

Submission to the Senate Standing Committee of Economics regarding the Pacific Banking Guarantee Bill 2025

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Introduction

The Development Policy Centre is a think tank based at the Crawford School of Public Policy at The Australian National University. We undertake independent research and promote practical initiatives to improve the effectiveness of Australian aid, to support the development of Papua New Guinea (PNG) and the Pacific island region, and to contribute to better global development policy. I am the Director of Development Policy Centre and a Professor of Economics.

Thank you for inviting me to make a submission regarding the Pacific Banking Guarantee Bill 2025. I apologise for missing your deadline. I misread your letter and understood the deadline to be 21 August. I am sending my submission in any case in the spirit of better late than never.

I understand that this bill has bipartisan support and will be passed as is. Nevertheless, I wish to raise some issues to promote transparency and good analysis, both of which have been sorely missing so far.

My submission has five sections. After this introduction, I discuss the nature of the guarantee, the need for transparency, the impact on competition, and the issue of correspondent banking relationships. There is only one recommendation, in the section on transparency. This is:

The Bill should have transparency requirements written into it, similar to those associated with community service obligations. These would stipulate at a minimum that the terms and conditions of any guarantee made under this Bill would be made public, and that the recipient of the guarantee would be required to report on its compliance with the obligations it has entered into.

PNG is often used below as an example. This is because it is the Pacific country I am most familiar with. However, most of the points made apply to the Pacific in general.

Nature of the guarantee

The first question to be asked about this bill is: What is being guaranteed? This is nowhere stated. The only constraints in the bill are that the bank receiving the guarantee must be Australian, that the guarantee must relate to the bank's banking business in the Pacific (including Timor-Leste), and that the guarantee must be consistent with the 2013 Public Governance, Performance and Accountability Act.

The Explanatory Memorandum appears to be quite misleading on this point. It says that "Any guarantees made will cover low risk exposures of the guaranteed ADI [Australian bank]" (1.4).

However, there is nothing in the legislation to require this. I think that what the Explanatory Memorandum is referring to is not the legislation but the deal with the ANZ. What does this surprising reference to “low risk exposures” point to? Why would a guarantee for something that is already low risk be valuable?

An additional clue is provided by the transcript of the Committee’s hearing on August 12 with a statement from officials that “The purpose of the guarantee ... is to release regulatory capital in Australia.”¹ This again sounds paradoxical as guaranteeing a low-risk asset should not release much regulatory capital. But we can perhaps solve the puzzle this way. In any country, loans to the government are the lowest-risk assets any bank can have *within that country*. But such loans and deposits can still be high risk from an Australian regulatory perspective. In fact, APRA prudential standards require that sovereign exposures to a government with a credit rating of PNG and other Pacific countries have a risk weighting of 100% when measuring the regulatory capital they are required to hold.² But if the Australian government guarantees ANZ’s holding of PNG bonds, the risk weighting goes to zero. In other words, this guarantee will exclude from its regulatory capital requirements the entire value of the sovereign loans ANZ has made in the Pacific.

What this means is that the guarantee is giving an immediate subsidy to the ANZ. This is because any reduction in the regulatory capital requirement (such as the one this guarantee brings about) enhances the profitability of the bank impacted, since it will, for example, be able to borrow more to lend more.

This is important to emphasise because, by the way the bill is written and talked about, it would be thought that the guarantee being provided is simply a type of insurance, payable only in times of catastrophe. For example, the ANZ in its press release about the deal with the government writes that “the Australian Government assesses the probability of the guarantee being called as very low.”³ That is true. If the PNG government defaults on its bond repayments, the Australian government will have to step in, and make those bond repayments to ANZ. And this is extremely unlikely. The PNG government has never defaulted on its bonds and is highly unlikely to in the future.

But this is not the whole story. What is more relevant and attractive to ANZ is that, by this guarantee, its risk-weighted capital requirement is waived completely for Pacific sovereign bonds. A lower regulatory capital requirement means higher profits.

The advantage of this approach is that the cost to the taxpayer is virtually zero. It is a very clever mechanism. Only in the highly unlikely chance of Pacific governments defaulting on their bonds

1

https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/PacificBanking2025/Public_Hearings

² <https://www.apra.gov.au/sites/default/files/2021-11/Final%20Prudential%20Standard%20APS%20112%20-%20Capital%20Adequacy%20-%20Standardised%20Approach%20to%20Credit%20Risk.pdf>; see Table 5.

³ <https://www.anz.com.au/newsroom/media/2025/march/Update-regarding-ANZs-Pacific-operations/>

will the Australian taxpayer be “on the hook”. To this extent, the ANZ deal is to be praised.⁴ It is a deal (albeit on a much smaller scale) similar to the one that underpins the entire multilateral lending system. There, countries with high credit ratings (such as Australia) underwrite the sovereign lending of institutions of the World Bank. It costs the high-credit-rating countries almost nothing, and the benefits for developing countries are large.

However, the disadvantage of this approach is the lack of transparency. The World Bank operates with transparency. So too should this bill. We turn to this aspect next.

The need for transparency

Since the actual nature of the guarantee is not specified in the bill, and since it is said to be highly confidential, it remains a secret. This must be objected to as a clear violation of transparency, and as awarding too much discretion to government and business officials.

Unfortunately, the government’s track record gives rise to suspicion that a very generous deal has been provided to the ANZ. Our analysis of the similarly confidential Digicel-Telstra deal is that the Australian government paid Telstra \$190 million to buy the highly profitable Pacific mobile telecom monopoly, Digicel, without any obligations at all.⁵

Moreover, future deals could be more costly to the taxpayer. The government could decide to guarantee any aggregate losses made in the Pacific by an Australian bank, or, indeed, the government could decide to guarantee every loan made by that bank in the Pacific. We would never know. In the end, whatever the likelihood of the guarantee being invoked, it is taxpayers’ money that is being put on the line. The taxpayer has the right to be informed, and to be reassured that they are not being taken for a ride.

The Australian government funds a number of domestic community service obligations whereby businesses are paid to undertake a variety of services that benefit the community, and which are unprofitable for them to undertake. These arrangements apply to both government businesses (e.g. Australia post)⁶ and private businesses (e.g. pharmacies).⁷

What the Australian government is here asking ANZ to do is to undertake a “foreign service obligation”. In return for its guarantee, ANZ is agreeing, over the next ten years (the duration of the deal): (a) to pay an annual fee; (b) to continue to operate in the Pacific; (c) to make a modest

⁴ I leave aside here the principle that “risks should be borne by the party best placed to manage them”, which is applied to the issuance of Australian government guarantees unless there is an explicit political (e.g. Cabinet) instruction. See Part 6 of Public Governance, Performance and Accountability Delegation 2022 at https://www.finance.gov.au/sites/default/files/2024-07/PGPA%20%28FM%20to%20AA%20of%20NCEs%29%20Delegation%202022%20-%20compilation%203%20July%202024_0.pdf

⁵ <https://devpolicy.org/australian-government-gifts-190million-to-telstra-to-buy-digicel-20220421/>

⁶ <https://www.transparency.gov.au/publications/communications-and-the-arts/australian-postal-corporation/australian-postal-corporation-annual-report-2023-24/other-important-information/community-service-obligations-for-the-year-ended-30-june-2024>

⁷ <https://www.ahaconsulting.com.au/resources/community-service-obligation-funding-pool/>

investment in the Pacific (\$50 million); and (b) not to charge fees for digital money transfers within the Pacific.

Making the terms and conditions of this deal public, as they are for domestic community obligations, would have several advantages.

First, analysts could judge whether the deal represents value for money. At the moment, this is simply not possible. It might be possible to work out or estimate ANZ's sovereign bond holdings in the Pacific. But we have no idea of the value of the fee that ANZ is paying or the cost of its additional commitments. Note that the \$50 million investment may in itself be profitable for ANZ.

Second, making the details public would make it possible to judge whether ANZ is holding up its end of the bargain. (It is not even clear if the government will have any visibility via confidential reporting of ANZ's performance in the Pacific.) Note that the way the guarantee is structured gives no incentive to the ANZ to lend more to the private sector in the Pacific. The only incentive that may be present (depending on how the guarantee is structured) is to lend more to Pacific governments. So, ANZ might just take the guarantee and, without closing down its Pacific operations, do as little as possible in the Pacific, short of shutting down.

Third, making the terms and conditions public would remove a lot of the confusion currently present. For example, in the second reading speech, the Assistant Treasurer said that the guarantee was "not a subsidy" because the Australian banks that receive it will pay a fee.⁸ This is hard to believe. If the fee equals the benefit to ANZ of its reduced capital requirement (that is, if there is no subsidy), why would ANZ agree to the deal? As already noted, the risk reduction is very low. The main benefit to ANZ is the increased profitability from a reduced regulatory capital requirement. If this extra profit is offset by fees there is very little in the deal for ANZ and the bank probably would not have signed on.

Because of the lack of transparency, there is also confusion about the impact of the bill on interest rates in the Pacific. BSP in its submission models the guarantee as reducing the interest rates ANZ charges on its loans.⁹ It will have no such impact.

No doubt the objection will be made that the negotiations are "commercial in confidence" and the details cannot under any circumstances be released. I disagree. Any corporation receiving a benefit from the taxpayer should be required to disclose the terms and conditions on which such benefits are provided and should be obliged to report on what it is doing in return.

The real-world problem standing in the face of a more transparent approach is that ANZ has a lot of bargaining power. It and Westpac are the only two Australian banks with a presence in the Pacific, and ANZ's presence is more extensive. Only a very small portion of ANZ's profits come

8

<https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22chamber%2Fhansard%2F28811%2F0040%22>

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https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/PacificBanking2025/Submissions

from the Pacific, and it is clear that the ANZ has been considering pulling out from the Pacific altogether. (In 2018, ANZ sold its retail banking in PNG to Kina Bank, and it only provides banking services for businesses operating in PNG now.) ANZ might have refused to enter into this foreign service obligation if the terms and conditions were made public, and if had to report on its performance.

On the other hand, ANZ profits enormously from the Australian market, and it is unlikely that it would resist a deal that the government wanted it to make, and that would also enhance its profits, even if that deal was made transparent. It is also likely that the government will want to make further details with Australian companies, whether in the banking sector, telecom sector, or other. It is very important that a precedent of transparency be established before further deals are entered into.

Finally, it might be argued that the Australian government and the Pacific benefit in intangible ways from the ANZ not pulling out: this might be seen to be in Australia's strategic interest; and it might be a negative for the Pacific's reputation if ANZ were to pull out. Financially, ANZ benefits from these arguments, and can drive a harder bargain as a result of them. But that should not mean that that bargain, even if more in favour of ANZ than would otherwise be the case, should remain hidden.

My recommendation is therefore that the Bill should have transparency requirements written into it, similar to those associated with a community service obligation. These would stipulate at a minimum that the terms and conditions of any guarantee made under this Bill would be made public, and that the recipient of the guarantee would be required to report on its compliance with the obligations it has entered into.

Impact on competition

It is not plausible to suggest, as government officials have done in defending this bill, that it levels the playing field between domestic banks in the Pacific and international banks.¹⁰ If that were true, then Australia and every other country with multinational banks should offer this guarantee to all their banks in every country in which those banks operate. But obviously Australia doesn't do this, and I'm not aware of any other country doing it either.

It simply doesn't make sense to argue that Australian banks need a guarantee from the Australian government to level the playing field for them overseas. When international and domestic banks compete, they have a range of advantages and disadvantages. BSP claims in its submission that

¹⁰ See the remarks of Mr Baird: "The guarantee in effect places ANZ on the same level footing as banks operating in the Pacific today."
<https://parlinfo.aph.gov.au/parlInfo/search/display/display.w3p;query=Id%3A%22chamber%2Fhansard%2F28811%2F0040%22>

ANZ already offers lower rates on its PNG loans than BSP.¹¹ How could ANZ do that if the playing field is tilted against it?

Keeping ANZ in Pacific markets by provision of government support is definitely a distortion, that is, a government policy that influences market outcomes. ANZ competes not only with BSP, the dominant bank in PNG and several other Pacific markets, but also with other much smaller local banks, such as Kina Bank (which bought ANZ's PNG domestic banking business from them in 2018). Is the guarantee worth the distortion? On the one hand, more competition is a good thing; on the other, it is unfair that a government subsidy should be provided to only one bank: this is the opposite of levelling the playing field. We cannot possibly judge the pros and cons without the terms and conditions being publicly available, and ANZ's performance under the guarantee being monitored.

Addressing correspondent banking relationships

The explanatory memorandum and the Minister's speech lay a great emphasis on the decline in correspondent banking relationships in the Pacific. This is indeed a serious problem. Between 2011 and 2022, CBRs in the region dropped by 50-80%, more rapidly than the global average decline of 30%.¹² And yet this banking guarantee is a very indirect way to tackle that problem. All it does is ensure that banks covered by the guarantee banks – so far only ANZ – can make international transactions. This is very important in Kiribati, where ANZ is the only bank. But it is less significant in other countries where there are multiple banks.

For example, in PNG three new local banks have been given banking licenses. As far as I know, none of them have a correspondent banking relationship. The ANZ guarantee does nothing to help them.

There is a World Bank project which has the explicit objective of protecting remaining correspondent banking relationships in the Pacific and ensuring that no Pacific country is left stranded.¹³ No doubt the Australian government is supporting this.

If the Australian government wanted to do more to protect and enhance the Pacific's correspondent banking relationships it could: (a) set up a subsidy system to incentivise more banks (Australian or foreign) to offer correspondent banking relationships in the Pacific; (b) incentivise (whether by subsidies or moral suasion) more Australian banks to operate in the Pacific, as it has successfully with the Commonwealth Bank entering Nauru; and (c) explore a more direct role for RBA to facilitate international transactions involving the Pacific along the

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https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/PacificBanking2025/Submissions (p.21)

¹² <https://www.rba.gov.au/publications/bulletin/2023/jun/correspondent-banking-in-the-south-pacific.html>

¹³ <https://documents1.worldbank.org/curated/en/099070825073028096/pdf/P502591-fb62dad7-3218-4a17-a1fb-3f8fa9226df7.pdf>

lines of what New Zealand's central bank has trialled in relation to remittance payments to Tonga.¹⁴

The decline in correspondent banking relationships is a serious issue for the Pacific but should not be put forward as a major justification for this bill.

¹⁴ <https://documents1.worldbank.org/curated/en/552411525105603327/pdf/The-decline-in-access-to-correspondent-banking-services-in-emerging-markets-trends-impacts-and-solutions-lessons-learned-from-eight-country-case-studies.pdf>