Division/Agency: Australian Securities and Investment Commission
Question No: 013
Committee Member: Mr Andrew Wallace MP

Question:

CHAIR: I want to change the tone of little bit and talk about Greensill and supply chain financing. Mr Shipton, if you wouldn't mind, please, I would like you to give us an explanation of how traditional factoring works in the first instance.

Mr Shipton: I'm going to hand to my colleague Karen Chester who's on top of this item.

Ms Chester: What I might do, Chair, is take you through the Greensill business model. As I do, I'll try to make clear the distinction between what you might refer to as traditional—

CHAIR: And reverse.

Ms Chester: SCF and what's a little bit different.

CHAIR: While you're doing that, please give us the traditional factoring as opposed to reverse factoring.
Ms Chester: Traditional factoring is where an entity provides a payment arrangement, which sometimes can become a credit arrangement, where they take the invoices from an underlying entity and pay them earlier for a fee, and then they have the ownership of the asset of that invoice. That's the traditional model in a very short nutshell.

CHAIR: What's the usual spread of that fee?

Ms Chester: I don't know what that is off the top of my head. I'd need to take that on notice.

CHAIR: I know every business model would be different, but do you have any idea whether it's 10 per cent, 20 per cent, 30 per cent?

Ms Chester: I think there'd be several drivers to that fee, and that gets to where I think you're going with respect to the spectrum of business models that emerged here around SCF. So if it's purely a time payment management issue then it would be the risk-free rate plus a percentage point based on the underlying risk that they would see attached to the invoice—that is, the underlying business—and whether they've a got diversified portfolio of those invoices. That's the traditional end of the spectrum. You can have another end of the spectrum where you have what we call higher risk businesses for whom you've taken the invoices and you're paying the amounts upfront—that's probably a little more in terms of the Greensill model—and you don't a very diversified portfolio; you've got large licks of exposure to large invoices not from a large number of underlying entities and businesses so much so that you might then look at insuring against the risk. You can imagine that you've got fees at this end of the spectrum and then you've got fees at that end of the spectrum. Where you are driving the fees is really the underlying risk and what you've done to mitigate that risk. Here there was a whole perimeter of insurance and reinsurance arrangements around the SCF arrangements for Greensill, which obviously would have resulted in much higher fees, plus you've then got a situation of where that was securitised and put into funds. So you can see what was a traditional time management, cash management arrangement for businesses—

CHAIR: Cash flow, yes.

Answer:

ASIC does not collect data on the factoring and supply chain finance sector, including the range of usual fees supply chain providers charge to suppliers and buyers. We are also not aware of any other Australian data sources that fully assess the costs of the supply chain financing solutions for both the suppliers and buyers of goods and services.

We however understand that the fees charged to customers will vary, depending on factors such as the:

- credit risk of the borrower as assessed by the supply chain finance provider (essentially, the borrower does not pay back the debt)—this can be a complex assessment based on a variety of factors, including: the individual characteristics of the company taking on the debt, the type of the debt, whether the debt is secured by assets of the borrower, and the concentration of the supply chain financer's portfolio to the borrower,
- length of payment terms—the longer the time that the buyer has to pay the invoice, the cost will be higher, and
- the margin that the provider charges to cover its expenses (which could include passing on some of the costs of the insurance to the borrowers) and profits.

The Supply Chain Finance Review – Final Report (March 2020) conducted by the Australian Small Business and Family Enterprise Ombudsman outlines some indicative cost ranges for a variety of funding sources for small businesses, from data provided by Greensill in their submission to its position paper.[1] An extract of the table is below.

Small Business Finance Options	
Finance type	**Cost ***
Overdraft	6.5% - 9%
Business credit card	13% - 14%
Factoring	12% - 30%
Term Debt	7% - 36%
Supply-Chain Finance	2% - 7%

* Cost is based on $1 million of finance, unsecured, and expressed as an APR (annual percentage rate).

Source: Bank and comparison websites

[1] See page 11 of the report available at https://www.asbfeo.gov.au/sites/default/files/Final%20Report%202.pdf