

# Why the RBA must cut and keep cutting in 2020

**Monetary policy**  
The central bank still has some way to go to reduce joblessness and rekindle inflation.



Richard Holden

The Reserve Bank of Australia made three 25 basis point cuts to official interest rates in June, July and October last year, bringing the cash rate to a historically low 0.75 per cent. With the effective lower bound being 0.25 per cent, this year is all about whether, and when, the bank will cut to that level.

Plenty of commentators have warned against a cut when the RBA board meets on Tuesday – including the experienced and thoughtful former board member Warwick McKibbin.

And although there are reasonable arguments about the effectiveness and side effects of further cuts, there is really no question that the RBA should cut rates on Tuesday.

The RBA has a fairly clear objective: it wants to get unemployment down to the lowest rate before inflation takes off – currently estimated to be 4.5 per cent – and it wants inflation to be between 2 per cent and 3 per cent.

The best hope of achieving this is to cut rates once more. Measured against these objectives, the cuts made last year have been showing promise.

The RBA had missed its 2 to 3 per cent inflation target systematically and comprehensively through the earlier part of Philip Lowe's term as governor, but there has lately been progress. From a low of 1.3 per cent in March 2019 – when the quarterly rate was zero – by last September the figure had risen to 1.7 per cent.

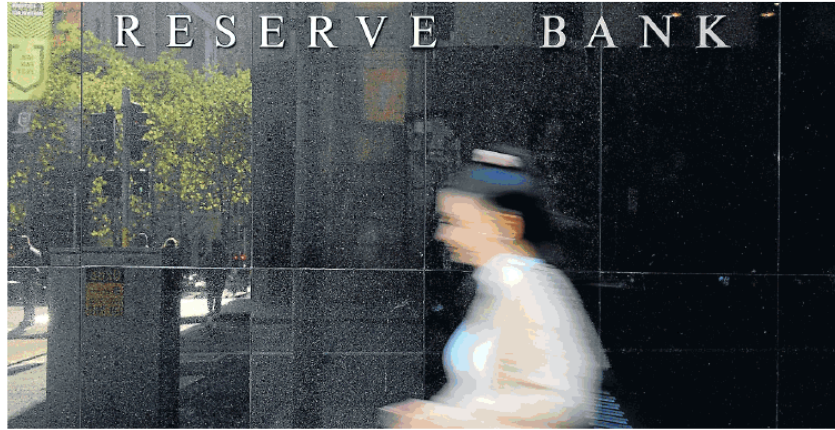
More needs to be done to get back into the target range and to help drive wages growth, but credit where it's due.

Above all, the truly scary prospect of a Japan-style deflationary spiral, which was a disturbingly real possibility in the middle of last year, seems to have disappeared.

Now is the time to capitalise on increased inflation expectations and drive the rate above 2 per cent.

Unemployment is too high at 5.1 per cent, and from the RBA's perspective the only thing it can do to push it towards 4.5 per cent is to cut rates.

Those sceptical about a cut say that low interest rates fuel asset bubbles – in housing and beyond. There's some truth in that, but it's hard to know the magnitudes. And macroprudential regulation through APRA



The RBA needs to play the hand it is dealt. That hand points squarely in the direction of another rate cut right away. PHOTO: AAP

is the primary tool for dealing with those issues. The same sceptics also say that cutting rates sends a signal that the RBA thinks the economy is in bad shape. Yet these very folks themselves say that the economy is in terrible shape.

Does anyone really think Lowe can fool people into believing the economy is in great shape simply by not cutting rates on Tuesday? That same logic suggests he should raise rates just to send a positive signal – but that seems absurd. People are smart.

The hard truth is that we live in an age of secular stagnation, where low GDP growth and low interest rates are the norm. This is a point I made on these pages in mid-2015.

We don't need to like it, but we'd better get used to it. To expect monetary policy to solve all of our growth problems is to fundamentally misunderstand the new economic challenges we face. Equally, to measure the success of monetary policy by its ability to achieve "old normal" growth numbers is a mistake.

That said, keeping official interest rates

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artificially high just makes things worse. It feels uncomfortable that rates should be at 0.25 per cent this year, but they should.

We certainly need much more aggressive fiscal policy in Australia, something that Lowe and every mainstream economist have said in unison.

Say what you will about Donald Trump's tax cuts – I'd say they were profligate and ill-advised – but the US has GDP growth at 2.1 per cent, inflation at 2.3 per cent, and wages growth in excess of 3 per cent. I give more credit to the Federal Reserve than the White House, but the bottom line is that stimulus stimulates.

Ultimately, the failure to use fiscal

stimulus isn't the RBA's fault. It needs to play the hand it is dealt. And that hand points squarely in the direction of another rate cut right away.

I was critical of the RBA early last year for failing to cut rates soon enough. I still think it acted too late, but act it did. And, now that it has updated its estimate of the unemployment target to 4.5 per cent, we now have a good sense of its aim. It has a framework and it needs to act on it.

Good central banking involves having a framework for thinking about interest rates. Sure, that involves plenty of art along with the science. But what good central banking decidedly is not – except in a 2008-style situation – is seat-of-the-pants macroeconomics.

And the cheerleaders for ad hoc deviations from what the monetary policy framework suggests is correct policy should be mindful of that.

Richard Holden is professor of economics at UNSW Business School.

# The problem isn't Huawei, it's tech monopolies everywhere

**Telecoms**  
The British government has wisely chosen a too-powerful Chinese 5G supplier over a bullying Washington.



Jeremy Warner

Congratulations to Boris Johnson for a gutsy, pragmatic and essentially correct decision on Huawei. Based on compromise, hard evidence and expert advice, rather than the shrill voices of political prejudice and sentiment all around him, it bodes well for the future.

The British government seems to have struck the right balance between the needs of the economy and the countervailing risks to security on the one hand, and Britain's relationship with the US and China on the other. The decision will certainly anger parts of the US administration, but I doubt it will significantly damage the chances of reaching a trade deal, or even British intelligence sharing arrangements with the US. In time, the whole thing will be seen as a fuss about nothing.

Nobody should be under any illusions about Huawei. As chronicled by James Bamford, the American author and journalist, security agencies the world over have a long history of actively using their telecom companies for surveillance and intelligence purposes. It stretches credulity to believe Huawei is not part of that tradition.

Yet the train has already left the station, with Huawei equipment widely installed not just in existing British networks but also in the build-out of 5G, on repeated assurances from the government that operators would not be obliged to strip the stuff out at a later date. To do so now would not only set 5G back at least a couple of years, it would also cost billions.

Be in no doubt, this is a deeply unsatisfactory position for Britain's government – and the country – to have got itself into. How on earth did the UK come to rely for critical infrastructure on a single supplier from a potentially hostile world superpower?

The Prime Minister must be cursing his predecessors for having left him with such a hot potato. Yet, in the end he had little option but to give Huawei a continuing role.

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Having so recently won a thumping majority, there could scarcely be a better time for making difficult decisions.

Other than potentially jeopardising a trade deal with the US, it is hard to see what this has to do with Brexit.

For some, Huawei is a "betrayal" tantamount to not delivering on the referendum. On the contrary, it demonstrates, encouragingly, a government tenaciously willing to act independently in its own perceived self-interest, rather than be bullied into submission by a paranoid US.

Some claim it is no good taking back control from Brussels only to hand it over to Beijing. But exactly the same thing might be said of handing control to the US, whose motivation in attempting to frustrate Huawei is largely protectionist in nature. For now, Donald Trump's America has no viable alternative to Huawei. Its position is entirely driven by fear of Chinese technological catch-up, which it has determined to thwart.

The three US senators who wrote this week to Britain's National Security Council are talking nonsense in claiming that the more countries that refuse Huawei, "the more market space there is for innovators and entrepreneurs to develop competing products". You don't improve on cutting-edge technology by closing borders and freezing it out; rather, you embrace it, copy it and advance it – something repeatedly demonstrated by both the US and more recently China in their economic development.

As it is, Britain has been granted unique access to Huawei's inner secrets and code, an arrangement that from a security point of view might be useful as more and more countries adopt the company's technologies. No other supplier – and, by the way, all of them use Chinese components to some extent – allows such access.

None of this is to deny that Britain and its mobile phone operators find themselves in a shameful position. It's never good business to rely on a monopoly supplier, and when it is one that hails from an alien

political system with vaulting geopolitical ambitions (I mean China, not the US), it is particularly dangerous.

Almost inevitably, the UK now finds itself between a rock and a hard place, with its greatest ally, the US, threatening to curtail shared security and trading relations if Britain doesn't dance to its tune. This is particularly unfortunate at a time when Britain is trying to secure a free trade deal with America. Yet to bend to US pressure is to forgo some of the potential for the immediate productivity improvement the British economy so desperately needs.

Britain used to have its own cutting-edge telecom equipment manufacturers – think Marconi, Plessey, and Standard Telephones and Cables, the last of which invented and developed groundbreaking technologies such as optical fibres and pulse code modulation. But they went the same way as much of the rest of British industry. In a fast globalising world, they found themselves outgunned by lower cost, state-subsidised rivals, until eventually the British find themselves enslaved by just one, having surrendered their former industrial prowess to the demeaning addiction of cheap consumer prices.

Britain is left walking a tightrope between the established and aspiring hegemonies of the world economy. Johnson's cleverly crafted stopgap on Huawei will temporarily solve the problem but, in a bipolar world, the underlying dilemma is not going away.

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