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Speech Notes

David Liddy

Managing Director

It is a pleasure to be here today to speak to such a learned group of banking and finance industry players.

Today I intend to put a premise forward that may seem contradictory:

The premise is that the four pillars policy is a disaster for Australia's big four banks.

And that it is also, potentially, a major impediment on the second and third tier of Australia's financial services sector.

In other words, that the Australian banking sector needs fewer big banks, but a strong second tier of financial services providers.

Now, the first thing you would all say is, well of course the Managing Director of Bank of Queensland wants a strong second tier of banking in Australia, and you would be right.

But not, perhaps, for the reason you surmise.

Firstly though, the need for rationalisation in Australian banking.

To speak of this, of course, means to speak of the Four Pillars policy.

There is little doubt, whether they are willing to speak about it publicly or not, that most if not all senior executives in Australian banking believe the Four Pillars policy has outlived its usefulness.

A lot can change in 15 to 20 years, and a lot has in Australia.

The real issue is, in fact, that more than outliving its usefulness, it is actually contributing to stress in the Australian banking sector, and that the end result is an unnecessary vulnerability to outside influences.

The fact is that the four pillars policy has inhibited the growth of Australian banks on the international stage to the extent where it now may be too late for them to ever be genuine international players.

It all smacks of a self-conscious protectionism which is at odds with government policy, both Labor and Liberal in almost every other area of the economy – from ports to transport, from airlines to fast foods.

Even those previously sacred cows of the motor industry and textiles have faced forced globalism over the last few years, but banking remains resolutely protected.

The reasoning behind this protectionism stretches back many years, but was reaffirmed by the current Federal Treasurer and adhered to as gospel by the current government.

I can understand why in political terms.

No government now wants to be the one to wind back the four pillars policy because any such winding back will inevitably lead to rationalisation, which will inevitably lead to job losses.

I don't dispute this as a probable short-term outcome.

This makes such a decision extremely difficult to stomach politically, and, as the advantages of dismantling the policy are many and complex, so the arguments against are simple and emotive.

The Financial Sector Union, for example, argues that not only should the policy be retained, but it should be strengthened to include a public interest test before any merger is allowed by the Treasurer. The FSU states that there should be, and I quote:

"the power to prevent mergers on the grounds that they are not in the public interest and the effect on jobs and communities must be a paramount public interest consideration. FSU has done extensive lobbying in the past on this issue and will continue to do all it can to ensure the Four Pillars policy remains."

An understandable position by the union.

However, as has been stated by John McFarlane and David Murray previously, there are inherent risks in this policy which can not be ignored, and which we are now seeing some sign of in the Australian financial services sector.

The risk is that Australia and, by default New Zealand, is left with a weakened, capital and market starved banking sector at the mercy of the large international banks.

Professor Ross Buckley from Bond University said it succinctly in February last year when he stated that, and I quote, *"the (four pillars) policy seems to have electoral appeal, but it flies in the face of the economics of international banking."*

In fact, as he also points out, the very international banks which have grown out of mergers in their own markets. Those like Citibank which came from the merger of four US banks, or HBOS, or even HSBC – all of which have become major international players.

They have succeeded where Australian banks have spectacularly failed in becoming genuine international banks, successful across a myriad of different countries and markets.

They have done it through having scale, access to capital, and powerful home bases to grow from and to support expansion.

Our Australian banks have failed due to the very competitiveness of the Australian market, and the lack of scale and access to capital to make genuine plays in markets like the US and Europe.

Instead our banks have inevitably stumbled, searching for niche entry points in those massive overseas markets instead of stepping confidently on to the international banking stage.

Right now, after unprecedented growth in the Australian economy and powerful returns, Australian banks have been forced to focus on their home markets and New Zealand.

I know there have been advances by some into the Asian markets, but again these have not been the dominant steps of confident, international banks. They have been entry points, slivers of market access rather than the heavy footprint of genuine players.

Right now the CEOs of the big four are forced to look to their home patch and devise new ways to protect existing market share from the ravages of smaller players or, even more threateningly, the very international banks they should be competing with overseas.

No longer is it just “cute” competition from St George or Suncorp, Bank of Queensland or Bendigo. Now the big boys are here, and they smell blood in the water.

GE Capital and its Wizard move, HBOS and BankWest, Citibank, HSBC and others are all taking a long hard look at the Australian market.

These are international banks that are to the National Australia Bank what the NAB is to Bank of Queensland. Massive in size, and with very deep pockets.

And all this at a time when the Big Four’s traditional strength of having the principle banking relationship with Australians is being constantly eroded.

Whether it is Bank of Queensland and Bendigo, the mortgage brokers and Aussie Homeloans, Virgin Money and credit cards, ING in the deposit space or even the ATM and Merchant markets, there is more competition than ever before, and the big losers are potentially the big four.

Instead of bursting unshackled out of a rampant Australian economy, they are forced to look behind and beneath themselves to ensure their hard-won market share across huge swathes of the financial services sector is not stolen from under their very noses.

Instead of leaping like financial tigers into the international banking scene off the strength of their powerful Australian base, they are forced to defend their home patches from the circling international banking behemoths and the more nimble regional players.

Why?

Well, to protect jobs.

This is a flawed premise.

As we have seen in the US, bank mergers did not necessarily cost jobs in the long or even medium term. Anyone in banking will tell you, now is an unbelievably competitive time in the job market. Good bankers are at a premium.

While a merger or two at the top end will lead to job shedding amongst the big four, I have no doubt, no doubt, that those jobs will be taken up by others in the financial sector industry, whether they be brokers, regional banks, credit unions or building societies.

In fact, we can see a parallel in the branch closing frenzy of the '80s and '90s.

The big four looked to efficiencies to bring them up to speed with where their global cousins were. These efficiencies were essentially driven through branch closures and staff cuts.

These closures, while admittedly overdone, came from a strong belief at the time that internet, phone banking and ATMs along with call centres would see the end of the need for many branches.

However, the policy went too far, the customers reacted negatively, and a market gap was left for some of the smaller players to fill the void.

Capitalism, robust market forces, in action.

Banks like Bank of Queensland and the mortgage broking industry thrived.

BOQ has opened almost 70 branches in the last four years, and will open many more. Our profits have more than trebled since 2001. It gave us a window of opportunity.

In the end, between us and others like Rabo and Bendigo Bank, we are filling the voids left in suburban, regional and rural Australia when it comes to banking services.

So, for a few years there was discomfort and inconvenience, but in the end it provided a more competitive, thriving financial services sector which has probably improved service to the customer, and led to a range of new products, and lower priced banking overall.

The Australian banking sector has been the foundation for the economy's strength over the last 15 years, and the platform for its massive growth.

The Big Four should take much of the credit for this success. Their strength has underpinned the economy and provided an environment of confidence and investor security almost unmatched in the world.

Surely then, this position of four pillars is too important, too vital to be unravelled?

Wrong, wrong, wrong.

We now face the prospect of hanging on too long. Of over-protectionism in a global market which is leaving us behind.

The issue which must be understood at the highest level of government and among the regulators is that surely two or three strong Australian-owned banks now is better than four internationally-owned banks in the future.

Or is New Zealand too far away to act as an example?

Australian banks now own all of New Zealand's banking industry. Are we that proud, that sure of ourselves, that we don't believe the same will happen here if we fail to act?

Now the Australian financial services sector faces the double whammy of cannibalism within and attack from without.

We are like a herd of buffalos who are about to gore ourselves to death in the race to escape external predators.

Let me set out a potential scenario for the next few years.

- **Regulation and capital needs drives the bottom tier of building societies and credit unions into forced mergers, or take overs from their larger regional banking cousins.**

- **The four pillars policy forces Australia's Big Four to snap up Australia's mortgage broking industry as a replacement sales force, and maybe a few of the remaining regional banks.**

- **The remaining, probably smaller, regional banks are then snapped up by international players forced to buy distribution networks because they are unable to move in through the big four.**

- **International trade agreements, globalisation and intense market pressures force the profit-squeezed Australian Big Four banks into the hands of those international players from which they were meant to be protected.**

So, at the end of this regulation and legislation-inspired scenario, Australia is left with four big banks which have swallowed up some of Australia's smaller players, only to be devoured themselves by large international predators.

Meanwhile, the smaller regional banks, building societies and credit unions have already disappeared in a flurry of market rationalisation forced upon them by over-regulation and market pressures, or been taken over themselves by international players looking for distribution networks and entry into the Australian market.

The end result is far fewer players, most not owned in Australia, and a much less competitive Australian financial services sector.

That means fewer jobs, higher prices for consumers and, I suspect, eventually a branch-office Australian economy sending its profits to overseas multi-nationals.

A doomsday scenario, I hear some of you say. Alarmist claptrap, I even hear muttered.

Possibly…possibly.

Let me paint you are more rosy picture. An alternative history, if you are willing.

- **The government unlocks the shackles and scraps the four pillars policy.**

- **A flurry of mergers occurs between the big four - probably the big six - and maybe even a couple of the large insurance players.**

- **Australia has two powerful financial services companies, maybe Nabanz and Westcomm, which can now stride out confidently on to the international stage.**

- **The second tier, now involving such fast-growing and market leading organisations as Bank of Queensland, become the main day-to-day financial services providers to Australians.**

- **While Nabanz and Westcomm stride the international stage, they can focus on corporate banking, wealth management and the other high-end product ranges within the Australian market without worrying about the consumer market.**

- **The surging second tier opens branches, picks up displaced staff from the former big four, and competes in a vibrant and growing domestic financial services industry, even involving those international players which are now competing in, rather than capturing, the Australian market.**

A pipe dream…a fantasy… I hear some of you saying.

Well, maybe, but you never know.

Surely the second scenario is in the better long term interest of Australians than the first.

Surely some courage now, as Sir Humphrey would once have said, will save us all much heartache in the future.

After all, globalism should not mean that Australia just becomes a market for overseas companies.

Doesn't it also mean we can be, and should be, with the strength of our economy, global players as well.

And before I am accused of letting the thriving regional banking sector off too lightly, I know there are a number in the banking industry, as well as analysts and merchant bankers, who see upside in a merger or two in the second and third tiers of Australian banking.

After all, I have stated clearly that a regional banking presence is vital for Australia's future, and therefore must also be robust and competitive.

It has been said to me, more than once, that, for example, BOQ, Bendigo and Adelaide have a great many synergies if brought together.

That might be true, but right now we are providing customers with what they want from retail banking.

An alternative.

In Bank of Queensland's case we focus on areas which, while the big guys talk about them, are much harder for the larger banks to actually deliver.

Areas like genuinely high levels of customer service, continuity of branch management, continuity of business banking personnel and face-to-face banking.

While retail customers have warmed to this, the battleground SME sector is embracing face-to-face and personal service options with open arms.

All three of us are doing it profitably too.

In BOQ's case we have been lucky enough to have taken a lot of the growth pain already, from having our own extensive ATM fleet of 2400 machines, to replacing our core computer system, to refitting all our branches and reinventing our brand, right through to repricing our deposit book to put us in good shape for the current low margin environment.

At the moment, individually, we may be considered too small for acquisition, although that is changing as the three of us regionals continue to grow our asset base.

So, I am sure there are interesting times ahead for the regional banks, and the smaller financial institutions as well.

Either way, what Australia can not afford is stagnation. Competition yes, but not at the expense of a turgid financial future.

So whether it is the doomsday scenario or the pipedream, one thing is certain - we must discuss this future seriously as an industry.

All too often we focus on our individual cases at the expense of the sector, and the economy, as a whole.

As an industry we have thrived on competition but, as the ABA no doubt could secretly attest, sometimes that competition stands in the way of good policy.

No-one wishes to admit the potential issues in case it is incorrectly sheeted back as a weakness within a specific organisation.

Analysts and journalists may take things the wrong way, and look for fear in the eyes.

The fear is not there, and nor should it be, but we must all take stock after such a strong economic performance over the last decade, and look to the future.

While some of my propositions may be extreme, I highlight them today to bring home the necessity not to bask in the glow of the past, but to ensure we all benefit from a better future.

Is the time right to go back to the Wallis inquiry of 1997 and look again at the reasoning behind the repeal of the then “six pillars policy” which became the four pillars policy?

I believe it is.

There is no doubt in my mind that finance sector players like Bank of Queensland play a vital role in the Australian economy, and will continue to do so.

I believe it is time that both government and the big four acknowledged that genuine, consumer-based banking is now more the premise of the smaller players like BOQ than the larger players.

Why force some sort of social responsibility on the big banks when the market is taking care of it anyway, through new players and old players like us who have been reborn.

I am sure that no such admission will be forthcoming from any of the big four anytime soon.

After all, where would be the fun in that!

But I bet they would like to be able to focus on the big international picture without the distraction of having to fight a guerrilla war in their domestic market at the same time.

So, we come back to my premise.

Its fundamental tenet is one of “live and let live”.

Remove the artificial boundaries on the Australian financial sector.

Let us thrive without the forced suppression of the four pillars policy.

I am more than confident in Bank of Queensland’s future either way, but I also, as a life-time member of the Australian banking industry, feel the need to step out from under my BOQ hat to look more widely at the times ahead.

And so I end with a quote from the oft-quoted former US President, John F Kennedy.

"There are risks and costs to a program of action. But they are far less than the long-range risks and costs of comfortable inaction."

Couldn't agree more.

Thank you.