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**John Quiggin**

**Australian Research Council Senior Fellow**

**School of Economics**

**Faculty of Economics and Commerce**

**Australian National University**

**EMAIL [John.Quiggin@anu.edu.au](mailto:John.Quiggin@anu.edu.au)**

**FAX + 61 2 61255124**

**Phone + 61 2 61254853 (bh)**

**+ 61 2 62578992(ah)**

**<http://ecocomm.anu.edu.au/quiggin>**

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## **The ‘People’s Bank’: the privatisation of the Commonwealth Bank and the case for a new publicly-owned bank**

Among the policies for which the Hawke–Keating Labor government is remembered, two of the most prominent were privatisation and financial deregulation. The combination of these two policies was symbolised by the conversion of the Commonwealth Bank from the ‘people’s bank’ to a private organisation devoted to maximising returns to its shareholders and managers, and free of any social or community obligations. Even more than financial deregulation, the Hawke–Keating government’s embrace of privatisation represented a fundamental break with the traditional policies of the Labor Party. The political damage associated with privatisation was immense. Not only was the sale of ‘icons’ like the Commonwealth Bank regarded with immense hostility, even in conservative sections of the electorate, but these actions, taken in breach of the most explicit promises, destroyed Labor’s credibility in arguing against the sale of Telstra in the 1996 election campaign.

More fundamentally, privatisation provided a clear refutation of the claims, put forward particularly by the NSW Right of the Labor Party, that the Hawke-Keating government was in the mainstream Labor tradition represented by such leaders as McKell. However far from dogmatic socialism McKell and others might have been, no one could imagine them selling off the Commonwealth Bank. Privatisation was a key factor in eroding Labor’s base of committed supporters, the 40 per cent or so of the population who could, until around 1987, be relied upon to vote Labor through thick and thin. By 1996, Labor’s primary vote had fallen to 38.7 per cent, the lowest since World War II, and one of the lowest since Federation.

Prior to the 1983 election, Labor had reaffirmed its socialist objective and condemned the proposals for financial deregulation put forward by the Campbell Committee. Labor’s position on financial deregulation was rapidly reversed. In December 1983, the dollar was floated and, by 1986, policies of deregulation more radical than those proposed by

the Campbell Committee had been adopted.

Labor's conversion to privatisation was more gradual. In 1986 Labor ran a successful South Australian state election campaign against privatisation, with Hawke and other Federal figures playing a prominent role. The ALP represented itself as an implacable opponent of privatisation.

The commitment of the leading figures in the government to privatisation was evident by the late 1980s, but it took some years before the opposition of the Labor party membership could be overcome, and large scale privatisation could be implemented. Over this period, the Labor leadership displayed almost unparalleled hypocrisy; attacking the coalition's proposals to privatise the Commonwealth Bank in the election campaign of early 1990, but making a decision in favour of partial privatisation later in the same year. At each stage in the privatisation of the Commonwealth Bank, solemn assurances were given that this sale would be the last.

From 1991 onwards, the policy of privatisation was essentially unchallenged within the Hawke–Keating government. The Commonwealth Bank was privatised in three stages, the last stage being implemented after Labor lost office in 1996. At each of the first two stages, apparently binding commitments to continued majority public ownership were made by the government, and subsequently broken.

A striking feature of this process was the way in which the failures of deregulation and privatisation simply paved the way for more deregulation and privatisation. The most notable examples were the collapses of the Victorian and South Australian State Banks.

These disasters were not the result of old-fashioned socialists interfering in the private sector, but followed the adoption of market-oriented policies advocated by Keating. The Cain and Bannon governments came to grief by dutifully adhering to the Keating gospel of financial deregulation. During the financial bubble of the late 1980s, they allowed a free rein to State Banks and to private, but state-regulated, financial institutions.

Both governments came to grief when Keating gave us ‘the recession we had to have’.

Amazingly, Keating not only escaped any blame for these disasters but used them to push his agenda further. The need to rescue the State Bank of Victoria was used to force through the full privatisation of the Commonwealth Bank, while the example of the State Bank of South Australia has been used repeatedly to press the case against all forms of public ownership.

The privatisation of the Commonwealth Bank was a financial disaster for the Australian public, although investors in the float did very well indeed. The capital structure established prior to the sale of the first tranche of shares in 1991 involved the issue of 835 million shares. Although the par value for the shares was set at \$2, the relevant consideration for valuation is the issue price which was set at \$5.40. This implies a valuation of \$4.5 billion for the Bank as a whole, (or about \$5 billion valued in 1995-96 dollars<sup>0</sup>). The procedure for the sale of the second tranche of shares in 1993 ensured that the government received an amount close to the market price of the shares at the date of sale, which turned out to be around \$9.50, implying a valuation for the Bank as a whole of \$7.9 billion, or about \$8.5 billion in 1995-96 dollars. The final share offer for the Bank was announced in June 1996. The sale price was around \$10 per share, also implying a valuation of \$8.5 billion in 1995-96 dollars. The total proceeds from the three stages of the sale amounted to about \$7.8 billion in 1995-96 dollars.

Average real annual profits over the period 1988–93 (which covers a complete business cycle) were around \$560 million. Computing the present value of this stream of profits at a discount rate of 5 per cent yields a value of \$11.2 billion for the Bank as a whole. Therefore, even if profits had not increased after 1993, the public would have incurred a loss of around \$3.5 billion from the privatisation. In fact, primarily because of the removal of restrictions on the monopoly power of the banks, profits have soared. Profits for the three years from 1998 to 2000 totalled \$5.4 billion, or more than half the total sale proceeds received by the Australian public.

Financial deregulation has been similarly disastrous. Since the advent of financial deregulation, banks have raised fees and charges, cut services and exploited their collective monopoly power whenever possible.

Prudential regulation is in a similar mess. As a result of recent reforms, no one knows whether or not bank deposits are guaranteed by the Australian government. However, because the major banks are considered 'too big to fail', they are generally considered to be effectively guaranteed. Of course, except when faced with irresistible political pressure, they reject any notion of a corresponding social obligation.

In these circumstances, it is encouraging to observe that New Zealand, which led the charge towards radical free-market reform is about to re-establish a publicly-owned bank. The 'Kiwi Bank' will be operated by the New Zealand Post Office, one of the few government business enterprises not sold off by the radical free-market governments that wrecked the New Zealand economy between 1984 and 1999.

Australia should follow New Zealand's lead. Moreover it should stop providing free insurance to profit-oriented banks. Deposit guarantees should be explicitly confined to savings banks that operate subject to a charter of community service obligations similar to that which would be followed by a publicly-owned bank. Other banks would have to give explicit warnings to their depositors that they were investing at their own risk.

The private banks (including, of course, the Commonwealth) would then be faced with a clear choice. They could spin off their merchant banking, insurance and other activities, and operate as savings banks. Alternatively they could live up to their free-market rhetoric and take their chances without the crutch of a public guarantee.