

Submission to Inquiry into Australia's financial system, 2014

In this submission, 'public' means Government-owned, and 'private' means non-Government-owned.

It would be generally agreed that Australia should have a financial system which is, sustainable, equitable, and supportive of a prosperous society.

This submission relates to the ROLE OF GOVERNMENT in the financial system, in particular probably the most important but least examined aspect of our financial system, the creation and distribution of money.

Currently in Australia:

1. Practically all money (except for banknotes and coins) is created as debt.
2. This money is created out of thin air by private banks for private profit.

The percent of debt-free money in the form of banknotes and coins has steadily decreased over the years, such that now less than 5% of our money supply is produced debt-free.

Hence, the more the money stock grows, the more debt there is, so our society is floating on a sea of debt, upon which more and more interest must be paid, depending of course on interest rates. This current system advantages a financial elite at the expense of the Government and general population. The proposals here would address this imbalance whilst still allowing private banks to operate profitably and provide good returns to shareholders.

This current arrangement is neither equitable nor sustainable, and our financial system should be restructured to make it equitable and sustainable. There are various ways this could be structured, but the key point is that Government should create debt-free a significant percentage of the money supply for circulation in the community.

Implementation

The aim is to evolve our financial system into one which is sustainable, equitable, and provide a basis for a prosperous society, and arranged in such a way as to minimise the potential for excessive inflation.

There are 2 aspects to consider:

1. The creation of debt-free money
2. How this money is to be distributed

Creation of money:

The Australian Government, either through its own Treasury, the RBA, via creation of a Public bank, or another independent body set up for the purpose, should create, debt-free, all the money it needs for its own operations. As current Government bonds mature, it create the money to pay out these bonds. Eventually our Government would become debt-free. The amount created could be limited by some feedback formula or by the charter of the independent body administering this money creation. Taxation arrangements could be amended from time to time if necessary to stabilise Government income.

What percent of the money stock should be created debt-free?

For the purposes of discussion it is suggested a figure of 25 to 28% would be appropriate. Economies have often functioned, and tended to function better, during periods when the money stock had a more appreciable debt-free content. For instance in Britain for the period 1950 to 1963 when, due to greater use of cash, the debt-free component of the money stock was around 21%, inflation was low, employment high, and growth was steady (1)

Distribution:

Money could be granted or lent by this public bank/Treasury/RBA at very low interest to the Commonwealth, State and local governments for their operations.

The existing private banking structure could be left as it is and lent by the Public bank/Treasury/RBA the money it needs to carry out its operations. This money could be lent to public and private banks at low but variable interest depending on economic conditions and policy,---- say 0.5% plus a risk adjusted premium based on the results of regular prudential audits. These banks could then lend money to individuals and businesses at competitive rates as per at present for normal banking operations. The only change for private banks is that they could not create credit (money) out of thin air, but have to borrow it from the Government. In addition, a public bank, or banks (say owned by individual States) could operate in tandem and competition with private banks in general banking operations. Current Australian prudential standards would apply to licensed banks .

Critics, particularly those who benefit most from the current system would contend that such an arrangement would be inflationary, but properly structured and managed this need not be so. For instance, the goods and services we buy have a lot of interest costs embedded in their price. By creating a proportion of the money supply debt-free, the interest cost component of goods and services would be reduced, making them cheaper.

Benefits

Such a system would have many benefits, such as:

Many taxes could be reduced or eliminated. An alternative to tax reductions could be the granting of a basic wage (perhaps means-tested) to all adult citizens. This would relieve the Government of the enormous administrative burden of dealing with a raft of pensions and welfare payments of all kinds. Reducing taxes would help level the playing field between Australian-based companies who pay full taxes and their foreign-based competitors who minimise taxes by manoeuvres such as transfer pricing.

Major works and nation-building projects that would otherwise be too expensive or uneconomic could be implemented, creating employment and economic activity, e.g long-distance high-speed rail links, investments in energy-efficiency, public housing etc.

The need for bank reserves could be reduced. Imaginative structuring could effectively comply with Basel accords at low cost. For instance, the Government could maintain a reserve fund (created debt-free as needed) which could be allocated as a reserve fund for all licensed banks, relieving them of the need to carry non-earning reserves on their books. Australian banks from time to time complain about the high costs of sourcing money overseas to carry out their activities. This issue would be eliminated under this proposed arrangement.

The financial system would be more transparent and the playing field more level.

Notes:. Public banks have operated successfully in Australia before. For instance the then Government-owned Commonwealth Bank shepherded Australia very well financially through the First World War. Some of the most successful modern economies, such as Taiwan, South Korea, Brazil and China have very large and successful public banking sectors which are playing a large part in their ongoing prosperity.

In the USA, the only state (at least until 2013) with a public bank is North Dakota. This long-standing public bank is highly profitable for the state and its citizens. In addition North Dakota has no state debt, has the lowest home foreclosure rate in the country, the lowest credit card default rate, and the lowest unemployment rate.

In summary, Australia should setup a system which provides debt-free money for Government activities, and low-cost money to the private banking system. There is a variety of ways this could be done, as long as it achieves the result of an equitable, sustainable and sound financial system.

“It doesn’t matter if a cat is black or white, as long as it catches mice.” Deng Xiaoping

Ref: “The grip of death’, Michael Rowbotham, 1998

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