

BUSINESS SERVICES

The RBA provides a range of banking, registry, note issuing and settlement services for its customers. Banking services are provided to the Commonwealth Government and one State Government (South Australia). Currency notes are processed and issued into the community via banks and armoured car companies, while registry and settlement facilities are provided almost exclusively to banks and other financial institutions. By and large, the RBA does not provide business services to the public - the exception is a small number of registry transactions (accounting for less than one per cent of total turnover in bonds).

A major focus of the Banking Department over the past year has been to position the business to manage the effects of the Government's competition policy on the market for transactional banking services. Responsibility for their own banking arrangements has been devolved to Government agencies themselves, and a number have market-tested their transactional banking requirements. This process will gather momentum during the coming year.

The combined effects of declining business volumes, technology and centralisation of functions by major customers have significantly reduced the role of the RBA's branches in providing banking services. In addition, the impact of the new polymer currency note technology has been of greater significance than originally envisaged. The volume of note processing undertaken by branches has diminished considerably as a result of the improved durability and security of polymer

notes and the effect of changes to note distribution arrangements. The combined impact of these reductions in activity in the banking and note issue functions led to a situation where staff numbers in branches were falling below what was considered to be the minimum viable size in terms of security and staff management. This situation had been developing over a number of years and finally the decision to close a number of branches became unavoidable. Darwin and Hobart branches were the first to be affected, closing in 1997 and 1998, respectively. An announcement was made to staff on 8 November 1999 of the pending closure of Melbourne, Brisbane and Perth branches, the cessation of cash-processing operations at Adelaide and Sydney branches and the establishment of a centralised note-processing facility at the RBA's subsidiary, Note Printing Australia Limited (NPA) at Craigieburn, Melbourne. The closure of branches and the transfer of the remaining branch activities to Head Office and Craigieburn has been a major task and has occupied a lot of the time of the Banking and Note Issue Departments.

A longer-term perspective of changes in the RBA's structure is provided in the next chapter.

GOVERNMENT BANKING

Commencing 1 July 1999, the RBA's banking business was separated into two components in order to comply with the Commonwealth Government's competitive neutrality and devolved banking arrangements. The non-contestable core account-keeping function undertaken on behalf of the Department of Finance and Administration (DoFA) was split



from the contestable transactional processing business conducted for Commonwealth agencies. From 1 July 1999, Commonwealth agencies were given responsibility for conducting their own banking arrangements.

In its core account-keeping role, the RBA maintains six accounts, including the Official Public Account (OPA), whose aggregate balances represent the Commonwealth's daily cash balance. In addition, it provides a limited overdraft facility for the Commonwealth. The core banking function also embraces the release of funds from the OPA to agencies, the sweeping of overnight balances from transactional bankers to the OPA and provision and maintenance of an agency term deposit scheme on behalf of DoFA.

The core account-keeping function also provides for the electronic collection of forecasting data from agencies and reporting on high value transactions on agencies' accounts by transactional banks to assist the RBA in discharging its monetary policy and liquidity management responsibilities.

As noted above, under the devolved banking arrangements, agencies which come within the scope of the *Financial Management and Accountability Act 1997 (FMA Act)* have been delegated the powers to open and operate bank accounts. These *FMA Act* agencies may operate official bank accounts, including trust accounts, with the RBA in its capacity as transactional banker or with a private sector bank provided the arrangements comply with the core protocols on devolved banking established by DoFA. Agencies must undertake

all significant foreign exchange transactions with the RBA in order to ensure that these transactions are put through the market in a manner consistent with exchange rate policy.

BUSINESS TRENDS

During the year, the RBA has been heavily involved with Commonwealth agencies in reviewing, refining and improving the banking arrangements put in place for them late in 1998/99. These arrangements had been established in time to allow agencies to take full responsibility for their own banking arrangements as from 1 July 1999, when DoFA withdrew its provision and support of centralised banking arrangements.

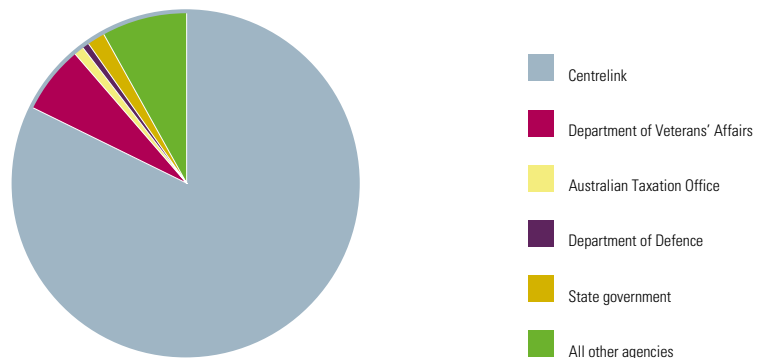
In line with DoFA's banking devolution guidelines, agencies are beginning to undertake the task of market-testing the banking services currently provided to them by the RBA. As at 30 June 2000, five lead agencies had completed market-testing; three chose to move their banking requirements to private sector banks and two elected to remain with the RBA. The Bank was requested by DoFA to assist in the development of a market-testing kit to simplify the process for agencies yet to undertake market-testing. The coming year is expected to see the majority of agencies complete the exercise. The outcome of this process, the take-up of the Commonwealth's e-commerce initiatives and the working-through of major customers' centralisation projects, are likely to lead to the need for further adjustments to the RBA's banking operations in the period ahead.

The effect of the loss of the Australian Capital Territory and Western Australian State Government banking businesses and increased acceptance of the Health Insurance Commission's efforts to encourage electronic crediting of Medicare rebates were the major reasons for the reduction in the RBA's paper transactions volumes during the year. Paper transactions declined by 4.5 per cent to 43 million items in 1999/2000.

Electronic transactions through the Government Direct Entry System (GDES) fell by less, mainly because of the Medicare initiatives and continuing efforts of the RBA's remaining customers to move from paper-based to electronic transactions. Electronic transactions declined from 226 million to 223 million transactions during the year.

The RBA fully supports customer initiatives to move away from the more expensive and less efficient paper-based payment mechanisms. It is directly involved in a range of finance-industry and government-sponsored developments aimed at fostering the growth of e-commerce. The RBA is represented on the Commonwealth Government's Electronic Payments Focus Group and the Commonwealth Procurement Online 2000 Steering Committee. One aim of these latter initiatives is to encourage Commonwealth agencies to introduce electronic arrangements (including Internet-based) which would enable up to 90 per cent of agencies' procurement needs to be conducted and settled electronically with suppliers by 31 December 2000.

ELECTRONIC BANKING TRANSACTIONS — 1999/2000





SYSTEM LINKAGES

Under the previous "whole of government" banking arrangements, most Commonwealth agencies were linked electronically to the RBA via DoFA. Most of the larger agencies running their own mainframe systems had direct data links to the RBA. Prior to the devolution of responsibility for banking to agencies themselves, DoFA outsourced the Commonwealth's centralised accounting and payroll system to an external supplier, CITEC. In order to facilitate the transition to the new devolved banking arrangements, the RBA agreed to provide CITEC with the same distribution services previously provided to DoFA until 31 December 2000, for those agencies which remained on the centralised system as at 1 July 1999.

As part of the devolution process, agencies were no longer required to use the Commonwealth's centralised accounting and payroll system. A panel of providers had been established by the Commonwealth for the provision of these systems and many agencies moved down this path. In moving to new accounting and payroll systems, agencies were required to establish their own data links to their transactional banker. For those agencies remaining with the RBA on 1 July 1999, who did not have direct mainframe links with it, this was achieved by installing the RBA's customer desk-top banking package, ReserveLink.

In order to satisfy agencies' devolved banking requirements, an upgraded version of ReserveLink was developed. This included new security measures, using smart card technology and enhanced reporting capabilities.

Sets of accounts for the RBA's various contestable businesses are given in the chapter "Pro Forma Business Accounts".

REGISTRY AND SECURITY

SETTLEMENT SERVICES

The Reserve Bank Information and Transfer System (RITS) provides its 143 members (representing 267 organisations) with facilities for the electronic settlement of transactions in Commonwealth Government securities (CGS). The system handles over 99 per cent of CGS turnover in the market and has securities with a face value of \$73 billion lodged in it.

The system also provides facilities for electronic tendering for CGS, automatic interest and maturity payments for securities lodged in the system and for settling the interbank component of equity transactions on CHES, the Australian Stock Exchange's electronic settlement system. RITS is also Australia's real-time gross settlement system and is the means through which banks and other approved institutions access their Exchange Settlement accounts with the RBA.

RTGS SYSTEM

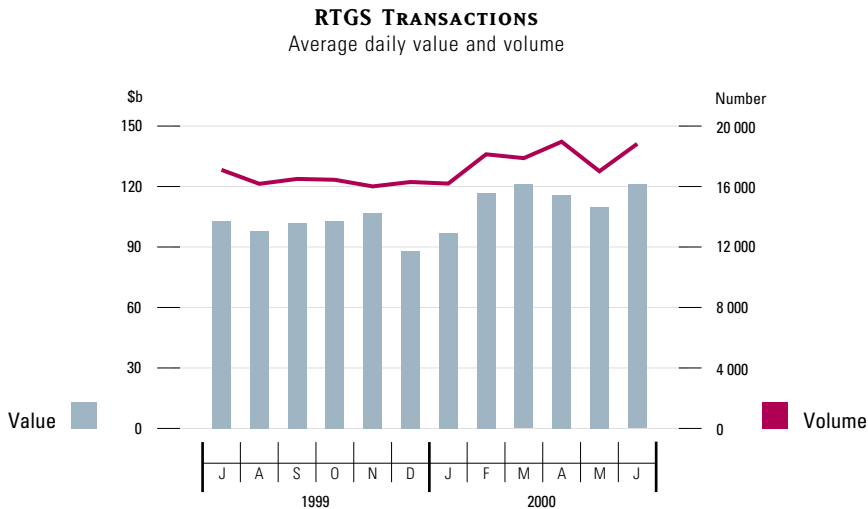
RITS provides the platform for the RTGS system. About 90 per cent of total values exchanged between banks is settled across RITS on an RTGS basis and hence is not subject to interbank settlement risk. RTGS payments include securities markets settlements, the Australian dollar leg of foreign exchange transactions and important or time-critical customer payments.

This financial year was one of consolidation as the RTGS system progressed through its second year of operation. On average, the daily number and value of transactions settled by RITS increased over the year. However, there was a noticeable decline around the century date-change followed by strong growth over the following months.

Work proceeded on a number of initiatives during the year. The RITS Regulations, which underpin the operation of the system, were amended to cater for widening of access to Exchange Settlement accounts. The first institution approved under the new arrangements, the Sydney Futures Exchange Clearing House, commenced operating its own Exchange Settlement account on 28 February 2000. Testing is well advanced for changes to RITS to

cater for the introduction of "continuous linked settlement" of foreign exchange transactions through the new CLS Bank in the second half of 2001. This will involve extended operating hours for RITS and participating banks, in order to line up with the CLS operating window during the European morning.

Work is also underway to permit optional real-time gross settlement of high-value equity transactions from CHES. This feeder system is scheduled to commence operations towards the end of 2000. To improve the efficiency of securities settlement further, RITS is also being enhanced to enable details of securities transactions to be passed using standard SWIFT messages. This is a major step towards straight-through processing and implementation is planned for the second half of 2001.





Settlement services are also provided for the RBA's own transactions in the domestic securities and foreign exchange markets, as well as for those arising from business conducted by official customers domestically and abroad. The RBA also acts as collator of banks' obligations arising from the low-value clearing streams (paper, and bulk and retail electronic) managed by the Australian Payments Clearing Association.

REGISTRY SERVICES

The RBA provides registry services on behalf of the Commonwealth Government, the State government borrowing authority of South Australia, and some other domestic and foreign official organisations. Services include the issuance of securities, maintenance of ownership records, payment of interest and redemption of securities at maturity.

In 1999/2000, registry activity continued to decline. At end June 2000, stock accounts totalled 21 400, down by seven per cent from the level 12 months earlier. As in previous years, the RBA maintained a program of review, to ensure that its registry service remained as cost-effective as possible, given the small scale of the operation. As a consequence, staffing levels in registry further declined in 1999/2000. The cost to the Government, through its agency the Australian Office of Financial Management (AOFM), for the operation of the registry declined by 19 per cent during the year and a further decline of around 20 per cent is forecast in 2000/2001.

NOTE ISSUE

The note issue functions of the RBA comprise the issue of notes (new and reissuable); the processing of notes returned from circulation for authentication and quality-control purposes; general oversight of cash distribution arrangements; and research into and development of note designs and security features.

The move to polymer currency notes has continued to have a significant impact on the RBA's note issue activities. The greater security and durability of polymer notes mean that they do not need to be checked for authenticity and fitness as frequently as in the past to keep the circulation clean and free of counterfeits. In combination with changes to cash distribution arrangements, this has resulted in a significantly reduced note-processing task.

Volumes of notes processed at the RBA's five note-processing centres declined during the year and were expected to decline further. Against that background, the decision was taken to centralise the Bank's note-processing activities at one site. After careful consideration, it was decided that a single note-processing operation should be established at the RBA's subsidiary, Note Printing Australia Limited (NPA), at Craigieburn. This site has geographical advantages and note processing complements a number of NPA's existing operations. Current plans are for the new facility to be established in the first half of 2001.

NOTE PROCESSING AND DISTRIBUTION

Notwithstanding continued strong growth in the volume and value of electronic financial transactions, demand for currency has continued to increase, with notes in circulation

VALUE OF NOTES ON ISSUE

(\$ million)

AT END JUNE	\$1 (a)	\$2 (b)	\$5	\$10	\$20	\$50	\$100	TOTAL	INCREASE (PER CENT)
1994	21	69	313	634	1795	6837	7907	17577	7.4
1995	20	49	332	614	1848	7193	8482	18538	5.5
1996	19	48	337	583	1868	7928	8399	19182	3.5
1997	19	47	351	601	1837	8912	8297	20064	4.6
1998	19	47	361	617	1804	9523	9280	21651	7.9
1999	o(c)	46	379	639	1850	10356	10282	23552	8.8
2000	o(c)	46	397	646	1917	11188	11240	25434	8.0

(a) Last issued May 1984

(b) Last issued June 1988

(c) See Notes To and Forming Part of the Financial Statements, Note 1(i)

again increasing at a faster rate than economic activity. The value of notes on issue in 1999/2000 rose by eight per cent to \$25.4 billion. \$50 and \$100 notes continue to show the strongest increase, with the two denominations increasing their share of the total value of notes in circulation from 82 per cent in the early 1990s to 88 per cent in June 2000. During 1999/2000, around \$107 billion in currency notes were issued into circulation and \$105 billion returned. These values are up significantly (by around 35 per cent) on last year, reflecting strong demand for notes by banks in the run-up to Y2K.

In early 1999/2000, changes to cash distribution arrangements enabled armoured car companies to service all their customers - banks and other commercial customers (authorised deposit-taking institutions, retailers, casinos and other large cash-handling organisations) - from the one combined note holding. Previously, the two groups were serviced from separate note holdings and this had inhibited the efficient recirculation of

currency. The changed arrangements provide greater opportunities for the redistribution of notes in the community and reduce the volume of notes moving in and out of the RBA.

Over the year, around 450 million notes, with a value of around \$18 billion, were returned to the RBA for processing through its high-speed note counting and sorting machines. This compares with one billion notes processed during 1998/99 (with a value of around \$40 billion). Close to 93 per cent of notes returned were classified as fit for reissue.

As explained in the chapter on "Financial System Stability", the RBA ordered additional notes in preparation for Y2K. Although most of the stocks of notes were held within the RBA, the distribution of notes to RBA branches, banks and armoured car companies was a major task during the year. In the event, although demand in the lead-up to 2000 was higher than in a normal year, the quantity of notes was more than adequate and the additional notes that had been distributed flowed back to the RBA in early 2000.



COUNTERFEITING ACTIVITY

Counterfeiting activity has continued at low levels with around 2 100 counterfeits being detected over the year. This is higher than the 1 700 detected during the previous year, but significantly lower than the outcomes of other recent years.

Most counterfeits detected during the year were relatively crude reproductions of polymer notes on paper. Despite the low level of activity, the risk of counterfeiting remains and the RBA continues to conduct research and further develop the security of polymer notes.

CENTENARY OF FEDERATION

- NEW \$5 NOTE DESIGN

The RBA announced plans in its 1998 Annual Report to issue a newly designed \$5 note in early January 2001 as a contribution to the Centenary of Federation celebrations.

It also announced at that time that one side of the note will feature Sir Henry Parkes, commonly known as the "Father of Federation". The other side of the note will depict Catherine Helen Spence, the author, political reformer and first woman to stand for election to public office in Australia. The designer of the note is Garry Emery, one of Australia's leading graphic designers, who also designed the current \$20 note. Production of the new note is underway and the project is on track for the first of the notes to be issued in January 2001.

COUNTERFEITS PASSED PER MILLION NOTES IN CIRCULATION

