Senate Standing Committee on Economics

ANSWERS TO QUESTIONS ON NOTICE

Treasury Portfolio

Additional Estimates

13 – 14 February 2013

Question: **AET 2-6**

Topic: **Banks Exposure**

Written: **Received from Committee – 14 February 2013**

Senator WILLIAMS asked:

2. The four major banks would appear to be very vulnerable to a run on funds, if the figures for liquidity (liquid assets to domestic liabilities) are only 16.9% and where 56% of the deposits are a call (only 44% of the deposits are for fixed terms).

   Given that 2 to 3% of total gross loans and advances are credit cards loans, and that additional secured loans are made by four major banks, how can 4.8 to 5.9% tier 1 capital be sufficient to protect the Australian investor and Federal Governments guarantee?

3. How exposed are the four major Australian banks' lending books in an economic climate where properties devaluing (in some places significantly up to 50%) and where 41% of total loan approvals were 60 to 80% LVR, and 33% of loans were greater than 80% LVR?

   Surely these statistics provided by APRA from last year's Senate estimates would promote great concern for APRA and what measures are APRA putting in place to reduce risk exposure of out banks?

4. Why doesn't APRA collect data on all unsecured lending by the banks, where it is surely a measure of risk exposure?

5. Given that the Australian banks have been offered a government guarantee for the investor deposits, how is APRA intending to shorten the exposure of that government insurance policy?

6. The Council of Financial Regulators are responsible for making recommendations as to which financial institutions should receive a government guarantee for investor deposits. As a member of that council, why does APRA not recommend to extend the government guarantee to those finance companies such as secured not issuing companies that on the face of it, would appear to be less risky than the banks?

a. Particularly those companies that have no exposure to development loans and low tolerance to non-performing loans and doubtful debts?

Answer:

2. Adequacy of liquidity. Australian banks are currently meeting APRA's prudential requirements for liquidity. Consistent with the Basel Committee's global reforms, APRA considers that it is appropriate that banks in future meet more conservative liquidity requirements. APRA has been consulting with industry on the implementation of the new global liquidity standard, and further consultations are planned. In the interim, APRA considers that Australia's banks are conducting reasonably prudent liquidity management policies.

In addition to 'on-balance sheet' liquidity, authorised deposit-taking institutions (ADIs) typically have access to liquidity support from the Reserve Bank of Australia, in times of market stress.

Adequacy of capital. The soundness of Australian Banks is assessed by credit rating agencies and global investors as among the strongest in the world. Capital ratios, the quality of capital and of assets, and bank profitability, are strong. Consistent with the Basel Committee's global reforms, APRA has introduced Basel III upgrades to capital requirements for ADIs, which will underpin a moderate increase in major bank capitalisation over the medium term.

3. APRA has stress tested Australian banks' resilience to home loan adversity. The results of these stress tests indicate that the banking system generally and Australian ADIs individually could be expected to survive any 'reasonably foreseeable' combination of increased default rates on home loans and declines in residential property prices.

4. APRA's capital requirements for ADIs outside residential property lending are not directly tied to loan security arrangements. Although more information on loan security status would be of prudential interest, APRA needs to balance safety and efficiency in its statistical collections. With major banks currently reporting approximately 8,000 data items each, APRA considers that its collections are reasonably complete for prudential purposes.

5. The general answer is that all of APRA's regulatory and supervisory efforts are focussed upon, to the extent reasonably possible, reducing the risk of regulated entities failing. Should an ADI fail and the Financial Claims Scheme (FCS) be invoked, the first call on any FCS funding will be on the failed ADI's assets, on the basis that non-protected creditors and capital providers are junior to the FCS liability. APRA's expectation is that any FCS payments would likely be resolved from liquidating the assets of the failed entity, without further recourse. However, if the failed entity's resources are inadequate to cover FCS payments, then a levy on the ADI industry may be applied to make up any shortfall.

   The Government will only need to make a net FCS payment in the combined event that:

   (a) one or more ADIs fails;
   (b) the failed entity's assets are insufficient to cover the FCS claim, which is senior to other creditor claims; and
   (c) any resultant shortfall is not made up from an industry levy.

6. and 6a. The FCS applies only to ADIs which are prudentially supervised by APRA. It is a matter for Government whether guarantees should be provided to non-supervised entities.