

31 March 2010

Mr John Hawkins
The Secretary
Senate Standing Committee on Economics
PO Box 6100
Parliament House
CANBERRA ACT 2600

Dear Mr Hawkins

SUBMISSION TO SENATE INQUIRY INTO ACCESS OF SMALL BUSINESS TO FINANCE

Commonwealth Bank of Australia (the Bank) welcomes the opportunity to make this submission to the Senate Standing Committee on Economics Inquiry into Access of Small Business to Finance.

This submission highlights how the Bank has been and continues to be committed to supporting the small business community to ensure sustainable business growth in the current economic environment.

The Commonwealth Bank also fully supports the Australian Bankers' Association's (ABA) submission covering in detail the Inquiry's Terms of Reference.

Business Banking is a key priority for the Bank

The Commonwealth Bank is one of Australia's leading providers of integrated financial services including retail, business and institutional banking, funds management, superannuation, insurance, investment and broking services. The Bank has over 130,000 small business customers and is a major provider of small business loans with over \$25.9 billion outstanding in loans and asset finance facilities.¹ The Bank has over 60 business banking centres across Australia providing our customers with the full range of financing, working capital, transactional and merchant solutions.

Since 2006, the Bank has identified business banking as one of its five key strategic priorities and it is the only priority that is specific to a line of business –

¹ As at 31 December 2009. Small business loans are defined consistently with the APRA monthly reporting (i.e. client loan balances less than \$2 million). Asset finance includes asset finance provided to small businesses in our Local Business Banking and Regional & Agribusiness segments.

the remaining four priorities reflect improving excellence in service areas across the Bank.²

To attract new clients and deepen our relationship with existing clients, the Bank has invested significantly in business banking by:

- opening 20 more business banking centres;
- placing more than 180 business bankers in local branches;
- embarking on a dedicated national decentralisation strategy to improve client access to business banking centres;
- providing businesses with 24 hour/7 day access to business bankers, who are located Australia-wide, through a market leading telephony platform;
- investing in our CommBiz and NetBank online channels;
- continuing to innovate payment technology to ensure that small businesses have convenient payment options for their customers; and
- protecting small businesses by investing in systems and processes to both prevent and detect fraud in the cards payments industry

We wish to make it clear to the Inquiry that the Bank is intent on serving the small business market as a strategic priority and we see alignment between the Bank's interests and the interests of small businesses. The discussion below demonstrates how the Bank has met and continues to meet this priority.

CBA is open for business for small businesses

There is a misconception that banks have stopped lending to small sized enterprises.

The Commonwealth Bank has lent, and continues to lend, to credit-worthy small businesses.

New business lending remains strong with the Commonwealth Bank advancing \$8.2 billion in 2009 to small sized businesses.³

The Bank increased its total outstanding loan balances to small business customers by 8.6 per cent from July 2008 to December 2009. This compares to the relatively flat growth of 0.3 per cent in total small business lending over the same period.⁴

² The other strategic priorities include: Customer service; Technology and operational excellence; Trust and team spirit and Profitable growth. Further information about each of these strategies can be found at <http://www.commbank.com.au/about-us/>

³ This includes business loans and asset finance facilities. Small business loans are defined consistent with Reserve Bank of Australia (RBA) and Australian Prudential Regulation Authority (APRA) monthly reporting (i.e. client loan balances less than \$2 million). Asset finance includes asset finance provided to small businesses in our Local Business Banking and Regional & Agribusiness segments.

⁴ RBA and APRA lending to business data for loans less than \$2 million.

The Bank also saw increased demand for asset financing as a result of the Federal Government's Investment Allowance⁵, complemented with the Bank reducing its standard asset finance rates (by up to 1 per cent) for small business customers. Over the year to January 2010, the Bank increased the total asset finance it provided to small businesses and agribusiness by 9.9 per cent. This compares with the asset financing market contracting by 1.1 per cent over the same period.⁶

This expansion in business lending is against a backdrop of some businesses deferring plans for further investment and/or expansion in the current environment, resulting in reduced demand for lending. This is evidenced by a significant fall in small and medium business confidence measured, for example, in the *Sensis Survey*.

Importantly, the Commonwealth Bank has not made any material changes to its lending policies for small businesses since the financial crisis commenced. Nor has the Bank undertaken unilateral risk re-rating of profitable businesses.

As part of our strategic imperative, the Bank made a commitment to not cap lending to small business. Our business lending approval rates remain around 93 per cent to 95 per cent of applications received throughout 2009 and continue at these levels in 2010. That is, our approval rates for loan applications have not changed before, during and after the financial crisis. This is despite other competitors exiting or scaling back their lending to the small business market.

We continue to lend to viable small businesses.

Along with our business banking priority, the Bank's highest priority is to ensure that our customers experience excellent service during their interaction with us. We continue to serve our customers better and we want to be the financial services organisation chosen by customers because of our outstanding service.

We price for sustainable growth

The strength in the Bank's lending to small businesses and commitment to this sector can be demonstrated by the Bank reducing small business interest rates more than any other major bank.

The Bank's residentially secured business loan reference rate – a product that is the most closely comparable to the retail home lending product – is currently at 7.36 per cent.⁷ This reference rate has been the most competitive rate among the big four banks for over a year with the Bank actively advertising this rate

⁵ The Federal Government's Investment Allowance provided businesses with an additional tax rate deduction with the rate depending on the turnover of the entity.

⁶ Australian Equipment Lessors Association (AELA) Asset Finance Net Receivables.

⁷ As at 26 March 2010

within the community in national and metropolitan newspapers (see attachment for our latest advertisement). Since the Reserve Bank of Australia's cash rate peaked in July 2008, the Commonwealth Bank reduced its residentially secured business reference rate by 2.53 per cent. Over the same period, comparative rates by other major banks have reduced by less than 2.10 per cent.

Small business customers have benefited from the Bank's interest rate decisions as the Bank has limited any increase in the cost of funds to small businesses. This is despite the Bank facing continual pressure on its cost of funds since the credit crisis commenced. The three sources of funding (deposits, short-term funding, and long-term funding) have all contributed to this pressure. For example, over the last 18 months the Bank's pricing for deposits for small business has increased from 32 per cent being priced above the Bank Bill Swap (BBSW) rate to 65 per cent being priced above BBSW rate. The increased cost of funding is well documented in a recent article by the Reserve Bank of Australia.⁸

It is commonly, but incorrectly assumed that the residentially secured business rate should equate to the standard variable rate for mortgages. At the Commonwealth Bank, the residentially secured business rate is 0.5 per cent above the standard variable home loan rate. This differential is 0.3 per cent lower than the average differential of around 0.8 per cent cited in the Reserve Bank's submission.⁹

The difference between the residentially secured business rate and the standard variable mortgage rate is due to the risk profile of small business customers and the cost of this additional risk as determined by quantitative models utilising data over an extended period to reflect changing business cycles. The risk profile takes into account the possibility that the loan may not be repaid by the client (probability of default). History has shown that small business loans, even those backed by a residential security, have a higher probability of default compared with a retail home loan customer. A higher risk margin is therefore required to cover this increased risk.

In addition, the Bank also reduced a number of its business banking fees for transaction accounts in October 2009 including its overdrawing approval fee (from \$30 to \$10) and dishonour fees (from \$35 to \$5).

We support small businesses in many ways

In the midst of the financial crisis, the Bank launched a range of initiatives to further support small businesses. These initiatives included the business 'health

⁸ A. Brown, M. Davies, D. Fabbro and T. Hanrick, *Recent Developments in Banks' Funding Costs and Lending Rates*, Bulletin, March quarter 2010.

⁹ Reserve Bank of Australia, *Submission to the Inquiry into Access of Small Business to Finance*, March 2010.

check', the Small Business Investment Package, asset financing stimulus and risk management solutions.

Our small business clients were encouraged to approach the Bank for a tailored discussion on their financial situation and goals. The Bank's business 'health check' was an opportunity for the Bank to help our clients uncover ways for them to effectively manage all of their financial issues and to ensure that their businesses were 'fighting fit' for the financial year.

The Commonwealth Bank also introduced the Small Business Investment Package in March 2009 to support small business growth. The Package included:

- **Rate cuts** to our Residentially Secured Business Loans by 0.25 percentage points for all customers.
- **Small business forums** held in April/May 2009 when business confidence was very low. The forums were held in 17 locations across the country to help small business understand how to present their business to obtain funding. Over 1,500 small business customers attended these forums and were led by Peter Switzer and Tim Pethick. There was no cost to the Bank's customers attending the forums. We are hosting these forums again over the next two months.
- **Special Training Rate** for small business customers who invested in recruitment and training (a 1 percentage point reduction on our Better Business Loan Benchmark Rate and a 0.25 percentage point reduction in the Residential Equity Rate).
- The **Business Banking Support Line** (13 26 07) was established to assist business customers that were experiencing financial difficulties. A dedicated team of business banking support specialists was established Australia-wide to assist these clients with their needs. The number of the Bank's clients who sought financial hardship assistance since its commencement in April 2009 remains less than five clients per week which comprises a significantly small proportion of the Bank's 130,000 small business customers
- **Discounted Investment Spend Interest Rate:** as discussed above, the Bank introduced a reduction of up to 1 per cent on standard asset finance rates for small business customers looking to take advantage of the Government's Investment Allowance.

In addition, the Bank focused on risk management solutions to ensure that small business customers, particularly regional agribusiness clients, were prepared for commodity, foreign exchange and interest rate risks.

The Bank was also supportive of the Victorian Government's initiative to support small businesses affected by the Victorian bushfires, including cash grants and repayment holidays to business loan customers whose business premises had been partly or completely destroyed.

The Bank has also supported small business customers who have recently faced natural disasters (including storms and flooding in New South Wales, Queensland and Western Australia). The Bank's special assistance package has been activated a number of times in the past year with key features of the package including:

- providing additional loans or changes to repayment arrangements for Commonwealth Bank home loan customers who may experience difficulties because of the flooding,
- loan restructuring for business customers with existing loans, without incurring the usual bank establishment fees,
- review credit card instalments for customers of good standing and consideration of requests for emergency credit limit increases,
- expediting claims to *CommInsure* for customers seeking help through their home, contents and motor vehicle insurance,
- waiving prepayment charges over the next month for affected customers wishing to access term deposits, Commonwealth Investment Bonds and CBFC debentures ahead of the maturity date,
- waiving branch service fees where the customer is looking to obtain a service from the Bank as a result of the disaster.

Each of these initiatives has been effective in ensuring that our small business customers received practical and accessible banking advice during uncertain times.

The future for viable small businesses

Our funding costs continue to increase and we expect it to be relatively higher over the next 18 months as less expensive funding acquired several years ago is replaced with more expensive credit priced in today's terms. Further, intense competition for small business deposits means that deposit rates offered to our customers continue to be higher than in the past. We are also seeing strong competition in lending markets and expect this to continue.

Despite these funding and competitive pressures, the Commonwealth Bank remains optimistic about the future for viable small businesses. The Commonwealth Bank expects that lending to viable small businesses to grow at similar levels in 2010. One of our key priorities is to ensure that customers experience excellent service during their interaction with us and we are determined to serve our customers better.

By continuing to look after the needs of all of our customers and be rated amongst the most solid banks in the world, the Commonwealth Bank continues to offer a strong and viable banking solution for small business customers. We wish to make it clear to the Inquiry that the Commonwealth Bank is intent on serving the small business market as a strategic priority.

Thank you for seeking the Bank's views on this occasion. If there is any further material that may be of assistance to the Inquiry, please contact John McLenaghan, Head of Government & Industry Affairs, on (02) 9118 7686.

Yours sincerely

A handwritten signature in black ink, appearing to be 'Ian Narev', with a stylized, flowing script.

Ian Narev
Group Executive
Business and Private Banking

Still the best business loan rate of all major banks. Period.

The Commonwealth Bank beats all the major banks on residentially secured business lending rates. Our variable rate of 7.36% p.a. is simply the lowest. The other major banks' rates just don't compare.

Bank	Residentially Secured Business Loan Reference Rate % p.a.
Commonwealth Bank	7.36
Westpac	7.66
NAB	8.18
ANZ	8.12

Talk to your Relationship Manager, call
13 1098 or visit commbank.com.au/businessloan



Determined to be different.

Important information: Commonwealth Bank interest rate is linked to the Bank's Residential Equity Rate. Our variable interest margin may apply. Based on a comparison of the four major banks' advertised rates for residentially secured business loans as at 30/06/10 excluding their other brands and subsidiaries. Applications for finance are subject to the Bank's normal credit approval. Full terms and conditions are included in the Loan Offer. Bank fees and charges are payable. Commonwealth Bank of Australia ABN 40 125 125 124. commbank.com.au