

The Costs of Financial Services Regulation in Australia: The Price of Consuming Regulation?

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Finsia – Melbourne Centre for Financial Studies: Symposium and
Academic Workshop
Consumer Finance, Investment &
Regulatory Issues

19 August 2008

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1. Introduction
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 4. Data
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1. INTRODUCTION

- . Project Team

- . Funding

- . Work in Progress – Stage 1

2. RESEARCH ISSUE

- . Financial services sector regulation around 2000
- . There has been a lot of analysis of the role and benefits of regulation
- . Comparatively little on measuring the costs of these regulatory changes

3. LEGISLATION

- General Insurance Reform Act 2001;
- Corporations Act 2001;
- Financial Services Reform Act 2001;
- Financial Services Reform (Consequential Provisions) Act 2001; and
- Australian Securities and Investments Commission Act 2001.

4. DATA

- . Data on listed companies classified by the ASX as being in the “Financials” sector

- . Listed Management Investments (LMIs) – 63 companies

- . Other Financial Services Firms (OFFs) – Excluding banks – 46 companies

- . Banks – 12 companies

Data for total assets and operating expenses was collected from annual reports

5. METHODOLOGY

The analysis has been conducted using the expense ratio (ER), where:

$$ER = \text{Operating Expenses} / \text{Total Assets}$$

. LMIs are a diverse group of companies.

. Examined - Diversified financials

- Real Estate

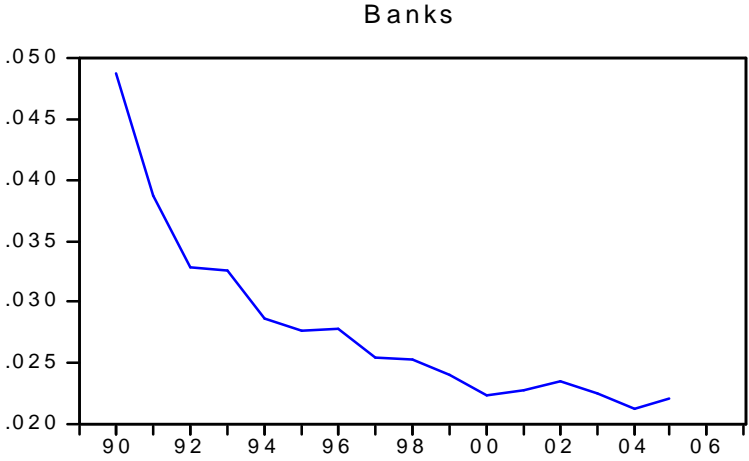
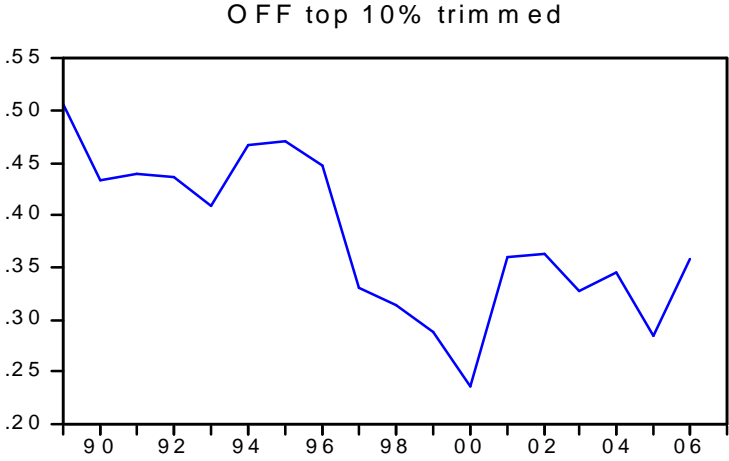
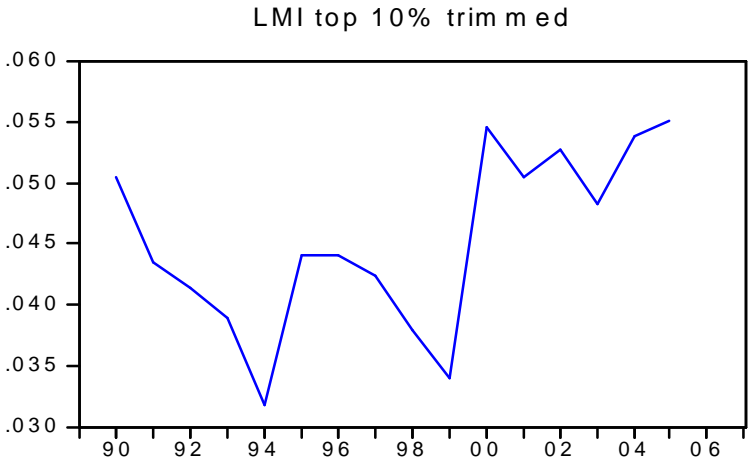
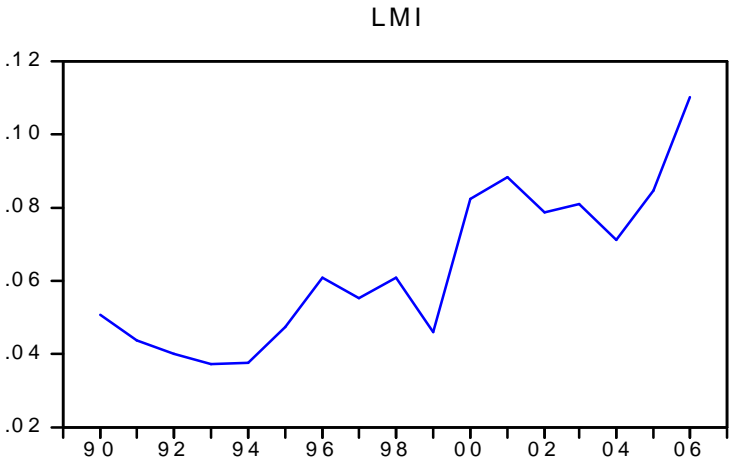
- Other

. Calculated mean ER for each year

Summary statistics for expense ratios

	Listed Management Trusts		Other Financials		Banks
	All - no outlier	10% trimmed	All	10% trimmed	All
Mean	0.067	0.047	0.617	0.364	0.026
Max	0.747	0.385	76.847	2.891	0.090
Min	0.001	0.001	0.002	0.002	0.011
Std Dev	0.118	0.072	3.482	0.430	0.012
JB stat	3627	15365	4374270	1808	737
n	667	603	505	454	168

Mean Expense Ratios



PANEL REGRESSION MODEL

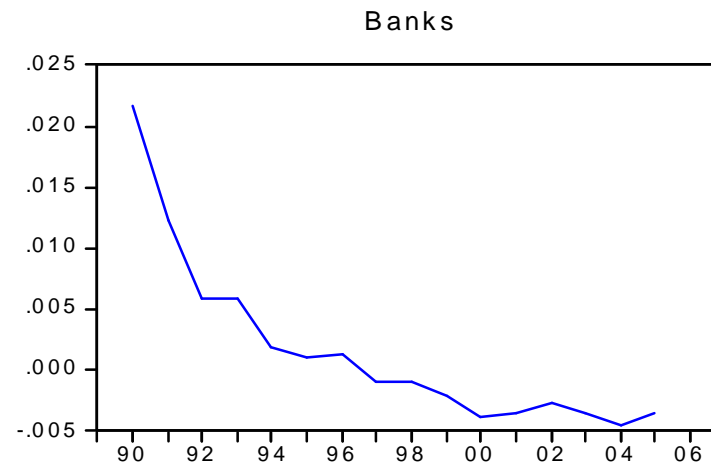
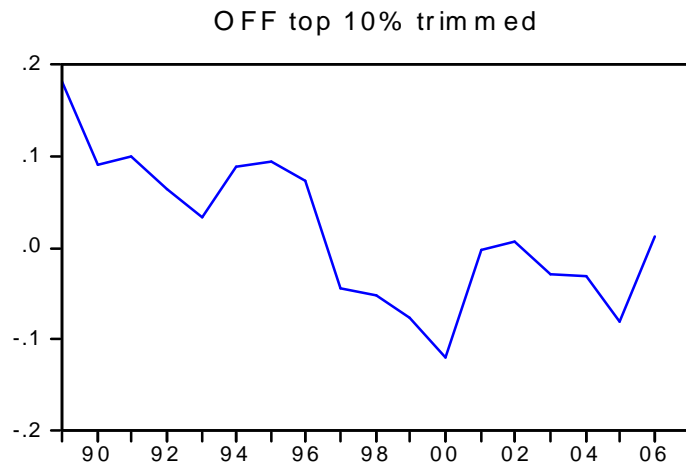
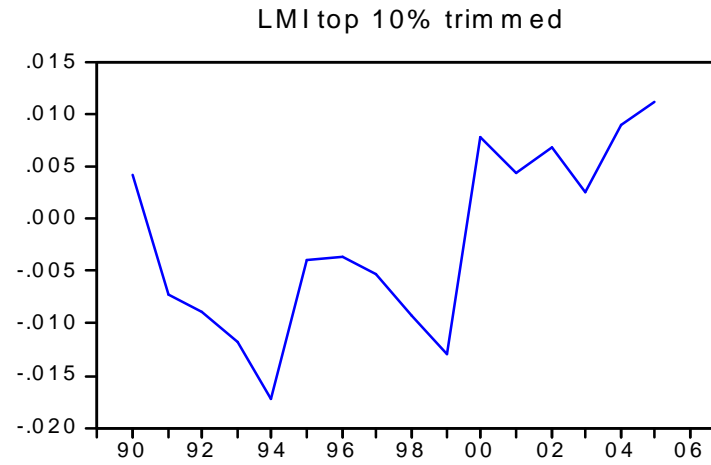
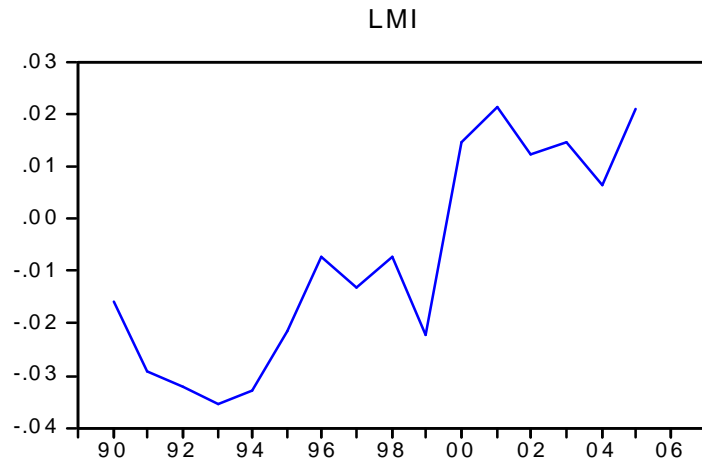
$$ER_{it} = a_0 + a_t + b_1 \log(TA_{it}) + u_{it}$$

- Fixed effects type panel model
 b_1 expected to be negative – economies of scale
 a_t measures year effect – equivalent to adding dummy variables for each year
- Normalised to sum to zero
- ER – expense ratio
- TA – total assets

ESTIMATION RESULTS

	Coefficient	p-value	R ²
LMIs – all firms included			
a_0	0.205	0.0000	
b_1	-0.00729	0.0032	0.0336
LMIs – top 10% trimmed			
a_0	0.142	0.0000	
b_1	-0.00502	0.0014	0.0278
OFFs – top 10% trimmed			
a_0	0.893	0.0000	
b_1	-0.0325	0.0026	0.0466
Banks			
a_0	0.050	0.0000	
b_1	-0.00102	0.0055	0.2336

ANNUAL FIXED EFFECTS – FIRM SIZE REMOVED



COMBINED MODEL

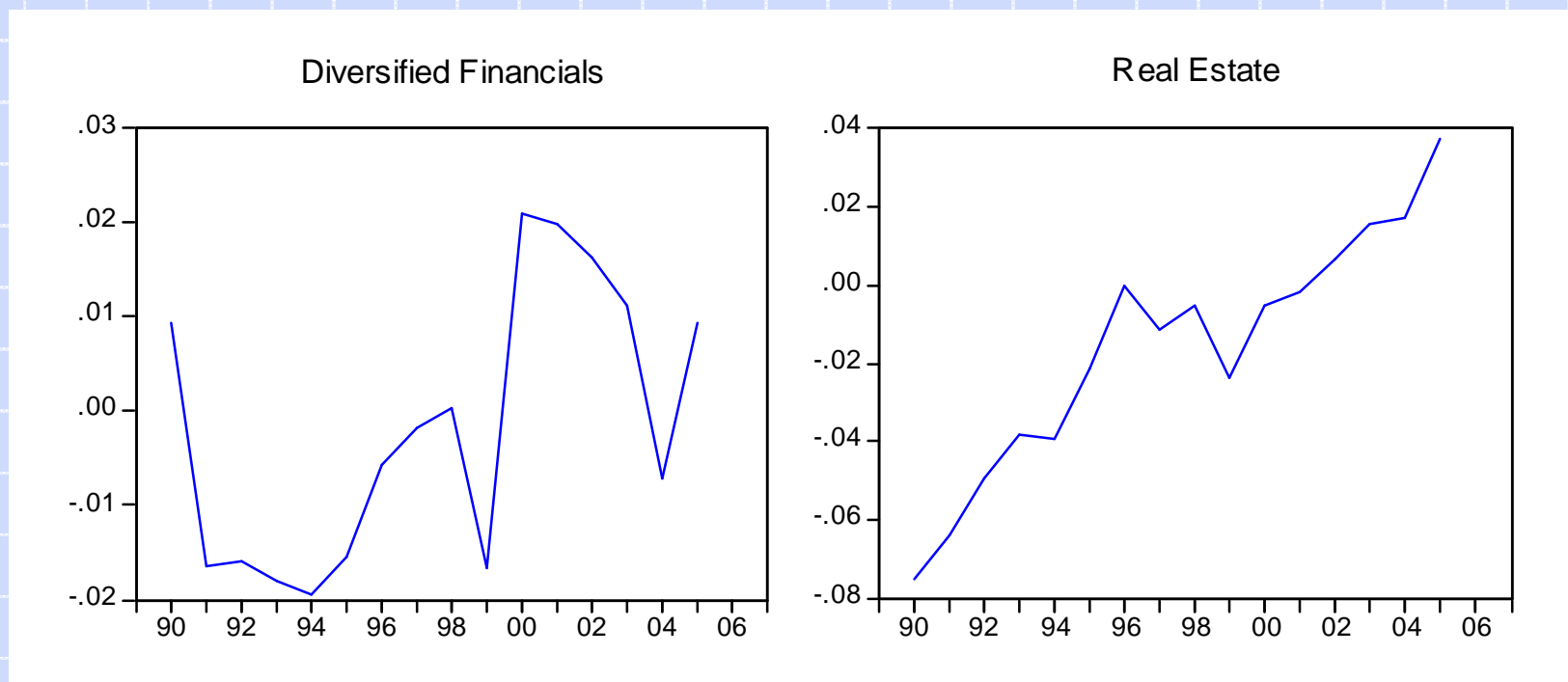
$$ER_{it} = a_0 + a_t + b_1 \log(TA_{it}) + b_2 LMI_i + b_3 Bank_i + b_4 LMI_i \log(TA_{it}) + b_5 Bank_i \log(TA_{it}) + u_{it}$$

- LMI and Bank are dummy variables for firm type
- Results show banks and LMIs have different intercept and slope to OFFs
- LMIs and banks do not have significantly different coefficients, but fixed effects are very different
- Three groups should be treated separately

FURTHER RESULTS

- No relationship found between fixed (annual) effects and annual stock market returns
- LMIs subdivided into “Diversified Financials”, “Real Estate” and “Others”.
- Combined model fitted with dummy variables.
- Significant differences were found between the categories
- Separate models were fitted – but not for “others” as it only had 13 firms

ANNUAL FIXED EFFECTS – FIRM TYPE



6. RESULTS

- . OFFs and LMIs show increases in mean ER in 2000 and 1999 respectively (even after adjusting for firm size)

- . No significant relationship between market returns and any of the fixed effects

- . ER for the banks have declined consistently over the study period

- . Real estate companies – steady increase in the ER over the entire period

- . Using the median asset value of a LMI of \$137m, the identified increase in the ER represent an approximate cost increase of \$4million in a single year for the typical firm (i.e. 3%)

7. FURTHER RESEARCH

- . Analysis of the possible causes of the results highlighted in Stage One.
- . Using the MorningStar database replicate this study to include some 1600 managed investment trusts.