THE AUSTRALIAN

$50bn bill to bolster big four

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The major banks will have to raise a combined $50 billion in additional capital over the next four years to better protect depositors and taxpayers against a collapse, despite being granted a reprieve by the prudential regulator on the amount.

The Australian Prudential Regulation Authority said the nation's largest banks would have to lift their total capital by three percentage points of risk-weighted assets by January 2024, watering down an initial proposal for an increase of four to five percentage points.

The regulator altered its stance after receiving feedback from banks that the bigger increase would flood the market with new subordinated debt and other instruments and increase bank funding costs.

Even so, the proposal will see bank funding costs increase at the margin, which could be passed on to borrowers.

The initial proposal by the bank regulator saw the industry pencilling in a combined tier-two capital increase of $75 billion.

The latest APRA requirements address a recommendation from the landmark 2014 Financial System Inquiry that the regulator implement a framework to ensure additional capital safeguards are in place to protect against a bank failure.

Moody's vice-president Frank Mirenzi yesterday said APRA's final decision was positive for senior bondholders.

"It will increase the amount of capital available to absorb unexpected losses," he said.

Fitch senior director Tim Roche said APRA's revised proposal reinforced his view that Australian regulators and governments had a "high propensity" to support senior unsecured bank creditors during times of stress.

"The final requirements appear to be calibrated to meet a more typical systemic loss event, rather than the worst case scenario," he said.

"The lack of an explicit bail-in feature for senior unsecured notes marks Australia as an outlier compared to North American and western European regimes, but in line with most of Asia-Pacific apart from Hong Kong."

S&P Global Ratings said while APRA's increased loss-absorbing capacity requirement could "lessen the need" for the Australian government to provide financial assistance to banks in a stressed scenario, it wouldn't stop a bail-out if necessary.

"We believe that this plan does not introduce any policy or process impediments to the government bailing out a systemically important bank," the analysis said.

"We perceive materially reduced uncertainty over the Australian government's future policy direction on supporting the banking sector. In particular, we now believe that government support is unlikely to diminish in the next two years."

S&P added that it had revised its outlooks on the four major Australian banks to "stable" from "negative", and the outlook on Macquarie Bank to "positive" from "developing". The APRA capital measures apply to domestic systemically important banks and the regulator made clear yesterday it eventually wanted large banks — which takes in the big four — to meet the higher total capital threshold.

The statement said the higher target would remain but APRA would consider the "most feasible alternative" method for reaching the additional one to two percentage points over the next four years.

Analysis by Realm Investment House labelled the APRA capital change a "good result for the stability of the system and for investors".

"It's the right market to be delivering this news into. A lack of general issuance and plummeting cash rates will provide a reasonable base of domestic demand, but it isn't a big enough sponge to soak up all of that issuance.

"The banks are not naive enough to extrapolate the current environment forward."

The reprieve was not enough to buoy bank stocks yesterday, which took a hit.

Share prices dipped across the big four, with the largest fall coming from ANZ, down 0.7 per cent to $27.69. National Australia Bank had the most modest decline, slipping 0.3 per cent to $26.68.

Citigroup research downgraded Commonwealth Bank to a "sell" rating yesterday, which weighed on the sector.

On the APRA capital proposal, deputy chair John Lonsdale said: "The global financial crisis highlighted examples overseas where taxpayers had to bail out large banks due to a lack of residual financial capacity.

"Boosting loss-absorbing capacity enhances the safety of the financial system by increasing the financial resources that an ADI (authorised deposit-taking institution) holds for the purpose of orderly resolution and the stabilisation of critical functions in the unlikely event that it fails."

APRA wants banks to lift their tier-two capital. Unlike tier one or core capital, it is supplementary capital and typically includes undisclosed reserves, subordinated debt and other items.

The major Australian banks are also navigating tougher proposed capital requirements in New Zealand, which are focused on a marked lift in common equity tier one. Australian banks dominate the NZ market.

Separate ASX statements by the banks showed Westpac and CBA would need to boost their capital coffers the most under the new APRA measures.

Westpac said that based on risk-weighted assets of $420bn as at March 31, it would need $13bn of additional capital, the "bulk of which" would be raised through tier-two instruments.

"It is too early to determine the actual total cost to Westpac given the pricing of any tier-two capital is expected to be impacted by the increase in supply of tier-two on issue by Australian banks."

CBA told the ASX that based on risk-weighted assets of $447 billion it expected an increase of about $13bn in total capital.

ANZ expects an incremental increase in total capital of about $12bn based on risk-weighted assets of $396bn. It also flagged an equivalent decrease in other senior funding.

NAB said the APRA change suggested a rise of $12.1bn of total capital. APRA estimates the higher requirements will have a "small impact" on overall bank funding costs.

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