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STATEMENT BY THE PRIME MINISTER,

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

MEASURES TO STEM INFLATION

Inflation is the major economic problem facing us today. It is robbing people by reducing the purchasing power of their savings. It is altering the distribution of income in an arbitrary and often vicious way. It is distorting resource allocation and encouraging a rush into supposedly inflation-proof real assets such as land or housing. It is anathema to all of us - and rightly so.

Inflation must be fought on all fronts. There is no panacea; no simple solution achievable through one line of policy. But the fact that there is no simple solution to inflation does not mean that we can just throw up our hands in the face of it. On the contrary, we have to tackle it head on.

One obvious area of concern is the broad field of monetary policy. The money supply increased in 1972-73 by 26 per cent. Most of that increase is traceable to developments in calendar year 1972. Actions we have taken since the election have considerably slowed the rate at which money is being injected into the economy. But present prospects are for a further over-large increase in the money supply in 1973-74. Such an outcome would be entirely inappropriate if we are to stand any chance of reining in the rate of increase of prices. We are determined that it must not occur.

Two initiatives are therefore being taken which together will have the effect of producing a sharp cut in liquidity.

First, in the market for Government securities, the Reserve Bank will, with the concurrence of the Government, press its open market operations vigorously with the aim of significantly increasing sales of Government securities. This will both mop up funds in the hands of the private sector and reduce the liquidity of private sector holdings of financial assets. In the process, a sharp rise can be expected in interest yields on existing issues of Australian Government securities and, in due course, in rates to be offered on new issues. Substantial increases in other interest rates will follow as effects of the operations spread through other markets for funds.

Increasing interest rates is not something to be undertaken lightly. But curbing the increase in liquidity and the money supply is an essential pre-condition if inflation is to be countered at all. We do not seek higher interest rates for their own sake. They are needed in order to make the purchasing and holding of government securities more attractive, which they must be if they are to compete effectively with alternative forms of investment. If, as a consequence, the higher interest rates have the effect of curbing the speculative rush into land and property, that will be all to the good.

The effects of this measure will be chiefly felt within the domestic economy. We have, however, also paid close regard to the state of our external accounts. There is a particular reason for doing so in this context: our prospective continuing external surplus (on both current and capital accounts) is itself a primary source of the strong growth of the money supply which is in prospect over the year ahead.

Measures were, of course, taken late in 1972 and in February 1973 to restrict capital inflow and reduce the external surplus. The tariff cut of last July will also have in due course a further significant effect in that direction. None the less, in 1973-74 reserves again seem likely to increase strongly from a level which still remains excessive.

After close and careful examination of the present situation and prospects in these regards it has been decided to appreciate the exchange value of the Australian dollar.

The exchange rate change will establish a new formal parity of 28.3848 Australian dollars per fine ounce of gold. This represents an appreciation of 5 per cent from the former parity. On this basis the rate for the U.S. dollar will become $A1 = $US1.4875 instead of the former $US1.4167.

This further appreciation in the exchange rate will help to reduce the growth in reserves and thereby moderate the growth in the money supply emanating from that source. It will also help to keep down the prices of imports. Figures published by the Statistician on 5 September indicated that, following the revaluation of Australian dollar last December, import prices fell by

5 per cent between the December quarter of 1972 and the June quarter of 1973. The appreciation will also serve to dampen somewhat the effects in domestic markets of high prices on world markets for exportable goods.

As on the occasion of the December 1972 revaluation, the Government stands ready to examine sympathetically the position of any industries which are seriously affected by, and find it particularly difficult to bear, the consequences of today's appreciation. It will take such action as may be necessary, in such cases, to ease the processes of adjustment to new conditions.

The International Monetary Fund has been notified of our decision on the exchange rate and we are anticipating its concurrence. The Governor of the Reserve Bank will be making a separate statement giving further details.

Canberra, A.C.T.

9 September 1973.