
DISCUSSION PAPERS

DP 2011/02

Fluctuations in the international prices of oil, dairy products, beef and lamb between 2000 and 2008: A review of market-specific demand and supply factors

Phil Briggs, Carly Harker, Tim Ng and Aidan Yao

This paper looks at the boom period between 2000 and 2008 in the international prices of four internationally-traded commodities: oil, dairy products, beef and lamb. All are important drivers of macroeconomic dynamics in New Zealand. Our aim is to provide overviews of the demand and supply factors specific to each market and product, thus adding colour to more general analyses of the macroeconomic and financial drivers of the cycles in world commodity markets over the period. For each commodity market we examine here, we set out the structures of the markets and the major drivers of world demand and supply, and discuss the apparent relative strength of each of the drivers.

NEWS RELEASES

Sector Risk Assessment released ahead of anti-money laundering requirements

29 March 2011

The Reserve Bank today released its Sector Risk Assessment to help registered banks, non-bank deposit taking institutions and life insurers prepare to meet upcoming requirements under the Anti-Money Laundering and Countering Financing of Terrorism Act 2009.

The Reserve Bank will be responsible for supervising the compliance of these organisations with this new legislation, which is expected to fully come into force in 2013.

An assessment focused on the risk of money laundering that these types of institutions may face has been carried out by the Reserve Bank. There is currently insufficient information about terrorism financing to widen this focus.

This assessment is intended to provide guidance to the institutions the Reserve Bank will supervise as to the money laundering risk in their sector. This in turn will help firms in undertaking their own risk assessments.

The ratings provided by the Reserve Bank in the assessment do not reflect on the financial stability of these sectors or the institutions within them, but merely provide an overview of the relative risk of money laundering.

Measures to counteract money laundering are already in place in banks and some of the other organisations the Reserve Bank will supervise. However, these controls have not been considered for the purpose of the assessment, but will be once the Act comes fully into force.

The Reserve Bank's assessment rates the banking sector as having a relatively high potential money laundering risk. This may mean that money launderers will target the sector for these purposes.

This rating is in line with similar assessments for banks globally and is largely due to factors such as the wide accessibility and availability of banks, the cash intensive nature of their products and services and the volume of transactions they process.

Overall, the non-bank deposit taking sector is described as having a "medium" potential risk rating. This is because their products and services are not generally as cash intensive, but

they process a high volume of transactions both in terms of value and volume.

However, within this sector credit unions are rated as "low" potential due to their strong domestic customer focus.

The assessment puts life insurers at a "medium/low" potential risk. Factors such as the large single payments and payouts involved can be attractive to money launderers. However, a large proportion of the transactions in this area are domestic and the sector is not cash-intensive.

The Reserve Bank Sector Risk Assessment can be found on the Bank's website at <http://www.rbnz.govt.nz/aml/4345201.pdf>. The Securities Commission and the Department of Internal Affairs are also releasing assessments relevant for the organisations they will supervise. These can be found on their respective websites.

New bank registered

31 March 2011

The Reserve Bank of New Zealand today announced that BOI (New Zealand) Limited has been registered as a bank in New Zealand.

BOI (New Zealand) Limited is a fully owned subsidiary of Bank of India. It will change its name to Bank of India (New Zealand) Limited before commencing operation.

There are now 20 registered banks in New Zealand, which are listed on the Reserve Bank website.

Reserve Bank Bulletin Released

31 March 2011

The Reserve Bank today released the March 2011 issue of the Reserve Bank of New Zealand *Bulletin*.

This first issue of the year explores the kind of economic and financial challenges New Zealand has faced in recent years. The lead article outlines a framework for analysing movements in government bond interest rates, concluding with a brief analysis of what those changes could mean for the countries in question, and ultimately for New Zealand.

The second article turns the spotlight on a recent research

conference held at the Reserve Bank with a focus on the transmission of economic and financial shocks from one country to another. This is particularly relevant given the synchronised nature of the recent international recession.

Article three updates the Reserve Bank's work towards improving the range and quality of statistical data on the debt securities market in New Zealand. The recent global economic upheaval highlighted the need for better data on this market, both here and abroad.

The *Bulletin* is rounded off with the Bank's submission to the Government-appointed Savings Working Group and Governor Alan Bollard's January speech to the Canterbury Employers' Chamber of Commerce.

Bank information more accessible

31 March 2011

Revised disclosure requirements for banks coming into effect today will make information more accessible for investors, depositors and analysts, Reserve Bank Deputy Governor Grant Spencer said.

The changes to shorter disclosure statements will also mean a significant reduction in compliance costs.

This marks the completion of a major review of the disclosure regime initiated in October 2009.

The changes follow two new Orders-in-Council setting out the new disclosure requirements, which were published in the *New Zealand Gazette* on 28 February. Banks' next disclosure statements, covering the period up to 31 March 2011, will mostly be on the new basis.

A transitional arrangement allows banks to continue disclosure on the previous basis as at end-March and end-June this year, in case any of them need extra time to make necessary adjustments to their reporting processes. However, the major banks at least will be taking advantage of the new regime immediately.

Further detail on the nature of the changes is in an earlier policy outcome document (PDF 169KB), and also in a Regulatory Impact Statement (PDF 210KB) which is published today. Both can be downloaded from the Reserve Bank's website.

Export prices deliver benefits to economy

12 April 2011

New Zealand's agricultural export prices are likely to remain strong for some time, delivering benefits to the New Zealand economy, Reserve Bank Governor Alan Bollard said in a speech.

Speaking to a farming group, the Grasshoppers, in Ashburton last night, Dr Bollard said the Bank expects the higher terms of trade to continue to be reflected in the exchange rate, as it is currently. The exchange rate would deliver the benefits of the rising terms of trade to the community at large – through higher wealth and cheaper imports.

Global commodity prices have experienced the largest boom in more than 100 years, Dr Bollard said. While hard commodities have seen the biggest surge, agricultural commodity markets have also seen a fundamental change. Another surge in prices has since seen food prices surpass the 2008 record level, boosted by supply disruptions, particularly in grain markets.

Analysis by the Bank indicates New Zealand's agricultural export prices are likely to remain elevated for some time. Although in the near-term, prices could fall slightly as supply becomes less weather-disrupted, demand is underpinned by urban and wealth growth in developing countries, especially China.

Given this outlook, monetary policy will remain focused on any medium-term inflationary pressures that arise, rather than the terms of trade shift in itself.

"If households and firms use the income boost from higher commodity prices and exchange rates to bring forward consumption and investment, or increase borrowing, then pressure on resources in New Zealand would lead to more inflationary pressure. Monetary policy would need to counteract any rise in inflation expectations."

Dr Bollard noted, however: "One thing we do know is that the projection will remain uncertain. History shows it is fiendishly difficult to predict the future path of commodity prices."

RBNZ, People's Bank of China announce currency swap facility

18 April 2011

The People's Bank of China (PBOC) and the Reserve Bank of New Zealand today announced the establishment of a reciprocal currency arrangement (swap line) to support the settlement in Chinese Renminbi (RMB) of trade transactions between New Zealand and Chinese businesses.

The size of the swap facility is RMB 25 billion (NZD 5 billion) and has a three year maturity which may be extended if both parties agree. The facility gives the Reserve Bank the capacity to borrow RMB for use in rare situations where financial market disruption makes it difficult for businesses to access RMB to settle transactions with Chinese businesses.

Reserve Bank Deputy Governor Grant Spencer said the arrangement followed on from recent actions by the PBOC to facilitate the settlement of transactions conducted by firms in RMB. Eight other countries, mainly in Asia, have swap facilities in place with the PBOC.

"While there is no need to use the facility right now, it is useful to have this capacity if markets were ever to become dysfunctional. In addition the signing of this swap line contributes to building the China-NZ relationship," Mr Spencer said.

Discussion document on disclosure requirements for non-bank deposit takers released

21 April 2011

The Reserve Bank, in conjunction with the Ministry of Economic Development, today released a discussion document on proposed disclosure requirements for the non-bank deposit taking (NBDT) sector.

The discussion document's main proposals include requiring NBDTs to disclose a standardised set of prudential information and for these disclosures to be updated six-monthly.

Reserve Bank Deputy Governor Grant Spencer said disclosure of standardised prudential information will provide investors with a framework for analysing an NBDT's risks, and allow investors to compare risks between NBDTs more easily. This

will improve market discipline, and confidence in the NBDT sector.

"The six-monthly frequency also aligns prudential disclosures with financial statements during the life of a prospectus," he said.

Other proposals in the Prudential Disclosure Requirements for Non-Bank Deposit Takers discussion document include: disclosures being subject to auditor reviews; and investors being notified when disclosures are updated as a result of material changes in an NBDT's circumstances.

The discussion document and information on existing prudential requirements are available on the Reserve Bank website. The discussion document can also be accessed from the Ministry of Economic Development website.

Submissions close on 19 May 2011.

Background

Prudential regulation of NBDTs is provided for in part 5D of the Reserve Bank of New Zealand Act 1989. The latest of these regulations came into effect in December 2010.

Since then the Reserve Bank and the Ministry of Economic Development have been working together to develop disclosure requirements for the prudential regulations under the Securities Act 1978.

OCR unchanged at 2.5 percent

28 April 2011

The Reserve Bank today left the Official Cash Rate (OCR) unchanged at 2.5 percent.

Reserve Bank Governor Alan Bollard said: "The outlook for the New Zealand economy remains very uncertain following February's Christchurch earthquake.

"As was expected, business confidence, consumer spending and tourism activity all declined sharply following the earthquake. The OCR was cut as insurance to help limit these adverse effects. Confidence and consumer spending have since shown signs of recovery, but many firms and households remain adversely affected in Christchurch. To

date, activity in the rest of the country appears relatively unaffected, with housing market turnover and business investment beginning to increase.

“Trading partner growth remains robust, helping push New Zealand’s export commodity prices higher. Along with relatively favourable climatic conditions, the improved price outlook is supporting a pickup in on-farm investment. Higher oil prices and the elevated level of the New Zealand dollar are both unwelcome. They will have some dampening effect on economic activity.

“Headline inflation is currently being boosted by recent increases in indirect taxes. Annual inflation is expected to settle comfortably within the target band once these tax increases drop out of the annual rate.

“Given the outlook for core inflation and continued economic disruption stemming from the earthquakes, the current level of the OCR is likely to remain appropriate for some time.”

Economic surveillance after the crisis: reflections from a small full service central bank

05 May 2011

The global financial crisis has changed the economic surveillance required by central banks, placing a greater emphasis upon using monetary policy and financial stability policy in tandem to help keep economies stable.

This is the message of a speech by Reserve Bank Governor Dr Alan Bollard, to be delivered in Singapore tonight by Assistant Governor Dr John McDermott.

Dr Bollard’s speech, presented to the Sim Kee Boon Institute Conference on Financial Economics, states that prior to the crisis there was a clear separation between monetary policy formulation and financial stability policy, even in “full service” central banks like the Reserve Bank that perform both functions.

However, the financial crisis challenged traditional economic forecasting models and moved central banks to pay greater attention to financial market information when formulating

monetary policy.

“Likewise, more attention is paid to economic imbalances and the financial health of sectors, by looking at household and business balance sheets, when assessing financial sector risks,” Dr Bollard says.

“Going forward, the aim is to set monetary and financial policy instruments to take account of the inter-relationship between the financial sector and the real economy. This will require a broader framework for economic surveillance.”

Since the crisis, information is being swapped more readily between central banks and regulators globally, and relations with treasuries and Ministers of Finance have become closer.

The Reserve Bank has also strengthened links with regulators in other countries, particularly Australia and Asian central banking partners, to help information sharing.

“Good surveillance usually will not stop nasty surprises, but it may buy some lead time and help policymakers to make better sense of surprises when they happen,” Dr Bollard says.

Financial system more resilient but still facing volatility

11 May 2011

New Zealand’s financial system is more resilient and positioned to support economic growth, but still faces a volatile and uncertain environment, Reserve Bank Governor Alan Bollard said today, when releasing the Bank’s May 2011 *Financial Stability Report*.

“The global economic recovery is now broader, and strong growth in Asia is supporting commodity producers like New Zealand and Australia. However, global wholesale funding markets remain fragile, given stretched fiscal positions and banking sector problems in some European countries,” Dr Bollard said.

“Efforts by households and businesses to cut or contain debt are reducing New Zealand’s overall external imbalance, but are also weakening domestic demand. Government too is looking to consolidate its financial position, which should help to improve the country’s overall external position.”

Dr Bollard noted the February earthquake had caused financial stress for households and businesses and created a challenge for the insurance sector in dealing with claim flows. But the banks' readiness to support recovery in Christchurch was encouraging.

"Rebuilding will add momentum to the economy and is likely to require access to credit, despite much of the damage being substantially insured."

Deputy Governor Grant Spencer said the New Zealand banking system has continued to strengthen.

"Bank profits have recovered over the past six months and bad debt charges declined. Bank funding has moved to a more stable footing and capital ratios are relatively high. Non-performing loans are elevated but remain manageable."

Mr Spencer said the Reserve Bank is currently evaluating the new Basel III global regulatory standards for bank capital adequacy and liquidity and expects to consult with banks on this later in the year.

Other matters under way include the restoration of more appropriate risk weights on rural lending from June, and an increase in the required minimum Core Funding Ratio for banks from 65 percent to 70 percent from 1 July. "These moves have been well signaled and largely anticipated by the banks."

The Reserve Bank is also consulting banks about pre-positioning their internal systems to enable Open Bank Resolution. This is a process that would allow a failing bank to be kept open by rapidly allocating losses across shareholders, depositors and other creditors.

"Having this option in the tool kit should reduce the pressure on Government to adopt taxpayer funded solutions when dealing with a distressed bank," he said.

The Reserve Bank recently assumed the role of insurance sector regulator. Following the recent earthquakes, the Government has had to support AMI to ensure an orderly claims process in Christchurch.

"The Bank has accelerated its work programme in light of the earthquakes and is monitoring this sector closely. While there remains considerable uncertainty over the extent of

total final claims, we believe the overall industry is sound," Mr Spencer said.

OCR unchanged at 2.5 percent

9 June 2011

The Reserve Bank today left the Official Cash Rate (OCR) unchanged at 2.5 percent.

Reserve Bank Governor Alan Bollard said: "The outlook for the New Zealand economy has improved since the publication of the *March Statement*.

"Economic activity has been significantly disrupted by the Christchurch earthquake. However, while many firms and households – particularly within Canterbury – continue to be adversely affected, it appears the negative confidence effect of the earthquake on economic activity throughout the rest of the country has been limited.

"The early signs of recovery noted in the *March Statement* have continued. Despite some continuing signs of weakness in the world economy, commodity prices remain very strong and firms expect to increase their hiring and capital investment. Reconstruction in Canterbury is projected to add about 2 percentage points to GDP growth over 2012, and boost the level of activity for several years thereafter.

"Despite the strong outlook for export earnings, household expenditure is expected to grow only modestly. Household debt remains very high and is expected to constrain retail spending and the housing market for some time. Continued fiscal consolidation will also act to dampen activity.

"The New Zealand dollar has appreciated substantially over the past two months. This appreciation, supported by high export prices for primary producers, is negatively affecting other parts of the tradable sector, constraining rebalancing of the New Zealand economy.

"Headline inflation is currently being boosted by recent increases in indirect taxes, food and petrol prices, and surveyed expectations of future inflation have edged up. Despite this, indicators of capacity usage and core inflation suggest underlying inflation remains constrained.

“As GDP growth picks up, underlying inflation is expected to rise. A gradual increase in the OCR over the next two years will be required to offset this, such that CPI inflation tracks close to the midpoint of the target band over the latter part of the projection. The pace and timing of increases will be guided by the speed of recovery, but for now the OCR remains on hold.”

View the *Monetary Policy Statement* page <http://www.rbnz.govt.nz/monpol/statements/> for the current policy assessment, *Monetary Policy Statement*, and data file.

PUBLICATIONS

Regular publications

Annual Report

Financial Stability Report

Monetary Policy Statement

Reserve Bank of New Zealand Statement of Intent, 2010-2013

Published in October each year.

Published six-monthly. A statement from the Reserve Bank on the stability of the financial system.

Published quarterly. A statement from the Reserve Bank on the conduct of monetary policy.

Recent Reserve Bank Discussion Papers

2010

- DP2010/01 Evaluating household expenditures and their relationship with house prices at the microeconomic level
Mark Smith
- DP2010/02 All together now: do international factors explain relative price co-movements?
Özer Karagedikli, Haroon Mumtaz and Misa Tanaka
- DP2010/03 Multi-period fixed-rate loans, housing and monetary policy in small open economies
Jaromír Beneš and Kirdan Lees
- DP2010/04 Internationalised production in a small open economy
Aurélien Eyquem and Güneş Kamber
- DP2010/05 Using estimated models to assess nominal and real rigidities in the United Kingdom
Güneş Kamber and Stephen Millard
- DP2010/06 Sharing a risky cake
David Baqaee and Richard Watt
- DP2010/07 Exporting and performance: market entry, expansion and destination characteristics
Richard Fabling and Lynda Sanderson
- DP2010/08 Intertemporal choice: a Nash bargaining approach
David Baqaee
- DP2010/09 Debt dynamics and excess sensitivity of consumption to transitory wealth changes
Emmanuel De Veirman and Ashley Dunstan
- DP2010/10 Does the Kiwi fly when the Kangaroo jumps? The effect of Australian macroeconomic news on the New Zealand dollar
Andrew Coleman and Özer Karagedikli
- DP2010/11 A theoretical foundation for the Nelson and Siegel class of yield curve models, and an empirical application to US yield curve dynamics
Leo Krippner
- DP2010/12 Monetary policy implementation and uncovered interest parity: empirical evidence from Oceania
Alfred Guender and Bevan Cook
- DP2010/13 What drives core inflation? A dynamic factor model analysis of tradable and non-tradable prices
Michael Kirker
- DP2010/14 Monetary policy, inflation and unemployment
Nicolas Groshenny

2011

- DP 2011/01 Any port in a storm? The impact of new port infrastructure on New Zealand exporter behaviour
Richard Fabling, Arthur Grimes and Lynda Sanderson
- DP 2011/02 Fluctuations in the international prices of oil, dairy products, beef and lamb between 2000 and 2008: a review of market-specific demand and supply factors
Phil Briggs, Carly Harker, Tim Ng and Aidan Yao

A full list of Discussion Papers is available from Administration, Economics Department.

Selected other publications

Testing stabilisation policy limits in a small open economy: proceedings from a macroeconomic policy forum
Finance and Expenditure Select Committee inquiry into the future monetary policy framework: submission by the Reserve Bank of New Zealand

Pamphlets

Explaining Currency

Explaining Monetary Policy

The Reserve Bank and New Zealand's Economic History

This is the Reserve Bank

Your Bank's Disclosure Statement – what's in it for you?

Snakes and Ladders – a guide to risk for savers and investors, by Mary Holm

For further information, go to www.rbnz.govt.nz, or contact:

Knowledge Centre

Knowledge Services Group

Reserve Bank of New Zealand

2 The Terrace, P O Box 2498

WELLINGTON

Phone (04) 472–2029

Articles in recent issues of the Reserve Bank of New Zealand *Bulletin*

Vol. 73, No. 2, June 2010

The Reserve Bank and macro-financial stability
Financial sector amplification and credit cycles in New Zealand
World trade interdependencies: a New Zealand perspective
The Reserve Bank's new approach to holding and managing its foreign reserves

Vol. 73, No. 3, September 2010

Connecting the dots: a yield curve perspective on New Zealand's interest rates
The New Zealand dollar through the global financial crisis
Anti-money laundering and countering the financing of terrorism - the Reserve Bank's responsibilities and approach
The currency denomination of New Zealand's unhedged foreign reserves

Vol. 73, No. 4, December 2010

Regulating non-bank deposit takers
Bringing financial stability legislation to the insurance industry - the Insurance (Prudential Supervision) Act 2010
Global currency trends through the financial crisis
New Zealand's imbalances in a cross-country contest

Vol. 74, No. 1, March 2011

Making sense of international interest rate movements
We're all in this together: the transmission of international shocks to open economies
Towards better data on New Zealand debt securities markets
Submission to the Savings Working Group
Looking into the crystal ball: a forecast and some risks for the year ahead