Australian Citizens Party

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MEDIA RELEASE

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Warning to Australian investors: Beware hybrid securities, aka 'bail-in' bonds!

Australia's big banks are careening along a cliff's edge at breakneck speeds with ordinary investors strapped to their bumpers as human shock absorbers.

Bank regulator APRA is allowing the big banks to sell to unsuspecting Australian investors products that are illegal for banks in other countries to sell to anyone but other financial institutions.

The products are hybrid securities known variously as CoCo (contingent convertible) bonds or bail-in bonds. These complex securities are sold as bank bonds, often bearing a very high interest rate. However, buried in their fine print are numerous triggers that, if the bank gets into trouble, convert the bonds into far less valuable or even worthless shares in the bank.

The investors think they are first in the line of bank creditors and will have their bonds honoured even if the bank fails, only to discover they are holding worthless shares which may or, more likely, may not come good.

Australia's banks are aggressively selling these bail-in bonds to so-called retail investors—mums, dads and retirees. To suck them in, the predatory banks are offering amazingly high interest rates. In February CBA issued a $910 million tranche of hybrid securities at 7.5 per cent interest—*a very generous 5.2 percentage points higher than the standard bank rate*. Most hybrid issues are around 3 percentage points higher than the bank rate. "CBA is offering the fattest premium in history", Jonathan Shapiro observed in the 27 February *Australian Financial Review*.

As one market watcher asked, "If you are a self-funded retiree desperate for a return in this low-interest climate, and Australia's biggest and 'strongest' bank, CBA, offers you 7.5 per cent interest on bonds, are you going to think twice about the fine print? Probably not."

In recent weeks, Westpac, NAB and ANZ have all announced big hybrid bond issues, ANZ's being the first US dollar-denominated hybrid since 2008.

In 2014 the UK's Financial Conduct Authority stopped British banks from selling bail-in bonds to retail investors because of the risks associated with the securities that such investors might not readily understand.

It is therefore shocking that in Australia, APRA is allowing the banks to *target* retail investors with the same products. The banks list their hybrids on the Australian Securities Exchange (ASX) and sell them to individuals via stockbrokers. In his February article the *AFR*'s Shapiro noted they are especially targeting self-managed super funds which "have proved to be a deep pool of capital. *These investors know and trust the banks* ..." (Emphasis added.)

This trust in the banks is built on a scaffold of lies peddled by bankers, politicians and the media. Most retail investors wouldn't know, for instance, that:

- During the 2008 global financial crisis when the public was reassured Australia's banks were "sound" the Big Four and Macquarie spent the weekend of 11-12 October on their knees begging the Rudd government for guarantees, without which they would be "insolvent, sooner rather than later".
- Following the GFC, when globally the volume of gambling in derivatives levelled off and even shrank, the derivatives gambling of Australia's banks skyrocketed, *doubling* between 2009 and 2015 from $14 trillion to $28 trillion (now $32 trillion); in 2012 CBA, which had the fastest growth in derivatives gambling, suddenly and suspiciously stopped disclosing its true derivatives position.
- The big four banks are so exposed to the property bubble in Australia that, when one of any number of triggers bursts that bubble, Australia's banks will suffer the same fate as Ireland's banks in 2008 and go bankrupt.

The hybrids are called "bail-in bonds" because APRA is expected to let Australia's banks count them towards their TLAC—*total loss absorbing capacity*—which is a requirement of the global “bail-in” regime that the Bank for International Settlements is dictating to the world. Bail-in is intended to preserve Too Big To Fail (TBTF) banks by ensuring that significant losses from their reckless speculation are worn by ordinary depositors and investors, not the banks, so that such losses don’t trigger another 2008-style meltdown.

Hence the human shock absorber analogy. The banks are knowingly selling a product that will make unsuspecting investors wear their losses so they can continue recklessly gambling in the property bubble and derivatives. Australia as yet doesn’t have depositor bail-in, because the CEC exposed and defeated the plans for such legislation in 2013-14, so APRA is bringing in bail-in through the back door.

Solution: Investigate the banks; Glass-Steagall

The CEC has been warning about bail-in bonds in our weekly *Australian Alert Service* magazine since the start of the year, after thousands of Italian investors were wiped out by similar products. In the lead-up to and during the federal election, a number of political parties including Labor, the Greens, NXT, Jackie Lambie, and One Nation put an investigation of the banks on to their party platforms. Such an investigation must include APRA’s plans for bail-in.

The immediate solution is clear: Glass-Steagall legislation to split up the big four banks and any other conglomerate banks into completely separate institutions—dedicated deposit-taking banks that serve the real economy and are protected by the government on one side, and investment banking, wealth management, stockbroking and insurance businesses on another. Bail-in will destroy people to save banks; Glass-Steagall will save people by dismantling TBTF banks and ensuring real banks are truly sound. The CEC is leading, in Australia, the global campaign to enact Glass-Steagall as the first step to solving the global financial mess that is about to erupt into another crisis. If you want to survive it, and want your country to survive that crisis, join the CEC and campaign for Glass-Steagall.
