

1934

Story Reserve Bank established

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(Singleton, 2012)

What is a Reserve Bank?

Central, or reserve, banks are not-for-profit public policy agencies that stand between governments and banks. They issue bank notes and provide banking services to the government and commercial banks. Reserve banks have oversight of the banking system and may act as an emergency lender of last resort. They are a primary source of bank reserves, and have the ability to influence monetary conditions and spending in the economy by operating in financial markets or through regulation. By controlling the supply of money in the economy they can influence both interest rates and inflation.

Before the Reserve Bank

Before the creation of the Reserve Bank each trading bank in New Zealand issued their own bank notes. Most of the banks also operated in Australia. They held the bulk of their reserves in British pounds and British government securities in London.

During the late 1920s and early 1930s the financial situation in Australia was much worse than it was in New Zealand. Trading banks in New Zealand (four out of six of which were Australian-owned) were also losing reserves because of the Australian crisis – basically the Australian banks were running out of money. Since banks' New Zealand and Australian reserves were indistinguishable, their capacity to sustain business in New Zealand was reduced.



Bank notes



Sir Otto Niemeyer
in Rotorua, 1930



First Reserve Bank
board of directors,
1934

Dragging at Australia's coat-tails?

In 1932 Montagu Norman, governor of the Bank of England, had discussions with William Downie Stewart, the New Zealand minister of finance. According to Norman's notes, he 'suggested that the first and most important thing for New Zealand was to determine their attitude as an economic unit: were they to be dragged at the tail of Australia or to face their own affairs: in short, did his Government intend to form a Central Bank?'

Forming the Reserve Bank

Sir Otto Niemeyer, a senior official of the Bank of England, went to Australia in 1930 to discuss the financial crisis with the Australian government. The New Zealand government took this opportunity to ask Niemeyer to advise New Zealand on exchange-rate policy. The Bank of England's policy was to promote central banking in other parts of the world, and Niemeyer recommended the establishment of a central bank in New Zealand. By encouraging the spread of central banking, the Bank of England hoped to bolster the financial network based in London, to ensure that other governments serviced and repaid their sterling debts, and to deter the adoption of unconventional monetary policies.

First governor of the Reserve Bank

Leslie Lefeaux, the first governor of the Reserve Bank, was a stuffy Englishman who had been deputy chief cashier and assistant to the governors at the Bank of England. He did not adapt well to life in Wellington. When Labour achieved power in 1935, with plans to take the Reserve Bank into full state ownership, Lefeaux was outraged and considered resigning. But his former colleagues at the Bank of England persuaded him to remain at his post.

Neither the Bank of England nor the New Zealand government believed that a central bank would solve the depression, however, and the formation of a central bank was not regarded as a matter of urgency in Wellington. Gordon Coates, who became minister of finance in January 1933, was the main supporter of the scheme, which finally secured parliamentary endorsement later that year. The Reserve Bank opened for business in 1934 and by 1935 it had 60 staff. It was two-thirds owned by the government and one-third by private shareholders. At the request of the New Zealand government, the first governor, Leslie Lefeaux, was recommended by the Bank of England. The Reserve Bank became the main source of reserves for the trading banks. Monetary separation from Australia was reinforced, but the central bank did not initiate New Zealand's recovery from the depression – recovery was already in progress by 1934.

Footnotes:

1. Bank of England Archive, OV59/1, Notes of informal meeting between the Governor and Downie Stewart at the Hotel Metropole, London, 15 September 1932.

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