Chapter 5

Where to from here? Possible responses to changing funding mix and costs

5.1 Submissions to inquiries into the banking sector generally raise a number of possible regulatory changes or issues that need to be addressed which, in the view of the individual or organisation supporting them, would benefit the system as a whole in some form. This inquiry received a number of specific proposals. Significant and complex issues such as the interaction of superannuation savings with the banking system were also raised. This section examines these matters.

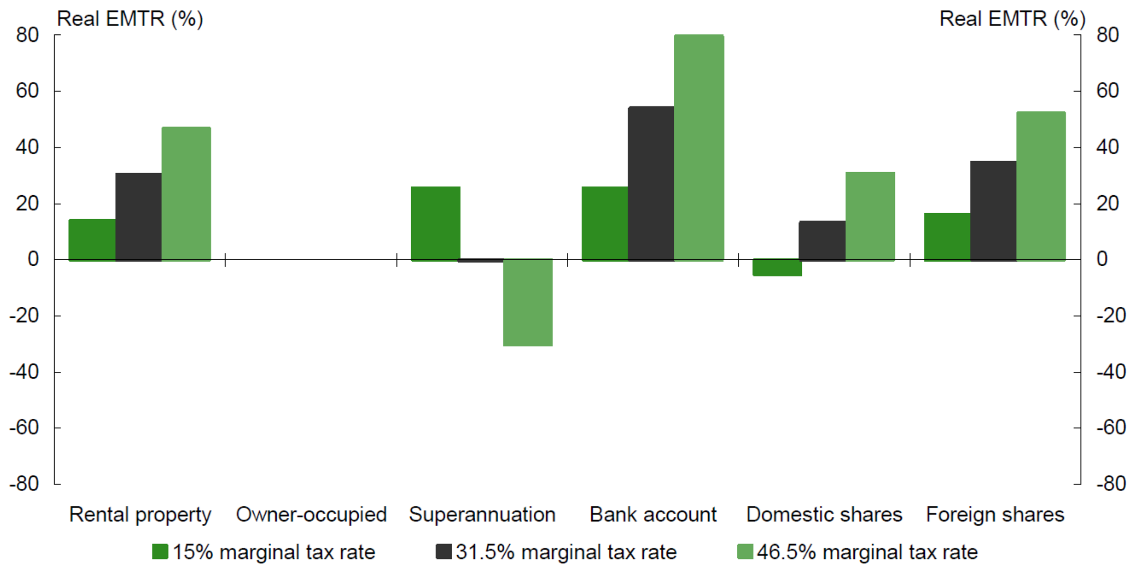
Tax treatment of deposits

5.2 The Henry Review found that tax liabilities for different types of savings vary considerably, noting that the effective tax rate on income from interest-bearing deposit accounts offered by ADIs exceeds a taxpayer's marginal statutory rate. The report argued:

> A tax system for the future would tax these different forms of investment as consistently as possible, and also take account of the way inflation affects the effective tax rate on savings.[1]

5.3 The relatively unfavourable tax treatment of deposits compared to other savings and investments is demonstrated by Figure 5.1.

Figure 5.1: Real effective marginal tax rates on savings depend on asset class



Source: *Australia's future tax system: Report to the Treasurer*, part 2: detailed analysis, vol. 1, p. 67; based on Treasury estimates.[2]

---

1 *Australia's future tax system: Report to the Treasurer*, part 2: detailed analysis, vol. 1, p. 4.

5.4 In the 2010–11 Budget the government announced a 50 per cent income tax discount of up to $1,000 of interest earned by individuals, to commence on 1 July 2011. The policy was subject to a number of revisions; later in 2010 it was announced that the eligible cap would be lowered to $500 for income earned in 2012–13; in 2011 it was announced that it the measure would be delayed until 1 July 2013. Finally, in the 2012–13 Budget the measure was abolished altogether.

5.5 The ABA called for distortions in the tax treatment of various savings options to be minimised so as not to significantly affect an individual's investment decision:

> We would be very keen to see government policy that removes tax distortions against people saving and investing through deposits. At the moment, of course, we are seeing very strong savings rates in Australia and incredibly strong competition for deposits as banks seek to try to minimise that reliance on overseas money. But, in the longer term, Australia does not have a strong record of saving through the banking system and we think part of the answer lies there.[3]

5.6 Abacus expressed a similar view:

> The unfair taxation of deposits must be addressed to reduce pressure on ADI funding costs, to reduce distortions and biases in the taxation of savings, and to ease the burden on Australian households who choose the simplest and safest savings vehicle.[4]

5.7 While deposits are more expensive for banks as a funding source compared to the past decade, and this is currently beneficial for deposit holders, if the higher cost of deposits is sustained it may have an impact on competition in the long-term. The RBA was questioned about how the major banks were able to maintain their net interest margin despite rising funding costs, yet regional banks and credit unions, which source a greater proportion of their funding from deposits, were not able to:

> Dr Debelle: The regional banks, and particularly credit unions and the like, have a much larger share of their funding coming from deposits.

---

2 Notes: Real effective marginal tax rates show the tax levied on the normal real return to saving, and reflect the tax treatment of the income from which savings are made (where it deviates from tax payable if that income had been immediately consumed), earnings on those savings, and the final use of the accumulated savings. A zero effective tax rate corresponds to an expenditure tax benchmark, with the investment funded out of post-tax wages, and earnings and the subsequent realisation of the investment untaxed. The negative rate for superannuation reflects the reduction in tax otherwise payable on wages by making contributions out of pre-tax income. The estimates do not model interactions with the transfer system. Assumptions: 6 per cent nominal return; 2.5 per cent inflation; for rental property, 50 per cent of the return is attributable to capital gain and 50 per cent to rental income and the rental property is held for seven years then sold; shares are held for seven years then sold; superannuation is held for 25 years and the individual is eligible for a tax-free payout at the end of the period.

3 Mr Steven Münchenberg, Chief Executive Officer, Australian Bankers' Association, *Committee Hansard*, 8 August 2012, p. 15.

4 Abacus-Australian Mutuals, *Submission 150*, p. 7.

> Particularly over the last year or so, the competition in the deposit market has been pretty intense, so the relatively high cost of deposits has a bigger effect on someone who uses more deposits to fund themselves, which is the regionals and the credit unions.
>
> CHAIR: That makes sense. Their costs have gone up by more, but they have not been able to maintain their net interest margins. The large banks' costs have also gone up, but they have been able to maintain their net interest margins.
>
> Dr Debelle: Because over that period they potentially had other sources of funding which have not gone up as much as deposit costs have gone up.
>
> CHAIR: So that is the answer? They have a degree of market power that enables them to maintain their profits?
>
> Dr Debelle: No. As I said, there is plenty of competition in deposit rates. They pay varying amounts, but they are all pretty much paying the same amount. In the lending rates, again, there is not much variation between all the lenders. It just matters if you have more deposits in your funding base as to whether that means your costs are relatively high.
>
> …
>
> CHAIR: So if there is a competitive impact at play, it is probably forcing those banks that have the higher funding costs to have a lower net interest margin whilst the others can maintain theirs at the level they have because they have a lower cost base?
>
> Dr Debelle: Yes. That is not a bad way of putting it.[5]

Committee view

5.8 The higher than usual interest rates on term deposits and to a lesser extent other savings products (relative to other benchmark rates) that the banks have been offering since the global financial crisis is good news for deposit holders, although some of the costs are ultimately passed on through other banking activities, such as lending.

5.9 The degree to which different banks, depending on their size, are able to address these developments without impacting their profitability is an issue that the committee has been concerned with from a competition viewpoint. The committee examined this issue in the report of its 2011 Competition Inquiry. It concluded that the taxation arrangements applied to bank deposits and mutual ADI deposits should be reviewed by a broad-ranging inquiry into the financial system. In the committee's view, nothing has alleviated the committee's earlier concerns. Encouraging domestic deposits would provide banks with a larger source of stable funding, reducing some of the risk from sourcing funds from unstable international wholesale debt markets. Further, an increased pool of deposits may help alleviate any long-term competition

---

5 Dr Guy Debelle, Assistant Governor, Financial Markets, RBA, *Committee Hansard*, 9 August 2012, p. 38.

implications arising from the major banks encroaching on a funding source relied on by smaller ADIs.

Recommendation 5.1

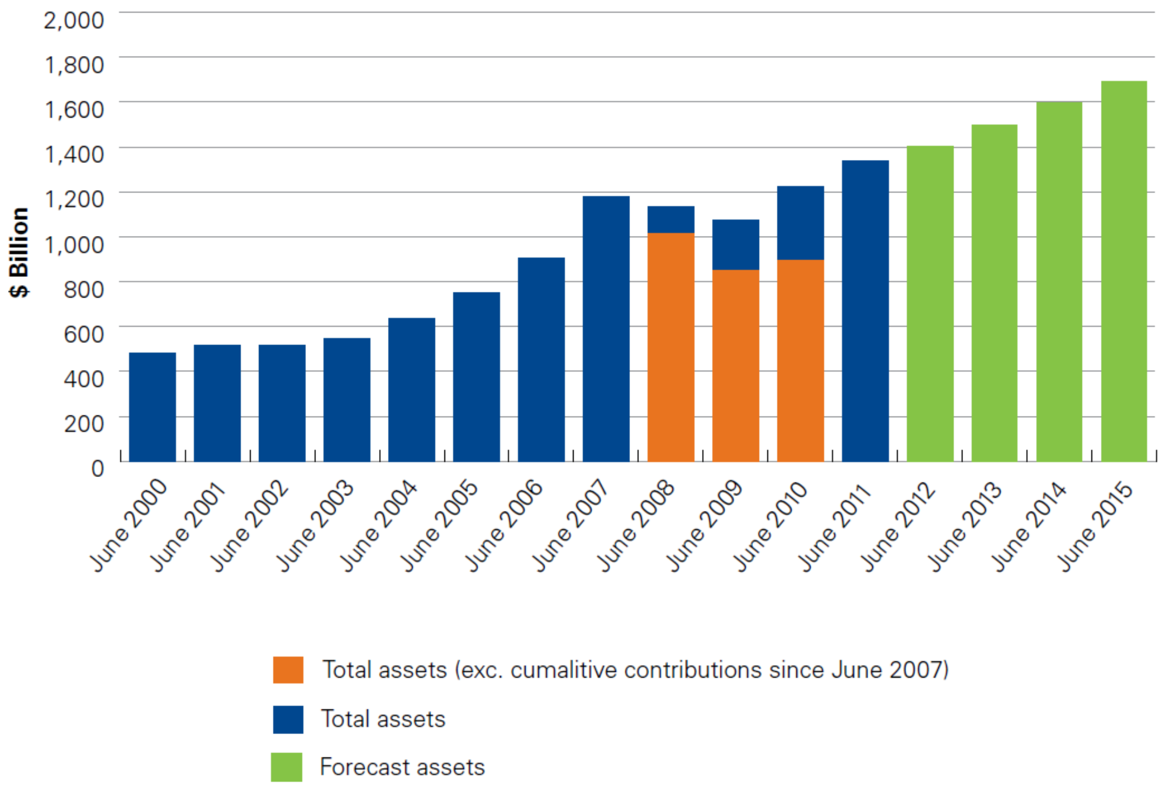
5.10 Inconsistencies between the taxation arrangements applying to interest earned by individuals on deposits held in authorised deposit-taking institutions compared to other methods of saving should be addressed.

Interaction of the superannuation and banking systems

5.11 Australia has substantial domestic savings within the superannuation system. While some of these savings return to the banking system through the investments made by superannuation funds, banks remain significantly reliant on offshore borrowing in volatile wholesale debt markets. Whether there are changes that could be made to encourage additional superannuation savings to be directed towards the banking system in a way that helps meet the banks' funding needs was an issue discussed.

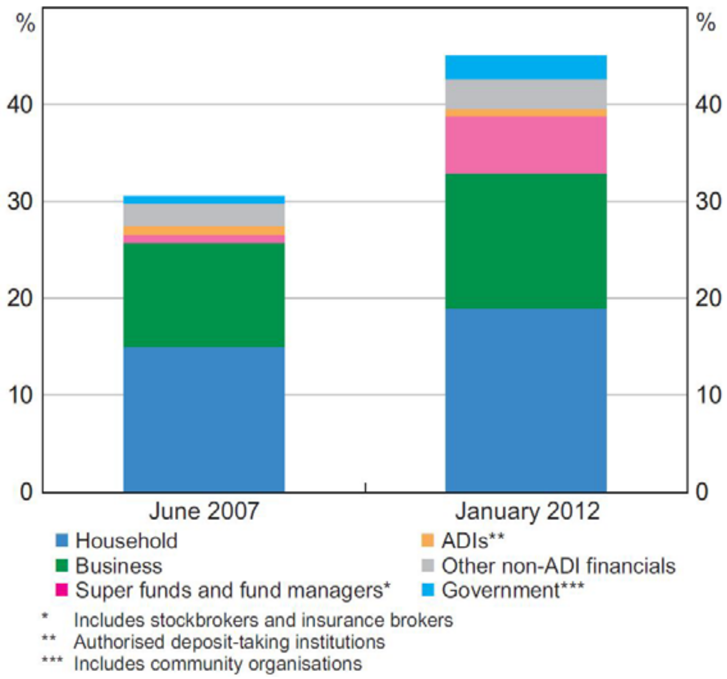
5.12 It is an interesting time for this discussion, as superannuation assets have grown significantly and will grow at an increased rate in the coming years due to the gradual increase in the superannuation guarantee (from nine per cent to 12 per cent by 2019–20 starting from 2013–14) (see Figure 5.2). Depending on the future average propensity to save among households and the attractiveness of other savings vehicles, this could place pressure on the level of deposits while, at the same time, banks will need to rely on more stable funding sources such as deposits due to Basel III. The degree to which deposits will be able to meet the banks' requirements will be impacted by the behaviour of household and superannuation funds—while households are currently risk-averse and deposits are an attractive investment option, an improvement in economic sentiment could change this. Superannuation funds are also investing in term deposits at a heightened level at the moment (Figure 5.3), however, the extent to which this will be sustained is unclear.

Figure 5.2: Total superannuation assets



Source: KPMG and Australian Centre for Financial Studies, *Superannuation trends and implications*, November 2011, p. 5; cited in Australian Centre for Financial Studies, *Submission 49*, p. 15. Based on APRA data.

Figure 5.3: Term deposits with banks in Australia (as a percentage of total A$ domestic deposits)



Source: Cameron Deans and Chris Stewart, 'Banks' Funding Costs and Lending Rates', *RBA Bulletin*, March 2012, p. 38; based on data from APRA.

5.13 Abacus predicts that:

> Competition for deposits will intensify further when the current period of global instability and uncertainty comes to an end. Households and other savers will look to alternatives to deposits that are more favourably taxed, such as equities and superannuation.[6]

5.14 The ABA observed that while the level of savings is relatively high at the moment, from a long-term perspective 'Australia does not have a strong record of saving through the banking system'. It argues that 'appropriate ways' of encouraging some superannuation savings into the banking sector need to be examined as the superannuation sector is more inclined towards investing in equity compared to deposits and other fixed income securities:

> We know that the Australian super industry for whatever reason is heavily weighted towards equities by international comparison and underweight things like fixed income products. Were super funds to invest in some of those products, it would mean money flowing through the banking system into the economy rather than chasing further returns in the equities markets here or overseas. What we are not suggesting in any way is that the trustees of those super funds be under any direction or requirement to do that.[7]

5.15 Some banks are already coming up with ways to utilise superannuation savings to meet their funding needs; at its hearing in August 2012 ING Direct advised the committee that it would enter the market by launching a basic superannuation savings product (which it did in September).[8]

Corporate bond market

5.16 In Australia, companies have been inclined to turn to banks for funds rather than to issue bonds. This increased during and since the global financial crisis when many companies found accessing funds through bond issuance too difficult or costly.[9] The corporate bonds that are issued are generally in overseas markets. The Australian Financial Markets Association (AFMA) advised that at the end of March 2012, $146 billion in bonds were on issue in those overseas markets. The AFMA gave some insight into where these issuances were targeted and why:

> The US private placements market is particularly attractive to Australian companies and an important source of finance to them because it has good

---

6 Abacus-Australian Mutuals, *Submission 150*, p. 6.

7 Mr Steven Münchenberg, Chief Executive Officer, Australian Bankers' Association, *Committee Hansard*, 8 August 2012, p. 16.

8 Mr Vaughn Richtor, Chief Executive Officer, ING Bank (Australia), *Committee Hansard*, 10 August 2012, p. 30.

9 Susan Black, Anthony Brassil and Mark Hack, 'Recent Trends in Australian Banks' Bond Issuance', *RBA Bulletin*, 2010, no. 1 (March), p. 28.

> liquidity, long dated debt finance is available and deals may be brought to market quickly.[10]

5.17 A number of submitters called for the development of a stronger corporate bond market in Australia. The ASF argued that such a market could potentially reduce the banking system's reliance on offshore funding, thus insulating 'to some degree, Australia's vulnerability to shifts of sentiment amongst offshore investors'.[11] This is linked to the superannuation system as, assuming the bonds are attractive to the superannuation funds, they could invest in these bonds rather than offshore investments and equity. NAB explained that, rather than lending directly to large Australian corporations, if it could lead them to a developed Australian bond market with superannuation funds willing to invest in the bonds, it would 'not put stress on the bank balance sheets'.[12] NAB also contended that Australia's superannuation is 'poorly allocated at the moment':

> … arguably, by international standards, typically at least 50 per cent of superannuation money should be in fixed income securities like bonds, government securities and the like. In Australia it is not—the vast majority is in equities.[13]

5.18 As Professor Davis put it in a March 2012 article:

> On the one hand, almost everyone seems to support initiatives to develop a local corporate bond market to broaden corporate funding sources. On the other, almost everyone believes that super funds have an excessive equity bias and need more fixed interest (bond) investments.[14]

5.19 However, Professor Davis noted some issues that, in his view, would impede the development of a stronger corporate bond market in Australia:

> If banks focus more on leading corporates to the debt markets rather than on-balance sheet lending, their funding requirements also decline. One possible adjustment process could be reduced bank reliance on international capital markets, with more of our balance of payments financing involving direct foreign purchase of Australian assets such as equities. While that might help super funds reduce their equity bias, it is only one among a wide range of adjustment possibilities (about which we understand relatively little).

---

10 Australian Financial Markets Association, *Submission 87*, p. 6.

11 Australian Securitisation Forum, *Submission 150*, p. 7.

12 Mr Mark Joiner, Executive Director, Finance, National Australia Bank, *Committee Hansard*, 10 August 2012, p. 67.

13 Mr Mark Joiner, National Australia Bank, *Committee Hansard*, 10 August 2012, p. 68.

14 Kevin Davis, *Can a Corporate Bond Market solve the Super Equity Bias?*, 19 March 2012, www.australiancentre.com.au/publications-and-articles/2012/03212012-davis-corporate-bond-market-super-equity-bias-commentary.pdf (accessed 13 September 2012), p. 1; cited in Australian Centre for Financial Studies, *Submission 49*, p. 7.

> Another possibility could be less bank reliance on domestic term deposits, with investors switching from deposits to corporate bonds. And here is a real killer in terms of the much desired retail corporate bond market. What yield must be offered to individual investors (including self managed super funds) to encourage them to invest in risky corporate bonds rather than bank deposits which are guaranteed up to $250,000 at each bank.[15]

5.20 The 2009 Johnson Report recommended that regulatory requirements on corporate debt issuance to retail investors be reduced. It concluded that a deeper domestic corporate bond market would improve the diversity of potential funding sources for companies and place added competitive pressure on banks as a source of corporate finance.[16] Since that report, there have been some policy announcements regarding the development of a bond market—as part of the 2010 *Competitive and Sustainable Banking System* package, the government announced that it would streamline disclosure requirements and prospectus liability regulations.[17] However, the steps to implement this have taken some time. In December 2011, a year after the initial announcement, a discussion paper was released by Treasury on streamlining disclosure and liability requirements.[18] Submissions closed in February 2012.

Committee view

5.21 That Australian banks need to obtain a significant share of their funding from volatile offshore wholesale debt markets when Australia has substantial, and growing, savings in its superannuation system is a curious aspect of the financial system. Attempts to influence this apparent imbalance must be carefully considered. Superannuation trustees need to make investment decisions that are in the best interest of the funds' members. The committee supports measures to encourage the growth of a more diverse range of attractive domestic investment options, such as the regulatory changes underway to help facilitate a deeper and more liquid corporate bond market. However, the committee considers that the interaction of the superannuation system and the banking system warrants further consideration. This issue is discussed further

---

15 Kevin Davis, *Can a Corporate Bond Market solve the Super Equity Bias?*, 19 March 2012, www.australiancentre.com.au/publications-and-articles/2012/03212012-davis-corporate-bond-market-super-equity-bias-commentary.pdf (accessed 13 September 2012), p. 2; cited in Australian Centre for Financial Studies, *Submission 49*, p. 7.

16 Australian Financial Centre Forum, *Australia as a financial centre: Building on our strengths*, November 2009, p. 40. The report also noted that a deeper corporate bond market could assist financing of large scale, long-term infrastructure projects.

17 Australian Government, *Competitive and Sustainable Banking System*, December 2010, p. 24. The government also announced that it would facilitate the trading of Commonwealth Government Securities (CGS) on a securities exchange. Legislation to facilitate CGS retail trading was introduced in June 2012 (Commonwealth Government Securities Legislation Amendment (Retail Trading) Bill 2012). In July 2012 ASIC released a consultation paper on market integrity rules for the CGS retail trading.

18 See www.treasury.gov.au/ConsultationsandReviews/Submissions/2011/Development-of-the-Retail-Corporate-Bond-Market-Streamlining-Disclosure-and-Liability-Requirements.

in chapter 10, which examines whether a broad-ranging independent inquiry into the banking system is required.

Interest withholding tax

5.22 Another issue also examined by the 2011 Competition Inquiry was interest withholding tax, and the implications this has for competition in the banking sector. Interest withholding tax is a tax levied on interest paid by an Australian borrower to a non-resident lender. The tax is particularly relevant to bank funding costs and competition in the banking sector as it applies to interest paid by Australian subsidiaries of foreign financial institutions when they borrow money through their offshore parent and use that money in Australia.

5.23 Both the Henry Review and the Johnson Report recommended that financial institutions operating in Australia should generally not be subject to interest withholding tax on foreign raised funds. The Johnson Report observed that the application of the tax on offshore borrowing by financial institutions:

> … sits uneasily with the Government's desire to develop Australia as a leading financial centre and is putting Australia at a competitive disadvantage with respect to overseas financial centres, which increasingly do not charge interest withholding tax on such transactions.[19]

5.24 The government has announced changes to the application of interest withholding tax, but they have not yet been implemented. In the 2010–11 Budget it was announced that interest withholding tax on financial institutions would be phased down from 2013–14.[20] In November 2011, however, the government announced that this would be deferred until 2014–15.[21]

5.25 ING Direct argued that interest withholding tax inhibits its ability to bring an offshore pool of funds into Australia in a more cost-effective manner:

> Mr Richtor: … one of the challenges is that if we look to the offshore capital markets, unless we meet certain strict conditions, if we bring the funds back in we have to pay withholding tax, which makes it unattractive for somebody to lend us those funds. Basically, we have to go out to funds that are capable of wide distribution—and, forgive me, I have forgotten the detail of this—whereas there are many investors who would happily give us money but they are not going to wear the withholding tax. If we pay the withholding tax—and I think that is the same for all banks; it is not just for

---

19 Australian Financial Centre Forum, *Australia as a Financial Centre: Building on our Strengths,* November 2009, p. 68.

20 As announced in the 2010–11 Budget, the tax rate applying to foreign bank branches would be reduced from the five per cent to 2.5 per cent in 2013–14 and to zero from 2014–15. The rate for other financial institutions would be reduced from 10 per cent to 7.5 per cent in 2013-14 and to five per cent from 2014–15, with an aspirational target of zero. See Australian Government, *2010–11 Budget: Budget paper no. 2,* pp. 43–44.

21 Australian Government, *Mid-year economic and fiscal outlook 2011–12,* p. 166.

> us, it is more of an Australian issue—then of course it is much more expensive.
>
> Mr Baker: The key point that we would just add is that there are means. There is the section 128F exemption that allows us to do wide distribution debt issues, but it is the rule that inhibits associates from giving you funds. That is the block that puts the inability to bring ING funds from other jurisdictions into Australia.
>
> Senator WILLIAMS: So if you go to do that you have to pay the withholding tax.
>
> Mr Baker: That is right, yes.[22]

Committee view

5.26 Interest withholding tax distorts funding decisions and is an impediment to foreign banks competing in the Australian banking sector. Although removing this tax from applying to financial institutions creates a direct financial cost to the government, by providing an impetus for greater competition in the banking sector such a reform would have wider benefits to the economy. Accordingly, the committee supports the removal of interest withholding tax applying to foreign bank branches and other financial institutions, although it acknowledges that such action would need to be sensitive to budgetary circumstances.

Recommendation 5.2

5.27 That interest withholding tax applying to financial institutions be abolished as fiscal circumstances permit.

The Canadian securitisation model

5.28 Non-banks have previously played a key role in injecting competition into the market for residential lending. As discussed in chapter 2, one of the results of the global financial crisis is the significantly diminished market share that non-bank lenders now have. To address this development, the MFAA called for the securitisation market to be supported in a way similar to the model adopted in Canada and administered by the Canada Mortgage and Housing Corporation (CMHC)[23]:

> The Australian Government, if it is serious about attacking the hard issues, must closely examine the success and characteristics of the Canadian

---

22 Mr Vaughn Richtor, Chief Executive Officer; Mr Glenn Baker, Chief Financial Officer, ING Bank (Australia) Ltd, *Committee Hansard*, 10 August 2012, p. 36.

23 The CMHC was created in 1946 to house returning war veterans and to lead Canada's social and rental housing programs. It currently has three broad objectives: (1) help Canadians in need; (2) facilitate access to more affordable, better quality housing for all Canadians; and (3) ensure the Canadian housing system remains one of the best in the world. See Canada Mortgage and Housing Corporation, 2012–2016 Summary of the corporate plan, www.cmhc-schl.gc.ca/en/corp/about/anrecopl/upload/2012-2016CPSCMHC_E.pdf (accessed 3 September 2012), p. 3

> Mortgage and Housing Corporation's securitisation programs, viz Mortgage backed Securities and Canadian Mortgage Bonds. These programs provide a proven efficient and effective template for competitively priced mortgages, whose features should be incorporated into the Australian mortgage market.[24]

5.29 The CMHC undertakes two securitisation programs under its mission to promote housing quality, affordability and choice for all Canadians. The first program, National Housing Act Mortgage-Backed Securities (NHAMBS), commenced operation in 1987. As its name suggests, the program follows the passage of the National Housing Act (in 1985) which was during a period of high interest rates and associated concerns about housing affordability. The NHAMBS program was intended to respond to these high interest rates, instability of rates and the prevalence of one year mortgages.[25] The second program is the Canada Mortgage Bonds (CMB) program, which was introduced in 2001. As CMBs are bullet bonds,[26] it was intended that CMBs would be a more attractive option for investors than NHAMBS instruments.[27] The proceeds of the bonds are used to purchase mortgage backed securities issued under the NHAMBS.

5.30 Both securitisation programs provide a guarantee to investors, ultimately backed by the Canadian government, that payments of interest and principal will be timely. As the MFAA explained, the government guarantee lends the sovereign rating to the instruments (currently AAA) and for this guarantee, the government profits through the premium charged:

> Mr Naylor: The key feature is that the government guarantees it. The funds that go into the securitised system in Canada have a AAA rating. They produce funds that are lower than any other source of funding except for the price of deposits in Canada. So they are lower than what we have heard many times from the banks in the global wholesale lending market. The margins are much lower. They produce a benefit to investors, because they are pretty close to guaranteed—they are very low-risk investments—and they produce a surplus for the government.
>
> Senator WILLIAMS: Just to add to that, at what cost to government would that come at—to do what you just suggested in terms of the Canadian model?

---

24 Mortgage and Finance Association of Australia, *Submission 52*, p. 2.

25 KPMG, *Canada Mortgage Bonds Program evaluation: Final report*, June 2008, www.cmhc.ca/en/hoficlincl/in/camobo/upload/CMB-Evaluation-Jun08.pdf (accessed 3 September 2012), p. 7.

26 Bullet bonds are debt instruments that cannot be redeemed prior to maturity. The face value of the bond is paid on the maturity date, rather than a series of payments occurring over several dates.

27 KPMG, *Canada Mortgage Bonds Program evaluation: Final report*, June 2008, www.cmhc.ca/en/hoficlincl/in/camobo/upload/CMB-Evaluation-Jun08.pdf (accessed 3 September 2012), p. 9.

Mr Naylor: The government makes a profit out of it.[28]

5.31 The MFAA provided further evidence on how aspects of the programs, including risk, are managed:

> They have a reverse auction so they say, 'We have $25 billion in the pool' and they invite people to tender for it. The big banks, the small banks and the non banks can all tender for it. There are a lot of requirements around the integrity of the process. No one lender can access more than 25 per cent of the pool so that means the smaller guys can get a chop at it. I think the minimum tender has to be $20 million … This is not a free handout. You have to be able to show that you are part of the system, that you have skin in the game so that you are assuming some of the risk. If you are interested, there are reams and reams of rules about how the system works and the type of loan that is acceptable, who can invest and all that sort of stuff.[29]

5.32 The Canadian approach to securitisation may be particularly instructive given the similarities in the Australian and Canadian economies and financial sectors, such as the similar population size, number of major banks and size of the mortgage market, as well as that the banking sectors of both countries avoided the worst of the global financial crisis.[30] While the MFAA is strongly supportive of such schemes being adopted in Australia, others are less sure. Professor Davis argues:

> I would suggest that we should stay away from it, because it involves governments providing guarantees in various forms. The Canadian system is a very complex one, as far as I can see—it is not simple. And I think the last thing governments should be getting into is providing guarantees. It is very hard to price them, and very hard to operate them, I think. So I think there are other ways in which we could get the securitisation industry back into a better position to provide greater competition in the housing market than going down that route.[31]

5.33 In 2009, Treasury noted that a Canadian-style program 'could potentially enhance smaller lenders' access to funds', however it balanced this view with the following statement:

> However, it is not clear that such an intervention would necessarily result in substantially greater choice and lower interest rates for mortgage borrowers,

---

28 Mr Phil Naylor, Chief Executive Officer, Mortgage and Finance Association of Australia, *Committee Hansard*, 8 August 2012, p. 30.

29 Mr Phil Naylor, Mortgage and Finance Association of Australia, *Committee Hansard*, 8 August 2012, p. 34.

30 Mortgage and Finance Association of Australia, *Submission 52*, p. 20.

31 Professor Kevin Davis, Australian Centre for Financial Studies, *Committee Hansard*, 8 August 2012, p. 43. In its submission, the Australian Centre for Financial Studies also argues that it would be unlikely to easily achieve "fair pricing" of the government guarantee; *Submission 49*, p. 12.

> or that the benefits of the proposal would outweigh the associated risks and costs.[32]

5.34 The RBA expressed similar reservations, noting that the mortgage market in Australia is 'reasonably competitive at the moment' and advising the committee that it was aware of issues being raised about the Canadian programs:

> Dr Debelle: … The Canadians at the moment are dealing with a situation where they are a bit concerned about where their housing market is going, particularly in terms of the lending side of things. So that might be a reasonable test of the resiliency of the system they have had, over the next couple years.
>
> Senator CAMERON: On the up side or the down side?
>
> Dr Debelle: On the up side.
>
> Mr Aylmer: In fact, they are concerned about the exposure of taxpayers, now, to the Canada Mortgage and Housing Corporation, because it is a government financed thing.[33]

Committee view

5.35 While it is desirable for the securitisation market to be reinvigorated to enhance competition in the sector, the committee is aware that a Canadian-style scheme would be a significant change to the Australian banking sector; and one that would commit the government to be involved in the securitisation market on an ongoing basis. The committee is particularly concerned about the transfer of risk from the private sector to taxpayers.

5.36 The committee is not dismissing the scheme entirely, as the Canadian scheme has apparently operated effectively for some time. In the report of its 2011 Competition Inquiry, this committee recommended that further research be done into how the Canadian model could be applied in Australia so that it could be implemented quickly in case of future deterioration in the securitisation market. At this time, the committee maintains this view. The potential benefits and costs of such a scheme would need to be closely examined, and this could perhaps take place as part of a broad-ranging inquiry into the financial sector.

---

32 Treasury, *Submission 167* to House of Representatives Standing Committee on Infrastructure, Transport, Regional Development and Local Government's inquiry into the impact of the global financial crisis on regional Australia, August 2009, p. 8. As at February 2011, this submission still reflected the views of Treasury (which directed this committee to this submission during the Competition Inquiry); see Treasury, answer to question on notice, Competition Inquiry, no. 14, 4 February 2011, pp. 3–4.

33 Dr Guy Debelle, RBA, *Committee Hansard*, 9 August 2012, p. 44.

Other securitisation issues

5.37 The Australian Securitisation Forum (ASF) advised the committee that demand among investors for Australian securitisation has been impacted by changes in the attitude of central banks in key jurisdictions towards what securities are eligible for repo operations.[34] The ASF advised that up until 2010 the European Central Bank (ECB) accepted Euro-denominated bonds collateralised by Australian assets (such as RMBS), but since then the ECB has restricted eligible bonds to those where the collateral is from Europe or G8 countries outside Europe.[35]

Committee view

5.38 Investor demand and the liquidity of Australian asset-backed securities could be enhanced if foreign currency bonds collateralised by Australian assets were "repo-eligible" in foreign jurisdictions. While this is a matter for the central banks concerned, the government could push for wider acceptance of Australian securitisation.

Recommendation 5.3

5.39 To enhance investor demand for Australian securitisation, the committee recommends that the government encourage central banks in other jurisdictions to accept Australian asset-backed securities denominated in foreign currencies for repurchase agreements in the foreign jurisdiction.

---

34 Repurchase agreements (commonly shortened to 'repos') involve the sale or purchase of securities with a commitment to reverse the transaction at an agreed date in the future and at an agreed price. The RBA uses repos to conduct its domestic market operations (i.e. to ensure that the actual cash rate is close to the target cash rate).

35 Australian Securitisation Forum, *Submission 153*, p. 7.