



**Submission by CHOICE
to the
Senate Economics Committee
Inquiry into Aspects of Bank Mergers**

30 January 2009



CHOICE is a not-for-profit, non-government, non-party-political organisation established in 1959. CHOICE works to improve the lives of consumers by taking on the issues that matter to them. We arm consumers with the information to make confident choices and campaign for change when markets or regulation fails consumers.

A. Introduction

During 2008 the Australian banking market entered a dramatic period of consolidation. In September 2008 the 4th biggest Australian bank obtained its final approval to acquire Australia's 5th largest bank. And by December 2008, West Australia's biggest bank was absorbed by Australia's largest bank. Australia has a long history of mergers and acquisitions in the retail banking markets which have slowly led to the current heavily concentrated oligopoly of the Big Four banks. Even before the two recent mergers, the major banks had been growing through acquisitions. Westpac, for example, was formed in 1982 with the merger of the Bank of New South Wales with the Commercial Bank of Australia. Since then Westpac has swallowed the Challenge Bank (1995), the Bank of Melbourne (1997), BT Financial Group (2002) and now St George Bank (2008), which itself grew by taking over the Advance Bank (1997).

It is timely for the Senate Economics Committee to consider what such activity means for the Australian community and whether the Government and its agencies have acted to protect and promote the public interest throughout this period.

In this submission, CHOICE suggests that changes are required to the way bank mergers and acquisitions are reviewed, approved and enforced. We also believe the competitiveness of the retail banking market requires ongoing and regular scrutiny. Finally, the adverse affects of heavily concentrated markets may need to be addressed through divestiture or law and policy reform.

B. Recommendations

CHOICE makes the following recommendations to the Committee:

- 1. That the ACCC be appointed the agency responsible for enforcement of approval conditions issued under the *Financial Sector (Shareholdings) Act 1998*, with a requirement to report publicly on compliance with the approval conditions during the period for which the conditions apply.**



- 2. That the ACCC be asked to commence investigations into compliance with the merger conditions placed on the Westpac/St George and Commonwealth/BankWest mergers.**
- 3. That the *Financial Sector (Shareholdings) Act 1998* be amended to include a broader range of penalties for non-compliance with approval conditions, consistent with penalties under the Trade Practices Act.**
- 4. The ACCC together with the Reserve Bank of Australia establish an annual report to Parliament on retail banking competition which (at a minimum) documents the following aspects of retail banking markets:**
 - number of providers
 - rates of customer switching
 - customer satisfaction
 - interest rate margins
 - concentration ratios and disaggregated market share data
 - local points of service
- 5. The ACCC make all submissions to its Merger Review consultations publically available, subject to a specific reasonable confidentiality request.**
- 6. Noting contradictory statements about the confidentiality of the ACCC’s customer survey, we further recommend the ACCC should be asked to release the results of the customer surveys undertaken during its review process for the Westpac/St George and Commonwealth/BankWest mergers.**

C. Merger Conditions

The recent bank merger approvals granted by the Treasurer under the *Financial Sector (Shareholdings) Act 1998* contained a number of approval conditions. Some approval conditions relate to employment relations under the merged entity while other conditions relate directly to the bank’s relationship with bank customers. This Inquiry will consider the adequacy of such conditions. CHOICE research suggests that there is no system to enforce approval conditions and they are not currently enforced, that the penalties for non-compliance are too narrow and, as a consequence, that approval conditions are not currently operating to protect the public interest.

One of the ten conditions placed on the Westpac/St George merger specified that during the period of integration the bank was required to work with consumer advocates and community stakeholders “to minimise community concerns about the merger and its impact on customers and the community”. The bank was further required to address any concerns “as sensitively and quickly as possible” in the approval granted on 23 October 2008. The period of integration began when the merger took effect on 1 December 2008.



CHOICE is Australia's leading consumer organisation with a subscriber base of more than 200,000 consumers. As one of the most vocal critics of the merger throughout the ACCC's authorisation process, the organisation is a natural stakeholder to consult on retail banking matters. At the time of publishing this submission on 30 January 2009, CHOICE can confirm that neither Westpac nor St George have made any attempt to work with or even contact our organisation with respect to the integration of the two banks. We have contacted a series of other state-based consumer advocates operating in the retail banking sector who, similarly, have confirmed no contact from the banks. We believe Westpac should reasonably have identified our organisation as one of its key stakeholders and consulted with us on the business integration in accordance with the conditions placed on the merger. It is reasonable to conclude that Westpac is in breach of at least one condition placed on the merger approval granted by the Treasurer under the *Financial Sector (Shareholdings) Act 1998*.

CHOICE understands that the sole remedy available for a contravention of a merger approval condition is the revocation of the approval by the Treasurer. Of course it would not be appropriate to revoke the Westpac/St George merger on a condition such as this. Such punishment would not fit the stated breach. Indeed, once a merger is complete it is questionable whether such a penalty would be possible. The breach highlights the flaws in a merger approval process that relies heavily on unenforced and penalty-free approval conditions to protect employee and consumer interests. Many conditions imposed on mergers have been flouted and no doubt will continue to be flouted. Under the current law the conditions placed on mergers are no safeguard to protect the public interest.

We recommend that the ACCC be appointed the agency responsible for enforcement of approval conditions issued under the *Financial Sector (Shareholdings) Act 1998*, with a requirement to report publicly on compliance with the approval conditions during the period for which the conditions apply.

We recommend that the ACCC be asked to commence investigations into compliance with the merger conditions placed on the Westpac/St George and Commonwealth/BankWest mergers.

We further recommend that the *Financial Sector (Shareholdings) Act 1998* be amended to include a broader range of penalties for non-compliance with merger approval conditions, consistent with penalties under the Trade Practices Act.

D. Impacts of recent bank mergers

The Committee is required to consider the social, economic and employment impacts of the recent mergers among Australian banks, as well as the impact on consumer choice.



At the heart of CHOICE's concern about bank mergers is the substantial likelihood of reduced consumer welfare. These concerns are strong at any time but currently exacerbated by the prevailing global financial crisis. The crisis has already reduced competition and will continue to alter the nature of markets for some time. If the recent mergers were being proposed during a period of robust competition, there would at least be non-bank competitors able to keep rates and fees in check in the lending markets. But at this time, in this environment, competition cannot sufficiently constrain excessive market power.

The four largest banks are protected under Australia's four pillars policy. Following the recent mergers the market share of the four largest banks has reached critically high concentration levels in transaction, savings, wealth services and lending markets. CHOICE supports the four pillars policy, which acts to prevent the banking market being a duopoly or even monopoly. However, given the recent consolidation in the market, it may be time to consider revisiting the policy to extend its reach further. An extension of the policy could assure Australian consumers that their support of mid-tier banks won't simply lead to the bank becoming a takeover target from one of the Big Four.

CHOICE has considered what the excessive market power held by the banking oligopoly means for the Australian community. We have formed the view that such excessive market power risks the following outcomes:

- crowding out new entrants,
- poor customer service,
- poor employee satisfaction
- excessive fees and interest rates
- low rates of customer switching
- poor product innovation
- reduced access to essential banking services
- reduced diversity in local areas

We discuss some of these potential impacts below. Where possible we comment on the experience in the marketplace to date. Our overall recommendation is to establish effective systems to monitor these and any other relevant aspects of retail banking markets in an annual survey of Australian banking competition. We note that the recent House of Representatives Inquiry into Competition in the Banking and Non-Banking Sectors raised concerns about the adequacy of current mechanisms to monitor the state of competition within the banking and non-banking sectors. The House Committee subsequently recommended reviewing the *Trade Practices Act* to provide the ACCC powers to investigate and address issues of concern in markets and regulated sectors.

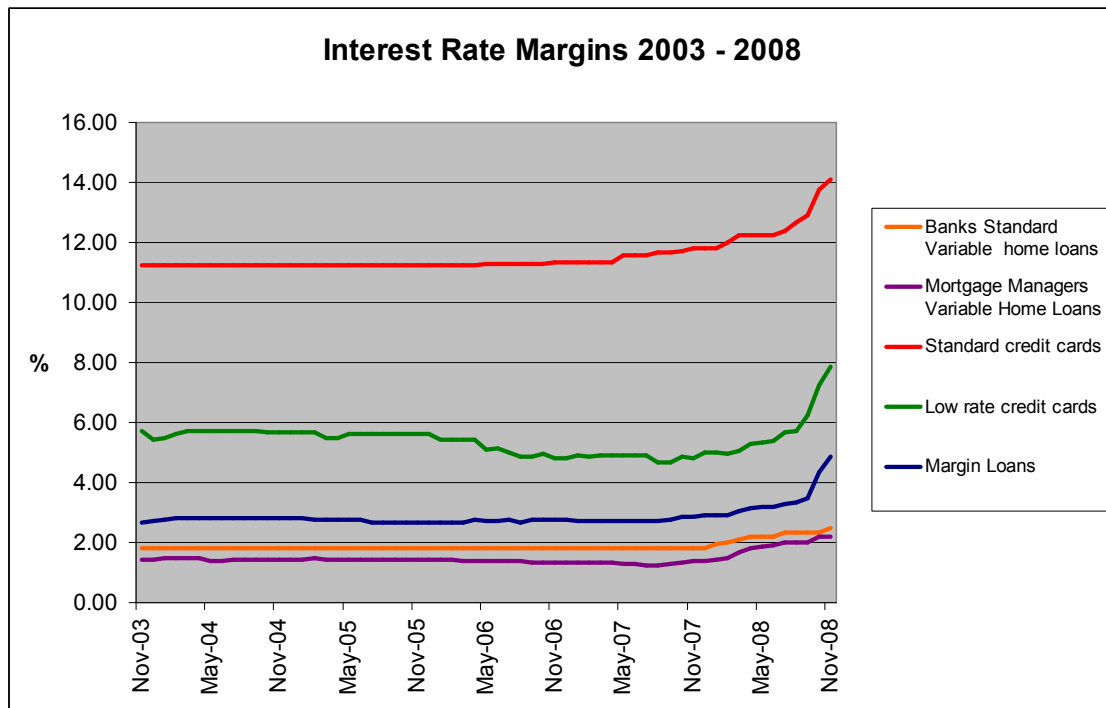


Fees and charges

The potential for uncompetitive fees and excessive interest rate charges is the most tangible risk presented by excessive market power in Australia’s banking markets.

Fees and charges have become a particular issue in the home loan market because of the collapse of non-bank mortgage originators. In its September 2008 Financial Stability Review, the Reserve Bank of Australia (RBA) confirmed that the global financial crisis has impacted directly on the competitive dynamics of the Australian financial system. The RBA’s specific concerns were in the collapse of non-ADI mortgage originators in the owner-occupied home loan market and the corresponding sharply rising dominance of the Big Four banks. While other banks had been increasing their market shares until late 2006, they dipped and recovered just after mid 2008 but only to their 2006 peak; they have dipped markedly since then.

In recent months interest rate margins on credit cards, home loans and personal have all crept above their long term average. The graph below shows the margin of the average rate over the prevailing cash rate. It demonstrates a sharp increase in margins in the period corresponding to the global financial crisis.



Source: RBA, F05 Indicator Lending Rates, November 2008 and RBA Official Cash Rate Target

CHOICE is very concerned about the sharp increase in interest rate margins across all consumer credit markets. While increase in the costs of borrowing on international



money markets are key drivers of rate increases, there are already indications that money markets have stabilised from the turbulence that dominated late 2007. Policy makers are largely relying on competition to bring interest margins back down to their competitive level. But given the renewed dominance of the major banks in consumer credit markets it appears unlikely this policy will succeed in the short to medium term.

New entrants

In normal circumstances it might be reasonable to expect some new entrants in the retail banking market. But in the current global financial conditions we suggest that it would be unrealistic to expect any expansion in banking services into the Australian market in the near or even medium term. Australia's Big Four banks are among the most profitable in the world, weathering the current period of turmoil with relative ease and ongoing profitability (RBA 2008). There is some evidence that even prior to the crisis, the Australian market was uncompetitive. At least one bank has observed that most core Australian banking products deliver higher margins relative to the United Kingdom (BankWest 2008).

Even under normal market conditions, there exist barriers to entry in the retail banking market. The structure of the Australian banking market is such that there are significant hurdles for new entrants. This includes incumbents' branch network size, a payments system based on bilateral relations and the obstacles to consumer switching only partly alleviated by reforms instigated by the Treasurer in 2008. By its own admission BankWest was only able to enter the market because of the backing of a very powerful parent company (HBOS) and because pricing in the Australian market was uncompetitive. But BankWest has also acknowledged that complex and cumbersome switching procedures make it difficult to gain market share.

Customer switching and customer satisfaction

With four big players dominating the market, it's easy for consumers to think there are no significant differences between their products and services. The market dominance drives a perception that 'it doesn't matter who you're dealing with, because they're all the same'. The perception that switching banks won't yield significant benefit stifles competition and reinforces the status quo. And indeed the Australian banking market is characterised by low levels of switching. The Australian Payments and Clearing Association (APCA) analysis has documented very low levels of transaction account switching. It estimates that 3.1% of financial institution customers switch their accounts to alternative providers on an annual basis, compared with United Kingdom customers who switch at nearly double that rate.

A high level of consumer inertia in the transaction account market means that market forces cannot be relied upon to constrain anti-competitive outcomes. Customers in the



sector have historically displayed a high level of inertia. In the early 1990s the then Governor of the Reserve Bank observed that:

Competition in the real world, however, seldom works in the manner described in the textbooks. There it is assumed that customers will actively play their part, and be prepared to shop around and switch their business if necessary... But in practice many borrowers are reluctant to shop around for a number of reasons, including inertia and the convenience of current 'packaged' services (comprising housing loan, cheque account, credit cards and so on), reluctance to try non-traditional sources of funds, and the actual or perceived costs of switching some or all transactions from one bank to another. To the extent that customers do not shop around for individual products, however, the competitive pressure on banks is reduced. (Fraser 1994)

Customer satisfaction surveys are one measure of the quality of competition. They help to ascertain the quality of service and the match between what consumers' desire and what financial institutions deliver. In Roy Morgan's regular reviews of customer satisfaction the Big Four banks consistently rate below their credit union and building society cousins. Smaller banks consistently achieve higher levels of customer satisfaction. For example, while the Big Four scored between 66 – 74% on the customer satisfaction scale in the September survey, BankWest hit 78.1%. Market dominance does not necessarily generate positive consumer outcomes. When combined with data about switching rates, it is possible to paint a picture about the actual existing state of competition in retail banking markets.

Points of presence

Technology has changed how some banking transactions are undertaken but the physical presence of bank points of service are still an essential part of the retail banking. CHOICE has analysed publicly available data from the Australian Prudential Regulatory Authority on points of presence by Authorised Deposit-taking Institutions (ADI) in Australian markets. This data aims to provide information about access to banking services, particularly in regional and rural areas. The Points of Presence data is provided by ADIs to APRA under the *Financial Sector (Collection of Data) Act 2001*. APRA includes in its data set service channels that accept cash and other deposits, facilitate the keeping of accounts, open and close accounts, undertake credit assessments and offer other banking services. These are the services that typically constitute the transaction account market.



Market share of Banking Customer Physical Service Points				
State	Big Four pre-mergers	Big Four post-mergers	Westpac (with St George)	Commonwealth (with BankWest)
ACT	46%	58%	22%	17%
NSW	52%	61%	21%	18%
NT	36%	41%	16%	6%
QLD	43%	45%	13%	10%
SA	46%	69%	33%	12%
TAS	63%	63%	14%	27%
VIC	61%	64%	15%	20%
WA	52%	67%	18%	25%

Source: APRA ADI Points of Presence, June 2008, issued 13 November 2008

Following the recent merger activity, the Big Four banks will have a 60-70% share of all ADI points of presence in NSW, South Australia, Tasmania, Victoria and Western Australia. In South Australia the newly merged Westpac/ St George bank will operate one in every three banking customer service points. While in Western Australian and Tasmania the Commonwealth/ BankWest bank will operate one in every four service points in the state. In assessing the Commonwealth/BankWest merger, the ACCC was able to further disaggregate this information to the postcode level. Any future survey of competitiveness in the retail banking sector would benefit from including data disaggregated and analysed to the postcode level.

We recommend the ACCC together with the Reserve Bank of Australia establish an annual report to Parliament on retail banking competition which (at a minimum) documents the following aspects of retail banking markets:

- **number of providers**
- **rates of customer switching**
- **customer satisfaction**
- **interest rate margins**
- **concentration ratios and disaggregated market share data**
- **local points of service**

E. Adequacy of ACCC authorisation process

The recent acquisitions by Westpac and the Commonwealth Bank were considered under the informal merger review process. Despite the fact that the ACCC assessed both bank mergers in accordance with the Draft (now final) Merger Guidelines, CHOICE has a number of concerns about the way in which the authorisation process was undertaken by the ACCC. We believe that the process should be more transparent, enable greater accountability and dedicate greater resources to evaluating consumer experiences in relevant markets.



The policy underlying competition law requires anti-competitive mergers to be blocked for the welfare of the community, not simply for the sake of competition itself. The object of the *Trade Practices Act 1974* “is to enhance the welfare of Australians through the promotion of competition and fair trading and provision for consumer protection”. CHOICE has taken a prominent position in opposition to recent mergers because we believe that the Australian community will suffer through higher prices, lower levels of service and reduced access to essential banking services.

Corporations can seek formal or informal authorisation for a merger or acquisition from the ACCC, who uses the Merger Guidelines to assess whether the proposed merger or acquisition is compliant under s50 of the *Trade Practices Act 1974*, which states:

50 (1) A corporation must not directly or indirectly:
(a) acquire shares in the capital of a body corporate; or
(b) acquire any assets of a person;
if the acquisition would have the effect, or be likely to have the effect, of substantially lessening competition in a market.

In authorising major corporate mergers the ACCC is required to undertake a delicate balancing act. It must guarantee confidentiality for highly sensitive commercial information while at the same time ensuring the public interest is protected through open and public processes. The ACCC claims to adopt the guiding principles set out by the International Competition Network to ensure this balance is achieved. However, CHOICE’s experiences of the recent bank authorisations have led us to believe that the ACCC could and should do more to protect and promote the public interest in its authorisation process.

Currently the ACCC treats all submissions it receives as confidential. While in some cases submissions may indeed contain commercially sensitive information, we believe it is inappropriate to provide no space for public review of the issues raised by interested parties where there are no confidentiality concerns. For example, in the ACCC’s review of the Westpac/St George merger more than 40 members of the public made copies of their submissions to the ACCC available to CHOICE. The individuals not only made important points but were also articulate in expressing their concerns and it is a shame that their voices are not available on the public record. Instead of treating all submissions as confidential, we believe it would be more transparent to publish submission unless an appropriate request for confidentiality is made. This would enable a fuller discussion of issues arising from the review, as well as giving stakeholders, including members of the public, a more prominent position in the review process.

CHOICE also believes the ACCC erred in refusing to release the results of its customer surveys undertaken as part of its examination of the mergers. During the course of reviewing the Westpac/St George merger, the ACCC conducted an on-line survey of



business and household customers. Some 240 members of the public completed the household customer survey. The ACCC states that results of the survey were used to inform their decision making. CHOICE supported efforts from the ACCC to pro-actively seek the views of consumers and undertake primary research into the banking habits of consumers. After reviewing the survey we concluded that the information gathered was a necessary and useful contribution to the debates about the structure of the Australian retail banking markets. It was therefore a great frustration to us that the ACCC refused to publicly release the results of their survey.

During the merger review CHOICE wrote to the ACCC requesting that the survey results be released. We subsequently made the same request in our submission to the ACCC's Statement of Issues. The request being denied CHOICE made a Freedom of Information request seeking the survey results. We were formally refused access citing confidentiality and public interest concerns.

Our frustration is compounded by the ACCC's contradictory claims about confidentiality of the survey. The ACCC's Public Competition Assessment (PCA) states that it does not use confidential information to justify publically its decisions, specifically it states:

Many of the ACCC's decisions will involve consideration of both non-confidential and confidential information provided by the merger parties and market participants. In order to maintain the confidentiality of particular information, Public Competition Assessments do not contain any confidential information or its sources.

(ACCC Public Competition Assessment, 13 August 2008, Westpac Banking Corporation – proposed acquisition of St George, p 2)

But the ACCC then goes on to use its customer survey data to support various pieces of analysis and final decisions made in the Public Competition Assessment. These contradictory remarks suggest that the ACCC has employed double standards in the use of confidential information. The ACCC has relied on its customer survey to gain public support for its decision yet refuses to release the results to the public. CHOICE is of the firm view that the results of the ACCC's customer survey should be made publically available. The ACCC has failed to be suitably transparent and accountable throughout the merger review process. As a result the public is not fully informed of the impacts of the merger activity.

We recommend the ACCC make all submissions to its Merger Review consultations publically available, subject to a specific reasonable confidentiality request.

Noting contradictory statements about the confidentiality of the ACCC's customer survey, we further recommend the ACCC should be asked to release the results of the customer surveys undertaken during its review process for the Westpac/St George and Commonwealth/BankWest mergers.



F. Alternative approaches to bank merger reviews

Bank mergers inevitably raise questions about the consequences of fewer competitors in the market for essential banking services. In the recent mergers, CHOICE called on the ACCC to undertake more thorough research into consumers' experiences of and attitudes towards competition in the retail banking sector. Despite such requests being made, the ACCC did not believe it was necessary or appropriate to conduct its own research into the market. CHOICE disagrees with this position. We believe there is inadequate information publically available about consumers' banking habits. We suggest that regular surveys of the competitiveness of the retail banking market, such as that described above, would be put to good use by the ACCC and stakeholders in any future consideration of bank mergers and acquisitions.

G. Competition Law: Power to require divestiture of assets

CHOICE is concerned that current Australian competition law does not provide sufficient protection to consumers from reduced consumer welfare caused by market concentration. Current law provides that the ACCC may refuse to approve a merger where there is a substantial lessening of competition. But mergers are not the only way in which concentration and consequent harm to consumer welfare can occur. Creeping acquisitions, failure of competitors, organic growth and potentially other market developments can also result in excessive competition over time. The problem of creeping acquisitions is currently on the policy agenda, with a discussion paper being released by the Commonwealth in 2008, however this will not address the potential for harmful reductions in competition through other causes.

Authorities in other countries have been granted powers to review markets where competition has been reduced and/or to require divestiture of assets or seek court orders for divestiture (eg the USA: Antitrust Section of the American Bar Association 2007 *Antitrust Law Developments* 6th Ed). CHOICE believes that the Committee should review the desirability of providing the ACCC with enhanced powers to *review* the competitiveness of particular markets including banking markets (possibly including in response to a Super Compliant lodged by approved organisations as is the case under the United Kingdom's Enterprise Act 2002).

Equally the Committee should review the desirability of providing to the ACCC a power to require divestiture of assets where after review it concludes that a market is not competitive and the divestiture would be likely to be in the public interest.



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