“FACING THE FUTURE – OPPORTUNITY BECKONS”

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“Facing the Future - Opportunity Beckons”

Early last month, the world commemorated sixty years since the fall of Berlin. This was the culminating event which ended the Second World War in Europe. It’s been a time for widespread remembrance and grief.

In that traumatic post-war period many thousands of Jewish and other European migrants found in Australia a safe haven to raise their families, and a nation grateful for their magnificent contributions to its development.

The Australia-Israel Chamber of Commerce is one of those great contributions. It’s a real pleasure to join you today here in Melbourne, my home town.

Today I want to talk about the state of play in Australian banking and outline the competitive realities – both the drivers of progress and the inhibitors of change - that will potentially shape the sector’s future.

But I am not going to confine my remarks to banking. Banking is an ideal place to begin any analysis of the state of the broader Australian environment – because banking is the blood supply of our economy. It provides the vital conduit for the flow of business investment and the management of household wealth.

Fifteen years ago the banking sector represented about 14% of the Australian stock market. Today it represents 23% - and that’s in the context, as you know, of a broadly expanding economy.

So the future of banking in Australia will continue to be profoundly affected by the overall health of our economy. The interests are entwined and mutual.

And, today I shall argue that government-led renovation is urgently required in both - and that corporate Australia has a major productive role to play.

**Banking outlook**
Let me start specifically with banking.

Australia today is well served by its banking sector. Banking is easier and more convenient than ever. Competition has never been stronger and indeed, it pervades everything from pricing and service, to technology options and brand appeal.

Australian businesses and households are reaping the benefits. Just ten years ago, for example, the average interest rate spread earned by the major banks was around 4 percent; today it is nearer 2 percent.

Based on total banking loans and advances of around $825 billion today, Australian institutions, businesses and individuals are some $16 billion better off each year - in terms of the interest they pay to and receive from banks - than if the spreads had stayed at the level they were 10 years ago.
Critics counter by pointing out that fee income has grown strongly over the same period. Yes it has, but it has largely grown in line with the growth in banking system transaction and asset growth and with the diversification of bank earnings into wealth management and insurance.

The more salient point is that intense competition has seen aggregate bank fees decline from a peak of around 1.1% of banking assets to 0.9% today. In fact, total bank income as a proportion of banking assets has declined sharply over the past 10 years from around 4% to around 2.9%.

As I’ve indicated, competition for customers today is nothing short of fierce.

You only have to watch TV advertising to witness the explosion of choice for Australian customers, as domestic and international firms seek to carve out niche markets for specialised financial services.

Foreign banks and large multi-national enterprises are very visible in pouring resources into a renewed bid to capture a large slice of the Australian market.

Broad spectrum, global companies like GE Money now dominate finance company business here and are pushing hard to establish themselves just as firmly in credit cards and other banking related products.

And even non-bank brands like Virgin Money and Aussie Homes Loans continue to push new product innovation and pricing.

At Westpac we formed a partnership with Richard Branson’s Virgin Money group targeting the budget-priced segment of the consumer credit market. The success of this strategy has seen 500,000 new credit cards being issued in just over 12 months.

There’s both growth potential and very tough competition, for traditional banking and for emerging market niches: battles to win customer patronage in everything from credit cards to business finance to mortgage origination.

And there are exciting opportunities in wealth management and infrastructure development.

In my view, you’d be hard pressed to find a more dynamic and internationally competitive sector in the Australian economy. In fact, one of the big challenges facing the industry going forward is skill shortages. There’s only 2% unemployment in the financial services sector compared to 5% in the wider economy.

At the same time, the Australian banks increasingly have to compete on a true global basis – head to head with the global best.

Indeed, if I were tell you that two Scots, an Australian, a South African and a New Zealander walked into a bar, you might think I was about to tell a joke. In fact, of course, it’s a description of the top echelons of Australian banking.

It’s a clear indication of the continued internationalisation of our banking sector that when Ralph Norris takes over at CBA I will be the only Australian born among the CEOs of the top five banks in Australia; indeed the only Australian born CEO among the top seven companies in Australia, excluding NewsCorp.
In banking, skill shortages and competitive and efficiency pressures are forcing the industry to actively consider and in some cases implement a range of solutions.

These include outsourcing functions to specialised service providers domestically or offshore, automating administration and processing tasks, or joining with other banks in pooling back-office and non-competitive functions such as cheque, cards or mortgage processing.

While I am confident that the Australian banks can successfully deal with these challenges, there is one key constraint to our ability to remain fully competitive on a global basis.

As you know, the four pillars policy still decrees that the four big Australian banks must compete with large overseas owned banks, many times our size, with one arm tied behind our backs. This policy may have had some relevance a decade ago but now it is just regulatory nostalgia.

Prohibiting mergers between the Australian owned bigger banks, stymies the immense possibilities for Australia in having an Australian owned bank, or banks, with true global scale. At the very least, banks should be treated exactly the same as other corporations from a competition policy viewpoint, with any competitive issues assessed on their merits by the ACCC.

The four pillars policy today is simply a pointless retardant – to the efficient development of the financial services sector – and arguably to our broader national prosperity.

**The broader environment**

Which brings me to the broader economic environment.

We all know that Australian households have spent the past ten years or so passionately investing in home renewal. It’s been a time of refurbishment and upgrade. Now the household boom is slowing down.

But we have an historic opportunity for a new burst of renovation - from another quarter. It’s time for our political leaders, in partnership with business, to invest in national refurbishment and upgrading. It’s time for national renovation.

The need is very clear and this very message is already being sent out by business groups like the Business Council of Australia and the Australian Industry Group.

It’s being echoed by scientific and environment groups deeply concerned about the widespread impacts of climate change in this country.

It’s being repeated by community groups, concerned about the quality of life in Australian cities and in regional communities.

The Treasurer and the Treasury have drawn attention to the long term challenges posed by Australia’s ageing population. And of course, at the recent Council of Australian Governments meeting, the Prime Minister and State Premiers acknowledged the need for a big, cooperative approach to investment in our nation, for the sake of our future prosperity.

But today, from all levels of government, and of all persuasions, Australia needs a burst of national renovation. We have had a strong period of growth. We are economically stable. Our economy is in many respects one of the most successful and envied in the world.
The legislative opportunity is there before us with the rare political luxury of a Federal Government in control of the Senate. I urge all our political leaders to seize the opportunity and to expect enthusiastic support from the banking community.

I want to mention specific areas where further reform will have major benefits for long term Australian competitiveness.

**Taxation**

To put it bluntly, our national web of taxes looks more like a series of knots.

The whole system needs to be unpicked and harmonised. The complexity of the income tax legislation alone imposes very significant compliance costs on business.

The fact that the Australian income tax legislation has increased from around 80 pages in 1936 to in excess of 4,500 pages today is indicative of the problem. The GST legislation runs to some 540 pages, I believe, and so it goes on.

At the Federal level we need to deal with the distortions from the lack of alignment of tax rates. The top personal tax rate is still a long way from the company rate, and the tax rates on capital gains and superannuation are different again.

The present system is less likely to encourage rational, productive investment and work effort than the pernicious idea that the most important part of wealth creation is clever tax planning.

In another area, the Treasurer has legitimately called on the State Governments to eradicate the business and financial taxes that should have been eliminated years ago following the introduction of the GST.

It’s simply short changing everyone for State Governments to cry poor and hold enterprises to ransom by not removing these inefficient taxes. A fully efficient and effective tax system is a critical part of the framework needed to support a sustainable vibrant and competitive economy.

**Regulation**

It is important to acknowledge upfront that regulations don’t arise in a policy vacuum.

If our corporations are not meeting the community’s legitimate expectations, then the community inevitably looks to government to rectify the problem. It is incumbent upon our companies to deliver on trust, transparency and ethics.

We need to remove the negatives that drive regulation. It’s not good enough simply to exhort Governments to wind back, corporations must also move forward as responsible citizens.

Nevertheless, it’s clear the legal and regulatory burden upon business has scaled up to mountain size. I’m not exaggerating.

As the Business Council of Australia says, on average the Commonwealth Government now passes 350 pages of new laws for every week it sits.
Astonishingly, half of all legislation passed by the Commonwealth Parliament since Federation has been passed in just the past 14 years. No wonder then that the Commonwealth spends $5 billion a year administering business regulation.

The State Governments also churn out new laws and regulations. In 2003, Commonwealth and State governments together produced 33,000 pages of new laws, rules and regulations.

Westpac's own experience is that the writing of a simple mortgage requires reference to no less than ten separate pieces of Commonwealth legislation and national regulation, plus seven separate State Fair Trading Acts.

Within a flawed regulatory environment businesses lose money and opportunities, consumers pay higher prices, and taxpayers pay the higher costs of inefficient public administration.

With control of the Senate, the Federal Government is now in a position not only to craft clean regulation, but to revisit existing regulation and clean that up too.

Governments can have little excuse for failing to review, reform or remove inefficient or unnecessary existing regulation. It's an opportunity too important to be neglected.

Commonwealth-State Relations

I think it is now widely accepted that the Federalist model designed more than a hundred years ago requires a dramatic overhaul. The system was established to delegate responsibility for funding and managing certain tasks in an environment where travel and communication between state and regional areas was difficult.

Today, overlaps, gaps and massive inefficiencies are legion and well-documented in everything from education to health to infrastructure development.

One simple but bizarre example is first aid. Few of you would know that first aid kits in Westpac branches are required to have different contents depending on which State they are in.

A first aid kit in New South Wales has to have dressing tape 2½ centimetres wide, in West Australia it has to be 1¼ centimetres. In Victoria, 60 mls of eye wash is a requirement, in Queensland it's 250 mls, in South Australia you don't need it at all. And so on.

This is a small but telling example of a widespread and costly disease affecting the efficiency of our businesses and the prosperity of our country. We need to fix our first aid kits! It's bad enough to have these duplications in such areas.

But even emerging policy arenas are subject to irrational resource management.

Take greenhouse gas policy. The Commonwealth and some States have different programs and even use different output measures for awarding credits for good greenhouse practice. The climate change issues are here and now.

Australia cannot afford the lack of a unified approach to emission targets and trading mechanisms. Governments claim to be interested in encouraging businesses to sign on to these programs. Surely the Commonwealth and States can coordinate better than this. Surely they can see that business confidence in collaborating with governments on broader agendas is seriously...
affected by these unprofessional inconsistencies. An agreed national approach would make participation more rewarding.

It’s going to take massive political energy to deal with these problems but I think the Australian community would overwhelmingly be supportive of the agenda.

**Trans-Tasman relations**

And there are other opportunities for us to pursue.

The Europeans fought two all out-conflicts in the last century alone and countless wars before that – and yet it’s now decades since they overcame their differences and mutual suspicion to form a powerhouse economic union.

Yes, there are challenges today to how far the union will go as communities grapple with issues of national sovereignty. But the benefits for Europe are clear.

Australia and New Zealand are allies, comrades and cultural partners, yet despite the best efforts of both Peter Costello and Michael Cullen, we haven’t been able to agree upon a uniform regulatory approach in key areas, let alone a single economic market.

If we are to build scale and opportunity across both trans-Tasman markets, it’s essential we move as quickly as possible to merge our regulatory environments and ultimately our two economies.

And, it will come as no surprise that I will argue that true banking regulatory harmonisation is the vital next step. It would prove to be an enabler of the broader integration.

The onus is on Australia to assure New Zealanders that we both have much to gain, and that New Zealand will not risk losing either identity or sovereignty in the process.

But if Luxembourg can cope with being a tiny part of a 25 member state economic union, I think New Zealand can face a bilateral partnership in uniform regulation with confidence.

The sum of all these reform measures – tax, regulation, Commonwealth-State relations, Trans-Tasman relations, together with the Governments proposed reforms in the industrial relations area - will be far greater than their individual parts.

Together they would set Australia up for the next burst of national prosperity. They would constitute a national renovation.

**Role of business**

Before I conclude I want to say something about the role in this process for business.

The unfortunate truth is that the opinions of senior business leaders don’t carry much popular weight today. Our corporations simply do not enjoy sufficient popular trust.

At Westpac we have come through a long period of patiently reshaping and reorienting ourselves to win back the trust of the community. We’ve made a lot of progress but we are anything but complacent.
The challenge for all of us in leadership roles in big corporations is to rebuild our standing as responsible corporate citizens. We need to repair the public trust.

Today when corporations endorse national reform agendas, their motives are more often than not viewed with scepticism and suspicion. We need to get to a point where the views and suggestions of big corporations are judged on their merits by the community.

We need to demonstrate that the interests of big business and the broader community are not divergent, but profoundly intertwined. This is still a major task ahead of us.

And, being a good corporate citizen must also include being prepared to be advocates against populist solutions, against easy fixes, against empty applause-winning gestures.

Protection always sounds like a vote winner, but corporate Australia must be prepared to argue the case for further internationalisation of our economy and lend its intellectual capital to the cause. We must also be prepared to argue against accepted wisdoms.

So corporate Australia must always be prepared to contribute and improve the quality of the public policy debate.

Conclusion

Let me conclude. Most of these reforms I have suggested are not of the old left versus right variety. They are not about ideology. They are about pragmatic realities.

They demand a rethink of how government and business operates; a vision of how much better things could be; and a patient determination to effect real change.

I started off by saying that banking is the blood supply of the economy. If we don’t unclog the arteries in banking we won’t get it right elsewhere. But the task goes well beyond financial services alone.

The opportunity is now before us to reshape the way Australia operates and to lay the groundwork for national prosperity for decades to come. We all have our roles to play.

And we must pledge our full support to those national and state leaders who are prepared to take on the challenge and see the reform process through.

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