

Topic 1 – The Global Economy

International economic integration

Today we live in a global economy, where the economies of individual countries are linked to each other and changes in a single economy have similar effects on others. The global economy consists of all the countries in the world that produce goods and services and contribute to Gross World Product (GWP) or global output. These economies also engage in world trade in goods and services and are responsible for flows of foreign direct and portfolio investment. A reduction in global trade barriers has led to greater **international economic integration** (threatened by global trade war in 2018).

Economic integration refers to the **liberalisation of trade** between two or more countries or many countries within a region. Examples of regional economic integration involves: European union (European union), North American free trade agreement (North America) and Asia Pacific Economic Co-operation Forum (Asia). Increased economic integration between regional grouping countries has led to **intra-regional trade** and **intra-industry trade**. International economic integration has been accompanied by an increasing proportion of world trade carried out by multinational corporations (intra-company trade).

Benefits of economic integration (example foreign direct investment provides employment and can increase competition between businesses in an industry):

- Increased trade
- Increased investment flows
- Rising standards of living

Main forms of economic integration:

Free trade area	Group of member countries abolish trade restriction amongst themselves, however, maintain restrictions against non-member countries. Example: United States-Mexico-Canada-Agreement / NAFTA
Customs union	Trade restrictions are abolished between member countries. Further involves adopting a common set of trade restrictions against non-member countries (external protection). Example: European Economic Community (preferential trading agreement)
Common market	Features of a customs union however allows the free mobility of labour and capital within the common market countries as well as the free flow of goods and services . Example: European Community
Monetary union	Features of the common market with free movement of financial flows. Also adoption of a common currency and the co-ordination of monetary policy through a single central bank. Fiscal, welfare and competition policies may also be coordinated between member countries. Example: European Central Bank and Euro currency

A subsidy increases supply, thus eliminating the needs for imports. Subsidies are generally more preferred by economists compared to other forms of protection. This is because they are paid by the government – **hence they are regularly under review and are likely to not be enforced for extended periods of time** // and unlike tariffs and quotas subsidies decrease prices for consumers.

However, they distort resource allocation and redistribute income away from taxpayers to the subsidised industry. Continuation of subsidies may also raise government expenditure and increase the taxation burden. Subsidisation of inefficient industries causes a misallocation of resources, since inefficient industries are favoured over efficient industries that are competitive in the market without government subsidies.

4. Local content rules

Local content rules specify that goods or services must contain a minimum percentage of locally made parts. (broadcast services standards act – 55%)

5. Export incentives

Exports incentives attempts to reduce the cost of production for exports by providers grants, loans, taxes, benefits, technical achieve for domestic business looking to export their goods.

In Australia, **Export Market Development Scheme (EMDG)** attempts to reduce the costs of production for exporters.

6. Tariff quotas

Form of protection where goods imported up to a certain quantity pay a standard tariff rate. Any amount of goods imported above the quota pays a higher tariff rate.

7. Voluntary export restraints are sometimes agreed by a country in change for a similar concession by the other nation

Extension – effect of tariff

Tariffs lead to a consumer and producer surplus:

Consumer surplus: The excess value attained by consumers when they are able to purchase products at a price below what they were willing to pay. (after the tariff is imposed the consumer surplus reduces)

Producer surplus: the difference between the minimum price a producer would accept to produce a given quantity and the price they actually receive. (producer surplus increases after the tariff is applied)

Key affect of Tariff: **Deadweight loss:** consumers value the good above the cost of obtaining it in the world market however cannot purchase it means that there is a net loss incurred by

The negative supply and demand shock amidst the COVID-19 pandemic has had significant ramifications on the Chinese economy prompting the government to implement a wide range of measures through monetary and fiscal policy to provide ongoing support amidst the outbreak. Against the backdrop of the pandemic China has adopted a more proactive fiscal policy stance with fiscal stimulus measures totalling RMB 4.8 trillion. In particular the central government has implemented tax relief measures towards households and firms worth 2.37 trillion yuan in 2020 while also allowing loan repayments of major firms to be deferred by 6 months. Additionally, fiscal subsidies totalling RMB 400 billion has been provided to firms in order to minimize unemployment, help cover interest payments and incentivize business investment. Moreover, as part of an expansionary monetary policy the People's Bank of China has engaged in a quantitative easing cycle through OMO and the reversal of repurchase agreements, injecting over 2.2 trillion yuan into the financial system. As such fiscal and monetary support demonstrated by an increase in the government's budget deficit to 12% of GDP (figure 2.2) has decreased the unemployment rate from 6.2% in February 2020 to 5.2% in December while also restoring business and consumer confidence leading to an increase in economic growth from -6% in January 2020 to 6% in 2021. As part of fiscal policy, the Chinese government further reduced the tariff rate from 15% to 7.5% on USD\$370 billion worth of medical imports. This has allowed the nation to gain access to greater volumes of cheaper high tech medical apparatus in order to effectively mitigate the effects of COVID-19 pandemic and improve health and economic development. Stabilisation policies have overall been effective in rebounding economic growth, thus maintaining employment, income and health of individuals allowing for an improvement in development.

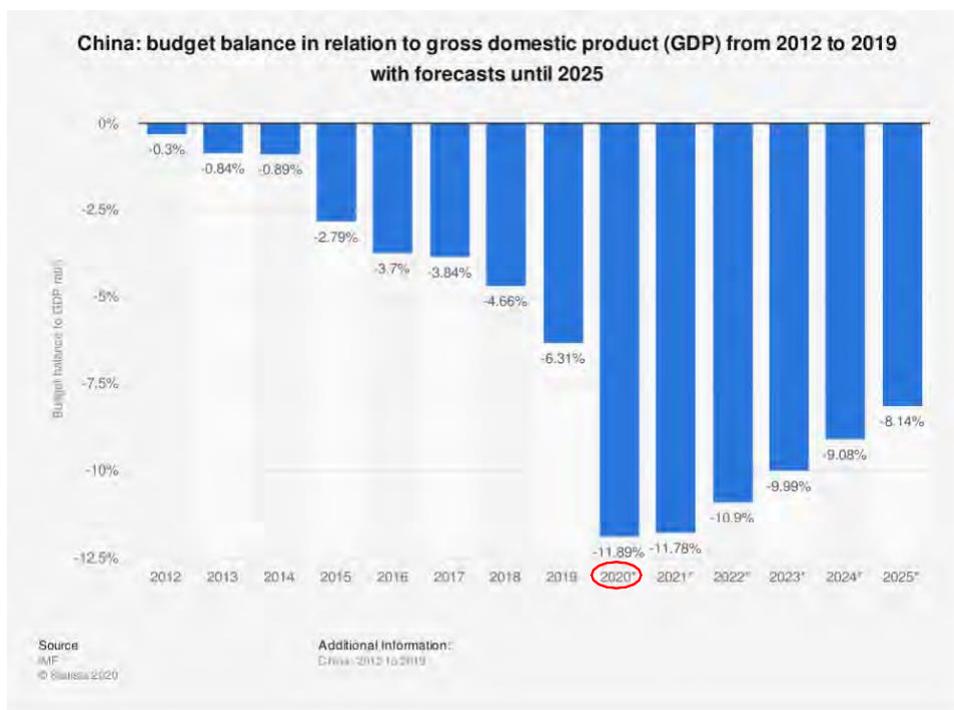


Figure 2.2

Australia's trading relationships with Japan and then China represent trade with rapidly industrialising economies which act as complimentary economies. Hence the next logical replacement for China would be India, where the Indian economy could almost entirely replace China's demand for Australia's exports. Alternatively, Australia could shift to focus its exports on the services sector (currently second largest export). In recent decades, Australia has grown substantial export markets for education services (2 billion to 20 billion between 2000 and 2019), financial services, insurance and tourism, as well as smaller markets for transport, health and communications services. – these services can be exported to the rising middle class in Asian economies.

Exports in 1963-64:

- 7.7%: China
- 22.4%: Japan
- 23.5%: United Kingdom

Exports in 2013-14:

- 36.7%: China
- 18%: Japan
- 1.4%: United Kingdom

Australia's top export markets 2019-20

1. China	35.3% of total share
2. Japan	11.8%
3. South Korea	5.8%
4. United States	5.8%
5. United Kingdom	4.4%
6. APEC & ASEAN	90%
7. Europe	8.4%

Australia's top import markets 2019-20

1. China	21%
2. United States	13.4%
3. Japan	5.8%
4. Germany	4.2%
5. Thailand	4.1%
6. United Kingdom	4%
7. APEC & ASEAN	83%
8. EU	16%

Other:

- Intellectual property (IP) protection in Korea to be broadly equivalent to Australian IP protections

Criticisms:

- There was backlash to the inclusion of an investor-state dispute settlement mechanism which allows foreign investors to resolve investment disputes often with the domestic government. Argued that this infringes upon the government's sovereignty as foreign corporations may sue sovereign governments if they feel changes to policy or parliamentary laws negatively impact on their profits.

Impacts of KAFTA:

- Removal on agricultural tariffs: beef X increased by 10% per annum
- Increased two way trade with Korea by 8.3% over last 5 years
- Increased inwards investment from Korea by 12.8% over the last 5 years
- Changes in goods trade under the KAFTA → GDP is projected by be \$650m higher by 2030
- Net increase in employment by 1,745 jobs in 2015 and 950 jobs by 2030 is projected due to the agreement

2. CHAFTA (China – Australia) {in 2014}**Goods outcomes: (dairy industry will save \$630m 2016-2025)**

- 98 % tariff free
- Significant removal in agricultural tariffs – dairy, beef, wine, horticulture, rice, wheat, cotton
- 93% of China's imports of resources, energy and manufacturing products will enter China duty free (removal on coal, copper, diamonds etc.)
- Allowed Wine X to double in 2018 to \$1Bn
- Angus beef X increased 200%
- Baby formula industry grown to \$1.5Bn when in 2010 it was negligible
- Hearing Aid industry decreased 5% tariff allowed Aus industry to grow to \$80Bn

Services outcomes:

- Law firms are able to establish associations with Chinese firms
- Tourism: Australian operators are able to operate in China.
- Financial: RMB clearing bank will allow overseas trading of China's currency for the first time
- Health: Australian health firms allowed to be established in China
- Largest source of full-paying education

Worker mobility:

- New investment facilitation arrangements allowed for infrastructure projects over \$150 million allowing Chinese companies to bring in Chinese migrant workers to

- Changes to the global economic conditions will influence demand for exports. E.g. when the global economy is in an upturn demand for exports rises. However, eventually if prices continue to rise too much then this can reduce the competitiveness of Australian exports and therefore reduce demand
- Tastes and preferences of global consumers will influence the amount of Aus exports

Supply for the AUD is represented by those who wish to sell the A\$. It is only effected by Australians. The supply is determined by:

1. The level of financial flows out of Australia for investors who wish to buy foreign currency and sell AUD
 - The level of foreign interest rates relative to Aus interest rates. Lower interest rates overseas will make investment savings overseas more attractive and hence increase the demand for the foreign currency.
 - Availability of investment opportunities overseas will determine how much money will flow out of Australia.
2. Speculators who expect the value of the AUD to go down will sell the AUD increasing its supply
3. Domestic demand for imports since Australian importers who buy from overseas need to sell A\$ in order to obtain foreign currencies to make import payments.
 - Demand for imports will be determined by level of domestic income (this will be dependent on Australia's economic growth)
 - Domestic inflation and competitiveness of domestic firms that compete with imports. If Australia's domestic inflation rate is higher and its import-competing firms are relatively uncompetitive, imports will be relatively cheaper than domestic products and demand for imports will be higher.
 - Preferences of foreign goods compared to domestic goods.

An appreciation refers to the increase in the value of an economy's currency in terms of another currency due to an increase in demand or decrease in supply.

A depreciation refers to the decrease in the value of an economy's currency in terms of another currency due to a decrease in demand or an increase in supply of the currency.

Only foreigners can affect demand for the AUD

Only Australian's can effects supply for the AUD.

e.g If a foreign takes out an investment from Australia it doesn't effect supply.

- The GFC which led to financial contagion and a global monetary shock caused a short term depreciation in the value of the AUD from 0.96USD in 2008 to 0.64USD in 2009
- This was primarily due to speculation and a herd mentality where investors pulled funds out from the Australian market to invest into a more secure USD or gold (“safe heaven”). Since 95% of currency trading is conducted through speculative activity, this large amount of capital flight in a compressed time frame exacerbated a sudden depreciation in the value of the AUD {can mention decrease in demand for exports due to lower economic growth}
- However following this depreciation, between 2009-2012 the AUD experienced a rebound and hence appreciated from 0.64USD to 1.05USD in 2013.
 - This was primarily due to the second phase of the mining investment boom: a period of rising commodity prices and increasing FDI allocated towards the mining industry
- A rise in commodity exports synergistic with the commodities boom and the rebound of the Chinese economy increased commodity prices, where the iron ore price rose to a high of 180USD per tonne in 2011. Due to the inelastic demand of iron ore, a rise in commodity prices was associated with increased export revenue and stable demand. As such the increase in demand for Australian exports increased the trade balance from a deficit of -3% to 1.5% of GDP overall reflecting an increase in demand for the AUD
- As a country which holds a comparative advantage in commodity exports, the growth in the mining industry reflected greater investment opportunities in Australian mining and thus over 80% of Australia’s mining industry is foreign owned. As such the increase in inwards capital was associated with greater demand for the AUD and a subsequent appreciation
- Moreover, strong economic growth amidst the commodities boom supported by a tightening of monetary policy has meant interest rates in Australia between 2010-2013 have been comparatively higher. This is reflected during the end of the mining investment boom where Australia’s cash rate was 4.75% while US fed reserve rate was 0.25% and Japan’s rate was 0.1%. As such prospects of a greater return on investment in Australia increased capital inflow and led to a steep decline in the NPY account. This reflected an increase in demand for the AUD, overall supporting an appreciation to 1.1USD in 2011

Effects:

- This led to a rising BOGS surplus in the short term due to the inelastic demand of iron ore and subsequent surge in export revenue {the effects of the J – curve were minimized}
- Undermined the competitiveness of non-mining exports due to the Dutch disease: The appreciation in the AUD diminished the exporting competitiveness of non-mining {demand in non-mining sector is more elastic} industries due to higher import costs for foreigners.
 - This damaged the already struggling PMV industry – closure of Holden, Ford and Toyota manufacturing plants – increase in structural unemployment -- a 1% rise in unemployment from 2011 -2014 – this was worsened since people in the manufacturing sector have non transferable skills requiring government payments {1.5 billion to help displaced workers}
 - X in services such as education and tourism also suffered where service exports decreased from 20% to 17% during this time period

boom in commodity exports, leading to the nations 4th biggest trade surplus in December 2020. Thus, the economic growth of China and rising commodity prices has increased the demand for the AUD by 30% since March.

- Additionally despite its reputation as a 'safe haven' speculators have lost confidence in the USD. This meant when economies such as China and Australia started reopening faster than expected and performing much better than the US, speculators became increasingly willing to hold Australian currency -> increasing demand
- Moreover, despite rising income due to stimulus payments the Australia's recession has driven greater savings, with the savings ratio increasing from 1.6% to 19.6%. Hence import consumption in Australia have reduced by 5.6% in October 2020, decreasing the supply of the AUD and supporting an appreciation
- Recently in the past month the growth of the AUD has begun to stagnate, with its value falling 2% between January and February 2021.
 - This is primarily due to speculation, where more certainty through the COVID-19 vaccine and Biden's \$1.9 trillion COVID recovery relief is expected to improve global economic conditions

{future expectations}

- Despite a recent appreciation, there has been uncertainty in the stability of the AUD due to threats in Australia's role as a major commodities exporter
 - Recently China's tastes and preferences have shifted away from Australian exports since implementing tariffs on Australian seafood, wine, barley and cotton. Moreover, jawboning by the Chinese government has led to China shifting away from Australian exports of coal and more towards Russia and Indonesia. As such this is likely to deteriorate Australia's trade balance and reduce demand of the AUD, causing a depreciation
 - Moreover, more environmentally focused economic policies from the Biden administration threaten Australian exports of fossil fuels. Since fuels exports comprise 25% of Australia's exports, a shift towards greater environmental sustainability sentiments driven by the Biden administration is likely to reduce Australian exports causing a subsequent depreciation.

7. Impact on the government

Increase in inflation -> increase in welfare expenditure due to greater inequality
Higher inflation will also support government revenue (GST)

Benefits of inflation

- Avoid deflation. Impacts of deflation:
 - o Decrease d'd --> recession
 - o Decreased incentive to borrow money --> since value of the original debt will be greater than that of the asset
 - o Deflation reduces profit for businesses (price decrease) --> unemployment
 - o Loss of investor confidence --> reduced investment etc.
- As such positive inflation avoid the above issues with deflation
- Inflation also decreases the real value of debt overtime since debt is a fixed quantity and inflation causes an increase in wages

Unemployment

Unemployment refers to a situation where individuals want to work but are unable to find a job and as a result labour resources in an economy are not utilized. Reflects people who are not employed but are actively seeking work.

Labour force

Labour force is the section of the population 15 years or above who are working or actively seeking work. **Labour force = Employed + Unemployed**

Influenced by the size of the population, level of migration, age distribution, participation rates.

Participation rates

Percentage of working age population in the labour force

$$LFPR = \frac{\text{Labour force}}{\text{Working age population}}$$

Unemployment rate

Labour force which is not employed but actively seeking work.

$$\text{Unemployment rate (\%)} = \frac{\text{Number of person unemployed}}{\text{Total labour force}}$$

Underutilisation rate = unemployment rate + underemployment rate

- Sources of economic growth
 - o Factors influencing AD
 - Consumption (**income**, consumer expectations, **I/R**, distribution of income)
 - Investment (**cost of capital equipment, business expectations**)
 - Government expenditure (**discretionary changes, non-discretionary changes**)
 - X & M (domestic and overseas income, exchange rates and international competitiveness, consumer tastes and preferences)
 - o Factors influencing AS (efficiency and technology)
 - Quality and quantity of natural resources (capital widening and capital deepening)
 - **Supply of capital**
 - **Investment in new technology** – has a multiplier effect
 - **Productivity**

Causes of unemployment

- Causes of unemployment
 - o Economic growth
 - o Macroeconomic policy (in response to EG)
 - o BOP constraint (in response to EG)
 - o Productivity
 - o Participation rates
 - o Structural change
 - o Labour costs

M – macroeconomic policy

P – participation rates

C – labour costs

G – economic growth

P – labour productivity

S – structural change

Causes of inequality – contemporary

- Changes to social security payments and cuts to family payments
- Income tax cuts in mid 2000s benefitted those with higher incomes {tax reform}s
- Slow wage growth
- Decentralisation of the labour market {enterprise bargaining}
- Growth in part-time employment and rising levels of underemployment

More causes

- Labour market reforms
- Economic growth (particularly the mining sector)
- Social: English speaking, migrants, geographical location, migration rates

Causes of unemployment

- Economic growth
 - Economic growth and fluctuations in the business cycle is influenced by the level of AD through consumption and investment within the economy. Since the labour is derived from the d'd of goods and services an increase in EG / AD → decrease in unemployment. On the other hand, a contraction within the global economy and fall in AD → a decrease in **cyclical** U/E.
 - During the COVID-19 pandemic consumption reduced -2.7% (2020) leading to a 7% contraction in eco growth (July 2020) → increase in **cyclical** U/E to 7.5% (labour market is significantly above the NAIRU)
 - In response to level of economic growth within the economy, the government will attempt to smooth out fluctuations in the business cycle through the implementation of fiscal and monetary policy – by either taking an expansionary or contractionary stance. An expansionary macroeconomic policy during an eco-downturn → increase AD and d'd for labour → decrease in unemployment whereas a contractionary stance would cause an increase in U/E. Due to the current economic downturn the RBA has implemented an expansionary MP, reducing the cash rate to 0.1% and undertaking a \$100 billion dollar quantitative easing scheme. This in combination with government wage subsidies through the JobKeeper → increased level of AD seen particularly evident within the housing market → 3.3% increase in consumption and 3.8% increase in private investment in 2021 → reduction in U/E to 5.6% (December Q 2020).
 - Productivity
 - The productivity of labour will influence the level of output and efficiency within the production process. An increase in labour productivity and output per unit of labour will in the short-term increase unemployment since when operating at a fixed level of supply less labour is required per unit of output. However, in the long term the increase in labour productivity relative to other factors of production will lead to capital substitution, thus reducing the level of unemployment. Conversely a fall in labour productivity → decrease in unemployment since more labour is required to produce the same level of output. However in the long term labour will be substituted with capital to maximize efficiency and EOS -> increase in unemployment
 - Labour market productivity growth is well below the market sector's long run trend rate of 2.2% per year, with labour productivity growth being well under 2% since 2016 and was a 1.2% in 2019. This has somewhat contributed to slight increase in U/E in 2019. Low labour market productivity growth in the future relative to other advanced economies --> increase rate of labour-capital substitution and increase U/E
- Cause for the ↑ in the underemployment rate (excess supply in the labour market)

- Fall in labor productivity
- Fall in multifactor productivity

- Closure of inefficiency industries has led to an increase in structural unemployment → forces governments to increase expenditure on unemployment benefits and training programs
- Has also increased income inequality as high-income earners and asset earners enjoy benefits of MER

Environmental management policies (check essay for most of this)

Address enviro sustainability issues such as:

- Preservation of natural environments
- Addressing pollution and climate change
- Managing the use of renewable and non-renewable resources

However increases costs for firms and individuals and hence can conflict with goals such as unemployment and EG.

{intergenerational equity, ecological sustainable development}

1. Regulations

Laws or rules which govern economic behavior. They are traditional policy tools for addressing environmental sustainability goals.

2. Market based policies

Involve financial incentives or disincentives to influence the behavior of households and firms: taxes and subsidies.

- Taxes

Shift in the supply curve to the left which increases the market prices and decreases quantity. **This internalizes the externality as consumers or producers will have to pay for the environmental cost.**

- Subsidies

Government provides grants to producers to reduce production costs and promote environmentally beneficial activities.

- Targets

Use of targets to guide environmental policies

- International agreements

International agreements recognize that collective international actions is required to address global environmental problems.

- E.g the removal of the two-airline policy allowed for the emergence of low-cost airlines such as Jetstar and Tigerair
- ↑ in the number of domestic flights from 15 million in 1990 to 60 million in 2015
- Competition and Consumer Act (2010) established to protect business rights, regulate the industry and prevent anti-competitive behaviour:
 - Bans monopolisation, price discrimination between markets, collusion and price fixing and exclusive dealing.
 - Competitive neutrality: ensuring a level playing field for government business enterprises and public trading enterprises where they are forced to compete with the private sector
 - Manages anti-competitive behaviour: Visy and Amcor price fixing
 - 3rd party access to infrastructure, where businesses who own a monopoly infrastructure asset must give competitors access to the infrastructure at a reasonable price. Includes Telstra who was fined for excessive charging for access to network

Stats:

- Inflation has decreased from 10% in 1980s to 2-3% now
- ↓ in telecommunication prices by 30%
- Electricity bills ↓ by 30% and gas prices by 50% for major industrial use

{Reform of publicly traded enterprises}

- Public trading enterprises are government owned companies → receive government funding / support and hence reduce competition in markets and the incentive to maximize productivity and efficiency
 - Hence the government opted for corporatisation and privatisation
- Corporatisation: encourage PTEs to operate independent of the government without political supervision
 - They must compete with the private sector and operate in competitive markets without government support and subsidies with the incentive to maximize profit. E.g. Sydney Water, Australia Post
- Privatisation: involves the selling of a PTE so they become privately owned
 - Businesses which were previously government owned operate under private costs → increasing incentive to maximize profit. These businesses operate under more traditional pricing behaviour → increases overall competition in specific industries
 - Australia has 2nd most privatised businesses in the OECD
 - Estimated that productivity increased 60% in the electricity and water industries, and doubled in the transport and telecom industries in the 1990's.
 - Most recently, Medibank was privatised in 2014 after 38 years of government ownership: their profit increased by 55% in just 4 years of privatisation

{Removal of protectionist policies}

- Prior to the 1970s, Australia was a highly protected economy with an average tariff rate of 30% on almost all imported goods in industries such as manufacturing, agriculture and TFC industries → lead to significant inefficiency and loss of productivity as there was a misallocation of resources towards inefficient industries

Fair Work Act 2009

The current Australian labour market legislation, Fair Work Act 2009 set out the rules for the national workplace relations system. Involved: **legal framework** for determining → minimum employment standards, minimum wages, modern awards, enterprise agreements and employment contracts.

- Set of 10 national employment standards covering matters such as hours of work and leave entitlements, providing a safety net for workers in the national system.
- National minimum wage
- Modern awards: more streamlined award system of determining wages and working conditions for employees specific to their industry, job classification and level of skill. They contain a **flexibility clause where wages and conditions can be negotiated between employees and employers to meet specific enterprise conditions.** (4000+ to 121)
- Enterprise agreements and common law contracts: BOOT test
- Conciliation & arbitration (A is the legally binding one) (other one is collective bargaining)
- **Overall with the aim to raise productivity more streamlined dispute resolution system and safety nets: greater economic and employment growth** {greater flexibility in enterprise agreements etc} {number of industrial disputes have reduced from 90 in 2016 – 30} (working days lost has decreased from 110 in 2012 to like 20)

Simplification of the awards system has made it easier to higher labour -> casualisation of the workforce

Skills for the future package in 2006 committed \$850M to support skills creation in the VET sector.

The Realising Our Potential package in the 2007 budget increased funding for university, vocational and school education, vita for increasing labour force skills, productivity and participation.

- **Stat: Employees on Awards fell from 23% in 2000 to 16% in 2012 and enterprise agreements rose from 37% to 42% over the same period**

One microeconomic policy used in Australia is the implementation of universal education. This provides all children with opportunities for educational attainment, regardless of their socioeconomic background. This is important as lower income families would otherwise lack the financial resources needed to pay the price of their child's tuition in full. Increasing the level of educational attainment of children, especially those from lower socioeconomic backgrounds, will provide them with better prospects in finding higher paying jobs in the future. This may help poorer families to remove themselves from a vicious intergenerational-poverty cycle.

- Over the past two decades, the RBA has been primarily successful in pre-emptively implementing MP in order to achieve economic objectives of price stability and full employment
- Monetary policy is a macroeconomic policy where its countercyclical nature aims to influence the level of demand within the economy and smooth out fluctuations in the business cycle, thus influencing the economy's ability to achieve price stability and full employment
 - Full employment also known as the non accelerating inflationary rate of unemployment refers to the natural rate of unemployment at which there is no cyclical unemployment within the economy and only structural and frictional unemployment exist. Price stability on the other hand is the objective of achieving stable inflation of 2-3%
- Since MP control was handed to the RBA, it has been an extremely effective macroeconomic policy tool, allowing Australia to achieve an average inflation rate of 2.5% while further being able to reduce unemployment in the long term from 10% in the 1990s to an average of 4-6%. However it is also important to consider the effects of LTMER, FP and X d'd in contributing to this
 - However, most recently during the COVID-19 pandemic MP has been rendered ineffective. This is due to its limitations:
 - Liquidity trap, blunt tool, inability to impact supply, long impact time lag
 - This has resulted in the RBA having to implement unconventional MP

Theory

- Monetary policy involves the control of the cost and supply of money within the economy to achieve its key objectives of:
 - price and exchange rate stability, full employment and the general economic prosperity and welfare of the Australian people
- Monetary policy is conducted through changes in the cash rate. The cash rate refers to the interest paid on funds in the short term money market (or the overseas cash market). The cash rate is changed through shifts in the interest rate policy corridor. As shown in diagram ... the interest rate policy is defined by a price floor and price ceiling around a cash rate target ...
- Changes in the cash rate in turn influence key outcomes in the domestic economy such as employment and inflation through the various channels of transmission:
 - Savings investment, exchange rate, cash flow, asset price
- In 1983 the RBA implemented inflation targeting by setting a target range of inflation of 2-3%: this was a significant reform factor in allowing the RBA to anchor inflationary expectations and achieve stable inflation in the LT without having to influence interest rates: 10% in 1990 to an average of 2.5% (in the middle of the target)

Bodies

GFC

resulted in 30% ↓ in average domestic airline tickets thus reducing cost push inflationary pressure

- Moreover the policy facilitated the establishment of the Australian competition and consumers act: which banned monopolisation, price discrimination, price fixing, colluding etc.
 - The policy ensured for competitive neutrality: where by banning monopolisation and reducing government assistance to privately owned ensured for a level playing field between government owned enterprises and private firms -> ↑ in overall levels of productivity -> force innovation, efficiency to ↑ AS in the LT: gas prices reduced 50% for major industrial use
 - Furthermore manages anti-competitive behaviours such as Visy and Amcor price fixing → ↑ competition in markets
 - Facilitated third-party access to infrastructure : for example large telecommunication firms such as Telstra were forced to provide access to smaller competitors: ↑ competition within the industry and reduced telecommunication prices by 30%
- Hence overall by promoting competition: ↓ in inflation from 10% to 2-3% in the past 2 decades
- The increase in competition further force innovation and ↑ efficiency: ↑ in multifactor productivity and Economic growth.

Reform of publicly trade enterprise:

- Moreover, government implemented significant reforms in publicly traded enterprises: to ↑ in the overall level of competition -> effective in promoting economic growth / more stable inflation.
- Publicly trade enterprises: enterprises which are managed and financed by the government: due to their financial support they generally have a lack of incentive to innovate / ↑ efficiency -> further ↓ competition in product markets since they have an artificial advantage
- Government opted for corporatisation and privatisation:
 - Corporatisation is when a government removes funding / provision / control of PTE -> where the businesses are forced to operate under more traditional pricing methods without financial support and an artificial advantage. In this case the managers are accounted for in terms of their profitability and hence are forced to compete with the domestic market and operate under more traditional pricing methods and managerial stance. Now accounted for their profit: incentivised to ↑ productivity and efficiency
 - Privatisation: selling of the government owned enterprise to the private sector
 - Private sector do not receive financial support from the government and are accounted for by their actions to satisfy stakeholders: hence must return a profit -> hence are similarly driven to maximize productivity and efficiency to gain a cost-advantage:
 - The privatisation of Sydney water and electric industries is expected to have increase their productivity by 60%
 - Further reflected in the privatisation of Medibank in 2014: who experienced a 55% increase in profit just 4 years after privatisation
 - Hence ↑ in productivity response for the ↓ in inflation