3 April 2001

Mr Guy Eastwood
Senior Manager
Capital & Risk Analysis
Australian Prudential Regulation Authority
GPO Box 9836
SYDNEY NSW 2001

Dear Mr Eastwood

Re: New Basel Accord

Adelaide Bank welcomes the opportunity to comment upon the proposed New Basel Accord.

The Bank supports the underlying principles of the New Accord, but would like to raise some issues for consideration.

The first issue is the risk weighting applied to housing loans under the standardised approach.

In its submission to the Basel Committee on Banking Supervison, APRA established that the credit risk on Australian housing loans is low. The Committee has not seen fit to respond positively to that submission. There appear to be some options open within the proposed accord to achieve a lower risk weighting for housing loans.

The first option is that some recognition be given to loans with a low loan to valuation ratio. Under this suggestion loans with a loan to valuation ratio of less than, say seventy percent would qualify for a lesser risk weighting.

The Accord recognises that "retail portfolios" may have a lower level of credit risk due to the high level of granularity of these portfolios. We note that further work is to be undertaken on "retail portfolios" and that this may result in a lower risk weighting being applied to housing loans.

The Accord also recognises the existence of credit risk mitigation. Mortgage loss insurance is not specifically recognised as a credit loss mitigant, although its primary purpose is to transfer credit risk from the Bank to the insurer. Whilst it is acknowledged that extensive use of mortgage loss insurance may give rise to large credit exposures to the insurers, there should be some allowance for this form of insurance as a mitigant.

It is also worthy of note that a claim on a securitisation vehicle rated AAA to AA- would qualify for a risk weighting of 20%. This means that a bank would have a better capital position if it securitised all of its mortgage loans and invested the proceeds in mortgage-backed paper. There is essentially no change in the risk profile and yet the risk weighting is reduced.

By using one or more of the above avenues it would be possible to grant a lower risk weighting to housing loans.

The second issue that we would like to raise is that of collateral lending. The definitions within this section of the Accord include "margin lending" whereby monies are advanced against the security of shares listed on a recognised stock exchange. Unfortunately, the detail within the Accord only allows recognition of collateral, and the resultant concessional risk weighting, if a credit assessment has been carried out on the borrower. The nature of margin lending is such that it is not normal practice to perform credit assessment of borrowers. The disciplines applied to this business include a forced sell-down of shares if the margin payment is not made within twenty-four hours. Other restrictions are put in place to avoid lending against shares that are not liquid. I have set out below a summary of the portfolio restrictions on margin lending at Adelaide Bank.

Concentration Restrictions
- At least 95% must be ASX top 15%
- At least 40% must be ASX top 50
- At least 65% must be ASX top 100
- Internet / new Telco stocks with no profit history must comprise less than 4% of total security
- Resource stocks cannot exceed 25%
- Stocks must have a market cap of at least $100M
- Any one Managed Fund not to exceed $10M

Single Stock Restrictions
- Big Four banks or Telstra - maximum 20% each
- Top 10 ASX stocks not more than 15% each
- Top 50 ASX stocks not more than 12% each
- Outside top 50 ASX - not more than 8%
- Outside of ASX Top 15% - not more than 1%
- Stocks pending listing - not more than 10%
- Any stock rated less than investment grade or unrated - not more than 5%

Turnover Parameters

- Restricted by the average total turnover
- For each stock, total portfolio exposure is restricted to not more than 5 times the average turnover based on the past 12 months turnover

The final issue that Adelaide bank would like to raise in respect of the Accord is that of Market Discipline. Adelaide Bank is broadly supportive of a full and meaningful disclosure, but believes that the Accord goes further than is required for an investor's understanding of the risks undertaken by the business. In some cases, for example disclosure of the scores used in credit decisions, a bank would be disclosing proprietary information that may assist competitors more than it would investors.

As a rule of thumb, Adelaide Bank supports disclosure, provided this does not result in disclosure of proprietary information.

There are several other issues that relate to implementation of the Accord and I would hope that APRA will see fit to consult on these issues at an appropriate time.

Yours sincerely

Brian Walker
Strategic Planning Manager