Reserve Bank of Australia
Annual Report

2018

RESERVE BANK OF AUSTRALIA

RESERVE BANK OF AUSTRALIA

65 Martin Place
Sydney NSW 2000

GPO Box 3947
Sydney NSW 2001

+61 2 9551 9507
lowep@rba.gov.au

Philip Lowe
GOVERNOR

27 August 2018

The Hon Josh Frydenberg MP
Treasurer
Parliament House
CANBERRA ACT 2600

Dear Treasurer

RESERVE BANK OF AUSTRALIA ANNUAL REPORT 2018

In accordance with section 46 of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), I am pleased to submit the Reserve Bank's Annual Report for 2018 for presentation to the Parliament. The annual report has been prepared in accordance with the rules under section 46(3) of the PGPA Act.

Yours sincerely

Philip Lowe

Reserve Bank of Australia

Annual Report 2018

Contents

Governor's Foreword 1

Part 1: About the Reserve Bank

Our Role 5
Governance 8
Reserve Bank Board 15
Accountability and Communication 30
Operational Structure 43

Part 2: Our Operations

Operations in Financial Markets 53
Banking and Payment Services 65
Banknotes 71
International Financial Cooperation 80
Community Engagement 92

Part 3: Management and Accountability

Our People 103
Management of the Reserve Bank 112
Risk Management 117
Earnings, Distribution and Capital 124
Pro Forma Business Accounts 128
Annual Performance Statement for 2017/18 129
Statutory Reporting Requirements 141

Part 4: Financial Statements

Statement of Assurance 147
Financial Statements 148
Notes to the Financial Statements 153
Independent Auditor's Report 184

Part 5: Indexes

Statutory Reporting Requirements Index 191
List of Tables 193
List of Graphs 194
List of Figures 195
Abbreviations 196
Contact Details 198

This report is available electronically in PDF and HTML formats on the Reserve Bank's website: <www.rba.gov.au/publications/annual-reports/rba/index.html>.

The Reserve Bank welcomes comments on this report. Feedback and enquiries about any aspect of this report may be directed to:

Secretary's Department
Reserve Bank of Australia
65 Martin Place
Sydney NSW 2000

GPO Box 3947
Sydney NSW 2001

Telephone: +61 2 9551 8111
Facsimile: +61 2 9551 8033
Email: rbainfo@rba.gov.au

© Reserve Bank of Australia 2018. All rights reserved. The contents of this publication shall not be reproduced, sold or distributed without the written prior consent of the Reserve Bank of Australia.

The graphs in this report were generated using Mathematica.

ISSN 1448-5303 (Print)

ISSN 1448-5192 (Online)

Governor's Foreword

The global economic expansion continued over the past year. Unemployment rates in many countries have declined further and, in some cases, are at multi-decade lows. Inflation rates remain low, but have generally moved closer to central bank targets. Financial conditions are still expansionary, although they are gradually becoming less so.

This improvement in the global environment is helping the Australian economy. Higher commodity prices and stronger employment growth have provided a welcome boost to incomes. Economic growth has gradually picked up and inflation is moving closer to the Reserve Bank's target. Higher levels of public and private investment are also supporting the economy.

Against this more positive backdrop, the Reserve Bank focused on a number of developments over the past year. The first was the risk to the global economy from a move towards protectionism. Australia is a major beneficiary of the open, rules-based international system and has a strong stake in this system continuing. A second issue was the subdued growth in wages in Australia. The slow growth in wages has boosted the number of Australians with a job, but has also led to slower income growth for many individual households and less inflation pressure than otherwise. A third issue was the high level of household debt in Australia, which carries certain risks. The Bank has worked closely with the other members of the Council of Financial Regulators to ensure that lending standards are appropriate for this environment. Close cooperation between the various regulatory agencies continues to be a positive and distinguishing feature of Australia's regulatory arrangements.

The Reserve Bank Board held the cash rate steady at 1.5 per cent over the past year, with the most recent change in monetary policy having been in August 2016. Over this period, the Bank has sought to be a source of stability and confidence while further progress is made in having inflation return to target and the Australian economy move closer to full employment.

The past year was marked by the completion of some major national interest projects by the Reserve Bank. These have required significant investments in technology. One of these projects was the development of a core part of the payments infrastructure that allows Australians to move money between bank accounts easily in real time and with detailed information about the payment. As the banker to the Australian Government, the Reserve Bank has also made significant investments in its banking systems to allow government agencies to use this new payment system. A major upgrade of the arrangements for the storage and distribution of banknotes was also completed. The new highly automated and secure storage facility and processes are designed to meet Australia's banknote needs well into the future. A new high-tech $10 banknote was issued as part of the Bank's efforts to keep Australia's banknotes safe and secure. This follows the issue of the new $5 note in 2016. Plans are well advanced for the issue of a new $50 banknote later this year, with the same world-leading security features.

The Reserve Bank is committed to a high degree of transparency and accountability as Australia's central bank. Over the past year, senior staff gave over 50 public speeches and had many meetings with business and community groups. The Bank has also devoted considerable resources to its public education program, with a particular focus on economics students and teachers. Our aim is to support and encourage the study and understanding of economics in Australia.

Reflecting the completion of some large projects, there was a small decline in the number of Bank staff over the past year and a further reduction is expected in 2018/19. The Bank's general operating costs, excluding depreciation, increased by 1.4 per cent in 2017/18. Capital expenditure declined by more than half, reflecting the completion of projects.

The Bank recorded an accounting profit of $3.8 billion in 2017/18. Earnings were boosted by valuation gains on the Bank's foreign assets because of the depreciation of the Australian dollar. An amount of $669 million was available for distribution to the Australian Government, comprising underlying earnings less realised valuation losses. A revised risk-based capital framework was introduced in 2016/17, with the current level of capital slightly above the Board's target level. Accordingly, the Reserve Bank Board did not seek a transfer to the Bank's reserves and the full amount of $669 million available for distribution will be transferred to the Australian Government. The Bank continues to have a strong balance sheet.

The Reserve Bank's staff share a strong commitment to high standards and serving the public interest. They go about their work with a high degree of professionalism and have achieved much over the past year. The Reserve Bank Board joins me in thanking the staff for their work and for their service to the Australian community.

Philip Lowe
Governor
23 August 2018

Part 1:

About the Reserve Bank

Our Role

In its role as Australia's central bank, the Reserve Bank of Australia determines and implements monetary policy, fosters financial stability, undertakes a range of activities in financial markets, acts as a banker to the Australian Government, issues Australia's banknotes and has policy, supervisory and operational roles in the payments system.

The Reserve Bank of Australia is established by statute as Australia's central bank. Its enabling legislation is the *Reserve Bank Act 1959*. The Bank pursues national economic policy objectives. Its responsibility for monetary policy is set out in section 10(2) of the Reserve Bank Act, which states:

It is the duty of the Reserve Bank Board, within the limits of its powers, to ensure that the monetary and banking policy of the Bank is directed to the greatest advantage of the people of Australia and that the powers of the Bank … are exercised in such a manner as, in the opinion of the Reserve Bank Board, will best contribute to:

a. the stability of the currency of Australia;

b. the maintenance of full employment in Australia; and

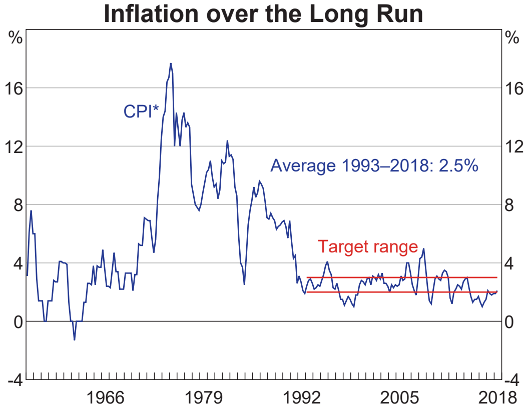
c. the economic prosperity and welfare of the people of Australia.

Policies in pursuit of these objectives have found practical expression in a flexible, medium-term inflation target, which has formed the basis of Australia's monetary policy framework since the early 1990s. The policy objective is for consumer price inflation to average between 2 and 3 per cent over time. By achieving this objective, the Reserve Bank can help promote sustainable economic growth and employment.

The seventh *Statement on the Conduct of Monetary Policy*, agreed by the Treasurer and the Governor on 19 September 2016, records the common understanding of the government and the Reserve Bank on key aspects of the monetary policy framework. This update of the statement confirmed the monetary policy framework in Australia, explicitly recognising that it is appropriate for the Reserve Bank Board to take account of financial stability considerations in determining the appropriate setting of monetary policy.

The Reserve Bank works with other regulatory agencies in Australia to foster overall financial stability, which is an important underpinning of a stable macroeconomic environment.

Inflation over the Long Run



* Excludes interest charges prior to September quarter 1998 and adjusted for the tax changes of 1999–2000

Sources: ABS; RBA

The Governor chairs the Council of Financial Regulators (CFR), a non-statutory coordinating body for Australia's main financial regulatory agencies, whose role is to contribute to the efficiency and effectiveness of regulation and to promote the stability of the Australian financial system. Its members – the Reserve Bank, the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission and the Australian Treasury – share information, discuss regulatory issues and, if the need arises, coordinate responses to potential threats to financial stability. The CFR also advises the Australian Government on Australia's financial regulatory arrangements.

Australia's financial stability policy framework includes mandates for financial stability for both APRA and the Reserve Bank. APRA is responsible for prudential supervision of financial institutions and the Bank is responsible for promoting overall financial system stability. In the event of a financial system disturbance, the Bank and relevant agencies would work to mitigate the risk of systemic consequences. The Bank's responsibility to promote financial stability does not, however, equate to a guarantee of solvency for financial institutions and the Bank does not see its balance sheet as being available to support insolvent institutions. Nevertheless, the Bank's central position in the financial system – and its position as the ultimate provider of liquidity to the system – gives it a key role in financial crisis management, in conjunction with the other members of the CFR.

The Reserve Bank conducts operations in domestic and international financial markets and undertakes analysis of markets and institutional developments in support of its policy objectives. These include ensuring there is sufficient liquidity in the domestic money market on a daily basis, in support of the Bank's monetary policy and financial system stability objectives. The Bank operates in the foreign exchange market to meet the foreign exchange needs of its clients (the largest of which is the Australian Government) and to assist with liquidity management in domestic markets. It holds and manages Australia's foreign currency reserves, and has the capacity to intervene in the foreign exchange market to address any apparent dysfunction in that market or significant misalignment in the value of the currency, consistent with the objectives of monetary policy.

The Reserve Bank has responsibility for ensuring the stability, efficiency and competitiveness of the payments system through the Payments System Board, which was established in 1998. The Bank's powers in relation to the payments system are set out in a number of statutes, including the *Payment Systems (Regulation) Act 1998* and the *Payment Systems and Netting Act 1998*. Under the *Corporations Act 2001*, the Bank, through the Payments System Board, has responsibility for determining financial stability standards for licensed clearing and settlement facilities and assessing facilities' compliance with those standards.

The Reserve Bank also has an operational role in the payments system, as owner and operator of Australia's high-value real-time gross settlement system – the Reserve Bank Information and Transfer System (RITS). In November 2017, significant new capability was added to RITS with the Fast Settlement Service commencing live operations. This system settles obligations arising from individual payments exchanged on the New Payments Platform in real time on a 24/7 basis. A separate area of the Bank assesses RITS against international standards for such infrastructure on an annual basis.

The Reserve Bank provides specialised banking services to government and foreign official institutions, including payments and collections as well as general account maintenance and reporting.

The Reserve Bank works with its wholly owned subsidiary, Note Printing Australia Limited, to design and produce Australia's banknotes. The Bank issues banknotes with the objective of providing a safe, secure and reliable means of payment and store of value.

Governance

The Reserve Bank has two boards: the Reserve Bank Board, which has responsibility for monetary and banking policy and the Bank's policy on other matters excluding payments system policy; and the Payments System Board, which has responsibility for payments system policy. Under the *Reserve Bank Act 1959*, the Bank is managed by the Governor.

The Reserve Bank's governance structure is set out in the *Reserve Bank Act 1959*. The Governor is the accountable authority of the Bank for the purposes of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act). The Governor is assisted in fulfilling his responsibilities to manage the Bank by two key management committees, the Executive Committee and the Risk Management Committee.

Reserve Bank Board

The Reserve Bank Board has responsibility for monetary and banking policy and the Reserve Bank's policy on all other matters except payments system policy. The Board comprises the Governor (Chair), Deputy Governor (Deputy Chair), Secretary to the Treasury and six non-executive members appointed by the Treasurer, a total of nine. Attendance by members at meetings of the Board during 2017/18 is shown opposite and members' qualifications and experience are provided on pages 15–26.

The Reserve Bank Board meets 11 times a year, on the first Tuesday of each month except in January. Five members form a quorum for a meeting of the Board. In accordance with the Reserve Bank Act, the Board makes decisions by a majority of the votes of the members present

The Reserve Bank Board with members of staff; (clockwise from centre) Board members Governor Philip Lowe, Deputy Governor Guy Debelle, Catherine Tanna, Treasury Secretary Philip Gaetjens, Ian Harper, Carol Schwartz AM, Anthony Dickman (Reserve Bank Secretary), Mark Barnaba AM, Wendy Craik AM, Allan Moss AO; staff members: Christopher Kent (Assistant Governor, Financial Markets) and Luci Ellis (Assistant Governor, Economic); (back row) Andrea Brischetto (Deputy Secretary), Alex Heath (Head of Economic Analysis Department) and Ellis Connolly (Deputy Head of Domestic Markets Department), August 2018

Board Meetings – 2017/18
Attendance by members

	No. of meetings attended	No. of meetings eligible to attend
Philip Lowe (Governor)	11	11
Guy Debelle (Deputy Governor)	11	11
John Fraser (Secretary to the Treasury)	9[a]	11
John Akehurst[b]	2	2
Mark Barnaba[c]	8	9
Wendy Craik[d]	1	1
Kathryn Fagg[e]	10	10
Ian Harper	11	11
Allan Moss	11	11
Carol Schwartz	9	11
Catherine Tanna	11	11

(a) (Nigel Ray (Deputy Secretary, Macroeconomic Group, Australian Treasury) attended the December 2017 and June 2018 meetings in place of John Fraser, in terms of section 22 of the Reserve Bank Act
(b) John Akehurst's term on the Board ended on 30 August 2017
(c) Mark Barnaba's term on the Board commenced on 31 August 2017
(d) Wendy Craik's term on the Board commenced on 7 May 2018
(e) Kathryn Fagg's term on the Board ended on 6 May 2018
Source: RBA

and voting, with the chair having a casting vote, if necessary, in addition to a deliberative vote.

Reserve Bank Board meetings are usually held at the Reserve Bank's Head Office in Sydney. Meetings are held in two other Australian cities each year. The Board's interstate meetings during 2017/18 were in Brisbane in September 2017 and in Adelaide in May 2018.

The Reserve Bank Board has an Audit Committee and a Remuneration Committee, whose activities are described below.

Payments System Board

The responsibilities of the Payments System Board are set out in the Reserve Bank Act. In particular, the Act requires the Board to ensure, within the limits of its powers, that the Reserve Bank's payments system policy is directed to the greatest advantage of the people of Australia and that its related powers are exercised in such a way that, in the Board's opinion, will best contribute to:

- controlling risk in the financial system
- promoting the efficiency of the payments system
- promoting competition in the market for payment services, consistent with the overall stability of the financial system.

The Payments System Board also has responsibility to ensure that the powers and functions of the Bank under Part 7.3 of the *Corporations Act 2001* (dealing with licensing of clearing and settlement facilities) are exercised in a way that will best contribute to the overall stability of the financial system.

The Payments System Board issues a separate annual report.

Conduct of Reserve Bank Board Members

On appointment to the Reserve Bank Board, each member is required under the Reserve Bank Act to sign a declaration to maintain confidentiality in relation to the affairs of the Board and the Reserve Bank.

Members must comply with their statutory obligations as officials of the Reserve Bank, including those set out in the PGPA Act. Members' obligations under the PGPA Act include, but are not limited to, obligations to exercise their powers and discharge their duties with care and diligence, honestly, in good faith and for a proper purpose. Members must not use their position, or any information obtained by virtue of their position, to benefit themselves or any other person, or to cause detriment to the Reserve Bank or any other person.

In order for members to discuss and decide monetary and financial stability policies, notwithstanding any material personal interest in the outcome, the Reserve Bank Act requires them to furnish a confidential disclosure of material personal interests to the Treasurer annually and, during the year, to notify any substantial change since their most recent annual disclosure. Members must declare to the other members of the Reserve Bank Board any material personal interest they have in a matter relating to the affairs of the Board other than monetary policy and financial stability. Members may give standing notice to other members outlining the nature and extent of a material personal interest in such matters.

A Code of Conduct for Reserve Bank Board members supplements these statutory requirements and imposes obligations on members that are designed to ensure that members observe the highest possible standards of ethical conduct. The Code of Conduct, which is available on the Reserve Bank's website, addresses a range of matters including conflicts of interest and restrictions on undertaking, or being involved in, financial transactions of certain types at certain times. Following a review of the Code of Conduct by the Board in June 2018, some minor drafting changes were agreed.

Audit Committee

The Audit Committee is constituted as a subcommittee of the Reserve Bank Board. Its primary objective is to assist the Governor and the Board in fulfilling certain obligations in terms of the Reserve Bank Act and the PGPA Act. In particular, the Audit Committee assists the Governor and the Board in relation to:

- preparing the annual report, including a report of operations, a performance statement and the financial statements
- establishing and maintaining appropriate systems of internal control
- establishing and maintaining appropriate systems of risk oversight and management.

Audit Committee Meetings – 2017/18
Attendance by members

	No. of meetings attended	No. of meetings eligible to attend
John Akehurst[(a)(b)]	1	1
Sandra Birkensleigh	4	4
Rahoul Chowdry[(c)]	2	2
Michael Coleman[(d)]	2	2
Kathryn Fagg[(a)(e)]	3	3
Allan Moss[(a)(f)]	3	3

(a) Member of the Reserve Bank Board
(b) John Akehurst's term on the Audit Committee ended on 30 August 2017
(c) Rahoul Chowdry's term on the Audit Committee commenced on 14 February 2018
(d) Michael Coleman's term on the Audit Committee ended on 13 February 2018
(e) Kathryn Fagg's term on the Audit Committee ended on 6 May 2018
(f) Allan Moss's term on the Audit Committee commenced on 31 August 2017
Source: RBA

Membership of the Audit Committee is comprised of two non-executive members of the Reserve Bank Board, one of whom chairs the committee, and two external members, typically former senior audit partners of major accounting firms with extensive experience in auditing in the finance sector. Attendance by members at meetings of the Audit Committee during 2017/18 is shown below and members' qualifications and experience are provided on pages 27–29.

Consistent with contemporary governance standards, no Reserve Bank executive is a member of the Audit Committee. Representatives of the Bank's internal and external auditors participate in meetings as appropriate at the invitation of the chair. The Deputy Governor attends meetings of the committee on a regular basis as the chief representative of the Bank's management. Other senior Bank executives attend meetings of the committee on a regular basis or as required.

During 2017/18, the Audit Committee met on four occasions. At its July 2018 meeting, the committee considered the draft consolidated financial statements for the Reserve Bank for the year ended 30 June 2018 and agreed that the statements be presented to the Governor and the Reserve Bank Board with its endorsement. The committee meets at least annually with the external auditors without management present; in respect of 2017/18, this occurred immediately following the July 2018 meeting.

Remuneration Committee

The Remuneration Committee of the Reserve Bank Board is established in terms of section 24A of the Reserve Bank Act to recommend to the Board 'terms and conditions relating to the remuneration and allowances' for the Governor and Deputy Governor. Membership of the committee is drawn from the non-executive members of the Board and comprises Catherine Tanna (Chair), Ian Harper and Carol Schwartz. During 2017/18, the committee met on three occasions.

The offices of Governor and Deputy Governor are Principal Executive Offices in terms of the *Remuneration Tribunal Act 1973*, which provides for the Remuneration Tribunal to determine the applicable remuneration reference rate for these offices. The Remuneration Committee reviews the terms and conditions (including remuneration) applying to the Governor and Deputy Governor annually and recommends adjustments to the Reserve Bank Board for approval, providing that such terms and conditions are consistent with the framework for Principal Executive Offices determined by the Remuneration Tribunal. In accordance with section 21A of the Reserve Bank Act, neither the Governor nor the Deputy Governor takes part in decisions of the Reserve Bank Board relating to the determination or application of any terms or conditions on which either of them holds office.

Remuneration Committee Meetings – 2017/18
Attendance by members

	No. of meetings attended	No. of meetings eligible to attend
Catherine Tanna	3	3
Ian Harper	3	3
Allan Moss[b]	1	1
Carol Schwartz[a]	1	2

(a) Carol Schwartz's term on the Remuneration Committee commenced on 31 August 2017
(b) Allan Moss's term on the Remuneration Committee ended on 30 August 2017
Source: RBA

The Remuneration Committee is also kept informed of the general remuneration arrangements for Reserve Bank staff. The Governor attends meetings of the committee at the invitation of the chair to discuss remuneration matters in the Bank, but not those relating to his own remuneration. The committee communicates with the Remuneration Tribunal as required.

Remuneration and Allowances

Remuneration and travel allowances for the non-executive members of the Reserve Bank Board are set by the Remuneration Tribunal. Remuneration of Board members for their membership of the Audit Committee is determined by the Remuneration Tribunal. The longstanding practice of the Reserve Bank has been to provide the same level of remuneration to members of the Audit Committee who are not also members of the Reserve Bank Board. Membership of the Remuneration Committee is not remunerated.

Induction of Board Members

The induction program assists newly appointed Reserve Bank Board members to understand their role and responsibilities, and provides them with an overview of the Reserve Bank's policy framework and operations. Separate briefing sessions are tailored to meet particular needs or interests of members.

Policy Risk Management Framework and Board Review

Risks associated with the formulation of monetary and payments policies are the direct responsibility of the Reserve Bank Board and the Payments System Board, respectively. The boards review management of these risks periodically as part of their decision-making processes. Operational risks are managed by executives in terms of the Reserve Bank's risk management framework, as discussed in the chapter on 'Risk Management'.

Towards the end of 2017, the Reserve Bank Board conducted its annual review of the key risks inherent in the formulation of monetary policy and the monetary policy risk register and control framework. The Board endorsed modest refinements to the risk register and concluded that the monetary policy risk control framework had continued to operate effectively.

At the same time, the Reserve Bank Board conducted its annual review of its own operation and processes, based on a survey of Board members. It concluded that Board processes were functioning effectively. The Board agreed that the special topics for discussion at several meetings in 2017, which had allowed the Board to spend more time on medium-term issues relevant to monetary policy, had been valuable. The performance of the Board's Audit and Remuneration committees is assessed as part of the annual review of the effectiveness of the Board itself. The most recent review concluded that the committees and their processes were functioning effectively.

Executive Committee

The Executive Committee is the key decision-making committee of the Reserve Bank for matters of a management and/or administrative nature. It is a management committee, whose role is to assist and support the Governor in fulfilling his responsibilities to manage the Bank. The committee, which is chaired by the Governor and comprises the Bank's most senior executives, generally meets weekly. The heads of the Audit, Information and Risk and Compliance departments and the General Counsel attend meetings of the Executive Committee in an advisory capacity.

Risk Management Committee

The Risk Management Committee has responsibility for ensuring that operational and financial risks are identified, assessed and properly managed across the Reserve Bank in accordance with its Risk Management Policy. It is a management committee chaired by the Deputy Governor and comprises senior executives drawn mainly from the operational areas of the Bank. During 2017/18, the Risk Management Committee met on six occasions and kept the Executive Committee and Reserve Bank Board Audit Committee informed of its activities. Details of the Reserve Bank's risk management framework are provided in the chapter on 'Risk Management'.

Note Printing Australia Limited

Note Printing Australia Limited (NPA) is a wholly owned subsidiary of the Reserve Bank operating under a charter reviewed and approved annually by the Reserve Bank Board. NPA's prime function is the efficient and cost-effective production of high-quality and secure Australian banknotes, in accordance with specifications and requirements set by the Reserve Bank. NPA is governed by a board of directors appointed by the Reserve Bank. As at the date of this report, the NPA Board comprised four Reserve Bank executives and one former member of the Reserve Bank Board: Chris Aylmer (Head of Risk and Compliance Department) as Chair; Michelle McPhee (Head of Banking Department); Robert Middleton-Jones (Chief Financial Officer); Greg Johnston (Head of Payments Settlements Department); and Kathryn Fagg, a former member of the Reserve Bank Board. The NPA Board has an Audit and Risk Committee, whose membership comprises Michelle McPhee (Chair), Robert Middleton-Jones and an external member, Alan Beckett, a company director and former senior audit partner of a major accounting firm with extensive experience in the corporate sector, including manufacturing.

More detail about the activities and operational structure of NPA is provided in the chapters on 'Banknotes' and 'Operational Structure'.

Indemnities for Members of Boards and Staff

Members of the Reserve Bank Board and the Payments System Board are indemnified against liabilities incurred by reason of their appointment to the relevant board or by virtue of holding and discharging such office. Indemnities for those members appointed prior to 1 July 2014 were in accordance with section 27M of the *Commonwealth Authorities and Companies Act 1997* (CAC Act), which specified when indemnity for liability and legal costs was not allowed. Indemnities for members appointed after 1 July 2014, when the CAC Act was repealed, have reflected the substance of the previous CAC Act restrictions. A revised form of the indemnity for new members of both boards, which continues to reflect the substance of the previous CAC Act restrictions, was approved by the Reserve Bank Board in March 2017. In December 2017, the Reserve Bank Board approved indemnities being given to members of the Audit Committee who are not also members of the Reserve Bank Board on substantially the same terms as the indemnities given to Board members.

The Reserve Bank has also provided an indemnity in accordance with section 27M of the CAC Act to senior staff of the Bank in relation to liabilities they may incur in the conduct of their duties at the Bank. In relation to events on or after 1 April 2017, the Bank's policy on assistance to staff for legal proceedings applies. This policy applies to all staff, not only senior staff, and is closely based on the rules that apply to the provision of assistance to staff for legal proceedings in non-corporate Commonwealth entities set out in Appendix E to the *Legal Services Directions 2017*.

Certain other indemnities given prior to 1 July 2014 in accordance with section 27M of the CAC Act continue. These indemnities were provided by the Reserve Bank to current and former senior staff and Reserve Bank Board members who, at the request of the Bank, are serving on the board of Note Printing Australia Limited or formerly served on that board or the board of CCL Secure Pty Limited (formerly Innovia Security Pty Ltd and, prior to that, Securency International Pty Ltd).

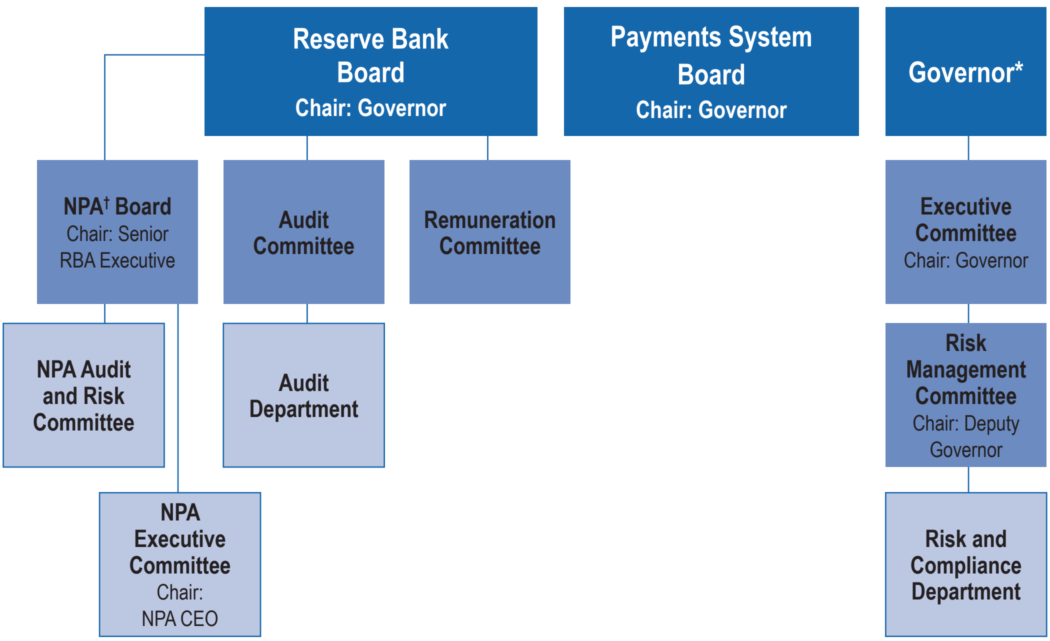
As the Reserve Bank does not take out directors' and officers' insurance in relation to members of its boards or other officers, no premiums were paid for any such insurance in 2017/18.

Other Policy Matters

As part of the governance arrangements to assist the Reserve Bank Board discharge its obligations in relation to the Reserve Bank's policies other than monetary policy, the Governor reports annually to the Board on the process of review and implementation of the key Reserve Bank policies that are determined and managed by the Governor. This report includes information on compliance arrangements. An annual report covering matters relating to work health and safety in the Bank is also presented to the Board. The reports for 2017/18 were provided to the Board at its August 2018 meeting.

Reserve Bank of Australia Governance Structure

August 2018



† Note Printing Australia Limited

* Under section 12 of the *Reserve Bank Act 1959*, the Governor is responsible for managing the Bank and under section 7A of the Reserve Bank Act, the Governor is the accountable authority of the Bank for the purposes of the *Public Governance, Performance and Accountability Act 2013*.

Reserve Bank Board

The Reserve Bank Board comprises nine members: the Governor (Chair), Deputy Governor (Deputy Chair), Secretary to the Treasury (ex officio member) and six other non-executive members appointed by the Treasurer. Further to the legislative requirements, and in recognition of their responsibility to uphold the integrity of the Board and the Reserve Bank, members have adopted a Code of Conduct.

There were two retirements from the Reserve Bank Board in 2017/18, John Akehurst in late August 2017 and Kathryn Fagg in early May 2018. Tributes by the Board to Mr Akehurst and Ms Fagg recorded at their final meetings are shown on pages 24 and 25 respectively. In July 2018, John Fraser resigned from his position as Secretary to the Treasury and thus retired from the Board. Philip Gaetjens was appointed as his successor. A tribute by the Board to Mr Fraser is shown on page 26.

Information about members of the Reserve Bank Board Audit Committee is shown on pages 27–29.

August 2018

Philip Lowe

BCom (Hons) (UNSW), PhD (MIT)

Governor and Chair

Governor since 18 September 2016
Present term ends 17 September 2023

Philip Lowe was Deputy Governor from February 2012 until his appointment as Governor took effect in September 2016. Prior to that, he held various senior positions at the Reserve Bank, including Assistant Governor (Economic) and Assistant Governor (Financial System), where he was responsible for overseeing economic and policy advice to the Governor and Reserve Bank Board. He spent two years at the Bank for International Settlements working on financial stability issues. Mr Lowe has authored numerous papers, including on the linkages between monetary policy and financial stability. He is a signatory to The Banking and Finance Oath.

Other roles

Chair – Payments System Board

Chair – Council of Financial Regulators

Chair – Financial Markets Foundation for Children

Chair – Bank for International Settlements Committee on the Global Financial System

Member – Financial Stability Board

Co-Chair – Financial Stability Board Regional Consultative Group for Asia

Member – Trans-Tasman Council on Banking Supervision

Director – The Anika Foundation

Guy Debelle

BEc (Hons) (Adelaide), PhD (MIT)

Deputy Governor and Deputy Chair

Deputy Governor since 18 September 2016
Present term ends 17 September 2021

Prior to his appointment as Deputy Governor, Guy Debelle was Assistant Governor (Financial Markets) from March 2007. In that role he had oversight of the Bank's operations in the domestic and global financial markets. He has also worked at the Australian Treasury, International Monetary Fund and Bank for International Settlements, and he was a Visiting Professor at the Massachusetts Institute of Technology in 2003. Until May 2017, Dr Debelle was Chair of the Bank for International Settlements Foreign Exchange Working Group, which developed the Global Code of Conduct for the Foreign Exchange Market. He is a signatory to The Banking and Finance Oath.

Other roles

Chair – Reserve Bank Risk Management Committee

Mark Barnaba AM

BCom (Hons) (Western Australia), MBA (Harvard)

Non-executive member

Member since 31 August 2017
Present term ends 30 August 2022

Mark Barnaba has extensive experience in finance and commerce, having spent most of his career with McKinsey and Company, both in Australia and overseas, with companies he founded and in several senior executive roles at Macquarie Group. At the time of his retirement from Macquarie Group at the end of August 2017, Mr Barnaba served as Chair and Global Head of Natural Resources for Macquarie Capital. He was co-founder (and previously Co-Executive Chair) of Azure Capital and previously served as the Chair of Western Power, the Black Swan State Theatre Company of WA, the West Coast Eagles Football Club and Alinta Infrastructure Holdings. In 2009, Mr Barnaba was the recipient of the Western Australian Citizen of the Year award in industry and commerce. In 2012, he was awarded an honorary Doctor of Commerce from the University of Western Australia. Mr Barnaba is a Fellow of the Australian Institute of Company Directors.

Other roles

Co-Vice Chair – Fortescue Metals Group Ltd

Chair – Audit and Risk Committee, Fortescue Metals Group Ltd

Chair – The University of Western Australia Business School Board

Adjunct Professor – Investment Banking and Finance, University of Western Australia

Senior Adviser – EY Oceania

Reserve Bank Board committee membership

Chair – Audit Committee

Wendy Craik AM

BSc (Hons) (ANU), PhD (Zoology) (British Columbia)

Non-executive member

Member since 7 May 2018
Present term ends 6 May 2023

Wendy Craik is an independent public policy advisor, particularly on issues related to natural resource management, and has over 25 years' experience in public policy. Senior positions she has held include Commissioner at the Productivity Commission (2009–14), Chief Executive of the Murray-Darling Basin Commission, President of the National Competition Council, Chair of the Australian Fisheries Management Authority, Executive Director of the National Farmers Federation (1995–2000) and Executive Officer of the Great Barrier Reef Marine Park Authority. She has also been a director on a number of boards in the Australian public sector. Dr Craik is a Fellow of the Australian Institute of Company Directors, the Australian Rural Leadership Foundation and the Academy of Technology, Science and Engineering. She was awarded a Centenary Medal in 2001.

Other roles

Chair – Climate Change Authority

Chair – Steering Committee, National Environmental Science Programme Earth Systems and Climate Change Hub

Chair – Steering Committee, National Red Imported Fire Ant Eradication Program – South East Queensland

Chair – NSW Marine Estate Management Authority

Director – Australian Farm Institute

Member – Advisory Board for the Centre for Strategy and Governance

Philip Gaetjens

BA (Hons) (Flinders), Grad Dip (Professional Accounting) (Canberra)

Ex officio member

Secretary to the Treasury

Member since 1 August 2018

Philip Gaetjens was appointed Secretary to the Treasury with effect from 1 August 2018. He has held leadership roles in the Commonwealth and state public sectors, including as Secretary of the New South Wales Treasury between 2011 and 2015, and has served as a senior executive in the Commonwealth Treasury, the Department of the Prime Minister and Cabinet, and the South Australian Department of Treasury and Finance. He was the Chief of Staff to the Treasurer, the Hon Scott Morrison MP, for three years from mid 2015 and Chief of Staff to former Treasurer the Hon Peter Costello AC from March 1997 to December 2007. Mr Gaetjens served as the inaugural Director of the Asia-Pacific Economic Cooperation (APEC) Policy Support Unit in Singapore between 2008 and 2010.

Other roles

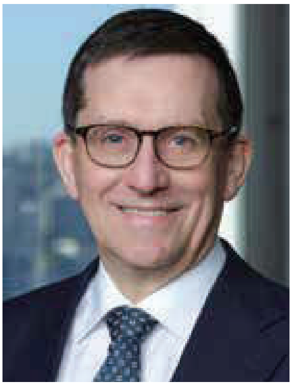
Chair – Global Infrastructure Hub

Ex officio member – Board of Taxation

Member – Council of Financial Regulators

Member – Sir Roland Wilson Foundation

Member – Trans-Tasman Council on Banking Supervision



Ian Harper

BEc (Hons) (Queensland), MEc, PhD (ANU)

Non-executive member

Member since 31 July 2016
Present term ends 30 July 2021

Ian Harper has extensive experience in public policy development, academia and economic consulting. Professor Harper chaired the Competition Policy Review (Harper Review), served as a member of the Financial System Inquiry (the Wallis Inquiry), and was the inaugural Chairman of the Australian Fair Pay Commission. He spent two decades as a Professor at the University of Melbourne – first as the NAB Professor of Monetary and Financial Economics (1988–92), then as the Ian Potter Professor of International Finance (1992–2002) and the Sidney Myer Professor of Commerce and Business Administration (2002–08) at Melbourne Business School. Professor Harper spent eight years as an economic consultant – first as a director of Access Economics Pty Ltd (2008–11) and then as a partner of Deloitte Touche Tohmatsu (2011–16).

Other roles

Dean and Director – Melbourne Business School Limited

Chair – Stipends Committee, Anglican Diocese of Melbourne

Director – Harper Associates Australia

Director – Mt Eliza Graduate School of Business and Government Ltd

Director – Ridley College Limited

Reserve Bank Board committee membership

Member – Remuneration Committee

Allan Moss AO

BA, LLB (Hons) (Sydney), MBA (Harvard)

Non-executive member

Member since 2 December 2015
Present term ends 1 December 2020

Allan Moss has extensive experience in financial markets. He held various positions at Macquarie Bank before becoming Managing Director and Chief Executive Officer of Macquarie Bank Limited and subsequently Macquarie Group Limited from 1993 to 2008. Prior to this, Mr Moss was a director of Hill Samuel Australia and led the team responsible for preparing the submission to the Australian Government to form Macquarie Bank in 1983.

Other roles

Principal – Allan Moss Investments Pty Ltd

Advisory Board member – Eight Investment Partners Pty Ltd

Advisory Board member – Evans and Partners

Reserve Bank Board committee membership

Member – Audit Committee

Carol Schwartz AM

BA, LLB, MBA (Monash)

Non-executive member

Member since 14 February 2017
Present term ends 13 February 2022

Carol Schwartz has extensive experience in business, property, the arts and community organisations. Past high-level leadership roles, including a portfolio of diverse board appointments, have spanned the business, government, arts, health and community sectors. In 2007, Mrs Schwartz was awarded an Order of Australia for her service to business and commerce and her support for health promotion organisations, preservation of historic buildings and the arts. She received the Centenary Medal in 2001 in recognition of her outstanding service as a leading business executive and committee participant. Mrs Schwartz is a Fellow of the Australian Institute of Company Directors.

Other roles

Founding Chair – Women's Leadership Institute Australia

Chair – Creative Partnerships Australia

Chair – Our Community

Director – Qualitas Property Partners

Director – Stockland

Director – Trawalla Group

Reserve Bank Board committee membership

Member – Remuneration Committee

Catherine Tanna

LLB (Queensland)

Non-executive member

Member since 30 March 2011
Present term ends 29 March 2021

Catherine Tanna has extensive experience in the resources sector with BG Group, Royal Dutch Shell and BHP. She held senior executive roles with responsibility for liquefied natural gas, gas transmission and power-generation businesses across Africa, North Asia, Russia, North America, Latin America and Australia. From April 2012 to the end of June 2014, Ms Tanna was Chairman of BG Australia. She is a member of Chief Executive Women.

Other roles

Managing Director – EnergyAustralia Holdings Ltd

Board Member – Business Council of Australia

Reserve Bank Board committee membership

Chair – Remuneration Committee

Retirements from the Board

John Akehurst retired from the Board on 30 August 2017

Kathryn Fagg retired from the Board on 6 May 2018

John Fraser retired from the Board on 31 July 2018

John Akehurst

MA (Oxon)

Non-executive member

Member from 31 August 2007 to 30 August 2017

John Akehurst has had extensive experience in the oil and gas industry. He held a number of engineering and management positions with Royal Dutch Shell (1976–96) and as CEO of Woodside Petroleum Ltd (1996–2003). Mr Akehurst is a former chairman of Alinta Ltd and Coogee Resources Ltd and a former director of CSL Ltd, Oil Search Ltd and the University of Western Australia Business School. Mr Akehurst is a Fellow of the Institution of Mechanical Engineers.

Other roles (as at 30 August 2017)

Chair – National Centre for Asbestos Related Diseases

Chair – Transform Exploration Pty Ltd

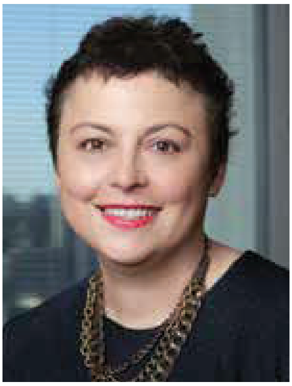
Director – Origin Energy Limited

Reserve Bank Board committee membership

Chair – Audit Committee

Resolution passed by the Reserve Bank Board – 1 August 2017

On the occasion of his final meeting, members paid tribute to John Akehurst's decade of public service on the Board. On behalf of all members, the Governor expressed appreciation for Mr Akehurst's incisive contribution to the Board's deliberations. He applauded Mr Akehurst's constructive and probing style in contributing to the pragmatic conduct of monetary policy, drawing on his extensive experience in the resources and energy sectors. The Governor also thanked Mr Akehurst for chairing the Reserve Bank Board Audit Committee for four years and for his strong support for the internal audit function of the Bank. Members thanked Mr Akehurst for his service to the Bank and the nation and wished him well in the future.



Kathryn Fagg

BE (Hons) (Queensland), MCom (Hons) (UNSW)

Non-executive member

Member from 7 May 2013 to 6 May 2018

Kathryn Fagg has broad experience across a range of industries, including logistics, manufacturing, resources, banking and professional services, having worked in senior executive roles at Linfox, BlueScope Steel and the ANZ Banking Group. Earlier, she worked at McKinsey & Company after commencing her career as a petroleum engineer with Esso Australia. She has led businesses in Australia, New Zealand and Asia. Ms Fagg is President of Chief Executive Women and a Fellow of the Australian Academy of Technology and Engineering. She was awarded a Doctor of Business, *honoris causa* by the University of New South Wales Business School in November 2015, and a Doctor of Chemical Engineering, *honoris causa* by the University of Queensland in December 2016.

Other roles (as at 6 May 2018)

Chair – Breast Cancer Network Australia

Chair – Melbourne Recital Centre

Director – Boral Limited

Director – Djerriwarrh Investments Limited

Director – Incitec Pivot Limited

Director – Note Printing Australia Limited

Reserve Bank Board committee membership

Chair – Audit Committee

Resolution passed by the Reserve Bank Board – 1 May 2018

On the occasion of her final meeting, members paid tribute to Kathryn Fagg's five years of public service on the Board. On behalf of all members, the Governor expressed appreciation for Ms Fagg's contribution to the Board's deliberations, drawing on her extensive experience in a wide range of industries, and applauded her constructive and collegial style. The Governor thanked Ms Fagg for being a member of the Reserve Bank Board Audit Committee since the end of 2015, including as Chair for the most recent nine months. He thanked Ms Fagg for her strong support for the internal audit function of the Bank and the Bank's staff more generally. The Governor also acknowledged Ms Fagg's role as the Board's representative on the Note Printing Australia Limited Board since early 2017, in which she had supported the company in achieving high standards and helped to mentor other directors. Members thanked Ms Fagg for her service to the Bank and the nation and wished her well in the future.

John Fraser

BEc (Hons) (Monash)

Ex officio member

Secretary to the Treasury

Member from 15 January 2015 to 31 July 2018

John Fraser was Secretary to the Treasury from January 2015 to July 2018. He was Chairman and CEO of UBS Global Asset Management from late 2001 to 2013, based in London. During this time, he was also a member of the UBS Group Executive Board and Chairman of UBS Saudi Arabia. In 2014, Mr Fraser remained as Chairman of UBS Global Asset Management, Chairman of UBS Saudi Arabia and Chairman of UBS Grocon Real Estate. Prior to joining UBS and its predecessor organisations in 1993, he served for over 20 years with the Australian Treasury, including as Deputy Secretary (Economic) from 1990 and postings at the International Monetary Fund and as Minister (Economic) at the Australian Embassy in Washington, DC. Mr Fraser was a member of the ASX Board from 1998 to 2002 and Chairman of Victorian Funds Management Corporation from 2009 to early 2015. In 2013, Mr Fraser was awarded an honorary Doctor of Laws by Monash University and in 2015 was appointed an Honorary Professor at Durham University (UK).

Resolution passed by the Reserve Bank Board – 7 August 2018

Members paid tribute to John Fraser's three-and-a-half years of public service on the Board. On behalf of all members, the Governor expressed appreciation for Mr Fraser's contribution to the Board's deliberations, drawing on his extensive experience in both financial markets and economic policymaking. The Governor observed that Mr Fraser had been a strong supporter of the Reserve Bank and the Board. Members acknowledged Mr Fraser's service to the Bank and the nation.

Reserve Bank Board Audit Committee

Membership of the Audit Committee comprises two non-executive members of the Reserve Bank Board, one of whom chairs the committee, and two external members, typically former senior audit partners of major accounting firms with extensive experience in auditing in the finance sector.

The retirement of John Akehurst from the Reserve Bank Board on 30 August 2017 led to Kathryn Fagg becoming Chair of the Audit Committee until the end of her term on the Board on 6 May 2018. Allan Moss, who succeeded Mr Akehurst as a member of the committee, was Interim Chair from 7 May until 7 August 2018. Mark Barnaba became a member of the committee on 23 July 2018 and assumed the Chair on 8 August.

In mid February 2018, Rahoul Chowdry succeeded Michael Coleman as an external member of the Audit committee. Mr Coleman, who completed a six-year term on the committee, is a company director and former senior audit partner of a major accounting firm. At the final meeting attended by Mr Coleman in October 2017, the Chair, on behalf of all committee members, paid tribute to the balanced and constructive contribution Mr Coleman had made to the work of the committee, drawing on his extensive background and experience in the finance sector and auditing.

Mark Barnaba AM

Chair

Member since 23 July 2018
Term ends 30 August 2022

See page 17 for Mr Barnaba's professional details.

Sandra Birkensleigh

BCom (UNSW)

Member

Member since 9 September 2015
Term ends 8 September 2020

Sandra Birkensleigh has extensive experience in financial services, with a particular focus on risk management, compliance and corporate governance. Ms Birkensleigh's career includes 24 years at PricewaterhouseCoopers, where she was formerly a Global Lead for Governance Risk & Compliance, a National Lead Partner Risk and Controls Solutions, and a Service Team Leader for Performance Improvement. Ms Birkensleigh holds several directorships and is chair of the audit committees for most of the organisations listed below. She is a qualified chartered accountant, a member of the Institute of Chartered Accountants in Australia and New Zealand and a member of the Australian Institute of Company Directors.

Other roles

Non-Executive Director – Auswide Bank Limited

Non-Executive Director – Horizon Oil Limited

Non-Executive Director – MLC (Insurance) Limited

Non-Executive Director – National Disability Insurance Agency

Non-Executive Director – 7-11 Holdings Limited and its subsidiaries

Non-Executive Director and Audit Committee Member
– The Tasmanian Public Finance Corporation

Rahoul Chowdry

BCom (Hons) (Calcutta)

Member

Member since 14 February 2018
Term ends 13 February 2023

Rahoul Chowdry has extensive experience in the professional services industry, which enabled him to build a reputation as a leading adviser on governance, regulation and risk to major banks and other large financial institutions in Australia and Canada. Until the end of 2017, Mr Chowdry was the Global Banking and Capital Markets Assurance Leader at PricewaterhouseCoopers and a partner for almost 30 years in the firm's financial services practice. He is a qualified chartered accountant and a fellow of the Institute of Chartered Accountants in Australia and New Zealand and a member of the Institute of Chartered Accountants in England and Wales, and the Institute of Chartered Accountants in Ontario.

Other roles

Partner – MinterEllison Consulting

Allan Moss AO

Member

Member since 31 August 2017
Term ends 1 December 2020

See page 21 for Mr Moss's professional details.

Accountability and Communication

The Reserve Bank is an independent central bank, accountable to the Parliament of Australia. The Bank engages with the Australian Government at a range of levels and seeks to enhance the community's understanding of its responsibilities, policies and actions through a broad communication program.

Relationship with Government

The Reserve Bank is a body corporate distinct from the Commonwealth of Australia. This body corporate, established under the *Commonwealth Bank Act 1911* and continued in existence under the *Commonwealth Bank Act 1945*, was preserved and continued in existence with the name Reserve Bank of Australia under the *Reserve Bank Act 1959*. The Reserve Bank has two boards: the Reserve Bank Board and the Payments System Board. The Governor, Deputy Governor and other members of the Reserve Bank Board are appointed by the Treasurer. Six of the eight members of the Payments System Board, including the Governor, are appointed by the Treasurer, with one member each appointed by the Reserve Bank and the Australian Prudential Regulation Authority.

The Reserve Bank's two boards are afforded operational independence under the Reserve Bank Act to determine and implement the policies of the Bank, as will best contribute to the objectives set out in the Act. In terms of monetary policy, the *Statement on the Conduct of Monetary Policy*, as updated from time to time, has recorded the common understanding of the Governor, as Chair of the Reserve Bank Board, and the government on key aspects of Australia's monetary and central banking policy framework since 1996, as outlined in the chapter on 'Our Role'. The Payments System Board issues its own annual report, which outlines its role and activities.

Accountability and Communication

The Reserve Bank seeks to ensure a high degree of transparency about its activities, goals, decision-making processes and the basis of its policy decisions. Transparency facilitates the Bank's accountability, to accompany its operational independence. Importantly, it also increases the effectiveness of policy decisions by promoting a better understanding of those decisions in the community. There are a number of steps the Bank takes to achieve this transparency, as discussed below.

The Reserve Bank Board has an obligation to inform the government of its monetary and banking policy 'from time to time'. This obligation is discharged mainly by regular contact between the Governor and other senior executives and the Treasurer, who is the Bank's responsible Minister (during 2017/18, the Hon Scott Morrison MP), usually by way of a monthly discussion following Board meetings. The Governor

Photo: CEDA

(Top, from left) Assistant Governor (Financial System) Michele Bullock, Deputy Governor Guy Debelle, Governor Philip Lowe and Assistant Governor (Economic) Luci Ellis at a hearing of the House of Representatives Standing Committee on Economics, Sydney, February 2018; (above) Deputy Governor Guy Debelle addresses the CEDA Mid-year Economic Update, Adelaide, July 2017

(Top) Assistant Governor (Economic) Luci Ellis speaking at an Infrastructure Partnerships Australia Leaders' Luncheon, Sydney, June 2018; (above left) Head of Domestic Markets Department Marion Kohler speaking at the Australian Securitisation Forum, Sydney, November 2017; (above right) Assistant Governor (Financial Markets) Christopher Kent speaking at the Debt Capital Markets Summit, Sydney, March 2018

Assistant Governor (Financial System) Michele Bullock answering questions from the House of Representatives Standing Committee on Economics, Sydney, February 2018

also meets regularly with the House of Representatives Economics Committee and the Senate Economics Committee. The Reserve Bank Act sets out a clear process for managing differences of opinion between the Reserve Bank Board and the government on policy matters.

The Reserve Bank is a corporate Commonwealth entity under the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), of which the Governor is the 'accountable authority'. Under section 46 of the PGPA Act, the Governor is responsible for preparation of this annual report and for providing it to the Treasurer for presentation to the Parliament, following approval by the Reserve Bank Board of the Bank's annual financial statements. That approval was given by the Board at its meeting on 7 August 2018.

The House of Representatives Economics Committee has, in its Standing Orders, an obligation to review the annual report of the Reserve Bank and the annual report of the Payments System Board. The committee holds twice-yearly public hearings, at which the Bank presents its views on the economy and financial markets and other matters pertaining to the Bank's operations, and responds to questions from committee members. In 2017/18, the Governor and senior Bank officers attended hearings of this committee for this purpose in Melbourne in August 2017 and in Sydney in February 2018. The committee issued its report on the August 2017 hearing – *Review of the Reserve Bank of Australia Annual Report 2016* (Second Report) – on 11 September 2017. The committee's report on the February 2018 hearing – *Review of the Reserve Bank of Australia Annual Report 2017* (First Report) – was issued on 8 May 2018.

No report on the Reserve Bank was issued in 2017/18 by the Commonwealth Ombudsman, the Office of the Australian Information Commissioner or the Auditor-General, apart from that dealing with the audit of the Bank's annual financial statements.

Regional and industry liaison

The Reserve Bank has staff in four State Offices across Australia, who work with staff in the Sydney Head Office to conduct the Bank's business and community liaison program. These offices are located in Adelaide, Brisbane, Melbourne and Perth. Staff from the Bank meet regularly with businesses, associations and agencies across the country. The liaison program aims to cover all parts of the economy, although greater weight is given to more cyclical industry sectors, which tend to be more responsive to monetary policy. In 2017/18, staff involved in the liaison program conducted around 750 liaison meetings. Staff from the State Offices also regularly visit Tasmania and the Northern Territory, as well as various regional centres, to obtain information on economic conditions outside of Australia's largest cities. In 2017/18, liaison staff visited Ballarat, the Barossa Valley, Bunbury, Cairns, Geraldton, Newcastle, Townsville and Wollongong.

Information from the liaison program provides a valuable complement to available data in forming the Reserve Bank's assessment of developments in the Australian economy. It allows the Bank to develop a more nuanced view of the economy and better understand the factors that are affecting decision-makers and driving economic conditions. It can also be timelier than other sources of data, which is particularly useful when the Bank needs to quickly assess the impact of unusual events on the Australian economy, such as drought, floods and other natural disasters. Importantly, liaison provides an independent source of information that can be used to help the Bank distinguish between signal and noise in official data releases, and identify structural changes in the economy.

In 2017/18, liaison staff visited Ballarat, the Barossa Valley, Bunbury, Cairns, Geraldton, Newcastle, Townsville and Wollongong

In addition to gathering economic intelligence, a key role of the Reserve Bank's State Offices is to represent the Bank in a range of capacities, contributing to a broader understanding of the Bank's work and hearing the views of the community. In 2017/18, staff members in the State Offices gave over 40 presentations to members of the community at schools, business roundtables and regional chambers of commerce. Employees of the Bank also presented overviews of the *Statement on Monetary Policy* to over 400 participants in the liaison program.

The Reserve Bank also continues to convene its Small Business Finance Advisory Panel, which was established in 1993. The panel meets annually to discuss issues relating to the provision of finance and the broader economic environment for small businesses. Membership of the panel is drawn from a range of industries across the country. The panel provides a valuable source of information on financial and economic conditions faced by small businesses. In addition, the Bank hosted two roundtable discussions in 2018 on small business finance, involving entrepreneurs, banks, innovative lenders and the Bank hosted two **roundtable discussions** in 2018 on small business finance, involving **entrepreneurs,** banks, **innovative lenders** and government representatives

government representatives. The participants discussed the challenges faced by small businesses when borrowing, along with a range of ideas for addressing these challenges.

Consultation and other engagement

In carrying out its various responsibilities, the Reserve Bank consults extensively with interested parties. In early 2017, the Bank, as part of the Council of Financial Regulators (CFR) and in collaboration with the Australian Competition and Consumer Commission (ACCC), conducted a consultation in relation to policy guidance regarding arrangements that would support safe and effective competition in cash equity settlement in Australia. After considering the responses received, in September 2017 the

Deputy Governor Guy Debelle speaking at the FINSIA Signature Event: The Regulators, Sydney, September 2017

CFR agencies and ACCC published a policy statement setting out the *Minimum Conditions for Safe and Effective Competition in Cash Equity Settlement in Australia*.

The Reserve Bank maintains ongoing engagement with a wide variety of groups to inform its policy and operational activities. Senior Bank staff meet regularly with representatives of various domestic and international official agencies, business groups and financial market participants to discuss economic and financial developments.

Head of Financial Stability Department Jonathan Kearns speaking at an Aus-China Property Developers, Investors & Financiers event, Sydney, November 2017

During the year in review, senior staff members from the Payments Policy Department participated in a number of industry conferences and public events discussing payments issues. Topics covered included the provision of least-cost routing for card payments, industry efforts to reduce card-not-present fraud, and cryptocurrencies and distributed ledger technology. Staff from Payments Settlements Department continued to conduct regular liaison meetings with Reserve Bank Information and Transfer System (RITS) members and industry groups, such as the Australian Payments Network (AusPayNet). Staff also participated in various industry forums, including AusPayNet's High Value Clearing System Management Committee. In 2017/18, Reserve Bank staff participated actively in the industry's New Payments Platform (NPP) project committees in the lead-up to the public launch of the NPP. Post launch, senior staff from Payments Settlements and Banking departments represent the Bank on NPP operating committees. A senior staff member sits on the board of AusPayNet and another senior staff member sits on the board of NPP Australia Limited, the company established to build and operate the NPP. Participation in these groups and a number of other banking and payments industry forums ensures the Bank remains abreast of developments in these areas and can contribute to innovations in the banking and payments industry. Bank staff closely follow developments in new technologies, including distributed ledger technology, digital currencies and payments-related financial technology (or fintech) more broadly.

The Reserve Bank sponsors, and its International Department provides the secretariat to, the Australian Foreign Exchange Committee (AFXC). Among other things, in 2017/18 the AFXC worked

to promote the adoption of the FX Global Code in the Australian wholesale foreign exchange market. The code is maintained by the Global Foreign Exchange Committee, of which the AFXC is a member committee.

During the year in review, staff from the Note Issue Department also continued to engage extensively in relation to the new banknote series, as discussed in the chapter on 'Banknotes'.

Research

The Reserve Bank publishes the results of longer-term research conducted by staff in the form of Research Discussion Papers (RDPs), which stimulate discussion on policy-relevant issues. The views expressed in RDPs are those of the authors and do not necessarily represent those of the Bank. During 2017/18, 10 RDPs were published on a range of topics in the Bank's areas

(Top) Head of Payments Policy Department Tony Richards speaking at the 2017 Australian Payment Summit, Sydney, December 2017; (above) Governor Philip Lowe addressing the Australian Payment Summit, Sydney, December 2017

Head of Economic Research John Simon (centre) and Reserve Bank Historian Selwyn Cornish (right) at the annual Reserve Bank conference, Sydney, April 2018

of interest, including: housing prices; monetary policy and uncertainty; the term structure of interest rates; and wages. Staff from the Bank also published their research in various external journals and working paper series, including the *Computational Statistics & Data Analysis Journal* and *Journal of International Economics*.

Research undertaken at the Reserve Bank is frequently presented at external conferences and seminars. In 2017/18, Bank staff presented at various conferences and institutions in Australia and overseas, including in Hong Kong SAR, China and Europe.

The Reserve Bank hosts regular conferences, which foster interaction between academics, central bankers and other economic practitioners on topical policy issues. The Bank's annual conference for 2018 titled 'Central Bank Frameworks: Evolution or Revolution?' was held in April 2018 and focused on the experience of inflation targeting by central banks over the past 20 to 30 years. Four Bank staff contributed to papers presented at the conference as authors and co-authors. A volume containing the conference papers and discussions will be published in the second half of 2018. The next annual conference is scheduled for the first half of 2019.

The Reserve Bank also hosted visits in 2017/18 from a number of policymakers from overseas institutions, including the International Monetary Fund, US Federal Reserve banks, the European Central Bank, the Organisation for Economic Co-operation and Development, Sveriges Riksbank, the Bank of England and the Bank of Japan, as well as academics from a range of institutions, including the University of Adelaide, University Carlos III, University of Graz, Harvard University, Indiana University and Texas A&M University. During their visits, these visitors presented seminars, taught short courses and participated in research activities at the Bank.

Public Communication

The Reserve Bank communicates its policy decisions, analysis and information about the Bank's operations through its website, publications, speeches and media releases throughout the year.

Announcements about monetary policy decisions are made shortly after each Reserve Bank Board meeting and minutes are released two weeks after each meeting. A media release is published following each Payments System Board meeting outlining issues discussed at the meeting and foreshadowing any forthcoming documents to be released by the Bank.

The quarterly *Statement on Monetary Policy* provides information about the Reserve Bank's assessment of current economic conditions, both domestic and international, along with the outlook for Australian inflation and output growth. The *Statement* contains a detailed analysis of conditions in the economy and financial markets and describes the outlook for inflation and the economy more generally.

The *Financial Stability Review*, published semiannually, provides a detailed assessment of the condition of Australia's financial system and potential risks to financial stability. In 2017/18, areas of focus included the risk profile of new

Governor Philip Lowe addresses the Australia-China Relations Institute at the University of Technology Sydney, May 2018 housing lending and the resilience of household balance sheets, which improved somewhat over the year, as well as risks in the commercial property market. Developments in overseas markets and related risks are also covered in the *Review*. Key risks noted during the year in review included the risk of a disruptive correction in financial markets in an environment where compensation for risk is very low for many assets, and the risks in the Chinese financial system. The *Review* also reports on international and domestic regulatory developments and the Reserve Bank's involvement, including through the Bank's work with the CFR.

The Reserve Bank's quarterly *Bulletin* contains analysis of a broad range of economic and financial issues as well as aspects of the Bank's operations. During 2017/18, the *Bulletin* contained articles on Australia's neutral interest rate, the labour market (both in Australia and abroad), structural change in the Australian economy over the past 50 years, and the adjustment of the economy to the recent mining investment boom and its subsequent unwinding. Housing access for first-home buyers, the availability of business finance, and a range of aspects of Australia's financial institutions, markets and the Reserve Bank's role in the financial system were examined. There were also educational articles on the transmission of monetary policy and the inflation target in Australia, as well as an introduction to the Bank's new macroeconomic model. Other articles reported on economic and financial developments in China, India and other countries in Asia. The volume of high-denomination banknotes in circulation in Australia, Canada and the United Kingdom, the growing demand for cash in Australia, developments in Australia's ATM industry and trends in global foreign currency reserves were also explored. From March 2018, the *Bulletin* became available in a digital-only format on the Bank's website, publishing insights into the economy and financial system from teams throughout the Bank, as discussed further below.

During 2017/18, the Governor, Deputy Governor and other senior officers gave 51 public speeches on various topics. Questions were taken after almost all speeches. Senior staff also participated in a number of public panel discussions. In addition to communicating the Reserve Bank's analysis of domestic and global economic and financial developments, and how they have influenced monetary policy decisions, speeches covered a review of Australia's inflation-targeting framework since its inception, a retrospective on central bank independence, structural change in the Australian economy and why the Bank does not currently see a case for issuing a digital form of the Australian dollar. Senior officers also addressed, among other things, the decline in economics enrolments in Australian high schools,

During 2017/18, the Governor, Deputy Governor and other senior officers gave 51 public speeches

Australia's deepening economic relationship with China, the FX Global Code and interest rate benchmark reform, as well as fast payments, merchant payment costs and least-cost payment routing in Australia. Audio files of these speeches, the associated question and answer sessions and panel discussions were published on the Bank's website to facilitate transparency and accountability.

To assist further with public understanding of the Reserve Bank's role, in June 2018 the second event in the new Teacher Immersion Series was held, providing secondary school economics teachers with the opportunity to hear directly from senior Bank staff. See the chapter on 'Community Engagement' for further details.

The Reserve Bank publishes information in both electronic and hard copy formats, though access to information is now mostly online. Followers of the Bank's Twitter account, @RBAInfo, have grown in number to over 37,000, while the number of subscribers to the conventional email alert service has continued to fall (to less than 10,000 at the end of June 2018). Visitors to the Bank's website also made use of the RSS feeds, which allowed them to receive alerts about updates to selected data, media releases, speeches, research papers and other publications (including those related to Freedom of Information requests).

The Reserve Bank's website has continued to evolve with new and refreshed content. In March 2018, the Bank relaunched the *Bulletin* as an online-only publication, making it easier to share and search articles. The new format is more accessible and will involve a greater use of visual communications to cater to a broad readership. A new education section of the website has been created in support of the Bank's public education program. It contains a suite of resources about economic concepts and the Australian economy that have been designed to support students and educators, as well as being relevant for a more general audience. This site has been popular with school students and teachers (with over 100,000 page views and downloads during 2017/18). The Bank's website, and the Banknotes microsite in particular, has continued to be used to communicate information about the new banknote series being issued by the Bank; in 2017/18, the new $10 banknote entered general circulation and the design of the new $50 banknote was revealed.

In March 2018, the Bank relaunched the *Bulletin* as an online-only publication … to cater to a broad readership

The Reserve Bank of Australia Museum website also continued to evolve with new content in 2017/18. The online exhibition *From Bank to Battlefield*, which was launched in 2014 to mark the centenary of the commencement of World War I, was expanded in 2017/18 to mark the

Head of Information Department Jacqui Dwyer speaking at a Teacher Immersion Event, Sydney, June 2018

centenaries of the defining Western Front battles of 1918.[1] This exhibition pays tribute to Bank staff who served in World War I and to those who helped establish central banking in Australia at that time. Another online exhibition, *Make Your Money Fight!*, was launched on the Museum website during 2017/18, exploring how the Australian Government addressed the economic challenges faced by Australia during World War II and the role of Australia's central bank.[2] See the chapter on 'Community Engagement' for further details.

A new education section of the website … contains a suite of resources about economic concepts and the Australian economy

1 See <https://museum.rba.gov.au/exhibitions/from-bank-to-battlefield>.

2 See <https://museum.rba.gov.au/exhibitions/make-your-money-fight>.

Operational Structure

The Reserve Bank is managed by the Governor, Philip Lowe*, and the Deputy Governor, Guy Debelle*†. It has five operational groups – Business Services Group, Corporate Services Group, Economic Group, Financial Markets Group and Financial System Group – and six supporting departments.

Business Services Group

Assistant Governor: Lindsay Boulton*†

Business Services Group comprises Banking Department, Note Issue Department and Payments Settlements Department.

Banking Department

Head: Michelle McPhee

Deputy Head: Bipan Arora, Stephanie Connors

Banking Department provides a range of banking services to Australian Government departments and agencies as well as a number of overseas central banks and official institutions. The services broadly comprise two activities – management of the government's core accounts and transactional banking. Sydney-based staff are responsible for the direction, administration and development of the department's work, while the day-to-day interaction with customers is largely managed by staff in the Canberra Branch.

Note Issue Department

Head: Melissa Hope

Deputy Head: James Holloway

Note Issue Department is responsible for all aspects of the banknote lifecycle from research into and development of new banknote designs and security features, to the supply of high-quality banknotes to meet the community's needs. The department works with the Reserve Bank's wholly owned subsidiary, Note Printing Australia Limited (NPA), to design and produce the banknotes. (See below for information about the activities, governance and structure of NPA.) The department manages laboratories to assess new and used banknotes, develop new security features and assess counterfeits detected in circulation. It operates the highly secure National Banknote Site for the storage, processing and distribution of banknotes. The department also has an extensive public engagement program with commercial banks, retailers, cash-in-transit companies, law enforcement agencies and banknote equipment manufacturers. Staff participate in a number of international groups as part of the Bank's efforts to address the risks posed by counterfeiters.

Payments Settlements Department

Head: Greg Johnston

Deputy Head: David Emery (Acting), Peter Gallagher

Payments Settlements Department is responsible for the settlement of high-value payments and interbank obligations arising from the conduct of Exchange Settlement Accounts and the

Reserve Bank's own trading activities, as well as operation of the Reserve Bank Information and Transfer System (RITS), Australia's real-time gross settlement system (RTGS). RITS also includes the Fast Settlements Service, which Payments Settlements Department operates on an RTGS basis 24 hours a day, seven days a week for settlement of New Payments Platform transactions. Services are also provided for the clearing and settlement of low-value payments, such as those arising from cheque and direct entry transactions.

Corporate Services Group

Assistant Governor: Susan Woods*†

Corporate Services Group is responsible for the delivery of technology systems and infrastructure, and facilities management services to support the day-to-day operations of the Bank. It comprises the Information Technology Department and Workplace Department.

Information Technology Department

Chief Information Officer: Gayan Benedict†

Deputy Head: Andrew Pade (Acting), Peter Speranza

Information Technology Department is responsible for developing and maintaining reliable, resilient and secure information technology functions to support the Reserve Bank's policy, operational and corporate functions. In fulfilling these responsibilities, the department delivers and maintains the Bank's technology systems and infrastructure, provides ongoing system quality assurance, and maintains the Bank's cyber-security defensive controls. The department also supports technology planning for the Bank, which includes catering for emerging and future technology requirements.

Workplace Department

Head: Bruce Harries

Deputy Head: Ed Jacka

Workplace Department is responsible for management of the Reserve Bank's physical assets, the maintenance of its properties and building infrastructure, and the delivery of workplace services. Key activities include workspace fit-outs, engineering, physical and protective security, catering, cleaning, procurement and strategic vendor management, and environmental risk management for the effective operation of the Bank and the safety, security, amenity and wellbeing of staff.

Economic Group

Assistant Governor: Luci Ellis*

Economic Group is responsible for analysis of economic trends, both domestic and overseas, forecasting and research relevant to the framing of policy in a number of areas of the Reserve Bank's responsibility. It consists of Economic Analysis Department and Economic Research Department.

Economic Analysis Department

Head: Alexandra Heath

Deputy Head: Lynne Cockerell, Merylin Coombs, Michael Plumb

Economic Analysis Department monitors and forecasts trends in the domestic and international economies, provides regular advice on these developments and monetary policy to the Governors and the Reserve Bank Board, contributes to the work of various external bodies, maintains contacts with relevant external analysts, undertakes applied research and prepares reports for publication.

The Reserve Bank maintains four State Offices to conduct economic liaison across Australia. These offices hold regular discussions with individual firms and organisations in both the private and public sectors, and assist with communication to the wider community.

The Bank also has an office in Beijing, which is responsible for monitoring Chinese economic and financial developments as well as maintaining relationships with government and private sector entities in China.

Economic Research Department

Head: John Simon

Deputy Head: Vacant

Economic Research Department undertakes longer-term research into issues relevant to the Reserve Bank's responsibilities, including research on the Australian economy, monetary policy, financial stability, the payments system and the operation of financial markets. Results of this research are published in the Research Discussion Paper series. The department organises a major annual conference and an annual research workshop. In addition, it organises a program of internal seminars, hosts a number of invited visitors each year and is responsible for administering a comprehensive library service for the Bank.

Financial Markets Group

Assistant Governor: Christopher Kent*†

Financial Markets Group is responsible for implementing the Reserve Bank's operations in domestic and foreign exchange markets, monitoring developments in financial markets and coordinating the Bank's relationships with international institutions. The group consists of Domestic Markets Department and International Department.

Domestic Markets Department

Head: Marion Kohler

Deputy Head: Ellis Connolly

Domestic Markets Department is responsible for the Reserve Bank's operations in the domestic money and bond markets. The department analyses developments in domestic financial markets, including the cost and availability of finance through financial intermediaries and capital markets, and provides regular advice to the Governors and the Reserve Bank Board on these issues.

International Department

Head: Bradley Jones

Deputy Head: Matthew Boge, David Jacobs

International Department is responsible for the Reserve Bank's foreign exchange operations, the investment of international reserve holdings of gold and foreign exchange, and the provision of regular advice on developments in international financial markets to the Governors and the Reserve Bank Board. The department is also responsible for maintaining the Bank's relations with a number of major international institutions.

The Representative Offices in London and New York come under the umbrella of the Financial Markets Group. The European Representative Office in London maintains liaison with central banks and other institutions and authorities in Europe, including the Bank for International Settlements and the Organisation for Economic Co-operation and Development. The New York Representative Office performs similar functions in North America. Both of these offices monitor economic and financial developments in their respective local markets, and assist with foreign exchange operations and investment of international reserves.

The Financial Market Group's Business Support Services area provides project delivery, market data management and operational support services, in conjunction with the Information Technology Department, for the Reserve Bank's investment and trading operations.

Financial System Group

Assistant Governor: Michele Bullock[*]

Financial System Group supports the Reserve Bank's broad responsibilities for financial system stability and its role in payments system oversight and regulation. The group consists of Financial Stability Department and Payments Policy Department.

Financial Stability Department

Head: Jonathan Kearns

Deputy Head: Darren Flood, David Orsmond

Financial Stability Department analyses the implications for financial system stability of developments in the macroeconomy, financial markets and the financial sector more generally, including areas such as patterns of financial intermediation, financial products and risk management techniques. The department provides advice on these issues to the Governors and the Reserve Bank Board and supports the Reserve Bank's representation on bodies such as the Council of Financial Regulators, the Financial Stability Board and the Basel Committee on Banking Supervision. It is responsible for producing the Bank's semiannual *Financial Stability Review*.

Payments Policy Department

Head: Tony Richards

Deputy Head: Sarah Harris, Chris Thompson

Payments Policy Department is responsible for developing and implementing the Reserve Bank's payments system policy. It provides analysis and advice to the Payments System Board on improving the safety, efficiency and competitiveness of the payments system. The department is also responsible for oversight of Australia's high-value payments, clearing and settlement facilities, and represents the Bank on the Committee on Payments and Market Infrastructures of the Bank for International Settlements.

Audit Department

Head: Darryl Ross[†‡]

Audit Department is responsible for conducting independent appraisals of the Reserve Bank's activities, functions and operations to ensure that an adequate framework of internal control has been established and is operating effectively. The Head of Audit Department reports to the Deputy Governor and the Chair of the Reserve Bank Board Audit Committee.

Finance Department

Chief Financial Officer: Robert Middleton-Jones[*†]

Financial Controller: Sam Tomaras

Finance Department is responsible for the Reserve Bank's financial statements and taxation reporting obligations, prepares the Bank's budget and provides a range of support services, including corporate payments, payroll and travel. Finance also manages the Bank's Enterprise Portfolio Management Office.

Human Resources Department

Head: Michael Andersen[*†]

Human Resources Department provides a range of people-related services to support the Reserve Bank in maintaining a productive and engaged workforce. This includes sourcing high-quality staff as well as implementing policies and programs that cover employment conditions, reward, development, diversity and workplace health and safety.

Information Department

Head: Jacqui Dwyer[†‡]

Information Department is responsible for the Reserve Bank's records management system, information governance and its archives, and for facilitating public access to Bank records.

It also manages the Reserve Bank of Australia Museum and a program of public education, with particular focus on supporting students and educators.

Risk and Compliance Department

Head: Chris Aylmer†‡

Risk and Compliance Department supports the consistent and effective application of the Reserve Bank's framework for managing risk, both at the enterprise level and for individual business units. It assists departments to identify, understand and manage their compliance obligations. It also monitors and reports on portfolio risks and compliance with respect to the Bank's operations in financial markets. The department is responsible for secretariat and coordination services and advice for the Risk Management Committee. The Head of Risk and Compliance Department reports to the Deputy Governor.

Secretary's Department

Secretary: Anthony Dickman*

Deputy Secretary: Andrea Brischetto

General Counsel: Catherine Parr†‡

Deputy General Counsel: Peter Jones

Secretary's Department provides secretariat and coordination services and advice on governance matters for the Governors, the Reserve Bank Board and its Audit and Remuneration committees, the Payments System Board and the Executive Committee. Secretary's Department is responsible for the Reserve Bank's communication, including preparing and publishing Reserve Bank information, maintaining the Bank's websites and handling enquiries from the media and general public. In addition, the department provides legal services to the Bank through the General Counsel (who reports directly to the Deputy Governor), coordinates a range of contacts with government, the parliament, other central banks and international organisations, and arranges programs for international visitors.

Wholly owned subsidiary: Note Printing Australia Limited (NPA)

NPA is a wholly owned subsidiary of the Reserve Bank that produces banknotes. NPA operates under a charter reviewed and approved annually by the Reserve Bank Board. See the chapter on 'Governance' for further detail about the governance of NPA.

NPA's prime function is the efficient and cost-effective production of high-quality and secure Australian banknotes, in accordance with specifications and requirements set by the Reserve Bank. NPA also undertakes other activities, including developing and producing passports for the Department of Foreign Affairs and Trade, producing banknotes for other issuing authorities and producing other security products.

NPA's Executive Committee, comprising its Chief Executive Officer and the heads of NPA's eight business areas, is responsible for the operational and administrative management of NPA. As at the end of June 2018, NPA employed 244 permanent staff.

The financial accounts of NPA are consolidated with those of the Reserve Bank.

* Member of Executive Committee
† Member of Risk Management Committee
‡ Advisor to Executive Committee

Reserve Bank of Australia Operational Structure

August 2018

Governor
Philip Lowe

Deputy Governor
Guy Debelle

Business Services

Assistant Governor
Lindsay Boulton

- Banking Department
  - **Head** *Michelle McPhee*
  - **Deputy Head** *Bipan Arora*, *Stephanie Connors*
- Note Issue Department
  - **Head** *Melissa Hope*
  - **Deputy Head** *James Holloway*
- Payments Settlements Department
  - **Head** *Greg Johnston*
  - **Deputy Head** *David Emery (Acting)*, *Peter Gallagher*

Corporate Services

Assistant Governor
Susan Woods

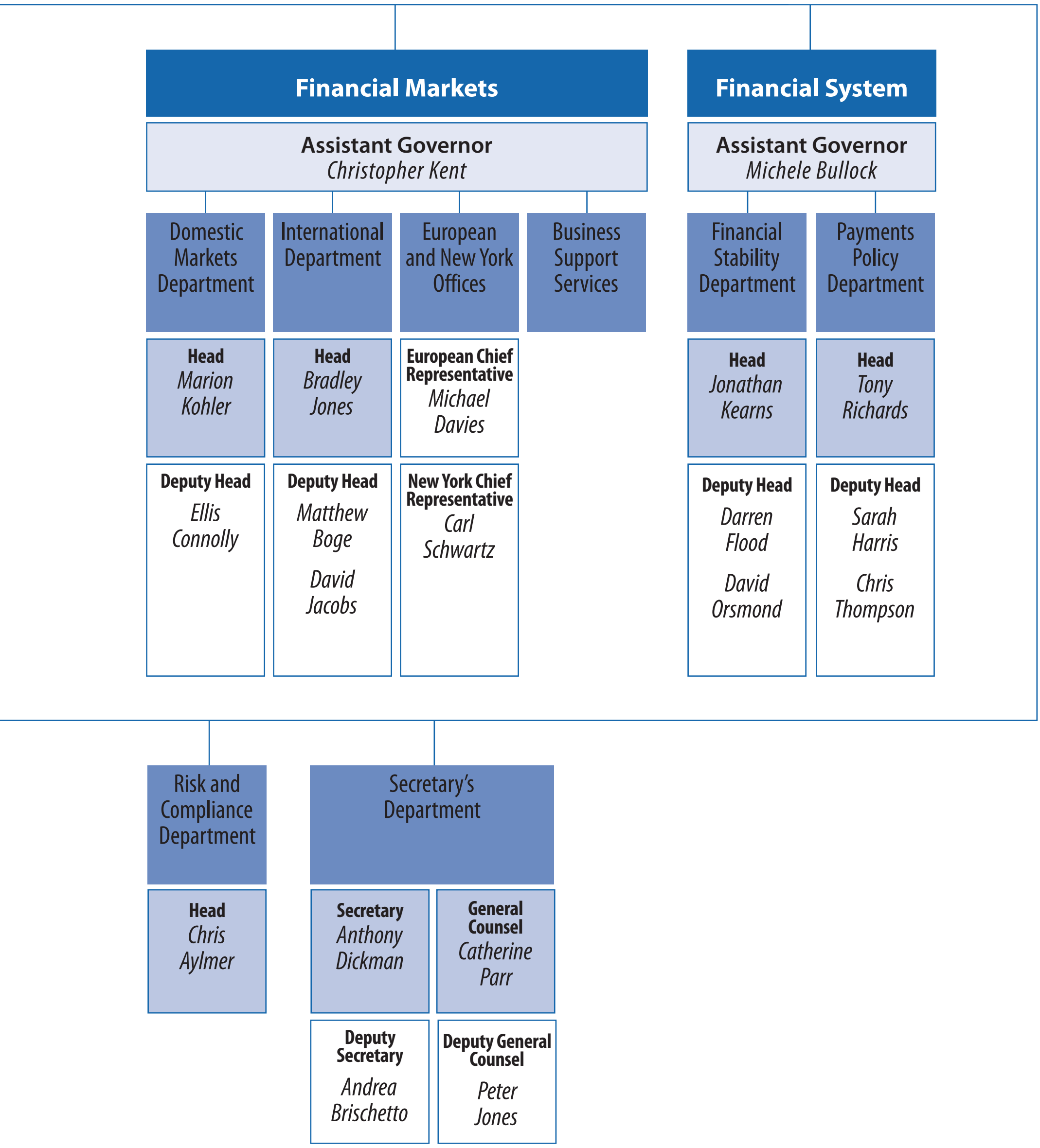
- Workplace Department
  - **Head** *Bruce Harries*
  - **Deputy Head** *Ed Jacka*
- Information Technology Department
  - **Chief Information Officer** *Gayan Benedict*
  - **Deputy Head** *Andrew Pade (Acting)*, *Peter Speranza*

Economic

Assistant Governor
Luci Ellis

- Economic Analysis Department
  - **Head** *Alex Heath*
  - **Deputy Head** *Lynne Cockerell*, *Merylin Coombs*, *Michael Plumb*
- Economic Research Department
  - **Head** *John Simon*
  - **Deputy Head** *Vacant*

- Audit Department
  - **Head** *Darryl Ross*
- Finance Department
  - **Chief Financial Officer** *Robert Middleton-Jones*
  - **Financial Controller** *Sam Tomaras*
- Human Resources Department
  - **Head** *Michael Andersen*
- Information Department
  - **Head** *Jacqui Dwyer*


Financial Markets
Assistant Governor
Christopher Kent
Domestic Markets Department
International Department
European and New York Offices
Business Support Services
Head
Marion Kohler
Head
Bradley Jones
European Chief Representative
Michael Davies
Deputy Head
Ellis Connolly
Deputy Head
Matthew Boge
David Jacobs
New York Chief Representative
Carl Schwartz
Financial System
Assistant Governor
Michele Bullock
Financial Stability Department
Payments Policy Department
Head
Jonathan Kearns
Head
Tony Richards
Deputy Head
Darren Flood
David Orsmond
Deputy Head
Sarah Harris
Chris Thompson
Risk and Compliance Department
Head
Chris Aylmer
Secretary's Department
Secretary
Anthony Dickman
General Counsel
Catherine Parr
Deputy Secretary
Andrea Brischetto
Deputy General Counsel
Peter Jones

Part 2:

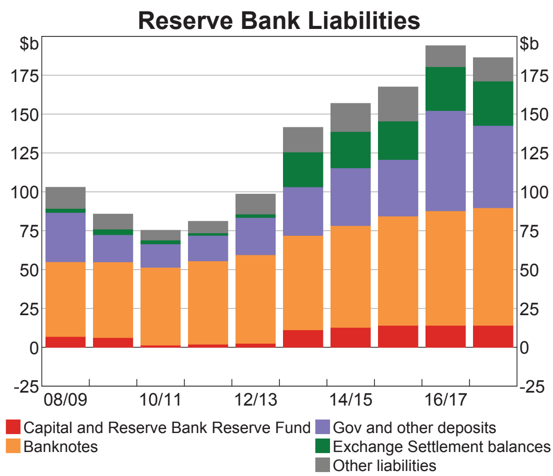
Our Operations

Operations in Financial Markets

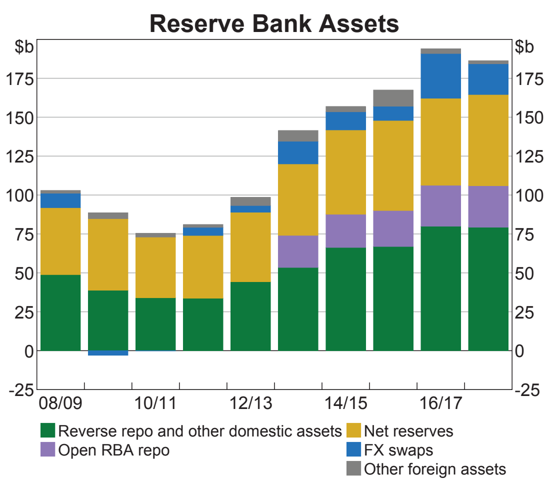
The Reserve Bank operates in domestic and international financial markets in order to achieve the policy objectives for which it is responsible. These operations include implementing the monetary policy decisions of the Reserve Bank Board, facilitating the smooth functioning of the payments system, managing the nation's foreign exchange reserve assets and providing banking services to clients (mainly the Australian Government and foreign central banks).

Balance Sheet

Over the past year, the Reserve Bank's balance sheet decreased by $8 billion and ended the 2017/18 financial year at $186 billion. The decrease in liabilities was mainly due to a decrease in deposits held by the Australian government with the Bank. These deposits are used by the government to manage the timing of its receipts and outlays, and can vary considerably over the course of a year. On the asset side of the balance sheet, the decrease in liabilities was matched by a decrease in foreign currency assets sourced via foreign exchange swaps.



Source: RBA



Source: RBA

Domestic Market Operations

Monetary policy implementation

The Reserve Bank Board's operational target for monetary policy is the cash rate – the rate at which banks borrow and lend to each other on an overnight, unsecured basis. The Board decided to leave the cash rate target unchanged at 1.50 per cent throughout 2017/18. The cash rate is also a significant financial benchmark referenced in overnight indexed swaps and ASX's 30-day interbank cash rate futures contract.

Over the course of the year, the daily liquidity management operations of the Reserve Bank were conducted so as to ensure that the cash rate remained consistent with the target set by the Board on all days.

The funds traded in the cash market are the balances held by financial institutions in their Exchange Settlement Accounts (ESAs) at the Reserve Bank. These accounts are held by around 100 financial institutions and are used to settle payment obligations between these institutions. The aggregate level of Exchange Settlement (ES) balances changes as a result of payments made or received by customers of the Bank (principally the Australian Government) and ESA holders. The Bank also undertakes transactions on its own behalf to affect ES balances available to financial institutions. This includes undertaking repurchase agreements (repos) collateralised with eligible securities, buying or selling government securities on an outright basis, or using foreign exchange swaps involving Australian dollars. The Bank conducts these transactions with a view to maintaining the aggregate level of ES balances consistent with demand at the cash rate target.

The bulk of ES balances arise from 'open RBA repos' (that is, repos contracted without a maturity date) contracted with the Reserve Bank by financial institutions to meet their liquidity needs outside of normal banking hours. As these balances are remunerated at the cash rate target and are held to facilitate the effective operation of the payments system, they have no implications for the implementation of monetary policy. At the end of June 2018, these balances were around $27 billion.

The remainder of ES balances, referred to as surplus ES balances, fluctuated around $2 billion in line with demand during 2017/18. There is no scope for ESA holders to allow their accounts to be in deficit and any surplus balances are remunerated at an interest rate that is 25 basis points below the cash rate target. Therefore ESA holders typically aim to maintain their accounts with a small positive balance. Day-to-day demand for these surplus ES balances can be volatile for a number of reasons, including because, at times, some institutions choose to hold ES balances as high-quality liquid assets (HQLA) to comply with prudential requirements. There can also be increased demand for holding liquid balances at the central bank at certain times of the year.

On 12 June 2018, the Reserve Bank conducted an additional round of dealing to address a technical issue in the payments system that arose at one of the major banks; the Reserve Bank injected $8.7 billion under reverse repo for an overnight term and the reverse repo book temporarily rose to $76.5 billion. Conditions reverted to normal the following day after the technical issue was resolved.

As well as ensuring that the cash rate remains consistent with the target, the Reserve Bank is responsible for calculating the cash rate. The Bank calculates the cash rate directly from market transactions, sourcing individual transaction data from the Reserve Bank Information and Transfer System (RITS). In 2017/18, there were around 35 cash market transactions each day, with aggregate daily activity in the cash market averaging around $5 billion.

the Reserve Bank's **balance sheet** was $186 billion

Open market operations

On a day-to-day basis, the Reserve Bank transacts in domestic markets to ensure that the demand and supply for ES balances remains consistent with attaining the cash rate target set by the Board. Through these open market operations (OMO), ES balances are supplied in order to offset the effect on the availability of ES balances arising from the payment flows between ESA holders and the Bank (discussed above), and to accommodate changes in aggregate demand for ES balances by financial institutions. The Bank publishes the aggregate results of its OMO dealing rounds on market data services and on its website each day.

Most of the Reserve Bank's transactions in the domestic market are reverse repos contracted as part of its regular morning OMO.[1] Reverse repos involve the purchase of high-quality collateral securities where the Reserve Bank acquires the security for a period of time in return for providing cash. As a result, there is very little risk of the Bank suffering financial loss in its operations. These include securities issued by the Australian Government, the Australian states and certain approved sovereign and supranational international issuers. Securities issued by banks, such as bank bills, bonds and residential mortgage-backed securities (RMBS), are also eligible for repo in the Reserve Bank's OMO.

A new calculation methodology for the bank bill swap rate (BBSW) was introduced during 2017/18; BBSW is a major interest rate benchmark for the Australian dollar and is widely referenced in many financial contracts. The new methodology, which was fully implemented in May 2018, strengthens the benchmark by calculating it directly from transactions in the bank bill market. Because of the change to the calculation methodology, from November 2017 the Reserve Bank's main OMO dealing round was brought forward from 9.30 am to 9.20 am, so that it is generally concluded before the BBSW 'rate-set window' for trading bank bills, which runs from 8.30 am to 10.00 am. This provides market participants the opportunity to trade bank bills during the rate-set window taking into account their repo allocation in the OMO dealing round.

1 A reverse repo involves an agreement to buy and then later sell securities; this is economically similar to a secured loan, with the difference between the purchase and sale price representing the interest earned on the transaction.

During 2017/18, the cash rate remained consistent with the target set by the Board on all days

In conducting its operations, the Reserve Bank takes account of its forecasts of the liquidity needs of the financial system, as well as of the pricing of the bids and offers received in the OMO dealing round. In 2017/18, the repo transactions conducted in these operations had an average maturity at origination of around 35 days and a maximum term of around four and a half months. Reflecting the role that repos play in managing system liquidity, the total amount of cash lent by the Bank under repo (the 'repo book') averaged around $59 billion during the financial year. The Bank lent cash under repo to banks, insurance companies, non-bank securities firms and government institutions.

To ensure that unexpected payment flows during the day do not adversely affect the cash rate, the Reserve Bank has the option of undertaking additional rounds of market operations in the late afternoon. Such additional rounds were announced, on average, five times per month during 2017/18, with around two-thirds of these operations offering to inject additional liquidity into the system. Terms for these operations are typically shorter than the morning operations, with a maximum term of around 10 days in 2017/18. In the event of unforeseen liquidity developments in the evening, further dealing rounds can be announced to ensure the appropriate level of ES balances in aggregate. The Bank conducted one such round in 2017/18.

The Reserve Bank also uses foreign exchange swaps when managing system liquidity (swapping Australian dollars for foreign currencies increases the supply of ES balances in the same way as a repo transaction).[2] This is necessary because of the limited capacity of the domestic repo market to absorb sizeable fluctuations in the Bank's positions, such as those associated with large maturities of Australian Government Securities (AGS). Reflecting the role of the Bank's foreign exchange swaps in assisting with short-term liquidity management, these swaps have typically been contracted at maturities of around three months.

The Reserve Bank purchases government securities on an outright basis to assist in the management of large AGS maturities. This reflects the Bank's need to mitigate the liquidity impact on the maturity date of the funds that are paid out of the Australian Government's account at the Bank into ESAs (for the credit of the security holder). These purchases for liquidity management purposes are carried out for near-to-maturity securities (usually less than 12 months). They have no implications for the stance of monetary policy. To offset the liquidity effect of AGS maturities, the Bank purchased $9.2 billion of the July 2017 bond and $7.9 billion of the January 2018 bond prior to their maturity. Given the overall size of these maturities, the Bank also contracted sizeable reverse repos and foreign exchange swaps to offset their impact on ES balances. In recent years, the Australian Office for Financial Management (AOFM) has also started to buy back AGS directly in the secondary market prior to the maturity date, but typically ceases to do so around the time that the Bank enters the market to commence its purchases. These buybacks by the AOFM assist the Bank in managing ES balances on the day of a maturity. In preparation for the large AGS maturities scheduled for the current financial year, by the end of June 2018 the Bank had purchased $3.4 billion of the October 2018 bond and $4.0 billion of the March 2019 bond. The Bank's outright holdings of AGS are published monthly on the Bank's website.

The Reserve Bank holds a small amount of longer-term semi-government securities (semis) on an outright basis in its domestic portfolio. These are available to be sold as collateral under repo when the Bank conducts operations to drain liquidity from the overnight money market. At the end of 2017/18, the Bank held around $2.8 billion of semis on an outright basis. These securities are generally purchased as part of the Bank's daily OMO or separately through outright purchase operations. The latter, which are conducted over the Yieldbroker DEBTS trading platform, occurred three times in 2017/18.

The Reserve Bank continues to operate a Securities Lending Facility on behalf of the AOFM. The securities available through the facility comprise all Treasury Bonds and Treasury Indexed Bonds currently on issue. The Bank sells these securities under intraday or open repos to RITS members eligible to participate in the Bank's domestic market operations.

2 While the use of foreign exchange swaps increases the Reserve Bank's holdings of foreign exchange, it has no effect on net foreign reserves, as the increased holdings of foreign exchange are matched with a commitment to sell foreign exchange at a predetermined price and date. For the same reason, the use of swaps has no effect on the exchange rate.

Standing facilities

Separate from its OMO, the Reserve Bank also provides certain standing facilities, primarily to support the smooth functioning of the payments system. Through these facilities eligible counterparties transact with the Bank on pre-arranged terms, with liquidity made available via repos. The most frequently used standing facilities are those for the provision of intraday liquidity to ESA holders. The Bank can also extend overnight funding via repo where an ESA holder faces a shortage in ES balances that cannot be borrowed from another financial institution; such funding is extended at an interest rate 25 basis points above the cash rate target. During 2017/18, this arrangement was used on six occasions.

Open repos are provided under the Reserve Bank's standing facilities for ESA holders that have to settle payment obligations outside normal business hours, such as 'direct-entry' payments. Open repos are also used to facilitate the settlement of after-hours transactions through the New Payments Platform (see also chapter on 'Banking and Payment Services' for details). At the end of June 2018, 16 financial institutions had open repo positions with the Bank, valued at around $27 billion. To collateralise these open repos, the Bank has permitted the use of certain related-party assets issued by bankruptcy remote vehicles, such as self-securitised RMBS.

Eligible securities

The Reserve Bank has established criteria that determine which securities are eligible to be purchased under repo in its domestic market operations. To protect against a decline in the value of the collateral securities should the Bank's counterparty not meet its repurchase obligation, the Bank requires the value of the security to exceed the cash lent by a certain margin. These margins, which are listed on the Bank's website, are considerably higher for securities that are not issued by governments.[3] From time to time, the Bank reviews its eligibility criteria and the margin schedule. In March 2018, the Bank updated its policy for margins by announcing it would also apply margin on the securities it sells under repo. Securities sold under repo by the Bank are sourced from its outright holdings of AGS and securities issued by the state and territory borrowing authorities ('semis'). Unlike reverse repos, which involve the purchase of securities against cash and are conducted to inject liquidity, the Bank conducts a very small number of repos involving the sale of securities against cash, which are conducted in order to drain liquidity. Reverse repos form the great bulk of the Bank's domestic operations.

Participants in the Reserve Bank's market operations tend to be the fixed-income trading desks of banks and securities firms, as well as bank treasuries. Reflecting this, over half of the securities held by the Bank (excluding those under open repo) are government-related obligations, with most of the remainder being bank-issued debt securities and RMBS.

Domestic securities purchased by the Reserve Bank are held for safe custody in an account that the Bank maintains in Austraclear, the securities depository and registry operated by the ASX. Securities transactions conducted between the Bank and its counterparties are settled in the Austraclear system, mostly on a bilateral basis. The Bank also settles repo transactions contracted in its OMO within ASX Collateral, a collateral management service. During 2017/18, around 30 per cent of the total amount of securities the Bank purchased under repo was settled within ASX Collateral, up from around 20 per cent in 2016/17. The use of this system reduces the manual processing, mark-to-market

3 See <https://www.rba.gov.au/mkt-operations/resources/tech-notes/margin-ratios.html>

and margin maintenance activities associated with managing collateral securities.

Asset-backed securities form a significant share of the collateral securities the Reserve Bank purchases under open repo. Around 95 per cent of the outstanding amount of open repos is backed by self-securitised RMBS. Self-securitised RMBS used in open repos do not have directly observable market prices, as they are retained in full by the bankruptcy remote trusts of originating institutions and therefore are not traded. As a result, the Bank uses an internal valuation model for self-securitised RMBS based on observed market prices of similarly structured RMBS; this internal model has been externally reviewed.

Asset-backed securities – particularly self-securitised RMBS – are also the major asset provided as collateral for the Committed Liquidity Facility (CLF) (see below). Given the importance of asset-backed securities to the Reserve Bank's operations, the Bank has mandatory reporting requirements for securitisations to remain eligible for repo. In 2017/18, the Bank received around 3,600 monthly data submissions on around 300 asset-backed transactions from issuers or their appointed information providers. For eligible RMBS, this covers 1.7 million underlying individual housing loans with a combined balance of around $410 billion, which is around one-quarter of the total value of housing loans in Australia. The required data include key information on the structure of the RMBS and the relationships among counterparties within the RMBS structure; the required data also include anonymous information on each of the residential mortgage loans and the underlying collateral backing the RMBS structures.

Reflecting the Reserve Bank's interest in promoting increased transparency for investors in asset-backed securities, issuers are also required to make securitisation information available to investors and other permitted users. The data provided to these users are broadly similar to the data provided to the Bank; however,

Australian Dollar Securities Held under Repurchase Agreements[(a)]

	June 2015		June 2016		June 2017		June 2018	
	$b	per cent of total	$b	per cent of total	$b	per cent of total	$b	per cent of total
AGS	22.8	28	32.8	35	43.8	43	49.9	48
Semis	11.3	14	7.4	8	6.2	6	8.7	8
Supranational	4.7	6	3.4	4	3.5	3	3.6	3
Government guaranteed	0.0	0	0.0	0	0.0	0	0.0	0
ADI issued	16.1	20	16.8	18	12.5	12	8.1	8
Asset-backed securities	25.3	31	31.6	34	35.6	35	32.7	32
– Of which for open repo	24.1	30	27.2	29	33.5	33	32.3	31
Other	0.1	0	0.6	1	0.6	1	0.6	1
Total	80.3	100	92.5	100	102.2	100	103.7	100
– Of which for open repo	25.6	32	29.3	32	35.7	35	34.2	33

(a) Market value of securities before the application of margins; includes securities held under triparty repurchase agreements
Source: CEIC; RBA

issuers may redact particular fields where the information poses a potential risk to privacy obligations and provide aggregated data instead.

The mandatory reporting requirements allow the Reserve Bank (and other investors in RMBS) to analyse in detail the underlying risks in asset-backed securities and to price and manage risk for such securities accurately.[4]

Committed Liquidity Facility (CLF)

Banks subject to the Liquidity Coverage Ratio (LCR) under Basel III prudential standards are required to hold sufficient HQLA (which, in the Australian context, consist of AGS and semis) to meet outflows during a period of stress of 30 days. Given the relatively low levels of government debt outstanding in Australia, there is a shortage of HQLA securities. To address this, the Reserve Bank provides some institutions with a contractual repo funding commitment – the CLF – subject to certain conditions. These conditions include a fee of 15 basis points per annum on the committed amount that financial institutions pay. In addition, any bank seeking to use the CLF must have positive net worth in the opinion of the Reserve Bank, having consulted with the Australian Prudential Regulation Authority (APRA). The banks are able to contract these repos using securities eligible in the Bank's domestic market operations. The full terms and conditions of the facility are available on the Bank's website.[5]

The Reserve Bank administers the CLF, while APRA determines which banks have access and the amount available (in aggregate and to each bank). During 2017/18, 14 banks were permitted to access the CLF. The aggregate size of the CLF is the difference between APRA's assessment of banks' overall LCR requirements and the Reserve Bank's assessment of the amount of HQLA securities that could reasonably be held by banks without unduly affecting market functioning. For 2018, APRA assessed banks' overall LCR requirements to be $474 billion and the Reserve Bank assessed the banks' reasonable holdings of HQLA securities to be $226 billion, such that the total size of the CLF was $248 billion. This was $31 billion higher than the total size of the CLF in 2017, largely reflecting banks targeting higher buffers over the minimum LCR requirement of 100 per cent. For 2019, the Reserve Bank has assessed that banks can reasonably hold $225 billion of HQLA securities, which represents a quarter of the projected stock of these securities. In determining the amount that banks can reasonably be expected to hold, the Reserve Bank takes into account factors such as the holdings of other market participants and the impact on the liquidity of HQLA securities in secondary markets.

Foreign Exchange Operations

The Reserve Bank transacts in the foreign exchange market on almost every business day. The majority of these transactions are associated with providing foreign exchange services to the Bank's clients, the most significant of which is the Australian Government. During 2017/18, the Bank sold $10 billion of foreign currency to the government (not including sales related to International Monetary Fund (IMF) financing).

The Reserve Bank typically purchases the necessary foreign exchange in the spot market. However, the Bank retains the option – especially during periods of market stress – to use its existing stock of foreign currency reserves to fund its customer business, subsequently

4 Some analysis of the securitisations data was included in speeches by Christopher Kent, Assistant Governor (Financial Markets), in August 2017 and by Marion Kohler, Head of Domestic Markets Department, in November 2017. See <https://www.rba.gov.au/speeches/2017/sp-ag-2017-08-14.html> and <https://www.rba.gov.au/speeches/2017/sp-so-dm-2017-11-20.html>.

5 The CLF legal documentation is available at <https://www.rba.gov.au/mkt-operations/resources/tech-notes/pdf/clf-terms-and-conditions.pdf> and <https://www.rba.gov.au/mkt-operations/resources/tech-notes/clf-operational-notes.html>.

Net foreign currency assets were … US$35.7 billion

replenishing those reserves when market conditions have stabilised. Using foreign currency reserves in this manner has not been considered necessary since 2008, at which time global financial market functioning was significantly impaired. Similarly, the Bank has not intervened in the foreign exchange market since 2008. During 2017/18, the Bank's assessment was that trading conditions in the market were sufficiently orderly and it was not necessary to support liquidity in the market through its own transactions. The Bank nevertheless retains the discretion to intervene in the foreign exchange market to address any apparent dysfunction and/or a significant misalignment in the value of the Australian dollar. Intervention data are published, with a lag, on the Bank's website.

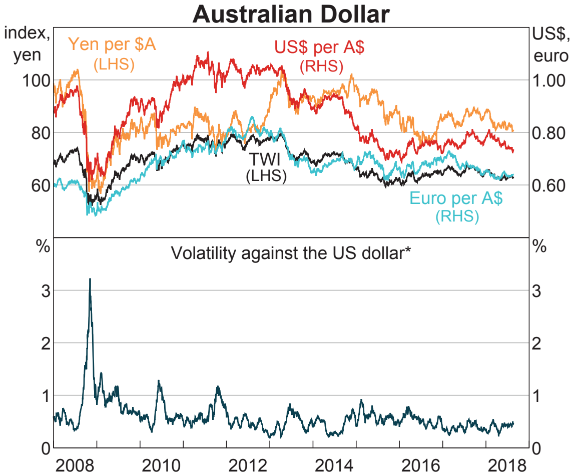
The Reserve Bank also transacts in the foreign exchange market when managing its foreign currency reserves. As discussed below, the relative weightings of foreign currencies in the Bank's portfolio are tightly managed against a benchmark. To maintain the portfolio at these benchmark weights, or to accommodate discrete changes in the weights, the Bank transacts in spot foreign exchange markets. The final settlement of these rebalancing flows may be deferred through the use of foreign exchange swaps, whereby one currency is exchanged for another with a commitment to unwind the exchange at a subsequent date at an agreed (forward) rate. Swaps can also be an efficient way to manage the shorter-term investments within the reserves portfolio. During 2017/18, the Bank generally maintained around $20 billion in swaps for these purposes.

As discussed above, the Reserve Bank also makes use of foreign exchange swaps in its domestic market operations. Swapping Australian dollars for foreign currencies does not affect the exchange rate, but alters the supply of ES balances in the same way as the Bank's repo transactions. Throughout the year, the amount of foreign currency held under swaps against Australian dollars can vary significantly. In 2017/18, the amount held by the Bank ranged between $10 billion and $35 billion.

Foreign currency swaps executed by the Reserve Bank are generally for no more than three months' duration. The resulting forward foreign exchange positions with each of the Bank's counterparties are marked to market daily and collateral is held against net exposures. The terms under which collateral is exchanged are defined in two-way credit support annexes to the International Swaps and Derivatives Association Master Agreements, which the Bank has executed with each of its counterparties (see the chapter on 'Risk Management').

The Reserve Bank's activities in the foreign exchange market are conducted in a manner consistent with the principles of the FX Global Code. A 'Statement of Commitment to the FX Global Code' has been signed on behalf of the Bank.[6] Further, the Bank now transacts in the foreign exchange market only with counterparties that have also signalled their adherence to the code by signing such statements.

6 For the Reserve Bank's Statement of Commitment, see <https://www.rba.gov.au/mkt-operations/pdf/statement-of-commitment-to-fx-global-code.pdf>.



* Daily absolute percentage change, 22-day rolling average
Sources: RBA; Thomson Reuters

Reserves management

Australia's official reserve assets include foreign currency assets, gold, Special Drawing Rights (SDRs – an international reserve asset created by the IMF) and Australia's reserve position in the IMF. At 30 June 2018, these assets totalled $75.8 billion. All components of official reserve assets are owned and managed by the Reserve Bank with the exception of Australia's reserve position in the IMF, which is an asset of the Australian Government.[7]

Official foreign currency assets are held by the Reserve Bank to facilitate various policy operations, including in the foreign exchange market (described above) and to assist the Australian Government in meeting its commitments to the IMF (discussed below). The Bank's capacity to undertake such operations is best measured by its foreign currency holdings net of any forward commitments (such as foreign currency the Bank has obtained from short-term swaps against the Australian dollar). As at 30 June 2018, these net foreign currency assets were SDR25.4 billion or US$35.7 billion. (In Australian dollar terms, net foreign currency assets totalled $48.3 billion, an increase of $1.6 billion from 12 months earlier, reflecting valuation effects.) The amount held represents the level assessed as necessary to meet policy requirements.

To ensure a strong balance sheet, the Reserve Bank holds capital against certain risks arising from its reserve assets (see the chapter on 'Earnings, Distribution and Capital' for more detail). These assets can expose the Bank to market, liquidity and credit risk, which the Bank seeks to mitigate where possible, such as by holding a diversified portfolio and investing only in assets of high credit quality and appropriate liquidity (see the chapter on 'Risk Management' for more detail).

The composition of the Reserve Bank's net foreign currency assets is managed against an internally constructed benchmark. This benchmark is assessed to be the combination of foreign currencies and foreign currency assets that maximises the Bank's expected returns over the long run, subject to the Bank's tolerance for risk. The structure of the benchmark is reviewed periodically and in response to significant changes in market conditions.

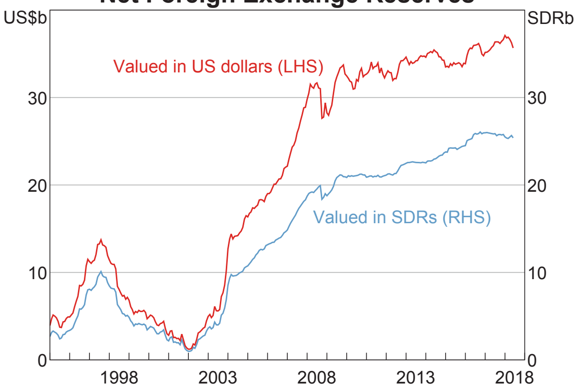
Foreign Assets
June 2018

	A$m
Official Reserve Assets	75,790
Foreign Currency	65,139
Gold	3,739
SDRs	5,557
Reserve Position in the IMF	1,355
Other Foreign Currency Assets	68
Net Forward Commitments	–16,336
Foreign currency	–16,940
Gold loans	604
Net Foreign Reserves	59,522
Memo item:	
Net Foreign Currency Assets	48,266

Source: RBA

7 For information on recent changes made to the reporting of Australia's official foreign currency assets, see <https://www.rba.gov.au/publications/bulletin/2017/dec/1.html>.

Net Foreign Exchange Reserves



Source: RBA

During 2017/18, no changes were made to the currency allocation of the benchmark portfolio. The Reserve Bank maintains the largest allocation to the US dollar at 55 per cent, reflecting the significant liquidity in US dollar currency and asset markets.

Reflecting the generally low level of global interest rates, duration targets have remained short for most of the foreign currency portfolios. Short duration targets reduce the risk of capital losses in the event yields in these currencies increase in the future.

Investments in the benchmark currencies are limited to deposits at official institutions (such as central banks) and debt instruments issued (or guaranteed) by sovereign entities, central banks and supranational agencies. Debt instruments issued by quasi-sovereign entities can also be accepted as collateral under reverse repos.

Sovereign credit exposures are currently limited to the United States, Germany, France, the Netherlands, Canada, Japan, China, the United Kingdom and South Korea.

At the end of June 2018, the Reserve Bank's foreign currency reserves included $19.8 billion of foreign currency sourced from swaps against Australian dollars. Foreign currency obtained in this manner does not comprise part of the benchmark portfolio but reflects domestic liquidity operations. It is invested to ensure that the Bank's forward commitments to sell foreign currency are hedged against currency and interest rate risk.

As has been the case for some years, when the cost of hedging currency risk is taken into account, yields on short-dated Japanese investments have generally exceeded those available in the other currencies in the Reserve Bank's portfolio. Reflecting this, the bulk of the foreign currency the Bank obtains from swaps against Australian dollars is Japanese yen.

For the same reason, the Reserve Bank also swaps other currencies in its foreign exchange reserves portfolio against the yen to enhance returns. As a consequence, while the Bank's exposure to changes in the value of the yen remains small (consistent with the yen's 5 per cent allocation in the benchmark), an additional $21 billion of yen was held at the end of June 2018 as a result of swaps against other foreign currencies in the portfolio.

A small component of the Reserve Bank's net foreign currency reserves sits outside the benchmark framework. This encompasses investments in a number of Asian debt markets through participation in the Executives' Meeting

Benchmark Foreign Currency Portfolio

30 June 2018

	US dollar	Euro	Japanese yen	Canadian dollar	Chinese renminbi	UK pound sterling	South Korean won
Currency allocation (per cent of total)	55	20	5	5	5	5	5
Duration (months)	6	6	<3	6	18	3	18

Source: RBA

Foreign Currency Assets[a]
A$ million, 30 June 2018

Currency	Securities held outright	Securities lent under repurchase agreements	Deposits at official institutions[b]	Total (gross)	Forward foreign exchange commitments[c]: Against AUD	Forward foreign exchange commitments[c]: Against other currencies[c]	Forward foreign exchange commitments[c]: Other	Total (net)
US dollar	9,354	–447	749	9,655	185	14,429	1,890	26,159
Euro	5,953	–550	6,378	11,781	–6,770	3,714	943	9,668
Japanese yen	20,680	0	15,911	36,591	–13,192	–21,040	0	2,360
Canadian dollar	790	0	5	795	0	1,566	0	2,361
Chinese renminbi	1,741	0	611	2,352	0	0	0	2,352
UK pound sterling	837	0	1	838	–1	1,546	0	2,384
South Korean won	2,343	0	9	2,353	0	0	0	2,353
Total	41,698	–997	23,664	64,365	–19,777	215	2,834	47,636

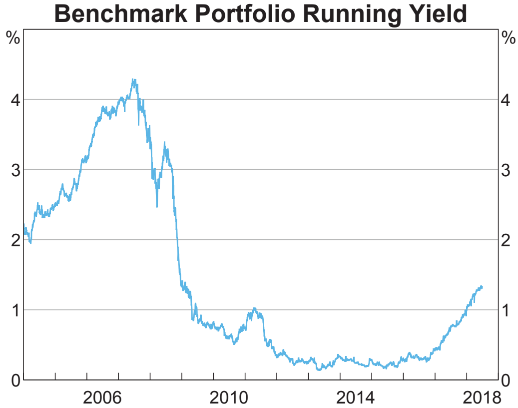
(a) Excludes investments in the Asian Bond Fund
(b) Includes deposits at foreign central banks and the Bank for International Settlements
(c) In accordance with IMF guidelines, 'forward commitments' reflect notional values of unsettled spot and forward transactions, converted to Australian dollars at the prevailing forward exchange rate; other forward commitments largely reflect cash lent under repurchase agreements
Source: RBA

of East Asia and Pacific Central Banks (EMEAP) Asian Bond Fund Initiative. This initiative was established following the Asian currency crisis in the late 1990s to assist in the development of bond markets in the region. At the end of June 2018, the total allocation of the Bank's reserves to these funds was $628 million and the return on these investments in 2017/18 was 0.3 per cent when measured in SDR terms, with capital losses on bond holdings and depreciation of Asian currencies partially offsetting interest earnings.

Measured in SDRs, the overall return on the Reserve Bank's foreign currency assets over 2017/18 was 0.8 per cent. This return was slightly lower than that in each of the previous three years, reflecting the negative impact of exchange rate valuation changes. Capital losses on bond holdings also partially offset the positive impact on returns from higher yields. The running yield on the benchmark portfolio increased by 0.6 per cent to 1.3 per cent over 2017/18, driven by an increase in yields for the US dollar, Canadian dollar, UK pound sterling and Korean won portfolios. Yields remained negative and relatively stable for the euro portfolio.

The Reserve Bank's holdings of SDRs at 30 June 2018 amounted to $5.6 billion, $0.4 billion higher than the previous year, mainly owing to a depreciation of the Australian dollar against

Benchmark Portfolio Running Yield



Source: RBA

the SDR. Under voluntary arrangements with the IMF, the Bank is willing to transact in SDRs upon request from other countries or prescribed holders. In these transactions, the Bank will generally either buy or sell SDRs in exchange for foreign currencies (such as euros or US dollars). While such transactions do not alter the level of Australia's reserve assets (only the respective proportions held in SDRs and foreign currency), the Bank occasionally chooses to replenish foreign currency sold in exchange for SDRs by purchasing additional foreign currency against Australian dollars in the spot market.

Australia's reserve position in the IMF comprises that part of Australia's quota in the IMF that is paid in foreign currency as well as other credit that Australia has extended to the IMF in support of its lending programs. At the end of June 2018, Australia's reserve position in the IMF was $1.4 billion, $0.3 billion larger than the previous year, reflecting both the depreciation of the Australian dollar and greater provision of foreign currency to the IMF. As noted above, Australia's reserve position in the IMF is not held on the Reserve Bank's balance sheet. However, the Bank will sell to (or purchase from) the Australian Treasury the foreign currency the Treasury needs to complete its transactions with the IMF. In contrast to other foreign exchange transactions with the Australian Government, the Bank will typically draw on (or add to) its foreign currency reserves when providing (or receiving) foreign currency for IMF-related purposes because these transactions do not alter the level of Australia's reserve assets. Nevertheless, as with SDR transactions, on certain occasions the Bank may decide to offset the impact on foreign currency holdings of these IMF transactions by buying or selling foreign currency in exchange for Australian dollars in the spot market.

Gold holdings (including gold on loan) at the end of June 2018 were around 80 tonnes, unchanged from the previous year. Gold prices rose by 5 per cent in Australian dollar terms over 2017/18, increasing the value of the Reserve Bank's holdings of gold by around $0.2 billion to $4.3 billion. At $0.71 million, income from gold loans was slightly lower than the previous year, as a result of lower lending rates.

Bilateral currency swaps

In April 2018, the Reserve Bank renewed a bilateral local currency swap agreement with the People's Bank of China. The agreement allows for the exchange of local currencies between the two central banks of up to A$40 billion or CNY200 billion. The agreement is for a further three years and can be extended by mutual consent. The Reserve Bank has similar agreements with the Bank of Japan, Bank of Korea and Bank Indonesia. The purpose of these agreements is to allow each central bank to support trade settlement in local currencies, particularly in times of market stress, or to support financial stability.

RBA Bilateral Local Currency Swap Agreements[(a)]
June 2018

	Agreement signed/renewed	Size (A$b)
People's Bank of China	April 2018	40
Bank of Japan	March 2016	20
Bank Indonesia	December 2015	10
Bank of Korea	February 2017	10

(a) All swap agreements have 3-year terms
Source: RBA

Banking and Payment Services

The Reserve Bank provides banking and payment services to support the efficient and stable functioning of the Australian financial system. The Bank is currently engaged in projects to renovate and strengthen its banking and settlement capabilities and operate new infrastructure to support real-time payments by households and businesses on a 24/7 basis. This will enable the Bank to continue to meet the banking and payment needs of its government and agency customers and, in turn, the Australian public.

Banking

The Reserve Bank's banking function provides services in two broad groups: central banking services and transactional banking services. Both are provided with the objective of delivering secure and efficient arrangements to meet the banking and payment needs of the Australian Government and its agencies. In addition, the Bank provides banking and registry services to a number of overseas central banks and official institutions.

The key aspect of the Reserve Bank's central banking services is the role it plays as banker to the Australian Government. Among other things, this requires the Bank to manage the consolidation of all Australian Government agency account balances, irrespective of the financial institution that provides transactional banking services to each Australian Government agency. These balances are transferred at the end of the business day into a group of accounts known as the Official Public Accounts (OPA) Group, which is where the Commonwealth's overnight at call cash balances are held. Daily payment instructions from the Department of Finance are then processed to move funds from the OPA to agency bank accounts to meet agency payment obligations. The Bank also provides the government with a term-deposit facility for investment of its cash holdings, as well as a very limited short-term overdraft facility to cater for occasions when there is unexpected demand for government cash balances. While the Bank manages the consolidation of the government's accounts, the Australian Office of Financial Management has responsibility for ensuring there are sufficient cash balances in the OPA to meet the government's day-to-day spending commitments and for investing excess funds in approved investments, including term deposits with the Bank.

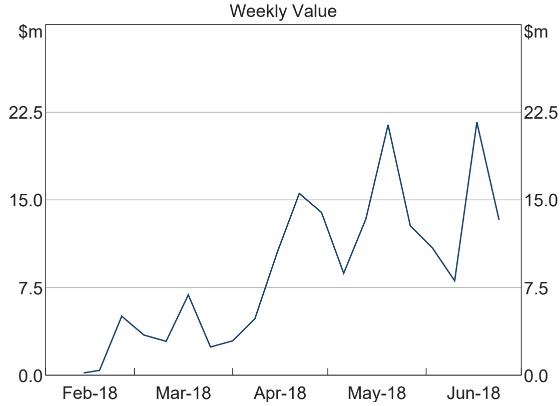
The transactional banking services offered by the Reserve Bank have evolved rapidly over recent years as its government agency customers look to embrace new technology to deliver convenient, secure, reliable and cost-effective payment options to the public. The public launch of the New Payments Platform (NPP) in February 2018 was an important milestone in this evolution. The NPP allows fast, versatile and data-rich payments to be made 24/7. In the six months since the NPP's launch, the Bank's government clients have received NPP payments to the value of $179 million, primarily from individuals and businesses to pay tax liabilities. The Bank is working with government agencies, such as the Department of Human Services and the Australian Taxation Office (ATO), to ensure they are able to fully utilise the new payments technology, including via future planned overlay services. The Bank expects that the NPP will affect volumes for its more traditional payment and collection services in coming years.

The Reserve Bank also continues to provide a number of other channels to make payments from government agencies to recipients' accounts. In 2017/18, the Bank processed around 312 million domestic and 1.1 million international payments, totalling $534 billion and $11.6 billion respectively, for government agencies. Most of these payments were direct entry payments made on behalf of the Department of Human Services. The Australian Government also makes payments by the real-time gross settlement (RTGS) system, cheque, BPAY and prepaid cards. After declining over recent years, cheque payment volumes were steady in 2017/18.

In addition to payments, the Reserve Bank provides government agency customers such as the ATO with access to a number of services through which they can collect monies owed

RBA's Government Clients' NPP Receipts

Weekly Value



Source: RBA

The New Payments Platform allows fast, versatile and data-rich payments to be made 24/7

from both domestic and international payers. These include direct entry, RTGS, BPAY, cheque, eftpos, cash, and card-based services via the internet and phone. The Bank processed 36 million collections-related transactions for the Australian Government in 2017/18, amounting to $509 billion. Agencies continue to actively encourage customers to use lower-cost electronic payment options, with cheque and cash payments declining by 17 per cent to $4.8 million and electronic payments representing 98 per cent of all collections-related transactions in 2017/18.

The provision of transactional banking services is consistent with the Reserve Bank's responsibilities under the *Reserve Bank Act 1959*, which requires the Bank to provide these services to the Australian Government if so required. The Bank provides transactional banking services to over 90 Australian Government agencies. A key difference between the Bank's central banking and transactional banking services is that the latter are offered in line with the Australian Government's competitive neutrality guidelines. To deliver the services, the Bank competes with commercial financial institutions, in most instances bidding for business via tenders conducted by the agencies themselves. The Bank must also cost and price the services separately from its other activities, including central banking services, and meet a prescribed minimum rate of return.

Pro forma business accounts for transactional banking are provided on page 128 of this report.

The Reserve Bank works closely with its transactional banking customers, the Australian Government and the payments industry more broadly to ensure that its customers have access to the services which meet their needs and those of the public. For some services, the Bank combines its specialist knowledge of the government sector with specific services and products from commercial providers to meet the government's banking needs. In 2017/18, the Bank explored new options for collecting online payments. The Bank will continue to make use of combined service arrangements with commercial providers as the government's banking needs evolve.

Registry services are also provided by the Reserve Bank to supranational organisations issuing Australian dollar-denominated securities. Eight organisations currently use these services, with this number having been relatively steady over recent years.

In the six months since the NPP's launch, the Bank's government clients have received NPP payments to the value of $179 million

The Reserve Bank has undertaken a significant program of work to upgrade its banking systems since 2012, moving them to a more modern programming language and architecture, and re-engineering a number of related business processes. Further milestones in the program were achieved during 2017/18, with work on renovating the systems used to process most government payments and collections almost complete. The Bank has also made good progress with the project to upgrade the Bank's account maintenance system, with the first phase completed. This program of work is on schedule to be completed during the September quarter 2019.

Since the launch of the NPP, the Reserve Bank has continued to develop further capabilities that will assist in providing more reliable, cost-effective, faster and better-integrated services to expand the usage of the NPP. As part of this work, an Application Programming Interface (API) will be introduced by the end of 2018 to facilitate open, secure and automated communications between the Bank and its agency customers.

After-tax earnings from the Reserve Bank's transactional banking services were $1.5 million in 2017/18, $1.9 million lower than in the previous year. The fall was due largely to higher project costs associated with systems development and service improvements combined with reduced interest income.

Settlement Services

The Reserve Bank owns and operates the Reserve Bank Information and Transfer System (RITS), which is used by banks and other approved institutions to settle their payment obligations. Settlement in RITS is effected across Exchange

Settlement Accounts (ESAs) held with the Reserve Bank, and is final and irrevocable. Around 90 per cent of the value of payments exchanged between financial institutions in Australia is settled in RITS individually on a real-time gross settlement (RTGS) basis. This includes high-value customer, corporate and institutional payments, wholesale debt and money market transactions and the Australian dollar legs of foreign exchange transactions. By providing a mechanism for RTGS, RITS eliminates the settlement risk that would otherwise arise between participants in high-value payment, clearing and securities settlement systems. On average, 47,600 RTGS transactions worth $182 billion were settled in RITS each day in 2017/18. In recent years, the value of transactions has increased at a lower rate than the volume of transactions. In addition, RITS provides deferred net settlement services for low-value retail payment systems, equity settlements and settlement of property-related transactions.

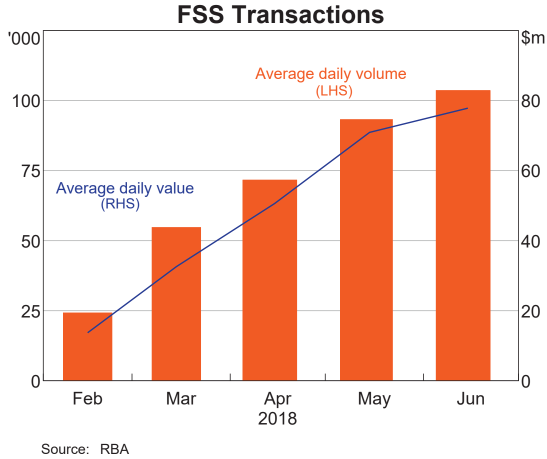
RITS also provides a real-time settlement service to support the operation of the NPP. The public launch of the NPP in February 2018 was the result of a large collaborative undertaking by payment service providers and the Reserve Bank. The key features of the NPP include: enabling users to make retail payments in real time; allowing more complete remittance information to be sent alongside the payment; enabling easy addressing of payments to payee accounts using simple identifiers (called PayIDs), such as email addresses, mobile phone numbers or ABNs; and facilitating the sending and receiving of payments outside normal business hours with 24/7 operation. To support innovation in the Australian payments system, the NPP is structured so as to allow the commercial development of new payment and related services using the capabilities of NPP's infrastructure. At the end of June 2018, more than 60 financial institutions offered NPP payments to their customers, with around 1.8 million registered PayIDs. Many of these institutions are smaller authorised deposit-taking institutions (ADIs) connecting via the services of an aggregator. The number of registered PayIDs is expected to grow significantly through 2018/19 as participants progress their NPP roll-out.

NPP transactions are settled in the RITS Fast Settlement Service (FSS). This is a new system within RITS designed to process and settle a high volume of transactions in real time, but without the transaction queuing and management capabilities provided by core RITS for the management of high-value transactions. The real-time settlement of NPP transactions via the FSS removes the credit risk that would otherwise exist if these transactions were settled on a deferred net basis as is currently done for other low-value payments. Transaction volumes settled via the FSS have grown steadily since launch, reaching over 100,000 transactions per day in June 2018, with an average transaction value of around $750. This amounted to a total of 10.2 million transactions with a total value of $7.3 billion settled via the FSS between public launch and the end of June 2018. To support the FSS, the hours of operation of the RITS Help Desk were extended to provide 24/7 technical assistance to members. Since its launch, the FSS has operated smoothly, with no major disruptions to operations.

While the introduction of the NPP has resulted in more low-value payments being settled in real time, the bulk of low-value payments continue to settle in RITS on a net basis. The average daily value of net settlements in RITS was around $12 billion in 2017/18. This includes obligations for payments exchanged through low-value clearing systems for cheques, debit and credit cards, BPAY and direct entry transactions. For these transactions, RITS combines multiple bilateral obligations submitted by members into a single net obligation for each member, which are then settled in RITS at predetermined times. During 2017/18, these low-value clearing arrangements accounted for a net daily average of $9.5 billion, of which around 85 per cent was intraday settlement of direct entry transactions. The substantial increase in the value of these low-value clearing arrangements over the past five years reflects a fragmentation of settlement arrangements, with the introduction of the five intraday settlement runs for direct entry and other new batch settlement arrangements, which supplement the long-established arrangement of a morning settlement session of net deferred obligations at around 9.00 am.

In the batch settlement arrangements, an approved administrator for each batch is responsible for calculating the net obligations of the batch participants and submitting those to RITS for settlement. The Clearing House Electronic Sub-register System (CHESS) batch, which effects settlement of payments arising from stock market transactions and is administered by ASX Settlement Pty Limited, averaged around $1 billion per day in 2017/18. The Mastercard batch, for settlement of domestic Mastercard obligations and administered by Mastercard International, averaged around $684 million over the same period. On 30 August 2017, a new eftpos batch, administered by eftpos Payments Australia Limited, went live for settlement of point-of-sale transactions processed through the eftpos system. Previously, these transactions had been settled the next day at around 9.00 am. The eftpos batch averaged around $284 million per day for the part of 2017/18 during which it was operational.

The FSS settled 10.2 million transactions totalling $7.3 billion between public launch and the end of June 2018



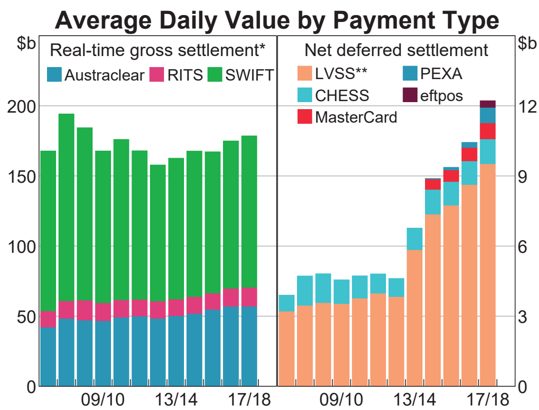
A batch feeder arrangement in RITS also supports the settlement of obligations arising from electronic property transactions processed by Property Exchange Australia Limited (PEXA). Timelines for migration to electronic e-conveyancing set by several state governments have contributed to ongoing strong growth in the number and value of property settlement batches processed in RITS, although off a low base. During 2017/18, the PEXA batch settlements averaged $668 million per day, more than double the figure for the previous year.

Reflecting the critical importance of RITS to the Australian financial system, the Reserve Bank conducts regular reviews of the resilience of RITS. An important part of this is the annual assessment of RITS against the *Principles for Financial Market Infrastructures* (PFMI) set by the Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO). The May 2018 assessment of RITS against the PFMI concluded that RITS adhered to all relevant principles. It noted the existing high level of resilience of RITS, which includes replication of critical components and duplication of systems across two geographically separate sites, while also supporting the Bank's ongoing work to enhance resilience. Key examples of this work are an investigation into the potential use of non-similar technology to enhance recovery from cyber attacks, and the implementation of the remaining recommendations from the Bank's major reviews of security and resilience conducted through 2015 and 2016. The Bank has also commenced a multi-year project to upgrade the core network and application infrastructure of RITS.

At the end of June 2018, 58 RITS members were using their own ESA to settle their payment obligations. An additional 41 RITS members held a dormant ESA, settling all their obligations through another ESA holder acting as their settlement agent. There were also 65 RITS members that did not hold an ESA, but held RITS membership to satisfy requirements for participation in the Reserve Bank's open market operations.

Recent changes in bank regulations seeking to enhance competition and innovation in payment services have resulted in corresponding changes in the Reserve Bank's ESA Policy. In May 2018, the *Banking Act 1959* was amended to allow all ADIs to use the term 'bank'. The Australian Prudential Regulation Authority is also introducing a phased approach to authorising new ADIs, which allows new entrants to fast track a restricted ADI licence. As the bank designation is no longer a useful criteria for determining the appropriate type of RITS membership, the prior requirement for all banks to hold an ESA has been removed. The requirement for ADIs contributing more than 0.25 per cent of total wholesale RTGS value to hold and operate their own ESA remains. The new policy means that holding a dormant ESA has become optional for many existing ESA holders, although the Reserve Bank continues to offer the use of a dormant ESA to eligible banks and other payment service providers for contingency purposes.

The Reserve Bank offers accounts to other central banks and official institutions overseas to allow for settlement of certain Australian dollar payments, and provides safe custody services to these overseas agencies. The face value of securities held in custody by the Bank in this capacity was around $72 billion at the end of June 2018. The Bank also provides settlement services for banknote lodgements and withdrawals by commercial banks.



* Excluding FSS transactions

** RITS Low Value Settlement Service, including cheque, direct entry, ATM and Visa settlements

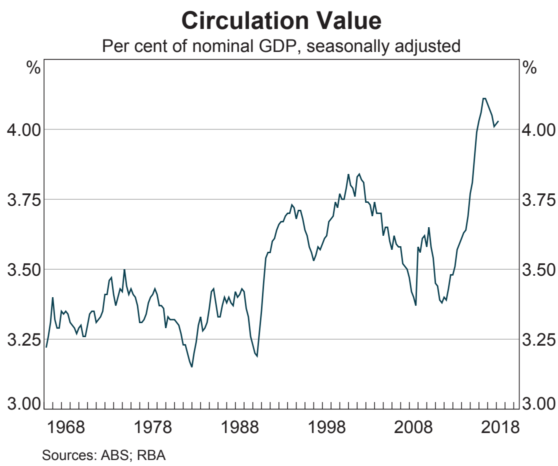
Source: RBA

Banknotes

The Reserve Bank is responsible for producing and issuing Australia's banknotes. Public demand for banknotes stems from the role of banknotes as both a payment mechanism and store of value. To maintain the capacity of banknotes to perform these roles, the Bank seeks to ensure banknotes in circulation are of high quality and sufficient volume to meet public demand. The Bank conducts research and development to ensure that Australia's banknotes remain secure against counterfeiting. Based on this work, the Bank is issuing an upgraded series of banknotes with world-leading security features.

Circulation

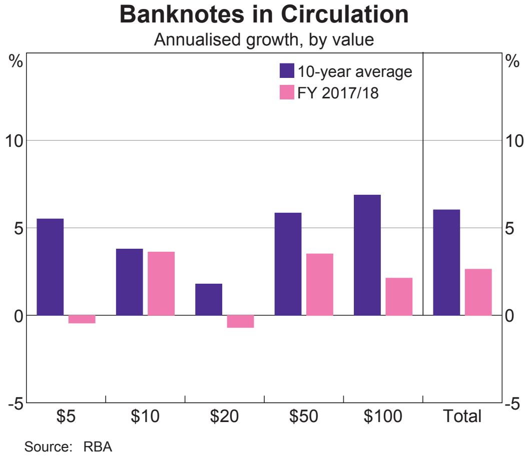
The value of banknotes in circulation increased by 2.5 per cent over 2017/18, somewhat slower than in recent years. As at the end of June 2018, there were 1.6 billion banknotes, worth $76 billion or around 4 per cent of nominal GDP, in circulation. The ratio of the value of banknotes in circulation to nominal GDP remains at a historically high level, despite consumers increasingly using electronic payment alternatives for transactions. Growth in the $10 denomination was boosted by the introduction of the new $10 banknote, with many of the existing $10 banknotes not yet returned to the Reserve Bank. As at the end of June of 2018, new series banknotes made up around 60 per cent of all outstanding $5s and around 35 per cent of all outstanding $10s.



Distribution

The Reserve Bank maintains banknote holdings to accommodate: growth in the number of banknotes in circulation; seasonal fluctuations in demand; and contingency needs in the event of systemic shocks and production disruptions. The Bank has established distribution agreements with a number of commercial banks, which provide the banks with timely access to banknotes. The Reserve Bank issued banknotes worth $8.3 billion in 2017/18, of which around $1.9 billion had been in circulation previously and around $6.3 billion were new.

The Reserve Bank aims to maintain a high quality of banknotes in circulation to ensure their



suitability as a payment mechanism and store of value. High-quality banknotes are more readily handled by machines and make it more difficult for counterfeits to be passed. For this reason, the Bank has arrangements that encourage the commercial banks and the cash-in-transit companies to continue to distribute banknotes that remain fit for circulation and return those that are unfit to the Bank's processing site in Craigieburn. These unfit (damaged) banknotes are assessed to confirm their authenticity and quality. In 2017/18, the Bank received $2.4 billion worth of banknotes, and almost all were deemed to be unfit for recirculation.

The Reserve Bank provides an additional service through its Damaged Banknotes Facility. The facility is offered to members of the public who have unwittingly come into possession of damaged banknotes or whose banknotes are accidentally damaged, with the aim to ensure that they do not face financial hardship. Claims that meet the requirements set out in the Bank's Damaged Banknotes Policy are paid based on their assessed value. The Bank processed 12,899 claims and made $6.9 million in payments in 2017/18. Of the damaged banknote claims processed in 2017/18, 31 claims worth $3.3 million were for banknotes that had been contaminated as a result of floods resulting from Cyclone Debbie in Queensland and New South Wales.

Counterfeiting Rates

The level of counterfeiting in Australia remains relatively low by international standards. In 2017/18, around 26,000 counterfeits, with a nominal value of nearly $2 million, were detected in circulation. This corresponds to around 16 counterfeits detected per million genuine banknotes in circulation, a 20 per cent reduction from 2016/17.

To combat counterfeiting in Australia, the Reserve Bank works closely with domestic and international law enforcement agencies to monitor trends and identify emerging threats. As part of this arrangement, the Bank provides analytical and counterfeit examination services and prepares expert witness statements and court testimonies to assist the agencies with their investigations.

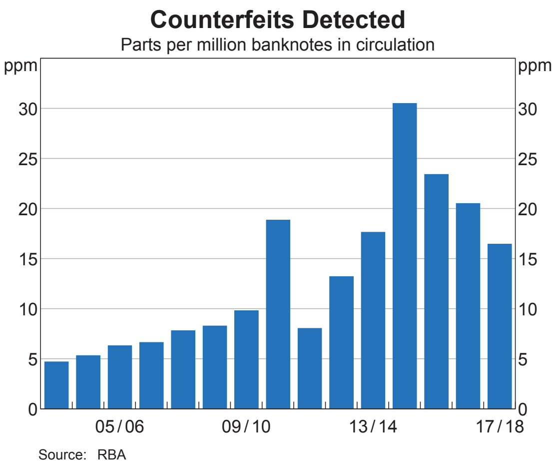
In 2017/18, the Australian Federal Police and state police made a number of arrests and disrupted production of counterfeit banknotes on a number of occasions. During the year, the Commonwealth Department of Public Prosecutions prosecuted 44 matters involving

Counterfeit Banknotes in Australia[(a)]
2017/18

	$5	$10	$20	$50	$100	Total
Number	41	276	592	15,351	9,614	25,874
Nominal value ($)	205	2,760	11,840	767,550	961,400	1,743,755
Parts per million	0.2	2.0	3.5	21.6	28.2	16.4

(a) Figures are preliminary and subject to upward revision because of lags in counterfeit submissions to the RBA
Source: RBA

Assistant Governor (Business Services) Lindsay Boulton (centre) discusses banknote counterfeit detection on *Studio 10* with presenters Sarah Harris, Denise Scott, Joe Hildebrand and Angela Bishop, May 2018



possession, uttering (passing) and making of counterfeit currency.

Next Generation Banknote Program

To ensure that Australian banknotes remain secure against counterfeiting, the Reserve Bank is issuing an upgraded series of banknotes. The new $5 banknote was released in 2016 and the new $10 banknote was released on 20 September 2017. A new $50 banknote is scheduled to enter general circulation in October 2018, with the remaining two denominations –$20 and $100 – to be issued in subsequent years.

The Reserve Bank revealed the design of the new $50 banknote in February 2018. The design features David Unaipon and Edith Cowan, two Australians who were prominent campaigners for social change.

With $50 banknotes accounting for almost half of the banknotes in circulation, and the most targeted for counterfeiting, the release of the new $50 will enhance the security of the most widely circulating banknote. The new banknotes incorporate the latest technology such as the top-to-bottom window that contains optically variable security features, including a flying bird and reversing number, as well as the patch with rolling colour effect. The new banknotes also retain many of the key design elements of the first polymer banknote series, including the people portrayed, size and colour palette.

The cost of the Next Generation Banknote program, which was established in 2007, is budgeted at $37 million for all five denominations. The majority of the work program, focused on the new banknote development, has been completed and the Bank is on track to issue the remaining denominations within budget. To date, $32.2 million of this has been spent on designing and testing the

(Top) The new $50 banknote will be issued in October 2018 and features the same innovative security features that appear on the new $5 and $10 banknotes; the $50 banknote retains the portraits of Aboriginal writer and inventor David Unaipon and (middle) the first female member of an Australian parliament, Edith Cowan; (above) the new $50 banknote in production ahead of its October 2018 release

Muriel Van Der Byl, whose painting portraying the practices of miwi and navel cord exchange features on the new $50 banknote, examines the new design during banknote development, November 2015

… the release of the new $50 will enhance the security of the most widely circulating banknote

new banknote series, as well as the related community consultation, communication and education initiatives.

Industry Readiness

It is estimated there are now around half a million pieces of equipment, including ATMs, self-service checkouts, gaming machines and vending machines in Australia that need to process the new banknotes. The $50 is the most common banknote in circulation and accounts for the vast bulk of notes used in ATMs. Therefore, the Reserve Bank's engagement with machine manufacturers, deployers and owners has increased in focus and scope to help ensure the large number of machines will be ready for the new $50 banknote.

Regular communication with the industry is carried out and an online central hub of information is maintained to assist the cash-handling industry (including equipment manufacturers, financial institutions and other high-volume cash handlers, such as retailers and hospitality venues) to manage their equipment upgrades and educate their staff and customers about the new banknote series. Similar to the program for the new $10, the Reserve Bank is providing education and training materials. Bank staff have also continued to attend industry events and deliver presentations to share information about how to identify the security features of the new banknotes.

Public Communication

The Reserve Bank implemented a communication strategy to ensure that the public was well informed about the new banknotes and could readily identify the new security features.

Building on the high levels of awareness following the release of the new $5, a smaller advertising campaign was run for the new $10, predominantly on digital channels and also included some radio advertisements.

(Top) the 'New Australian banknotes: $10 security features' video, available at <https://banknotes.rba.gov.au/resources/videos/new-10-security-features/> has been viewed more than 40,000 times; (above) Governor Philip Lowe (right) speaks to David Koch from Channel 7's *Sunrise* program on 20 September 2017, the day the new $10 entered general circulation

Members of the public queuing in the Head Office Banking Chamber to be among the first to acquire the new $10 banknotes, Sydney, September 2017

Additionally, for the new $10, the focus was on deepening the understanding of the security features of the new series of banknotes. The Reserve Bank hosted information stalls in various cities across Australia in places where members of the public are likely to be using cash to make payments. The face-to-face interaction with members of the public allowed the dynamic new features on the banknotes to be demonstrated.

During 2017/18, staff from Note Issue Department also continued to engage extensively with industry and members of the public to increase knowledge about the new and existing banknotes. More than 150 banknote-related presentations were given by Reserve Bank staff during 2017/18, with the majority delivered to visitors to the Reserve Bank of Australia Museum.

Banknote Infrastructure Modernisation Program

In preparation for the logistical demands arising from the introduction of the new banknote series, the Reserve Bank has completed a program to upgrade its existing banknote infrastructure. The program achieved its objectives to increase banknote storage and processing capacity, and to introduce new technologies and systems to improve banknote logistics processes and simplify distribution arrangements.

The upgrade involved construction of the National Banknote Site (NBS) at the Bank's existing Craigieburn site in Victoria. The NBS is a significant piece of national infrastructure that will store, process and distribute our banknotes for decades to come.

The main objectives of the upgrade were to introduce new sophisticated technologies and systems to improve banknote logistics processes and simplify distribution arrangements with cash-in-transit companies, and the implementation of new high-speed banknote processing machines. Banknote processing commenced at the NBS in December 2017 and, following a settling in process, banknote distribution operations commenced in August 2018.

The NBS consolidates all of the Reserve Bank's vaults in Victoria, and as a result, the banknote storage facility in the Bank's building in the Melbourne CBD was officially closed on

23 March 2018, marking the end of a significant chapter in the Bank's history.

The cost of constructing the NBS was $77 million over five years. Additional costs associated with modernising the infrastructure for banknote storage, processing and distribution amounted to $61 million over the same period. The amount is consistent with the budget approved by the Parliamentary Public Works Committee in 2015.

Research and Development

The Reserve Bank maintains an active research and development (R&D) program focused on researching new and emerging technologies that can be developed into future generations of security features and detection equipment. The primary aim of this program is to ensure that our banknotes remain highly secure against counterfeiting and easy to authenticate for a wide variety of users.

This is achieved in part through collaboration with domestic and international experts from various external organisations, including universities, public and private companies, research institutes and other central banks. Fundamental to this program is a continuing assessment of the vulnerability of banknotes to different forms of counterfeiting, the mechanisms by which banknotes wear in circulation, and how the public and banknote processing machines use and authenticate banknotes.

The Reserve Bank also works closely with its partners and suppliers to incorporate new technologies and features into the banknote production process. In 2017/18, the research program continued to focus on providing technical advice and expertise as part of the development of the new series of Australian banknotes by: conducting trials, assessing new technologies and developing strategies to ensure the durability

(From left) Sivakumar Pavani from Bharatiya Reserve Bank Note Mudran Private Limited with Reserve Bank of Australia Assistant Governor (Business Services) Lindsay Boulton and Micaal Sidorov of Reconnaissance speaking at the High Security Printing Asia Conference, Melbourne, December 2017

Wael Mrad of Crane Currency (left) with Deputy Head of Note Issue Department James Holloway at the High Security Printing Asia Conference , Melbourne, December 2017

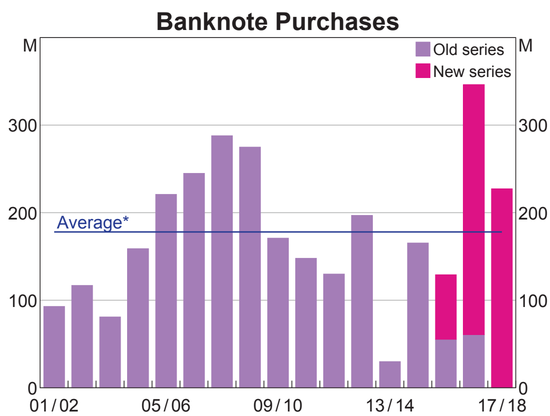
of the new security features; providing advice on the security merit of designs; and developing instrumentation for banknote examination. This was done in conjunction with a redesign of the Reserve Bank's quality assurance program for new banknotes and development of new testing methodologies that will form part of this program.

Note Printing Australia Limited (NPA)

NPA is a wholly owned subsidiary of the Reserve Bank that produces banknotes and supplies other related services to the Bank and some other entities. In 2017/18, NPA delivered 227 million Australian banknotes to the Bank, comprising around 44 million new series $10 banknotes and around 184 million new series $50 banknotes. This compared with 346 million Australian banknotes delivered to the Bank by NPA in 2016/17.

The aggregate amount paid by the Bank to NPA in 2017/18 for the supply of banknotes and related services was $82 million, compared with $99.9 million in the previous year.

In addition, NPA delivered 185 million banknotes under contract to Papua New Guinea, Singapore and Vanuatu in 2017/18, dealing directly with the respective central banks in those countries. NPA also produced 1.9 million P Series passports for Australia's Department of Foreign Affairs and Trade.



* Average banknote purchases over displayed time period

Source: RBA

International Financial Cooperation

The Reserve Bank participates actively in initiatives that seek to address the challenges facing the global economy and improve the global financial architecture. It does so through its membership of global and regional forums and its close bilateral relationships with other central banks.

Group of Twenty (G20)

Purpose

The G20 facilitates international cooperation on economic, financial and other policy issues among 19 systemically important economies from all regions of the world – including Australia – as well as with the European Union, International Monetary Fund (IMF) and other international organisations.

Reserve Bank Involvement

The Reserve Bank is represented at high-level meetings of the G20 by the Governor and Assistant Governor (Economic), while other senior staff participate in G20 working groups and contribute to the G20's financial regulation reform agenda.

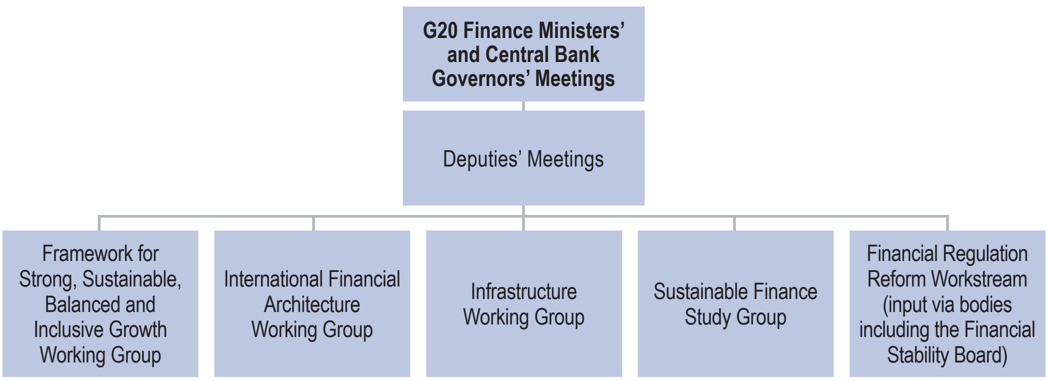
The G20 presidency was held by Germany from December 2016 to November 2017. In December 2017, the G20 presidency rotated to Argentina. A key theme of the Argentinian presidency is the future of work, where the focus has been on harnessing the benefits of technological change and identifying appropriate policy responses to support the associated economic transition and foster inclusive growth. Another important theme has been the promotion of infrastructure investment. Argentina established the Infrastructure Working Group, which is co-chaired by the Australian Treasury, to pursue this work. In April 2018, the G20 endorsed the Roadmap to Infrastructure as an Asset Class, which sets out a wide-ranging plan to address common barriers to private investment in infrastructure.

The G20 has continued to focus on strengthening the international monetary system. As part of this, the G20 has reiterated its commitment to further strengthening the Global Financial Safety Net, with a strong, quota-based and adequately resourced IMF at the centre. Accordingly, the G20 has committed to complete a review of the IMF's permanent 'quota' resources by late 2019; this review could influence the IMF's lending capacity over coming years. The G20 has also recently discussed the management of risks stemming from excessive volatility in capital flows, as well as how to promote sovereign debt sustainability and optimise multilateral development banks' balance sheets.

Financial regulation reform remains another important area of focus for the G20. Following the global financial crisis, major reforms were introduced globally, including Basel III (to build resilient financial institutions) and policies to mitigate the risks posed by systemically important financial institutions. As many of these post-financial crisis policy reforms have now been

Deputy Governor Guy Debelle (fourth row, fourth from left) with participants at the G20 Finance Ministers and Central Bank Governors Meeting, Washington DC, April 2018

Reserve Bank Involvement in the G20



implemented, the G20 and Financial Stability Board (FSB) are increasingly focusing on assessing the effectiveness of the reforms, and whether there have been any material unintended consequences. Accordingly, work is currently under way to assess whether core financial reforms are achieving their intended outcomes. The G20, in conjunction with the FSB and the global standard-setting bodies, also continues to monitor new and emerging developments and risks. This includes cyber threats and the financial stability implications of financial technology ('fintech'), including crypto-assets. The Reserve Bank, along with other Council of Financial Regulators (CFR) agencies, continues to work with overseas counterparts on these and other global regulatory issues.

Bank of Japan Governor Haruhiko Kuroda, Governor Philip Lowe, Federal Reserve Chairman Jerome Powell, European Central Bank President Mario Draghi and moderator Stephanie Flanders of Bloomberg Economics at the ECB Forum on Central Banking, Sintra, Portugal, June 2018

Financial Stability Board (FSB)

Purpose

The FSB promotes international financial stability by coordinating national financial sector authorities and international standard-setting bodies as they work towards developing strong regulatory, supervisory and other financial sector policies. It also plays a central role in assessing new and evolving trends and risks.

FSB members include representatives from 24 economies as well as the main international financial institutions – including the Bank for International Settlements (BIS) and the IMF – and standard-setting bodies such as the Basel Committee on Banking Supervision (BCBS).

Reserve Bank Involvement

The main decision-making body of the FSB is the Plenary. The Governor is a member of the Plenary, as well as the Steering Committee and the Standing Committee on Assessment of Vulnerabilities. The Governor is also Co-Chair of the Regional Consultative Group for Asia.

Senior staff members of Financial Stability Department participate in meetings of the:

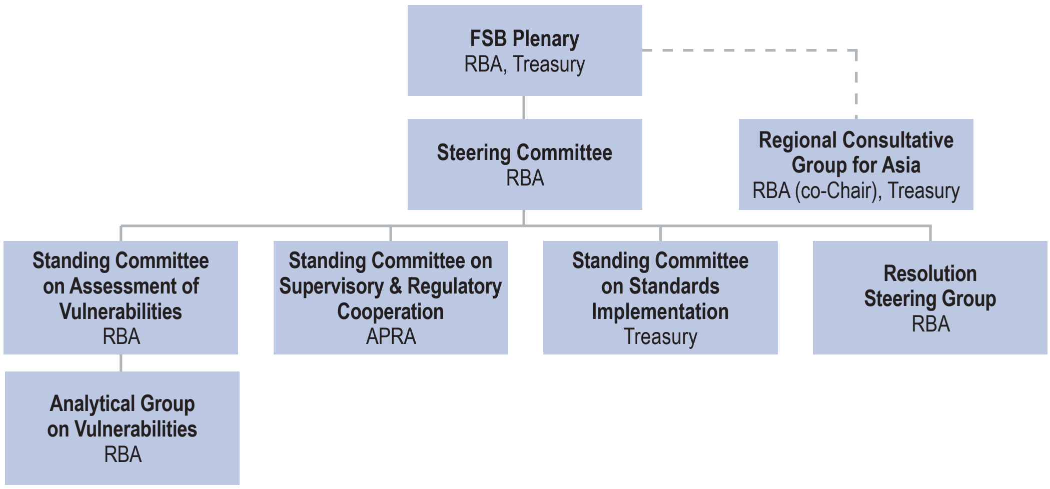
- Analytical Group on Vulnerabilities, which supports the work of the Standing Committee on Assessment of Vulnerabilities
- Resolution Steering Group
- Financial Innovation Network.

While the FSB has continued to pursue regulatory reforms of the global financial system, its focus has shifted in recent years from policy design and development to monitoring the implementation of the post-financial crisis reforms.[1] As noted above, it has also begun examining the effects of reforms and has commenced evaluations of the effects on financial intermediation and on incentives to centrally clear over-the-counter derivatives.

The Standing Committee on Assessment of Vulnerabilities is the main FSB body for identifying and assessing risks in the global financial system. Supporting this committee is the Analytical Group on Vulnerabilities, with the Financial Innovation Network providing input to both groups in relation to financial innovation and the degree to which it could be a source of systemic risk. Risks associated with fintech remain a focus

1 Further detail on FSB activities is reported in the Reserve Bank's semi-annual *Financial Stability Review*.

Australian Involvement in Key FSB Committees



of the Standing Committee on Assessment of Vulnerabilities and the FSB and G20 more broadly, particularly in light of the growth of crypto-assets.

The FSB continues to examine 'shadow banking' (defined as credit intermediation involving entities and activities outside of the regular banking system) and its transition to resilient market-based financing. In a report to the G20 in 2017, the FSB noted that aspects of shadow banking that contributed to the financial crisis (such as collateralised debt obligations) had declined substantially since the crisis, and generally are no longer considered to pose financial stability risks. Nonetheless, the report noted that new forms of shadow banking are likely to develop in the future, emphasising the importance of continued monitoring to mitigate associated risks. This monitoring is conducted in part by the FSB's Shadow Banking Experts Group, on which the Reserve Bank is represented.

Reserve Bank staff members were also involved in a number of other key FSB work areas during 2017/18, including:

- meetings of the Resolution Steering Group, which is progressing the FSB's work on enhancing resolution frameworks in line with its *Key Attributes of Effective Resolution Regimes for Financial Institutions* (the Key Attributes). The Resolution Steering Group has worked on several specific areas during the year in review, including: the adequacy of resources for central counterparty resolution; principles for bail-in execution; guidance on bank resolution funding plans; and a Key Attributes assessment methodology for the insurance sector
- meetings of the Cross-border Crisis Management Group for Financial Market Infrastructures, a Resolution Steering Group subgroup working on resolution arrangements for central counterparties
- meetings of the Regional Consultative Group for Asia, one of six regional groups established to expand the FSB's outreach activities with non-member economies and to examine issues relevant for the region.

As a member of several FSB committees, the Reserve Bank hosts committee meetings from time to time. In November 2017, the Bank hosted meetings in Sydney of the Analytical Group on Vulnerabilities and the Regional Consultative Group for Asia.

Bank for International Settlements (BIS)

Purpose

The BIS and its associated committees play an important role in supporting collaboration among central banks and other financial regulatory bodies. They do so by bringing together officials to exchange information and views about the global economy, vulnerabilities in the global financial system and other issues affecting the operations of central banks.

Reserve Bank Involvement

The Reserve Bank is one of 60 central banks holding shares in the BIS. The Governor or Deputy Governor attends the bimonthly meetings of governors and participates in meetings of the Asian Consultative Council. The Governor chairs the Committee on the Global Financial System, and the Assistant Governor (Financial Markets) is a member of the Markets Committee and the Committee on the Global Financial System.

The Committee on the Global Financial System seeks to identify potential sources of stress in the global financial system and promotes the development of well-functioning and stable financial markets. During 2017/18, the committee's discussions included analysing the structural changes that have emerged in the banking industry since the global financial crisis and the implications of rising household debt for financial and macroeconomic stability. The Markets Committee considers how economic and other developments, including regulatory reform and technological change, may affect financial markets, particularly central bank operations. Recent topics of discussion have included: developments in major financial markets, including in China; the functioning of short-term funding markets; the potential implications of central bank digital currencies for monetary policy implementation; and central banks' role in the reform of financial benchmarks.

During 2017/18, Reserve Bank staff have participated in a number of working groups of the Markets Committee and Committee on the Global Financial System, including:

- a Committee on the Global Financial System experts group on the implications of short-lived changes in banks' balance sheets around reporting dates ('window dressing')
- a Markets Committee study group on fast-paced electronic markets, which is due to report later in 2018
- a Committee on the Global Financial System working group on establishing viable capital markets, which is due to report later in 2018
- a Committee on the Global Financial System working group on the financial stability implications of a prolonged period of low interest rates.

Basel Committee on Banking Supervision (BCBS)

Purpose

The BCBS is hosted by the BIS and is the international standard-setting body for the banking sector. It provides a forum for regular cooperation on banking supervisory matters among its 28 member jurisdictions. It seeks to enhance understanding of key supervisory issues and improve the quality of banking supervision worldwide.

Reserve Bank Involvement

The Governor is a member of the Group of Governors and Heads of Supervision, which is the oversight body for the BCBS.

The Assistant Governor (Financial System) is a member of the BCBS.

A Deputy Head of Financial Stability Department is a member of the Macroprudential Supervision Group.

During 2017/18, the Group of Governors and Heads of Supervision endorsed a package of reforms to the Basel III capital framework, which are designed to reduce unwarranted variability in banks' risk weights as well as to increase the simplicity, comparability and risk sensitivity of the Basel framework. The finalisation of the reforms is the culmination of several years of work, with the Reserve Bank and the Australian Prudential Regulation Authority (APRA), as BCBS members, contributing to these discussions. Domestically, APRA has issued a consultation paper on modifications to the domestic capital framework that take account of these Basel III reforms.

The Macroprudential Supervision Group focuses on supervisory policies designed to address systemic risk arising from the banking sector, especially those posed by systemically important banks (SIBs). The group discussed several issues during 2017/18, including the sources of macrofinancial risks, finalising the review of the identification methodology for global SIBs, and country experience with implementing the Basel III counter-cyclical capital buffer.

Committee on Payments and Market Infrastructures (CPMI)

Purpose

The CPMI is hosted by the BIS, and serves as a forum for central banks to monitor and analyse developments in payment, clearing and settlement infrastructures and sets standards for them. It has members from 27 jurisdictions.

Joint working groups of the CPMI and the International Organization of Securities Commissions (IOSCO) bring together members of these two bodies to coordinate policy work on the regulation and oversight of financial market infrastructures.

Reserve Bank Involvement

Senior staff members from Payments Policy Department are members of the CPMI, CPMI-IOSCO Steering Group, CPMI-IOSCO Implementation Monitoring Standing Group, and CPMI-IOSCO Policy Standing Group. Senior staff have also participated in the Working Group on Digital Innovations and a task-force on wholesale payments security. A senior staff member from Payments Settlements Department has participated in the CPMI's RTGS (Real-time Gross Settlement) Working Group.

A senior staff member from Payments Policy Department contributed to developing a framework for supervisory stress tests. Another senior staff member contributed to a joint CPMI and Markets Committee (of the BIS) report on central bank digital currencies which was published in March 2018. Staff members also contributed to a number of CPMI-IOSCO implementation monitoring reports that have been published in 2017/18, including a follow-up assessment of certain aspects of central counterparties' financial risk management arrangements.

Cooperative Oversight Arrangements

Purpose

Several overseas-based financial market infrastructures hold Australian clearing and settlement facility licences, for which the Reserve Bank has certain regulatory responsibilities under the *Corporations Act 2001*. An overseas-based payments system also plays an important role in Australia's financial system. The Reserve Bank participates in several multilateral and bilateral arrangements to support its oversight of these financial market infrastructures as set out below.

Reserve Bank Involvement

Staff from Payments Policy Department participated in:

- an arrangement led by the Federal Reserve Bank of New York to oversee CLS Bank International, which provides a settlement service for foreign exchange transactions
- a global oversight college and a crisis management group for LCH Limited, both chaired by the Bank of England
- an information-sharing arrangement with the US Commodity Futures Trading Commission, in relation to CME Inc.
- the Society for Worldwide Interbank Financial Telecommunication (SWIFT) Oversight Forum, chaired by the National Bank of Belgium.

International Monetary Fund (IMF)

Purpose

The IMF oversees the stability of the international monetary system via:

- bilateral and multilateral surveillance, which involves monitoring, analysing and providing advice on the economic and financial policies of its 189 members and the linkages between them – Article IV consultations, which are a key means to do this, are conducted for Australia every year
- the provision of financial assistance to member countries experiencing actual or potential balance of payments problems.

Reserve Bank Involvement

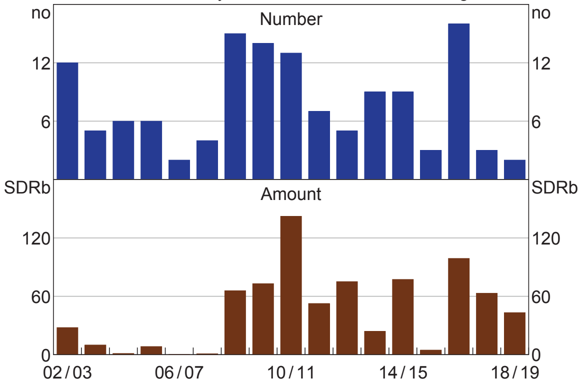
Australia holds a 1.39 per cent quota share in the IMF and is part of the Asia and the Pacific Constituency, which is represented by one of the IMF's 24 Executive Directors. The Reserve Bank supports the Constituency Office at the IMF by seconding an advisor with expertise in economic and financial sector matters. The Bank also works with the Australian Treasury to provide support to the Constituency Office on matters that are to be discussed by the IMF's Executive Board.

A core function of the IMF continues to be the provision of conditional financial assistance to member countries encountering balance of payments difficulties. During the IMF's 2017/18 financial year (which runs from May to April), the IMF provided three new lending arrangements (excluding concessional facilities) with a total value of 63 billion Special Drawing Rights (SDRs). There have been two new lending arrangements since the start of the IMF's 2018/19 financial year. This included a three-year SDR35 billion stand-by lending program to Argentina. IMF non-concessional credit outstanding increased by around 6 per cent in the 12 months to July 2018, with repayments by debtors more than offset by Argentina's use of its new arrangement.

The Reserve Bank and other CFR agencies worked closely with the IMF during 2017/18 as part of the IMF's 2018 Financial Sector Assessment Program (FSAP) review of Australia's financial system and regulatory framework. The FSAP is conducted every five years or so in jurisdictions with systemically important financial sectors (Australia's previous FSAP was in 2012). The IMF is focusing on assessing financial sector vulnerabilities and the overall framework for systemic risk oversight. The FSAP will include an assessment of Australia's banking regulatory

IMF New Arrangements*

IMF financial years, non-concessional lending



* IMF financial year runs from May to April; the observation for 18/19 is for May to July 2018; excludes augmentations of existing arrangements

Sources: IMF; RBA

framework and supervisory practices. It will also include reviews of the regulation of financial market infrastructures and the insurance sector, and crisis management arrangements. Following initial discussions in December 2017 on the scope of the review, the IMF FSAP team conducted an advance mission in June 2018 that involved in-depth meetings with the Bank and other CFR agencies, other government bodies, and private sector firms such as banks. The IMF's main mission is planned for the second half of 2018. A report with the key findings of the FSAP review is expected to be published early in 2019.

Executives' Meeting of East Asia-Pacific Central Banks (EMEAP)

Purpose

EMEAP brings together central banks from 11 economies in the east Asia-Pacific region – Australia, China, Hong Kong SAR, Indonesia, Japan, South Korea, Malaysia, New Zealand, the Philippines, Singapore and Thailand – to discuss issues relevant to monetary policy, financial markets, financial stability and payments systems in the region.

Reserve Bank Involvement

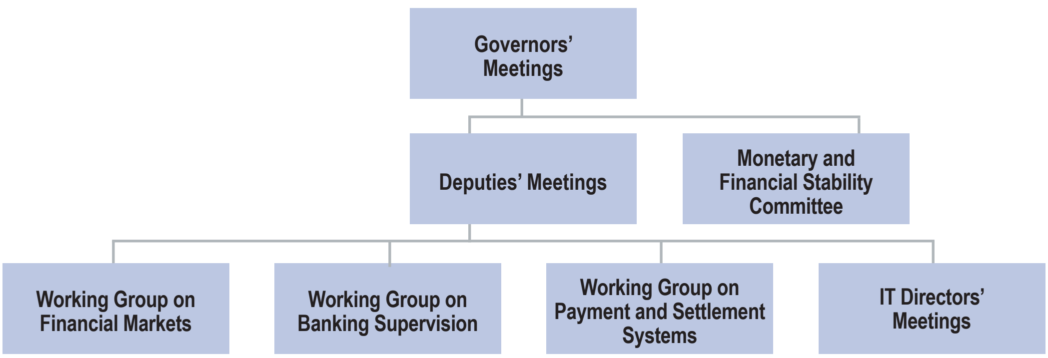
The Reserve Bank participates in EMEAP, including at the Governor and Deputy Governor levels. Senior staff also participate in the EMEAP Working Groups on Financial Markets, Banking Supervision, and Payment and Settlement Systems, and in meetings of Information Technology (IT) Directors. These groups also maintain close relationships with international institutions, such as the IMF and the BIS, through regular dialogue on topical issues.

The Monetary and Financial Stability Committee meeting provides an important forum for the discussion of current economic and financial market issues of direct relevance to EMEAP members. As Committee Chair, the Reserve Bank chaired two meetings of the Monetary and Financial Stability Committee in 2017/18, which were hosted by Bank Indonesia and the Monetary Authority of Singapore. Among other matters, these meetings considered the risks of trade protectionism, the effect on the region of monetary policy actions in advanced economies, macroprudential policies and capital flows, and the outlook for inflation in the region. Developments in fintech were also an important focus, given the potential risks and benefits for the financial system and possible implications for policymakers.

The Working Group on Financial Markets focuses on the analysis and development of foreign exchange, money and bond markets in the region. Every second meeting of this group is held in conjunction with the BIS Financial Markets Forum. The group continued its work on developing local currency bond markets, through the Asian Bond Fund Initiative (see the chapter on 'Operations in Financial Markets' for details of the Reserve Bank's investments in the Asian Bond Fund). The focus

Deputy Governor Guy Debelle (fifth from left) with participants at the 53rd EMEAP Deputies' Meeting, Jakarta, November 2017

Reserve Bank Involvement in EMEAP



in 2017/18 continued to be on development of money markets and securities lending in Asia.

The Working Group on Banking Supervision (which also includes representatives of EMEAP members' prudential regulators, including APRA) is a regional forum to share experiences about best practices in banking supervision and to discuss issues of relevance in the region. During the year, the group discussed issues such as the implementation of Basel III and other post-financial crisis reforms in the region, crypto-assets, and the importance of cyber-security risk management in financial institutions. The group also continued its focus on more traditional banking-related issues, such as bank resolution regimes and recovery planning, liquidity and loan loss provisioning.

The Working Group on Payment and Settlement Systems (which has recently been renamed the Working Group on Payments and Market Infrastructures) is a forum for sharing information and experiences relating to the development, oversight and regulation of retail payment systems and financial market infrastructures. The group discussed a range of issues during the year in review, including the:

- application of new technologies and other enhancements to financial market infrastructures, particularly those focused on building resilience
- development of fast retail payment systems and other efforts to facilitate the shift towards electronic payments
- emergence of crypto-asset markets
- initiatives to promote fintech development.

A study group of the Working Group on Payment and Settlement Systems has been examining the development and impact of various digital innovations on financial systems and central banks in the EMEAP region. The areas of focus for this group have included payments-related fintech, distributed ledger technology, cryptocurrencies and central bank digital currencies.

The IT Directors' Meeting provides a forum for discussions on developments in IT and its implications for central banks. Recent meetings have focused on IT developments within central banks, including the delivery of services and the IT underpinning payments systems.

Organisation for Economic Co-operation and Development (OECD)

Purpose

The OECD comprises the governments of 36 countries and provides a forum in which governments can work together to share experiences and seek solutions to common problems, including economic and financial ones.

Reserve Bank Involvement

The Reserve Bank's Chief Representative in Europe participates in the OECD's Committee on Financial Markets and the Advisory Task Force on the OECD Codes of Liberalisation.

The OECD Committee on Financial Markets examines a range of financial market issues and aims to promote efficient, open, stable and sound financial systems. As part of this effort, the committee holds semi-annual discussions with private sector experts, which recently covered long-term financing of sustainable infrastructure, convertible bonds and GDP-linked debt. The committee has also continued to review and contribute to the OECD's work on fintech and digitalisation, financial sector guarantees, long-term investment financing and green financing.

The OECD's Codes of Liberalisation are rules-based frameworks to promote the freedom of cross-border capital movements and financial services. All OECD members adhere to the codes. The Advisory Task Force on the OECD Codes of Liberalisation meets periodically to address questions and discuss policy issues related to the codes. It also examines specific measures by individual adherents with relevance to their obligations under the codes. During 2017/18, the task force continued to focus on its review of the Code of Liberalisation of Capital Movements.

Technical Cooperation and Bilateral Relations

The Government Partnership Fund

The Australian Government's 'Government Partnership Fund' program has supported an exchange of skills and knowledge between Australian public sector institutions and their Indonesian counterparts through a series of attachments and workshops since 2005/06.

In 2017/18, a total of 18 Bank Indonesia staff members were attached to the Reserve Bank, covering the areas of economic modelling, financial stability and human resources. These visits brought the total number of individual attachments since the start of the program to 215.

Engagement in the South Pacific

The Reserve Bank fosters close ties with South Pacific countries through participation in high-level meetings, staff exchanges and the provision of technical assistance across a wide range of central banking issues.

In November 2017, the Reserve Bank participated in the annual meeting of South Pacific Central Bank Governors, held in Nuku'alofa, Tonga. In addition to discussing recent economic developments in the region, there was considerable discussion of developments in correspondent banking and remittance flows in the region. There was also a meeting with the major regional commercial banks to discuss banking issues.

The Reserve Bank of Australia Graduate Scholarship for Bank of Papua New Guinea officers to undertake postgraduate studies at an Australian university in the areas of economics, finance and computing was first awarded in 1992. The most recent recipient of this scholarship commenced studies at the University of Queensland in July 2018; the previous recipient completed their studies in October 2016.

Governor Philip Lowe (third row, centre) at the European Central Bank (ECB) Forum on Central Banking, Sintra, June 2018

During 2017/18, Bank officers visited Papua New Guinea and Samoa to discuss monetary policy issues.

International visitors and secondments

As in previous years, the Reserve Bank hosted a number of overseas visitors, predominantly from foreign central banks. The visits covered the full range of the Bank's activities and included delegations from China, Indonesia, South Korea, Papua New Guinea, Russia, Saudi Arabia and the United States. The Bank also hosted a number of secondees from the Bank of Canada, the Bank of England and the Reserve Bank of New Zealand. A number of Reserve Bank staff were seconded to other central banks and various international organisations, including the BIS, the Bank of Canada, the Bank of England, the United States Federal Reserve, the IMF, the OECD and the Reserve Bank of New Zealand. These arrangements facilitate a valuable exchange of skills and expertise between the Bank and the broader global economic and financial policymaking community.

Community Engagement

The Reserve Bank devotes considerable effort to community engagement. Staff in the Bank's Head Office and State Offices work to help the community understand the Bank's role and, in turn, to understand the community's perspectives. The Bank supports academic research, continues to build its public education program, and also engages with the public through the Reserve Bank of Australia Museum.

Reserve Bank staff speak with many different groups across the general public, business and government to explain the Bank's role and actions and to hear the community's perspectives, priorities and concerns. In addition to the specific details of community engagement set out in this chapter, many more individual engagements of Bank staff – from the Governor through to staff from all parts of the Bank – occur each week with different individuals and groups throughout the community. These range from the public speeches given by senior Bank staff, as discussed in the chapter on 'Accountability and Communication', to small private discussions.

As noted in the chapter on 'Governance', the Reserve Bank Board meets in state capitals outside of Sydney on a regular basis. When the Board meets in a city where the Bank has an office (Adelaide, Brisbane, Melbourne or Perth), the Board meeting takes place in that office. Following the Board meeting, a dinner is held with members of the local community, including representatives and leaders from politics, business, the public sector, and educational and community organisations. Every few years, a similar dinner is held in Sydney. In 2017/18, dinners were held in Brisbane in September 2017 and in Adelaide in May 2018. These dinners provide an

Governor Philip Lowe speaking at a Reserve Bank Board community dinner, Brisbane, September 2017

(Left) Public Education Officer Mitchel De Los Mozos shows teachers the Bank's new education resources, June 2018; (right) teachers gather in the Bank's Head Office foyer at the second annual Teacher Immersion Event, Sydney, June 2018

opportunity to strengthen relationships between local communities and the Bank.

Public Education

A key part of the Reserve Bank's community engagement is interacting with students and educators, particularly in the field of economics. In 2016, the Bank significantly expanded and formalised its approach to public education, creating a Public Access & Education team. This team is dedicated to supporting educators and students and coordinates the efforts of staff across the Bank to deliver a public education program. The team's focus is on supporting economics students and educators at senior secondary and tertiary level. The program also extends to students at different stages of learning. Economic literacy is important to all Australians: individuals' everyday lives are affected by their own economic decisions and by the quality of economic decision-making by both business and government.

Nationally, the number of high school students studying economics in Year 12 has fallen by around 70 per cent over the past 25 years. The share of high schools offering economics as a subject has also fallen significantly over this period, with the decrease being most pronounced in comprehensive government schools. In addition, females have accounted for a sharply declining share of high school economic

The Bank's Public Access & Education team's focus is on supporting economics students and educators

(Top) Economist Alexandra Brown presents to students; (above left) Senior Research Manager Giancarlo La Cava addresses teachers at the Bank's Teacher Immersion Event, Sydney, June 2018; (above right) a participant at the Bank's 2018 Teacher Immersion Event, Sydney, June 2018

students. This is resulting in a student base for economics that is diminishing in both its size and diversity. The Bank is aiming to help redress this by ensuring that students have a stronger appreciation of what economics is, its relevance and the career opportunities that are available. The Bank is also creating content that is aligned with curricula, making more staff available for presentations and providing teachers with professional development opportunities.

Reserve Bank staff gave presentations to around 7,200 students and over 1,500 educators during 2017/18, across all states. In addition, they attended several major careers fairs and spoke directly with a further 2,000 students. The extent of interaction was made possible by the Bank's Ambassador program, which involves around 50 (mainly young) economists engaging with students and educators. The Ambassadors work closely with staff in the Bank's State Offices, who

A teacher examines the Bank's new education resources, Sydney, June 2018

participate in educational talks and help ensure that these talks are available to students and educators across the country. Visits are also made to universities.

The public education team continued to produce an array of resources in 2017/18. While these have been designed to support students and educators, they are also relevant for a more general audience. They range from simple one-page explanations of economic issues and concepts (the 'In a Nutshell' series) through to more detailed explanations of issues that students have frequently asked about (the 'Explainer' series). A suite of classroom activities was also produced, along with posters and videos that further explore key issues and explain the value of economics. The resources can be found in the newly developed education section of the Reserve Bank's website.

A second Teacher Immersion event for economics teachers was held at the Reserve Bank in June 2018. The event was formally acknowledged as professional development for maintaining Proficient Teacher Accreditation in New South Wales, as well as meeting accreditation requirements in other states. The event included presentations from a range of Bank staff on core economic topics relevant to teaching senior high school students. There were also practical sessions on how this content could be delivered in the classroom, along with opportunities for teachers to talk with the Bank's Ambassadors and participate in an economics Q&A with senior staff.


Photo: University of Sydney

Indigenous students from the University of Sydney's Wingara Mura-Bunga Barrabugu program who did some intensive economics immersion with Bank economists, Sydney, January 2018

the Bank's Ambassador program, … involves around 50 economists engaging with students and educators

In addition to the delivery of the public education program, research continued on enrolments in economics and the factors contributing to the falling size and diversity of the economics student population in Australia – both at high school and university. Key findings were communicated to the Reserve Bank's Educators Advisory Panel as well as publicly in speeches and external presentations.

The Educators Advisory Panel – which comprises external education experts to advise on the strategic direction of the Reserve Bank's public education program – met twice during 2017/18 to review progress with the program.

Reserve Bank of Australia Museum

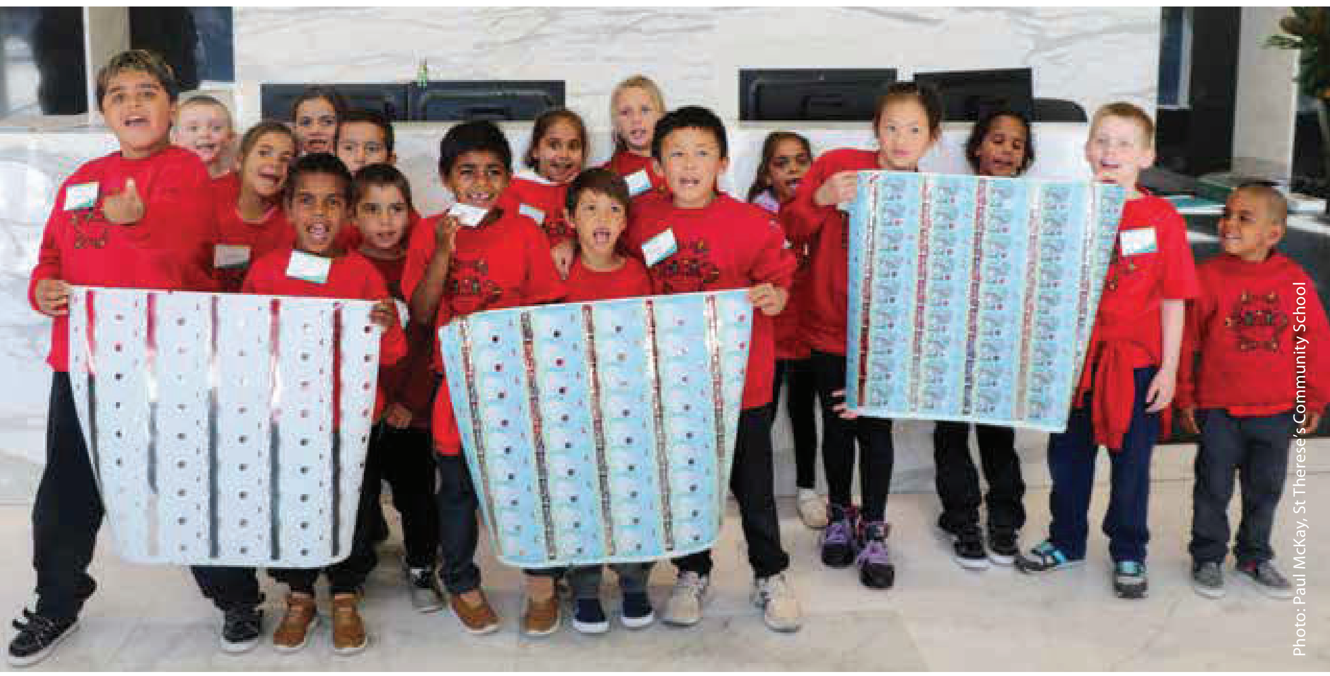
The Reserve Bank's Museum houses a permanent collection of artefacts and hosts periodic exhibitions. It also offers regular talks and tours for visitors and students. In the permanent collection, visitors can view the various types of money used before Federation through to the current innovative new series of banknotes. Visitors can observe the evolution of the nation's identity as expressed through its banknotes and learn about the influential women and men depicted on them. They can also see the artwork used in banknote design, learn about how banknotes are made and discover their security features.

The Museum has been showcasing banknotes from the new series in an additional permanent display called *A New Vision for Banknotes*. In

2017/18, information about the new $10 banknote was added to that for the $5 banknote, which had launched the new series in 2016. The display has been designed to capture the innovative qualities of the new banknote series, the details of their production and the fact that these banknotes allow the vision-impaired community to recognise each denomination more easily by having a tactile feature. The display highlights the new banknotes' artistic design and production process. In addition, a large multi-touch screen enables visitors to explore the design elements and security features of the new banknotes, along with the historical and social context of the imagery and stories that they contain.

Given the ongoing commemoration of the centenary of World War I in the community, the Museum retained its temporary exhibition entitled *Before Sunset: The Bank & World War I* for another year. The exhibition shows how World War I was associated with the emergence of central banking in Australia. It explains central bank functions, originally performed by a part of the Commonwealth Bank of Australia that later became the Reserve Bank, and showcases artefacts related to the Bank's involvement in the war, including financial documents and rare letters sent to the Governor of the day from the battlefields.

Around 13,000 people visited the Museum during 2017/18, fewer than in recent years, with construction works in Martin Place reducing the number of walk-in visitors. However, the number of organised visits to the Museum continued to increase. Nearly two-thirds of visitors were educational groups, spanning primary schools, secondary schools and universities. The number of secondary school students visiting the Museum has increased significantly in the past two years, consistent with the Reserve Bank's



Students from St Therese's Primary School in Wilcannia learn about the $10 banknote during a visit to the Reserve Bank of Australia Museum, Sydney, September 2017 public education initiatives. Senior school groups are offered talks about the role of the Bank and the economy that are aligned with their syllabus for economics and commerce. Talks are also available about the Museum exhibits and the new banknotes, including talks specifically on the Indigenous design elements in Australia's banknotes.

The Reserve Bank once again participated in Sydney Open in 2017 – an event designed to give the public access to important or unique buildings. There were over 1,600 visitors to the Bank's public foyer areas and Museum. These visitors attended talks about the architecture and design of the heritage-listed Head Office building. They also attended talks on the processes involved in the artistic design of a banknote, with visitors able to meet a designer of the new $10 banknote. In addition, smaller groups enjoyed access to select parts of the building where they received presentations about the Bank's art collection, which forms part of the cultural legacy of former Governor HC Coombs.

Most of the information in the Museum is depicted on the Museum's website. Additional resources were added to the Museum website in 2017/18, including an expansion of the existing online exhibition associated with World War I to mark the centenaries of the defining Western Front battles of 1918 in which former Bank staff were involved. There was also an online exhibition called *Make Your Money Fight!* in which rare archival items were curated and shared with the public digitally. The exhibition explored the central bank's response to the threat of inflation that stemmed from the dramatic reduction in unemployment and the scarcity of consumer goods during World War II. It explained the war loans campaign, the introduction of rationing and the austerity measures designed to support the war effort and restrain inflation – an exercise in which Australia's central banking functions were further developed.

Assistance for Research and Education

The Reserve Bank sponsors economic research in areas that are closely aligned with its primary responsibilities. This sponsorship includes financial support for conferences, workshops, data gathering, journals and special research projects, and encompasses areas of study such as macroeconomics, econometrics and finance. In addition, the Bank provides financial support to the Centre for Independent Studies and the Sydney Institute. It is a corporate member of the Lowy Institute for International Policy and The Ethics Centre. The Bank is a member organisation of the Committee for Economic Development of Australia (CEDA); the Bank's membership of CEDA includes an annual research contribution.

In 2017/18, the Reserve Bank continued its longstanding contribution towards the cost of a monthly survey of inflation expectations undertaken by the Melbourne Institute of Applied Economic and Social Research at the University of Melbourne. The Bank also maintained its contribution to a quarterly survey of union inflation and wage expectations undertaken by the Australian Council of Trade Unions.

The Reserve Bank continued to provide financial support for the *International Journal of Central Banking*, the primary objectives of which are to disseminate first-class, policy-relevant and applied research on central banking and to promote communication among researchers both inside and outside central banks.

The Reserve Bank is providing financial support for research on population ageing being conducted by the Australian Research Council Centre of Excellence for Population Ageing

Research, based at the University of New South Wales.

The Reserve Bank supports a number of conferences on economics and closely related fields. In 2017/18, these conferences included: the Economic Society of Australia's Australian Conference of Economists; the Melbourne Money and Finance Conference; the University of New South Wales Australasian Finance & Banking Conference; the University of Technology Sydney's Investment Management Research Program Conference; the PhD Conference in Economics and Business, held at the University of Melbourne; the Melbourne Institute Macroeconomic Policy Meetings; and the Government Economist Network Conference, held in Canberra. The Bank also supports the discussion of economic issues in the community by providing a venue for the Economic Society of Australia's Lunchtime Seminar and Emerging Economist Series.

In conjunction with the Australian Prudential Regulation Authority (APRA), the Reserve Bank has continued to sponsor the Brian Gray Scholarship Program, initiated in 2002 in memory of a former senior officer of the Bank and APRA. Three scholarships were awarded under this program in 2018. The cost to the Bank of these scholarships in 2017/18 was $22,500.

The total value of support offered for research and education in 2017/18 was $399,507.

Over 2017/18, the Reserve Bank responded to over 230 research requests for information from its archives and hosted a number of visitors to its dedicated research room. The majority of requests received were from Australian and overseas academics, post-graduate students, authors, numismatists, philatelists and genealogists. The Bank's archives contain a rich collection of records about its own activities and are in a variety of formats, which include documents, volumes, an extensive photographic collection, films, advertising material, banknotes and stamp printing items. The archives also have a collection of records of savings banks that amalgamated with the Commonwealth Bank of Australia, which date from 1832; these early colonial records were a focus of interest by researchers during 2017/18. They contain the banking records of convicts and significant figures in Australia's colonial past. With the continued interest in World War I, and in response to the Bank's *From Bank to Battlefield* online exhibition, requests for information on the Bank's role in the war effort increased, as did enquiries from descendants of Bank staff who fought in the war. Other enquiries of note related to women in banking and the role of Commonwealth Bank branches in regional Australia, and there were multiple requests for access to the archives' rich collection of historical photographs dating from 1913. Following the launch of the new Australian banknote series, requests for information relating to earlier banknote designs and the history of note issue in Australia were also received.

The program to digitise the Reserve Bank's most significant archival records continued during the year in review, with hundreds of thousands of records (including rare colonial ledgers and economic reports spanning the twentieth century) scanned and being made available electronically to researchers.

The Reserve Bank's Historian, Professor Selwyn Cornish of the Australian National University, is at an advanced stage of his research for the next volume of the official history of the Reserve Bank, which covers the period 1975–2000.

Charitable Activities

During 2017/18, the Reserve Bank made its 16th annual contribution of $50,000 to the Financial Markets Foundation for Children, which is chaired by the Governor. For many years, the Bank has donated a signed uncut banknote sheet to the ASX Thomson Reuters Charity Foundation for auction, which usually raises over $30,000. The Foundation includes the Financial Markets Foundation for Children in the distribution of auction proceeds. In August 2018, the Governor delivered his second address to the Anika Foundation's annual public event to raise funds to support research into adolescent depression and suicide; this was the 13th such event supported by the Bank in this way.

The Reserve Bank's corporate philanthropy program involves several initiatives, key among which involves dollar-matching staff payroll deductions (totalling $105,000 in 2017/18) organised by the Reserve Bank Benevolent Fund.

Reserve Bank staff participated in a number of volunteering activities in 2017/18 with The Smith Family, Foodbank, The Fred Hollows Foundation and Oxfam Australia.

The Reserve Bank's contributions under all these initiatives in 2017/18 totalled $167,875. In addition, the Bank facilitates staff salary sacrificing under a Workplace Giving Program.

Note Issue Department staff in Craigieburn volunteered at Foodbank, Melbourne, January 2018

Part 3:

Management and Accountability

Our People

The Reserve Bank seeks to attract, develop and retain high-quality people, and to foster an environment where there is a strong focus on values and behaviour, and a clear understanding of the Bank's risk appetite. This is supported by the Bank's People and Culture Strategy, which focuses on leadership development, diversity and inclusion. In 2017/18, the proportion of women in management increased and the Bank created additional employment opportunities for Indigenous Australians and those seeking flexible work arrangements. The total number of employees declined slightly. The composition of the workforce changed, reflecting the completion of a number of large projects.

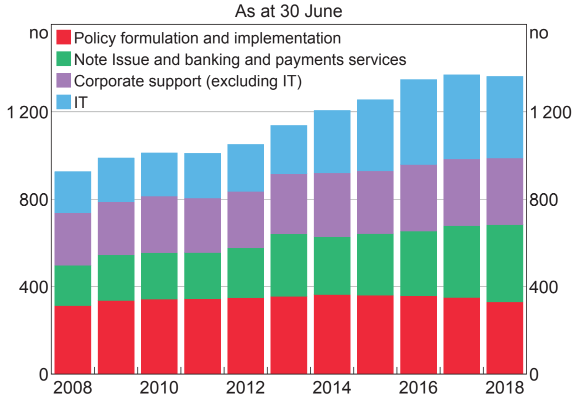
Workforce Profile

In June 2018, the Reserve Bank (excluding Note Printing Australia Limited) had 1,362 employees, of which 8 per cent worked part time. As such, the Bank's workforce comprised 1,327 full-time equivalent (FTE) employees. During 2017/18, there was a decrease in project resourcing as a number of large projects were completed, which was largely offset by an increase in staff to operate and support the new activities and services resulting from these projects. The overall number of employees is expected to decline in 2018/19 as further projects are completed.

During the year, the Reserve Bank hired 222 employees, of which 70 per cent were recruited on fixed-term contracts largely to support project-related work. The new recruits included information technology (IT) and project-related professionals. For non-project-related work, recruitment has taken place across all areas of the Bank. The graduate and internship programs continue to be an important recruitment channel for the Bank, particularly in the policy formulation and implementation areas. In 2017/18, these early career programs were supplemented by a number of mid-career hires.

RBA Employee Numbers*

As at 30 June



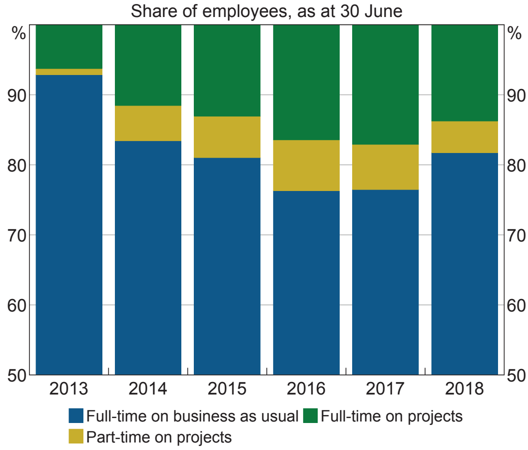
* Excludes NPA

Source: RBA

In the year to June 2018, the Reserve Bank hired 28 university graduates and 22 vacation-work interns. These graduates and interns work in the Bank's policy, business services and corporate support areas and hold degrees in economics,

RBA Employees Working on Projects*

Share of employees, as at 30 June



* Excludes NPA; calculation methodology revised in 2016

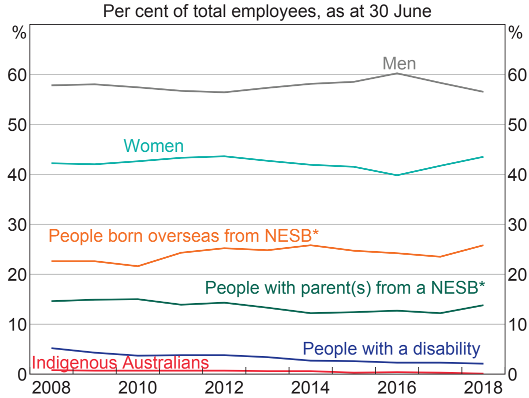
Source: RBA

commerce, IT and other professional disciplines. The Bank's workforce diversity profile has remained relatively stable over recent years.

The average age of Reserve Bank employees is 39 years, with almost two-fifths of employees under the age of 35. This reflects the Bank's strong focus on early-career hires each year through its graduate, internship and traineeship programs. The median tenure of employees is five years. During 2017/18, around 11 per cent of employees left the Bank. Resignations and retirements accounted for almost two-thirds of

Diversity Profile at the RBA

Per cent of total employees, as at 30 June



* Non-English-speaking background

Source: RBA

these exits. Contract expiration accounted for one-third of exits, given the high level of project-related work under way.

People and Culture

The Reserve Bank's core values, as set out in its Code of Conduct, help shape the Bank's culture and guide expectations and standards around workplace behaviour and professional conduct. The Bank's values are as follows.

1. Promotion of the public interest

We serve the public interest. We ensure that our efforts are directed to this objective, and not to serving our own interests or the interests of any other person or group.

2. Integrity

We are honest in our dealings with others within and outside the Bank. We are open and clear in our dealings with our colleagues. We take appropriate action if we are aware of others who are not acting properly.

3. Excellence

We strive for technical and professional excellence.

4. Intelligent inquiry

We think carefully about the work we do and how we undertake it. We encourage debate, ask questions and speak up when we have concerns.

5. Respect

We treat one another with respect and courtesy. We value one another's views and contributions.

There is a strong focus on these core values within the Reserve Bank, led by the Governor, and supported by the Bank's multi-year People and Culture Strategy. In 2017/18, the focus of this strategy remained to:

- identify aspects of the Bank's culture and work environment that are strengths, as

well as areas that need improvement, and measure progress in making improvements
- develop a deep and diverse pool of well-trained potential leaders
- fully utilise the talents of the Bank's people
- foster an inclusive and flexible work environment.

Steady progress in implementing the People and Culture Strategy continued to be made in 2017/18. In 2017, to support the first objective, the Reserve Bank undertook its third employee engagement survey. The survey is a useful tool for identifying our strengths as an organisation and opportunities for improvement. In the survey, employees reported a high level of engagement, consistent with the previous two surveys. Results also reflected the effectiveness of departmental and enterprise-wide action plans, particularly work aimed at improving the areas of empowerment and communication. The survey indicated that our key strengths are in the areas of leadership, diversity, a shared focus on the Bank's values among staff at all levels and providing a supportive work environment. Efforts will continue to address issues identified in this and previous employee engagement surveys, with a focus on improving collaboration, organisational change, decision-making, retention and career opportunities. Recent areas of focus have also included further encouragement for staff to speak up when they have a different opinion or a concern, and enhancing their understanding of appropriate risk-taking in pursuit of the Bank's objectives. A further survey will be conducted in around two years to assess progress and identify new opportunities.

The Reserve Bank continued its focus on leadership development, talent management and diversity and inclusion during the year in

Our key strengths are leadership, diversity, a shared focus on the Bank's values and a supportive work environment

review. Following completion of the Bank's Executive Leadership Development Program and Empowering Leaders Development Program for future leaders, a new Engaging Leaders Program was introduced for people managers to build capability and confidence across the cohort in core leadership and people management.

The People and Culture Strategy also places emphasis on ensuring that the talents of employees are fully utilised and developed. On-the-job development opportunities are supplemented by formal training and professional development programs, including:

- the eight-week Internship Program, which provides high-performing university students work experience and training through the completion of an applied research project. This program is an important source of early-career professionals for the Reserve

Bank's Graduate Development Program. In 2017/18, 22 interns joined the Bank

- the two-year Graduate Development Program, consisting of a range of tailored training programs to develop policymaking frameworks, effective business writing, critical thinking, presentation, communication and negotiation skills. A total of 63 graduates participated in the program in 2017/18
- training as required in technical, management and leadership skills, resilience and other general competencies, such as communication skills
- regular training in the Bank's compliance obligations, including in relation to work health and safety, mental health and wellbeing, fraud awareness and anti-money laundering/counter-terrorism financing.

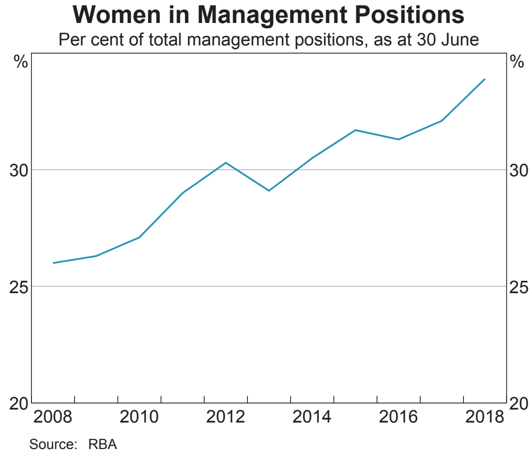
Development opportunities are provided to employees by facilitating internal rotation programs between different areas of the Reserve Bank and external secondments. The Bank also hosts secondees from external institutions to foster corporate networks and share understanding of best practice. In 2017/18, the breadth of secondment activities increased, involving a wide range of Australian institutions, including the Australian Bureau of Statistics, the Australian Competition and Consumer Commission, the Australian Prudential Regulation Authority, the Australian Treasury and the Commonwealth Department of the Prime Minister and Cabinet, as well as a range of international institutions (see the chapter on 'International Financial Cooperation' for details).

almost **80 per cent** of employees reported that they had **worked flexibly** in some way

The Reserve Bank encourages employees to develop their skills continually and provides financial support to employees for part-time study in disciplines related to their work, with 71 employees benefiting from this support during 2017/18. In addition, the Bank provided support to nine employees undertaking full-time postgraduate study at universities in Australia and overseas during this period.

The People and Culture Strategy actively promotes an inclusive work environment. The Reserve Bank's Diversity and Inclusion Council and Employee Resource Groups (ERGs) continued to pursue activities and practices that support the Bank's Diversity and Inclusion Plan. The Bank continues to support flexible work practices, including part-time work and job-share arrangements. The Bank also enables flexible ways of working full time, by supporting changes in work patterns or location, including altering start or finish times, working compressed work weeks, and working from home or other locations. In the 2017 employee engagement survey, almost 80 per cent of employees reported that they had worked flexibly in some way in the preceding 12 months. In 2017/18, an additional flexibility initiative, the MOVE program (Managerial roles Offering Variable and flexible Employment), was launched. The program seeks to attract candidates with skills and experience that are important to the Bank, and to tailor roles to meet the flexibility candidates need to be successful and engaged in meaningful work. So far, two roles at the senior management level have been filled through the program. Training and resources were also offered to managers to ensure they are equipped to manage flexible work requests.

The overall representation of women in management at the Reserve Bank was 34 per cent in June 2018, up from 32 per cent in the previous year. During the year, 50 per cent of managerial vacancies were filled by women, and 80 per cent of roles at the senior manager level and above were filled by women. The Bank has a gender target of 35 per cent of management positions to be filled by women by 2020, with a longer-term aim of 50 per cent. In support of the



50 per cent of managerial vacancies were filled by women, and 80 per cent of roles at the senior manager level and above were filled by women

Assistant Governor (Corporate Services) Susan Woods speaking to staff at the Reserve Bank's town hall event, Sydney, March 2018.

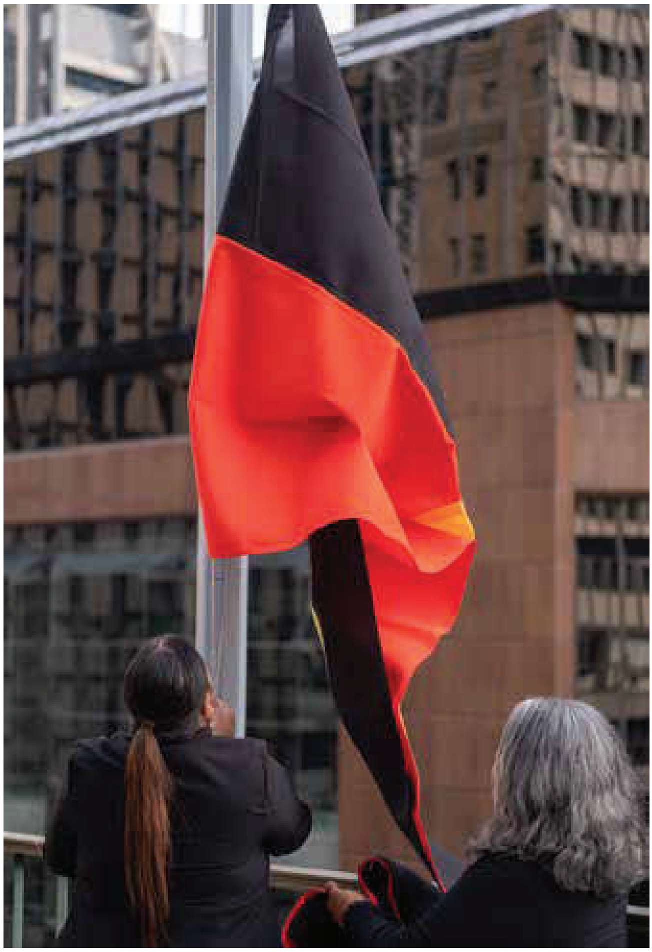
gender target, there is a strong focus on talent management at the Bank, including succession and development planning for both women and men, and measures to ensure diversity of candidates in all selection processes.

The Reserve Bank actively works to promote economics, finance, mathematics and IT as career options for women. The Bank's Public Access & Education team is dedicated to providing learning experiences and information to schools, universities and educators about the economy and the role of Australia's central bank (see the chapter on 'Community Engagement' for details). The Bank awarded its second annual scholarship for teachers in 2017 to help promote and support the study of economics in schools, particularly by females. The first scholarship recipient worked closely with the Bank during the year in review on a research project examining factors that may encourage the participation of female students in economics at secondary and tertiary levels.

To promote the inclusion of Indigenous Australians in the workplace, the Reserve Bank's Reconciliation Action Plan (RAP) Working Group launched the Bank's first RAP. A major initiative was the installation of a second flagpole at the Reserve Bank's Head Office to permanently display the Aboriginal flag as a symbol of the Bank's commitment to reconciliation. A flag-raising ceremony, accompanied by an Acknowledgement of Country, was conducted during National Reconciliation Week in late May 2018. Flag stands displaying both the Australian and Aboriginal flags have also been installed at the Bank's other locations around Australia. An Acknowledgement of Country is also now incorporated into major Bank events.

The Reserve Bank continued to fund an internship for Indigenous Australian university students, with four recipients in 2017/18. The internship was facilitated by CareerTrackers,

The Reserve Bank's first Reconciliation Action Plan was launched



Trainee Shakeela Williams, assisted by Susan Moylan-Coombs (granddaughter of the Bank's first Governor, Dr HC Coombs), raises the Aboriginal flag at the Bank's Head Office building during National Reconciliation Week, May 2018

Wayne Byres (Payments System Board member and APRA Chairman), Governor Philip Lowe, Shakeela Williams and Susan Moylan-Coombs at the flag raising ceremony, May 2018

a not-for-profit agency that works with organisations to provide work experience, networking and professional development opportunities for Indigenous Australian university students. The internship involved vacation work at the Bank as well as professional development training. During the year, the Bank refocused its traineeship program on providing work experience and a nationally recognised qualification to Indigenous Australians. Four trainees were involved in the first year of the program. The Bank also welcomed two tertiary students with a disability through the Australian Network on Disability's 'Stepping Into' internship program and continues to provide long-term employment for individuals with intellectual disabilities through the JobSupport program.

The Reserve Bank raised employees' awareness and involvement in diversity and work health and safety matters by supporting staff participation in external events and hosting guests at the Bank to speak on diversity, inclusion and health-related topics. Diversity events included speakers on gender and race matters, along with events to mark NAIDOC week, Reconciliation Week, Harmony Day, Wear It Purple Day, International Women's Day and Global Accessibility Awareness Day. In addition, the Bank continued to raise awareness about mental health in the workplace, including through R U OK?Day activities, and other initiatives from its newly developed mental health strategy to support the prevention of workplace mental health issues.

Remuneration

Remuneration packages for Reserve Bank staff are designed to attract and engage high-calibre employees. In line with the Bank's commitment to openness and transparency, the distribution of remuneration paid to Bank executives and other senior employees on a cash basis is set out in the tables below. The provision of this information is consistent with similar information provided by other Commonwealth entities.

The Reserve Bank's Workplace Agreement provides for a performance-based salary increase distributed from a pool equivalent to 2 per cent of salaries. The agreement makes available an additional lump-sum performance-based payment distributed from a pool of 2 per cent of salaries.

Remuneration of Executives

Remuneration paid to executives in 2017/18 ($)[(a)]

Remuneration band	Number	Reportable salary[1]	Superannuation[2]	Lump sum[3]	Total
$0 to $200,000	4	137,928	21,429	–	159,357
$200,001 to $225,000	1	184,998	29,250	–	214,248
$250,001 to $275,000	1	222,968	35,412	1,295	259,675
$275,001 to $300,000	1	249,108	39,111	5,036	293,255
$300,001 to $325,000	1	267,891	43,667	2,290	313,848
$325,001 to $350,000	9	287,544	46,806	4,607	338,957
$350,001 to $375,000	6	308,203	46,595	5,594	360,392
$375,001 to $400,000	3	322,525	52,117	5,572	380,214
$400,001 to $425,000	2	348,154	57,630	6,833	412,617
$425,001 to $450,000	1	370,676	61,632	6,567	438,875
$450,001 to $475,000	3	385,767	65,004	4,204	454,975
$475,001 to $500,000	3	405,615	69,111	6,125	480,851
$500,001 to $525,000	3	437,561	74,266	8,495	520,322
$550,001 to $575,000	2	476,679	82,109	8,261	567,049
$575,001 to $600,000	1	486,739	82,735	6,260	575,734
$600,001 to $625,000	1	521,582	89,520	9,540	620,642
$625,001 to $650,000	1	542,080	92,807	14,483	649,370
$750,001 to $775,000	1	679,000	85,963	–	764,963
$1,000,001 to $1,025,000	1	903,418	114,617	–	1,018,035
Total	**45**				

(a) Includes total remuneration earned in Australia during the reporting period by executives at desk (or on parental or annual leave) as at 30 June 2018; each row shows an average figure based on the number of employees within each remuneration band based on total remuneration earned on a cash basis; an executive for the purpose of this table is anyone holding a position of Deputy Head of Department (or equivalent) or above

Source: RBA

Notes

(1) The 'reportable salary' column is prepared on a cash basis using reportable salary, defined as the sum of gross payments (excluding lump sum payments); reportable fringe benefits amount; reportable employer superannuation contributions; and exempt foreign employment income, as reported in an individual's payment summary.

(2) The 'superannuation' column is calculated as: the actual defined contribution amounts for individuals who are in a defined contribution scheme; and for individuals who are in a defined benefit scheme, an amount equal to 15.4 per cent of superannuable salary plus any employer productivity contributions.

(3) The 'lump sum' column is prepared on a cash basis using actual lump-sum performance-based payments paid to individuals during the reporting period.

Remuneration of Other Senior Employees

Remuneration paid to other senior employees in 2017/18 ($)[(a)]

Remuneration band	Number	Reportable salary[1]	Superannuation[2]	Lump sum[3]	Total
$200,001 to $225,000	66	178,029	29,733	3,368	211,130
$225,001 to $250,000	37	198,880	33,940	3,570	236,390
$250,001 to $275,000	23	221,398	36,354	3,721	261,473
$275,001 to $300,000	8	240,153	39,608	5,564	285,325
$300,001 to $325,000	6	261,503	42,383	4,292	308,178
Total	**140**				

(a) Includes total remuneration earned in Australia during the reporting period by other senior employees at desk (or on parental or annual leave) as at 30 June 2018; each row shows an average figure based on the number of employees within each remuneration band based on total remuneration earned on a cash basis.

Source: RBA

Notes

(1) The 'reportable salary' column is prepared on a cash basis using reportable salary, defined as the sum of gross payments (excluding lump sum payments); reportable fringe benefits amount; reportable employer superannuation contributions; and exempt foreign employment income, as reported in an individual's payment summary.

(2) The 'superannuation' column is calculated as: the actual defined contribution amounts for individuals who are in a defined contribution scheme; and for individuals who are in a defined benefit scheme, an amount equal to 15.4 per cent of superannuable salary plus any employer productivity contributions.

(3) The 'lump sum' column is prepared on a cash basis using actual lump-sum performance-based payments paid to individuals during the reporting period.

Management of the Reserve Bank

The Reserve Bank has a strong emphasis on efficiency and cost control, supported by a focus on continuous improvement and established budget processes. Technology plays a key role in the Bank's ongoing operations and forms a major component of a number of the Bank's strategic projects. Further significant progress was made on projects in 2017/18, with completion of the settlements infrastructure supporting the New Payments Platform (NPP) and enhancements to banknote logistics. Accordingly, project costs declined, although the Bank's general operating costs increased as a result of operating this new infrastructure.

Financial Management

The Executive Committee supports the Governor in overseeing the Reserve Bank's budget and the Investment Committee – comprised of a smaller group of senior executives, with the Deputy Governor as chair – oversees the Bank's portfolio of project work. The Investment Committee ensures spending on projects is prioritised to those that generate the most effective outcomes.

The Reserve Bank's costs arise from its ongoing activities associated with its key policy and operational responsibilities, and from its investment in strategic projects to support these responsibilities. Operating costs associated with the provision of banking and payments services are largely recouped through fee income for these services. Earnings arising from the Bank's investments in financial markets are detailed in the chapter on 'Earnings, Distribution and Capital'.

The Reserve Bank's general operating costs, excluding depreciation, rose by 1.4 per cent in 2017/18. Staff costs continued to represent about two-thirds of the Bank's general operating

General Operating Costs[a]
$ million

	2013/14	2014/15	2015/16	2016/17[b]	2017/18
Staff costs	184.6	195.3	212.8	216.3	223.8
Other costs	66.0	65.7	71.9	88.3	85.2
General operating costs (excluding depreciation)	250.6	261.0	284.7	304.6	309.0
Depreciation	21.9	23.3	25.6	38.4	51.8
General operating costs	272.5	284.3	310.3	343.0	360.8
Of which:					
Cost of projects	18.4	28.0	34.9	43.7	35.0

(a) Excluding NPA and banknote management expenses, and costs directly linked with transaction-based revenue
(b) Some costs have subsequently been reclassified
Source: RBA

expenses. The increase in costs reflected new operating costs associated with the implementation of major strategic projects. The delivery of the strategic initiatives in recent years led to a notable rise in depreciation, such that total costs for ongoing activities rose by about 5 per cent in 2017/18.

Total project-related costs declined during 2017/18, as several large projects that had begun in previous years were completed, including the settlements infrastructure supporting the NPP and delivery of an automated banknote storage and processing facility in the new National Banknote Site.

The Reserve Bank has an ongoing program of investment to maintain the value of its physical assets, including buildings, to ensure that services remain effective and resilient and that associated risks are managed appropriately. The extent of the Bank's investment in its strategic initiatives is reflected in its capital expenditure over recent years. Capital outlays declined by more than half in 2017/18, to $45.7 million. This expenditure was concentrated on completing the major initiatives noted above. With much of this work now having been completed, capital spending is expected to remain around this level in coming years, which is sufficient to maintain the Bank's core systems and infrastructure.

In 2016/17, the Reserve Bank commissioned an external review of its operations, to help gain assurance that those operations were being conducted in a way that is both appropriate and makes effective use of public money. 2017/18 saw the implementation of the recommendations, with the most significant being the creation of a shared services capability and centralisation of various support services, including selected finance, procurement and administrative functions. The Bank will work to improve the efficiency and effectiveness of these support services further over coming years.

The Reserve Bank engages consultants from time to time where it lacks specialist expertise or if independent research, review or assessment is required. Consultants are typically engaged to: investigate or diagnose a defined issue or problem; carry out defined reviews or evaluations; or provide independent advice or information to assist in the Bank's decision-making. Prior to engaging consultants, the Bank takes into account the skills and resources required for the task, the skills available internally and the cost-effectiveness of engaging external expertise. Spending on consultancies over the past eight years is shown below. As in previous years,

Spending on Consultancies[(a)]
$

2010/11	102,000
2011/12	535,000
2012/13	1,190,000
2013/14	387,000
2014/15	773,000
2015/16	622,520
2016/17	987,388
2017/18	596,157

(a) Sum of individual consultancies that cost $10,000 or more
Source: RBA

Capital Expenditure[(a)]
$ million

	2013/14	2014/15	2015/16	2016/17	2017/18
Capital costs	44.2	56.5	108.1	100.7	45.7
Of which:					
Cost of major projects[(b)]	18.6	42.9	92.8	85.8	39.5

(a) Excluding NPA
(b) Projects on the Enterprise Master Schedule
Source: RBA

(Top; above) Machines at the automated banknote storage and processing facility in the new National Banknote Site, Craigieburn

consultancy support during 2017/18 covered a range of activities, with around one-third of spending related to the upgrade of Australia's banknotes and banknote-related infrastructure.

Information Technology Management

Many of the Reserve Bank's activities depend heavily on information technology (IT) systems and infrastructure. This includes more than 200 business applications, two highly available data centres and a highly resilient network infrastructure across multiple Bank sites.

As noted above, major projects in 2017/18 included completion and rollout of the NPP and its supporting Fast Settlement Service (FSS), and delivery of the automated banknote storage and processing facility in the new National Banknote Site. The Bank's PeopleSoft Financials platform was also upgraded and a new Bank-wide Learning Management System was implemented.

Work has also continued on the modernisation of the Reserve Bank's own banking platforms used to service its customers (the largest of which is the Australian Government), the transition to the Windows 10 desktop platform for all staff, and the development of the Bank's business intelligence platform.

Cyber security continues to be a key focus for the Reserve Bank and in 2017/18 significant resources were applied to further strengthen the Bank's cyber security capabilities. The Bank has been independently certified as complying to a mature standard with the cyber security strategies recommended by the Australian Signals Directorate for containing cyber threats, and will continue to build on its security controls as these strategies and standards evolve. The Bank has also attained certification of its internet gateway to the ISO 27001 global standard for Information Security Management.

With several major IT projects of recent years now largely complete, the IT function continues to transition to a steady-state model. This transition involves an uplift of steady-state capacity to accommodate the support and maintenance of the new applications introduced by these projects, and the addition of new capabilities to support the evolving nature of technology, including cyber security, cloud, big data and outsourcing. The Reserve Bank also continues to pursue strategies to ensure IT assets are highly resilient, fit for purpose, appropriately innovative and support workplace efficiency. These include investigating capabilities in the fields of blockchain and distributed ledger technologies, software-defined networks and machine learning.

Facilities and Environmental Management

The Reserve Bank owns premises in locations where there is a business need to do so. The Bank's facilities include the Head Office in Sydney; the H.C. Coombs Centre for Financial Studies in Kirribilli, Sydney; office buildings in Melbourne and Canberra; the note-printing facility and National Banknote Site at Craigieburn, north of Melbourne; and the Business Resumption Site in north-west Sydney. In addition to the buildings it owns, the Bank leases accommodation for its State Offices in Adelaide, Brisbane and Perth and for its offices in London, New York and Beijing. Independent valuers estimated that the value of the Bank's property assets increased by $72.4 million to $594.7 million in 2017/18, reflecting increased property values in Sydney and Melbourne.

Accommodation in the Reserve Bank's properties that is not required for its own business purposes is leased to external tenants. Net income from these leases amounted to $12.3 million in 2017/18, compared with $11.4 million in the previous year.

During the year in review, major projects included the commissioning of the facilities, security infrastructure and operational arrangements at the National Banknote Site, modernisation of the passenger and goods lifts at Head Office to improve reliability and performance, and upgrades to the fire safety systems at Head Office. The Reserve Bank also undertook a review of its property portfolio to ensure it remains appropriate for the purposes of the Bank. Following the commencement of operations at the National Banknote Site in late 2017, the Bank's building at 60 Collins Street, Melbourne, was no longer needed to store and distribute banknotes. Accordingly, a decision was made to sell this building and that process has commenced. The Bank is also planning building works at its Head Office at 65 Martin Place, Sydney, and the H.C. Coombs Centre for Financial Studies in Kirribilli, Sydney. These works are aimed at upgrading base building infrastructure that is at end of life and ensuring a safe, efficient and effective workplace to meet the long-term needs of the Bank, while preserving heritage features.

The Reserve Bank is committed to improving the environmental performance of its operations. The Bank has developed policies that are consistent with the principles of ecologically sustainable development as set out in the *Environment Protection and Biodiversity Conservation Act 1999*. These policies serve to reduce the impact of the Bank's operations on the environment and include initiatives to:

- reduce energy, water and paper consumption
- increase the recycling of paper, co-mingled waste and printer cartridges
- adopt environmentally sustainable office fit-out designs
- implement sustainability measures such as use of 50/50 recycled paper and biodegradable takeaway coffee cups in the staff cafeteria
- increase the use of fuel-efficient vehicles.

Specific improvements to the performance of the infrastructure of the Reserve Bank's buildings in 2017/18 included:

- implementation of an integrated energy metering and data monitoring system to measure overall energy consumption across specific buildings, enabling the Bank to optimise its energy use
- ongoing data centre load monitoring and balancing at the Business Resumption Site and Head Office to reduce electricity consumption
- implementation of LED lighting on a progressive basis across all sites and reductions in the use of artificial lighting, reducing electricity consumption for lighting needs
- improved performance of heating systems at each site, including a hot water system upgrade at Head Office, to reduce gas consumption.

In addition, the Reserve Bank is developing plans for increased use of renewable energy (solar power) at its sites.

Electricity consumption at all Reserve Bank-operated sites increased by 3.29 per cent in 2017/18, compared with average consumption over the preceding five years. This reflects higher usage associated with a full year of operations at the National Banknote Site and increased loads in the Bank's data centres as a result of new systems coming into operation. Gas consumption in 2017/18 declined by 9.36 per cent compared with the previous year, as a result of optimising the heating systems and upgrades to domestic hot water systems. Water consumption in 2017/18 was 1.9 per cent higher than in the previous year, reflecting the additional usage for the National Banknote Site.

Risk Management

In meeting its objectives, the Reserve Bank takes on a variety of risks. The framework through which these risks are managed is overseen by the Risk Management Committee. The Bank seeks to promote a strong risk management culture and deploys a framework designed to ensure the consistent management of strategic, operational and financial risks.

Objectives and Governance Structure

The Reserve Bank encounters a broad range of risks in fulfilling its responsibilities. Management of these risks is the responsibility of all staff. In particular, managers have a responsibility to evaluate their risk environment, put in place appropriate controls and ensure that these controls are well developed and implemented effectively. The Bank identifies, assesses and manages risk at both an enterprise ('top-down') and business ('bottom-up') level, a process that is subject to ongoing review. These risks are managed to a level that is consistent with the Bank's risk appetite through processes that emphasise the importance of integrity, intelligent inquiry, maintaining high-quality staff and public accountability. The development and maintenance of an active risk management culture that acknowledges the need for careful analysis and management of risk in all business processes is an important objective of this framework.

Oversight of the Reserve Bank's arrangements for risk management is undertaken by the Risk Management Committee. The committee is chaired by the Deputy Governor and comprises: the Assistant Governors for the Business Services, Corporate Services and Financial Markets groups; the Chief Financial Officer; the Chief Information Officer; the Heads of the Audit, Human Resources, Information, and Risk and Compliance departments; and the General Counsel. The Risk Management Committee meets at least six times each year and keeps the Executive Committee and the Reserve Bank Board Audit Committee informed about its activities.

The Risk Management Committee is responsible for ensuring the proper assessment and effective management of all the risks the Reserve Bank faces, with the exception of those arising directly from its monetary and financial stability policies and payments policy functions. These risks remain the responsibility of the Governor, the Reserve Bank Board and the Payments System Board. The risks associated with the Bank's ownership of Note Printing Australia Limited (NPA) are overseen by the Reserve Bank Board. The NPA Charter, which is reviewed annually by the Reserve Bank Board, defines the scope of NPA's activities and sets out the approach to risk management to be taken by the NPA Board. However, responsibility for the day-to-day activities of NPA rests with the NPA Board and management. The Bank's risk management framework covers the relationships that it has with NPA other than its ownership –

for example, the relationships of customer and supplier, and landlord and tenant.

The Risk Management Committee is assisted in its responsibilities by the Risk and Compliance Department. The department's main role is to assist individual business areas to manage their risk and compliance environment effectively within a framework that is broadly consistent across areas. It also monitors risk and performance associated with the Reserve Bank's activities in financial markets and supports the business areas by implementing Bank-wide control frameworks covering fraud, bribery and corruption, business continuity and compliance-related risks. The Head of Risk and Compliance Department reports directly to the Deputy Governor.

The Audit Department undertakes a risk-based audit program to provide assurance that risks are identified and key controls to mitigate these risks are well designed and working effectively. This includes periodic reviews of the Reserve Bank's risk management framework and testing key controls in business areas on a sample basis. The Head of Audit Department reports directly to the Deputy Governor and the Chair of the Reserve Bank Board Audit Committee.

Portfolio Risks

The Reserve Bank holds domestic and foreign currency-denominated financial instruments to support its operations in financial markets in pursuit of its policy objectives. These instruments account for the majority of the Bank's assets and expose its balance sheet to a number of financial risks. The primary responsibility for managing these risks rests with the Financial Markets Group. Risk and Compliance Department monitors these risks and assesses compliance with approved authorities and limits. Compliance with financial management guidelines and developments in portfolio risks are reported to the Risk Management Committee.

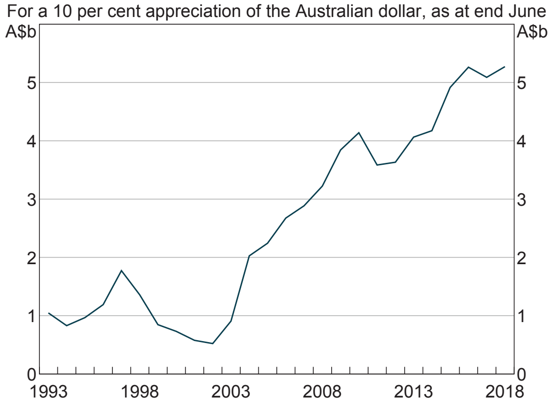
Exchange rate risk

The Reserve Bank is exposed to exchange rate risk as a large share of the Bank's assets are denominated in foreign currency, while most of the Bank's liabilities are denominated in Australian dollars. As foreign currency assets are held for policy purposes, the Bank does not seek to eliminate or hedge this exposure. However, the Bank mitigates some of this risk by diversifying these assets across various currencies. The foreign benchmark portfolio has target shares of 55 per cent in US dollars, 20 per cent in euros and 5 per cent each in Japanese yen, Canadian dollars, UK pound sterling, Chinese renminbi and Korean won. This benchmark portfolio composition reflects the Bank's risk appetite and desired liquidity to meet policy objectives. Some limited variation in actual portfolio shares from the target shares is permitted to limit the cost of replicating the benchmark portfolio. The Bank's holdings of gold and Special Drawing Rights (an international reserve asset created by the International Monetary Fund) are not managed relative to an internal benchmark. The Bank's Asian Bond fund investment is managed externally by the Bank for International Settlements.

The Australian dollar value of the Reserve Bank's foreign portfolio increased slightly over 2017/18.

Exchange Rate Risk on RBA Foreign Currency Portfolio

For a 10 per cent appreciation of the Australian dollar, as at end June



Source: RBA

Based on the level of reserves as at 30 June 2018, a 10 per cent appreciation of the Australian dollar would result in a mark-to-market loss of $5.3 billion. The increase in exchange rate risk over the previous decade and a half mainly reflects the increase in the size of net foreign exchange reserves over that period.

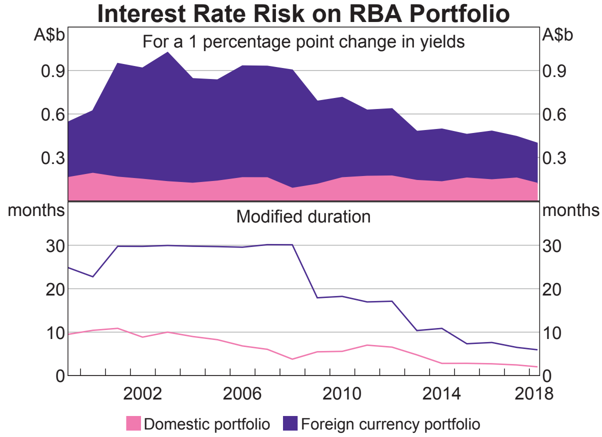
Interest rate risk

The value of the Reserve Bank's financial assets is also exposed to movements in market interest rates, as the bulk of the domestic and foreign portfolios comprises fixed-income securities.

Total holdings of domestic securities decreased by $2.2 billion over 2017/18 to $114.3 billion. At 30 June 2018, domestic securities held on a temporary basis under repurchase agreements (repos) accounted for $103.7 billion and securities held outright accounted for $10.6 billion. Interest rate risk faced by the Reserve Bank on its outright holdings of domestic securities fell slightly over 2017/18 owing to reduced holdings of Australian Government Securities (AGS). These securities are typically purchased to manage the liquidity impact of maturing AGS, and have a very short term-to-maturity.

The Reserve Bank's foreign currency assets are managed relative to benchmark portfolios in each currency with duration targets that reflect the Bank's long-term appetite for risk and return. These duration targets are reviewed periodically. During 2017/18, the duration target of the Japanese benchmark portfolio was reduced from six months to less than three months. Duration targets were unchanged in the other benchmark portfolios – the duration target for the US, European, and Canadian portfolios is six months, for the UK portfolio it is three months and for the Chinese and Korean portfolios it is 18 months. The weighted-average benchmark duration target for the Bank's total foreign portfolio was little changed over 2017/18 at around 6¾ months. This is low by historical standards, reflecting the generally low level of

Interest Rate Risk on RBA Portfolio



Source: RBA

interest rates, which offer little compensation for the risk of capital losses should longer-term bond yields return to more normal levels.

The overall level of interest rate risk on the Reserve Bank's domestic and foreign financial assets fell over 2017/18. The Bank would incur a valuation loss of around $426 million if interest rates in Australia and overseas rose uniformly by 1 percentage point across the yield curve.

The Reserve Bank is exposed to very little interest rate risk on its balance sheet liabilities. Banknotes on issue account for about 41 per cent of total liabilities and carry no interest cost to the Bank. Other sizeable obligations include deposits held by the Australian Government and its agencies, and Exchange Settlement Account balances held by authorised deposit-taking institutions. These deposits have short maturities that broadly match the Bank's domestic assets held under repo. Interest paid on these deposits reflects domestic short-term interest rates, effectively hedging part of the interest rate exposure of the domestic asset portfolio.

Credit risk

Credit risk is the potential for financial loss arising from the default of a debtor or issuer, or from a decline in asset values following a deterioration in credit quality. The Reserve Bank manages its

The Reserve Bank **develops and maintains** an **active risk management culture**

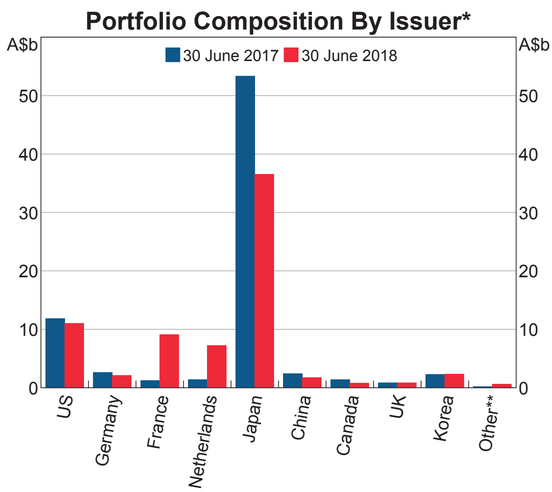
credit exposure by applying a strict set of eligibility criteria to its holdings of financial assets and to counterparties with which it is willing to transact.

The Reserve Bank is exposed to very little issuer credit risk on its outright holdings in the domestic portfolio as it invests only in securities issued by the Australian Government or by state and territory government borrowing authorities. The Bank is exposed to a small amount of counterparty credit risk on domestic assets that are held under repo. The Bank would face a loss only if a counterparty failed to repurchase securities sold to the Bank under repo and the market value of the securities fell below the agreed repurchase amount. The Bank manages this exposure by requiring that these securities meet eligibility criteria, and applying an appropriate margin to the securities, which is maintained throughout the term of the repo through two-way margining. The required amount of over-collateralisation increases with the risk profile of the security.

Counterparties with which the Reserve Bank is willing to deal in carrying out policy operations in the domestic market must be subject to an appropriate level of regulation and be able to settle transactions within the Austraclear system.

Repo transactions with the Bank are also governed by a Global Master Repurchase Agreement as part of the Reserve Bank Information and Transfer System (RITS) Regulations.

Investments in the Reserve Bank's foreign currency portfolio are typically confined to highly rated and liquid securities, as well as deposits with foreign central banks. The majority of the Bank's outright holdings are securities issued by the national governments of the United States, Germany, France, the Netherlands, Japan, Canada, the United Kingdom, China and South Korea, with modest holdings of securities issued by highly rated supranational institutions and government agencies. At 30 June 2018, gross holdings of Japanese yen-denominated assets accounted for the largest share of the Bank's foreign currency issuer exposures, with the majority of these assets funded under short-term foreign exchange swaps (see the chapter on 'Operations in Financial Markets' for more detail). A limit on the size of exposures to individual currencies based on the Bank's capital was introduced during 2017/18 to mitigate concentration risk.



* Includes assets held outright, funded by foreign exchange swaps, and held under repurchase agreements

** Includes supranational securities, government agency securities and investments with the Bank for International Settlements

Source: RBA

The Reserve Bank holds a portion of its foreign currency portfolio in short-term repos. This exposes the Bank to the small amount of residual credit risk that is inherent in repos, as noted above. The Bank manages this risk by requiring 2 per cent over-collateralisation, which is maintained through two-way margining in the local currency, and accepting only high-quality and liquid securities as collateral. Credit exposure on foreign repos is further managed by imposing limits on individual counterparty exposures and requiring execution of a Global Master Repurchase Agreement (or Master Repurchase Agreement where appropriate) with each counterparty.

The Reserve Bank undertakes foreign exchange swaps as part of its policy operations and as a means of enhancing returns on the foreign currency portfolio. Credit risk on these instruments is managed by transacting only with counterparties that meet strict eligibility criteria, including the requirement to have executed with the Bank an International Swaps and Derivatives Association (ISDA) agreement with a credit support annex. Exposures generated by movements in market exchange and interest rates are managed through two-way margining in Australian dollars.

The Reserve Bank undertakes some limited lending of its gold holdings. The lending is either fully collateralised or the borrower has government support. As at 30 June 2018, 11.1 tonnes of gold valued at $604 million was on loan.

Operational Risks

The Reserve Bank faces a diverse range of operational risk in its day-to-day activities. These risks relate to a range of areas from availability of technology and facilities services to retaining high-quality staff to perform the Bank's functions, as well as the unintentional disclosure of confidential and sensitive information. Generally, the Bank has a low appetite for these types of risk but recognises that it is neither possible nor necessarily desirable to eliminate some risks inherent in its activities. The acceptance of some risk is often necessary to foster innovation and efficiencies in business practices.

While all parts of the Reserve Bank are exposed to operational risk of varying degrees, the most significant risks are those associated with financial transactions undertaken by the Bank for its own activities and that of its clients. During 2017/18, Financial Markets Group executed around 52,700 transactions, generating an average daily settlement value of around $35 billion. The risks associated with such a large volume of transactions are managed by ensuring that systems and processes are efficient and robust, including through ongoing work to improve systems. The Bank is also the primary banker for a number of government entities, including the Australian Taxation Office, Medicare and Centrelink, and it maintains the infrastructure to facilitate real-time interbank payment and settlement services through RITS. Any operational failure in these critical activities could have widespread consequences, so the Bank has in place a range of processes to facilitate ongoing and effective management of its operational risks to maintain a suitably robust control environment.

The continuity of critical business functions during and after a disruptive event, such as a natural disaster, power outage or terrorist attack, is a key area of focus for the Reserve Bank. Extensive back-up plans have been established, which include the use of a dedicated Business Resumption Site (BRS) in north-west Sydney, where permanent staff from some of the Bank's most critical operational areas are located. Departments regularly test their back-up plans at the site, including combined exercises involving multiple areas testing the capacity of the facilities and also testing plans in a 'work-from-home' environment. Regular workshops are scheduled

The continuity of critical business functions during and after a disruptive event … is a key area of focus for the Reserve Bank

with critical business areas to discuss response strategies to situations such as technology service disruptions and the unavailability of staff. The Bank also participates in contingency exercises with external organisations to ensure that staff are well briefed in their roles during disruptions and that effective internal and external communication arrangements are in place. The results of such exercises are monitored by the Risk Management Committee.

The Reserve Bank's policy and business operations are highly dependent on information technology (IT) systems. The Bank's risk management framework supports an ongoing focus on managing the risks associated with complex IT systems. The Bank's IT Department collaborates with relevant business areas to facilitate the monitoring, assessment and management of IT-related risks and ensure IT-related initiatives are consistent with the Bank's IT strategy. This work is supported by the continuous evaluation of industry developments in order to ensure that the Bank's systems and procedures conform to current IT standards and remain robust. Assessment of appropriate staff resourcing, the adequacy of controls over IT processes and the level of security over information management are all incorporated in the Bank's risk management framework.

As part of the Reserve Bank's management of the risks associated with technology and operational systems, a significant focus is placed on the ongoing security of these systems. The Bank invests in significant security controls and risk assurance functions, which are supported by a regular controls testing regime. These activities are informed by liaison with the security services, other central banks, the Australian Government and industry participants. The Bank receives regular independent assurance of its compliance with security strategies endorsed by the Australian Signals Directorate, and maintains independent certification for the International ISO Standard for Information Security Management ISO27001.

During 2017/18, the Reserve Bank continued to direct significant resources towards the delivery of a number of large and complex multi-year projects. These include the renovation of banking applications and systems, the upgrade of Australia's banknotes and the development of infrastructure to facilitate real-time retail payments, which was publicly launched in February 2018. Successful completion of these projects will ensure high-quality services are maintained for the Bank's clients and the Australian public. The risks associated with project work are carefully managed so that adequate resources are available, nominated project deadlines are met and change management is effective. Project steering committees play an important role in overseeing the management of these risks.

The Reserve Bank does not tolerate dishonest or fraudulent behaviour and is committed to deterring and preventing such behaviour. It takes a very serious approach to cases, or suspected cases, of fraud. All staff involved in financial dealing have well-defined limits to their authority to take risks or otherwise commit the Bank. These arrangements are further enhanced by separate front-, back- and middle-office functions, where staff involved in trading, settlement and reconciliation activity remain physically separate and have separate reporting lines. For non-trading activities, several layers of fraud control are in place, including preventative, detective and corrective controls. A clear decision-making hierarchy, separation of duties and physical controls over systems and information are all in place and are subject to regular review. Ongoing training and awareness programs are also conducted. The Bank requires all staff to undertake fraud awareness training. The Bank has arrangements in place for staff and members of the public to report concerns anonymously. All concerns are fully investigated. During 2017/18, there were no reported instances of fraud by employees.

The Reserve Bank remains strongly committed to maintaining and strengthening a workplace culture in which employees uphold the highest standards of behaviour. The Code of Conduct sets out requirements of the Bank's employees and others who are involved in its activities. The code articulates the values that staff are expected to demonstrate when pursuing the Bank's objectives. These values require employees to conduct themselves with a high degree of integrity, strive for excellence in the work they perform, treat others with respect and courtesy, exercise intelligent inquiry and promote the public interest. All staff attest that they have read and understood the code. The Bank has arrangements in place for staff to report concerns about breaches of the Code of Conduct, including channels by which concerns can be reported anonymously. Initiatives are under way to enhance arrangements and ensure greater comfort for staff reporting concerns across a range of issues.

The effective management of compliance risk is central to the Reserve Bank's activities. Risk and Compliance Department collaborates with all business areas to ensure this risk is being managed effectively and keeps the Risk Management Committee informed regarding the level of compliance in key areas. In 2017/18, a key area of focus was preparation for the introduction of the Notifiable Data Breach Scheme, which came into force in February 2017 and the *Privacy (Australian Government Agencies – Governance) APP Code 2017*, which came into force on 1 July 2018. Staff also complete a number of compliance-based electronic training modules each year, focusing on areas such as privacy and workplace health and safety.

Notwithstanding these measures, events can occur from time to time that may adversely affect the Reserve Bank's reputation or lead to financial or other costs. Timely reports on any such incidents and near misses are provided to the Risk Management Committee. These reports outline the circumstances, including impact and cause, as well as identify areas where new controls may be needed or where existing controls should be strengthened.

The Reserve Bank continues to act as the administrator of the Guarantee of State and Territory Borrowing. Applications for new guaranteed liabilities under this scheme closed in 2010, although existing liabilities will continue to be guaranteed until maturity, at the latest in 2023. To date, a total of $417 million in fees has been collected for state and territory borrowing since the scheme commenced in 2009, with $7 million collected in 2017/18.

Earnings, Distribution and Capital

In 2017/18, the Reserve Bank recorded a net profit of $3.8 billion. In accordance with the *Reserve Bank Act 1959*, unrealised gains are not available for distribution and are transferred to the unrealised profits reserve. Earnings available for distribution amounted to $0.7 billion. The Reserve Bank remains well capitalised.

The Reserve Bank's Earnings

The Reserve Bank's earnings come from two sources: underlying earnings, comprising net interest and fee income, less operating costs; and valuation gains or losses. Net interest income arises because the Bank earns interest on almost all of its assets, albeit currently at low rates, while it pays no interest on a large portion of its liabilities, namely banknotes on issue and capital and reserves. Fees paid by authorised deposit-taking institutions in relation to the Committed Liquidity Facility also contribute significantly to underlying earnings.

Valuation gains and losses result from fluctuations in the value of the Reserve Bank's assets because of movements in exchange rates or in yields on securities it holds. A depreciation of the Australian dollar or a decline in interest rates results in valuation gains. Conversely, an appreciation of the Australian dollar or a rise in market yields leads to valuation losses. These gains and losses are realised only when the underlying asset is sold or matures. Valuation gains and losses are volatile, as both exchange rates and market interest rates fluctuate in wide ranges over time. Market risk is managed by the Bank within strict parameters, although it is not eliminated given the policy purposes for which the Bank's assets are held.

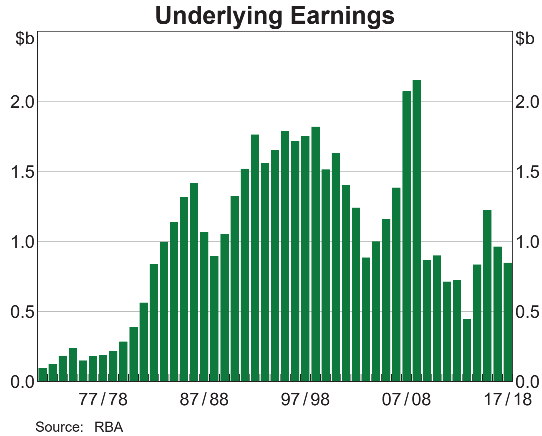
Management of the Bank's assets is discussed in the chapter on 'Operations in Financial Markets'; the associated risks are considered in the chapter on 'Risk Management'.

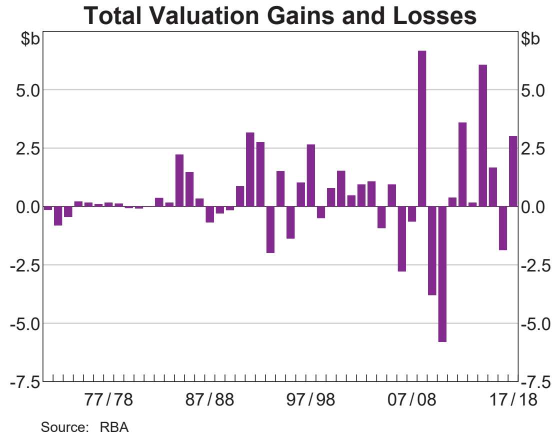
The Reserve Bank reports net profit as income from all sources, in accordance with Australian Accounting Standards, while the distribution of profits is determined by section 30 of the Reserve Bank Act. In terms of the act, net profit is distributed in the following way:

- Unrealised gains (or losses) are not available for distribution and are transferred to (absorbed by) the unrealised profits reserve. The remainder of net profit after this transfer is available for distribution.
- The Treasurer determines, after consultation with the Reserve Bank Board, any amounts to be placed from distributable earnings to the credit of the Reserve Bank Reserve Fund (RBRF), the Bank's general reserve.
- The remainder of distributable earnings after any transfer to the RBRF is payable as a dividend to the Commonwealth.

In 2017/18, the Reserve Bank recorded a net profit of $3,847 million, comprising:

- underlying earnings of $845 million, which were $115 million lower than the previous year. The





decline in this component of earnings mainly reflected an increased use of foreign exchange swaps (rather than domestic securities) for domestic liquidity management purposes. The bulk of the foreign currency obtained from these swaps was invested in Japanese yen assets, which currently earn a very low or negative rate of interest. On a 'total returns' basis, earnings on foreign exchange swaps were generally higher than domestic securities of equivalent term as the total return from swaps includes the cost of hedging the currency risk, which was favourable during 2017/18, but recorded as an unrealised foreign currency gain rather than as underlying earnings. The decline in underlying earnings was partly offset by higher earnings on the Bank's US dollar assets, in line with the rise in US interest rates

- net valuation gains of $3,002 million, primarily from the depreciation of the Australian dollar during 2017/18. Unrealised gains amounted to $3,178 million, partially offset by realised losses of $176 million. Realised losses were largely the result of sales and maturities of Australian Government Securities purchased in the prior year at a premium to their face value. Taking into account coupon payments received while this stock was held, the relevant holdings were profitable for the Bank.

Earnings available for distribution amounted to $669 million, compared with $1,286 million in the previous year, reflecting the lower underlying earnings and realised losses.

Capital, Reserves and Distribution

The RBRF is the Reserve Bank's general reserve and is the main component of the Bank's capital. This reserve is funded from transfers from earnings available for distribution. Its purpose is to provide the capacity to absorb losses when it is necessary to do so.

The Reserve Bank Board has a framework to assess the target balance of the RBRF by assessing and appropriately assigning capital to exposures of different risk. The largest potential for loss from the Reserve Bank's assets comes from market risk, comprising foreign exchange and interest rate risk. The capital assigned to each component of market risk is derived from the Bank's historical experience of loss and stress tests of the balance sheet, which incorporate significant adverse movements in exchange rate and interest rates drawn from historical experience. Since the largest potential for loss is associated with the Bank's unhedged holdings of foreign exchange assets, materially more capital is assigned to exchange rate risk than to interest rate risk.

While the Reserve Bank has no history of loss from credit risk, credit risk is also incorporated into the capital framework. The capital held against credit risk is currently a small sum, reflecting the quality of assets the Bank holds, the soundness of counterparties with which the Bank deals, the fact that repurchase agreements and foreign exchange swaps are well collateralised and that the Bank follows a set of conservative policies for managing credit risk, consistent with its very low appetite for such risk. Capital, therefore, is held only against the Bank's very small exposures to commercial banks that are not collateralised. This overall approach to credit risk is consistent with the practice of a range of major central banks.

The current balance in the RBRF ($14,119 million) slightly exceeded the Reserve Bank Board's target at the end of 2017/18. Accordingly, the Board viewed the balance sheet as being very strong and members saw no need to seek further capital from 2017/18 profits. The Treasurer, after consulting the Board, therefore determined that all earnings available for distribution in 2017/18, a sum of $669 million, would be paid as a dividend to the Commonwealth.

The balance of the unrealised profits reserve stood at $5,860 million on 30 June 2018, a rise of $3,178 million from the previous year. This movement largely reflects unrealised valuation gains associated with the depreciation of the Australian dollar. The balance of this reserve is available either to absorb future valuation losses or to be distributed over time as the gains become realised when relevant assets are sold.

Asset revaluation reserves are held for non-traded assets, such as gold holdings and property. Balances in these reserves represent the difference between the market value of these assets and the cost at which they were acquired. The total balance for these reserves was $5,020 million at 30 June 2018, $299 million higher than at the end of the previous financial year, largely reflecting the increase in the Australian dollar value of the Reserve Bank's holdings of gold. The balance of the superannuation reserve was $338 million at 30 June 2018.

Details of the composition and distribution of the Reserve Bank's profits are contained in the table on page 127.

The Financial Statements (and accompanying Notes to the Financial Statements) for the 2017/18 financial year were prepared in accordance with Australian Accounting Standards, consistent with the Finance Reporting Rule issued under the *Public Governance, Performance and Accountability Act 2013*.

Governor Philip Lowe (third from left) witnesses Auditor-General for Australia Grant Hehir (fourth from right) sign his audit opinion; also present (from left) KPMG National Managing Partner Andrew Yates, Reserve Bank Chief Financial Officer Robert Middleton-Jones and Secretary Anthony Dickman, Australian National Audit Office Senior Executive Director Jocelyn Ashford, KPMG Partner Kim Lawry and Chair of the Reserve Bank Board Audit Committee Mark Barnaba AM

Composition and Distribution of Reserve Bank Profits

($ million)

	Composition of Profits[a]				Distribution of Profits				Payments to Government		
					Transfer to/from (–)						
	Underlying earnings	Realised gains and losses (–)[b]	Unrealised gains and losses (–)	Accounting profit or loss (–)	Unrealised profits reserves	Asset revaluation reserves	Reserve Bank Reserve Fund	Dividend payable	Payment from previous year's profit	Payment delayed from previous year	Total payment
1997/98	1,750	966	1,687	4,403	1,687	–558	548	2,726	1,700	–	1,700
1998/99	1,816	2,283	–2,773	1,326	–2,349	–1	–	3,676	2,726	–	2,726
1999/00	1,511	–708	1,489	2,292	1,489	–	–	803	3,000	–	3,000
2000/01	1,629	1,200	320	3,149	320	–5	–	2,834	803	676	1,479
2001/02	1,400	479	–11	1,868	–11	–10	–	1,889	2,834	–	2,834
2002/03	1,238	1,157	–222	2,173	–222	–2	133	2,264	1,889	–	1,889
2003/04	882	–188	1,261	1,955	1,261	–	–	694	1,300	–	1,300
2004/05	997	366	–1,289	74	–1,289	–	–	1,363	374	964	1,338
2005/06	1,156	4	933	2,093	933	–17	–	1,177	1,063	320	1,383
2006/07	1,381	72	–2,846	–1,393	–2,475	–3	–	1,085	1,177	300	1,477
2007/08	2,068	614	–1,252	1,430	27	–	–	1,403	1,085	–	1,085
2008/09	2,150	4,404	2,252	8,806	2,252	–	577	5,977	1,403	–	1,403
2009/10	866	–128	–3,666	–2,928	–2,248	–	–680	–	5,227	–	5,227
2010/11	897	–1,135	–4,651	–4,889	–23	–	–4,866	–	–	750	750
2011/12	710	405	–39	1,076	–20	–	596	500	–	–	–
2012/13	723	–135	3,725	4313	3,725	–	588	–	500	–	500
2013/14	9,242[c]	790	–640	9,392	–640	–3	8,800	1,235	–	–	–
2014/15	832	2,622	3,434	6,888	3,434	–	1,570	1,884	618	–	618
2015/16	1,223	3,389	–1,729	2,883	–1,729	–	1,390	3,222	1,884	618	2,501
2016/17	960	322	–2,179	–897	–2,179	–4	–	1,286	3,222	–	3,222
2017/18	845	–176	3,178	3 847	3,178	–	–	669	1,066	–	1,066

(a) As originally published
(b) Excludes gains or losses realised from the sale of fixed assets that had been held in asset revaluation reserves
(c) Includes the Commonwealth grant of $8,800 million
Source: RBA

Pro Forma Business Accounts

The following set of accounts for the Reserve Bank's contestable business has been prepared in accordance with competitive neutrality guidelines. These accounts do not form part of the audited financial statements.

Transactional Banking

	2016/17 $ million	2017/18 $ million
Revenue		
– Service fees	105.7	104.5
– Other revenue	3.5	2.3
Total	109.2	106.8
Expenditure		
– Direct costs	104.9	105.3
– Indirect costs	0.0	0.0
Total	104.9	105.3
Net profit/(loss)	4.3	1.5
Net profit/(loss) after taxes[(a)]	3.4	1.5
Assets[(b)]		
– Domestic markets investments	1,354.8	2,183.0
– Other assets	39.8	45.2
Total	1,394.6	2,228.2
Liabilities[(b)]		
– Capital & reserves	25.0	25.0
– Deposits	1,351.2	2,185.4
– Other liabilities	18.4	17.8
Total	1,394.6	2,228.2

(a) In accordance with competitive neutrality guidelines, income tax expense has been calculated and transferred to the Commonwealth as a notional part of the Reserve Bank's annual profit distribution
(b) As at 30 June
Source: RBA

Annual Performance Statement for 2017/18

I, as the accountable authority of the Reserve Bank of Australia, present the annual performance statement of the Reserve Bank for the 2017/18 reporting period, prepared under paragraph 39(1)(a) of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act). In my opinion, this annual performance statement accurately presents the performance of the Reserve Bank in the reporting period and complies with subsection 39(2) of the PGPA Act.

Philip Lowe
Governor, Reserve Bank of Australia
23 August 2018

Introduction

This performance statement outlines the key purposes of the Reserve Bank as set out in the 2017/18 corporate plan and provides the results of the measurement and assessment of the Bank's performance in achieving those purposes for the year ended 30 June 2018. Where necessary, additional context is provided, including an analysis of the significant factors that have contributed to the performance of the Bank in achieving its purposes in 2017/18.

As noted elsewhere in this annual report, the Reserve Bank of Australia is Australia's central bank and it conducts central banking business. The Bank has two boards, the Reserve Bank Board and the Payments System Board. The Reserve Bank Board is responsible for the Bank's monetary and banking policy and the Bank's policy on all other matters, except for payments system policy, for which the Payments System Board is responsible.

Monetary Policy

Purpose

It is the duty of the Reserve Bank Board to ensure that the monetary and banking policy of the Bank is directed to the greatest advantage of the people of Australia and that the powers of the Bank are exercised in a way that, in the Board's opinion, will best contribute to:

a. the stability of the currency of Australia;

b. the maintenance of full employment in Australia; and

c. the economic prosperity and welfare of the people of Australia.

In support of the above duties, the most recent *Statement on the Conduct of Monetary Policy* agreed by the Treasurer and the Governor, dated 19 September 2016, confirms the Bank's continuing commitment to keeping consumer price inflation between 2 and 3 per cent, on average, over time, consistent with its duties under the *Reserve Bank Act 1959*. Ensuring low and stable inflation preserves the value of money and facilitates strong and sustainable growth in the economy over the longer term.

Reserve Bank of Australia – Performance Summary 2017/18

Corporate Plan Purpose[a]	Performance objectives	Summary Performance Measures	Results
Monetary policy	Achieve inflation target	Consumer price inflation maintained between 2–3 per cent, on average, over the medium term	Consumer price inflation is forecast to be between 2 and 3 per cent over much of the forecast period; see the Bank's quarterly *Statement on Monetary Policy* for details. Consumer price inflation has averaged around 2½ per cent over the inflation-targeting period, although it has been below 2 per cent recently
Financial stability	Support overall financial stability	A stable financial system that is able to support the economy. The Bank assesses a range of economic and financial data to help gauge the soundness of the financial system and identify potential vulnerabilities, and communicates this assessment, primarily in the Bank's half-yearly *Financial Stability Review*	The financial system has continued to support economic activity without disruption
		Work with the Council of Financial Regulators (CFR) agencies to identify and appropriately address evolving systemic risks	The Bank has continued to work productively with the other CFR agencies
Financial market operations	Achieve cash rate target	Overnight cash rate equal to the target each business day	Overnight cash rate was equal to the target each business day
	Manage reserves to portfolio benchmarks	Portfolio managed within small deviations around the asset and duration benchmarks	Deviations from the reserve portfolio benchmark were small and in line with pre-defined limits
	Intervene in foreign exchange market as appropriate	Publish data and explanations of any interventions	No foreign exchange market intervention was conducted
Payments and infrastructure	Support competition and efficiency in the payments system and financial system stability	Maintain and improve where possible the efficiency and competitiveness of the payments system, consistent with financial system stability. Monitor and publish information on the effect of new card standards. Complete new statistical collection system for retail payments	New interchange and surcharging standards are now fully implemented and well understood (see *Payments System Board Annual Report 2018* for further details). The Bank has been actively encouraging the provision of least-cost routing functionality to merchants. The Bank's retail payments statistical collection was revamped and a new reporting system was introduced
	Stability in the provision of financial market infrastructure (FMI) services	Stability of FMI service provision. Assess Reserve Bank Information and Transfer System (RITS) and licensed clearing and settlement facilities against relevant standards and take action where required to ensure standards are met	Assessments of RITS and all licensed clearing and settlement facilities have been completed and published. Where necessary, the Bank has set and monitored the response to regulatory priorities

Reserve Bank of Australia – Performance Summary 2017/18

Corporate Plan Purpose[a]	Performance objectives	Summary Performance Measures	Results
		Contribute to international policy work on central counterparty resilience and FMI crisis management. Adapt domestic regulatory standards in response to international developments. Support international supervisory cooperation	No change to domestic regulatory standards was required
	RITS operational reliability	RITS availability at 99.95 per cent during core hours	RITS availability was 100 per cent during core hours in 2017/18
		Fast Settlement Service (FSS) go-live; FSS availability at 99.995 per cent on a 24/7 basis, with most transactions processed in less than one second	FSS publicly launched on 13 February 2018. Between launch and 30 June, FSS availability was 100 per cent on a 24/7 basis and the median response time was 50 milliseconds
	RITS cyber security	Ongoing investment and regular reviews and testing to support cyber resilience	The Bank's ongoing program of cyber resilience work helped underpin the reliable operation of RITS in 2017/18
Banking	Maintain transactional banking competitiveness	Minimum return on capital equivalent to 10-year Australian Government Security rate plus a margin for risk	The Bank's banking services achieved the minimum required return on capital in 2017/18
	Progress on projects to deliver convenient, secure, reliable and cost-effective banking services to customers	Provision of high-quality, cost-effective banking services to government and other official agency customers and, in turn, the public supported by: • Continued work on replacing the Bank's core account maintenance system • Completion of initial capabilities to participate in the New Payments Platform (NPP)	In 2017/18, the Bank continued to work on a number of projects to renovate its banking applications and systems. Work is nearing completion, with good progress made on the project to upgrade the Bank's core account maintenance system Following the public launch of NPP in February 2018, the Bank has processed on behalf of the Australian Government transactions valued at $179 million

Reserve Bank of Australia – Performance Summary 2017/18

Corporate Plan Purpose[a]	Performance objectives	Summary Performance Measures	Results
Banknotes	Maintain public confidence in banknotes as follows:		
	• Meet banknote demand	99.5 per cent of banknote orders from commercial banks fulfilled by the Reserve Bank on the day requested	100 per cent of orders were fulfilled on the day requested in 2017/18
	• Increase security of Australian banknotes	Issuance of new $10 banknote with upgraded security features as part of Next Generation Banknote program	The new $10 banknote was released on 20 September 2017 as planned and achieved wide acceptance and distribution
	• Ensure high-quality banknotes	Reserve Bank banknote production orders to be met by Note Printing Australia Limited in full, on time and to required quality standard	All orders were met in full, on time and to the required quality standard in 2017/18
		Maintain quality of banknotes in circulation in excess of a minimum quality standard	The quality of banknotes in circulation was broadly unchanged at a high level in 2017/18

(a) See the Reserve Bank of Australia Corporate Plan 2017/18
Source: RBA

Low inflation assists businesses and households in making sound investment decisions, underpins the creation of jobs and protects the savings of Australians. The *Statement on the Conduct of Monetary Policy* also recognises the importance of financial stability for a stable macroeconomic environment.

Results

Assessing the conduct of monetary policy by the Reserve Bank during 2017/18 involves judging whether the policy decisions taken by the Reserve Bank Board, based on the information available at the time, were consistent with achieving the inflation target of between 2 and 3 per cent, on average, over time to foster sustainable economic growth in Australia. Because there are lags between changes in the cash rate and their effect on the economy, such an assessment needs to give weight to both actual outcomes and the forecasts for inflation, output and the unemployment rate. These forecasts are published quarterly in the *Statement on Monetary Policy*.

Towards the end of 2017, the Reserve Bank Board undertook a review of the forecasts and monetary policy decisions it had taken since 2011, including the reasons behind the forecast errors and what the Bank's staff had learnt about the economy as a result. The review concluded that, based on the information available at the time the decisions were made, the Board had struck a reasonable balance in achieving its broad objectives in relation to the inflation target and financial stability considerations over the preceding several years.

Following a period of below-average growth, GDP is likely to have expanded by 2¾ per cent in 2017/18. From there, growth is expected to pick up a little further, to a bit above 3 per cent in subsequent years, as remaining new liquefied natural gas (LNG) production capacity comes on line. These rates are somewhat above the Reserve Bank's estimate of trend growth in productive capacity, implying that spare capacity is likely to be absorbed over this period. The unemployment rate is therefore expected to decline. Consumer price inflation has averaged around 2½ per cent over the inflation-targeting period, although it has been below 2 per cent recently. Consumer price inflation was 2.1 per cent over the year to the June quarter 2018 and is expected to be above 2 per cent for much of the 2½-year forecast period. However, temporary factors are expected to hold down year-ended inflation in the near term.

After lowering the cash rate by 25 basis points in August 2016, the Reserve Bank Board has left the cash rate unchanged since then. The Board has judged that this has been consistent with achieving sustainable growth in the economy and inflation consistent with the target over the medium term. Over the past two years gradual progress has been made in reducing unemployment and bringing inflation back towards the target range, and further progress is expected over the period ahead. The Board's view has been that holding the cash rate steady at 1½ per cent would assist that progress, with steady monetary policy promoting stability and confidence.

The Governor's statement and the minutes following the monetary policy meetings provide further details of the Reserve Bank Board's assessment of economic developments, the outlook and monetary policy decisions. A brief summary of analysis by the Reserve Bank of these issues is provided below. Further details of this analysis are provided in the Bank's quarterly *Statement on Monetary Policy*, the Governor's regular appearances before the House of Representatives Standing Committee on Economics, and speeches by the Governor and other senior Bank officials. These communications support the effectiveness of monetary policy, by improving understanding of monetary policy decisions across the community, and the transparency of monetary policy, which facilitates the Bank's accountability for the performance of its monetary policy responsibilities.

Analysis

On the global economy, the incoming data and the outlook for economic growth improved compared with a year ago. Consistent with this, monetary policy has been tightened in the United States and a few other economies, while further monetary easing is no longer expected in other major advanced economies. However, global interest rates and measures of underlying inflation remain low. Because Australia is a small open economy with a floating exchange rate, shifts in global monetary conditions can affect financial conditions in Australia.

The period of adjustment that has followed the end of the mining investment boom is close to its end. Non-mining investment has picked up and labour market conditions have strengthened. Over the past year, the unemployment rate has declined and inflation has increased a little. Further progress on both these fronts is expected over the period ahead. Internal assessments suggest that the performance of the forecasts presented to the Reserve Bank Board has been a little better than the average of recent years.

Over the past year, the Reserve Bank Board has been considering a range of risks to the outlook and their implications for the policy decision. A significant escalation in trade protectionism or risk aversion could derail the global expansion. On the other hand, growth and inflation in the United States could be higher than expected given the substantial fiscal stimulus that is in train. The Chinese authorities continue to balance the aim of supporting near-term growth with the more medium-term priorities of containing financial risks and improving environmental outcomes. Domestically, the introduction of further supervisory measures to improve lending standards, together with increased public scrutiny, has helped limit the build-up of risks in household balance sheets. In the context of weak growth in wages and household incomes, however, risks to consumption from this source remain.

Financial Stability

Purpose

The Reserve Bank has a responsibility for fostering overall financial stability in Australia. This stems from the Bank's duties to exercise its powers in a way that will best contribute to 'the maintenance of full employment in Australia' and 'the economic prosperity and welfare of the people of Australia'. Given the serious damage to employment and economic prosperity that can occur in times of financial instability, the Reserve Bank Act has long implied a mandate to pursue financial stability. This mandate has been made more explicit by successive governments. More recently, the Treasurer and the Governor have recorded their common understanding of the Bank's longstanding responsibility for financial system stability, as part of the periodically updated *Statement on the Conduct of Monetary Policy*.

The Reserve Bank works with other regulatory bodies in Australia to foster financial stability. The Governor chairs the Council of Financial Regulators (CFR) – comprising the Reserve Bank, the Australian Prudential Regulation Authority (APRA), the Australian Securities and Investments Commission (ASIC) and the Australian Treasury – whose role is to contribute to the efficiency and effectiveness of regulation and the stability of the financial system. The Bank's central position in the financial system, and its position as the ultimate provider of liquidity to the system, gives it a key role in financial crisis management, in conjunction with the other members of the CFR.

The Reserve Bank's operations in domestic financial markets, discussed in the 'Financial Market Operations' section of this performance statement, and oversight and operational roles in the payments system, discussed in the 'Payments and Infrastructure' section of this performance statement, also contribute to the stability of the financial system.

Results

The ultimate measure of performance in financial stability policy remains the stability of the financial system itself as it performs its function of supporting the economy. The Reserve Bank assesses a range of economic and financial data to help gauge the soundness of the financial system and potential vulnerabilities. During 2017/18, the Reserve Bank assessed that the resilience of the Australian financial system increased a little further. The financial system continued to facilitate economic activity and financial market infrastructures continued to function effectively, as noted in the Bank's *Financial Stability Review* in October 2017 and April 2018. However, there were a number of potential domestic sources of systemic risk and shocks to financial stability that might come from abroad. Domestic vulnerabilities related to household debt and the housing market more generally continued to be a focus during the past year, as well as risks related to commercial property lending. Tighter lending standards by banks and other authorised deposit-taking institutions, in part induced by regulatory actions by APRA and ASIC, have assisted in enhancing resilience to potential risks; none of the domestic risks on their own appears to be enough to be a direct source of significant domestic financial instability in the near term.

The Reserve Bank uses its powers, influence and public communications to ensure as far as possible that the Australian financial system remains stable and that financial stability risks and how they can be addressed are well understood across the community. During 2017/18, the Bank highlighted the key issues and risks for the Australian financial system in its *Financial Stability Review*, as well as in several public speeches.

The Bank contributed to work with other CFR agencies on a range of issues during the year, including: developments and risks in the housing and mortgage markets; crisis management and resolution preparedness; financial technology ('fintech'); shadow banking activity; and the financial risks of climate change.

In 2017/18, the Reserve Bank also contributed to work undertaken in relation to financial stability under the auspices of various international regulatory bodies, including the Financial Stability Board (FSB), the Basel Committee on Banking Supervision and the Trans-Tasman Council on Banking Supervision. The Governor participated as a member of the FSB Plenary (the decision-making body of the FSB), Steering Committee and Standing Committee on Assessment of Vulnerabilities, and served as Co-Chair of the FSB Regional Consultative Group for Asia. Other Bank staff participated as members of various committees and working groups. For further information, see the chapter on 'International Financial Cooperation' in this annual report.

Analysis

Financial stability in Australia has been assisted by the sustained strong financial performance of the domestic banking system. Australian banks have improved their resilience to future financial and economic shocks by increasing their capital and liquidity ratios over recent years. They have also taken steps to improve the quality of lending and raise lending standards, especially in relation to their mortgage business. As noted above, the Reserve Bank, together with other CFR agencies, has been closely monitoring developments in residential mortgage lending and household balance sheets. Both APRA and ASIC have taken measures to address risks in this area. As risks have moderated from elevated levels, APRA has removed the temporary benchmark on investor lending growth for banking institutions that have been able to provide an assurance on the strength of their lending standards. However, the CFR agencies would consider further measures in the future should circumstances change. In the period ahead, the Bank and other CFR agencies will also carefully consider the implications for the resilience of the financial sector arising from findings and recommendations of the final report of the Productivity Commission's review of competition in the financial system, as well as the outcomes of the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry. Further relevant analysis by the Reserve Bank is provided in the *Financial Stability Review* and speeches by the Governor and other senior Bank officials.

Financial Market Operations

Purpose

The Reserve Bank has a sizeable balance sheet, which will continue to be managed through financial market operations in support of the Bank's policy and other objectives over the period of the 2017/18 corporate plan.[1]

The Bank's operations in domestic financial markets are conducted to ensure that the cash rate trades at the target and that there is sufficient liquidity in the domestic money market on a daily basis. This promotes the objectives of monetary policy as described in the 'Monetary Policy' section of this performance statement

1 Section 8 of the Reserve Bank Corporate Plan 2017/18 covers the Bank's management of its financial position and capital.

and the stable functioning of the financial system, in particular the payments system.

The Reserve Bank's foreign reserves are held to give the Bank the capacity to intervene in the foreign exchange market. In particular, they enable the Bank to address any apparent dysfunction in that market and/or a significant misalignment in the value of the currency, consistent with the objectives of monetary policy. Regular transactions in the foreign exchange market are conducted to manage these reserves, to provide foreign exchange services to the Bank's clients (the largest of which is the Australian Government) and to assist in liquidity management in domestic markets.[2]

Results

The Reserve Bank's operations in financial markets support its monetary policy objectives through ensuring that the operational target in the domestic money market is met; this target (the cash rate target) is a decision of the Reserve Bank Board. When supplying liquidity to the domestic money market, the Bank seeks to ensure that the overnight cash rate is maintained at the prevailing cash rate target each day. The Bank collects information on each participant's activity in the money market and publishes the resulting measure of the overnight cash rate daily. The cash rate was equal to the target every day during 2017/18.

The Reserve Bank manages its foreign reserves portfolio relative to a benchmark. During 2017/18, the portfolio was managed so that any deviations around the benchmarks for exchange rate and interest rate risk were small and in line with pre-defined limits.

The Reserve Bank did not intervene in foreign exchange markets during 2017/18.

2 The Banking section of this performance statement discusses the Bank's responsibility to act as banker for the Commonwealth.

Analysis

The Reserve Bank's financial markets operations continue to be influenced by the diverging monetary policy trends among the major central banks, as well as the regulatory regimes that apply to financial markets in which the Bank transacts and/or the counterparties with which it deals, both domestically and internationally. During 2017/18, the Bank continued to monitor and, where necessary adjust to, the environment where market functioning and structure are evolving significantly following a period of substantial regulatory reform and unusually low interest rates.

Payments and Infrastructure

Purpose

There are several distinct aspects to the Reserve Bank's role in the payments system, including those of policymaker, overseer and supervisor, and owner and operator of key national payments infrastructure.

In relation to the policymaking role, it is the duty of the Payments System Board to ensure that the Bank's payments system policy is directed to the greatest advantage of the people of Australia, to ensure that the powers of the Bank under the *Payment Systems (Regulation) Act 1998* and the *Payment Systems and Netting Act 1998* are exercised in a way that, in the Board's opinion, will best contribute to:

a. controlling risk in the financial system;

b. promoting the efficiency of the payments system; and

c. promoting competition in the market for payment services, consistent with the overall stability of the financial system.

In addition, it is the Payments System Board's duty to ensure that the powers and functions of the Bank under Part 7.3 of the

Corporations Act 2001 are exercised in a way that, in the Board's opinion, will best contribute to the overall stability of the financial system. These powers and functions relate to the supervision of central counterparties (CCPs) and securities settlement facilities, which are key components of the central infrastructure that supports financial markets. The Bank's payments policy area also acts as overseer of Australia's high-value payment system, RITS, which is another key part of Australia's financial market infrastructure.

The Bank's operational role in the payments system is effected through its ownership and management of RITS, which is used by banks and other approved institutions to settle their payment obligations efficiently on a real-time, gross settlement basis. This ensures that there is no build-up of settlement obligations associated with high-value transactions and thereby promotes the stability of Australia's financial system.

The Bank's work in these areas supports its other work, discussed in the 'Financial Stability' section of this performance statement, directed towards fostering overall financial stability.

Results

As is discussed further in the *Payments System Board Annual Report 2018*, the Reserve Bank's new interchange standards became fully effective from July 2017. As a result of the schemes modifying their interchange fee schedules to ensure compliance with the new standards, interchange payments on many transactions have fallen, particularly for transactions at smaller merchants that previously faced higher interchange rates. The reduction in interchange payments will be reflected in lower merchant service fees for many merchants. Interchange-like payments in the American Express companion card system are now also subject to equivalent regulation to that applying to the Mastercard and Visa credit card systems, helping ensure competitive neutrality and broadening the effect of the reforms.

After taking effect for large merchants in September 2016, the Reserve Bank's new surcharging framework became effective for all remaining merchants in September 2017, helping prevent excessive surcharging. To assist merchants' surcharging decisions, acquirers and payment facilitators were required from June 2017 to provide their merchants with easy-to-understand information on the cost of acceptance for each designated card scheme.

The Reserve Bank successfully encouraged industry progress on providing merchants with the ability to route contactless dual-network debit card transactions to their lowest-cost processing network, known as least-cost routing (LCR). Some small acquirers are now offering LCR functionality to their merchants, and the four major banks have committed to do so within the next year. LCR is aimed at increasing competitive pressure in the debit card market, and thereby holding down payment costs in the economy.

The Reserve Bank revamped its retail payments statistical collection to ensure its ongoing relevance and to minimise industry reporting burden. This was launched alongside a more efficient and secure data reporting system.

In support of the Payments System Board's responsibility to promote efficiency in the payments system, the Reserve Bank contributed to the industry project to deliver the New Payments Platform (NPP), which was publicly launched in February 2018. The NPP is a major development in Australia's retail payments infrastructure that facilitates real-time, data-rich, easily addressed payments on a 24/7 basis for households, businesses and government entities. To enable the settlement of NPP transactions between financial institutions in real time on a 24/7 basis, the Bank developed the RITS Fast

Settlement Service (FSS). From November 2017, the FSS operated in a 'live testing' mode as part of broader industry testing of NPP-related infrastructure ahead of the NPP's public launch.

The Reserve Bank published annual assessments of each of the licensed clearing and settlement facilities as part of its ongoing oversight of these facilities. Assessments were published of the ASX clearing and settlement facilities (in September 2017), of LCH.Clearnet Limited's SwapClear service (in December 2017) and of Chicago Mercantile Exchange Inc. (in March 2018). In these assessments, the Bank judged that all the entities had met the relevant standards and set out a series of regulatory priorities for the facilities for the subsequent year. The Bank's 2018 assessment of RITS against the *Principles for Financial Market Infrastructures*, which was published in May 2018, concluded that RITS observed all of the relevant principles.

In support of the Reserve Bank's oversight approach and of its policy framework, Bank staff also actively participated in international policy development on crisis management of financial market infrastructures and implementation monitoring related to CCP resilience. No change was required to domestic regulatory standards in 2017/18 as a result of international developments.

As the owner and operator of RITS, the Reserve Bank seeks to ensure that this system operates with extremely high levels of reliability and security, while also adapting to the needs of a 24/7 payments world. A broad range of operational metrics were tracked in real time during 2017/18, including measures of system liquidity, participants' transaction values and volumes, and system throughput and performance. For RITS, the system availability target is 99.95 per cent during core system hours. The Bank achieved this target during 2017/18, with system availability of 100 per cent achieved in core system hours. For FSS, the system availability target is 99.995 per cent on a 24/7 basis. The Bank met this target during 2017/18, with system availability of 100 per cent from the public launch of the NPP in February 2018 until 30 June 2018.

The Reserve Bank is committed to ensuring that RITS is well protected from cyber attack and has an ongoing program of work to maintain high levels of cyber resilience. The Bank made its first compliance attestation under the new SWIFT Customer Security Controls Framework in December 2017 and, in July 2018, the Bank's payment settlement systems received certification under the International Organization for Standardization (ISO) 27001 Information Security standard.

Analysis

The Reserve Bank's work in the payments area in 2017/18 occurred in an environment that was continuing to change rapidly, with higher expectations of users and the industry concerning the speed of payments and the capacity to combine information with payments. Use of cash and cheques is declining relative to other payment instruments, while use of cards and other electronic forms of payment continues to grow strongly. New technologies, including distributed ledger technologies and other forms of fintech, have the potential to change the payments landscape and the operation of financial market infrastructures significantly. Bank staff liaise actively with the private sector to better understand trends in these areas and have participated in a range of domestic and international working groups with other regulators. An important recent focus for the Bank has been on the implications of crypto-assets and the possible case for the Bank issuing an e-AUD (or digital cash) or providing a new form of central bank liability that could be used to settle a wider range of transactions than those currently settled via exchange settlement accounts.

Banking

Purpose

Insofar as the Commonwealth requires it to do so, the Reserve Bank must act as banker for the Commonwealth. In common with many other central banks, the Bank also provides banking and custody services to a number of overseas central banks and official institutions. These services include payments and collections as well as general account maintenance and reporting.

Results

The Reserve Bank must compete with other organisations to provide banking services to Australian Government agencies. The Bank must cost and price these services separately from its other activities. In addition, the return of providing these services must meet an externally prescribed minimum rate of return on capital over a business cycle. At present, this measure, equivalent to the 10-year Australian Government Security rate plus a margin for risk, is the Bank's principal measure of financial performance for its transactional banking business. In 2017/18, the Bank met the prescribed rate. Pro forma accounts for the transactional banking business are published in a separate chapter of this annual report.

As the provider of the Commonwealth's Official Public Account (OPA), the Reserve Bank works closely with both the Department of Finance and the Australian Office of Financial Management to ensure the central banking services it provides remain fit for purpose. The Department of Finance and the Bank have initiated a review of the Commonwealth's cash management principles to ensure the ongoing efficiency of cash flows into the OPA.

During 2017/18, the Reserve Bank completed several important banking projects, including the capability to participate in the NPP. Work on the renovation of banking applications and systems has continued as planned. Key milestones reached during the year included: the completion of the first phase of work to replace the Bank's core account maintenance system; the development of capability to deliver notifications to government agency customers using the Bank's renovated banking applications; and the delivery of the second phase of work on the functionality to process bulk electronic payments, which is currently in its final testing phase. The Bank has also commenced work to implement Application Programming Interfaces (APIs) to expand the Bank's capability to interact securely with agencies.

Analysis

The banking and payments landscape has continued to evolve, particularly in the area of payment services with the public launch of NPP in February 2018. The broader community is embracing new technology and continues to demand real-time digital services. Reflecting this demand, government agencies continue to push ahead with their own initiatives to improve service delivery and achieve productivity gains. Those initiatives that will impact the Reserve Bank include: the Department of Human Services Welfare Payment Infrastructure Transformation (WPIT) project; collections and payments programs for the Australian Taxation Office; and the Department of Finance's project to automate Commonwealth cash management processes using the NPP. During 2017/18, the Bank continued to ensure that it remained in a position to respond appropriately with convenient, secure, reliable and cost-effective services as the provider of both central banking and transactional banking services to the Australian Government.

Banknotes

Purpose

The Reserve Bank is responsible for the issue, reissue and cancellation of Australian banknotes. Its primary purpose in carrying out this role is to maintain public confidence in the supply, security and quality of Australian banknotes. The Bank works with its wholly owned subsidiary, Note Printing Australia Limited (NPA), to design and produce banknotes. The Bank distributes banknotes to financial institutions, monitors and maintains banknote quality in circulation and withdraws unfit banknotes from circulation. It also monitors and analyses counterfeiting trends and conducts research into banknote security technology.

Results

Public confidence in Australian banknotes is measured directly by a Reserve Bank survey on perceptions of Australian banknotes conducted every two years. The next survey is scheduled to be conducted in early 2019. Indirectly, 2018 evaluative research results from the Next Generation Banknote communication campaign showed sustained high levels of awareness of the new series of banknotes, with security understood to have been the main reason for the upgrade.

Fulfilment of banknote orders from commercial banks provides an indication that the public's demand for banknotes is being met. The Reserve Bank aims to fulfil 99.5 per cent of banknote orders on the day requested; during 2017/18, 100 per cent of orders were fulfilled on the day requested.

The Reserve Bank's key initiative to enhance banknote security is the release of the new banknote series with upgraded security features. Work on the Next Generation Banknote program continued during 2017/18, with the new $10 banknote entering circulation on 20 September 2017 as planned. The Bank implemented a comprehensive communication strategy to assist with public recognition of the new banknotes. The new $50 banknote is expected to enter circulation in October 2018.

The Reserve Bank continued to monitor Australian banknote counterfeiting rates, which remained low by international standards. The estimated counterfeiting rate remained stable at 16 parts per million in 2017/18, after having risen over the preceding decade or so. The Bank also continued to monitor international developments in counterfeiting. This was assisted by the Bank's engagement with other central banks and international organisations.

NPA met the Reserve Bank's orders for existing and new series banknotes in full, to the required quality standard and as per the agreed delivery schedule.

The quality of banknotes in circulation, as measured by the Reserve Bank in agreement with commercial banks, was broadly unchanged at a high level in 2017/18.

Analysis

While the proportion of payments made using banknotes is declining relative to electronic payments, the number and value of banknotes on issue continues to rise, highlighting their continued importance as a store of value as well as a payment mechanism. The Reserve Bank has continued to meet demand for banknotes by ensuring orders are fulfilled. The release of the new series of banknotes with upgraded security features is expected to maintain public confidence in banknotes. Australia's level of counterfeiting remains low by international standards, although it has tended to increase over time as advances in technology make it easier and cheaper to produce counterfeit banknotes.

Statutory Reporting Requirements

The Reserve Bank has a number of statutory reporting requirements that extend beyond its policy objectives and cover areas such as equal employment opportunity, work health and safety and freedom of information requests.

Equal Employment Opportunity

The Reserve Bank is strongly committed to ensuring that all employees are treated with respect and dignity, and experience equal opportunity throughout their careers with the Bank. This commitment is underpinned by a strong emphasis on embedding the Bank's values across all organisational practices and through its Diversity and Inclusion Plan. The Bank's policies and procedures seek to embed equity, diversity and inclusion principles in work practices. Its People and Culture Strategy and Diversity and Inclusion Plan outline key initiatives and priorities and are discussed further in the chapter on 'Our People'. During 2017/18, work was conducted to understand whether there are any systematic differences in the salaries of men and women at the Bank, as well as the factors that might account for any of these differences. The analysis showed that, while there were no systematic differences, there was evidence of a 17 per cent difference between the average salaries of males and females. This is largely due to the higher proportion of men in more senior positions. Differences in less senior roles are due to factors such as tenure, education and the types of positions in which men and women are employed. The review reinforces the importance of the Bank's commitment towards increasing the representation of women in management positions, as well as its continued focus on talent management and succession planning. There are plans to conduct ongoing reviews to monitor progress towards addressing these gender pay gaps.

the Bank is committed to increasing the representation of women in management positions

The Reserve Bank's Diversity and Inclusion Program is overseen by the Executive Committee, in consultation with the Diversity and Inclusion Council, which is responsible for monitoring the development and implementation of diversity and inclusion initiatives, policies and practices in the Bank. Full details and outcomes of the 2017/18 Diversity and Inclusion Program are provided in the Bank's the Bank's Health & Wellbeing Program aims to maximise the physical and psychological health of employees

Equity & Diversity Annual Report 2018, which will be tabled in the Parliament in accordance with the requirement under the *Equal Employment Opportunity (Commonwealth Authorities) Act 1987*. The *Equity & Diversity Annual Report 2017*, which reported on the Bank's diversity profile and progress on the diversity program in 2016/17, was tabled in the Parliament on 14 September 2017.

Work Health and Safety, Compensation and Rehabilitation

The Reserve Bank is strongly committed to maintaining and improving the safety, health and wellbeing of its employees and workers. The Bank fosters a safety culture that focuses on the Bank's work health and safety (WHS) risk profile through preventative and proactive due diligence and practices. The Reserve Bank Board and the Bank's executive management receive regular reports on WHS matters to assist them in exercising their duty of care.

During the year in review, the Bank continued to focus on workplace mental health issues, following the development of its mental health strategy in 2016/17. A mental health advisory panel was established to provide a channel for employees to provide input into the Mental Health and Wellbeing Strategic Plan and initiatives. Improvements were also made to the equipment, operating procedures and working environment for the new National Banknote Site following the introduction of automated systems at the site.

The Reserve Bank implemented initiatives through the Health & Wellbeing Program to maximise the physical and psychological health of employees through promotion of positive health outcomes and prevention of potential health risks, including:

- physical health activities, such as fitness classes at Head Office, an annual health challenge, influenza vaccinations and health checks for senior managers and executives
- mental health initiatives, such as mental health and resilience training, access to the Bank's Employee Assistance Program, awareness-raising activities and seminars on topics related to mental health and wellbeing.

There were 106 reported WHS incidents in 2017/18, 13 per cent higher than in the previous year. Four were notified to Comcare. The most prevalent cause of incidents were slips, trips and falls (14 per cent), incidents involving contractors (12 per cent) and sporting injuries sustained during breaks (9 per cent). There were four accepted workers' compensation claims in 2017/18. Two of these related to workplace injuries and two involved a sporting injury sustained during a break. The Reserve Bank's Lost Time Injury Frequency Rate (number of lost time injuries per million hours worked) increased in 2017/18 to 2.2 from 0.9 in the previous year,

Summary of Notifiable Incidents, Investigations and Notices under the WHS Act

Action	2017/18	2016/17
Death of a person that required notice to Comcare under section 35	0	0
Serious injury or illness of a person that required notice to Comcare under section 35	1	1
Dangerous incident that required notice to Comcare under section 35	3	5
Internal Investigations conducted	9	6
Investigations conducted under Part 10	0	0
Notices given to RBA under section 90 (provisional improvement notices)	0	0
Notices given to RBA under section 191 (improvement notices)	0	0
Notices given to RBA under section 195 (prohibition notices)	0	0
Directions given to RBA under section 198 (non-disturbance notices)	0	0

Source: RBA

reflecting the higher number of reported incidents. Nine internal WHS investigations were conducted in 2017/18. The investigations indicated that there were no systemic issues that would point to deficiencies in the way the Bank manages health and safety. No investigations were conducted by Comcare during 2017/18 that related to businesses or undertakings conducted by the Bank, and no improvement, prohibition or non-disturbance notices were issued by Comcare under Part 10 of the *Work Health and Safety Act 2011* (WHS Act).

The Reserve Bank is a Licensed Authority under the *Safety, Rehabilitation and Compensation Act 1988*. This licence requires the Bank to report to the Safety, Rehabilitation and Compensation Commission each year on WHS and workers' compensation and rehabilitation matters as they affect the Bank. Compliance with the relevant legislation – and the conditions of the Bank's licence as a Licensed Authority – was validated during the period by external audits of the Bank's safety, compensation and rehabilitation arrangements. The Safety, Rehabilitation and Compensation Commission subsequently confirmed that the Bank retained the highest rating for its prevention, claims management and rehabilitation practices in each area for 2017/18.

In 2017/18, the Australian Postal Corporation commenced Claims Management and Rehabilitation services for the Bank. This is in addition to the services already being provided by the Australian Postal Corporation under the existing licence, namely Reconsideration Services and AAT/Federal Court Representation.

Freedom of Information (FOI)

The Reserve Bank is an Australian Government agency subject to the *Freedom of Information Act 1982* (FOI Act). As required by Part II of the FOI Act, the Bank publishes information as part of the Information Publication Scheme (IPS). Details of the Bank's obligations under the FOI Act and the IPS can be found on the Bank's website.[1]

Fifteen requests for access to documents under the FOI Act were received in 2017/18. No relevant documents were found in response to nine requests and three requests were withdrawn. Access was granted in full in relation to one request and in part in relation to one request. One request was outstanding at the end of the financial year. Information that was released in response to FOI access requests was published on the Reserve Bank's website, as required by

1 See <https://www.rba.gov.au/foi/index.html>.

the FOI Act, with RSS feeds to these releases also available.

No applications were received for the internal review of FOI decisions made by the Reserve Bank in 2017/18.

The estimated amount of staff time spent dealing with all aspects of FOI requests in 2017/18 was around 171 hours, compared with around 196 hours in 2016/17. The total cost to the Reserve Bank of administering the FOI Act in 2017/18 is estimated to have been about $44,800, compared with $61,200 in the previous year. Processing charges of $160 were received in 2017/18.

Ministerial Directions

The Reserve Bank received no new directions from its responsible Minister (the Treasurer) or from any other Minister during 2017/18.

No government policy orders under section 22 of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act) were applied in relation to the Reserve Bank during 2017/18.

No issues relating to non-compliance by the Reserve Bank with finance law were reported to the Bank's responsible Minister (the Treasurer) under paragraph 19(1)(e) of the PGPA Act.

As one of the corporate Commonwealth entities 'prescribed' under section 30 of the Public Governance, Performance and Accountability Rule 2014, the Reserve Bank continues to be required to apply the Commonwealth Procurement Rules (CPRs) when performing duties relating to certain procurements.

The CPRs apply to the Reserve Bank whenever it undertakes a procurement where the expected value of the property or service being procured exceeds $400,000 for non-construction services or $7.5 million for construction services. For purchases of lower value, the Bank follows detailed guidelines based on the principles contained in the CPRs. The broad objective is to ensure that all goods and services procured by the Bank support its policy and operational responsibilities in an efficient and cost-effective manner.

Other Statutory Reporting Obligations

There were no significant activities or changes affecting the operations or structure of the Reserve Bank in 2017/18.

There were no judicial decisions or decisions of administrative tribunals made during 2017/18 that have had, or may have, a significant effect on the operations of the Reserve Bank.

Other statutory reporting obligations applying to the Reserve Bank that are covered elsewhere in this report are identified in the 'Statutory Reporting Requirements Index' on pages 191–192.

Part 4:

Financial Statements

Financial Statements

For the year ended 30 June 2018

Statement of Assurance

In the opinion of each of the Governor, as the accountable authority of the Reserve Bank of Australia (RBA), and the Chief Financial Officer, the financial statements for the year ended 30 June 2018 present fairly the Reserve Bank's financial position, financial performance and cash flows, comply with the accounting standards and any other requirements prescribed by the rules made under section 42 of the *Public Governance, Performance and Accountability Act 2013* and have been prepared from properly maintained financial records. These financial statements have been approved by a resolution of the Reserve Bank Board on 7 August 2018.

Philip Lowe
Governor and Chair, Reserve Bank Board

Robert Middleton-Jones
Chief Financial Officer

23 August 2018

Statement of Financial Position – as at 30 June 2018

Reserve Bank of Australia and Controlled Entity

	Note	2018 $M	2017 $M
Assets			
Cash and cash equivalents	6	373	221
Australian dollar investments	1(b), 15	104,253	104,769
Foreign currency investments	1(b), 15	75,912	83,577
Gold	1(d), 15	4,344	4,147
Property, plant and equipment	1(e), 8	679	741
Other assets	7	780	557
Total assets		186,341	194,012
Liabilities			
Deposits	1(b), 9	81,474	92,669
Distribution payable to the Commonwealth	1(h), 3	889	1,286
Australian banknotes on issue	1(b)	75,565	73,623
Other liabilities	10	3,036	4,671
Total liabilities		160,964	172,249
Net Assets		25,377	21,763
Capital and Reserves			
Reserves:			
Unrealised profits reserve	1(g)	5,860	2,682
Asset revaluation reserves	1(g), 5	5,020	4,721
Superannuation reserve	1(g)	338	201
Reserve Bank Reserve Fund	1(g)	14,119	14,119
Capital	1(g)	40	40
Total Capital and Reserves		25,377	21,763

The above statement should be read in conjunction with the accompanying Notes.

Statement of Comprehensive Income – for the year ended 30 June 2018

Reserve Bank of Australia and Controlled Entity

	Note	2018 $M	2017 $M
Net interest income	2	901	1,023
Fees and commission income	2	475	473
Other income	2	57	50
Net gains/(losses) on securities and foreign exchange	2	3,002	(1,857)
General administrative expenses	2	(421)	(406)
Other expenses	2	(167)	(180)
Net Profit/(Loss)		3,847	(897)
Gains/(losses) on items that may be reclassified to profit or loss:			
Gold		197	(420)
Shares in international and other institutions		28	(1)
		225	(421)
Gains/(losses) on items that will not be reclassified to profit or loss:			
Property		74	72
Held for sale assets		–	–
Superannuation		137	383
		211	455
Other Comprehensive Income		436	34
Total Comprehensive Income		4,283	(863)

The above statement should be read in conjunction with the accompanying Notes.

Statement of Distribution – for the year ended 30 June 2018

Reserve Bank of Australia and Controlled Entity

	Note	2018 $M	2017 $M
Net profit/(loss)		3,847	(897)
Transfer (to)/from unrealised profits reserve		(3,178)	2,179
Transfer from asset revaluation reserves		–	4
Earnings available for distribution		669	1,286
Distributed as follows:			
Transfer to Reserve Bank Reserve Fund		–	–
Payable to the Commonwealth	3	669	1,286
		669	1,286

The above statement should be read in conjunction with the accompanying Notes.

Statement of Changes in Capital and Reserves – for the year ended 30 June 2018

Reserve Bank of Australia and Controlled Entity

	Note	Unrealised profits reserve $M	Asset revaluation reserves $M	Superannuation reserve $M	Earnings available for distribution $M	Reserve Bank Reserve Fund $M	Capital $M	Total capital and reserves $M
Balance as at 30 June 2016		**4,861**	**5,074**	**(182)**	**–**	**14,119**	**40**	**23,912**
Net Profit/(Loss)	1(h)	(2,179)			1,282			(897)
Gains/(losses) on:								
Gold	1(d)		(420)					(420)
Shares in international and other institutions	1(b)		(1)					(1)
Property	1(e)		72					72
Superannuation	1(i)			383				383
Other comprehensive income			(349)	383				34
Total comprehensive income for 2016/17								**(863)**
Transfer from Asset revaluation reserves	1(g)		(4)		4			–
Transfer to Reserve Bank Reserve Fund	1(g), 3				–	–		–
Transfer to distribution payable to the Commonwealth	1(h), 3				(1,286)			(1,286)
Balance as at 30 June 2017		**2,682**	**4,721**	**201**	**–**	**14,119**	**40**	**21,763**
Net Profit/(Loss)	1(h)	3,178			669			3,847
Gains/(losses) on:								
Gold	1(d)		197					197
Shares in international and other institutions	1(b)		28					28
Property	1(e), 5		74					74
Held for sale assets	1(k), 5		–					–
Superannuation	1(i)			137				137
Other comprehensive income			299	137				436
Total comprehensive income for 2017/18								**4,283**
Transfer to Reserve Bank Reserve Fund	1(g), 3				–	–		–
Transfer to distribution payable to the Commonwealth	1(h), 3				(669)			(669)
Balance as at 30 June 2018		**5,860**	**5,020**	**338**	**–**	**14,119**	**40**	**25,377**

The above statement should be read in conjunction with the accompanying Notes.

Cash Flow Statement – for the year ended 30 June 2018

Reserve Bank of Australia and Controlled Entity

For the purposes of this statement, cash includes the banknotes and coin held at the RBA and overnight settlement balances due from other banks.

	Note	2018 Inflow/ (outflow) $M	2017 Inflow/ (outflow) $M
Cash flows from operating activities			
Interest received		2,213	1,890
Interest paid		(1,203)	(1,054)
Net fee income received		390	381
Net payments for investments		11,003	(35,984)
Net cash collateral (provided)/received		(1,502)	3,437
Other		(378)	(360)
Net cash from operating activities	6	10,523	(31,690)
Cash flows from investment activities			
Net expenditure on property, plant and equipment		(20)	(69)
Net expenditure on computer software		(32)	(36)
Other		–	(2)
Net cash from investment activities		(52)	(107)
Cash flows from financing activities			
Distribution to the Commonwealth	3	(1,066)	(3,222)
Net movement in deposit liabilities		(11,195)	31,459
Net movement in banknotes on issue		1,942	3,414
Net cash from financing activities		(10,319)	31,651
Net increase/(decrease) in cash		152	(146)
Cash at beginning of financial year		221	367
Cash at end of financial year	6	373	221

The above statement should be read in conjunction with the accompanying Notes.

Notes to and Forming Part of the Financial Statements – for the year ended 30 June 2018

Reserve Bank of Australia and Controlled Entity

Note

1	Accounting Policies	154
2	Net Profit	161
3	Distribution Payable to the Commonwealth	162
4	Interest Income and Interest Expense	163
5	Asset Revaluation Reserves	163
6	Cash and Cash Equivalents	164
7	Other Assets	164
8	Property, Plant and Equipment	165
9	Deposits	165
10	Other Liabilities	166
11	Contingent Assets and Liabilities	166
12	Key Management Personnel	168
13	Auditor's Remuneration	169
14	Superannuation Funds	169
15	Financial Instruments and Risk	174
16	Fair Value	181
17	Subsequent Events	183

Note 1 – Accounting Policies

The RBA reports its consolidated financial statements in accordance with the *Reserve Bank Act 1959* and the *Public Governance, Performance and Accountability Act 2013* (PGPA Act). These financial statements for the year ended 30 June 2018 are a general purpose financial report prepared under Australian Accounting Standards (AAS) and accounting interpretations issued by the Australian Accounting Standards Board, in accordance with the *Public Governance, Performance and Accountability (Financial Reporting) Rule 2015*, which is issued pursuant to the PGPA Act. The RBA is classified as a for-profit public sector entity for the purposes of financial disclosure. These financial statements comply with International Financial Reporting Standards. In preparing them, the RBA has not 'early adopted' new accounting standards or amendments to current standards that apply from 1 July 2018.

All amounts in these financial statements are expressed in Australian dollars, the functional and presentational currency of the RBA. Revenue and expenses are brought to account on an accruals basis. All revenues, expenses and profits of the RBA are from ordinary activities.

(a) Consolidation

The financial statements show information for the economic entity only; this reflects the consolidated results for the parent entity, the RBA, and its wholly owned subsidiary, Note Printing Australia Limited (NPA). The results of the parent entity do not differ materially from the economic entity and have therefore not been separately disclosed.

Note Printing Australia Limited

NPA was incorporated as a wholly owned subsidiary of the RBA on 1 July 1998.

NPA Balance Sheet	2018 $M	2017 $M
Assets	173.9	158.6
Liabilities	35.5	24.5
Equity	138.4	134.1

The assets, liabilities and results of NPA have been consolidated with the accounts of the parent entity in accordance with AASB 10 – *Consolidated Financial Statements*. All internal transactions and balances have been eliminated on consolidation. These transactions include items relating to the purchase of Australian banknotes, lease of premises and the provision of general administrative services.

(b) Financial instruments

A financial instrument is defined as any contract that gives rise to both a financial asset of one entity and a financial liability or equity instrument of another entity. The RBA accounts for its financial instruments in accordance with AASB 139 – *Financial Instruments: Recognition and Measurement* and reports these instruments under AASB 7 – *Financial Instruments: Disclosures* and AASB 13 – *Fair Value Measurement*. The RBA brings its securities transactions and foreign exchange transactions to account on a trade date basis. Deposits and repurchase agreements are brought to account on settlement date.

Financial assets

Australian dollar securities

The RBA holds on an outright basis Australian Government Securities and securities issued by the central borrowing authorities of state and territory governments.

Australian dollar securities, except those held under reverse repurchase agreements, are classified under AASB 139 as 'at fair value through profit or loss', as they are held to implement monetary policy and may be sold or lent, typically for short terms, under repurchase agreements. The securities are valued at market bid prices on balance date; valuation gains or losses are taken to profit. Interest earned on securities is accrued as revenue in the Statement of Comprehensive Income.

Reverse repurchase agreements

In carrying out operations to manage domestic liquidity and foreign reserves, the RBA enters into reverse repurchase agreements in Australian dollar and foreign currency securities. A reverse repurchase agreement involves the purchase of securities with an undertaking to reverse this transaction at an agreed price on an agreed future date. As a reverse repurchase agreement provides the RBA's counterparties with cash for the term of the agreement, the RBA treats it as an asset by recording a cash receivable. Repurchase agreements result in cash being paid to the RBA and are treated as a liability, reflecting the obligation to repay cash.

Reverse repurchase agreements are classified under AASB 139 as 'loans and receivables' and valued at amortised cost. Interest earned is accrued over the term of the agreement and recognised as revenue.

RBA open repurchase agreements are provided to assist eligible financial institutions manage their liquidity after normal business hours. An RBA open repurchase agreement is an Australian dollar reverse repurchase agreement without an agreed maturity date. The RBA accrues interest daily on open repurchase agreements at the target cash rate.

Foreign government securities

Foreign government securities, except those held under reverse repurchase agreements, are classified under AASB 139 as 'at fair value through profit or loss', as they are available to be traded in managing the portfolio of foreign exchange reserves. These securities are valued at market bid prices on balance date and valuation gains or losses are taken to profit. Interest earned on securities is accrued as revenue.

Foreign deposits

Some foreign currency reserves are invested in deposits with central banks and the Bank for International Settlements (BIS), while small working balances are also maintained with a small number of commercial banks. Deposits are classified as 'loans and receivables' under AASB 139 and recorded at face value, which is equivalent to their amortised cost. Interest is accrued over the term of deposits.

Foreign currency swaps

The RBA uses foreign currency swaps with market counterparties both to assist daily domestic liquidity management and in managing foreign reserve assets. A foreign currency swap is the simultaneous purchase and sale of one currency against another currency for a specified maturity. The cash flows are the same as borrowing one currency for a certain period and lending another currency for the same period. The pricing of the swap therefore reflects the interest rates applicable to these money market transactions. Interest rates are implicit in the swap contract but interest itself is not paid or received. Foreign currency swaps are classified as 'at fair value through profit or loss' under AASB 139.

Interest rate futures

The RBA uses interest rate futures contracts on overseas exchanges to manage interest rate risk on its portfolio of foreign assets.

Interest rate futures positions are classified under AASB 139 as 'at fair value through profit or loss' and reported within 'Foreign currency investments'. Futures positions are marked to market on balance date and valuation gains and losses are taken to profit.

Asian Bond Fund

The RBA invests in a number of non-Japan Asian debt markets through participation in the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP) Asian Bond Fund. This investment comprises units in the local currency-denominated fund, ABF2.

ABF2 is classified under AASB 139 as 'at fair value through profit or loss' and is valued on balance date at the relevant unit price of the fund, with valuation gains and losses taken to profit. ABF2 is reported within 'Foreign currency investments'.

Shareholding in Bank for International Settlements

Shares in the BIS are owned exclusively by the central banks and monetary authorities that are its members, including the RBA.

Under AASB 139, the RBA's shareholding is classified as 'available for sale'. The shareholding is valued at fair value and revaluation gains and losses are transferred directly to the revaluation reserve for shares in international and other institutions (Note 5). The uncalled portion of this shareholding is disclosed as a contingent liability in Note 11. Dividends are recognised as revenue in the Statement of Comprehensive Income.

Financial liabilities

Deposit liabilities

Deposits held with the RBA include both deposits 'at call' and term deposits. Deposits are classified as financial liabilities under AASB 139 and recorded at their amortised cost, which is equivalent to their face value. Interest is accrued over the term of deposits and is paid periodically or at maturity. Interest accrued on deposits but not paid is included in Other Liabilities (Note 10). Details of deposits are included in Note 9.

Australian banknotes on issue

Banknotes on issue are a financial liability recorded at face value.

The RBA pays interest on working balances of banknotes held by banks under cash distribution arrangements. Details of the interest expense are included in Note 4.

Costs related to the production of banknotes are included in 'Other expenses' in Note 2.

Repurchase agreements

A repurchase agreement involves the sale of securities with an undertaking to repurchase them on an agreed future date at an agreed price. Securities sold and contracted for repurchase under repurchase agreements are retained on the balance sheet and reported within the relevant investment portfolio (refer to 'Australian dollar securities' and 'Foreign government securities', above). The counterpart obligation to repurchase the securities is reported in 'Other liabilities' (Note 10) at amortised cost; the difference between the sale and purchase price is accrued over the term of the agreement and recognised as interest expense.

(c) Foreign exchange translation

Assets and liabilities denominated in foreign currency are converted to Australian dollar equivalents at the relevant market exchange rate on balance date in accordance with AASB 121 – *The Effects of Changes in Foreign Exchange Rates*. Valuation gains or losses on foreign currency are taken to profit. Interest revenue and expenses and revaluation gains and losses on foreign currency securities are converted to Australian dollars using exchange rates on the date they are accrued or recognised.

(d) Gold

Gold holdings (including gold on loan to other institutions) are valued at the Australian dollar equivalent of the 3.00 pm fix in the London gold market on balance date. Revaluation gains and losses on gold are transferred to the asset revaluation reserve for gold.

The RBA lends gold to institutions that participate in the gold market. Gold provided under a loan is retained on the balance sheet. Interest is accrued over the term of the loan and is paid at maturity. The interest receivable on gold loans is accounted for in accordance with AASB 139.

(e) Property, plant and equipment

The RBA accounts for its property, plant and equipment in accordance with AASB 116 – *Property, Plant and Equipment* and AASB 13.

Property

The RBA measures its property at fair value. The RBA's Australian properties are formally valued annually by an independent valuer; overseas properties are independently valued on a triennial basis with the most recent valuation conducted for 30 June 2016. Reflecting their specialised nature, the RBA's Business Resumption Site and National Banknote Site are valued at depreciated replacement cost. Valuation gains (losses) are generally transferred to (from) the asset revaluation reserve of each respective property. Any part of a valuation loss that exceeds the balance in the relevant asset revaluation reserve is expensed. Subsequent valuation gains that offset losses that were previously treated as an expense are recognised as income in the Statement of Comprehensive Income.

Annual depreciation is calculated on a straight line basis using assessments of the remaining useful life of the relevant building.

Plant and equipment

Plant and equipment is valued at cost less accumulated depreciation. Annual depreciation is calculated on a straight line basis using the RBA's assessments of the remaining useful life of individual assets.

Depreciation rates for each class of depreciable assets are based on the following range of useful lives:

	Years
Buildings	15–50
Fit-out	5–10
Computer hardware	4
Motor vehicles	5
Plant and other equipment	4–20

Assets are assessed for impairment at the end of each financial year. If indications of impairment are evident, the asset's recoverable amount is estimated and an impairment adjustment is made if the recoverable amount is less than the asset's carrying amount.

Annual net expenditure, revaluation adjustments and depreciation of property, plant and equipment are included in Note 8.

(f) Computer software

Computer software is treated in accordance with AASB 138 – *Intangible Assets*. Computer software is recognised at cost less accumulated amortisation and impairment adjustments, if any (refer to Note 7).

Amortisation of computer software is disclosed in Note 2 and is calculated on a straight line basis over the estimated useful life of the relevant asset, usually for a period of between four and six years. The useful life of payments settlements and core banking software may be for a period of between 10 and 15 years, reflecting the period over which future economic benefits are expected to be realised from these assets.

(g) Capital and reserves

The capital of the Reserve Bank is established by the Reserve Bank Act.

The Reserve Bank Reserve Fund (RBRF) is also established by the Reserve Bank Act and is regarded essentially as capital. The RBRF is a permanent reserve maintained to provide for events that are contingent and not foreseeable, including to cover losses from falls in the market value of the RBA's holdings of Australian dollar and foreign currency securities that cannot be absorbed by its other resources. The RBRF also provides for other risks such as fraud and operational risk. In accordance with the Reserve Bank Act, this reserve is funded only by transfers from net profits.

The Reserve Bank Board assesses the adequacy of the balance of the RBRF each year.

In line with section 30 of the Reserve Bank Act, the Treasurer, after consulting the Board, determines any amounts to be placed to the credit of the RBRF from net profit (refer Note 1(h)). The balance of the RBRF currently stands at a level that the Board regards as appropriate for the risks the RBA holds on its balance sheet.

The RBA's equity also includes a number of other reserves.

Unrealised gains and losses on foreign exchange, foreign securities and Australian dollar securities are recognised in net profit. Such gains or losses are not available for distribution and are transferred to the unrealised profits reserve, where they remain available to absorb future unrealised losses or become available for distribution if gains are realised when assets are sold or mature.

The balance of the Superannuation reserve represents accumulated remeasurement gains and losses on the RBA's defined benefit superannuation obligations (refer Note 1 (i)). These unrealised gains and losses are included in Other Comprehensive Income in accordance with AASB 119 – *Employee Benefits*.

Balances of asset revaluation reserves reflect differences between the fair value of non-traded assets and their cost. These assets are: gold; property; and shares in international and other institutions. Valuation gains are transferred directly to the relevant reserves and are included in Other Comprehensive Income; gains on these assets are not distributable unless an asset is sold and these gains are realised.

(h) Net Profits

Net profits of the RBA are dealt with in the following terms by section 30 of the Reserve Bank Act:

(1) Subject to subsection (2), the net profits of the Bank in each year shall be dealt with as follows:

(aa) such amount as the Treasurer, after consultation with the Reserve Bank Board, determines is to be set aside for contingencies; and

(a) such amount as the Treasurer, after consultation with the Reserve Bank Board, determines shall be placed to the credit of the Reserve Bank Reserve Fund; and

(b) the remainder shall be paid to the Commonwealth.

(2) If the net profit of the Bank for a year is calculated on a basis that requires the inclusion of unrealised gains on assets during the year, the amount to which subsection (1) applies is to be worked out as follows:

(a) deduct from the net profit an amount equal to the total of all amounts of unrealised gains included in the net profit; and

(b) if an asset in respect of which unrealised gains were included in the net profit for a previous year or years is realised during the year – add to the amount remaining after applying paragraph (a) the total amount of those unrealised gains.

(i) Superannuation funds

The RBA includes in its Statement of Financial Position an asset or liability representing the position of its defined benefit superannuation funds measured in accordance with AASB 119. Movements in the superannuation asset or liability are reflected in the Statement of Comprehensive Income. Remeasurement gains and losses are transferred to the Superannuation reserve. Details of the superannuation funds and superannuation expenses are included in Note 14.

(j) Committed Liquidity Facility

The RBA provides a committed liquidity facility (CLF) to eligible authorised deposit-taking institutions (ADIs). Fees received from providing the CLF are recognised as fee income in the Statement of Comprehensive Income. Additional information on the CLF is provided in Note 11.

(k) Non-current assets held for sale

A non-current asset is classified as being held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. This classification requires the asset to be available for immediate sale and for the sale to be highly probable. Held for sale assets are measured at the lower of their carrying amount or fair value less sale costs, in accordance with AASB 5 – *Non-current Assets Held for Sale and Discontinued Operations*.

(l) Rounding

Amounts in the financial statements are rounded to the nearest million dollars unless otherwise stated.

(m) Comparative information

Certain comparative information may be reclassified where required for consistency with the current year presentation.

(n) Application of new or revised Australian Accounting Standards

A number of new and revised AAS will apply to the RBA's financial statements in future reporting periods, as set out below.

AASB 9 – Financial Instruments

The new standard, which is applicable for annual reporting periods beginning on or after 1 January 2018, contains the principles for the recognition and measurement of financial assets and financial liabilities. It will replace the corresponding requirements in AASB 139. The new standard amends the assessment criteria for the classification of financial assets and introduces a new expected credit loss model for assessing impairments arising from deterioration in credit quality.

Application of the new standard is not expected to materially impact upon the recognition or measurement of the RBA's financial assets and liabilities. AASB 9 will result in some additional disclosures, mainly additional qualitative information on the RBA's management of credit risk.

AASB 15 – Revenue from Contracts with Customers

AASB 15 is applicable for annual reporting periods beginning on or after 1 January 2018. The new standard contains requirements for the recognition, measurement, classification and disclosure of revenue arising from contracts with customers. AASB 15 provides a principles-based approach for revenue recognition, centred around the satisfaction of performance obligations under a contractual agreement.

This new standard is not expected to have a material effect on the recognition and measurement of revenue from the RBA's contracts with its customers, but additional disclosures on the nature of these contracts will be made in the notes to the financial statements.

AASB 16 – Leases

AASB 16 contains requirements for the recognition, measurement and classification of leases for both lessees and lessors. The new standard, which will be applicable for annual reporting periods beginning on or after 1 January 2019, will replace corresponding requirements currently contained in AASB 117 – *Leases*. Application of this standard is currently being assessed, but is not expected to have a material effect on the RBA's financial statements.

Note 2 – Net Profit

	Note	2018 $M	2017 $M
Net interest income			
Interest income	1(b), 4	2,101	2,109
Interest expense	1(b), 4	(1,200)	(1,086)
		901	1,023
Fees and commissions income			
Committed liquidity facility	1(j)	349	347
Banking services		105	106
Payment services		21	20
		475	473
Other income			
Sales of note and security products		42	32
Rental of Bank premises		10	9
Dividend revenue	1(b)	4	5
Other		1	4
		57	50
Net gains/(losses) on securities and foreign exchange			
Foreign investments	1(b)	(99)	(169)
Australian dollar securities	1(b)	(160)	(400)
Foreign currency	1(b)	3,261	(1,288)
		3,002	(1,857)
General administrative expenses			
Staff costs		(226)	(218)
Net gains/(losses) on employee provisions		12	20
Superannuation costs	1(i)	(58)	(77)
Depreciation of property, plant and equipment	1(e), 8	(47)	(41)
Amortisation of computer software	1(f), 7	(17)	(10)
Premises and equipment		(64)	(61)
Other		(21)	(19)
		(421)	(406)
Other expenses			
Banking service fees		(88)	(89)
Materials used in note and security products		(45)	(49)
Banknote distribution		(1)	(2)
Other		(33)	(40)
		(167)	(180)
Net profit/(loss)		3,847	(897)

Note 3 – Distribution Payable to the Commonwealth

Net profits of the RBA, less amounts set aside for contingencies or placed to the credit of the RBRF, are paid to the Commonwealth as required by section 30 of the Reserve Bank Act (see Note 1(h)). Also under section 30, unrealised profits from foreign exchange, foreign securities and Australian dollar securities are not available for distribution. Instead they are transferred to the unrealised profits reserve where they remain available to absorb future valuation losses or are realised when relevant assets are sold or mature. Unrealised losses are, in the first instance, absorbed within the unrealised profits reserve where they are offset against unrealised profits accumulated from previous years. For purposes of distribution, if such losses exceed the balance of the unrealised profits reserve, the amount by which they do so is initially charged against other components of net profit, and any remaining loss is absorbed by the RBRF.

In 2017/18, the RBA recorded a net profit of $3,847 million. Unrealised valuation gains of $3,178 million were transferred to the unrealised profits reserve. Earnings available for distribution therefore amounted to $669 million in 2017/18.

As the Board regarded the balance of the RBRF as appropriate for the risks held on the balance sheet, it recommended that no transfer to this reserve be made from net profit in 2017/18. Accordingly, the Treasurer, after consulting the Board, determined that the full sum of earnings available for distribution be paid as a dividend to the Commonwealth. An amount of $1,066 million from earnings in 2016/17 was paid to the Commonwealth in 2017/18, with the balance of $220 million paid in July 2018.

	2018 $M	**2017 $M**
Opening balance	1,286	3,222
Distribution to the Commonwealth	(1,066)	(3,222)
Transfer from Statement of Distribution	669	1,286
As at 30 June	889	1,286

Note 4 – Interest Income and Interest Expense

Analysis for the year ended 30 June 2018

	Average balance $M	Interest $M	Average annual interest rate Per cent
Interest income			
Foreign currency investments	74,878	345	0.5
Australian dollar investments	91,865	1,744	1.9
Overnight settlements	494	6	1.3
Cash collateral provided	283	4	1.5
Gold loans	399	1	0.2
Loans, advances and other	42	1	1.4
	167,961	2,101	1.3
Interest expense			
Exchange Settlement balances	27,529	408	1.5
Deposits from governments	40,700	699	1.7
Deposits from overseas institutions	2,478	30	1.2
Banknote holdings of banks	3,284	41	1.2
Foreign currency repurchase agreements	1,627	16	1.0
Australian dollar repurchase agreements	61	1	1.4
Cash collateral received	321	5	1.5
Other deposits	4	–	0.2
	76,004	1,200	1.6
Net interest income	91,957	901	1.0
Analysis for the year ended 30 June 2017			
Interest income	160,245	2,109	1.3
Interest expense	70,254	1,086	1.5
Net interest income	89,991	1,023	1.1

Interest income for 2017/18 includes $1,501 million calculated using the effective interest method for financial assets not at fair value through profit or loss ($1,376 million in 2016/17). Interest expense for 2017/18 includes $1,200 million calculated using the effective interest method for financial liabilities not at fair value through profit or loss ($1,086 million in 2016/17).

Note 5 – Asset Revaluation Reserves

The composition of the RBA's asset revaluation reserves (Note 1(g)) is shown below.

	Note	2018 $M	2017 $M
Gold	1(d)	4,217	4,020
Shares in international and other institutions	1(b), 7	397	369
Property[(a)]	1(e), 8	300	332
Held for sale assets[(a)]	1(k), 7	106	–
As at 30 June		5,020	4,721

(a) An amount of $106 million was transferred from the asset revaluation reserve for property to the asset revaluation reserve for held for sale assets, representing the cumulative revaluation gain on the Bank's office building in Melbourne ($40 million of which was recorded during 2017/18, prior to its reclassification). Further detail is provided in Note 7

Note 6 – Cash and Cash Equivalents

	2018 $M	2017 $M
Cash	51	42
Overnight settlements	322	179
As at 30 June	373	221

Reconciliation of net cash used in operating activities to Net Profit	**Note**	**2018 $M**	**2017 $M**
Net profit/(loss)		3,847	(897)
(Decrease)/increase in interest payable		(20)	23
Net loss on overseas investments	2	99	169
Net loss on Australian dollar securities	2	160	400
Net (gain)/loss on foreign currency	2	(3,261)	1,288
Decrease/(increase) in income accrued on investments		130	(210)
Cash collateral (provided)/received		(1,502)	3,437
Depreciation of property, plant and equipment	2	47	41
Amortisation of computer software	2	17	10
Net payments for investments		11,003	(35,984)
Other		3	33
Net cash used in operating activities		10,523	(31,690)

Cash and cash equivalents include net amounts of $322 million owed to the RBA for overnight clearances of financial transactions through the payments system ($179 million at 30 June 2017). Other cash and cash equivalents include NPA's bank deposits. Cash and cash equivalents exclude Australian and foreign short-term investments held to implement monetary policy or as part of Australia's foreign reserve assets. These investments are disclosed as Australian dollar investments and foreign currency investments, respectively; further detail is disclosed in Note 15.

Note 7 – Other Assets

	Note	**2018 $M**	**2017 $M**
Shareholding in Bank for International Settlements	1(b)	440	412
Held for sale asset	1(k)	108	–
Computer software	1(f)	98	82
Superannuation asset	1(i), 14	57	–
Other		77	63
As at 30 June		780	557

At 30 June 2018, the gross book value of the RBA's computer software amounted to $140.1 million and the accumulated amortisation on these assets was $42.5 million ($110.0 million and $27.9 million, respectively, at 30 June 2017). During 2017/18, there were $30.1 million in net additions to computer software ($30.7 million in 2016/17) and $16.5 million in amortisation expense ($10.1 million in 2016/17).

The RBA had contractual commitments of $7.2 million as at 30 June 2018 for the acquisition of computer software ($9.6 million at 30 June 2017).

The RBA has commenced a process for the sale of its office property in Melbourne. The decision to sell the property via market follows a review of the RBA's property assets and its operational requirements. Completion of the sale is expected in the first half of 2018/19. Accordingly, the property has been reclassified as being held for sale, as required by AASB 5, and disclosed as part of Other Assets (see Note 1(k)). The property was disclosed as part of property, plant and equipment at 30 June 2017 (refer to Note 8).

Other assets include receivables of $23.5 million as at 30 June 2018 ($25.9 million at 30 June 2017), none of which is impaired.

Note 8 – Property, Plant and Equipment

	Land and Buildings $M	Plant and Equipment $M	Total $M
Gross Book Value as at 30 June 2017	552	296	848
Accumulated depreciation	(1)	(106)	(107)
Net Book Value	551	190	741
Additions	2	18	20
Depreciation expense	(13)	(34)	(47)
Net gain/(loss) recognised in Other Comprehensive Income	74	–	74
Disposals	–	(1)	(1)
Transfer to held for sale assets	(108)	–	(108)
Net additions to net book value	(45)	(17)	(62)
Gross Book Value as at 30 June 2018	508	307	815
Accumulated depreciation	(2)	(134)	(136)
Net Book Value	506	173	679

The net book value of the RBA's property, plant and equipment includes $12.0 million of work in progress ($29.0 million at 30 June 2017).

As at 30 June 2018, the RBA had contractual commitments of $5.6 million for the acquisition or development of property, plant and equipment ($10.4 million at 30 June 2017), all of which are due within one year.

Note 9 – Deposits

	2018 $M	2017 $M
Exchange Settlement balances	28,546	28,215
Australian Government	49,012	59,086
State governments	149	232
Foreign governments, foreign institutions and international organisations	3,766	5,126
Other depositors	1	10
As at 30 June	81,474	92,669

Note 10 – Other Liabilities

	Note	2018 $M	2017 $M
Provisions			
Provision for annual and other leave		21	21
Provision for long service leave		43	44
Provision for post-employment benefits		94	106
Other		1	–
		159	171
Other			
Securities sold under agreements to repurchase	1(b)	1,797	1,580
Payable for unsettled purchases of securities	1(b)	694	1,533
Foreign currency swap liabilities	1(b), 15	219	1,150
Interest accrued on deposits		76	95
Superannuation liability	1(i), 14	–	55
Other		91	87
		2,877	4,500
Total Other Liabilities as at 30 June		3,036	4,671

The RBA's provision for its post-employment benefits was $11.8 million lower in 2017/18, largely due to a decline in the assumed growth rate for the cost of providing these benefits in future periods. Benefits of $4.6 million were paid out of the provision for post-employment benefits in 2017/18. The balance of the provision for post-employment benefits will change if assumptions about the length of staff service, the longevity of retired staff, future costs of providing benefits, or the discount rate varies.

Other provisions consist of $622,000 for workers compensation ($488,000 at 30 June 2017).

Note 11 – Contingent Assets and Liabilities

Committed Liquidity Facility

Since 1 January 2015, the RBA has provided a CLF to eligible ADIs as part of Australia's implementation of the Basel III liquidity standards. The CLF provides ADIs with a contractual commitment to funding under repurchase agreements with the RBA, subject to certain conditions. It was established to ensure that ADIs are able to meet their liquidity requirements under Basel III. The CLF is made available to ADIs in Australia because the supply of high-quality liquid assets (HQLA) is lower in Australia than is typical in other major economies; in other countries, these liquidity requirements are usually met by banks' HQLAs on their balance sheet. While the RBA administers the CLF, the Australian Prudential Regulation Authority (APRA) determines which institutions have access to the facility and the limits available. Any drawdown must meet certain conditions, including: APRA does not object to the drawdown; and the RBA assesses that the ADI has positive net worth. Accordingly, the potential funding under the CLF is disclosed as a contingent liability; repurchase agreements associated with providing funding are disclosed as a contingent asset. If an ADI drew on the CLF, the funds drawn would be shown as a deposit liability of the RBA, and the counterpart repurchase agreement as an Australian dollar investment.

The aggregate undrawn commitment of the CLF at 30 June 2018 totalled about $223 billion for 14 ADIs (about $193 billion for 14 ADIs at 30 June 2017).

Bank for International Settlements

The RBA has a contingent liability for the uncalled portion of its shares held in the BIS amounting to $68.4 million at 30 June 2018 ($65.1 million at 30 June 2017).

NPA and Securency

Charges were laid in 2011 against NPA and Securency International Pty Ltd (Securency) alleging that the companies and a number of individuals conspired to provide or to offer to provide, at various times between December 1999 and September 2004, benefits to foreign public officials that were not legitimately due. A number of former employees of the companies were charged between 2011 and 2013 with engaging in the alleged conspiracies, with false accounting offences or with both. The RBA has accounted for the costs, and potential costs, to the consolidated entity related to these charges in accordance with AASB 137 – *Provisions, Contingent Liabilities and Contingent Assets*. Specific information about these charges and the associated costs have not been disclosed in the notes to the accounts as these matters remain before the courts. In light of several uncertainties, it is not possible to make reliable estimates of all of the potential costs associated with the charges, or potential claims in connection with them, at the date of preparing these accounts.

In February 2013, the RBA completed the sale of its 50 per cent interest in Securency (now known as CCL Secure Pty Ltd) to a related entity of Innovia Films, a UK-based film manufacturer, which had previously owned the other half of Securency. An amount covering 50 per cent of certain potential liabilities of Securency relating to events prior to the sale was placed in escrow in February 2013. In February 2020 the RBA will receive the balance then remaining in escrow after relevant claims have been paid, settled or lapse. Where it is not possible to estimate the likelihood of the RBA receiving any payment from the amount held in escrow, this amount is treated as a contingent asset, in accordance with AASB 137.

Under the sale agreement the RBA also provided the owner of Securency with a number of indemnities in relation to the period during which Securency had been jointly owned by the RBA and Innovia Films. The RBA is unable to reliably estimate the potential financial effect of any obligation to make payment under or in connection with the sale agreement. Accordingly, these potential costs are treated as contingent liabilities in accordance with AASB 137.

Insurance

The RBA carries its own insurance risks except when external insurance cover is considered to be more cost-effective or is required by legislation.

Performance Guarantees

In the course of providing services to its customers, the RBA provides performance guarantees to third parties in relation to customer activities. Such exposure is not material and has not given rise to losses in the past.

Similarly, the RBA has provided a performance guarantee for pension payments to members of the Reserve Bank of Australia UK Pension Scheme in relation to a UK insurer. This exposure is not material. Further detail is provided in Note 14.

Note 12 – Key Management Personnel

The key management personnel of the RBA are the Governor and Deputy Governor, non-executive members of the Reserve Bank Board, non-executive members of the Payments System Board and the Assistant Governors, who are the senior staff responsible for planning, directing and controlling the activities of the RBA. There were 20 of these positions in 2017/18. A total of 23 individuals occupied these positions for all or part of the financial year. This compares with 25 in the previous year, reflecting the conclusion of the terms of, and the appointment of successors for, a number of occupants of positions in the group of key management personnel.

The positions of Governor and Deputy Governor are designated as Principal Executive Offices in terms of the *Remuneration Tribunal Act 1973*, which provides for the Remuneration Tribunal to determine the applicable remuneration for these positions. Within the parameters determined by the Remuneration Tribunal, the Reserve Bank Board Remuneration Committee, comprising three non-executive members, makes a recommendation on remuneration for these positions for the approval of the Board, which is the 'employing body' for the positions. In accordance with provisions of the Reserve Bank Act, neither the Governor nor the Deputy Governor takes part in decisions of the Reserve Bank Board relating to the determination or application of any terms or conditions on which either of them holds office.

The remuneration reference rate for the position of Governor is $1,020,000 (superannuable salary of $744,600) and that for the Deputy Governor is $765,000 (superannuable salary of $558,450). Remuneration of each of the Governor and Deputy Governor in 2017/18 was at the applicable reference rate. No performance payments were made to either the Governor or Deputy Governor in 2017/18.

Fees for non-executive members of the Reserve Bank Board and the Payments System Board are determined by the Remuneration Tribunal. The Governor, after consulting with the Board, determines the rates of remuneration of Assistant Governors. For staff generally, remuneration aims to be market competitive and designed to attract and retain appropriately skilled people. Remuneration levels for employees are externally benchmarked.

The disclosure of key management personnel remuneration is based on AASB 124 – *Related Party Disclosures*, as shown below. The figures are disclosed on an accruals basis and show the full cost to the consolidated entity; they include all leave and fringe benefits tax charges.

	2018 $	2017 $
Short-term employee benefits	4,857,890	5,331,771
Post-employment benefits	815,019	884,655
Other long-term employee benefits	277,765	596,005
Termination benefits	–	–
Total compensation[(a)]	5,950,674	6,812,431

(a) Within the group of key management personnel, 21 individuals (23 in 2016/17) were remunerated and included in this table; the two key management personnel that are not remunerated are the Secretary to the Treasury, as a member of the Reserve Bank Board, and the Chairman of APRA, as a member of the Payments System Board

Short-term benefits include cash salary and, where relevant for executives, lump-sum payments, motor vehicle benefits, car parking and health benefits and the fringe benefits tax paid or payable on these benefits.

Post-employment benefits include superannuation benefits and, in the case of executives, health benefits. Other long-term employee benefits include long service leave and annual leave as well as the cost of (or gain on) revaluing previously accrued leave entitlements in accordance with AASB 119 (refer Note 10).

There were no loans by the RBA to any key management personnel during 2017/18 and 2016/17.

There were no related party transactions with Board members or other key management personnel during 2017/18 and 2016/17. Transactions with Board member-related entities that occurred in the normal course of the RBA's operations were incidental and conducted on terms no more favourable than similar transactions with other employees or customers; any vendor relationships with such entities were at arm's length and complied with the RBA's procurement policy.

Note 13 – Auditor's Remuneration

	2018 $	2017 $
Fees paid or payable to the statutory auditor (Australian National Audit Office) for audit services	425,000	459,000

KPMG has been contracted by the Australian National Audit Office (ANAO) to provide audit services for the external audit of the RBA and the RBA's subsidiary NPA. The amount for 2016/17 also included audit services for the Reserve Bank of Australia Officers' Superannuation Fund (OSF), which was transferred to a multi-employer fund via a successor fund transfer in March 2017.

During 2017/18, KPMG earned additional fees of $125,286 for non-audit services that were separately contracted by the RBA ($80,069 in 2016/17). These fees, which included taxation services and advice provided to the RBA and the OSF, are mainly included in General administrative expenses in Note 2.

Note 14 – Superannuation Funds

The RBA sponsors two superannuation funds: RB Super and the Reserve Bank of Australia UK Pension Scheme. Current and future benefits are funded by member and RBA contributions and the existing assets of these schemes. The RBA's superannuation expenses are included in net profit and shown in Note 2.

RB Super is a hybrid plan, with a mix of defined benefit members, defined contribution members and pensioners. Defined benefit members receive a defined benefit in accordance with RB Super's plan rules. Most members have unitised accumulation balances, which comprise employer contributions and members' personal contributions plus earnings on these contributions. Defined benefit membership was closed to new RBA staff from 1 August 2014. From that date, new staff have been offered defined contribution superannuation. The RBA does not have a role in directly operating or governing RB Super and has no involvement in the appointment of the RB Super Trustees.

The UK Pension Scheme is a closed defined benefit scheme subject to relevant UK regulation. The Trustees, with agreement from the RBA, have entered into a bulk purchase annuity (BPA) contract with a UK insurer as part of a process to eventually wind up the UK Pension Scheme. Defined benefit accrual for current members ceased on 30 June 2018. From that date, current and new staff have been offered defined contribution arrangements.

Funding valuation

Independent actuarial valuations of RB Super and the UK Pension Scheme are conducted every three years.

The triennial actuarial valuation for RB Super was completed for the financial position as at 30 June 2017 using the Attained Age Funding method. Accrued benefits were determined as the value of the future benefits payable to members (allowing for future salary increases), discounted by the expected rate of return on assets held to fund these benefits. At the time of this review, the surplus was $190.1 million. On the same valuation basis, the RB Super surplus as at 30 June 2018 amounted to $284.1 million. The RBA maintained its contribution rate to fund defined benefit obligations at 18.3 per cent of salaries in 2017/18, consistent with the actuary's recommendation.

The latest funding valuation for the UK Scheme was at 30 June 2016 and was also based on the Attained Age Funding method. At the time of this review, the UK Pension Scheme was in a small surplus with assets of $25.6 million compared with accrued benefits of $25.5 million. The bulk of the scheme's assets are currently invested in the BPA, with the balance invested in short-term money market securities and UK government bonds. The purchase of the BPA has significantly reduced funding risk for the scheme. Once a full due diligence is completed, a balancing payment will be made to the UK insurer to finalise the BPA. This amount is currently unknown, though it is expected that there will be sufficient assets in the scheme to fund the BPA balancing payment. To the extent this is not the case, the RBA would cover any shortfall.

Accounting valuation

For financial statement purposes, the financial positions of RB Super and the UK Pension Scheme are valued in accordance with AASB 119. This standard requires disclosures of significant actuarial assumptions, a maturity analysis of the defined benefit obligation and key risk exposures. Information is provided only for RB Super, as the UK Pension Scheme is not material.

Actuarial assumptions

The principal actuarial assumptions for the AASB 119 valuation of RB Super are:

	2018 Per cent	2017 Per cent
Discount rate (gross of tax)[(a)]	4.4	4.5
Future salary growth[(b)]	3.0	3.0
Future pension growth[(b)]	3.0	3.0

(a) Based on highly rated Australian dollar-denominated corporate bond yields
(b) Includes a short-term assumption of 2.0 per cent for the first three years of the projections (2.0 per cent for the first four years in 2017)

Maturity analysis

The weighted average duration of the defined benefit obligation for RB Super is 18 years (19 years at 30 June 2017). The expected maturity profile for defined benefit obligations of RB Super is as follows:

	2018 Per cent	2017 Per cent
Less than 5 years	17	18
Between 5 and 10 years	16	16
Between 10 and 20 years	28	26
Between 20 and 30 years	20	19
Over 30 years	19	21
Total	100	100

Risk exposures

Key risks from the RBA's sponsorship of the RB Super defined benefit plan include investment, interest rate, longevity, salary and pension risks.

Investment risk is the risk that the actual future return on plan assets will be lower than the assumed rate.

Interest rate risk is the exposure of the defined benefit obligations to adverse movements in interest rates. A decrease in interest rates will increase the present value of these obligations.

Longevity risk is the risk that RB Super members live longer, on average, than actuarial estimates of life expectancy.

Salary risk is the risk that higher than assumed salary growth will increase the cost of providing a salary-related pension.

Pension risk is the risk that pensions increase at a faster rate than assumed, thereby increasing the cost of providing them.

The table below shows the estimated change in the defined benefit obligation resulting from movements in key actuarial assumptions. These estimates change each assumption individually, holding other factors constant; they do not incorporate any correlations among these factors.

	2018 $M	2017 $M
Change in defined benefit obligation from an increase of 0.25 percentage points in:		
Discount rate (gross of tax)	(61)	(62)
Future salary growth	14	16
Future pension growth	47	47
Change in defined benefit obligation from a decrease of 0.25 percentage points in:		
Discount rate (gross of tax)	65	66
Future salary growth	(14)	(15)
Future pension growth	(45)	(45)
Change in defined benefit obligation from an increase in life expectancy of one year	48	43

Asset distribution

The distribution of RB Super's assets used to fund members' defined benefits at 30 June is:

	Per cent of fund assets	
	2018	**2017**
Cash and short-term securities	2	2
Fixed interest and indexed securities	8	10
Australian equities	34	34
International equities	23	24
Property	12	12
Private equity	6	6
Infrastructure	12	10
Hedge funds	3	2
Total	100	100

AASB 119 Reconciliation

The table below contains a reconciliation of the AASB 119 valuation of RB Super. The opening balance figures in 2017 are for the OSF, which was transferred to a multi-employer fund via a successor fund transfer in March 2017 and became RB Super. These details are for the defined benefit component only, as the RBA faces no actuarial risk on defined contribution balances and these balances have no effect on the measurement of the financial position of RB Super.

	2018 $M	2017 $M
Opening balances:		
Net market value of assets	1,157	991
Accrued benefits	(1,213)	(1,388)
Opening superannuation asset/(liability)	(56)	(397)
Change in net market value of assets	113	166
Change in accrued benefits	–	175
Change in superannuation asset/(liability)	113	341
Closing balances:		
Net market value of assets	1,270	1,157
Accrued benefits	(1,212)	(1,213)
Closing superannuation asset/(liability)	57	(56)
Interest income	52	35
Benefit payments	(49)	(45)
Return on plan assets	88	152
Contributions from RBA to defined benefit schemes	22	24
Change in net market value of assets	113	166
Current service cost	(43)	(53)
Interest cost	(55)	(49)
Benefit payments	49	45
Gains/(losses) from change in demographic assumptions	42	–
Gains/(losses) from change in financial assumptions	(40)	253
Gains/(losses) from change in other assumptions	46	(21)
Change in accrued benefits	–	175
Current service cost	(43)	(53)
Net Interest (expense)/income	(3)	(13)
Productivity and superannuation guarantee contributions	(8)	(7)
Superannuation (expense)/income included in profit or loss	(54)	(73)
Actuarial remeasurement gain/(loss)	137	383
Superannuation (expense)/income included in Statement of Comprehensive Income	83	310

The components of this table may not add due to rounding.

Note 15 – Financial Instruments and Risk

As the central bank in Australia, the RBA is responsible for implementing monetary policy, facilitating the smooth functioning of the payment system and managing Australia's foreign reserve assets. Consequently, the RBA holds a range of financial assets, including government securities, repurchase agreements and foreign currency swaps. As to financial liabilities, the RBA issues Australia's banknotes and takes deposits from its customers, mainly the Australian Government, and eligible financial institutions. The RBA also provides banking services to its customers and operates Australia's high-value payments and interbank settlement systems.

Financial Risk

The RBA is exposed to a range of financial risks that reflect its policy and operational responsibilities. These risks include market risk, credit risk and liquidity risk. The chapters on 'Operations in Financial Markets' and 'Risk Management' provide information on the RBA's management of these financial risks. The RBA's approach to managing financial risk is set out in the Risk Appetite Statement available on the RBA website.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises foreign exchange risk and interest rate risk.

Foreign exchange risk

Foreign exchange risk is the risk that the fair value or cash flows of the RBA's foreign currency assets and liabilities will fluctuate because of movements in exchange rates. The RBA's net foreign currency exposure as at 30 June 2018 was $53.8 billion ($51.8 billion as at 30 June 2017). An appreciation in the Australian dollar would therefore result in valuation losses, while a depreciation would lead to valuation gains. The overall level of foreign currency exposure is determined by policy considerations. Foreign currency risk can be mitigated to a limited extent by holding assets across a diversified portfolio of currencies. The RBA holds foreign reserves in seven currencies – the US dollar, euro, Japanese yen, Canadian dollar, Chinese renminbi, UK pound sterling and South Korean won.

The RBA also undertakes foreign currency swaps to assist its daily domestic liquidity management and to manage foreign reserve assets. These instruments carry no foreign exchange risk.

Concentration of foreign exchange

The RBA's net holdings of foreign exchange (excluding Special Drawing Rights and Asian Bond Fund 2) were distributed as follows as at 30 June:

	Per cent of foreign exchange	
	2018	**2017**
US dollar	55	55
Euro	20	20
Japanese yen	5	5
Canadian dollar	5	5
Chinese renminbi	5	5
UK pound sterling	5	5
South Korean won	5	5
Total foreign exchange	100	100

Sensitivity to foreign exchange risk

The sensitivity of the RBA's profit and equity to a movement of +/–10 per cent in the value of the Australian dollar exchange rate as at 30 June is shown below. These figures are generally reflective of the RBA's exposure over the financial year.

	2018 $M	2017 $M
Change in profit/equity due to a 10 per cent:		
appreciation in the reserves-weighted value of the A$	(4,896)	(4,715)
depreciation in the reserves-weighted value of the A$	5,984	5,763

Interest rate risk

Interest rate risk is the risk that the fair value or cash flows of financial instruments will fluctuate because of movements in market interest rates. The RBA faces interest rate risk because most of its assets are financial assets that have a fixed income stream, such as Australian dollar and foreign currency securities. The price of such securities rises when market interest rates decline, and it falls if market rates rise. Interest rate risk increases with the maturity of a security. Interest rate risk on foreign assets is controlled through limits on the duration of these portfolios. Interest rate risk on Australian dollar assets is relatively low as most of the portfolio is held in short-term reverse repurchase agreements.

Sensitivity to interest rate risk

The figures below show the effect on the RBA's profit and equity of a movement of +/–1 percentage point in interest rates, given the level, composition and modified duration of the RBA's foreign currency and Australian dollar securities as at 30 June.

	2018 $M	2017 $M
Change in profit/equity due to movements of +/–1 percentage point across yield curves:		
Foreign currency securities	–/+284	–/+287
Australian dollar securities	–/+142	–/+157

Liquidity risk

Liquidity risk is the risk that the RBA will not have the resources required at a particular time to meet its obligations to settle its financial liabilities. As the ultimate source of liquidity in Australian dollars, the RBA can create liquidity in unlimited amounts in Australian dollars at any time. A small component of the RBA's liabilities is in foreign currencies, namely foreign repurchase agreements.

Liquidity risk may also be associated with the RBA, in extraordinary circumstances, being forced to sell a financial asset at a price less than its fair value. The RBA manages this risk by holding a diversified portfolio of highly liquid Australian dollar and foreign currency assets.

The analysis of portfolio maturity in the table that follows is based on the RBA's contracted portfolio as reported in the RBA's Statement of Financial Position. All financial instruments are shown at their remaining term to maturity, which is equivalent to the repricing period. Other liabilities include amounts outstanding under repurchase agreements. Foreign currency swaps reflect the gross contracted amount of the RBA's outstanding foreign currency swap positions.

Maturity Analysis – as at 30 June 2018

	Balance sheet total $M	Contracted maturity $M					No specified maturity $M	Weighted average effective rate (%)
		On demand	0 to 3 months	3 to 12 months	1 to 5 years	Over 5 years		
Assets								
Cash and cash equivalents	373	50	322	–	–	–	1	1.25
Australian dollar investments								
Securities purchased under repurchase agreements	93,503	–	66,832	–	–	–	26,671	1.85
Securities sold under repurchase agreements	780	–	–	780	–	–	–	1.92
Other securities	9,729	–	3	7,350	1,454	922	–	2.05
Accrued interest	241	–	210	31	–	–	–	na
	104,253							
Foreign currency investments								
Balances with central banks	23,164	22,420	744	–	–	–	–	0.05
Securities purchased under repurchase agreements	2,834	–	2,834	–	–	–	–	1.26
Securities sold under repurchase agreements	996	–	471	79	446	–	–	0.80
Other securities	47,813	–	25,311	10,046	6,049	220	6,187	0.70
Deposits	602	–	601	–	–	–	1	3.50
Cash collateral provided	411	–	411	–	–	–	–	1.50
Accrued interest	92	–	71	21	–	–	–	na
	75,912							
Gold								
Gold holdings on loan	605	–	219	386	–	–	–	0.15
Gold holdings	3,739	–	–	–	–	–	3,739	na
	4,344							
Property, plant & equipment	679	–	–	–	–	–	679	na
Other assets	780	–	23	8	6	1	742	na
Total assets	186,341	22,470	98,052	18,701	7,955	1,143	38,020	1.27
Liabilities								
Deposits	81,474	34,966	46,508	–	–	–	–	1.63
Distribution payable to the Commonwealth	889	–	605	284	–	–	–	na
Australian banknotes on issue	75,565	–	–	–	–	–	75,565	0.04
Cash collateral received	17	–	17	–	–	–	–	1.50
Other liabilities	3,019	–	2,860	–	–	–	159	0.46
Total liabilities	160,964	34,966	49,990	284	–	–	75,724	0.86
Capital and reserves	25,377							
Total balance sheet	186,341							
Swaps								
Australian dollars								
Contractual outflow	(246)	–	(246)	–	–	–	–	
Contractual inflow	19,995	–	19,995	–	–	–	–	
	19,749	–	19,749	–	–	–	–	
Foreign currency								
Contractual outflow	(41,077)	–	(41,077)	–	–	–	–	
Contractual inflow	21,328	–	21,328	–	–	–	–	
	(19,749)	–	(19,749)	–	–	–	–	

Maturity Analysis – as at 30 June 2017

	Balance sheet total $M	Contracted maturity $M					No specified maturity $M	Weighted average effective rate (%)
		On demand	0 to 3 months	3 to 12 months	1 to 5 years	Over 5 years		
Assets								
Cash and cash equivalents	221	41	179	–	–	–	1	1.21
Australian dollar investments								
Securities purchased under repurchase agreements	90,303	–	63,198	800	–	–	26,305	1.65
Securities sold under repurchase agreements	–	–	–	–	–	–	–	na
Other Securities	14,068	–	4,579	7,048	1,383	1,058	–	1.77
Accrued interest	398	–	392	6	–	–	–	na
	104,769							
Foreign currency investments								
Balance with central banks	20,340	19,624	716	–	–	–	–	0.04
Securities purchased under repurchase agreements	4,134	–	4,134	–	–	–	–	1.06
Securities sold under repurchase agreements	1,580	–	–	842	738	–	–	1.30
Other securities	57,265	–	34,178	11,440	5,806	122	5,719	0.40
Deposits	194	–	193	–	–	–	1	1.05
Cash collateral provided	–	–	–	–	–	–	–	na
Accrued interest	64	–	45	19	–	–	–	na
	83,577							
Gold								
Gold holdings on loan	365	–	209	156	–	–	–	0.21
Gold holdings	3,782	–	–	–	–	–	3,782	na
	4,147							
Property, plant & equipment	741	–	–	–	–	–	741	na
Other assets	557	–	25	7	5	2	518	na
Total assets	194,012	19,665	107,848	20,318	7,932	1,182	37,067	1.05
Liabilities								
Deposits	92,669	33,682	58,987	–	–	–	–	1.56
Distribution payable to the Commonwealth	1,286	–	1,066	220	–	–	–	na
Australian banknotes on issue	73,623	–	–	–	–	–	73,623	0.05
Cash collateral received	1,108	–	1,108	–	–	–	–	1.50
Other liabilities	3,563	–	3,354	–	–	–	209	0.42
Total liabilities	172,249	33,682	64,515	220	–	–	73,832	0.88
Capital and reserves	21,763							
Total balance sheet	194,012							
Swaps								
Australian dollars								
Contractual outflow	(170)	–	(170)	–	–	–	–	
Contractual inflow	28,815	–	28,815	–	–	–	–	
	28,645	–	28,645	–	–	–	–	
Foreign currency								
Contractual outflow	(52,745)	–	(52,745)	–	–	–	–	
Contractual inflow	24,100	–	24,100	–	–	–	–	
	(28,645)	–	(28,645)	–	–	–	–	

Credit risk

Credit risk is the potential for financial loss arising from an issuer or counterparty defaulting on its obligations to repay principal, make interest payments due on an asset, or settle a transaction. The RBA's credit exposure is managed within a framework designed to contain risk to a level consistent with its very low appetite for such risk. In particular, credit risk is controlled by holding securities issued by a limited number of highly rated governments, government-guaranteed agencies and supranational organisations and holding high-quality collateral against reverse repurchase agreements.

The RBA's maximum exposure to credit risk for each class of recognised financial assets, other than derivatives, is the carrying amount of those assets as indicated in the balance sheet.

The RBA's maximum credit risk exposure to derivative financial instruments is:

1. ***Foreign exchange swaps*** – As at 30 June 2018, the RBA was under contract to purchase $21.3 billion of foreign currency ($24.1 billion at 30 June 2017) and sell $41.1 billion of foreign currency ($52.7 billion at 30 June 2017). As of that date there was a net unrealised gain of $0.1 billion on these swap positions included in net profit ($1.5 billion unrealised gain at 30 June 2017).

   The RBA has a credit exposure from foreign exchange swaps because of the risk that a counterparty might fail to deliver the second leg of a swap, a sum that would then have to be replaced in the market, potentially at a loss. To manage credit risk on swaps, the RBA exchanges collateral with counterparties under terms specified in credit support annexes (CSAs), which cover the potential cost of replacing the swap position in the market if a counterparty fails to deliver. The RBA's CSAs specify that only Australian dollar cash is eligible as collateral. Under CSAs, either party to the agreement may be obliged to deliver collateral with interest paid or received on a monthly basis. At 30 June 2018, the RBA provided $0.4 billion of collateral ($1.1 billion of collateral was held at 30 June 2017).

2. ***Interest rate futures*** – As at 30 June 2018, the amount of credit risk on margin accounts associated with interest rate futures contracts held by the RBA was approximately $0.9 million ($0.8 million at 30 June 2017). As at 30 June 2018, there was an unrealised loss of $0.5 million brought to account on those contracts ($0.3 million unrealised gain at 30 June 2017).

The RBA held no past due or impaired assets at 30 June 2018 or 30 June 2017.

Collateral held under reverse repurchase agreements

Cash invested under reverse repurchase agreements in overseas markets is secured against government securities or securities issued by US agencies; the RBA takes and maintains collateral to the value of 102 per cent of the cash invested. Cash invested under Australian dollar reverse repurchase agreements is secured by securities issued by Australian governments, supranational organisations, banks and various corporate and asset-backed securities. The RBA holds collateral equivalent to the amount invested plus a margin according to the risk profile of the collateral held. If the current value of collateral falls by more than a predetermined amount, the counterparty is required to provide additional collateral to restore this margin; the thresholds are specified in the legal agreements which govern these transactions. The management of collateral and cash associated with tri-party repurchase agreements is conducted through a third party, in this case the Australian Securities Exchange. The terms and requirements of tri-party repurchase agreements are broadly consistent with bilateral agreements and the RBA manages the risk in a similar way. The RBA does not sell or re-pledge securities held as collateral under reverse repurchase agreements.

Collateral provided under repurchase agreements

At 30 June 2018, the carrying amount of securities sold and contracted for purchase under repurchase agreements was $1,789 million ($1,580 million at 30 June 2017). Terms and conditions of repurchase agreements are consistent with those for reverse repurchase agreements disclosed above.

Concentration of credit risk

As noted, the RBA operates to minimise its credit risk exposure through comprehensive risk management policy guidelines. The following table indicates the concentration of credit risk in the RBA's investment portfolio.

	Risk rating of security/issuer[(a)]	Risk rating of counterparties[(a)]	Per cent of investments	
			2018	2017
Australian dollar investments				
Holdings of Australian Government Securities	Aaa	na	3.7	6.1
Holdings of semi-government securities	Aaa	na	0.5	0.5
	Aa	na	1.1	0.8
Securities sold under repurchase agreements	Aaa	Aa	0.4	–
Securities purchased under reverse repurchase agreements	Aaa	Aa	30.2	27.4
	Aaa	A	10.9	10.1
	Aaa	Baa	0.8	0.2
	Aaa	Other[(b)]	1.9	1.3
	Aa	Aa	2.4	2.8
	Aa	A	1.8	1.7
	Aa	Baa	0.3	0.2
	Aa	Other[(b)]	0.1	0.1
	A	Aa	0.8	1.7
	A	A	0.8	1.0
	A	Baa	0.2	–
	Baa	A	0.1	0.1
Foreign investments				
Holdings of securities	Aaa	na	9.7	9.3
	Aa	na	3.3	1.6
	A	na	12.4	17.7
Securities sold under repurchase agreements	Aaa	A	–	0.8
	Aaa	Baa	0.2	–
	Aa	Aa	0.3	–
Securities purchased under reverse repurchase agreements	Aaa	Aa	0.4	0.3
	Aaa	A	0.5	1.4
	Aaa	Baa	0.3	–
	Aa	Aa	0.3	–
	A	A	–	0.4
Deposits	na	Aaa	0.7	0.5
	na	Aa	3.4	0.6
	na	A	8.6	9.5
Other	Aaa	A	0.1	–
	Aaa	Other[(b)]	–	0.1
	Aa	A	0.1	–
	na	Aa	0.3	0.5
	na	A	0.1	0.3
Other assets			3.3	3.0
			100.0	100.0

(a) Average of the credit ratings of the three major rating agencies, where available
(b) This category includes counterparties which are not rated

Note 16 – Fair Value

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at measurement date. This is the quoted market price if one is available. The RBA's financial assets measured at fair value include its holdings of Australian dollar securities, foreign government securities, interest rate futures, foreign currency swap contracts and its shareholding in the BIS. Non-financial assets carried on the balance sheet at fair value include the RBA's property and gold holdings. Other than derivatives, there are no financial liabilities measured at fair value.

AASB 13 requires financial and non-financial assets and liabilities measured at fair value to be disclosed according to their position in the fair value hierarchy. This hierarchy has three levels: valuation for Level 1 assets is based on quoted prices in active markets for identical assets; for Level 2 assets, valuation is based on quoted prices or other observable market data not included in Level 1; Level 3 assets include inputs to valuation other than observable market data.

The table below presents the RBA's assets and liabilities measured and recognised at fair value and their classification within the fair value hierarchy at 30 June 2018.

	Fair Value			Amortised Cost	Total
	Level 1 $M	Level 2 $M	Level 3 $M	$M	$M
As at 30 June 2018					
Financial assets					
At fair value through profit or loss					
Australian dollar securities	10,572	53	–	na	10,625
Foreign government securities	44,038	4,168	–	na	48,206
Foreign currency swaps	34	275	–	na	309
Available for sale					
Shares in other institutions	–	–	444	na	444
Loans and receivables	na	na	na	121,428	121,428
	54,644	4,496	444	121,428	181,012
Non-financial assets					
Land and buildings	–	–	506	na	506
Gold holdings	4,344	–	–	na	4,344
Other	–	–	108	371	479
	4,344	–	614	371	5,329
Total assets	58,988	4,496	1,058	121,799	186,341
Financial liabilities					
At fair value through profit or loss					
Foreign currency swaps	6	196	–	–	202
Not at fair value through profit or loss	na	na	na	160,561	160,561
	6	196	–	160,561	160,763
Non-financial liabilities	na	na	na	201	201
Total liabilities	6	196	–	160,762	160,964

	Fair Value			Amortised Cost	Total
	Level 1 $M	Level 2 $M	Level 3 $M	$M	$M
As at 30 June 2017					
Financial assets					
At fair value through profit or loss					
Australian dollar securities	14,276	75	–	na	14,351
Foreign government securities	52,552	4,661	–	na	57,213
Foreign currency swaps	111	1,395	–	na	1,506
Available for sale					
Shares in other institutions	–	–	416	na	416
Loans and receivables	na	na	na	115,530	115,530
	66,939	6,131	416	115,530	189,016
Non-financial assets					
Land and buildings	–	–	551	na	551
Gold holdings	4,146	–	–	na	4,146
Other	–	–	–	299	299
	4,146	–	551	299	4,996
Total assets	71,085	6,131	967	115,829	194,012
Financial liabilities					
At fair value through profit or loss					
Foreign currency swaps	–	42	–	na	42
Not at fair value through profit or loss	na	na	na	171,946	171,946
	–	42	–	171,946	171,988
Non-financial liabilities	na	na	na	261	261
Total liabilities	–	42	–	172,207	172,249

The RBA's Level 2 financial instruments include Australian dollar-denominated discount securities and some foreign currency swaps priced with reference to an active market yield or rate, but which have been interpolated to reflect maturity dates. Prices for some Australian dollar and foreign currency-denominated securities are derived from markets that are not considered active.

Level 3 assets include the RBA's shareholding in the BIS and its property. The shareholding in the BIS is valued using the net asset value, as published in annual financial statements of the BIS, less a discount of 30 per cent. The discount applied is based on a Hague Arbitral Tribunal decision on compensation paid to former private shareholders, and subsequent transactions involving the re-allocation of BIS shares. Fair values of the RBA's property incorporate factors such as net market income and capitalisation rates, for property valued using an income capitalisation or a discounted cash flow approach, and depreciation rates for property valued using a depreciable replacement cost methodology.

There were no transfers between levels within the fair value hierarchy during the financial year. Movements in the fair value of the RBA's property during the financial year are detailed in Note 8; the increase in value of the RBA's shareholding in the BIS solely reflects a valuation gain recognised in Other Comprehensive Income.

Note 17 – Subsequent Events

There are no events subsequent to 30 June 2018 to be disclosed.

Auditor-General for Australia

Australian National Audit Office

INDEPENDENT AUDITOR'S REPORT

To the Treasurer

Opinion

In my opinion, the financial statements of the Reserve Bank of Australia and its Controlled Entity (together the consolidated entity) for the year ended 30 June 2018:

(a) comply with Australian Accounting Standards and the *Public Governance, Performance and Accountability (Financial Reporting) Rule 2015*; and

(b) present fairly the financial position of the consolidated entity as at 30 June 2018 and its financial performance and cash flows for the year then ended.

The financial statements of the consolidated entity, which I have audited, comprise the following statements as at 30 June 2018 and for the year then ended:

- Statement of Assurance;
- Statement of Financial Position
- Statement of Comprehensive Income;
- Statement of Distribution;
- Statement of Changes in Capital and Reserves;
- Cash Flow Statement; and
- Notes to and forming part of the financial statements, including Accounting Policies and other explanatory information.

Basis for Opinion

I conducted my audit in accordance with the Australian National Audit Office Auditing Standards, which incorporate the Australian Auditing Standards. My responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of my report. I am independent of the consolidated entity in accordance with the relevant ethical requirements for financial statement audits conducted by me and his delegates. These include the relevant independence requirements of the Accounting Professional and Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants* (the Code) to the extent that they are not in conflict with the *Auditor-General Act 1997*. I have also fulfilled my other responsibilities in accordance with the Code. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgement, were of most significance in my audit of the financial statements of the current period. These matters were addressed in the context of my audit of the financial statements as a whole, and in forming my opinion thereon, and I do not provide a separate opinion on these matters.

GPO Box 707 CANBERRA ACT 2601
19 National Circuit BARTON ACT
Phone (02) 6203 7300 Fax (02) 6203 7777

Key audit matter

Accuracy of the liability for the Australian Banknotes

Refer to note 1 'Accounting Policies'

The balance of Australian banknotes on issue represents the value of all banknotes on issue and the liability ($75,565m as at 30 June 2018) is measured at the face value of all Australian banknotes issued less any banknotes withdrawn from circulation.

Australian banknotes on issue relates directly to one of the Reserve Bank of Australia's key roles, the issuance of currency, as defined in the *Reserve Bank Act 1959* and is a key audit matter for me due to:

- high interest to the users of the financial statements;
- the balance is significant relative to the Reserve Bank of Australia's Statement of Financial Position; and
- the accuracy of the liability for Australian banknotes on issue is dependent on the assumption that all Australian banknotes on issue retain their legal tender status. The audit of this assumption requires significant auditor judgement.

How the audit addressed the matter

To audit the Australian banknotes on issue, I performed the following audit procedures:

- Tested key controls relevant to the accurate recording of the issuance and return of bank notes, including general IT controls over the Note Control System.
- Agreed to the liability for Australian banknotes on issue recorded per the financial statements against the balance recorded per the Note Control System as at 30 June 2018.
- Assessed the movement in Australian banknotes on issue against known comparative trends. Demand for banknotes is driven, in part by underlying economic activity. I therefore compared movements in Notes on Issue against underlying economic activity, in particular household final consumption expenditure (HFCE). HFCE is produced by the Australian Bureau of Statistics and measures household expenditure.
- Performed a comparison of current year movements against prior year patterns, and investigated significant variances. I also performed a trend analysis on Australian banknotes on issue against prior periods focussing on the number of notes issued by denomination and investigated significant inconsistencies.

Key audit matter

Valuation of Australian dollar and foreign currency investments

Refer to note 1 'Accounting Policies' and note 15 'Financial Instruments and Risk'

Valuation of Australian dollar and foreign currency investments was a key audit matter due to their significant size relative to the Reserve Bank of Australia's statement of financial position ($180,165m as at 30 June 2018) and the complexity inherent in auditing a wide range of investments which use different valuation methodologies.

The portfolio of investments primarily comprises Australian dollar securities, foreign currency securities, repurchase agreements, deposits with other central banks, and foreign currency swap contracts. All investments are measured at fair value except for repurchase agreements and deposits which are measured at amortised cost.

How the audit addressed the matter

- Tested key relevant controls to the accurate recording of the purchase and sale of investments, including general IT controls on the Reserve Bank of Australia's investment trading system.
- Tested key controls relevant to the ongoing monitoring of the collateralisation of repurchase agreements.
- Tested year end valuations of Australian dollar and foreign currency securities using the following procedures to address the different valuation methodologies:
  - Checked all year end valuations of Australian dollar and foreign currency securities against independent pricing sources.
  - Tested the year-end valuations of all foreign currency swaps using independent publicly available information.
  - Checked whether all repurchase agreements were appropriately

	collateralised in line with the Reserve Bank of Australia's policy. As part of this, for a sample of securities held as collateral I agreed valuations to independent pricing sources. • Requested and obtained independent confirmation from other central banks regarding the value of deposits held with them.

Other Information

The Accountable Authority is responsible for the other information. The other information obtained at the date of this auditor's report is the Earnings, Distribution and Capital Chapter and the Voluntary Remuneration Disclosures for the year ended 30 June 2018 but does not include the financial statements and my auditor's report thereon.

My opinion on the financial statements does not cover the other information and accordingly I do not express any form of assurance conclusion thereon.

In connection with my audit of the financial statements, my responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work I have performed, I conclude that there is a material misstatement of this other information, I am required to report that fact. I have nothing to report in this regard.

Accountable Authority's Responsibility for the Financial Statements

As the Accountable Authority of the Reserve Bank of Australia the Governor is responsible under the *Public Governance, Performance and Accountability Act 2013* for the preparation and fair presentation of annual financial statements that comply with Australian Accounting Standards and the rules made under that Act. The Governor is also responsible for such internal control as the Governor determines is necessary to enable the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Governor is responsible for assessing the consolidated entity's ability to continue as a going concern, taking into account whether the entity's operations will cease as a result of an administrative restructure or for any other reason. The Governor is also responsible for disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the assessment indicates that it is not appropriate.

Auditor's Responsibilities for the Audit of the Financial Statements

My objective is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian National Audit Office Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with the Australian National Audit Office Auditing Standards, I exercise professional judgement and maintain professional scepticism throughout the audit. I also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;

- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the consolidated entity’s internal control;
- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Accountable Authority;
- conclude on the appropriateness of the Accountable Authority’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the consolidated entity’s ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor’s report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my auditor’s report. However, future events or conditions may cause the consolidated entity to cease to continue as a going concern;
- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation; and
- obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the consolidated entity to express an opinion on the financial report. I am responsible for the direction, supervision and performance of the consolidated entity audit. I remain solely responsible for my audit opinion.

I communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.

From the matters communicated with those charged with governance, I determine those matters that were of most significance in the audit of the financial report of the current period and are therefore the key audit matters. I describe these matters in my auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, I determine that a matter should not be communicated in my report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Australian National Audit Office

Grant Hehir

Auditor-General

Sydney

23 August 2018

Part 5:
Indexes

Statutory Reporting Requirements Index

The *Reserve Bank Annual Report 2018* complies with the reporting requirements of the *Public Governance, Performance and Accountability Act 2013* (PGPA Act), rules made under the PGPA Act and other applicable legislation.

To assist readers locate this information, the index of statutory reporting requirements identifies where relevant information can be found in this annual report.

Public Governance, Performance and Accountability Act 2013	**Page numbers**
Annual performance statement	129–140
Annual financial statements	147–187
Public Governance, Performance and Accountability Rule 2014	
Approval of annual report by accountable authority	1–2, 33
Establishing legislation	5, 30
Objects and functions	5–7
Purposes	129–140
Responsible Minister/s	30
Ministerial directions	144
Government policy orders	144
Annual performance statement	129–140
Compliance with finance law	144
Details of accountable authority	8, 15–16
Organisation structure	43–49
Location of offices and facilities	115
Corporate governance	8–14
Significant activities or changes affecting the Reserve Bank	144
Judicial decisions or decisions of administrative tribunals	144
Reports by outside bodies	33
Indemnities	13–14
***Work Health and Safety Act 2011* – reporting requirements**	
Health, safety and welfare initiatives	142–143
Health and safety outcomes	142–143
Statistics of notifiable incidents	142–143
Investigations conducted	142–143
***Environment Protection and Biodiversity Conservation Act 1999* – reporting requirements**	
Report on implementation of Ecologically Sustainable Development principles	116
Effect of the Reserve Bank's activities on the environment	116
Measures to minimise the impact of the Reserve Bank's activities	116
Mechanisms for reviewing/increasing effectiveness of measures	116

List of Tables

	Page number
Board Meetings – 2017/18	9
Audit Committee Meetings – 2017/18	10
Remuneration Committee Meetings – 2017/18	11
Australian Dollar Securities Held under Repurchase Agreements	58
Foreign Assets	61
Benchmark Foreign Currency Portfolio	62
Foreign Currency Assets	63
RBA Bilateral Local Currency Swap Agreements	64
Counterfeit Banknotes in Australia	72
Remuneration of Executives	110
Remuneration of Other Senior Employees	111
General Operating Costs	112
Capital Expenditure	113
Spending on Consultancies	113
Composition and Distribution of Reserve Bank Profits	127
Transactional Banking	128
Reserve Bank of Australia – Performance Summary 2017/18	130–132
Summary of Notifiable Incidents, Investigations and Notices under the WHS Act	143

List of Graphs

	Page number
Inflation over the Long Run	5
Reserve Bank Assets	53
Reserve Bank Liabilities	53
Australian Dollar	61
Net Foreign Exchange Reserves	62
Benchmark Portfolio Running Yield	63
RBA's Government Clients' NPP Receipts	66
FSS Transactions	69
Average Daily Value by Payment Type	70
Circulation Value	71
Banknotes in Circulation	72
Counterfeits Detected	73
Banknote Purchases	79
IMF New Arrangements	87
RBA Employee Numbers	103
RBA Employees Working on Projects	104
Diversity Profile at the RBA	104
Women in Management Positions	107
Exchange Rate Risk on RBA Foreign Currency Portfolio	118
Interest Rate Risk on RBA Portfolio	119
Portfolio Composition by Issuer	120
Underlying Earnings	125
Total Valuation Gains and Losses	125

List of Figures

	Page number
Reserve Bank of Australia Governance Structure	14
Reserve Bank of Australia Operational Structure	48–49
Reserve Bank Involvement in the G20	81
Australian Involvement in Key FSB Committees	83
Reserve Bank Involvement in EMEAP	88

Abbreviations

A glossary of relevant terms is available on the Reserve Bank website.[1]

24/7	24 hours per day, 7 days per week
AAS	Australian Accounting Standards
ABF	Asian Bond Fund
ABF1	Asian Bond Fund 1
ABF2	Asian Bond Fund 2
ADI	Authorised deposit-taking institution
AGS	Australian Government Securities
AGV	Analytical Group on Vulnerabilities (of the FSB)
ANAO	Australian National Audit Office
AOFM	Australian Office of Financial Management
API	Application Programming Interface
APRA	Australian Prudential Regulation Authority
ASD	Australian Signals Directorate
ASIC	Australian Securities and Investments Commission
ATFC	Advisory Task Force on the Codes
ATO	Australian Taxation Office
AusPayNet	Australian Payments Network
BCBS	Basel Committee on Banking Supervision (of the BIS)
BIS	Bank for International Settlements
BRS	Business Resumption Site
CAC Act	*Commonwealth Authorities and Companies Act 1997*
CCP	central counterparty
CEDA	Committee for Economic Development of Australia
CFR	Council of Financial Regulators
CGFS	Committee on the Global Financial System (of the BIS)
CHESS	Clearing House Electronic Sub-register System
CLF	Committed Liquidity Facility
CNY	Chinese renminbi
CPMI	Committee on Payments and Market Infrastructures (of the BIS)
CPRs	Commonwealth Procurement Rules
CSA	Credit support annex
EMEAP	Executives' Meeting of East Asia-Pacific Central Banks
eftpos	electronic funds transfer at point of sale
ERG	Employee Resource Group
ES	Exchange Settlement
ESA	Exchange Settlement Account
fintech	financial technology
FIN	Financial Innovation Network (of the FSB)
FMI	financial market infrastructure
FRR	Financial Reporting Rule
FOI	Freedom of Information
FOI Act	*Freedom of Information Act 1982*
FSAP	Financial Sector Assessment Program (of the IMF)
FSB	Financial Stability Board
FSS	Fast Settlement Service (of RITS)

1 See <http://www.rba.gov.au/glossary/>.

FTE	full-time equivalent
FX	foreign exchange
FXWG	Foreign Exchange Working Group (of the BIS)
G20	Group of Twenty
G-SIB	global systemically important bank
GHOS	Group of Governors and Heads of Supervision
GPF	Government Partnership Fund (with Indonesia)
HQLA	high-quality liquid assets
IMF	International Monetary Fund
IMSG	Implementation Monitoring Standing Group (a CPMI-IOSCO group)
IOSCO	International Organization of Securities Commissions
IPS	Information Publication Scheme
ISDA	International Swaps and Derivatives Association
IT	information technology
LCR	Liquidity Coverage Ratio
MC	Markets Committee (of the BIS)
MEF	multi-employer fund
MFSC	Monetary and Financial Stability Committee (of EMEAP)
MPG	Macroprudential Supervision Group (of the BCBS)
NBS	National Banknote Site
NGB	Next Generation Banknote
NPA	Note Printing Australia Limited
NPP	New Payments Platform
OECD	Organisation for Economic Co-operation and Development
OPA	Official Public Account
OSF	Officers' Superannuation Fund
PEXA	Property Exchange Australia Limited
PFMI	Principles for Financial Market Infrastructures
PGPA Act	*Public Governance, Performance and Accountability Act 2013*
PSG	Policy Standing Group (a CPMI-IOSCO group)
RAP	Reconciliation Action Plan
RBA	Reserve Bank of Australia
RBRF	Reserve Bank Reserve Fund
RCG FSB)	Regional Consultative Group (of the
RDP	Research Discussion Paper
R&D	research and development
repo	repurchase agreement
ReSG	Resolution Steering Group (of the FSB)
RITS	Reserve Bank Information and Transfer System
RMBS	residential mortgage-backed securities
RTGS	real-time gross settlement
SCAV	Standing Committee on Assessment of Vulnerabilities (of the FSB)
SCSI	Standing Committee on Standards Implementation (of the FSB)
SDR	Special Drawing Right
Semis	Semi-government securities (Australian state and territory government securities)
SRC	Standing Committee on Supervisory and Regulatory Cooperation (of the FSB)
SWIFT	Society for Worldwide Interbank Financial Telecommunication
TWI	trade-weighted index
WHS	work health and safety
WHS Act	*Work Health and Safety Act 2011*
WGPSS	Working Group on Payment and Settlement Systems

Contact Details

Head Office

65 Martin Place
Sydney NSW 2000
Telephone: (02) 9551 8111
Toll Free: 1800 300 288[1]
Website: https://www.rba.gov.au/
Email: rbainfo@rba.gov.au

State Offices

Queensland

Senior Representative: Paul Gardiner
Level 7, 12 Creek Street
Brisbane QLD 4000
Telephone: (02) 9551 8111
Toll Free: 1800 300 288[1]

South Australia

Senior Representative: Matthew Carter
Level 19, 25 Grenfell Street
Adelaide SA 5000
Telephone: (02) 9551 8111
Toll Free: 1800 300 288[1]

Victoria

Senior Representative: Gordon Flannigan
Level 13, 60 Collins Street
Melbourne VIC 3000
Telephone: (02) 9551 8111
Toll Free: 1800 300 288[1]

Western Australia

Senior Representative: Aaron Walker (Acting)
Level 11, London House
216 St Georges Terrace
Perth WA 6000
Telephone: (02) 9551 8111
Toll Free: 1800 300 288[1]

Canberra Branch

General Manager: Paul Martin
20–22 London Circuit
Canberra ACT 2600
Telephone: (02) 6201 4800
Email: canberrabranch-cn@rba.gov.au

Overseas Offices

China

Senior Representative: Adam Cagliarini
Australian Embassy
21 Dongzhimenwai Dajie
Beijing 100600
People's Republic of China
Telephone: +86 10 5140 4491
Fax: +86 10 5140 4244
Email: chinaenquiries@rba.gov.au

Europe

Chief Representative: Michael Davies
Deputy Chief Representative: Markus Hyvonen
53 New Broad Street
London EC2M 1JJ
Telephone: +44 20 7600 2244
Email: euenquiries@rba.gov.au

1 Freecall – not available to callers in Sydney. Excludes calls from mobile phones, which are charged at the applicable rate.

New York

Chief Representative: Carl Schwartz
Deputy Chief Representative: Sean Dowling
16th Floor
505 Fifth Avenue
New York, NY 10017
Telephone: +1 212 566 8466
Email: nyoffice@rba.gov.au

Note Printing Australia Limited

Chief Executive Officer: Malcolm McDowell
1–9 Potter Street
Craigieburn VIC 3064
Telephone: (03) 9303 0444
Website: https://www.noteprinting.com/