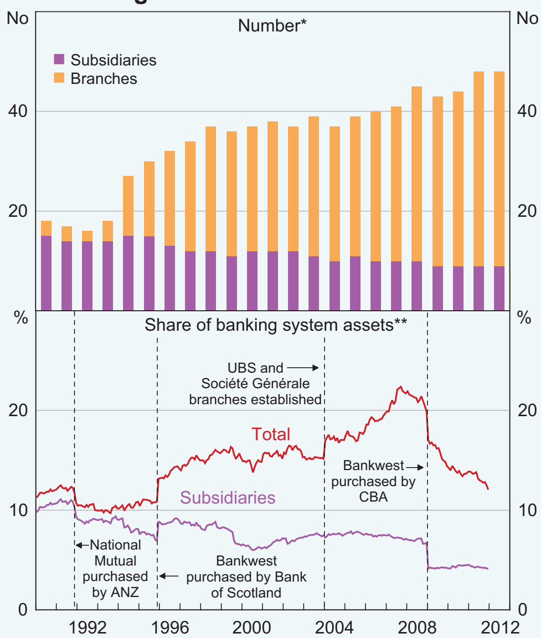
Box A

Foreign-owned Bank Activity in Australia

Since entry conditions for operating in Australia were further liberalised in 1992, the number of foreign-owned banks in Australia has been increasing steadily (Graph A1).[1] There are currently 48 foreign-owned banks in Australia, of which 39 are branches and 9 are subsidiaries, with some foreign-owned banks operating both a branch and a subsidiary. Subsidiaries are incorporated in Australia, must hold capital locally and are subject to the same prudential standards and supervision as Australian-owned banks. By contrast, branches are not locally incorporated, do not hold capital locally and are mainly supervised by the prudential regulator in their home country. Branches are not permitted to accept initial retail deposits from Australian residents of less than $250 000.

Increasingly, foreign-owned banks in Australia have tended to operate as branches: the number of branches has increased over the past two decades, while the number of subsidiaries has declined from 15 to 9. This mainly reflected some foreign banks replacing their Australian subsidiaries with branches and others selling their subsidiaries to Australian-owned banks, as well as new foreign branch entrants. Consistent with this, branches now account for around two-thirds of foreign-owned bank assets, up from about one-eighth in 1990. Branches vary in size, from less than $100 million to $20 billion in assets, and are typically smaller than subsidiaries. The largest subsidiary currently has around $47 billion in assets, making it the eighth largest bank in Australia; by comparison, the smallest of the four major banks has about $400 billion in resident assets.

Graph A1
Foreign-owned Banks in Australia



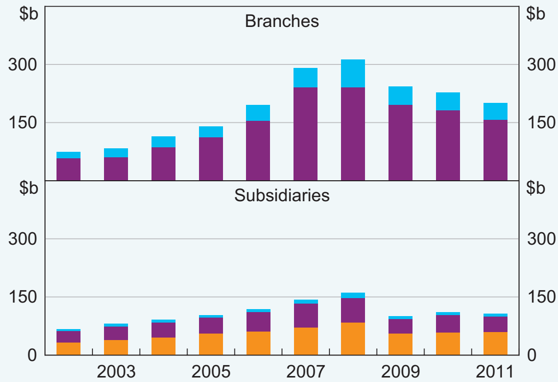
* As at end December, except for 2012 which is end February
** Domestic books
Sources: APRA; RBA

Branches tend to concentrate on wholesale banking operations because they have more flexibility to access funding globally, including through their parents, and are less constrained by large exposure limits, which helps them meet the demands of large corporate clients. By contrast, subsidiaries tend to be more retail focused, where large exposures are less significant, and their access to local retail depositors means they fund a larger share of their lending through deposits. This difference in business models is evident in the allocation of assets: the bulk of branches' assets are in commercial loans and securities, while the largest share of subsidiaries' assets are loans to households (Graph A2).

1 Further information on the history of foreign-owned banks operating in Australia is available in RBA (2007), 'Box C: Foreign-owned Banks in Australia', *Financial Stability Review*, March, pp 47–49.

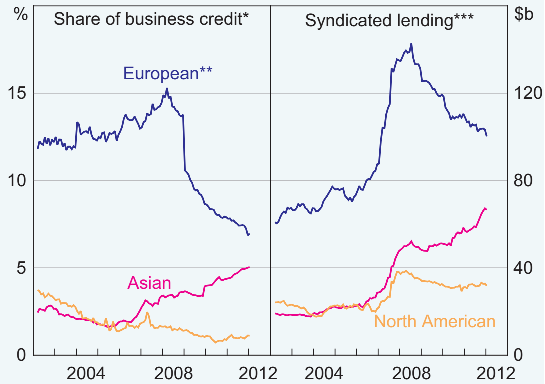
Graph A2
Foreign-owned Banks' Assets

Domestic books, end December



Source: APRA

Graph A3
Foreign-owned Bank Activity



* Bank credit; non-seasonally and non-break adjusted; includes securitisations
** Decline at the end of 2008 due to purchase of Bankwest by CBA
*** RBA estimates; includes offshore banks; mostly lending to non-financials
Sources: APRA; RBA; Thomson Reuters

Although the number of foreign-owned banks operating in Australia has more than doubled since the early 1990s, their share of bank assets at the end of 2011, at 12 per cent, was broadly the same. From around the mid 1990s to 2007, they noticeably increased their share of bank assets, from around 10 per cent to 22 per cent, due to a combination of acquisitions, new entrants and organic growth. Since the onset of the financial crisis, however, the foreign-owned banks' share of assets has fallen. Only part of this was due to CBA's purchase of Bankwest in 2008, which was the largest foreign-owned bank at the time. The foreign-owned banks that expanded the most in the years leading up to the crisis have typically also seen the largest contractions in their assets in recent years.

Many European-owned bank branches, in particular, have been reducing their activity in the Australian market over recent years, while Asian-owned banks have become more prominent. European-owned banks' share of business lending has declined by about 4 percentage points since early 2009, while Asian-owned banks have increased their share by about 2 percentage points (Graph A3, left panel). Much of the pullback by European-owned banks has been in commercial property lending, where their aggregate exposures have declined by about 60 per cent since the peak in 2009, compared with a 16 per cent fall for all banks. This may partly reflect their response to the relatively high impairment rates they have experienced on their commercial property loan portfolios in recent years. Some European banks have also been under pressure to deleverage because of difficulties their parents have been facing. The growth of Asian-owned banks over recent years reflects a growing appetite to expand their existing Australian operations as well as some new entrants from China and other countries in the region. Since 2010, seven new foreign bank licences have been granted in Australia, four of which were to Asian-owned banks.

Another way that foreign-owned banks provide finance in Australia is through cross-border lending. This is where an offshore bank provides loans directly to entities in Australia, typically large non-financial businesses, rather than through a domestic subsidiary or branch. Much of this lending is likely to be to businesses with a connection to the home country of the foreign bank. As with foreign banks lending through their Australian entities, cross-border lending has also moderated over recent years. Estimates suggest that outstanding cross-border loans to non-financial businesses in Australia declined from about $48 billion in 2007 (equivalent to 8 per cent of domestic business credit) to about $27 billion in December 2011 (4 per cent of business credit).

The recent changes in the involvement of foreign banks in Australia have also been evident in the syndicated loan market. The estimated outstanding value of syndicated loans to Australian borrowers provided by foreign-owned banks nearly tripled over the decade to 2008, to about $240 billion, but has since fallen by around 14 per cent (Graph A3, right panel). The recent fall was driven by European banks, partly offset by an increase in syndicated loans provided by Asian banks. European banks now account for a little over one-quarter of the outstanding value of syndicated loans provided by banks, down from over one-third in 2008, while Asian banks' share has increased to close to one-fifth.