Proposal
Establish Australian Development Bank

I suggest the ADB (Australian Development Bank) should exactly mirror the old CDB (Commonwealth Development Bank) established in 1959 and taken over / closed down in 1995.

The late Ron Ramsdale, prior to his retirement, held the positions of State Manager, Western Australia and later Victoria, for the Commonwealth Development Bank of Australia. The following comes from an article written by him and reported in the News Weekly in July 1998.

The CDB was initially funded by a special capital injection of $1 million from the Federal Government. From that time onwards, its ongoing lending program was funded from retained profits, from term deposits raised from the public, and from the money market at favourable rates of interest obtainable because the bank was guaranteed by the Federal Government which had a AAA credit rating.

Under its charter, the CDB was required to provide loans to persons and business enterprises engaged in primary and secondary industry where, in the opinion of the Bank, such financial assistance resulted in an increase in productivity and was not otherwise available on suitable and reasonable terms.

Consequently, its role was to supplement other sources of finance and to follow a lending philosophy under which prospect of success, rather than value of security, was the primary consideration. As a supplementary lender, the CDB would not consider an approach until an applicant had first unsuccessfully discussed his requirements with, at least, his own trading banker.

As security was not the primary consideration in CDB's lending, the raw materials upon which the Bank worked were:

* The person - his integrity and his managerial capacity;

* His financial position - his assets, his liabilities (with their repayment implications) and his equity in his venture;

* His property - its inherent potential, its existing state of improvement and its past performance (if any); and

* His program - its technical feasibility, its productive potential and its economics.

In the assessment of lending proposals and in the absence of security being the prime consideration to a loan being approved, the CDB was staffed by highly experienced and competent lenders to assess the long-term viability of proposals.

To assist in this process, the staff included a range of specialists qualified in the areas of agricultural science, economics, management, accounting, and engineering. They spent much of their time in the field undertaking assessment and investigation work.

In determining the inherent prospects of a lending proposal, it was the practice of CDB to prepare budgets of estimated income and expenditure.

Frequently budgets were projected over a number of years, until the stage was reached where the full expected outcome of the development program was reflected in the projections of income and outgoings.

This budgeting process enabled the Bank to assess the ability of the applicant to repay his overall borrowings, including the proposed Development Bank loan.

In all cases, the term of the loan was based on the Bank's assessment of the ability of the applicant to repay without undue strain, with an appropriate principal repayment holiday being granted in particular circumstances.

Major impact

The CDB is no longer in existence, but during its first 30 years, it fulfilled a very meaningful role in the banking industry by helping almost 400,000 businesses.

In its formative years, the Development Bank was heavily involved financing individual farmers who took up holdings in the Ord River project, the Esperance Land Settlements Scheme in Western Australia, the Coleambally Irrigation Scheme in New South Wales, the Brigalow Scheme in Queensland and the Heytesbury Scheme in Victoria, to name a few.

In the opinion of the writer, the Commonwealth Development Bank played a most significant role during its lifetime in the development of rural and industrial undertakings and was the catalyst for the economic success of many individuals and entities who/which otherwise would have been denied the opportunity to have made a meaningful contribution to the Gross National Product and the nation's overall quality of life.

HOW ADB WILL LOWER INTEREST RATES

1. The major banks are credited rated at AA whereas the Australian Government is rated AAA and therefore can borrow at at least ½% better than the major banks.

2. The major banks charge line fees, at present 2 – 3% over BBSW and plus another margin to create their profit. There is no need for ADB to charge more than a token 0.1% line fee.

The justification to the establishment of this bank is the fact that the major banks work on a cost plus policy to create profits. The injustice is that they can then pass off their costs and profit margin to the rural community (and others); this is accepted as good prudent governance by the banks but is a direct cost to their rural customers.

These rural customers cannot pass on these direct overhead costs to anyone else. Therefore I suggest that the rural industries should be given relief particularly from bank charges and interest charges **provided there is no subsidisation <u>or</u> cost to the Australian Tax Payer.**

PRESENT MAJOR BANK LENDING PROFILE

Financial Institution	ANZ	CBA	NAB	WBC	Suncorp	Total
Date	30/09/2009	31/12/2009	30/09/2009	30/09/2009	31/12/2009	
Value	B$	B$	B$	B$	B$	B$
Segment						
Consumer	191.65	352.32	218.24	177.27	29.00	968.48
Agriculture	17.07	16.40	13.54	6.34	3.40	56.74
Mining		4.80		1.67		6.47
Manufacturing	16.98	15.90	7.41	11.36	4.10	55.74
Energy & Utilities		8.80		3.26		12.06
Construction	8.21		3.68	4.58		16.47
Retail & Wholesaling	24.87	17.60				42.47
Transport	7.37	9.70		7.05		24.13
Trade				11.60		11.60
Banks	59.44	65.90	15.17	58.88		199.39
Finance - other		29.00				29.00
Business Services	8.82			6.81		15.63
Property	30.49	50.00	33.70	28.67	11.50	154.36
Sovereign/Government	15.29	28.20	1.17	8.26		52.92
Health & Community						0.00
Culture & Recreation	8.55			4.24		12.79
Other - Commercial & Industrial			41.73			41.73
Other	18.94	52.80	17.35	8.13	4.10	101.32
Total B$	407.67	651.42	351.97	338.11	52.10	1,801.27
	4.20%	2.50%	3.80%	1.80%	6.50%	3.15%

Banks are lending $1,801,270,000,000
It is expected that the four major banks will report a net profit after tax of over $20 billion.

Agricultural lending by the major banks total about $56.74 billion
Surprisingly only 3.15% of Major Bank lending is in Agriculture – as low as only 1.8% by Westpac.

Assume that the ADB could lend up to 10% of this value – say $5.6 billion.

NB The ADB is only a lender of last resort, i.e. the customer must be refused credit by its present bank. The ADB lending would be secured on a 2nd mortgage. The client remains a client of his present bank.

This bank lending profile highlights two facts

1. The total insignificance of bank lending to Agriculture in the big picture.

2. The most important thing that hit me was that every category on the list operates on the principal of cost plus to make a profit – EVERY CATEGORY EXCEPT AGRICULTURE

Setting up the Australian Development Bank Requires

1. Commonwealth Government guarantee
2. Expertise

Theoretical Bank Budget Comparison

	ADB	**Major Bank**	
Wholesale Cost of Funds	4.50	4.5	
Bank Borrowing Margin	0.25	0.75	
Risk Margin	0.50	0.50	
Bank Operating Cost	0.50	0.50	
Line Fees	0.10	2.5	(2 – 3%)
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	5.85%	8.75%	

Proposal

The Federal Government appoints a board of independent directors.
The Federal Government provides a Bank Guarantee to borrow money.

I suggest that ADB could be established by:

1. ADB becomes a new bank from scratch.
2. ADB takes over the Agricultural bank business of Suncorp.
3. ADB takes over the Rural Bank of Victoria.

We must ensure the ADB operates under a similar charter to the old CDB.

The ADB must be set up with high quality officers. Suncorp has recently shed quite a few experienced staff, plus head hunt experienced agricultural people from other banks, preferably with degrees in agriculture, accounting, economics, geology and engineering.

The Federal government provides no cash to the ADB.

The Federal Government only provides the guarantee for the source of funds.
The farmer / borrower provide security for the loan with the bank and makes repayments to ADB. This is normal banking practice and ADB would operate as a normal bank. Very few rural loans end in default and banks loose very little money on bad debts on rural land. The price of rural land does continue to increase, i.e. the banks security continually increases, and thus the Federal Government could provide an ADB that could genuinely help rural producers at no cost and no subsidy.

There is a need for this Australian Development Bank

1. There is no doubt that lower interest rates are needed in rural Australia. The Major Banks need to charge higher interest rates to satisfy their investors. Rural producers need an alternative.
2. Banks will argue that pre the Global Financial Crisis that risk costing was too low and was repriced upwards but is now falling. This risk pricing would also fall for ADB.
3. Banks will argue that they are seeing more competition coming into the market amongst the four Major Banks and this will gradually reduce line fees down to perhaps under 2%
   Banks don't want any other competition
   But
   If the ADB was operating I suggest there would be more competition to the big Banks.
   Don't forget all the Major Banks are doing with competition is competing to reduce the present screwing of the rural producer.
   It was reported by AFG (a big mortgage group) that housing finance by the major banks fell to 82% in March 2010 with non major banks accounting for 18% of all new housing loans.

The Australian Housing Market has alternative sources of finance. Rural Producers and secondary industry requires the same opportunities.

4. There is a need to have the opportunity to borrow when the producers
   current bank won't lend any more because the customer has reached the bank limit of his securities.

   The original CDB lent to approximately 400,000 clients over the 36 years of its existence.

   There are plenty of opportunities for the ADB to lend to increase productivity – loans not available on suitable and reasonable terms from major banks.

   For example
   - Irrigation efficiencies up and down the Murray Darling Condamine system and any other irrigation development.
   - More watering points in the North to increase carrying capacity

- Money to contract blade plough or Hire Purchase / Lease money to purchase crawler tractor, blade plough, etc to do your own development to increase carrying capacity
- Purchase additional areas to create size efficiency.

The ADB would look at a client's development program, its technical feasibility and its productive potential to decide on a loan.

Why Primary Industry should be given reduced interest rates

1. Every segment of bank lending works on a cost plus formula to make a profit – subject to competition.

2. Wage and salary personnel
   Protected by a minimum wage which is adjusted up taking into account the cost of living.
   Also that we have unions and private negotiated contracts that ensure wages and salaries go up – e.g. Teachers 10% pay rise over 3 years to cover cost of living

3. The Mining Boom
   As this AUSTRALIAN WONDER continues, the general population gets more affluent – the RBA raises interest rates to control inflation. This will automatically increase the value of the Australian dollar (without any other overseas influence).

Then the primary producer has to pay the minimum wage increase – he pays more for transport, all the increased cost as a result include interest.

As the A$ goes up, farmers and graziers income must go down when they sell to the Abattoir or the Grain Exporter or the Milk Processor.

The Australian primary producer is stuffed unless they increase their efficiency and production and gets some protection from this apparent and obvious long term trend.

The Australian Development Bank would be the vital first step to provide an institution that could supply loans to increase the efficiency and productivity on suitable and reasonable terms.

Additional Supplementary Information

1. The lending of the ADB is not restricted to any size loan – big or small, as long as it is consistent with the charter of the bank to increase efficiency and production.

   The loans will be available to all primary and secondary investments in rural Australia. This clause will ensure that the ADB cannot cause market aberrations by giving any advantage to any group in the rural community.

2. The Bank will be available to encourage and supplement in any way the decentralisation of rural Australia that both major parties seem to be recognising.

3. Other major countries are using their financial strength and guaranteeing credit availability to their own corporations to take over Australian assets.

   We need similar access to Australian Government guaranteed credit to compete with these countries. Countries such as China, Brazil and Malaysia, have taken equity in Australian industries e.g. Swifts, in the meat industry. China is reported to have invested $55 billion in the take over of Australian companies in the last five years - $22 billion in 2009.

   Other corporations in countries such as Japan, Italy, USA, UK, India and the UAE have access to loans in their own countries that are extremely low. These foreign corporations have been able to take over whole Australian industries, e.g. Japan through Kerin and Italy through Parmalot totally control the Australian fresh milk industry. Our sugar industry has just met the same fate.

   This ADB will significantly help retain these VITAL ASSETS in Australian ownership.

4. Our own four major Australian Banks are obviously focused on lending the vast majority of their loans to the Australian Housing Industry. Over 50% of their lending goes to this totally unproductive segment of the Australian economy.

   The ADB will be an alternative source of funds to productive industries. We need a source of finance to keep funds flowing to the bush. The major banks - in their wisdom – decided that there were two businesses in rural Australia

   viz. an income producing business such as cattle raising, grain and sugar production, etc

   And a real estate business

   In the immediate past, these banks have significantly lent on rural real estate with little regard to the ability of the business to make repayments. Now these Banks have seriously withdrawn credit from the bush.

   The ADB charter is specific – to lend on the project viability and the ability of the customer to have a viable business with much less emphasis put on security and asset backing.

The ADB charter will ensure that there will be credit available in the bush – (decentralised area). Cattle finance has become very difficult since the G.F.C. Our banks have changed policies on the old sources of money – the old stock houses are not what they were – and now NZ companies are using NZ Banks through NZ companies are starting to provide this source of finance.

Why not from an Australian Bank?

5. The Economic Ratbags will consider two main points.
   a) Will this new bank direct money from other more worthy Australian enterprises
   b) Or will it adversely affect any other segment of investment or any other corporation.

a) The ADB will source credit using the Federal Government Guarantee that is not being used at present (except perhaps in the roll out of the news cable net worth)

Remember this ADB is not another QIDC or Rural Reconstruction Board. It will be a serious Bank with independent directors that will be held responsible as any other professional directors.

The bank will have security for any loans provided by farmers and graziers. The rural people will be responsible to repay these loans just as they are now to any major Bank.

b) The ADB will certainly provide competition to the major banks.

The table presented shows that the average lending to Agriculture is only 3.15% of total bank lending. This ADB will not replace that present lending but will lend to increase efficiency and production in decentralised areas. These Major Banks will make over $20 billion net profit after Tax this year. They can hardly cry poor that this new bank will be anything but a flea bite.

In fact the major banks prime security will be increased with developments being carried out on their first mortgaged secured assets. Thus they should be able to post additional profits by snaffling the risk margin they had already built into each and every loan they made in the decentralised area (bush) or so they tell us.
Surely the Major Banks cannot object to a Federal Government Guarantee to establish the ADB after these four banks were Federal Government Guaranteed during the GFC at the expense of all other banking and financing institutions – These banks received massive inflows of Australian savings from their oppositions during the crisis.

I can't see that the open market / level playing field ideals of the Economic Ratbags would affect the flow of money from Banks to other segments of industry would be affected because the ADB is essentially tapping a new source of finance.

At lease it is a channelling of finance to a productive and export earning enterprise vs. what the banks majority of loans go to now – about 54% to building non-earning houses, etc.

I ask that this meeting endorses the immediate establishment of the Australian Development Bank and formally puts this proposal to the Australian Government.

John McNamee