Banks under pressure to raise interest rates independent of RBA hikes

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DETERIORATING funding conditions for Australia's banks will likely prompt rate hikes independent of any RBA move, a senior banker says. Bank of Queensland chief operating officer Ram Kangatharan said tougher funding conditions were putting pressure on banks’ margins. The cost of wholesale borrowing for banks has come under renewed scrutiny after Westpac last week issued new five-year debt at a risk premium higher than some expected, highlighting fresh strains in the market on the back of Europe's debt crisis. Having enjoyed some improvement during the first six months of the year, risk aversion has returned to investors and an improvement in funding costs isn't expected in a hurry, Mr Kangatharan told Dow Jones Newswires in an interview. "On the wholesale side, things are getting tougher," Mr Kangatharan said. Competition for retail deposits remains fierce, with the only growth in this sector solely driven by "hot money" chasing special offers, he said. "Sustainable retail deposit growth is pretty tough in this environment," Mr Kangatharan said. "All of the banks are starting to feel the pinch in terms of deposit margins." The net result of the rising pressures will likely prompt the major banks to raise their own lending rates, irrespective of whether or not the Reserve Bank of Australia moves the official target -- Bank of Queensland is a price taker in the mortgage market. "As the pressure continues on the majors, they would want to move outside the RBA rates, I think what's holding them back is election year," Mr Kangatharan said, referring to a general election expected to be called in coming weeks. The RBA is forecast to hold official rates steady at 4.50 per cent when its policy board gathers tomorrow. Offsetting the volatility is an improvement in the securitisation market where falling risk premiums mean issuance of residential mortgage-backed securities is now viable and one which Bank of Queensland will consider. The highest rated tranche of the most recent RMBS offer in Australia was priced at 105 basis points over swap, around 25 basis points tighter compared with similar offerings earlier this year. "Everything under 150 basis points is viable, it's now closer to 100 basis points, it's definitely viable," Mr Kangatharan said. The regional lender is well ahead of its funding task and is continuing to eye any suitable acquisition opportunities. "It's not a market where you would chase acquisitions, if it comes to you and it's a good deal you can look at it," he said. On the topic of covered bonds, Mr Kangatharan said if they were introduced in Australia, it would alleviate the funding strains on larger banks, possibly opening up the local market to smaller lenders, but will do nothing for competition. "What has been suggested is covered bonds is a panacea for competition - that it is not," he said. Consolidation among regional banks is no longer the hot topic it was during the global financial crisis, though if it happens, fair value will be paid rather than any fire sale value. "We're now in a situation where consolidation opportunities can be evaluated at a true value," Mr Kangatharan said.