Australian Greens Dissenting Report

When the big banks start suggesting they might not give you a mortgage because sea-level rises will affect the value of your home, or that they'll second guess a loan to a farmer because global warming means less rain is falling in that region, it's time to sit up and pay attention.

The big four banks failed to see the Global Financial Crisis coming. Regulators were likewise blind to the looming catastrophe. The public paid a double price, first hit with job losses and wealth destruction, then left to pay the costs of government intervention to prop up the banks and to avoid the country plunging into depression.

We may be on the verge of two more massive shocks and, going by the evidence of the big four banks to this committee, it's not clear that we'll be any better prepared than going into the GFC. The first concerns housing and the second concerns climate change. While the housing outlook seems bleak, the steps being taken by 3 of the big 4 on the climate front give cause for hope, though Westpac unfortunately remains stubbornly of the view that new coal mines like the Adani Carmichael venture might be worth financing.

The housing crisis: the banks join the war on the young

Australia has a problem with housing. A very big problem. The price of a house is, depending on where you live, likely to be high, very high or ridiculous. We have the dubious honour of spending the highest proportion of income on housing in the world. The proportion of people who own their own home, particularly amongst the young, is in decline and is now at the lowest level in 60 years. Inequality is being created on a generational scale, the economy is being distorted, and the financial system is being loaded up with risk.

We have household debt over 120 per cent of GDP. In the US, it did not even reach 100 per cent before they got into trouble pre-GFC. We have household liabilities now getting up to almost twice the level of disposable income.

It has always been the case that the young and the poor are the less likely to own their own home.[1] But the widening gap in home ownership between the old and the young, and the rich and the poor is an enormously concerning trend. We are witnessing the creation of a structural divide in our society.

It's very easy to understand why home ownership is in decline. Housing in many parts of Australia is overpriced. Australians are paying world record amounts to

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[1] HILDA statistical reports also show a marked difference between income equality, with a Gini coefficient of 0.30; and wealth equality—of which housing is the biggest single component—has a Gini coefficient of 0.63.

buy a house. As a result, people either can't afford to buy a house or, if they decide they can, they are being saddled with world record levels of debt. And it's the youngest who are hit hardest. In 1990 house prices were approximately six times the income of a young Australian. By 2013 that had doubled to a multiple of twelve.

Australia's housing market is being driven by a tax system that favours investors above owner-occupiers. The nexus between negative gearing and a concessional capital gains tax has created an uneven playing field that gives property speculators an unfair advantage over prospective home owners. On any given Saturday, young home seekers are being priced up or priced out because they don't have the taxpayers shoulder's to stand on. Tax concessions for investors have supercharged the housing market by increasing the number of prospective buyers. This is what is behind the decline in home ownership rates. This is what is behind the record levels of household debt. This is the problem that needs to be fixed first and foremost.

But it is also becoming clear through this inquiry that housing is becoming more and more important to the banks' bottom line. The higher the price of the house, the bigger the mortgage and the more profits banks make. Even better for the bank when the same investors who bid prices up and up and up can then be given an investor loan by the bank, because the bank knows the investor has the promise of tax break from the government in their back pocket. By pricing young people out of the market, the system helps big banks make even more money.

While many voices join the fray to argue that housing is overpriced and government must act, the big banks stand almost alone in backing the Liberal government and pretending there is no problem.

When asked directly whether the bank thought housing was overpriced, the CEO of NAB, Mr Thorburn replied that he still believed 'the answer is no' (p27 Hansard). And you could hear jaws dropping around the country when the head of Commonwealth Bank offered this astounding observation:

> "Mr BANDT: There are a lot of people, especially young people, who think that houses in Sydney and Melbourne are overpriced. Do you share that view?
>
> Mr Narev: I am not sure they are saying they are overpriced. I think they are saying it is difficult to afford it, and we share that view. …" (p31)

The median house price in Melbourne is now over $843,000, while in Sydney it is an eye-watering $1.15m.[2] If the people running our biggest banks think houses aren't overpriced, then they've joined the war against young people.

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[2] https://www.domain.com.au/news/melbournes-median-house-price-soars-to-843674-in-march-quarter-domain-group-20170419-gvn64k/, including this observation: "The median is more than

There is an unstated 'big four' policy in Australia, which means that the government treats each of ANZ, Commonwealth, Westpac & NAB as 'too big to fail', implicitly promising to bail them out if times get tough. And as we saw during the GFC, when this government support crystallises, it helps the big banks increase their market share and maintain their oligopoly. But when the big four banks' business model involves profiting off the misery of young people by defending ridiculously high house prices, they have torn up their social licence.

Some commentators predict the housing bubble will burst rather than deflate, with significant potential consequences for the economy. If this happens, government would do well to remind any big bank coming cap-in-hand seeking assistance that they steadfastly denied there was a problem while quietly boosting their bottom line.

What does '2 degrees' mean for our banks?

In the 'Paris agreement' climate treaty, Australia joined many other countries in pledging to limit global warming to less than two degrees above pre-industrial levels. The treaty has been ratified in Australian domestic law. 'Two degrees' is a target that each of the big four banks has endorsed.

The world is now working out just what it will take to meet this target. As part of the treaty, governments have agreed to submit further pledges to cut pollution. Banks and the finance sector are now on notice that there will be significant economic shifts and that while current government policies may not be enough to meet the 2 degree target, one can 'work backwards' from the target to understand the series of massive changes required in the Australian economy over the next few years.

The big bank's regulator, APRA, has sounded the alarm bell. On 17 February 2017, one of the three members of APRA's Executive Group, Geoff Summerhayes, delivered a critical speech, stating (emphasis added):

> "while climate risks have been broadly recognised, they have often been seen as a future problem or a non-financial problem. The key point I want to make today, and that APRA wants to be explicit about, is that this is no longer the case. Some climate risks are distinctly 'financial' in nature. Many of these risks are foreseeable, material and actionable now. Climate risks also have potential

$110,000 higher than this time last year, and has more than doubled in a decade; in 2007, it was $386,411."; https://www.domain.com.au/news/sydney-median-house-price-hits-115-million-buying-becoming-out-of-the-question-20170419-gvmnp8/

system-wide implications that APRA and other regulators here and abroad are paying much closer attention to. …

we now have a much more sophisticated, granular, quantifiable understanding of the impacts, risks and probability distributions around climate change. This is true on the planetary scale. For example, it is estimated that in order to have a two-in-three chance of keeping global warming below 2 degrees, we need to restrict future global emissions to around 800 gigatons of CO2.[2] (That's equivalent to around 25 years or so of current annual global emissions). …

The [Paris] agreement establishes a binding global commitment to limit warming to between 1.5 and two degrees Celsius, and provides a pathway for more ambitious emissions reductions efforts if current policies are falling short of that goal. The host of new policies and commitments is significant. **Even more significant is the framework the agreement provides for monitoring and ratcheting up these commitments and contributions over time.**

The agreement provides an unmistakable signal about the future direction of policy and the adjustments that companies, markets and economies will need to make. This global agreement is being complimented by initiatives at national, state and city level. …

The general point is that the transition now in train could potentially lead to significant repricing of carbon-intensive resources and activities and reallocation of capital. This process will be highly sensitive to changes in regulation, technology, the physical environment and behaviour by investors and institutions – and interrelated perceptions and sentiment about all of the above. Inevitably, even under a sanguine view of how smoothly this transition happens, there will be systemic impacts and implications that have to be carefully monitored. …

There are two related, broader points I want to make here. First, while physical risks are obviously a very serious matter, it is transition risks that are likely to be especially important for financial entities. The developments I have spoken about today are bringing these transition risks forward. **The Paris Agreement provides a very reliable signal that policy and regulatory efforts will intensify.** …

Second, the transition risks that stem from existing and anticipated policy and regulatory changes may not be averted or minimised **even if these policy changes are delayed or do not eventuate in**

> **some jurisdictions. It may be that the latter scenario could make risks greater and more abrupt.** This is because there could be either sharper, more significant policy changes and market adjustments down the track, or the physical impacts of climate change could become more severe, more likely and more unpredictable.

One would expect the CEOs of the big four banks to be paying close attention to utterances from the senior members of their own regulator, but there was a mixed level of understanding and awareness of APRA's intervention.

The Commonwealth Bank CEO had read summaries of the speech and agreed conceptually that there is now only a finite amount of fossil fuel that can be burnt, but declined to nominate how big the remaining 'carbon budget' is nor whether any new fossil fuel projects have been refused finance because of the bank's commitment to 2 degrees.

The NAB CEO had read part of APRA's speech and said that it may cause the bank to review its policies during the year, including the bank's exposure to fossil fuels and potentially to 'stranded assets'.

The CEO of ANZ didn't disagree with APRA's 'carbon budget' assessment and perhaps went further than any of the other banks in displaying an understanding of what it might mean for the bank's balance sheet, noting also:

- the bank was seeking to understand the impact of changing weather patterns, rainfall and drought, so as to better inform lending practices. This included meeting with the Australian Bureau of Meteorology to better 'understand how climate change is affecting the suitability of farming land for crops or livestock that have traditionally been raised in any given location' (ANZ29QW); and
- mortgage lending might be affected by rising sea-levels because 'as a bank lender, that is probably where we have the greatest risk' (p66). This might affect LVR but also whether to grant a mortgage at all.

Either at the public hearings or in written answers provided later, each of the above three banks advised the Committee that they were reviewing their policies in light of the '2 degree' target. This approach is welcomed. The mathematics of '2 degrees' will keep asserting itself ever more strongly, with its demand that 80% of known fossil fuel reserves stay in the ground. This will drive massive economic change, creating both stranded assets and new wealth. Perhaps the strongest point made by APRA is that banks need to look past any immediate government policy on climate change and see the new legally-enshrined '2 degree' target as the destination we'll arrive at in only a couple of decades.

Unfortunately, Westpac is taking a different tack. Like the other banks, the CEO of Westpac was familiar with the APRA speech, agreed conceptually with APRA's 'carbon budget' and told the committee that sea-level rise and other climate impacts formed part of the bank's current approach to risk. Indeed, Westpac said that it was currently reviewing its loan book to see whether the '2 degree' limit meant that the bank was exposed to potentially stranded assets. Westpac was also in the middle of updating its policies in light of the '2 degree' target.

However, Westpac insisted on leaving the door open to financing new fossil fuel projects, including as soon as this year. Westpac also clearly wanted to have its cake and eat it too, accepting in principle that at some point it may be bank policy to not lend to expand coalmines but rubbishing a suggestion that it might happen this year, saying only that the transition would be supported 'over time' (p30). This raises the question as to whether the 'review' being currently undertaken is serious, given that the CEO has already ruled out having a policy this year against further exposing the bank by lending to new fossil fuel projects, notwithstanding what the '2 degree' target might require.

In particular, unlike the other banks, Westpac seemed particularly keen to signal it may support the Adani coal mine if approached. Whereas most other banks were willing to signal a reluctance to take on new coal projects like this mega-mine, Westpac headed in the other direction.

As the 'Stop Adani Alliance' makes clear (stopadani.com):

> Adani's mine won't just be the biggest coal mine in Australia, it will be the biggest new coal mine in the world, more than five times the area of Sydney Harbour.
>
> When we need to urgently reduce carbon pollution, this mine takes us in the completely wrong direction.
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> The Great Barrier Reef has already experienced devastating coral bleaching from rising sea temperatures as a result of global warming. If current climate trends continue, scientists estimate that in less than twenty years, coral on the Great Barrier Reef will experience serious bleaching every second year. The Great Barrier Reef, now teeming with life, will become a graveyard in decades. Burning the coal from Adani's mine will help lock-in this tragic fate for one of the world's natural wonders.
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> Climate change will also be accelerated by the land clearing required to build the mine. In total, 20,200 hectares of land, equivalent to over 28,000 soccer fields or 200,000 quarter-acre blocks, would be cleared. Over half of the land that would be cleared is mature woodland and bushland - important habitat for many animals including threatened species such as koalas and echidnas and endangered birds.

Burning 2.3 billion tonnes of coal is something we simply cannot afford to do if we are to remain within a carbon budget consistent with 2 degrees.

The penny doesn't seem to have fully dropped when banks like Westpac still think they can commit to a 2 degree target but leave the door open to expanding coal mines. The days of dealing with climate change simply by putting a polar bear in your ad are long gone.

The Greens hope that when Westpac next appears before the Committee, it is in a position to advise that its new climate policy is consistent with the '2 degrees' policy published on its website and that it will not aid in the extraction and burning of untapped fossil fuel reserves, including the Adani Carmichael mine.

Recommendations

The Greens repeat our recommendations from the first report, including that there be a Royal Commission into the big banks. None of the evidence to date persuades us that there has been any substantial shift in big bank culture. We also repeat our recommendations from the committee's inquiry into home ownership, because the system is clearly broken and the big four banks have an interest in maintaining the status quo. We also have further recommendations arising out of this second round of hearings:

Recommendation 1: That banks expressly endorse APRA's sentiment that to meet the banks' stated goal of '2 degrees', it will be necessary to keep the overwhelming majority of fossil fuel reserves in the ground.

Recommendation 2: Noting that there is currently a dissonance between banks' publicly stated climate policies (which accept the 2 degree target) and some of their lending practices for new or expanding projects (which would likely directly contribute to exceeding the 2 degree target), if the banks refuse to rule out providing finance for new or expanding fossil fuel projects, APRA should be empowered to impose lending requirements on banks consistent with a '2 degree' carbon budget. APRA's power should be broad and should include the power to limit or stop a bank's exposure to fossil fuel projects.

Recommendation 3: APRA conduct a 'climate stress test' of each of the big four banks, assessing each bank's preparedness to deal with transition risks, liability risks and physical risks associated with climate change and meeting the Paris Agreement '2 degrees' target.

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