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THE GOVERNANCE OF FINANCIAL REGULATORY REFORM: THE AUSTRALIAN EXPERIENCE

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The dominant perspective in the literature linking governance, globalization and public policy argues that globalization undercuts state capacity, weakening a government's ability to effectively regulate its domestic affairs. This paper shows otherwise with special reference to the Australian experience in financial regulation. It challenges the conventional wisdom that the Australian state is weak and cannot adopt anticipatory industrial policies. This paper argues that the adoption of the 'twin peaks' model of financial regulatory arrangements is an example of the existence of government-led steering in Australia which can adopt a proactive approach to financial regulation by steering and coordinating policy networks. 'Governance through hierarchy' in the financial services industry may be a function of the government's political entrepreneurship; its skill in setting and implementing an agenda; and an ability to create new policy communities and networks.

INTRODUCTION

With regard to economic governance in Australia, it is often assumed that purposeful and coordinated steering by the Australian government is unlikely to take place due to the fragmentation both of the state apparatus and business associations as well as the existence of pressure pluralist networks. It would, then, appear reasonable to expect a lack of government steering in the Australian financial services. This paper challenges this conventional wisdom.

In 1998, Australia became the first country in the world to adopt the so-called 'twin peaks' model of regulatory reform. This was based on the radical recommendations of the Wallis Inquiry (FSI 1997), the third major national Inquiry to review the Australian financial system. In particular, Australia's focus on organizationally based financial regulatory arrangements shifted towards functionally based regulation. Two new regulators – prudential (Australian Prudential Regulation Authority, APRA) and disclosure (Australian Securities and Investment Commission, ASIC) – were created. At the same time, the then existing 10 regulators operating at federal, state and territory levels were abolished and the Reserve Bank of Australia (RBA) lost its bank regulation powers.

It is puzzling that this radical decision took place when there was no natural constituency pressuring for a change. In addition, there was no market failure that necessitated a case for government intervention. Furthermore, the then existing multiple financial regulators and the majority of the key regulated firms initially resisted the government's attempt to consolidate the supervisory structure in accordance with the 'twin peaks' model. Indeed, the government's policy preferences were in conflict with those of its regulatory agencies and most of the key private sector actors. Nor was the government's anticipatory response attributable to international pressure for the convergence of financial regulatory policy outcomes towards this model.

If highly fragmented financial regulatory arrangements and conflict within the financial policy community pointed to a weak state capacity in the financial services industry

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during the era of the Wallis commission (1996–97), how did this radical reform take place? This paper is about this puzzle. It provides strong support for 'governance through hierarchy' thesis by providing evidence from one of the most internationalized policy domains – financial regulation. It argues that 'governance through hierarchy' in the Australian financial services industry is a function of policy entrepreneurship which carries and implements new ideas that do not emanate from the policy network, and government's skill of setting and implementing its agenda, rather than the type of a policy network. This paper shows that the adoption of the 'twin peaks' model of financial regulatory arrangements is an example of the existence of a government leadership in Australia which can adopt a proactive approach to financial regulation by steering and coordinating policy networks. The government-led governance process shows that the government has the capacity to create new networks in order to make and implement public policy decisions. As such, the regulatory policy change did not take place because of a financial policy network.

In terms of the theoretical focus, this paper largely adopts a state-centric model of analysis, 'because the state, despite persistent rumours to the contrary, remains the key political actor in society and the predominant expression of collective interests' (Pierre and Peters 2000, p. 25; see also Peters 1997; Peters and Pierre 2006; Bell and Hindmoor 2009). The Australian experience holds important implications on the literature linking governance, globalization and public policy. First, states may have their own interests not necessarily equivalent to, or fused with, the interests of their regulatory bureaucracy or private actors. A policy change can be a function of policy entrepreneurship mobilizing new ideas effectively towards policy and institutional change. One of the major weaknesses of the state capacity framework, an integral part of policy network analysis in the interest intermediation school, is an assumption that equates the state to its formal institutions (that is, the state strength in the financial services industry is a function of bureaucratic centralization and a balance between Treasury and Central Bank). Second, states can create new networks to make, implement or influence public policy decisions while dismantling the old ones. In doing so, states can consolidate their position to follow an anticipatory approach to policy-making in the face of challenges posed by financial globalization. Third, network analysts ignore the role of knowledge or ideas in the financial policy process. The framing of policy problems based on knowledge can be a strong agent for change exogenous to the policy community, especially if it does not emanate from the community itself. Fourth, the coordination and collaboration of the policy entrepreneur, steering bureaucracy, and government may also play a significant role in setting the agenda, consensus building, and policy change. Thus, a policy change is not necessarily a function of the policy network but may be in part a function of this coordination and collaboration which catalyses the change. A policy change may be in part the result of policy entrepreneurship rather than the outcome of structural circumstances. Finally, the key variable affecting financial regulatory outcomes is domestic political economy which still continues to shape the impact and trajectory of financial globalization. As such, there is a continuing divergence of domestic policy outcomes across countries, and thus an enhanced role for domestic political struggles.

This paper is organized as follows. The first section offers a review of the governance with(out) government thesis. The second section examines state capacity in the Australian financial services industry before the radical regulatory reform, with special reference to the policy network framework. The third section discusses governance through hierarchy during the regulatory reform process. The final section summarizes the main argument.

GOVERNANCE, GLOBALIZATION AND PUBLIC POLICY

The dominant perspective in the literature linking governance, globalization and public policy argues that globalization undercuts state capacity, weakening government ability to effectively regulate its domestic affairs (Strange 1994, 1995; Ohmae 1995; Reinicke 1999). The opponents of this view argue that the key variable affecting financial regulatory outcomes is domestic political economy, which still continues to shape the impact and trajectory of financial globalization (Sobel 1994, 1999; Vogel 1994, 1996; Evans 1997; Hirst and Thompson 1999; Weiss 1998, 2003; Drezner 2007).

There are also number of different perspectives and approaches to governance (see Pierre 2000; Flinders 2002). For Rhodes, 'there are at least seven separate uses of governance relevant to the study of Public Administration: corporate governance, the new public management; ''good governance''; international interdependence; socio-cybernetic systems; and the new political economy; and [policy] networks' (Rhodes 2000, p. 55). This paper limits itself to two dominant competing versions of the governance thesis: 'governance without government' – a horizontal self-coordination between key state and societal actors (that is, governance through networks) – versus 'governance with government' (that is, governance through hierarchy) – the steering of societies and economies from the centre by the state.

According to the proponents of the ultra-network thesis, we are in a world of 'governing without government'. In such a world, policy network structures (or institutional arrangements between public and private sectors), characterized by non-hierarchical coordination (that is, governance), are the main forms of mediating public and private interactions. Thus, the argument continues, a movement from 'government' to 'governance' facilitates the emergence of these policy networks where non-state actors have a pivotal role. Here, self-organizing (that is, autonomous and self-governing), inter-organizational policy networks are regarded as alternatives to governance through nation states, both at the national and supranational level (Rhodes 1996, 1997, 2000; Reinicke 1998, 1999). From this governance perspective, as Peters observes, it is assumed that states 'are not particularly good at either directly administering programmes or at providing direction to society' (Peters 1997, p. 55). Furthermore, '[n]etworks resist government steering, develop their own policies and mould their environments. . . . Policy networks make public policy' (Rhodes 2000, pp. 61–2). Not surprisingly, the core argument of the network thesis is that 'policy change generally took place only when the relevant ''policy community'' agreed it was necessary and consensus existed on the direction of change' (Richardson 2000, p. 1006). In particular, in this literature, the roles of non-state actors in politics, rather than the state, are emphasized. States are regarded as passive actors who adapt the best regulatory practices in the face of global challenges, leading to policy convergence (Drezner 2001; Heichel *et al*. 2005). It is held that growing international financial integration leads to a convergence of financial policy outcomes, and hence downplays socio-economic and cultural differences between countries, the importance of domestic political conflict, and the role of states (Busch 2002).

A more balanced version of 'governance through networks' is found in the policy network literature in the interest intermediation school (for reviews, see Thatcher 1998; Borzel 1998). The main argument underlined in this literature is that policy networks affect policy processes and outcomes (Atkinson and Coleman 1989a, b, 1992; Coleman 1996; Daugbjerg 1998; Marsh 1998). In this view, it is the type of policy network, or structures linking public and private actors, which determines whether states have the capacity to take leadership roles in domestic policy-making. This literature holds that in a world of global finance it is the degree of state capacity that has a direct bearing on the type of the financial industrial policy adopted by policy-makers. State 'capacity' refers to the government's ability to formulate, pursue and implement its policies (Coleman 1996; see also Weiss 1998; Skocpol 1985). As state capacity increases, policy-makers have options to choose whether to follow an anticipatory or a reactive approach to policy-making in the financial services industry (Coleman 1996, Ch. 4). Anticipatory policies aim to promote a change in industry and to help industry adjust to emerging challenges posed by competitive pressures via state intervention. Strong states can adopt anticipatory policies by intervening in markets to promote industrial change and to help industry adapt to competitive pressures. Weak states, however, are assumed to adopt reactive policies that are basically responses to political pressure from business. According to Atkinson and Coleman (1989a, p. 61), '[w]hat distinguishes an anticipatory approach from a reactive one is the predisposition on the part of the state to intervene in the industrial organization of the sector . . . [anticipatory policies] aim beyond existing products and organisation'. There is a strong parallel between state-directed policy networks (Atkinson and Coleman 1989a, 1992) and 'governance through hierarchy' (Bell and Hindmoor 2009) since they both recognize the central role of the political-administrative machinery with its formal processes in policy-making. The 'governance through hierarchy' perspective, however, emphasizes the state's more co-operative and less intrusive role in steering networks.

Financial market governance is about 'the regulation of competitive conditions and prudential control' (Moran 2002, p. 258). Following the state capacity framework, the state's strengths and weaknesses in financial market governance is based on: (1) the degree to which ultimate decision-making power is concentrated in the hands of a relatively small number of officials; and (2) the balance between the perspectives of the Central Bank and the Finance Ministry (Coleman 1996, Ch. 4; see also Katzenstein 1978; Zysman 1983).

The 'business interest mobilization' concept is also utilized in order to illustrate to what extent a business community is mobilized to assume a role in the making and implementing of a policy (Atkinson and Coleman 1989a, b, 1992; Coleman 1996). It is assumed that the existence of peak associations provides opportunities for the formation of common interests and for pushing those interests in the policy process (Coleman 1996, p. 65).

The 'state capacity' and 'interest organization' parameters are operationalized to identify the type of policy network dominating an issue area. With regard to the dominant type of policy network in Australia, it is widely accepted that Australian policy networks mostly confirm the pressure pluralist model and the Australian state has a reactive approach to industrial policy. If there is a dominant view that runs through the economic governance literature in Australia, it is that '[i]nstances of strong state coordination or centralization are rare in Australian experience due to fragmentation of the Australian State and business interests which, in turn, facilitate *neither state-led or business-led leadership* for anticipatory, proactive or coherent policymaking' (Bell and Head 1994, p. 60; emphasis added; see also Bell 1994, 2002; Atkinson and Coleman 1989a, p. 60).

STATE CAPACITY IN THE AUSTRALIAN FINANCIAL SERVICES INDUSTRY

Following the policy network framework in the interest intermediation school, the assessment of state capacity to engage in anticipatory or reactive policy-making in the financial services industry requires an analysis of the institutional supervisory structure and the policy preferences of key public and private sector actors.

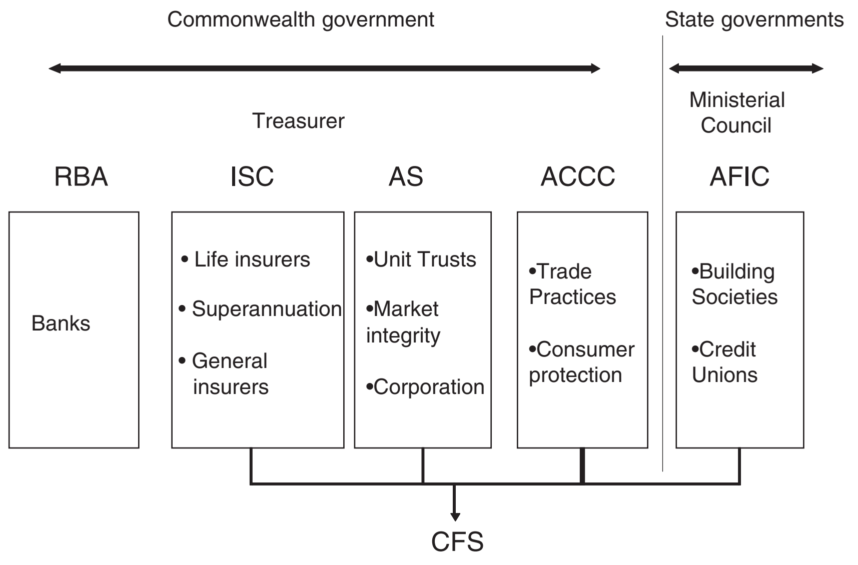

FIGURE 1 *The institutional approach to regulation in Australia: the pre-Wallis framework*
Source: B. Goldsworthy, D. Lewis and G. Shuetrim. 2000. 'APRA and the Financial System Inquiry'. Working Paper, 3. Sydney: Australian Prudential Regulation Authority, p. 2, reproduced with permission.

The institutional supervisory structure

As figure 1 shows, the prudential framework, before regulatory reform, was organization-specific, with separate agencies regulating different types of organizations according to their roles or legal titles. The RBA had responsibility for the prudential supervision of banks. The Insurance and Superannuation Commission (ISC) had responsibility for insurers as well as superannuation funds. The state- and territory-based State Supervisory Authorities (SSAs) were responsible for the day-to-day supervision of building societies, friendly societies and credit unions under the administration of the Australian Financial Institutions Commission (AFIC).

In addition to these prudential supervisory agencies, investor protection was ensured by the Australian Securities Commission (ASC). The Council of Financial Supervisors (CFS) was responsible for coordination of and cooperation among these supervisory agencies. In addition to these financial supervisory agencies and the CFS, the Australian Competition and Consumer Commission (ACCC) was responsible for competition policy.

The RBA, the ASC and the ISC all had responsibilities at the Commonwealth level. These agencies reported to the Treasurer. However, the AFIC operated at the state/territory level and reported to the Ministerial Council of Financial Institutions. This fragmented institutional supervisory structure was largely a product of history, since the constitutional responsibilities for regulation were divided between the Commonwealth and the state supervisory agencies (Thomson and Abbott 2000, pp. 75–6; see also FSI 1997, Ch. 14). Accordingly, there were 11 financial supervisory agencies (that is, RBA, ISC, ASC, and eight SSAs under the umbrella of the AFIC) positioned at the core of the policy network. Apart from these financial services industry supervisors, it should be noted that the Markets Group at the Treasury was charged with advising the government on a framework of legislation and financial supervision (Treasury 2001a, p. 7). Thus, the large number of key bureaucratic agencies operating at federal, state and territory levels might have been expected to lower state capacity due to the difficulties of coordination and consensus building among supervisors.

Policy preferences of the financial policy community

Debate within the financial policy community centred on whether an institution-specific prudential regulation was to be replaced by a function-specific regulation with a new commonwealth prudential supervisor; or whether the existing institution-specific regulation was to be preserved and the RBA involved in bank supervision. Proponents of the former policy option included one of the largest banks, the largest two insurance companies, the Treasury and the Treasurer; all financial regulators and the remaining largest three banks supported the latter option.

Key societal actors include large financial firms rather than their interest associations. For example, each of the four major banks, as the largest financial conglomerates, are among the most powerful private actors in the Australian political economy (Bakir 2004) and they mobilize individually rather than collectively to pressure governments in banking related policy outcomes (Bakir 2005). During the Wallis era, key private sector actors of the policy community included the largest four banks and two insurance companies. These actors had conflicting views over the nature of financial regulatory arrangements. On the one hand, the Australian and New Zealand Banking Group (ANZ 1996, pp. 3–6), the Commonwealth Bank of Australia (CBA 1996, Ch. 5), and the Westpac Banking Corporation (WBC 1996, pp. 4–12), were proponents of the preservation of the organizationally based prudential regulation and of the RBA's supervisory powers. They voiced concerns about safety, soundness and systemic stability. On the other hand, the National Australia Bank (NAB 1996, Ch. 6), the Australian Mutual Provident Society Limited (AMP 1996, p. 10), and the National Mutual Holdings Limited (NM 1996, pp. i–iii, Ch. 6), were broadly in agreement with the supervisory change towards the functionally based regulation and the establishment of a new single prudential supervisor. They emphasized the regulatory burden and arbitrage caused by an institution-specific regulatory regime. They argued that much would be achieved in the supervision of financial conglomerates under the new consolidated regulatory arrangements, including regulatory neutrality, efficacy and efficiency, economies of scale and scope, and flexibility. They proposed that prudential supervision should be function-specific, with a single agency supervising different types of organizations providing similar products and services. It can thus be argued that there was no consensus over the financial supervisory change among the key private sector actors of the financial policy community. In fact it was apparently due to internal division among the largest four banks and insurance companies over the regulatory policy issue that the state's capacity increased.

Key sectoral actors and bureaucratic agencies, according to Atkinson and Coleman, 'form the core of 'policy network' at sectoral level' (Atkinson and Coleman 1989a, p. 47). From this perspective, key bureaucratic agencies refer to industry regulators. However, it may be useful to make a distinction between the two types of key bureaucratic agencies. Following the 'governance through hierarchy' perspective, key public sector actors can be grouped into 'rowing agencies' and 'steering agencies' (Osborne and Gaebler 1992, p. 20). 'Rowing agencies' are responsible for the supervision and/or regulation of a sector whereas 'steering agencies' (both organizations and individuals) are responsible for setting broad policy direction in policy areas (Osborne and Plastrik 1997). In Australia, contrary to the divisions among the key private sector actors, the rowing agencies united against the change in the focus of financial regulation from organizations to functions and the removal of the RBA's banking supervision powers. For example, the RBA (1996, pp. i, v), the ISC (1996, pp. v, viii), the ASC (1996, p. v), and the AFIC (1996, p. 7), did not welcome the proposals for a change to function-specific supervision. In particular, the RBA recognized that its bureaucratic powers in bank regulation would be threatened; the ISC, ASC and AFIC on the other hand realized that their very existence was in jeopardy. Not surprisingly, these regulators, along with ANZ, CB, and WBC, lobbied hard against the prudential shake-up (*Sydney Morning Herald* 8 July 1997).

Although the Treasury department had neither a direct nor ancillary role in the regulation and supervision of financial services firms, it was the main bureaucratic agency pushing for such a supervisory change. The Treasury has a privileged position in the economic bureaucracy due to the following: (1) its traditional function as a financial controller; (2) its combination of neutrality and superior knowledge; (3) its monopoly, being responsibility for the whole of the Australian economy; (4) its relative insulation from sectoral and sectional interests; and (5) its dedication to giving advice based on the public interest (Whitwell 1986, pp. 20–4). During the Wallis era, the Treasury, as a steering agency, demonstrated that it had the skills to diagnose changes in the domestic and global environment (Bakir 2003). Its bureaucratic agenda included a financial regulatory change from organizationally based arrangements towards one that was functionally based with new prudential and disclosure regulators (Treasury 1996, pp. 3, 4, 17, 24). For the Treasury, 'Australia's financial regulatory system needs to be attuned with those of the rest of the world if we are to continue to attract the foreign savings needed to sustain economic growth and Australia's banks are not to be disadvantaged in terms of their capacity to compete in international markets' (Treasury 1996, p. 92). In particular, the regulatory arrangements at the time were becoming increasingly ineffective in dealing with the structural transformation of markets and firms (FSI 1997, Chs 4, 6, 11; Lewis 1997; Harper 1998). The main examples included the increasing growth of financial conglomeration and the blurring of distinctions between firms, sector and products in the financial services industry (FSI 1997). As a member of the Wallis Committee observed, 'there was a sense that the industry was changing in such a way that the old regulatory framework, particularly those focused on industries rather than functions, were constraining the industry in an unhelpful way' (Interview 19 February 2001). In particular, the Treasurer and the Treasury argued that organizationally based regulatory arrangements were creating regulatory burdens and opportunities for regulatory arbitrage among financial firms providing similar services and products. Not surprisingly, trust in regulatory processes and agencies decreased as the then existing arrangements were increasingly becoming obsolete in dealing with market changes. In particular, concerns of safety and soundness heightened as affiliated institutions of financial conglomerates were supervised by different agencies, none of whom had responsibility for consolidated supervision of the whole conglomerate organization. As a senior APRA official noted, 'there was a strong sense that . . . prudential regulator should have a *group-wide risk management system*. . . due to increasing financial conglomeration' (Interview 19 February 2001; emphasis added). Thus, risk and its management were also legitimate regulatory/supervisory concerns at the time. Accordingly, it was assumed that consolidated financial supervision with a functional focus might have greater flexibility in responding to changes in markets. Furthermore, due to its concern about potential unstated liabilities associated with compulsory superannuation, the Treasury wanted more supervision of the superannuation sector (Treasury 2001b).

Unsurprisingly, there was conflict rather than consensus between the 'Treasury block' (the Treasurer and the Treasury) and the supervisors (the RBA in particular) over the financial supervisory change during the policy process. From this one should expect a low state capacity, making it difficult to change the scope and structure of financial regulation and the consolidation of several financial supervisors under two new agencies. The application of the policy network framework in the financial services industry confirmed the conventional wisdom that Australia had a fragmented state apparatus, fragmented business interests, and pressure pluralist networks.

GOVERNANCE THROUGH HIERARCHY IN THE AUSTRALIAN FINANCIAL SERVICES INDUSTRY

Financial globalization poses a threat to national regulatory authorities because it gradually undermines the efficacy of existing national regulations and eventually challenges the state capacity in financial market governance (Reinicke 1995; Braithwaite and Drahos 2000; Drezner 2007). This section will show that the Australian financial regulatory governance reflected the government's anticipatory response to the challenges posed by financial globalization.

The abstract financial regulatory model (that is, the 'twin peaks' model) and its specific solutions were already out there. Michael Taylor, a former officer of the Bank of England, was the first academic to advocate functionally based financial regulation with prudential and disclosure regulators in an article entitled '"Twin Peaks": A Regulatory Structure for the New Century' (Taylor 1995). The 'twin peaks' model, however, was not adopted by the British Treasury (see Westrup 2007, pp. 1104–5). The United Kingdom, like three Scandinavian countries (Norway in 1986, Denmark in 1988, and Sweden in 1991), established a single financial regulator in 1997.

Prime ministers play a pivotal role in the institutional reform of the Australian economy (Goldfinch and 't Hart 2003). Accordingly, no political leadership for financial regulatory reform is complete without a Treasurer (for example, a policy entrepreneur) backed by a prime minister. In terms of Australia, for example, although the then Labor government Treasurer shared the views of the Treasury on the review of the Australian financial regulatory structure before the 1996 federal election, the Labor Prime Minister was not considering such a review (Bakir 2003, p. 517). However, a 'political window' for the 'twin peaks' idea, and a policy entrepreneurship together with a political leadership for the regulatory change was opened following the 1996 federal election. The new Howard government coming to power after 13 years of Australian Labor Party rule following the federal election was keen to achieve financial regulatory reforms in order to proactively address future regulatory challenges. Furthermore, the new Treasurer, Peter Costello, wanted to consolidate his power within markets and politics. Costello, as a 'policy entrepreneur', coupled the Treasury's solutions to problems and to the political process (for a theoretical framework, see Kingdon 1995). As has been documented in detail elsewhere (Bakir 2003), the twin peaks idea had significant influence over the Treasury block and the Wallis Committee members in Australia.

Further, the Australian government's successful use of the Inquiry as a 'venue' to legitimize its intervention in markets, and to generate consensus and cooperation about the policy change, was a significant political entrepreneurship skill, enhancing state capacity.

> The Wallis Committee was 'packed' by the government in accordance with its regulatory policy preferences. Its role was to legitimise the government's policy preferences publicly, and to transfer the 'governmental agenda' into the 'public agenda'. However, this was not a case of the government pressuring for its policy preferences over the financial services industry. In fact, the Inquiry was used as a 'venue' to generate industry and public support for the regulatory changes, and was used to build a network of alliances within and outside the parliament. (Bakir 2003, p. 511)

A government's attempt to implement its own policy preferences requires a sufficiently robust partnership between public and societal actors that the required policy changes can be negotiated and implemented (Coleman and Chiasson 2002, p. 169). This partnership is also known as 'embedded autonomy' (Evans 1995, p. 12) or 'governed interdependence' (Weiss 1998, p. 38). However, in Australia, the 'governed interdependence' may not be enough to achieve successful policy changes. By reason of the difficulties in consensus building inherited in Australia's fragmented state apparatus (Bell and Carr 2002, p. 310), the division of authority between state governments and federal government, and the sharing of this authority by Parliament and the Senate, are regarded as significant factors hindering the state's capacity. Accordingly, in the Australian context, major policy changes may require not only the 'governed interdependence' but also the support of the political parties. This was clearly the case during the Wallis era: the Liberal Howard government did not have the majority to control the Senate and therefore any legislation could be blocked, amended or delayed in the Senate if the opposition were to vote against the government. Thus, the Australian Labor Party support for the regulatory change was significant. The opposition Treasurer, Gareth Evans, welcoming the Wallis mandate on prudential regulation and in Labor's first detailed response to the report in August 1997, said, 'While the current system generally works well, there are *no compelling arguments against moving to a new structure* that will accommodate more naturally the profound changes that are taking place in the financial services market' (*Sydney Morning Herald* 20 August 1997; emphasis added). There is no doubt that the intellectual justification legitimizing the government's network steering by the Inquiry members played a vital role in generating this much-needed political support. Our findings support the view that traditions of Australian governance are 'less depend on political party ideologies, and more on competing conceptions of the different significant problems and the way that they should be addressed' (Wanna and Weller 2003, p. 1).

In sum, in contrast to the predictions based on the policy network thesis in the interest intermediation school, the Australian state acted strongly in the financial services industry. As a Wallis committee member put it, 'the State was a leader, it was an initiator' steering the whole policy process during the Wallis era (Interview 30 May 2001). The prudential framework was consolidated with two new industry regulators. The RBA lost the responsibility for the prudential supervision of banks, while the remaining 10 regulators were abolished.

CONCLUSION

With regard to the first parameter of the state capacity framework, a large rather than a small number of bureaucratic agencies were involved in financial policy-making.

With regard to the second parameter, there was no balance between the supervisory perspectives of the RBA and the Australian Treasury. In fact, there were sharp differences in supervisory preferences between key industry supervisors and those of the Treasury and Treasurer. In addition, a conflict within the financial policy community and a lack of the peak interest organization confirmed the pressure pluralist network prediction that the state could not act proactively. As such, in the financial services industry, the state was not expected to maximize its own political power potential and to adopt anticipatory policies.

Contrary to the predictions of the policy networks framework which, both in theory and practice, pointed to a weak state capacity for financial policy-making, the Australian government adopted an anticipatory rather than a reactive approach to financial supervision. The government set the regulatory policy agenda and controlled the direction of change by pushing its solutions against the policy preferences of some of the private and public sector actors of the day. Moreover, in contrast to the core argument of the network thesis, the financial regulatory policy change took place at a time when the financial policy community did not agree it was necessary; in addition, there was conflict on the direction of the change. The empirical evidence detailed in the sections above have indicated that the then financial supervisors and the three major banks neither agreed to the change that came with the new supervisory and regulatory arrangements nor were they able to stop it. Like turkeys facing Christmas, the supervisory consolidation with its functional focus took place – whether they liked it or not. Accordingly, financial supervisory change did not occur because there was a financial policy community or network. Thus, the change in the financial supervisory arrangements could not be attributed primarily to the behaviour or characteristics of the financial policy community as such. In fact, the Australian state was strong in creating new 'rowing agencies' (that is, APRA and ASIC) to implement its policy preferences.

If 'strong' here refers to government ability to set and implement its own agenda on an issue through steering policy networks, then where does this ability come from? This paper has shown that effective coordination and collaboration among the steering bureaucratic agency (in this case the Treasury), the Treasurer, and the government which were guided by the twin peaks idea, were the key factors behind state-led financial governance in Australia during the Wallis era.

Finally, there is no doubt that the state capacity and policy networks framework provides a useful, systematic means of analysing state strength at sectoral level. Of course, financial policy communities and networks are important, because in a political process actors interact and bargain. Government consultation in policy-making takes place via policy communities and networks. Moreover, policies are implemented through policy communities. However, to analyse state capacity only in terms of formal institutional arrangements between the key regulators and regulated firms leaves out too many other important explanatory factors. The state may have its own interests – not necessarily equivalent to, or fused with, the interests of its regulatory bureaucracy or private actors. Furthermore, the state capabilities to achieve its policy goals through steering networks should not be neglected. As has been shown, the Australian government acted strongly, in spite of the resistance of the then existing regulators operating as a part of a fragmented state apparatus, and the conflict within the financial policy community over the policy change. Perhaps the study of state strength should be directed away from policy network structures and instead towards the role of ideas, policy entrepreneurship and steering bureaucracy as well as a government's political entrepreneurship in steering and, when necessary, creating new networks in policy change processes. The state as an actor external to the policy community/network, and new policy ideas based on the knowledge about functionally based prudential regulations – those were the exogenous shocks at work. Specifically, the twin peaks idea, linked effectively to the policy-aking process by the Treasurer, was a powerful change agent because it did not emanate from the policy community itself. Arguably, such forces were more important as sources of policy change than were policy network characteristics. In addition, notions of state power alone cannot explain the policy change. The role of political entrepreneurship of government, as well as knowledge and ideas, should also be considered in policy analyses. Finally, there is still a continuing divergence of domestic policy outcomes across countries, and thus an enhanced role for governments and domestic political struggles in financial regulation. As this paper has shown, domestic politics and government steering are important in domestic-level regulatory reforms in a world of global finance.

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