

BANK FUNDING AND COMPETITION

Concerns with sourcing adequate bank funding has been a key discussion item at recent FSAC meetings. The Council recommended a number of measures to the Government at its August 2010 meeting to address these concerns. Additionally, community concerns have emerged at a perceived decline in banking sector competition in the wake of the Global Financial Crisis.

This paper seeks further advice from you on options to address those issues.

Bank funding

FSAC members representing lending institutions have previously advised that their institutions have been experiencing difficulties in sourcing adequate funding. It has been suggested that these difficulties could be exacerbated by Basel III capital holding requirements, noting also, that there is evidence of fierce competition for deposits. Some members have also expressed concern that a possible over-reliance on foreign funding sources poses risks to the banking sector and the broader community.

The Government announced measures to address this issue in the 2010-11 Budget, including a phasing down the interest withholding tax paid by financial institutions on most interest paid on offshore borrowings and a tax discount on interest earned on deposits.

A number of options have been identified by members to strengthen and diversify sources of bank funding, including.

- covered bonds;
- corporate bonds;
- further AOFM interventions in RMBS/securitisation markets;
- retaining the deposit guarantee, and at a relatively high level; and
- implementing the reduction in the rate of interest withholding tax on interest paid on offshore borrowings in full at this time rather than in the phased approach previously announced.

Further options may include, but not be limited to:

- bullet RMBS and other innovative structures; and
- encouraging the superannuation industry to provide funding to the banking system.

Discussion issues:

1. What are the advantages and disadvantages of each of these possible methods and how would they impact large versus smaller lenders?

2. How useful/material would each possible method be in addressing any funding shortfall?
3. Can the Council rank the initiatives in order of importance?
4. Are there other possible methods to address any bank funding shortfall that should be added to this list?

Competition in the banking sector

Competition in mortgage lending is perceived by sections of the community to have declined due to structural changes in the banking sector stemming from the Global Financial Crisis.

Members have previously recommended a number of methods in which the Government could bolster banking sector competition, including:

- further AOFM interventions in RMBS/securitisation markets, noting that a number of small lenders have utilised this previously;
- retaining the deposit guarantee, and at a relatively high level, noting that smaller lenders are relatively reliant on deposits as a funding source; and
- implementing the reduction in the rate of interest withholding tax on interest paid on offshore borrowings in full at this time rather than in the phased approach previously announced.

A further option may include, but not be limited to:

- extending the Government's Account Switching Package to make it easier for consumers to switch between mortgage products and providers.

Discussion issues:

1. What are the advantages and disadvantages of each of these possible methods?
2. How useful/material would each possible method be in addressing competition?
3. Can the Council rank the initiatives in order of importance?
4. Are there other possible methods to address competition that should be added to this list?
5. What role are non-regulated market participants, such as mortgage brokers, playing in enhancing or diminishing competition in the banking sector?