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*Inquiry into Reserve Bank Amendment (Australian Reconstruction and
Development Board) Bill 2013*

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Submission in support ARDB

This submission supports the introduction of the bill establishing the Australian Reconstruction and Development Board.

Many individuals and industries are in need of relief. A cursory look in to the empirical data supports the need for and appropriateness of this initiative. This will be the first step to stabilise; the next must be explored through the white paper process. I recommend the adoption of *Reserve Bank Amendment (Australian Reconstruction and Development Board) Bill 2013*

Introduction and Background

In 2010 an extraordinary flooding event occurred in Southern Queensland. It had tragic effects for many primary producers and the wider community, and was symptomatic of a particular seasonal condition, in Eastern Australia where long dry periods are followed by very wet periods. This was a one in 50 year event, though some assert a one in 100.

Many in my community were damaged financially and psychologically dreadfully, as we were, so too was our dear old bankers who took the hit with us.

On its own this information is insignificant, to lose the odd producer is not statistically relevant, but as I began talking, in my own community and then wider, throughout the states I discovered that mine and my communities' situation were replicated over and over around our nation.

Analysis requested from economist Ben Rees set the backdrop for the nationwide catastrophe, the debt/ net income graph should be embedded in all our minds.

In October of 2011 there was a meeting of bankers, farmers, economists, agri representatives, ABARE and treasury, called together by the then Treasurer Wayne Swan MP, and the Minister for agriculture Senator Joe Ludwig and Bob Katter MP in Brisbane. The meeting was told that particular problems in the northern cattle industry were of an extraordinary magnitude and that in fact perhaps more than 30% of station owners of the North were then in default with their lenders. In Western Australia in some districts every property was for sale with farmers unable

to see any hope at all after a series of poor years, and amongst the dairy industry, significant shake outs were under way in all states. In Victoria some 10,000 dairy cows (this has escalated since October 2012) had been taken into the control of the bankers, and this was not quarantined to Victoria, each state had massive dairy industry failure occurring.

Of importance for the economics committee is to recognise that each industry can be similarly described as in crisis, yet each has quite different causes, but in common are the weak profit situations, high levels of borrowings and falling capital values. This circumstance has set each industry up to fail at the first major hiccup.

Having recognised the shape of the crisis it is simple to decide on a path forward, assuming first that it is accepted that “something” must be done. If on the other hand a philosophical resistance to “acting to fix the problem” is to characterise the work of this committee then no amount of logic or argument will do.

At the meeting at QUT in Brisbane following the treasurer’s roundtable, a working group was formed. The Rural Finance Roundtable Working Group decided on a path forward;

1. first to obtain emergency relief for producers who needed funding to fund the next crop or to feed starving dairy cows or beef cattle effected by drought in the north,
2. then to set about a debt reconstruction plan to remove the pressure from bankers and farmers who were endeavouring to manage out of order loans,
3. then to move on to remedy the poor financial performance of primary producers, stabilising incomes and returning confidence and renewal to the communities of country Australia, making profit the main driver of policy...at least till profit returned.

The Commonwealth government of the time, a Labor administration were accepting of the need for some relief, to that effect they offered a package of some \$420,000,000.00 over two years, to be delivered via the states in equal proportion. Discussions with our group had indicated this to be inadequate, but with a federal Budget in deficit and a determination to attempt surplus, both from government and also from the opposition, any offers of assistance were not to be rejected. The political chaos which followed is a historical record, but more generally seemed to

those of us observing to be a battle of states resistance and Commonwealth lack of communication; I doubt a single member of our working group would have recognised what was game and what was reality.

One of the hot spots of the time was the wheat-belt of WA. It is possible to find bank customers who, if able to plant into the wheat year 2013/14 would have survived to farm another day, yet at this very moment and finally, as a result of minimal income due to lack of funding for the crop are being "adjusted". This is a sad triumph for politics and economic philosophy over pragmatic reasoning, matching capital cost with need and plain common sense and decency.

It is to be hoped that this new initiative will not attract games which in the end just make it more difficult to deliver in the face of desperate need.

Need for Agricultural Reconstruction

Financial reconstruction is needed to stabilise rural Australia. Without prompt attention a fully blown shake out will occur (underway now) and those with huge knowledge of local climate, soil and contemporary production systems will be lost for ever. Families who have weathered all that the toughest climate can throw at them, production difficulties, seasonal wildcards, who are best skilled to operate the land will be gone.

The shakeout will be of such magnitude that will effect dramatically both rural communities and rural business and will have damaging effects wider, including no less than the banks themselves, who are as responsible for the lending as the borrowers are for borrowing.

The reconstruction is needed not only for the farm businesses and families who are under pressure, but also for the feed in businesses who today are under significant pressure as well, as they endeavour to take up the shortfall of funding from the retreating banks. This includes those many small businesses in rural towns who are in fact part of the fabric of our community.

The phenomenon of suicide haunts our communities; this is often the end game of economic failure. We hear with disturbing regularity that one or more of these events have occurred in this district or that. The national Rural Health Alliance

(may 2009) suggested men in regional and remote Australia are “1.3 to 2.6 times more likely to end their lives by suicide than urban counterparts”. They went on to list the first two factors relevant as financial insecurity and stress caused by drought, flood and bushfires.

That the authorities publicly spin the need for councillors to resolve this problem is a terrible insult, when much of this is a result of failed industry policy leading to empirically demonstrated low profits and finally overbearing debts and a feeling of complete abandonment. We can do better; we must do better in 2014.

There may deeper theoretical phenomena at work, like the theoretical reality of Engle’s law, or the apparent pervasive effect of inverse scales of production. A full exploration of these and other issues may well offer up sound directional information.

Political disconnect, testing assertion against results

There has grown a ‘disconnect’ from farmers and their politicians and in some cases between farmers and their agri –politicians. All too often the official line is that everything is rosy, yet a conversation with a connected accountant will confirm this is not the case, yet on and on in the media we hear how good it is, even after 2011, when grain prices tumbled to way below the cost of production, reports in various papers that “grain farmers have never had it so good!” At the time I wrote a letter to the Queensland paper protesting, that the ten pages of farm sales including mortgagee in possession farms was in stark conflict to the published material asserting “as good as it gets, “you cannot have it both ways” I said, “it is either as good as it gets or it is pretty shitty.” The latter was and is the truth and is still today.

Nothing signals this disconnect from the agri- political representatives more than the then president of the National Farmers Federation telling our group in Canberra (2012) that “ the banks have told us that they own more of the farm than farmers” At the time several of our group offered expletives, it does not take a mathematician to conclude this was of the most serious nature we had heard, that to have the knowledge that this circumstance existed and then do nothing is among the very reasons the NFF has been so comprehensively abandoned by its farmer membership.

“So what have you done about it I said”, The response I received left me speechless,
“We thought some more R and D would help!”

What is needed in the bush is recognition that the helter skelter race away from required intervention is destroying industries and communities and wrecking people’s lives. Doing nothing, the refrain of the free market brigade, cannot solve problems.

Engle’s law with its pervasive effect of declining profits and all the other exceptional climatic and price phenomena Australian farmers deal with are way beyond a declining profit to cope with.

You would think it would not be too hard.

The truth is that as the proportion of income spent on food and fibre declines, so there is a shift of resources from the producer to the consumer, it is not difficult to comprehend farmers have long been subsidising the food and fibre needs of the wider community while farmers try to make ends meet on diminishing returns. It has resulted in severe social dislocation and properly belongs in the hands of those who have prescribed this policy mix.

Of course many have contemplated why it is that the obvious disconnect exists. The difficulty with running a representative organization while numbers are constantly diminishing is well recognised, it is neither a new phenomenon nor one with easy answers. What seems to have occurred though is that many rural organizations, with only few exceptions have sought external assistance, often from the very businesses farmers find utilise dominant market power to extort excessive and sometimes unconscionable margins at, the expense of that very farmer.

It would seem very poor planning or foresight to accept the funds with the knowledge your representation of your membership will be tarnished.

In the early nineties as a young branch president of the local branch of the then QGGA, while engaged in a circumstance with a local bank and one of our members, I well remember the conversation with the then president “to pull the dogs off as this bank is a sponsor and you will hurt our income”; Our branch was not of that mind.

The point is that representation is corrupted by financial relationships that extend to funding the working life of the organization.

Organizations need to be clear in their minds just who they represent. A new administration has the opportunity to once again hear and reflect the needs of our industries and communities, those family operators who make up the producers of country Australia.

It extends much further though, to testing the outcomes of policy changes, the industry organizations embarked with government on a push to remove all forms of intervention from agricultural production, it was a clear change in direction, now some decades old from its inception, the worse of it began with the introduction of the reforms as a result of the Hilmer review into competition policy.

Some among us have seen the proposed changes from a historic perspective, from a backdrop of the new direction being driven by philosophical beliefs. Surely the various organizations who have advocated these changes, would be concerned that the new direction, dare I even say a “*New Horizon*” and would want to test the asserted benefits against results, to ground truth the outcomes. The graphical presentation of the outcome should indicate a rise in profits. The empirical data should support the assertion that the outcome would be better. Of course the debate has to date been won by that particular philosophical set, yet the rural communities wait in despair for advocated outcomes to eventuate.

If it were an old problem at last behind us we could take some comfort that the future may improve, still the advocates of unfettered free markets including the arrangement inappropriately named *free trade agreements*, which are in *fact bi-lateral arrangements*, with such nations as the U.S. have failed miserably to deliver the pot of gold. Yet almost daily we hear of more arrangements being entered into willy-nilly.

Has anyone taken a look and reported the variation in outcome from the spin of politics to the financial performance at the farm, of course usually the advocates of this direction will offer the refrain when failure is demonstrated, “we have not gone far enough” I expect that to still be the case.

Appropriate Funding Source

As it goes, funds are needed to rebalance the financial circumstance of many farmers and related industries. Producers who have as a result of a change in government opinion, and policy, had all risk amelioration removed from their industries, dairy, grain and every industry which has lost its protection, whether countervailing market power, import protection via tariffs, or simply drought and exceptional circumstance provisions. Government have effectively passed all the risks of production on to the producer, this has been both deliberate and profound. Unfortunately many have carried excess debt, in the circumstance, provided and based upon a system, which now simply does not exist. It may well be there is an argument for compensation to readjust debt levels more in line with risk now set by policy.

This systematic removal of these protections, in the face of a basic knowledge of the effects of 'Engle's Law', *that as economies mature, consumers pay a lesser and lesser proportion of their incomes on their food and fibre needs*, would on the face of it seem quite the opposite of what is needed to maintain some semblance of reasonable income distribution throughout our nation.

On the basis of equity surely an inexpensive and easily achievable intervention in the form of the ARDB is justified.

- There are further needs, which the ARDB could provide, to wind back substantive costs caused by inappropriate funding sources, expensive and impatient.
- Further to fund a new generation who are right now choosing to walk away from farming altogether.
- And, as a generation of youngsters choose to withdraw, so too do a generation find it difficult to exit, thus in some cases there will be a need for some level of consolidation.
- In some particular districts there may be deemed a need for a high level of reconstruction, in particular the eastern wheat belt of WA may well be suffering the effects of shifting rain patterns making grain production less achievable and a need to restructure back to the next most profitable production system, perhaps stock, in particular maybe sheep. The required

infrastructure for stock is dilapidated and in need of renewal. Precedence of course in the successful adjustment in the Charleville districts some two decades ago.

- Further industry development is needed, replacement of infrastructure and new industry in keeping with the nations desire to advance into efficient and modern freight corridors and even into renewable fuels in line with the ever diminishing carbon based systems.

RM Williams (visionary)

I visited RM Williams at his home just outside Toowoomba with Hon Bob Katter MP, some years before his death; it was one of the most important exchanges in my early opinion formation. RM walked to the table and handed Mr Katter a wad of paper and said “these pages hold the changes you will need to make to the Reserve Bank act, to make it work for all Australians.” In essence, what the dear old gentleman was suggesting was a development bank providing the opportunities to, like so many other countries, provide the necessary finance provided by our own central bank, to retain control over our nation and our destiny and grow our nation with our needs.

It seems ludicrous perhaps worse, to suggest we borrow money created by the governments of overseas nations, to borrow money from the printing presses of overseas nations to fund domestic needs.

The source of credit via the ARDB is anticipated to be, depending of the state of the domestic economy, either from within the central bank itself, from within the domestic economy or in the event it was deemed most suitable, from elsewhere.

Our returned serviceman must find sleep hard to find as they contemplate the behaviour of governments of the last several decades, we risk becoming peasants in our own nation, slaves to the printing presses of more enlightened nations whose planning horizons are described in centuries and half centuries and understand well how short sighted self-interest can lead us to a place where they can exploit us.

Empirical data demonstrates that as foreign ownership climbs in our economy, so does the drain on the economy as a result of the flow of both dividends and interest

repatriations overseas. This exceptionally short-sighted philosophy, to sell our nations interests to all and sundry is coming home to bite us, it is responsible for the interest rate held higher than competitor countries, this is to a large degree responsible for the resultant high value currency and the corollary of manufacturing and agricultural decline and in some places complete collapse. It will follow that unemployment will climb, that the budget deficit will be damaged by the need to sustain higher numbers of unemployed and that the balance of payments will further be eroded by importation of what were once domestic manufactures.

ABA Reminds us of EC Benefits.

In 2013 together with Dr McGovern we visited the Australian Bankers Association (ABA).

The conversation was direct and it became apparent one of the fears of the bankers association was the possibility of competition in their market by a new publicly owned entry. We indicated that was not the intended role of the ARDB, we would go places they could not was our response, and that is the intention of those who in the beginning advocated for the formation of the ARDB.

However well may they harbour these fears, the returns posted by the big banks as reported on the ABC (below) are at odds with a theoretical competitive market, much more like an oligopoly with little real competition. Logic asks the question about effective countervailing machinery in the public interest.

Return on Equity

CBA 19%	Barclays 7%
WBC 15%	STD Chartered 11%
ANZ 16%	Goldman Sachs 9%
NAB 12%	JP Morgan 11%
	HSBC 6%

Source; ABC News 'the business'

However, of great interest to the roundtable working group was the report that the bankers had indicated by way of submission to the Commonwealth that if the Exceptional Circumstance (EC) provisions were removed from agricultural policy that many people would certainly get hurt, their contention is and was correct and I have great sympathy for them as they are ultimately the business who will bear the brunt of this final risk amelioration removal from agricultural producers.

However, it should be made clear to this committee that the bankers and their receivers and liquidators have at times behaved in an unconscionable way, both lending into farm business which were clearly not going to be able repay the loans, trading loan books at discounted values, then recouping the money and destroying a family's life in the process. Previous enquiry has documented some of this behaviour, which all too often leads to people taking actions which lead to losses of life itself, which once more explains the reality that multi-generational farm business is often the hardest to adjust while retaining human dignity, which is of course another good reason to effect the ARDB.

Reports recently garnered from our community suggest some are now faced with no income, the banks are in retreat and unprepared to further lend, some people are said to be unable to feed themselves. As an Australian I am embarrassed to have come to this place. I imagine the bankers would feel no particular comfort; the solutions rightly belong in the public domain.

Appropriate Development Funding

For a young Nation with the particular infrastructure and development needs of Australia, a large landmass with long distances between cities, growing rapidly, much opportunity will be lost if we fail ourselves by neglecting both our infrastructure and development needs.

Further, that it is possible for us to utilise our own capital rather than the capital of the treasuries of other nations would seem more than just common sense. Less than the full utilisation of our own capacity would seem unconscionable and both

misrepresent our own ability to deal with our future and in a very serious way, less than is expected by those we elect to govern on our behalf.

Patient capital, used by our nation and others, is eminently suited to the very low returns available from certain capital investments including infrastructure and agriculture.

So how will it look.

Administration

When in Sydney, Dr McGovern and myself met with Reserve bank staff, they were of course completely non-committal about our proposals, but we were able to observe plenty of room to house the ARDB. We jested the proposition, well Mark and I were not really jesting.

The Act we are requesting support for, sets out the shape of the board and fit into the financial machinery of our nation.

There are choices of course about the rules and systems which will be needed to operate, in the first instance the reconstruction role of the ARDB.

In setting out the possible shape of the Rural Reconstruction leg of the ARDB I recognise many of these choices, yet with minimal difficulty successful models of the past and currently operating are available, in Queensland the Queensland Rural Adjustment Authority (QRAA) has an exemplary reputation for effective delivery of commonwealth and state funding, the QIDC and the Commonwealth bank have been successful models. The Rural and Industries Bank of Western Australia was a tremendous success.

The problem of course as demonstrated with the recent Farm Finance Package is that some states do not have effective machinery for delivery; many have lost the ability or simply refuse to participate. This situation leaves little choice then, for a Federal government wishing to provide effective and equitable policy delivery across all states but to set a central administration, I suggest minimal rent as we could take available space in the reserve bank building in Sydney.

The board will need to utilise an experienced administrator to initiate the machinery, firstly in Sydney and as need arises in subsequent states, branch offices which have sufficient staff, sufficient to undertake the needs of particular states.

The establishment should be staged with a functional head office in Sydney first established, provided the Treasurer is comfortable further extension to the states from there.

A Customer View

There are many customer styles, from customers who are now a problem for their bankers, becoming a problem or soon to become a problem.

The Board would receive applications from potential customers for acceptance into the facilities of the reconstruction board, by way of an application form signed off by the financial advisor, accountant or banker of the customer. It will be necessary to fit the guidelines set by the board to be accepted as a client.

If the customer is in default with its funder a conversation will be had between the banker or his representative and the ARDB as to a buyout of the mortgage, a discount may apply in the event there is no expectation of full recoupment of the outstanding funds. However it should be clear that the likely settlement would be greater than achievable through the regular sell down process. The result that the bank will have its capital loss minimised, while the customer will be far more able to repay the new mortgage at appropriately priced money, commensurate with anticipated and historically received profits.

Of upmost importance is the agreement on a viable or sustainable level of debt, the ARDB will not under any circumstances accept a level of debt which may make a customer unviable or unsustainable.

Most customers need just a breathing space, a year or two at concessional interest rates to get on their feet, a 'hand up' for a short time, this is provided by way of the lower cost of funding, with an agreed period of capital pay down, to be once again free to go back to the commercial banking industry.

In many ways this is not at all unlike the Commonwealth Development Bank with a measure of rural reconstruction.

A banker's view

It is unclear how large the actual level of debt which is impaired or at risk. Some have estimated from three to five billion, yet the National Farmers asserted in Canberra to members of our working group that bankers themselves apparently suggested that the level may be much higher, as they said; the bankers felt that the bankers themselves owned more of our farms than farmers. On the surface this is greater than 50% leaving a debt ratio of greater than 50% of the 66 Billion.

Some have made the suggestion that the trouble is with the larger operators who constitute the 20% that produces the 80%. This would be a much larger number and signal huge/ unprecedented dislocation if bankers set about resetting their books. Common sense would suggest that the level of debt reflective in the gross number is more likely owed by larger borrowers and without doubt work needs to be done by APRA to appropriately report. If the 20% that produce the 80% are about to fall over or half of them even, then the nation's food producing capacity will be at huge risk.

Full and accurate numbers seem very hard to acquire, reports by the banks that it is all ok flies in the face of ground truthed information. It is one of the shortcomings of the current information that clarity is not available. Whether the bankers are compelled to provide full reporting to the APRA is unclear, but for certain whatever data is available does not offer the requisite information for clarity around quantum.

However, assuming the lesser number, bankers are now left with a circumstance where very few properties are able to achieve reasonable values, more generally a dearth of confidence and lack of profitability set a scene for severe pain and in many cases high losses.

The operation of the ARDB will remove the severe pain, the write-downs will be less than otherwise and a modicum of confidence will begin to establish itself in the various areas most disrupted, dignity will return to the adjustment process, losses limited, viability and sustainability enhanced.

Of note to members of this committee should be an understanding that the banking have received various , rather large sums at critical times to stabilise dangerous situations, like for instance the Commonwealth intrusion into the short term housing market to the tune of tens of billions, the public have at times saved the bacon of the

banks, rumours that the banks care not one squat for clients who have gotten into difficulty are hopefully just a few unthinking bankers who have not thought through the effects of their form of adjustment to the end game. This has not been my experience, though it has been for others.

Given a 'worse scenario' of several billion dollars of write down, there is little doubt that both the profitability and confidence which underpins capital values of the banks themselves will be in jeopardy, executives at very high levels will need to think very carefully if they choose this path, and this says nothing of the flow on effect through the economy, the damage to community and to fabric of our nation if the Paul Howe's model is to be followed will be dramatic, painful, historic and with little doubt destabilising politically, the presentation to the world of Australia's own subprime problem, the Fannie -Mae of the bush does not bear contemplation. Far better to act early to remove the problem with appropriate financial machinery.

The Losers

Mostly the losers will be margin takers in human misery.

There will be some industries and individuals who are worse off as a result of the enactment of the ARDB. The industries which make a living from selling stressed rural properties, which make a living from liquidating the work of generations of rural families, will have a diminished workload.

The Rural financial councillors likely will find a place still facilitating reconstruction for a time, and then many will find diminished opportunity in the RFCS. Their counselling needs will diminish.

Those who pedal Australian Rural properties to foreign speculators will certainly find that in the main Australians will be the purchasers of our land, and overseas investment speculators will see far less opportunity to simply speculate on the misery of our farmers. They may well still wish to participate in building farm business, this however will be a net positive as it likely will be around relationship extension, bringing new management techniques or perhaps entrenching marketing relationship's as the world evolves

The public good is well served with the confidence that will result from the stabilisation inherent in the ARDB Bill.

On behalf of rural communities and individuals over the entirety of our great nation I ask this committee to assist where ever it can to see this bill is enacted and the Australian Reconstruction and Development Board accepted by the Cabinet and the Parliament of Australia.

Rowell Walton