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From the Desk of CIO

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Printing of Money by Governments

During the 2019-20 pandemic, many governments were forced to save their countries by spending more in the form of subsidies, provisions of liquidity etc. If a government has excess reserves, this is a non-issue. However, if a government is already running an excessive deficit with high borrowings, a more innovative mean of financing is needed. Issuing bonds is the most common method to raise funds such that the government will bear the burden of paying back the liabilities in the future by way of taxes, sales of assets etc. Excessive issuance of bonds may strain the liquidity of the financial system. Alternatively, governments may resort to printing money to finance the spending!

Malaysian government debt has been growing over the years and hit a high of RM1.08tn by end of last year or 60% of the nominal GDP (*see Exhibit 1*).

In the recent parliament sitting, the Member of Parliament from Selayang asked "whether the government has considered debt monetisation as a way to increase revenue". The Ministry of Finance replied that the government has no intention to use debt monetisation or the method of selling government bonds to Bank Negara Malaysia (BNM) directly as a financing strategy.

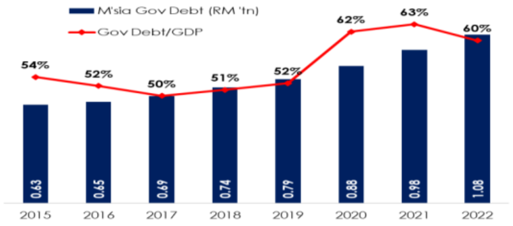
Is debt monetisation a way to raise government revenue?

Debt monetisation is a euphemism for printing money in the modern economy. It is no longer necessary to print new currency in this electronic era if a government wants to increase spending capacity. Debt monetisation is essentially asking for an overdraft from the central bank for creating fresh money. If a government can issue bonds which can be purchased by the market where there is sufficient liquidity, debt monetisation is unnecessary. As such, debt monetisation is the last resort if there is insufficient liquidity to absorb the issuance of government bonds or if external borrowing is not possible.

There is another indirect method of money creation. This is the quantitative easing (QE) actively conducted by the US Federal Reserve (Fed) in recent decades. Essentially, the purchase of government bonds floated in the market will create new supply of money. US Fed has been actively using QE to increase the supply of money since the 2008 GFC (see Exhibit 2).

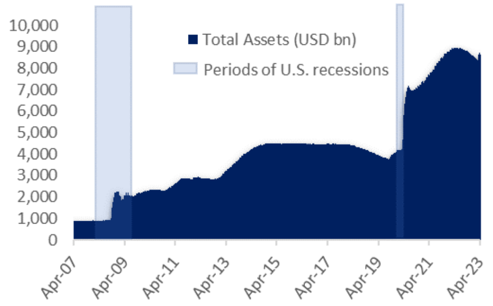
BNM has also started to mop up more government bonds from 1% of total government bond issuance to over 6% (*see Exhibit 3*).

Exhibit 1: M'sia Gov Debt



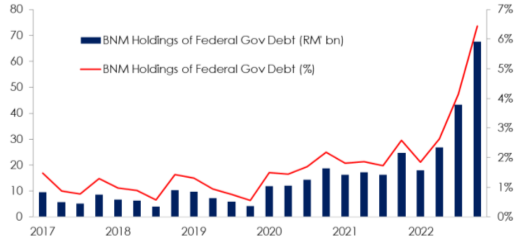
Source: BNM, PCM, Apr 23

Exhibit 2: US Fed Balance Sheet



Source: Board of Gov. of the Federal Reserve System (US), PCM, Apr 23

Exhibit 3: BNM Holdings of Gov Debt



Source: BNM, PCM, Apr 23