Wilson Asset Management
Making a difference

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General Manager
Policy
Policy and Advice Division
Australian Prudential Regulation Authority

Email: policydevelopment@apra.gov.au

RE: APRA's Discussion Paper titled 'A more effective capital framework for a crisis' on the proposed phase out of Additional Tier 1 (AT1) capital which are commonly known as ('bank hybrids')

Dear General Manager for Policy,

On behalf of Wilson Asset Management, we welcome the opportunity to provide a response to the Australian Prudential Regulatory Association's (APRA) 'A more effective capital framework for a crisis' Discussion Paper on the proposed phase out of financial institutional Additional Tier 1 (AT1) capital from Australian banks, commonly known as 'bank hybrids'.

Wilson Asset Management is the investment manager for eight listed investment companies, investing over $5.5 billion on behalf of more than 130,000 retail investors. We are passionate about making a difference, including advocating for the fair and equitable treatment of retail shareholders.

We object to the proposed phase out of retail access to 'bank hybrids' as we believe they play an important role in both retail investors' portfolios and banks' capital structures. Retail investors represent around 20% to 25% of the $40 billion plus bank and insurance company ASX-listed hybrid market. This is predominantly held through self-managed super funds (SMSFs).

Hybrids are very popular with Australian retail investors as they offer higher-yielding franked-income streams with both debt and equity characteristics. The removal of these securities from the retail investors' investment universe, would deprive their investment portfolio of diversification benefits with respect to risk and returns. It would also reduce valuable franked income streams, especially for retirees and those in SMSFs.

We object to the proposed changes based on the following:

'Bank hybrids' play an important role in many retail investor's portfolios

- 'Bank hybrids' fall outside traditional asset classes such as equities and debt by offering retail investors a security with both debt and equity characteristics. Given their unique structure, the removal of 'bank hybrids' as an investment option would reduce portfolio diversification;
- In addition to its diversifying benefit, 'bank hybrids' are generally high-yielding and provide franked income, making them a valuable income generating option for retail investors' SMSFs, superannuation funds and retirees.

Phasing out access to 'bank hybrids' will limit retail investor's investment options

- Retail investors do not have access to wholesale unlisted subordinated debt. By phasing out access to bank hybrid securities, it will result in the exclusion of retail investors from an important Australian fixed income type product;
- The proposed changes leave retail investors with fewer lower-risk income investment options, pushing them towards higher risk options. Where will this money be redirected? Will retail investors buy equity or debt as a replacement? 'Bank hybrids' offer a different risk profile to equity and debt and serve a purpose in managing risk in portfolios. Removal of such options could force investors to move up the risk curve e.g. towards retail dominated bank equities that are generally riskier than bank hybrids.

If APRA perceives the risk of 'bank hybrids' as too high, why can retail investors invest in wholesale structures that own 'bank hybrids'?

Retail investors can still invest in 'bank hybrids' through wholesale vehicles e.g. through a managed fund. This means retail investors are still exposed to the same supposed level of risk identified by APRA albeit through a different investment structure.

Australia has different and conservative prudential conditions to the rest of the world

The Credit Suisse example provided by APRA as the reason for the proposed removal of listed bank hybrids was the result of an issue-specific clause. Credit Suisse's collapse and subsequent bailout by government-supported UBS saw hybrid owners lose their funds whilst shareholders got paid. It's important to highlight that Australia's prudential framework is much more conservative compared to its global peers. There is no history of Australian banks collapsing. Our current regulatory framework is extremely strong, and our banks' credit ratings are some of the highest in the world.

Why can insurance companies still offer hybrids?

If APRA perceives the risk of hybrids as too high, why can insurance companies still issue hybrids directly to retail investors?

Proposed solution – educating investors on the associated risk of 'bank hybrids' like equities/debt

Retail investors are free to own bank equities which are higher risk securities in a bank's capital structure than 'bank hybrids', so why take away the option of owning lower risk investments? We suggest investors should be able to make up their own mind by assessing the risks of investing in hybrids. They can either educate themselves or consult with existing adviser and broker channels.

In conclusion

We thank APRA for allowing us to highlight the impact of removing 'bank hybrids' from retail investors' investment universe. Wilson Asset Management believes that all shareholders should be treated fairly and equitably. In our experience, retail investors understand the risks of owning equities and have the capacity to understand the complexity of 'bank hybrids' and any associated risks. We would welcome the opportunity to address APRA at a hearing on this matter if required.

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If you have any questions on our submission, please call myself or the team on the below contact details:

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Yours sincerely,

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Chairman & Chief Investment Officer	**Chief Executive Officer**	**Chief Financial Officer**
Wilson Asset Management	**Wilson Asset Management**	**Wilson Asset Management**