Failed TFF a success, says RBA

By Elisa Barwick

As if performing a deft sleight-of-hand conjuring trick, Christopher Kent, the Assistant Governor (Financial Markets) of the Reserve Bank of Australia, revealed that the government's hurriedly concocted COVID money-pumping scheme, the Term Funding Facility (TFF), was a failure, even as he claimed its success. A critical reading of Kent's 9 October speech at the Sydney RBA offices shows that the TFF:

- was unnecessary;
- did not increase overall business lending;
- triggered inflation;
- fuelled house price growth; and
- resulted in huge financial losses for the RBA and government.

The RBA's financial supremo admitted these things in his speech yet insisted that "The TFF delivered on its goals." The TFF, reported the RBA's just-released 2024 "Review of the Term Funding Facility", was effective in "stabilising sentiment" and "keeping credit flowing to the economy". Though "the economy" here, appears to mean the housing bubble and the banks' balance sheets.

So where did $188 billion of our money go?

Unnecessary, undirected credit

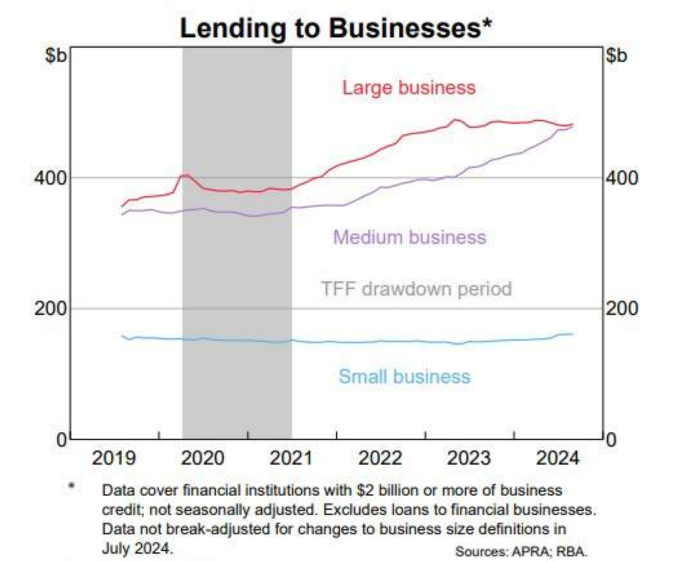
The TFF—"the insurance the RBA took out against a catastrophic economic outcome", in Kent's words—was created in March 2020 in case the banks were reluctant to continue to lend as COVID-19 emerged and spread.

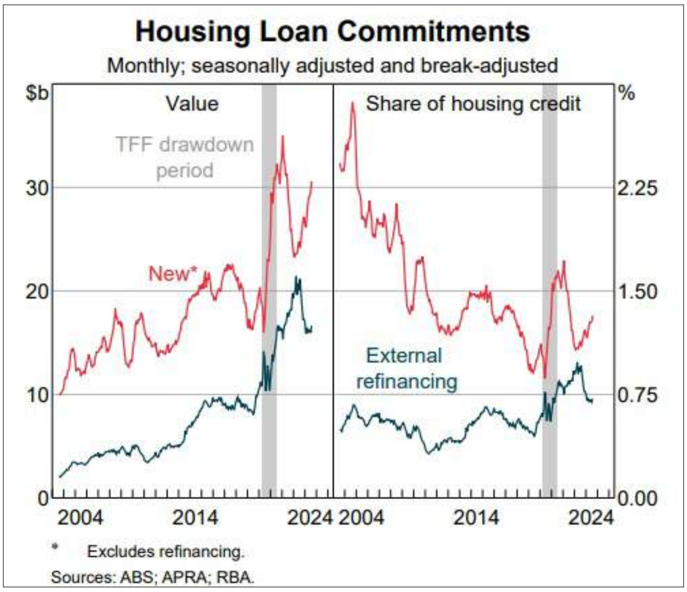
The TFF provided low-cost funding to banks, first at 0.25 per cent, and then lowered to 0.1 per cent interest rates. The funding was meant to, firstly, "lower the cost of borrowing for businesses and households" and, secondly, encourage greater lending to businesses, "particularly small and medium-sized enterprises (SMEs)—given that business credit tends to fall in downturns."

But the RBA's Review states that "Total business lending was little changed" during the TFF's term. While some banks loaned more to business, the lending of others declined. Econometric estimates, RBA reported, found "no statistically significant effects of the TFF on bank credit growth for SMEs" and no measurable increase of business lending by TFF-eligible banks compared to banks that did not use the facility, or ineligible non-banks. Kent sheeted the lack of expansion of total business credit to government support programs and lack of confidence, which was particularly pronounced with the main target of the scheme—SMEs.

The RBA had already admitted in a December 2022 review that: "Using bank-level data and a difference-in-differences approach, we find no statistically significant evidence that the TFF increased credit supply to businesses." Answering a question in Senate Estimates from Greens Senator Nick McKim on 26 October 2023, Kent waved aside the suggestion that the TFF didn't impact business lending, theorising that "If we hadn't had those banks step up because of this incentive, maybe business lending would have contracted."

The RBA plan was to foster lending, firstly, by lowering interest rates to encourage demand for credit from business; and, secondly, by encouraging banks to expand business lending in order to access "additional low-cost TFF loans". It made available an extra dollar of TFF funding for each dollar of additional credit banks loaned to large businesses; and an additional five dollars for extra lending to SMEs.





During the TFF drawdown period (grey bar) there was no statistically significant increase in business lending (top), but housing lending did shoot up dramatically (above). Photos: RBA Review of the Term Funding Facility

This was a weak and ineffective mechanism, in contrast with alternative methods as China, for instance, has deployed (p. 8). Therefore, banks took advantage of the cheap credit and simply continued to lend into the sectors which advantaged their bottom lines. The banks "made commercial decisions" notes the RBA Review, in response to the cheap funding.

The TFF thus fuelled the housing bubble, driving up prices. "[M]onetary policy contributed to housing price growth", conceded the Review, adding that "Mortgage lending rose to its highest share on record". Most new lending, for the banks' "commercial" reasons, took the form of fixed rate mortgages. The percentage locked in at low rates rose from 15 per cent in early 2020 to 45 per cent by mid-2021, as house prices surged more than 20 per cent, preparing a future rate shock when the fixed term of three years reset.

Senior Economics Correspondent Shane Wright's headline in the *Sydney Morning Herald* of 10 October read: "RBA's $200 billion stimulus powered house prices, not small business". He reported that "Over one 12-month period during the pandemic, Sydney's median house value climbed by $843 a day while Melbourne's jumped by $473 a day."

Subsidising private banks

The late take-up of the scheme, said Kent, "suggested that the banks did not need TFF funding to compete for, or satisfy, the demand for borrowing from households and businesses". When the September 2020 decision to extend the TFF was taken, the banks had only taken up 60 per cent of their allowances—and nearly half of that at the veritable "last minute"—in the month before its expiry. The RBA acknowledged that with the benefit of hindsight it may not have made the decision to extend the scheme.

The RBA decided to extend the facility for the best part of another year because its lending targets had not been met. This almost doubled the ultimate cost to the RBA, which was around $9 billion. The RBA ventured that this was effectively "a transfer to the private sector". But instead of highlighting the benefit to the private banks, it claims much of it flowed to households and businesses, while acknowledging that banks, unlike the rest of us, were able to hedge against rate increase risk by lending at fixed rates and utilising derivatives.

"While the TFF was profitable for the RBA until May 2022", said Kent, "once the cash rate increased, the RBA was paying banks more interest for the balances that they kept at the RBA than the low fixed rate the banks were paying on the TFF."

This only proves that the TFF, as Independent Senator Gerard Rennick has described it, amounted to "directly subsidising private banks". It was basically free money (0.1 per cent) provided to the banks, which they could either park at the RBA-risk free to earn the overnight cash rate of more than 3 per cent, or lend out commercially for even higher returns.

The interest rate rise commenced because the "increase in inflation turned out to be much stronger, and started much earlier, than the initial upside scenarios considered by most economists and the RBA", said Kent. The inflation, that is, that the RBA admits it contributed to.

The RBA also acknowledged the risk that banks may have proved incapable of paying back the TFF loans. To assist banks, the RBA froze the valuation of bank securities they provided to the central bank as collateral for the TFF scheme for three years, until early 2023. There was a chance that banks may not have handled the flood of margin calls, to put up additional collateral, when those valuations were unfrozen but in the end, as Kent noted, "Banks repaid all TFF funds as scheduled by mid-2024 without incident." From all accounts this period was "touch and go"; only close monitoring by the RBA and prudential regulator APRA, along with favourable market conditions, overcame potential liquidity issues.

In conclusion, the RBA believes, as Kent divulged, that this type of lending tool is worth using again if warranted, incorporating of course, "valuable lessons learnt". Notwithstanding the fact that, as Wright reported, the program significantly contributed to RBA "accounting losses of almost $47 billion since COVID", the policy is now part of the RBA's unconventional monetary policy tool-box, because it has proven "particularly valuable when the standard interest rate lever is already near zero and significant downside risks to the economy remain", said Kent.

The RBA would have been better to do what crossbench Senators suggested in Senate Estimates hearings from early 2021—directly lend straight into the productive sector, or use its power to *make* the banks do it!

From big shots to 'finance rats': How bankers have fallen in China

A BBC article from 11 October heralds a paradigm shift taking place in China, which the world should be rushing to copy. "How China's crackdown turned finance high-flyers into 'rats'", by Fan Wang, reports that China's crackdown on financial crime, corruption and speculation has crushed the swanky lifestyle of bankers and brokers. No longer can they afford Louis Vuitton suits or Burberry accessories, reported the bankers who were interviewed, and—shockingly—they have to holiday in cheaper destinations such as Southeast Asia rather than Europe.

Many have taken a pay freeze, experienced a declining workload, or seen their bonuses disappear; social media posts about "quitting finance" go viral. Morale in the finance industry is low.

Worse, finance workers are seeing more of their bosses carted off to jail, such as the former chairman of the Bank of China, or the former vice-governor of the People's Bank of China (central bank), Fan Yifei, who after being found guilty of accepting bribes was sentenced to death with a two-year reprieve.

One of the policies singled out in the BBC piece—albeit just one of a whole suite of financial and regulatory reforms of recent years—was an August 2022 rule adopted by the Chinese finance ministry to "optimise the internal income distribution and scientifically design the salary system". Following that, reported BBC, China's "top corruption watchdog criticised the ideas of 'finance elites' and the 'only money matters' approach, making finance a clearer target for the country's ongoing anti-corruption campaign". Although it is not official, finance workers claim there is now a cap on bankers' salaries.

Chinese society has "fallen out of love with finance", according to a private equity employee cited by BBC. "We are no longer wanted even for a blind date. You would be told not to go once they hear you work in finance." These days his kind are routinely mocked as "finance rats".

But the attitude shift signifies something far more important: that China's crackdown on speculative, non-productive activity is working. Policies to direct economic effort and financial flows into physical development have not only transformed the economy, but are laying a cultural bedrock that venerates people engaged in constructive work rather than making money out of money. Particularly since the 2008 global financial crisis, China has done this through a gradual reform agenda based on regulations that foster the real economy and discourage speculative ventures, which *AAS* has documented every step of the way. (For the most recent report, see "Contrasting China with Chalmers and 'one tool' Bullock", *AAS*, 9 Oct.)

Offering up the high priests at the journalistic alter?

By Elisa Barwick

Something has shaken the boffins in the world's central bank complex to the point where one of their inner circle, the Brit recently installed at the Reserve Bank of Australia, Andrew Hauser, felt compelled to talk to journalists about the secrecy of his world. In a speech at the Walkley Business Journalism Awards in Sydney on 8 October, Deputy Governor of the RBA and Deputy Chair of the RBA Board, Hauser, made an offering of sorts. Perhaps in the hopes of staving off a full sacrifice, he delivered some morsels that might satisfy those in the press being buffeted by the tide of popular opinion which has turned against the privileged and unelected central bankers dictating the living standards of Australians.

Hauser is the first foreigner to take up such senior positions at the RBA. He previously worked at the Bank of England for 30 years, heading the markets division where he oversaw the BoE balance sheet and foreign exchange reserves. Trained in Oxford's prestigious politics, philosophy and economics program and at the London School of Economics, he has also represented the UK on the IMF's executive board.

His speech "From the Shadows to the Podium: Central Banks and the Press" pulled the curtain aside ever so slightly to prove "there's nothing to see here". In the question-and-answer period, Hauser demurred: "sometimes people say, you know, it must be great being a Central Banker—you've got all these secrets. The truth is, the dirty secret about Central Banking is, there aren't many secrets! The biggest secret is obviously the interest rate decision—that's discussed in the board and it's put out almost straight away afterwards". He later argued against those who demand complete transparency, saying, "If we made everything 'on the record', it's so dry people would say, 'Dear God, can you please stop?'"

High priest, Montagu Norman

Hauser opened his remarks saying that "our central banking predecessors a hundred years ago would have been surprised to see us here", because they never engaged with the public. He then spent an inordinate portion of his remarks discussing the model set by the founder of the modern doctrine of central banking, the key player in establishing the network of central banks that coordinate policy across the globe—today through the forum of the Bank for International Settlements.

"The high priest of central banking in the mid-1920s was Montagu Norman, Governor of the Bank of England", said Hauser. "Norman was an extraordinary character—a devotee of mysticism, who wore a long flowing cloak and travelled under the fake name of Professor Clarence Skinner. His communications strategy was succinctly summarised in the pithy phrase 'never explain, never apologise'.

"He regularly put those words into practice. When asked by a Parliamentary select committee in 1930 to rationalise a particular course of action, for example, he simply tapped the side of his nose three times and stared into the distance.

"Despite—or perhaps because of—this unusual behaviour, journalists loved him. A breathless 1932 *New York Times* pen portrait, entitled 'Banker and Legend', purred: 'Mr Norman is all elusiveness, technique, finesse … he sits silent, discreet, unseen … exercising a power unthought of by old-fashioned tyrants and only glimpsed by alchemists of long ago poring over their crucibles.'

"Sadly, that passion went unreciprocated. Indeed, Norman made titanic efforts to avoid the press. Once, aboard ship in rough seas, word reached him that reporters were gathering to question him at the next port. He promptly leapt over the rails, shimmied down a rope ladder, and made his escape in a dinghy.

The RBA's Andrew Hauser addressing the Walkley Business Journalism Awards. Photo: YouTube

"'Never explain, never apologise' permeated every aspect of the Bank of England's operations at that time. Not for them, the modern paraphernalia of glossy reports, explainers and press conferences. For much of the 20th century, changes in official interest rates were communicated solely through the medium of a large printed card, placed in the Bank's ornate lobby, and a simultaneous verbal announcement by the 'government broker' to traders in the government bond market. To effect that announcement, the broker removed his top hat, stood upon a bench, and bellowed at the top of his voice. Fleet Street's finest played no role.

"Indeed, even when I joined the Bank of England in the early 1990s, the main job of the Head of the Press Office was still said to be, with little irony: 'keep the Bank out of the press and the press out of the Bank'."

Hauser then developed the same theme in the USA, mentioning the secrecy surrounding the founding of the Federal Reserve and quoting Alan Greenspan's words to Congress in 1987: "since I've become a central banker, I've learned to mumble with great incoherence … if I seem unduly clear to you, you must have misunderstood what I said." He was only half joking, said Hauser.

He then went on to contrast today's supposed new era in which "central banks have emerged blinking into the sunlight of greater transparency" and in which central banks "now produce a vast stream of material" and are subject to "Parliamentary scrutiny, conference panels, on-the-record interviews and press conferences". Incredibly, Hauser claimed that this "explicit public accountability" is a *quid pro quo* in response to the "huge powers conferred on central banks by the granting of operational independence"! He called on the press gallery to help the central banks get their messages across to the public—that is, to help create the impression the high priests want to project—and even noted that "The goal of these Awards is to encourage journalists to pursue rigorous and fearless reporting in the field of business, economics and finance."

For all of that, it appears that none of the media reported on Hauser's speech—but then, this was a memo to the messengers, not the public.

When it comes to the messaging for the broader population, no doubt Hauser and his central bank compatriots are secretly counting on the success of misinformation and disinformation laws being propelled through parliament by the Australian and UK governments—laws which censor information which may challenge the integrity of the financial system in a way that might undermine public confidence, but from which professional media are exempt. This may explain why Hauser is working overtime to get the media on side, but the proposed laws are now subject to a Senate Inquiry in Australia and there is a fighting chance they will be defeated.