



Good Shepherd  
Microfinance

**Response to the  
Financial System Inquiry  
Final Report**

**Submission by:  
Good Shepherd Microfinance**

**March 2015**

Senior Adviser,  
Financial System and Services Division  
The Treasury  
Langton Crescent  
PARKES ACT 2600

Good Shepherd Microfinance  
192 -198 High Street, Northcote  
NORTHCOTE, VIC 3070  
March 25<sup>th</sup> 2015

Good Shepherd Microfinance welcomes the opportunity to respond to the Financial System Inquiry's (FSI) final report which has set out significant recommendations under five specific themes which will establish a direction for the future of Australia's financial system.

In this submission we respond primarily to the report's findings and recommendations for increased consumer protection, for increased regulation, and for increased financial resilience.

Good Shepherd Microfinance shares the FSI's stance that sustainable growth of economies can only be achieved by meeting the financial needs of its users, and by operating in an efficient, fair and resilient manner. We applaud the FSI's recommendation to invest in industry and Government efforts to increase financial inclusion, and welcome the recommendation to explore ways to facilitate the development of the impact investment market and encourage innovation in funding service delivery.

We now urge the Government and the Reserve Bank of Australia (RBA) to make direct investments to strengthen financial inclusion and resilience through the expansion of microfinance and alternative financial services options for people on low incomes.

We re-iterate the recommendation put forward in our previous submissions, namely that the RBA is best placed to contribute directly to further development of microfinance initiatives, in line with its charter, specifically through an investment of \$500m in capital and \$100m in annual operating funding of microfinance initiatives. This investment would contribute to a potential modelled savings to Government of \$2.6 million, and driving GDP growth of \$19.7 billion.

We also have strong evidence that such investment by government, business and civil society, in leading microfinance schemes such as those developed by Good Shepherd Microfinance, is highly effective in creating economically strong, vibrant connected communities where families thrive, are self-sufficient and take care of themselves. We provided evidence in our previous submissions that Good Shepherd Microfinance schemes improve access to, and use of, small amount credit, confirming that investment in microfinance schemes will expand consumers' access to safe, affordable credit in a market sector vacated by the big banks and replaced by expensive and hazardous fringe lenders.

We strongly re-iterate our belief and position (outlined in our previous submission) that financial inclusion and building resilience is a means by which to drive economic mobility and to mitigate the consequences of financial hardship in Australia. We believe that financial inclusion and building resilience should be a stated aim of the Australian financial system.

We also re-iterate our position that there **is** a role for the Government in addressing the post-GFC failure of the market to achieve financial inclusion, and further recommend that this could be achieved by the RBA making a direct contribution and investment under its obligations to ensure ....“....that the monetary and banking policy of the Bank is directed to the greatest advantage of the people of Australia.....”<sup>1</sup>

Increasing financial inclusion and resilience in the Australian community will drive economic growth and have positive impacts on competition, innovation, efficiency, and stability and consumer protection.

Although Good Shepherd Microfinance was disappointed that there was no mention of microfinance initiatives per se, we welcome the focus on increasing consumer protection, and would encourage the Treasury to apply the same protection to those who are excluded from the Australian financial system. .

We re-iterate some recommendations made in our previous submissions, all of which are in line with the intent of the FSI final report, and which reflect our values of human dignity, respect, social justice, compassion, audacity and reconciliation. Good Shepherd Microfinance will continue to inform stakeholders and take action to provide increased and improved access and services to realise financial inclusion for all Australians.

We look forward to the Treasury’s implementation of the FSI final report’s recommendations, and trust that our submission is considered as being a strategic and beneficial enhancement to them, building financial inclusion and resilience for Australia’s financial system.

Please do not hesitate to contact us if there is any further information we can provide (03 9495 9644).



Adam Mooney  
CEO  
Good Shepherd Microfinance  
March 25<sup>th</sup> 2015

---

<sup>1</sup> The Reserve Bank Board’s obligations with respect to monetary policy are laid out in Sections 10(2) and 11(1) of the Reserve Bank Act 1959. Section 10(2) is often referred to as the Reserve Bank’s ‘charter’

## GOOD SHEPHERD MICROFINANCE RESPONSE TO THE FINANCIAL SYSTEM INQUIRY FINAL REPORT

Good Shepherd Microfinance welcomed the release of the Financial System Inquiry (Murray) final Report on Dec 7<sup>th</sup> 2014 and its forty-four recommendations relating to the Australian financial system.

We submit this response to The Treasurer, the Hon Joe Hockey, who now has carriage of the report (instigated at his request in Dec 2013) and who has indicated that *“The Government intends to consult with industry and consumers before making any decisions on the recommendations.”*

It is hoped that this submission is duly considered by the Treasury. Our submission contains a number of areas that we believe require further extension and inclusion.

At its core, we argue here that Government build on the FSI recommendations for regulation to protect consumers, particularly those excluded, but also that a resilient financial system is built with people who are resilient. Resources also need to be directed to assist those who experience the most crises with the least resilience, but who aspire to lives that are inclusive and valued.

We note and support the FSI’s approach to identify five themes, under which to make recommendations. We believe this ensured that issues such as consumer protection were addressed specifically, rather than being consolidated into broader categories where their importance may have been diluted. We equally strongly support and encourage the aspiration of the FSI to:

- Strengthen the economy by making the financial system more resilient.
- Lift the value of the superannuation system and retirement incomes.
- Drive economic growth and productivity through settings that promote innovation.
- Enhance confidence and trust by creating an environment in which financial firms treat customers fairly.
- Enhance regulator independence and accountability, and minimise the need for future regulation.

Good Shepherd Microfinance is in agreement with the report’s recognition that, based on the characteristics (efficient, resilient and fair) and pre-requisites of a well-functioning financial system and financial regulation, the Australian financial system actually has a number of weaknesses, despite having performed relatively well since the Wallis report:

- Taxation and regulatory settings have distorted the flow of funding to the real economy
- The financial system remains susceptible to financial shocks
- Superannuation is not being delivering retirement incomes efficiently
- Unfair consumer outcomes remain prevalent, and
- Policy settings do not focus on the benefits of competition and innovation

We agree, that as a result of these weaknesses, the Australian financial system is in need of more regulation, rather than further de-regulation, and concur with the tightening of regulation around a number of areas, but predominantly around superannuation, with a strong recommendation that the objectives be “enshrined in legislation”. The recommendation that a new board – the financial Regulator Assessment Board – be instigated to assess the performance of regulators, with ASIC and APRA being given a three-year funding model to provide them with more autonomy, is sound. Importantly, to prevent regulatory oversights occurring in the future or inappropriate conduct, the report recommends that the state of competition in the financial sector should be reviewed every three years.

Good Shepherd Microfinance is heartened by the report’s approach to tighter regulation and monitoring, especially as outlined in *Chapter 4: Consumer Outcomes*. However, it was in this chapter that Good Shepherd Microfinance most wanted to see some recognition of financial exclusion and possible recommendations that would have assisted people to more safely and easily access the Australian financial system. While our microfinance products enable people on low incomes to access credit for essential household goods and services at no or low interest rates supporting their financial wellbeing and resilience, the 170,000 people we have reached represents only six per cent of those that need fair, safe and affordable financial services. Thus we would prefer to see Government invest in the further development of microfinance initiatives that focus on increasing financial inclusion, thereby supporting the country’s most financially disadvantaged people, and ensuring that the financial system is fair for everyone.

Regrettably Chapter 4 (and the overall report) contains no reference to microfinance nor puts forward recommendations for investment in the microfinance sector. However there is recognition that consumer protection is important and that self-regulatory and regulatory changes are needed to strengthen financial firms’ accountability. There is a strong recommendation the law should be changed to introduce a principles-based product design and distribution obligation to boost consumer confidence and trust. Our concern though is that it is not clear how this may play out to protect the financially excluded. Instead the focus is entirely on those consumers who are already included within the financial system and who own some amount of superannuation. For example, the recognition of the need to raise financial literacy is couched in sections discussing superannuation and investment advice – both only available to the financially included.

Good Shepherd Microfinance strongly argues that building financial literacy and resilience in those excluded from the financial system has substantial benefits in that it economically mobilises people towards inclusion and self reliance and results in substantial and extensive savings of Government expenditure on health, welfare and justice. Just as the report shows recognition of the importance of resilience in relation to the Big 4 banks’ capacity to absorb shock and cope with crises, the same principles can also be applied to the resilience of

individuals to build protective factors and minimise risk factors at times of personal, family and community financial crisis. More recently Good Shepherd Microfinance undertook a redefining of financial exclusion to include *resilience*, which has resulted in us developing, and refining targeted microfinance initiatives that will ensure even more people are moved towards financial inclusion. And financial inclusion is a driver of economic growth. Drawing from our research that found our programs realise financial inclusion, a modelled GDP uplift of \$19.7 billion is possible, as people become economically mobile.

We therefore encourage the Treasury to consider greater investment in microfinance programs that build resilience in individuals and therefore ultimately in society and the financial system they use. Investment in microfinance makes not only makes good business sense for this country – it has a large positive impact on people who are excluded from mainstream financial services. Government, business and the community all have an important role to play.

We re-iterate the recommendation we put forward in our previous submissions, namely that the Reserve Bank would be best placed to contribute directly to further development of microfinance initiatives, in line with its charter, by a direct contribution and investment of \$500m in capital and \$100m in annual operating funding in microfinance initiatives.

Similarly we believe that the Government, the Reserve Bank of Australia and other stakeholders should invest in microfinance banking and financial services as a long-term proposition, in collaboration with the not for profit and community sector. We believe this could be achieved by:

- Sector building investment in Community Development Finance Institutions (CDFIs).
- Mandatory minimum proportions of bank risk weighted assets (RWA) or bank profits being invested in economic inclusion programs for people on low incomes
- Scalable and sustainable income generating microenterprise development schemes
- Performance oriented financial capability programs (financial capability bonds)
- Insurance cover for people on low incomes
- Investment in alternative people centred financial services similar to Kiwibank in New Zealand

Good Shepherd Microfinance acknowledges that the report is strong in arguing for safe and protective mechanisms for consumers in its overall approach to examining the role of Government in the financial system.

We also agree with the Inquiry's recognition of the central role of market forces, and the particular mention of its strong belief that sector-specific regulation is needed because:

*...“More so than other sectors, the financial system has the ability to create or amplify economic shocks because of its use of leverage, its complexity and its interconnectedness with the rest of the economy. The significant harm to consumers that may result from complex financial decisions, or from dishonest and predatory practices, requires specialist regulation to promote fair treatment”. (p.10)*

Although some of the greater and broader regulation of the financial system that the report calls for may not impact directly on Good Shepherd Microfinance clients, the report’s recognition of disempowering and more closely regulating the operation of agencies that are not transparent, are not fair or equitable (such as the industrial relations system hold over superannuation funds) is welcomed. We believe it reflects the Government’s commitment to, and recognition of the need for greater consumer protection within the Australian financial system, something we advocated strongly for in our original submission, under the heading of protection from the payday lending and rent-to-buy sectors.

A key finding of the report is the recognition of the vulnerability of the Big 4 banks in Australia, and that they are only average by international standards in the amount of cash they hold to cover potential loan losses. Two of the most significant proposals out of the report’s forty-four recommendations relate directly to how much shareholder-funding banks need to hold. In this respect, we agree with the FSI that the “Big4” be held more accountable and will have to invest more in securing their resilience against future shocks such as the GFC. Importantly this means the “middle ground and regional banks” will now have more leverage and viability within the system. This is a positive from Good Shepherd Microfinance’s perspective in that we argued in our submission that the overtaking of smaller credit unions and regional banks by the Big 4 had removed a line of banking that some “working poor” might otherwise have accessed. In David Murray’s own words “*What we’re trading off here is the cost to the community in a crisis versus an insurance premium in the capital of the banks*”. Recognition of the community good is a positive in the report. Equally we support that recognition and recommendations for the RBA to place further restrictions over credit and debit cards, namely:

- Cap card fees paid by business to issue cards to consumers
- Ban merchants surcharging for debit cards
- Set up different rules for low cost, medium cost and high cost cards
- Set a cap on surcharges for Visa and MasterCard
- Allow high cost cards like Amex and Diners to surcharge, but only at reasonable cost.

Good Shepherd Microfinance encourages the Treasury to support the FSI recommendation for increased regulation over the financial system both in terms of the RBA placing further controls around the issuing of credit, and in terms of greater funding and resourcing for ASIC.

We agree with the report recommending that key regulators, particularly ASIC, receive increased resources. Particularly given the increased demand on ASIC to proactively limit damage from disasters such as Storm Financial, Timbercorp, Trio and the Commonwealth Bank financial planning scandal, and to contribute to policy reform.

Indeed, Good Shepherd Microfinance argues that ASIC should play an even bigger role in safeguarding the financial system, including potentially giving the agency a role in regulating competition in the financial sector.

We applaud the recent work of ASIC in relation to the breaches brought against significant players in the payday lending and fringe lending fields. It is imperative that the Australian financial system is as equitable and fair as possible and this can only be achieved where there are affordable credit and loan services available safely to all.

In summary, Good Shepherd Microfinance applauds Government's commitment to review the Australian financial system. The forty-four recommendations of the FSI's final report are certainly positive steps towards a more efficient, fair and resilient system. However, we argue strongly for Government to invest in continuing and extending financial inclusion initiatives and to create conditions that promote impact investment that will realise increased social and financial returns. Not only will such initiatives ultimately save Government substantial expenditure in the welfare, health and justice sectors, it will build stronger, resilient Australian communities, families and individuals.

Dr Gillian McLwain  
Manager, Research and Policy  
Good Shepherd Microfinance  
March 25<sup>th</sup> 2015