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Committee Secretary
Senate Standing Committee on Economics
Department of the Senate, Parliament House, CANBERRA ACT 2600
By email: [redacted]

Dear Sir/Madam

Inquiry into Australian Business Growth Fund Bill 2019 ("BGF bill") – RBA Letter

I refer to the letter from the Reserve Bank of Australia (***RBA***) to the Senate Committee dated 17 February 2020 (and made available on the website at 6pm yesterday).

In their submission, the RBA lists six (6) studies "*that include analysis of small business financing conditions*". My colleagues & I have reviewed each of those studies overnight. **Not one of the RBA's studies** makes the briefest mention of any data or analysis into SMEs access to equity finance, let alone suggesting a "funding gap" in relation to equity for established SMEs with revenue >$2m -$100 million.

The only reference in any of the listed RBA reports regarding a "*funding gap*" is for start-ups. The Ombudsman has testified that the BGF will not apply to start-ups. And, as the Committee is aware, qualifying criteria is $2m revenue, profitability and 3 years of revenue growth. These criteria rule out start-ups.

If there was an identified funding gap for established SMEs with revenue of $2 million - $100 million, 3 years of revenue growth, and profitability, then why does no RBA report refer to this, especially when one report is referring to a funding gap for start-ups?

The RBA has been asked to make a submission to the Senate Committee and it could not provide one study that it has undertaken that refers to SMEs access to equity finance, let alone analysis that suggests a funding gap for established SMEs. How then, is it plausible, that Treasury and the Ombudsman claim to "*rely heavily upon the advice of the Reserve Bank*", and it "*relies very heavily on the data and input that we've had from the Ombudsman and the Reserve Bank*" when the Reserve Bank cannot produce evidence of any RBA study undertaken in relation to the subject matter and has not produced a recommendation?

The RBA submission is also most telling for what it **does not say**:

- the RBA letter does not say (as the Treasury official and Ombudsman suggested) that RBA has done a "*lot of work on this*" or "*has data*" in relation to SME access to equity finance or there is a "*funding gap*" for SMEs of >$2m-$100m revenue. Hence, despite the RBA stating that it "*has a long-standing interest in the availability of finance for small business*", it is misleading for the Ombudsman to imply that the RBA has done sufficient work that it is authority that can be relied on (such that the Ombudsman or Treasury did not need to do the work).
- It does not quote any RBA studies on the subject that refer to 'funding gaps' for established SMEs.
- The RBA does not purport to have examined the UKBGF and the Ombudsman misrepresented the RBA by responding to a question about what independent analysis had been done by saying *"The*

UK model—both the British growth fund and—the data around both of those funds is on the public record. I would believe that the RBA has had a pretty good look at what the issues are in this space."

- The RBA reports do not provide any analysis or data into SME access to equity finance, let alone the access to equity for SMEs with $2m-$100m revenue, 3 years of revenue growth and profitability
- The RBA reports do not provide any recommendation of a BGF, or any Government fund (remarkable given APRA rule changes allow the BGF to receive $5 billion of concessional equity out of CET1 equity).
- The RBA reports do not make any reference to any investigation of the likely effect of the BGF crowding out private capital.
- The RBA reports do not say that the BGF will increase equity for established SMEs, or provide any analysis or data on the impact on the equity financing market for SME's that do not meet the BGF criteria
- The RBA does not say why the BGF, controlled by profit-seeking (naturally) banks, will choose SMEs that would otherwise would not have received private sector finance
- The RBA does not address the effect of dividing SMEs into two distinct classes; "BGF invested" and "BGF rejects" and whether this will diminish access to equity for SMEs in the "BGF rejects" class
- RBA doesn't answer how it reconciles this "funding gap" assertion with the vast majority of SME IPOs last year (and most, if not all years over the last decade), have <$100m revenue, raising billions in equity investment from the private sector investors

The RBA states that it "obtains information" from its annual Small Business Finance Advisory Panel and its liaison program. The RBA does not state that it has raised the topic of the BGF at these round-tables with SMEs. Even if it had raised the topic of a BGF during these discussions, the sample size (a handful of people) would not constitute a reasonable amount of work to be deemed a study or analysis from which a recommendation could be drawn.

The strongest statement that the RBA can give in relation to the BGF is that "*small businesses also report that the cost of equity financing is high*". This is not market failure. This is simply an efficient market that reflects the risk and liquidity associated with small business.

The above quote from the RBA is broad and without context. The RBA makes no reference to the number of small businesses that have reported this, nor what they deem to be a "*high*" cost of equity finance. "High" is qualitative. Is it relative to larger companies? How can the RBA assess the veracity of this qualitative assessment of "*high*" based on hearsay? Does the RBA allege that these anecdotes are sufficient and compelling evidence that the entire, competitive Australian marketplace is unable to efficiently price the risk?

The RBA's letter refers to a "*suggestion*" from "*its liaison with small business … that there is a funding gap*". However, this 'suggestion' was not even strong enough for the RBA to undertake a formal study of the market or the competitive impact of Government intervention. This is despite having conducted 6 studies during this time that it considered relevant enough to refer to in its letter to the Senate Committee.

The RBA letter illustrates that neither Treasury, the Ombudsman or the RBA have undertaken the work required to identify any issues associated with SME access to equity finance or an SME equity finance funding gap. This exemplifies the failure to undertake the necessary research and analysis to determine if market intervention in the form of a BGF is warranted and if so, what form it should take. If this work has not been done, then it is not possible to determine whether the its investment guidelines are in the public interest, whether the Government should commit $100m of tax-payer funding, or whether it should enable the banks to access $5 billion of concessionary prudential treatment for their investment in the fund.

Most tellingly, there is no suggestion by the RBA in its letter that it believes, or has a reasonable basis for believing, that the current BGF proposal will increase access to equity for SMEs, and not simply cherry-pick SMEs that would have otherwise received finance from the private sector.

Yours sincerely

[redacted]

Ben Bucknell
CEO and co-founder
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