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Senate Economics References Committee
Department of the Senate
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Parliament House
Canberra ACT 2600 Email: economics.sen@aph.gov.au

INQUIRY INTO COMPETITION WITHIN THE AUSTRALIAN BANKING SECTOR

Introduction

The Australian Finance Conference (AFC) appreciates the opportunity to make a submission to the Inquiry. By way of background, the AFC (membership list attached) was formed in 1958 and has evolved to become a non-institutionally-based financial services association. Our membership includes participants actively involved in both the bank and non-bank sectors. AFC caters for members' association/lobbying/compliance information needs in relation to their consumer and commercial activities across Australia, including consumer credit and housing finance, equipment leasing and finance, wholesale and receivables finance, deposit-taking and other fundraising activities.

General Comments

A competitive financial market contributes to strong economic outcomes and provides real benefits for consumers. These benefits are well recognised and include:

- lower loan interest rates
- lower fees and charges
- greater contribution to the Australian economy including regional communities
- greater customer satisfaction
- stronger markets provided by diversity.

Prior to the Global Financial Crisis (GFC) the Australian economy had experienced a lengthy period of growth. In parallel with this, growth in financial aggregates and markets had been buoyant, competition had been fierce and, at the margins, financial inclusion had been expanded as a growing mainstream lending industry had been able to provide services further along the risk spectrum. Given Australia's generally lower savings levels and the impact on available retail deposit funds due to the priority given to superannuation, financial intermediaries had needed to diversify their funding sources, particularly to overseas wholesale debt and securitisation markets.

From mid-2007, the lead-in to the GFC saw these markets, initially securitisation and then wholesale, tighten significantly and by the second half of 2008 close completely. The GFC's monumental consequences internationally are well known and are still playing themselves out. In Australia, the pre-existing fiscal and monetary policy positions, prudential and other regulatory frameworks and the generally sound management of the banking and finance institutions, meant a much lesser trauma. The Government's prompt action on retail and wholesale guarantees supported confidence in ADIs and its directions to the AOFM added liquidity to RMBS markets; also its fiscal stimulus achieved the preferred GDP and employment outcomes. In addition, the quality of the lending further along the risk spectrum locally meant that there were none of the "sub-prime" issues that added further shocks overseas.

The Australian financial market was nonetheless considerably affected by the GFC. Many overseas domiciled banks ceased new lending and over time repatriated their capital and/or debt and as several of these provided funding to local financiers, there was a multiplier effect on the reduction in competitors. Similarly, overseas non-bank financiers announced withdrawal from all or part of their local operations or were without funding due to truncation of the global credit line to and hence from, the parent. M&A activity among ADIs reduced the number of large as well as smaller players, both specialist as well as diversified. For domestic financiers which raised retail deposit funds but who fell outside of the Government guarantee, the curtailed fundraising ability that followed, meant absorption into their parent, cessation of business or capacity for new business matched to loan repayments net of redemptions. Wholesale or private investment in local finance businesses virtually ceased and those competitors with business models premised on high leverage exited the market. As a consequence, the number of bank and non-bank intermediaries sufficiently "in funds" to be available to quote on new business applications or rollovers of existing lines was significantly reduced from earlier times. This was understandably compounded by prudential and commercial concentration ratios by client or by market segment. Pricing also reflected the scarcity and costs of funding.

Over the last two years funding markets have gradually improved; ADIs with and without the wholesale guarantee have topped-up with local and overseas liquidity; securitisation markets have shown modest recovery, more for RMBS than for other assets classes such as auto and equipment loans/leases; and several overseas parents' own boosted credit lines have become available locally. The quantum of funds is however subdued compared with five and more years ago and there is no sign of the re-entry of overseas, particularly US and European, players which previously underpinned directly or indirectly significant competition.

Notwithstanding the improving conditions in financial markets, there are a number of issues which are adversely impacting on the competitive ability of individual entities and the sector overall. These are detailed below.

Securitisation.

Securitisation has been a major driver of competition in local financial markets, allowing lesser-rated lenders access to new funding at a price reflective of the quality of the underlying assets in the pools. As indicated, while there has been some recovery over the past two years, it continues relatively subdued locally, with overseas markets particularly skittish.

Recognising the need to support a risk spectrum in market participants and underlying assets which does not engender "moral hazard", AFC believes that the Government should consider all mechanisms for enhancing and adding vitality to the securitisation and like markets (eg. that for covered bonds). Also, while such consideration for RMBS is important, other asset classes should not be neglected.

Government Guarantee
AFC supported the Government's guarantee of ADI deposits as it was vital to ensure confidence, stability and competition in the banking system at a very difficult time. An unfortunate result was the relative difficulty in retail funding created for non-ADIs and we believe more consideration should be given to temporary support mechanisms for the future.

In relation to the ADI sector specifically, AFC supports Government consultation with the industry to ensure that any changes to the operation of the deposit guarantee provided under the Financial Claims Scheme does not result in distortions to depositor access or perception leading to competitive disruption to future lending, including regional areas.

Also, because the expiry-date for the guarantee (12 October 2011) is less than a year away, and terms deposits will increasingly straddle that date, ADIs are keen for the Government to determine its policy so they may reassure depositors.

Legislative Issues – Impact on Competition and Efficiency
AFC has supported the Government moves for a national approach in relation to regulation in areas such as consumer credit, finance broker regulation, personal property securities, occupational health and safety laws and a national electronic conveyancing system. These reforms carried out to a workable time-frame and with due regard to evidence-based best practice regulation making principles, can reduce costs and foster competition. Absent this considered approach, regulation can be a major barrier to entry. For example, a large bank recently estimated its cost to comply with Phase 1 of the new National Consumer Credit legislation at $50 million and a former non-bank player, credited with boosting competition in the residential mortgage market from the 1990s, commented that such entry would not be practicable under the new regime.

Yours sincerely

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AFC MEMBER COMPANIES

Advantedge Financial Services
Advance Business Finance
Alleasing
American Express
Automotive Financial Services
Bank of Queensland
BMW Australia Finance
Branded Financial Services
Capital Finance Australia
Caterpillar Financial Australia
Centrepoint Alliance
Citi Australia
CNH Capital
Collection House
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Key Equipment Finance
Komatsu Corporate Finance
Leasewise Australia
Liberty Financial
Lombard Finance
Macquarie Equipment Rentals
Macquarie Leasing
Max Recovery Australia
Members Equity Bank
Mercedes-Benz Financial Services
Nissan Financial Services
Once Australia t/as My Buy
PACCAR Financial
Provident Capital
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RABO Equipment Finance
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