



26 August 2014

Mr David Murray AO
Chairman
Financial System Inquiry
GPO Box 89
Sydney NSW 2001

Dear Mr Murray

SECOND SUBMISSION TO THE FINANCIAL SYSTEM INQUIRY

P&N Bank, WA's member-owned bank, is in full support of a strong and robust financial services sector in Australia. It is imperative that our financial system is globally competitive and also one that affords Australians security, confidence and choice. We recognize that Australian banks should not be disadvantaged against their international peers.

That being said, we believe the playing field between the majors, regionals and customer-owned banks in Australia is not balanced. This inequality limits the value that P&N Bank creates for its current members and prospective members, in turn restricting our ability to compete in the West Australian market.

Whilst we raised a number of points in our original submission, the two key issues we request the Inquiry considers carefully are:

Competitive Disadvantage – Standardised Approach and IRB

In simple terms, the banks that have been accredited IRB status receive a funding advantage on home loans that we estimate to be around 20-25 basis points given the combination of risk weighting differentials and variances in the Prudential Capital Ratios (PCR). *Our modeling is not dissimilar from APRA's published estimate.*

Our analysis indicates that for every 1% difference in risk weighting of assets "RWA" between the Standardised Approach and the IRB Approach, it costs organisations such as P&N Bank the equivalent of an additional 0.7 of a basis point.

Together with this difference above, smaller ADI's such as P&N also incur a higher PCR as determined by APRA. We accept that a higher PCR may be warranted but this should be the method of differentiating capital requirements. Under the current system smaller ADIs not only have a higher PCR but must also use risk weighting of approximately twice that of the banks operating under the IRB approach.

We welcome the introduction of a High Loss Absorption buffer for D-SIBs (domestic systemically important banks) to overcome the issue of "too big to fail" whilst

noting that this alone is unlikely to redress the competitive imbalance enjoyed by those banks operating under the IRB model.

We recommend that the differential between the Standardised & the IRB risk weightings on residential mortgages is narrowed.

Sub Brand Transparency

On behalf of all Australian consumers and in the interests of transparency and choice, we would like to see that all bank sub-brands be overtly transparent in their disclosures to consumers i.e. openly disclose that they are a division of their parent bank and do not hide their ownership in fine print.

Australians have a low level of knowledge about the true ownership arrangements of smaller competitors such as Aussie Home Loans, Bank of Melbourne, Bank SA, Bankwest, RAMS, St George and Ubank. There is limited awareness that each of these brands are owned by one of the big 4 banks.

This was quantified in the EMC Research Paper "Attitudes to Banking Competition in Australia" Feb 2014. EMC's recent July & August 2014 paper of the same title shows that 62% of those surveyed have little or no trust in the big four banks giving independent financial advice.

The four major banks together with AMP, own almost 80% of the financial planning networks, many of which market themselves under a number of sub-brands. P&N Bank concurs with our industry body, COBA, and suggests that if full and overt disclosure of ownership is not given serious priority, the trust in an open and competitive financial system could be eroded even further.

Clear and overt disclosure of the real identity of lenders, financial planners, mortgage brokers and deposit-takers would deliver:

- a better informed market;
- more empowered consumers;
- more accountability and
- greater transparency.

We recommend that all bank sub-brands be required to be overtly transparent in their disclosures to consumers.

Summary

We fully recognise the importance of the major banks to the health of Australia's financial system and the need for them to compete effectively on the global stage. Similarly, regional banks also fulfill an important role to ensure competition and choice at a national level. Alongside these entities, we strongly believe that a competitive customer-owned banking sector will further improve financial stability and offer a true and sustainable choice for all Australians both now and in the future.

We only need to look to the strength of the European mutual sector to see the value that their consumers enjoy. If the Australian customer-owned sector is left behind, true choice and diversity within Australia's banking sector will be greatly diminished and potentially lost altogether.

We trust the Committee will closely examine our recommendations and address this imbalance.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Andrew Hadley', with a large, sweeping flourish extending to the right.

Andrew Hadley
Chief Executive Officer

cc COBA