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25 September 2017

Competition in the Australian Financial System Inquiry

Productivity Commission

GPO Box 1428

CANBERRA CITY ACT 2601

This submission focuses on the domination of the Four Major Banks and the adverse impact it has in the Australian Market.

The submission suggests two opportunities to address these concerns.

Personal background of Mr Caji DeSouza FCA.

Fellow of Chartered Accountants ANZ.

Joined Metropolitan Permanent Building Society in 1974.

Involved in the Conversion into regional bank, METWAY Bank in 1988 and in various mergers and acquisitions including that by the Queensland Government of Metway Bank in 1996.

CFO of Metway Bank and Suncorp Metway Group until retirement in October 1997.

Presently Chairman of an advisory committee of the Chartered Accountants ANZ Queensland Branch. Volunteer with two Charity organisations, one assisting the poor in Queensland and the other in Micro Finance assisting the very poor in some neighbouring Asian countries.

The Submission

The domination of the four major banks, particularly in recent years has been counter productive and has caused concern as by expressed by Government and the opposition parties and the community in general.

It has also raised some concerns in International markets.

This domination has also reduced competition in banking and the financial sector in general.

Some action has been undertaken by Government and others are proposed.

Some of these proposals will lead to more regulations and cause banks to be treated differently to other public companies.

Whilst the target by Government is on the four major banks it will clearly adversely impact the smaller banks.

In particular the proposal to introduce the Banking Executive Accountability Regime (BEAR).

This will significantly impact executives including non executive directors and the banks. This may lead to loss of appropriate talent to the banking sector.

It would appear a similar structure of regulation was introduced in the UK. It is to be noted that as a result of the GFC crisis the UK taxpayers had to bail out and or support many banks including some of the largest. Australian banks performed amongst the best during the GFC crisis.

In my opinion this over reaction might be good politics at the present time and appeal to some sections of the general public it may have long term adverse consequences.

It is to be noted the banking sector and that the majors in particular, have been most successful and profitable over many years. They are amongst the top five capitalised companies on the ASX

One could argue that some of these changes will adversely impact one of the strongest banking sectors globally.

It is to be noted that there are under consideration some proposals to improve competition in the financial sector like introduction of new technologies by new players and current participants

Whilst this will happen, the positive impact is likely to accrue in the longer term.

The continuing concern is the domination of the four major bank into the future and the lack of competition in the financial sector.

To address this issue it is pertinent to look into how and when this domination occurred.

In my opinion this commenced in 1980 with the establishment of the Campbell Committee of Inquiry to deregulate the financial sector to improve the efficiency and flexibility of the Australian Financial System.

A key proposal in this respect was the issue of banking licences to some four foreign banks.

As a defensive and immediate reaction to this threat of foreign bank entry there were mergers amongst the six major domestic banks. The Bank of NSW merged with the Commercial Bank of Australia to form Westpac Bank. The National Bank of Australia merged with the Commercial Bank of Sydney to form the Nab

This occurred in June 1981. ANZ missed out and CBA was at that time a Government Bank.

The Campbell Committee completed its report in November 1981. The Government delayed its consideration of the report.

The Labor Government in 1983 undertook a review of the Campbell report by appointing Mr Vic Martin. His committee adopted most of the Campbell Committee recommendations.

But instead of issuing 4 foreign bank licences it offered 16 foreign bank licences. 15 eventually commenced operations with having to operate as subsidiary operations.

With lack of adequate capital and lack of commitment these banks were not able to compete with the now much stronger four major banks. Many of these foreign banks handed back their licences.

In my opinion this was a lost opportunity of having some four foreign banks enter the market.

However one positive outcome was the conversion of several large Building Societies into listed Regional Banks. These Regional Banks were most successful increasing market share particularly in housing loans over a period of some 10 years.

Westpac progressively acquired some of these regional banks from 1995. Their acquisition of St George bank in 2008 was significant in that St George had previously acquired Advance Bank. These two regional banks were significantly larger than the other regional banks. It seems that this acquisition should not have proceeded as it reduced competition in the market.

CBA in 2000 acquired the Colonial Group which included the Colonial bank, a wealth management company and State bank of Victoria in 1990. In 2008 CBA acquired Bank West.

These acquisitions by Westpac and CBA significantly reduced competition in the market.

Major Banks further increased market share by acquiring mortgage brokers like Aussie Home Loans and wealth management and insurance companies.

The four pillars policy introduced in the 1990s protected the major banks but also allowed them to grow at the expense of the smaller banks.

The major banks continued to benefit by having lower capital ratios apply to them on assets compared to smaller banks.

During the GFC period they had the benefit of paying a lower guarantee levy apply to them

The smaller banks made submissions to reduce these additional imposts without success.

Until recently, the major banks dominated Government policy and their influence over the regulators.

Whilst some of these adverse impacts on the smaller banks over time may be reduced, the major bank domination will continue particularly as they divest their interest in wealth management and insurance companies as indicated by some of them. CBA has recently sold some insurance businesses.

Conclusion

1 In my view serious considerations needs to be given to allow one or two foreign banks to enter the market to undertake full banking operations including retail operations.

In this regard a survey by Davis and Lewis (1982) considered that foreign banks have three advantages relative to domestic competitors (1) significant knowledge capital (2) ownership of new technology and (3) superior skill in funds allocation. The RBA considered that foreign bank entry would provide a competitive stimulus to the banking system (Davis and Lewis 1982)

Foreign banks were considered to innately possess economies of scale and so were capable of immediately competing with incumbent banks (RBA 1994)

Foreign banks have an active preference for operations as branches rather than subsidiaries (Davis and Lewis 1982)

However since that time the four major banks have become stronger in all respects.

Australia has one of the strongest and profitable banking global sectors. This should attract the best and strongest to enter the market. The scale of banking will increase significantly. This would be most welcome by large businesses that may need funding for major projects.

Major Banks should be able to compete successfully with the entry of foreign banks for the benefit of Australian business and the community in general and provide a level playing field for all participants.

2 For this to proceed it will necessary to have the Four Pillars policy dismantled as previously recommended by the Wallis Committee in their Final report of the Financial System Inquiry report in 1997.

This submission reflects my personal views, with input from any organisation or persons

Caji DeSouza

Brisbane 25 September 2017