
Reserve Bank of New Zealand

Statement of Intent

For the period 1 July 2009 to 30 June 2012

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Introduction

Under section 162A of the Reserve Bank of New Zealand Act 1989 (the Act), the Reserve Bank is required, prior to each financial year, to provide the Minister of Finance with a Statement of Intent (SOI) traversing the following three years.

Section 162B of the Act states that the Reserve Bank's SOI must contain:

- key background information about the Bank and its operating environment;
- the nature and scope of the Bank's functions and its principal areas of operation;
- the specific impacts, outcomes or objectives that the Bank seeks to achieve or contribute to;
- how the Bank intends to perform its functions and conduct its operations to achieve those impacts, outcomes or objectives;
- if a direction has been given under section 68B, how the Bank has had regard to the direction;
- the proposed strategies for managing the organisational health and capability of the Bank;
- a statement of the projected income and expenditure for the first financial year in the period to which the SOI relates;
- a statement of the principles in accordance with which the Bank must determine the amount it recommends to the Minister as appropriately payable by the Bank to the Crown as an annual dividend;
- the main financial and non-financial measures and standards by which the future performance of the Bank may be judged;
- the matters on which the Bank will consult or notify the Minister before making a decision, the matters on which it will report to its Minister, and the frequency of reporting; and
- any other matters that are reasonably necessary to achieve an understanding of the Bank's intentions and direction.

What we do

The Reserve Bank of New Zealand is the nation's central bank, established by an Act of Parliament, the Reserve Bank of New Zealand Act. The Bank has three main functions, which are designed to promote a sound and dynamic monetary and financial system aimed at meeting the goal of improving New Zealand's economic performance. These functions are: (1) the management of monetary policy to maintain overall price stability; (2) the maintenance of a sound and efficient financial system; and (3) the supply of legal tender to meet the currency needs of the public.

The functions and operations that the Bank performs to achieve these objectives are described in the following pages. In performing them, the Bank ensures that it works effectively with Ministers, the Treasury, other relevant government departments and the private sector on all matters where there is a shared interest.

Vision

We promote a sound and dynamic monetary and financial system.

Values

Integrity – Being professional and exercising sound judgement

Innovation – Actively improving what we do

Inclusion – Working together for a more effective Bank

Foreword

We have prepared this *Statement of Intent* in the aftermath of a series of global financial shocks that have shaken confidence in markets, severely disrupted pricing and trading, destroying vast amounts of wealth, and making credit difficult and more expensive to access. The loss of confidence and subsequent credit crunch have stalled trade and production in many economies, sinking many into recession. The shocks have drawn unprecedented policy responses from governments and central banks.

When this financial crisis hit, New Zealand was already in a shallow recession, caused by drought and a correction in housing and consumption brought on by higher petrol prices and interest rates. Nevertheless, we have got off remarkably lightly so far compared with larger Northern Hemisphere economies. We have lowered the Official Cash Rate 575 basis points to 2.5 percent, its lowest level ever; we have expanded liquidity facilities; Government has offered guarantees on retail deposits in financial institutions and on wholesale funding. But we have been spared the necessity of zero interest rates, massive capital injections to shore up banks and companies, and unorthodox quantitative easing measures that have occurred particularly in the US and Britain.

Nevertheless, financial aftershocks still rock our markets, with New Zealand dollar investments swinging in and out of favour by the day as market appetite for risk fluctuates.

The New Zealand economy has been under pressure from the international crisis, global recession and weak domestic spending. Global credit supplies have contracted, heightening risks associated with New Zealand's reliance on external funding. Highly leveraged households and firms are having to adjust to falling housing and other asset prices. Banks are needing to make provision for more impaired loans, but at the same time play an important role in New Zealand's recovery by passing on recent OCR cuts into short-term lending rates. How long recovery will take is uncertain, though it is likely that it will be some significant time before economic activity returns to robust and healthy levels.

Moreover, the world is now being swept by influenza A H1N1 09. It looks likely this will impact the economy by hitting staffing, through sickness, childcare and precautionary behaviour. If the incidence is severe, it would delay recovery. Meantime, the Bank is ensuring that it can maintain its operations if the virus escalates.

In these volatile and uncertain circumstances, we have re-set some of our Strategic Priorities to ensure outcomes that we would take for granted in normal times: that our markets can still deliver sufficient funding to the economy; that our banks have adequate capital. To casual observers, our primary objective of maintaining price stability may seem the least of our concerns in the current climate, but an enormous challenge looms in the inflationary risks once confidence returns to normal in global markets when there is so much liquidity around. We will be focused on these risks as we consider the likely nature of a recovery.

Although stabilisation is our pressing need at present, we have not lost sight of the need to press on with enhancements to our roles and our tools. We will develop and implement the new regulatory framework for non-bank deposit takers and insurance companies. We will be upgrading our statistical data collection systems.

And, coincidentally, we will establish a small Auckland office to provide backup for essential payments and financial markets operations in the event of a physical disaster in Wellington.

We also want to ensure that the right staff are doing the right work, that they remain focused and motivated, and that they have the opportunity to continue to develop their skills and knowledge.

Under legislative changes enacted last year, we are now required to include key performance indicators (KPIs) in our SOI. Last year we voluntarily included KPIs for our external functions to provide us with experience in setting indicators that could be measured meaningfully. Most of those initial KPIs have stood the test and are included again in this SOI. We note that the quarterly *Monetary Policy Statement* and six-monthly *Financial Stability Report* are already required by statute as accountability documents.

The SOI covers a three-year period which overlaps the final year of the current five-year Funding Agreement, which expires at 30 June 2010, and the first two years of the next Funding Agreement, which has yet to be negotiated with the Minister of Finance.

The Bank's budget for 2009–10 shows an increase in operating expenditure from \$52.1 million to \$55.1 million, primarily reflecting the expansion of the Bank's regulatory responsibilities for non-bank financial institutions, the costs of establishing a new office in Auckland, and depreciation of new systems.

As a financial institution with approximately \$29 billion in assets, the Bank faces a wide range of financial risks. The global financial crisis has significantly affected exchange rates and interest rates. This has resulted in large changes to our projected interest income and to the values of our foreign currency assets and liabilities and holdings of New Zealand government securities. The open foreign exchange position in particular will cause increased volatility in the Bank's financial performance and financial position.

The Reserve Bank of New Zealand Amendment Act 2008 changed the framework governing payment by the Bank of an annual dividend to the Crown. It changed the regime from a formula-based approach (i.e., the Act previously contained the formula, known as 'notional surplus income', for calculating the annual dividend the Bank recommended to the Minister each year) to a principles-based approach.

Overall, this SOI reflects the Bank's continuing strategy of endeavouring to ensure stability in New Zealand's financial system and economy despite an uncertain environment.



Alan Bollard
Governor



Grant Spencer
Deputy Governor

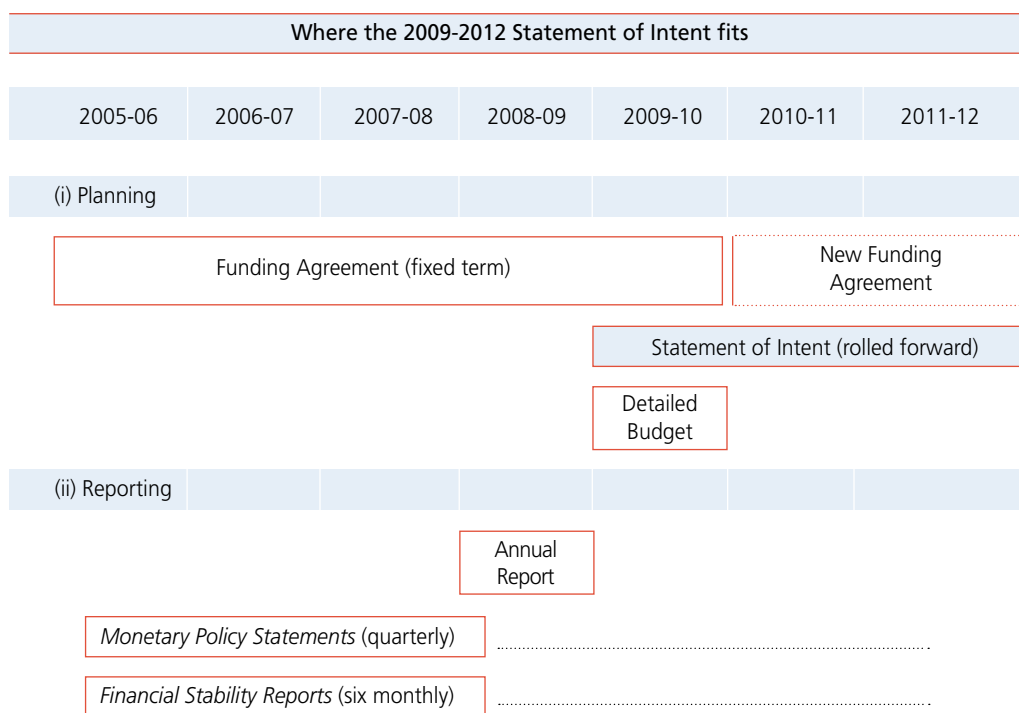
Reserve Bank Strategic Priorities for 2009-10

Department	Priority	Explanation
1 Financial Markets	Ensure the banking system has sufficient liquidity to meet its ongoing funding needs.	The ongoing global credit crisis is making it more expensive for banks to maintain adequate levels of liquidity and to raise term funds. The Bank has already implemented several measures to ensure adequate liquidity, and is assessing options should the need for further measures arise.
2 Prudential Supervision	Ensure that the registered banks maintain adequate capital, through close monitoring of asset quality and prompt supervisory responses.	The Reserve Bank will further increase its monitoring of registered banks' prudential status with a particular focus on early identification of any deterioration in asset quality and of any impact this may have on capital adequacy. If necessary, the Bank will take supervisory action to ensure that any problems identified are dealt with promptly and effectively. The Bank will finalise and implement new liquidity requirements for registered banks and will review capital requirements in the light of international developments and experience in New Zealand.
3 Economics	Support effective monetary policy for inflation targeting in a world of volatile financial and economic conditions.	The economic and financial crisis has markedly changed the shocks hitting the economy. It has also complicated the influence of monetary policy on financial conditions. The Bank will develop analytical tools and research knowledge in response. In particular, this includes coping with the challenges presented by asset price and credit boom/bust cycles, advising on the appropriate mix of monetary policies for economic stabilisation, and enhancing data collection and communication with other agencies.
4 Knowledge Services/ Economics	Implement our Financial Sector Information System (FSIS), significantly improving the management of statistics and enabling new prudential data collections.	FSIS is a computer application that will integrate the Bank's statistical data and enhance the processing and storage of, and access to, the data. The project is entering its second phase, in which existing surveys will be migrated into FSIS, and new surveys will be established for non-bank deposit takers (NBDTs) and the insurance sector and for other external data.

Reserve Bank Strategic Priorities for 2009-10

	Department	Priority	Explanation
5	Prudential Supervision	Introduce a prudential regime for the insurance sector, and implement new regulatory arrangements for NBDTs.	<p>In 2008, legislation was enacted to make the Bank the prudential regulator of NBDTs. In 2009–10, the Bank will progressively develop and implement the new regulatory framework for NBDTs. Legislation for the prudential regulation of insurers is being drafted under the Insurance (Prudential Supervision) Bill, expected to be enacted during 2010 and covering life, general and health insurers.</p> <p>The Bank's objective is to regulate NBDTs and the insurance sector so as to promote the maintenance of a sound and efficient financial system, and to avoid damage to the financial system that might result from the failure of an NBDT or an insurer.</p>
6	Bank-wide	Improve business continuity and disaster-recovery capability through the establishment of a business support office in Auckland.	<p>The Bank has been ensuring it has systems in place to enable it to continue functioning in the event of a range of crises. It will establish a small office in Auckland to provide business continuity in payments and market functions in the event of a physical disaster in Wellington.</p>
7	Bank-wide	Engage and develop staff to meet the challenges of a volatile financial and economic environment.	<p>In challenging economic times, staff are affected both professionally and personally. The challenge can motivate staff because of the nature of the work, but they will be under pressure nevertheless. We must ensure that the right staff are doing the right work, that they remain focused and motivated, and that they have the opportunity to continue to develop their skills and knowledge.</p>

Planning and reporting framework



Our SOI, which traverses three years, is set in the context of our longer-term planning and funding. The Bank is funded through a five-year funding agreement between the Governor and the Minister of Finance. The funding agreement specifies how much of the Bank's income can be retained by the Bank to meet its operating costs.

The current Funding Agreement, signed in April 2005 and subsequently ratified by Parliament, covers the five years to 30 June 2010. This SOI covers the last year of the current Funding Agreement and the first two years of the next scheduled funding agreement, which has yet to be negotiated.

While key performance indicators cover the three-year term of the SOI, priorities, initiatives, strategies and budget are defined for the first year only, i.e., 2009–10.

Governance and structure

Board of Directors

The Reserve Bank has a Board of Directors whose primary function is to review the performance of the Governor and the Bank. The Board holds regular meetings at which it receives extensive briefings on the Bank's activities, decisions and policies. At these meetings, the Board also provides advice to the Governor on a range of Bank functions.

The Board, through an Audit Committee, reviews the Bank's financial statements, risk management and internal audit activity. Each year, the Board writes an assessment of the Bank's and the Governor's performance, which is provided as advice to the Minister of Finance and made public later in the Bank's *Annual Report*.

When required, the Board makes recommendations to the Minister on the appointment or reappointment of the Governor. The Minister can only appoint a Governor recommended by the Board. The Board can recommend to the Minister that the Governor be dismissed if the Board believes that the Governor's performance has been 'inadequate' in various respects. The Board appoints the Deputy Governor on the Governor's recommendation.

The Board typically meets formally nine times a year, with provision for additional meetings. The current Board members are Dr Arthur Grimes (Chair); Mrs Alison Paterson, QSO (Deputy Chair, and Chair of the Board's Audit Committee); Dr Chris Eichbaum; Mr Hugh Fletcher; Mr John Goulter, DCNZM, JP; Ms Sue Sheldon CNZM; and Dr Alan Bollard (Governor). From 1 July 2009, Mr Keith Taylor replaces Mr Paul Baines, whose second term expired on 30 June. Board members are appointed for five-year terms and are eligible for reappointment.

Management structure

Under the Act, the Governor – who is also the Bank's Chief Executive – is accountable for the Bank's actions. In monetary policy, and in many other matters, decision-making authority resides with the Governor alone, although in practice he receives widespread advice, and takes monetary policy decisions on the formal advice of the Official Cash Rate Advisory Group.¹ The Governor is appointed for a five-year term and can also be reappointed for further terms of up to five years. The Act sets specific procedures for the appointment, reappointment and dismissal of the Governor.

The Reserve Bank's senior management team is made up of the Governor, a Deputy Governor, two Assistant Governors and the heads of the Bank's various departments, as outlined on page 9. The positions of Governor and Deputy Governor are required and their roles defined by statute. Currently, the Deputy Governor is also the Head of Financial Stability. The two current Assistant Governors are the Head of Operations and the Head of Economics.

The Governor receives advice from a number of internal committees within the Bank.

¹ This group includes key economic advisers within the Bank and two external monetary policy advisers.

Reserve Bank organisational structure

Governors	Department/Heads	External Functions	Internal services	
Governor <i>Alan Bollard</i>	Assistant Governor/ Head of Economics <i>John McDermott</i>	Economics	Monetary policy formulation	
	Deputy Governor/ Head of Financial Stability <i>Grant Spencer</i>	Financial Markets <i>Simon Tyler</i>	Market operations Foreign reserves management	
		Prudential Supervision <i>Toby Fiennes</i>	Financial system surveillance and policy	
		Currency and Building services <i>Alan Boaden</i>	Currency operations	Property management Security
	Financial services <i>Mike Wolyncewicz</i>	Settlement services Registry and depository services	Accounting services Treasury services	
	Knowledge services <i>Tanya Harris</i>		Library services Technology services Project management Web publishing	
	Assistant Governor/ Head of Operations <i>Don Abel</i>	Human Resources <i>Lindsay Jenkin</i>		Human resources strategy and services
		Communications/ Board secretariat <i>Mike Hannah</i>		Communications strategy and services Reputation management Board secretariat
	Risk assessment and assurance <i>Steve Anderson</i>		Risk assessment and assurance Audit services Legal services	

Functions and operations

Monetary policy formulation

Outcome

Stability in the general level of prices.

Objective statement

To achieve and maintain stability in the general level of prices. The current Policy Targets Agreement (PTA)² requires that the Bank “keep future CPI inflation outcomes between 1 and 3 percent on average over the medium term”. It also requires that: “In pursuing its price stability objective, the Bank shall ... seek to avoid unnecessary instability in output, interest rates and the exchange rate.”

Environment

- The recent upheavals in the global financial system and economy have increased uncertainty about the outlook for inflation.
- Official interest rates around the world are at their lowest levels in decades. With their official interest rates approaching or having hit zero, some central banks have had to resort to using other approaches to provide monetary stimulus.
- The New Zealand economy is under pressure from the international crisis and weak domestic spending. The ongoing risks to the inflation outlook are mainly to the downside.
- Reductions in the Official Cash Rate (OCR) are flowing through to borrowers but the impact on activity and inflation is clouded by falling house prices and funding difficulties in the banking sector.
- The Bank is expected to be independent and accountable for its actions, and to make sound, credible and transparent judgements.

Scope of operations

- Setting an OCR eight times a year, or as is required, with the aim of keeping inflation within the target band.
- Publishing the Bank’s quarterly *Monetary Policy Statements (MPSs)* at the same time as four of the OCR decisions. The *MPSs* set out the Bank’s views on the economy and inflationary pressures, and the basis for the OCR decision.
- Announcing the other four OCR decisions approximately halfway between each *MPS*.
- Intervening in the foreign exchange market, where appropriate and feasible, to influence the level of the exchange rate, consistent with the objectives of the PTA.

Issues

- The contraction in global credit supply and heightening of risks associated with New Zealand’s reliance on external funding.
- The reaction of New Zealand households and firms to high levels of debt and falling housing and other asset prices.

² The PTA specifies the monetary policy target agreed by the Governor and the Minister of Finance.

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- Considerable uncertainty about the depth and duration of the current global recession, due to impaired and volatile global financial markets and the synchronised nature of the global downturn.
 - The central role of housing, credit and the financial sector in the current downturn, reinforcing the need for ongoing judgement to be applied to our economic models.
 - Access to timely and comprehensive data on bank funding and credit market conditions for monitoring the monetary policy transmission channel.
 - New evidence about the influence of asset and house price cycles on the business cycle.
 - International re-examination of macroeconomic stabilisation policy and of how inflation-targeting monetary policy can be augmented by appropriate modifications to prudential policy and fiscal policy.
 - Ongoing developments in economic modeling techniques, new data compilation methods and increasing computing power, requiring continued investment by the Bank in these areas to maintain its standards of quality against its peers.

Initiatives and strategies

- Increase monitoring and assessment of global economic and financial markets developments.
- Increase monitoring of domestic credit conditions and their impact on the domestic economy.
- Monitor and evaluate international thinking about how monetary and financial stability policy should interact.
- Enhance the use of tools for evaluating uncertainty about the economic outlook and the impact of monetary policy.
- Regularly consult with government agencies on current economic conditions and government responses to these.
- Improve the quality, accessibility, relevance and reliability of Reserve Bank statistics, including by setting up the core framework for the FSIS, which will integrate Reserve Bank statistics.
- Research the ways in which flexible inflation targeting may be augmented to take account of the effects of housing and asset-price cycles, leverage and prudential and fiscal policy on activity and inflation.
- Ensure that best-practice modeling and analytical methods and an appropriately wide range of data are used in generating monetary policy advice, including using the newly developed forecasting model of the New Zealand economy as the basis for producing regular forecasts.
- Continue to deepen the Bank's understanding of the inflation process in New Zealand, including price, wage and expectations formation, the impact of commodity markets, and the impact of sectoral and national debt levels.

Key performance indicators

- Reserve Bank forecasts of CPI inflation should be comfortably within the target range in the second half of our forecast horizon.
- Measures of underlying inflation should generally lie within the target range.
- Unnecessary instability in output, interest rates and the exchange rate should be avoided.
- The *MPS* provides a basis for assessment of the Bank's performance in pursuing its price stability target as defined in the PTA.

Domestic market operations

Foreign reserves management

Outcomes

- Sufficient liquidity in the domestic banking system to meet its ongoing needs.
- Confidence in the efficient functioning of New Zealand financial markets.
- Short-term interest rates consistent with the Bank's monetary policy stance.
- Foreign reserves readily available to assist in foreign exchange intervention and crisis management where appropriate.
- Any foreign exchange market intervention conducted efficiently.

Objective statement

To support the effective implementation of monetary policy; to assist in the efficient functioning of the New Zealand financial system; to manage official foreign reserves; to provide effective support and execution for the Bank's foreign exchange market intervention policy; to manage the Crown's financial liquidity; and to maintain an effective crisis intervention capability.

Environment

- Changes to the financing and management of New Zealand's foreign currency reserves and our liquidity management regime have increased the focus of the Bank's market operations towards foreign exchange and swaps markets.
- Increased turbulence in credit markets has made investment of foreign reserves more challenging as liquidity and credit spreads have been changing rapidly.
- The ongoing credit crisis is making it more expensive for banks to maintain adequate levels of liquidity and to raise term funds.

Scope of operations

- Providing advice on financial market developments and issues for the formulation of monetary policy.
- Ensuring the effective implementation of monetary policy through the level of the OCR.
- Managing official foreign reserves for use in times of financial distress or when foreign exchange intervention is needed for monetary policy purposes.
- Managing liquidity in the banking system.
- Providing and managing the Crown Settlement Account.
- Acting as lender of last resort to the financial system if necessary, as well as assisting in the resolution of any financial market or banking crisis.

Issues

- Maintaining and continuing to develop the Bank's foreign exchange intervention capability to enhance the effectiveness of monetary policy implementation and the maintenance of orderly foreign exchange markets.
- Managing the liquidity management regime so that the payments system continues to operate, the banking system has adequate liquidity, and risks (both to the Bank and the market) are balanced appropriately.
- Maintaining facilities that allow financial market participants to manage their funding and liquidity needs in the face of ongoing strains in credit markets.
- Promoting the development of capital markets in areas where the Bank has powers and responsibilities (i.e., in money, bond and foreign exchange markets).

Initiatives and strategies

- Assist in the formulation and implementation of bank liquidity policies and ensure that they are operational.
- Provide backup liquidity facilities that allow banks to effectively manage their own and corporates' funding needs in the face of ongoing strain in credit markets.

Key performance indicators

- Short-term wholesale interest rates should be relatively stable and maintained at levels consistent with the OCR.
- No evidence of payment failures due to shortage of cash in the banking system.
- Domestic market operations are expected over the medium term to generate a positive return for the domestic markets function, as an indicator that operations are running effectively.
- Foreign reserves are held at the level agreed with the Minister.
- Foreign reserves are held in a liquid and secure form, suitable for foreign exchange market intervention.
- The net return from foreign reserves management meets or exceeds the agreed benchmark.

Financial system surveillance and policy

Outcomes

- A sound and efficient financial system in New Zealand.
- International and local confidence in New Zealand's financial system.

Objective statement

To register and supervise banks so as to maintain a sound and efficient financial system, and to limit damage to the financial system that could result from a bank failure. To regulate non-bank deposit takers, and, assuming legislation is passed, to regulate and supervise the insurance sector. This will be done in a manner that delivers a cost-effective balance between regulatory requirements and self- and market-discipline.

Environment

- Global recession and credit constraints increase risks to the balance sheets of banks, NBDTs and insurance providers.
- Policies need to be in place to manage the scheduled expiry of the Government's guarantees on retail deposits in October 2010.
- The Bank became the prudential regulator of NBDTs through legislation enacted in September 2008. Legislation making the Reserve Bank the supervisor of insurers is expected to be enacted in 2010.
- The new regulatory regime for NBDTs will require deposit takers to comply with a new set of prudential requirements including capital, liquidity, governance, risk management, credit ratings and restrictions on related-party exposures.
- The Bank continues to bed down the Basel II capital adequacy framework with a continued focus on sectors that form an important part of banks' balance sheets.
- Other legislative changes include measures to counter money laundering and terrorist financing, which will result in the Bank becoming the anti-money laundering (AML) supervisor for registered banks, NBDTs and life insurers; and amendments to Part 5C of the Reserve Bank Act, which will broaden its scope from payment systems to include settlement systems generally. Both are expected to be enacted in late 2009.

Scope of operations

- Setting specific criteria for bank registration.
- Subjecting banks to a specific monitoring regime.
- Publishing regular *Financial Stability Reports (FSRs)* assessing the soundness and efficiency of the New Zealand financial system.
- Strengthening the Bank's capacity to respond in times of financial crisis.
- Monitoring the Crown's exposures in relation to the Deposit Guarantee Scheme (DGS) on behalf of the Treasury.
- Overseeing and setting specific criteria for designation of payment systems.
- Progressively developing and implementing the prudential regulatory framework for NBDTs and insurers, throughout 2009 and 2010.

Issues

- Ensuring that banks maintain adequate capital, through close monitoring of asset quality and prompt supervisory responses.
- Implementing a regulatory regime for the NBDT sector, through appropriate consultation with the sector and trustees.
- Ensuring the Crown's exposures under the DGS are actively monitored and that the Treasury is promptly advised of any potential issues.
- Implementing the Insurance (Prudential Supervision) Bill in line with Cabinet decisions and the legislative timetable.
- Implementing the prudential liquidity regime for banks.
- International re-examination of macroeconomic stabilisation policy and of how appropriate modifications to prudential policy may support and interact with monetary policy.

Initiatives and strategies

- Enhance the Bank's monitoring of risks to bank balance sheets and profitability.
- Develop, with the Treasury as required, the high-level features of durable bank and NBDT regulatory arrangements for the post-deposit guarantee environment.
- Implement new regulatory arrangements for the NBDT sector.
- Preserve and enhance the features of Basel II implementation: through-the-cycle and conservative calibration.
- Refine our crisis preparedness, focusing on practical solutions and developing trans-Tasman arrangements.
- Develop and implement the supervisory framework for the insurance sector.
- Monitor and evaluate international thinking about how monetary and financial stability policy should interact.

Key performance indicators

- Banks comply with Conditions of Registration and maintain the required minimum capital ratios and liquidity requirements.
- NBDT regulations in place and NBDTs comply with the regulatory regime in line with transition requirements.
- The Treasury is notified promptly of any issues with any entities in the DGS.
- The Bank has in place the people, procedures and systems to implement new prudential supervision law for the insurance sector when it comes into force.
- The Bank has publicised the core features of the regulatory arrangements for banks and NBDTs on the expiry of the DGS.
- Measures included in the FSR provide a basis for assessment of the New Zealand financial system's stability and the performance of the surveillance function.

Currency operations

Outcomes

Legal tender that meets the currency needs of the public.

Objective statement

To meet the currency needs of the public by ensuring, as the sole issuer of currency, the supply and integrity of bank notes and coins.

Environment

- The demand for notes and coins continues to grow each year. Cash remains an important means of making payments in New Zealand.
- The Bank's cash operations have changed considerably over the past decade and a new management information system is now required for a more efficient and secure management of cash processes.
- The rate of counterfeiting in New Zealand is very low by international standards. However, the current bank note series is 10 years old and is due for review. Surveys of notes in circulation have shown that the quality of most denominations is very good, but that many \$5 notes are showing considerable wear.

Scope of operations

- Procuring, storing, processing and issuing bank notes and coins to the banking system.
- Maintaining the quality, and verifying the authenticity of, currency in circulation.
- Issuing legal tender collectors' currency through an outsourcing arrangement.

Issues

- The currency operations inventory management system needs replacing to provide the information required for more effective management of cash handling operations.
- The current polymer bank note series is now 10 years old and the security features are due for review.
- The quality of \$5 notes in circulation is falling below the desired quality standard.

Initiatives and strategies

- Develop and implement a new information system for the management of currency operations.
- Investigate possible enhanced security features for bank notes.
- Develop and implement a plan to improve the quality of \$5 notes in circulation.

Key performance indicators

- All orders for notes and coins from banks that meet the Reserve Bank's guidelines are supplied within agreed times.
- Notes and coins in general circulation are of a good quality as indicated by biennial surveys of the condition of currency in circulation.
- The number of counterfeit notes in circulation should be fewer than 10 per million notes in circulation.

Depository and settlement services

Outcomes

An efficient, reliable and secure payments system that supports the smooth functioning of the economy.

Objective statement

To ensure that payments system infrastructure services are provided efficiently and meet international standards.

Environment

- Competition for depository services in New Zealand is emerging.
- The upgraded Exchange Settlement Account System (ESAS)/Austraclear system is allowing the Bank to deliver a stream of functional enhancements to users.
- Standards for system performance and resilience are being lifted.

Scope of operations

Operating the ESAS and Austraclear systems, including the infrastructure required for settlement of foreign exchange transactions through Continuous Linked Settlement (CLS) Bank.

Issues

- Enhancing ESAS and Austraclear system functionality.
- Emergence of new payment and settlement systems by other providers.
- Improving business continuity planning and disaster recovery capabilities, and responding to higher international operating standards.
- Meeting changing industry requirements for settlement times.

Initiatives and strategies

- Continue to enhance Austraclear and ESAS as agreed with industry representatives.
- Establish interfaces that will facilitate inter-operability between ESAS/Austraclear and other providers' payment and settlement systems, to increase efficiency and meet user needs.
- Improve business continuity planning and disaster recovery capability by arranging for Auckland office business support for payment systems.

Key performance indicators

- Availability of ESAS/Austraclear during core hours is at least 99.95 percent.
- Customer satisfaction with operations and with system development is demonstrated through an annual customer survey.
- All risks are well managed.
- International standards for payment and settlement systems (CPSS and IOSCO³) are complied with.

³ Committee on Payment and Settlement Systems; and the International Organisation of Securities Commissions.

Organisational health and capabilities

Human resources

Objective statement

To provide strategic human resource advice and support services.

Environment

The current volatile financial and economic conditions create a challenging environment for Bank staff. Staff need to be supported and given tools and resources to perform at their best under increased pressure. The Bank's priorities reflect the need to keep staff engaged and focused as well as continuing to develop personally. The Bank will continue to provide leadership development opportunities. The Bank will be recruiting additional staff to carry out its expanded prudential regulation functions.

Scope of operations

- Organising specific bank-wide training and development programmes, key-person risk planning, and secondment and study arrangements.
- Assisting departments with recruitment, contract negotiation, employment relations, legislative advice and terminations.
- Facilitating the annual remuneration review and performance management programmes.

Issues

- In challenging economic times, staff are affected both professionally and personally. The challenge can be motivating because of the nature of the work, but staff will be under pressure nevertheless.
- Maintaining staff focus and morale.
- Ensuring high-quality staff for the Bank through training and recruitment.
- Identifying areas where skills can be enhanced and developed to meet current and future business requirements.
- Maintaining staff wellbeing and Bank operations in the event of an influenza pandemic.

Initiatives and strategies

- Engage and develop staff to meet the challenges of a volatile financial and economic environment.
- Support management in further developing their values-based leadership competencies.
- Continue an annual review of key-person risk within the Bank and mitigation strategies.
- Enrich the Bank's staff appraisal and personal development programme.
- Facilitate excellent management processes and decision making throughout the Bank; provide a supportive environment for staff to perform at their best; and continue to develop the skills and knowledge required.
- Ensure the Bank values of integrity, innovation and inclusion are central to all staff initiatives.
- The biennial staff satisfaction surveys will be completed in 2009 and 2011.
- Ensure staff are adequately informed to cope with an influenza pandemic, and that there is sufficient back-up to ensure Bank operations are maintained.

Knowledge services

Objective statement

To provide knowledge management and information technology services, direction and support.

Environment

The technology platforms must provide a high level of uninterrupted service, functionality and security, while the Knowledge Centre must provide easy access to a broad range of information sources.

Scope of operations

- Developing and maintaining the Bank's core technology infrastructure.
- Providing business analysis and applications development.
- Delivering help desk and web support.
- Maintaining library, information and records management.
- Providing project and programme management services.
- Providing payments systems support.

Issues

Managing capital expenditure to:

- maintain and upgrade information technology, information management and applications;
- provide efficient payments systems services;
- enhance data management and reporting systems; and
- improve business continuity.

Initiatives and strategies

- FSIS implementation: The core system will be built by July 2009. The second phase will ensure key business benefits are realised by completing the migration of remaining surveys, and developing new surveys for NBDTs and the insurance sector and for other external data.
- Develop systems to make our management of the information technology environment more efficient.
- Review and where appropriate upgrade older internally supported computer applications.
- Extend the Bank's knowledge management strategy by automating frequently used processes; implementing tools that allow easy sharing of information and documents across teams; and continuing digital capture of archive records and physical documents.
- Make the Bank's information, records and data management more flexible and user-friendly.
- Continue to enhance the Bank's web services.
- Continue to enhance the Bank's business continuity infrastructure, by establishing of an Auckland business support centre for critical functions and other backup computing arrangements.

Internal financial services

Objective statement

To provide support services for the Bank's key financial operations, including financial reporting and management reporting; compliance with corporate governance and accountability responsibilities; settlement operations; and treasury accounting and compliance reporting.

Environment

The Bank's financial systems must be of a high standard to enable management of a very large and complex balance sheet.

Scope of operations

- Settling transactions and treasury accounting and compliance reporting in support of the Bank's domestic market operations and foreign reserves functions.
- Preparing financial statements, and carrying out monthly management and Board reporting.
- Facilitating the Bank's strategic planning and annual budgeting processes.
- Delivering financial support services and balance sheet management advice.
- Liaising with external auditors.

Issues

- Ensuring systems are constantly developed to meet changes to the Bank's financial operations and environment. The Bank's financial management system is due to be replaced.
- Maximising efficiency through process improvement and systems changes.
- Development of the new Funding Agreement for the period 2010–11 to 2014–15.

Initiatives and strategies

- Continue to enhance workflows, reports, and processes for financial operations and securities transactions.
- Replace the Bank's own financial management information system before 2011.
- Preparation of the Bank's Five-Year Strategic Plan and Funding Agreement for the period 2010–11 to 2014–15.

Communications

Objective statement

To provide strategic advice and management for the Bank's external and internal communications and for the maintenance of its reputation and credibility.

Environment

- The Bank is adopting a highly visible role in responding to the current uncertain and volatile financial and economic environment.
- Regulations covering prudential supervision of NBDTs and insurance supervision legislation are expected to be introduced. Credit ratings will require a specific focus.
- A business support office is being established in Auckland to enhance business continuity capability.

Scope of operations

- Supporting the Bank's functions with communication and relationship strategies for key audiences.
- Editing and publishing Bank statements and documents.
- Sponsoring education initiatives.
- Coordinating responses to Official Information Act requests, ministerial correspondence, parliamentary questions and public inquiries.
- Supporting the Board by providing secretariat and administrative services.

Issues

- Ensuring the Bank's messages are informed, well constructed, timely and delivered to target audiences through the most appropriate channels.
- Maintaining preparedness in a volatile environment by coordinating with New Zealand and Australian agencies.
- Improving New Zealanders' financial literacy.
- Further enhancing internal communications.

Initiatives and strategies

- Ensure the Bank's key messages are delivered and understood.
- Communicate the Bank's expanded role in the new regulatory regimes for non-bank financial institutions.
- Provide the Bank with timely information, and with strategies to address credibility risks and opportunities.
- Provide communications services for crises, including simulation exercises and the Auckland business support centre.
- Enhance financial literacy, by promoting the Bank's role as prudential regulator and support for inter-agency financial literacy programmes.

Risk assessment and assurance

Objective statement

To assist in the maintenance of effective and efficient risk management; to audit operations and internal control systems; and to provide legal advice.

Environment

The Bank's financial exposure from changes in its balance sheet structure and regulatory exposure from changes in its regulatory responsibilities increase overall risks faced by the Bank.

Scope of operations

- Assisting management to identify and analyse sources of risk.
- Assisting management to design risk management systems and processes.
- Monitoring risk management implementation and providing risk management advice to Governors and to the Board through the Board's Audit Committee.
- Providing ongoing internal audit review and evaluation of the Bank's operations and control systems.
- Providing legal advice and services.

Issues

Ensuring risks are being managed in a proactive, coordinated, prioritised and cost-effective manner.

Initiatives and strategies

- Monitor the Bank's approach to risk management, utilising the enterprise-wide risk map.
- Continue a comprehensive internal audit programme to provide assurance on the Bank's control environment.
- Continue to provide quality legal advice.

Property management Security

Objective statement

To provide appropriate accommodation for the Bank to ensure that all functions, including cash operations, can be conducted unimpeded in a secure environment.

Environment

- The expansion of regulatory functions requires the Bank to take over additional floor space at 2 The Terrace, Wellington.
- An additional site is to be established in Auckland by July 2010 to ensure business continuity.
- For efficiency and environmental reasons, the Bank needs to maintain and extend energy-saving and recycling programmes.

Scope of operations

- Maintaining the Bank-owned building at 2 The Terrace, and managing leases on eight of the 14 floors.
- Maintaining a secure working environment and the safe custody of currency reserves.
- Maintaining business continuity sites in Wellington and Auckland.

Issues

- Additional accommodation is required for new staff in the Prudential Supervision Department.
- The Bank will need to maintain an Auckland business continuity site.
- The Bank's standby power generator is due for replacement.

Initiatives and strategies

- Refurbish Bank accommodation as required to meet the needs of additional staff.
- Assist in locating and setting up a suitable Auckland office.
- Purchase and install a new power generator.
- Implement cost-effective measures to further enhance energy efficiency.

Financial management

Financial structure

Balance sheet overview and funding of the Bank's operations

The Reserve Bank is both a statutory agency and a financial institution. It receives no direct funding through the central government budgetary process. Instead, the Bank's main source of income is the return on the substantial investments the Bank holds, which are funded by the issue of currency and by the Government's equity contribution to the Reserve Bank. Currency in circulation is a liability on which no interest expense is incurred. The funds received when currency is issued are invested and earn interest income which is known as seigniorage.

The nature and extent of the Bank's principal activities affecting its balance sheet are described in the *Annual Report 2007–2008* (pages 67–69). Foreign reserves management, New Zealand dollar liquidity management and currency operations materially affect the size and structure of the Bank's balance sheet.

Under the Act, the Minister and the Governor are required to enter into a funding agreement to specify the amount of the Bank's income that may be used to meet expenses in each financial year. The funding agreement comes into force only after it is ratified by Parliament. The Act provides for each funding agreement to apply for a period of five consecutive financial years. This contrasts with the arrangements for government departments, which are funded on an annual basis. The Bank's funding arrangements are designed to strike an appropriate balance between providing a high degree of operational independence, and providing strong incentives for effective management of operating expenditure, while ensuring accountability for use of resources. Capital expenditure is funded by the Bank, with depreciation of fixed assets included in annual operating expenses. If operating expenses (net of specified revenue) in any year exceed the amount provided in the funding agreement, the Bank is required to fund that excess from equity.

The current funding agreement, ratified by Parliament on 23 June 2005, covers the five years ending 30 June 2010. Funding in this agreement was projected to rise from \$39 million in the first year (2005–06) to \$43 million in 2009–10. This was an increase in spending compared with the previous five-year period and reflects various factors, including the need to:

- invest in the replacement and upgrading of our treasury and document management systems, our economic forecasting and data systems, and our core financial reporting system;
- strengthen our supervisory capability; and
- ensure that robust business continuity arrangements remain in place.

The funding agreement was amended in April 2008 by increasing the approved level of net operating expense for 2008–09 from \$41.0 million to \$43.3 million and that for 2009–10 from \$43.0 million to \$46.9 million. These changes were required to fund increased policy advice responsibilities and activities associated with greater oversight of non-bank financial institutions.

Annual distributions paid by the Bank

The Reserve Bank of New Zealand Amendment Act 2008 changed the framework governing payment by the Bank of an annual dividend to the Crown. It changed the regime from a formula-based approach (i.e., the Act previously contained the formula, known as 'notional surplus income', for calculating the annual dividend the Bank recommended to the Minister each year) to a principles-based approach.

The Reserve Bank of New Zealand Amendment Act 2008 removed the concept of 'notional surplus income' from the Act and instead requires the Bank to publish in its SOI a statement of dividend principles it must apply in determining its dividend recommendation each year. The Bank's statement of dividend principles is shown below.

Statement of dividend principles

The Bank should maintain sufficient equity for the financial risks of performing its functions. Equity in excess of that required to cover those risks will be distributed to the Crown.

In general, unrealised gains should be retained by the Bank until they are realised in New Zealand dollars. However, the Bank may recommend the distribution of unrealised gains where the Bank believes that the probability of the gain being realised is high.

Each year the Bank recommends to the Minister of Finance of the amount to be paid as a dividend. The Minister decides how much should be paid having regard for the recommendation of the Bank, the views of the Board of the Bank and any other relevant matters.

Drivers of the Bank's financial performance and changes in financial structure

The principal drivers of the Bank's financial performance are:

- *The size of the Bank's open foreign exchange position and related changes in foreign exchange rates and interest rates.*

During 2007–08, the Bank changed its exposure to foreign exchange risk to better meet its statutory responsibilities, after concluding that it would be appropriate to hold a portion of the Bank's foreign currency reserves on an unhedged basis. At 30 April 2009, the Bank had an open foreign currency position of \$4.2 billion.

- The value of currency in circulation.

Currency in circulation has grown steadily from \$2.9 billion in 2004 to \$4.0 billion as at 30 April 2009.

- *Interest rates earned on the Bank's investment in government securities and other securities.*

The Bank adopted New Zealand equivalents to International Financial Reporting Standards from 1 July 2007. From this date, the Bank's holdings of New Zealand government securities are valued at market value, with unrealised gains and losses on those holdings booked to equity.

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- *The size and performance of the Bank's foreign reserve management and market operations functions.*

The Bank has increased its holdings of foreign reserves that can be liquidated at short notice to support its functions, including monetary policy objectives and the maintenance of orderly markets. During 2006–07, the Bank changed the way it manages its New Zealand dollar liquidity management operations by significantly increasing the level of settlement cash held by financial institutions.⁴ This change added about \$7 billion to assets and liabilities reported on the Bank's and Crown's balance sheets.⁵ The Bank introduced a further range of measures during 2008–09 to support New Zealand dollar liquidity in response to global market disruptions.
 - *Operating expenditure incurred by the Bank.*

The level of operating expenditure has increased, reflecting significant capital expenditure in renewing or replacing existing systems; improvement of business continuity capabilities; and additional staff for our expanded regulatory responsibilities.
 - *The dividend paid by the Bank and the level of equity available for investment.*

As noted, for 2008–09 a new statutory regime applies for the determination of the Bank's dividend.

Open foreign exchange position

Since 2007, the Bank has held a portion of its foreign reserves on an unhedged basis as opposed to the historical approach of holding foreign reserves fully hedged. This has been achieved by funding part of the Bank's foreign reserves using New Zealand dollar liabilities rather than foreign currency-denominated loans. As a benchmark, the Bank will hold SDR 1.0 billion unhedged foreign reserves with the ability to hold more or less than the benchmark over the exchange rate cycle. At 30 June 2008, the Bank held a net open foreign currency position of SDR 2.1 billion (NZD 4.4 billion), higher than the benchmark amount. During the 2008–09 financial year, the Bank has gradually reduced its holdings of unhedged foreign currency reserves. At 30 April 2009, the Bank had an open foreign currency position of SDR 1.6 billion (NZD 4.2 billion).

Impact of turmoil in global financial markets

The recent turmoil in global financial markets has resulted in greater volatility in interest rates and exchange rates and other financial prices, and has adversely affected liquidity in financial markets. The Bank introduced a further range of measures over the past year to help alleviate New Zealand dollar liquidity pressures. The range of acceptable securities for domestic market operations has been progressively expanded and now includes high credit quality residential mortgage-backed securities and asset-backed securities.

The Bank has a diversified portfolio of high credit quality foreign currency assets that can be converted to cash quickly.

⁴ See RBNZ *Annual Report 2006–2007*, page 25.

⁵ The rationale for this change is explained in the document *Reform of the Reserve Bank of New Zealand's Liquidity Management Operations*, June 2006, which is available on the Bank's website www.rbnz.govt.nz

The Bank's balance sheet has changed significantly since the last *Annual Report* was prepared. As at 30 April, total assets were \$29 billion, up from \$25 billion at 30 June 2008. The main drivers have been:

- *\$600 million capital injection.*

On 2 July 2008, the Bank received a capital injection of \$600 million from the government to provide sufficient cover for potential mark-to-market losses on the Bank's government securities portfolio.

- *New liquidity management facilities.*

The Bank introduced new liquidity facilities during the year aimed at supporting New Zealand dollar liquidity in the event of global market disruptions. The range of acceptable securities for domestic market operations has been progressively expanded and now includes residential mortgage-backed securities and asset-backed securities. In addition, the Bank has recommenced issuing Reserve Bank bills as a tool for managing the level of New Zealand dollar liquidity in the banking system. These changes have added about \$7 billion to assets and liabilities reported on the Bank's balance sheet at 30 April 2009.

- *Changes in foreign exchange rates and interest rates.*

Exchange rates and interest rates have changed significantly since 30 June 2008. The Bank has also closed out some of its open foreign exchange position by selling foreign currency and buying New Zealand dollars. This has resulted in significant changes to the values of foreign currency assets and liabilities and holdings of New Zealand government securities. As foreshadowed in the *Annual Report 2007–2008*, the open foreign exchange position in particular will cause increased volatility in the Bank's financial performance and financial position.

Principal financial risk management considerations

As a financial institution with approximately \$29 billion in assets, the Bank faces a wide range of financial risks. These arise mainly because of the Bank's operations in the domestic financial system and because of the Bank's holdings of foreign exchange reserves. The risks include:

- credit risks and market risks associated with day-to-day dealings with financial institutions in the process of managing liquidity in the financial system;
- risks associated with the Bank's holdings of foreign currency reserves, including credit risk, liquidity risk, interest rate risk, and exchange rate risk; and
- operational risks in the transactions and processing areas of the Bank.

More detailed information on the Bank's approach to managing these risks is outlined on pages 78–89 in the *Annual Report 2007–2008*.

Financial projections

The following table outlines the Reserve Bank's budgeted income and expenditure for 2009–10. The budgeted income and expenditure have been prepared using the accounting policies used in the preparation of the Bank's financial statements for the year ended 30 June 2008.

The key assumptions underlying the budget for the year ended 30 June 2010 are that:

- the Bank's current functions will continue, with the Bank undertaking preparatory work for the prudential supervision of non-bank financial institutions;
- the Bank will maintain an open foreign currency position during the year equal to \$4.2 billion, being the position at 30 April 2009;
- interest and exchange rates will be those prevailing as at 30 April 2009;
- there will be no change in the credit worthiness of the Bank's counterparties; and
- there will be no material changes to the Bank's liquidity management operations.

The following table sets out projected income and expenditure for the Bank for the year ended 30 June 2010.⁶

⁶ The Bank's accounting policies are disclosed in its *Annual Report 2007–2008* on pages 61–67. An explanation of transition to New Zealand equivalents to International Financial Reporting Standards is provided on pages 104–105.

Projected financial performance 2009 – 2010

<i>For the year ended 30 June</i>	Budget	Budget
	2009/10 \$m	2008/09 \$m
Operating income:		
Net investment income	174.7	302.9
Other income	7.9	8.2
Total operating income	182.6	311.1
Operating expenses:		
Personnel	27.2	24.6
New currency issued	5.3	5.7
Asset management	8.3	7.7
Administration	1.4	1.6
Other	12.9	12.5
Total operating expenses	55.1	52.1
Operating surplus	127.5	259.0
Net expenditure under the Funding Agreement	47.3	43.9
Funding Agreement Under-Expenditure (Over-Expenditure)	(0.4)	(0.6)
Funding Agreement	46.9	43.3

The budget is based on an assumption that no changes to interest rates or foreign exchange rates will occur during the financial year and the Bank retains for the full year its open foreign exchange position that it held at 30 April 2009.

The significant reduction in budgeted investment income reflects the impact of much lower interest rates compared with those prevailing 12 months ago.

It is important to note that the Bank's assets and liabilities are sensitive to changes in interest rates and exchange rates, and that actual financial results could differ materially from those budgeted.

At 30 April 2009, a 10 percent increase in the value of the New Zealand dollar would reduce the Bank's comprehensive income⁷ by \$420 million, and conversely a 10 percent decrease in the value of the New Zealand dollar would add \$420 million to comprehensive income. A 1 percent across-the-board increase in interest rates would reduce comprehensive income by about \$160 million, and a 1 percent across-the-board reduction in interest rates would increase comprehensive income by about \$170 million.

The increase in operating expenditure from \$52.1 million to \$55.1 million primarily reflects the expansion of the Bank's regulatory responsibilities for non-bank financial institutions, the costs of establishing a new office in Auckland, and depreciation of new systems.

One feature of the projected income and expenditure is that, as anticipated, the Bank forecasts that net operating expenses will be \$47.3 million against \$46.9 million provided for in the variation to the Funding Agreement.

The additional \$0.4 million of expenditure in 2009–10 will be drawn from underspending in the previous four years of the Funding Agreement. At 30 June 2009, the cumulative underspending of the current Funding Agreement is forecast to be \$11.2 million.

Net expenditure by function

For the year ended 30 June	Net Expenditure*	
	Budget	Estimated Actual
	2009/10	2008/09
	\$000	\$000
Functions:		
Monetary Policy Formulation	10,144	9,450
Market Operations	7,627	5,448
Financial System Surveillance/Policy	12,527	11,628
Currency Operations	9,050	9,188
Foreign Reserves Management	7,062	7,571
Settlement Services	593	405
Registry and Depository Services	(140)	(313)
Other Outputs	417	478
Net expenditure	47,280	43,855

* Net Expenditure comprises operating expenses less income earned from certain Bank operations as specified in the Funding Agreement.

⁷ Comprehensive income includes earnings booked to the Bank's Income Statement and also changes booked directly to equity. The majority of sensitivity to changes in foreign exchange rates is booked to the Income Statement, whereas the majority of interest rate sensitivity arises on the Bank's portfolio of New Zealand government securities and is booked directly to equity. Refer to note 19 on page 83 of the Bank's *Annual Report 2007-2008* for a detailed sensitivity analysis as at 30 June 2008.

Monitoring the Bank's performance

The Bank has been, and will continue to strive to be, a world leader in the openness and transparency of its processes and policies. Transparency assists the Bank to achieve its policy and operational goals effectively and efficiently, while allowing others to scrutinise the Bank's performance and to provide feedback, so helping the Bank improve the way it works.

The principal mechanisms for externally communicating the Bank's views include:

- the six-weekly OCR decisions, four of them in the quarterly *Monetary Policy Statements*;
- the six-monthly *Financial Stability Reports*;
- the Bank's *Statement of Intent*, *Annual Report* and financial statements;
- the quarterly *Bulletin*;
- the Bank's website (www.rbnz.govt.nz);
- occasional publications such as the *Briefing for the Incoming Minister*, and issue-specific books and brochures; and
- addresses given by the Governor and other senior Bank staff.

The Bank formally assesses its performance or is externally assessed in the following ways.

The Board reviews the Bank's performance and the discharge of its statutory obligations. In addition to providing the Governor with ongoing advice and feedback, the Board is also required to report annually on the Bank's performance. The Board's report is published in the Bank's *Annual Report*.⁸

The Audit Committee of the Board reviews the Bank's financial statements and risk management, and provides advice to the Governor before the Governor and Deputy Governor sign the related management statements. It also monitors the Bank's internal audit function.

The Bank publishes its *SOI* at the commencement of each financial year. The *SOI* sets out the Bank's principal functions, objectives, strategies, and key performance indicators for the next three years; comments on strategies for managing organisational health and capability; sets out initiatives and projected income and expenditure for the first year of that three-year period; and includes a statement of principles determining the annual dividend payable to the Minister.

The *Annual Report* includes both the financial statements and an assessment of the performance of the Bank's various functions, in terms of both the day-to-day responsibilities and progress against priorities and key performance indicators published in the *SOI*. It is tabled in Parliament.

Parliament's Finance and Expenditure Committee reviews the quarterly *MPS*, the six-monthly *FSR*, and the Bank's *Annual Report*, and can ask the Bank to appear before it.

⁸ For example, see pages 8–11 in the *Annual Report 2007–2008*.

Under section 167 of the Act, the Minister may, from time to time, initiate an assessment of the Bank's performance and how it has exercised its powers under the Act.

The Bank's financial statements are audited by external auditors who are the agent of the Controller and Auditor-General. The critical payment systems operated by the Bank are subject to review by external auditors quarterly in respect of the Austraclear depository system, and annually in respect of ESAS. An annual report is presented to Austraclear members.

From time to time, the Bank engages experts to assess the Bank's processes, research, and technical performance. In the past, assessments have been provided in the fields of monetary policy development; financial system policy; forecasting processes; bank-failure management; computer systems and network security; management; and leadership assessment and development. The Bank funds a Professorial Fellowship in Monetary and Financial Economics at Victoria University of Wellington. Also, two external advisers help to provide advice to the Governor regarding his interest-rate decisions. Before the release of the *MPS*, these two advisers fully participate in the deliberations leading to the formulation of the *MPS*.

The Bank's performance is also subject to international scrutiny. Every 12 to 18 months, the International Monetary Fund (IMF) undertakes an 'Article IV' assessment of the New Zealand economy, which includes sections on monetary policy and financial system stability. The resultant report is made public. Likewise, every two years, the Organisation for Economic Co-operation and Development undertakes a similar assessment, which is also published. The IMF is expected to undertake a Financial Sector Assessment Programme investigation every six or seven years; the last was in 2003.

Appendix

Key document references

Title	Purpose	Location
Policy Targets Agreement	Agreement between the Governor and the Minister of Finance specifying the inflation target in detail	www.rbnz.govt.nz/monpol/pta
<i>Monetary Policy Statement*</i>	Quarterly publication of the Bank's view of how the Bank proposes to meet its monetary policy targets, including extensive economic projections	www.rbnz.govt.nz/monpol/statements/index.html
<i>Financial Stability Report*</i>	Six-monthly publication of the Bank's view on the soundness and efficiency of the New Zealand financial system	www.rbnz.govt.nz/finstab/fsreport/
<i>Annual Report*</i>	Key accountability document, plus presentation of financial statements	www.rbnz.govt.nz/about/whatwedo/0094054.html
Austraclear New Zealand System Report to Members	Accountability document, plus presentation of financial statements	www.rbnz.govt.nz/about/whatwedo/rbnz_2006ar_2.pdf
Board of Directors' <i>Annual Report</i>	Board of Directors' report on the Bank's performance	Reproduced in the Bank's <i>Annual Report</i> www.rbnz.govt.nz/about/whatwedo/0094054.html
Briefing on the Reserve Bank of New Zealand*	Description of the role and functions of the Reserve Bank, prepared for an incoming government	www.rbnz.govt.nz/about/whatwedo/0122541.html
Reserve Bank of New Zealand Act 1989	Reserve Bank's statutory authority	www.rbnz.govt.nz/about/ourlegislation/
Funding Agreement	Basis of Bank's funding, setting how much of the Bank's revenues can be retained by the Bank	www.rbnz.govt.nz/about/whatwedo/1846117.html
<i>Statement of Intent*</i>	A statement of what the Bank intends to achieve over the next three years, with forecast income and expenditure for one financial year	www.rbnz.govt.nz/about/whatwedo/1764296.html
Letter to Minister of Finance on foreign exchange market intervention policy	Description of how the Bank may intervene in the foreign exchange market under section 16 of the Reserve Bank Act to influence the exchange rate	www.rbnz.govt.nz/foreignreserves/intervention/index.html
Letter from Minister of Finance to the Bank on foreign exchange intervention	Provision of delegated authority for the Bank to intervene in the foreign exchange market under section 17 of the Reserve Bank Act, should that market become dysfunctional	http://www.rbnz.govt.nz/foreignreserves/intervention/0148293.html
Memorandum from the Minister of Finance to the bank on foreign exchange intervention	Provision of delegated authority for the Bank to intervene in the foreign exchange market under section 17 of the Reserve Bank Act, should that market become dysfunctional	www.rbnz.govt.nz/finmarkets/foreignreserves/intervention/0148214.html www.rbnz.govt.nz/finmarkets/foreignreserves/intervention/index.html
<i>Reserve Bank Bulletin*</i>	Quarterly publication of articles relevant to central banking in New Zealand	www.rbnz.govt.nz/research/bulletin
Title	Purpose	Location
Statement of Principles	Explanation of the Reserve Bank's approach to bank registration and supervision	www.rbnz.govt.nz/finstab/banking/regulation/bs1.pdf
<i>This is the Reserve Bank*</i>	Introductory brochure about the Reserve Bank	www.rbnz.govt.nz/about/whatwedo/0109157.html
Vision Statement and Values	Expression of the Bank's organisational aims and culture	Inside front cover of <i>Annual Report</i> http://www.rbnz.govt.nz/about/whatwedo/0094054.html

* Also available in print from: the Knowledge Centre, Reserve Bank of New Zealand, PO Box 2498, Wellington, New Zealand.
knowledge@rbnz.govt.nz, www.rbnz.govt.nz

