



AUSTRALIAN BANKERS' ASSOCIATION INC.

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Mr John Hawkins
The Secretary
Senate Standing Committee on Economics
P O Box 6100
Parliament House
CANBERRA ACT 2600
Economics.sen@aph.gov.au

Dear Mr Hawkins,

The Banking Amendment (Keeping Banks Accountable) Bill 2009

Thank you for the opportunity to provide a submission on this Bill. The Bill legislates for the Treasurer to intervene in commercial decisions in respect of interest rate changes. This fundamentally changes the current regulatory approach to banking.

The Australian Bankers' Association (ABA) believes the Committee should recommend against the Bill for the following reasons.

1. The first point to make is that the Bill is flawed in design. It assumes that changes in official Reserve Bank determined interest rates fully reflect changes in bank funding costs. This is a false assumption. The Reserve Bank Governor has implicitly warned against drawing this conclusion¹.
2. The Bill politicises interest rate setting by giving the Treasurer the power to determine bank product prices (interest rates).
3. This is a form of price control which is inconsistent with a market-based economy and has been rejected by the last two major inquiries into

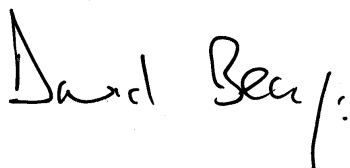
¹ RBA Governor: "*The presumption that their lending rates would and should move only in line with the cash rate, which had arisen in an earlier period when all these rates were much more closely related, has not been a realistic one in the recent environment. Of course, in setting the cash rate, the Reserve Bank has taken account of these shifting relationships, just as it does shifts in other relationships in the monetary transmission mechanism.*" (Glenn Stevens, Governor, Address to Smart Capital 2008: The Euromoney Australian Financial Markets Innovation Congress, Sydney - 27 March 2008)

Australia's financial system – the Wallis Inquiry (1997) and the Campbell Inquiry (1980).

4. One of the reasons why the Campbell Inquiry rejected price control was that it ultimately proved unfair to low-income earners.
5. Politicisation of interest rate setting is inconsistent with sound monetary policy whereby it is recognised that interest rate setting should be independent of the political arm of Government. This is why the Government has exchanged letters with the Reserve Bank assuring the central bank that it should act independently in setting official interest rates. The same principle should apply to retail rates.
6. As a result of this politicisation, uncertainty will be introduced into bank commercial decision-making.

For these reasons, the ABA urges the Committee to recommend against the Bill. We note for the record as well that the bank funding guarantees are proving very beneficial to the Australian taxpayer. The Commonwealth Government is collecting around \$500m per year from the banks in return for the wholesale guarantee. For the deposit guarantee under \$1m, there is no realistic scenario in which any taxpayer's money is at risk.

Yours sincerely



David Bell