Submission to the Petitions Committee

In support of Positive Money's petition CRM:0124357 asking parliament to inquire into the use of direct monetary financing for infrastructure

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Executive Summary

This petition asks Parliament to initiate an inquiry into the responsible use of Direct Monetary Financing—a credible, historically proven public-finance tool that could significantly reduce the long-term cost of New Zealand's essential infrastructure investment. Direct monetary financing would operate alongside existing mechanisms such as taxation and bond issuance, not replace them.

New Zealand faces a large and urgent infrastructure deficit, with conventional borrowing greatly inflating project costs through interest. Financing $31 billion of annual investment at current bond rates could more than double the expense over 30 years. Direct monetary financing allows the Reserve Bank to issue new money directly for approved public projects, offering a way to fund long-lived, productivity-enhancing assets with little or no interest burden, freeing future fiscal space for core public services.

Treasury has confirmed there is no legislative barrier to using direct monetary financing, and New Zealand has previously employed similar tools for state housing, rural credit, and industrial development with strong economic results. International precedents—from Canada to Japan—show that direct monetary financing can support nation-building when paired with strong institutional controls.

This petition proposes a ring-fenced, rules-based model in which Parliament sets strict boundaries, independent entities oversee project pipelines, and the Reserve Bank provides low-cost funding within defined limits. Such a framework would mitigate risks often associated with direct monetary financing—such as inflation, bond-market concerns, or political misuse—while improving infrastructure delivery and strengthening monetary sovereignty.

With major infrastructure investment unavoidable and global monetary systems in flux, now is the right time for Parliament to examine direct monetary financing as a strategic complement to existing financing tools and to develop the institutional settings needed for its safe and effective use.

What this petition is about

On 14 May 2020, as the first shockwave of Covid hit New Zealand, officials from the Treasury and Reserve Bank delivered a paper to the finance minister. It compared two methods the government could use to finance its crisis response. One was quantitative easing (QE), called Large Scale Asset Purchases (LSAP) by the Reserve Bank. The other was monetary financing, also known as direct monetary financing (DMF), the subject of this petition.

In both cases, the Reserve Bank provides financing to support the government. But QE works through the financial markets (by using the new money to buy back bonds from financial institutions), while direct monetary financing bypasses them (by spending the new money directly into the economy). Both options have strengths and weaknesses as the officials' paper outlines.

QE was the method chosen in this particular instance and, as we saw, it had both strengths—it helped to stabilise jittery financial markets and supported government borrowing—and weaknesses—it helped drive a massive housing bubble and cost more than $11B in financial losses to the government. It's likely that direct monetary financing would have avoided or reduced these problems.

Direct monetary financing is not new and has been used before in New Zealand and elsewhere. It is a powerful public financing tool that is sitting idle, ready to use—like much of the human and physical resources that could be put to work with it.

What direct monetary financing can do

As Treasury has confirmed, no new legislation is needed to use direct monetary financing. We could use it today to put people and resources to work building critical infrastructure and filling the productivity-sapping gaps from decades of underinvestment.

New Zealand has a pressing and costly need for public infrastructure after years of underinvestment. The Infrastructure Commission estimated in 2022 that we needed $31B/year to tackle current and future infrastructure challenges. Add interest to that bill and the cost could more than double.

To illustrate this, if the government borrowed at the recent 10-year bond coupon rate of 4.5%, then $31B would become $72B over 30 years. Under direct monetary financing there would be little or no interest charged and that extra $41B could fund public services or the maintenance and operation of those assets.

Our petition asks parliament to consider using direct monetary financing to reduce this interest bill on major infrastructure. In addition, as we show, it can improve infrastructure delivery and grow the economy, and strengthen monetary sovereignty at a time of disruptive global change.

What we are asking parliament to do

In our view, before direct monetary financing can be used responsibly and effectively outside times of crisis, it needs a robust institutional framework. This is the key issue we are asking parliament to consider.

The need is there and a financing tool that can help address it is available, but it is poorly understood. Its advocates often claim too much for it ("We can have anything we want! We can eliminate taxes!"), and its critics are too quick to dismiss it ("Politicians will misuse it! It will turn us into a Zimbabwe or Venezula!").

We believe it is time to start a wider, more informed and nuanced conversation about how we finance our economy with its considerable investment needs, and the part that direct monetary financing can play. An inquiry by parliament can start and inform this conversation, and now is the time to do it.

The slow-burning crisis of infrastructure underinvestment gives us the opportunity. It has been at times of major investment that it has been used most successfully here and elsewhere.

And if we have any more doubts about timeliness, the upheaval taking place in the global monetary system right now should tip the scales. Technology and geopolitics are fast converging in ways that will impact the sovereignty of currencies like ours. This makes it even more important that we are deeply engaged with the issues and arrangements underpinning our monetary sovereignty.

We are not proposing that direct monetary financing should replace current forms of public financing, such as tax or bonds, only that it should be an important addition to the public financing toolkit.

In this submission, we:

- Show how DMF would work within our monetary and public finance systems
- Offer some high-value use cases and explain its benefits compared to other forms of financing
- Address some of the concerns commonly raised
- Outline institutional guardrails that would allow us to enjoy the benefits while minimising the risks
- Explain why it is timely now to undertake this inquiry.

What is direct monetary financing?

With direct monetary financing, the Reserve Bank issues currency directly. It does this with simple accounting entries on its balance sheet that create new electronic money which is then spent into the economy by the government. It is like issuing the government with electronic cash rather than physical banknotes. It may be non-repayable or structured for repayment.

Direct monetary financing is not Modern Monetary Theory (MMT) or Quantitative Easing but shares some characteristics of both while addressing downsides.

While it is not currently used (it has been in the past), there is no legal or technical impediment to using it. In response to an OIA request, our Treasury stated, “There is nothing in New Zealand legislation that would prohibit or preclude the government from using [direct] monetary financing.”

Who issues New Zealand’s money and how it can be done better

Direct monetary financing is a form of ‘central bank money’ that differs from the way most money is issued today. The majority of money in circulation is issued by commercial banks when they make loans (‘private money’). Effectively, the government outsources most of its money-issuing powers to private banks.

To many people, this seems counter-intuitive to their understanding of money.

New Zealand’s money is what is called fiat money. It is not a physical good or anchored to a commodity like gold. Rather, money is just an accounting entry—a liability—that sits on a bank’s balance sheet. For commercial bank money, that liability is the deposits in the bank’s customer accounts. For banknotes and ‘settlement cash’ (a form of electronic cash available only to banks and the government), that liability sits on the Reserve Bank’s balance sheet.

Direct monetary financing is an electronic form of public money. Like cash, it is issued by the Reserve Bank, backed by the government, and can be directly spent into the economy, rather than loaned to someone first as commercial bank money is.

This presents an opportunity—to strike a better balance between the money-issuing powers of the commercial banking system, which now account for about 98% of the money supply, and the money-issuing powers that the government retains for itself.

To realise this opportunity—while also getting more public infrastructure built more cost-effectively—we ask parliament to investigate the design of a robust institutional framework that supports responsible use of direct monetary financing.

As well as providing a source of finance and a framework for delivery of vital public infrastructure, direct monetary financing can help to address some shortcomings of the current system.

The money supply should expand to keep up with a growing economy, but as we have seen, most of the new money created in this system through lending has gone to households for increasingly expensive housing, rather than to businesses for productive investment. Household indebtedness exploded from 1990 as a monetarist system, anchored by new Reserve Bank and Public Finance acts, leaned on household balance sheets to expand the money supply via high cost bank debt. In 1990, household debt was 35% of GDP. It reached just over 90% of GDP by the GFC where it has hovered since, with a brief peak of 99% in 2021.

This places New Zealand's household debt among the highest in the world, while our government debt is among the lowest. Shrinking government spending has been paid for by monetary expansion, most of it sitting on household balance sheets—we've been putting the economy on the mortgage.

Introducing more public money into the economy will help households to deleverage and lower their interest costs, leaving them more money to spend in the economy. While public money can sit interest-free on the Reserve Bank/government balance sheet, it costs about $40B a year in interest (about 10% of GDP) for it to sit on commercial banks' balance sheets. A little over half is returned to savers, but it remains an expensive way to issue our money. Each year, billions of dollars are diverted away from spending in the productive economy because we choose such an expensive way to finance our money supply.

Banks currently create the money they lend back to the government for infrastructure, then charge interest on that newly created money. We are simply asking the Reserve Bank to create the money directly, without the burden of interest to the tax payer. Economist Raf Manji said during the Canterbury rebuild, why pay interest on money for infrastructure when we do not have to?

The general process of money creation is described in detail by the Reserve Bank in its paper *Money creation in New Zealand*.

How direct monetary financing can be harnessed to build infrastructure and improve economic management

The successful uses of direct monetary financing, both past and present, have coincided with periods of nation-building, when a greater share of a country's labour and resources is claimed by the state for provision of public goods.

It has been used to smooth spending peaks and troughs, such as price stabilisation schemes and full employment commitments. And it has been used to finance infrastructure, and in industrial policy, through industrial banks and direct subsidies or favourable finance terms for strategic industries.

Examples of its use in New Zealand in the period from the mid-1930s to the mid-1980s include the financing of state housebuilding, price stabilisation schemes for primary industries, international market development for strategic sectors, e.g. the Dairy Board, and industrial development banks (the Rural Bank and Development Finance Corporation).

In the period from 1936–1939, the Reserve Bank created NZ£30 million of credit to support the government. This was between 2–7% of GDP in each of those years, and econometric analysis from 2002 found that the Reserve Bank's expansionary credit policy enabled the country to grow more rapidly following the 1930s Depression with real GDP growth of 30 per cent over four years.

While there are many possible uses for direct monetary financing, our petition proposes that it be narrowly focused on large scale public infrastructure financing at zero or very low interest rates for which it is particularly well suited.

As proposed in this petition:

- It is a limited, rules-based use of central bank capacity to finance nation-building infrastructure—essentially public credit issued against the nation's future productive capacity.
- It is ring-fenced and only contributes finance to projects developed and delivered within an independent entity(s).
- The limits to its use are set and regularly reviewed by parliament.

Institutional arrangements for use of direct monetary financing

In our view, common concerns about direct monetary financing can be addressed with robust institutional design and clear rules on when this valuable public financing tool can be used as part of the government's monetary and fiscal toolkits.

Below, we provide two examples to outline how this might be achieved. The first is for the sovereign currency issuer (central government), the second is for a currency user (local government in this example).

Public infrastructure—Central government

- An independent infrastructure body is established to develop, prioritise and deliver major public infrastructure projects. This could be a NZ Transport Agency-type of structure.
- Parliament sets the scope, legal and financial boundaries for eligible investment.
- The Reserve Bank directly purchases long-term bonds issued by the entity, and/or credits its designated accounts, for these approved capital projects.
- This infrastructure body ensures transparency and compliance.
- Parliament regularly reviews performance and must authorise any further tranches of direct monetary financing.

Water infrastructure—Local government

Positive Money developed a model for financing water infrastructure using a mixture of direct monetary financing and market finance. More details of this use case can be found here.

- An independent body ('the Water Infrastructure Agency') is established to assess and prioritise water infrastructure investment cases. We suggest working with the Infrastructure Commission which can apply both a local and national interest lens to the public funding applications.
- Council water entities submit water infrastructure proposals to this body.
- Parliament sets the scope, legal and financial boundaries for eligible investments and assesses the submitted shortlist of projects against this. It authorises a financing envelope for the direct monetary financing contribution.

- With this authorisation from parliament, and a payment schedule coordinated with the 'Water Infrastructure Agency', the Reserve Bank directly purchases *repayable* long-term bonds issued by the Local Government Funding Agency (LGFA) on behalf of council water entities.
- The 'Water Infrastructure Agency' and Reserve Bank monitor the project delivery and financial performance of the borrowers.
- Parliament regularly reviews performance and must authorise any further tranches of direct monetary financing.

We hope these simplified frameworks will provide a starting point for detailed policy consideration.

Precedents and case studies

Direct monetary financing and DMF-like mechanisms have been successfully implemented when:

- Directed toward long-term productive assets
- Governed by strong legal and institutional frameworks
- Coordinated between monetary and fiscal authorities

Historical and international examples

- New Zealand (1935–1979): The Reserve Bank funded state housing, industry development and infrastructure through controlled credit issuance
- Canada (1935–1974): The Bank of Canada financed public infrastructure without increasing sovereign debt
- Japan (1950s–1970s): Direct lending from the Bank of Japan enabled rapid industrialisation
- China (present): The People's Bank of China supports long-term development through targeted infrastructure investment, including injecting low cost funds into public industry development banks (called 'policy banks').

Addressing objections to direct monetary financing

Objections to direct monetary financing commonly stem from two sources: fears of misuse by politicians, and misunderstanding of how money works in a modern economy.

With the right institutional framework, direct monetary financing can be a disciplined, transparent, and effective way to finance public investments. These arrangements allow us to enjoy the benefits while reducing negative impacts.

Impact on bond markets and credit ratings

Objection: Direct monetary financing could undermine investor confidence, reduce demand for government bonds, and trigger credit rating downgrades.

Response: Clear institutional rules and transparency can reassure credit rating agencies and financial markets that direct monetary financing is not a blank cheque. Direct monetary financing is not a replacement for bond issuance, it's a complement. Ring-fenced direct monetary financing for targeted investment can reduce future borrowing needs and improve long-term fiscal sustainability—exactly what financial markets are calling for.

Inflation risk

Objection: Injecting money directly into the economy could fuel inflation.

Response: Inflation depends on *where* and *how* money is spent rather than the source of the money. Direct monetary financing targeted at underutilised capacity (e.g., infrastructure, housing, climate adaptation) is less inflationary than general consumption.

Further, the long-term planning and coordination that should be part of the institutional settings would help to address resource bottlenecks before they became inflationary, e.g. through workforce planning and upskilling, and a reliable work pipeline that would encourage private sector capital formation. These actions would also raise productivity, to the benefit of the wider economy.

Crowding out

Objection: Direct monetary financing might crowd out private investment or distort resource allocation.

Response: This is partly true but not in the way that its proponents usually mean. Unlike bond issues, direct monetary financing does not compete in the financial markets for investors, which is typically the basis for the crowding out argument; so it doesn't operate in a way that would drive up interest rates and lower private sector investment.

However, because the money will be spent on building infrastructure, there will be pressure on the economy's real resources which might lead to some reduction of private investment until the industry capacity (workforce, capital, skills etc.) increases. This is not a bad thing where the public projects make good, productivity-enhancing uses of those resources. We know from studies by the Infrastructure Commission and others that there are a lot of high quality public investment opportunities available.

To make the most of this synergistic relationship, direct monetary financing should be reserved for areas where private investment is insufficient or inappropriate—like public goods, resilience infrastructure, or intergenerational assets where benefits accrue over very long timescales. Proper guardrails and a long term perspective ensure direct monetary financing complements rather than competes with private capital.

Having a reliable, long term source of financing for a construction pipeline can assist the long term resource planning to the benefit of private sector investment. The result is more likely to be *crowding in*—boosting private investment through government spending—rather than crowding out.

Misuse or pump-priming

Objection: Politicians may misuse direct monetary financing for vote-buying or short-term stimulus.

Response: This is a governance issue, not a flaw in the tool itself, and can be addressed with good governance arrangements. Strong institutional design—including transparent independent oversight, parliamentary approval, and spending directly tied to long term project pipelines—can prevent misuse. Direct monetary financing should be boring, rule-bound, and focused on long-term value.

There are plenty of other mechanisms that politicians currently use for pump-priming, including deficit spending financed by conventional bond issues or tax cuts.

With the sort of safeguards we are advocating, direct monetary financing will probably be one of the hardest sources of funding for politicians to tap into to juice the economy.

Why it is timely now to have this inquiry

We are about to start spending large sums on infrastructure. Direct monetary financing is historically tied to periods of nation-building and large-scale public investment. This has been true in New Zealand and around the world, as we've shown in examples cited earlier. After years of infrastructure neglect and underserviced population growth, we are back there again.

New Zealand's $200 billion infrastructure deficit is well documented, and there is widespread consensus across political parties on the urgent need for investment. One way or another, New Zealand will be spending significant money on infrastructure in the coming years. Now, therefore, is the perfect time to look at an alternative funding option that will save billions of dollars in annual interest, and add the financing certainty to build a long term pipeline of work. In turn, this will boost private investment and productivity as firms gain confidence to employ and train workers and make capital investments.

For the past forty years we have heard the catch-cry, "but the government cannot afford it" when it comes to funding major public investments. But affordability has been considered only in the narrow context of borrowing from the private sector, with interest. This perspective overlooks the unique financial mechanisms available to sovereign currency-issuing governments such as New Zealand, with the ability to issue currency at low or zero interest, as we propose. We ask parliament to take advantage of this unique moment.

Conclusion

New Zealand stands at a pivotal moment. We face an unprecedented infrastructure deficit, intensifying economic headwinds, and a rapidly evolving global monetary landscape. Meeting these challenges will require not only sustained investment but also a more flexible and forward-looking approach to public financing. Direct monetary financing—used

successfully in New Zealand's past and by comparable nations today—offers a credible, disciplined, and high-impact addition to our existing toolkit.

This petition does not advocate replacing established funding mechanisms. Rather, it calls for Parliament to examine how a modern, rule-based, and transparent framework for direct monetary financing could unlock long-term, low-cost financing for essential public assets while strengthening monetary sovereignty and reducing the burden of interest costs on future generations. With appropriate guardrails, independent oversight, and clear parliamentary authority, direct monetary financing can support a stable construction pipeline, enhance productivity, and improve fiscal resilience.

An inquiry now would enable a well-informed national conversation about how best to deploy our sovereign monetary capacity for the public benefit. It would help ensure that New Zealand's future infrastructure is not constrained by outdated assumptions about affordability, but instead supported by financing arrangements fit for the demands of the coming decades.

About Positive Money NZ Inc

Positive Money NZ is an independent, non-profit group. For more than a decade, we have advocated for a fairer, more productive monetary system that benefits everyone, not just a few. Our patron is Bryan Gould and we are part of a global movement of organisations campaigning to change money and banking so they serve society better.

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