27 October 2022

Review Panel
Review of the Reserve Bank of Australia
Australian Government

Online & via email: enquiries@rbareview.gov.au

Dear Review Panel

COBA submission to RBA Review

Thank you for the opportunity to contribute to the first wide-ranging review of the RBA since current monetary policy arrangements were put in place in the 1990s. We note the Review will consider the RBA's objectives, policy implementation, governance processes and public communications. It will also consider the relationship between monetary, fiscal and macroprudential policy settings.

COBA is the industry association for Australia's customer owned banking institutions (mutual banks, credit unions and building societies). Our sector is distinguished by its unmatched customer focus, prudent lending and long-term commitment to its communities such as essential worker groups (e.g. teachers, police & nurses) and regional Australia.

Collectively, our sector has $160 billion in assets and 5 million customers. Customer owned banking institutions account for around two thirds of the total number of domestic Authorised Deposit-taking Institutions (ADIs).

As the voice of the smallest players in the banking market, we bring a unique perspective to discussion about banking and policy. This point of view is particularly relevant in a market whose enduring condition is dominance by four major players with few sustainable new entrants.[1]

The themes we address in this submission are:

- Interaction of monetary, fiscal and macroprudential policy
- RBA performance
- RBA communications, and
- RBA Board composition.

Observations and recommendations

1. The RBA engages effectively with stakeholders to gather information and consult on policy matters.
2. The RBA acted effectively during the pandemic to support the stability of the financial system.

[1] The last two years have seen exits or takeovers of neobanks Xinja, 86 400 and Volt, the sale of Citigroup's Australian consumer banking business to NAB, the sale of ME Bank to Bank of Queensland and the proposed sale of Suncorp Bank to ANZ, i.e. 4th largest bank swallows 9th largest bank.

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3. We strongly support contributions by the RBA to debates about regulatory proportionality and better regulatory co-ordination.
4. Recent experience in retail banking should be considered highly relevant for the shortlist of candidates for the RBA Board and the selection process should consider business models other than listed companies.

Sector profile

Customer owned banks deliver competition, consumer choice and market leading customer satisfaction[2] in the retail banking market.

Customer owned banking has been meeting customer needs in Australia for more than 150 years. Our original communities were diverse, including geographic, employer-based, industry-based, ethnic and faith-based. While once restricted to serving our particular ‘niches’, customer owned banks now serve a broader concept of community with many serving customers across Australia.

Of COBA’s top 10 member banks, only two are based in the traditional banking capitals of Sydney and Melbourne, with the other head offices in Brisbane, Adelaide, Perth, Newcastle, Wollongong and Toowoomba.

Our sector’s share of the household deposits market is around 10 per cent. Our share of the new owner-occupier home loan market is around 7 per cent, with a focus on first home buyers. Our non-performing loans ratio is around one third that of the broader banking system.

Around 90 per cent of our funding is deposits and around 85 per cent of our deposits come from households, while 97 per cent of our lending is to households.

RBA engagement

As outlined in the Review’s Issues Paper, the Review will consider the breadth and depth of the various inputs that the RBA draws on in supporting monetary policy decision making. The Review will also examine how the RBA engages with households, businesses and financial market participants.

COBA has engaged positively with the RBA over a long period in the RBA’s role as payments system regulator. The RBA has always given us a fair hearing in retail payments regulatory policy debates. The RBA’s reasonable approach was illustrated by its decision in March 2020 to temporarily put on hold its retail payments regulatory review “to reduce the demands on industry stakeholders at a time when they are focused on dealing with the impact of COVID-19.”

COBA greatly appreciated the RBA’s willingness to engage directly with our sector during the COVID-19 pandemic. The RBA Governor and senior RBA executives held monthly videoconference meetings in 2020 and 2021 with COBA and small groups of COBA member CEOs to discuss the impact of the pandemic, and policy responses to the pandemic, on the banking market, consumers and businesses. Representatives of our sector were able to regularly provide the RBA with ‘live’ updates about conditions in funding and lending markets and on a wide range of other topics.

As the impact of the pandemic and policy responses evolved, topics discussed at these liaison meetings included:

- support for households and businesses
- operational and business continuity issues
- managing customer hardship
- housing market developments, including regional markets

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[2] https://www.customerownedbanking.asn.au/news-and-resources/media-releases/Customer-owned-banks-serve-the-most-satisfied-banking-customers

- operation of the RBA's Term Funding Facility (TFF)
- promoting economic recovery
- regulatory co-ordination
- workplace trends
- lending market trends
- inflation and wages
- skilled staff shortages, and
- digitalisation.

We believe these meetings provided the RBA with useful inputs for its decision-making on monetary policy and system stability because COBA members discussing the above topics were able to bring their unique customer focus and distinct insights about, for example, regional Australia.

Financial stability

As outlined in the Review's Issues Paper, the RBA took actions during the pandemic to support the stability of the financial system and the functioning of financial markets that are core to the transmission of monetary policy.

As publicly acknowledged by the RBA[3], the provision of exceptional liquidity assistance to illiquid but solvent banks is a core responsibility of central banks.

> "While each financial institution is responsible for managing its own liquidity, situations can arise when the provision of liquidity to a specific institution by the central bank can be in the public interest. Doing so can reduce unnecessary disruptions to the financial system and help preserve financial stability.
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> "The regulatory framework for authorised deposit-taking institutions (ADIs) in Australia anticipates that institutions may at times face unexpected outflows or difficulty accessing liquidity. ADIs are required to maintain holdings of liquid assets above a regulatory minimum and to plan how they would respond to liquidity stress. Larger ADIs are also expected to hold additional 'contingent liquidity' assets that could be used in a crisis situation to access liquidity from the Bank via repurchase agreements (repos) of self-securitised mortgages – that is, debt securities backed by pools of mortgages created and held by ADIs specifically to be used in repos with the Bank.
>
> "In situations of market-wide liquidity stress, the Bank can boost system-wide liquidity through open market operations, reducing uncertainty about the availability of liquidity in the banking system and contributing to a lower cost of liquidity than otherwise. The Bank has done this on multiple occasions in the past, notably during the global financial crisis and during a period of pandemic-related stress in March and April 2020."

Due to the impact of the pandemic on the economy and the financial system, in March 2020 APRA directed ADIs subject to the Minimum Liquidity Holdings (MLH) regime, e.g. COBA members, to increase the size of their existing self-securitisations as a precautionary measure. APRA views self-securitisation as one of the preferred options to provide liquidity support to ADIs via the existing financial market infrastructure with the RBA.

This strengthening of the contingent liquidity framework was adjusted by APRA in October 2020 due to improved conditions and APRA is currently proposing to further ease settings to reflect the further improvement in conditions.[4]

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[3] https://www.rba.gov.au/monetary-policy/rba-board-minutes/2021/2021-09-07.html

[4] https://www.apra.gov.au/contingent-liquidity-proposed-guidance-0

> "However, APRA also expects that ADIs will be able to increase their self-securitisation levels on a timely basis if needed in stress."

These developments in the contingent liquidity regime for ADIs depend on the financial market infrastructure of the RBA.

Uniquely in the Australian market, the mutual ADI sector has its own self-funded and operated liquidity scheme, CUFSS[5]. CUFSS is certified by APRA under s11CB of the *Banking Act 1959* and its objectives are to protect the interests of member depositors and promote financial sector stability, particularly in relation to mutual ADIs.

Such schemes are a feature of credit union systems around the world.

Each individual CUFSS member's commitment to the system is through the Industry Support Contract (ISC), which sets out their obligations, rights and responsibilities. These include providing information to CUFSS for monitoring purposes and pledging a contingency commitment of a percentage of assets for emergency liquidity support should it be required. As an industry support vehicle, this supervision system is independent from, and additional to, that undertaken by APRA.

During the pandemic, CUFSS worked with APRA and the RBA to increase the size of the available funding pool, as noted in the CUFFS 2020-21 annual report.

> "This increase in emergency liquidity is via allowing Members with Repurchase Agreements to draw on these and provide emergency liquidity to other Members under the CUFSS umbrella. The project was successfully completed in March 2021 resulting in a significant additional pool of emergency liquidity being available from the RBA and APRA recertifying the Industry Support Contract."[6]

We see this outcome as an excellent example of key regulators, i.e. APRA and the RBA, working effectively together with an important retail banking stakeholder, i.e. CUFSS, to deliver enhanced arrangements underpinning system stability.

Council of Financial Regulators

As outlined in the Issues Paper, the RBA works closely with other agencies through the Council of Financial Regulators (CFR) to promote financial stability.

COBA strongly supports contributions by the RBA to debates about regulatory proportionality and better regulatory co-ordination.

Proportionate regulation and high-quality regulatory policymaking contribute to financial stability. Overlapping regulatory projects can mean multiple changes to complex systems at the same time which creates operational risk for the broader financial sector.

In July 2021, the RBA thanked COBA for our feedback and suggestions on the coordination and communication of financial regulatory initiatives. The RBA advised COBA that the CFR discussed this topic at its quarterly meeting in June 2021. The RBA noted that while Council members routinely discuss the broad range of financial regulatory initiatives being developed and implemented, it was acknowledged that more public visibility could be valuable. The CFR agreed to further explore ways to communicate regulatory initiatives that will affect financial sector entities. The Regulatory Initiatives

[5] http://cufss.com.au/

[6] http://cufss.com.au/pdf/CUFSS-FY21-Financial%20Statements-30-08-21-v5-Final-with-THP.pdf

Grid[7] published by the UK Financial Services Regulatory Initiatives Forum would be considered in this context and this work would be led by Treasury.

COBA's view is that the increasing pace, volume and complexity of regulatory change is a challenge for all financial services entities but is most acute for smaller players. As best practice, industry participants and consumer groups should have sufficient time and notice to participate effectively in consultation processes. The financial sector should also have sufficient time to constructively make the changes to meet these regulations.

We believe that better and more transparent coordination will assist policymakers, regulators, and legislators to make more informed decisions when developing policy and setting implementation timeframes.

COBA applauds the RBA speaking out about the risk of over-regulation. The RBA Governor issued a warning about this issue to the Senate Select Committee on COVID-19 in May 2020:

> "I fear that one result of the virus, one of the shadows cast by the virus, is that we're going to become even less dynamic. There's going to be more conservativism, more caution and a lot of structural change. I can see real benefits in reinvigorating the sense of dynamism in the economy, and regulation is one way to do that. It's broader than that. It's kind of the culture and our approach: when we see things going wrong, do we regulate them or do we have a different approach?
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> "I fear that over time we've erred too far in the direction of regulation. It's perfectly sensible to stop bad problems from happening, but that also limits the other side, the upside, as well. As I said, it's a very, very high level, but it's something we should think about. Somehow reinvigorating the dynamism in our economy is going to be a critical issue over the next few years because I think we are less dynamic."

The RBA can be an influential voice in reminding policymakers and other regulators about the need to recognise and respond to the impact on competition, innovation and consumer choice of constantly ratcheting up regulatory compliance costs.

The increasing diversion of scarce resources away from customer service and innovation to meet new compliance obligations hits challenger banks hardest and gifts a competitive advantage to major banks. The ultimate losers from this entrenched trend are all banking customers who need a vibrant, dynamic and innovative retail banking market.

Warning about these risks is entirely consistent with the RBA's charter to contribute to the economic prosperity and welfare of the people of Australia.

COBA suggests that the capacity of the RBA and its peers on the CFR to respond to new risks and co-ordinate regulatory change would be enhanced if the CFR were to establish to establish a formal dialogue with the Finance Industry Council of Australia (FICA).

FICA brings together the leading financial services industry associations in Australia – Australian Banking Association, Australian Finance Industry Association, Australian Financial Markets Association, Australian Securitisation Forum, Financial Services Council, Insurance Council of Australia and COBA.

A formal dialogue between the CFR and FICA would allow industry and regulators to more effectively work together to navigate future challenges while underpinning economic growth.

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[7] https://www.fca.org.uk/publications/corporate-documents/regulatory-initiatives-grid

Composition of RBA Board

As noted in the Issues Paper, the Treasurer appoints RBA Board members from a shortlist of candidates maintained by the Secretary to the Treasury and the Governor. The current members are from a range of backgrounds, including business, academia, public policy and the not-for-profit sector.

For obvious conflict-of-interest reasons, the Act disqualifies directors, officers, or employees of an ADI from being a member of the Board but we see a case for former retail bankers to be successful candidates.

The banking system is the means of transmission of monetary policy. As noted in the Issues Paper, the RBA primarily conducts monetary policy by setting a target for the cash rate and changes in the cash rate influence other interest rates in the economy, such as rates on home loans and bank deposits.

A strategic perspective on, and operational experience in, retail banking markets should constitute relevant experience and capacity to foster internal deliberation and effective decision-making by the RBA Board. A Board member or members with recent experience in retail banking could productively challenge the view of the ex-officio "bankers" on the Board.

Given that the perspective of listed companies has always been well represented on the RBA Board, we suggest the process of drafting a candidate shortlist should give due weighting to experience with different business models – such as the customer owned model.

I am very happy to meet with you to discuss any aspect of this submission.

Yours sincerely

MICHAEL LAWRENCE

Chief Executive Officer