Australia-India Comprehensive Economic Cooperation Agreement

ANZ Submission
October 2011

Introduction

ANZ welcomes the agreement by the Indian and Australian Governments to commence negotiations on a bilateral free trade agreement (Comprehensive Economic Cooperation Agreement) and appreciates the opportunity to comment on issues specific to financial services which we believe could be usefully addressed in any agreement.

ANZ's operations in India

ANZ has a long-standing, substantial and growing presence in the Asia-Pacific region. The breadth of ANZ's network puts it among the top five banks in Asia, with operations in 15 markets. ANZ has some of Australia's largest investments in Asia, including in India, Greater China, Indonesia and Vietnam. We are also the leading bank in the Pacific, operating full service retail and commercial banking operations in 11 countries.

ANZ's strategy is to become a 'super regional' bank in the Asia Pacific – that is, a bank that has the scale and quality of a global bank but with a regional focus. As part of our strategy, we have identified a number of priority markets in the region, of which India is one, in which we intend to significantly grow our business.

ANZ is strongly committed to building its business in India. Our India strategy is initially focused on establishing our Institutional business with the next phase of our strategy aimed at broadening our franchise to include the Private/Affluent Banking and broader wealth management business.

Since receiving final approval in October 2010 to open a branch in Mumbai, we have invested significantly in technology, operations, compliance and risk management systems in support of our new branch. We have hired an experienced team and injected more than the required regulatory capital into the business. At the same time, we continue to invest significantly in our Operations, Technology and Shared Services Centre in Bangalore which currently employs around 5,000 people. This is ANZ's largest pool of staff in any country other than Australia and New Zealand.

ANZ's AA rating, experience and focus on natural resources, infrastructure and agriculture, puts it in a unique position to play a role in supporting India's economic growth agenda. ANZ is supporting increasing numbers of Indian companies as they build their trade links with Australia, New Zealand and across the Asia Pacific region where we have a substantial and growing banking presence. We are confident that we could serve our Indian customers better through a wider network in India.

We are committed to building financial services capability and capacity in India and are investing in developing the skills sets of our staff. Within the last three years, the number of staff employed by our business has increased from less than 10 to over 80. And our ongoing expansion will continue to provide long-term, rewarding employment opportunities for our staff in India.

Financial services reform in India

In January 2011, the Reserve Bank of India (RBI) released a discussion paper on the presence of foreign banks in India. The paper provides a detailed outline of RBI thinking regarding the potential role of foreign banks in the Indian banking sector and policy options for the liberalisation of financial services more broadly.

The discussion paper was drafted to take into account the 'lessons learned' from the global financial crisis and follows the release in 2005 by the RBI of a two-phase 'liberalisation roadmap' for the financial services sector. This laid out a two track and 'gradualist approach' aimed at increasing the efficiency and stability of the banking sector in India. The first phase (March 2005 – March 2009) was divided into three mutually exclusive channels for foreign banks to enter the Indian market:

(i) Open a branch, subject to meeting capital and regulatory requirements. A commitment has been made through the WTO to allow at least 12 foreign bank branches per annum (inclusive of branch licences to existing players as well). A minimum initial capital requirement is US$25mn.

(ii) Set up a wholly-owned subsidiary, subject to capital and regulatory requirements, which would potentially allow for greater flexibility (ie. less restrictions) in building a branch network.

(iii) Invest in a private sector banks. Investment of up to 5% shareholding currently does not require RBI approval. Approval by the RBI to invest up to 74% in a bank deemed 'weak' by the RBI.

[Note: The RBI also proposed that banks which already have a full branch presence be prevented from gaining greater than 5% holding in a local bank, requiring a single mode of presence.]

The January 2011 discussion paper sets out the key principles of the RBI's proposed wholly owned subsidiary approach for foreign banks under which foreign banks will receive "similar" treatment as local banks, provided they incorporate locally. The key incentive to incorporate will be that (i) branch expansion across India will be made possible on a scale at par with local banks and (ii) foreign banks will be permitted to raise long-term rupee funding.

Some of the key costs/constraints to such a proposal from ANZ's perspective are broadly as follows:

- There should be some relaxation for new entrants like ANZ to create scale prior to meeting requirements to open branches in smaller cities/towns. New entrants (like ANZ) should be allowed to open branches in cities to create scale before opening branches in smaller cities/towns.
- Higher priority sector lending targets (PSL), under which foreign banks will be required to deploy 40% of their net bank credit to priority sectors determined by the National Credit Council and RBI but which generally include sectors such as: small scale industries, agriculture, village industries and micro enterprises; and
- The loss of parent company's counter party guarantees/credit rating

ANZ provided the RBI with specific comments on the paper. The key issue identified in our submission was that RBI should consider certain relaxations/flexibility to new entrants such as ANZ, including:

- A gradual (and viable) branch expansion requirement to allow for banking 'scale' to be built up over time;
- A greater transition period for meeting PSL requirements; and
- No requirement to divest ownership to a third party

We believe a number of our comments on the paper in our March 7th, 2011 letter could be usefully addressed by any CECA, particularly issues pertaining to branch expansion and the use of a parent company's guarantee/credit rating.

Australia-India Comprehensive Economic Cooperation Agreement

A comprehensive economic cooperation agreement covering trade in goods, trade in services, as well as investment between Australia and India would build on the complementary and rapidly developing economic and trade relationship between our two countries. Deeper economic relations would also build on growing bilateral engagement across a range of areas, including commercial, strategic and security matters.

For an advanced, predominantly services based economy such as Australia's, delivering outcomes on services as part of the CECA will be important. Negotiating better access or more certainty for Australian service providers investing in India will help expand and diversify Australia's export base, particularly as demand for services in India grows. Australia's growing trade in services with India will involve the interaction of increasing numbers of Australians with clients, customers and service providers in India, contributing directly to Australia's connections with India, including already strong, and growing people to people links.

ANZ would be supportive of Australian efforts to work with India to strengthen the relationship and co-operation between both countries and to enhance institutional capacity to effectively exploit new market opportunities created by an Australia-India CECA. In this context, ANZ would welcome further relationship and capacity building exercises between Australia and India financial services regulators and would stand ready to assist wherever possible.

Market access remains challenging for foreign banks in India. While the RBI's January 2011 Discussion Paper proposes to liberalise branch licensing requirements, foreign banks will continue to find it difficult to expand their operations organically. This is due to the fact that there remains a high degree of uncertainty around the extent to which foreign banks will be permitted to open branches in desired locations while having to meet the RBI's specified criteria (outlined above).

ANZ's presence in India through its bank branch means that it now faces many of the same regulatory requirements as for Indian banks pertaining to the sorts of banking products we can offer our customers. Notwithstanding, the regulatory approvals process for obtaining multiple licenses and authorisation to enable ANZ to offer its current suite of products (approximately 26 separate licenses in total) was resource intensive which resulted in delays in our ability to deliver products to our customers. Streamlining of the licencing process will be extremely beneficial to all banks.

An Australia-India CECA should ideally seek to liberalise the rate at which banks can open branches in India. We are aware that currently RBI is issuing more than 12 branch licenses per annum (12 is the minimum number under India's WTO commitments), inclusive of foreign banks that already have a branch presence in India, however the number of licenses issued remains well below current demand. In this context, the CECA could potentially draw on other such agreements as a model for further liberalisation. The CECA signed between India and Singapore in 2005 has allowed (for the most part) more rapid entry into each other's financial services markets than that permitted for banks of other countries, including an agreement to give qualifying full bank (QFB) status to three banks from each country.

Notwithstanding, it took until 2008 for prudential and investment issues to be resolved. In March 2008, the RBI granted licenses to two Singapore banks – (i) DBS, which received approval to open eight branches and (ii) United Overseas Bank (UOB) which received approval to open one branch in Mumbai. In turn, the Monetary Authority of Singapore approved a full bank licence to State Bank of India with privileges to establish up to 25 outlets, including ATMs, making SBI the first Indian bank to obtain QFB status in Singapore. Other banks, including Bank of Baroda and Bank of India, have also applied for a QFB licence.

The CECA also supports greater cooperation between India and Singapore on financial services, including between their respective stock exchanges.

It is worth noting that there are a number of tax-related issues, principally withholding tax, that impact on the operations of Australian banks in India. The table below highlights key countries with which India has signed a Direct Tax Avoidance Agreement (DTAA) and the rates at which tax is withheld (WHT) in India on the interest income earned by the banks in these countries. For Australia, the WHT rate is 15 %, comparatively higher than WHT for the other countries listed.

Country	WHT Rate (%)
Australia	**15%**
USA	10%
UK	10%
Germany	10%
China	10%
Singapore	10%
New Zealand	10%

While taxation issues do not represent direct trade barriers and do not necessarily lend themselves to inclusion in FTA negotiations, they do impact on the operations of Australian financial service providers in the Indian marketplace. In this context, we would welcome consideration being given to establishing a dialogue with Indian officials on these issues with a view to reviewing these requirements as part of the existing Australia-India double taxation agreement.

Impact of an Australia-India Comprehensive Economic Cooperation Agreement on ANZ

In any consideration of whether to invest or establish operations offshore, ANZ looks for transparent regulations and corporate governance based on international standards, rule of law (and enforcement thereof), clearly defined dispute mechanisms and a well resourced and independent regulatory structure with strong prudential oversight.

In the case of financial services, regulatory transparency and policies governing activities of financial institutions are integral in facilitating access of foreign financial institutions to markets. In the context of an Australia-India CECA, Australia could seek to ensure the agreement enhances the regulatory and governance arrangements for financial services to ensure Australian companies are treated no less favourably than their Indian counterparts in most, if not all, aspect of business.

There is scope for an Australia-India CECA to lock in reforms that will result in a more open and competitive market, providing further opportunities for Australian companies to invest in growing their business in India. A comprehensive, high quality agreement could facilitate the provision of a greater range of services to Indian companies from Australian services providers, and vice-versa, further boosting bilateral economic and trade links. Any gains made under a Australian-India CECA could also potentially make decisions to invest in growing ANZ's business in India more attractive.

Conclusion

ANZ strongly welcomes the decision to commence negotiations on a bilateral CECA between Australia and India. As Australia's largest services sector investor in India, we are strong supporters of efforts to deepen relations between Australia and India, including initiatives designed to help build capacity and capability in India.

We believe a CECA between Australia and India would lead to increased bilateral trade and investment flows and have a positive impact over time on the business and regulatory culture in India. In doing so, the Agreement would deepen economic with Australia's fastest growing trade partner.

ANZ looks forward to being involved in future Australia-India CECA consultations. Should you require further information about this submission please contact:

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