

Scratch an economist who proffers sage words about the state of government debt and you will find someone who believes we are at full employment. If we are below full employment, then the government can monetise debt via quantitative easing and undertake fiscal expansion. That is, we can have more spending without contributing to debt. Spending may involve scaling up policies to among other things: encourage R&D in our exports; transition the economy to low carbon energy sources; fight domestic violence; pivot our manufacturing sector away from cars to other elaborately transformed manufactures or re-build our marginalized technical education sector. This list is far from exhaustive.

Success of QE in the UK and USA

On most accounts, quantitative easing, or QE, has been responsible for the near continuous growth of the US and UK economies since 2009. By most measures, both economies have improved. Home prices, gross domestic product, the total number of jobs and industrial production have all risen. And both UK and US stock markets have trebled since the trough of early 2009. But are there limits to the amount of quantitative easing that an economy can bear? Yes, of course. Taken to an extreme it can cause prices, especially asset prices to rise too quickly. But the question is are we anywhere near this extreme?

Will it create inflation?

There is little reason to be concerned that fiscal expansion financed by QE will lead to wage inflation. In the Australian context, 'too much' fiscal expansion occurs when a higher demand for workers (a good thing) is accompanied by average wages that rise faster than productivity (a bad thing). It may lead to an inflation spiral (also a bad thing). But we know that strong demand for workers does not always explode into inflation. Witness the recent mining boom. Runaway wages in a few areas but with a limited spread to other parts of the economy.

Reserve Bank believes labour market has spare capacity

According to [Ballantyne, De Voss and Jacobs](#) at the Reserve Bank, creating unemployment is less effective way to moderate inflation than previously. The Reserve Bank estimates that

there is currently considerable spare capacity in the labour market. This is economist-speak meaning that there is room to raise employment without sacrificing productivity levels or inflation rates. In any case, Australia in 2016, does not have an inflation problem, and if it did, we should be as concerned about a growth of export demand as we are about an increase in government spending.

Unhealthy asset price inflation?

So will fiscal expansion with QE lead to unhealthy asset price inflation? Or should I say, exacerbate asset price inflation, for growth and volatility in asset prices is a normal consequence of a private investment behaviour. Yes, QE can have this effect. It is actually the desired, not undesired, goal in the US and UK. In Australia is it not as desired. But this does not mean we have to sacrifice the job prospects of 700,000 unemployed Australians in order to tame housing prices. The edge can be taken off excessive housing prices by other policies such as the removal of negative gearing or the removal of interest payments from as allowable tax deductions. There is no reason why the provision of jobs for the 700,000 should be sacrificed for the profits of investors in assets.

Are the unemployed employable?

Are there reasonable prospects that more jobs for unemployed people in Australia will cause a wage inflation spiral? Who are these people and what are their skills? About half of the 700,000 had post-school qualifications – an estimated 100,000 had a degree or diploma. A recent conversation with a budget-deficit worrier revealed he was not aware that there were so many unemployed graduates – and University of Melbourne graduates at that. According to the [graduate surveys of 2014](#), one in four new graduates (not in further study) were defined as unemployed four months after graduation.

Why are (some) economists so hung up on government debt?

So back to the original statement: why do financial commentators and macro-economists rarely articulate why government debt cannot be monetised in today's climate? Why are they not explicit about their assumption that a 5-6% unemployment rate is equivalent to full employment?

Economists should step out of their bubble more often

Written by The Conversation

Only they can tell you the answer. I suspect either they do not fully understand what they are assuming about the labour market or they don't care.

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