Hi Kathleen,

I refer to the Senate Standing Committee on Economics and its' consideration of the Reserve Bank Amendment (Australian Reconstruction and Development Board) Bill 2013.

As mentioned on our earlier call, EY is a world leading professional services firm and we have a strong interest in the considerations of Government in relation to the agricultural sector, and in particular the debt levels that currently exist. We have given careful consideration to the issue of rural debt, and reflected on the considerable investor appetite we are seeing from the capital markets and why this does not necessarily flow to the sector.

Based on our experiences and insights in this area, we have identified and presented to Government two innovative solutions that could be implemented to support the sector and which would both comprise an alternative and/or a complement to the currently proposed Australian Reconstruction and Development Board. These solutions are outlined in the attached presentation but at a high level comprise:

1) Commercial advisory and capital raising – to assist in attracting new debt and equity capital, to support in the growth, innovation and development of the sector; and
2) Restructuring of agricultural problem loans – to undertake a wholesale restructure of underperforming loans utilising third-party investor capital, rather than the Commonwealth balance sheet, thereby creating a platform for these farmers to remain on the land. This would involve a ~$2bn plus funding vehicle being established to enable the restructure of $4bn to $5bn in distressed farming loans, thereby creating a renewed platform of stability for the sector.

These solutions have been presented in person to Minister Joyce and Minister Truss' offices as well as the Department of Prime Minister and Cabinet, Treasury, the Department of Agriculture and various farming sector industry associations. They have all demonstrated keen interest in our solutions and indicated that they are worthy of further consideration.

We would welcome the opportunity to discuss these initiatives further with the members of the Committee, and look forward to your feedback on the matter.

Best Regards

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EY Capital and Debt Advisory

Capital Raising Alternatives for Agribusiness

March 2015

EY

Building a better working world

The overall funding challenge for farmers

As a result of changing business models within the global banking and investment communities, we have seen a situation emerge where investor capital is directed to "larger investment grade enterprises" in preference to "small business" – impacting smaller family owned farming operators.

This changing landscape has seen some of the following impacts:

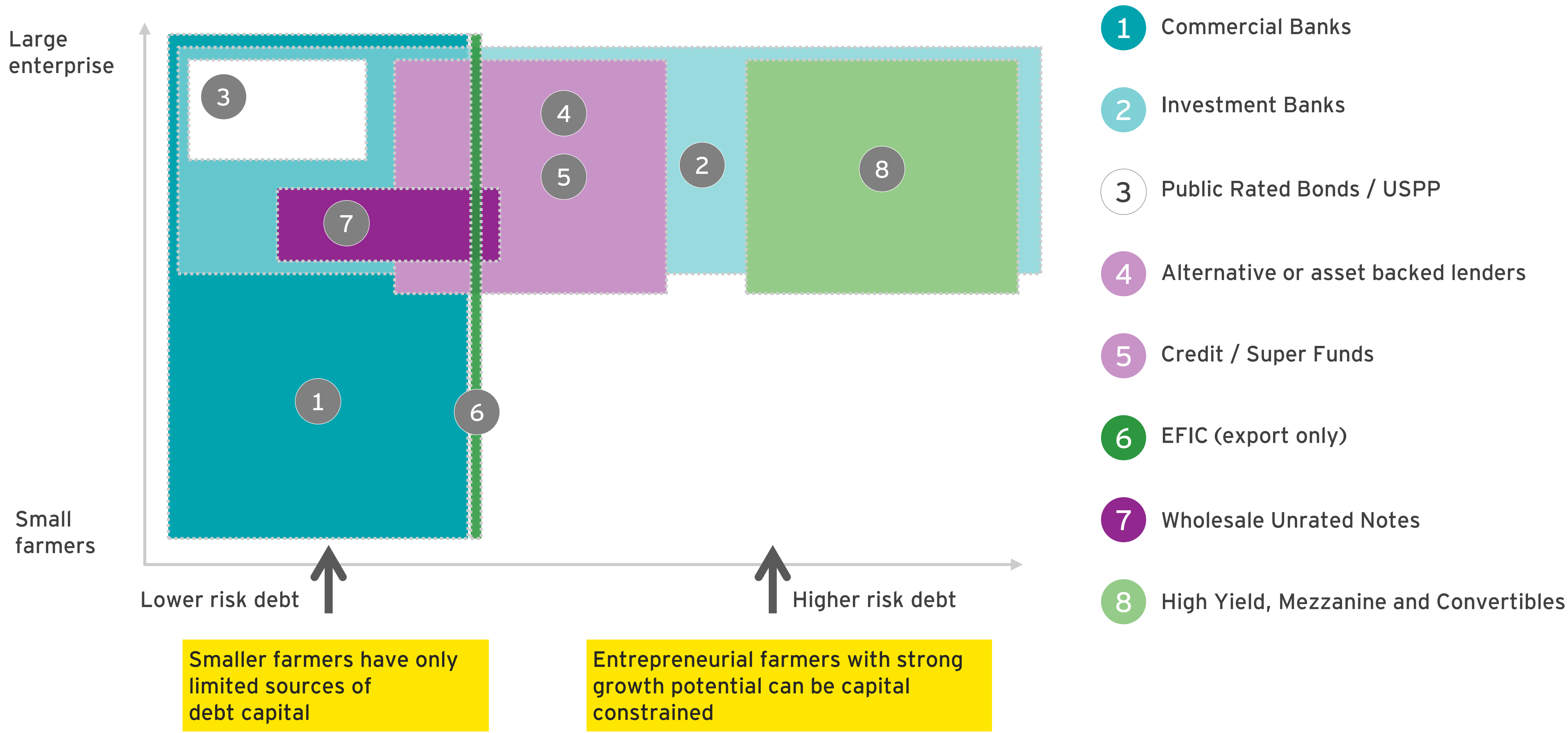
- Reduced debt and equity risk appetite – **"reduced capacity for growth"**
- Less investment of people resource by financiers/investors – **"lower quality of advice"**
- Existing capital solutions are not made available – **"competitive disadvantage is created"**
- Holistic capital restructures are not arranged – **"bank led foreclosures and farmers exiting"**

These are now further exacerbated by the challenges identified within the Australian Government's Agricultural Competitiveness Green Paper, including the impact of drought and lower commodity prices on the level of debt across the sector – now at ~$64bn.

Ultimately this has a wider negative social and economic impact on all rural communities, and can stifle innovation in the sector.

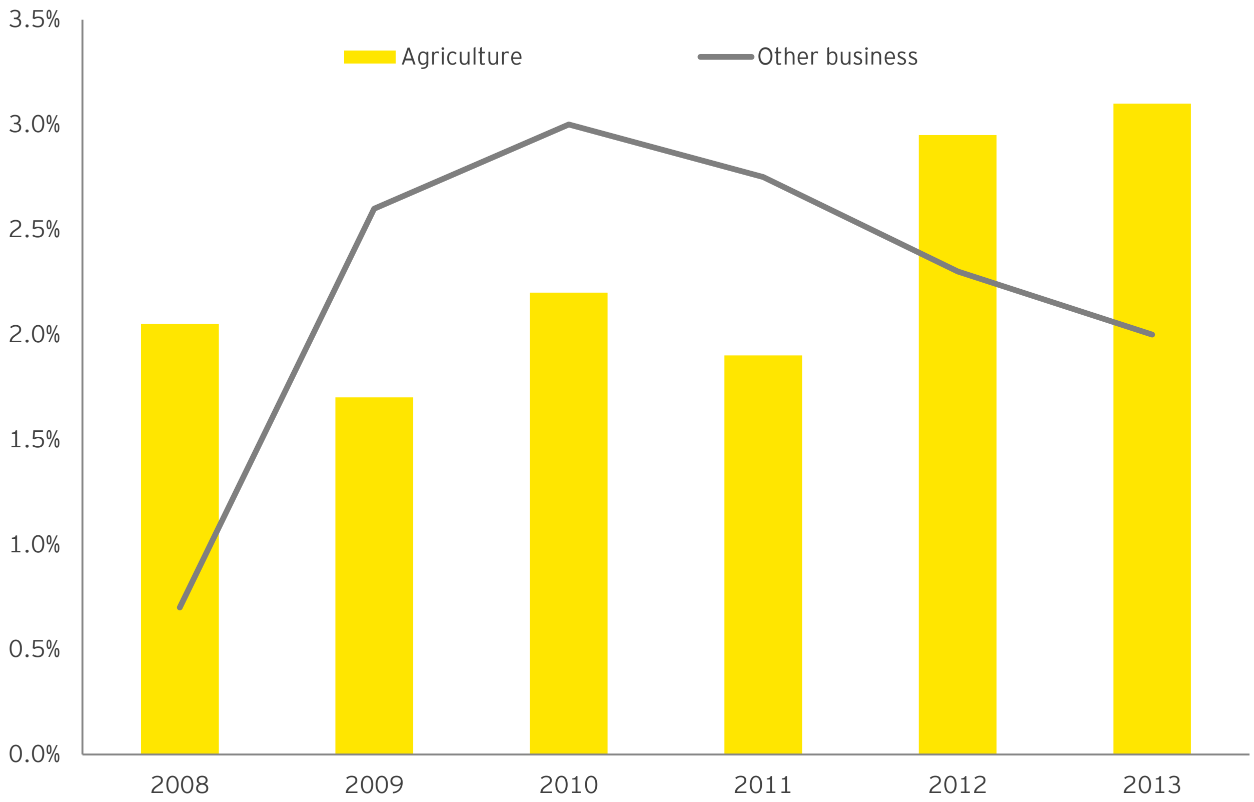
The ‘funding gap’ that has emerged for farmers

The changing lending landscape is reflected in the overall debt market map outlined below:



Now also impacted by arrears and record high problem debt levels

Arrears on Bank Lending (%)



- **i** Arrears for farmers now above GFC levels experienced by the wider business community
- **ii** Farmers have limited capacity to repay debt from cashflows and limited access to other sources of 'capital'
- **iii** Current reliance on asset sales/foreclosures has a negative impact on farmers and the community
- **iv** Post-GFC business arrears took 5 years to remedy even with access to equity capital/asset sales
- **v** Government assistance 'to date' provides short term liquidity not long term capital restructure/solution

"Based on EY market observations, an additional 3% could possibly also be in 'arrears for less than 90 days' or 'in difficulty but meeting commitments', which would then see a total problem debt situation of up to $3.8bn."

Source: ABA submission IP687 as used in the Australian Government's Agricultural Competitiveness Green Paper

Why only "leaving it to the market" won't work

Based on EY's direct involvement in advising lenders and farmers alike in regards to distressed debt, in addition to the successful completion of debt restructures, refinancings, debt sales and debt portfolio sales, we would note that some of the challenges in progressing a solution to date would include:

- **Banks** – are rarely the drivers of the capital solution and expect to see the borrower fix the problem. In addition, in an absolute sense the problem is small in comparison to overall balance sheet size.
- **Farmers** – often lack market knowledge and expertise to resolve the problem, and have limited capacity given high loan to value ratios and limited cash flows (due to drought/commodity prices).
- **Investors** – focussed on larger, more profitable situations that deliver a better return. However, with the right mechanisms/structures in place would have appetite to invest.
- **Government** – limited by desire to not interfere in the market and/or use its balance sheet where the market should find a solution.

As a truly independent advisor and with in-depth understanding of these challenges, EY is uniquely positioned to assist in delivering solutions that can address the needs of all stakeholders involved.

EY Proposed Solutions

Agribusiness support opportunities

In reviewing the government Agricultural Competitiveness Green Paper and considering the challenges in the sector, EY has initially identified two ways the Government can support the sector with a limited use of its own "balance sheet". These initiatives:

- Create systematic change to deal with the Agribusiness distressed debt overhang
- Have the potential to create significant community and economic benefits
- Will need to be further tested with investors to confirm structure/appetite levels
- Are in the context of EY's "Independence" and the ability to find 'middle ground' options

This presentation covers two initiatives that the Government may look to consider:

i	Commercial Advisory and Capital Raising	Helping the sector grow
ii	Restructure of farming problem loans	Fixing the bad debt problem

1) Commercial Advisory and Capital Raising – creating upside/growth opportunities

Existing Capital Markets Flows

Co-operatives

Large private companies

ASX listed companies

- Extensive dialogue and interaction
- Large volumes of capital available
- Well known structures/platforms
- Financial sophistication/knowledge
- Lower risk/better return on investment

Individual Farmers and SMEs

- Limited deal flow/transactions
- Limited dialogue/interaction
- Lower financial sophistication
- Higher risk and lower return

Investor Market

Commercial banks

Investment banks

Super funds

Debt funds

Equity funds

Fund managers

Private equity

Private investors

- Currently the "risk vs reward" investment proposition for investing in farms is not always attractive for debt and equity investors with better returns often available elsewhere
- This is further restricted by the lack of scale from these small investments and the lack of market knowledge held by farmers to create better structures to attract capital

1) Commercial Advisory and Capital Raising – creating upside/growth opportunities

Proposed Government Advisory Support Mechanism

Co-operatives

Large private companies

ASX listed companies

- Extensive dialogue and interaction
- Large volumes of capital available
- Well known structures/platforms
- Financial sophistication/knowledge
- Lower risk/better return on investment

Individual Farmers and SMEs

Commercial Advisory & Capital Raising

A. Provides commercial advice on new markets/solutions
B. Finds structures that are appealing to investors
C. Brings "Institutional" level solutions to smaller enterprises/farmers
D. Creates platform for increased equity investment in the sector
E. Where true gap in funding is present provides credit wrap or funding support

Investor Market

Commercial banks

Investment banks

Super funds

Debt funds

Equity funds

Fund managers

Private equity

Private investors

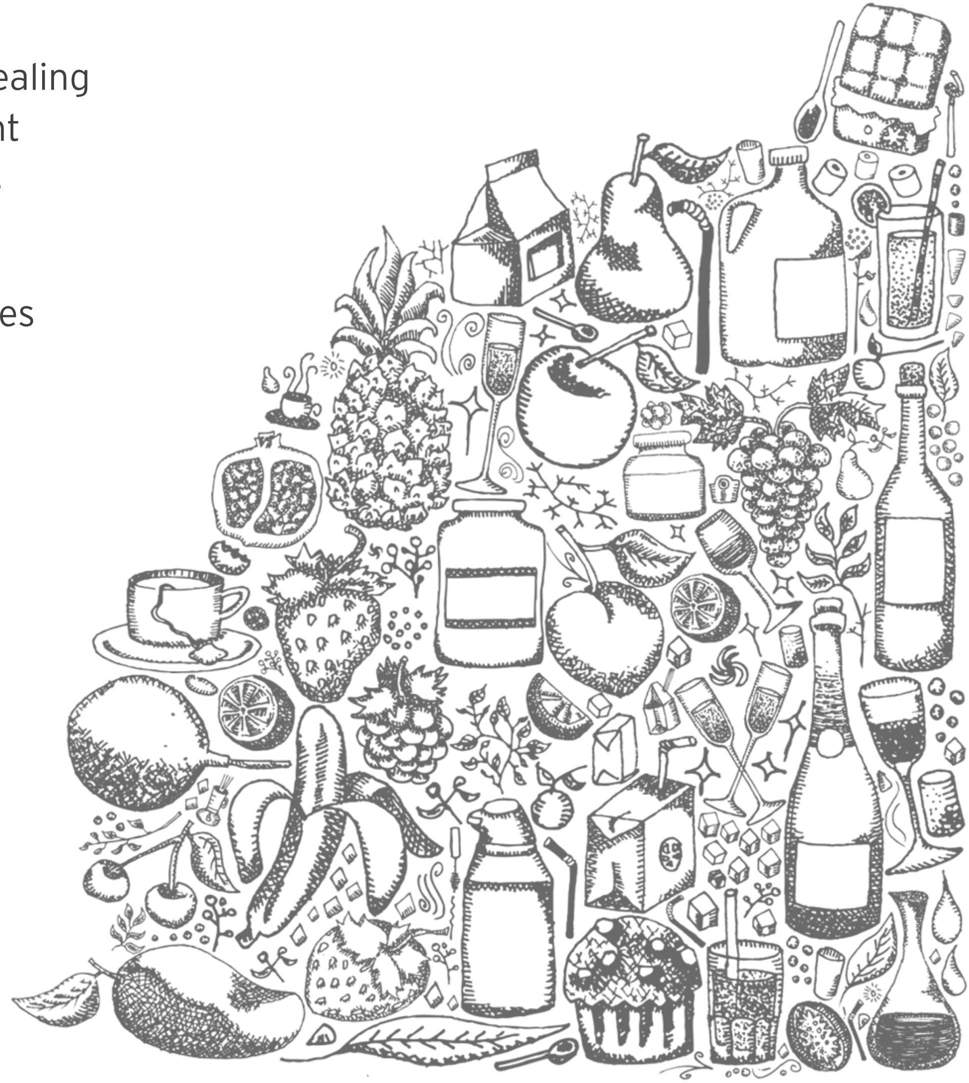
- Government run Commercial Advisory and Capital Raising to focus full-time on finding appropriate new markets, commercial solutions, financing structures, liaise with investors and add a level of needed financial sophistication for farmers

EY

2) Restructure of Farming Problem Loans – fixing the "rural debt" problem

a) What happened post the Global Financial Crisis?

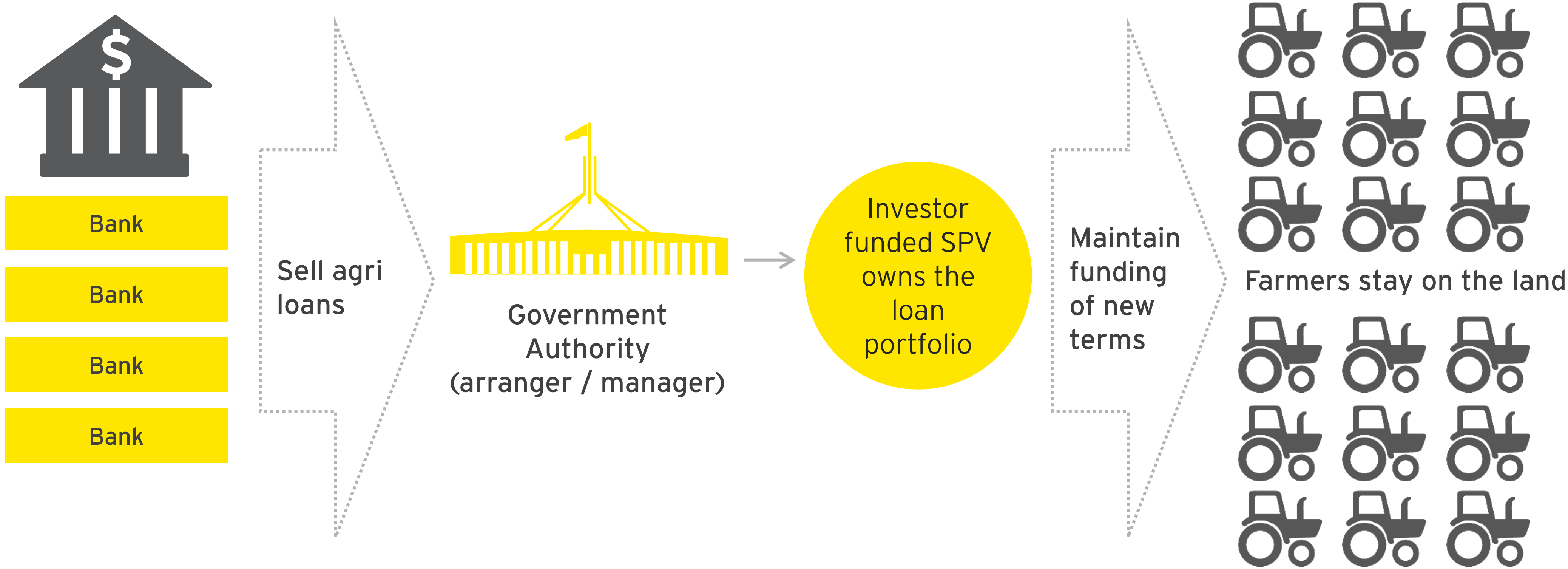
- In an effort to deal with the problem loans on their books, banks undertook considerable portfolio repair activities – in addition to dealing with loans on a stand-alone basis, some banks undertook significant single debt and portfolio sales transactions to the investor markets
- Even the Australian market saw well over $10bn in secondary non-performing and performing loan portfolios and single loan exposures traded/restructured over this period



2) Restructure of Farming Problem Loans – fixing the "rural debt" problem

b) How can this be applied to the farming sector "bad debt" problem?

- EY believes a transaction can be structured and managed on behalf of the Government, that utilises **third party investor capital** (ie not the Government balance sheet) to undertake a permanent restructure/reset of these loans



2) Restructure of Farming Problem Loans – fixing the "rural debt" problem

c) How would it work?

Establish an **investor funded** special purpose vehicle that allows for:

- As an example, a $10m agribusiness loan may be provisioned to $5m by a bank against $6m of assets. By purchasing the loan for $5m and re-lending that amount, this reduces debt in the business and creates $1m of equity in the business

i

An independent assessment of each loan or portfolio purchase

ii

Agrees a debt purchase or restructure amount based on the underlying value (possibly equal to the bank's already provisioned amount)

iii

The authority raised third party external investor capital to fund the program

iv

The authority purchases the loan and extends a new loan to the farmer at the revised amount - this may also be subject to conditions of approval that enhance the commerciality of the farm

v

This provides the farmer with a funding platform to continue on the land

d) What is the potential benefit?

Farmer - would see a permanent reset of the debt and able to stay on the farm

Banks - losses already provisioned and able to exit their positions without public relations stigma

Economy - immediate benefit to rural communities, reset of agricultural land prices and banks release capital to then relend to the sector. Encourage innovation for those good farmers who had previously operated on over-levered farming operations.

Next steps

An investigation and market sounding of investor appetite and suitable structures is needed to fully explore the most optimal solutions that will:

- Meet all stakeholder objectives and raise sufficient capital
- Have a limited cost to Government and no impact to the balance sheet
- Create a platform for improved commerciality of the farming sector
- Moves quickly to limit the current pain being experienced
- Delivers a permanent fix rather than short term liquidity

EY | Assurance | Tax | Transactions | Advisory

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

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