FOR PRESS

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23 December 1972
(Eastern Summer Time)

STATEMENT BY THE PRIME MINISTER

THE HON. E. G. WHITLAM, Q.C., M.P.

EXCHANGE RATE OF THE AUSTRALIAN DOLLAR

It has been decided to revalue the Australian dollar. The International Monetary Fund has been consulted and has concurred with this decision.

The gold parity of the Australian dollar, expressed in terms of U.S. dollars, will be changed from the present $US1.2160 = $A1 to $US1.2750 = $A1, representing an appreciation of 4.85 per cent. At the same time, the market rate will be fixed until further notice at the new parity. This will mean an overall appreciation of 7.05 per cent over the present market rate of $US1.1910 = $A1.

As well, it has been decided to strengthen the existing measures to control the volume of capital inflow. The present embargo on overseas borrowings which are repayable, or carry options to repay, within two years will be continued and its coverage will be broadened. This measure will be supplemented as from today by the introduction of a variable deposit requirement scheme in respect of borrowings with a maturity in excess of two years. Under this scheme, borrowers will be required to lodge a proportion of the proceeds of overseas borrowings in a special account with the Reserve Bank, on which no interest will be paid. This deposit will be held frozen until the time of repayment of the borrowing, at which time it will be released to the borrower. Initially the deposit requirement will be fixed at 25 per cent.

The Governor of the Reserve Bank will be issuing a separate statement giving further details.

The purpose of these measures is to correct the fundamental disequilibrium in Australia's balance of payments. That such a disequilibrium exists has been clearly evident for the past twelve months or more. It is taken for granted by Australia's own business community, and is being increasingly recognised abroad.

In the calendar year now ending, there was an overall surplus in Australia's balance of payments of some $2,000 million. This huge surplus was attributable both to an excessive rate of capital inflow, especially in the form of borrowings, and to a large and unprecendented excess of exports over imports of goods and services. The outcome of these trends, in combination, has been to swell our holdings of official reserve assets to almost $5,000 million, over three times their level of only two years ago. No responsible Government could allow such a situation to continue.

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Because they do not necessitate immediate and drastic solutions in the same way as do the opposite problem of low and falling reserves, it is sometimes supposed that fast-growing reserves are not a problem at all. But they are a problem. They represent a waste of potential resources at our disposal, they are potentially inflationary, they make more difficult the task of effective economic management, and in themselves they raise expectations of exchange rate changes which in turn lead to still further reserve increases.

That being said, I want to make it clear that our decision to appreciate the exchange rate does not derive principally from the fast growth in our overall balance of payments surplus and reserves, which have been heavily influenced by the large inflow of capital from abroad. Rather, it is a product of developments in our current account. From a position where, in 1968-69, Australia was incurring a current account deficit of over $1,000 million, we have moved progressively into surplus.

The particular strength of the current account at the present time does, it is true, owe something to the depressed level of imports which has resulted from the slow-down in the economy during 1971-72. As overall activity in the economy picks up, so will the level of imports. But so, we believe will the level of exports, as our major markets abroad grow apace and their demand for our products increases. In short, while we both expect and will welcome the growth in imports that 1973 will bring, we see no likelihood of the overall current account position being transformed as a result.

The rapid growth of Australia's export and import-competing industries which underlies this progressive strengthening of our current account is, in itself, a matter for satisfaction. But the foreign excchange earned from the proceeds of exports is of no value to Australians, unless it can be used to enlarge the real resources actually available for use within our economy. It has been clear for some time that, with our previous exchange rate, this was impossible.

The appreciation of the Australian dollar will have differing effects on different sectors of the economy. Some groups will initially be advantaged, other disadvantaged. Maintaining an undervalued currency can bring temporary gains to some sectors of the economy; but in the medium and longer term these gains are illusory because of the harm which the resulting inflationary forces inflict on each and every member of the community.

The Government's responsibility is to the Australian people. It is their interests that we have kept centrally in mind in taking the decisions I have announced today. Gains and losses to individual sectors of the community - gains and losses which in any event are of a once-for-all character - cannot be allowed to over-ride this primary consideration.

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The Government recognises that some of the rural industries, which are already facing difficulties and problems of adjustment to changed circumstances, may find it particularly difficult to bear the consequences of the exchange rate appreciation. Should this prove to be the case, the Government will be prepared to examine sympathetically the position of those industries and take such action as may be necessary, in their case, to ease the processes of adjustment to new conditions.

In the Government's view, any appropriate appreciation of the exchange rate would not in itself be sufficient to deal fully with the problem of excessive capital inflow, although it is an essential prerequisite to tackling this problem successfully. That is why we have also moved specifically to restrain the inflow of foreign capital by the introduction of the deposit requirement scheme. That scheme will raise the effective final cost of overseas borrowings and will thereby deter such borrowings. At the level of 25 per cent at which the deposit has initially been set, the effective interest cost of funds borrowed overseas will be increased by one-third. For example, a borrowing at 6 per cent will now effectively cost 8 per cent to any borrowers who still wish to proceed.

Action of this kind is long overdue. The former Government took some steps, three months ago, to discourage some forms of capital inflow. The action then taken had been long delayed, it was of a very modest kind, and it dealt with only part of the problem. The result of this delay has been a build-up of domestic liquidity to a dangerously excessive level.

This Government will do everything within its power to remedy this situation. We accept the responsibility for managing Australia's affairs in the interest of Australians, and we are determined to establish and maintain the conditions that make this possible.

The former Prime Minister announced in September that his Government was examining further means of giving effect to the aim of ensuring that overseas capital was employed in Australia in real partnership with Australian-owned capital. This Government has a similar objective: the difference is that we are prepared to take, and we will take, decisive measures to give effect to that objective.

The impact of the deposit requirement scheme will be on capital inflow, and the main initial impact of the appreciation of the exchange rate will also be on the capital account of the balance of payments. But as I have said, the appreciation of the Australian dollar is chiefly directed, in the medium and longer run, towards adjusting the quite excessive strength of the balance of payments on current account.

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In the months immediately ahead, the effects in this latter regard will be relatively small. It has been the recent experience of all countries adjusting their exchange rates - and all of the main trading countries of the world have done so in recent years - that the chief effects of adjustment on the current account occur only after some considerable time. This is only to be expected.

In Australia's case the delayed reaction of exports and imports to the exchange rate change will work to our advantage, because quick reactions - if they were to occur - might slow the process of recovery in economic activity and delay the return to full employment. Given the time-lags, we do not see that as a danger. However, in the unlikely event that the reactions were felt more quickly than we expect, the Government would not hesitate in taking appropriate internal measures to offset any such developments.

In the longer run, of course, the somewhat slower growth of exports and the rather faster growth in imports which exchange rate appreciation will bring will be very much in Australia's total interests. It will increase the real resources at our disposal, and will therefore materially assist us, as a Government, in maintaining the strong forward momentum of the economy and providing the real resources which will be involved as we come to introduce the policies and programmes we have promised to the Australian people.

In recent years, the trends in our balance of payments have meant that the resources available for use within Australia have risen more slowly than Australian production. As the Government progressively establishes conditions in which available resources can expand more rapidly - and the decisions I have announced today are an essential ingredient of those conditions - so it will be possible for us to improve materially the living conditions of the Australian people, both in their quantitative and, importantly, their qualitative aspects. That is the task to which we have set our hands. Our decisions which I have announced today will assist in its achievement.

CANBERRA. A.C.T.

23 December 1972