Australian Citizens Party

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MEDIA RELEASE

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Bail-in bonds 'a ticking time bomb'

"A ticking time bomb!" That is what outgoing Australian Securities and Investments Commission (ASIC) boss Greg Medcraft last week called the bail-in bonds, a.k.a. hybrid securities, that APRA has allowed banks to sell to thousands of Australians.

The Australian Prudential Regulation Authority (APRA) is ostensibly the bank regulator. Yet it has repeatedly aided and abetted the banks' most egregious behaviour, including by encouraging them to focus all of their lending into mortgages, which created the dangerous property bubble.

Its complicity in bail-in bonds is APRA's most damning action yet. While the Bank of England forbids UK banks from selling hybrid securities to retail investors—so-called mum and dad investors—because they are unlikely to recognise the extreme risk they carry, APRA gives Australia's banks *carte blanche* to target self-funded retirees and those with self-managed superannuation to buy these securities.

There are potentially hundreds of thousands of such investors in Australia who should be very nervous at Greg Medcraft's exchange with Greens Senator Peter Whish-Wilson in the hearings of the Senate Economics Legislation Committee on 26 October.

Senator Whish-Wilson asked Medcraft, whose tenure as chairman of ASIC ends 12 November: "You've recently said that selling hybrid securities to retail investors is ridiculous. Would you care to expand on those comments? And do you believe it is a systemic risk, or presents systemic risks?"

In his reply, Medcraft said: "There are two reasons we believe a lot of the retail investors buy these securities. One is they don't understand the risks that are in over 100-page prospectuses and, secondly—and this is probably for a lot of investors—*they do not believe that the government would allow APRA to exercise the option to wipe them out* in the event that APRA did choose to wipe them out." (Emphasis added.)

When Senator Whish-Wilson raised the spectre of "bail-in", Medcraft confirmed: "Yes, they'll be bailed in. The big issue with these securities is the idiosyncratic risk. Basically, they can be wiped out—there's no default; just through the stroke of a pen they can be written off. For retail investors in the tier 1 securities—they're principally retail investors, some investing as little as $50,000—these are very worrying. *They are banned in the United Kingdom for sale to retail*. I am very concerned that people don't understand, when you get paid 400 basis points over the benchmark [4 per cent more than normal rates], *that is extremely high risk*. And I think that, because they are issued by banks, people feel that they are as safe as banks. Well, you are not paid 400 basis points for not taking risks…"

He emphasised: "I do think this is, frankly, *a ticking time bomb*."

The Citizens Electoral Council has been a lone voice warning about these hybrid securities, including in an 8 July 2016 release headlined, "Warning to Australian investors: Beware hybrid securities, aka 'bail-in' bonds".

That release pointed out that banks such as CBA were targeting unsuspecting retail investors to buy bail-in bonds with interest rates up to 7.5 per cent, which in this low-interest investment climate most self-funded retirees would find very hard to resist, especially from a "strong" bank like CBA.

Medcraft singled out self-funded retirees as especially vulnerable, saying that "if they're being bought by retirees, the problem you will have is that, if a government actually has to choose to wipe them out, the problem is that those same people may end up going back onto the pension".

APRA's complicity in exposing self-funded retirees to this "ticking time-bomb" of bail-in bonds underscores again why the government must not be allowed to give sweeping emergency powers to this failure of a regulator. APRA is causing the financial crisis it will manage, and setting up ordinary Australians to wear the cost of propping up the banks through these bail-in bonds, and possibly even their deposits, given the broad language of the APRA bill.