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Australian banks taking unnecessary risks, says US academic

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Australian banks are taking unnecessary risks by relying on large amounts of debt to fund their business, a leading US academic has warned.

Stanford professor Anat Admati says all large banks, including Australia's big four lenders, do not have enough of their own cash in reserve to draw on during a crisis.

"Banking crises have always happened because banks chose to be more fragile than is good for the economy": Stanford University Professor Anat Admati.

Photo: Paul Jeffers

large. And banking crises have always happened because banks chose to be more fragile than is good for the economy," she told Fairfax Media.

"Fundamentally, they like to live more dangerously."

The financial inquiry, chaired by former Commonwealth Bank boss David Murray, is currently examining the equity levels of Australia's biggest lenders.

It comes amid a global push to make the world's banking system safer.

Mr Murray has signalled it could consider forcing banks to raise more equity to make the system more resilient to future global shocks.

The head of the Australian Prudential Regulation Authority, Wayne Byres, has also called for measures to strengthen the current equity regime.

"Capital ratios are the cornerstone of any analysis of bank financial health, for investors as much as regulators," he told a forum on Wednesday.

"APRA's preference is to find ways to strengthen the current risk-based regime."

Ms Admati, who is in Australia to argue for tougher global banking standards, says regulators need to step in and force banks to reign in their debt levels.

"It's unhealthy for any corporation, including banks, to live on a lot of debt," she says.

"In the case of banks, just because they can, doesn't make it efficient or useful for the rest of the economy."

She says while it's possible for banks to run on large amounts of debt, it creates an unnecessary hazard.

"It's like driving too fast. You burn the engine and you risk an accident.

"You can certainly live like that, but you don't have to."

Australian banks have fended off the suggestion they need meet tougher equity requirements, claiming their current requirements compare well to global standards.

being paid, including depositors," she says.

"The fact is, we don't expect corporations to live on so little equity."

Ms Admati was one of five economists to meet with US President Barack Obama in July for a private lunch.

She is a guest speaker at the University of Melbourne's David Finch lecture series tonight.

"Regulators need to force banks to retain their earnings and to issue more equity so they can keep functioning and be ready for a downturn."