FINANCIAL REVIEW

Fundies challenge RBA on rate cuts

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The fund managers who wrote to Reserve Bank of Australia governor Philip Lowe in 2016 urging him not to cut interest rates still stand by their argument, and say low rates are enabling the free-wheeling disruption of decent businesses by upstarts that aren't held to the same standards of profitability.

Investors Mutual's Anton Tagliaferro and Hugh Giddy implored the then incoming governor to resist joining other advanced economies in the race to the bottom on rates. They asserted that such a policy response rewards excessive borrowing and fails to foster investment.

They also claimed low rates are simply unfair. As of Tuesday, the Australian cash rate is at a record low 1 per cent and the Reserve Bank has agreed it could keep cutting "if needed".

Mr Giddy acknowledged on Thursday that Australia's economy cannot be isolated from the rest of the world, but central banks did not appear to have a solution, or perhaps an appreciation, for the fact their policies distort the allocation of capital.

"Globally, central banks have kept rates low and inflated the money supply, declining to let rates be set by market forces. Free markets work best when prices are set by competitive market forces," he said.

"Low rates mean that struggling companies survive and companies like Uber can disrupt other businesses without needing to show a profit or any prospect of making a profit."

This year, Wall Street has welcomed a rush of Silicon Valley IPOs from Lyft to Pinterest to Slack. Uber told investors in its prospectus that it might never make money and it lost $US1 billion ($1.4 billion) in its first quarter.

"Manipulating and suppressing interest rates may seem like a good idea because it avoids short-term pain that may result from allowing market forces to operate," Mr Giddy said. "However, strong long-term growth will not be possible with a continuing misallocation of resources and disincentives to saving that result from such low rates."

Global life insurers have been casualties of the zero per cent rate regime which inflates the value of their liabilities and reduces investment income. Europe's banks have struggled with the imposition of negative interest rates.

Ordinarily, fund managers welcome low interest rates which flatter valuations in the equity market and make dividend income more attractive relative to cash. The S&P/ASX 200 Index is at an 11 and a half year high, and the S&P 500 is at a record high.

"Lower rates have also tended to inflate asset prices," Mr Giddy said, but this disproportionately benefits a narrow portion of the population, exacerbating inequality.