

GOVERNOR'S FOREWORD

For the world economy, the twelve months covered by this Report have been a period of relative calm and prosperity, after the turbulence of the previous two years. Domestically, it was a good year for the economy, with strong growth and falling unemployment, although inflation was somewhat higher than it had been for several years. Because of the combination of ongoing strength in economic activity, and rising inflation, it has been a more eventful year than its immediate predecessors for monetary policy, with a series of tightenings occurring, the first since 1994.

It is always difficult to start the tightening phase of monetary policy, particularly if it is done pre-emptively as it should be - that is, before clear signs of overheating have emerged. An important part of the task was to communicate the idea that the stance of monetary policy that had been reached in 1998/99 was expansionary, and hence no longer appropriate for the stronger economic environment we faced in late 1999 and 2000. The task was made somewhat easier on this occasion because most other developed countries reached a similar conclusion at approximately the same time. In all, there were four tightenings of monetary policy in Australia during 1999/2000 and another in August 2000, which amounted to a cumulative increase in the overnight cash rate of 150 basis points.

Detailed accounts of monetary policy have been provided on an ongoing basis through the year, such as in the two *Semi-Annual Statements on Monetary Policy*, the two quarterly reports on the economy and financial markets, testimony to the House of Representatives Standing Committee on Economics, Finance and Public Administration, speeches and the media releases accompanying the monetary policy changes. As such, this Report focuses on other important events which had an impact on the activities of the Reserve Bank during 1999/2000. In summary, the main points were as follows:

- In its market operations, the main task on the domestic side was to bring about the tightenings of monetary policy and to maintain the cash rate steady at the new levels. The biggest challenge in this area was to cope with the declining volume of government paper. The solution has been to make greater use of repurchase agreements, both on government securities and, more particularly, foreign exchange (the latter usually known as foreign exchange swaps). On the foreign side, the RBA did not undertake any direct intervention during the year, although a large part of its sales to the Government was not passed through to the market, in line with the usual practice when the exchange rate is low.
- International responsibilities are now absorbing more time and resources than even a few years ago. In conjunction with other areas of government, the RBA has made a strong effort to ensure that Australia is well-represented in the various new international groupings that will effectively be "writing the future rules" of international financial markets. Australia is now one of



the eleven countries in the Financial Stability Forum, and one of the Group of Twenty. Along with the other international and regional groups of which the RBA was already a member, this has led to a significant increase in work and travel. The RBA has also continued to participate in technical assistance programs, both on a bilateral basis and through IMF-sponsored missions.

- The experience in the business services area has been mixed, with some key areas still very busy, but others having to contract further as technological change and a loss of customers reduce demand. As mentioned in the previous Report, the Western Australian and Australian Capital Territory Governments have taken their banking business elsewhere, as has the Commonwealth Department of Finance and Administration for its own departmental transactions business. This follows earlier moves by the Queensland, Northern Territory and Tasmanian Governments. As well, existing key Commonwealth Government customers have tended to centralise their banking in one or two locations, rather than maintain operations in each State.
- The situation was finally reached where the volume of work needed to be performed in most of our branches fell to the point where we could no longer justify maintaining staff at a level that would constitute a viable branch. Following the closure of Darwin and Hobart branches in earlier years, the decision was reluctantly taken to close Melbourne, Brisbane and Perth branches during 2000. Adelaide branch remains in operation as it is supported by the banking business of the South Australian Government. In the case of Melbourne, although the CBD branch has closed, the note-processing function will be centralised at Note Printing Australia. The branches, at their peak, performed an important operational role in banking, registry and cash distribution, and, to a limited extent, they acted as a conduit for information about local economic conditions, though they were not designed specifically for that purpose. We are extremely conscious, however, that if no offsetting measures are taken, the closure of branches would run the risk of putting us out of touch with regional issues at a time when they are becoming more important. As a result, we are in the process of strengthening our capacity for monitoring local conditions, and seeking to improve our channels of communication with States and regions. This will involve, among other things, a small, but targeted, representation in State capitals.
- The year just completed was the second year in which supervision of banks has been carried out by the Australian Prudential Regulation Authority. With the departure of bank supervision, the RBA retained responsibility for the overall stability of the financial system and for regulation of the payments system. Apart from overseeing the smooth transition into the new century (the so-called Y2K problem), carrying out the former of these responsibilities



was relatively uneventful - as would be expected, the financial system is in very good shape from a prudential perspective at this stage of a long economic expansion. The RBA's work in overseeing the payments system is moving away from the wholesale side, now that real-time gross settlement (RTGS) is well-established, towards more focus on retail payments systems.

- Note Printing Australia had an extremely busy year, producing 656 million notes, more than double the previous year's figure. Demand for notes was augmented by the Australian contingency order for Y2K purposes, and by a large export order from Indonesia as well as others from New Zealand and Papua New Guinea. Brazil and Taiwan have also been added to the list of countries to use polymer notes, both printing their own on substrate produced in Australia.

As in the past few years, I would like to conclude this foreword by thanking the staff for the job they have done during the year, and recording my appreciation of the way they have coped with the almost continuous downsizing of the RBA, which has been going on for many years. Instead of simply outlining in a paragraph or two the main changes that have occurred in the past year, we have decided to devote a whole chapter of this Report to an account of the evolution of the RBA over the past decade and a half. It is an interesting story in itself, and also a microcosm of the changes that have been happening in the economy as a whole.

I J Macfarlane

Chairman, Reserve Bank Board

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