



Submission on Capital Review

Federated Farmers of New Zealand

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SUBMISSION ON CAPITAL REQUIREMENTS REVIEW

TO: RBNZ

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ABOUT FEDERATED FARMERS

Federated Farmers of New Zealand is a membership organisation, which is mandated by its members to advocate on their behalf and ensure representation of their views. Federated Farmers does not collect a compulsory levy under the Commodity Levies Act and is funded from voluntary membership.

Federated Farmers represents rural and farming businesses throughout New Zealand. We have a long and proud history of representing the needs and interests of New Zealand's farmers.

Federated Farmers aims to empower farmers to excel in farming. Our key strategic outcomes include provision for an economic and social environment within which:

- Our members may operate their business in a fair and flexible commercial environment;
- Our members' families and their staff have access to services essential to the needs of a vibrant rural community; and
- Our members adopt responsible management and sustainable food production practices.

1. SUBMISSION ON 2025 REVIEW OF KEY CAPITAL SETTINGS

- 1.1 Federated Farmers welcomes the opportunity to comment on the 2025 Review of Key Capital Settings Consultation Paper (25 August 2025).
- 1.2 The proposal introduces more granular standardised risk weights for residential mortgages and agricultural lending. This is a positive shift from the current flat framework and gets closer to reflecting the reality of lending risk.
- 1.3 However, this review still fails to address the persistent conservatism in New Zealand's capital regime, highlighted in the Oliver Wyman report (30 July 2025, Section 3.3).
- 1.4 While the risks weights have improved, the proposed changes risk delivering only modest efficiency gains. Our submission focuses on Chapter 5 (Questions 29, and 30) and advocates recalibration to deliver meaningful benefits to agriculture.

2. SUMMARY OF RECOMMENDATIONS

- 2.1 Recognise the reality of New Zealand's banking market structure in agriculture.
 - A non-Domestically Systemically Important Bank (D-SIB) lender (Rabobank) holds around 22% of agricultural lending yet is required to use standardised risk weights by default, unlike the four majors that apply Internal Ratings-Based (IRB) models.
 - This creates a structural imbalance, as Rabobank's risk weights are materially higher than the weighted-average IRB settings already applied by its competitors.
 - Standardised settings should therefore be calibrated to reflect this market reality, instead of assuming the standardised approach is used only by small, niche lenders; rather than a single lender with nearly a quarter of the market share.
- 2.2 Set proportionate, risk-sensitive standardised agricultural risk weights
 - Reduce standardised rates to **30% for LVR ≤30% and 55% for LVR 30–50%** (compared with IRB averages of 21.7% and 41.8% respectively).
 - Introduce an ultra-low tier of 10–15% for highly secured, low-LVR loans, consistent with stress test and historical loss data.
 - Consider sector-specific factors such as farm type, diversification, hedging, and collateral quality to ensure risk weights genuinely reflect Loss-Given-Default (LGD) exposures.
 - Align standardised weights more closely with IRB averages while still applying a conservative buffer, avoiding capital requirements materially harsher than international norms (Oliver Wyman benchmarking).

3. GENERAL DISCUSSION ON RISK WEIGHTS

- 3.1 The Reserve Bank proposes standardised risk weights for agricultural lending of 50% for LVR $\leq 30\%$ and 75% for LVR 30.01–50%. While these are lower than the current blanket 100%, they remain far higher than the risk actually borne in the market.

Type of lending	Current standardised risk weight (%)	Proposed standardised risk weight (%)
Owner-occupier residential mortgage lending (RML) with loan-to-value ratio (LVR) ≤ 50	35	25
Owner-occupier RML with LVR 50.01 – 60	35	30
Investor RML with LVR ≤ 50	40	30
Investor RML with LVR 50.01 – 60	40	35
Small and medium enterprise (SME) retail	100	75
SME corporate	100	85
Agriculture with LVR ≤ 30	100	50
Agriculture with LVR 30.01 – 50	100	75
Community housing providers / housing co-operatives	New standardised category with the same risk weights as investor RML. IRB accredited deposit takers would be required to use the new standardised category.	

- 3.2 By contrast, D-SIB banks using Internal Ratings Based (IRB) models report averages of 21.7% for LVR $\leq 30\%$ and 41.8% for LVR 30–50%. The proposed standardised weights therefore around double the capital that would be required under IRB for the same exposures.

Table 15: Simple and weighted average IRB risk weights used by New Zealand IRB deposit takers for agricultural lending and proposed standardised risk weights

LVR	Simple average	Weighted average	Proposed risk weight
LVR ≤ 30	23.5%	21.7%	50%
LVR > 30 to 50	42.2%	41.8%	75%
LVR > 50	92.5%	92.1%	100%

- 3.3 This mismatch creates a structural competitive imbalance. D-SIBs are able to hold materially less capital against low-risk agricultural loans, allowing them to offer sharper pricing, greater flexibility, and more capacity to grow. Non-D-SIBs such as Rabobank must carry significantly more capital even on highly secure exposures, leaving them at a built-in disadvantage.
- 3.4 The scale of that disadvantage is unique internationally. Rabobank is the second-largest agricultural lender in New Zealand and currently holds around 22% of the agricultural lending market. We have not identified any other market worldwide where a “tier-two” lender with such a significant share is forced to operate solely under standardised settings. In comparable jurisdictions, such institutions are almost always part of groups with IRB accreditation.
- 3.5 The financial effect of this imbalance is visible in performance. Rabobank’s return on equity averages 5–7%, compared with 11–13% for D-SIBs. Despite this, Federated Farmers’ Banking Surveys - which the Reserve Bank itself cited in the Capital Review - show Rabobank’s average lending rates (6.69% in May 2025) is close to the market average of 6.60%, ranking mid-pack among major agricultural lenders.

4. SPECIFIC FEEDBACK ON QUESTIONS

4.1 Do you agree that the Reserve Bank should introduce more granular standardised risk weights for mortgage, corporate, and agricultural lending?

- 4.2 Yes, particularly for agricultural lending. More granular, LVR-based risk weights improve risk sensitivity, align capital charges with actual loss-given-default (LGD) exposures, and better reflect the true risk of each loan.
- 4.3 Low-LVR agricultural loans carry comparable or even lower risk due to strong land collateral. Yet the proposed standardised rates (50% for LVR $\leq 30\%$ and 75% for 30–50%) are well above actual risk as identified by D-SIB's Internal Ratings-Based (IRB) averages are 21.7% and 41.8% respectively.
- 4.4 This misalignment creates a structural disadvantage for non-D-SIB lenders, which must hold substantially more capital than necessary. It also **distorts competition**, given the size of the market share non-DSIB banks hold in agriculture.
- 4.5 A more proportionate approach is needed. We propose reducing standardised agricultural risk weights by 20 percentage points - to 30% for LVR $\leq 30\%$ and 55% for LVR 30–50%. These levels remain conservative compared with IRB averages but are closer to the true risk profile as judged by D-SIBs through their own modelling.
- 4.6 Stress test evidence (Figure 21, page 82) and historical loss rates suggest that even lower risk weights (10–15%) could be justified for highly secured loans.
- 4.7 Aligning standardised rates closer with IRB averages, while still applying a conservative buffer, would strengthen financial stability without retaining the most punitive elements of the current proposal.

5.1 Do you have any comments on the proposed changes to standardised risk weights for mortgage, corporate and agricultural lending?

- 5.2 The proposed standardised rates are excessively conservative relative to actual risk:
- Low-LVR loans: 50% proposed vs IRB average 21.7%. Reduce to 30%.
 - Mid-LVR loans: 30–50% 75% proposed vs IRB average 41.8%. Reduce to 55%.
- 5.3 These adjustments preserve financial stability while correcting the structural disadvantage imposed on non-D-SIB lenders. Adopting an ultra-low tier for highly secured, low-LVR loans (10–15%) would ensure capital requirements are more genuinely risk sensitive.
- 5.4 This is particularly important for Rabobank, which under current settings faces capital requirements appropriate to a small, low-market-share bank - an outcome that is globally unusual. Reducing the standardised risk weights would:
- Level the playing field between D-SIBs and non-D-SIBs, who are directly competing in the same game.
 - This would add significant competitive pressure to the market, encouraging lower rates for farmers.