Commonwealth Development Bank inspired ‘bold new schemes’

In 1959, the chairman of the Commonwealth Banking Corporation Board, Warren McDonald, announced that the main function of Australia’s new Commonwealth Development Bank (CDB) “would be to provide finance for primary production and for the establishment or development of industrial undertakings, particularly small ones, in cases where it considered the provision of finance was desirable and the finance would not otherwise be available on reasonable and suitable terms and conditions”. When the CDB commenced operation the following year, the 17 June 1960 *Canberra Times* reported that McDonald declared he was confident the newly formed bank would “help to encourage a resurgence of the pioneering spirit, inspiring men to undertake bold new schemes, which would not only benefit them personally, but the nation as a whole”. McDonald said it was the duty of the CDB to be concerned with the applicant’s prospects of success, rather than the value of their security. McDonald believed that “in every undeveloped area of Australia, particularly in the north and north-west, the bank can, and will, play a vital role in stepping up development”. In the CDB’s annual report the following year, McDonald lauded the “immense development prospects of Australia on a long-term basis”. The steady increase in demand for financial assistance from the CDB “clearly confirm[ed] the real and growing need for the type of finance which this Bank was designed to provide”.

The history and unique role of the CDB was documented in a 19 July 2019 article, “Who Remembers the Commonwealth Development Bank?”, authored by retired political economist and former University of Sydney lecturer, Dr Evan Jones. According to Dr Jones, the CDB “filled a niche in dealing with the particular needs of family farmers and small businesspeople. Such a niche must necessarily be filled by a public bank as profit driven banks are not interested in the necessary commitment of personnel resources and a ‘non-commercial’ low profit return.”

friendship or support.

BANKING CORPORATION TO INSPIRE “BOLD NEW SCHEMES”

MELBOURNE, Thursday. — Australians must recapture the pioneering spirit of the past if they are to effectively develop the country’s sparsely populated areas, the chairman of the Commonwealth Banking Corporation, Mr. Warren McDonald, said to-day.

Canberra Times, 17 June 1960.

The dismantling of the Commonwealth Development Bank

Despite its evident utility and specialist lending expertise, the Commonwealth Development Bank was dismantled as part of the deregulation policies implemented in Australia from the 1980s onwards. As the Citizens Party has reported, Australia’s modern financial system was based on principles developed by the 1981 Campbell Committee, namely, the “efficient markets theory”—the belief that government and regulatory intervention should be kept to a minimum, because the competitive market would cure all ills. In a 6 August 2001 opinion piece for the *Canberra Times*, Dr Evan Jones described an ideological notion which had “taken hold across a wide spectrum of decision-makers” during the 1980s-1990s—the belief that “comprehensive financial deregulation was inevitable and universally beneficial”. The Campbell Report had “set the tone”, by asserting wrongly that “there would be no role for specialist lenders after a full regime of ‘competition’ had replaced the then regulatory structure. … The CDB was seen as an unwelcome accessory to a glorious commercial future. The representation of the Development Bank in the parent bank’s annual reports shifted from a celebration of new loan approvals to hand-wringing about the CDB’s viability without government subsidy.”

In its final report, the Campbell Committee asserted that if government funding or assistance was deemed necessary in future, this “could be channelled through commercial lenders just as effectively as through a government-owned institution and in ways that minimise disturbance to competitive neutrality”. Although the Committee acknowledged the specialist lending expertise that the CDB had built up, the Committee “[saw] no sound economic case for retaining the CDB simply in order that it may act as a channel for concessional finance”.

The privatisation of the Commonwealth Bank commenced in mid-1991 and was completed in three stages, finalising in 1996. According to Dr Jones, in February 1991 the CDB was “cynically” made a subsidiary of the Commonwealth Bank to “boost the Commonwealth Bank’s assets”, shortly before the first tranche of privatisation. Although the dismantling of the CDB’s lending culture had begun several years earlier, in 1996 the Howard Government effectively abolished the Commonwealth Development Bank. The CDB’s specialist lending approach was not carried over into the rural lending division of the newly-privatised Commonwealth Bank, despite Treasurer Peter Costello’s promises to the contrary.

Competition fails to deliver to small business

The Campbell Committee believed that “in time the role of the CDB as a small business specialist commercial financier will decline, and its *raison d’être* will disappear, if the committee’s program of deregulation were implemented”. The Committee ideologically presumed that “in a more competitive, less regulated environment there will be increased opportunities for small businesses (including primary producers), with good prospects of success but without full collateral, to secure required finances from private sector intermediaries. For example, banks … would be expected to play directly a more active role in financing the development of businesses presently financed by the CDB”. The 1997 Financial System Inquiry (Wallis Inquiry), which further refined and championed the Campbell Inquiry’s principles, admitted that the increase in competition envisaged by the Campbell Committee had been “slow to arise”, including in the arena of small business lending. Nevertheless, the Wallis Inquiry remained resolutely committed to the “efficient markets” ideology. The Wallis Committee believed that “improving competition in the banking sector… will help deliver cheaper and more flexible credit” to small and medium sized businesses, claiming that “continued competitive pressure in the financial sector … should yield benefits” to small businesses.

Almost thirty years after the Campbell report, the promised benefits of a competitive, deregulated environment to small business had still not materialised. In testimony to a 2010 Senate inquiry into “Access of small business to finance”, small business owners stated that banks had lost the ability to value small businesses. A representative of the Council of Small Business testified that Australia needed a government-owned bank to fund small business development, because “[i]f you trust the [big four] banks it will not happen … They should treat farmers and small business as people. That is the issue. They are not.”

The 2010 inquiry’s final report acknowledged that submissions had called for a development bank to be established to “fill perceived gaps in lending by the private banks”. The pervading influence of the Campbell Committee’s ideology is evident in the response to that proposition. The banks claimed that there was “no compelling case” for a development bank, arguing that the establishment of a major government-owned bank would “erode competition”. Representatives from Treasury warned that a development bank could “lead to market distortions”. Although the final report of the Senate inquiry acknowledged the calls for a development bank (shrewdly observing that “[u]nsurprisingly, the banks were not keen on a rival being established”), the Senate Committee did not support the notion, instead “prefer[ring] to increase competition within the existing commercial banks”.

The following year, the same Senate Committee held an inquiry into competition within the Australian banking sector. Although witnesses told this inquiry that the supposed benefits of competition were actually having the opposite effect, by causing the major banks to force out any alternative providers, the Committee doubled down on its position. It still held the view that “the best way forward is to increase competition within the existing commercial banks rather than pursue a development or rural bank or to convert Australia Post into a bank”.

Several years later, the 2014 Financial System Inquiry (Murray Inquiry) acknowledged that some submissions had called for the government to “establish a Government-owned bank to direct funding to particular causes, such as rural businesses”. Demonstrating commitment to the “efficient markets” ideology of the Campbell Committee, the Murray Inquiry did not support a development bank because “to maximise the efficiency of the financial system policy makers should not set out to favour one particular funding destination over another”.

Almost four decades after the Campbell report was published, it is indisputable that the purported benefits of competition for small business and primary industry lending have not materialised. In June 2018, the Productivity Commission described Australia’s banking sector as “an established oligopoly”. The four major banks’ market power was “substantially supported by regulatory settings, which contribute to the major banks’ structural advantages.”

‘Officialdom in denial’ on the need for public banking

In witness testimony to numerous parliamentary inquiries over the last few decades, representatives of primary industry and small business have emphasised the urgent need for the re-establishment of a development bank. However, politicians and bureaucrats have continually brushed these needs aside, demonstrating a profound disconnection from the real-life impact of their ideological policies. As Dr Jones observed in his 2019 article, “Officialdom has been in denial since Campbell on the need for special purpose public credit institutions.”

For example, this denial was demonstrated in the 2010 “Access of small business to finance” inquiry. When the suggestion of small business loans guaranteed by the government was raised, Reserve Bank of Australia (RBA) Assistant Governor Guy Debelle responded: “The question you have to ask is: what is the reason that a financial institution is not willing to lend to this small business off its own bat? Are you going to be able to find small businesses that have viable propositions which a regular financial institution is not going to be willing to lend to?” In response to questioning from Senator Nick Xenophon, Debelle admitted that the RBA had not undertaken any studies to examine whether the presence of the Commonwealth Development Bank had resulted in competitive pressure on the other big banks when it was in operation. A search of the RBA’s website indicates that no such study has been undertaken since. In 24 March 2021 parliamentary testimony, a decade after the 2010 inquiry, now-Deputy Governor Debelle ironically revealed the real-world impacts of the RBA’s obtuseness, when he lamented that the RBA’s regular small business forums continually demonstrated how difficult it was for small businesses to access credit: “It begs the question as to whether we have the balance right. … We’ve had the same story [from small businesses] basically for the past 25 years.”

In an 18 March 2021 bulletin, “Australia’s Economic Recovery and Access to Small Business Finance”, the RBA reported that COVID-19 had disproportionately impacted small businesses. However, despite record low interest rate levels, lending activity to small and medium-sized businesses had little changed since the onset of COVID-19. According to the RBA, small businesses had less appetite for taking on additional debt, partly because of an uncertain economic outlook and the availability of government support measures, but “[m]ore generally, businesses tended to prefer to use retained earnings [i.e. savings] to finance investment when possible because it is less costly”. It is evident that the market has failed to meet the community’s need for reasonably-priced finance, and that the niche the Commonwealth Development Bank formerly filled has still not been met despite decades of deregulation and “efficient markets”.

The tide turns towards national banking

The findings of a 2020 parliamentary inquiry into regional inequality were consistent with the “many, many” inquiries which had been held previously; the inquiry’s final report noted that a number of witnesses had commented on the “large numbers of inquiries that have occurred with little result”. The Committee concluded: “Given the extensive research done into regional Australia and the many reports that have been written, it is the view of the committee that now is the time to take stock of those findings and advance a positive regional development program—a program that builds on what has been learned through the many and varied inquiries and *the expertise of those who live in the regions*.” (Emphasis added.) For decades, small business and primary industry representatives have testified to parliamentary committees that the re-establishment of a development bank is imperative, but to no avail. A year after the regional inequality inquiry’s report was published, the Morrison government has still not bothered to respond.

The ideological resistance to a national development bank, which prevails in bank-loyalist politicians and bureaucrats, is a carry-over from the Campbell inquiry. Forty years of failed policies have utterly discredited the Campbell Committee’s “efficient markets theory”, which justified the dismantling of the Commonwealth Development Bank.

However, the tide is turning. The Citizens Party has documented the rising crescendo of parliamentary calls for a national development bank, which are coming from members of all political parties, who are responding to the demands of their constituents and the genuine need in the community. A national development bank will inspire “bold new schemes” and power Australia’s “immense development prospects”, as envisaged by Commonwealth Banking Board Chair, Warren McDonald, over sixty years ago.

By Melissa Harrison, Australian Alert Service, 15 December 2021