NEP panellists unanimously condemn the behaviour of Australia's retail banks, calling for radical overhauls

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A question on whether badly-behaving retail banks can be reined in has delivered the first-ever unanimous response from panellists to an NEP poll.

In the wake of the Royal Commission's findings of gross malpractice by the big retail banks in Australia, a selection of the nation's top economists were asked whether anything could be done to improve banks' behaviour. Panellists were asked to respond to the following proposition:

> *There is no way to significantly increase the degree to which Australian retail banks act in the interests of consumers.*

The 20 economists out of 50+ who chose to respond – all academics, bar one – were in unanimous disagreement with the proposition that nothing could be done. More striking even than the unanimity and low response rate, this month's poll results delivered a wide breadth of suggestions from panelists about what can be done. The majority answer is that current regulations should be improved: i.e., that we should install more overseers who implement more rules. Mathew Butlin's comments typify the "regulation" approach of most respondents:

> "The incentive structures for bank staff, from the top down, play a key role in shaping behaviour. A more complete set of performance measures linked to remuneration that strongly penalises behaviour not in the consumer interest would provide stronger incentives for better behaviour, especially when linked with reliable information on non-compliance going to management and ultimately the bank board and a requirement for both to take action."

The key words here are 'performance measures', 'compliance' and 'requirement'. Similar terms that convey the same idea were 'performance based regulation' (Uwe Dulleck), '[royal commission] recommendations' (Tony Makin), 'transparent' (Brian Dollery), 'to..mandate..bankers' (James Morley), 'prudential regulation' (Brian Dollery), 'accountable' (Beth Webster, Lata Gangadharan), and 'transparent requirement' (Jeffrey Sheen). Beth Webster and Allan Fels also mentioned the culpability of banking culture, and Allan Fels specifically singled out the cultures at APRA and ASIC, though without suggestions of how to produce change; as he writes, "[t]his will prove to be harder to do than it sounds. People have been talking for over twenty years about the ASIC and APRA culture needing improvement."

John Quiggin, Gigi Foster, and Allan Fels all quite openly doubted that any type of regulation would help, because none of them trusted the current regulators or the politicians to devise and truly enforce good regulations, whatever those regulations would be. They called for very different approaches. Paul Frijters did not respond to the survey because he was instrumental in setting the question – although his co-question writer and co-summariser Gigi Foster clearly did not feel the same compunction! – but his answer would have been in line with these three.

Allan Fels gave the most damning answers and openly questioned the ability of both the government and the current regulators to escape their current lack of morality. His main practical recommendations were to regulate fees and have external authorities, though he was not optimistic about either since he recognised they were both more of the same as what has hitherto failed. One suggestion by Paul Frijters in his direction is to copy the example of the Netherlands and cap the total payments to whole layers of the sector, such that for instance no one in the finance industry is allowed to earn above a certain threshold amount (such as 150% of what the prime minister earns).

In the same 'broad legislation' vein, Geoffrey Kingston recommended mandatory minimum sentences for financial crimes, arguing that at the moment the law courts are complicit in the maintenance of financial crimes by being reluctant to jail white-collar criminals. Similarly, James Morley and Gigi Foster suggested the revocation of operating licenses as another legal stick to apply against naughty banks. Like Joaquin Vespignani, Geoffrey Kingston also flagged the sector's oligopolistic nature, before then raising the hope that the "big data" revolution would democratize banking and re-empower consumers, similar to the hope that presumably underpins the Australian government's Consumer Data Right initiative. Also targeting market concentration, Allan Fels, James Morley, and John Quiggin all called for the separation of banking powers into different units, à la Glass-Steagall in the US, presumably in order to bring about the diffusion of power and profitability across a larger number of institutions.

Gigi Foster called for foreign regulators, i.e., she wants us to admit the reality that any Australian regulator would be corrupt. She wants foreign countries to send competent regulators to sort out the Australian banking system, just as if financial regulation were an international test match wherein one could not trust domestic referees.

John Quiggin calls for a 'no frills' public bank modelled on the Kiwibank of New Zealand, essentially saying that the government should provide competition itself because no regulator can be trusted to truly enforce pro-competition measures. This is a suggestion also made by Gigi Foster and that Paul Frijters also endorses.

What are the main barriers to implementing any of these diverse approaches to curing the banks of their bad behaviour? It seems clear that at least some barriers are not economic: our best economists, like well-meaning doctors, see prescriptions that "should" work despite the clear evidence that the patient is dying. This strongly indicates that some barriers are not in the medicine available but in the way it is administered, implying that the way forward must involve in some way to disrupt political links or processes related to running the banking system. As John Quiggin states, "These proposals may be beyond the realm of political feasibility," or to repeat Allan Fels' more blunt statement, "I do not have great confidence in politicians fixing the problems." The suggestion of recruiting international regulators is in line with this reasoning that the problem is at least in part political.

The second major ingredient required to discipline the banks is the bread and butter of economists: the removal of the large incentives available to those willing to behave badly enough to get them. Salary caps for bankers, fee caps, minimum jail terms for white-collar crimes, license revocation, and the creation of a public bank are all means of trying to take money previously available to bankers off the table, thereby – hopefully – putting it back into the pockets of everyday Australians. Of course, to do this requires, yet again, political will. Does Australia have enough of that scarce commodity to meet the country's clear demand? Time will tell.