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Dear Mr Bull

Submission on proposed merger of Westpac Banking Corporation and St George Bank Limited

The Finance Sector Union (FSU) represents 50,000 members employed in the finance sector across Australia, with the majority of these employed in the major banks.

Our knowledge of the industry, and the experience of our membership, provides the FSU with a unique perspective of the needs of consumers and other stakeholders in banking. The FSU has seen the consequences of many mergers in the finance sector over the past few decades and has strong reservations about the proposed acquisition of St George Bank Limited (St George) by Westpac Banking Corporation (Westpac). We do not believe the proposed merger will enhance the welfare of Australians through increased competition within the industry.

We submit that the ACCC should block the proposed merger on the basis that:

- it will remove an effective and vigorous competitor from the market;
- barriers to entry make it unlikely that a new effective and vigorous competitor will emerge;
- a substantial lessening of competition will occur in markets for transaction accounts;
- it will result in substantial employment losses;
- there will be an increased likelihood of less competition in the banking sector through the four major banks launching takeovers for the remaining smaller players.

The proposed merger presents numerous issues and the FSU has done its best to produce a submission within the time available. Given the size, complexity and importance of the proposed merger we would encourage the ACCC to release a 'statement of issues' and establish a secondary timeline to ensure wide consultation over a longer period of time.

We note that the ACCC is moving away from simple quantitative or market share thresholds in determining whether a substantial lessening of competition has occurred. We understand and, to a certain extent, endorse these sentiments. However, we still believe that market share data can be useful to get a preliminary perspective on what the post-merger market might look like. We understand the reasons why the ACCC declined to give the FSU access to its data but we would argue there is a bigger principle at stake – meaningful and informed public consultation on mergers. Information could be shared with interested parties on a confidential basis – this could only assist the quality of the ACCC's assessment processes.

Furthermore, we understand that section 50 of the *Trade Practices Act 1974 (Cth)* contains a ‘substantial lessening of competition’ test but does not include an assessment of ‘the public benefit’ (as might be considered in an authorisations context). The FSU firmly believes that it should; especially when considering mergers of essential services providers. The FSU has advocated these views to government and will continue to do so.

The FSU is concerned that while there are mechanisms to identify competitive and prudential problems with bank mergers, there is no mechanism to evaluate the impact of mergers on people, communities (particularly rural and regional communities) and society. We agree wholeheartedly with the sentiments of the Consumer Action Law Centre who observed that:

“. . . the consideration of social issues in bank mergers is an issue that tends to fall between the regulatory cracks in Australia.”¹

Market definition and concentration

We note the Commission’s previous position in adopting a state based market definition for transaction accounts and deposits. Regardless of whether this definition is retained or changed to a national market we submit that the merger will entrench a two tiered concentrated market where players are simply big or small. We believe this is supported by the data in confidential **attachment 1** which shows market share for deposits, transaction accounts, home loans and credit cards.

Removal of a “vigorous and effective competitor”

“Maverick firms may drive significant aspects of competition, such as innovation or product development, even though their own market share may be modest.”²

The FSU submits that St George fits this description and the merger would effectively result in their removal from the market which must be considered under section 50(3)(h).

St George Bank has successfully differentiated itself from competitors by building a customer friendly brand, focussed on product innovation and local communities. This strategy has successfully evolved from their long history as a local building society and more recently as a bank. We submit that part of the reason St George has been so successful is its longevity, which in turn helps to establish the critical elements of trustworthiness and reliability which are essential to gaining and retaining bank customers. In 1979, St George had 130 branches and 800 staff. The combined group today has 357 branches and employs over 8,000 staff (approximately a third the size of one of the major banks).

Its last reported profit was \$1.19 billion and it continues a remarkable run of over 20% return on equity. Its share price continues to out perform Westpac’s and has done for at least the past 5 years.

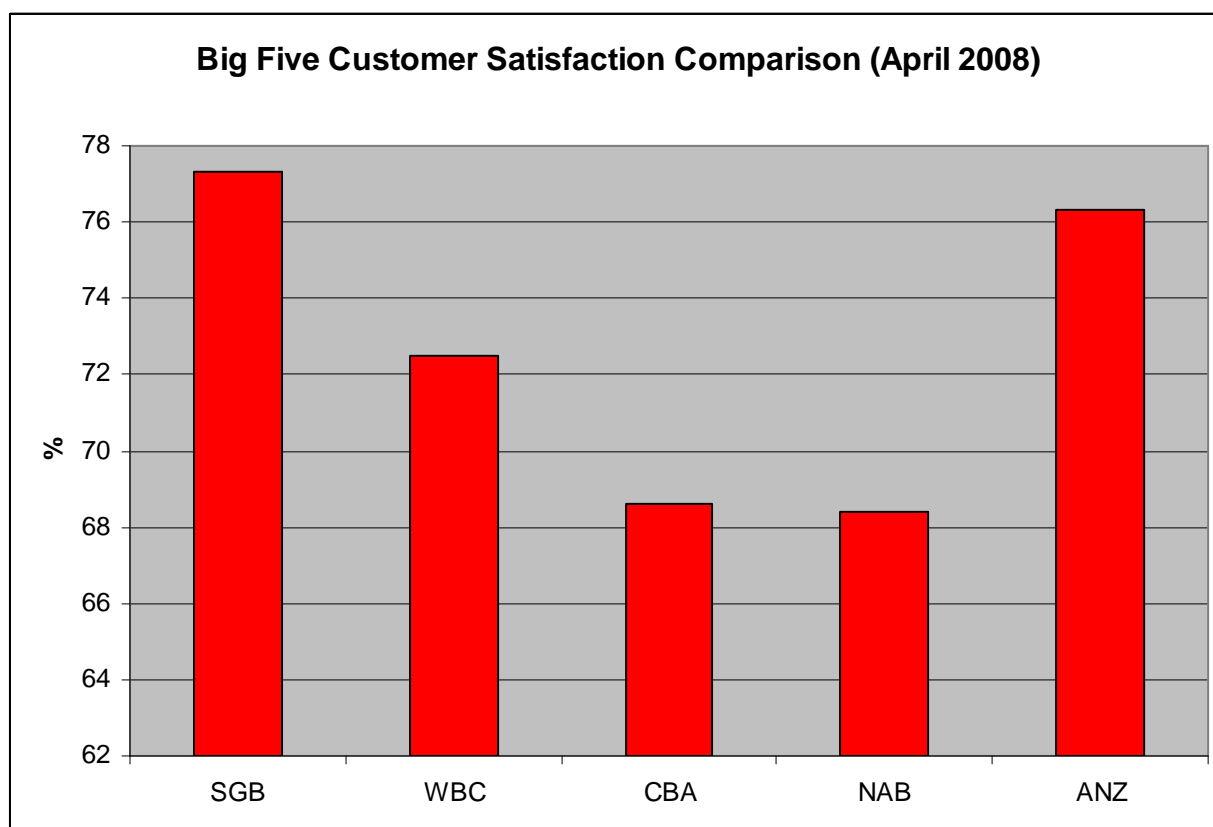
¹ “Defining ‘public benefit’ - Social and Environmental Considerations in Part VII of the Trade Practices Act 1974 (Cth)” *Consumer Action Law Centre*, August 2007

² *ACCC Merger Guidelines 2008*, page 44.

Customer satisfaction

St George's niche positioning strategy in the banking market is reflected through its continued leadership in customer satisfaction ratings. Since 2001, St George has rated as much as 10% higher in customer satisfaction than Westpac. Most recent results show St George at 77.3% very or fairly satisfied customers against Westpac's 72.3%. Five percentage points are very telling in this measure.³

Chart 1: Comparison of "Big Five" Customer Satisfaction (6 Months to April 2008)⁴



The FSU believes that St George have pushed other market participants to improve their customer service and product offerings. Since its inception, St George's customer focused approach has seen it become an innovator and developer of products and services which are now common place. These include extended branch opening hours, automatic teller machine networks and call centres that approved personal loans⁵.

Examples of St George's product innovation include being one of the first financial institutions to offer their customers Visa Debit Cards (or Visa Payment Cards) in 1985. Due to the advent of online internet services, the popularity of such debit cards has increased and is now offered by other banking institutions.⁶ St George has also led

³ Roy Morgan Data (as cited in *The Sheet*), 28 May 2008

⁴ Roy Morgan Data (as cited in *The Sheet*), 28 May 2008

⁵ "As small banks innovate, the big four salivate", *Sydney Morning Herald* (16/05/08)

⁶ "Go into Debit", *Sydney Morning Herald* (6/12/2006)

the market in embracing new technology by introducing a new feature of SMS and email alerts to allow customers to monitor the activity of accounts.⁷

Such product development is vital to St George's niche role and sets it apart from the 'four pillars'. The FSU maintains that should St George be acquired by Westpac, the incentive for product innovation and differentiation would be compromised and have significant repercussions for competition within the finance industry. We submit that this will occur even if the two brands are maintained in the market. (Retention of brands is discussed in a latter section).

Employee satisfaction

St George employee satisfaction is the envy of its competitors. They have improved their employee satisfaction ratings from 48% in 2002 to 75% in 2007. Undoubtedly, this is a result of the different position they have taken in the market, built on a strategy of:

“pursuing low-risk, organic growth strategy that focuses on forming strong customer relationships, building our internal culture and making our operations as efficient as possible.”⁸

Our experience also clearly shows that St George's industrial practices and management have helped to deliver high employee satisfaction ratings, this has resulted in higher staff retention and pushed the other major banks to effectively 'lift their game'. For these reasons we believe that St George plays a critical role in the market that goes well beyond its market share percentages.

Profitable and solid

St George has almost 10% of all retail deposits and home loans in Australia.⁹ In the last six years it has doubled its dividend payout to shareholders and remains on track to deliver a target of 10% earnings per share growth for 2008.

Its home loan portfolio, deposits, business banking and wealth management are all enjoying growth with their overall market share increasing from 8% to 8.2% last financial year.¹⁰ Both the CEO and Chairman of St George were optimistic about St George's future at the 2007 AGM and confident of delivering performance targets.

As one investment manager noted:

“By January, when St George obtains elements of advanced risk accreditation from the regulator, its capital burden should fall substantially. In fact, it will likely be the most well-capitalised bank of them all in Australia.”¹¹

Consequently, we submit that reports about St George being unable to stand alone as a result of the rising cost of obtaining credit are grossly overstated.

⁷ “SMS Email alerts”, *St George Website* (retrieved 20/06/08)

⁸ St.George Bank Ltd CEO Address to AGM 2007, p. 8

⁹ APRA, 2008.

¹⁰ St.George Bank Ltd CEO Address to AGM 2007, p.5

¹¹ Dushko Bajic as quoted in, “St.George deal stinks, says big shareholder.” *The Australian* p.19. 22/5/08

St George and its effect on the market

We note previous comments by the ACCC about the importance of St George¹² in maintaining a healthy level of competition in the retail banking markets. We submit that the increasing dominance of the four major banks makes the role played by St George even more critical.

For the reasons outlined we believe that St George can be characterised as a ‘vigorous and effective competitor’. It has been very successful by deliberately differentiating itself from the major players and consequently plays a very valuable role as a market innovator and provider of superior customer service, which in turn forces other market participants to respond. The removal of St George from the market would have a detrimental effect well beyond its modest market share and would have negative consequences for the entire market which would translate into negative consequences for consumers.

Job losses

A primary concern for the FSU is, unashamedly, the potential loss of jobs as a consequence of the proposed merger. We understand that the ACCC does not specifically consider job losses, however FSU believes that mass job losses (whether by attrition or redundancies) is a significant consequence of any merger and should not be overlooked. Our past experience indicates that if the merger proceeds, it is reasonable to anticipate a significant number of jobs will be lost.

Across the two entities, several thousand staff are employed in the two head offices, administrative divisions including back office processing and in call centres. The FSU is concerned that the duplication of functions in the merged entity is likely to result in significant job losses in the administrative and shared services areas of one or both of the entities. **Attachment 2** sets out the non-branch networks of St George and Westpac in various states.

FSU estimates that at least 5,000 jobs will be lost purely as a result of amalgamating the support functions of the banks should the merger proceed.

FSU estimates of job losses in previous mergers are as follows:

- Commonwealth/State Bank of Victoria – 8,000
- Westpac/ Bank of Melbourne – 1,400
- Commonwealth/ Colonial – 4,500

While an increased ‘footprint’ of branches is likely, past experience suggests that rationalisation of those locations with duplicated branches across the merged entity is inevitable. FSU is concerned that the combined effect of the change in management structure and philosophy and the cuts in employment levels resulting from the merger will have detrimental effects on the service that customers will receive from the network of merged branches and agencies.

¹² R Jones, “ACCC’s perspective on the future of the regional banking in Australia”, ACCC, 2001

FSU is also concerned that any job creation opportunities will be lost offshore to low cost centres as has been witnessed in most of the major banks in recent years, with Westpac and St George being consistent adopters aggressive off-shoring strategies.

Forecasts indicate that the merger would not deliver positive earnings until 2011, i.e. some three years after the two companies come together.¹³ In this environment, FSU's experience suggests that those employees who remain in employment immediately following the merger can expect a long period of uncertainty. The FSU is concerned about the effect such uncertainty and instability to the occupational health and safety of staff in the lead up to the merger and during the merger implementation process.

Branch closures

Westpac has signalled in their merger proposal document that there will be 'no net reduction' in branches. St George has 357 branches, 247 branches are located in the same postcode as Westpac branches. FSU believes that branch closures will be an inevitable outcome if the merger goes ahead and will result in a significant loss of banking services for many communities.

Retention of both brands

Within the merger implementation material that has been released to the market, both parties have stated they will maintain all existing brands with no net reduction in branches. We submit that the ACCC should be concerned about these assertions for the following reasons:

1. The merged entity will move quickly towards shared back office processing and a single management structure. They may appear as two brands in the market but the commercial reality will be one entity. We would argue that this is just the illusion of choice and competition in the market; and
2. Retaining dual branch networks is costly and a key rationale for many mergers is the opportunity to remove duplication and cut costs. Experience also suggests that as soon as any undertakings expire one of the brands will disappear from the market.

Given these factors we remain unconvinced by statements regarding retention of the two brands. We believe such statements are primarily designed to reduce public concerns and clear regulatory hurdles rather than genuinely reflecting longer term commercial intentions or realities.

We also note comments by ACCC Commissioner Ross Jones that:

“... over the years the Commission has received a large number of complaints from consumers particularly after the time period of the undertakings lapsed. In particular, the expectation that Bank of Melbourne would have an identity

¹³ St George and Westpac Merger Implementation Agreement, 26th May 2008

and autonomy independent of Westpac has not been realised, according to complainants.¹⁴

Consequently, we urge the ACCC to be sceptical about the motivation and intent behind statements regarding retention of the two brands.

More mergers, less competition

The FSU appreciates that the ACCC will not engage in speculation in rapidly evolving markets, however if the merger between Westpac and St George goes ahead then it would be very difficult to envisage that further banking mergers would not be pursued by the other major banks.¹⁵

The FSU's experience from previous mergers suggests that 'rationalisation' decisions are often oriented towards short term profit outcomes that have detrimental impacts on the interests of consumers, employees, communities and the industry.

The FSU strongly believes that the ACCC must look at the totality of the proposed outcome and all the flow-on effects of the merger. The FSU does not believe it is realistic to look at the proposed merger in isolation. The threat of mass consolidation of 'second tier' banks into the remaining 'big four' banks poses serious questions surrounding competition policy within the finance industry.

The existence of such banks has long been recognised as having an important role in stimulating competition in all Australian banking markets. The Wallis Report in 1997 recognised that not only have regional banks become an increasingly important source of competition, but also have successfully lead the way on service, innovation and pricing on some products.¹⁶

In their paper on competition analysis of Australian bank mergers, Garry Goddard and Greg Walker outlined that such banks:

“. . . were considered to be efficient, innovative, geographically focused, close to their customers and sufficiently differentiated from the 'look-a-like; majors to provide an incentive for the major banks to remain competitive' by the TPC and later reiterated by the ACCC.”¹⁷

More recently, the importance of “considering the competitive restraint that regional banks continue to place on the four major banks” has been reiterated by Graeme Samuel in his address to the Australian Bankers Association in September 2005.

Given the importance of existence of second tier banks, we do not believe it can be argued that a merger of St George and Westpac will actually generate an increase in competition within the industry, especially when the most likely outcome is that the remaining three major banks will seek to acquire the remaining small regional banks

¹⁴R Jones, “Bank Mergers and the Trade Practices Act in the light of the Westpac/Bank of Melbourne and Commonwealth/Colonial State Bank Mergers”, ACCC, 2002

¹⁵ A Khoury, “Banks now in play”, *Australian Banking and Finance Magazine*, Vol. 17, Number 8 2008.

¹⁶ G Samuel, “Competition issues in regional and rural Australia - speech to Australian Bankers Association 3rd Annual Regional banking and Agribusiness Forum”, ACCC (09/09/05)

¹⁷ Goddard, K and Walker, G, “Competition Analysis of Bank Mergers in Australia”, *Journal of Law and Financial Management*, 1,1,2002

in order to compete with the new entity. The historical precedent of similar mergers and acquisitions which have led to the demise of second tier regional banks have demonstrated a minimising of the potential for additional competitors to grow and disrupt what has been described as the “oligopolistic structure” of the four pillars.¹⁸

The affect of a significant acquisition of second tiered banks on domestic competition is a deep concern for innovation, consumer choice (in particular, the effect on bank fees), customer satisfaction, particularly when smaller banks poll significantly better than their larger counterparts.¹⁹

A recent national poll of 1,000 people conducted by McNair Ingenuity²⁰ found that Australians are not satisfied with the current state of the banking market and sceptical about the merger delivering better outcomes for consumers:

- 87% believe that the big banks make too much profit;
- 75% believe that the merger would mean less competition;
- 72% are already of the view that there is not enough competition between banks;
- 89% do not believe that the merger would result in lower fees; and
- 69% believe that this merger would mean less pressure on banks to reduce fees and charges.

Barriers to entry

The banking sector has a number of significant barriers to entry – prudential requirements, licensing, training, infrastructure costs and the rising cost of credit flowing from the ‘sub-prime’ crisis. Most of these barriers are entirely appropriate and reflect the important role that banking plays in society.

In addition, banking is an essential service and customers will often want a higher degree of trust in their relationship with their bank as opposed to other service providers. This element of trust is perhaps the most difficult for any new bank to obtain and arguably the most valuable commodity once it is acquired. This trust is usually earned over long periods of time as consumers and the market observe and form a view about a new institution.

¹⁸ Goddard, K and Walker, G, “Competition Analysis of Bank Mergers in Australia”, *Journal of Law and Financial Management*, 1,1,2002

¹⁹ “[Not so satisfied with NAB](#)”, *the Sheet* (retrieved 30/05/08)

²⁰ McNair Ingenuity Research, June 2008.

If St George did exit the market through the Westpac acquisition, then we believe it is unlikely that any other bank could step into its role as an effective and vigorous competitor for the following reasons:

1. St George's brand and market position were developed over a 70 year period. It is very unlikely that any second tier bank could begin to play a similar role in the market within the next few decades.
2. If a second tier bank did begin to emerge as an effective and vigorous competitor then it would quickly become a takeover target for the other big banks in the wake of a Westpac/St George merger.
3. It is unlikely that a foreign bank would enter the Australian retail banking market to fill the void if St George merges with Westpac. The national market share data shows that individually (and even collectively) foreign banks are very small players in the retail market and "have a larger presence in the business banking market, reflecting the focus of foreign bank branches on wholesale operations."²¹

Undertakings

Past performance is often the best predictor of future performance. Based on our experience with mergers involving large finance sector organisations, FSU believes that the undertakings provided were often complied with in a perfunctory and minimalist fashion rather than observed in good faith.

In some cases, complex processes appear to be built into undertakings transactions, sometimes obscuring the outcome and often providing companies with the leeway to avoid or dilute the impact of the undertakings.

FSU supports the ACCC being given authority to build extra safeguards into undertakings.²² For example, clauses that ensure the wording of the undertaking will be interpreted with regard to the objectives of the parties, as set out in the undertakings document, as well as any ancillary documentation.

FSU also supports the appointment of independent auditors with appropriate industry expertise to monitor, day by day, that companies are living up to the promises they make.

²¹ Reserve bank of Australia, "Foreign-owned Banks in Australia" *Financial Stability Review* – March 2007

²² G Samuels, "Regulator seeks best outcome for all", *Australian Financial Review*, 30/09/06

Conclusion

In summary, the FSU is opposed to the merger on the basis that:

- it will remove an effective and vigorous competitor from the market;
- barriers to entry make it unlikely that a new effective and vigorous competitor will emerge to replace St George;
- a substantial lessening of competition will occur in the markets for transaction accounts;
- it will result in substantial employment losses;
- there will be an increased likelihood of less competition in the banking sector through the four major banks launching takeovers for the remaining smaller players.

FSU experience in the previous mergers of large financial institutions has highlighted not only reductions in competition and service but the absence of any long term benefits beyond those to shareholders and senior executives holding stock. It is also clear that mergers of essential service providers such as banks and insurance companies impact on a wide range of issues beyond narrow definitions of competition.

We encourage the ACCC to ensure that any undertakings are clear and transparent with quantifiable monitoring arrangements. Finally, we encourage the ACCC to take account of the 'domino effect' of this merger on further industry rationalisation.

If you have any questions in relation to this submission please contact James Bennett on (02) 6247 7172

Yours sincerely



Leon Carter
National Secretary

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