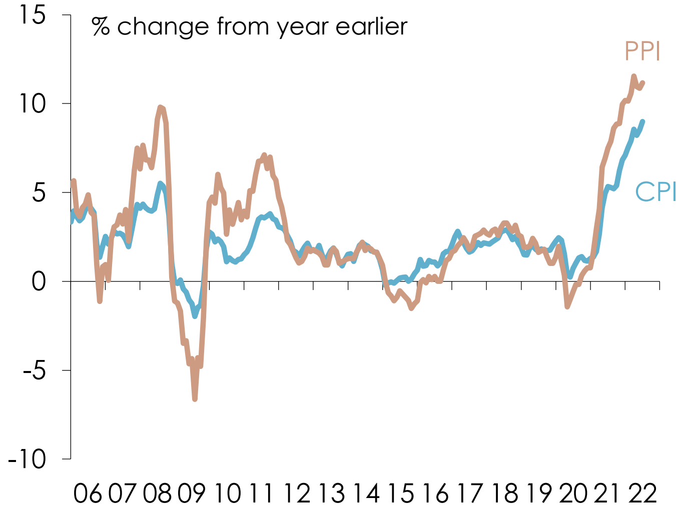
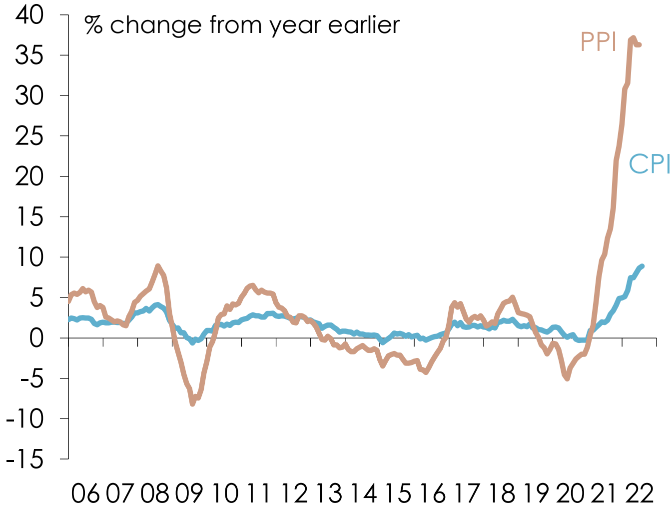
Almost all developed economies, and many ‘emerging’ economies, are confronting the highest inflation in decades

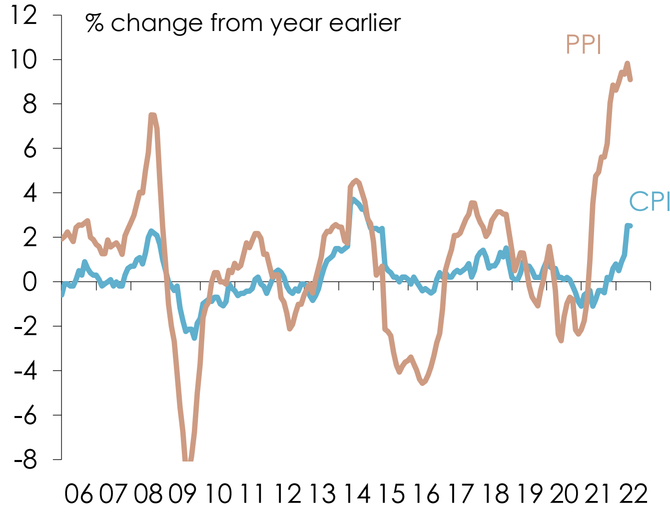
United States



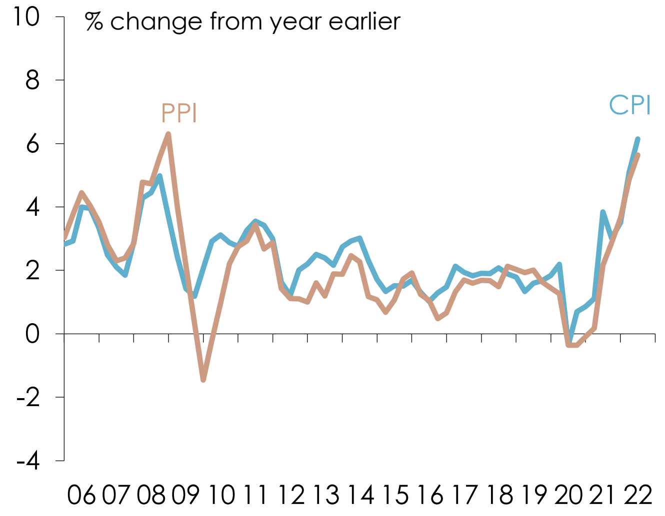
Euro area



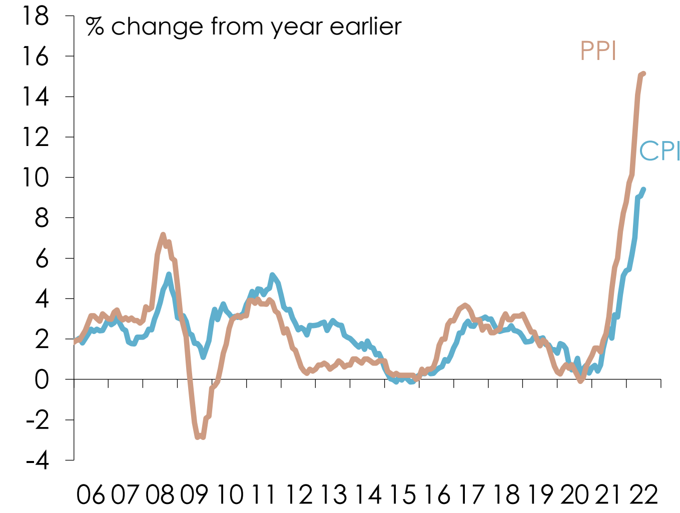
Japan



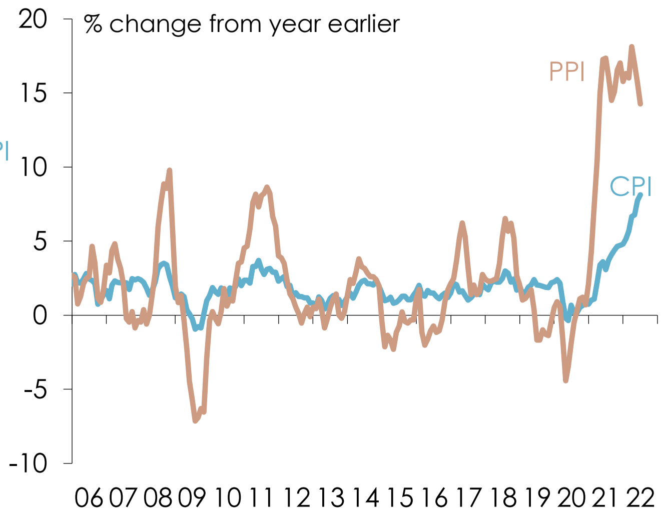
Australia



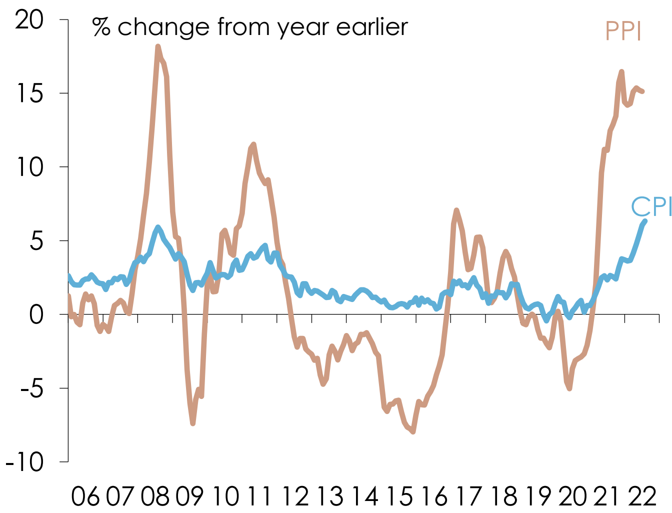
United Kingdom



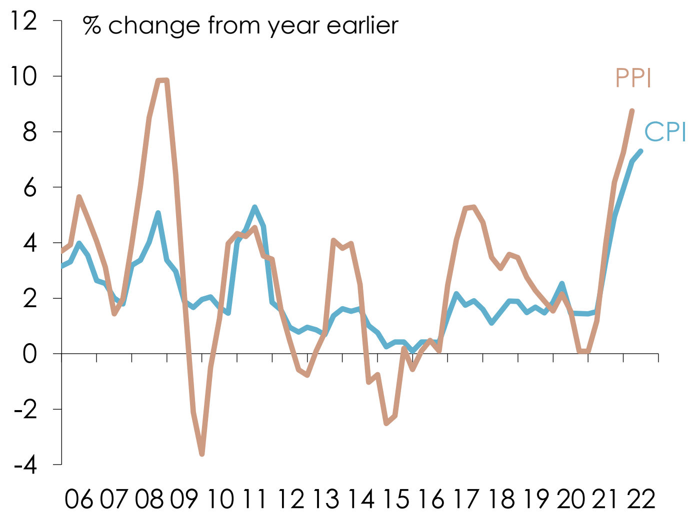
Canada



Korea



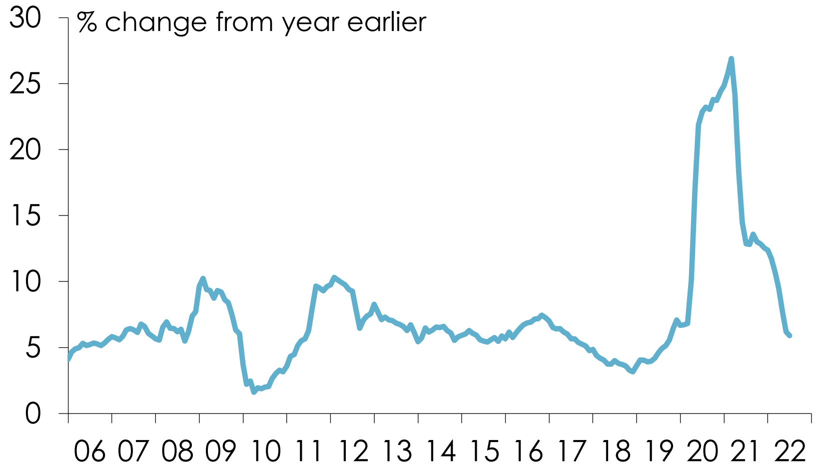
New Zealand



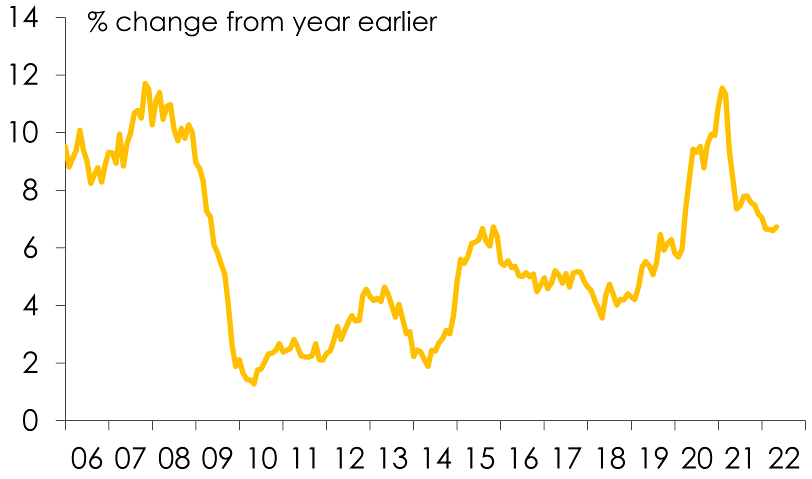
Note: ‘PPIs’ are producer price indexes, measuring prices of items produced by (in most cases) manufacturing firms. CPI is the consumer price index.
Sources: US Bureau of Labor Statistics; UK Office for National Statistics; Eurostat; Statistics Canada; Statistics Bureau of Japan; Statistics Korea; Australian Bureau of Statistics; Statistics New Zealand.

Monetarists would say, "I told you so" about the inflation – but they would also now have to say that inflation will come down again

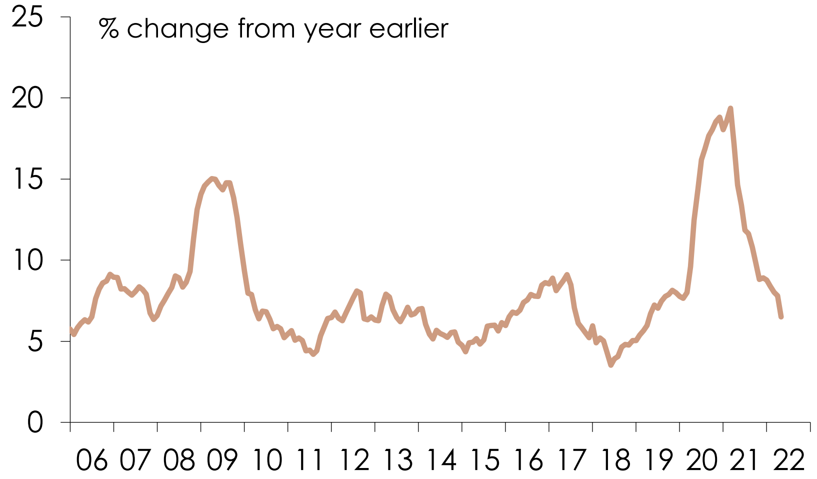
US M2



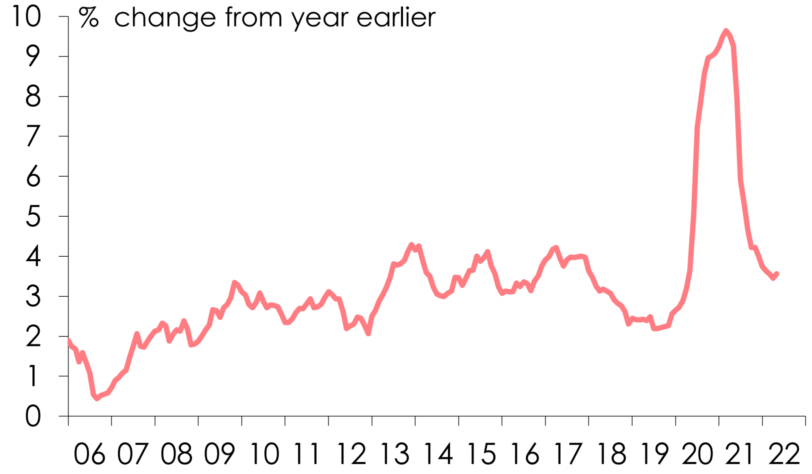
Euro area M2



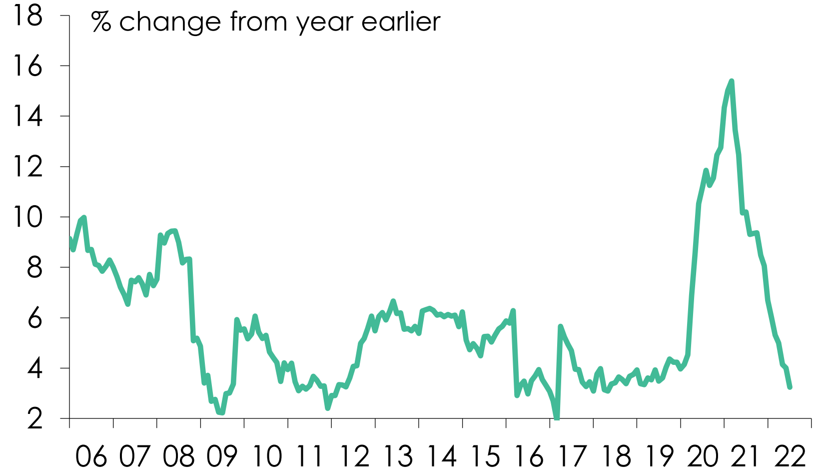
Canada M2



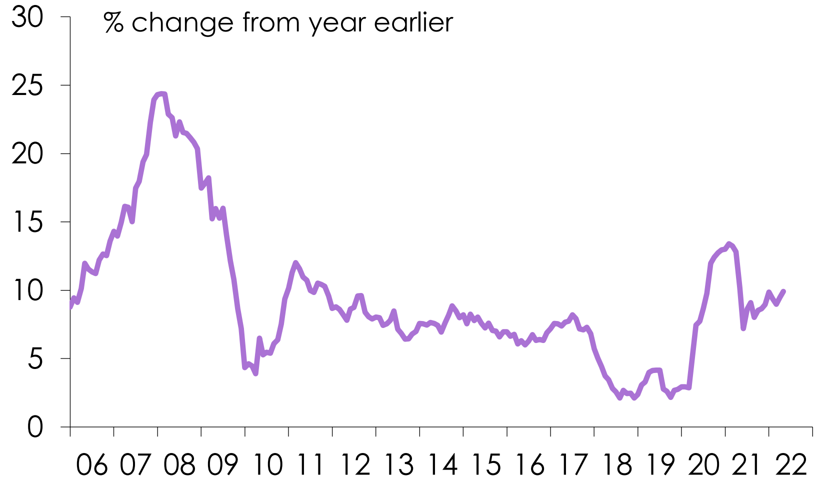
Japan M2 + CDs



UK M2



Australia M3



Sources: US Federal Reserve; Bank of Japan; European Central Bank; Bank of England; Bank of Canada; Reserve Bank of Australia.

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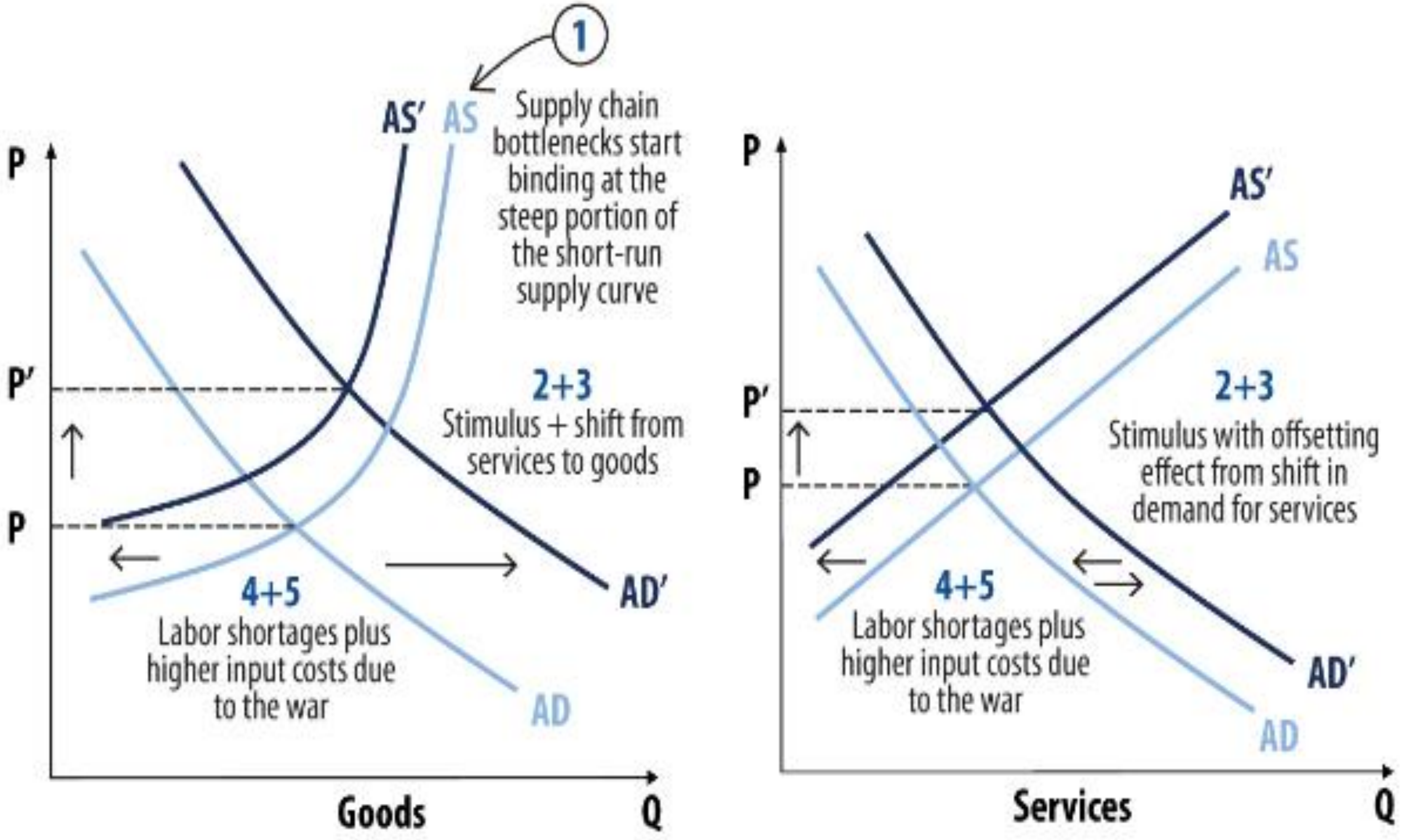
Two IMF researchers have provided a helpful stylized depiction of the sources of upward pressure on inflation over the past 15 months

An aggregate supply- aggregate demand (AS-AD) curve illustration of the factors behind the rise in inflation over the past 15 months



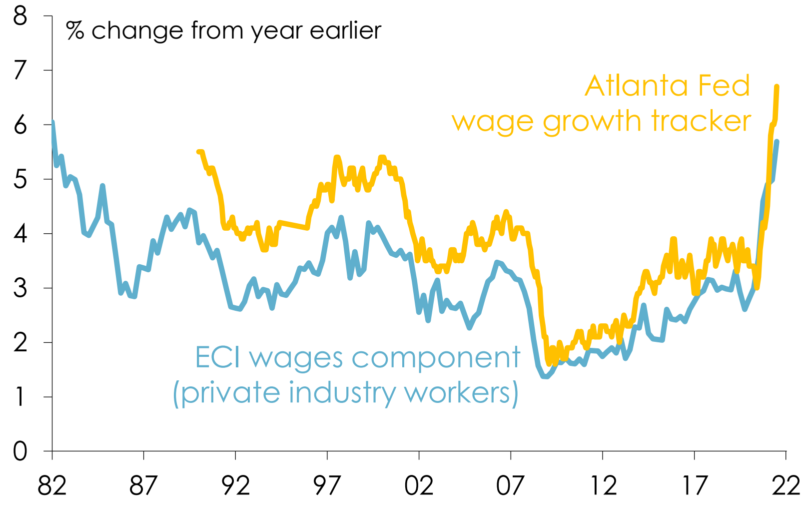
1. Supply chain bottlenecks reducing supply of durable goods – aggregate supply curve shifts to left (AS → AS′)
2. Shift in demand from services to goods (prompted by public health restrictions), with opposite effects on demand for services and goods – aggregate demand curve for goods shifts to right, for services shifts to left (AD → AD′)
3. Policy stimulus, followed by economic recovery, shifts aggregate demand curve (for both goods and services) to the right (increased demand)
4. Labour shortages (prompted by Covid-19, immigration restrictions, etc) shift aggregate supply curves to the left (AS → AS′)
5. Supply shocks to energy and food due to the war in Ukraine shift aggregate supply curves to the left (AS → AS′)

– all resulting in upward movements in prices (P → P′)

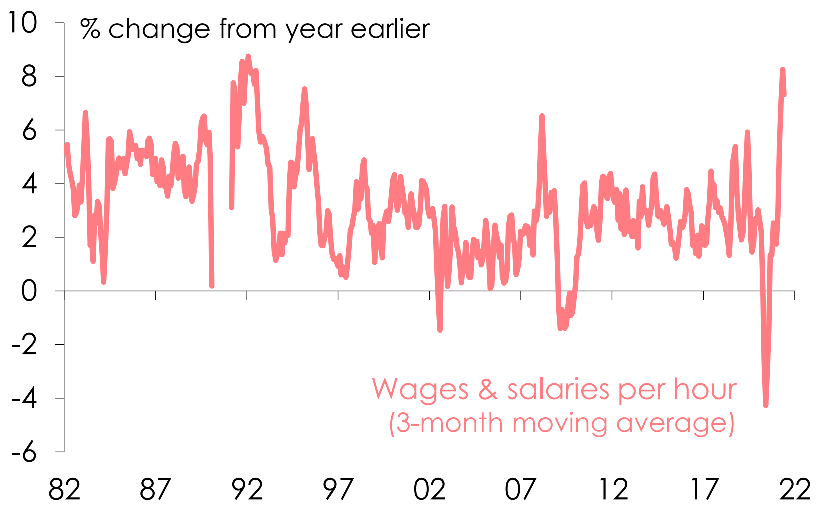
Source: Ruchir Agawal and Miles Kimball, *Will inflation remain high?*, International Monetary Fund, 7th April 2022.

Tight labour markets and rising labour costs have contributed to rising inflation in some economies – though not (so far) in Australia

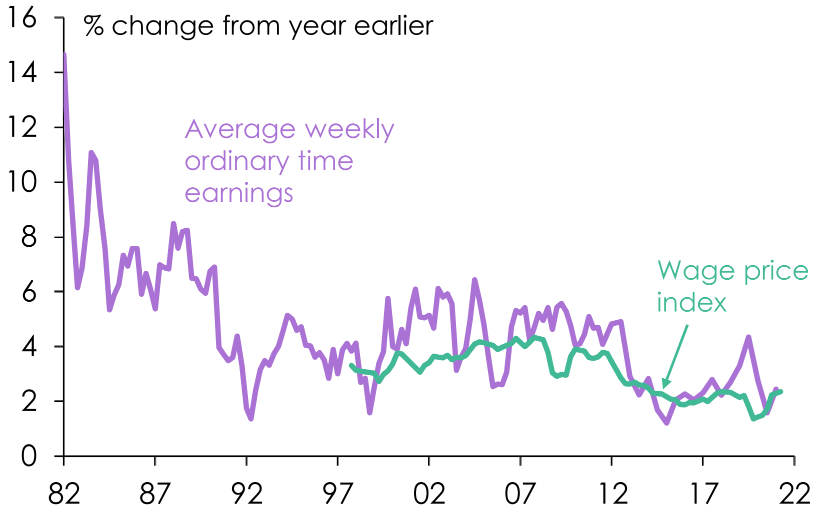
US



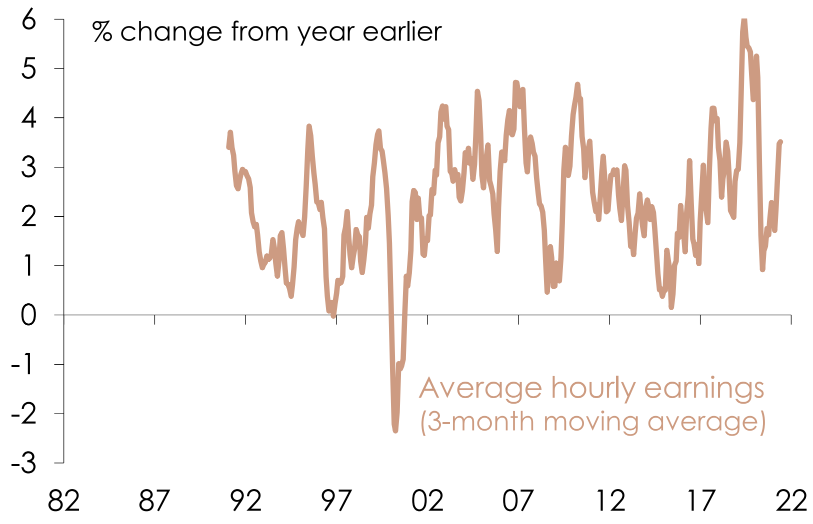
Germany



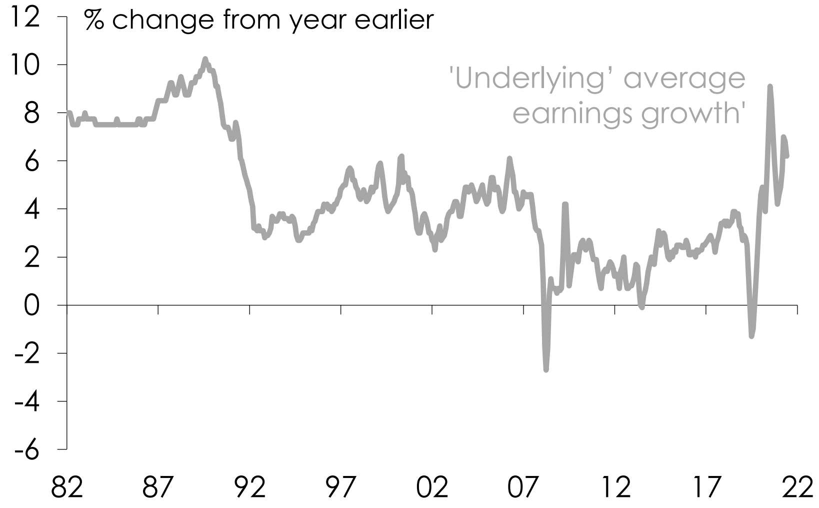
Australia



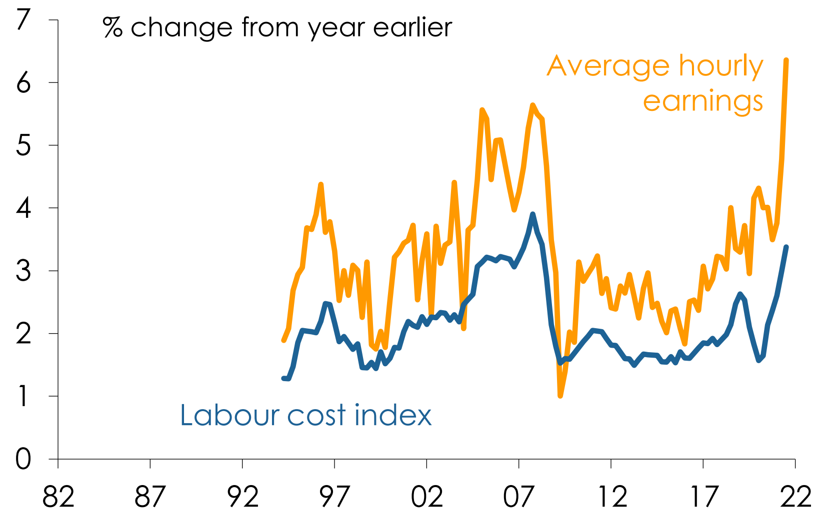
Canada



UK



New Zealand



Sources: US Bureau of Labor Statistics; Federal Reserve Bank of Atlanta; Statistics Canada; Statistiches Bundesamt; UK Office for National Statistics; Australian Bureau of Statistics; Statistics New Zealand.

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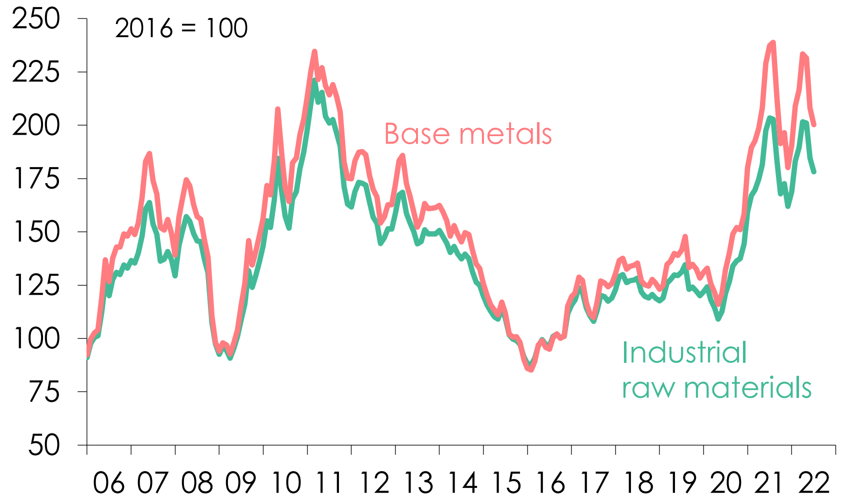
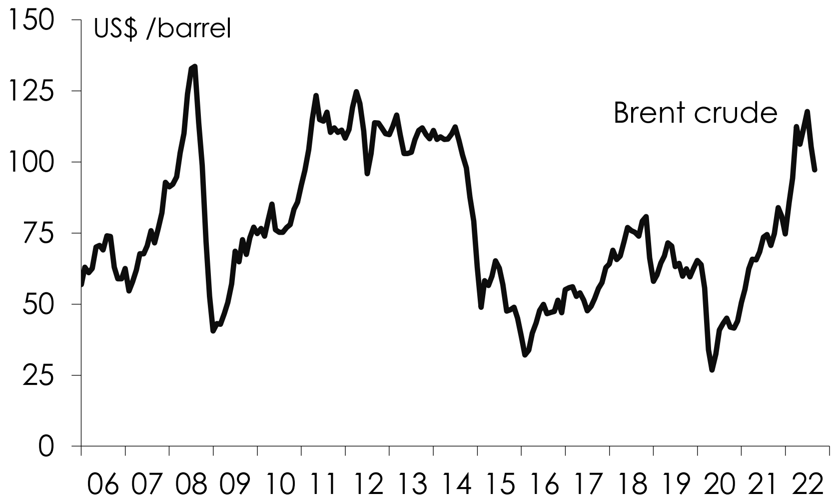
Commodity prices, apart from gas, are now falling – and supply chain pressures are easing too

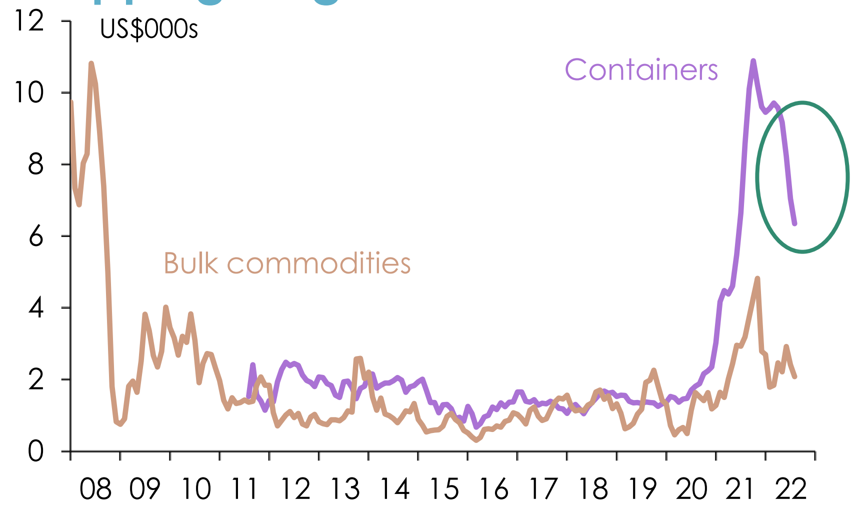
'Hard' commodity prices



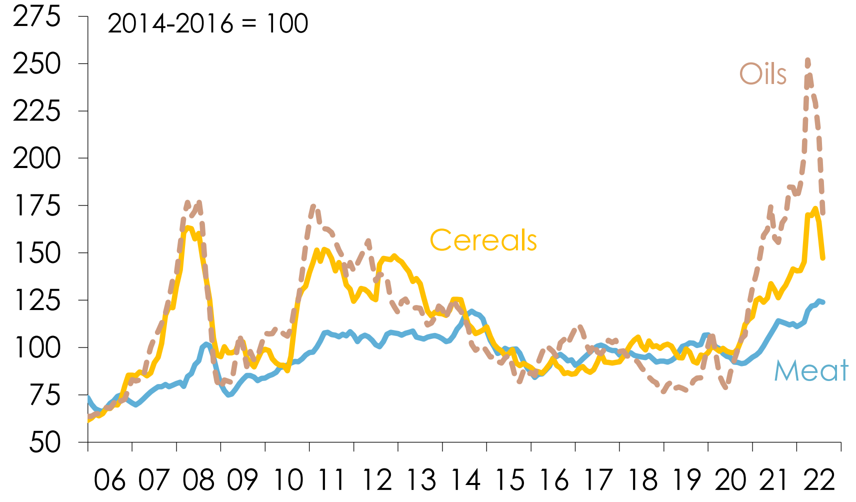
Crude oil price



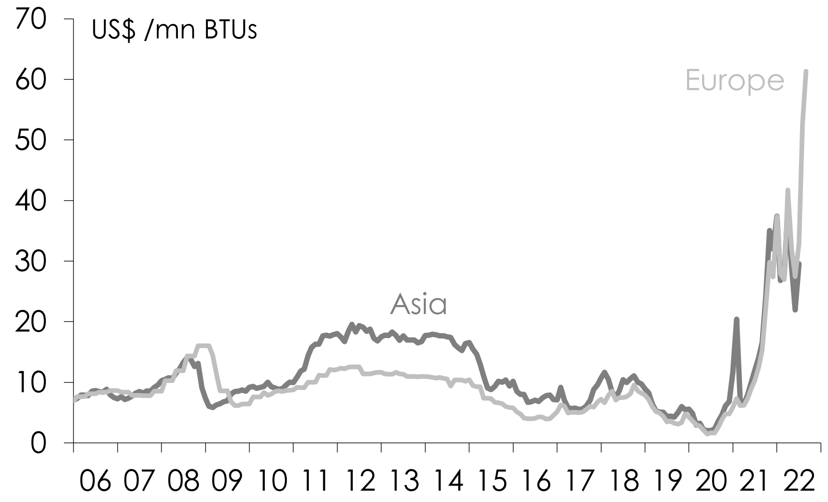
Shipping freight costs



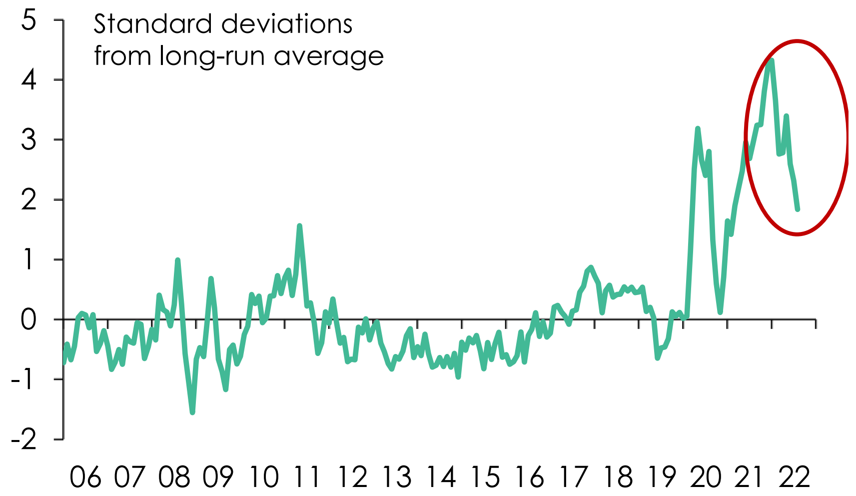
Food commodity prices



Natural gas prices



Global supply chain pressure index



Sources: International Monetary Fund; UN Food and Agriculture Organization; Freightos; Drewry; The Baltic Exchange; Federal Reserve Bank of New York.

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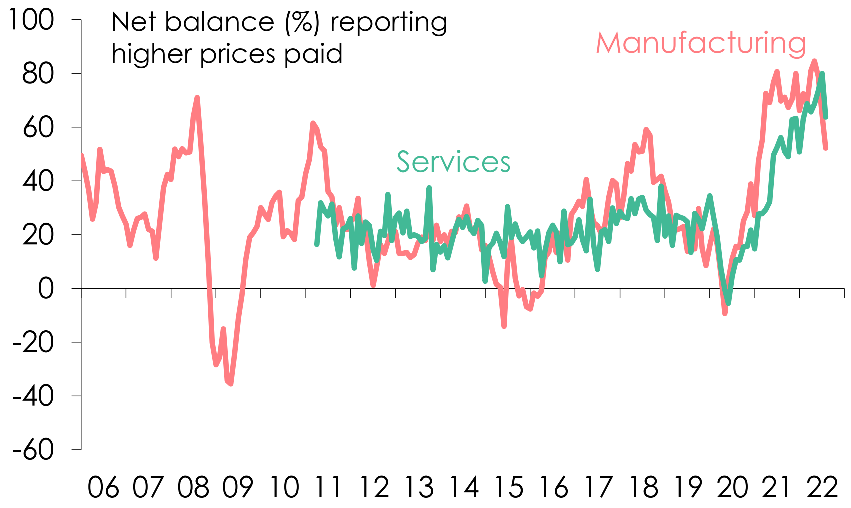
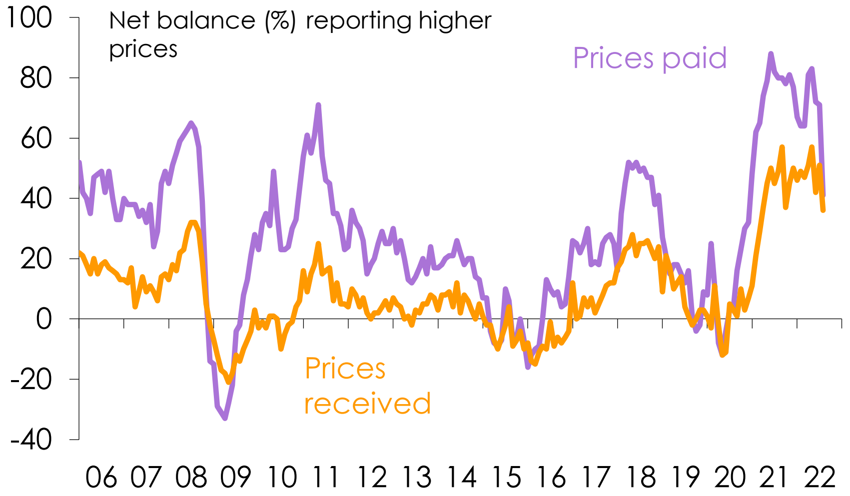
A range of US surveys are now hinting that 'upstream' inflation may have peaked – while longer-run household inflation expectations have fallen

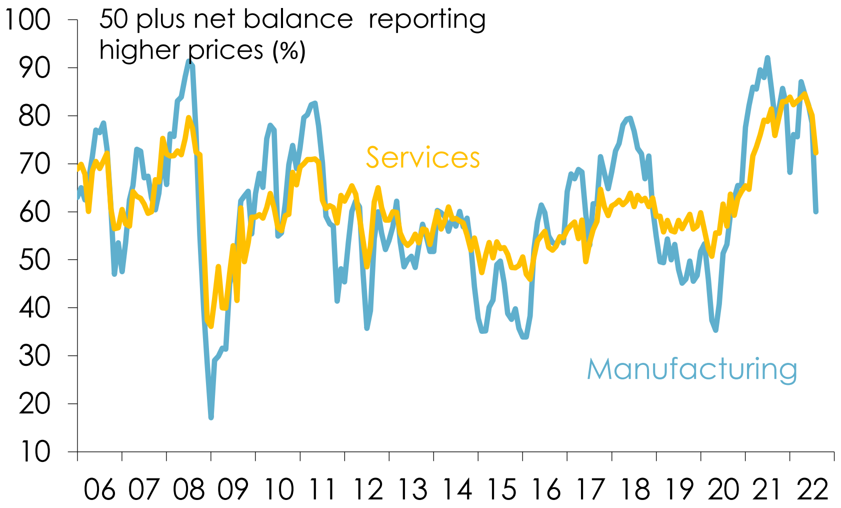
'Philly' Fed survey – prices paid



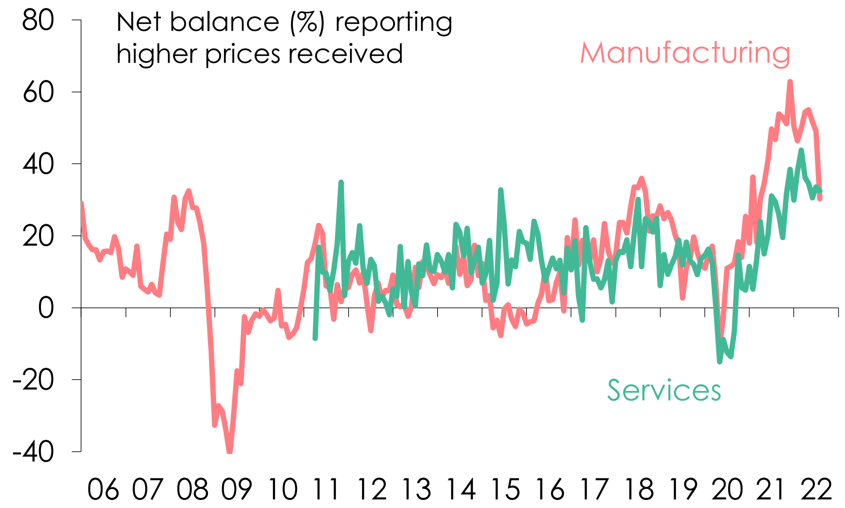
Kansas City Fed manufacturers survey



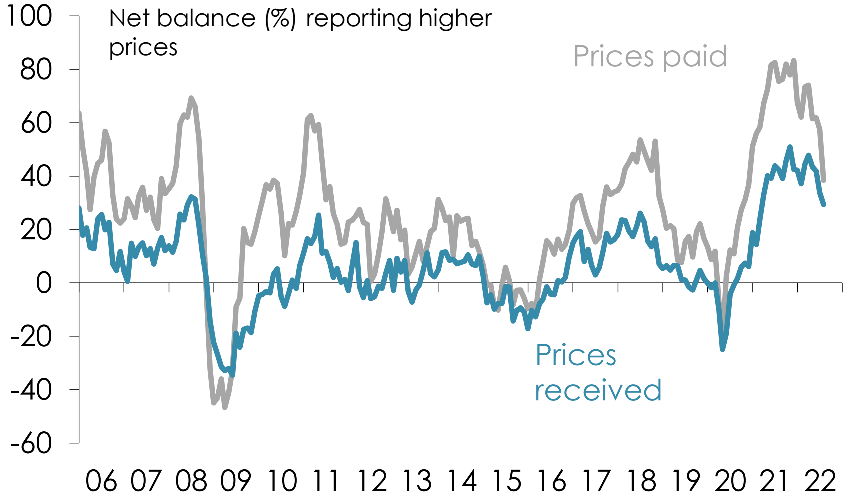
ISM survey – prices paid



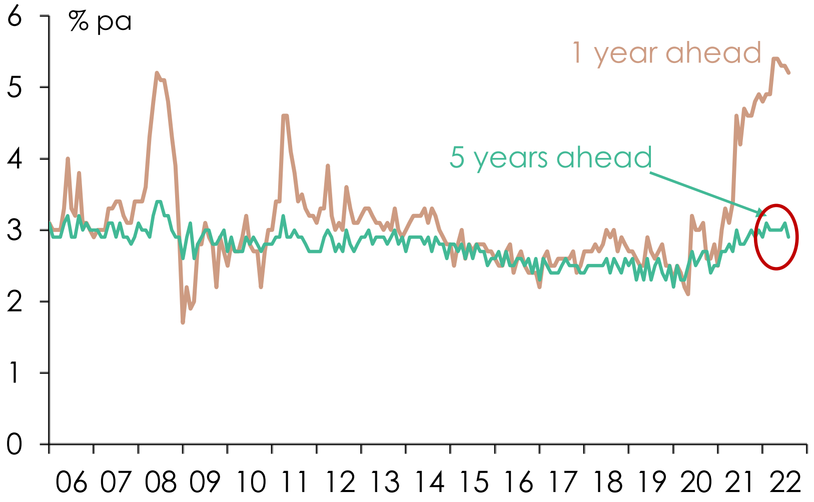
'Philly' Fed survey – prices received



Dallas Fed manufacturers survey



Household inflation expectations



Sources: Federal Reserve Bank of Philadelphia; Federal Reserve Bank of Kansas City; Federal Reserve Bank of Dallas; Institute of Supply Management; Michigan University Survey Research Center.

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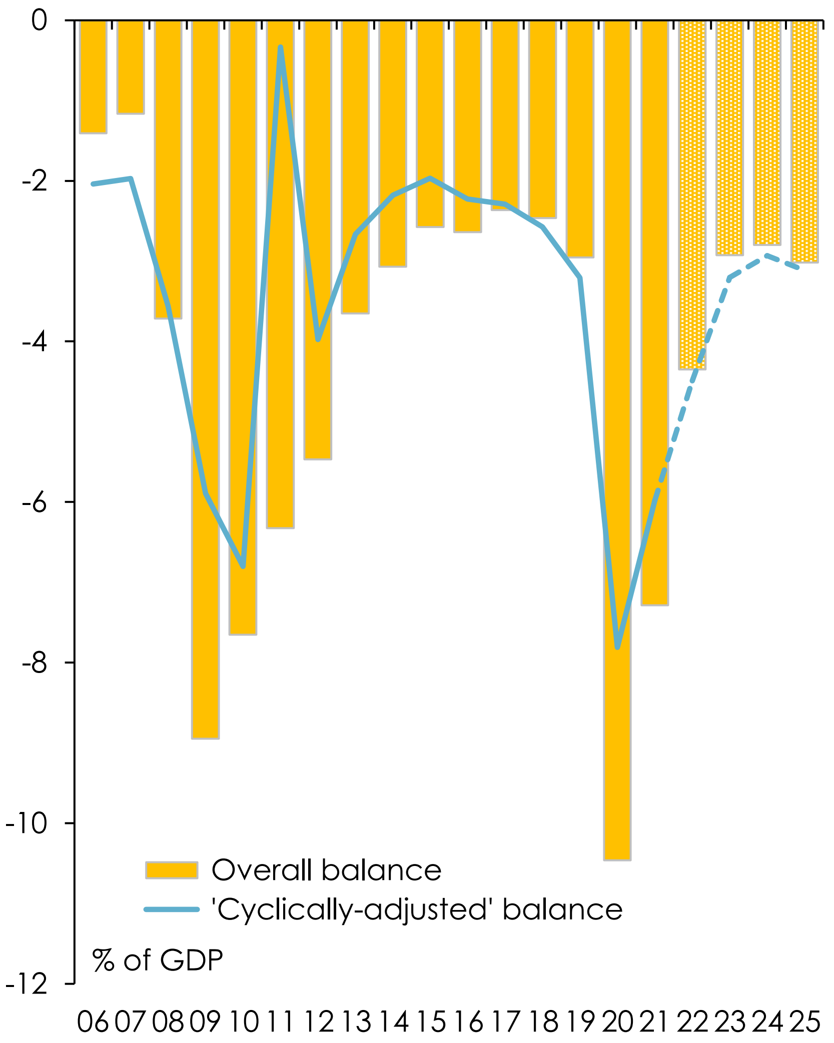
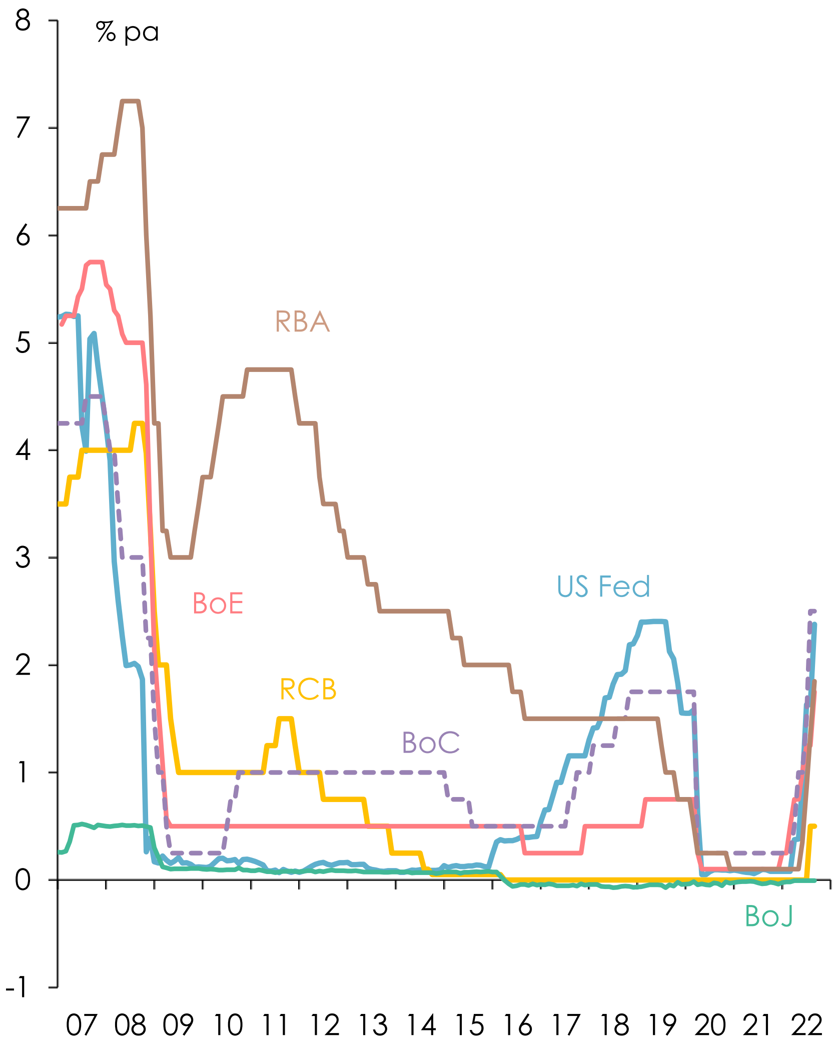
With the benefit of hindsight (always 20-20), governments and central banks did 'too much' stimulus

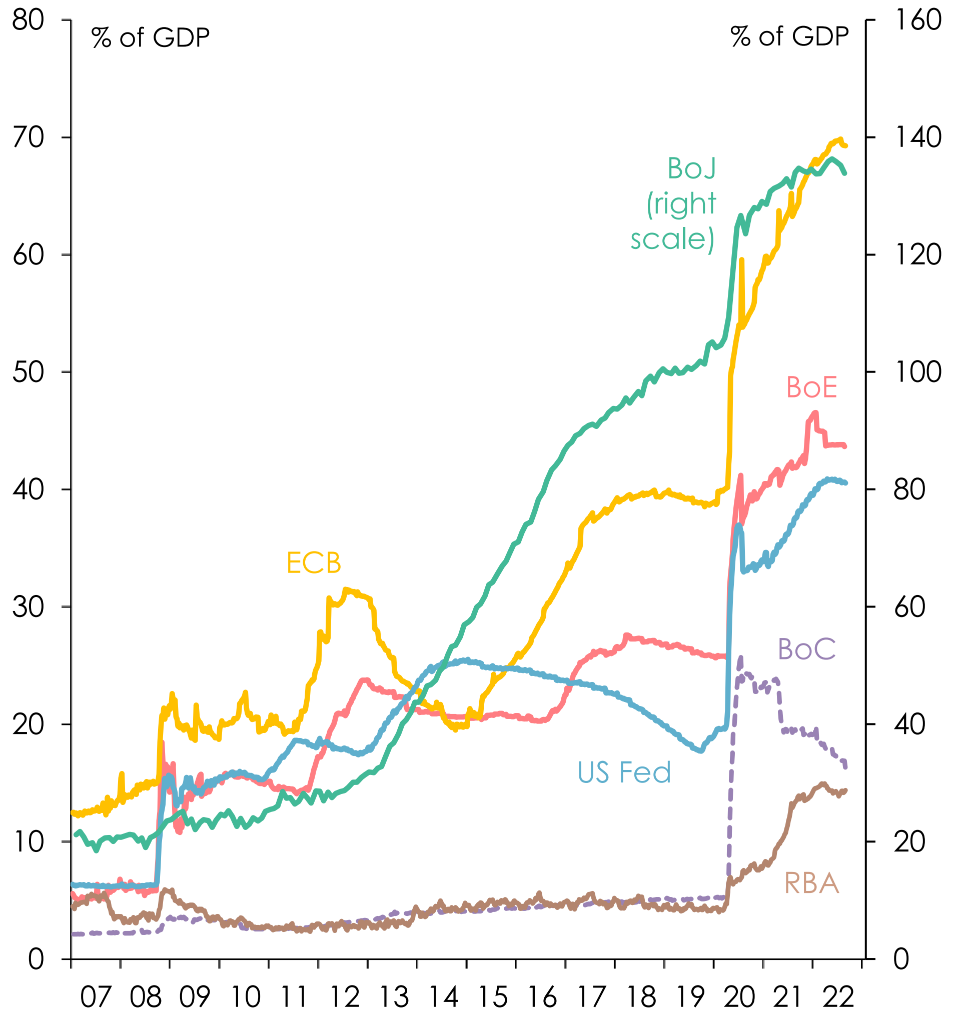
'Advanced' economies general government balances



'Advanced' economies central bank policy interest rates



'Advanced' economies central bank balance sheets



Sources: International Monetary Fund, *Fiscal Monitor*, and *World Economic Outlook*, April 2022; US Federal Reserve; European Central Bank; Bank of Japan; Bank of England; Bank of Canada; Reserve Bank of Australia; and national statistical agencies; .

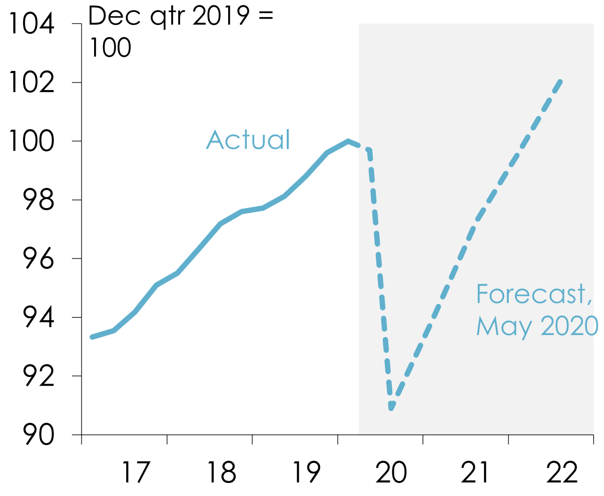
The 'policy mistake' wasn't in doing 'too much' initially – it was in not starting to wind it back, once it was clear that it was no longer needed

- **With the benefit of hindsight, governments and central banks provided 'too much' fiscal and monetary policy stimulus in response to the economic downturns wrought by the restrictions imposed to deal with Covid-19**
  - but when Covid-19 first struck, and no-one knew what effects it might have or how long it would take to develop safe and effective vaccines, the economic outlook was almost universally expected to be dire
  - the probability that they could have calibrated exactly the 'right' amount of stimulus in these circumstances was zero
  - So the 'right mistake' to have made, at least initially, was to err on the side of doing 'too much'
- **The 'big' mistake was in failing to wind back the stimulus once it was clear – as it should have been by around this time last year – that governments and central banks had provided more stimulus than was needed**
  - unfortunately, most of them didn't

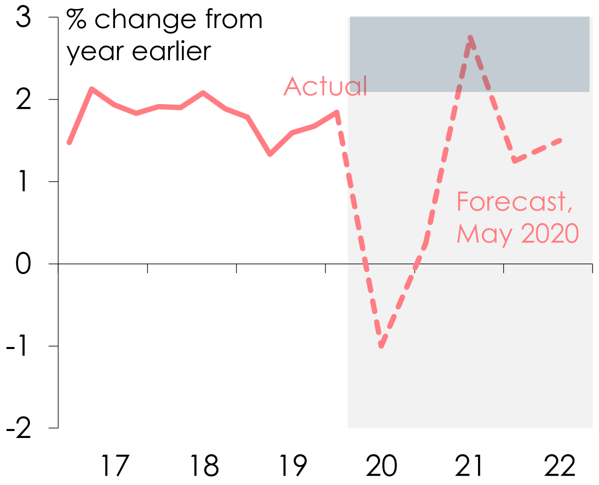
It's hard to fault the RBA's policy responses to the initial onset of Covid-19 – but it should have realized things hadn't turned out so bad a year later

RBA's forecasts as at May 2020

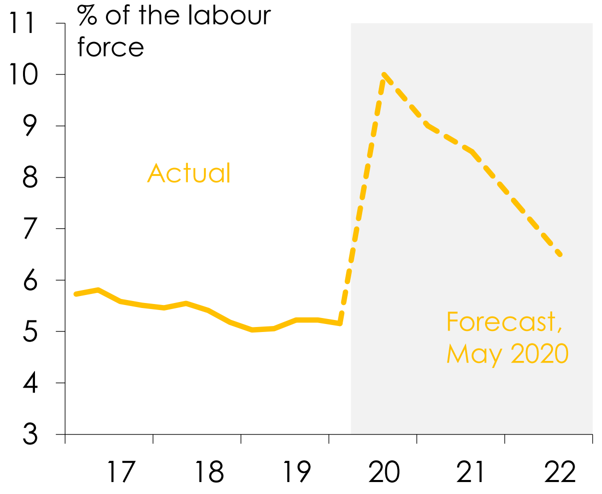
Real GDP



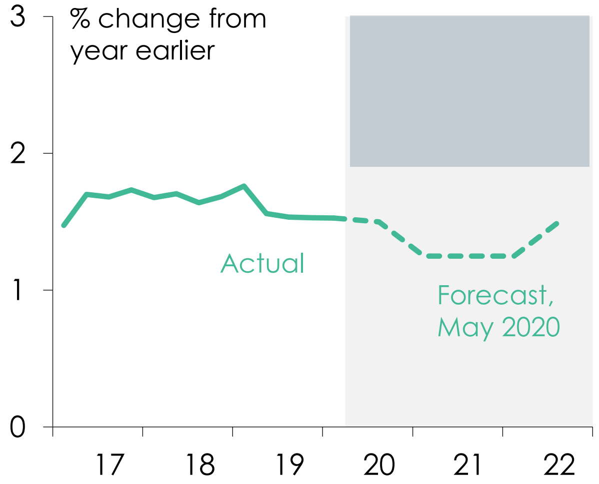
'Headline' inflation



Unemployment

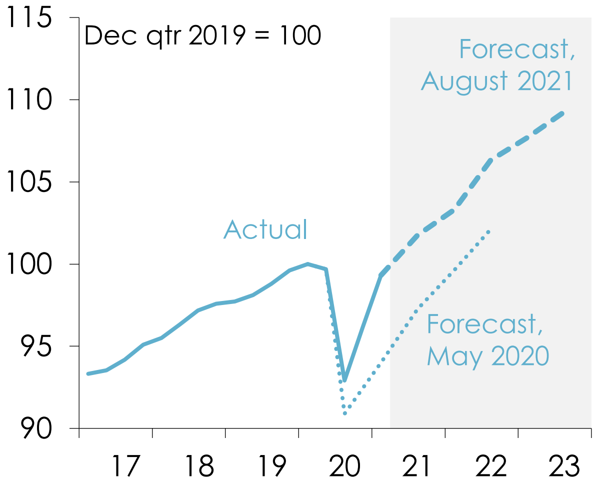


'Underlying' inflation

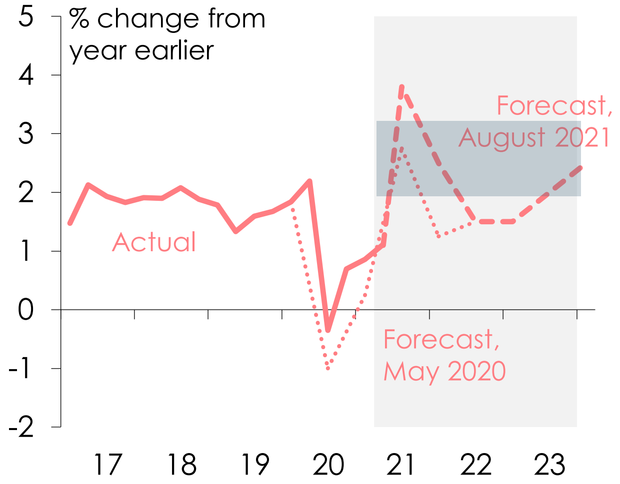


RBA's forecasts as at August 2021

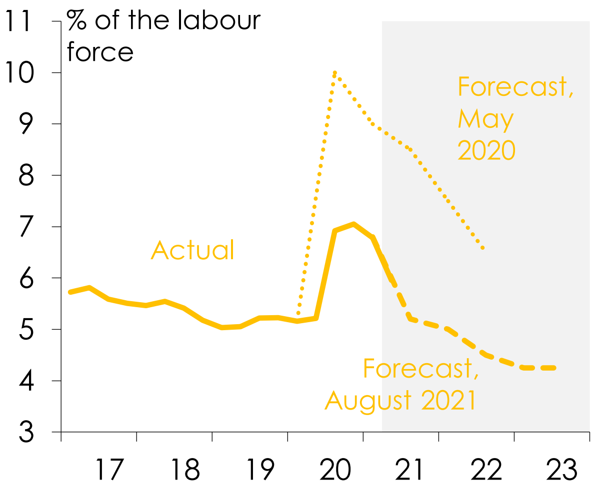
Real GDP



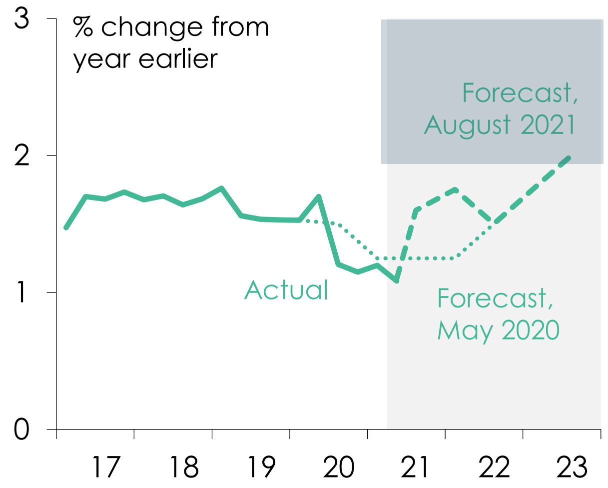
'Headline' inflation



Unemployment



'Underlying' inflation



Note: Darker shading represents the RBA's 2-3% inflation target range. *Sources:* ABS; RBA, Statements on Monetary Policy.

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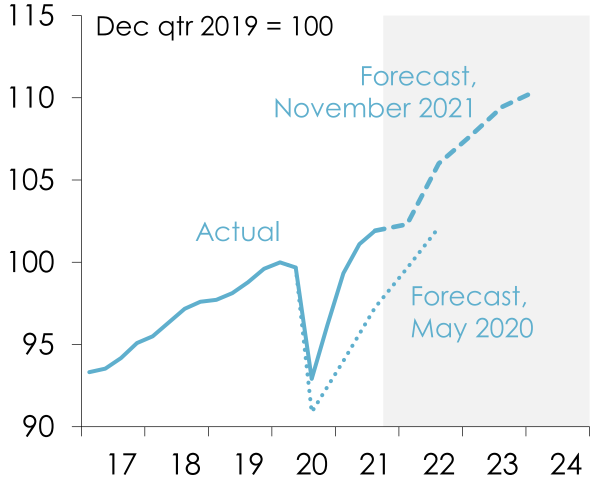
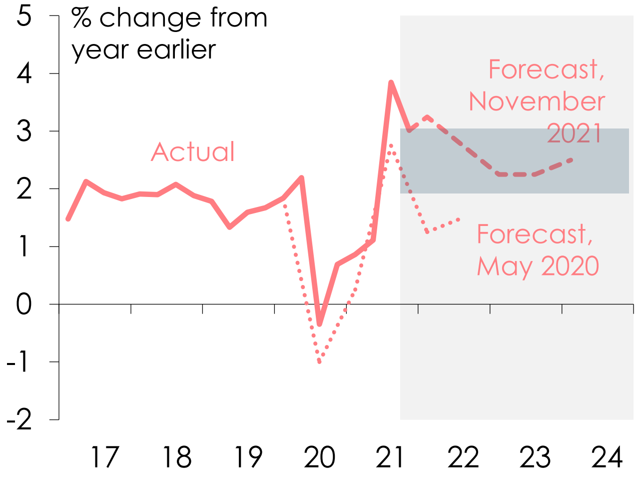
By November last year, the RBA's forecasts *should* have prompted a re-think of monetary policy settings – and certainly by February this year

RBA's forecasts as at November 2021

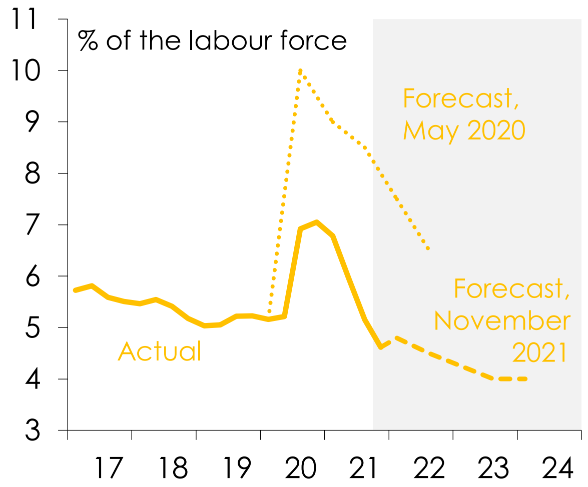
Real GDP



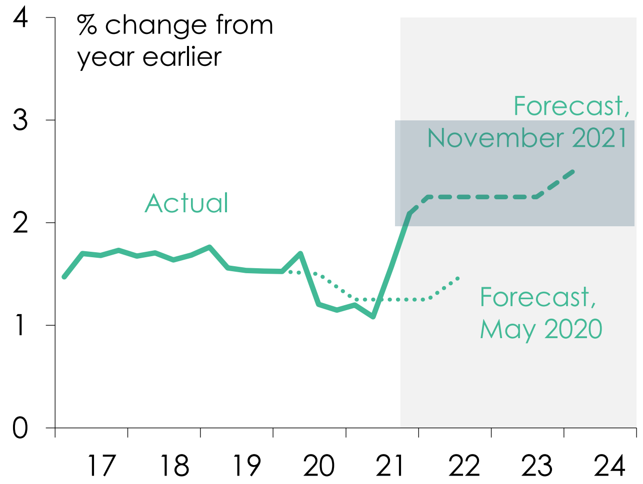
'Headline' inflation



Unemployment

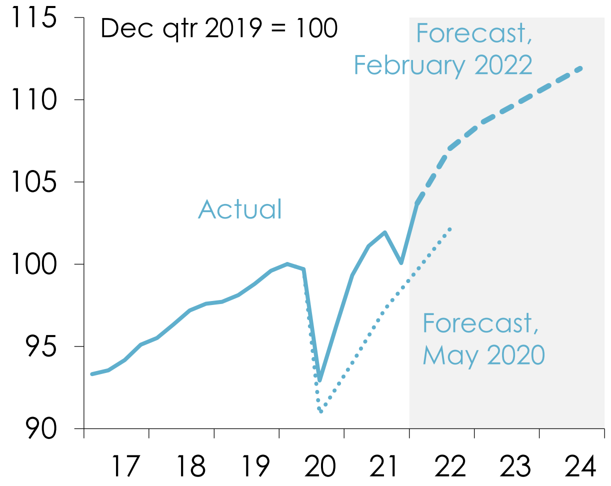


'Underlying' inflation

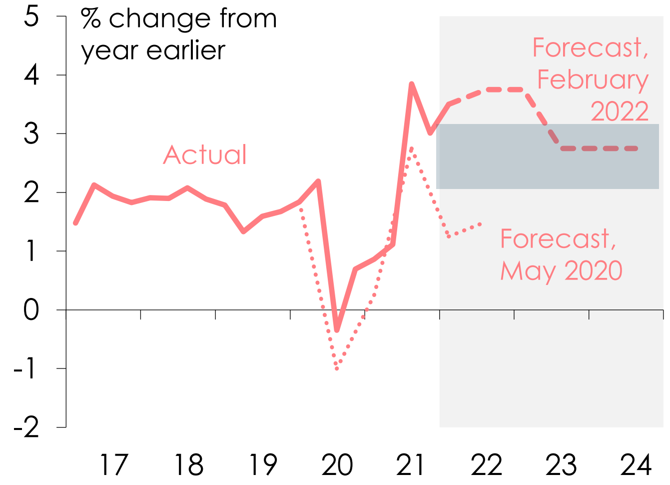


RBA's forecasts as at February 2022

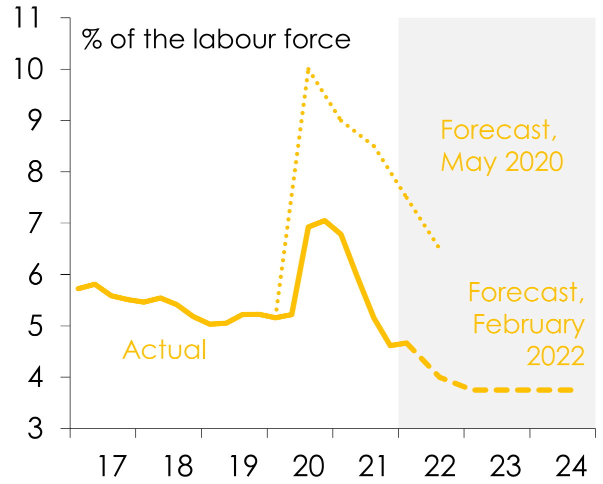
Real GDP



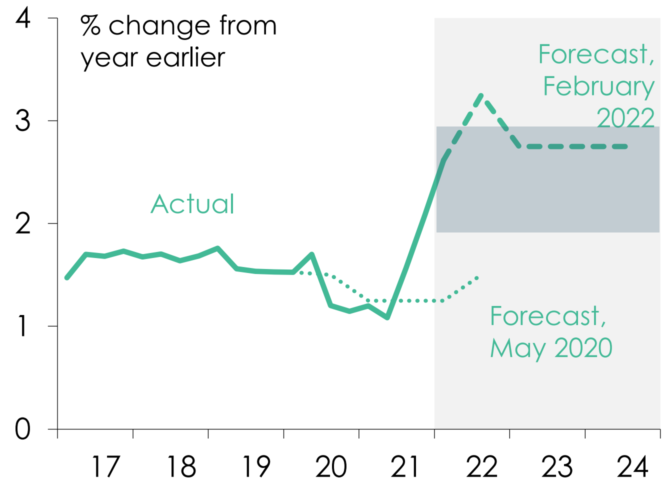
'Headline' inflation



Unemployment



'Underlying' inflation



Note: Darker shading represents the RBA's 2-3% inflation target range. *Sources:* ABS; RBA, Statements on Monetary Policy.

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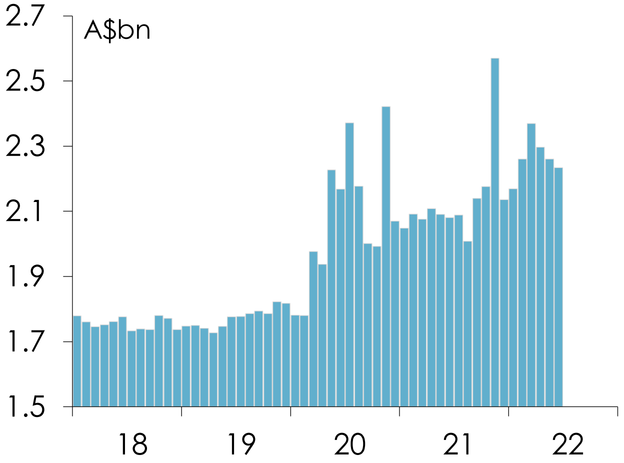
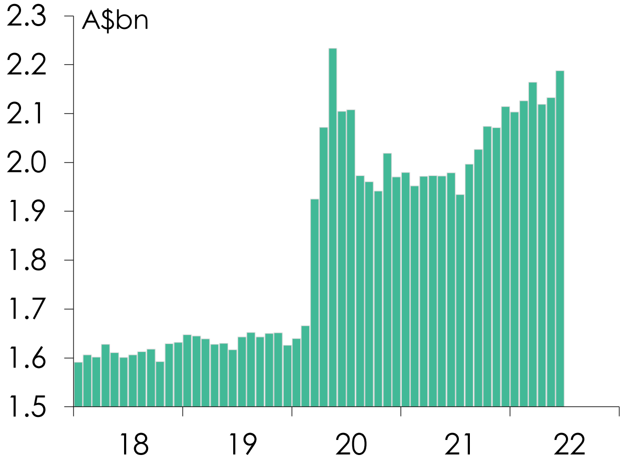
The continued strength (through June) in a wide range of 'discretionary' spending indicates how strong aggregate demand has been (and is)

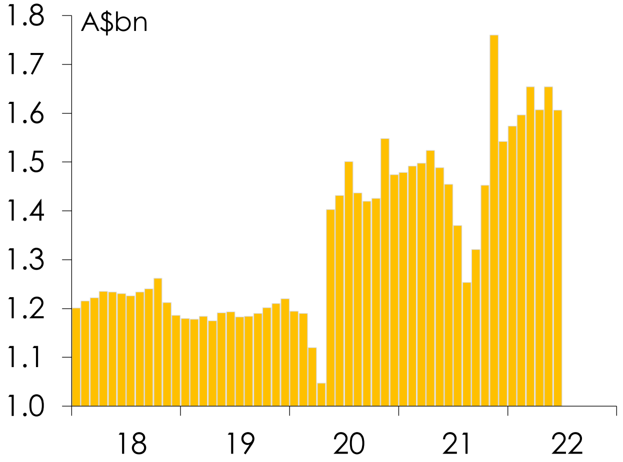
Electronic & electrical goods



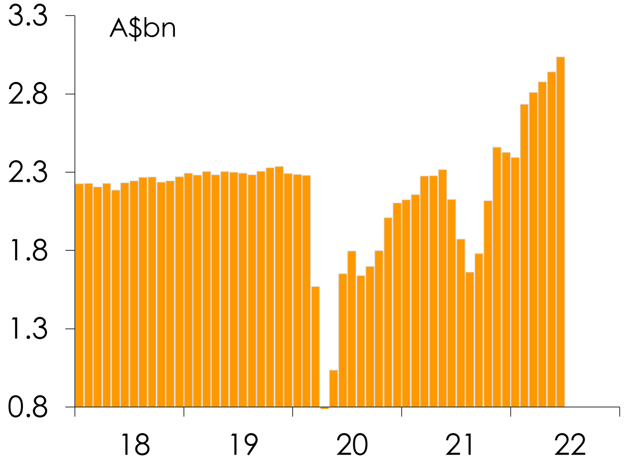
Hardware, building & garden supplies



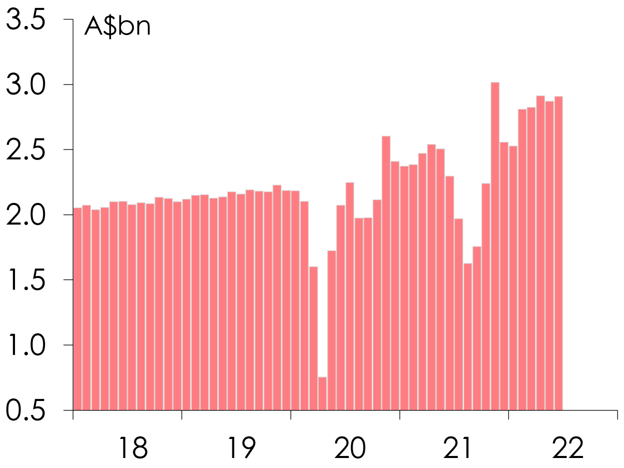
Floor coverings, furniture, housewares etc



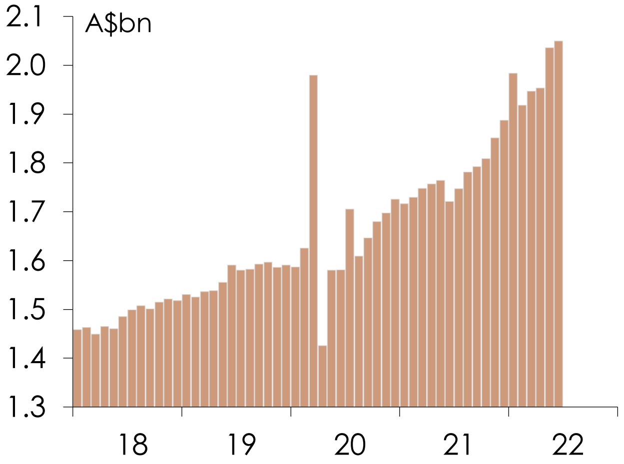
Cafes and restaurants



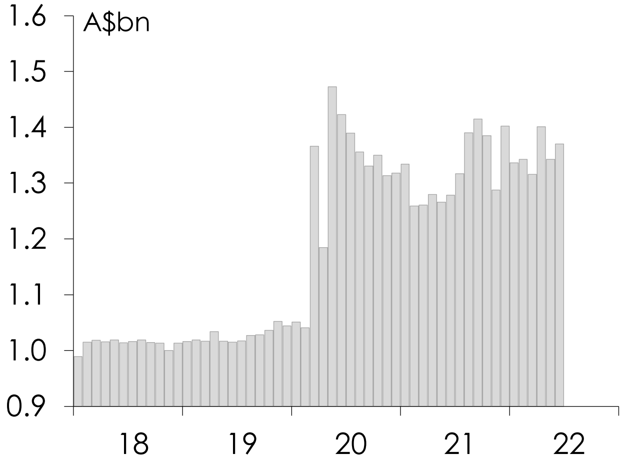
Clothing, footwear & personal accessories



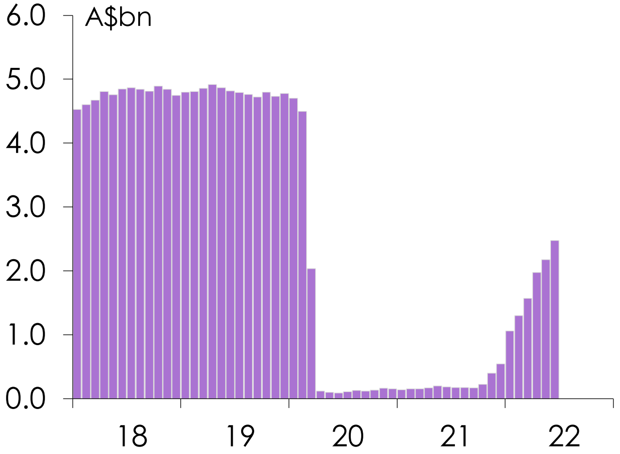
Pharmaceuticals, cosmetics & toiletries



Alcoholic beverages



Overseas travel



Sources: ABS, *Retail Trade, Australia*, June 2022; and *International Trade in Goods and Services, Australia*, June 2022.

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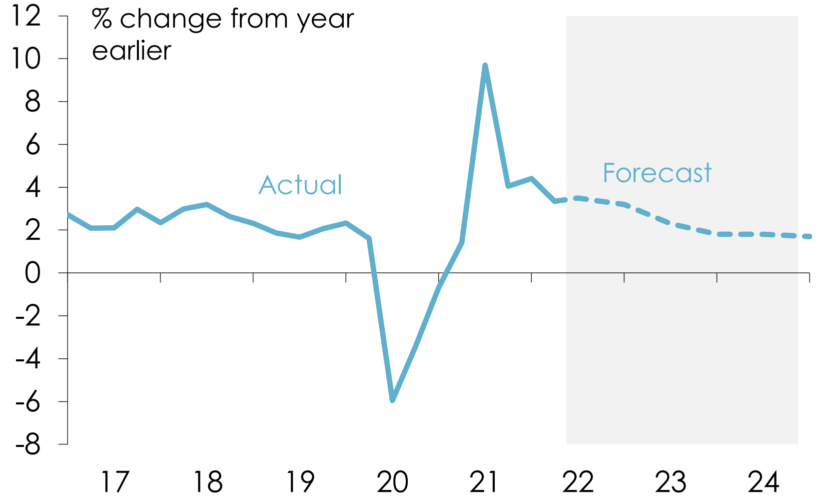
Leaving aside forecasting errors (where they were hardly Robinson Crusoe), the RBA made two significant mistakes

- **Putting a date on how long interest rates would remain at record lows**
  - most other central banks stipulated economic criteria which would need to be met before they would start 'normalizing' monetary policy settings
  - and nearly all of them emphasized that achieving those criteria would "take patience and time" (or words to that effect)
  - but no other central bank sought to put a date on how long interest rates would remain at record lows
  - or sought to underscore that time-specific commitment with targeted asset purchases

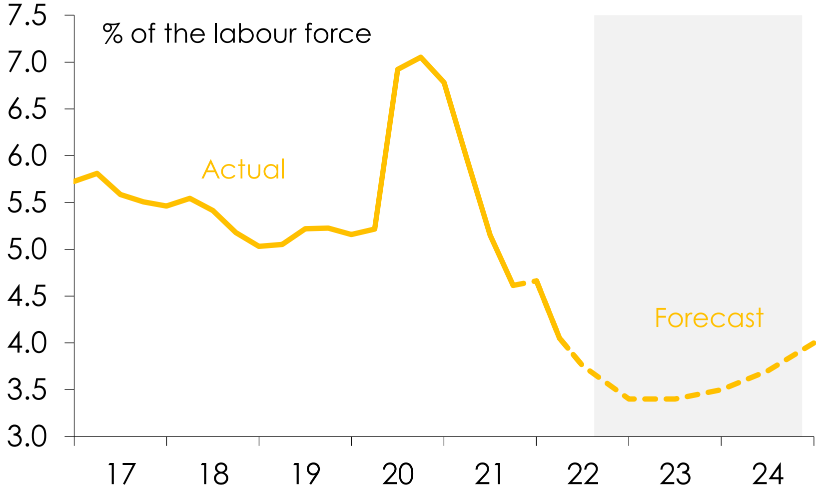
- **Having a 'model' of inflation which (implicitly) assumed that a 'sustainable' rise in inflation could only come from faster wages growth**
  - which led the RBA into failing to appreciate the consequences of the various sources of inflationary pressure which did emerge during 2021
  - and seems to have been a major reason why they were slow to respond to the rise in inflation

The RBA's latest SoMP forecasts seem plausible, although GDP growth may slow more, and unemployment rise further, than they expect

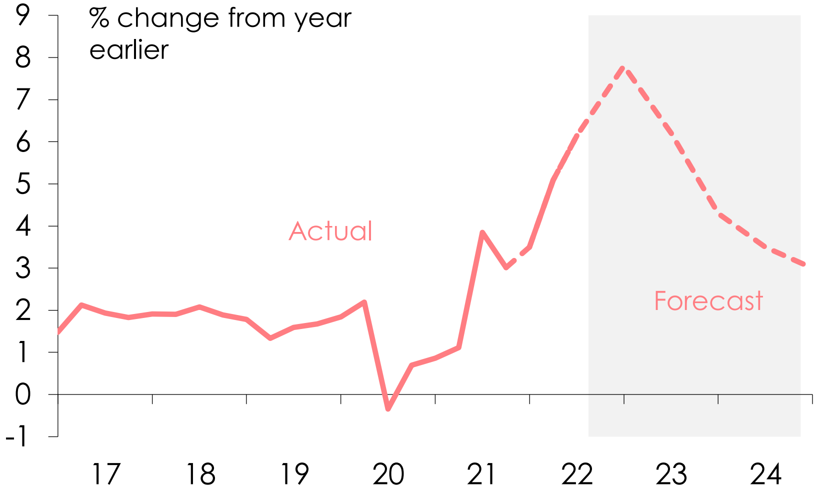
GDP



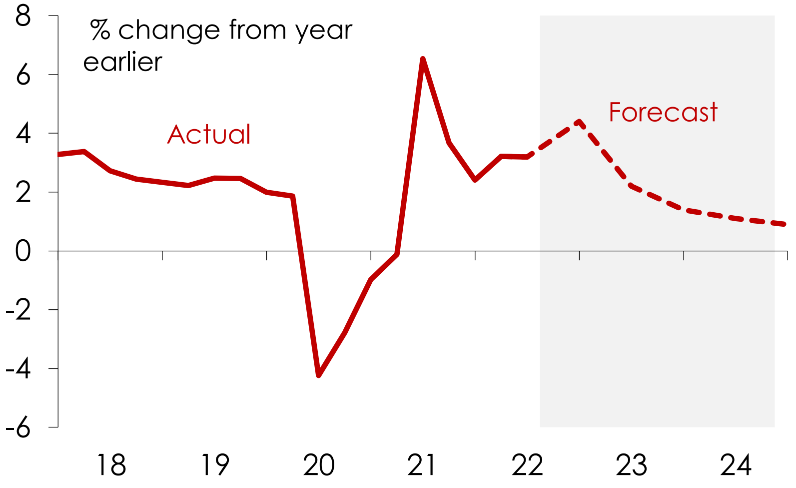
Unemployment



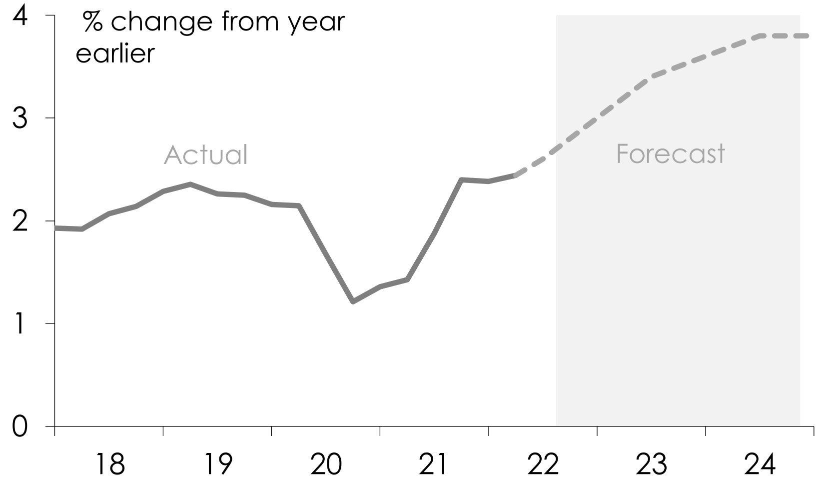
'Headline' inflation



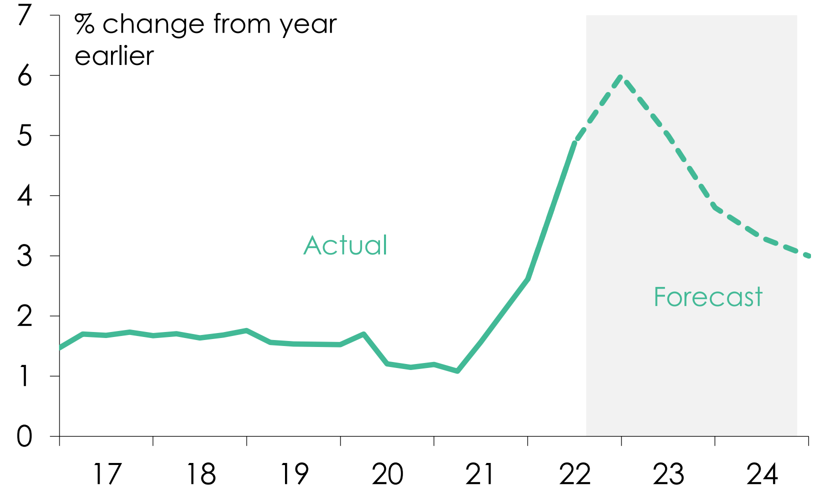
Employment



Wage price index



'Underlying' inflation



Source: Reserve Bank of Australia, *Statement on Monetary Policy*, 5th August.

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Although the RBA is a lot more 'transparent' than it used to be, there is still considerable room for improvement

- **Why doesn't the RBA publish the data behind all the charts in its *Statements on Monetary Policy* in spreadsheet form on its website – as many other central banks do?**

Bank of England

Home / Monetary Policy Report - August 2022

Monetary Policy Report - August 2022

Downloads

Download the Monetary Policy Report (PDF)

Download the chart slides and data (ZIP)

NORGES BANK

MONETARY POLICY REPORT

Number: 2/2022

Monetary Policy Report 2/22 (pdf)

Data for charts in MPR 2/22 (xlsx)

Data for annex in MPR 2/22 (xlsx)

Reserve Bank of New Zealand
Te Pūtea Matua

Monetary Policy Statement May 2022

Data for the May 2022 MPS XLSX 496.76 KB

May 2022 Monetary Policy Statement briefing PDF 3.22 MB

Monetary Policy Statement Snapshots May 2022 PDF 162.13 KB

BANCO CENTRAL DO BRASIL

Inflation report

Thursday, 24 | Statistical annex - 880.7 Kb

CNB CZECH NATIONAL BANK

Monetary Policy Report – Spring 2022

Chartbook and underlying data

» Underlying data – Monetary Policy Report (xlsx, 262 kB)

» Underlying data – Chartbook (xlsx, 573 kB)

» Underlying data – Boxes (xlsx, 490 kB)

BANK OF KOREA

Monetary Policy Report (June 2022)

Monetary Policy Report (June 2022).pdf

Data sets for figures_June 2022.xlsx

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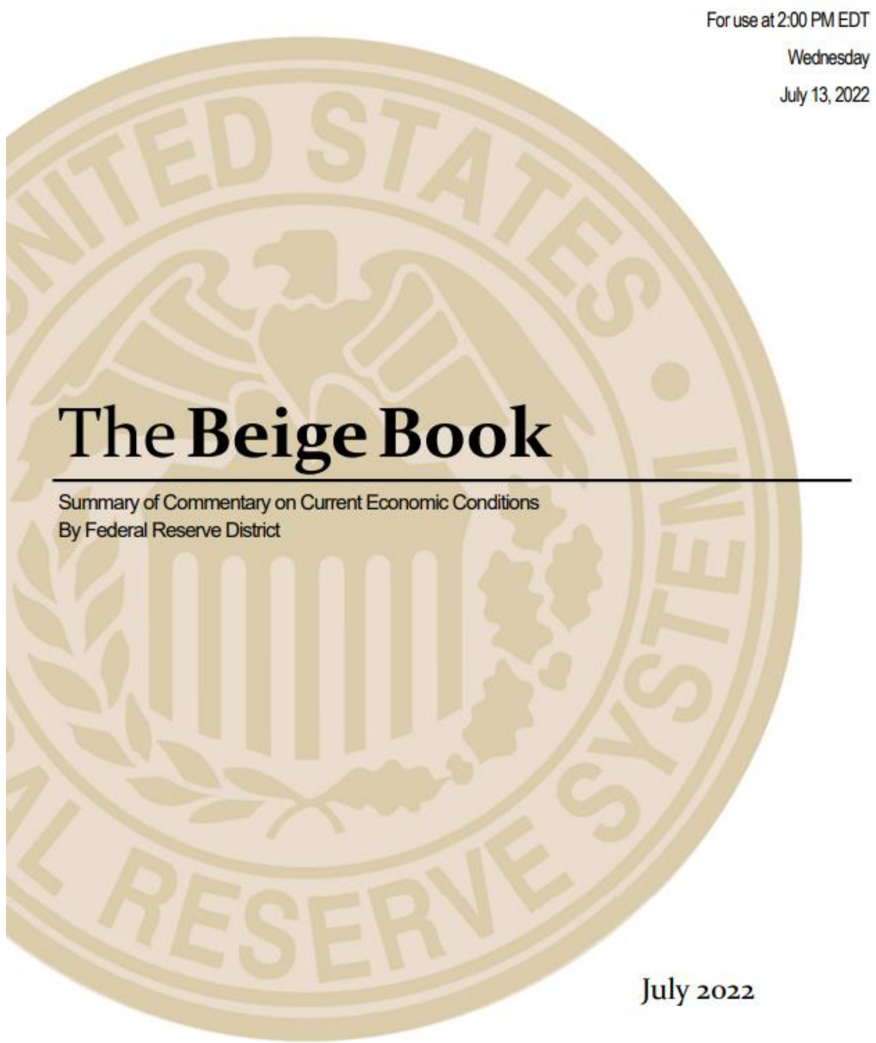
Although the RBA is a lot more ‘transparent’ than it used to be, there is still considerable room for improvement

- **Why doesn’t the RBA publish the results of its ‘business liaison program’ – as many other central banks do with their equivalents?**



Bank of England

Agents' summary of business conditions - 2022 Q2

We regularly publish a summary of reports compiled by our twelve regional Agents following discussions with at least 700 businesses across the UK every reporting period.

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BANQUE DU CANADA

Business Outlook Survey—Second Quarter of 2022

Business Outlook Survey Data

Each quarter, the Business Outlook Survey results are based on interviews with senior management of about 100 firms. You can view the latest quarterly data and download all available data. You can also find four quarter moving average data by **firm size**, **region** and **sector**.

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Although the RBA is a lot more 'transparent' than it used to be, there is still considerable room for improvement

- Why does the RBA publish so little (timely) information about the composition of its balance sheet compared with other central banks?

Published each Friday afternoon

A1 RESERVE BANK OF AUSTRALIA - LIABILITIES AND ASSETS - SUMMARY										
Title	Capital and Reserve Bank Reserve Fund	Notes on issue	Exchange settlement balances	Deposits (excluding Exchange Settlement balances)	Other liabilities	Total liabilities	Gold and foreign exchange	Australian dollar investments	Other assets (including clearing items)	Total assets
Description	Capital and Re	Notes on issue	Exchange settl	Deposits (exclu	Other liabilities	Total RBA liabili	Gold and forei	Australian dollar	Other assets	Total RBA assets
Frequency	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly
Type	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original
Units	$ million									
Source	RBA									
Publication date	05-Aug-202									
Series ID	ARBALCRF									
4-May-2022	154									
11-May-2022	154									
18-May-2022	154									
25-May-2022	154									
1-Jun-2022	154									
8-Jun-2022	154									
15-Jun-2022	154									
22-Jun-2022	154									
29-Jun-2022	154									
6-Jul-2022	154									
13-Jul-2022	154									
20-Jul-2022	154									
27-Jul-2022	154									
3-Aug-2022	154									

Published with a lag of more than 3 months

A1 RESERVE BANK OF AUSTRALIA - LIABILITIES AND ASSETS - DETAILED																
Title	Capital and Reserve Bank Reserve Fund	Notes on issue	Exchange settlement balances	RBA term deposits	Deposits of overseas institutions	Australian Government Deposits	State Governments Deposits	Other Deposits	Other liabilities	Total liabilities	Gold and foreign exchange	Australian dollar investments	Loans and advances	Clearing items	Other assets	Total assets
Description	Capital and Re	Notes on issue	Exchange settl	RBA term depo	Deposits of ove	Australian Governr	State Governmen	Other Deposits	Other liabilities	Total RBA liabili	Gold and forei	Australian dollar	Loans and ad	Clearing item	Other assets;	Total RBA assets
Frequency	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly	Weekly
Type	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original	Original
Units	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million	$ million
Source	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA	RBA
Publication date	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022	05-Aug-2022
Series ID	ARBALCRFW	ARBALNOIW	ARBALESBW	ARBALRTDW	ARBALDOOIW	ARBALDOGIAGW	ARBALDOGISW	ARBALDOOW	ARBALOLW	ARBALTLW	ARBAAGFXW	ARBAAASTW	ARBAALAW	ARBAACIW	ARBAAOAW	ARBAATAW
2-Feb-2022	15406	102425	443415	0	20537	40792	76	0	21264	643915	74792	567206	1	457	1459	643915
9-Feb-2022	15406	102281	444675	0	29102	38004	373	0	17213	647054	75891	568950	1	755	1457	647054
16-Feb-2022	15406	102112	452896	0	23614	35542	193	1	14886	644650	74949	567804	1	425	1471	644650
23-Feb-2022	15406	101960	442566	0	24432	45274	155	0	12203	641996	73511	566167	1	849	1468	641996
2-Mar-2022	15406	101815	442668	0	19195	52152	31	0	16183	647450	74177	571342	1	479	1451	647450
9-Mar-2022	15406	101835	437967	0	28344	48839	607	1	7168	640167	72465	565470	1	794	1437	640167
16-Mar-2022	15406	101890	442737	0	25475	46789	365	1	5794	638457	72735	563787	1	476	1458	638457
23-Mar-2022	15406	101949	421467	0	31110	60988	181	0	-1351	629750	70923	556588	1	802	1436	629750
30-Mar-2022	15406	101997	436252	0	19863	55362	69	0	-601	628348	72145	554324	1	451	1427	628348
6-Apr-2022	15406	102302	436483	0	17945	57152	48	0	-8178	621158	68416	550561	0	763	1418	621158
13-Apr-2022	15406	102615	441143	0	19958	48152	713	0	-6292	621695	70881	548891	0	483	1440	621695
20-Apr-2022	15406	102547	431189	0	11765	68872	322	2	-9657	620446	69253	548828	0	933	1432	620446
27-Apr-2022	15406	102499	426998	0	12846	68368	95	0	-5162	621050	72882	545961	0	759	1448	621050

- The RBA does publish details of its holdings of Commonwealth and State & Territory government securities once a month

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Although the RBA is a lot more 'transparent' than it used to be, there is still considerable room for improvement

- Other central banks such as the Fed publish much more detail about their balance sheets every week

H.4.1

Factors Affecting Reserve Balances of Depository Institutions and Condition Statement of Federal Reserve Banks

August 4, 2022

1. Factors Affecting Reserve Balances of Depository Institutions

Millions of dollars

Reserve Bank credit, related items, and reserve balances of depository institutions at Federal Reserve Banks	Averages of daily figures			Wednesday Aug 3, 2022
	Week ended Aug 3, 2022	Change from week ended		
		Jul 27, 2022	Aug 4, 2021	
Reserve Bank credit	8,847,741	- 18,258	+ 659,077	8,838,997
Securities held outright[1]	8,447,773	- 16,560	+ 790,576	8,439,018
U.S. Treasury securities	5,727,943	- 5,814	+ 457,879	5,719,119
Bills[2]	326,044	0	0	326,044
Notes and bonds, nominal[2]	4,933,455	- 7,004	+ 396,108	4,924,116
Notes and bonds, inflation-indexed[2]	374,719	0	+ 25,434	374,719
Inflation compensation[3]	93,725	+ 1,190	+ 36,337	94,240
Federal agency debt securities[2]	2,347	0	0	2,347
Mortgage-backed securities[4]	2,717,483	- 10,746	+ 332,698	2,717,552
Unamortized premiums on securities held outright[5]	330,302	- 877	- 22,356	330,094
Unamortized discounts on securities held outright[5]	-25,935	- 44	- 11,260	-25,938
Repurchase agreements[6]	1	+ 1	+ 1	0
Foreign official	0	0	0	0
Others	1	+ 1	+ 1	0
Loans	19,029	- 671	- 65,602	18,862
Primary credit	2,806	- 259	+ 2,469	2,731
Secondary credit	0	0	- 1	0
Seasonal credit	17	+ 6	+ 3	24
Primary Dealer Credit Facility	0	0	0	0
Paycheck Protection Program Liquidity Facility	16,205	- 418	- 68,074	16,107
Other credit extensions	0	0	0	0
Net portfolio holdings of Corporate Credit Facilities LLC[7]	0	0	- 22,657	0
Net portfolio holdings of MS Facilities LLC (Main Street Lending Program)[7]	26,119	+ 79	- 4,426	26,138
Net portfolio holdings of Municipal Liquidity Facility LLC[7]	5,548	+ 2	- 4,214	5,549
Net portfolio holdings of TALF II LLC[7]	2,160	- 21	- 2,378	2,157
Float	-467	- 281	- 143	-171
Central bank liquidity swaps[8]	213	+ 7	- 265	213
Other Federal Reserve assets[9]	42,999	+ 108	+ 1,802	43,076
Foreign currency denominated assets[10]	18,003	+ 211	- 3,358	17,877
Gold stock	11,041	0	0	11,041
Special drawing rights certificate account	5,200	0	0	5,200
Treasury currency outstanding[11]	51,216	+ 14	+ 582	51,216
Total factors supplying reserve funds	8,933,201	- 18,032	+ 656,301	8,924,330

Note: Components may not sum to totals because of rounding. Footnotes appear at the end of the table.

H.4.1

1. Factors Affecting Reserve Balances of Depository Institutions (continued)

Millions of dollars

Reserve Bank credit, related items, and reserve balances of depository institutions at Federal Reserve Banks	Averages of daily figures			Wednesday Aug 3, 2022
	Week ended Aug 3, 2022	Change from week ended		
		Jul 27, 2022	Aug 4, 2021	
Currency in circulation[11]	2,274,415	- 37	+ 87,429	2,275,786
Reverse repurchase agreements[12]	2,516,245	+ 9,355	+1,256,151	2,447,840
Foreign official and international accounts	281,871	- 6,523	+ 2,917	265,602
Others	2,234,374	+ 15,879	+1,253,234	2,182,238
Treasury cash holdings	104	+ 5	+ 56	101
Deposits with F.R. Banks, other than reserve balances	816,656	- 28,100	+ 82,544	791,735
Term deposits held by depository institutions	0	0	0	0
U.S. Treasury, General Account	594,115	- 8,830	+ 101,447	566,577
Foreign official	8,604	- 562	+ 2,493	9,695
Other[13]	213,937	- 18,707	- 21,396	215,464
Treasury contributions to credit facilities[14]	17,940	0	- 22,338	17,940
Other liabilities and capital[15]	48,829	- 1,393	- 975	48,412
Total factors, other than reserve balances, absorbing reserve funds	5,674,189	- 20,170	+1,402,867	5,581,813
Reserve balances with Federal Reserve Banks	3,259,011	+ 2,136	- 746,567	3,342,517

Note: Components may not sum to totals because of rounding.

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Although the RBA is a lot more 'transparent' than it used to be, there is still considerable room for improvement

- Other central banks such as the ECB publish much more detail about their balance sheets every week

1.1 Consolidated financial statement of the Eurosystem

1.1.1 Assets
(EUR millions)

	1 July 2022	8 July 2022	15 July 2022	22 July 2022	29 July 2022
Gold and gold receivables	604,274	604,274	604,275	604,273	604,273
Claims on non-euro area residents in foreign currency	519,276	519,014	519,473	520,267	521,097
Claims on euro area residents in foreign currency	26,911	27,505	26,954	26,319	25,698
Claims on non-euro area residents in euro	11,562	10,317	10,336	10,230	10,313
Lending to euro area credit institutions in euro	2,126,085	2,125,648	2,125,519	2,125,580	2,125,795
Main refinancing operations	1,483	1,041	916	976	1,077
Longer-term refinancing operations	2,124,603	2,124,603	2,124,603	2,124,603	2,124,718
Fine-tuning reverse operations	0	0	0	0	0
Structural reverse operations	0	0	0	0	0
Marginal lending facility	0	4	0	1	0
Credits related to margin calls	0	0	0	0	0
Other claims on euro area credit institutions in euro	34,469	28,433	28,802	27,557	30,794
Securities of euro area residents in euro	5,129,109	5,122,977	5,119,252	5,123,301	5,125,630
Securities held for monetary policy purposes	4,963,479	4,956,883	4,953,862	4,956,687	4,958,861
Other securities	165,629	166,094	165,390	166,614	166,769
General government debt in euro	21,677	21,677	21,677	21,677	21,680
Other assets	315,399	314,568	309,398	309,082	299,199
Total assets	8,788,761	8,774,413	8,765,687	8,768,286	8,764,480

Source: ECB.

1.1.2 Liabilities
(EUR millions)

	1 July 2022	8 July 2022	15 July 2022	22 July 2022	29 July 2022
Banknotes in circulation	1,603,570	1,606,447	1,608,685	1,606,761	1,600,872
Liabilities to euro area credit institutions in euro	4,591,783	4,642,804	4,622,903	4,605,124	4,568,576
Current accounts (covering the minimum reserve system)	3,853,327	3,914,718	3,910,299	3,904,414	3,855,461
Deposit facility	736,337	726,026	710,260	698,545	711,059
Fixed-term deposits	0	0	0	0	0
Fine-tuning reverse operations	0	0	0	0	0
Deposits related to margin calls	2,118	2,061	2,343	2,165	2,056
Other liabilities to euro area credit institutions in euro	71,008	55,928	49,823	50,945	60,534
Debt certificates issued	0	0	0	0	0
Liabilities to other euro area residents in euro	835,002	819,916	835,291	843,514	844,168
Liabilities to non-euro area residents in euro	433,962	396,518	397,159	412,133	442,153
Liabilities to euro area residents in foreign currency	11,531	11,440	11,470	11,274	11,487
Liabilities to non-euro area residents in foreign currency	6,195	6,136	5,864	5,997	5,725
Counterpart of special drawing rights allocated by the IMF	184,896	184,896	184,896	184,896	184,896
Other liabilities	327,456	326,970	326,239	324,284	322,710
Revaluation accounts	608,538	608,538	608,538	608,538	608,538
Capital and reserves	114,820	114,819	114,819	114,819	114,820
Total liabilities	8,788,761	8,774,413	8,765,687	8,768,286	8,764,480

Source: ECB.

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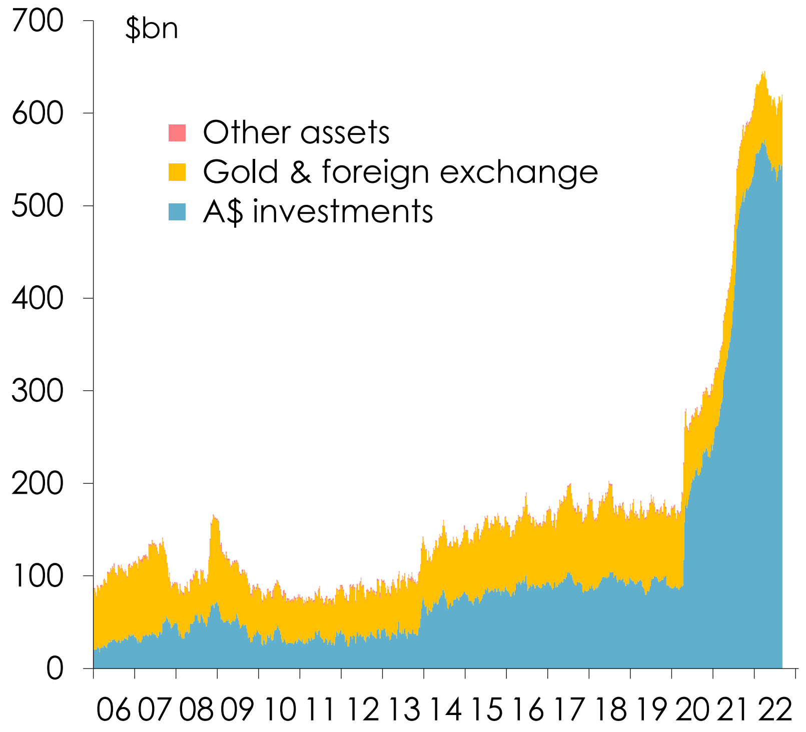
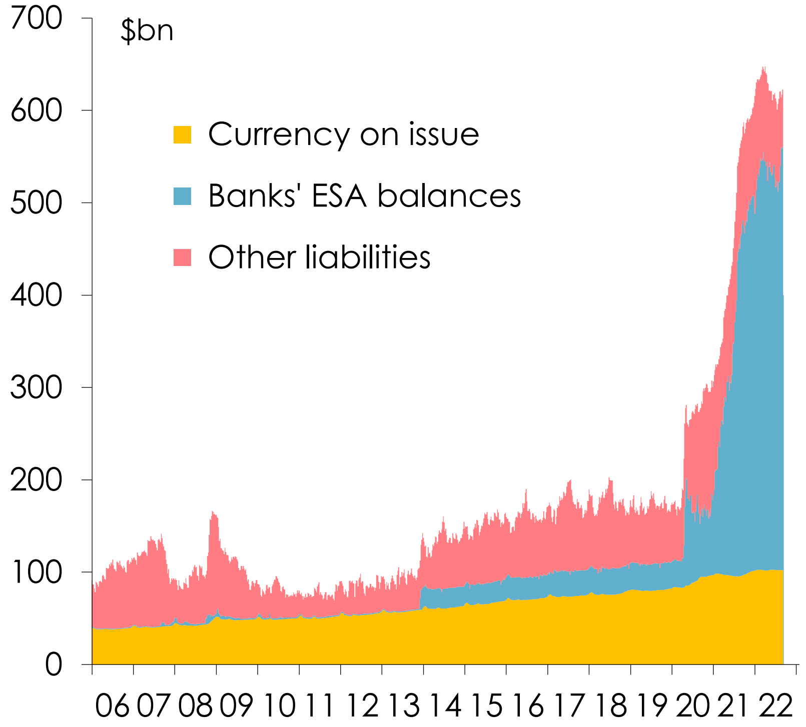
The RBA's 'QE' has left it exposed to much higher interest payments on the banks' ESA balances – which may wipe out its capacity to pay dividends

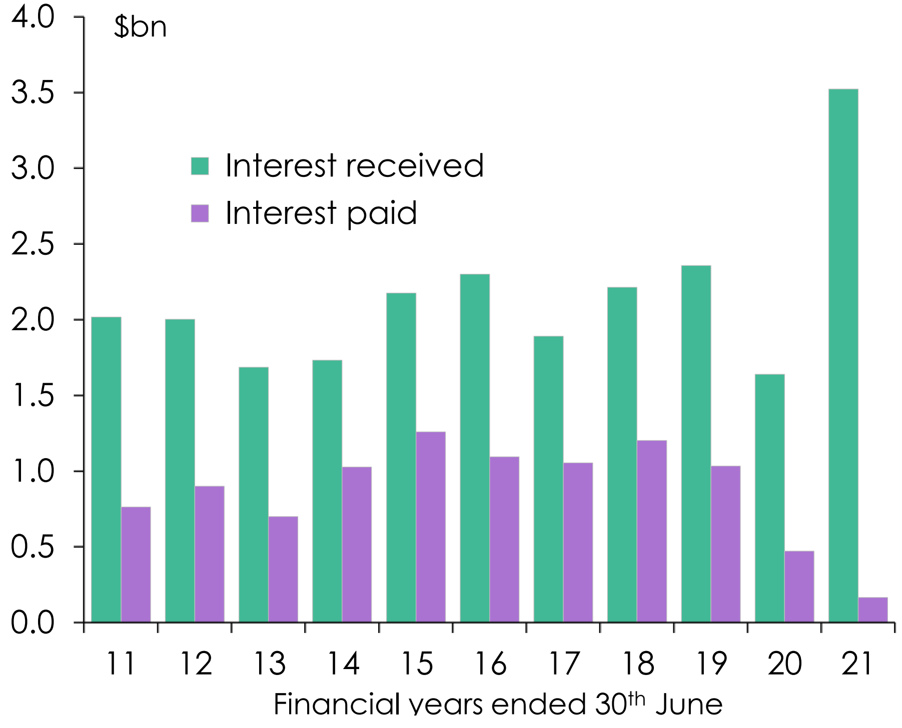
RBA assets



RBA liabilities



RBA interest receipts & payments

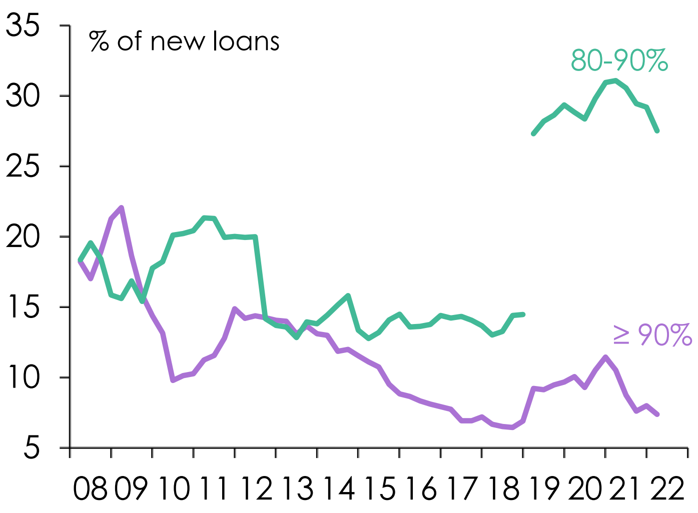


- **From the standpoint of the public sector as a whole, 'quantitative easing' has entailed the substitution of floating- rate debt (the banks' ESA balances at the RBA) for fixed-rate debt (bonds)**
- **When the cash rate was 0.1%, the banks ESA balances were in effect 'free money' for the RBA (which 'created' it)**
- **But with the cash rate at 1.85% pa the RBA would be paying the banks ~ $8bn pa in interest on $459bn of ESA balances**
- **If the cash rate gets to (say) 3% then the RBA could be paying upwards of $10bn pa to the banks in interest, depending on how rapidly its balance sheet (and hence the banks' ESA balances) shrink**
- **Whereas the interest the RBA receives on its holdings of bonds won't be going up**

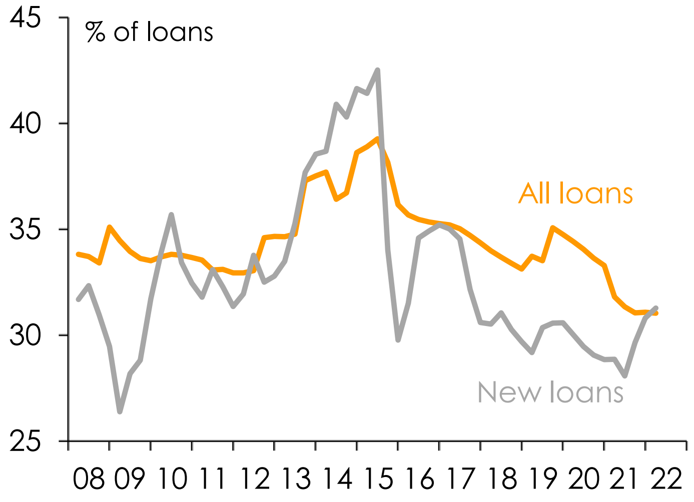
Sources: RBA Statistical Table A1, and Annual Reports.

The RBA Review will look at the interaction between monetary and 'macro-prudential' policy – but not at who should conduct it

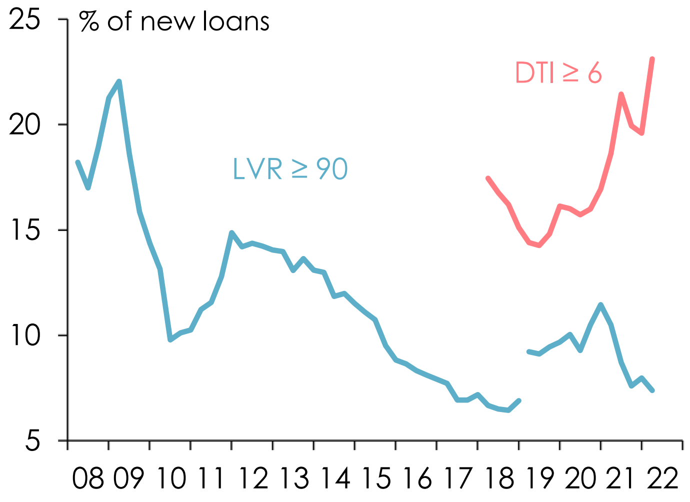
High-LVR mortgages



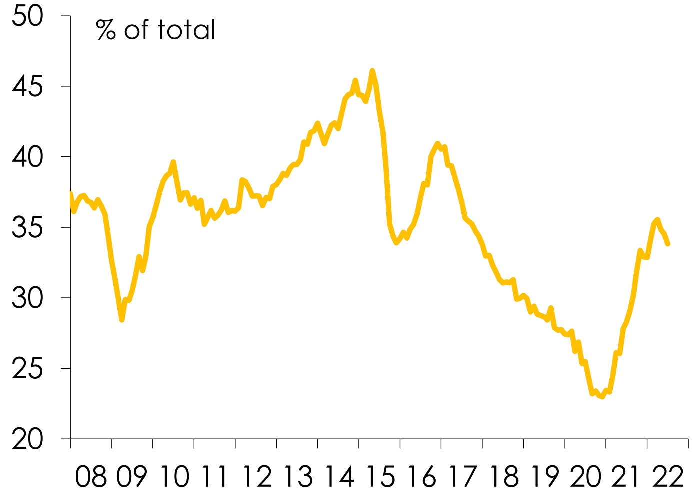
Number of loans to investors



High LVR & DTI mortgages



Investor share of new mortgages



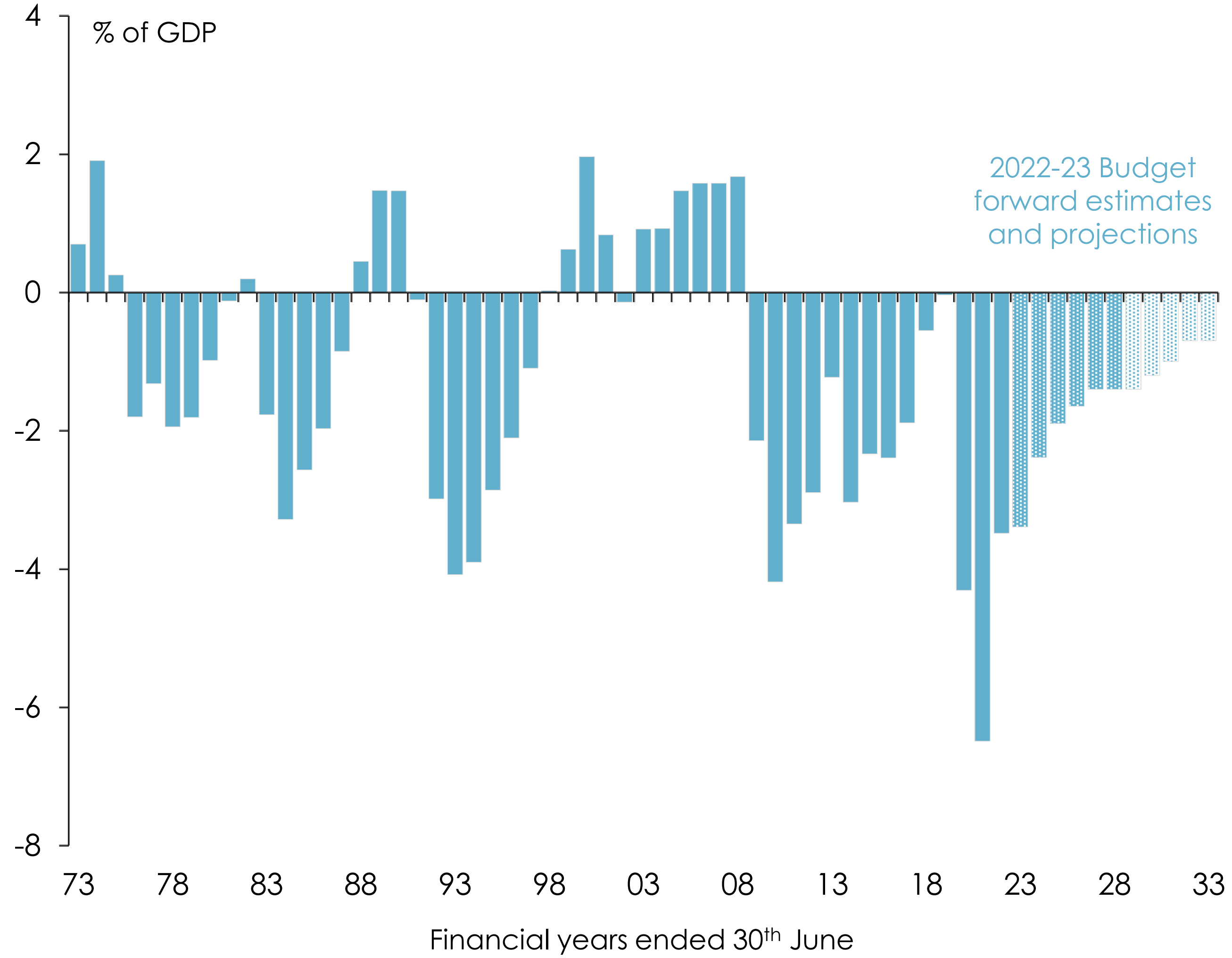
- The Terms of Reference for the Review of the RBA "include Australia's macroprudential governance arrangements, but exclude APRA's statutory role or functions"
- Was the RBA unwilling to cut interest rates between mid-2016 and mid-2019 – despite inflation being persistently below its target range, and unemployment remaining stubbornly above 5% - because of 'financial stability' concerns?
  - ie that cutting interest rates during this period might have resulted in another surge in house prices?
- Why did APRA do nothing to moderate or dampen the impact of ultra-low interest rates on 'risky' lending (eg at high LVR or DTI ratios), or to restrain growth in lending to property investors – as it had successfully done in the first half of the 2010s?
- Does APRA have the same independence from government in deploying 'macro-prudential' policy instruments as the RBA does in implementing monetary policy?
- Unfortunately the Review seems to have been precluded from revisiting the separation of APRA from the RBA

Sources: APRA, *Quarterly authorised deposit-taking institution statistics*; ABS, *Lending Indicators*.

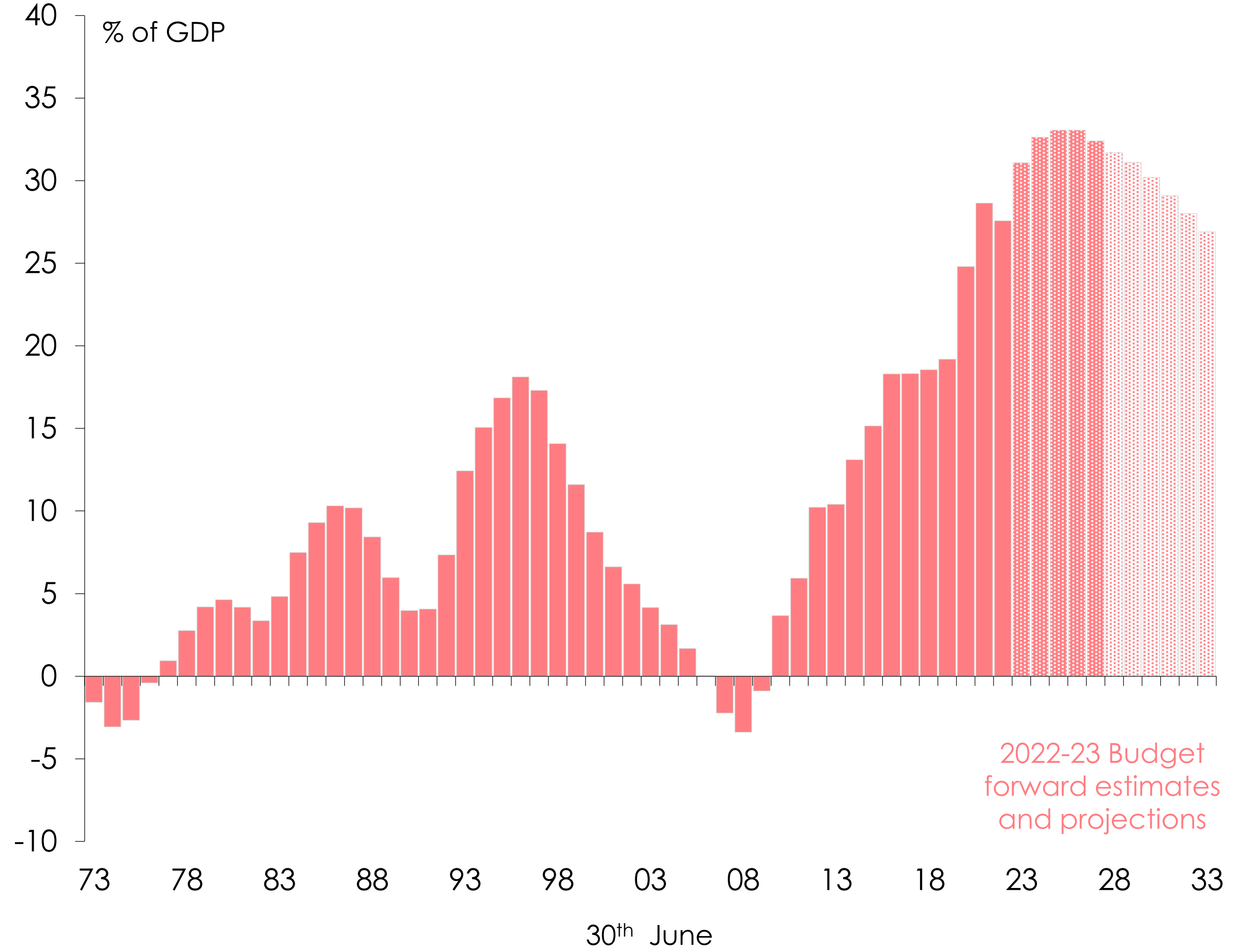
The new Federal Government has a significant medium-term challenge in putting the budget on a more sustainable footing

'Medium-term' projections of the 'underlying cash balance' and net debt

'Underlying' cash balance



Net debt



Source: Australian Government, 2022-23 Budget Paper No. 1, Statement No. 3 and Statement No. 10, 29th March 2022. Return to "What's New".

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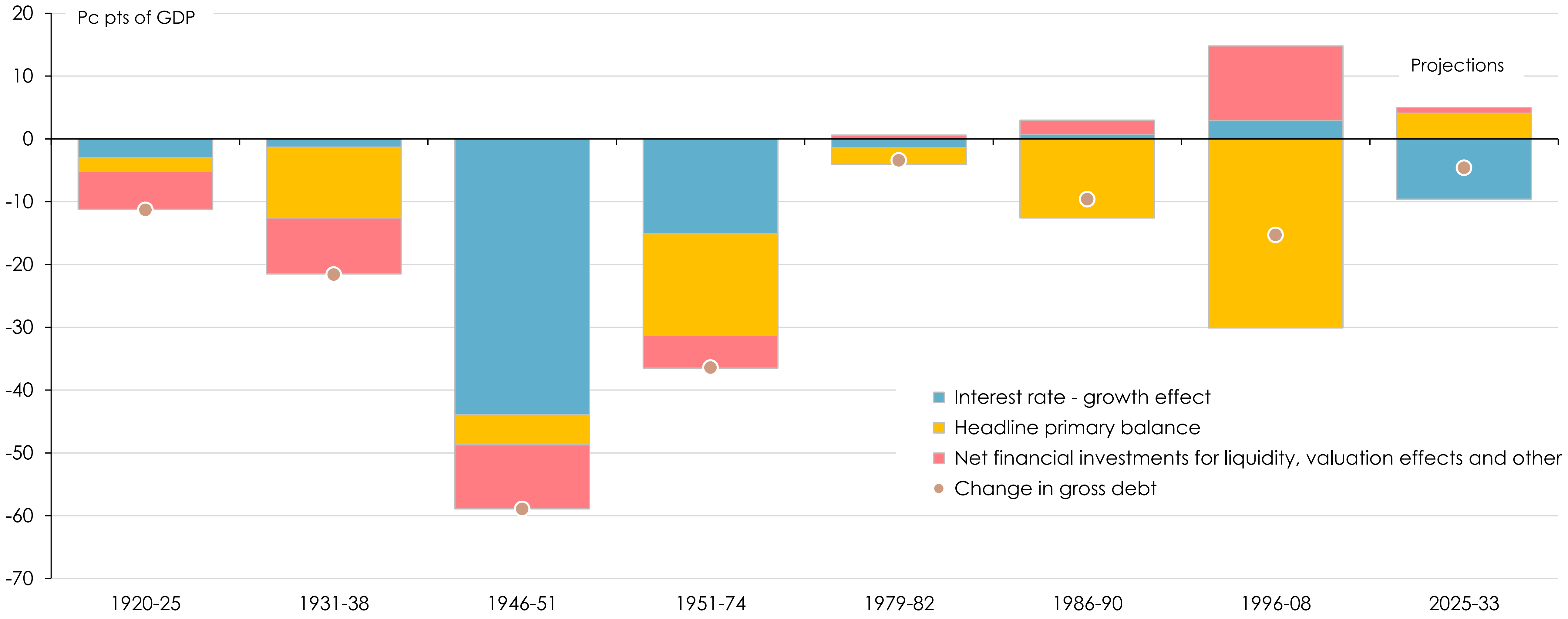
Current projections of declining debt-to-GDP rely solely on interest rates being less than GDP growth, with no contribution from budget surpluses

Sources of reductions in Federal Government gross debt as a pc of GDP during previous episodes of debt reduction, compared with projections for the period 2025 (when debt is currently forecast to peak) and 2033



Note: Data are in financial years. Debt excludes issuance for the states. The contribution of interest rates less growth captures the combined direct effect of the former increasing debt and of the latter growing GDP, but not their effects on the headline *primary balance* (the budget balance excluding interest payments). *Source:* Steven Kennedy (Secretary to the Treasury), *Post-Budget economic briefing - opportunities and risks*, address to Australian Business Economists, 8th June 2022.

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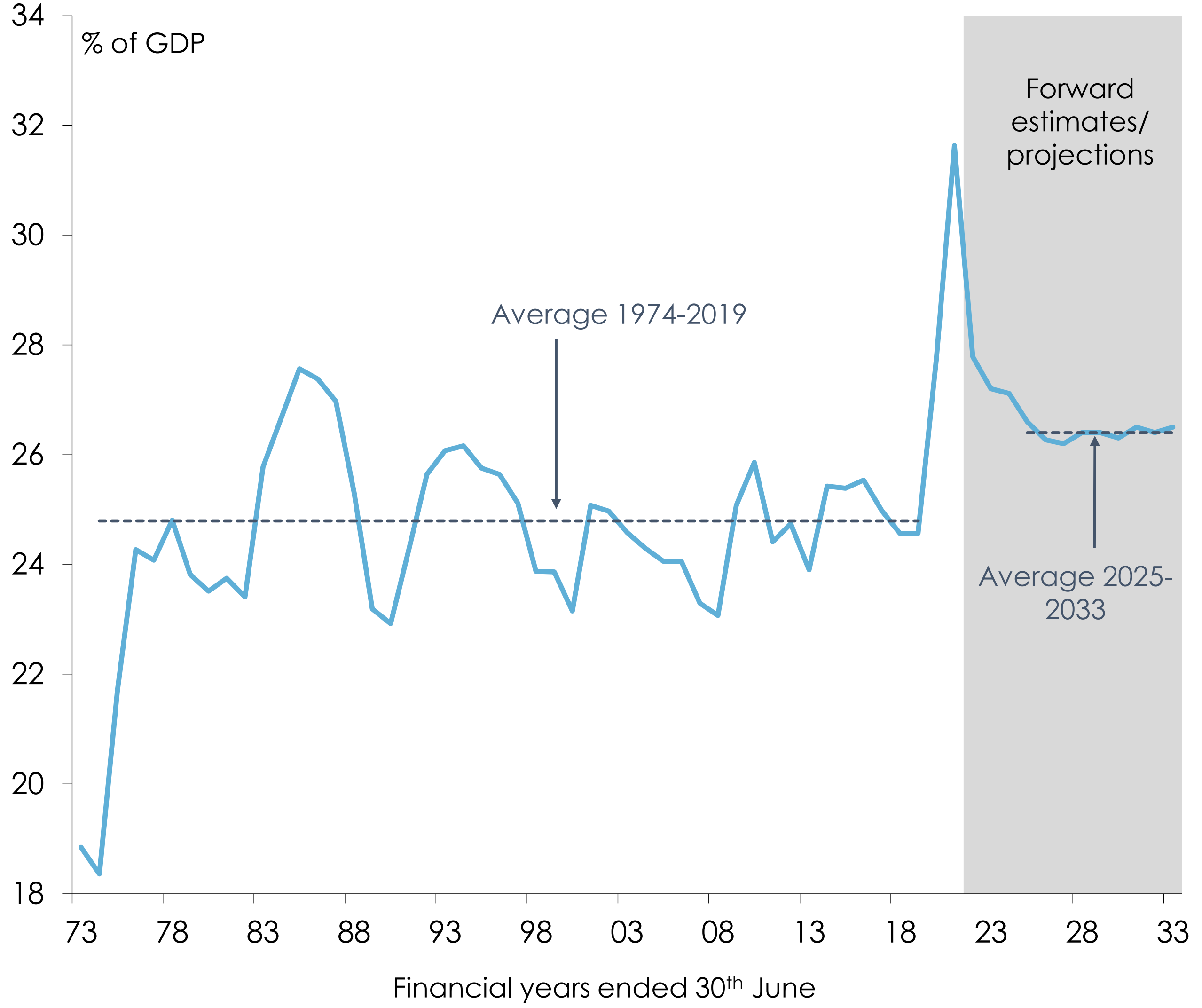
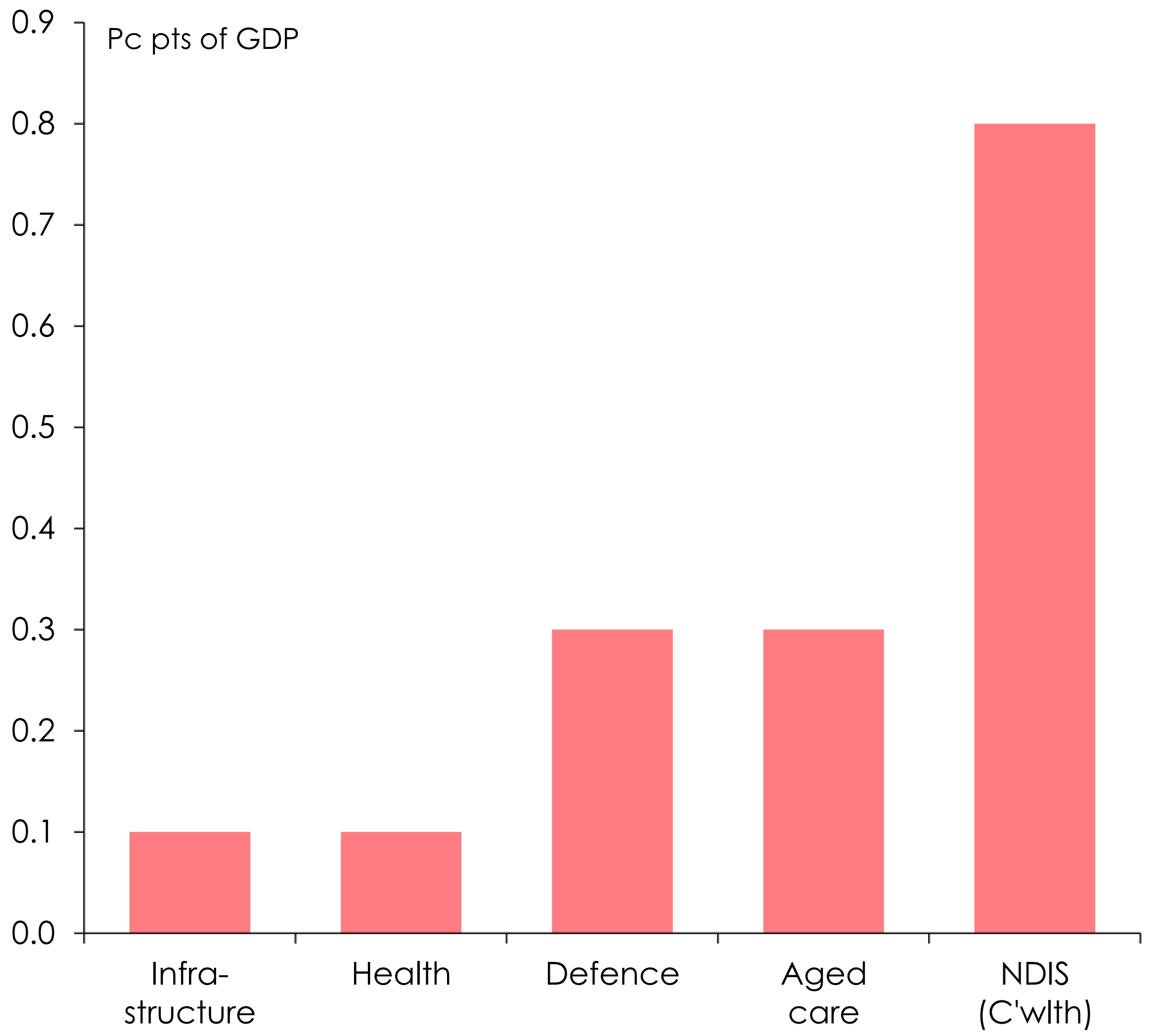
Federal Government spending seems likely to be around 1½ pc pts of GDP higher over the next decade than over the five decades

'Underlying' cash payments as a pc of GDP



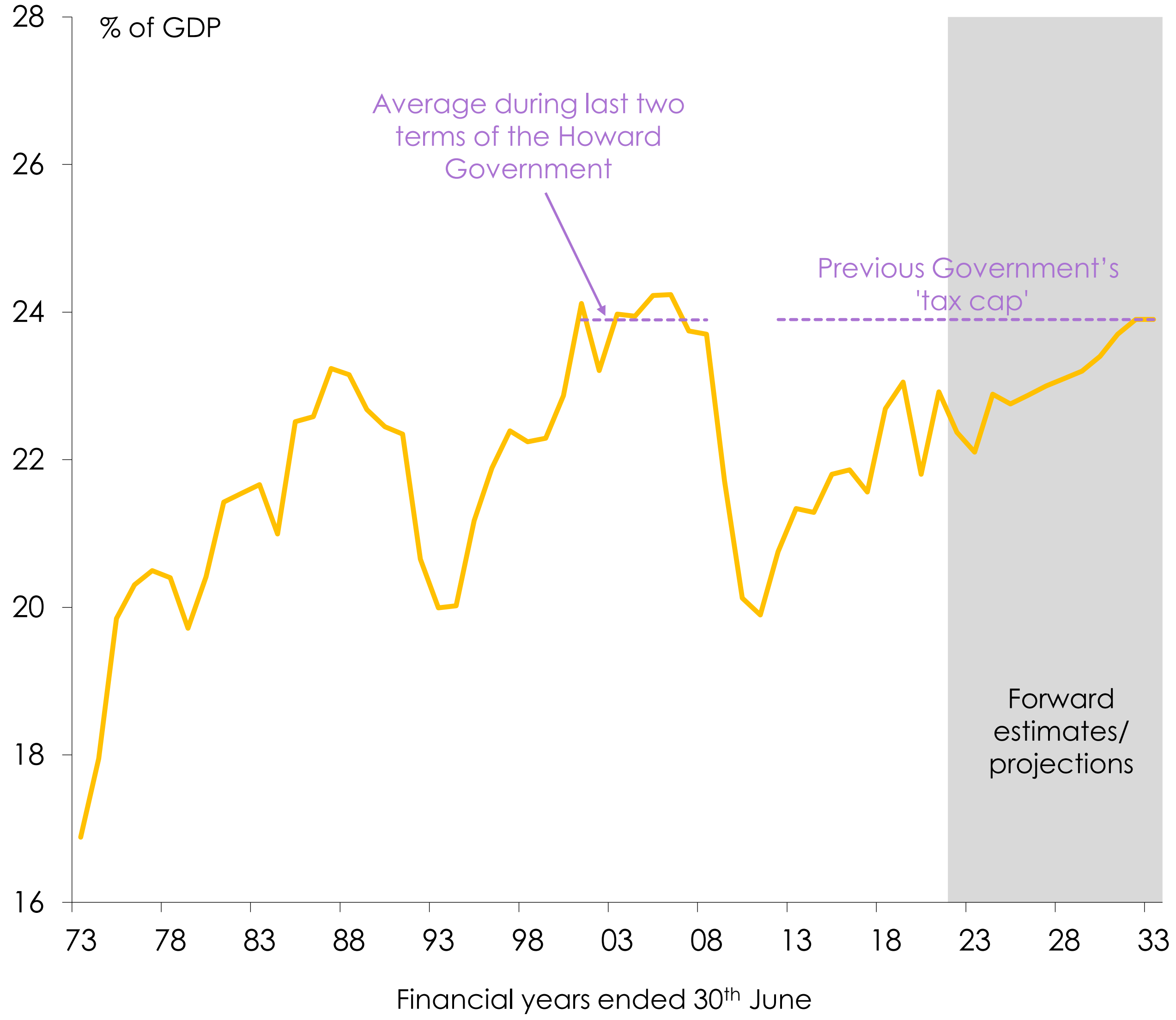
Changes in payments between 2018-19 and 2025-26



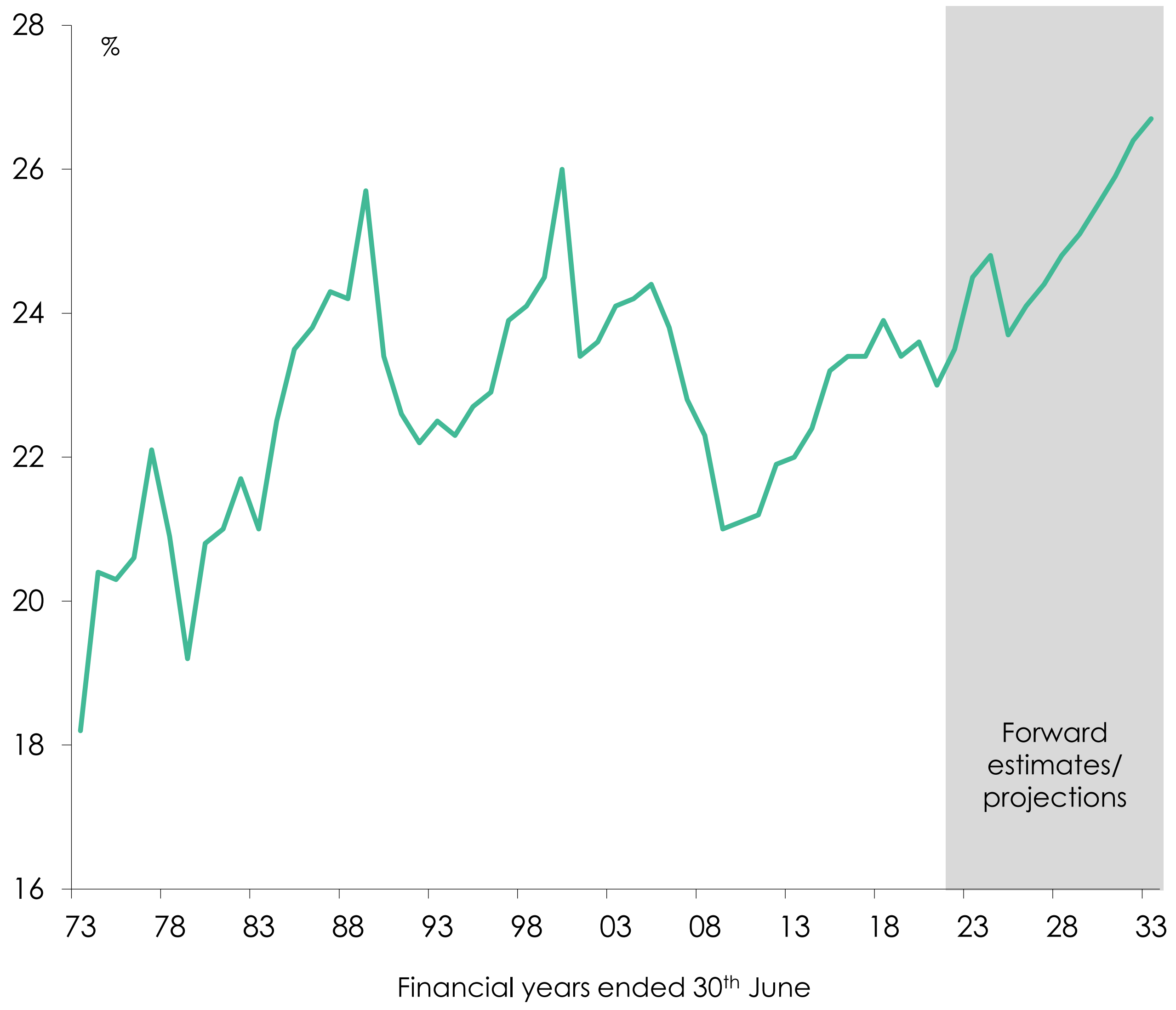
Sources: Australian Government, 2022-23 *Budget Paper No. 1, Statement No. 3* and *Statement No. 10*, 29th March 2022 ; and Steven Kennedy (Secretary to the Treasury), *Post-Budget economic briefing - opportunities and risks*, address to Australian Business Economists, 8th June 2022.

Much of the 'budget repair' task will need to be accomplished from the revenue side – ideally through tax reform, not via 'bracket creep'

Taxation receipts as a pc of GDP



Average personal income tax rate



Sources: Australian Government, 2022-23 *Budget Paper No. 1, Statement No. 3* and *Statement No. 10*, 29th March 2022 ; and Steven Kennedy (Secretary to the Treasury), *Post-Budget economic briefing - opportunities and risks*, address to Australian Business Economists, 8th June 2022.

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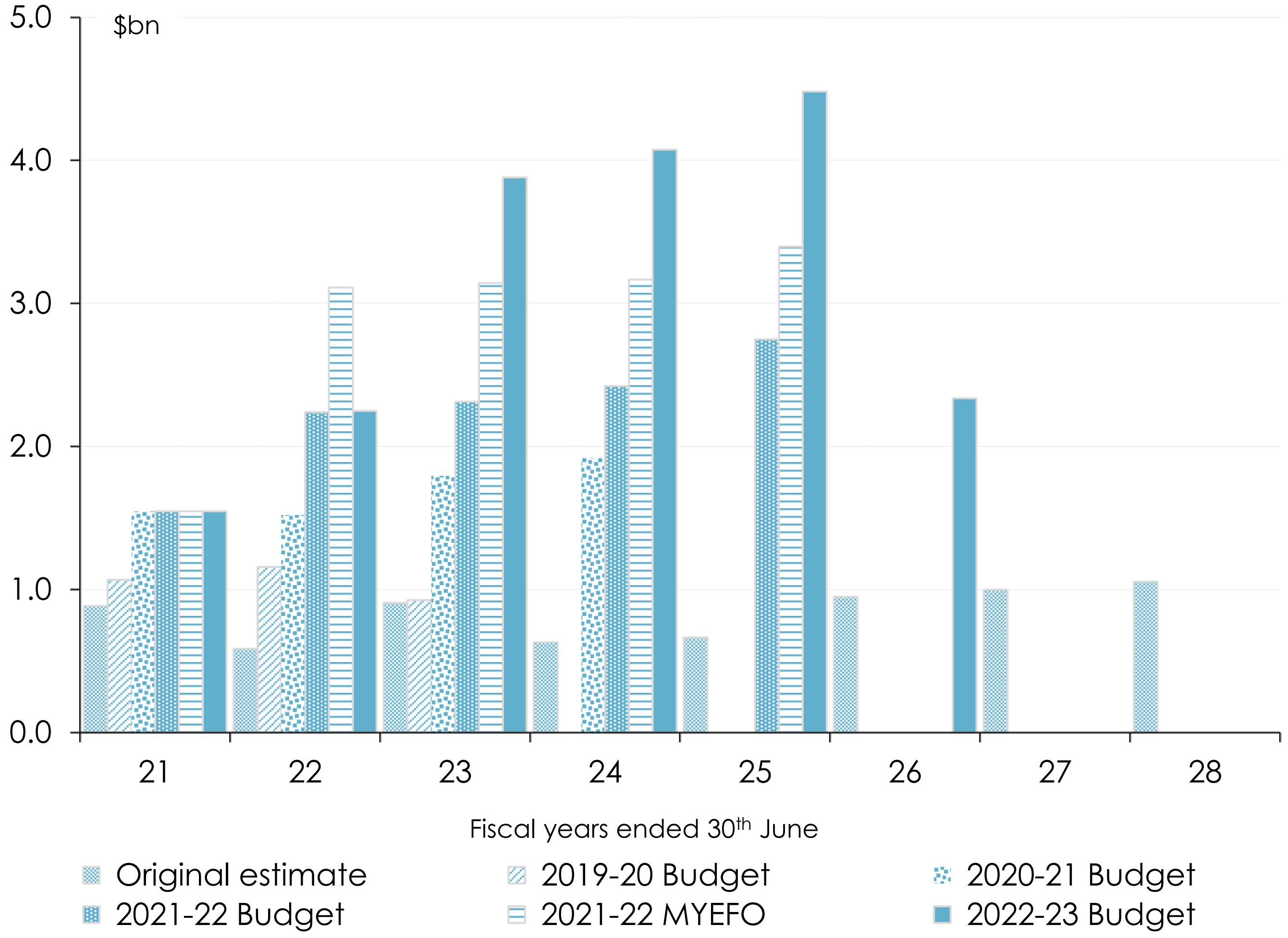
A useful contribution to the budget repair task would ideally come from unpicking one of the worst public policy decisions of the past 20 years

Successive estimates of the cost to the Federal Budget of the 'transition' to the new GST revenue-sharing arrangements 'agreed to' in 2018



- **The 2022-23 Budget Papers put the cost to the Federal Budget of the 'deal' imposed on the states and territories in 2018, in order to appease Western Australia's demands for larger share of GST revenues than it was 'entitled' to under the long-standing principles hitherto used by the Grants Commission to recommend how that revenue should be distributed among the states and territories, at $18.6bn over the six years to 2025-26**
  - this is four times the original estimate of $4.6bn
  - because the iron ore price has stayed much higher than assumed when the original estimate was made,
  - so the 'guarantee' that no other state would be worse off while WA never gets less than 70% of what it would have obtained under a notional 'equal per capita' distribution has become much more expensive
- **It's simply scandalous that the Federal Government has to add almost $20bn to its deficits in order to transfer a similar amount to the only government in Australia which is running budget surpluses**

Sources: Australian Government, *Interim response to Productivity Commission inquiry into horizontal fiscal equalization*, 5th July 2018; and 2022-23 *Budget Paper No. 3: Federal Financial Relations*, 29th March 2022.

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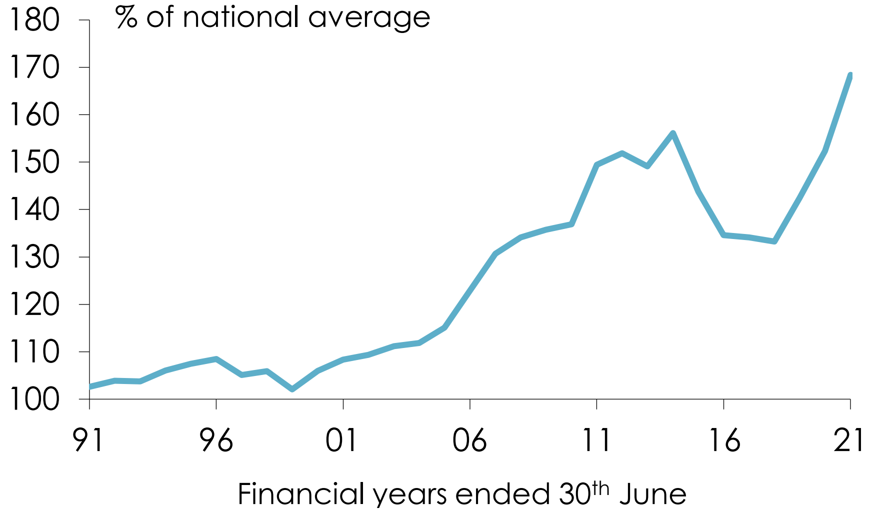
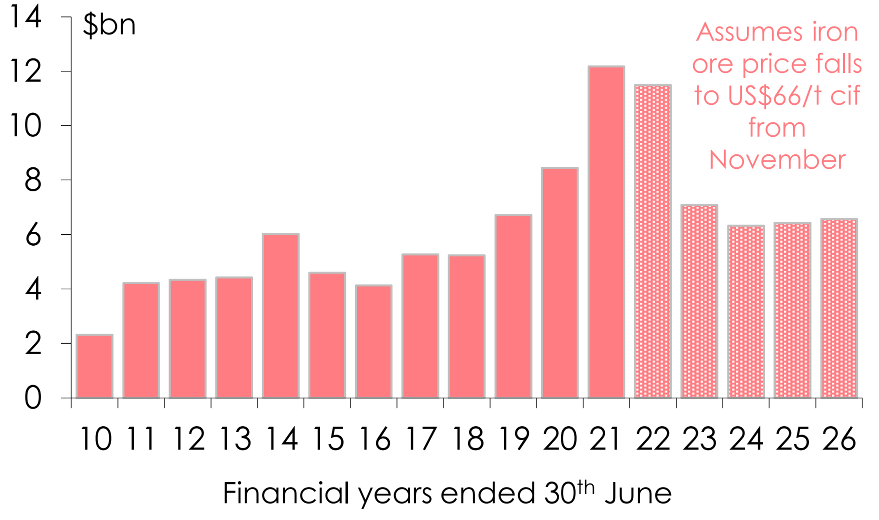
WA is Australia's richest state, by a bigger margin than NSW or Victoria ever were – it's swimming in revenue, and running budget surpluses

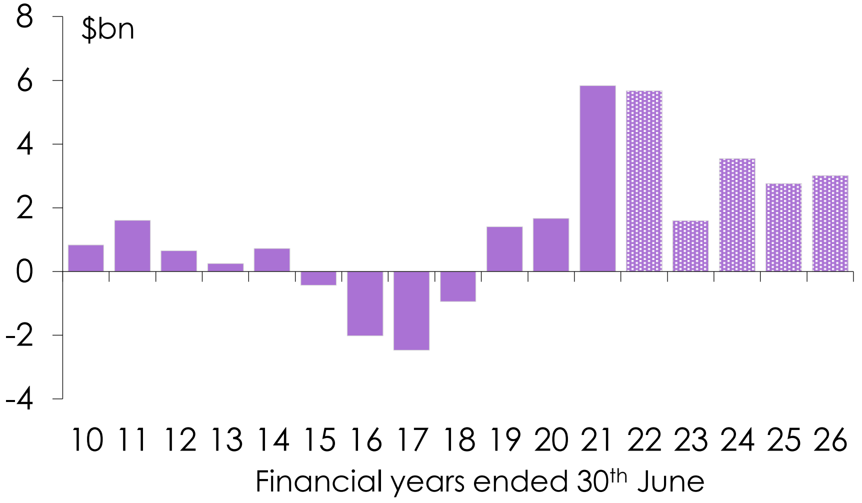
WA per capita GSP



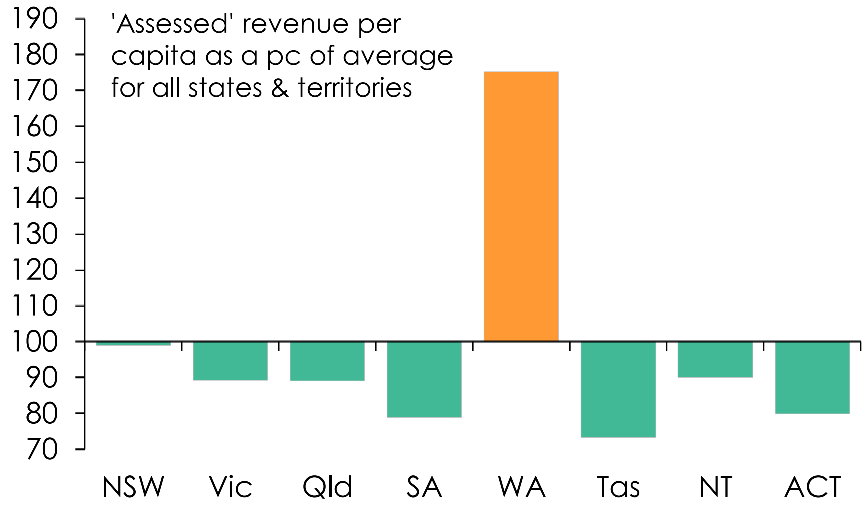
WA mineral royalty revenues



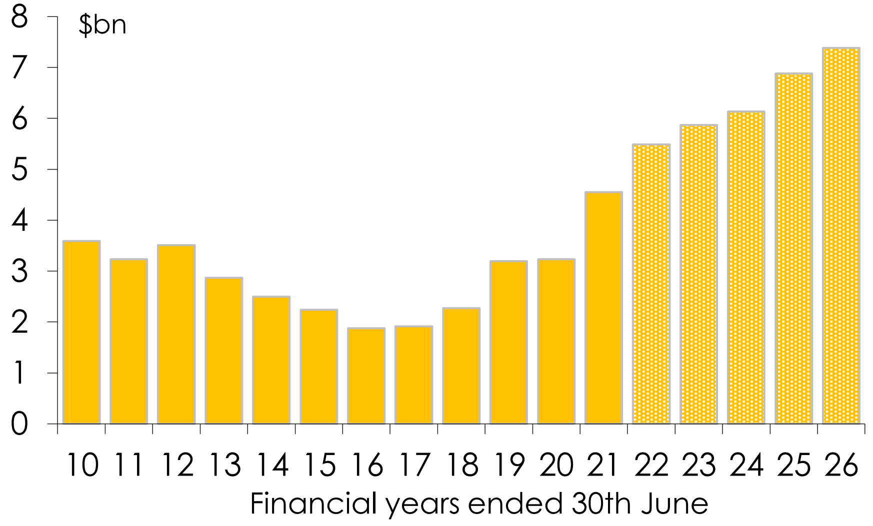
WA net operating balance



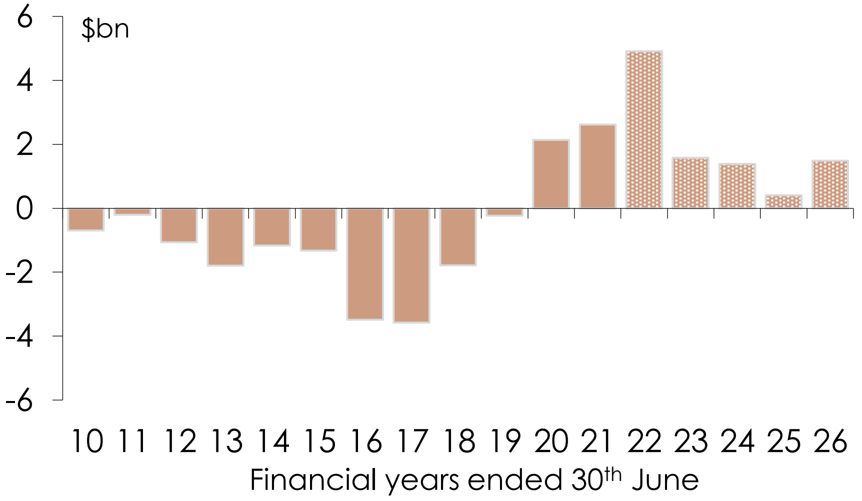
Revenue-raising capacity, 2019-20



WA GST revenues



WA cash balance



Sources: ABS, Australian National Accounts: State Accounts, 2020-21; Commonwealth Grants Commission, 2022 Update of GST relativities; Government of Western Australia, *2022-23 Budget Paper No 3 - Economic and Fiscal Outlook*.

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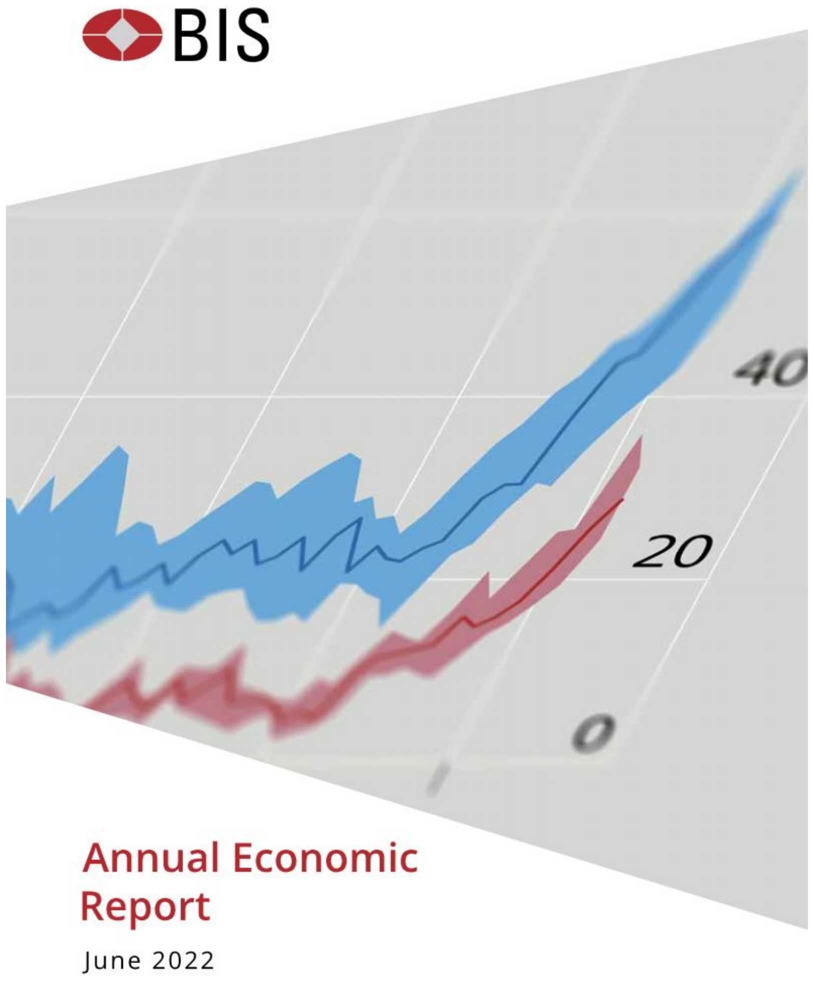
Sound advice from the Bank for International Settlements' (the "central bankers' central bank") latest Annual Report

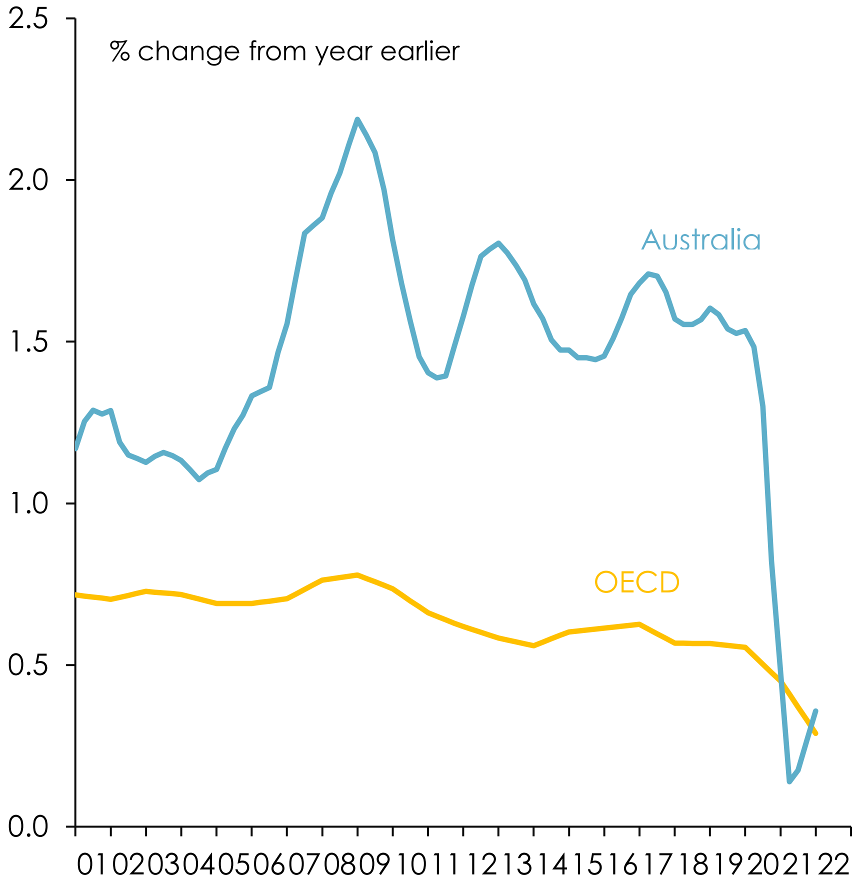


"For far too long, there has been a temptation to turn to fiscal and monetary policy to boost growth, regardless of the underlying causes of weakness. For fiscal policy, in particular, loosening during contractions has not given way to consolidation during expansions. The temptation to postpone adjustment has been too strong. Such a strategy has arguably generated unrealistic expectations and demands for further support …

[T]he only way of promoting robust long-term growth is to implement ambitious structural reforms. Unfortunately, such reforms have been flagging for too long".

In Australia's case, we've become increasingly dependent on population growth (through immigration) as a driver of economic growth

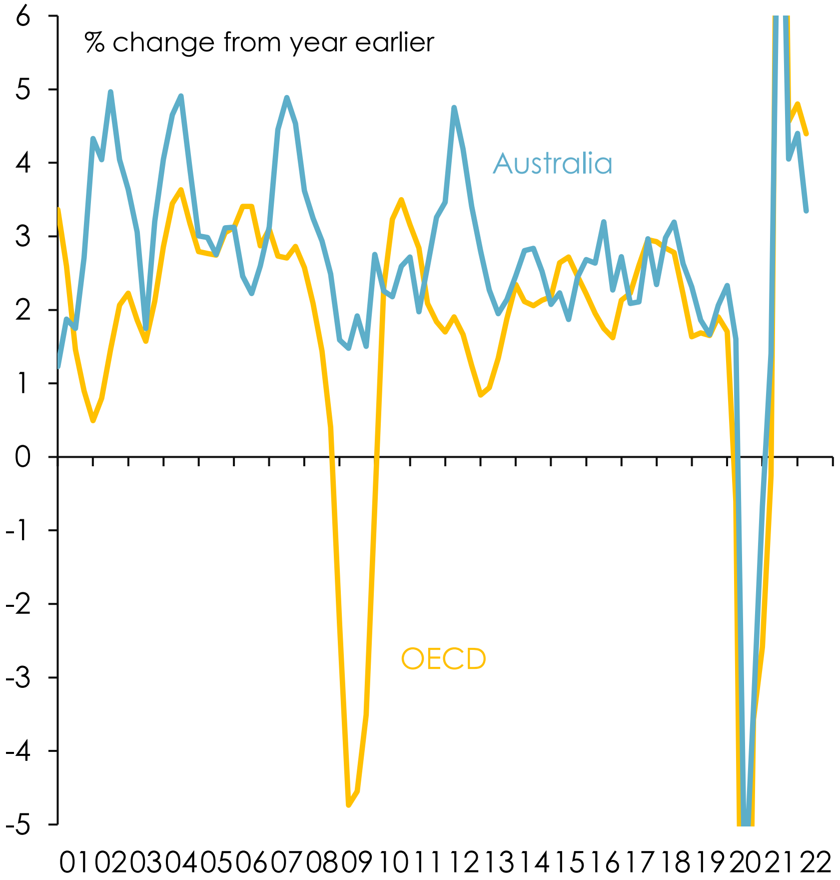
Population growth



Average over 2011-2019:

Australia	**1.6% pa**
OECD	**0.6% pa**

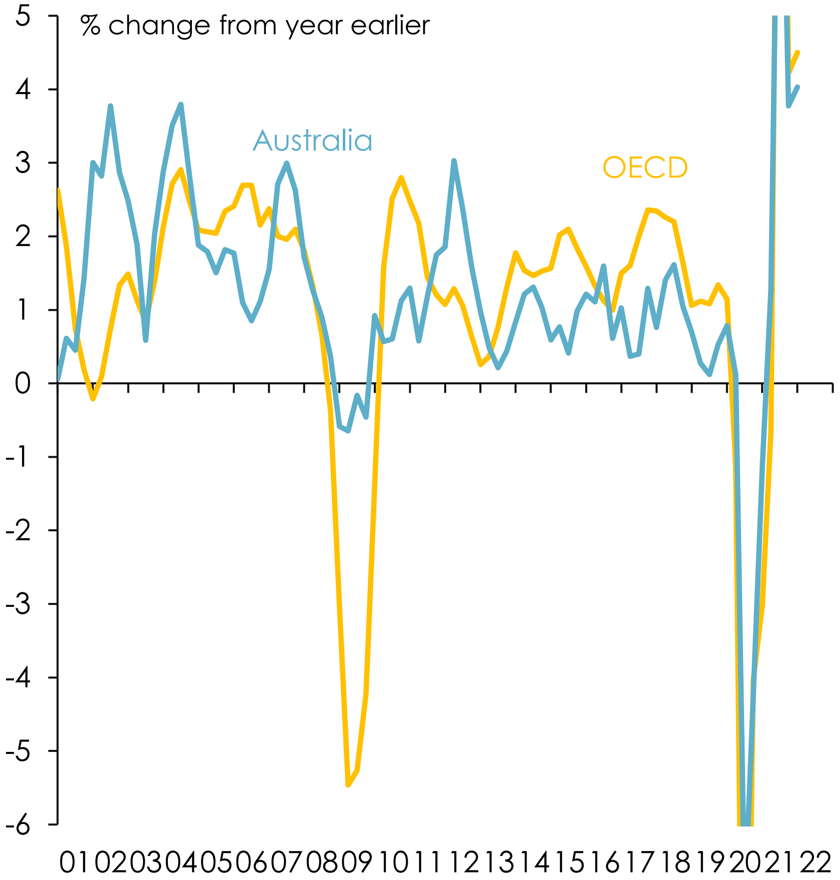
Real GDP growth



Average over 2011-2019:

Australia	**2.6% pa**
OECD	**2.0% pa**

Real per capita GDP growth



Average over 2011-2019:

Australia	**1.0% pa**
OECD	**1.4% pa**

Sources: OECD; ABS.

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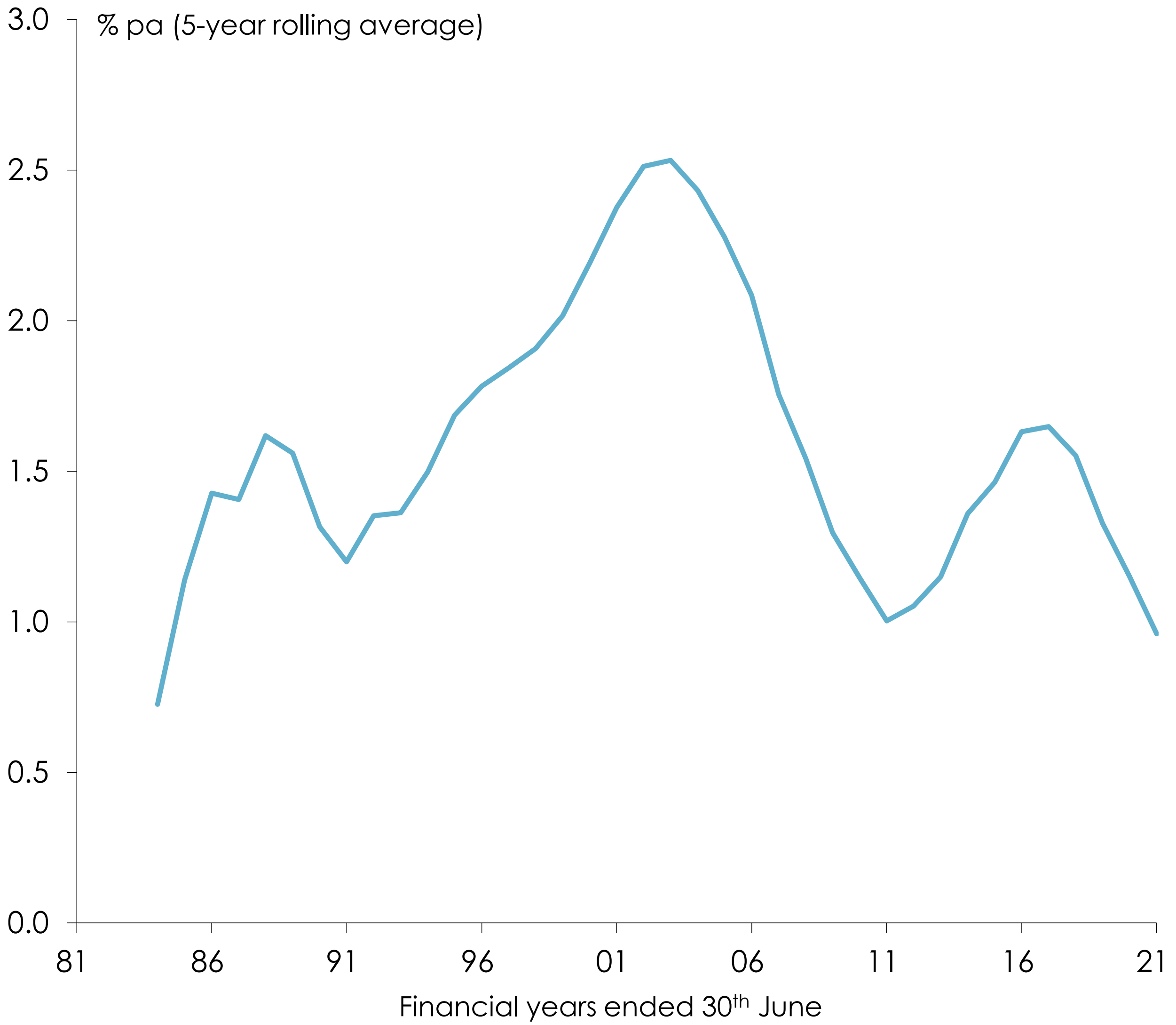
Australia's productivity performance over the past decade has been very disappointing – although we're not alone in that

Australian labour productivity growth



Australian and G7 labour productivity growth

Sources: ABS, *Australian System of National Accounts*, 2020-21; The Conference Board, *Total Economy Database*, April 2022.

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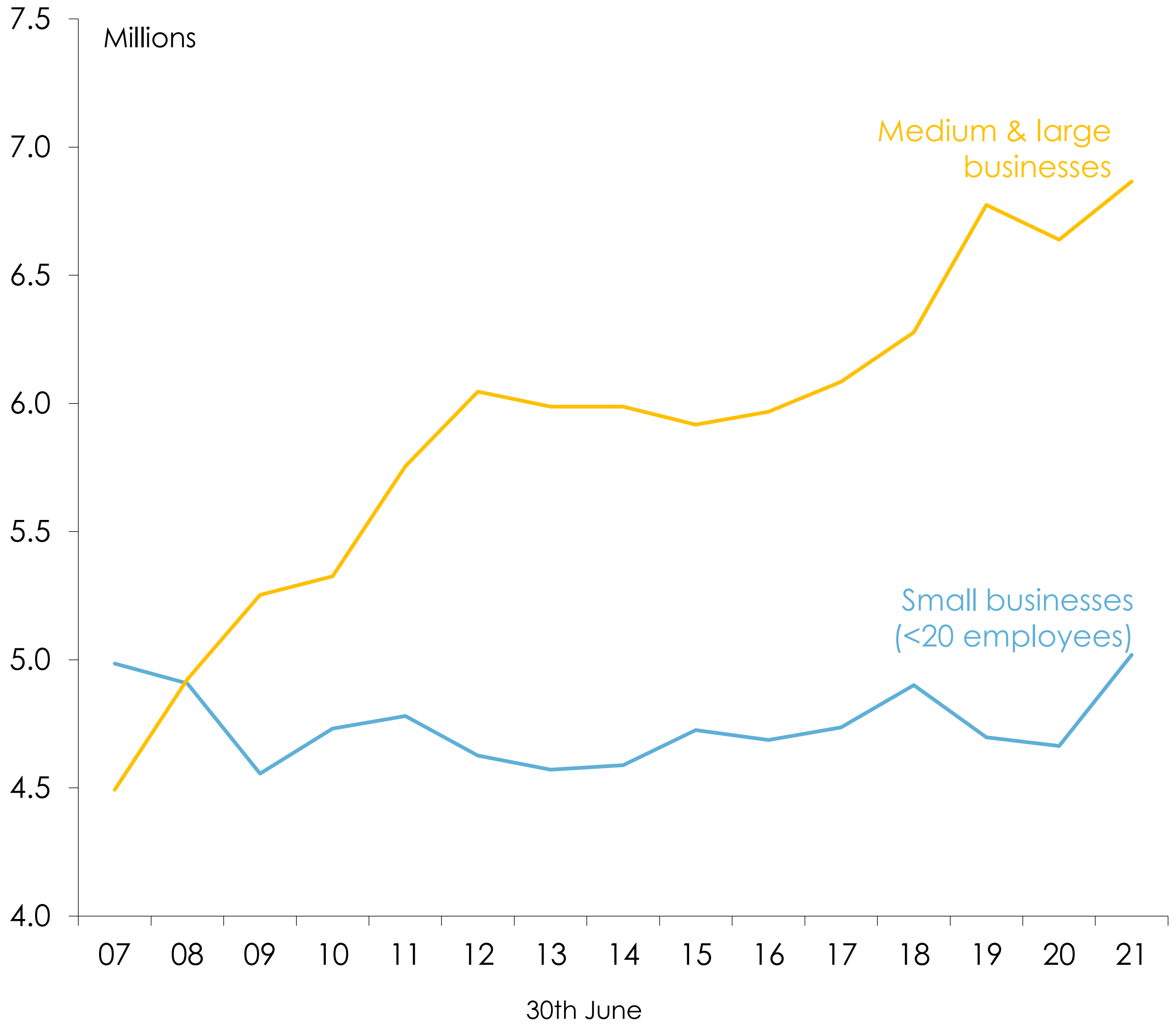
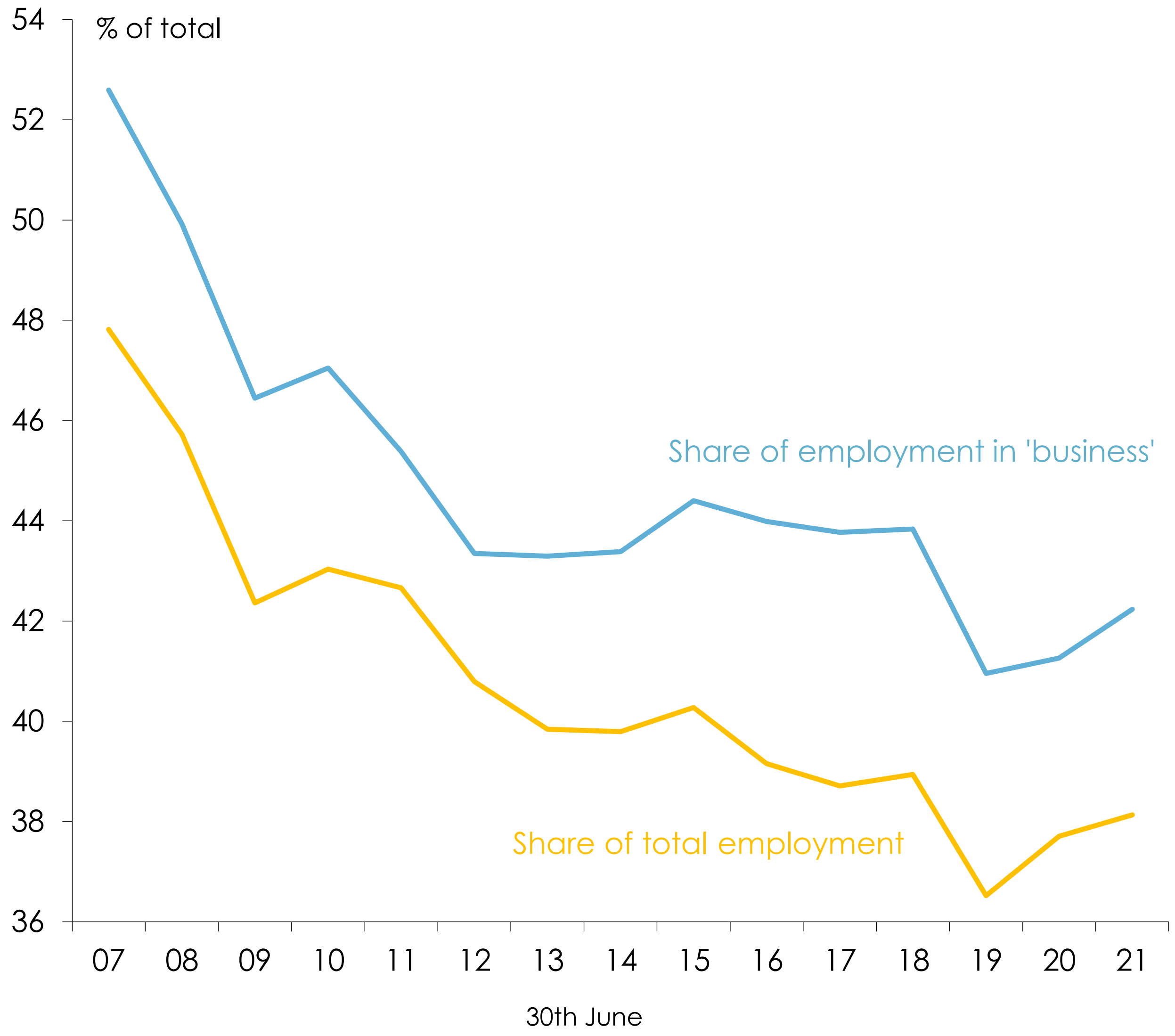
Contrary to widely-held beliefs, small business is not the 'engine room of the Australian economy'

Employment by business size



Small business share of employment



Sources: ABS, *Australian Industry*, 2020-21 and previous issues.

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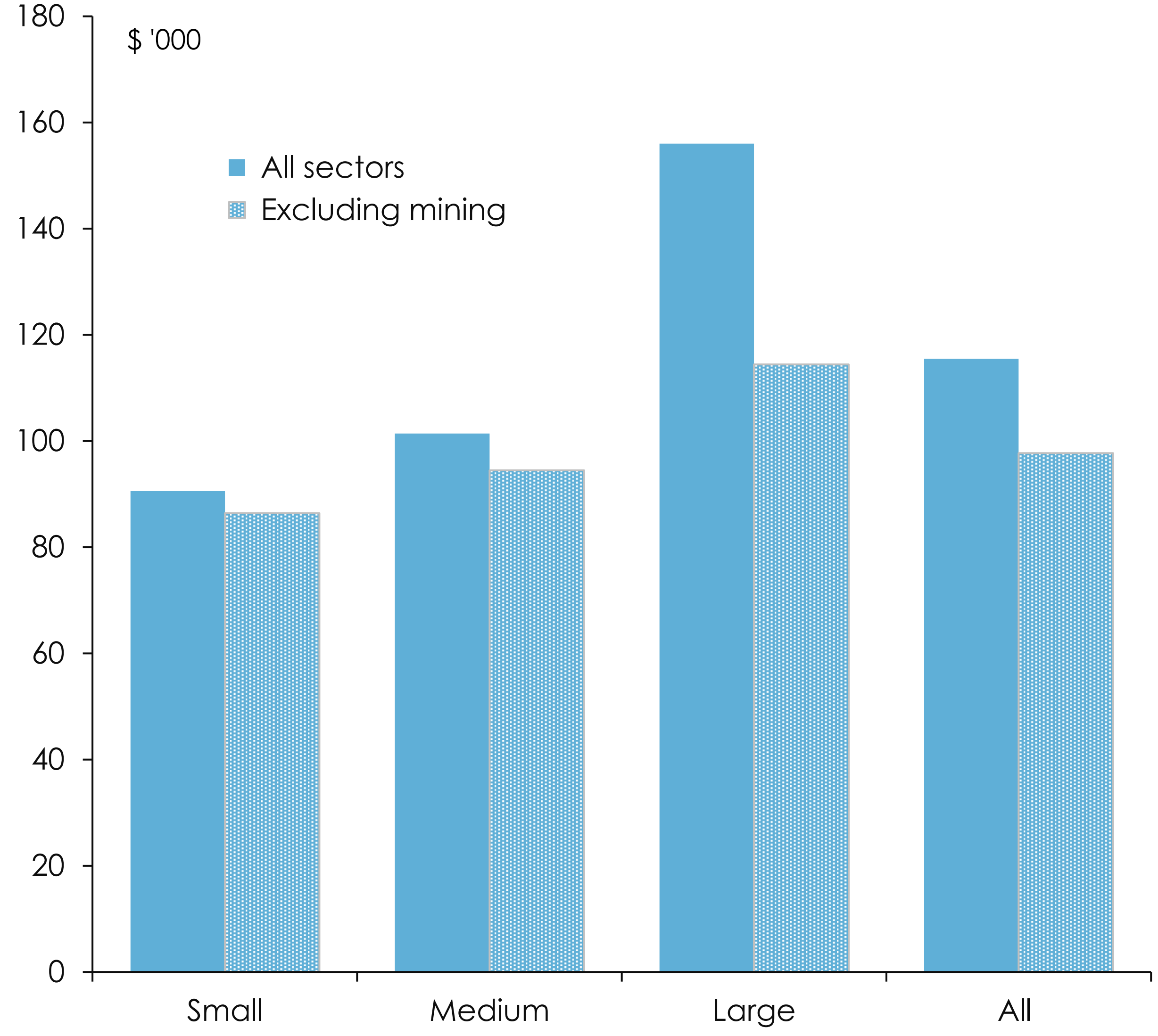
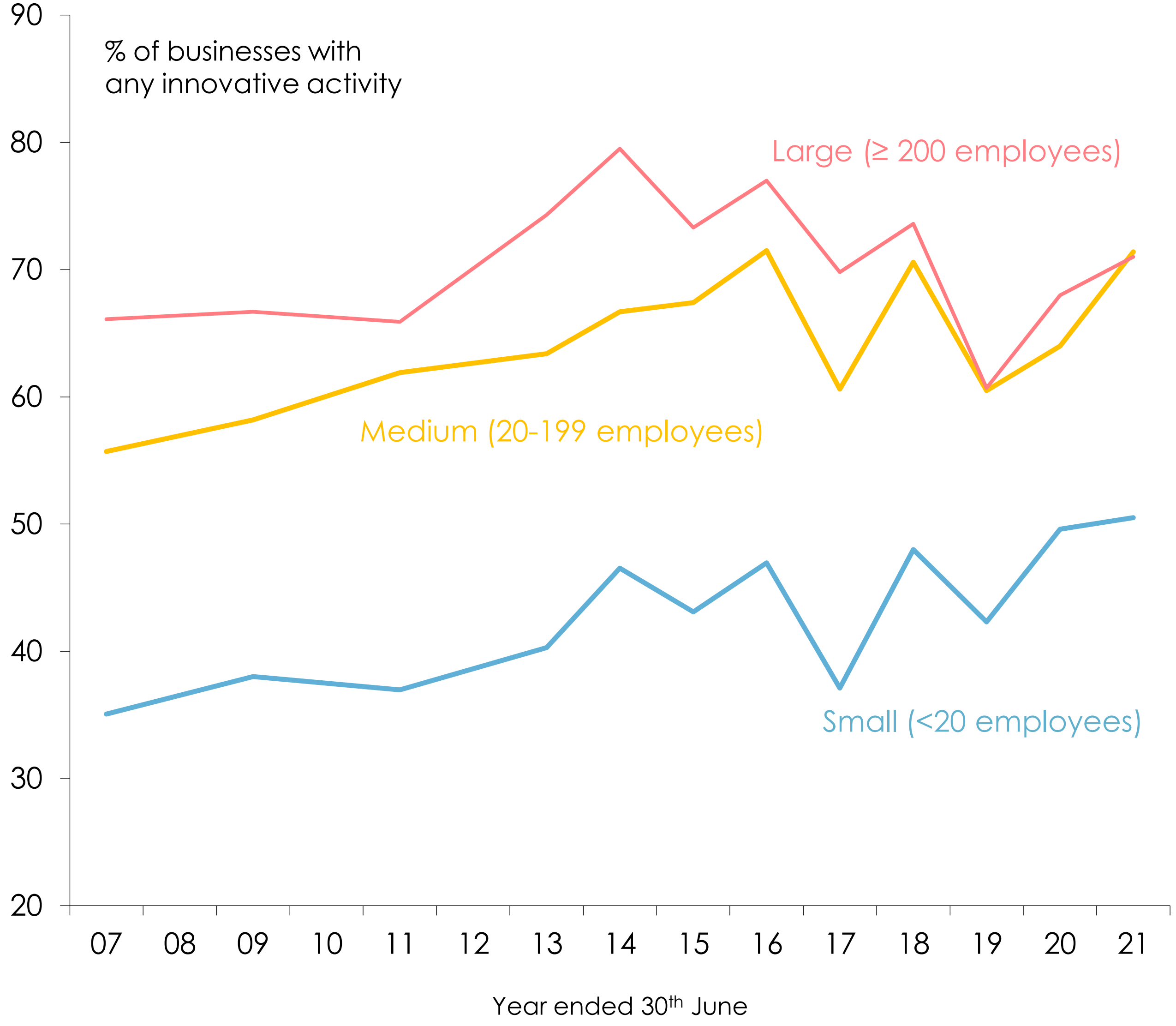
Small businesses have lower labour productivity than medium-sized or large businesses – and they are less innovative

Gross value added per person employed, 2020-21



Innovation activity by business size



Sources: ABS, *Australian Industry*, 2020-21; *Innovation in Australian Business*, 2020-21.

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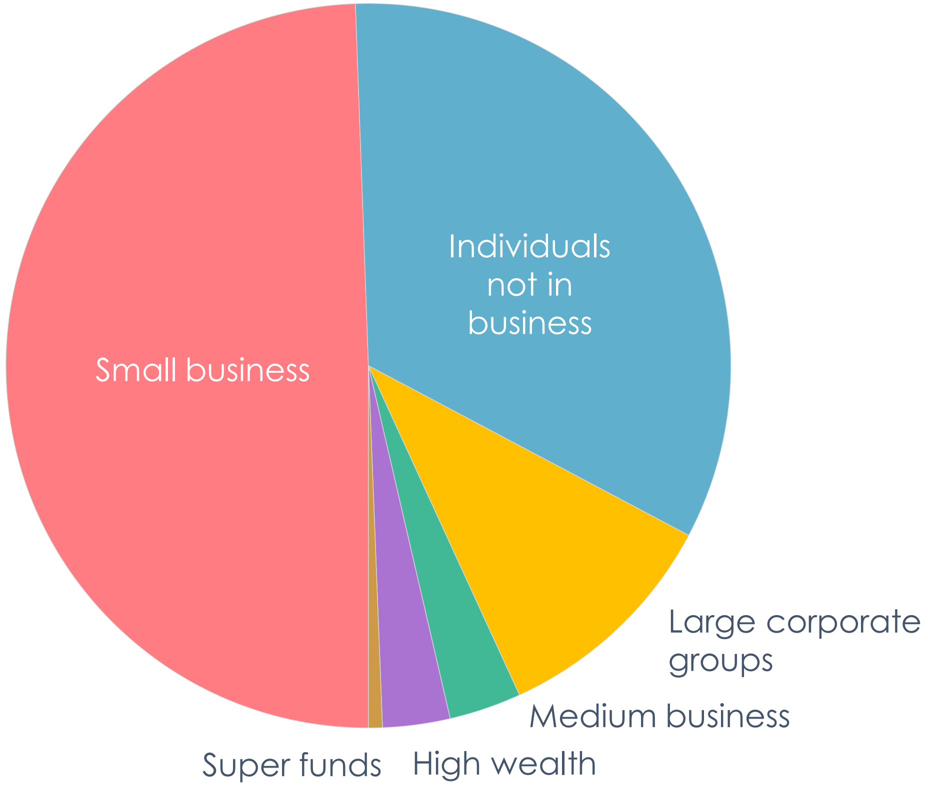
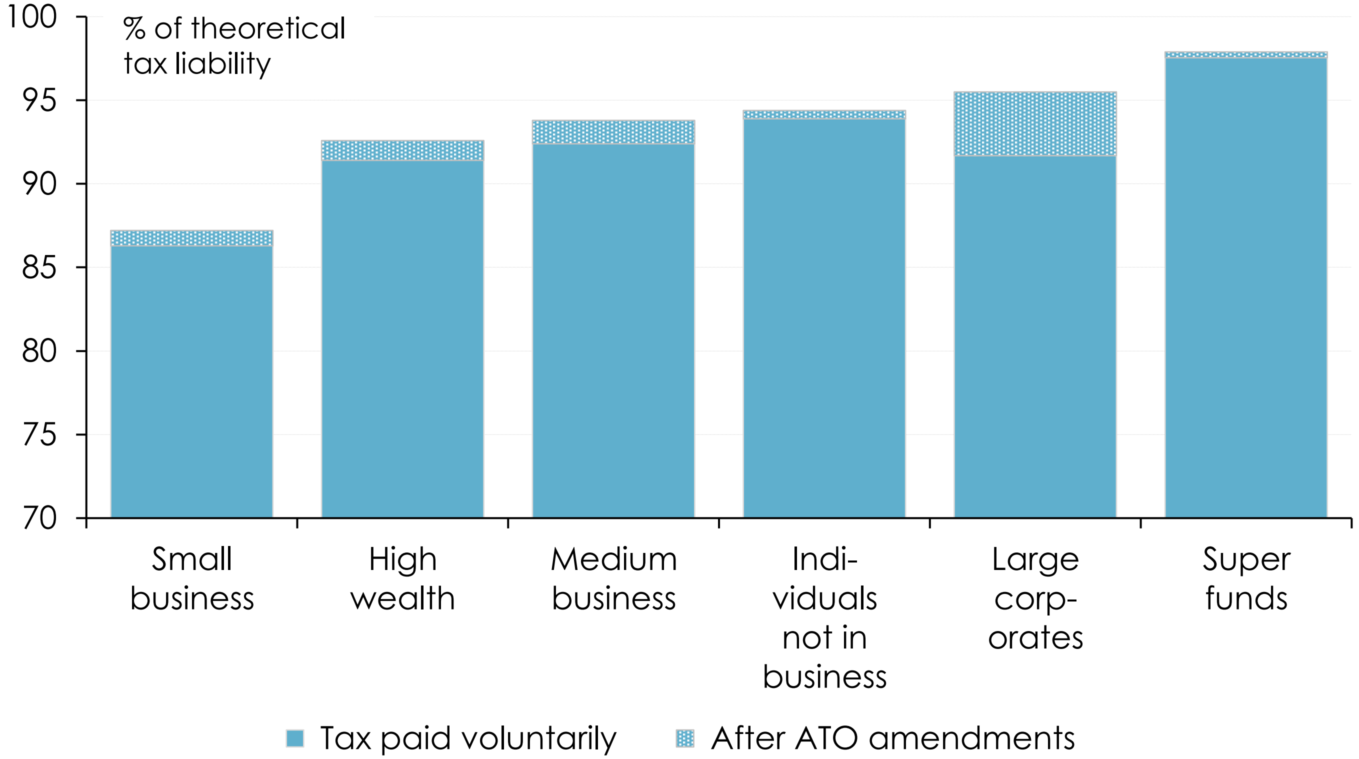
What small business is really good at is avoiding tax

Share of total income-based 'tax gap' by class of taxpayer, 2018-19



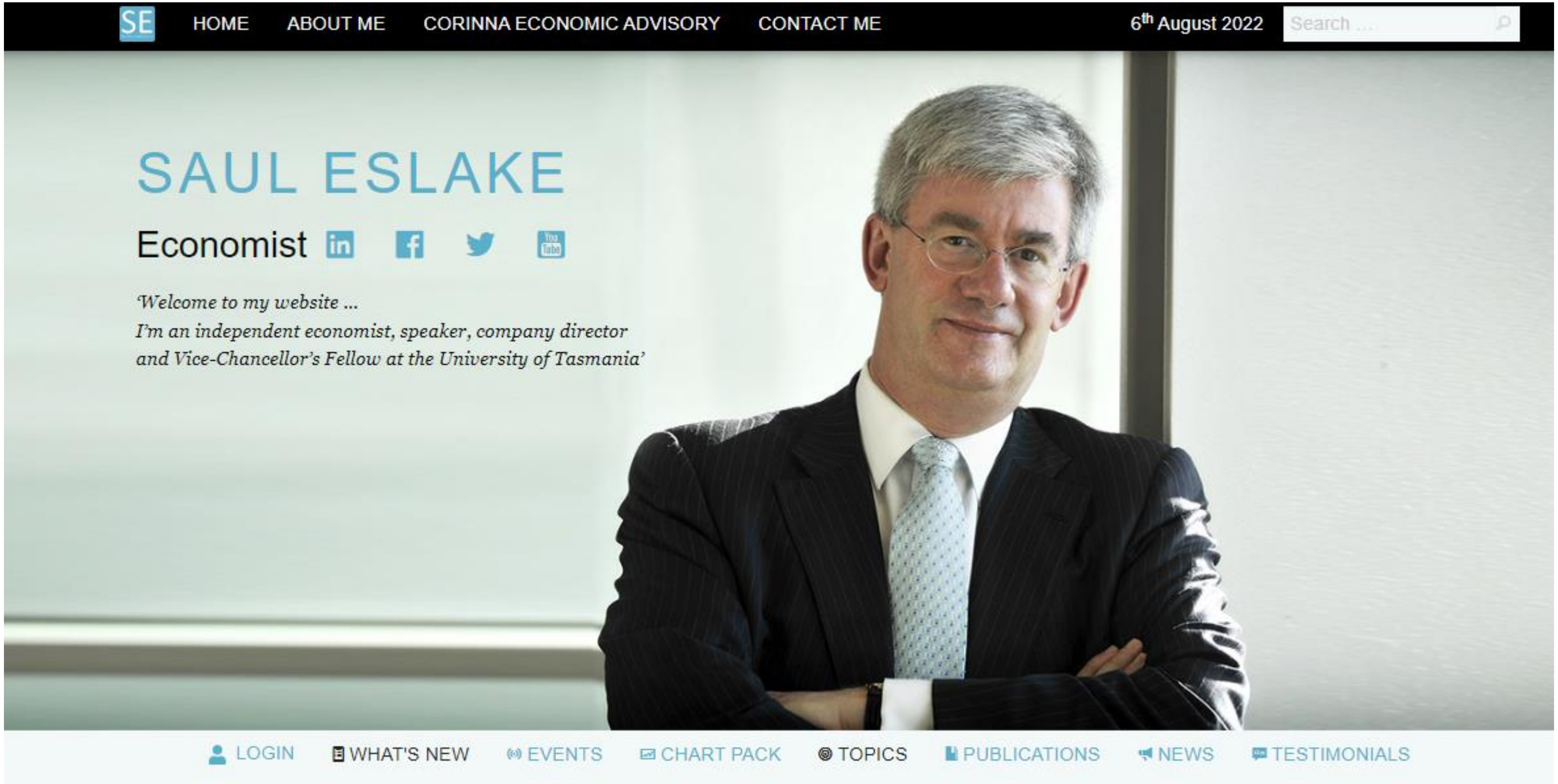
Share of theoretical tax liability paid voluntarily and after ATO amendments, 2018-19



- **Small businesses account for 49% of the total 'gap' between what the ATO collected in 2018-19 from various income-based taxes and what it estimates it would have collected given 100% compliance with the tax law – cf. large corporates 10% and high wealth individuals 3%**

- **Small businesses pay a smaller proportion of the tax which the ATO estimates they 'should' than either large corporates or high net worth individuals – contrary to the popular perception that the latter two are the groups least likely to be paying their 'fair share' of tax**

Note: 'small' businesses are those with income of up to $10mn; medium businesses are those with income of up to $250mn; and large corporates those with income of over $250mn. 'High wealth' individuals are those who (with associates) control wealth of more than $50mn. *Source:* Australian Taxation Office, Annual Report 2020-21.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