MEDIA STATEMENT

28 November 2018

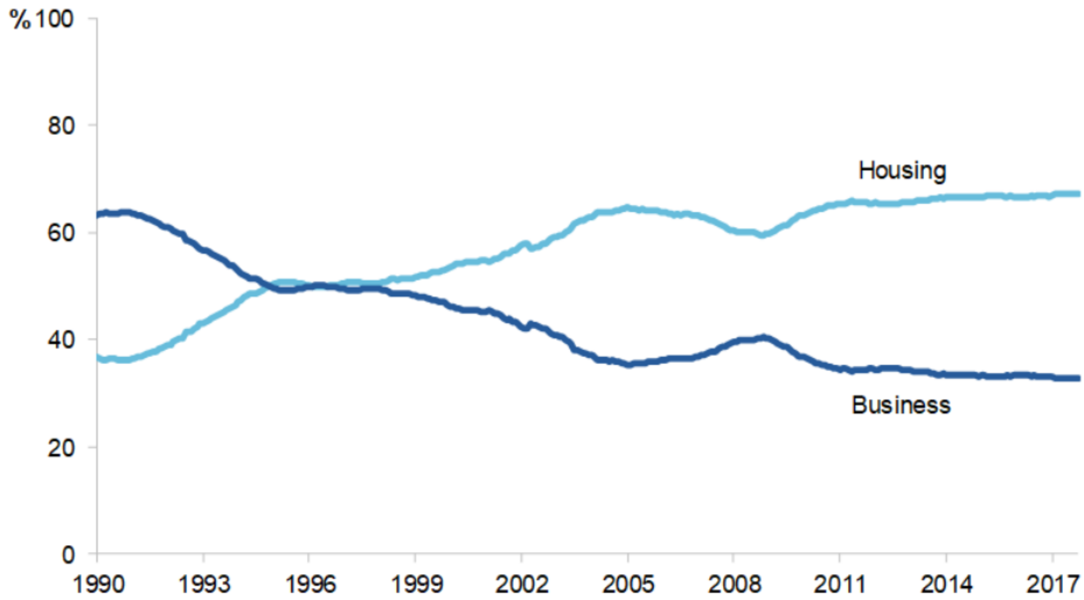
Confusion reigns: Australian Business Securitisation Fund explained

There is much confusion and misinformation in the media on how the $2 billion Australian Business Securitisation Fund will provide a source of wholesale funds for smaller lenders at interest rates comparable to rates available to the major banks and increase competition in the market for lending to small to medium enterprises (SMEs).

The Reserve Bank of Australia has reported that over recent years, competition has been less rigorous for small business lending and the interest rates on small business loans have remained relatively high. The lack of competitive pressure is evident in the share of lending provided to small business by the major banks, over 80%. This compares with a share of two-thirds for large business lending.

As identified in the Productivity Commission's review into competition in the financial system, "The cost of sourcing funds is the single largest expense for all lenders in the Australian financial system. It is, in turn, a key influence on institutions' ability to compete in the market for lending (or to increase profits). With their better credit ratings and a perception of being 'too big to fail', the major banks are able to source funds from investors and depositors at lower interest rates than are smaller institutions."

Figure 16.8 **Business and housing lending, as a share of total lending**



Source: RBA (2017b)

It is recognised that with this higher cost to source funds, the focus of lending has shifted to residential property as it is relatively more profitable. As a result, SMEs are unable to access capital when they need it or, if they can, it will be at a cost that is not sustainable.

Simply put, SME lending is not as profitable for lenders compared to personal loans or lending for residential property. The Productivity Commission concluded that it “is essential to lessen market power and address an imbalance that has emerged in lending between businesses and housing.”

While the exact structure is yet to be finalised, a securitisation product allows lenders to move loans off their balance sheet. A lender can package its performing loans to SMEs, say for a total of $10 million, which the Securitisation Fund will then buy for a cost providing the lender with $10 million of capital. The cost to securitise is expected to be in line with the costs paid by the majors to source their funds from investors and depositors.

To be clear, the Securitisation Fund:

- is not the Business Growth Fund. The Business Growth Fund will have a separate and different purpose – long term equity funding. It will be funded by investors from the private sector, not the government. However, the government will facilitate discussions with potential investors and stakeholders

- will not provide loans directly to Australian SMEs. It offers wholesale funding to smaller lenders at interest rates comparable to those available to the major banks

- will not mean that riskier small businesses will get access to more bank funding. The Fund increases the capital pool available to the smaller lenders; smaller lenders will continue to apply their assessment process before approving a loan.

The Fund aims to boost competition outside the major banks by increasing the supply of affordable capital for smaller lenders to build their pool of capital and provide more lending products to the SME market.

The Fund is the first step in levelling the playing field between our entrenched major banks and smaller lenders that can offer tailored solutions to SME borrowers.

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