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Raising interest rates in Australia the wrong move, says UWS expert

November 7 2007

The decision today to raise interest rates by a quarter of a per cent was an overreaction by the Reserve Bank of Australia to what it perceived as an "overheating" economy, says a University of Western Sydney economist.

The rate increase will not fix the underlying problems in the economy, rather it could exacerbate them, says Associate Professor Steve Keen from the UWS College of Business.

"Most of the inflation recorded in the last Consumer Price Index figures was caused by factors that an interest rate rise will exacerbate. Ironically, increasing rates now to control inflation may actually contribute to inflation," he says.

Associate Professor Keen says private debt is a far bigger danger to future economic prosperity than inflation.

"The interest payment burden today is already higher than it was during the Great Depression. I simply don't believe that the economy can comfortably cope with an even higher burden. Given our debt levels, deflation is more of a concern than inflation," he says.

Associate Professor Keen points to the past as a guide to what will likely happen to the economy. Two previous debt bubbles were followed by recessions which were made worse by deflation - falling prices, he says.

"If history once again rhymes, and today's excessive debt is followed by a serious debt-induced downturn, then the last thing we want is to have deflation occur as well. Driving inflation lower now may well set up a serious economic problem for the future," he says.

Source: University of Western Sydney

Citation: Raising interest rates in Australia the wrong move, says UWS expert (2007, November 7) retrieved 1 May 2024 from https://phys.org/news/2007-11-australia-wrong-uws-expert.html