Macroeconomic Objectives

• The performance targets of the whole economy
• Usually cyclical variations in economic activity mean the benchmarks are not achieved each year
• The three key objectives are:

  o **Economic growth**
    
    ▪ The increasing capacity of the economy to satisfy the needs and wants of its members
    ▪ Rate of growth is important in defining the country’s future opportunity set
    ▪ An annual rate of 4% is considered desirable
    ▪ Usually measure by rate of change in GDP
    ▪ **A sustainable rate is between 3-4% per annum**
      • If growth is too fast exposes bottlenecks in the economy and will place pressure on prices
      • If too slow resources are not fully employed
      • Between 2005-2007 the booming economy saw low unemployment, skills shortages in several sectors and pressure on prices
      • The 2008 GFC saw the economy slow and jobs were shed; Australia did not suffer as much as other economies

  o **Price stability**
    
    ▪ The RBA has an explicit inflation target
    ▪ “In pursuing the goal of medium term price stability, both the Reserve Bank and the Government agree on the objective of keeping consumer price inflation between 2 and 3 per cent, on average, over the business cycle”
    ▪ Achieving price stability is important because inflation has adverse effects on households and firms, erodes international competitiveness, distorts the distribution of income and influences the allocation of resources throughout the economy

  o **Full employment**
    
    ▪ Occurs when everyone who is willing and able to work can find employment
    ▪ Zero unemployment is not possible
      ▪ Due to the existence of frictional unemployment and structural change
In Australia the natural rate of unemployment – the lowest rate that can be achieved without inflationary pressures developing – seems to be about 4%.

There are three more recognised Government Economic Objectives:

**External Balance**

- To balance the external transactions between Australia and the rest of the world
  - To achieve a sustainable trade balance (CAD), to avoid excessive exchange rate fluctuations and have a sustainable foreign debt ratio as a proportion of GDP
- The government has little control over external balance
- The BOP records overall balance between current and capital accounts
- Since the floating of the Australian dollar in 1983 – the government has no control over the exchange rate

**Equitable Income distribution**

- To evenly share out the income and wealth of the nation
- To improve the inequality of income inequality in Australia
  - Income inequality is measured by the **Lorenz Curve**

**More efficient allocation of resources**

- To satisfy as many consumer wants and needs as possible
- There are three goals to achieve:
  - **Technical efficiency**: producing output at a lower cost
  - **Allocative efficiency**: ensuring resources are out to their best use
  - **Dynamic Efficiency**: the ability of the economy to adapt over time

**Demand Management Policies**

- Both the boom and the trough phases of the cycle impose costs on the economy
- Using demand management policy these costs can be reduced; the government can lift economy activity in the trough and reduce it in a boom
- Deliberate government action to stabilise is called counter cyclical (against the cycle) policy or demand management policy

**Fiscal Policy**
• The deliberate use of government spending and revenue powers to change the level of economic activity
• The overall position of the budget is called the budget outcome
• If there is an excess of revenue over expenditure the budget is in surplus; if there is an excess of expenditure over revenue there is a deficit – if they are equal it is said to be balanced
• **Surplus budgets has a contractionary** effect on the economy because they reduce the level of aggregate expenditure and economic activity: Deficit budgets are expansionary for the opposite reason
• Generally periods of weaker growth (especially less than 2%) are followed by a deficit budget – periods of higher economic growth bring higher taxation receipts so the budget moves back into surplus

**Monetary Policy**

• Actions taken by the central banks to affect the availability of credit
• RBA meets first Tuesday of each month to set the cash rate
  - **Cash rate:** the interest rate banks charge for very short term loans so they can meet the obligations to other banks
• When the cash rate is changed, key interest rates will also change
• Technically the RBA is independent of the Government to reduce the potential for political influence on economic policy
• If the economy is expanding too fast, the RBA will rise cash rate the reduce aggregate spending in the economy
• If conditions suggest that the conditions are worsening the RBA will cut rates