Governing the Reserve Bank

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The Reserve Bank (RBA) is Australia's central bank. It is responsible for Australia's monetary policy—the setting of short-term official interest rates—and for the overall stability of the financial system. When the Australian Prudential Regulatory Authority (APRA) was created, the Reserve ceased also being responsible for the prudential supervision of the banks, but its Governor retains an interest in that subject by virtue of his being Chair of the Council of Financial Regulators.

When Australia's exchange rate was fixed, the Reserve bank had responsibility for monetary policy without the necessary powers to conduct monetary policy with reasonable independence from that of other nations in the world community. In theory, now that Australia has a floating exchange rate, Australia can run its own monetary policy, although with many direct and indirect linkages between countries and companies, especially within the banking community, the independence is not as complete as the text books would suggest it is.

In recent years, the Reserve Bank has been declared 'independent' of political government in Australia, by virtue of an exchange of letters between the Treasurer and the Bank's Governor. The Reserve Bank is formally accountable to parliament. It must listen to political leaders just as it must take account of other players in the international financial system. During recent times, comments by senior politicians about the appropriate course of interest rates have been particularly pointed. No man, certainly no central bank governor, is an island.

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The RBA has power without any immediate accountability. If it puts up cash interest rates, mortgage rates rise, and if it lowers them mortgage rates fall. The same applies to rates for business loans, credit card debt, etc, etc. By running a tight (that is, high interest rate) monetary policy, the Reserve can raise the Australian exchange rate, or prevent it falling, and so influence the price of imports, exports and overseas trips. Tight monetary policy can create recession, just as easy monetary policy creates inflation. Both inflation and recession have great influence on the welfare of all Australians.

Ultimately, though, the Reserve Bank is accountable to parliament. Someone once remarked that 'sunlight is a great steriliser'. The Reserve Bank is currently in the spotlight, in part because it is not committed to allowing the antiseptic qualities of sunlight into its dimly illuminated boardroom.

The Reserve Bank leadership team makes regular speeches and the Bank issues quarterly monetary policy statements. In addition, twice a year, the Governor makes a presentation to the House of Representatives committee on economic policy. These speeches, statements and presentations are generally of good quality and convey reasonably clear messages about where the Reserve thinks the economy is headed and about its general policy stance.

The Bank does not, however, give immediate information about its views when it decides to leave interest rates unchanged. Press reports say that this providing such information is strongly opposed by the Bank's Governor, Ian Macfarlane. Macfarlane is also opposed to releasing minutes of the meetings on the board.

The Reserve Bank is said to allow wide distribution of the papers its officers write for the board. Copies go to each member of the board and, in the case of Treasury, they are distributed widely within the department. 'Well connected' journalists and former Treasury colleagues might well be tempted to ask for gobbets of opinion.

As was reported recently, a 'well connected' private agency has been telling people in the financial markets that it was 'certain' that there would be no rate hike after a recent meeting of the Board. A lucky guess? This hypothesis strains belief.

Then, after said board meeting, two directors took it upon themselves to talk selectively to journalists—and goodness knows who else—neatly illustrating that selective briefings are not unknown at the Reserve Bank. During my time at the Bank I was once moved to remark to a senior colleague (still at the Bank) that in my view he had gone far too far in talking to a private financial institution over lunch. His response, as I recall it now, was to the effect that 'markets have to be informed of our thinking'. He added: 'Why do you think they ask us to lunch?'

I have long suspected that selected journalists act as unofficial spokesmen for the Reserve Bank. This, too, is a perception of other experienced observers. While the recent briefings were unofficial—and branded as such by the Bank—again the episode betrays a mindset. If the tradition were to issue an explicit statement immediately after the meeting of the board—or not later than 9.30 am the following day when the board's decision about monetary policy is announced—things would be far better. If this policy were adopted, and if Reserve Bank board papers were far more limited in their distribution, there would be a good chance that all interested parties would be informed fairly and equally and at the same time.

But there is a more important point. Having to explain oneself clearly and simply and in writing to the general public—and to the journalists who will retail one's material—is a great way to sharpen one's thought processes. If explanations were required after each meeting of the board, analysis would be better, possibly a good deal better.

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I have one further point to make about the Reserve Bank's endemic, ahem, reserve. Recently we learned that, during the last election campaign, the Reserve Bank was concerned by the emphasis on interest rates. A truly independent central bank would have issued a clarifying comment about its attitude more or less immediately. But the Reserve Bank fretted about this matter in private and, according to reports, only passed on to the Electoral Commission a document that was clearly misleading when it was sent to them with a request that they do something about it.

The Electoral Commission reportedly said that there is no legal requirement that electoral material be true (why not? I hear you cry.) But there is no reason relevant public institutions cannot do their best to encourage honesty in government.

A writer to the editor of *The Sydney Morning Herald*, a Vincent Scoppa of Leichhardt, said: 'I am not aware of any law that prevents the Reserve Bank from acting in a public-spirited manner to reject the politicisation of interest rates by a political party during an election campaign. If the Reserve Bank was deeply uneasy at the intense politicisation of interest rates by the Coalition during the last federal election, why didn't it perform its public duty and speak up? Silence may be golden, but a gram of openness is worth a kilogram of silence.' Hear, hear, Mr Scoppa.

Was the Reserve Bank's concern at incorrect claims being made not of legitimate general interest during the election campaign? Again we have a mindset issue.

My views on what is needed to improve things have long been on the record. In 1988, shortly after leaving the Reserve Bank, I wrote: 'Evaluation of policy will be greatly enhanced by the fullest disclosure of why policies are as they are. It seems to me that there is no satisfactory alternative to full and frank discussion of monetary policy within a relatively short period of decisions being taken'.

The Reserve Bank should be far more forthcoming about its thinking about the economy. It should explain its views after each meeting of the board and minutes of meetings of the board should be released (with some delay) after each meeting of the board. This will improve policy-making as well as providing a more fully and fairly informed market.

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