Saturday, October 6 2012

Common Currency Dilemma

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As the saying goes, "Once bitten, twice shy!"

Even if not bitten before, one would learn from experiences of others.

A draft of a study (the Study) on *Strengthening Trans-Tasman Economic Relations*, released in mid September by the Australian and New Zealand (ANZ) Productivity Commission says "No!" to a common currency for the Tasman neighbours!

Obviously, the ongoing Eurozone crisis is responsible for the Study finding.

Economic cooperation between the two countries will soon complete a very successful 30-year period under the *Australia New Zealand Closer Economic Relations Trade Agreement (ANCERTA)*, which came into effect on 1 January 1983. The study commends the benefits of ANZ economic cooperation, which include growth in trade volume and increased mobility of labour and capital. Tariffs and quantitative restrictions have been eliminated on almost all goods and there is free movement of citizens between ANZ. The ANCERTA has also extended into new areas, beyond trade, in services as well.

At the last annual meeting, the prime ministers of ANZ asked their Productivity Commissions to submit a joint report on further areas of cooperation for consideration at the next meeting in 2013.

New measures

The Study recommends new measures for further strengthening of economic cooperation. They include (i) dismantling of 'rules of origin' for all goods for which tariffs are at 5 percent or less so that compliance and administrative costs for a significant proportion of trans-Tasman trade are eliminated; (ii) reducing transport and telecommunication costs, promoting greater trade volume; and (iii) exploring improvements in three areas: foreign direct investment, taxation and banking.

The Study wants the investment protocol to be extended for lessening remaining ownership restrictions in 'sensitive' areas. Further, it suggests companies be allowed imputation credits on trans-Tasman investment so company income is not taxed twice if it crosses the Tasman. Regarding banking, the Study wants a common approach to prudential supervision.

On Single currency

On common currency for ANZ, the Study recognizes the likely benefits. These include savings in transaction, since there will be no more currency conversion and exchange rate risks. However, the Study feels there are other costs, which would far exceed benefits.

The structures of two economies are different. The NZ economy is more agricultural, whereas the Aussie economy is a mineral based export economy with a larger manufacturing sector. The two economies have been experiencing divergent business cycles. If the Kiwi dollar is replaced by another currency either Australian dollar or altogether a new currency, *ANZAC* dollar or *Tasman* dollar, the dominant economy would be Australian. A common monetary policy would be more geared to Australian economy.

An anti-inflationary policy, if adopted by the common central bank for fighting inflation in the dominant economy, would not be suitable for the NZ economy, if the latter goes through recession. Secondly, if external shocks affect the two economies in two different ways, the policy response has to be different. For example, a slowdown of Chinese economy affecting mineral exports of Australia would elicit a response which would be different from the one needed for New Zealand, if the latter is not affected by the shock to the same degree. Similarity in economic structures and impacts of external shocks is essential for success of common monetary policy, in the event of a single currency and one exchange rate.

A high degree of convergence of the two economies is a critical requirement for a monetary union.

Single currency for the Region

If a monetary union has to become successful, it has to be a fiscal union as well. A common fiscal policy will have to evolve over time. That means surrender of political sovereignty as well, besides monetary sovereignty.

Twelve years ago, a former Governor of Reserve Bank of New Zealand, Don Brash told a Rotary Club audience in Auckland that the time for a common currency had not yet arrived since the pre-conditions of convergence were not yet fulfilled. The situation continues to remain the same.

In 2003, an Australian Senate Committee proposed the Australian dollar for Pacific island countries (PICs) as a common currency for ensuring greater monetary discipline. However, Professor Phillip Powell of Indiana University argued against it in a Canberra Conference in 2005 describing PICs, as not yet ready for a union. Apparently, he was recalling a contemporary American television film, in which two 17-year old teenagers thinking they are in love decide to get married, despite their parents disapproval, only to realize soon they have very different views on the future.

The title of the television film was “Too Young to Marry!”

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