# Briefing to the Incoming Minister

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**Reserve Bank of New Zealand**

Reserve Bank of New Zealand
PO Box 2498
Wellington
NEW ZEALAND

www.rbnz.govt.nz

# Contents

# Governor’s foreword

Te Pūtea Matua, the Reserve Bank of New Zealand, acts to promote the prosperity and well-being of New Zealanders.

We do this by promoting a sound and dynamic monetary and financial system, which best supports a sustainable and productive economy. As the current kaitiaki (guardians) of Te Pūtea Matua, we are committed to meeting the challenges and risks that are ever present in the financial system, and making the most of opportunities for the New Zealand economy.

This year, New Zealand faced an unanticipated global health and economic challenge. The COVID-19 pandemic has created new, and accentuated current, challenges. Our response has been significant and at times untested and innovative. These challenges include:

- Ensuring financial sector resilience and the ability of the banking sector to effectively support economic recovery and focus on customer outcomes. This includes monitoring all parts of financial services delivery, especially where the pandemic has exacerbated economic vulnerability;
- Developing and deploying alternative monetary policy tools to meet our policy objectives of price stability and maximum sustainable employment. This includes building our own and the sector’s capability as we design these tools, and deploy them to maximise effectiveness and efficacy;
- Co-ordinating with other regulatory organisations to ensure collaboration, cohesion and sequencing of regulatory improvements across the financial system. This includes being mindful of any unintended regulatory costs and burdens on the financial sector; and
- Remaining vigilant to our own transformation and managing our programme of Bank-wide transformation and wide-ranging law reform in the current environment.

We are working collaboratively with our Council of Financial Regulators (CoFR) partners to ensure we face these challenges head on and are transparent and accountable for our activities. This allows our stakeholders – the New Zealand public – to have full confidence in our actions.

We are also aware of a number of longer-term challenges and opportunities which will impact our ability to deliver our mandate effectively. These include:

- Contributing to regulatory settings that support effective labour market adjustment, and foster productivity and innovation in New Zealand. This means ensuring we are maximising efficiencies, promoting private sector involvement, and encouraging both competition and innovation.
- Maintaining financial sector confidence and certainty. This includes the busy slate of legislative reforms already underway and being clear on what the financial sector needs to respond to. The more certainty we can provide on finishing what we have started, the better prepared our industries will be to implement and benefit from the reforms.
- Ensuring regulatory stewardship and a co-ordinated and cohesive approach which focuses on the greatest risks and harms to our objectives. This includes continually scanning the financial system for undue regulatory burden, regulatory overlaps or gaps and not creating barriers to competition and innovation.
- Addressing vulnerability and access to the financial services – research has shown that young workers, ethnic minorities, and people with children are likely to experience greater unemployment than others during recessions. We want to ensure the financial sector and regulators have adapted sufficiently to address the growing divide between those who are included and those who are not.

- Supporting economic growth that is environmentally sustainable – ensuring we are making the right choices that are long-term, inter-generational, bring us closer to a zero-carbon economy and are in the best interests of future generations of New Zealanders.

Our current strategic objectives set the foundations for a cohesive response to these longer term challenges, but there is more we can do across the system. We welcome the opportunity to discuss these longer term challenges and opportunities.

We aim to be a modern Central Bank and have a vision of being a 'Great Team, Best Central Bank'. This means we operate transparently; are open to learning and adapting as necessary; work collectively and collaboratively; and are an active, relevant, cornerstone of New Zealand's economy and society. This applies to our activities, our people, and the way we interact and engage with our stakeholders.

We look forward to continuing to work with you to support us and hold us to account in delivering this vision.

# Introduction

The Reserve Bank of New Zealand (Te Pūtea Matua) acts to enhance the prosperity and well-being of New Zealanders by promoting a sound and dynamic monetary and financial system.

In performing this role we establish, implement, and enforce appropriate policies, and operate critical components of the financial system. Most notably, these components include the supply of New Zealand currency, and the operation and oversight of critical payment and settlement services including providing banking services for the Crown.

We have a broad mandate relative to many central banks globally which we achieve in a cost-effective manner. Our mandate includes:

- The setting and implementation of monetary policy – keeping inflation between 1 and 3 percent in accordance with our Monetary Policy Remit[1], and ensuring our monetary policy settings contribute to maximum sustainable employment;
- Prudential regulatory policy and oversight of deposit takers and insurance providers;
- Meeting the currency needs of the public; and
- Operating and supervising core payment and settlement systems in the financial sector.

In undertaking these activities we aspire to achieve our vision – Great Team, Best Central Bank. By 'Best', we mean the most cost-effective and fit-for-purpose central bank for New Zealand. By 'Great', we mean our people are capable, well-resourced, resilient and energised to succeed.

We welcome questions or engagement on any of the challenges and activities.

# Format of the Briefing to the Incoming Minister

| | **Chapter 1 – Challenges** | **Chapter 2 – The Reserve Bank response: our priorities and goals** | **Chapter 3 – How the Reserve Bank operates** | **Chapter 4 – Upcoming key publications and consultations** | **Chapter 5 – Our legislation, governance and structure** |
|---|---|---|---|---|---|
| **Topics** | *Highlights the challenges in the external environment across:*<br>○ *Economic prosperity*<br>○ *Environmental sustainability*<br>○ *Social cohesion*<br>○ *Cultural inclusion* | *Outlines the Bank's response to these challenges as outlined in the Statement of Intent* | *Focuses on the Bank's vision, values and culture, how we deliver our priorities and the upcoming opportunities for transformation* | *Highlights Upcoming key publications and consultations in H2 2020* | *Background information on the legislation, functions, governance, and accountability structure at the Bank* |

[1] Monetary Policy Framework

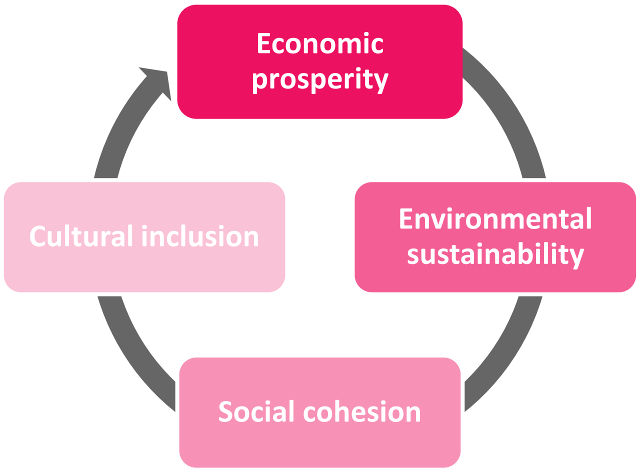
# Chapter 1 - Challenges

The New Zealand Treasury's economic wellbeing framework focuses on natural, human, social, and financial and physical assets. These assets are core to generating sustainable wellbeing for all current and future New Zealanders. We support this focus by acting consistently with our mandate in promoting a sound and dynamic monetary and financial system.

Our role is primarily one of guardianship (kaitiakitanga). As kaitiaki (guardians), we remain vigilant of a broad range of risks that could be detrimental to achieving our purpose and are prepared to overcome these challenges. As such, it is useful to outline what we see as the key current challenges which directly and/or indirectly impact our effectiveness in delivering against our mandate and policy objectives.

Table 1 lists the key challenges which directly or indirectly impact New Zealand and the Bank.

These challenges are arranged under the headings of: economic prosperity, environmental sustainability, social cohesion and cultural inclusion. The Bank views these as important cornerstones to sustainable wellbeing[2].




The Government's economic objective is to improve the wellbeing and living standards of New Zealanders through a sustainable, productive and inclusive economy[3]. Monetary policy plays an important role in supporting the Government's economic objective. The Reserve Bank of New Zealand Act 1989 requires that monetary policy promote the prosperity and wellbeing of New Zealanders, and contribute to a sustainable and productive economy. Monetary policy contributes to public welfare by reducing cyclical variations in employment and economic activity whilst maintaining price stability over the medium term.

We aspire to create an environment where New Zealanders can achieve economic security and prosperity and use this wealth in a sustainable environment where they are able to live and contribute in a safe place, of social cohesion – being accepted and appreciated, and where everyone can participate.

[2] Speech: Geopolitics, New Zealand and the Winds of Change, Sept 2018
[3] New Zealand Government: Economic plan for a productive, sustainable, and inclusive economy

| External challenges: | | | |
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| *Economic Prosperity* | *Environmental Sustainability* | *Social Cohesion* | *Cultural Inclusion* |
| • Extreme COVID-19 driven uncertainty | • Climate change and associated risks – physical and financial | • Labour substitution for technology | • Workforce and public policy diversity and inclusion |
| • Rising unemployment – temporary and persistent | • Policy and market failure to address issues of environmental sustainability | • Technological pace of change and influence of 'big tech' firms | • Ageing population and associated needs |
| • Low and falling inflation rates | • Changing investor and consumer expectations and preferences | • Public institutions capability and capacity | • Protectionism of borders, trade, and domestic employment |
| • Persistent low economic productivity | | • Financial exclusion – technology, geographic, demographic | • Rapid global urbanisation |
| • Effective lower bounds of interest rates | | • Persistent wealth and income inequality | |
| • Asset price bubbles and systemic risk | | • Infrastructure deficits – public and private | |
| • Political instability – trade agreements | | • Public perception of financial institutions | |
| • Rising public and private debt – declining 'fiscal headroom' | | | |
| • Changing currency and payments systems | | | |
| • Financial system and institution stress | | | |
| • Cybersecurity, cloud and data protection | | | |
| • Intergenerational inequity | | | |

Table 1 – a summary of the significant external challenges impacting New Zealand and the Bank.

# Chapter 2 - The Reserve Bank's response: our priorities and goals

We respond to these challenges by operating within our mandate and collaborating with domestic and international stakeholders as necessary. The table below highlights the range of strategies and initiatives as outlined in our most recent *Statement of Intent*[4].

| External challenge | Summary of the impact on RBNZ | Current initiatives and strategies |
|---|---|---|
| ***Economic Prosperity*** | | |
| Extreme COVID-19 driven uncertainty | The economic outlook remains highly uncertain, with the balance of health and economic risks tilted to the downside. Health risks include another global wave of infections and prolonged vaccine development. Economic risks include the likely tapering in fiscal support as a headwind to growth, lingering uncertainty from COVID-19 weighing on consumer confidence and business investment.<br><br>This may constrain the economic activity of consumers, investors and businesses and impact price inflation, FX rates, and general economic activity in New Zealand. | • Earlier this year we acted on a number of fronts to cushion the impact of the COVID-19 shock. This has included supporting the financial system, the domestic economy, the functioning of domestic financial markets and the provision of notes and coins to the public. We are continuing to work with our stakeholders to understand the impact and effectiveness of our tools in this environment by:<br>  o Working collaboratively with stakeholders to understand and analyse the impacts of the COVID-19 pandemic on New Zealand.<br>  o Supporting and mobilising co-ordinated and constructive policy responses to support recovery.<br>  o Engaging with, and learning from, our counterparts overseas to build our understanding of the effectiveness of different responses and tools.<br>• Supporting government, CoFR agencies, industry, and the public as joint-lead agency for financial services in any future lockdowns e.g. publishing guidance, answering questions, and sharing information.<br>• Undertaking a review of the Monetary Policy Committee (MPC) Remit in 2024 to consider lessons learnt, including the effectiveness of tools in response to the COVID-19 pandemic and establishing best practice by learning from international counterparts. |

[4] Statements of Intent

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| Rising unemployment – temporary and persistent | Global labour markets remain significantly impacted by the pandemic. While a recovery is expected, it is likely to be only partial and slow. Fiscal policy support to date has helped to limit the decline in employment rates in most key trading partners, however this is temporary and unemployment is likely to rise once it is withdrawn.<br><br>Historical patterns indicate that the COVID-19 recession may result in a large and persistent fall in employment below its maximum sustainable level, with Māori and Pasifika people being particularly hard hit.<br>Employment trends impact financial stability and our monetary policy decision making to support maximum sustainable employment. Shifts in industry and geographic location of jobs will require support for labour market adjustment. | • Preparing future alternative monetary policy (AMP) tools[5], such as forward guidance, a Funding for Lending Programme (FLP), Negative Interest Rates[6] and large scale Purchases of Foreign Assets (PFA)[7] to meet our policy objectives of price stability and maximum sustainable employment.<br>• Working with Treasury and other stakeholders to ensure effective co-ordination between fiscal and monetary policy.<br>• Undertaking economic research on:<br>○ Understanding the economic impact of COVID-19.<br>○ how different ethnicities, age groups, sexes, and regions have been impacted by previous labour market cycles to gain insights into how COVID-19 may impact New Zealand's labour market<br>○ Monetary policy transmission.<br>○ The aggregate and distributional consequences for the labour market, and policy influences on the structural level of unemployment.<br>○ Distributional consequences and effectiveness of alternative monetary policy. |
| Low and falling inflation rates | Post-Global Financial Crisis (GFC), global inflation and interest rates have been low and New Zealand's neutral interest rate has declined considerably – this creates downward pressure on domestic inflation. This impacts the effectiveness of monetary policy tools in managing price stability. | • Further developing AMP tools, such as forward guidance, a Funding for Lending Programme (FLP), Negative Interest Rates and Large Scale Purchases of Foreign Assets (PFA).<br>• Working with Treasury and other stakeholders to ensure effective co-ordination between fiscal and monetary policy.<br>• Undertaking economic research on:<br>○ Monetary policy transmission.<br>○ Distributional consequences and effectiveness of alternative monetary policy. |

[5] Alternative Monetary Policy tools
[6] Letter to Banks re: Negative interest rates (May 2020)
[7] *AMP tools can create financial risks for the Bank and the Crown. In recognition of these risks, the Bank and Minister of Finance have agreed a Memorandum of Understanding (MOU) regarding the use of AMP tools. Under this MoU, the Bank may request a Crown indemnity before implementing any AMP tool. The merits of the requests are considered by the Minister against requirements specified in the Public Finance Act. The Bank and Treasury are currently reviewing the institutional arrangements set out in the MoU to see if they can be streamlined and improved. To date, the Bank has obtained a series of four indemnities in relation to the Large Scale Asset Purchases programme which began in March 2020. Under these indemnities, any profits or losses that the Bank incurs in relation to the programme are passed onto the Crown each month. In order to ensure the Bank is able to maximise the effectiveness and efficiency of its AMP tools, further capital and/or indemnities may be required from the Crown. The Bank will report to, and engage with, the Minister ahead of any request.*

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| Persistent low productivity | New Zealand has a low level of labour productivity and low productivity growth when measured amongst OECD countries – this may impact long-term economic prosperity and financial stability. | • Monitoring productivity as part of our financial stability and monetary policy considerations.<br>• Supporting MBIE's 'consumer data right' initiative to enable consumers to securely share data that is held about them with trusted third parties. This could provide significant benefits for consumer welfare and economic development including – enabling access to a wider range of products and services, encouraging innovation, and helping build the digital economy. |
| Effective lower bounds of interest rates | The Official Cash Rate (OCR) is at an historic low and may limit the effectiveness of traditional monetary policy tools.<br>The scale of stimulus needed to support a domestic recovery is more than our traditional monetary policy tool – a positive OCR – can provide. This has meant the Bank has had to accelerate its development of alternative monetary policy tools – with the implementation of a large scale asset purchase programme now underway.<br>The development of new tools has required us to update our decision making and operational frameworks to be fit-for-purpose in this new environment. The efficacy of alterative monetary policy tools and fiscal policy in this environment is still uncertain. | • Developing a set of alternative monetary policy tools that our Monetary Policy Committee can use if further stimulus is required. This work programme includes:<br>  o Developing a funding for lending programme<br>  o Establishing the ability to effectively introduce a negative OCR<br>  o Developing new institutional arrangements for management of AMP risks<br>  o Ensuring our communications strategy is effective and the public understand our new policies<br>  o Assessing the financial stability implications of these tools<br>• Working with Treasury on effective coordination of monetary and fiscal policy<br>• Undertaking a review of the MPC Remit in 2024 to consider lessons learnt including the effectiveness of tools in low interest rate but rising asset price environments. |
| Asset price bubbles and systemic risk | The revaluation of assets would impact price stability, the Bank's balance sheet, and the stability of the financial system. This is mainly driven by global markets and is not unique to New Zealand. | • Reviewing loan-to-value (LVR) restrictions to ensure a stable housing market and the flow of credit in the economy. LVR restrictions were removed as part of our COVID-19 response until at least May 2021. We will engage with the public, industry and the Minister early in 2021 as we consider imposing restrictions on higher-risk lending.<br>• Monitoring asset prices as part of our on-going assessment of financial system and financial market developments, as part of our six-monthly Financial Stability Reports, and in our regular engagement with supervised entities.<br>• Implementing planned increases to banks' capital requirements. In response to the impacts of COVID-19 and to support credit availability, we initially decided to delay the start date of increased capital requirements for banks by 12 months - to 1 July 2021. A further delay – until July 2022 –will be announced on 11 November 2020. |

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| Political instability – trade agreements, changing political dynamics | Ongoing US-China tensions, Brexit, and other political unrest may impact the NZD and FX stability and the general level of economic activity in New Zealand. | • Considering changes in economic activity as part of our monetary policy considerations and monitoring the value of the NZD as part of our on-going management or balance sheet.<br>• Using foreign currency interventions as a monetary policy tool when there is significant divergence in the New Zealand dollar from its fair value. The primary focus is on our achieving policy objectives in the most efficient manner and on diversifying risk rather than on maximising profit in all circumstances. |
| Rising public and private debt – declining 'fiscal headroom' | Increased debt may weaken spending and put constraints on the effectiveness of monetary policy tools.<br><br>Although objectives between fiscal and monetary policy have coincided, there may be a time when they diverge to enable the Bank to meet policy objectives – i.e. manage prices and support sustainable employment. | • Preparing future alternative monetary policy (AMP) tools, such as forward guidance, a Funding for Lending Programme (FLP), Negative Interest Rates and large scale Purchases of Foreign Assets (PFA).<br>• Working with Treasury and other stakeholders to ensure effective co-ordination between fiscal and monetary policy.<br>• Undertaking economic research on:<br>o Understanding the economic impact of COVID-19.<br>o How different ethnicities, age groups, sexes, and regions have been impacted by previous labour market cycles to gain insights into how the COVID-19 recession may impact New Zealand's labour market<br>o Monetary policy transmission.<br>o The aggregate and distributional consequences for the labour market, and policy influences on the structural level of unemployment.<br>o Distributional consequences and effectiveness of alternative monetary policy. |
| Changing currency and payments systems (e.g. digital currencies and reduced use of physical money) | New Zealanders are changing the way they transact, provide or access cash services – this trend was accelerated by COVID-19. Although transactional cash use and the multi-party cash supply system are contracting at increasing rates, the value and volume of cash in the hands of the public is continuing to increase.<br><br>We must remain on top of developing trends and ensure developing technology is able to maintain the trust and security of cash and developments continue to serve all New Zealanders. | • Building our stewardship of the cash system by working across government and with system participants and users to understand and monitor the public's needs and trends.<br>• Exploring our options for refreshing, investing, and implementing new vaulting and distribution arrangements which are flexible and support the efficient use of infrastructure across New Zealand.<br>• Reviewing the Bank's strategies and approaches for physical currency management to ensure they are appropriate and sustainable.<br>• Considering FinTech innovations and engaging with CoFR partners. |

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| Financial system and institution stress | Economic and health challenges are creating increasing financial and operational stress for financial institutions and their consumers, weighing on consumer confidence and business investment.<br><br>We are mindful of creating additional pressure through regulatory change. This impacts our ability to allocate resources, work with regulated firms, and ensure stability and preparedness. If deployed, some of our Alternative Monetary Policy tools (e.g. Negative Interest Rates) may compress banks' net interest margin/profitability. | • Undertaking bank stress testing[8] to:<br>  ○ Investigate and understand the implications of current and emerging risks to financial stability;<br>  ○ Assess the resilience of participating banks when subject to severe stress;<br>  ○ Support improvements in the use of stress tests by individual banks to identify and manage the risks facing their business.<br>• Reviewing the Insurance (Prudential Supervision) Act 2020 (IPSA) and Solvency Standards – to consider improving resilience and efficiency in the sector. Consultation[9] on each module is expected to start in late November 2020 and be finalised late-2022. The consultation modules will be followed by Cabinet decisions, where required, and drafting of the legislation. The legislative process is expected to occur in the second half of 2023 at the earliest.<br>• Working with Treasury to progress the Deposit Takers Act – to modernise, strengthen and unify our regulatory framework for all deposit takers. The final policy decisions are expected from Cabinet in early Q2 2021. The Bank will then be responsible for drafting instructions and reporting to the Minister on progress.<br>• Working to progress the Financial Market Infrastructures Bill – establishing a new regulatory regime for New Zealand's critical financial market infrastructure. The Bill provides certain FMIs with legal protections relating to settlement finality, netting, and provides new enforcement and oversight powers to the joint regulators, FMA and the Reserve Bank. The Bill is awaiting a Second Reading and the House needs to determine a timetable for reporting back.<br>• Increasing our supervisory capacity and capability over the next 3-5 years by expanding our Auckland presence and adopting a more intensive supervisory approach with a complementary and transparent enforcement regime. This will allow the Bank to make effective use of new powers and implement a deposit insurance regime (through the proposed Deposit Takers Act).<br>• Monitoring the more vulnerable parts of the financial sector closely, planning for recovery and resolution measures if required, and where |

[8] Reserve bank bulletin - Outcomes from a COVID-19 stress test of New Zealand banks
[9] Review of the Insurance (Prudential Supervision) Act (IPSA)

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| | | possible modifying design of alternative monetary policy and other initiatives to minimise adverse impacts.<br>• Implementing planned increases to banks' capital requirements[10], as outlined above.<br>• Producing a monthly Financial System Roundup to the Minister of Finance and publishing a six-monthly *Financial Stability Report* – setting out our assessment of the soundness and efficiency of the New Zealand financial system. The next release is 25 November 2020.<br>• Working with MBIE to consider a new Executive Accountability regime to introduce legislative requirements on senior executives at financial firms to act responsibly and prudently. This work will be progressed outside of, and build on, the Deposit Takers Act, and will need to address coherence with other 'fit and proper' regimes. We expect work to commence mid-2021. |
| Cybersecurity, cloud and data protection | As financial services become more digital (including the Bank and other regulators) – there is a need for heightened awareness of cybersecurity and appropriate priority placed on tools and responses to ensure stability of financial institutions and the payment and settlement systems. This includes our own technology and security infrastructure. | • Delivering the Reserve Bank's Digital Strategy – including an initial focus on cyber security, cloud based data and analytics platforms, digital channels and workspaces, business tools, and resilient technology infrastructure. This aligns with the wider government IT strategy.<br>• Reducing our operational risk through targeted investment in platforms that are nearing end of life.<br>• Producing cyber resilience guidance for all regulated entities – note, this work was delayed as part of our COVID-19 response but restarted in September 2020 with consultation ending Q4 2020. |
| Intergenerational equity | Intergenerational disparities in wealth distribution may affect debt sustainability and levels of asset ownership. | • Monitoring equity disparities as part of our financial stability and monetary policy considerations. |

[10] Review of the capital adequacy framework for registered banks

| *Environmental Sustainability* | | |
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| Climate change and associated risks – physical & financial | Financial stability is best maintained when all relevant risks are adequately identified, priced, and allocated to those best able to manage them. Climate change and its associated risks provide a direct challenge to financial stability as the risks are material but extremely difficult to identify, price, allocate, and manage with accuracy. | • Managing our own direct impact on the climate, reflecting climate risks within our core functions, and contributing to wider efforts to identify, monitor and manage climate risks domestically – and as part of the global regulatory community.<br>• Monitoring risks and promoting strong risk management by financial institutions and training our staff to recognise the financial stability risks of climate change. Foremost our interest is in the exposure of the financial sector, such as banks and insurers, to climate-related risks.<br>• Supporting efforts to increase climate-related financial disclosures as a mechanism to help a smooth transition and mitigate financial stability risks. |
| Policy and market failure to address environmental sustainability | A failure to achieve environmental sustainability would have wide environmental and economic impacts on society and result in repricing of assets, financial instability of both insurers and banks, changes to economic structure and employment practices. | • Collaborating with the Network of Central Banks and Supervisors for Greening the Financial System and the Sustainable Insurance Forum to ensure we have the latest advice on areas such as prudential supervision, macroeconomic research and analysis and portfolio management.<br>• Engaging with domestic stakeholders to contribute to the policy/regulatory landscape.<br>• Raising awareness of the impacts of climate change on financial stability.<br>• Leading the Council of Financial Regulators' climate change work stream.<br>• Collaborating with others such as the Climate Change Commission, the New Zealand Superannuation Fund, the Ministry for the Environment and the Iwi Chairs' Forum Climate Change working group, to contribute to a COVID-19 recovery that takes account of climate risks and investment opportunities.<br>• Encouraging the mobilisation of public and private capital using a toolbox of instruments such as increased disclosure/reporting and ultimately targeted investment through vehicles such as a climate action fund. |

| ***Social Cohesion*** | | |
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| Labour substitution for technology | Increasing use of technology to replace labour impacts the efficacy of our tools to achieve maximum sustainable employment and impacts economic activity. | • We are considering shifts in labour markets as part of our on-going monitoring of the financial system and in our considerations of monetary policy and our economic research programme. |
| Technological pace of change and influence of 'big tech' firms | The acceleration of technological change and growing influence of 'big tech' firms impact the effectiveness of public policy and regulation.<br><br>Open banking developments, new shadow banking arrangements and credit/lending platforms offer new customer services and beneficial competitive pressures, but also bring new oversight challenges as entities may fall outside traditional regulatory frameworks and carry new operational, conduct and financial risks.<br><br>We want our regulatory settings to support innovation and industry-based solutions in financial services. We are keen to ensure that we and the regulatory frameworks we operate do not block digital innovations in financial services from flourishing in New Zealand.<br><br>Over time, such developments may require changes in our supervisory approach and a change in the types of entities or activities that are captured within the perimeter of prudential regulation. | • We are considering developments as part of our on-going monitoring of the financial system and as part of CoFR engagements on FinTech<br>• Engaging and exploring opportunities which may enable us to achieve our mandate more efficiently or effectively. Currently, there are three topics at the top of our agenda:<br>   ○ RegTech & SupTech – We are keen to learn about technology which can increase our ability to perform our operational and regulatory roles, and reduce the cost and complexity for financial services firms of complying with and implementing the regulations.<br>   ○ Analytics – We are interested in understanding the range of analytical tools which will enable us to undertake efficient, timely and insightful analysis of regulatory returns and data.<br>• Digital currencies – We continue to keep abreast of developments on central bank digital currencies and research and current projects by our international peers. |
| Public institutions capability and capacity | The cumulative impact of external challenges and changing expectations is impacting the effectiveness and efficiency of public institutions resulting in difficulties in implementing policy change and creating a consistent approach across regulators. | • Agreeing a new Funding Agreement for the five years commencing 1 July 2020 which will substantially increase our ability to address past underinvestment.<br>• Operationalising the new Reserve Bank Act to modernise our functions. Further details are provided in Chapters 3 and 4 – we expect it to receive Royal assent in 2021 to become effective from 1 July 2022.<br>• Aligning our new digital strategy with our government peers and ensure the Bank has the right tools and resources in place.<br>• Ensuring a 'one voice' approach and creating a clear and consistent regulatory pathway so firms can navigate New Zealand's regulatory landscape with confidence by working with CoFR. |

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| Financial exclusion – technology, geographic, demographic | Financial inclusion drives macroeconomic growth by mobilising savings and investments in the productive sector, and reducing information, contracting and transaction costs across the economy, leading to efficiency gains, which lead to growth.<br><br>A lack of inclusion impacts our ability to engage with stakeholders and the effectiveness of our activities to promote maximum sustainable employment | • Engaging with CoFR on financial inclusion to improve consumers' access to, and understanding of, financial services, particularly in hard to reach communities.<br>• Working with domestic stakeholders to identify challenges related to access to capital for Māori businesses.<br>• Increasing our presence on social media and engaging with stakeholders to explain our role, policies and approaches in plain, simple-to-understand, language<br>• Building strong and collaborative strategic relationships with tangata whenua, iwi, rūnanga, Māori-owned businesses, government agencies, other central banks, heads/representatives of Māori banking, and other Māori organisations.<br>• Integrating the unique intergenerational and long-term overviews of Te Ao Māori into our core policy functions. |
| Persistent wealth and income inequality | Wealth and income inequality affect the efficiency and effectiveness of monetary policy tools to achieve maximum sustainable employment. | • Monitoring distributional impacts of policies and economic trends as part of our financial stability and monetary policy considerations. |
| Infrastructure deficits – public and private | Infrastructure deficits constrain the optimal movement of people and goods around the country impacting economic productivity. | • Monitoring economic activity as part of our financial stability and monetary policy considerations. |
| Public perception of financial institutions | Following the economic impacts of the COVID-19 pandemic and the recent Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry and Bank Conduct and Culture review there been increased scrutiny and public interest in financial institutions and regulators.<br><br>Public perceptions impact investor and consumer confidence and can impact economic activity and consumer willingness to engage with regulated or unregulated entities. | • Increasing external communications and engagement using plain language over LinkedIn, Twitter, Facebook, Instagram and YouTube to reach wider audiences.<br>• Making our Governor and SLT available for interviews, speeches and stakeholder engagements.<br>• Deepening our engagement across CoFR agencies and ensuring optimal information flows and co-ordination.<br>• Refreshing our brand and website to enable better engagement with our stakeholders.<br>• An indirect impact of many of our activities under 'Financial system and institution stress' will also increase public confidence in financial institutions. These include: |

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| | | ○ reviewing the Insurance (Prudential Supervision) Act 2020 and Solvency Standards;<br>○ working with Treasury to progress the Deposit Takers Act;<br>○ working with Treasury to progress Financial Market Infrastructures Bill; and<br>○ working with MBIE to create a new Executive Accountability regime. |

| ***Cultural Inclusion*** | | |
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| Workforce and public policy diversity and inclusion | A lack of diversity creates miscommunication, barriers to meaningful engagement, and limits innovation.<br>Diversity of experience, thought, background and inclusivity of all employees is recognised as an imperative for higher performing organisations and effective policy development. | • Embedding the Bank's Diversity and Inclusion (D&I) strategy including gaining external recognition for our D&I approach, and implementing Te Whāriki, our diversity and inclusion ecosystem.<br>• Engaging with a wider range of stakeholders to identify challenges and work together to find solutions which work for all e.g. identifying issues related to access to capital for Māori businesses.<br>• Leveraging our partnership with BERL and its Māori Economic Research to better understand the Māori economy. |
| Ageing population and associated needs | An ageing population may result in a lower aggregate labour force participation rate. This affects the efficiency and effectiveness of monetary policy tools to achieve maximum sustainable employment. | • Considering shifts in labour markets and savings trends as part of our on-going monitoring of the financial system and in our considerations of monetary policy and our economic research programme.<br>• Undertaking economic research on the aggregate and distributional consequences for the labour market of the COVID-19 pandemic. |
| Protectionism of borders, trade, and domestic employment | Protectionist policies and limited trade capacity impact New Zealand exports, the value of the NZD and the general level of economic activity in New Zealand. | • Considering changes in economic activity as part of our monetary policy considerations and monitor the value of the NZD as part of our on-going management our balance sheet.<br>• Using foreign currency interventions as a monetary policy tool when there is significant divergence in the New Zealand dollar from its fair value. The primary focus is on our achieving policy objectives in the most efficient manner and on diversifying risk rather than on maximising profit in all circumstances. |
| Rapid global urbanisation | Rapid urbanisation is expected to drive shifts in regional labour markets. | • Considering shifts in labour markets as part of our on-going monitoring of the financial system and in our considerations of monetary policy and our economic research programme. |

Table 2 – The Bank's response to the external environment challenges.

# Chapter 3 - How the Reserve Bank operates

## Our vision and values

We aim to be a modern Central Bank and have a vision of being a 'Great Team, Best Central Bank'. This means we operate transparently; are open to learning and adapting as necessary; work collectively and collaboratively; and are an active, relevant cornerstone of New Zealand's economy and society.

This vision describes our activities, our people, and the way we interact and engage with our stakeholders. Delivering on this enables us to be the best kaitiaki (guardians) of the financial system we can and ensures we deliver our responsibilities to all stakeholders reliably, transparently, inclusively, with integrity, and with innovation.

Our *Statement of Intent*[11] outlines the activities we are undertaking to achieve this vision. These activities are supported by an enterprise-wide, and mandate specific, approach to recognising and managing operational, financial, legal and reputational risk. The Bank has a series of risk appetite statements which enable us to be accountable for our decisions and empower staff to recognise risk and avoid undue risk. This promotes consistency in our decision making and enables us to build strong public confidence.

A key part of our culture is embracing diversity and inclusion. This means broadening our workforce, our approach to stakeholder engagement, and our policy knowledge. This enables us become a more inclusive, effective, and innovative central bank, and is key to enhancing and unlocking the potential of our people, our policies, and the economic well-being of all New Zealanders.

As New Zealand's central bank, Māori values are part of our national identity. We remain committed to our Te Ao Māori strategy[12] and using storytelling to connect with our stakeholders and tell the story of the Reserve Bank[13]. By building understanding and embracing our history and heritage, we are able to explore how Māori culture and businesses operate and gain unique insights into their contribution and impact on the New Zealand economy. This allows us to take a long-term view of our core mandate and promote the well-being and prosperity of all New Zealanders.

## Working with our stakeholders

We are committed to building positive and future-focussed relationships which support our priorities. This supports our ambition for the Bank to become:

- a targeted thought-leader in the international community, and
- an 'outstanding international citizen' among central banks.

We are an active member of several international and regional groupings (e.g. International Monetary Fund, the Bank for International Settlements (BIS), Executives' Meeting of East Asia-Pacific Central Banks (EMEAP)), and the meetings cover a range of the Bank's priorities. They also support relationship building with other central banks and regulators.

One of our key domestic stakeholders is the Council of Financial Regulators (CoFR) - responsible for joint stewardship of a healthy and efficient financial system that benefits all New Zealanders[14]. CoFR comprises of the Bank, the Financial Markets Authority, the Treasury, the Ministry of Business, Innovation and Employment, and the Commerce Commission.

[11] Statements of Intent
[12] Te Ao Māori: an evolving and responsible strategy
[13] The Journey of Te Pūtea Matua: Our Tāne Mahuta
[14] CoFR work priorities for 2020

The group contributes to maximising New Zealand's sustainable economic well-being through responsive and coordinated financial system regulation. We work together to identify and monitor important issues, proactively work together on issues and responses that require cross-agency involvement, and develop a shared view on longer-term strategic priorities for the financial system.

## Opportunities for the Reserve Bank

There are a number of opportunities which will lay the foundations for the Bank to continue to assist the longer-term wellbeing of New Zealanders for years to come and enable us to meet our vision of Great Team, Best Central Bank:

- **Transformation** – The implementation of the new Reserve Bank Act and new Funding Agreement will enable us to undertake considerable transformation of the Bank. This will allow us to continue to effectively and consistently deliver our mandate – including a focus on our new Board, new ways of working, new processes, policies and delegations, our independence, our transparency and accountability.
- **Monetary policy** – The current and forecast environment has required us to use our monetary policy and alternative monetary policy tools in ways which are new to New Zealand. There is a possibility that more capital and/or more indemnities may be needed to maximise the effectiveness and efficiency of our AMP tools, fiscal and monetary policy working in tandem. These tools will assist us in achieving and maintaining price stability and supporting maximum sustainable employment throughout any upcoming economic recovery. We welcome discussions with the Minister on the optimal policy mix required to achieve these objectives and enable the Bank to meet its mandate. Early engagement and transparency on monetary and fiscal policy and maintaining an effective relationship with Treasury and other parts of government is key to promoting the prosperity and well-being of New Zealanders.
- **The future of prudential regulation and supervision** – The Deposit Takers Act, FMI legislation and new Funding Agreement will allow us to shape how we prudentially regulate New Zealand's financial sector – including a focus on deposit insurance and failure management, and strengthening our capacity and capability in supervision and enforcement.
- **Our role as system steward and contributor** – We support and promote New Zealand's economic well-being through leadership, collaboration and stewardship across financial services. We will continue this by forming stronger relationships across financial regulators (e.g. supporting MBIE's Consumer Data Right proposals), engaging with our international peers on mutual challenges (e.g. remittances across the Pacific), contributing to the discussions on the impacts of climate change on financial services, and embedding our Te Ao Māori strategy to better understand the Māori economy and responding to challenges and opportunities for all New Zealanders.

Our ability to engage and communicate in a manner which all New Zealanders can understand is key to delivering on these opportunities. We must work collectively and collaboratively with other regulators and the financial services industry to continue to be active, relevant and a cornerstone of New Zealand's economy and society. Our integrity is critical to our success, and we maintain this integrity by operating transparently – being open to learning and adapting as necessary. For this, strong future governance is critical.

# Chapter 4 – Upcoming key publications and consultations

In November we are publishing a *Financial Stability Report* (FSR) and *Monetary Policy Statement* (MPS).

Given the economic environment and outlook, we expect both publications to receive considerable media attention.

The FSR is a six-monthly report which assesses and reports on the soundness and efficiency of the New Zealand financial system. It assesses the health of the banks and other deposit taking institutions, the insurance sector and the payments system in New Zealand. It highlights potential risk areas and measures the Reserve Bank is taking to respond to them.

The quarterly MPS reports on the approach and tools the Monetary Policy Committee (MPC) has agreed on to achieve its policy objectives of maintaining price stability and supporting maximum sustainable employment. The Statement includes reasoning for adopting that approach, and transparency and accountability requirements of the MPC Charter including if inflation outcomes (and/or expected outcomes) are outside of the target range[15] and outlining how monetary policy is currently supporting maximum sustainable employment.

We are also issuing a significant number of consultation documents in November 2020 relating to our bank capital decisions and our review of the insurance prudential framework as noted below. More details on these will be included in a separate briefing.

The table below highlights the Bank's key upcoming publications and consultations. The table also highlights key speaking engagements. We share key messages, draft speeches and media releases with the Minister ahead of engagements or publications:

| | |
|---|---|
| November | • *Monetary Policy Statement* – 11 Nov<br>• Capital Review: Exposure Drafts; revised timetable; and banking handbook exposure consultation – 17 Nov<br>• *Financial Stability Report* – 25 Nov<br>• IPSA consultation – 30 Nov<br>• Speaking engagements:<br>    ○ Climate Change & Business Conference – 12 Nov<br>    ○ European Investment Bank Finance in Common Summit – 12 Nov |
| December | • Speaking engagements:<br>    ○ Sir Leslie Melville Lecture, Australian National University – 2 Dec – Monetary policy in a small open economy during COVID-19 |

Table 3 – Key publications, consultations and events for H2 2020.

We welcome engagement and support from the Minister on these.

[15] Remit-for-the-Monetary-Policy-Committee-April-2019

# Chapter 5 - Our legislation, governance and structure

## Legislation and functions of the Bank

The Reserve Bank is a Crown agency and performs functions derived from four key pieces of legislation, namely:

- the Reserve Bank of New Zealand Act 1989 (Reserve Bank Act), which specifies the Bank's and the Governor's capacity, functions and powers, as well as its monetary policy, banking supervision and financial markets infrastructure oversight functions;
- the Insurance (Prudential Supervision) Act 2010 (IPSA), which provides for the Bank's role as the prudential supervisor of the insurance sector;
- the Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (AML/CFT), which confers responsibility on the Bank as an AML/CFT supervisor; and
- the Non-bank Deposit Takers Act 2013 (NBDT Act), which establishes the Bank as the prudential regulatory and licensing authority for non-bank deposit takers.

When enacted, the Bank will also have duties under the Financial Market Infrastructures Act as joint regulator with the Financial Markets Authority.

Under the Reserve Bank Act the Bank exercises its authority through the Governor, apart from monetary policy, which is operated by the MPC.

Under the legislation set out above the Bank carries out the following functions:

- Implements monetary policy for the objectives of achieving and maintaining stability in the general level of prices over the medium term; and supporting maximum sustainable employment.
- Prudentially regulates registered banks, licensed non-bank deposit takers and licensed insurers.
- Supervises banks, non-bank deposit takers and life insurers for the purposes of the Anti-Money Laundering and Countering Financing of Terrorism Act 2009.
- Regulates payment and systems and, along with the Financial Markets Authority as co-regulator, regulates settlement systems.
- Issues banknotes and coins to meet the needs of the public.
- Provides settlement accounts for qualifying entities to settle their daily and intraday balances.
- Provides NZClear to enable qualifying entities to settle the transfer of securities.
- Provides a suite of liquidity facilities to qualifying financial entities for the purposes of managing liquidity in the financial system and supporting the soundness of the financial system.
- Carries out a range of surveys to support the operation of the Bank and to inform the public about the economy.

Both the formulation and implementation of monetary policy and the Bank's statutory regulatory functions are carried out at arm's length from the government of the day to ensure we can focus on the long term objectives of price stability, maximum sustainable employment and financial stability.

We are held to account by the Bank's Board of Directors and the Minister for our performance against legislative purposes and duties. The Bank publishes a range of accountability documents each year including our *Monetary Policy Statements*[16], *Financial Stability Reports*[17], *Statement of Intent*[18] and *Annual Report*[19].

The Bank's activities are also examined by Parliament's Finance and Expenditure Committee.

[16] Monetary Policy Statement
[17] Financial Stability Report
[18] Statement of Intent
[19] Annual Reports

The committee receives a copy of our accountability reports and holds hearings following delivery of the quarterly monetary policy statements, the six-monthly financial stability reports and the *Annual Report*.

## Operationalising our new Reserve Bank Act

In 2017 the Government undertook a review of the Reserve Bank Act. This is the governing legislation that outlines the Bank's purpose and how it operates as a central bank independent of government. It includes the Bank's monetary policy functions as well as its regulatory and supervisory powers.

With the current Reserve Bank Act being 30 years old, reviewing and modernising it is a crucial part of ensuring that the Bank remains fit for purpose. It is an exciting time for the Bank and means that we will have a robust governance and accountability framework in place. The new Reserve Bank New Zealand Bill was introduced to Parliament on 28 July 2020[20], and we anticipate it will progress through its stages to receive Royal assent in 2021, becoming effective from 1 July 2022.

We are ensuring the Bank is well positioned and ready to embrace significant change and deliver on its responsibilities under the new Reserve Bank Act from its commencement date. We are currently scoping the plan, budget, resourcing and governance for the implementation of the new Reserve Bank Act and ensuring that the level of change required to meet the provisions of the Act is understood across the Bank. The benefits will be to ensure external stakeholders (including Government, our Minister, new Board, new monitoring agency and public) and internal stakeholders (staff, board, management) have confidence in the Banks' ability to operate as intended under the new Reserve Bank Act.

The new Reserve Bank Act will replace our existing institutional legislation (Reserve Bank of New Zealand Act 1989). The Bill adopts many provisions of the Crown Entities Act. The Bill:

- establishes a board responsible for the management of all the functions of the Bank, except those undertaken by the MPC;
- removes the powers of the Governor as single decision maker and recreates the role as Chief Executive under the direction of the board (albeit appointed and removed by the Minister);
- provides a revised financial stability objective of protecting and promoting the stability of New Zealand's financial system and requires the Minister to issue a Financial Policy Remit that provides relevant considerations for the Bank when pursuing the objective; and
- will enhance the Bank's accountability through greater alignment with state sector practice of reporting and monitoring requirements, with the Treasury acting as the external monitor.

Our current Board will continue to operate until July 2022. A transitional board will be appointed under the new Act and will be fully operational at the commencement of the Act, intended at this stage to be 1 July 2022.

## Operationalising the Deposit Takers Act

We are working with Treasury to progress the Deposit Takers Act. The Deposit Takers Act is expected to modernise, strengthen and unify our regulatory framework for all deposit-takers – both banks and non-bank deposit-takers, and maintain a regulatory approach that is proportionate to financial stability risks. Consultation for the final Phase 2 closed in October.

Deposit takers play a critical role in the economy, enabling both saving and borrowing and transactions between economic agents, and facilitating economic activity more generally. The failure of a bank or other deposit taker can therefore have very significant impacts on the stability of the overall financial system and on the wellbeing of individual depositors.

The Deposit Takers Act seeks to enhance the existing prudential regime, the aim being to reduce

[20] Reserve Bank of New Zealand Bill

these risks. This is achieved by setting requirements that promote the soundness and resilience of deposit takers, supported by a supervision and enforcement regime that promotes compliance. It is also critical that, in the event of a crisis, there are clear and credible mechanisms to protect the more vulnerable depositors (such as a deposit insurance scheme) and for managing the crisis and resolving any deposit taker failures.

Final policy decisions are expected to be taken to Cabinet in early Q2 2021, with legislative drafting to follow.

## Senior Leadership Team

The Reserve Bank Act confers considerable day-to-day operational autonomy on the Bank. This is co-ordinated across the Senior Leadership Team and through their respective business units:

- **Adrian Orr**, Governor
- **Geoff Bascand**, Deputy Governor/General Manager Financial Stability
- **Christian Hawkesby**, Assistant Governor/General Manager Economics, Financial Markets and Banking
- **Patrick Hoerler**, Assistant Governor/General Manager Business Operations
- **Simone Robbers**, Assistant Governor/General Manager Governance, Strategy and Corporate Relations
- **Juliet Tainui-Hernandez**, Assistant Governor/General Manager Transformation and Culture
- **Mike Wolyncewicz**, Assistant Governor/Chief Financial Officer

## Board of Directors

The Reserve Bank Act and the Board Charter set out the responsibilities of the Board and its members. The Board keeps the performance of the Bank, including the use of its resources, and the performance of the Governor, Deputy Governor, and the Monetary Policy Committee (MPC) and its members under constant review. The Board nominates candidates for appointment as Governor, Deputy Governor, internal members of the MPC and external members of the MPC. The Board may provide advice to the Governor on any matter relating to the performance of the Bank's functions and the exercise of its powers. The Board approves the Code of Conduct adhered to by MPC members.

The Board's performance assessments rely on a variety of monitoring mechanisms, including:

- review of the performance of the MPC;
- access to the records of the MPC;
- the Bank's accountability documents (SOI, Annual Report, FSRs);
- regular reporting from the Bank on progress in meeting the strategic priorities in the SOI;
- regular dashboard reporting on the Bank's operational performance; and
- meetings with stakeholders in conjunction with Board meetings and outreach functions.

Current members:

Non-executive members:

- **Professor Neil Quigley,** Chair
- **Tania Simpson,** Deputy Chair
- **Dr Chris Eichbaum**
- **Fiona Mules**
- **Susan Paterson, ONZM**
- **Jonathan Ross**

Executive members:

- **Adrian Orr, Governor**

## Monetary Policy Committee

The MPC is responsible for formulating monetary policy directed at achieving the economic objectives of price stability and supporting maximum sustainable employment, as set out in section 8 of the Reserve Bank Act.

The current Remit[21] requires the Bank to keep inflation between 1 and 3 percent on average over the medium term, with a focus on keeping future average inflation near the 2 percent target midpoint. There is no numerical target for employment, as the Bank uses a range of different indicators to assess the maximum sustainable level.

Monetary policy decisions are reviewed seven times per year, or more frequently if required. Over recent decades, the Bank has typically implemented monetary policy by setting the OCR. More recently, the Bank has started to use a wider range of tools to support economic activity, such as purchases of New Zealand Government bonds through the Large Scale Asset Purchase (LSAP) programme. Additional tools, such as a Funding for Lending Programme (FLP), and large scale Purchases of Foreign Assets (PFA) are additional monetary policy tools which can be used in the future.

The MPC is subject to the monetary policy framework[22] – the Remit, Charter and Code of Conduct are key components of the framework. The remit sets the operational objectives for monetary policy. The charter provides for decision-making procedures, transparency and accountability. The code of conduct sets out minimum standards of ethical and professional conduct that must be adhered to by members of the MPC.

Internal members:

- **Adrian Orr**, Governor
- **Geoff Bascand**, Deputy Governor/ General Manager of Financial Stability
- **Christian Hawkesby**, Assistant Governor/General Manager of Economics, Financial Markets and Banking
- **Yuong Ha**, Chief Economist

External members:

- **Professor Bob Buckle**
- **Peter Harris**
- **Professor Caroline Saunders**

## The Role of the Minister of Finance

The Minister of Finance sets the operational objectives for monetary policy through the Remit. While the Bank's prudential regulation functions are carried out at arms' length from the Minister, the Minister has a range of powers in the event that a bank is about to or has failed. These include advising the Governor General to place a failing bank into statutory management, consenting to directions given to a registered bank by the Reserve Bank. The Minister appoints the Governor, the Deputy Governor and members of the MPC (in each case on the recommendation of the Board).

A Memorandum of Understanding[23] between the Minister and the Governor commits the Bank to consult the Minister and the Treasury before implementing macro-prudential tools covered by that Memorandum. The Minister can also direct the Reserve Bank to intervene in the foreign exchange market.

The Bank meets regularly with the Minister and the Treasury to discuss a range of issues, including developments in the prudential policy work area and other matters affecting financial

[21] Remit-for-the-Monetary-Policy-Committee-April-2019
[22] Monetary Policy Framework
[23] Memorandum of Understanding between the Minister of Finance and the Governor of the Reserve Bank of New Zealand

stability. The Bank also receives an annual Letter of Expectations[24] from the Minister setting out the Minister's expectations for the Bank for the year ahead. The Minister's letter is published on the Reserve Bank website.

## How the Bank is funded

The Bank does not receive appropriations through the central government budgetary process to cover its operating expenses. Instead, the Bank's funding is based on a funding agreement,[25] a five-yearly agreement between the Governor and the Minister, which specifies how much of the Bank's revenue can be used to meet its operating costs (Reserve Bank Act, sections 159-161).

This revenue comes from the return on the Bank's investments, the seigniorage, and deposits (held by banks and the Crown). The remainder of realised earnings is potentially available to be distributed to the Crown as a dividend.

The amount of the dividend to be paid to the Crown is determined by the Minister on the recommendation of the Bank, having regard to the views of the Board of Directors, the views of the Treasury and any other relevant matters.

The Bank publishes the principles for determining the amount it recommends to be paid as an annual dividend as part of our *Statement of Intent*. These principles are:

- the Bank should maintain sufficient equity for the financial risks associated with performing its functions. Equity in excess of that required to cover those risks will be distributed to the Crown; and
- in general, unrealised gains should be retained by the Bank until they are realised in NZ dollars. However, the Bank may recommend the distribution of unrealised gains where the Bank believes that the probability of the gains being realised is high

This year, the bank recommended not paying a dividend due to the uncertainty about further actions that may be needed in the near term to achieve our policy objectives given the impacts of COVID-19 on the New Zealand economy. Retaining earnings strengthens our balance sheet and gives us the ability to absorb further risk in the future if required. This action was consistent with the dividend principles.

In June 2020 a new Funding Agreement[26] for the five years commencing 1 July 2020 was agreed. The new Funding Agreement, ratified by Parliament on 30 June 2020, substantially increases the Bank's net operating expenses, with an average annual increase of $46 million. The new agreement provides the Bank with an average $115 million a year for its operations over the next five years, with a further average of $13 million a year for the issuance of currency[27].

The Bank will use this increased funding to focus on addressing critical risks to delivering its mandate, responding to areas of past underinvestment and establishing the long-term operating model to promote the well-being of all New Zealanders. This includes a substantial increase in the Bank's supervisory capability, as recommended by the International Monetary Fund's (IMF) 2017 Financial Sector Assessment Programme Review[28].

[24] Letter of Expectations
[25] Funding Agreements
[26] Reserve Bank Funding Proposal and Agreement
[27] We consider currency issue expense separately as this is externally demand driven and not controllable by the Bank.
[28] Financial Sector Assessment Programme

**Reserve Bank of New Zealand Te Pūtua Matua**



PO Box 2498
Wellington
NEW ZEALAND

www.rbnz.govt.nz

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