

MACROECONOMICS AT WORK EXERCISE

MACROECONOMIC CONDITIONS AND POLICY

REFERENCES: ‘RBA signals interest rates on hold’ (by Morgan Mellish), ‘The next move may be down’ (by Alan Mitchell), ‘Farm output will rally next year’ (by Alan Mitchell), ‘Signs of oversupply in investor property’ (by Craig James), ‘World recovery falls short of the mark’ (by Morgan Mellish) and ‘Plenty of life left in the profits of boom’ (by Cherele Murphy), *Australian Financial Review*, 12 November, 2002, pp. 1, 6 7.

CHAPTERS RELEVANT TO THIS EXERCISE: Chapters 11-16.

OVERVIEW

This series of articles in one day’s *Australian Financial Review* followed the announcement by the Reserve Bank of Australia of its decision not to alter interest rates, and its more general quarterly statement on monetary policy. The articles relate to the major macroeconomic variables that determine economic policy and, in particular, *monetary* policy. The overall prediction about economic conditions (and hence the rate of economic growth) is (in the term used in the article) ‘downbeat’. Also noted are the comments of the Treasurer that ‘the risks we see on the economy are on the downside’. In contrast to the situation earlier in the year, when the concern was rather with the possible inflationary pressures of strong economic growth (and hence the widespread view that interest rates would be raised by the RBA during the remainder of the year) the consensus now is that interest rates will be kept ‘on hold’ and indeed (as the headline of one of the articles puts it) ‘the next move may be down’. Other articles review some of the major variables influencing aggregate demand and inflation and thus likely to be major determinants of monetary policy.

QUESTIONS

1. What predictions are made about ‘farm output’? Explain the significance of this variable for economic growth and macroeconomic policy.
2. Why might it be the case – and on what basis is it argued in fact – that the housing boom is abating? What is the significance of this for monetary policy?
3. How do you interpret the headline ‘Plenty of life left in the profits of boom’ and what is the significance of the observation?
4. What generalisations can be made about ‘global’ economic growth and what implications does this have for the Australian economy and economic policy?
5. Why is it widely accepted that the Reserve Bank has done the ‘right thing’ in keeping interest rates constant?

6. Explain how it is that, whereas earlier in 2002 (up to say June or July) it was widely believed that the RBA would be *raising* interest rates over the second half of the year, in November it was being argued (as in one of the articles) that 'the next move may be down'.