



The Liberal Democrats believe that inflation is taxation by stealth, that the Reserve Bank should be more accountable, and that banks should be free to fail.

The Liberal Democrats will:

- legislate so that the Reserve Bank targets zero inflation, holds assets and carries out transactions only for this purpose, and is prohibited from acting for other purposes.
- fund the Reserve Bank solely by an appropriation approved by the parliament, assign responsibility for decision-making on monetary policy to the Reserve Bank Governor rather than a Board, and link the remuneration of Reserve Bank officers to the achievement of the inflation target.
- repeal prudential regulation and abolish the Australian Prudential Regulation Authority.
- repeal government deposit insurance and similar schemes.
- prohibit the bail out of any financial institution by any government body.
- privatise the clearing house for the inter-bank transfers underpinning EFTPOS, cheques, etc. and
- remove restrictions on private currencies.

### **Discussion**

The libertarian tradition includes rich and varied policy prescriptions for money and finance. The Liberal Democrats believe that achieving these policy prescriptions will initially require reforms within the current monetary policy framework.

## **Zero inflation**

Inflation is recognised in mainstream economic literature as akin to taxation, and is often referred to as inflation tax. The 'dividends' provided by the Reserve Bank to the Government in part reflect the inflation tax imposed on users of the Australian currency. Uncertainty surrounding the extent of inflation discourages people from entering into long term contracts, which underpins economic prosperity. Inflation also leads those who are ignorant of it to incur losses, such as reductions in their real wages.

Keynesian prescriptions for positive inflation in order to reduce the risk of deflation exaggerate its risk and the additional thrift that deflation would prompt, and venerate discretionary consumption over thrift.

Restricting the Reserve Bank to the targeting of zero inflation will mean that economic booms and busts would continue to be countered by monetary policy, but that the long-term economic benefits of sound money will also be recognised.

Restricting the Reserve Bank to the targeting of zero inflation would mean it would not seek to manage the exchange rate and would not be able to support domestic and foreign financial institutions and markets.

Responsibility for monetary policy decision-making should rest with the governor of the Reserve Bank, rather than a Board. Members of the Reserve Bank Board are well placed to oversee the Reserve Bank. However, they typically have no expertise in monetary policy, as Australia does not have a deep pool of monetary policy experts upon which to draw. Moreover, Reserve Bank Board members can feel pressure to represent their sectoral interests when making monetary policy decisions. This in turn can lead to unnecessary secrecy about monetary policy deliberations.

## **Prudential regulation and bail outs**

Various regulations are imposed on financial institutions in Australia including requirements to maintain reserves at certain levels. This attempt to prevent bank failures makes government responsible for keeping banks in business and creates pressure on government to bail out bank creditors and shareholders in the event of a bank failure.

In addition to this implicit, wide-ranging bail out guarantee, the Government has also issued an explicit and specific bail out guarantee of deposits up to \$250,000.

Bailouts are a poor use of taxpayer funds. They represent a transfer from taxpayers without savings and taxpayers who manage their savings prudently, to people who have savings

but concentrate them in a poorly managed bank. The prospect of bail outs discourages scrutiny of bank management, and poor management contributes to the risk of bank failure.

The Liberal Democrats will abolish explicit deposits guarantees and remove implicit guarantees by repealing prudential regulation. As a result, banks will maintain reserves at a level that they consider necessary to win the confidence of depositors, shareholders and creditors.

Well managed banks do not need a bail out guarantee, as the risk that they will fail is small. Traditionally, people have been concerned that the failure of a poorly managed bank will bring down a well-managed bank to which it owes money. However modern technology means that this risk is negligible, as interbank debts, such as those that arise through EFTPOS payments and cheques, can now be cleared quickly.

The Liberal Democrats will privatise the clearing house for inter-bank transfers so that it is no longer part of the Reserve Bank and operates like other privately-owned clearing houses, such as the Australian Securities Exchange.

The Liberal Democrats will remove restrictions on how people transact with each other. The Reserve Bank Act currently prevents organisations, individuals and State Governments from issuing a 'bill or note for the payment of money payable to bearer on demand and intended for circulation'. The Currency Act currently requires every contract and transaction involving money to be done according to the currency of the Australian Government or a foreign government.

The Liberal Democrats will remove these and other restrictions to ensure that new and old forms of non-government money, from gold to Bitcoin, are allowed a chance to prosper as a store of value and means of transaction. Opening up the Australian dollar to competing currencies will ensure that Australians have alternatives to prevent their savings and income being eroded by the hidden and insidious effects of inflation.