

**Inquiry into Aspects of Bank Mergers
Senate Standing Committee on Economics**

Committee Secretary
Senate Standing Committee on Economics
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Canberra ACT 2600
Australia

Dr David Morrison (1)

Dear Sir/Madam

The following is submitted in relation to the Inquiry into Aspects of Bank Mergers. I have had the benefit of reading submission numbers 1-14 set out at the Standing Committee website:
http://www.aph.gov.au/senate/committee/economics_ctte/bank_mergers_08/submissions/sublist.htm

Introduction

Banks are those defined by the *Banking Act* and are distinct from non-bank financial institutions and other bodies that offer deposit and lending services within the market place. In Australia the difficulty is that we have very few banks in number as compared with other countries, the number never having exceeded 60 as compared with the United States where, population differences notwithstanding, the number of banks reached 14,500 in the 1980s. It therefore follows that Australians wanting to deal with banks don't have a lot of choice and this in turn suggests that fewer offerings are made in terms of the diversity of services and prices that might otherwise be made. Whilst it does not necessarily follow that Australian banks offer an inferior or more expensive service relative to economies where there are more banks, it may certainly be implied that such behaviour is likely where competition is less fierce. This is good news for bank shareholders however it comes at the expense of bank customers.

Further, Australia does not have a truly deregulated banking system, notwithstanding wide attribution of this apparent fact. (2) Deregulated banking would mean just that. In fact Australia has a complex array of laws that govern and influence the conduct of banking practice, including remarkably significant barriers to entry in the form of *inter alia* capital requirements that preclude interested persons with relevant expertise from establishing and carrying on the business of banking in this country. The barriers to entry limit the number of banks able to be established within Australia and that in turn limits

the competitive forces that might otherwise exist as between an increased number of banks offering services.

The major four banks in Australia operate within an oligopoly that allows for remarkable bank profit, current financial conditions notwithstanding and, no doubt in part due to a lack of competition that has allowed cost-cutting in various forms including a diminution of the number of bank branches by half in the past 40 years. Presumably in order to prevent the market from becoming highly oligopolistic, there are various measures in place, most notably the so called 'four pillars policy' that attempts to ensure that the already strong major banks do not move to an almost monopolistic position within the sector. The former governor of the Reserve Bank of Australia, Ian Macfarlane takes the view that the policy has also gone some way to protecting the industry within Australia from the full impact of the global financial crisis by preventing "a destructive form of competition" due to the big four banks not being able to merge. (3) This may be so however it seems more likely that the role of the Australian banking system in not taking a larger role in the global financial crisis is because the regulatory requirements around capital adequacy and a lack of funds (deposits) held by Australian banks (relative to loans) precluded greater and more damaging participation.

In any event, it seems clear that the paucity of banks as competitors within Australia means that there is reduced competition, by definition compared with a truly deregulated market and by comparison with offshore markets. Any inquiry into aspects of mergers therefore ought to start with the state of play and be cautious of the assumptions that are easily and generously made about the state of competition within the Australian banking market.

The economic, social and employment impacts of the recent mergers among Australian banks

Whilst there is some information published at the APRA site (4), there is very little real information around the sector that allows for informed public comment. Clearly there is a great need for information to be publicly available and to be commented upon. The lack of response to this inquiry suggests either that there are no problems at all or more likely that any dissatisfaction is difficult to back up with data. Incomplete data makes it very difficult to comment specifically on the questions that have been posed by the Committee and therefore one may only opine. Whilst somewhat informative, the lack of comment and information generally available means that this is not the most productive means to answer the questions posed.

The measures available to enforce the conditions on the Westpac Banking Corporation/St George Bank Limited merger and any conditions placed on future bank mergers

The capacity for the Australian Competition and Consumer Commission to enforce divestiture in the banking sector if it finds insufficient competition

The adequacy of section 50 of the Trade Practices Act 1974 in preventing further concentration of the Australian banking sector, with specific reference to the merits of a 'public benefit' assessment for mergers

These questions are very difficult to answer. Section 50 of the *Trade Practices Act* might be said to be working perfectly adequately since there are few cases around mergers. The alternate view is that the provision is relatively weak and that weakness accounts for its operation. In any event, the process of evaluation whereby banks seek to merge is mysterious and in the absence of clear published data and decision making procedure will remain so. The difficulty appears to be in striking a balance in keeping highly sensitive proprietary information confidential as against achieving the aims of the *Trade Practices Act* generally. The question of the relative importance of stakeholders is clouded by the very lack of competition in the Australian banking market and therefore it is very difficult, in the absence of data, to precisely answer the questions posed.

The impact of mergers on consumer choice

Where customers are presented with fewer choices, it seems unlikely that they will properly understand the dimension of that lack of choice – there is nothing to compare against. Even customers, who have lived in different jurisdictions and have witnessed increased customer choice, can do little about banking services if they choose to live in Australia. Fewer competitors mean less competition and it follows that where competition is lessened that there is little incentive to offer greater choice to an existing and guaranteed customer base. This is the clear position of the banks within Australia.

The extent to which Australian banks have 'off-shored' services such as credit card and loan processing, information technology, finance and payroll functions

The impact 'off-shoring' has on employment for Australians

This is simply an example of cost-cutting and it is difficult to see how that ought not to be available to all businesses (banks included), unless it presents a threat of some kind to the particular business. It may have an impact on reducing customer service and satisfaction; however compared to a lack of choice generally as between banks, it does not appear to be the central issue. Cost cutting gives rise to job losses, whether those jobs are replaced by others or different opportunity for the economy as a whole is the key question, rather than a focus upon a particular job that is lost. The global financial crisis will see continued sovereignty behaviour on the part of governments and business, including banks. It might therefore follow that there is a reverse of such practices for those reasons. This is a question that cannot be precisely answered with the data available, except in relation to those employed by specific banks.

Alternative approaches to applying section 50 of the Trade Practices Act 1974 in respect of future mergers, with a focus on alternative approaches to measuring competition

Competition is difficult to measure. Bodies such as the ACCC are only able to respond within the framework of the enacted legislation and government policy. It is very difficult to understand how the ACCC might be an effective monitor on bank business competitiveness, where the four-pillar status quo is taken as a given. If this must be so then it is vital that more information is available publicly and that more data be collected for proper inquiry.

End of submission.

References and notes

- (1) Dr David Morrison, TC Beirne School of Law, The University of Queensland, Australia and Visiting Professor, University of Illinois College of Law, United States of America
- (2) Thomson GJ, *The Wallis Inquiry: Perspectives from the Reserve Bank*, paper delivered to the Economic Society of Australia (Victorian Branch) Conference, The Financial System in 2010 and the Wallis Inquiry, Melbourne, 5 September 1996 at http://www.rba.gov.au/Speeches/1996/sp_dg_050996.html accessed 1 March 2009
- (3) Yates C, *Four pillars policy saved us: Macfarlane*, Brisbane Times, March 2, 2009 at <http://business.brisbanetimes.com.au/business/four-pillars-policy-saved-us-macfarlane-20090302-8mdt.html> accessed 2 March 2009
- (4) APRA at <http://www.apra.gov.au>