

This submission consists of a brief executive summary with extensive footnotes, indexed here, which are intended to be read as a single document. Terms and acronyms are in the Glossary on the last page. I refer to exhibits to my CBA/Bankwest submission #54 by a page number in brackets (123) and to exhibits to this GFC submission by (G123).

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The IMPACT of the GFC on AUSTRALIA and its BANKS

AUSTRALIA'S CURRENT EXPOSURE to the GFC

And what POLITICIANS CAN DO ABOUT IT

Conclusions;

1. For 30 years globalisation and the GFC¹ have been fuelled by capitalism as the most dominant of many forces. The World is now predominantly a business and accounts⁸ must be drawn that way.
2. The World has more assets per capita than ever before especially if measured at intrinsic value² while many Western economies have developed unserviceable debt³ and are approaching insolvency.
3. China with \$3.5t (trillion) in Net Foreign Reserves^{4a} and others have grown their assets by more than the Western economies have lost.
4. The impact of the GFC on Australia was minor as we were not *impacted* by the Sub-Prime Crisis¹⁰.
5. Our Government did not limit the *impact* of the GFC; however it increased our *exposure* to it.
6. Australia being \$1t in Net Foreign Debt³ is now more *exposed* to the GFC than any other country¹⁷.
7. Australia has a \$2t problem⁷ - \$1t in net debt when it should have \$1t in net reserves. **“the Problem”**.
8. In 1944 Australians defended their country¹⁴ when it was being bombed. Now it is being bought because its assets are being, and will be, effectively exchanged for debt¹⁹. The mechanism is different but the consequence is identical. Loss of Sovereignty. And no one will even discuss **the Problem**.
9. **The Problem** arises internally from monetary greed¹⁵ evolving to dominate every other motive. The Australian workforce, particularly at board level, moved from being productive and devoid of monetary greed in 1945¹⁴ to being driven by monetary greed to the exclusion of all else including compliance with the law. As in the US (Inside Job) our courts and regulators have been ineffective.
10. **The Problem** equally comes from Australia being run by meritocracies that exclude business skills entirely²⁵. We are run by immensely talented people who got to the top on merit, but it's like sending our test cricket team to play chess against the Chinese chess team.
11. Bank profits, though not alone, are the major contributor¹⁸ to our foreign debt³ and are at the expense of Australian customers. Mining profits are earned from foreign countries and reduce foreign debt.
12. The banks used the GFC as an excuse to double profits in two years (see sub #54).
13. Our Governments privatised monopolies to fund the promises that got them elected. They justified this because the public sector did not have the structure, skills and incentives to run them efficiently, however, monopolies cause even more harm in the private sector^{21,18}.
14. Australia's financial policies are based on figures which have been compiled on the basis of what was historically possible. Many of them are now absurdly out of touch with reality;
 - (a) Employment numbers mislead – what matters is whether the worker is producing or destroying wealth rather than the number of them that are doing it³⁴.
 - (b) GDP does not measure production⁹; it measures the price paid for it and covers up overcharging.

- (c) Public and business confidence³⁶ should be accurately based on reality not on charismatic speeches or spin which prevent corrective action.
- (d) Wealth only comes from work³³. Not out of thin air. There are no exceptions.
- (e) While productivity³⁵ cannot be criticised our problem is with lack of, or negative, production.

Actions Called For

1. The Government should prepare a ten year plan to maximise Australia's financial prosperity. That plan should at least meet the standards for intensive plans used by IBM to run its business.
2. Australia should add to and reorganise its management structure so that our best business skills run the country as profitably as they run our major companies. The powers could be separated but we need that fourth meritocracy to determine financial policy. It costs \$20m a year to hire the CEO of a major bank which is one twentieth the size of Australia. It is absurd to expect Australia to be run properly as a business by someone who is paid 2% of that.
3. The correct, and now the only viable solution is to move the monopolies and the business structure, people and skills into the public sector.
4. The Government should prepare accounts for Australia in the same form as a company would do.

Consequences of Doing Nothing

If Australia does not reduce its Net Foreign Debt our Sovereignty will come under pressure.

We must show the world that we can service our debt or we will have to sell more assets to foreign countries. They will choose the best assets - our farmland and mining companies, our best technology. Foreign owners will have political influence here roughly in proportion to their ownership. Immigration policy will come under pressure. If they buy our most profitable assets our debt will increase again.

China, alone, has enough foreign reserves to buy every worthwhile asset on this continent that is not already foreign-owned and even then China would have no foreign debt. Do they have any reason to look after our people ahead of their own? 1,500,000 people form a very long queue.

We are a tiny country. Democracy has developed major flaws and cannot save us anyway. In a globalised world we would have 15 million votes out of 5 billion.

Our sovereignty is our only hope. We must not let it be diminished by unserviceable debt.

FOOTNOTES – which may be read as a narrative.

1 **GFC** is used with many different meanings and I have no authority for preferring one use to another. The extensive diagnosis carried out by NAG concluded that what is now called the GFC is the product of human evolution and as such has occurred simultaneously in many Nations. The trigger or catalyst for its growth in particular Nations seems to have been the reality or perception of financial prosperity and a domination of monetary greed over other motivations. National accounts show it has affected the prosperous Western world adversely and the rest of the world positively. It is not contagious. An exception is that the Sub-Prime Crisis¹⁰ (SPC) which emerged in the US created such a large volume of fraudulently securitised assets that other countries bought them and were affected by that contagion. Australia was not substantially affected as the banks show securitised assets having fallen from less than 4% to 1% of assets.

1a **The dominant symptom of GFC exposure is always debt³.** It is imperative to distinguish between the “**impact**” of the GFC as referred to in the Terms of Reference and our **exposure** to it in the future. For Nations, debt³ has many variants and descriptors and all of them are deliberately confused for political purposes. I have relied on the ABS definitions.

The GFC really started in Australia about 1975. Once the causes are understood it is obvious that the GFC is like financial tectonic plates grinding away incessantly. Occasionally one plate fails and there is a tsunami. What we refer to as the GFC (2008) is that tsunami. There will be more tsunamis because we have done so little to understand or address the *cause*.

The GFC is a feature of the Western World. It is offset by positive outcomes in China (\$3.5tr in NFR), India, South America, Indonesia, Africa and elsewhere. At intrinsic value there are more assets per capita on Earth than ever before. Insolvency in Europe and approaching insolvency here and in the USA are more than offset by equivalent increases in prosperity elsewhere.

1b **The Best Measure of GFC exposure is NFD⁴ per capita.** That is consistent with the global economic assessment by Merrill Lynch (G2, 263) in early 2009 that Australia was the most *exposed* Nation on Earth to the GFC then called the “Sub-Prime Crisis”. ML’s assessment did not surprise me as our NAG work in the 1990s produced similar but much more detailed results.

1c **Australia has the highest exposure of all nations to the GFC** according to ML (G2, 263) who ranked 60 nations from most exposed to least exposed. It is part of the cause of the GFC that ML’s work was irrationally and emotionally brushed aside when the alternative was to read the 25 pages of expert analysis that led to their conclusion. This requires diagnosis;

A Federal Minister who had no bias referred the ML report to a respected expert in banking who dismissed it by saying ML had had financial issues himself and gave no other reason. It was referred to Senior Counsel who dismissed it for the same reasons. Both made irrational decisions that are destructive for Australia. ML employed 30 well-qualified and well-paid unbiased economists. One was Australian. I found ML’s report thoroughly consistent with NAG’s work. It was completely irrational to connect ML’s financial problems with the report. It is a political error that is typical of how Australia is run financially. Our leaders lack the time and qualifications to read such a comprehensive technical report themselves. So they give it to a public servant. Where business and commerce is concerned our public service, despite their exceptional expertise in other areas, is not able to give good or experienced advice.

2 **Intrinsic Value** is the real or fundamental value of anything. It is approximated by the price that a good or service would achieve in a market with perfect competition. Alternatively it is the cost of efficiently producing the product for its people. It is always possible to determine one or the other of these measures approximately. It is extremely important in the present context because China, based on the intrinsic value of its assets and its human capital, is already the dominant economy on Earth. And Australia is less than 1% of the Earth’s economy. Consider any common object which can be

manufactured. How does its intrinsic value vary? Why would a bicycle's intrinsic value be more or less in China than here? The general answer is that there are variations however they are small and there is no better basis for comparison than intrinsic value. For instance it could be said that bicycles are more valuable in China than here because there is more demand. Motor cars may have higher value here because taxi fares are much higher. However the difference is the cost of getting the car here from China. This leads to the realisation that the intrinsic value of the Chinese labour required to make a car is little different than the Australian labour. And if the Chinese have a more labour-efficient way of doing it, as they do, the Chinese labour is arguably worth more.

- 3 **Debt is dominant in any balance sheet.** If a Co has assets of \$100bn and regularly earns \$5bn profit per annum its value depends entirely on its debt. If debt is \$100bn the assets would be extinguished by the debt and the profit would be extinguished by the interest on the debt. The Co would be worth nothing. If the debt were zero the Co would be worth up to c. \$200bn depending on the price earnings multiple which would be based on assets and the assessment of reliability of future earnings. **Foreign Debt** is the amount owed by a Nation to all other Nations. It is an ambiguous term.

Gross Foreign Debt (GFD) is the total amount owed by a Nation to other Nations.

- 4 **Net Foreign Debt (NFD)** is GFD less loans to other countries. That is what matters. NFD arises when a Nation consumes more than it produces. It must import the difference. That causes a Trade Deficit. Trade Deficits add to NFD. A Nation which produces more than it consumes will be a net exporter, will have trade surpluses and accumulate NFR.

The crucial importance of NFD is misunderstood in Australia because;

- (a) Many of the publishers of Foreign Debt, like CIA, record GFD which is misleading.
- (b) NFD is almost always confused with Government Debt or National Debt. Most of our foreign debt is owed by the private sector and is secured by assets. It is argued that NFD so secured does not matter. That is untrue. If the Govt were to give \$100b to the IMF to bail out Europe they would have to tax the private sector. Sovereign debt is guaranteed by the Govt and they have the power to tax every asset on the continent. Including every private asset. If the debt were closely connected to business returns why did it go from \$3bn to \$1,000bn in 30 years? In the end we are \$1trillion in debt in a world where the average is zero. NAG concluded that it doesn't matter much who secured the debt – they are, at the end of the chain, Australians.
- (c) In recent years NFD has been expressed as a percentage of GDP⁹ by the ABS. Overcharging by monopolies is the principal cause of our NFD and this also inflates GDP. So expressing NFD as a percentage of GDP⁹ covers up the magnitude of the problem.
- (d) NFD is not published as a per capita figure which is required because the only source of production is a human being. The only consumer is a human being.
- (e) Australians believe, wrongly, that full employment means our workforce is productive. Production depends on what the workforce is doing, not how many of them are doing it.
- (f) Productivity is the current buzz-word when what we need is Production. There were 188m sheep in Australia in the late 1990s - 68m and falling now while the wool production efficiency of the producers has increased. Respected and independent authorities like the Productivity Commission - www.pc.gov.au and the Australian National Audit Office - www.anao.gov.au are not focused on projects which would address Australia's NFD.
- (g) Practically no weight is given to the major variable, %P, relating to jobs. %P is the degree to which the holder of the job is productive. Building houses or growing wheat is entirely productive, 100%P, because the worker or his employer invests money, takes risks, works hard, only gets paid if he produces a result and sells the finished product in a market in which there is perfect competition. Zero production, 0%P, is achieved by those who produce nothing and effectively steal the goods that are their income. Negative production, -x%P, is achieved by those workers who, without sufficient reason, get paid to prevent production.
- (h) Federal Politicians have a vested interest in making sure these vital issues are not understood. They know they won't increase their chances of election by raising negative issues which may

well be blamed on them. They have no idea how to solve the problem and cannot therefore obtain any advantage by raising it.

- (i) Australians will not accept that their country is not the best one on Earth.

So Nations “go broke”. The above is confirmed by the recent insolvency of Greece, Portugal, Spain and Ireland all of whom achieved that status prior to any internal political effort to redress the problem. All three had millennia of history which supported their belief that they were “The Greatest Country on Earth”. They suffered from the presumption that they were prosperous and that seems to lead the most successful residents to expect unlimited incomes and the least successful ones to expect that the rest of the economy can support them even though they do no work and produce nothing. These countries thought they didn’t need to do anything about their unserviceable NFD because they were “prosperous”. The rate of decline is worse in Australia, although we had more assets to start with. Our situation is also much simpler. We are an Island Continent which is not integrated into a larger complex economy. We can’t blame the Euro.

Only external debt matters. If a company has a subsidiary which owes money to another of its subsidiaries it does not affect the value of the company. It does not matter how much money has been borrowed by one lot of Australians from another lot of Australians even if the borrower loses the lot. Of course that is bad however it makes no difference to NFD whether the borrower lost it or the lender lost it. A doctor who can’t employ his savings might invest them with a builder. The Dr could start building as a sideline - but it’s not practical. Either he or the builder could lose. On average this process has evolved very positively – but there have been some huge and hideous exceptions like Bernie Madoff for instance. External debt, if not serviced, will lead to the sale of our assets.

Foreign Debt is also borrowed to invest in Australia. This often obscures the truth about NFD. Since 1788 Australia has borrowed money to invest. Those investments are still paying off. Sandstone buildings 200 years old still produce revenue. Lands cleared in the early 1800s still carry sheep or grow crops to produce revenue. The Harbour Bridge lets people who would otherwise spend an hour a day driving around the Harbour use that time to produce something instead. The Snowy Mountain Scheme still puts electricity, now more valuable than ever, into the grid. All that capital investment ran up NFD when it was borrowed but now it has paid off many times over.

NFD would be worse if we didn’t borrow capital. Economist Ross Gittens thought this to be so obvious that he didn’t refer to capital issues in his textbook on the subject. NAG analysed this extensively. A big capital injection can *increase* NFD however our NFD took 30 years to get where it is and overcame 200 years of successful investment. NFD is \$2 trillion more than it ought to be. And that is not because of some recent influx of capital. Even with the colossal growth in China they have NFR of \$3.5tr lent to the world and not a cent borrowed.

External Debt is the same as Foreign Debt – but used when referring to another Country. The money Australia owes to other countries we call our Foreign Debt. The money that Britain owes to other countries we call their External Debt.

- 4a Net Foreign Reserves** are the opposite of NFD. If two countries had never dealt overseas neither would have any NFD or NFR. If one lends the other \$1m it would have \$1m in NFR and the borrower would have \$1m in NFD. Every real country is both a borrower and a lender, so we record the net figures: NFR and NFD. Many sources, like the CIA, quote the gross figures which mean little.
- 5 International Investment Position (IIP)** is another form of debt represented by the difference between capital investment by overseas entities in Australia less our investments overseas. That adds about \$110 billion to our total debt as at September quarter 2011 (ABS). Total \$850 billion.
- 6 National Debt** is accumulated Federal Government Deficits. It is *not* Foreign Debt. If *instantly* collected from the people, by further tax collections from them or reduced payments to them, it would increase NFD by the same amount. If we have 2 identical countries except that one has \$100b of

public debt and the other has zero public debt the question is how does that require the nation's total debt to be adjusted, if at all, so that a proper comparison about financial exposure can be made? If the National Debt were reduced to zero private savings would be reduced. Reducing savings is the same as increasing debt. Private savings may have many repositories but in every case their removal would require replenishment from outside Australia as nothing within Australia has been (instantly) created which would replenish it. For instance;

- 1 The savings are in a bank. If withdrawn the bank would have to replace them.
- 2 The savings are overseas so bringing them back reduces our overseas assets and therefore increases IIP.
- 3 The payer sells a local asset. That requires the buyer to increase borrowings.

The National Debt will be paid by taxpayers. The Government's debt will go to the private sector. If it were to happen instantly the entire National Debt would add to NFD. Australia is therefore nearly \$1 trillion in debt. This is not a desirable position when China has \$3.5 trillion in NFR.

National Debt, Government Debt, Public Debt or "Labor's Debt" as John Howard called it, is a secondary issue. Misleading the Australian people was a very effective political strategy and has left most of us confused ever since. The Howard Government did get itself out of debt effectively, efficiently and intelligently by transferring every cent of it to the Australian people.

A good VAT is an excellent way to raise taxes because it tends to restrain consumption. Australia's GST a poor, complex and expensive variant under which Australia's NFD went from about \$120 billion to \$520 billion under PM Howard. As the new GST did not increase local production the payment of the GST increased NFD. Labor has done even worse as NFD is \$740 billion, our IIP has deteriorated, and our National Debt has increased.

Public Debt is the same as National Debt and Government Debt.

- 7 **Total Debt** for Australia is the sum of its NFD, IIP and National Debt – just less than \$1t. Given Australia's mineral and agricultural endowment and its high levels of education it should have net reserves of \$1t. We are looking for a \$2t problem.

Zero Sum of Debt. Earth is a closed economy. The sum of all the NFD and NFR is always zero. With that in mind we must consider Australia's position in owing \$1 trillion net to the rest of the world. Our expectation, as the lucky owner of enormous mineral and agricultural resources and a well-educated workforce, should be \$1 trillion in NFR not NFD.

The zero sum also applies to banking. The world can be realistically considered to be two accounts; Australia and others. Why is it that of the two our banks have borrowed about 30% of their assets from the others? And not the other way around? Chinese banks aren't net borrowers despite their phenomenal growth. Our banks do not profit from that borrowing because they could not, on average, lend it back into that market at a profit. They have no competitive advantage there. So they put 2% on top and make the entire profit from the Australians to whom they lend it.

NFD determines a Nation's *exposure* to any financial crisis and the GFC is no exception.

- 7a **Australia has the highest exposure of all nations to the GFC.** ML wrote their paper at the end of 2008 just before the Sub-Prime Crisis started to be called the GFC. They were measuring "Exposure to the Sub-Prime crisis" and showed that Australia had the highest exposure of all countries. NAG went through every sector of the Australian workforce as provided by the ABS and asked "Does it produce more than it consumes?" If not the extra consumption is funded by borrowing and flows through to NFD. NAG concluded that overcharging by monopolies is the principal cause of our NFD.
- 8 **All accounts are fundamentally and mathematically identical** – whether for a person, a company or a country. The translation of National accounts into commercial terms, in which Ferrier Hodgson

assisted, showed that only the language changes. “Income” for a person is called “salary” or “wages”. For a company it is called “gross sales” or “revenue” and for a country it is called “exports”. While specifics are beneficial, tax experts and others have complicated reporting to put the best light on a particular performance and this often leads to a misunderstanding of the fundamentals.

- 9 GDP does *not* measure production.** It measures the price paid for it. If one of Australia’s many near-monopolies gets paid 10 times the intrinsic value of its product that is what is counted in GDP. The ABS gives 3 different definitions of GDP (266); (a) the income approach (b) the expenditure approach and (c) the production approach. All 3 measure the price paid for production.
- 10 The Sub-prime crisis (SPC) caused the GFC Tsunami.** The SPC was a massive fraud by the banking sector in the USA who lent money to home buyers with no assets, no income and no-repayment-for-2-years on such a massive scale that the huge demand for housing increased both the supply and the price of housing in the US. Between 2001 and 2008 US housing prices went up by 430%. By 2008 there was a massive over-supply of housing in the US (2002). The problem grew to such enormous proportions because (a) no default could occur for 2 years (b) US home mortgages are almost always non-recourse and (c) there is a very high level of securitization of mortgages in the USA so that the individual security for a loan cannot be determined. To quantify and understand housing supply we must ask “on a tiny inaccessible island with a population of two how much is a third house worth?”

Citigroup, one of the largest banks on earth, was charged with fraud by the US Government, settled it for \$48 billion, became insolvent and was bailed out by the people of the USA who now own most of it. Thousands of other US banks have become insolvent including some which are bigger than the Australian banks. And yet the US is much more able to service its NFD than Australia. US NFD is \$4.47 trillion and Australia’s is about \$0.9 trillion. The US has 15 times as many people working to service that debt and its GDP confirms that. The US has massive Public Debt which, in the unlikely event that it is ever collected from the taxpayers, would bring the US Net Foreign Debt up to a per-capita level similar to ours.

- 10a Australia did not avoid the Sub-prime crisis** – we were not substantially affected by it. Australia is very different from the US;
- (a) The US had a massive housing oversupply compared with the shortage in Australia
 - (b) US had housing growth of 430% compared with 150% in Australia in 2001-2008
 - (c) Two-years-without-repayment loans do not happen in Australia
 - (d) Australia does not have non-recourse mortgages which are universal in the US
 - (e) Australia has 1-4% of loans securitised and falling compared with over 20% in the US

Australia was not greatly affected by the GFC. Australia ran up massive foreign debt almost unaided.

- 11 The first cause of our \$2t problem is the financial behaviour of all Australians;**

Australia went a further **\$54bn** into debt in the last September *quarter*. Source ABS (G3). It was not caused by the GFC. The majority of this increase was due to a weakening of the Australian dollar which increases NFD. The US recently doubled their money supply in just over 2 years and it made little difference to their economy however it became a major component in the strengthening of the Australian dollar because many of our accounts are denominated in \$US.

The \$2 trillion problem and the GFC were caused by the same underlying changes in human behaviour which took 30 years to evolve and accumulate. NAG diagnosed the causes of Australia’s NFD and therefore, inadvertently, found the causes of the GFC. Our work was repeated by Merrill Lynch (ML) in 2008 when the GFC was called the “Sub-Prime Crisis” (G2). ML confirmed NAG’s earlier decisions. NAG did a much more intensive job of analysing Australia’s situation whereas ML had done vastly more work on other countries.

11b Australians caused the NFD increase. We are not being invaded. Any trading we do with other countries, any borrowing, imports or exports is voluntary. Nothing is inflicted on us. Even the alleged increase in the cost of banks' borrowing overseas is the result of a deliberate decision by the banks to borrow extra money from outside the country, put a 2% margin on top of it, and lend it to Australians.

- (a) The cause of our NFD is that we import more than we export and we must ask "Why?"
- (b) Almost all Australia's production comes from its workforce. So analyse it first.
- (c) NAG went through every sector of the Australian workforce as provided by the ABS and asked "Does it produce more than it consumes?"
- (d) Some sectors charge a great deal more for their production than its intrinsic value. The major offenders are the providers of services, however it would be wrong to generalise.
- (e) %P of Services. Consider a wheat farmer who is 100% productive. He may not want to divert capital or time into the specialised truck required to take his harvest to the silo when he could be harvesting more wheat. He may hire a truckie. If that truckie frees up enough time and capital for the farmer to exactly pay for the truckie's service he is just as productive as the wheat farmer. If he charges more he is less productive and overcharging in economic terms.
- (f) Australia's NFD has reached its fatal proportions because major sectors of the economy have evolved so that some service industries charge a multiple of the intrinsic value of their service. We must ask "How can this come about?"
- (g) Major service industries, such as banks, destroyed competition. It is necessary, for a full and quantified understanding of this, to break down perfect competition into its component parts and measure them consistently for each industry sector (%P).
- (h) The obligation on directors to maximise shareholder value adds to the problem. The legal system provides little or no redress for the victims.
- (i) There is no competition in the Public Service. Public servants paid by the hour to follow a procedure rather than to produce a result. Their highest pay (consumption) occurs when there is no result the procedure continues forever.

13 (j) The intrinsic value of any service is what it would cost the people to do it for themselves through their Federal Government. The Government could take over all the banks, consolidate them into one, retain only the top private sector bank directors, provide all the banking services required by Australians through a comprehensive but single set of products and pay all the profits into consolidated revenue. The intrinsic value of the total banking services produced in Australia is about 15% of what the banks charge for it. Their charge equates to consumption. If their production is valued at intrinsic value the difference is an increase in Australia's Trade Deficit and its NFD. To measure how banking competition has been eliminated one would need to consider;

- 1 The Commonwealth Bank was owned by the people – now privatised – it didn't have to make a profit and was a fierce competitor for the people.
- 2 Every State bank, also operating for the people, has gone or been privatised.
- 3 Most foreign banks have withdrawn from the Australian market.
- 4 All the big lending Mutuals like AMP are no longer mutuals – they have been privatised.
- 5 The Building Societies which were not for profit have become banks or have gone.
- 6 The Credit Unions which used to be not-for-profit are now compelled to make a profit.
- 7 The barriers to entry have multiplied in size.
- 8 The cost of changing banks has multiplied tenfold as exit fees, termination fees, application fees, stamp duty, legal fees, valuation fees and accountant's fees combine.
- 9 Regulation has declined from almost absolute to almost nothing since the days when Menzies set interest rates by directing the RBA which was not independent in those days. Now we have the RBA which set interest rates at the highest level in the Western World when we have the highest level of NFD in the world and have to pay interest on it.
- 10 The banking industry is now an oligopoly and does not need to signal or conspire to approximate the performance of a monopoly (Samuelson ISBN0-07-452697-9).
- 11 The RBA is either so ignorant or so complicit in this that it continues to suggest that there is some meaningful level of competition between banks. The truth is that competition has reduced from about 90% to about 10% of perfect competition.

- 12 The depositor guarantee removed the last vestige of competition. While there was arguably a sound political reason for doing this it came on top of the existing lender-of-last-resort facilities and put the banks in a position where no non-bank could compete with them. The **result** was that something like \$80bn moved from the non-guaranteed sector to the big banks. The RBA and ANZ submissions show how the market shares varied and Samuelson would say bank competition may as well now be 0% of perfect competition. The cost of banking to the consumers of it is further increased by the farcical attempts to fake competition. If Australia had one bank its set of products would be superior to any of the four “competing” products and cost much less to deliver. I rely on Samuelson’s text books for the breakdown of perfect competition which allows %P to be calculated. Lack of competition leads to near monopoly and Samuelson would say that the 4 banks are worse than a monopoly because they have four different sets of products and practically no actual competition such as would regulate their pricing. Woolies and Coles are just as bad except that they have profited at the expense of the (Australian) producer rather than the (Australian) consumer. When you quantify these aberrations the results are astounding – but then they have to be in order to be consistent with our country being a trillion dollars in debt when it should have a trillion dollars in the bank.
- 13 A “snapshot” is that the CBA showed a 27% return on shareholders’ funds before tax in 2010 whereas my wife’s superfund invested in a range of equities showed 2% and that is typical of super funds at the time.

- 13 All this analysis of banking since 1976 insists that human evolution has come to the point where banking, and other monopolistic services cannot be trusted to the private sector. This is particularly important where we now have competitors, including China, who do not suffer from this disadvantage and seem to have been able to get the best business talent to work in a Government owned enterprise. We will only survive if we copy China, shift the best minds to the Public sector, pay them what they get now, or more, and set their job goals to benefit the nation only. To the extent that such earnings are politically incorrect they may be remedied by substantial income tax rates with compensation provided where the taxpayer has been productive. This structure was approximated under Menzies where capital investments in mining and agriculture were tax deductible from the higher tax, and provisional tax, rates applying in those days. Relevantly Australia had no NFD in those days.

Banking is not alone – just the worst example of a near-monopoly overcharging because it has eliminated competition and has no motivation other than monetary greed. The grocery retailers, petrol distributors and hundreds of others have evolved in the same way. Some of them, notably Woolies and Coles now increasingly acquire their goods from overseas having destroyed local suppliers, who were 100%P.

- 14 **The bottom line is that the Australian workforce has moved from being almost entirely productive, altruistic and devoid of monetary greed to its being driven by monetary greed to the exclusion of everything else.** In 1945 a typical Australian resident would probably have been able to say as I could have at the time had I known what I now know;

- 1 My Uncles are in New Guinea trying to stop the Japanese and are paid almost nothing.
- 2 My Dad is working in a tyre factory away from home making tyres for the war effort.
- 3 My Grandfather is a top public servant and paying 91% on his top dollar in tax.
- 4 Mum is bringing up 3 kids and working part-time as a dental nurse in the war effort.
- 5 No one is putting monetary greed ahead of helping their fellow Aussie.

Almost every economic sector has moved to the opposite extremity where they use their higher education, capital and intelligence to maximise profit by overcharging their mates. They consume more and cause others to produce less by depriving them of capital and income. The difference between what they consume and what they produce is imported and that adds to NFD.

The human trend to monetary greed dominating every other motivation was suppressed by two World Wars and a Depression. While Wars are conflicts between sides they are exactly the opposite within opposing sides. Australians were never more altruistic than at the end of WW2. They wouldn't steal from or overcharge their mates. Now that is predominantly what they are doing.

15 Monetary Greed – Causes and Effects.

16 Australia went \$54 billion further into NFD in the September *quarter* 2011 (2001, ABS 5302). That is probably a world record for a county of our size. Even worse - no politician or commentator has discussed it. Our politicians and bureaucrats get to the top of competitive meritocracies. While gifted in special ways, they do not have the practical business skills to formulate policy that would compete with the likes of China. China is in business – not economics. It will buy us.

Banking Offences caused the GFC in the US. I rely on “Inside Job” for an analysis of the causes in the USA. The use of derivative securitisation with poor unquantifiable mortgage lending and risk management practices and banking offences caused the SPC. The major credit agencies assessing these mortgage and derivative product risks were a crucial part of the problem. We must ask *why* those things occurred as a basis for developing policy which will remediate the situation.

17 Australia is the most exposed Nation to GFC. At the end of 2008 Merrill Lynch (ML) published a report (G2, 263) prepared by its 30 economists in every large country that publishes national accounts. It ranked the countries according to their exposure to the sub-prime crisis. Their ranking criteria could be summarized as evaluating the country's capacity to service its NFD. ML concluded that Australia was the most exposed of all countries (263). Please do not fall into the trap of dismissing the 25 pages of reasons given by the top economists, including an Australian, because ML itself had financial failures.

18 Banks profits tend to destroy a country financially as follows;

- (a) Increased profit lets the bank's employees, shareholders and tax recipients consume more. Where the proceeds are invested the economic effect is similar to deferred consumption.
- (b) The increased cost to the bank's small business and home-owning clients reduces production, including that of dwellings. The increased cost to consumers increases consumption slightly.
- (c) The increased consumption of imported goods and reduced local production both add to the country's trade deficit and this accumulates into NFD.

19 Net Foreign Debt increased by \$54 billion in the Sept quarter 2011. Australia needs a surplus of \$10 billion per quarter to pay the interest on the NFD. This debt is economically, but not physically, as threatening as the bombing of Darwin. So much NFD allows foreign countries to “buy Darwin”. Greece's lenders want their money back but the lenders to us want to exchange the debt for our best assets. A company that allows its debt to shrink its net tangible assets becomes a target for takeover. And we *choose* to have the world's highest interest rates!

20 RBA Statement about Competition. The Governor of the Reserve Bank has said that there is an acceptable amount of competition between banks. No senior officer has ever made a statement that is more ignorant and more damaging than that. Australia faces greater damage if the RBA really doesn't understand this than it faces if the RBA does understand it and chooses to mislead us. Either way the problem is serious enough to be fatal for Australia's future.

21 The Truth about Bank Competition. We now have 4 major banks which have over 80% of the market. They do not need to conspire, collude, act in concert or “signal” each other to effectively act as one. An ill-treated customer can hardly sue the bank. It is too expensive to change banks – application fees, legal fees, stamp duty, accounting fees are wholly extra costs. Very few write off the loss, pay their termination fees and then pay application fees, valuations and legals to start with another bank so that both banks make extra profits from his unfair treatment. Where a customer is

sold up his security may be purchased by a customer of the bank that sold him up. It matters little which bank gets the new security – the banks get the extra profit. That goes to why all 4 big banks increased their profits by between 40% and 80% year on year in 2010 (119). This process requires nothing other than evolution and the absence of effective law, protest or regulation in order to grow.

- 22 Bank Profits come from Australians.** These profits diminish the assets and incomes of other Australians by charging seven times as much for their service as it is intrinsically worth. At times more than 100% of banks' profits come from Australians if overseas expansions are being funded and if the cost of overseas borrowings are indeed more than returns given to Australian depositors.
- 23 Mining Profits come from Foreigners** they export nearly all their material into highly competitive markets. If they make huge profits it is not because they have rigged the market or eliminated competition. Their profit comes entirely from foreign countries.
- 24 It is impossible to rationally manufacture anything in Australia** - even steel which requires coal and iron ore as the essential inputs and we could build the mill in the same postcode.
- 24a Bottom Line.** Wealth comes only from human effort with varying ease. If our workforce is productive our exports will pay for our imports. If our best workers are predominantly employed to steal from Australians we will fail. That is what is happening in the Western World. That is what caused the GFC. It is getting worse. Our best educated and most intelligent workers are focused on getting paid more by their fellow Australians for the same amount of production. NAG proved it. If every country behaved this way it would not be a problem – but that has changed. The emerging countries, particularly China, do not suffer from that problem.

25 AUSTRALIA'S MANAGEMENT STRUCTURE

Background. In 1976 the PM had me lead his Department to make a long-range business plan for Australia. I got the job again with even greater resources with NAG in the 1990s. Ferrier Hodgson helped me translate National accounts into business accounts familiar to the senior businessmen on our planning panel. We only recorded decisions unanimously agreed to by all the planners. I ask Senators to be equally ruthless in demanding proof.

- 26** No senior executive could contribute to the prosperity of his company without an expert command of its balance sheet/profit and loss. NAG proved beyond any reasonable doubt that the position is no different for a person or a Nation.

Not one person running this country or commentating on it has this information. Consequently Australia's finances are an incomprehensible shambles when viewed by a financial expert who does have it. Australia is losing value faster than Greece ever did. It just has a lot more assets to dissipate before the Government can no longer increase tax to meet its sovereign debt.

I did not realise until recently that our group was probably the only one that had ever done this work.

That is why I want to get that work done again or promote the diagnosis that flowed from it. The diagnosis shows with compelling logic how such a well-endowed Nation can lose its assets to its creditors. It also shows how to fix it. It's 30 years too late and we haven't started yet.

- 27 Australia's management structure** has three divisions of power - all extremely competitive meritocracies. The very best do get to the top.
- a. The parliament. Politicians are the best at persuading us to vote for them and being respected by their constituents. They are the best leaders.
 - b. The judicature. The best get to the top. They are supremely good at interpreting the law. Unfortunately their power does not go beyond that.

- c. The administration is another meritocracy. The talent that gets to the top is that of following procedures. Results are not given sufficient weight.

Over the last 30 years the world has changed and Australia has changed in such a way as to make this particular structure ineffective in the modern world. Those changes have to be looked at separately;

- (a) Australia has become less like a business. In 1950 Australians could manufacture anything including jet aircraft, ships, clothing and electronic goods. Now we can't even make steel profitably when we live on top of the cheapest resources on the planet from which to make it. The reasons for that have been explained above by the entire population being prepared to predominantly steal, by overcharging, from their mates instead of producing.
- (b) At the same time the rest of the world has been led by countries who increasingly became more like a business – first the US, then Japan. Now China has bolted. No Nation has ever mastered capitalism to that extent before. Not being a democracy is an advantage. China is a business and to survive on the same planet as China countries will have to develop business skills in the managements of their nations. Survival is statistically unlikely.

28 Australia needs a business Management Structure. The management structure of an international Company with 300,000 employees would have a basic management framework with essential fundamental principles such as;

- Every member of the structure must have agreed job goals.
- Every member must have a manager.
- Every manager should ideally have 8 -12 members reporting to them.
- Every member should have their job goal performance reviewed at least every year.

- 29 Business skills are needed to run a Nation these days** whereas the skills, though extreme and admirable, owned by our leaders, are very different. It is exactly like sending our world class cricket, football, and golfing teams to compete at the world chess championships.

None of those three separations of power has any significant ability to run a business. Nor do they have reliable access to those skills. Businessmen will steal from their mates remember. They may get to the top by overcharging better than others. They will “talk their book” to the powers that be. So the integration of these skills within the others has to be done carefully.

- 30 The world is now a business.** Capitalism is driving globalisation. Business is the largest and most competitive of the meritocracies in Australia and everywhere else. We have gone backwards because of monetary greed. But more importantly the world has sped forward since WW2 from an economy to a business. China is producing 42% of all the new wealth on the planet and they have mastered capitalism more effectively than any nation ever has. Russia has learnt from its failures and has the ability to come back stronger than ever.
- 31 Democracy won't help us** in a globalised world because China has 1,200,000,000 votes and we have 15,000,000. We are a trillion dollars in (net) debt to other countries and China is owed (net) three and a half trillion dollars by other countries.
- 32 China has a great incentive to look after our assets and none to look after our people.**
- 33 New wealth is created only by work.** A person stranded on a tropical island will have to work a bit to feed himself. On a desert island he will have to work very hard. In either case it is certain that if he does no work he will starve. New wealth is the value of production less the value of the consumption required to produce it. It *always* requires work. Assets depreciate. Food very quickly – gold very slowly but if you don't spend money looking after gold someone will eventually steal it from you. Goods and services are identical and arise entirely out of labour. No wealth comes other than from labour. Submissions to this inquiry base conclusions on the error that goods are not just labour. A commentator on my submission commented that the view was “Marxist”. This is a repetition of the earlier irrationality that somehow the truth of the statement is less important than who said it.
- 34 Employment is never measured by the number of jobs** as our leaders and economists tell us. **What matters is what the workers are doing.** If they are growing wheat they are adding to Australia's exports and reducing NFD. If they are destroying wheat crops they are increasing NFD. If they are building aircraft to destroy another country's buildings we have the ultimate example. Over half of Australia's workforce is spending a major part of their time trying to charge more money for the same product. Banks, Woolies and Coles, and petrol distributors are prime examples. Some public servants are paid to effectively prevent production by excessive and protracted regulation. The growth of this behaviour is the dominant cause of Australia's record increase in NFD.
- 35 Percent Productive (%P)** is the intrinsic value of production by an entity expressed as a percentage of the consumption enabled by the price paid for that production. It is a measure of the extent to which a sector of the economy is overcharging Australians.
- 36 Confidence should not be misplaced.** The politician's skill in inspiring misplaced or unjustified confidence by the people in the economy is a major cause of Australia's debt and the insolvency of Greece and like countries. If confidence is not based on objective truth remedial policies are omitted. Things are as they are - the worse it looks the more likely it is that people will act to improve things.

GFC GLOSSARY

%P	Percent Productive. Intrinsic value of production divided by the price charged for that production.
ABS	Australian Bureau of Statistics.
CIA	Central Intelligence Agency (USA).
Consumption	The use of resources, goods, or services to satisfy wants and needs. At the microeconomic level, consumption is primarily analysed in the context of utility, demand and their importance to market exchanges. At the macroeconomic level, consumption is most important as expenditures by the household sector on gross domestic product, one of four aggregate expenditures (the other three being investment, government purchases, and net exports).
Current acct deficit	An imbalance in a nation's balance of payments current account in which payments received by the country for selling domestic exports are less than payments made by the country for purchasing imports. In other words, imports by the domestic economy are greater than exports. This is generally a not desirable situation for a domestic economy.
Exposed	Vulnerable, open to, subject to, in danger, liable, susceptible.
External Debt	Same as Foreign Debt – but used when referring to another Country.
Foreign Debt	The amount of money owed by a Nation to all other Nations.
Foreign Reserves	The opposite of Foreign Debt.
GDP	Gross Domestic Product.
GFD	Gross Foreign Debt The total amount owed by a Nation to other Nations
Human Capital	The intrinsic value of human beings having regard to the capital value that one would reasonably pay to have the benefit of everything they would produce during the rest of their lives.
IIP	International Investment Position is the difference between capital investment by overseas entities in Australia less our investments overseas.
ML	Merrill Lynch, arguably the world's largest group of financial analysts.
NAG	New Australia Group funded by Colin Ward who ran for the Senate. NAG went through every sector of the Australian workforce as provided by the ABS and asked "Does it produce more than it consumes?" If not the extra consumption is funded by borrowing and flows through to NFD.
National Debt	The accumulated Federal Government Deficits.
NFD	Net Foreign Debt. GFD less loans to other countries.
Non Recourse	A loan where the mortgagee has recourse only against the security property.
NPV	Net Present Value. Financial values brought to the equivalent figure for 2012.
Perfect competition	An ideal market structure characterized by a large number of small firms, identical products sold by all firms, freedom of entry into and exit out of the industry, and perfect knowledge of prices and technology. This is one of four basic market structures. The other three are monopoly, oligopoly, and monopolistic competition. While unrealistic, it does provide an excellent benchmark that can be used to analyse real world market structures. In particular, perfect competition efficiently allocates resources.
Product	A good or service.
Production	The process of transforming the natural resources of the land into consumer satisfying consumption and capital goods using scarce resources. In a world of scarcity, with unlimited wants and needs and limited resources, living standards are enhanced by transforming the planet's raw materials, that don't provide much satisfaction in their natural state, into goods, that provide more satisfaction.
Productivity	Measures the efficiency of production.
Public Debt	Same as National Debt and Government Debt.
Securitisation	A process of pooling mortgages and issuing securities from the pool.
Sovereign Debt	Debt guaranteed by the Federal Government.
SPC	Sub-Prime Crisis. The fraudulent use of derivative securitisation in the US with poor unquantifiable mortgage lending and risk management practices and banking offences

caused the SPC. The credit agencies assessing these mortgage and derivative product risks were a crucial part of the problem.

Trade deficit

Formally termed a balance of trade deficit, a condition in which a nation's imports are greater than exports. In other words, a country is buying more stuff from foreigners than foreigners are buying from domestic producers. A trade deficit is usually thought to be bad for a country. For this reason, some countries seek to reduce their trade deficit by--(1) establishing trade barriers on imports, (2) reducing the exchange rate (termed devaluation) such that exports are less expensive and imports more expensive, or (3) invading foreign countries with sizable armies.

Work

Human effort which produces something of intrinsic value either directly or indirectly. Goods and services are equivalent. Management and entrepreneurial activities are equivalent provided they cause an increase in the production of the entities being managed.

Zero Sum

The sum of all the NFD and NFR is always zero.