

## IN CONFIDENCE



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To: Minister of Finance

### **CONSULTATION PROCESS AROUND MACRO-PRUDENTIAL POLICY**

1. The Reserve Bank and Treasury have been working on a framework for macro-prudential policy, including:
  - Developing a list of instruments that could be deployed in certain circumstances.
  - Investigating the extent to which the instruments can be implemented using existing Reserve Bank powers.
  - Agreeing a draft Memorandum of Understanding that formalises the objectives and institutional framework of Macro-prudential policy – you received this draft earlier in the month.
2. The next key step will be to engage on a formal consultation process on the package of macro-prudential instruments. These include:
  - The countercyclical capital buffer.
  - Alterations to sectoral capital requirements.
  - Changes to the core funding ratio.
  - Restrictions on high loan to value ratio loans.
3. Prepositioning the four instruments is likely to require changes in bank conditions of registration. Consequently, the Reserve Bank's formal consultation process will be similar to that for other changes to conditions of registration. That is, a consultation paper will be published on the RBNZ website, interested parties will have 3-4 weeks to respond, and a paper will be prepared that summarises the consultation feedback and provides information on how the instruments will be applied.
4. The consultation document will focus on operational aspects of the four tools, but will also cover the objectives of macro-prudential policy. The draft MOU indicates that the main objective of macro-prudential policy is to increase the resilience of the domestic financial system to the risks arising from credit, asset, or liquidity shocks. It also notes that these instruments may help dampen extremes in the credit cycle and capital market flows. However, it is important not to overstate the potential effectiveness of macro-prudential instruments, and expectations in this area need to be carefully managed. The RBNZ has made this point in public a number of times, and will continue to do so as part of the consultation.

## IN CONFIDENCE

5. The consultation document will also outline the key accountability, consultation and reporting elements of the macro-prudential policy framework.
6. The consultation process should be completed before the release of the RBNZ's May *Financial Stability Report*. This would enable the final response to the consultation document and the Memorandum of Understanding to be released alongside the FSR. This would involve releasing the initial consultation paper by late March or early April.
7. The RBNZ will discuss the consultation document and the final response document with Treasury and yourself prior to their publication. Alongside the formal consultation, RBNZ staff could provide background briefings to interested parties, including members of Parliament (e.g. FEC, or caucuses).