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FINANCIAL REVIEW

Populism in Q&A and Parliament

Hanging over the 45th federal Parliament is the beguiling idea that Australia can defend its modern prosperity by blaming others: by taxing the rich and multinational corporations; by keeping out foreign people, goods or capital; or by putting the banks into the dock of a royal commission. In Australia, this populism feeds off the squeeze on national income from the collapse in the price of our biggest commodity exports. It is found on the cultural right of politics, such as Donald Trump in the US, in the centre such as Nick Xenophon, or among the left progressives who colonise ABC programs such as *Q&A*.

It appears both in the form of the formally uneducated Pauline Hanson or the imported Q&A intellectual.

The connecting populist idea is that the system is rigged against the mass of the people. In the left progressive version on Monday night's *Q&A*, rising inequality demands some fundamental reordering of capitalism. Yet, at a global level, income inequality has fallen sharply over the past 30 years of economic globalisation inspired by Margaret Thatcher and Ronald Reagan. The mass reduction of poverty achieved through the rise of an Asian middle class – along with big improvements in human health and lifespans – is a triumph of global capitalism.

The political problem now being exploited by the populists is that the reduction of global inequality has expanded the pool of reasonably skilled labour. So income inequality has risen in many rich nations, though not much in Australia. And that has driven the new populist politics of the typical Western nation state. Monday's *Q&A* was based on the idea that a lot more money should be redistributed from the well-off to all manner of people and causes. Income tax rates could be hiked as high as 70 per cent without shrinking the pie.

It took a well-grounded indigenous leader and former federal Labor president, Nyunggai Warren Mundine, to rightly frame this as a fantasyland. As Mr Mundine said, global capitalism has reduced global poverty. The billions spent in Australia on indigenous disadvantage shows that a lack of money is not the problem. Welfare can actually hurt, as shown by the now entrenched intergenerational unemployment in some indigenous communities. The central issue for the 45th Parliament should be how does Australia compete in a global marketplace so it can generate economic growth and jobs.

For frack's sake

Victoria's announcement of a "permanent ban" on fracking for gas but also on all conventional onshore gas exploration is yet more evidence of the rise of irrational populism. Labor Premier Daniel Andrews, whose state is powered by the dirtiest coal in the country, claims that the health and environmental risks threaten Victoria's reputation as a clean green food producer. What risks were those? Mr Andrews wouldn't know.

In 2014, the NSW government engaged the state's chief scientist, Mary O'Kane, to conduct a proper scientific review of coal seam gas exploration. Professor O'Kane found that, as in many things, there were risks. But these could be managed. And new technology would make "CSG production increasingly safe and more efficient". In contrast, the Andrews government preferred the madness of the crowd, calling a parliamentary inquiry which read 1600 letters from greenies and farmers who "mostly opposed" fracking. Evidently satisfied by this left-right coalition of populist discontent, Mr Andrews did not bother to explain the ban on uncontroversial conventional gas.

Showing an appalling lack of leadership, Mr Andrews has given the finger to every other state and the federal government working through the COAG energy council to increase the supply of onshore gas. Coupled with Victoria's ambitious target to generate 40 per cent of its energy through renewables by 2025, the drying up of the gas supply pipeline will drive up power prices and reduce the reliability of the state's power grid. It could even mean burning more coal.

From the Gallery — David Rowe

RBA's inflation goal fine for now

Economy

The Fed is going to raise rates over the coming months, which have big a big bearing on the RBA's future cutting trajectory.

Richard Holden

As the monetary-policy cognoscenti of the world met in Jackson Hole, Wyoming, US Federal Reserve chair Janet Yellen gave us great insight into short-term monetary policy in the US.

The Fed is going to raise rates over the coming months. This has big implications for Australia. In particular, it means the Australian dollar will depreciate, making a rate cut by the RBA less pressing.

The subject matter of the more academic discussions that followed hold important clues for how central banks around the world might conduct monetary policy going forward – particularly in Australia, under Reserve Bank incoming governor Philip Lowe.

Yellen laid the groundwork for a sequence of increases in short-term interest rates by the Fed. Like all good "Fedspeak", her words are open to interpretation, but I'm pretty sure the message is as follows.

The US economy has 4.9 per cent unemployment, inflation is about 2 per cent, and the last two job reports have been very positive. If a third good job report comes in (before the FOMC meeting in September), people are going to start asking: "what will it take the Fed to raise rates?"

And, given a good jobs report, I think they will raise the Fed funds rate by 25 basis points.

If one thinks of 2008 as, basically, the Great Depression but with smarter policymakers and better data, this is exactly how the Fed should react.

But, as the more wonkish discussions at Jackson Hole reveal, not everyone is so sure about that.

The big debate about how central banks should act long-term is what they should focus on.

The main problem facing the Fed, the RBA, and other central banks is that they are trying to control multiple things with one instrument. Witness poor Glenn Stevens, who tried valiantly to influence GDP growth, unemployment, inflation and property prices with just one tool – the cash rate.

What I refer to as the "Iron law of economics" is that with one instrument, one can target only one thing. The debate now is what that "one thing" should be.

For a long time, it has been inflation. Keeping inflation between 2 per cent and 3 per cent has been a strong commitment from the RBA for two decades. Such inflation targeting, as done around the world, has dampened inflationary expectations and led to a virtuous circle where (nominal) wages don't rise too fast, so interest rates can keep inflation under control, and (nominal) wages don't need to rise so fast.

The questions being asked by luminaries in Jackson Hole by scholars, such as former US Treasury secretary Larry Summers, is whether inflation is the right thing to target in future.

In a world where the worry was always that inflation could spiral upwards, targeting it made perfect sense for central banks.

But today, where the concern is about low inflation, anaemic growth, and advanced economies facing "secular stagnation" – a protracted period of very low GDP growth – perhaps central banks need to target something else.

So, should they – including the RBA – target nominal GDP instead of inflation? That's a good and hard question, and has been raised forcefully by senator Nick Xenophon in the Australian context.

There are pros and cons. Targeting inflation helps keep the wage-price spirals that led to mortgages with interest rates as high as 17 per cent in Australia from happening again. On the other hand, if the world is in a deflationary spiral – like Japan has been in for two decades – nominal GDP targeting might be a good idea.

I vote for using up our existing ammunition before changing course. The RBA can cut the cash rate further. It can also engage in bond-buying programs (so-called quantitative easing) to lower long-term rates.

The Fed and the RBA have two things in common: they face the same global savings glut that is forcing GDP growth lower, and they have only one tool they can use.

But the US Fed has already pumped a lot of money into the US economy through its "quantitative easing" bond-buying programs. And it looks like it is coming out the other end of that experience.

Australia, by contrast, may be only just starting that transition.

The big issue is whether low inflation, as we are now experiencing, will justify low interest rates.

Perhaps we will make it through with conventional monetary policy. But don't bet on it.

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