

## Australian government guarantees bank deposits and funding

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### Key Points

- In a welcome pre-emptive move designed to ward off further pressure on Australia's financial sector the government has announced three new measures to guarantee Australian Financial institutions.
- Under these measures, the government will guarantee all banking deposits for three years; will guarantee (for a fee) the wholesale (non-deposit) funding of financial institutions; and the AOFM will buy another \$4bn of RMBS.
- These measures aim to improve the availability of credit and cap the price of credit in Australia. But that is not to say that the supply and cost of funds will not fluctuate further from here.
- The policy announcement is very broad-brushed with very little detail. We understand the government and its advisers are still consulting to finalise the details. That being said the details are crucial and will be worked out over the course of this week within the global context. Indeed, the primary motivation for the PM measures to guarantee bank liabilities was to keep Australian arrangements in line with other countries.
- A list of institutions that are possibly covered is listed in the Appendix to this note.
- This policy announcement looks like it will ultimately be part of a global move by Governments to provide short to medium-term guarantees to banks. The Australian government's policy announcement is consistent with the G-7 Finance Ministers and Central Bank Governors Plan of Action announced over the weekend. While announcements are being made on a country-by-country basis, they nevertheless should be seen as part of a global co-ordinated response to the global financial crisis.
- These moves are all designed to restore investor confidence in the banking system and promote the proper functioning of money and credit flows within the economy. While they are hugely welcome, the success of these schemes will ultimately lie with the investor response. The local stockmarket has responded favourably this morning with banking shares bouncing. Also, the spread between 3-month BBSW and OIS has narrowed considerably this morning to 95bps from 112bps on Friday.

### Another pre-emptive strike

In a pre-emptive move designed to ward off further pressure on Australia's financial sector the government has announced three new measures to guarantee Australian Financial institutions.

- **Guarantee on deposits.** The Australian government will immediately guarantee all deposits on Australian banks, building societies and credit unions and Australian subsidiaries of foreign-owned banks. Foreign branches of Australian deposit taking institutions are covered, but deposits with offshore subsidiaries are not. Foreign currency deposits are also covered by the guarantee as are deposits held in banks by superannuation funds. Moreover, the guarantee reaches beyond just retail deposits as

The Government's guarantee aims to ensure Australian banks are not disadvantaged in the current global environment

credit advanced by an entity to a deposit-taking institution is included in the guarantee. In contrast to similar guarantees announced offshore, there will be no limit on the value of deposits guaranteed. This guarantee will be in place for three years (and then reviewed). This will be legislated as part of the Financial Claims Scheme (which previously had proposed a retail deposit guarantee capped at \$20,000). Given that Australian banks remain in a healthy financial position the Government's guarantee does not reflect any problems in the banking system. Rather, with other countries government's guaranteeing bank deposits the risk would be a loss of deposits overseas if Australia did not follow suit.

- **Guarantee of wholesale funding for institutions.** The Australian government will, for a fee, guarantee wholesale funding of Australian incorporated banks and other authorised deposit-taking institutions (ADIs) (including credit unions, building societies). The guarantee will be enacted through a government facility in which the institution pays a fee for the credit enhancement. There are no details of the fee determination mechanism but surely less credit worthy institutions will pay more for the fee than higher rated entities. Presumably this guarantee will apply to all non-deposit liabilities of banks and ADIs, although the statement from the PM refers to term funding but also non-deposit liabilities). This facility will be in place until financial market conditions normalise (there is no definition of normal).
- **The Australian Office of Financial Management (AOFM) will buy another \$4bn of residential mortgage backed securities (RMBS).** This is in addition to the \$4bn of RMBS purchases announced last month. The aim of this policy is to stabilise the RMBS market and ensure continued access to funding for non-ADI lenders (ie. lenders who are not banks, building societies or credit unions).

Full access to global funds is crucial for the proper functioning of the local banking sector

Of these policies the guarantee of wholesale funding for institutions is the most important. These are all the non-deposits liabilities of ADI's. As similar guarantees had already been announced by European governments, the absence of this guarantee would have put local banks and ADIs at a significant disadvantage in attracting global wholesale funding.

As wholesale markets account for around one half of the Australian financial sector's funding, full access to this source of funds is crucial for the proper functioning of the local banking sector. It is hoped that a sovereign guarantee for wholesale bank funding will also help to cap the cost of such funding, but that is not to say that the price of credit will rise further from here.

As this guarantee for deposits and funding applies equally across the banks and ADIs a consequence of this policy is may be that the Australian finance sector will not experience the same degree of consolidation that is now occurring in the US and European banking sectors. Likewise, the government's increased purchase of RMBS aims to create a more "level playing field" between the major banks, ADIs and non-ADIs. It remains to be seen if these outcomes are achieved. Large financial healthy institutions should continue to have an advantage over smaller more risky operations, even if this is via the cost the Government charges for the various guarantees.

In the long run these policies will hopefully mean that credit conditions are not squeezed as tight as offshore.

In the long-run, it is hoped that this will mean that access to credit for households and businesses in Australia is not squeezed to the same extent that is now occurring offshore (ie. in the US the combination of soft demand and constrained supply saw household credit decline in August).

The Australian policy is consistent with the G-7 Finance Ministers and Central Bank Governors Plan of Action

## Part of a global response

The policy response to the global financial crisis has moved into the sovereign jurisdiction. Policies will therefore be announced on a government-by-government basis. But these policies should together be seen as part of a co-ordinated, global response to this crisis.

The Australian government's policy announcement is consistent with the G-7 Finance Ministers and Central Bank Governors Plan of Action announced over the weekend:

*The G-7 agrees today that the current situation calls for urgent and exceptional action. We commit to continue working together to stabilize financial markets and restore the flow of credit, to support global economic growth. We agree to:*

1. *Take decisive action and use all available tools to support systemically important financial institutions and prevent their failure.*
2. *Take all necessary steps to unfreeze credit and money markets and ensure that banks and other financial institutions have broad access to liquidity and funding.*
3. *Ensure that our banks and other major financial intermediaries, as needed, can raise capital from public as well as private sources, in sufficient amounts to re-establish confidence and permit them to continue lending to households and businesses.*
4. *Ensure that our respective national deposit insurance and guarantee programs are robust and consistent so that our retail depositors will continue to have confidence in the safety of their deposits.*
5. *Take action, where appropriate, to restart the secondary markets for mortgages and other securitized assets. Accurate valuation and transparent disclosure of assets and consistent implementation of high quality accounting standards are necessary.*

*The actions should be taken in ways that protect taxpayers and avoid potentially damaging effects on other countries. We will use macroeconomic policy tools as necessary and appropriate. We strongly support the IMF's critical role in assisting countries affected by this turmoil. We will accelerate full implementation of the Financial Stability Forum recommendations and we are committed to the pressing need for reform of the financial system. We will strengthen further our cooperation and work with others to accomplish this plan.*

Source: <http://www.ustreas.gov/press/releases/hp1195.htm>)

The Australian government announcement is also consistent with policy arrangements announced by the UK, Ireland and New Zealand.

### **UK Treasury – 8 October 2008**

*"...the Government will make available to eligible institutions for an interim period as agreed and on appropriate commercial terms, a Government guarantee of new short and medium term debt issuance to assist in refinancing maturing, wholesale funding obligations as they fall due. Subject to further discussion with eligible institutions, the proposal envisages the issue of senior unsecured debt instruments of varying terms of up to 36 months, in any of sterling, US dollars or Euros. The current expectation is that the guarantee would be issued out of a specifically designated Government-backed English incorporated company. The Government expects the take-up of the guarantee to be of the order of £250bn, and will keep this under review alongside ongoing monitoring of capital positions and lending volumes "*

Source: [http://www.hm-treasury.gov.uk/press\\_100\\_08.htm](http://www.hm-treasury.gov.uk/press_100_08.htm)

Similar policy arrangements have been announced by the UK, Ireland and New Zealand.

**Irish Government - 29 September 2008**

*“The guarantee is being provided at a charge to the institutions concerned and will be subject to specific terms and conditions so that the taxpayers’ interest can be protected. The guarantee will cover all existing aforementioned facilities with these institutions and any new such facilities issued from midnight on 29 September 2008, and will expire at midnight on 28 September 2010. “*

Source: <http://www.taoiseach.gov.ie/index.asp?locID=586&docID=4026>

**New Zealand – 12 October 2009**

*The Minister of Finance announced today that the Government has introduced an opt-in deposit guarantee scheme. The scheme covers deposits for New Zealand-registered banks and eligible non-bank deposit-takers (including banking societies, credit unions and finance companies)...Eligible financial institutions, will be New Zealand registered banks and non bank deposit-taking financial institutions, who are fully compliant with the requirements of their trust deeds...The guarantee will be offered for a term of two years...The government will charge a fee for any guarantee offered on amounts in excess of \$5 billion...For covered liabilities in excess of \$5 billion a fee of 10 basis points per anum will be charged for the guarantee. The fee will be charged on the basis of the total covered liabilities, in excess of \$5 billion of the institution.*

Source: RBNZ

## Appendix

### **Australian-owned Banks**

Adelaide Bank Limited  
 AMP Bank Limited  
 Australia and New Zealand Banking Group Limited  
 Bank of Queensland Limited  
 Bendigo and Adelaide Bank Limited  
 Commonwealth Bank of Australia  
 Commonwealth Development Bank of Australia Limited (a subsidiary of Commonwealth Bank of Australia)  
 Elders Rural Bank Limited  
 Macquarie Bank Limited  
 Members Equity Bank Pty Limited  
 National Australia Bank Limited  
 St. George Bank Limited  
 Suncorp-Metway Limited  
 Westpac Banking Corporation

### **Foreign Subsidiary Banks**

Arab Bank Australia Limited  
 Bank of China (Australia) Limited  
 Bank of Cyprus Australia Limited  
 BankWest (the trading name of Bank of Western Australia Ltd, a foreign subsidiary bank following its sale to Bank of Scotland in December 1995)  
 Citigroup Pty Limited  
 HSBC Bank Australia Limited  
 ING Bank (Australia) Limited  
 Investec Bank (Australia) Limited  
 Laiki Bank (Australia) Ltd  
 Rabobank Australia Limited (a subsidiary of Rabobank Nederland from October 1994)

### **Branches of Foreign Banks**

ABN AMRO Bank N.V.  
 Allied Irish Banks, Public Limited Company  
 Bank of America, National Association  
 Bank of China Limited  
 Bank of Scotland plc  
 Bank of Tokyo-Mitsubishi UFJ, Ltd  
 Barclays Capital (the trading name of Barclays Bank plc)  
 BNP Paribas  
 09 December 1992  
 18 September 1986  
 Citibank, N.A.  
 Credit Suisse

Deutsche Bank Aktiengesellschaft  
Fortis Bank SA/NV  
HSBC Bank plc  
Industrial and Commercial Bank of China Limited  
ING Bank N.V.  
JPMorgan Chase Bank, National Association  
Mega International Commercial Bank Co., Ltd.  
Mizuho Corporate Bank, Ltd.  
Oversea-Chinese Banking Corporation Limited  
Rabobank Nederland (the trading name of Cooperatieve Centrale Raiffeisen-Boerenleenbank B.A.)  
Royal Bank of Canada  
Société Générale  
Standard Bank Plc  
Standard Chartered Bank  
State Bank of India  
State Street Bank and Trust Company  
Sumitomo Mitsui Banking Corporation  
The Hongkong and Shanghai Banking Corporation Limited  
The Royal Bank of Scotland Plc  
The Toronto-Dominion Bank  
Taiwan Business Bank  
UBS AG  
United Overseas Bank Limited  
WestLB AG

**Building Societies**

ABS Building Society Ltd  
B & E Ltd  
Greater Building Society Ltd  
Heritage Building Society Limited  
Home Building Society Ltd  
Hume Building Society Ltd  
IMB Ltd  
Lifeplan Australia Building Society Limited  
Maitland Mutual Building Society Limited  
Newcastle Permanent Building Society Limited  
The Rock Building Society Limited  
Wide Bay Australia Ltd  
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**Credit Unions**

Alliance One Credit Union Ltd  
AMP Credit Union Ltd  
Austral Credit Union Limited

Australian Central Credit Union Ltd  
Australian Country Credit Union Ltd (trading as Reliance Credit Union)  
Australian Defence Credit Union Limited  
AWA Credit Union Limited  
Bananacoast Community Credit Union Ltd  
Bankstown City Credit Union Ltd  
Berrima District Credit Union Ltd  
Big Sky Credit Union Ltd  
Broadway Credit Union Ltd  
CAPE Credit Union Limited  
Capital Credit Union Ltd  
Capricornia Credit Union Ltd  
Central Murray Credit Union Limited  
Central West Credit Union Limited  
Circle Credit Co-operative Limited  
Coastline Credit Union Limited  
Collie Miners Credit Union Ltd  
Community Alliance Credit Union Limited  
Community CPS Australia Limited  
Community First Credit Union Limited  
Companion Credit Union Limited  
Comtax Credit Union Limited  
Country First Credit Union Ltd  
Credit Union Australia Ltd  
CSR and Rinker Employees Credit Union Limited  
Defence Force Credit Union Limited  
Dnister Ukrainian Credit Co-operative Limited  
Electricity Credit Union Ltd  
Encompass Credit Union Limited  
Esso Employees' Credit Union Ltd  
Eurobodalla Credit Union Ltd  
Family First Credit Union Limited  
Fire Brigades Employees' Credit Union Limited  
Fire Service Credit Union Limited  
Firefighters & Affiliates Credit Co-operative Limited  
First Choice Credit Union Ltd  
First Option Credit Union Limited  
Fitzroy & Carlton Community Credit Co-operative Limited  
Ford Co-operative Credit Society Limited  
Gateway Credit Union Ltd  
Geelong & District Credit Co-operative Society Limited  
GMH (Employees) Q.W.L. Credit Co-operative Limited

Goldfields Credit Union Ltd  
Gosford City Credit Union Limited  
Goulburn Murray Credit Union Co-operative Limited  
H.M.C. Staff Credit Union Ltd  
Heritage Isle Credit Union Limited  
Holiday Coast Credit Union Ltd  
Horizon Credit Union Ltd  
Hunter Mutual Limited  
Hunter United Employees' Credit Union Limited  
Industries Mutual Credit Union Limited  
Intech Credit Union Limited  
Karpaty Ukrainian Credit Union Limited  
La Trobe Country Credit Co-operative Limited  
La Trobe University Credit Union Co-operative Limited  
Laboratories Credit Union Limited  
Latvian Australian Credit Co-operative Society Limited  
Lithuanian Co-operative Credit Society "Talka" Limited  
Lysaght Credit Union Ltd  
MacArthur Credit Union Ltd  
Macquarie Credit Union Limited  
Maleny and District Community Credit Union Limited  
Manly Warringah Credit Union Limited  
Maritime, Mining & Power Credit Union Limited  
Maroondah Credit Union Ltd  
MECU Limited  
Melbourne University Credit Union Limited  
MemberFirst Credit Union Limited  
MyState Financial Credit Union of Tasmania Limited  
New England Credit Union Ltd  
Newcom Colliery Employees Credit Union Ltd  
Northern Inland Credit Union Limited  
Nova Credit Union Limited  
NSW Teachers Credit Union Ltd  
Old Gold Credit Union Co-operative Limited  
Orange Credit Union Limited  
Phoenix (N.S.W.) Credit Union Limited  
Plenty Credit Co-operative Limited  
Police & Nurses Credit Society Limited  
Police Association Credit Co-operative Limited  
Police Credit Union Limited  
Polish Community Credit Union Ltd  
Powerstate Credit Union Ltd

Pulse Credit Union Limited  
Qantas Staff Credit Union Limited  
Queensland Country Credit Union Limited  
Queensland Police Credit Union Limited  
Queensland Professional Credit Union Ltd  
Queensland Teachers' Credit Union Limited  
Queenslanders Credit Union Limited  
Railways Credit Union Limited  
RegionalOne Credit Union Limited  
Resources Credit Union Limited  
R.T.A. Staff Credit Union Limited  
Satisfac Direct Credit Union Limited  
Savings and Loans Credit Union (S.A.) Ltd  
Select Credit Union Limited  
Service One Credit Union Limited  
SGE Credit Union Limited  
Shell Employees' Credit Union Limited  
South West Slopes Credit Union Ltd  
Southern Cross Credit Union Ltd  
South-West Credit Union Co-operative Limited  
St Mary's Swan Hill Co-operative Credit Society Limited  
StateWest Financial Services Limited  
Sutherland Credit Union Ltd  
Sutherland Shire Council Employees' Credit Union Ltd  
Sydney Credit Union Ltd  
Tartan Credit Union Ltd  
The Broken Hill Community Credit Union Ltd  
The Gympie Credit Union Ltd  
The Police Department Employees' Credit Union Limited  
The Summerland Credit Union Limited  
The TAFE and Community Credit Union Ltd  
The University Credit Society Limited  
Traditional Credit Union Limited  
TransComm Credit Co-operative Limited  
United Credit Union Limited  
Victoria Teachers Credit Union Limited  
Wagga Mutual Credit Union Ltd  
Warwick Credit Union Ltd  
WAW Credit Union Co-operative Limited  
Westax Credit Society Ltd  
Woolworths Employees' Credit Union Limited  
Wyong Council Credit Union Ltd



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