

Japanese eye a slice of big four's mortgage pie

Japan's banks could do a lot worse than send their spare cash to Australia where it could be used for home loans and earn interest rates of more than 6 per cent, writes **Matthew Drummond.**

Some business ideas seem so simple that you wonder why no one has already put them into action. Take the recently mooted idea of Japanese banks turning their hefty deposit books into mortgages here in Australia. Sitting in the vaults of Japan's three largest banks are just over ¥100 trillion (\$1.27 trillion) in deposits that are not being used to fund loans.

Japan is a nation of savers, so banks have more money than they can lend out. Two decades of stagnant economic growth and deflation means banks pay next to nothing to depositors; interest rates on savings accounts are among the world's lowest at around 0.10 per cent.

The Japanese could do a lot worse than send their spare cash to Australia, a nation of spenders where there is not enough savings to go around. Once in Australia, the money could be lent out for mortgages, an ultra-safe asset class, and earn interest rates of more than 6 per cent.

The Japanese could even undercut the major Australian banks who are paying 6 per cent for deposits and even more for wholesale money, and still earn more than 5 per cent a year.

Could there be a simpler way to make money? This may become a critical question for the fortune of Australia's big four banks.

Two of the three Japanese mega banks, Mitsubishi UFJ Financial Group, Sumitomo Mitsui Financial Group and Mizuho Financial Group, are understood to be investigating breaking into the Australian mortgage market which is dominated by Australia and New Zealand Banking Group, Commonwealth Bank of Australia, National Australia Bank and Westpac Banking Corp.

Such a move comes at a tricky time for Australia's banks. This year, they'll have to get their hands on about \$100 billion in wholesale debt, and thanks to the European debt crisis the cost of that money is shaping up to be more expensive than any money they've ever raised before.

That's going to force mortgage rates even higher, something that the big four can do rather easily because of the lack of competitive restraint from non-bank lenders.

"Timing-wise, it would be a good time to slip in," says Mark Bouris, the executive chairman of non-bank lender Yellow Brick Road. "They might get a bit of market share off the banks during that period and good on them."

It's generally agreed that Australia's big four banks had a very good financial crisis — pesky non-bank competitors were wiped out, regional banks gobbled up, and once-in-a-generation gains were made in market share.

Now further information has come to light of just how lucky the Australian banks were — the GFC gave them respite from the onslaught of a competitive attack from Japan.

According to sources, when the financial crisis hit in 2008, Challenger Financial, James Packer's attack vehicle on the major banks, was getting set to use Bank of Tokyo-Mitsubishi UFJ's balance sheet to fund mortgages into Australia.

The Japanese lender — now part of Mitsubishi UFJ — had taken a \$208 million stake of Challenger in August 2007 in a deal that was touted as a "long-term strategic relationship... to pursue opportunities in Australia, Japan and the Asian region".

The plan for mortgages was never spelt out but, according to a source, part of the vision was to use the Japanese bank's deposit book as funding for Australian mortgages.

"They were going to launch the balance sheet of Japan into Australia for lending. The Japanese are notoriously slow and it took a couple of years of work to get there. Then it all fell over because of the GFC."

Challenger declined to comment on the revelation — which would be a piece of business history but for the fact that four years later, history may be about to repeat.

If the arrangement with Challenger took

years of planning, one of the trouble spots is likely to have been regulators taking a dim view of running up loans in one country funded off deposits in another.

According to one bank analyst, the Australian Prudential Regulation Authority would likely require a Japanese bank to bring at least some of its deposits down into Australia before lending them out as Australian mortgages.

And Japanese regulators may well be unhappy about a Japanese bank taking deposits, a funding source that is seen as a safety valve, and sending them offshore.

"If the Japanese bank went belly up, APRA would want to be assured there was a stand-alone business in Australia," says one analyst, who declined to be named. "And I'm not sure the Japanese regulator would be happy if it saw a couple of billion dollars flowing to a holding company in Australia."

Then there is currency risk. Loans in one currency funded off deposits in another is the kind of mismatch that can seriously destabilise a bank. In the past 12 months alone, the Australian dollar and the yen have swung around by 20 per cent. In 2008, the change was almost 50 per cent.

For that reason, regulators would almost certainly expect a Japanese bank to fully insure itself against unfavourable currency moves,

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Mark Bouris, Yellow Brick Road

that is buy hedges, says Bouris. Once the cost of buying those hedges are factored in, the Japanese banks' cost of funds would be similar to the cost of an Australian bank raising deposits in Australia.

"It's very hard to arbitrage the market. If it was that easy, everyone would be doing it," he says. Bouris adds that if Australian banks were forced to fund new mortgages off money raised in wholesale markets in 2012, then the funding advantage could swing back in favour of the Japanese.

But then there is perhaps the biggest hurdle of all — a historic reluctance by Japanese banks to push aggressively offshore.

Tom Quarmby, the Hong Kong-based head of Asian banking research for Barclays Capital, says while Japanese banks are fairly hungry for anything in which to invest their spare deposits, they have tended to keep their money in safe fixed-income investments or take small slices of loans to top-tier companies.

And with European banks retreating to Europe, there are plenty of fresh assets coming up for grabs that will interest the Japanese.

"The European banks have €500 billion to €600 billion of exposure into Asia including Australia. The Japanese have about €100 billion and a lot of appetite to increase that. They've doubled their exposure over the last 18 months and they are on the record saying they are keen to pick up other offshore assets."

But Australian mortgages? "I can't see it," Quarmby says.

Not everyone is a doubter. Bouris believes the fat margins earned on Australian mortgages as well as their relative safety gives Japanese banks a good reason to try to overcome obstacles. And as one analyst says, history is turning in favour of over-funded Japanese lenders.

"In the old days, it was all about lending. Now it's all about borrowing, you have to have the funding to be able to lend. If the Japanese have the funds and they can get it down here and APRA is happy with that then, yeah, it will work," he says.

Indeed one reason Australian banks should be at least a little worried about a potential Japanese invasion lies right under their noses. In taking excess deposits out of Asia and lending them in Australia, Japanese banks would be looking to run the same sort of super-regional strategy that is making gains for ANZ Banking Group.

Vital airspace

Spectrum is necessary for all wireless technology and Canberra is counting on that — with a canny eye on the promised budget surplus, writes **David Ramli.**

Broadcast spectrum may be an invisible commodity but according to the federal government it's worth billions of dollars — money it needs to help bring the budget back to surplus. While the government's \$35.9 billion national broadband network often gets the headlines, all three of the biggest telcos are focusing on this year's licence renewals and auctions potentially worth more than \$5.5 billion.

As the profits generated by traditional fixed-line internet and phone services have gradually declined, the amount of mobile wireless broadband services rose by 39 per cent to 4.79 million services at June 2011 and the number of mobile phone internet services leapt by 43 per cent to reach 9.68 million.

Spectrum is the electronic airspace needed by all wireless technologies from radios and televisions to mobile phones and broadband internet devices. But spectrum bands are not born equal; the lower 700MHz and 800MHz bands traditionally used by TV sets around the world have the best penetration and data efficiency, allowing them to carry more data further into people's homes and workplaces than the cheaper and higher frequencies.

Without the high quality spectrum even the best mobile phone technology becomes less effective, leading to lower call quality, poorer reception and slower broadband speeds. Spectrum therefore becomes the lifeblood of telecommunications companies, which need it to hold onto fickle customers who will leave in droves if dissatisfied.

That's why Communications Minister Stephen Conroy believes he can extract a generous premium from telcos as the government struggles to fulfil its long-standing promise to get back to budget surplus by 2012-13.

As reported in *The Australian Financial Review*, Conroy's latest draft determination shows he expects to gain \$1.4 billion from

Up for grabs



Stephen Conroy Minister for Broadband, Communications and the Digital Economy

Telstra and Vodafone Hutchison Australia (VHA) when their 800MHz licences, set to expire by 2013, come up for renewal.

This is on top of the looming auction of 700MHz and 2.5GHz spectrum that the Royal Bank of Scotland estimates could be worth up to \$3.25 billion and \$925 million.

The secondary auction, marketed by the government as the "digital dividend", will come after the Australian Communications and Media Authority rearranges the analog spectrum as part of the switch to fully digital television in 2013.

The extra bit of leverage Conroy holds is

Building industry

A self-proclaimed workplace relations nerd, ABCC head Leigh Johns is out to prove he's neither a boss's boy nor a union yes-man. And he's passionate about the industry, writes **Rachel Nickless.**

He started out as a young lawyer at Holding Redlich advising the militant Construction, Forestry, Mining and Energy Union (CFMEU), but later advised employers. He hails from a blue-collar country family and is passionate about footy, but is a vegetarian who is so keen on dance that he became chairman of the Australian Ballet School board.

Australian Building and Construction commissioner Leigh Johns is now policing an industry in which people are expected to pick a side — employers or unions — but this self-proclaimed "workplace relations nerd" has shown he's happy to take a swing at either.

Much has changed at the ABCC since Johns took over from former commissioner John Lloyd in October 2010. "There's clearly been a commitment to being a more open regulator," Johns said in an interview with *The Australian Financial Review* at his offices in Melbourne's St Kilda Road.

The 42-year-old points to his decision to introduce a litigation policy to guide decisions on prosecution and to transform the ABCC into a full-service regulator that now pursues employers for underpaying

workers. Under Lloyd, the ABCC largely concerned itself with pursuing unions for illegal strikes and employers for the union-friendly practice of paying strike pay.

But Johns has so far recouped \$275,000 in wages for workers and says "we've done all that and not taken our eye off enforcement", pointing to a 30 per cent increase in total investigations.

Staff morale has also risen considerably under his leadership, according to two staff engagement surveys done a year apart. The latest shows overall staff engagement is at 44 per cent.

This is well up on the 32 per cent staff engagement in the 2010 survey and above the Australian benchmark of 36 per cent.

But not everything Johns has touched has turned to gold since he was promoted from deputy commissioner by the Gillard government.

When he took over he quickly initiated an "extensive" inquiry into sham contracting — a practice where employers are accused of labelling employees as contractors to avoid paying full entitlements. But his report, released just over a year later in November, failed to even determine the extent of the sham contracting problem. Instead, it made a range of modest reform recommendations and Johns recently launched yet another round of research. CFMEU national secretary Dave Noonan says the report is a "damp squib".

"It's a bit like announcing that you are going to bring the Moscow Circus to town and turning up with a clown on a unicycle," Noonan says.