



SETTING OF MONETARY POLICY

House Economics Committee report released today

Chair of the House of Representatives Economics Committee, Bruce Baird, today tabled the committee's first report following its meeting with the Reserve Bank Governor, Ian Macfarlane, held in Sydney on 18 February 2005.

"At that time there was a great deal of speculation about pending interest rate rises given the mixed signals coming from the economy," Mr Baird said.

"This report presented today discusses these conflicting signals and documents a number of supply side constraints which have become central to the debate about how Australia can continue to maintain a steady rate of growth without being compromised by inflationary pressures."

Mr Baird noted that every commentator has his or her own opinion about the appropriate course of action the Reserve Bank should take.

"The Governor and Board members not only have to weigh up all of the conflicting evidence and advice, but also have to come to an on-balance judgment about where the economy is likely to be in the next three to six months," he said.

"Given the high level of indebtedness of Australians, monetary policy has become a very powerful tool.

"The Governor acknowledged this when he spoke to the Committee in February about the Bank needing to adopt relatively small, well timed movements in rates, so as not to undermine growth, and at the same time fuel inflationary expectations."

According to Mr Baird, the interest rate announcements by the Board since the February hearing (25 basis points on 2 March and no change on 6 April) would seem to confirm that this course of action achieves the inflationary targets without compromising business expectations and growth.

The report presented today highlights the complexities of decision making particularly in a global economy where external influences cannot be easily managed from a domestic policy point of view. Mr Baird cited the impact of an over-valued dollar on Australia's international competitiveness, the maintenance of very low interest rates in the US, Japan and the European Union countries, and the willingness of global financial markets to finance both internal and external deficits in many developed countries as events outside of our control.

Mr Baird believed the major challenge facing Australia lies with its ability to address the barriers and bottlenecks preventing it from continuing to achieve an enviable long-term growth rate of around 3.5 per cent per annum. He said the report noted there were signs that some of these issues were being addressed but many of the infrastructure problems will require longer lead times.

"Any further interest rate rises will impact on households who are carrying record levels of debt. On the up side, households are enjoying high levels of disposable income and record low unemployment so the capacity to pay will not be the issue, rather it will be a question of spending priorities," Mr Baird said.

"This report, while not an end in itself, highlights the valuable role the bi-annual public meetings between the Reserve Bank and the House of Representatives committee play in enabling these issues to be discussed and providing a level of accountability to the Reserve Bank."

The next public hearing with the Governor of the Reserve Bank will be held in Melbourne on Friday 12 August 2005.

For interview: Please contact Committee Chairman, Bruce Baird, on (02) 9525 8200.

For copies of the report: entitled: *Review of the Reserve Bank of Australia annual report 2004 (first report)* are available from the secretariat by phoning 02 6277 4587, or visiting secretariat offices at R2.105 (near second floor glass link to Reps chamber from Mural Hall), or online from the committee's website www.aph.gov.au/house/committee/efpa