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Monetary Policy problems sit with MPs not the banks

The Finance and Expenditure Select Committee released its report on the Reserve Bank's Financial Stability Report on Wednesday acknowledging the ineffectiveness of our monetary policy. However, the report focuses largely on the role of the banks in causing the disparity between New Zealand's interest and exchange rates and those of the rest of the world. The New Zealand Manufacturers and Exporters Association (NZMEA) is urging politicians to assess why our monetary policy has failed rather than looking at the banks who have been able to benefit.

NZMEA Chief Executive John Walley says, "The fact that the Official Cash Rate (OCR) has failed to control retail interest rates or effectively control inflation is not the bank's or the Reserve Bank's problem."

"While the Reserve Bank has tended to act too late with OCR changes, it has applied the OCR instrument largely as intended. The banks have also acted in the expected way in attempting to maximise profits for their shareholders. The problem lies in the broader policy settings and the single and ineffective tool legislators have given the Reserve Bank."

The Select Committee noted that, "easy access to overseas funds weakened the Reserve Bank's ability to restrain the money supply."

"This means that a method to control the volume of credit in New Zealand is necessary as well as using the OCR to control the price of credit," says Mr. Walley. "Several methods of volume control have been suggested including a Variable Excise Tax,ⁱ a variable savings schemeⁱⁱ and a variable GST rate. These options all have the same affect of reducing the volume of money when inflation is high and increasing the volume when inflationary pressures subside."

"In broader policy terms we need to do away with the asset tax haven that encourages borrowing and increases the demand for credit. This incentive results in less productive investment and reduces the returns to exporters via the upward pressure on the exchange rate."

"These are the options the Select Committee needs to look at. The banks will look to take advantage of their position regardless of what the Select Committee or anyone else might say; therefore politicians should look to policy setting changes, rather than expecting complaints to change the way the banks behave."

ⁱ 'Would giving the governor power to vary the excise tax on fuel reduce the amplitude of exchange rate fluctuations?', <http://www.mea.org.nz/document.ashx?id=495>

ⁱⁱ 'A Case for Compulsory Superannuation', <http://www.mea.org.nz/document.ashx?id=36>