

2 March 2015

Mr Graeme Wheeler
Governor
Reserve Bank of New Zealand
PO Box 2498
WELLINGTON 6140

Dear Graeme

This letter sets out my expectations for engagement with the Reserve Bank in 2015/16, and provides an opportunity for me to inform the development of the Reserve Bank's Statement of Intent (SOI).

The Reserve Bank contributes to the Government's goal of improving New Zealand's economic performance through its statutory responsibilities directed toward maintaining stability in the general level of prices, maintaining a sound and efficient financial system, and providing legal tender to meet the currency needs of the public. The Reserve Bank's balance sheet is also a significant proportion of the Crown's balance sheet.

I appreciate the commitment shown in the funding agreement proposal and associated five-year plan to ensuring the Reserve Bank is a high-performing organisation while also efficient in its use of resources. Consistent with this, my expectation is that the Reserve Bank has sufficient capacity to monitor and proactively identify emerging risks, take all reasonable steps to keep financial stability risks low, and maintain sufficient capacity to respond to any future crises.

Two-way engagement is important given the interactions between the Reserve Bank's monetary and financial stability policies and the Government's fiscal, economic and social policies. I look forward to another year of constructive engagement, including through our regular financial systems meetings, briefings on the Monetary Policy Statement and our regular discussions with the Secretary to the Treasury. I expect the Reserve Bank and the Treasury will continue to collaborate in areas of joint interest in accordance with the Memorandum of Understanding on Information Exchange and Collaboration agreed in 2012.

My broad expectation for engagement with my office remains that the Reserve Bank will:

- actively engage with me by providing substantive information early in the policy-making process and well in advance of public consultation. There are two types of process involved:

- 1) Where policy issues will require Cabinet decisions in due course, I continue to expect discussion about the rationale for any changes and their potential economic and fiscal impacts early on in the policy development process. Having early sight will allow us to have a meaningful dialogue about the options you have considered, the trade-offs between innovation and regulation, the implications for economic efficiency, and what drives the conclusions you reach. It also provides an opportunity for my perspectives to be incorporated. Where such policy issues are being considered, a Preliminary Impact and Risk Assessment submitted to the Treasury at the earliest possible stage of policy development will help to ensure that there is timely engagement with Treasury officials;
 - 2) Where you intend to adopt policies under the powers provided in your legislation, I continue to expect to receive your assessments of the expected regulatory impacts of these policies in advance, and at appropriate intervals thereafter, in accordance with section 162AB of the Reserve Bank of New Zealand Act. Please agree with the Treasury a framework for deciding whether a policy is of a minor or technical nature.
- provide me with final consultation documents on material policy issues at least two weeks prior to their intended release in order to allow sufficient time to raise final queries;
 - advise me as soon as practicable if you consider that any significant institution regulated by the Reserve Bank faces a material risk of financial difficulty. This is in addition to your responsibility for ensuring that I am informed in a timely manner of any risk to financial institutions, where there is a material likelihood of your needing to recommend (within a month) that I exercise any of my powers; and
 - liaise closely with my office in advance of speeches and major communications to ensure I am well informed and prepared for any enquiries that may arise.

The Reserve Bank has visibly increased its public engagement and openness in recent years and I encourage this to continue. It also remains important that there is active and effective consultation with stakeholders (particularly the financial sector) on proposals that affect them.

Areas of particular interest for 2015/16

Looking ahead to the next year, the areas of particular interest to me include:

Macroeconomic policy in the coming economic cycle: I am interested in understanding the nature of this cycle, such as the implications of low inflation and developments in international monetary conditions for the exchange rate and domestic policy settings. I remain interested in understanding issues relating to the Reserve Bank's implementation of monetary policy and policies directed toward financial stability and their interaction with fiscal and wider policy settings. I also look forward to the Reserve Bank's analytical contributions to deepen our understanding of New Zealand's economic performance and macroeconomic imbalances.

Macro-prudential policy: I remain interested in the effectiveness and development of macro-prudential tools and look forward to being informed and consulted about developments in accordance with the Memorandum of Understanding agreed in 2013.

Regulatory institutions and practices: The Government has a strong interest in improving the quality and effectiveness of regulation. As you will be aware, the Productivity Commission reported in July 2014 with guidance on designing future regulations and recommendations on how to improve the operation of current regulations. The Government will be providing its response shortly and I will be interested in understanding what opportunities you identify to improve the quality and effectiveness of regulations or regulatory proposals made by the Reserve Bank, and to improve the operation of the regulatory regimes administered by the Bank.

Financial system: I remain interested in the Reserve Bank's activities related to supporting a well-functioning financial system. With respect to prudential regulation, I remain interested in the ongoing suitability of policies put in place to reduce the likelihood of the failure of a major financial institution in New Zealand, particularly in light of the recommendations made by the Australian Financial System Inquiry.

Mitigating fiscal risks: I remain interested in better understanding the risks to the Crown balance sheet that may arise from the failure of a financial institution, the bedding in of reforms that mitigate the Crown's exposure to the financial sector, including OBR, and any opportunities to reduce these risks further.

Trans-Tasman Banking Council [Withheld under s6(b)(i)]

I expect that you will continue to work closely with Australian stakeholders to build awareness of our resolution options and how they would work in practice.

I hope this provides you with a clear sense of my expectations for active engagement on significant matters of policy. I look forward to fruitful discussions on the Reserve Bank's SOI. In addition, I welcome your suggestions on other areas of engagement that may be important to New Zealand's macroeconomic and financial stability.

The Board's function is to keep the performance of the Reserve Bank and the Governor under constant review. In fulfilling this role, the Board should be aware of my expectations. As such, I am copying this letter to the Chair of the Board.

Yours sincerely,

Hon Bill English
Minister of Finance

cc: Dr Rod Carr, Chair, RBNZ Board of Directors