



Australian Government  
The Treasury

TSY/AU

# Australian Business Securitisation Fund Review

Consultation paper

December 2021



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# Consultation Process

## Request for feedback and comments

The Government is seeking feedback on the questions outlined in this discussion paper by 4 February 2022. In addition to accepting written submissions, Treasury will engage relevant stakeholders directly for input to this review.

While written submissions may be lodged electronically or by post, electronic lodgement is preferred. For accessibility reasons, please submit responses sent via email in a Word or RTF format. An additional PDF version may also be submitted. All information (including name and address details) contained in submissions will be made available to the public on the Treasury website unless you indicate that you would like all or part of your submission to remain in confidence. Automatically generated confidentiality statements in emails are not sufficient for this purpose. If you would like only part of your submission to remain confidential, please provide this information clearly marked as such in a separate attachment.

Following consultation, Treasury will draft a report for Government consideration based on stakeholder feedback. The Act requires the Minister to table a copy of the report in Parliament within 15 sittings of receiving the report.

Terms of reference for this review can be found at Attachment A.

### Closing date for submissions: 04 February 2022

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# Australian Business Securitisation Fund Review

## Introduction and background

The Australian Business Securitisation Fund Act 2019 (the Act) established the ABSF *“to increase the availability, and reduce the cost, of credit provided to small and medium enterprises (SME) by the Commonwealth investing in debt securities in accordance with this Act”*.

A vibrant SME sector is important to stimulate competition and innovation in Australia’s economy. According to a September 2021 Productivity Commission report: “Outside of the finance, insurance and public services sectors, SMEs employ about two-thirds of workers and generate more than half of Australia’s value added.”

Access to debt finance is often important for SMEs to run their operations and to fund growth, but access can be difficult. Some types of lending to SMEs are well provided by the market, such as lending secured by residential or commercial property, but large gaps exist particularly in the provision of unsecured lending. Moreover, the cost of such lending can be prohibitively high.

The Australian Business Securitisation Fund (ABSF) seeks to address this by investing in securitisation warehouse facilities and term securitisations of SME lenders, with the aim of crowding in investment to the sector, thereby increasing access and lowering the cost of funding available to SME lenders. By lowering cost and increasing access to funding, the ABSF aims to help SME lenders pass these benefits onto SMEs. The ABSF is administered by the Australian Office of Financial Management (AOFM).

In line with the ABSF Act, the Government has made available \$1 billion for ABSF investments. Further instalments of \$500 million will be made available on 1 July 2022 and 1 July 2023.

The ABSF Act requires a review of the Act to be undertaken as soon as practicable two years and five years after commencement of the Act to assess its effectiveness in meeting its objectives.

For much of 2020, ABSF activities were paused because of the impacts of the COVID-19 pandemic and rollout of related economic support measures such as the Structured Finance Support Fund (SFSF). The SFSF is also administered by the AOFM and similarly to the ABSF, was designed to support small bank and nonbank lenders via investments in securitisation structures.

The SFSF has a broader mandate than the ABSF, with SFSF investment open to lenders of all asset types rather than just SME lenders. The purpose of the SFSF was to alleviate securitisation market and funding pressure for nonbank and small bank lenders during the COVID-19 pandemic. The SFSF has not made any new investments since November 2020.

There is considerable symbiosis between the ABSF and SFSF. The work done to implement the ABSF by early 2020 allowed for the efficient establishment of the SFSF at the height of the COVID-19 crisis in March 2020. Meanwhile, the experience gained through SFSF investments in a wide range of asset classes, including securitisation facilities backed by unsecured SME loans, has accelerated the AOFM’s progress towards investing in underserved parts of the SME lending market.

Other economic support measures deployed during the pandemic, such as the Reserve Bank of Australia (RBA)’s Term Funding Facility (TFF) and record low official cash rate, have also worked to reduce lending interest rates across the economy, while the SME Guarantee and SME Recovery Loan schemes have provided direct support to SME lenders and borrowers.

It is likely that these measures have contributed to results which relate to the objectives of the ABSF Act. While this context is important to consider, consistent with the legislative requirements this review's focus is explicitly on the ABSF and its effect on SME lending and the SME securitisation market. The review will not assess any other program.

# Scope and terms of the review

## Access and cost of SME finance

Ideally, SMEs should have access to a wide variety of lending options to suit their heterogeneous needs. However, historically lending has been most available to SMEs which can offer residential or commercial property, or otherwise equipment, as security. Other types of lending to SMEs, such as working capital and unsecured loans, have been less available.

The Australian SME lending market remains dominated by banks. However, banks have been shifting away from the sector over the last two decades, due to the higher capital requirements for SME lending compared with lending to sectors such as residential property<sup>1</sup>. Small bank and nonbank lenders are emerging as larger players in SME lending and can potentially fill gaps in the market.

Isolating the impact of the ABSF on availability and cost of SME finance may be challenging at this early stage of the ABSF's implementation, particularly given the existence of other forces in the lending market.

Lending rates across the Australian economy have decreased since the onset of the COVID-19 pandemic in March 2020, driven primarily by a record low official cash rate and other economic support measures such as the TFF. In recent months, some lending market interest rates have risen, but interest rates generally remain well below pre-pandemic levels<sup>2</sup>. Meanwhile, the comparatively greater risks for SMEs in the operating environment of the COVID-19 pandemic, is a further confounding factor.

However, the ability of ABSF investees to provide SME credit either to a greater extent or at a lower cost than they otherwise would have, could be identifiable. The signalling affect that the ABSF may provide for the SME lending market, attracting more investors and more lenders to the sector, could also have influenced availability and cost of SME credit.

### Questions

1. How has the ability of lenders to provide SME finance improved and to what extent can this be attributed to the ABSF?
2. To what degree has the ABSF influenced SME lending rates?

## Developing the securitisation market

The primary means by which the ABSF is intended to achieve its objectives is by developing the securitisation market for SME lenders. Securitisation represents a cost-efficient means of funding for lenders, which potentially enables them to pass through lower lending rates.

SME assets historically have not been common collateral in the Australian securitisation market but there is some evidence of recent development. In September 2021, Prospa executed the Australian market's first public securitisation backed by unsecured small business loans and lines of credit. Prior

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<sup>1</sup> Productivity Commission, *Small business access to finance: The evolving lending market* research paper, available at: <https://www.pc.gov.au/research/completed/business-finance/business-finance.pdf>

<sup>2</sup> Reserve Bank of Australia, business lending rate statistics spreadsheet F7, available at <https://www.rba.gov.au/statistics/tables/#interest-rates>



to this deal, public transactions with SME exposure had mostly been backed by residential or commercial mortgages to SME customers.

The ABSF participates in private warehouse and term securitisation transactions. Warehouse transactions are a necessary step to SME lenders eventually being able to fund their lending in the public market. SME lenders typically face obstacles such as scale, investor mandate limitations, perceived credit risk, a lack of historical performance necessary to attain credit ratings, and first-mover costs.

ABSF investment is intended to help address some of these issues by crowding in investment to the asset class and proving its creditworthiness through the warehouse transactions in which it invests. The degree to which ABSF investments to date have expanded availability of funding for investees, rather than providing facilities that would have otherwise been provided by other financiers, is one potential measure of the program's impact.

The willingness of third-party financiers to co-invest alongside the ABSF when they otherwise may have been more hesitant to participate in the SME asset class, and importantly their willingness to invest in the asset class absent of ABSF support, is another potential measure.

One barrier to the SME securitisation market's development has been a lack of consistent loan performance reporting. To address this, the AOFM in conjunction with the Australian Securitisation Forum and industry participants, has used the ABSF to encourage the development of standardised data reporting in the SME lending market. A reporting template has been developed and is intended for use in the broader market, rather than just for the purposes of the ABSF.

Standardised reporting is intended to help build data reporting capability and history within the sector, which in turn will assist investors and rating agencies to better assess the creditworthiness of SME lenders. Attaining credit ratings also helps securitisation transactions to meet institutional investor mandates.

Whether the reporting template that has been developed is fit for purpose and broadly adopted by SME lenders will be important in the ABSF achieving its objectives and for the ongoing attractiveness of SME lending as an asset class for institutional investors.

## Questions

3. What effect has the ABSF had on the viability of securitisation funding for SME lenders in terms of cost and assets that can be funded in this way?
4. Has the ABSF had the effect of crowding in third-party investors to the SME securitisation market?
5. What contribution will standardised data reporting make to the development of the SME securitisation market?

## Investment principles and process

To guide its ABSF investments, the AOFM established investment principles under the categories of market impact and risk management.

Market impact principles include sustainable impact, transparency, additionality/additivity and competition. These principles aim to ensure ABSF investments assist demonstrable and sustainable improvement of the SME securitisation market.

Risk management principles comprise institutional quality, lending practices, social responsibility, transaction risk profile and compliance. These principles aim to ensure best practice in terms of credit risk, environmental, social and governance risk, and compliance with the ABSF Act, ABSF rules and ABSF investment mandate.



The AOFM has expressed its intention to use ABSF investment to help fill gaps in the institutional funding market for SME lenders and to sustainably develop the SME securitisation market. Initially the AOFM intended to make measured progress from more established parts of the market, such as secured finance, toward less established parts of the market such as unsecured loans<sup>3</sup>. However, as recorded by *KangaNews*, the AOFM has noted that its SFSF investments in unsecured lending segments necessitate an acceleration of ABSF investment in these parts of the market<sup>4</sup>.

In November 2021, the AOFM announced a change to its approach for receiving investment proposals. Instead of running time-limited investment rounds the AOFM will begin accepting investment proposals at any time. This change is intended to allow the AOFM more flexibility to engage proponents and reduce the burden of preparation on proponents.

## Questions

6. Are the investment principles and process established for the ABSF by the AOFM appropriate to meet the objectives of the ABSF Act and have these been abided by in ABSF investments to date?

## Legislative settings

The ABSF's investment mandate is to invest in authorised debt securities that meet certain requirements. These include investment risk and return parameters, investment strategies and policies and investment decision-making criteria.

The ABSF mandate directions state that investments must have an acceptable but not excessive level of risk and should aim to achieve a return over the medium term that is not lower than the corresponding return on the Bloomberg AusBond Treasury 0-1 Yr Index.

The ABSF must prioritise underdeveloped sectors of the SME securitisation market, encourage participation in the market by the private sector, assist long-term development of the market and promote competition.

ABSF investments must consider the potential effect on other market participants, whether the investment is reasonably required if it is at a rate of return lower than the market rate, whether the investment will affect the ABSF being able to exit the market in the long term and whether it is consistent with all other parts of the ABSF Act and mandate.

## Questions

7. Do the ABSF's legislative settings and mandate remain appropriate for the ABSF to achieve its objectives?

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<sup>3</sup> AOFM ABSF Information Sessions 26 July 2019, available at: <https://www.aofm.gov.au/publications/speeches/absf-info-sessions>

<sup>4</sup> Remarks reported by KangaNews: 'AOFM reviving ABSF with enhanced purpose from stalled 2020', available at: <https://www.kanganews.com/news/12988-aofm-reviving-absf-with-enhanced-purpose-from-stalled-2020>

# Australian Business Securitisation Fund Review: Terms of Reference

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The *Australian Business Securitisation Fund Act 2019* (the Act) established a fund intended to invest in authorised debt securities of lenders to small- and medium-sized enterprises (SMEs). The objects of the Act are to increase availability and reduce cost of credit provided to SMEs.

The Act requires that the Minister cause a review of the operation of the Act to be undertaken as soon as possible after the second and fifth anniversaries of the commencement of the Act. The review must assess the effectiveness of the Act in meeting its objectives. A report of the review must be tabled in each House of Parliament within 15 sitting days of that House after the report is given to the Minister.

To allow for the completion of the two-year review by 25 March 2022, Treasury will report to the Minister on:

- The effectiveness of the ABSF in increasing availability and reducing cost of credit provided to SMEs;
- The impact of the ABSF on the development of the securitisation market for SME lenders;
- Whether the AOFM, as administrator of the ABSF, has adopted an appropriate set of ABSF investment principles to codify its implementation of the investment mandate, and whether it is abiding by these principles; and
- Whether the settings of the ABSF, including investment mandate and credits to the account, remain appropriate.

The review will consider the context of the COVID-19 pandemic and the establishment of pandemic-related economic support measures such as the Structured Finance Support Fund, the Reserve Bank of Australia's Term Funding Facility and the SME Guarantee Scheme and SME Recovery Loan Scheme. However, the review will not provide an assessment of those support measures.