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## Section 4

# Other functions and activities

### Foreign reserves management

The Reserve Bank Act enables the Treasurer to direct the Bank to intervene in the foreign exchange market and requires the Bank to hold foreign exchange reserves to provide the capacity to implement such a directive. The target level of reserves is set by the Treasurer in consultation with the Bank. The current target level is NZ\$4.5 billion.

Foreign currency reserves are held to enable the Bank to intervene in the foreign exchange market in particular circumstances. Since the New Zealand dollar was floated in 1985, the Bank has generally limited its intervention objective to countering extreme disorderly conditions in the currency market. Although intervention has been considered on occasions since 1985, the Bank has not yet found it necessary to intervene.

The foreign reserves held by the Bank are financed by foreign currency borrowing undertaken by the Treasury's Debt Management Office. This has some important risk minimisation advantages in relation to the Crown's finances, by matching the maturity and currency of assets and liabilities, thereby minimising the risks associated with interest rate and exchange rate movements.

Although holding foreign currency reserves provides a benefit in the form of a degree of "risk insurance" against disorderly market conditions, it also entails costs. The costs arise because the government can typically only borrow at higher interest rates than we can expect to earn by investing in highly liquid, highly rated foreign government bonds. The cost fluctuates from year-to-year, but the annual cost to the Crown of maintaining New Zealand's current intervention capacity has averaged between NZ\$5 and 10 million in recent years. These costs have been falling as a result of looking for smarter ways to fund and hold reserves.

The Bank has two reserves-related reviews underway at present. The first review relates to the objectives of and circumstances in which the Bank would consider intervening in the foreign exchange market. Over recent years we have been reviewing the case for widening the circumstances in

which we would intervene in currency markets such as to ease exchange rate pressures in situations where the currency appears to have substantially over-shot (at either end of the cycle). Overseas experience suggests that, at the margin, sterilised intervention might be able to affect the exchange rate slightly, and internationally intervention has often had positive results. Notwithstanding these points, a key issue to be considered is whether the possible benefits of widening the intervention policy would outweigh the risks, given New Zealand's record of having had a clean float since 1985.

More recently, we have begun an extensive review of the target level of foreign reserves. The review was initiated in recognition that the level of target reserves has remained largely unchanged since 1988, despite substantial growth in foreign exchange turnover, in the size of the economy and in New Zealand's external debt since then.

### Reserve Bank registry and Austraclear operations

Section 35 of the Reserve Bank Act enables the Bank to provide securities registry services under terms and conditions agreed between the Bank and the person for whom they are supplied. The Bank provides these services as part of its role of promoting a sound and efficient financial system. The services provided can be divided into two categories:

- registrar and paying agent (registry) services; and
- securities clearing and settlement (Austraclear) services.

#### Registry services

Registry services are a specialist administrative function undertaken for organisations that borrow money by issuing debt securities. The Reserve Bank's registry service has competed with other providers of registry services since 1989 and has been offered to issuers meeting criteria relating to ownership, status and credit rating.

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Effective from 15 May 2000, the Bank out-sourced the registry services function. However, the Bank still remains responsible for the services carried out on its behalf.

The Bank has indicated its intention ultimately to exit the business of providing registry services. We will work with issuers with a view to achieving this end within the next one to two years.

## **Austraclear clearing and settlement system**

This system is an electronic securities clearing and settlement service provided on a subscription basis to both investors and financial service providers. The Austraclear system has been in operation for 12 years.

The provision of depository services is not a core central bank function. The Bank intends to continue to provide depository services using the Austraclear system until such time as an alternative system becomes available. The Bank would welcome the development and operation of a new depository system by a third party. Until such time as an acceptable alternative system becomes available, the Bank will continue to ensure the Austraclear system is supported.

## **Settlement Services**

Section 32 of the Act allows the Bank to provide settlement account services for financial institutions on such terms and conditions as may be determined by agreement. Presently there are 12 institutions with exchange settlement accounts. While all 12 institutions are registered banks, the Bank has a policy which allows non-bank financial institutions to obtain an exchange settlement account.

## **Currency issue and management**

Section 25 of the Reserve Bank Act gives the Reserve Bank the sole right to issue legal tender bank notes and coins in New Zealand, including determining their design and composition.

The Bank considers that one of its key roles is to ensure that New Zealand's notes and coins are meeting the needs of the

public as effectively as possible. To this extent we are continually monitoring usage and overseas trends in such areas as counterfeit avoidance and note durability.

Over the coming months the Bank will be reviewing coin usage. Any review will involve extensive consultation with interested parties.

The Bank is also working on the five dollar note, with a view to improving its durability.

## **International liaison**

An important aspect of the Bank's functions is its relationships with a wide range of overseas central banks, international financial institutions and international forums. The Bank derives significant benefit from its international relationships, including improved access to information and research, greater participation in international policy formulation, and an enhanced capacity to exchange views and experience on policy issues. We also see our involvement as contributing to New Zealand's wider international relationships, particularly in the Asia-Pacific region.

We maintain close working relationships with a number of central banks and active participation in a number of Asia-Pacific regional groups, including:

- the APEC Finance Ministers' process (Asia Pacific Economic Co-operation forum for finance ministries and central banks);
- EMEAP (Executives' Meeting of East Asia and Pacific central banks and supervisory agencies);
- SEANZA (South East Asia New Zealand Australia central banks and supervisory agency forum); and
- The Manila Framework Group (a group of central banks and finance ministries in the Asia-Pacific region).

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## Government cash and debt management

The Reserve Bank undertakes a number of functions for the Treasury. These include selling treasury bills and government bonds at competitive tenders, on a timetable and to amounts determined by the Treasury's Debt Management Office, under approvals from the Treasurer.

Undertaking these functions and the management of day-to-day government cashflows through open market operations assists the Bank to stay closely attuned to developments in domestic financial markets.

## Overseas Investment Commission

The Reserve Bank provides the Secretariat for the Overseas Investment Commission (OIC). The Governor of the Reserve Bank, or such officer the Governor may nominate, is an *ex-officio* member of the Commission. It is only for historical reasons that the OIC is associated with the Bank. There is now no congruence between the responsibilities of the Bank and those of the OIC; the OIC's role does not fit with the Bank's core functions. Accordingly, we propose to initiate discussions with the Government with a view to fully separating the OIC from the Reserve Bank.