RESERVE BANK
OF NEW ZEALAND
TE PŪTEA MATUA

Informed investment decisions support financial system stability

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Introduction

I join Andre Laboule and Diane Maxwell in welcoming you all to this meeting of the OECD International Network on Financial Education (INFE), and may I also welcome you to New Zealand. I know most of you have travelled long distances to attend the meetings this week. I hope you find your stay in Auckland productive and enjoyable.

I offer particular thanks to our joint host, Diane Maxwell and the New Zealand Commission for Financial Capability, for inviting me to your meeting today and for putting together an impressive program of meetings and activities over this week. As a founding member, the Commission has made a strong contribution to the INFE since its inception in 2008.

While not a member of the INFE, I certainly have a close interest in the network and its work. I chair the OECD Financial Markets Committee (CMF) which is one of the two OECD committees that oversee the work of the INFE. We take particular interest in the work around measurement and policy development that is mandated by the G20. A current issue of interest is the influence of new digital technology on financial education and financial inclusion. A session of our upcoming CMF meeting in Paris will be devoted to the potential implications of new Fintech developments across a number of fronts, including as a financial education tool.

The role of new technology in shaping financial behaviour is also relevant to me in my main job as Head of financial Stability at the Reserve Bank of New Zealand. The Bank is not responsible for investor protection, which is the role of the New Zealand Financial Markets Authority (FMA). Rather we are responsible for prudential regulation and the overall stability of the New Zealand financial system. Nevertheless, a well informed and educated investing public is crucially important for the safety of the overall financial system as well as for the welfare of the investing public. I would like to take a few minutes to expand on this theme and to describe some recent developments where we are using technology to improve the quality of bank disclosure, with the ultimate aim of a more informed and resilient banking system.

Three pillars approach to supervision

The Bank’s approach to promoting financial system stability is based on the ‘three pillars’ of market discipline, self-discipline and regulatory discipline. We have strengthened our regulatory discipline pillar in recent years, but still have a less intensive approach to supervision than other international regulators. We do not, for example, conduct on-site supervision of the entities we regulate.

Our main focus is on market and self-discipline. The self-discipline regime focuses on the responsibility of boards and senior management to ensure sound risk management practices through their organisations. For market discipline, two important elements are disclosure and the absence of deposit insurance. The Reserve Bank was an early pioneer in disclosure and it continues to be a key element in our regime. Banks and finance companies must disclose information that allows investors to make informed choices about where to put their money, in particular to understand the risks as well as the returns inherent in investment choices.

The absence of deposit insurance in New Zealand means that investors can lose money if a New Zealand financial institution fails. This underpins market discipline as investors are incentivised to be vigilant and make informed investment choices. This helps to promote a healthier and safer financial system. The Reserve Bank and the New Zealand Government believe deposit insurance blunts incentives for both financial institutions and depositors to monitor and manage risks properly.

Disclosure and education

Proper disclosure by financial institutions and market discipline clearly work best in an environment where everyone is financially educated. It is in people's own interests and in society's interest, that investors understand at least the basics of risk and return. Such understanding – based on education and information - certainly helps the Reserve Bank to achieve its system stability objective.

All investors, from individuals saving for a house deposit to professional fund managers, need to understand the risks involved, for example:

- In the current stretched housing market – what could happen to me financially if the market turned down? And how much debt can I really afford?
- In today's world of low interest rates, if I go for a higher interest investment, or shares, what risks am I really taking on?
- How can I protect the value of my retirement nest egg without taking undue risks?

Investors and their advisors need accurate and relevant information in order to answer such questions and to make sensible decisions about where to put their money.

Role of Technology

Looking forward, there is no doubt the transparency of investments can be enhanced by modern technology. Today's technology can be used to generate more timely, comparable and accessible information on investment alternatives. The Reserve Bank is currently undertaking public consultation on a proposed 'Dashboard' approach to public disclosure by banks. The Dashboard would provide a side-by-side comparison of the banks' financial health, located on the Reserve Bank's website and updated quarterly. This would supplement the more extensive but less comparable disclosure statements that banks currently prepare. The aim of the Dashboard would be to help investors with more timely and comparable information on banks, so that all investors can make better decisions about where to put their money.

Technology offers a huge range of opportunities for financial education, particularly in making information more accessible and more user-friendly. In New Zealand, an important recent example of this is the work that the Commission for Financial Capability have done to provide information about alternative KiwiSaver products on their 'Sorted' website http://fundfinder.sorted.org.nz/. The Reserve Bank sees its Dashboard very much in the same vein.

As a web-based tool, a major advantage of the Dashboard will be the ability to track its usage. This will help to assess the Dashboard's usefulness over time and allow us to regularly improve its content and structure to ensure it is achieving its purpose. Technology is giving us new and more dynamic ways of achieving this.

Role of regulation and tax

Transparency and a healthy financial system are supported by regulatory and tax frameworks that do not favour one investment over another and which facilitate the development of new financial products. The regulatory framework should also ensure that financial advisers are incentivised to look after their clients' interests, not their own. Recent changes to the Financial Markets Conduct Act have resulted in changes to the way financial products are offered and promoted. These frameworks play a key role in building confidence in our markets and providing a level playing field for investors.

Conclusion

Disclosure, technology and regulation are very important but can get us only so far. Society has a responsibility to give individuals at least a basic knowledge of financial risk and return. Financial regulators have a responsibility to provide the incentives and information that allow people to use that knowledge in making investment decisions. Educated investors, transparency of financial providers and advice geared to the needs of investors will all help to deliver fewer financial crises, higher quality investments and a stable financial system.

I wish you well for a productive meeting today which will see the discussion and approval of the program of work for the next biennium. And I am sure you will have a very successful Symposium tomorrow.