25 February 2022

[redacted]
Executive Director, Banking Division
Australian Prudential Regulation Authority
GPO Box 9836
SYDNEY NSW 2001

By email: [redacted]

CC: [redacted]
Australian Prudential Regulation Authority
By email: [redacted]

Dear Ms [redacted]

Re: Great Southern Bank response to APRA's consultation on macroprudential policy

Great Southern Bank welcomes the opportunity to provide feedback to APRA's consultation on the proposed APS 220 Attachment C – Macroprudential Policy: Credit Measures.

Background

For over 75 years we've been putting our customers first, and today we look after the financial needs of more than 381,000 Australians. We have changed our name from CUA to Great Southern Bank, but we remain customer-owned and firmly focused on helping all Australians own their own homes.

We are 100 per cent owned by our customers which means we don't have the same tensions between customer and shareholder interests as listed banks do. Our structure means we can remain constantly focused on the needs of our customer-owners.

Macroprudential Policy: Credit Measures

Great Southern Bank welcomes APRA's approach of codifying within the prudential framework whether macroprudential intervention is appropriate, and which tool or combination of tools would best achieve its intended objective. Given the increasing usage of such tools both in Australia and globally, we support APRA's transparency on this matter.

In APRA's letter to all ADIs dated 11 November 2021, APRA set out the two broad tools it has at its disposal to affect macroprudential policy, specifically lending standards and lending limits.

Lending Standards

Great Southern Bank considers lending standards to be the preferred tool to moderate systemic risks. Based on our firsthand experience, there are three main reasons why lending standards are the preferred tool:

1. Ease of implementation: Typically changes to lending standards can be implemented through a combination of policy and system changes.
   Whilst system changes may be complex, once they are implemented the result is a controlled process aligned to the requirement.
2. Competition and level playing field: Changes to lending standards, when clearly articulated to industry, result in a level playing field for all regulated entities. This reduces unintended consequences around competition that may have a disproportionately negative impact smaller ADIs.
3. Short-comings or operational challenges in implementing prudential limits.

Lending Limits

Lending limits are harder to implement and lack sound preventative controls. A driver of this is the inherent lag between a home loan application decision and when the application converts into a funded loan (at which point the loan is counted against the limit). This lag results in the need for assumptions and more complex forecasting as to when or if a pipeline application will result in a funded loan.

Complexity also arises from adverse selection, where application volumes flow to the lenders with less stringent lending criteria and the lowest rates. This can arise when a lender has not tightened lending controls enough relative to the most active lenders. Naturally an ADI's credit and pricing strategies are not transparent to other ADIs prior to implementation and in some cases after implementation. This is a bigger challenge for smaller lenders who are operating with a smaller denominator, where even a small shift in flows can have a material impact on compliance to a limit (even where it has an immaterial impact on systemic risks).

Lending limits are punitive to consumers in that the tools used to manage a lending limit are often opaque or unfair to customers. It can drive interest rates higher without a link to the individual customer's risk, and can drive the need for rapid and confusing changes to lending criteria. Rapid changes can also present challenges for back-office teams, resulting in delays in customer response times and the inefficient delivery of normal customer services.

Where a bank is able to closely monitor its pipeline, lending limits may result in a customer being declined credit. This is because the bank is pressed against its limit for that month or quarter but could have approved credit if the customer had applied in the next reporting period.

Part 6 and Part 8

Part 6 states that the serviceability buffer applies '*ignoring any discounted introductory rates offered for a limited period at origination of the loan*.' We note that many lenders have recently had low interest rates on select fixed rate terms. It is unclear whether APRA intends for this to apply to fixed rate products priced for the interest rate environment or whether it is intended to cover more overt introductory discounts on interest rates, such as 20bps off for the first year. Further clarity would help support a consistent implementation across industry.

Part 8 notes that '*APRA will notify ADIs of any decision to set a limit, including the limit level and the date from which it would apply…*' We believe this should apply to both limits and lending standards. To support implementation to systems and ensure fairness to customers, we encourage APRA to outline a minimum prior notice period, such as three months, before use of such tools.

Great Southern Bank would like to see APRA's final macroprudential policy recognise lending standards as the regulator's preferred tool for managing systemic risks, and that lending limits would only be introduced after considering customer outcomes, competition impacts and ease of implementation.

Thank you for the opportunity to provide a submission to APRA's consultation on the proposed APS 220 Attachment C – Macroprudential Policy: Credit Measures. If you have any questions or require additional information, please do not hesitate to contact [redacted] on [redacted]34 or by email: [redacted]

Kind regards

[redacted]

Rolf Stromsoe
Chief Risk Officer