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Productivity Commission
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Re: Productivity Commission draft report - Competition in the Australian financial system

Dear Commissioners,

We welcome your thorough Draft Report. It clearly describes the weakness of competition in several important banking markets. We support the general thrust of all the recommendations: lower barriers to new entrants, empower consumers with more transparent pricing, and root out conflicts of interest. All of these changes are needed to make competition work more effectively in banking markets, which will ultimately lead to lower prices and better service for consumers.

We are a money transfer start-up with a mission to bring fairness and transparency into our sector. This market is dominated by banks whose practices are dishonest and unfair, designed deliberately to boost their profits. In this Submission, we share information on two areas in particular for you to consider as you finalise your Report.

Firstly, on the New Payments Platform. As you have noted, the NPP faces a serious conflict of interest which is likely to prevent new entrants from becoming Members. Access to payment systems is an essential supply for competitors in the market for payment services. NPP's current governance model reinforces a situation whereby suppliers (banks) control access to this essential supply to their competitors (fintech payment companies). Due to so-called "de-risking" fintechs struggle to obtain and maintain access to payment services through banks in Australia. This makes direct access to NPP even more critical. We therefore ask that you strengthen Draft Recommendation 10.5 with the following two additional aspects:

- There should not be a requirement to purchase shares to become a direct member of NPP. If a new entrant connects to the system this does not raise costs for existing members. Therefore this entrance fee is a barrier to entry with little economic rationale. The equivalent payment scheme in the UK only charges for actual costs (e.g. software purchases) and has no requirement to purchase shares in order to connect directly.
- The requirement to be an ADI to connect to NPP effectively creates a \$5 million collateral requirement (the minimum amount set by APRA for ADIs). The UK has recognised that payment companies are already regulated under separate legislation and therefore mandated the payment system to allow direct access to these players. In Australia, an AFS Licensee (issued by ASIC) with permissions to handle payments is already a sufficient regulatory basis for these firms to operate with indirect access.

Gaining direct access does not change the scope of regulated activities. Also, RBA does not require an ADI licence to operate an Exchange Settlement Account. Therefore the requirement to be an ADI is an unnecessary barrier to entry and should be dropped.

Secondly, on the market for overseas money transfers. We agree that “the lack of transparency across the financial system makes it very difficult for consumers to identify the most suitable products for their circumstances”. Your report does not cover the market for overseas money transfers, in which an estimated \$3.1 billion is lost by consumers annually in hidden fees¹. The headline fee advertised by banks is a small portion of the total cost - the rest is generated in exchange rate mark-ups². Most consumers do not understand this and therefore cannot compare the total costs between providers: the table below illustrates the problem.

Provider	Exchange rate	Cost of rate mark-up	Disclosed transfer fee	Amount received (GBP)
Reuters	0.5995	N/A (this is a reference rate for comparison, not a transfer provider)		599.50
TransferWise	0.5995	0	6.95	595.33
ANZ	0.5699	\$51.90	18	569.92
CommBank	0.5667	\$ 57.77	22	566.73
NAB	0.5701	\$ 51.53	22	570.09
WestPac	0.5642	\$ 62.39	20	564.23

We request that you study this issue and would recommend the following additional Recommendation in the Report:

- ASIC already sets expectations for transparency in ASIC’s Regulatory Guide on Disclosure³ but banks (all the banks are AFS Licensees) have not complied with the spirit of this regulation. ASIC should clarify that their expectations apply to cross-border payments, and cite examples of good and bad practice. This will create real transparency and therefore more effective competition. Consumers will ultimately benefit from lower prices and improved service levels.

Kind regards,

Lukas May
Head of Banking, TransferWise

¹ See Appendix 2, Capital Economics

² See Appendix 1 for a worked example of this.

³ “We believe that the need for clear, concise and effective disclosure is most relevant for the disclosure of fees and charges [...] various costs, fees, charges, expenses, benefits and interests must be stated as amounts in dollars”
<http://download.asic.gov.au/media/1240931/rg168-published-28-october-2011.pdf>

Appendix 1: Examples of misleading practices

Fig 1.1

The screenshot shows a bank's website navigation bar with categories: BANKING, HOME BUYING, INVESTING, SUPER & RETIRING, BUSINESS, and INSTITUTION. Below the navigation bar is a breadcrumb trail: [Personal](#) / [International](#) / International Money Transfer. The main heading is "International Money Transfer" in a large, bold font. Below the heading is a sub-heading: "Send money overseas using NetBank or the CommBank app with transfer fees from \$6 (when you send in foreign currency)." A prominent yellow button labeled "Send now" is positioned below the text. A vertical yellow bar is on the left side of the main content area.

Fig 1.1 is a typical example of the advertising used by all the major banks in Australia. The transfer fee is cited as a fixed \$6 cost. A typical consumer would form a reasonable expectation that this represents the full cost of the transfer, as our evidence shows (see Appendix 2).

Fig 1.2

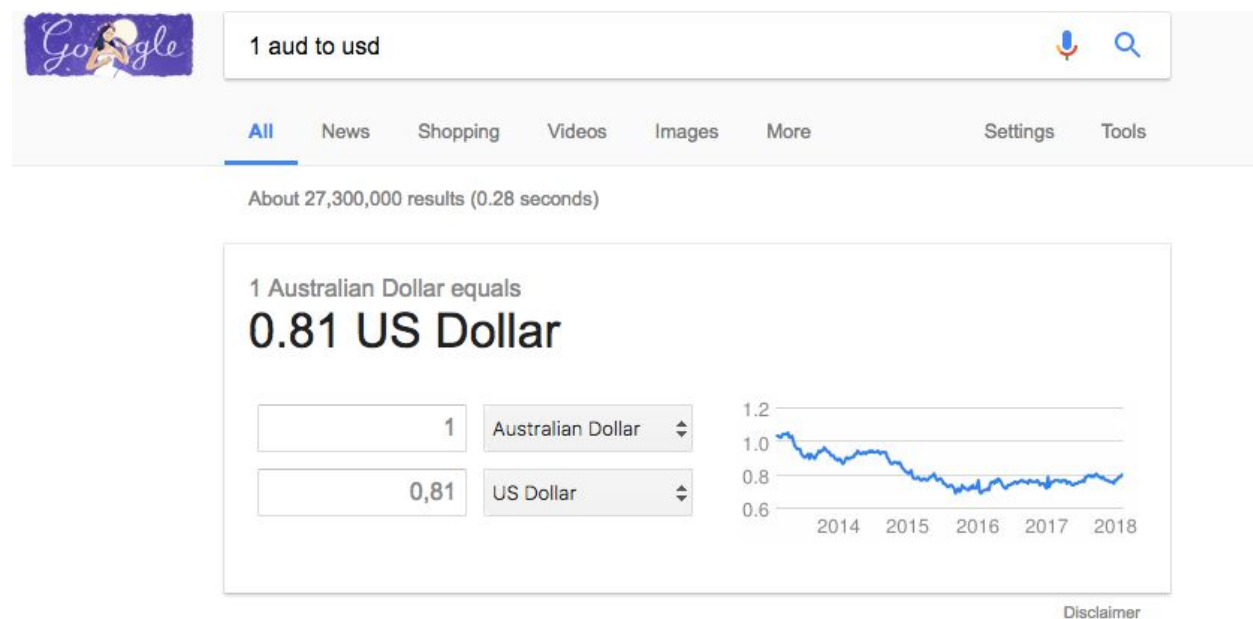
Amount

Transfer amount	<input type="text" value="1,000.00"/>	AUD	=	Recipient's currency	<input type="text" value="770.10"/>	USD	Exchange rate 1 AUD = 0.7701 USD Or enter a promo code
Transfer fee	AUD 6.00	✔ You're paying lower fees by sending in foreign currency					
Total amount	AUD 1,006.00	2018-01-29 15:51					
You're sending	USD 770.10						

Fig 1.2 shows a transfer of 1,000 AUD with CommBank, as shown to a customer (timestamp has been added to allow exchange rate comparison). As noted elsewhere in CommBank's advertising, there is a fixed fee of \$6 applied. The exchange rate is quoted to four decimal places, but there is no explanation as to how this rate is arrived at. The typical benchmark used by banks for exchange rates is the inter-bank spot market, which is also available through Google for comparison purposes. Fig 1.3 shows the spot rate for the same time that CommBank quoted 1 AUD = 0.7701 USD. This rate implies a further cost of USD 39.90 in the exchange rate mark-up that is levied by CommBank⁴. The majority of customers are unaware of this additional cost and the fact that it varies significantly between providers.

In Fig 1.4 (screenshots taken on a different day, therefore rates are different) we share a proposed, more transparent solution, that we believe would comply with the spirit of ASIC's transparency requirements as set out in the RG on Disclosure. Here a customer would be made aware of the \$6 fixed fee, as well as the exchange rate mark-up, by reference to a commonly accepted benchmark rate.

Fig 1.3



⁴ The additional US dollars that would be earned if the customer had been provided with the benchmark rate can be calculated by the amount sent in AUD multiplied by the gap in the AUD-USD exchange rate: $1000 * (0.81 - 0.7701) = 1000 * 0.0399 = 39.90$

Fig 1.4

Today

Payment details

From

Amount

USD (US Dollar)

1,000.00

Exchange rate 1 AUD = 0.7367 USD

[Or enter a promo code](#)

= AUD (Australian Dollar)

1,357.40

You're sending: USD 1,000.00

Amount: AUD 1,357.40

Transfer fee: AUD 22.00

Total amount: AUD 1,379.40

Required w/ transparency law

Payment details

From

Amount

USD (US Dollar)

1,000.00

Exchange rate 1 AUD = 0.7367 USD

[Or enter a promo code](#)

= AUD (Australian Dollar)

1,357.40

Amount: AUD 1,357.40

Transfer fee: AUD 22.00

Total amount: AUD 1,379.40

Benchmark rate: 0.78030

Bank rate: 0.73670

Benchmark amount: USD 1,043.60

Exchange rate markup: USD 43.60 / AUD 55.88

Total cost*: 77.88 AUD

You're sending: USD 1,000.00

Appendix 2: Survey data & research

(i) Galaxy Research survey of 1,004 Australians (December 2017)

Galaxy Research designed a questionnaire which was aimed at finding Australia's views on three areas:

- Living abroad
- Immigration
- Transferring money overseas

This study was conducted online among a representative sample of respondents aged 18 years and older. The sample comprises 1,004 respondents, distributed throughout Australia including both capital city and non-capital city areas. The data was weighted by age, gender and region to reflect the latest population estimates.

Each question was analysed by a series of a dozen demographic variables. The main findings related to transferring money overseas were:

- One in three Australians (35%) have transferred money overseas.
- Australia's banks lack transparency. Only one in five Australians (20%) understand that when transferring money overseas through a bank they pay an upfront fee and an exchange rate mark-up. Many (18%) think there is just an upfront fee or have no idea how banks carve out a margin (47%).
- Only 28% of those that have experience in transferring money overseas actually understand how the banks actually generate revenue - that banks add a margin to the exchange rate in addition to the upfront fee they disclose.
- More than one million Australians believe the banks provide money transfers overseas as a free service.
- Among those born outside of Australia, around half (49%) have transferred money overseas. The main reasons for transferring money overseas are family and friends (57%), in exchange for goods (34%) and travel related expenditure (20%).
- The most popular way to transfer money overseas is through a bank (67%). Others have used Western Union (29%) or else online transfer services such as TransferWise (17%).

(ii) Capital Economics analysis of consumer detriment (August 2017)

Capital Economics carried out a study into the costs of exchange rates for money transfers and card payments overseas.

Key Findings

Australian consumers and businesses spent A\$3.9 billion on foreign currency fees in 2016, of which over A\$3.1bn was in exchange rate mark-ups and card spending charges applied by banks and currency brokers to international transactions.

This equates to a loss of \$167⁵ in fees to banks and brokers for every Australian adult in 2016 or \$513 for each family.

Between 2012-2016, Australian consumers & businesses have spent over A\$14.7bn in fees on foreign currency transactions. As the world becomes more global this figure is increasing year on year.

Impact on Consumers

In 2016, Australian holidaymakers and work travellers paid \$1.1 billion in fees for exchanging currency.

This figure includes more than \$110 million in exchange rate mark-ups on cash exchanged before travelling overseas, more than \$930m in exchange rate mark-ups and fee charges applied to card purchases abroad, and almost \$170 million in charges for overseas cash withdrawals.

On average, \$180 is spent on exchange rate mark-ups and card fees for every trip abroad taken by an Australian.⁶

Impact on Businesses

The impact on Australian businesses in 2016 was large as well. Australian businesses importing and exporting goods and services paid A\$1.5 billion in rate mark-ups in 2016 alone. Just A\$15m was advertised to these businesses in upfront transaction fees. Small and medium enterprises in particular paid almost \$150m in exchange rate mark-ups on exports - 150 times more than the \$1m advertised to them in upfront fees.

Impact on Remittances

Remittance outflows from Australia totalled \$9.8 billion in 2016. Remitters paid nearly \$220 million in rate mark-ups in 2016. Over the past five years they have paid a total of almost \$960 million.

Methodology

This research was conducted by independent consultancy Capital Economics, commissioned by TransferWise in June 2017. It estimates the fees paid by consumers and businesses on foreign exchange transactions each year in Australia from 2011 to 2016 in four areas:

1. Spending by Australian consumers abroad – covering holidays, business trips and visits to friends and relatives

⁵ Population aged 18 and over = 18.771m

⁶ <http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Main+Features20Sep+2010>

2. Trade in goods and services – small and medium sized enterprises and large businesses import and export goods or services

3. Remittances from Australia – workers pay fees when they send money to family or friends who live abroad

4. Portfolio investment earnings abroad

Overall Summary

Fees (\$ million, current prices)						
Fees on remittance outflows from Australia	2011	2012	2013	2014	2015	2016
Total fees	714	785	804	740	858	883
<i>Of which, exchange rate margins</i>	157	173	185	169	213	219
<i>Of which, fixed transaction fee</i>	557	613	619	571	645	664
Fees on portfolio investment earnings from abroad	2011	2012	2013	2014	2015	2016
Fees on income from equity	83	90	101	120	139	151
<i>Of which transaction fees</i>	19	20	23	27	31	34
<i>Of which exchange rate margins</i>	64	70	79	93	108	117
Fees on income on debt	85	68	65	67	66	62
<i>Of which transaction fees</i>	19	15	15	15	15	14
<i>Of which exchange rate margins</i>	66	53	50	52	51	48
Fees on consumer spend abroad	2011	2012	2013	2014	2015	2016
Total fees	1 036	1 078	1 121	1 154	1 150	1 221
<i>Of which on spending by businesses</i>	152	161	175	164	159	160
<i>Of which on spending by households</i>	883	917	946	991	991	1 061
Credit and charge card purchases abroad	392	422	454	484	498	546
Debit card purchases abroad	236	265	295	325	344	388
Cash withdrawals abroad using credit or debit cards	197	194	190	184	171	169
Cash exchanged in Australia	211	197	181	162	136	117
<i>Of which exchange rate margins</i>	204	191	176	157	132	114
<i>Of which transaction/upfront fees</i>	6	6	5	5	4	4
Trade	2011	2012	2013	2014	2015	2016
Exports by large businesses	631	632	680	699	750	758

<i>Of which exchange rate margins</i>	625	626	674	693	743	752
<i>Of which transaction/upfront fees</i>	6	6	6	6	7	7
Exports by SMEs	121	116	124	147	142	147
<i>Of which exchange rate margins</i>	120	115	123	146	140	146
<i>Of which transaction/upfront fees</i>	1	1	1	1	1	1
Imports	568	595	620	644	668	635
<i>Of which exchange rate margins</i>	562	589	613	637	661	628
<i>Of which transaction/upfront fees</i>	6	7	7	7	7	7
Total	2011	2012	2013	2014	2015	2016
<i>Of which exchange rate margins and fees on using cards abroad</i>	2 624	2 697	2 838	2 938	3 061	3 127
<i>Of which transaction/upfront fees</i>	615	667	676	632	711	731
Total	3 239	3 364	3 514	3 571	3 772	3 858