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JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

Reference: Access for small and medium business to finance

FRIDAY, 4 MARCH 2011

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JOINT STATUTORY COMMITTEE

ON CORPORATIONS AND FINANCIAL SERVICES

Friday, 4 March 2011

Members: Mr Ripoll *(Chair)*, Senator Boyce *(Deputy Chair)*, Senators Cormann, Hurley and Stephens and Mr Fletcher, Mr Griffin, Mr Anthony Smith and Ms Smyth

Members in attendance: Mr Ripoll, Mr Anthony Smith and Senator Stephens

Terms of reference for the inquiry:

To inquire into and report on:

(1) the types of finance and credit options available to small and medium business (SMEs) in Australia;

(2) the current levels of choice and competition between lending institutions, but not limited to, credit availability, fees, charges, comparative interest rates and conditions for business finance;

(3) credit options available from banks, non-bank lenders and second tier lenders;

(4) the impact of financial institution prudential requirements and banking guarantees on lending costs and practices;

(5) comparison between the credit options available to SMEs located in regional Australia and metropolitan areas;

(6) the impact of lenders' equity and security requirements on the amount of finance available to SMEs;

(7) policies, practices and strategies that may restrict access to SME finance, and the possible effects this may have on innovation, productivity, growth and job creation;

(8) the need for any legislative or regulatory change to assist access by SME to finance; and

(9) any other related matters.

WITNESSES

Committee met at 9.03 am

CHAIRMAN (Mr Ripoll)—I declare open this public hearing of the Joint Committee on Corporations and Financial Services, the second in a series of public hearings the committee is holding to inform its inquiry into access for small and medium business to finance. The committee is to report by 30 April 2011. I welcome everybody here today and I remind everyone that witnesses giving evidence to the committee are protected by parliamentary privilege and any act which may disadvantage a witness on account of their evidence is a breach of privilege and may be treated by parliament as a contempt. It is also a contempt to give false or misleading information and evidence to our committee.

Witnesses should be aware that, if in the giving of their evidence they make adverse comment about another individual or organisation, that individual or organisation will be made aware of the comment and given a reasonable opportunity to respond to the committee. If a witness objects to answering a question, the witness should state the ground upon which the objection is taken and the committee will determine whether it will insist on an answer having regard to the ground claimed. If the committee determines to insist on an answer, a witness may request that the answer be given in camera. A request to answer in camera may also be made at any other time. The committee prefers to hear evidence in public but we may agree to take evidence confidentially. The committee may still publish confidential evidence at a later date, but we would consult the witness concerned before doing this.

[9.04 am]

LAWLER, Mr Luke, Senior Adviser, Policy and Public Affairs, Abacus-Australian Mutuals

CHAIRMAN—Welcome, Mr Lawler. I will ask you to make an opening statement or remarks and we will kick off, thanks.

Mr Lawler—Thanks for the opportunity to contribute to this inquiry. Abacus-Australian Mutuals is the industry body for the mutual banking sector. We represent 104 credit unions and nine mutual building societies, those organisations having 4½ million members across Australia and total assets of $77 billion. Credit unions and mutual building societies are authorised deposit-taking institutions regulated by APRA under the Banking Act and they provide a full range of consumer banking services. Credit unions and building societies collectively hold about 11.4 per cent of the household deposits market and 10.9 per cent and a growing share of the new home loan market. Generally speaking, mutual banking institutions are focused on consumer banking. However many of our members, particularly those based in the regions, also compete in the small-business market. At the end of 2010, loans to small businesses by credit unions totalled $1.4 billion and loans to small businesses by building societies totalled $900 million, so a total of $2.3 billion in small business lending by sector.

Credit unions and building societies engaged in this type of lending have invested in the necessary expertise and product range to compete in the business banking market. They see an opportunity to provide a personalised level of service for small businesses particularly microbusinesses in various regional markets where other lenders are not providing that personalised service. Any mutual banking institution entering the small-business market recognises that it requires significant investment and an appreciation of new and different risks. APRA, the prudential regulator, strongly advises mutual ADI boards—and when I say ADI, I mean authorised deposit-taking institutions—not to allow their institution to move into commercial lending without ensuring that they have the personnel, expertise and systems to do so prudently. APRA's position is that assessing, pricing and securing commercial exposures requires a set of skills distinct from those required for assessing standard mortgages and personal lending, which of course are the bread and butter for our sector. Small businesses rely more on debt funding than large companies and rely more on the banking sector for that debt funding than large companies. So a competitive banking sector is critical to small businesses.

Abacus is engaged with the government and other stakeholders to implement pro-competitive measures announced in the government's December 2010 policy statement, *A competitive and sustainable banking system*. The measures in that policy statement are divided into three streams and they will have short- to medium-term and longer term effects. Abacus strongly supports the government's undertaking to put mutuals and smaller banks at the centre of the Bank on a Better Deal campaign, a public information campaign, including introducing a new official government protected deposit symbol. We see this as a very important initiative. It is for a national community awareness and education campaign to properly inform consumers about the safe and competitive alternative mutuals and smaller banks offer to the big banks. The campaign and the forthcoming related announcement about the future level of the cap applying to deposits under the Financial Claims Scheme are both very important factors for smaller banking institutions in maintaining and expanding their access to funding.

Access to funding at a competitive price is critical for smaller banking institutions. The $1 million cap is reassuring to certain classes of large depositors who might otherwise stick to the major banks. Major depositors include: local councils, healthcare bodies, universities, schools, hospitals, church organisations, unions, super funds including self-managed super funds, corporate entities, sporting organisations, charitable foundations and wealthy individuals. Maintaining and expanding our funding sources is critical to our capacity to compete in lending markets, such as small-business lending, against the major banks. Thank you very much, that is all I would like to say in terms of my opening remarks.

CHAIRMAN—Continuing on that theme of some explanation of a range of differences, could you give us your view on the big differences between the big four banks, the major banks, and everybody else including mutuals and building societies in the way they do business and maybe the way they are perceived by the market as well?

Mr Lawler—In terms of the regulatory framework, there is no difference other than the major banks obviously engaging in a much wider range of activities than smaller ADIs. We represent the smallest ADIs. In our sector our main focus is very much on retail banking, and consumer retail banking. The banks have a wider range of activities. But we are all subject to exactly the same regulatory framework and exactly the same prudential standards on capital and liquidity and governance and risk management and all those sorts of issues.

As for the differences, size is a factor obviously. The major banks, and almost all the banks, are listed entities so they are driven to maximise returns to their shareholders. The other big distinction between us and banks, and particularly the major banks, is that we are customer-oriented institutions motivated to provide good service and good pricing and good products to our customers, who are our owners.

CHAIRMAN—But you do not exclude anybody based on who your owners are or membership or anything like that—it is a completely open market in terms of what you are providing?

Mr Lawler—A small number of our organisations still have bonds which require a connection to a particular profession or workplace or something of that nature but, generally speaking, anyone can join any building society or any credit union. As I say, a small number of credit unions still maintain a bond which requires some connection to, say, the teaching profession or the police force. But generally speaking, the bonds are entirely open and the regulatory framework does not compel us to engage in a particular kind of business and not in another kind of business. We are perfectly free to do it except that the prudential regulator is quite rigorous about making sure that if we are entering new lines of business, and commercial lending is a riskier form of business than home lending and personal lending, our individual institutions simply have to demonstrate to the prudential regulator that they have the capacity, the skills and the processes to engage in that business.

CHAIRMAN—What would you say is the biggest issue since the global financial crisis in terms of providing funds and continuing the pre-GFC terms and conditions and the amount of money that is available?

Mr Lawler—The biggest changes are the disappearance of certain sources of wholesale funding or the higher price of certain sources of wholesale funding or the dramatic shrinking of those sources of wholesale funding. All banking institutions have been looking more to deposit funding for a range of reasons. It is a more reliable form of funding and regulators prefer that banking institutions have more reliable sources of funding. Short-term wholesale funding in the context of the global financial crisis became a big problem because it got very expensive or it just disappeared.

Some issues arose about the funding models for certain kinds of businesses. For example, in the home lending market a lot of non-ADI lenders found that their business model became almost unviable, if not unviable, because of the lack of ability to tap markets where previously they could get well-priced funding. Those markets, and in particular the market for residential mortgage-backed securities, is yet to recover. The government is supporting that market and there is optimism that at some stage that market will return. No-one expects it to return in the form it was before the global financial crisis but we certainly hope that that market will recover to the extent that my members and a much wider group of lenders will be able to diversify their funding beyond, for example, deposits in the case of my members.

Deposits are always, and have always been and are always likely to be, the core source of funding for my members, but the extent to which they can tap other sources of funding increases their capacity to grow and compete. The big impact of the GFC is that these other sources of funding have disappeared or have become a lot more expensive and there is quite hot competition in the deposits market. That is one of the other changes which is good for savers—there has been a big change in that market.

CHAIRMAN—Is there equally hot competition for lending? If there is competition for deposits, are the banks—or all the lenders—just as eagerly putting money out the door as well?

Mr ANTHONY SMITH—It is a good question, Chair. Do you see a lag in that?

Mr Lawler—The structure of the market has changed as there are fewer lenders, fewer people out there. Through the change in the sources of funding some sources of funding have disappeared and others sources of funding have become more expensive. Also there has been the consolidation that we have seen in the banking market. We have seen some foreign banking competitors exit and we have seen some regional banks swallowed up by the majors.

You had probably best ask others about the state of competition in the small business lending market. We get a mixed picture from our members. It is a competitive market but how competitive compared to what it was before the global financial crisis, as a general comment you would have to say that it is likely to be less competitive simply because there are fewer competitors, funding has become more expensive and sources of funding have disappeared.

CHAIRMAN—The CPAs in their submission have said to us that perhaps pre-GFC money was a little bit too easy to get and that obviously, having the GFC and from what you have just told us, that has been redressed in a market sense. You get a sense that maybe also the pendulum has swung too far now, that there is a conservatism or a resistance to lending where there possibly should not be.

Mr Lawler—That is difficult to comment on. As I say, commercial lending is not a huge part of our business. But from the point of view of members—

CHAIRMAN—But even on mortgage lending or any other lending, just to get a sort of bigger picture of what your members do, do you think that has gone too far?

Mr Lawler—The changes in the market and the exit of some competitors, I guess, had an impact which was probably most clear a year or two ago in terms of the dominance of the major banks in markets like the home loan markets. But over the last year or so, our members in particular have been able to gain market share. We have a growing market share. Whereas two years ago, I think, our share of the new home loan market was around 6.5 per cent, it is now nearly 11 per cent, and that is partly taking some share off the majors. It is also filling the gap left by the exit of those non-ADI lenders. Our pricing is very competitive in the home loan market. It is also partly due to the fact that our profile has definitely been raised, partly because for the first time we have been spending money on a national marketing campaign. We are a very diverse sector with a lot of autonomous organisations, but they have agreed over the last year or so to spend money on a national marketing campaign. That has helped, but I think that it is the pricing and, for example, things like CBA doing that big rate increase on Melbourne Cup Day last year, which helped its competitors.

CHAIRMAN—Yes.

Mr ANTHONY SMITH—Just to follow on—and thank you for your opening statement which covered a lot of ground—you talked about microbusinesses in particular, and that is obviously one aspect of this inquiry we are very interested in. Could you just enlarge a bit on that with respect to the history of your organisations or the mutuals in terms of serving microbusinesses? This has been a very fast area of growth in the last five or 10 years and all the anecdotal evidence you hear on the ground is that the banks have not been particularly interested in it. I am interested in the microbusiness story, broadly, through the GFC and through to today.

Mr Lawler—Interestingly enough, one of our larger members, in fact our largest member, CUA, in evidence before another concurrent parliamentary inquiry, was asked about their exposure to commercial lending. They lend to 20,000 small businesses and most of those businesses would be microbusinesses.

Mr ANTHONY SMITH—Principally home-based, or micro-based as it is these days.

Mr Lawler—Lots of small businesses are obviously home based. In fact we think that our global number for the commercial lending that we do, which is $2.3 billion, probably understates the amount of lending we do to small businesses, because a lot of our home loans—$56 billion or so—would also have some element of funding for small businesses, so we probably do more—

Mr ANTHONY SMITH—Just because of the integrated nature—

Mr Lawler—Smaller business loans are secured against homes, so whether they get categorised as a commercial loan or simply as a mortgage I do not know. I am not quite sure where the boundary can sometimes shift. Certainly our sector—particularly in those regional areas where there is a longstanding main financial institution in a particular region—provides a lot of support for local small businesses, and has done for many decades.

Mr ANTHONY SMITH—Just following on from that, in evidence on Wednesday in response to a question from the chair—and the chair will remember whom he directed it to—we were told in evidence that one of the fundamental problems at the banking level, when it came to small business lending generally, was a decline or degradation in the expertise of bank lending officers. I would like your perspective on that particularly given the localised nature where so many of your organisations fit in.

Mr Lawler—Certainly opportunities have arisen for our members. Where you have had major bank lenders, for example, deciding to centralise all decision-making or have had some other kind of management policy or structural policy, which creates a sense of remoteness about decision-making, in situations like that in their local markets our members have been able to take advantage of that. Again, due to being small and risk-averse—we are a very risk averse, prudent sector, and we have a long record of that—we have the best record for lending by far across the banking industry. Our members do not rush into this kind of business, but where they are set up to engage in it, they certainly seize those opportunities.

We have a least two regional members where almost a third of their lending is commercial, which is highly unusual. It just goes to show that in those regional markets they are very well-established, they know those markets very well and they are able to do that—

Mr ANTHONY SMITH—That is getting to the nub of it really. You are saying that because they know the market and they have still got the resources on the ground, they are able to assess the capacity of the small businesses. The evidence we heard from two witnesses from ACCI, I think—and the second one confirmed it—was that the banks have lost a certain capacity to be able to assess a differentiation across small businesses, therefore, they are all lumped in together.

Mr Lawler—The other factor in this is that where there is an opportunity and where the local mutual organisation sees an opportunity, the issue that they have to confront if they have limited funding is where do they put it? Do they just keep it in consumer lending or do they turn to other lending? That is the constant issue. It is not as if there is an unlimited amount of funding, and one of the points that we are making is that access and being able to expand access to funding is really quite important for our sector. I do not speak on behalf of banks, obviously, but I think that regional banks and smaller banks would be in a similar position to us in terms of their access to funding.

Mr ANTHONY SMITH—That is a segue into my final question, which is very general. From the perspective of an umbrella group, who else around the world does this better in certain aspects of policy settings? Do not feel that you have to give a comprehensive answer now, but it is something that the chair agrees gives a perspective. It is not a major part of our inquiry and we are not about to matrix everything around the world, but we are interested in perspectives. You may want to just give it a very general answer now and reflect on it and send us something else in time.

Mr Lawler—What is unusual about the Australian banking regulatory system is that mutuals, credit unions and building societies are entirely integrated into the same regulatory system. You will find in other markets that mutuals, credit unions, will have their own regulatory system. The banks will be off separately. Our members meet all the requirements that banks meet. We are, I think, the only credit union system anywhere in the world which is fully compliant with the Basel international banking regulatory frameworks.

CHAIRMAN—This is Basel II?

Mr Lawler—Basel II, Basel III coming up—

CHAIRMAN—That is very good.

Mr Lawler—Whereas in other markets, they tend to be regulated separately. There might be arguments for that in other markets, but—

Mr ANTHONY SMITH—Like the US, for instance.

Mr Lawler—Like the US, for example. Over there the credit unions do not pay tax, but they are restricted in terms of acquiring customers. So there are issues there. I would imagine there would also be issues about, given this restriction on acquiring customers, what lines of business they can get into. We do not face those constraints. We are regulated in the same regulatory framework as CBA and Westpac. If our members want to enter into new forms of businesses, they can. They just have to make sure that they have the right level of expertise and capacity and risk management systems to do it. That is what makes mutual banking institutions here in Australia a bit unusual globally, in that we are integrated into the single common banking regulation framework, which is consistent with the global Basel principles.

Senator STEPHENS—I am a regionally based senator and a lot of the work that I do is with rural businesses and farmers. Many of the constituent issues that I deal with concern their sense of injustice and unfairness. They feel that people in the regions are being treated differently on issues of access to finance. Is that a factor in the mutual space as well?

Mr Lawler—I think the fact that we have such a big footprint in regional Australia reflects the fact that there is demand for institutions, and historically there has been demand for institutions like ours. People want to have access to banking services. They want to be able to retain their capital locally. They want to be able to speak to lenders who understand them, understand their business and understand the local community.

That is why it is a successful business model in those markets. But it is challenging to meet all the prudential regulatory requirements and to meet all the other regulatory compliance issues. We see ongoing consolidation in our sector. The sector itself continues to grow, and our assets are growing, but the number of participants is shrinking because the smaller mutuals either find the regulatory compliance burden too heavy or they see, for good strategic reasons, a case to merge with another institution to become larger and get access to economies of scale. Economies of scale help in the context of entering new lines of business, such as business lending.

On funding in those regions, I touched on the issue of the financial claims scheme and the current cap of $1 million. We have found a slightly curious, and in some ways slightly perverse, response to the global financial crisis. At the moment there is coverage of councils that lost money because they invested in particular securities which were highly rated but which nevertheless turned out to be worthless. We are finding now that a lot of councils around Australia require a credit rating before they will invest in a particular entity.

Most of our members do not have credit ratings. Our larger members have BBB credit ratings, but that is about the highest credit rating they have. There are not that many of them with credit ratings. Credit ratings generally are about access to wholesale markets and our members, except the largest members, do not directly access wholesale markets. But they are now faced with a situation where, to compete for the deposits of an entity like a local council—which is often the biggest business or entity in a local area—if that entity wants to keep the funds locally, the only option is their local building society or credit union. But if they are advised by their auditor or whatever that you can only invest in AA or AAA or whatever, they cannot invest in their local entity, so that capital has to go off somewhere else to a major bank—and that is a bit of an issue for us now. Certainly, the relatively high cap of the financial claims scheme helps. So to the extent that that is reduced or reduced dramatically, that will be a problem in terms of accessing those larger depositors. Accessing larger depositors helps us to grow.

Senator STEPHENS—So your recommendation is that the cap continue beyond October?

Mr Lawler—Yes, we think so. We think it should stay where it is. It is relatively high by global standards, but our market is very unusual. We have never had deposit insurance. In the US, where their cap is $250,000, they have had deposit insurance for decades. Other markets have had deposit insurance for decades. What we have had in Australia is an implicit guarantee, which probably attaches more to the major banks than anybody else. Now we have moved from that to an explicit guarantee and suddenly the guarantee has become, if you like, almost like a proxy for the prudential regulatory framework; whereas it is the prudential regulatory framework which protects depositors.

The cap of the financial claims scheme is the level to which you get early access to your funds. We would really like to see the whole financial claims scheme reframed very much more as an early access facility rather than having this sense of being a proxy for the whole prudential regulatory framework. If it becomes that, that creates a ceiling—for the most risk-averse investors, not all investors. People who know their credit union and know their building society, loyal members, are not concerned about those sorts of issues, but reaching out to new markets and new depositors becomes a bit harder.

Senator STEPHENS—I have a question that is a little bit left field. Given the recent disasters and the extent to which that has affected some small businesses, do the mutuals have a strategy about how to support small businesses for recovery and regeneration?

Mr Lawler—Yes, they do. We have our hardship packages. Interestingly, to date, requests for relief from loan repayments, for example—probably the main form of relief that you would expect to be sought—have been relatively low. For our members in those flood affected areas, the claims are relatively low. But our members are standing ready and have been looking after their members to the extent that they need relief—deferred loan repayments, fee relief et cetera.

They are certainly doing that. But, as a general observation, the feedback I get is that it is a little lower than you would expect—the claims are a little lower than you would expect, which hopefully is a good thing. It has been suggested that possibly some people have not yet faced up to it, but you have to take it at face value. It is presumably a good indicator.

CHAIRMAN—There is no question that there is less funding available for small and medium business enterprises, that everyone is doing it a bit tougher and perhaps there is a view—it is certainly the view of a range of submitters—that pre the GFC, as I said earlier, funding was too easy. Do you think the settings are now right, though? Do you think the market has balanced itself out—that people who should be able to get funding do and that people who perhaps should not be able to get more funds do not?

Mr Lawler—For small business borrowers, I would find it difficult to make a blanket statement. On the issue of lenders getting access to funding, we certainly think that, at this stage, the markets are still a bit too tight. Good, safe investments, such as residential mortgage backed securities here in the Australian market, where no-one has ever lost money on one, are kind of tainted by the fact that they were crook in the US. That market has not recovered, so that affects the capacity—

Mr ANTHONY SMITH—Almost like brand destruction.

Mr Lawler—Exactly. That has affected the capacity of the lenders to source the funds they need. There is a bit of a shortage of funds, so it is obviously going to the best credits.

CHAIRMAN—I suppose the real focus of my question, and what I am trying to figure out through this, is whether there are people, businesses, out in the marketplace who cannot get the money they need to grow, to expand, to buy more equipment and plant and so forth? Are there people missing out where they should not be—where they are a good risk and should therefore have access to funds but simply cannot find somebody to lend it to them?

Mr Lawler—I am sure there would be cases like that. A point one of our members made, which I think I put in the submission, is that the lender needs certain information—borrowers have to provide the information necessary to make the lender confident about making the loan. There are some issues that can be dealt with in the area of borrowers providing the necessary information for the lender to be confident. As a general observation about your threshold point, it is true that there is less funding available generally. Credit was probably too available globally for a while there, which caused the problems.

CHAIRMAN—On the question of city versus bush: is it harder for people in the bush to access funds? Are there some real barriers there, be it just fewer available lenders in smaller towns or in regions, or is it more a national and global market now where really people should not have any particular barriers, regardless of where they live?

Mr Lawler—There may be some particular regional issues about the bush and regional borrowers, which may go to data that helps lenders assess credit risk. In urban areas there might be more information available for people to make assessments; hence the local knowledge issue is quite critical out in the regions. I do not have data to back this up, but our experience is that our commercial lending is better quality lending in the regions than it is in urban areas. That partly reflects the fact that we have this strong—

CHAIRMAN—You have a larger network out in the regions.

Mr Lawler—Out in the regions. We are just not as strong in the big metropolitan areas. We just do not have the market presence there.

CHAIRMAN—The big four banks have a massive proportion of the market right across all lending but also in terms of deposit taking and products. Is it just generally because of size, so that they are much more visible; they are just out in front of everybody all the time? Or do they also offer more variety of products? Is it a better range? Are there really good reasons why somebody would choose one of the big four, just as a general concept, rather than go for a smaller enterprise, a mutual or a credit union?

Mr Lawler—They have got, as you say, a massive marketing presence. They have actually got a massive physical presence too. They do have an advantage over a lot of other lenders in terms of access. Our sector has more branches than the Commonwealth Bank—so we are a large sector—but we do not share all those branches. We also have the second largest financial institution ATM network, fee free.

CHAIRMAN—There is an opportunity.

Mr Lawler—So our credit union members all around Australia can access fee-free ATMs. Without that capacity, we would be at quite a disadvantage to the likes of CBA and Westpac, with massive ATM fleets. They do offer a wide range of products. The question is their motivation and their business structure. Is that what the borrowers want? They are totally focused on maximising their profit, possibly hitting sales targets or whatever. They are not focused on particular communities and they are not particularly focused on the benefit to the customer. That is reality; that is what they are. But certainly they are large. They have massive, gigantic, marketing budgets, which we cannot really compete with at all. So they have some natural built-in advantages, and of course there is the general perception that they are too big to fail, so they have a massive funding advantage over everybody else as well. All those large risk-averse depositors will just default straight to the majors. It is hard for us to compete for that funding.

CHAIRMAN—But there is no regulatory burden on mutuals or credit unions which means it is really any different in the end, apart from the perception of ‘too large to fail’.

Mr Lawler—Sometimes our members have issues with the way the prudential regulator administers the standards, the way that they say, ‘You must keep X amount of regulatory capital,’ or whatever.

CHAIRMAN—They get too tough.

Mr Lawler—They can be perceived sometimes to be too tough. But certainly in terms of the regulatory framework itself, no, there is no regulatory distinction.

CHAIRMAN—So really it is more a case of perception in terms of the deposits. We saw that through the global financial crisis—a flight of funds to particular institutions.

Mr Lawler—Yes. It was not so—

Mr ANTHONY SMITH—But that is a good point. Obviously there is an immediate effect, but you made the point just earlier that, with risk and perceived risk, the majors have a natural advantage for that reason. Do you see that taking five or 10 years to wash out?

Mr Lawler—It is very hard to shift perceptions, particularly because of our fairly unique depositor protection arrangements which have evolved over the years. The big four banks are so dominant that the perceptions about them being too big to fail was strongly reinforced, if anything, in the context of the GFC. Most people are completely unaware of the prudential regulatory framework, and you cannot blame them. That is hardly something they would be very interested in.

CHAIRMAN—Why would you know about that?

Mr Lawler—Exactly. Even the coverage of the deposit guarantee is very patchy. I have met members of parliament who did not realise that the deposit guarantee applies to them.

CHAIRMAN—Can you name them?

Mr Lawler—I will not name them, unless you compel me to!

CHAIRMAN—No. I was just interested. It is certainly not the three of us; we are safe!

Mr Lawler—It is just a fact that it is very hard to inform and educate the public about these sorts of issues. The majors are out there with their massive presence and their massive marketing budgets, which gives them a huge advantage over their competition.

Senator STEPHENS—On that point, is there an issue for us to think about around financial literacy?

Mr Lawler—Yes. That is why we are very supportive of the government's announcement that it will be running a 'Bank on a Better Deal' campaign later this year. That is certainly a very positive measure, from our point of view.

CHAIRMAN—Do you think there is anything more that we could do in that particular area from a regulatory or government perspective? This inquiry is interested in how we can improve competition and access.

Mr Lawler—To the extent that the inquiry can reflect on the need to have a better educated depositor community about the prudential regulatory framework and the safety of all ADIs—whether they are large or small, they are all equally safe. The regulator is totally focused on protecting deposits, no matter where they are.

Mr ANTHONY SMITH—Will APRA run that, do you think?

Mr Lawler—APRA is not a particularly outwardly facing agency; that is just in its nature. I do not know whether any prudential regulator—

Mr ANTHONY SMITH—Without being political about it, it strikes me on a perception level that it is the authority in charge that is going to be the most believable and compelling.

Senator STEPHENS—Yes.

Mr ANTHONY SMITH—People look back at where there have been failures in the past. Your point is that most people are oblivious to the rules of racing, so to speak, and the protections that they offer. I accept, without being overly critical of them, that they are not necessarily purpose built to be the world's best broad communicators, but they probably have a greater capacity than any other organisation to put the facts before people.

Mr Lawler—ASIC has a consumer education role, but it is a very broad consumer education role. It is everything from getting advice about superannuation to 'What is a deposit?' and 'What is an ADI?' One of the problems is this very phrase 'ADI'. It has been around for 10 years. There are banking reforms that many of you are intimately familiar with—excellent reforms, harmonisation of all deposit takers. But this phrase 'ADI'—no-one knows what it means. It is a very technical term. We have been lobbying for the adoption of a new term in the Banking Act which is 'authorised banking institution'. These might seem like cosmetic things, but everyone knows what banking is; no-one knows what an authorised deposit-taking institution is.

Mr ANTHONY SMITH—They immediately think, 'That's something different to a bank.'

Mr Lawler—Precisely. 'Bank' obviously has a few negative connotations in terms of PR, but it also has some very simple, well-understood connotations about what it does. It is safe and it is regulated. For whatever reason, the terms 'credit union and 'building society' just are not as well known widely across the community.

Mr ANTHONY SMITH—What has been the reticence to accept your advice on that, at a bureaucratic level?

Mr Lawler—We are not entirely sure. There is a discussion now with APRA about their administration of section 66 of the Banking Act, which is where they protect the terms 'bank' and 'banking', and 'credit union' and 'building society'. So that discussion is unfolding at the moment. That might shed a bit of light on where the regulator sees what these terms mean to the public and how it thinks they should be used. But at this point we certainly do not have a totally positive response to the suggestion of changing the Banking Act to get rid of 'ADI'.

Mr ANTHONY SMITH—To the extent that you have made public representations and the rest, would you be able to provide the committee with that?

Mr Lawler—Yes.

Mr ANTHONY SMITH—Consistent with what is possible and feasible—just in terms of a further submission. That is an issue that is worth us exploring.

CHAIRMAN—I think it is a good idea.

Mr Lawler—Yes. Will do.

CHAIRMAN—Finally from me, just following through on that theme, is there any sort of mark or logo, like a Heart Foundation tick of approval—that type of symbol—that is consistent right across the market that would say—

Mr Lawler—An authority of endorsement sort of thing?

CHAIRMAN—Absolutely, yes. It is the issue of confidence. I am talking about a consistent symbol that sort of stamps it and says, 'It doesn't matter what you're called, whether you're a bank, a credit union, a mutual or whatever.' Is there nothing like that?

Mr Lawler—There is not now, but there is a proposal. In fact, there is already a kind of draft example of it, which is the government protected deposit symbol, which is to be part of the Bank on a Better Deal campaign.

Mr ANTHONY SMITH—Is that being run from Treasury?

Mr Lawler—It is being run from Treasury. We are having discussions with Treasury and at the moment they are doing their research, preparing the campaign.

CHAIRMAN—Thank you, Mr Lawler. We very much appreciate your time and the information that you have provided.

[9.47 am]

BORDONARO, Mrs Kathryn, Committee Member, Commercial Asset Finance Brokers Association of Australia

GANDOLFO, Mr David, Committee Member, Commercial Asset Finance Brokers Association of Australia

CHAIRMAN—Good morning. Thank you very much for coming along. Do you have any comments to make on the capacity in which you appear?

Mr Gandolfo—I am the immediate past president of the Commercial Asset Finance Brokers Association.

CHAIRMAN—Thank you very much. We invite one or both of you to make some opening remarks.

Mr Gandolfo—We will both make some opening remarks, but I will just be a little broader in the background of our organisation and what we do. We are the Commercial Asset Finance Brokers Association of Australia and that name is very specific to what we do. We deal with commercial clients. We are finance brokers, but we are not home loan salesmen, car finance brokers or consumer brokers. It is all commercial and it is all about asset finance.

Our market is about what is generically known as leasing or equipment finance, hire purchase and chattel mortgage of business assets such as trucks, transport equipment, plant and machinery equipment, lathes, engineering presses, computers, desks and that sort of equipment. We deal with clients who are sole traders—professionals, doctors. We deal with some public and corporate entities and government entities, but 90 per cent of what we do is in the small to medium sized business sector. We are intermediaries between our clients and the banks and finance companies that provide the products that we provide. They are, typically, hire purchase, leasing and chattel mortgage.

Collectively, our membership is right around Australia. We represent about 150 individual broking firms, and that represents about 600 individual business writers. Collectively, those people write about $6 billion per annum in equipment finance transactions. We do not have nearly the number of people that perhaps the mortgage-broking industry has, but we certainly are significant in terms of the numbers and the sizes of the transactions that we do. We touch a huge range of small businesses and we are, we believe, quite expert in that market and we are not expert really in any other market.

Our own businesses are small businesses. I am a director of a company called Quantum Business Finance, which is a small business. Kathryn is involved with East State Credit, which is a small business. So we are small business people dealing with small business people. Our role as brokers, as individual business writers, is to deal in those specialised products and to have specialised knowledge of those products. We have long-term relationships with our clients, which is another distinction to perhaps mortgage brokers, who might write a new transaction every six or seven years. Our relationship with our clients is ongoing and we need to have a portfolio of lending facilities available to these clients from different lenders who specialise in different types of products and lending criteria.

The small and medium business areas frequently comment on the lack of access to knowledgeable and experienced bankers, and we fill that gap. I am not saying anything disparaging about the banks, but most business bankers have a limited knowledge of a wide range of products; we have a very deep knowledge of a limited number of products. Ninety-six per cent of small business lending would come under what we do.

CHAIRMAN—Can you explain that, please?

Mr Gandolfo—The market that we are in and any regulation which impacts potentially on our market, which would be phase 2, would affect 96 per cent of our business customers.

CHAIRMAN—Of your business customers?

Mr Gandolfo—Of our customers, yes. We regard ourselves as, and we are, a fairly vital distribution network. There are lenders in this market, such as Macquarie Leasing, which is a very prominent player in this market, which have no retail presence whatsoever. All of their products are distributed through intermediaries, such as equipment finance brokers.

The CPA's submission at page 19 has noted that a number of their members believe that the role of the equipment finance broker has been critical to their business. We have been severely impacted by the GFC. We used to have on our panel of lenders typically 20 to 25 lenders or places where we could go to obtain products for our clients. Now there are only eight main players and there are some second-tier lenders who are a little more expensive and more specialised. So we have got fewer places to go. Our clients have found it more difficult to raise funds in the market that they are in. Our members have found it more difficult to raise funds for their clients and we have been severely impacted by the GFC, for two reasons: the number of lenders and the more risk-averse nature of lenders for the last two or three years.

We have had an involvement with phase 1 of NCCP regulation. Even though it is all to do with consumer finance and we are not involved in that, we have been watching that very, very closely. As an industry, since long before regulation, CAFBA has been self-managed. CAFBA is the result of a merger between a New South Wales and Victorian state body and we have since gone national. That is going back some years now. But long before formal regulation and before SCOCA in New South Wales started this process, we were self-regulated and we have been self-regulated for as long as we have been an industry.

We have our own PI, or professional indemnity, insurance program, run by Insurance Advisernet in Sydney. We have our own education program. We have our own disciplinary committees. We have our own code of conduct, to which all members must adhere. Also, we are very strict. We have minimum education standards and minimum industry experience standards. We have kept our industry clean by self-regulation as long as we have been an industry.

That is a fairly important point and it dovetails into phase 2, where possibly we could be regulated. We would rather be the regulatory body or the self-regulatory body than being regulated externally, because we have proven that we can do that. Some years ago, at the beginning of this process, I had a meeting with the Victorian Department of Justice and we explained to them what it is that we do. They said they were largely unaware of our industry because there had been virtually no market failures in it. I hope you do not mind if I read some of this.

CHAIRMAN—Just before you do that, in terms of regulation, when you talk about the self-regulation within the sector and the 150 small businesses that you represent, you still meet all the normal regulatory requirements of carrying on a business—

Mr Gandolfo—Absolutely, yes.

CHAIRMAN—plus licensing requirements and so forth.

Mr Gandolfo—Yes.

CHAIRMAN—So, aside from self-regulation, there is the standard bucket, as it were, of eggs.

Mr Gandolfo—That is correct.

CHAIRMAN—Then, on top of that, you overlay your own code and practice, if I understand it correctly—

Mr Gandolfo—That is right, and voluntarily almost all of our members have complied with the regulations of phase 1, even though they are not really in that market.

CHAIRMAN—So you have an industry based code of practice, developed by the organisation and maintained by the organisation as part of membership, and you regulate that yourself.

Mr Gandolfo—That is correct, yes. I would also add that even though we are not involved with consumer lending, which comes under phase 1, most of our members have been compliant with all of the requirements of phase 1 in the event that inadvertently they deal with a sole trader who perhaps might not be as commercial as we think he is. In the event that there is regulation in phase 2, we are already compliant with it. Our main concern is that a set of regulations which applies to consumers and consumer lending is the right remedy for problems in that industry, but the same set of problems do not exist in our industry. To us, overlaying those regulations would be counterproductive and quite constrictive.

The consumer credit unit of Treasury released a green paper on phrase 2 of the COAG national credit reforms in July 2010, of which a major component was examining the provision of credit to small business. This paper flowed from the national consumer credit—NCCP—legislation that commenced on 1 July 2010 and it examined the possibility of applying consumer-style legislation in the provision of credit to small business. This would result in 96 per cent of Australian businesses being made subject to additional layers of compliance and regulation when seeking credit. Enforcing a regulatory regime on the provision of credit to small to medium enterprises will add a cost burden to small business as well as serve to restrict the amount of credit available to small business, which it clearly needs to continue to provide economic benefits to the nation.

Regulatory intervention in the business finance market would have adverse cost and time implications to equipment finance brokers, which would only serve to constrict commerce within the small to medium business sectors without delivering any corresponding benefit. Equipment finance brokers meet the business community’s need for prompt service and ongoing relationships and are integral to the equipment finance brokers’ business.

To properly act on a client’s behalf, it is common for equipment finance brokers to act and manage multiple credit facilities, as instructed by clients, where the ability to settle immediately is critical to the client’s business. Equipment finance transactions often need to be discussed, approved, documented and settled within a matter of days and sometimes within one day.

The broader imposition of unnecessary consumer-style protections would delay the provision of necessary finance facilities and would ultimately disadvantage small business operators. For example, the disclosure requirements of the NCCP would be logistically impossible in most instances and impose time delays and costs, which would be to the detriment of the commercial borrower. There is no market failure in the commercial asset finance broking space or not sufficiently significant to warrant the sort of legislation which has been mooted.

CHAIRMAN—Thank you.

Mrs Bordonaro—I started my career as an employee of one of the big four banks. I worked in that bank for 10 years and I spent most of my time in commercial asset finance products. I worked mainly in regional areas—in particular in Gippsland, Victoria. I particularly enjoyed working with small and medium business owners and I really enjoyed seeing their businesses grow as a result of the assets that they were financing.

In 1997 a decision was made by the bank that I worked for to close all of the regional asset finance departments across Australia and centralise all operations to Melbourne. I was given the option of moving to Melbourne or being made redundant. I chose to stay in Gippsland and I entered the world of commercial asset finance broking. I am pleased to say that many of my clients followed me and 14 years later they are still dealing with me.

The business that I work for has asset finance brokers located across regional areas in Australia. We have sites in Traralgon, Ballarat, Bairnsdale, Geelong, Mildura, Horsham, Albury, Wagga and Darwin. I know that Darwin is a capital city, but it is its own demographic. A diverse range of industries and agriculture are present in these areas, along with a mix of micro, small, medium and big business.

The commercial asset finance broker is a vital distribution network that provides small and medium businesses located in regional Australia an increased level of access to finance. Many regional towns or areas no longer have a bank branch physically present or, if they are one of the lucky ones, they might have one of the big branches represented. Outside of the big four, there are many lenders who provide asset finance to small and medium businesses—Capital Finance, the Bank of Queensland and Macquarie—but they do not have an extensive branch network in regional Australia. This is where the commercial asset finance broker provides access to finance for businesses located outside of major cities.

To my customers in regional Victoria, I bring a mobile shopfront of over 20 lenders. Yes, these regional businesses could access some of these lenders but it would be via a website or a call centre, and I am told every week how difficult it is, for example, for a potato grower in Thorpdale to explain to a call centre located in a capital city the intricacies of their business over the phone or over the web. Regional business owners want to deal with people who understand their area and their industries. Understanding comes through length of relationships. With the average stay for a bank branch manager at less than three years, it is difficult for a business to establish a long-term relationship. I have known that potato grower in Thorpdale for 20 years. I have red dirt on my car to prove it. I note that many of the submissions received by this inquiry echo these thoughts. The CPA, the New South Wales Business Chamber and the Australian Chamber of Commerce and Industry all echo these themes.

I thought I would just bring you a couple of examples of some of the regional businesses in my area that I look after. There was an industrial X-ray business that won a large contract to X-ray welds on a major pipeline and they needed additional equipment to do that. Their local branch said that they did not finance such equipment and the business did not know where to turn. We sourced that funding through a lender that does not have a regional infrastructure. Those finance contracts have run for three years and they are just about to be finalised. The business has since won further contracts and has increased its number of employees by five people—and five more jobs in regional Victoria is significant. A fertiliser seller and spreader business wanted to purchase a new design of spreader that would greatly improve their business efficiencies. Their local banker said no, they just did not understand the goods. The finance was secured via another mainstream lender but one that was not again physically present in the area. This was eight years ago. The business has since purchased four more of these spreaders via lenders not physically present in their area. All of these businesses are employers in regional Victoria and vital components of their regional communities.

I am also part of a small business and I am an employer in regional Victoria and proud to be so. I understand the highs and lows of small business, more so than any banker ever could, because I live that every day. The commercial asset finance broker is a vital distribution network that provides small and medium businesses located in regional Australia with a greatly increased level of access to finance. As David has mentioned, Treasury is currently consulting on regulating the provision of credit to small business, and the consultative committee that Treasury is working with does not have representation from our body or from small business. Small business and commercial asset finance brokers should be represented in this process, as the potential to further restrict access to credit is significant.

CHAIRMAN—Thank you both for really good introductions and giving us a bit more information. I am interested in understanding first from your perspective—because I think you sit in a unique place between a whole range of lenders and borrowers, particularly small business—the pre-GFC and post-GFC environments. There is a view—and I pursue this view—that it was perhaps too easy pre-GFC to access funds and that now it has become too tough or maybe that now it is balanced right. We would be very interested in your view as to whether that is the case.

Mr Gandolfo—We have to make the distinction that anything we talk about is our market and not the consumer market and quite often a lot of what you read is about the broader market. In our market, I do not think credit was too easy to get in the commercial space. I think it was probably about right prior to the GFC. It was probably too easy to get in the consumer space and too many people got home loans that perhaps they could not afford and car loans and consumer loans for products that they did not have the capacity to repay. Our industry is fairly tight in its lending practices and responsible lending practices, and that comes from the underwriters, who are the banks and finance companies. If credit had been too easy, there would be substantially more losses in that market than there have been.

In the early nineties recession, the banks were losing money left and right because of poor lending practices, but that simply did not happen during the GFC. In my experience, my own client base and most of my competitors' client bases are largely still intact. Mind you, they are finding it extremely difficult now to get funds for expansion and just to maintain or replace plant, machinery and equipment that they have already got. So my take on it is that, in our space, the environment was pretty right prior to the GFC. There were more low-doc or no-doc facilities available where you did not need to provide financial statements—those products have virtually gone now—and I would suspect that there would have been some losses in those areas, but none to the degree that you would say that lending was too easy. In the current space there are simply too few lenders and their lending guidelines are restrictive. Another issue, which is perhaps not directly as a result of the GFC but in terms of timing, is that the expertise within some of the banks is not perhaps what it should be, particularly in dealing with specialised industries.

CHAIRMAN—Do you think that the lenders, generically calling them lenders, have gone too far, that they have just become too risk averse or that it is more of a combination? To lead you down that path, either they have become too risk averse, too conservative in that space, or they just do not have enough funds and, therefore, the pie has gotten smaller and they are tightening the rules based around that smaller pie.

Mr Gandolfo—I do not think lack of funds is a problem. I think it was perceived to have been a problem and there was going to be a problem with funding. But that happened and it was resolved fairly early in the GFC. If the banks had to go overseas and get money at a higher premium, that is what they did. There are plenty of examples of lenders having plenty of funds available, even if it was at a higher basis point margin. So the availability of money is not so much the issue as the number of lenders who are actually in the market. There have been plenty who have exited and some of those lenders, perhaps like Societe Generale, did specific types of financial products or had different lending criteria that suited some borrowers, and those borrowers' needs simply are not being met at the moment. So that is one thing that has happened.

As for the lenders who are still in the market, there is a difference between banks and finance companies and some of these lenders are subsidiaries of banks. The banks comply with their own risk profiling and the banking code of practice but finance companies do not have to and they have got the discretion to lend a little more openly or adventurously—but that is probably not the right word. But there are simply not enough lenders out there to adequately cover the market. I can give you an example. Transport operators might have a fleet of, say, eight or 10 trucks. Those trucks could be $150,000 or $200,000 each, and one single lender may be comfortable with an exposure to one of those vehicles. There is nothing wrong with the business, but you cannot get the money for that ninth or tenth truck because you are out of lenders to get it from.

CHAIRMAN—If it stacks up in a business sense, is it just a case that the funds are harder to get because there are less funds? What I am trying to understand is whether it is: ‘Look, we’d love to lend you the money, but’—

Mr Gandolfo—It is a little bit interpretive about whether or not it stacks up in a business sense. The bank might want to see historical ability to service, but the ability to service that tenth truck will come from the income that it generates, not from the other nine he has on the road. If his business was a trust, it might be looked at differently by one bank than another, because banks assess the ability to service in different ways. Most start with pre-tax profit, and one starts with after-tax profit. So they do their own sums and we prepare our own submissions. A lot of these business owners do not have any idea of how to approach a bank, and that is where we come in. We write submissions which are factual but which highlight the benefits that this new asset will provide and, if it is a highly specialised asset, you have to put quite a bit of detail into that. We will do the exercise, but we have got to be convinced ourselves that the client can pay for it.

Mr ANTHONY SMITH—Is that what you put in formal submissions that are—

Mr Gandolfo—I am not in the business of writing bad loans. It must not hurt my business either. That does not help me at all. We have got to be convinced that the transaction is viable and we present it to the bank accordingly.

Mrs Bordonaro—Part of our role, as I see it, is that we are almost like an interpreter. We go and visit the business owner, we see what they do and we learn all about it and then we put that into bank speak.

Mr Gandolfo—But they are absolutely risk averse and they are risk averse with asset classes. It used to be that there were plenty of places to go perhaps if you were setting up a retail shop and you needed finance for the fit-out—demountable partitions, flooring, furniture and that sort of thing. It is almost impossible to get that now. There is nothing wrong with the borrowers. The borrowers have not changed. It is just that the asset class is no longer attractive. It is not because the repossession yards are full of shop fittings; it is just because it is deemed that that is a risky asset with no resale value. One of the distinctions with our business is that the only tangible security taken in almost all of the transactions we do is the asset that we finance. So we do not take the family home; it is never a part of the deal. If we are financing a truck or a concrete mixer or a wine press or something, that becomes the security for the transaction.

Senator STEPHENS—It is very interesting to see where you do fit within the landscape. Given the problems that you have just enunciated about the exiting from the market of many lenders, is that also shaping the way in which you have to offer products to your clients—someone might come to you for finance for something and you would normally have recommended one path but now you have to recommend something that would not be your first choice?

Mr Gandolfo—Sometimes we have to say to our client, 'We can't do this for you now; we have to see how you trade for another six months or perhaps you need to put a deposit into this that you didn't otherwise have to put in before,' or, "You might have to alter your repayment structure or offer some other inducement to the bank to take this transaction on.' It might be that they put the GST portion back into the loan in the fourth or fifth month to reduce the bank's exposure. But certainly we need to suggest more conditions to clients than we had to prior to the GFC.

Senator STEPHENS—In regard to the kind of due diligence that you do on these businesses for your clients, we had some evidence on Wednesday about some businesses being encouraged, urged—and more—to shift from, for example, a line of credit with their bank to a credit card with a higher interest rate. Are you seeing that kind of pressure on your clients as well to shift their own financial arrangements as part of the post-GST environment?

Mrs Bordonaro—We do not deal in those products, but I definitely do get some feedback from clients which, again, I think reflects on skill levels. If you are dealing with perhaps a banker that maybe has had two years experience, it is easier for that banker to pass them off to a credit card assessing centre where the computer does all the work than to sit down and look at that business, analyse it and work out whether the line of credit is the best fit. So I think it comes down to skill level and time efficiencies in the banking structure.

Mr Gandolfo—We do sometimes come along after the event and see that the wrong product has been used, and we might try to rectify that.

Mr ANTHONY SMITH—So you think it is more a skill issue than anything else, do you?

Mr Gandolfo—I am conscious that all of our comments are reported, but I listen to some of the bank advertising and I just want to shoot the radio.

CHAIRMAN—It has been raised by others that there is a lack of skill in this particular area, and I can imagine—

Mr ANTHONY SMITH—We had some evidence the other day along these lines.

Mr Gandolfo—Some credit assessment is done offshore. A call centre or a credit assessment centre in another country cannot assess a cane farmer's ability to service loans or his need for specialised equipment.

CHAIRMAN—I have heard in other forums—and we have certainly had evidence—that the banks put a lot of pressure on brokers, mortgage brokers in particular, to get rid of a whole heap by just reducing their fees in their ability to write loans. Has that been the case at all with your area?

Mr Gandolfo—No. The banks have probably reduced the number of introducers. But one thing which did happen prior probably to the GFC was that the rise of the mortgage broking industry did impact on our business. The level of education and training in the mortgage broking industry is not the same as it is in our industry. They are very different industries. But the banks were getting a whole lot of business from mortgage brokers—enormous volumes of business—

and then some of these mortgage brokers would say, ‘We’ve got these other equipment finance products. Can we offer those as well?’ Pressure was actually brought to bear on banks to allow some of the aggregated groups to allow access to other products by some of their brokers. What happened was that you had people, who were not qualified or sufficiently educated, dealing in some of these products and the banks have culled those. So what they have done is they have said, ‘No, you mortgage brokers, you stick to that product; you equipment guys stick to that product; factoring guys stick to that product,’ and so forth, which is fine. That is all we ever wanted. We never ever attracted the attention of regulators until the mortgage brokers came along.

Mrs Bordonaro—We all got lumped into the one pot.

Mr Gandolfo—The first couple of green papers or discussion papers that were out there 10 years ago were all about finance brokers and distribution channels and did not make the distinction between who does what.

CHAIRMAN—There is obviously a layer of really good, quality brokers at all different levels that do a good job and then that proliferation, I think, of people just entering the market because they see it as easy.

Mr Gandolfo—Yes. So the banks have culled in that area, but it is quite right that they should do that.

CHAIRMAN—But the point of my question is that there has been no pressure borne by your sector to reduce your size or numbers?

Mr Gandolfo—No.

CHAIRMAN—You are not competing directly with the banks—

Mr Gandolfo—We do actually compete directly with the banks, but—

CHAIRMAN—But the banks could do it themselves?

Mr Gandolfo—They could do.

CHAIRMAN—It would save some fee at some point.

Mr Gandolfo—Yes. But we would like to say that, if the banks did that with the same degree of service, we would not have an industry. And we have a very substantial one. They acknowledge that themselves. We are competing with business bankers, so the business reps who are out there on the road trying to get commercial business are our competition. Quite often we deal with them and their own customers because they can service some aspect of the customer’s requirement and we can service other aspects of it.

CHAIRMAN—You made a very interesting statement earlier when you said you used to have 25 lenders and now you only have eight. That is a big difference.

Mr Gandolfo—It is a big difference. That is the main point to note. There are the big four and then you would have Capital Finance, Bank of Queensland, Macquarie Leasing and others who are of a size. There would be eight to 10 of those at the most. Then there are second-tier lenders and perhaps branded lenders like Case New Holland, people who actually manufacture product and have a finance subsidiary that offers finance to buy their product. But there are not as many of those around anymore and there are certainly a number of banks who are no longer in our space. Bendigo, Adelaide Bank and Suncorp Metway are no longer in that market. We hope they get back into it, but they are not in it at the moment. They simply exited the market.

CHAIRMAN—Can you give us some idea as to why they are no longer in that market? Why have they pulled out? Obviously they have made a commercial decision, but is it a sound commercial decision or are they being, again, too risk averse and just not wanting to play a role?

Mr Gandolfo—Kathryn, do you want to answer that?

Mrs Bordonaro—I think, with the GFC, they wanted to go back to core business. Some of the lenders exited the market because they were overseas corporations and they had their own issues to deal with and some of them wanted to get back to and sort out their own core business. Some of those lenders are looking at coming back into the market. But again it is about having the skill level within their distribution network or seeking a distribution network that can deliver that skill level.

Mr Gandolfo—There is another reason that specifically some of them exited the market and that is that the transactions that we write, the loans that we write, typically run from three to five years; so they run off reasonably quickly. So if you were to stop dead the lending in that market, you would still get a lot of money coming in, relatively speaking, principal and interest, over the next two years or so.

A couple of lenders in the market had very big commitments on property projects and other projects for which they suddenly had no funding. So there was a big stream of money coming in here from the leasing market, the equipment finance market, and they simply shut up shop on us so that the book would run off back into their coffers. There were two banks, or one in particular, where that happened.

CHAIRMAN—From what you have described, you really run almost an essential service between the borrowers knowing where to go and how to access funds.

Mr Gandolfo—Indeed, yes, we do.

CHAIRMAN—And lenders themselves and having that choice of lenders.

Mr Gandolfo—Yes.

Mrs Bordonaro—Lenders are very happy to have us because, if you have a look at the cost that we can bear as a distribution model, particularly to cover large areas where the population is not as high, we can deliver that. If they were to have a couple of sales people and they had to provide them with a car and then they have to have a human resources manager and you put in place the whole infrastructure, our ability to deliver that product means we are a much more efficient distribution network. So the banks are very happy to have us.

Mr Gandolfo—And we are paid for results. We cost them nothing unless we produce it.

Mrs Bordonaro—But I would really like to draw the attention of the committee to the phase 2 process that is going on.

CHAIRMAN—I am sorry, which one?

Mrs Bordonaro—Phase 1 is the new consumer credit laws that were introduced.

CHAIRMAN—Future financial advice and financial services, yes.

Mrs Bordonaro—It is the national consumer credit protection legislation. But in the fine print of phase 2 there has been slipped in regulating the provision of credit to small business; that has been slipped in under the consumer banner. The committee, the consultative group, that has been put together has no small business there; there is no small business representation. Small business deserves better than just to have a consumer piece of legislation cut and pasted across.

Mr ANTHONY SMITH—What has been the response to why there is that apparent glaring omission?

Mrs Bordonaro—There have been a lot of closed doors.

Mr Gandolfo—We had been told during the consultative process of phase 1 that we were to be included, and we were told that very specifically from Treasury. And that actually did not happen.

CHAIRMAN—I am conscious of the time, but you have raised that point and we can have a look at that and take that up.

Mr ANTHONY SMITH—I would not mind asking a question or two. I am more than happy to shorten if not extinguish our break that we have scheduled, given that we are here, because I think it is an important point and I see it more as a bureaucratic issue than anything else. Would you mind just taking a minute of time to take us through that. You were told that you would be included and the next you heard was that you were not to be, or were you advised that you would not be, or was it by omission?

Mrs Bordonaro—When the consultative process first started for the consumer market, we were very aware that this putting everybody in the one pot was happening. So we wanted to be proactive and we went and met with Treasury and said to them, ‘We just want you to be aware that this is who we are and this is what we do.’ It is a bit like, if you have a sore toe, you go and see the right doctor for that; you do not go and see a heart specialist. You do not lump all doctors in the one pot; everybody has their own specialty. We wanted Treasury to be aware of us. They said, ‘Yes, we’re dealing with consumer legislation, but if our focus ever changes we will be in touch.’ That was five years ago. The phase 1 process has gone through and they have now decided that they would like to look at the provision of credit to small business. We put our hand up and said, ‘Hello, we’d like to be included in that.’ We have made numerous submissions, we have made phone calls to the people that we first met with in Treasury, we have written to the various ministers in charge of the departments that are rolling out these teams and we do not get our emails or our phone calls returned. When I look at the make-up of that consultative committee, it is big banks, it is consumer credit advocates—who rightly should be involved in the consumer credit space—and it is mortgage-broking groups, but there is not a small business and there is not a commercial asset finance broker involved in consulting in that process.

Mr ANTHONY SMITH—And you have been offering on behalf of your organisation?

Mrs Bordonaro—On behalf of the organisation, we will give as much time as we can—and we want to be involved in the process.

Mr ANTHONY SMITH—And you have had emails, letters and phone calls over what period of time?

Mrs Bordonaro—’We’ll get back to you.’ We had an email from Treasury in November last year: ‘Thank you again for getting in touch with us. We’ll get back to you within a week.’ Two weeks later I rang them up, emailed, ‘How are we going?’ No reply.

Mr ANTHONY SMITH—Respecting the chairman’s wish to keep to schedule, I have one final question. The outcome has been that you have just discovered by omission that you are not included. Is there still an opportunity for you to be included?

Mrs Bordonaro—I believe that they have launched a green paper and we have provided a submission in response to that green paper. They have the consultative group together and I know that the consultative group meets on a regular basis. I do not know how far down the track they are because I am not involved in the consultation.

CHAIRMAN—How about we take it on board?

Mr ANTHONY SMITH—Yes.

CHAIRMAN—I am more than happy with that.

Mrs Bordonaro—Just as a quick example of how consumer credit can work out: if a consumer has the capacity to service a loan is one set of maths. You cannot apply that set of maths to a business situation. The way that income is earned, the way that expenses are incurred—all of those things that happen—it is completely different—

Mr Gandolfo—We all have clients who just would not have got off the ground if all those principles applied to them.

Mr ANTHONY SMITH—That has been useful.

CHAIRMAN—We will take that on board and we will make some inquiries and look at it.

Mr ANTHONY SMITH—Could you perhaps put in a supplementary submission?

Mrs Bordonaro—Certainly. I will give it a time line of how we have tried to be involved.

Mr ANTHONY SMITH—Yes.

CHAIRMAN—That will give us a better picture too in terms of what Treasury are trying to achieve through the way they have structured it and it will give us a fuller understanding. We really appreciate that. Thank you both very much; you have been very helpful.

Mrs Bordonaro—Thank you.

Mr Gandolfo—We thank the committee as well. Thank you very much.

[10.31 am]

GREEN, Mr Micah Andrew, Economist, New South Wales Business Chamber

ORTON, Mr Paul, Director, Policy and Advocacy, New South Wales Business Chamber

CHAIRMAN—Welcome. I would ask you to make a short introductory statement.

Mr Orton—We welcomed the opportunity to have made a submission to the committee and we welcome the opportunity to appear here today. Perhaps just as a bit of background on what New South Wales Business Chamber is, we are, I guess, the largest business membership organisation in New South Wales. We are affiliated with 120 chambers of commerce around the state and there are about 14,000 businesses in that group. We have another 5,000 direct members and there are probably a total of about 30,000 employing businesses across New South Wales affiliated with the chamber in one form or another. We are a member of the Australian Chamber of Commerce and Industry, which represents about 350,000 businesses across the country. I guess, like everyone, we cannot help but keep acknowledging the critical role that small businesses have in the Australian economy. We all know the numbers. There are about 730,000 of them that employ people and there is probably a total of about 4.9 million in that employee group.

The key points we want to make are that reduced competition in small business lending arising both from finance sector consolidation and the reaction to the GFC has impacted negatively on small businesses access to finance; that the recent measures by the government to encourage lending competition, while welcome, need to be bolstered; that, during the time that it takes for a more competitive environment to develop, government jaw boning—and we can talk about that a bit more—should focus more on the performance of the financial system in dealing with small business lending and perhaps a bit less on residential mortgages or perhaps leave it where it is on residential mortgages and up the ante or comment on the performance of banks in responding to the needs of small business.

Residential mortgage backed security changes and additional funds, we believe, should be more closely tied to small business lending. We also believe that a temporary small business loan guarantee system, self-funded, would help take up the slack while the economy adjusts to the post-GFC environment. Finally, we think it would be worth while for the Productivity Commission to spend some time looking at how the small business lending system works and opportunities for improvement.

So while the issue has been a big one for small business for some time, the GFC obviously exacerbated existing difficulties that small business has in accessing finance. While some might suggest that credit was too cheap and easy prior to the GFC—

CHAIRMAN—And some have.

Mr Orton—Yes—it is equally true that the reaction to the GFC has gone, in our view, too far the other way. Our members continue to identify access to finance as an issue. Our most recent survey conducted towards the end of last year found that 22 per cent of small businesses, those employing fewer than 20 people, reported that conditions had got worse in trying to access finance while only four per cent said that things had got better. These findings have been reinforced through a survey we have been collaborating on with the Victorian university of about 1,000 businesses around Australia. The small business component of that said that 49 per cent of those that had applied for finance in the last two years had been unsuccessful on at least one occasion and 19 per cent had been completely unsuccessful in sourcing funds. Of those who had not been able to, 86 per cent thought this had constrained their business growth and 42 per cent said that it had probably increased their risk of bankruptcy. This survey also found that access to finance was a bigger obstacle to growth than labour market regulation's inadequate infrastructure and recruitment and retention of affordable labour.

Of course, costs of finance have increased significantly for small businesses. Spreads have blown out from around 200 basis points to around 400. While they have traditionally been more expensive than mortgage lending, the gap between the two has increased from about 65 basis points pre GFC to around 185 at the moment.

Mr ANTHONY SMITH—That is the difference between mortgage lending and—

Mr Orton—And small business lending rates. That lies at the base of our point about government statements about what needs to happen on the part of banks following interest rate decisions. More generally, that still tends to focus on residential mortgage rates. For obvious reasons that should continue to be the case; we just think that small business lending conditions need to be elevated in priority. Obviously the total volume of business credit has been falling recently. All this has meant that our members, both directly and through surveys, have quite vociferously let us know that this is an issue and that they are looking to their representative organisations to take up the cause. I will leave it there. Perhaps we can take some questions.

CHAIRMAN—Thank you. You have given us a good picture, a good idea, of how difficult it is. There is a view that, pre-GFC, money was too easy to get right across the board, by consumers as well as commercially, and that the GFC has redressed that. Maybe it has gone a bit too far; I think we would all agree with that. Can you give us a better idea of whether or not you think money was a bit too easy to get and commercial risk was not adequately measured? Perhaps now we are at a point where it is more balanced and is closer to where it ought to be—would that be your view?

Mr Orton—I do not have any specific evidence to support the view that conditions were too loose and lax pre-GFC. But the consensus is that perhaps that was the case. If so, the reaction post-GFC—and that is what we are dealing with right now—right at the time that businesses need finance to take advantage of glimmers of growth, is really where it is hurting.

CHAIRMAN—Obviously commercial lending is risky; there is no question about that. Do you find that your membership do not have the skills, are not adequately prepared or do not have a good understanding of how to access funds, rather than just finding it difficult? Do you find that is a really big issue?

Mr Orton—Yes. We find information deficiencies and differing rates of capability are issues on both sides of lending transactions. There is always more that can be done to improve the ability of small business to get across their business opportunity and prospects to a prospective credit provider. There is always room for that. Equally, we think there is room for improvement on the part of credit providers; they could do more to evaluate individual loan applications than simply applying a sectoral or regional template that they have developed as part of their credit systems.

To their credit, some of the banks have improved their capacity within regions. We saw a huge move out of regional banking and we are now seeing some tentative moves back into it; we can only endorse that. But there is still, in our view, a need to improve the capacity of banks to consider slightly difficult and out-of-the-ordinary proposals—proposals that involve, say, export or bringing a new product to market. They are the trickier ones to deal with and the ones that we think our proposed loan guarantee system could help with—proposals that are just a little bit outside of the banks' own criteria.

Mr ANTHONY SMITH—At this point, would you like to expand a bit more on that proposal and perhaps let us know about any overseas experience?

Mr Orton—Yes. I might ask my colleague Micah to speak to that.

Mr Green—Our submission talks about our proposal for a guarantee in some detail. I will not go through it all again; I will just make a few basic points. We would really like to see the introduction of a temporary government guarantee of small business loans. We foresee that working as a self-funded model, where the government would provide the option for banks to offer a loan product to a small business with some part of it guaranteed by the government. In return for that guarantee, the government would collect a fee as a margin on top of the interest rate, which would then be paid by the small business. That premium would reflect the risk to the government of that guarantee being called upon. In that way, we would expect, over time it would be broadly revenue neutral on the government's balance sheet.

To address potential risks about moral hazard, there is obviously a risk that if banks had a carte blanche guarantee they could offer it to anyone under the sun. In order to address that, we feel it would be important for the banks to continue to have some skin in the game by placing a cap on the amount of individual loans that could be guaranteed. You could also place a cap on the proportion of guarantees that any one financial institution could call on across its suite. We think that, by having a priced, market based product guarantee, it would be taken up by small businesses in the current environment, where conditions are very difficult for some to access finance. Over time, as competition returned to the market, paying the premium for the guarantee would become inefficient for the banks to charge and for small businesses to take up, so it would naturally wind itself down. Once it was clear that it was no longer a useful product and no longer needed, because banks were more accurately pricing risk, it could then be wound up.

CHAIRMAN—Thanks for that. That is predicated on the key principle that there are surplus funds in the market and that, under whatever guarantee system, there are surplus funds available to lend out. This is one of the questions we are really asking: has the market changed post-GFC so that the pie has gotten smaller? In fact, because there are fewer lenders, less funds and less access to funds, if you have less to lend you tighten the criteria and you are more selective, choosier, pickier. Is there any idea of the amount of funds that are available, regardless of what guarantees are in place, or would you be guaranteeing, in the end, the same people who are getting funds today?

Mr Green—It is certainly true players have left the market post-GFC. I think it would be a fair assumption to make that, even though a lot of the majors seem to be talking the talk about being out there lending, and lending more than they were before, the aggregate pool of funds may be smaller now. Perhaps the growth in funds that occurred prior to the GFC has stagnated now, so the supply-demand imbalance has become a bit more obvious. We would say that pricing a guarantee and allowing the banks to manage this risk properly might shift funds from one part of the market to another and allow more funds to be available for small business lending. So we still see it as useful in that regard.

CHAIRMAN—It does raise some issues in terms of the size of the market, the funds available and trying to encourage and grow that pool of funds. If you did that, through whatever mechanism—whether it was a market mechanism or whether in the end government stepped in and used a guarantee mechanism—it is not certain that that would give any further confidence to the banks; it might be something that already exists because of the high-quality processes and tougher selection criteria now.

Mr Green—We certainly agree that there are multiple angles that need to be taken, and a guarantee would not be the single solution to all the problems. The keys to getting things back in the longer run are increasing the size of that funding pool and getting the competition to return to the market. There are other policies, and we welcome some of the government interventions. The additional support from RMBS has been welcomed as a way to get additional funds into the market. We just see this as one pillar of a range of responses that would help out.

Senator STEPHENS—You have mentioned on page 5 of your submission that there are three examples of this kind of a guarantee: the UK, Canada and the United States. I wonder whether you could tell us a little more about those three approaches. How long have they been in practice? How long have those guarantee systems been in place? Has there been any evaluation of how effective they have been or whether they have created a better environment for small businesses.

Mr ANTHONY SMITH—Adding to that very good question, perhaps you could tell us what the plans are for the future life of those guarantee arrangements?

Mr Green—We set out the three examples—the UK, Canada and the US. That is not an exhaustive list. I cannot think of the others off the top of my head, but I understand that countries like Singapore and Korea also have similar products. While our submission does not cover it in as much detail, I believe that ACCI's submission has a lot more information about the backgrounds and histories of those programs. So I have to say that I do not have all that information on hand. My understanding is that the UK, Canadian and US schemes have all been run for a significant number of years and were in place well before the global financial crisis.

Mr ANTHONY SMITH—That was what I think the senator was getting at.

Mr Green—Certainly the UK program, I believe, was augmented and expanded—

Mr ANTHONY SMITH—Souped up, yes.

Mr Green—Yes, in response to the GFC. I am not sure exactly what the overall perception is, but certainly our communication with fellow chambers in the US and the UK has indicated that, as far as they are concerned, the view of their members is that these arrangements have been helpful in assisting the securing of funds.

Senator STEPHENS—It would be helpful if you were able to put your hands on some sort of evaluation or reporting on the impact and effectiveness of those arrangements. That would be helpful.

Mr Green—We can certainly take that on notice.

Mr ANTHONY SMITH—You mentioned the ACCI submission. We had ACCI before us on Wednesday. Their submission says that, in the United States, in small business administration, US government agencies have provided support for small business since 1953. That might be something—if you have further information on that—

Mr Orton—Yes. It is not as though there is not a precedent in Australia. The export finance insurance schemes, the EFICs, really run on pretty much the same principles—self-funding.

Senator STEPHENS—You mentioned the Victoria University survey?

Mr Orton—Yes.

Senator STEPHENS—It would be helpful if you could provide the questions in that survey. They would be quite interesting.

Mr Green—I will have to get back to you on that. I certainly should be able to track that down. I am in touch with the researcher at Vic University, who is still in the process of finalising his report. But I should be able to get my hands on those and provide them to the committee.

CHAIRMAN—You have access to a lot of small businesses and medium enterprises through your chamber. As a general view, how do you interpret where lending is today? How much impact is it having on firms attempting either to maintain or grow their business? How much effect is being—

Mr Orton—I think, based on the Victoria University survey and our own feedback from members, the impact is considerable, particularly for businesses that are looking to grow and do things in the post-GFC phase that we are in at present. Access to finance has been a waxing and waning issue over the years—during my time at the chamber from the mid-90s onwards it has peaked and troughed. But certainly the peak that we are at now is the most intense I have experienced in my time at the chamber. Not every business is experiencing difficulties. You do not necessarily hear from businesses that are trying to get more finance. Rather you hear from businesses which, in order to maintain their existing finance lines, have been required to stump up more collateral. Being fairly blunt, one suspects lenders are applying a template rather than looking at the individual merits of a business. Taking into account existing lines of finance and those who are looking to expand and do more, which we need to encourage in the post-GFC phase, it is a substantial issue.

CHAIRMAN—Do you know of any cases where businesses have decided not to reapply for funds or not to apply for further funds they need through fear of being reassessed and re-evaluated and having all their assets revalued?

Mr Orton—Certainly one of the responses from the Victoria Uni survey is that quite a large number have had applications rejected. I am not sure whether we obtained data on applications not made in anticipation of being unsuccessful.

Mr Green—We did get a number of respondents indicating that they were not looking at the moment because they thought they would be unsuccessful and that it is too hard. But I do not have specific case studies illustrating that point—the fear that they will turn up and the bank will then show attention to them and tighten their criteria.

CHAIRMAN—I would be interested if you could go back to your membership during this inquiry and report back to us as soon as you could—

Mr Orton—Yes.

CHAIRMAN—on that issue, but also on whether there are any instances of businesses that have actually gone to their bank, looking either to adjust their finance or to refinance, and found that, through doing that, they have damaged their business—whether they found that their assets had been revalued lower and that that has caused them hardship. If you have an example now and you could tell us a little bit about it, that would be great. If not, we are certainly keen to hear from you.

Mr Orton—We will come back to you, yes.

CHAIRMAN—I have certainly heard anecdotes about successful businesses in the normal course of operation—

Mr Orton—As have we. We will document that.

CHAIRMAN—These were businesses that were planning to grow or which thought they were in a really good place in their business cycle—and this is post the GFC—but which, when they have gone in to refinance, have found that the bank has reassessed values, rebalanced their liabilities and assets—

Mr Orton—Certainly falling property values have been an issue, yes.

CHAIRMAN—I know of specific cases. People have come to me and said that it actually killed their business—seeking refinance actually destroyed the business. So I would be very keen to hear of specific cases, if you have them, which could give us some indication of where that particular system within the banking sector has failed.

Mr Orton—Yes.

Proceedings suspended from 10.54 am to 11.01 am

BECKETT, Mr Ian, Principal Adviser, Financial Systems Division, Treasury

DEITZ, Mr Andrew, Manager, Infrastructure, Competition and Consumer Division, Treasury

LONSDALE, Mr John, General Manager, Financial Systems Division, Treasury

MURPHY, Mr Jim, Executive Director, Markets Group, Treasury

CHAIRMAN—I welcome our next witnesses from the Treasury. Mr Murphy, do you have any opening remarks?

Mr Murphy—Thank you for the invitation from the committee to appear. I think the starting point is that access to finance for small and medium business is a very important issue for the Australian economy. It was really one of the key issues that we were involved in, during the GFC and post-GFC, to ensure that there was appropriate access to finance. Small and medium enterprises are an important part of the Australian economy; they make a significant contribution to employment, productivity and value-added. According to the ABS, they accounted for 58 per cent of total value added by industry in 2008-09. Access to finance is important, allowing SMEs to maintain their significant contribution to the economy and to allow them to grow. The availability of reasonably priced credit allows SMEs to expand their activities, fund new and innovative investments, smooth cash flows and maintain employment.

Our submission concludes that the stock of lending to SMEs in Australia has held up relatively well since the onset of the financial crisis, especially compared with large business lending, which fell dramatically. Rates of new lending have remained broadly consistent with long-term trends. This suggests finance has generally remained available to credit-worthy SMEs.

The key difference since the crisis is that the cost of loans has risen. This reflects higher funding costs for banks and increased risk aversion on the part of lenders. During the financial crisis the government took action to maintain the lending capacity of financial institutions, including to the SME sector, through the introduction of deposit and funding guarantees as well as direct investment of up to $16 billion in the securitisation market. It also provided direct support to SMEs through a range of measures, including small business advisory services, the small business and general business tax break. It provided cash flow relief to eligible small businesses by reducing their pay-as-you-go tax instalment obligations. We set up a small business assistance program and we supported cash flowing into small business through the government’s guarantee of on-time payments for new small business contracts of up to $1 million with government departments.

As you are aware, in December last year the Treasurer announced a package of measures to enhance the competitiveness and sustainability of Australia’s banking sector. This package included specific measures aimed at improving SMEs’ access to reasonably priced finance by enhancing the capacity of lenders to raise the necessary funds. The government has also announced a further $4 billion in support for securitisation markets. It has also announced that ADIs would be permitted to issue covered bonds. We think we could anticipate that SME business conditions will improve as the economy recovers. Lending to SMEs is expected to continue to grow, with competition improving as some lenders are forced to scale back their activities as a result of the crisis as they re-enter the market.

In summary, I think we talk about reasonably priced credit to SMEs and we also talk about creditworthy SMEs. We have some statistics that my colleagues could take you through, if you need them to, on what we have garnered from the banks about the stock of lending and interest rates, and the rates of lending to SMEs compared to the cash rate. It seems to be that when you look at that there has been a consistent increase in the price of funding for SMEs. But it is post the GFC. Why has that occurred? We think that the banks themselves or the lenders have become—maybe you could call them—risk adverse, but at the same time it is more likely than not that they are pricing in risk much better post-GFC than they probably were beforehand. I will conclude on that and I am happy to answer questions.

CHAIRMAN—I will start in the same way as I did with the others. There is a view in the CPA Australia submission that pre GFC perhaps credit was too easy, certainly in a range of areas—in the consumer market and perhaps also in the commercial market—and that now it is too hard. I am just wondering about your view in terms of the balance between the pre GFC environment, in terms of how relaxed lending rules or lending criteria and requirements were, and now and whether that pendulum has swung too far.

Mr Murphy—Maybe my colleagues will comment. We have some analysis here. I do not think it is like a swing from black to white. Yes, there may have been a factor of profit lending or easy credit going into the GFC. But, when you think about it, the real area where the GFC affected Australia in terms of lending was lending to major corporations who had poor business models. I am talking the Centros, the Babcock and Browns. That was the major problem. I do not think that lending to small business in Australia was excessive.

Coming out of it, we think that where lending has been restricted and tightened up is actually in the lending to the bigger end of town, the majors, especially on the speculative side, whereas, from what we can see, yes, the price of funding has increased for SMEs but it has increased, taking account of the cost increases on obtaining funding by the lenders. In the international markets—we have gone through this in the banking competition side—that has increased. The borrowing costs have increased. That is a fact of life. That is going to flow through to their lending practices. From our analysis, it does not seem, from what we can see, that the banks are adding on or are excessive in what their lending rates are.

Yes, maybe it is tougher to get finance, but that is taking account of external factors. It is not an aversion of the banks. They are not saying, ‘We’re not interested in small business,’ or anything like that.

Mr Lonsdale—Can I add, just on a quantitative side, to what Mr Murphy was saying? On pages 6 and 7 of the Treasury submission it goes through quite a bit of discussion about pricing and restrictions on credit. When we look at pricing before GFC and now, on average what was being charged for small business was about 205 or 210 basis points above the cash rate prior to GFC; around the end of last year, it was probably just over the 400 basis point mark.

Mr ANTHONY SMITH—Are you referring to charts 3 and 4?

Mr Lonsdale—Pages 6 and 7 of the Treasury's submission, which talks about the price and conditions. As Mr Murphy said, that is pretty much driven by two factors—the high risk that has been built into that pricing and really a switch from probably some cheaper forms of funding, which may not exist as much now, to more expensive funding—for example, deposits and longer term wholesale funding.

Mr Murphy—I suppose that is the good point. We have been particularly concerned with the demise of the securitisation market, and that was a good funder of small business. The regional lenders especially—lots of representations have been made to us by institutions such as the Bank of Queensland and Suncorp and smaller lenders which may be closer to the market—have been affected by the demise of the securitisation market. That is why in the banking package we are pushing to try to revive the securitisation market and to try to get a corporate bond market going, because we think, again, that will provide funding.

CHAIRMAN—There are probably two concepts out of that. One is the concept: is the pie smaller in terms of funds available? There seem to be plenty of people saying that it is—that there are less funds available in the market. The other one is: if it is or is not the case, the requirements from lenders have tightened up. They are using a tougher set of criteria to lend. That is certainly what we are hearing. We are getting it in submissions and anecdotally, from talking to people on the street and in small business. It seems to be consistent across the board. If it is different, please tell us.

Mr Murphy—No. That is probably right. What we would be concerned about would be if it was an overreaction. You have got to think about it. The GFC was a huge shock to the financial sector. People have taken that on board. APRA is on its game, making sure. So, yes, it probably is tougher, but credit-worthy businesses can still get funding. As well as that, there was the phenomena coming through where businesses themselves pulled back a bit to avoid getting into too big a debt situation, because they also were affected by the GFC and the concerns there, when you look globally, about the number of businesses that were failing. On your latter point, yes, it is probably a tougher funding environment. We would agree with that.

Mr Lonsdale—I think that is right. I would point to page 4 of the submission. It is a difficult question to disentangle. When you look in aggregate at the total credit outstanding for small business, it has been pretty flat during the GFC. In fact, it has probably ticked up a little bit now. What about the demand and supply factors? As Mr Murphy said, some small businesses might have pulled back; some might be repaying debt. On the supply side, we have seen some indications, particularly lately, from some of the major banks that they want to have more small business lending. It is difficult to disentangle. The anecdotal evidence may well be different to some of the top-down, aggregate information.

CHAIRMAN—Certainly from my perspective—I am sure it is the case for other members and senators—we have received more inquiries about why it is so difficult for people to access funds. Some people had longstanding records, with 20 years in business, and had not had any particular problems in the past, but in the post-GFC environment the banks were not even prepared to look at it, and were just saying, 'No, we're no longer interested,' or the criteria were so tough that they really could not meet those new criteria. There seems to be a fear from small business as well, which is being relayed back to us, about going to their bank, just in case things are revalued.

Mr Murphy—Revalued and the loans are reassessed.

Mr Lonsdale—We talk a little bit about that in the submission. There is repricing. Banks do look at small businesses, factoring in more risk.

Mr Murphy—I suppose the answer to that is that one would hope you do not get an overreaction. When funding markets stabilise, which they sort of have, one cannot escape the fact that it is more expensive to borrow in the international markets. Lending by institutions is a business. To some extent it can become a very lucrative source of profit for financial institutions. They are not going to walk away from it. If the general economy is in good shape, SME finance will be available.

CHAIRMAN—Has the pie, the availability of funds, shrunk?

Mr Lonsdale—I do not think so. In aggregate, I do not think you can conclude that. There is the issue of what is a small business.

CHAIRMAN—It is one of our questions.

Mr Murphy—Yes.

Mr Lonsdale—So when you look at RBA data on the total amount of stock of credit outstanding, small and large—we have that on page 4 of the submission—it looks pretty steady.

CHAIRMAN—It just seems counterintuitive, given what has taken place and the anecdotal evidence that we are receiving about access and quality of applications and so forth.

Mr Lonsdale—Yes. But it is probably the case that there are distributional things happening underneath that data. So some small businesses may be finding it more difficult, whereas for others that is not the case.

CHAIRMAN—On the competition side of that, there obviously is less competition and there are fewer players in the market. Some have exited the market completely in particular products and particular types of lending. Some international banks have left. So is it the view of Treasury that there is less competition in that sense in the market today than there was pre-GFC?

Mr Murphy—There are various angles on the competition thing. I think you could say there might be some players that have exited the market, but we have over 120—

Mr Lonsdale—Table 1, page 4, basically outlines that there are still a lot of providers in the market and a lot of products, notwithstanding the point that players have exited the market and there has been more concentration.

Mr Murphy—The contraction of lending services is more to do with securitisation and those issues.

Mr Lonsdale—Yes. Pay whenever you want. Just jump in.

Mr Murphy—Securitisation and trying to get back that diversity of funding sources so that it is all not dependent on the major banks.

CHAIRMAN—Certainly what we are hearing from other submitters is that their access to the number of lenders has reduced massively. For example, from previous witnesses we heard that, from 25 available lenders in their market, the number has gone down to eight for the products they deal in. That is a significant lessening of competition. I am wondering how that carries across, if we are looking at the broader pool of small to medium enterprise.

Mr ANTHONY SMITH—If you take the Chair’s question, it is possible, Mr Lonsdale, is it not, that you are both right. On the face of it, the number of providers, notwithstanding some departures at a national level, might look competitive, but then when you get to regional areas it might be, particularly if they are the critical departures, much more of an issue.

Mr Murphy—The regional banks are still hanging in there. They have done reasonably well. It is the ones where you may have found that there has been an impact. We know it is in the finance company area. They were heavily affected by the GFC and they lent—I would not say to the more speculative end but the more—

Mr Lonsdale—The risk area.

Mr Murphy—The more risky area, the finance companies. So what you may have found was that you would go to the traditional sources of lending—by that I mean the banking institutions and that would mean probably cheaper finance—and they would probably get the best of the credit risks. Credit risk companies, at the more speculative end of the SME area that would have traditionally gone to finance companies, might have been finding it more difficult. That has been a contracting area.

Mr ANTHONY SMITH—We have had some witnesses and some submissions earlier today and on Wednesday, I think, advocating a guarantee of small business loans in reference to the system that operates in the US, the UK and Canada. Would you be able to give us a Treasury perspective, I suppose, on the history of these, the operation of them and what you perceive, I suppose, is their effectiveness, really?

Mr Murphy—It is on page 11. We looked at this during the GFC because, to be fair, the critical concern of the government was SME, given the employment arrangements there. We noted at the time, as we have set out here, a number of OECD countries had gone into this space of guaranteeing or giving direct assistance to that sort of business.

Mr ANTHONY SMITH—Some had been even beforehand—

Mr Murphy—Yes, they have always been—

Mr ANTHONY SMITH—They souped it up a bit.

Mr Murphy—Yes. We would think that that is not good policy, to be blunt. We looked at this and in terms of policy we were quite concerned and looked at various schemes—

Mr ANTHONY SMITH—A bipartisan study or assumption, as you would have looked at everything?

Mr Murphy—Yes, but particularly small business funding and small business loan guarantees. We can answer more. What surprised me was—and I do not know whether we mention it here—was that there was some OECD work that came out post-GFC which reported that the UK and the US schemes had been ineffective in supporting small business. That was some solace to us, because we looked at all these things and pulled back from recommending to the government we should do something. The government said to keep looking at these things. We can find you that. I am pretty certain it was reported that they were not effective.

Mr ANTHONY SMITH—That is a key point.

Mr Lonsdale—They were not effective.

Mr ANTHONY SMITH—I would not mind getting your perspective, Mr Lonsdale, because I know you have worked in this area. I read in one of the submissions, particularly on the history, that the US has had something since the 1950s. Let me be blunt. Can you fill in some of our gaps in knowledge, like what I think the Bush administration, I suppose initially, did in terms of boosting up in this area? Where are some of them at now?

Mr Lonsdale—I think we can come back on the chronology. We are happy to do that. To be honest, I cannot take you through the chronology from 1950 but I can certainly come back.

Mr Murphy—The other thing is that, once you do this, then everything reacts. If you guaranteed small business then, right, does that lead to the risk of the guarantee shifting to the government from the banks, because why not lend?

CHAIRMAN—It becomes priced into the market, does it not, and the market reacts accordingly?

Mr Murphy—It is a distortion, you see. That is your problem.

Mr Lonsdale—There are four dot points here that basically outline our key arguments. Our thinking has been probably twofold—that a better way to think about it would be to have a more competitive environment, if you can do that; and secondly, to make sure that regional lenders in particular—but not just regional lenders; big banks as well—have got a sustainable funding model and that goes to, again, securitisation, covered bonds and other things.

CHAIRMAN—The more competitive environment is the key part of what we are trying to better understand. What does that mean? What is it? Is it the number of lenders? Is it the size of the pool of funds? Is it just the rate? Is it the number of products? There are lots of variables. How do you see a more competitive environment?

Mr Lonsdale—I think it is every one of those things that you mention. I do not know of one definition of competition. Sometimes people look at concentration in the market. But that is just one. You have to look at the range of products, the number of providers. Spatially, are they in regional areas; are they in city areas? Then there are the different sorts of products and flexibility. All those things are important.

CHAIRMAN—How do we encourage that? How do we drive that?

Mr Lonsdale—One way to think about it is for you to have a market operating as flexibly as it can within the necessary regulation that you need to have in place in a financial system but to be careful, I guess, about putting roadblocks in place. We need to try to have the market determine what are the best options. That would be the general philosophy.

CHAIRMAN—The key thing for us in this inquiry—and we acknowledge there have been a number of inquiries in this space—if we are really going to look at how to improve the lot of SMEs and their access to finance, and obviously thereby competition, is: where do we drive this debate? How do we improve that market? I know in your submission you talk about interest withholding tax and improving things there. How much impact does that have, for example, in terms of allowing foreign currency, foreign funds, into our market? We saw in the Johnson review the concept of an Australian financial services hub.

Mr Murphy—People have argued strongly to us that a withholding tax is an impediment to business operating and so I think it is good policy to start to reduce that over time because that is what people are saying. You have got to do it; whether the money flows once you reduce it is another question.

Mr Lonsdale—It would certainly remove the barrier, if nothing else.

Mr Murphy—That is right. I think the whole thing on SME finance—and we can keep looking at it and all that—is that I think it should be at the forefront of government’s mind to ensure that there are proper funding arrangements in place. There is no harm in having inquiries and putting the pressure on lenders to make sure that they are looking critically and sensibly at their own lending practices. I think with SME lending it is going to reflect the general state of the economy and if people are confident and feel that now is the time for investment, they will go and seek funding. The financial institutions will lend. So I think it is very much tied to the state of the economy. I suppose that is just obvious, but it is worth saying.

Are there any specific measures that can be done particularly for SMEs? As a result of what we tried with the government on securitisation and with the assistance of AOFM, of the $16 billion there the government earmarked a large part of that to SME financing. What we are hoping, in terms of policy, is that the securitisation picks up and replaces that. There has been, in effect, an intervention by earmarking a large part of that $16 billion to four institutions to lend to small business. So an issue for us at the moment is that if you withdraw that you want the private market to pick it up.

Mr ANTHONY SMITH—To move in, yes.

Mr Murphy—That is an issue, but we still have not resolved it. You want the private market to pick it up. That is why it is very important that the private market accepts their responsibility. We are not saying that they should not be making proper assessments on lending.

Mr Lonsdale—Since we have got onto that issue, things have improved from a couple of years ago but they are still very fragile.

Mr Murphy—We do not see this as a given.

Mr ANTHONY SMITH—Some of it is time.

Mr Lonsdale—Yes, that is right.

Mr Murphy—So at the moment there is already government support there, indirectly through the securitisation. It is when we take that away. The Treasurer has announced another $4 billion in the package. What time would that take us through to?

Mr Lonsdale—Currently they have used about $12½ billion or $13 billion of the first two tranches of $16 billion. So it does depend on market conditions.

Mr Murphy—Yes, it has got another four.

Mr Lonsdale—But you would think it would go through this year easily.

Mr Murphy—And then the four come—

Mr Lonsdale—Yes, to the four on top.

Mr Murphy—Yes. So I think the question for us is still whether the private market can step into the space.

Mr ANTHONY SMITH—Is there any indication that that is the case, that that is—

Mr Murphy—Yes.

Mr ANTHONY SMITH—You would argue increasingly, as time goes on?

Mr Murphy—We hope so. But you have seen that securitisation was a major source of funding in this area. You just had—was it Westpac or the Commonwealth?

Mr Lonsdale—Westpac issued one billion dollars of RMBS very recently. That is not supported by the program but it is an indication that the players are coming in and accessing the market. That is a healthy sign. I think you mentioned time as well. It is important when you are looking at the measures that have been announced, that a number of them have not actually taken effect yet. IWT is one; covered bonds are another. A range of things are in the pipeline that will add to competitive pressure but they just have not flowed through yet.

Mr Murphy—I do not want to get back onto exit fees, but the government expressed a view on exit fees and, bingo, even just talking about it, you have got action by ANZ and NAB. They listen, to some extent, to the policy debate and they start to question their own practices and remove things which they really do not need. They can organise themselves differently. I think

SME finance is a very important issue and we are very much apprised of that. At the moment we are supporting it, to some extent, and what happens afterwards—

CHAIRMAN—Do you get a sense from lenders that there is too much attachment between what they do at the mortgage market level and the small to medium enterprise level? The links between the two are quite close, but often a small business will have their mortgage intertwined with their business. Does that pose an issue, particularly for smaller businesses, in terms of having those two very separate markets for people borrowing for a home and borrowing for a business?

Mr Murphy—There has always been the argument in Australia that the finance institutions are making easy money because they are lending to mortgagees and they are not lending to SMEs, right. It seems that there is a trade-off here in that lending to small business is profitable for them. The banks can talk about that, I suppose, but we would say it is more profitable for the banks to lend to small business. At the moment there seems to be a decline in appetite in the community for mortgage financing. We are starting to see it taper off a little bit.

Mr Lonsdale—Recently, yes.

CHAIRMAN—It is equity-type financing or—

Mr Murphy—No, there has just been a cooling in the housing market. So one would think that lending programs would then swing more towards where there is business to be made.

CHAIRMAN—But it is not the case, though?

Mr Murphy—I do not know. Again, it may be a timing thing. If there is a reduction in demand for housing finance—these are lending institutions—they are going to go more into business lending.

CHAIRMAN—It seems to me, on the surface, that the lending market has shrunk, and the banks or lenders are not necessarily chasing more business because they are making bigger margins. Their profitability has been maintained or increased, but their activity has not necessarily matched that.

Mr Murphy—There would be some stuff on margins.

Mr Lonsdale—We have a bit of stuff on margins, but it would be worthwhile putting that to the banks, I think. On page 5 of the submission we point out that NAB and Westpac in particular, and a few of the small lenders, have come out in the last few months and particularly highlighted small business as an area where they want to increase.

Mr Murphy—Yes.

Mr Lonsdale—That would be worthwhile teasing out with them, I think.

CHAIRMAN—It can be the case. Certainly, you can sometimes make more profit by doing less, taking less risk and just being less active. I am certainly interested in whether there is any data on that. After speaking to a number of lenders, such as the big banks and a number of people in that area, the competition within the market before the GFC was that you literally had to steal the customer from the bank next door to ensure you got their business, regardless of how much it cost you. So they were prepared to wear less and less of a margin and be ultra-competitive in that because it was a very competitive environment. But now that there are bigger margins to be made and safety in lending conditions and criteria, and that has maintained profits and sustainability of the business without necessarily chasing or even supporting continued growth in SMEs.

Mr Beckett—There has been a recent uptick in the total level, from an aggregate perspective, in the level of credit outstanding to SMEs. I think we are not arguing in our submission that there has been a reduction in credit to SMEs. It is more the pricing issue, and again that reflects funding and just different perceptions of risk after the crisis compared to before the crisis.

CHAIRMAN—This might be about how you define it, if the aggregate market has actually picked up, as you say. What we are hearing is that maybe a particular segment of the market is finding it more difficult than others. It might be a definitional problem.

Mr Murphy—There is a chart on page 5 and the bottom line is the SMEs. The lending in 2007-08 to the Babcocks and the Centros and whatever is reasonably consistent.

CHAIRMAN—It seems like a small but constant increase over a period of time.

Mr Murphy—Yes. There is a little drop there. It would be interesting if we got numbers to go with it.

Mr Beckett—I think that is the point. The RBA makes a similar point in its submission.

Mr Lonsdale—The other split that we looked at in the submission was on the agricultural side for small businesses. It is a similar sort of story. In aggregate it has been okay, with a steady sort of growth. We have not seen a tick down; it has been quite steady. Certainly recently, compared to other sectors, it has been okay, and probably a touch higher—notwithstanding the volatility in the agricultural sector.

CHAIRMAN—With the definition of a SME, it seems that there are multiple, varied and many. You have one; we have one. It seems everybody has one. Each bank might have a slightly different view. Does that pose an issue for regulation or criteria?

Mr Beckett—I do not think it does.

CHAIRMAN—Are there any issues maybe just for information and data?

Mr Lonsdale—On page 2 we set out some of the definitional issues. As you point out, there are lots of them. We tend to focus in this submission on the Reserve Bank's definition, which is where you have credit under $2 million. But the tax office has a definition and there is also an employee definition of less than 200. In terms of particular issues, our view is quite a broad one, so we will look at lots of different measures and try to draw conclusions from that.

Mr ANTHONY SMITH—You have them all there—a couple of pages worth.

Mr Lonsdale—I do not think there is a clear answer just because of the diversity of small business. It is very hard to come up with one.

CHAIRMAN—Clearly then, you are saying that it does not have any particular adverse impact or that it is not of any real consequence. Do we really need a singular definition of small or medium enterprise?

Mr Murphy—I suppose from the institution's point of view—you can test it with them—it is probably the size of the loan you are looking for. They determine whether it is a small business or a big business by how much you want.

Mr ANTHONY SMITH—Effective full-time employees can vary. If you have a pizza shop, for instance, it is lots of employees who want to do shift work only. It could be quite a large number, but it still is a family business nonetheless.

Mr Murphy—With SMEs, it is not an exclusive definition. It is just a guide.

Mr Lonsdale—When designing policy typically, whether it is tax policy or regulatory policy or whatever it is, you always take a broader view—it is not so much the definition but whom it is that you want to direct something to.

Mr ANTHONY SMITH—You might remind me—how do the capital gains tax small business-specific measures work?

Mr Lonsdale—We would take advice from our revenue group people on that. A lot of work has been done on the tax side to try to streamline the definition of small business.

Mr ANTHONY SMITH—Yes. Could you send us something on that—not that it is going to be a big focus? I think the chair raised it. Ultimately, in any report we will have to address this issue.

Mr Murphy—The National Australia Bank defines SMEs by using three bands of annual turnover: two to three, three to five, and five to 10.

Mr ANTHONY SMITH—I am sure it is turnover based—in that area, anyway, it is an indication of the size of the business.

Senator STEPHENS—On a slightly tangential issue, we had evidence this morning from the mutuals and credit unions representative around the government's undertaking in relation to the Bank on a Better Deal campaign. We had a discussion then about who might be overseeing that campaign, the authority with which the campaign would operate and the importance of consumer education around financial literacy and these issues. Does Treasury have a view? Would it be APRA? Would it be the Financial Literacy Foundation? Where do you think it would be most potently driven?

Mr Lonsdale—On the last one, I am not sure at this stage, but I can give you a sense of where the thinking is up to in terms of the broader campaign. The government announced in the statement it issued on 12 December that it wanted to look at a campaign approach. Some preliminary research has been done—market testing. Some preliminary results have come through, but it is very partial at this stage because it is quite qualitative. I have not yet seen the quantitative results of surveying, but the idea is that when that comes together—which has not yet happened—advice would be put to government on the form of the campaign. So whether that is advertising or a website approach—there are different forms that could take. No decision has been made on that. There is an established government process where that research would go and decisions would be made.

Senator STEPHENS—Is there a time frame involved? Do we know a target date and when it might start?

Mr Lonsdale—I can come back to you on that target date.

Senator STEPHENS—Thank you, it is interesting. To what extent do we need to do more about financial education on the issue of risk for small business?

Mr Murphy—The government has a financial literacy program being run out of the Australian Securities and Investments Commission. That program was inculcated into schools to try to improve financial literacy. It is a very important issue and probably even more important for small businesses. What do we do? There is a program. The best thing you can do, like the banking package that was announced, is to try to simplify the documents so you empower the consumer to understand what they are on about—what the deal is. The major institutions also see it as a way of attracting and keeping business if they can have clearer messages and simpler products. They see that as something the market is looking for.

Mr Lonsdale—There is a small business support line and a website that provides a variety of services about entering a small business, exiting a small business, running a small business, accessing finance—financial literacy material. If you are interested in that, it would be worth looking at.

Senator STEPHENS—We have had a lot of representations made to us as individuals that something like that is seen to be the face of the government, and that if you dare to step into that space you are marking your own card, and things might not be going well.

Mr Murphy—You are thinking of the tax office.

Senator STEPHENS—That is true. That is the real worry, isn’t it? People have a perception that—

Mr Murphy—Yes, but it would not be—

Senator STEPHENS—We know that.

Mr Murphy—It is a misperception.

Senator STEPHENS—That is true.

CHAIRMAN—I want to follow through on a theme of perception—the perception of safety in banks and institutions. If we just take the big four versus everybody else, particularly post-GFC, is there an issue? Is there any actual difference in the safety, or any other mechanism, regulatory or otherwise, of the big four versus everybody else, hence giving rise to this perception that you need to be with the big banks—the 'too big to fail' scenario?

Mr Murphy—I do not think so. Australia has had a very stable financial system. You now have prudential regulation of all financial institutions. APRA does not financially regulate the finance companies, but if you are looking at the regulated space, all financial institutions, whether they are the smallest credit union or NAB, are regulated by APRA. There are prudential standards. Underpinning that now, the government has a financial claims scheme and you have a deposit guarantee in place up until October. The government is still to announce what it does with that, but it has announced that it will continue on a financial claims scheme. That means all depositors' funds are safe. Different Australian governments have put in place a very strong regulatory regime. It has people on the job, with APRA and ASIC and the RBA, and the whole thing seems to work reasonably well compared to other countries.

CHAIRMAN—Absolutely. Given that is the case, does anything currently exist—I am leading you on to a point that I want to get to—which clearly demonstrates to customers, to people in the marketplace, that it does not matter whether you go from the smallest institution, fully approved obviously, through to the largest; really there is no difference in terms of safety or regulation or all the other features you would expect from banking?

Mr Murphy—The government is looking at who can call themselves a bank, because that seems to give you some cachet of stability and support. At the same time, a lot of people have their deposits with small institutions in regional areas because they get good service from those institutions. There is no history in recent times of bank failures in Australia.

CHAIRMAN—But there is a distortion in the market. The big banks, or the big lenders, have got pretty close to 90 per cent of the market. It seems disproportionate.

Mr Murphy—Yes. We were worried that there would be, in the GFC, a flight to the major institutions. That is why the government stepped in with the guarantee on all deposits. That did not seem to happen. Deposits in those small institutions remained at stable levels. The government has announced the Financial Claims Scheme. All depositors can claim. That will continue. The cap is still to be decided; at the moment it is a million dollars.

Mr Lonsdale—One thing which goes to the senator's question on the campaign is that the government has announced that it is looking at a logo—a new official government protected deposit symbol.

Mr ANTHONY SMITH—The chair was raising this issue earlier on.

Mr Lonsdale—That would be a very transparent symbol that would apply.

CHAIRMAN—It would be a singular symbol which would be across all institutions—

Mr Lonsdale—ADIs.

CHAIRMAN—similar to the Heart Foundation's tick of approval, to use a good example—everyone understands that.

Mr ANTHONY SMITH—I would use the RACV, or in your case, Chair, the RACQ.

CHAIRMAN—That is right.

Mr ANTHONY SMITH—Tested.

Mr Murphy—That is right.

CHAIRMAN—The Treasury sees value in that sort of a concept?

Mr Murphy—It might be all right our sitting here and saying there are no problems with stability, but there are a lot of people out there and that may give them some comfort, and there is no harm in that. We are saying that they are duly regulated by a prudential regulator and, if anything does go wrong, the government steps in.

Mr ANTHONY SMITH—There is a difference, with respect, Mr Murphy, between the institutions saying that and that being accurate and potential customers thinking, 'Is that right?' and the actual regulator.

Mr Murphy—Yes. So they will be branded. It may be a communication thing. That is what it is trying to do.

CHAIRMAN—It is a guarantee almost in its own right when you see that. It is a symbol of guarantee, a government stamp of some sort.

Mr Lonsdale—Exactly what it looks like and how it appears are still being worked through, but that is the idea—that you would be able to look at it and see—

Mr Murphy—In the US they have 'FDIC regulated' and the federal deposit insurance scheme for banks over there. But, no, I do not think that does any harm. It just adds to transparency if people can see that.

CHAIRMAN—I thank all four witnesses from Treasury, and I thank you for your submission.

Mr Murphy—If the committee wants any further assistance or information, we will be happy to provide it.

CHAIRMAN—Thanks, Mr Murphy.

Proceedings suspended from 11.51 am to 12.34 pm

CARROLL, Mr Stephen, Policy Director, Australian Bankers Association

MUNCHENBERG, Mr Steven, Chief Executive Officer, Australian Bankers Association

CHAIRMAN—Welcome. I invite you to make an opening statement and we will go from there.

Mr Munchenberg—Thank you for the opportunity to appear today. There is no doubt that financial arrangements for small business have changed over the past few years. We believe that any inquiry into small business needs to look carefully at what has changed and why. The first point to note is that in the years immediately prior to the global financial crisis the level of new loans to small businesses surged. We were seeing the value of new loans growing by more than 25 per cent quarter-on-quarter during 2007. Competition for lending to small business was intense, fuelled by the easy and cheap funding available to lenders. The cost of small business loans fell in relative terms and bank margins were squeezed. Even with the GFC there is a question mark over whether such lending conditions could have continued. Both the Reserve Bank and APRA have indicated a view that risk was being underpriced at that time.

We did, of course, have the GFC. That had two major impacts on lending to small business. The first was that the cost of funds to lenders increased dramatically. For many lenders, particularly smaller lenders, even access to funds became a real issue. In other words, money became less available and much more expensive. This inevitably affected bank lending. The other change was that the Australian economy slowed markedly. Different parts of the economy were affected at different levels. It meant that many businesses that had run okay before the crisis began to struggle. Insolvencies increased. The number of loans to business in arrears spiked sharply. Particularly through 2009 and last year, uncertainty around business conditions increased. In that environment banks had to re-price risk. In effect, the likelihood of a loan going bad increased significantly. Banks also sought more security for some loans, and some asset prices fell, making it more difficult for businesses to meet their security requirements. It is worth pointing out that in those circumstances banks stood by many small businesses and worked with them to put them on a more sustainable footing. A customer who gets back on his feet is of much more value to a bank than a customer who goes broke.

Demand for credit has also fallen significantly over the past few years. Given the economic circumstances, it would be very surprising if it had not. Today we are still dealing with the fallout from the GFC. Business conditions remain uncertain. The high dollar is hurting import competitors and exporters. Consumer saving is up, but that means spending is down. So risks remain in many sectors. The cost of money also remains high, although it has eased considerably from the height of the GFC. I suspect there is a tendency to compare the situation today with the period in the run-up to the GFC and use that period as the benchmark for how small business finance should be. The reality is we are not going back to those times of cheap and easy credit any day soon.

For all that, lending to small business is recovering. New loans of less than $2 million are back close to their peak before the effects of the GFC hit. The June 2010 and September 2010 quarters, our latest figures, make up the second strongest six-month period on record for new lending activity for loans under $2 million. The level of new loans is now higher than its long-run trend. Banks are specifically targeting small businesses through extensive advertising campaigns and have announced significant expansions in the hiring of business bankers. As recently as last week an international bank operating here said it wanted to increase its support for small business in Australia.

The government has also announced measures to improve the funding situation for banks, especially smaller lenders. This will also help drive competition in small business lending. While we remain far from the days of cheap and easy credit before the GFC, the signs are that small business lending is recovering, even with ongoing economic uncertainty. We would be very pleased to take any questions. Thank you.

CHAIRMAN—I am glad you finished on the point that the days of easy finance are behind us, because I have raised with other witnesses this concept that pre-GFC there was a relaxation of lending requirements. Some lending institutions had perhaps not followed their own guidelines for good lending practice, as has been recounted to me by some major bankers. You seem to have a similar view—that perhaps it was a bit too easy pre-GFC?

Mr Munchenberg—We are reflecting the view that has been expressed by APRA and the RBA; it does make sense to us. The issue I want to highlight is that at that time, when funding was very cheap and readily available, there was a tendency for people to compete really hard. You wanted to win every last customer you possibly could. We need to be mindful that that will inevitably push you further out on the risk curve. It will mean that you are prepared to take more risks—not necessarily inappropriate risks and not necessarily risks inconsistent with your own bank's lending requirements but, particularly in a time when the economy was running so strongly and had been for so long and cash flows to businesses were very strong, risks that seemed like reasonable risks to take at the time. Of course, all of that has changed. Not only is credit no longer as readily available but the economy is no longer as gangbusters as it was back in 2006-07.

CHAIRMAN—Through the Australian Bankers Association with the Basel II requirements, is it right across the board that everyone is adhering to those requirements in terms of risk weighted—

Mr Munchenberg—All banks do. How they go about it varies between the larger lenders and the smaller lenders.

CHAIRMAN—I suppose that is the real question—how they go about it. Obviously there is a great range of flexibility between lending requirements, what you use as an asset base to securitise, or collateral for a loan. How does that work? Does your association have guidelines, codes of practice? Is there something that you provide as a guide to good lending practice, or is that just too difficult?

Mr Munchenberg—We do have a code of banking practice, which covers both small business and individual customers. That is more about the interaction between banks and their customers. On the prudential side, we would be loath to tell APRA how to do its job; that is very much their responsibility. They look very carefully at how lenders go about that. So for the bulk of our members, the smaller banks, APRA sets how you do it, in simple terms. The larger banks—I think there are five of them, the four majors and Macquarie, from memory—are closely supervised but also have the machinery, not to be able to come up with their own way of doing it but to have a bit more flexibility in how they meet those prudential requirements. But they are still very much under intense scrutiny from APRA.

CHAIRMAN—It appears to me, from past inquiries as well, that for all the regulation we have—and many would say we are over-regulated—there is an enormous scope of variance and flexibility between a particular small business enterprise going to any particular lender and being accepted and going to another and not being not accepted. It is trying to find somewhere where you could describe to me how we do our job better and how we can make this a better environment and a better market. Is it too loose at one end? Is there not enough regulation? I am sure you would agree there is too much regulation.

Mr Munchenberg—I would be inclined towards that.

CHAIRMAN—You would be inclined to that; that is what I would imagine. But you can see what I am driving at.

Mr Munchenberg—Yes, I can.

CHAIRMAN—You have said—and others have said it in their submissions—that pre-GFC it was a bit too easy, if I can categorise it like that. Now maybe it is a bit too hard. Where is the good balance point?

Mr Munchenberg—I think we will return to an appropriate equilibrium. The situation before the GFC was exceptional. There is a chart in our submission that shows new loans of under $2 million. You will see in 2006-07 there is a real surge in lending. That was exceptional in and of itself. Obviously, that fell. It has now substantially recovered. New lending of less than $2 million—we use that as a surrogate for small business lending—is above its long-term trend at the moment. In terms of banks' different approaches, we need to be a little careful. I understand the frustration that small business has; it has been presented to me as well—they go to one bank and they want something different from the last bank they spoke to. The danger of standardising too much is that you effectively commoditise the lending, by which I mean everyone is offering the same. Yes, there may be competition on price, but that also then reduces the ability of different lenders to position themselves differently in the market. A lender may say, 'We are prepared to move a bit further out on the risk spectrum and we are interested in start-up companies', for example. Another lender may say, 'We are not interested in going into that area'. If you standardise too much you risk cutting off some of the finance, which is hard enough to get at the best of times for start-ups, let alone now.

Senator STEPHENS—One of the concerns that has been raised with us in other places has been the issue of how to fund and encourage innovation in this space when it is about start-up moneys and perhaps high risk. Are you finding now that there are lenders who are prepared to go down that path a little more?

Mr Munchenberg—I cannot say that I have hard evidence of that. It would make sense. We are seeing banks more actively chasing small business and medium business, with the desire to lend. You would expect that as part of that they would be more interested in lending to start-ups now than at the height of 2009. But I cannot honestly say that we have any evidence to back that up. We would expect that to be the case.

Senator STEPHENS—Can I go back to the Chair's other point, which was the issue around this code of practice. That was the recommendation of the Senate Economics Committee Inquiry into Access of Small Business to Finance and also it was recommended by the CPA that a code of practice should be developed around this particular part of the market. What is the ABA's position on that?

Mr Munchenberg—The existing code of practice does apply to small business. We did inform the previous hearing of that but, for whatever reason, it did not seem to register. The CPA has subsequently said it considers there to be gaps in that coverage. The CPA and I have been talking about getting together to talk about a lot of these small business issues.

Senator STEPHENS—Good.

Mr Munchenberg—Unfortunately, we have not managed to do that. But we are keen to talk to CPA and to small business representatives about what the concern is. I suppose this is a step back from that issue. Part of my view is that we do seem to be dealing with a lot of perceptional issues here. We look at the data, and we look at the RBA's submission to this inquiry, for example. You have to be very careful with aggregated data because it can hide a whole pile of issues.

Senator STEPHENS—Yes.

Mr Munchenberg—Nonetheless, the aggregated data seems to suggest that there were issues, and they are improving. Yet we do hear—and we regularly get this directly as well from small business groups—that they or their members are still very concerned about access to finance. There are obviously things going on, but there are perceptional issues as well. Part of the answer to those perceptional issues is that the industry and small business representatives need to talk about these things more frequently. We have had preliminary discussions about how that may come about.

Senator STEPHENS—Thank you for the updated information—the supplementary submission. That is very helpful to us in our considerations. The second question I want to ask you is about the regional and rural dimension of lending and access to finance. I live in a state that has come out of seven years of drought. People have mortgaged themselves to the hilt. They probably now have very little equity in their own places. Could you reflect on how the long-term financial challenge around weather events plays out for the banks, and how they consider these issues in terms of access, particularly for the small business community?

Mr Munchenberg—Yes. In a moment I will defer to my colleague, who has worked for many years on these sorts of issues. Just as an introductory comment, my sense is that the industry has come a long way in its attitude to regional and rural businesses. I am not just talking about farmers or agribusinesses, but those that rely on those areas as well.

Senator STEPHENS—Yes, that is right.

Mr Munchenberg—It recognises that it is not the same as many urban businesses. It is a very variable business to be in. Some years are incredibly good and many, many years are incredibly bad—we have certainly seen a lot of those recently. The overall attitude in the industry is a much deeper recognition of that. That has been demonstrated by the fact that, notwithstanding that we have had large parts of Australia in drought for long periods, by and large we are not seeing a lot of anger about the treatment of farmers by the banks. There will always be exceptional circumstances. There will always be circumstances where either perhaps the banks have not done what they should have done or, notwithstanding the banks doing everything they can do, people are still dissatisfied with where they end up. But overall, in that area the banks have stood by a lot of those businesses, and that is broadly recognised by the representatives of those sectors. Stephen, do you want to add anything further to that?

Mr Carroll—Yes. It has been a particularly cruel year from the perspective of what has happened with the climatic events. People were expecting that a lot of wealth would have been generated coming out of this production season. Even though that has been seriously dented, there will still be some impressive results coming out of harvests, even though those harvests are going to be downgraded in terms of quality issues. On a volume and price perspective, a lot of wealth will still be generated. It may not enable a lot of people to reduce the amount of debt that they were probably hoping to, but it will definitely put them in a position to proceed to the next production season knowing that the banks will be there to support them to do that. I guess it has delayed the opportunity to bounce back. The outlook from the banking sector is very positive for regional areas because of where commodity prices are.

Moving past the immediate impacts of the climatic events, we now have very good soil moisture profiles, and that leads to the potential for the next season to be extremely good. We are not expecting there to be large numbers of farmers and, therefore, those who service them, who find that they have got themselves into issues with their bankers which they cannot sort out. I think the expectation will be that people will be carried through for another season if they have the prospects to come out the other side.

Senator STEPHENS—Thank you for that. I appreciate you are right in that respect. My interest lies in how we can think through government policy, such as the Evocities initiative of the government, which identifies key regional areas to attract investment and population growth. It is a very proactive initiative of the government about getting people out of metropolitan areas and into regional communities.

There are a series of criteria around the communities that are participating in the Evocities initiative, beyond a population of 30,000 having a higher education presence. One of them is about having good financial institutions and access to the money to relocate and reinvest in a new community like that. If you drive out to western New South Wales, you see all of the little businesses that have been hanging on for so long closing their doors. That has a flow-on impact—people do not want to come there because the facilities are not there. The Evocities initiative is specifically targeted at growth. The big challenge for us is how we can sustain those communities if the little businesses are not there to keep the money flowing around the town. In many of those communities, those businesses represent people’s superannuation in some respects. For them to go down the gurgler for lack of investment or lack of access to capital or lack of confidence on the part of their financial provider means it is a never-ending cycle.

Mr Munchenberg—It is a chicken and egg—

Senator STEPHENS—It sure is. I know that factors are coming into lending formulas around regional communities and rural communities and those kinds of things, but how does the bank engage in the more strategic thinking that is going on around policy like regional development? Do you have a capacity to engage in that?

Mr Carroll—There are examples of individual banks that are investing in regional areas, as far as branch infrastructure and that sort of thing goes. You would not be surprised to find that they are targeting the regional growth areas—the areas where they see growth as most likely to occur. That can be at the expense of the smaller towns, and their role does change over time as demographics change. As far as bank support for regional growth areas goes, I do not think there will ever be a problem in that area. But as to how the smaller towns go through an adjustment cycle phase, that is tricky. It depends on the appetite of people to move into those areas, whether they are looking for a small town environment to retire into or some other form of use of that infrastructure other than what it probably was originally set up for.

Mr Munchenberg—At its simplest form, the thing that the banks will always be looking at is: how viable is the servicing of this loan? If you come to me and you want additional money, how viable is it that you can repay that loan? Despite suggestions we sometimes get, we are not interested in gathering up everyone’s assets when they default. Default is something we want to avoid. It becomes a bit of a chicken-and-egg situation. If you were in a town which does not appear to have a lot of future prospects, then that is the information the bank has to go on in terms of judging whether it should continue to lend to you.

There may be an issue here that comes back to the central theme of the inquiry. You mentioned CPA. It identified three purposes that small business said they wanted funding for that they were not able to get, if I read its submission correctly. Two of those purposes were to cover operating costs so the business survived. Straight away, both those things ring alarm bells in the lender’s mind, because if you are going into further debt to try to keep your business alive, then that in itself is a problem. There are no easy answers in this area. As Stephen has mentioned, over the last decade—and undoubtedly in reaction to some very strong negative reactions when they were closing branches—banks have put a renewed focus back into providing that infrastructure into regional and rural areas, but it will be drawn to those areas that appear to have the best prospects.

Senator STEPHENS—I appreciate that, but I am thinking in terms of where the government has had to come in to create and fund community stores in Indigenous communities. There are little communities all along the Hume Highway where, if the local IGA went bust, that would be the death of the town, the school, the police station and everything else. I would be interested in knowing to what extent the banks think about essential services in those communities, and how that might be factored into their lending policy for something like that. I understand what you are saying about keeping the business viable. But when it is the only place, when it is the only service station-cum-everything else in the town—

Mr Munchenberg—We have seen a number of the regional banks move into that space. One of them was community banking. Another one was a franchise model, which I imagine would also provide some answers. In other areas, particularly in Indigenous communities, the banks have worked with Indigenous credit unions, for example, to help and support them. If the question ultimately distils down to whether banks are looking at communities in Australia and saying, ‘That is completely commercially unviable, but we feel we have an obligation to open a branch there notwithstanding that’, probably not. We would be concerned if policy drove banks in that direction, because an overarching concern we have is where government policy drives banks into making non-commercial decisions. There was an element of that in the GFC in America, of course, around affordable housing.

This does not quite go to your question, Senator, but we have worked hand in glove with government to try to come up with mechanisms to encourage investment, either by or through banks, into areas for affordable housing, for example. There are examples, but we need to be careful about not pushing those too far. I understand the issue that you are concerned about; it is a very real one. But equally, we cannot build communities around a bank branch that is not ultimately commercially viable.

Senator STEPHENS—I totally understand that. My greater anxiety is not about having the bank presence, because we are all moving to online banking in many respects; we can use post offices and other opportunities to do that. It really is about the access to finance for businesses in those communities, particularly small businesses. That is one issue. We also had heard some anecdotal evidence—I think it was from the Real Estate Institute of Australia—about some of their members finding—

CHAIRMAN—There was the rent roll issue—

Senator STEPHENS—Yes, that their rent roll was not valued—that was one thing. Secondly, they were negotiating additional finance or working with their institutions, and banks wanted to change the terms and conditions of the existing loans. We heard strong evidence about that the other day. Could you tell me how the code of practice of the banks covers those issues? We heard, for example, of people being shifted from a line of credit or an overdraft into taking out credit cards.

Mr Munchenberg—Without having heard the precise circumstances, I am not sure. I cannot tell you precisely whether the code or the legislation would cover that sort of behaviour. We now have, from the beginning of this year, responsible lending obligations imposed by a statute as well. While they apply to individual customers, for a small business, whether it is doing individual banking or small business banking is quite blurred. We will find that certainly for small operations the banks will err on the side of caution and treat them as small customers.

We have probably seen the most substantial issues in the property area. This does not answer your question, but commercial property, in particular, has been under real pressure for a number of reasons. One is that we have seen commercial property asset values fall significantly. That in itself has had an impact for people who are borrowing against those assets. It is my own personal view, and others may differ, that the banks have long enough memories to remember the early nineties, when they got very badly burnt. Some banks were teetering as a result of over-exposure to commercial property. So commercial property was targeted very early when the GFC hit as an area of potential danger for the banks, and they pulled back very sharply from there.

Even with residential property, one of the things that we have butted up against is that as the level of activity of the non-major bank lenders, in particular, has decreased or they have exited, the major banks have stepped into that area to fill that gap. They can only do that to a certain extent, because they have their own, and APRA-imposed, risk exposure caps. So a particular bank will only want so much exposure in a particular location. This has been a big issue in Queensland, for example, or for a particular segment of an industry.

None of this is going directly to your question. I am not sure quite what the answer is in that area, except to say that banks are more wary these days than they would have been a few years ago. It gets back to my opening point. People are still comparing the situation. I get this directly from small business people, who say, 'Back then it was like this and now you are doing this to me'.

Senator STEPHENS—That is right.

Mr Munchenberg—I can understand it from their point of view. But equally—and it sounds glib—the world has profoundly changed from back then.

CHAIRMAN—On that point, there seems to be a perception that banks are now lending less, but there are greater margins. So from a banking perspective not a lot has changed. Profitability is strong.

Mr Munchenberg—Margins and profitability are not the same.

CHAIRMAN—No, they are not, but banks certainly are profitable. Some have had record profits. They seem to be doing quite well. The margin, the basis points that now exist on loans, particularly commercial loans, seems to be double what it was pre the GFC—from around the 200 or 210 basis points to now over 400, and in some cases higher.

Mr Munchenberg—There is no doubt that margins have increased. The reason margins have increased is risk repricing, and losses will have increased as well. Insolvencies are up. We saw very quickly, when the GFC hit, business loans in arrears. We used the 90 days in arrears; the number of people who were 90 days behind with their repayments spiked. It has come down but still remains much higher than it was pre the GFC. That works against the 'margins profitable' sort of argument. Even if there were—and I am not saying there is—any truth in that, it would be a temporary aberration because that just leaves the opportunity for people to come in and undercut.

We are seeing the major banks quite aggressively advertising in the business space, particularly targeting small business. We are seeing the international banks becoming more active in the retail area. Even if there were any widening of margins for a profitability purpose, under the current circumstances it would be eroded. I think our submission—I have read a number of submissions—indicated that the gap between small business loan rates and the cash rate spiked very sharply when funding costs and risk re-pricing went up in 2008-09 and has been tailing off since then. So it is still higher than it was pre GFC, but it is coming down. That is what you would expect to see as the level of competition increased.

CHAIRMAN—Again, competition. This is a big feature of what we are doing in trying to better understand the competitive environment. How do you see and define and explain competition within the banking sector from the perspective of the banking sector?

Mr Munchenberg—How long have we got?

CHAIRMAN—We have time. I am quite interested. I want to know.

Mr Munchenberg—I am sure you are aware that there is another parliamentary committee looking at that at the moment. We have turned our minds to that, as a lot of people have.

CHAIRMAN—Let me define with a little more focus for you, so we do not go too far astray. Let us look specifically at the number of lenders, the number of products, and the size of the pool of funds available to lend in that market—an environment where some people had access to 25, as we have heard from others, different lenders and now there are only eight; so the shrinking of that pool. Let us look at competition in those terms.

Mr Munchenberg—We need to be wary of necessarily equating the number of competitors with competition. Choice has certainly decreased and in very variable ways. I heard earlier the figure cited of around 25 down to eight. Obviously that is not across the board. Along the lines that a picture tells a thousand words, a chart in the Reserve Bank’s submission—I think it is at the top of the last page—shows the level of small business lending by segment: the major banks; the non—major banks, largely the regional banks; the finance companies and other lenders. The major banks have been increasing their lending as they have stepped in to fill gaps. The regional banks, because they faced more serious funding issues—which continue, as you heard from Treasury before lunch—decreased their lending. The finance companies decreased their lending markedly. That means that both the major banks could become more choosey and not as many people were out there fighting as hard to get the loan.

We have to remind ourselves that maybe they were fighting too hard before the GFC. Undoubtedly, that has happened. That is not a factor of any change of policy of any banks or anything, beyond the fact of dealing with the realities of less funding being available. The securitisation market, which is very important to the non-major bank lenders, effectively froze. The government has needed to intervene into that market to try to get some life back into it, and life is returning to that market, but it is still not anywhere near where it was pre GFC. Even the major banks, for a period at least, while they could continue to raise funding offshore, were nervous about both their ability to continue to do that and then, for a longer period of time, the price at which they were doing that.

All of this meant that you became a little more careful in your lending, not just because of the increased risks in the economy, which were very real and important, but also in a sense because of the increased risks of how you allocated the funds that were available to you. But we are seeing that correcting. A very important consideration is that these things will improve with time. Regrettably, there are going to be small businesses that do not have that time, but overall we will see these improvements. In fact, we believe we are already seeing them, with the pick-up in the number of new loans under $2 million, and with the behaviour of the banks, for example, in trying to attract more business customers.

CHAIRMAN—ABA—just give me a broad idea of who you represent. It is not every lending institution in the market?

Mr Munchenberg—No.

CHAIRMAN—You are specifically limited to?

Mr Munchenberg—We are limited to ‘banks’, which of course is an APRA-defined term—so not ‘authorised deposit institutions’, which include credit unions. We are banks, and the membership is basically the four majors, the three regional banks, plus other, smaller Australian banks and the international banks that operate here in Australia as well.

CHAIRMAN—What do you think of the idea of some sort of a symbol or a logo similar to the Heart Foundation tick of approval saying, ‘Everyone across this market is the same,’ because they all met the same requirements. So it would be APRA regulated, government approved, to equalise out the perception that certain banks have an advantage over other banks or are safer. Does ABA have a view on that?

Mr Munchenberg—It is part of the government’s package. Basically we are relaxed about that. Indeed, some of our smaller members are quite keen on the idea because they, like the credit unions, feel that that they suffer from this perceptional disadvantage. I can construct a scenario where it is a problem. I think it is unlikely, but you could have a smaller lender at some point in time who used that branding plus the deposit guarantee—this will depend a lot on where the cap is set on the guarantee—to become very aggressive in pricing deposits, to raise lots of money and, therefore, have to invest very aggressively and riskily to get the returns, which is like the savings and loans issue that arose in the US in the eighties.

The qualifier I must put on that is that we are subject to the same prudential regulation. Supervision becomes important. Supervision, more than regulation, was the reason Australia did so well throughout the GFC. So, provided supervision is kept to the levels it needs to be kept to, that situation should not arise. Hypothetically it could cause a problem, but it seems unlikely.

Mr Carroll—There is an obvious scale differential where there has to be a certain level of held assets.

CHAIRMAN—Held assets; absolutely.

Mr Carroll—To use the term ‘bank’, to get the bank licence.

CHAIRMAN—Yes. Something that has been raised in a number of forums is the ability of any particular lender to properly assess an application or to revalue or to understand the business that they are dealing with. Obviously not everyone can be everything to everybody. There appears to be a diminishing value of the skill set within banking—the people who have the capacity to make proper assessments. In particular, with regional businesses, farming and agriculture, things are a bit more complicated and you have to have some sort of knowledge about the business.

Mr Munchenberg—Again, I am familiar with this concern; it is consistently expressed. In some circumstances there may be some truth in it. But equally, we are seeing, particularly in regional and rural areas, more and more of the decision making being devolved down to people in the branches or the subregional managers for the very reason that they are the people who can make the soundest judgments about what is going on in that region. They have the local knowledge, which is important.

At the other end of the spectrum, there is a tendency to say, ‘If only these people understood my business they would give us the money.’ There may be circumstances where maybe the bank understands your business better than you think and, therefore, is not prepared to lend you the money. We are covering a wide range of business types and business operators here. Again, as we see the funding situation improve, as we see the economy become less uncertain—hoping that happens over the next 12 to 18 months—and as we see the competition for small business lending increase, we will start to see a stronger focus on service in that area. A number of the banks are already marketing themselves, having better service proposition—not just on price—for small business as well.

Senator STEPHENS—We have canvassed a few of the issues in the CPA submission, but there are still a few that we have not yet canvassed. Referring back to the Real Estate Institute’s example, the CPA has received feedback from its members on several things that the banks are doing—it is on page 8 of the submission. One of these was a decrease in the forms of security that the banks are willing to accept, including, for example, a lesser willingness to accept intangibles such as goodwill, cash flow and profitability. Another is that the banks are increasingly asking businesses to take up additional insurance. That is quite expensive—a significant business expense. Another thing the banks are doing is increasing the requirement not just for compliance reporting but for information that is outside the current loan agreement or covenant. Can you comment on those issues raised by the CPA and whether they reflect your understanding of business practices post the GFC?

Mr Munchenberg—It is not necessarily how I would have described them. Part of what is driving what the banks are doing relates to the point that the Chairman just raised—that is, the banks are trying to get to know the businesses better. When times are riskier, the banks want to see more information. There may be an issue about whether the banks are explaining adequately to business owners why they suddenly require information which they had not previously required.

The cash flow issues are a good illustration. In 2007, we lauded that Australia had had 16 continuous years of economic growth, that we had survived financial crises, that everything was great and that the economy was going gangbusters. At that time, a business’s cash flow projections were probably looked at with less scepticism than they would have been if a bank came in 18 months later—in the middle of 2009, for example. I think a banker in that latter circumstance would want to say: ‘That is fine. Can you substantiate why you are so confident that your cash flow is going to be so strong?’ So those sorts of changes in the interaction between small business and banks will have occurred. Again, it is this risk issue and again we hear small businesses say, ‘But I work in a sector that is doing fine, et cetera.’ Okay, but who are your suppliers? What is your market? If you are manufacturing widgets that are being used, for argument’s sake, in commercial property, you might be going fine, but if a couple of big commercial property companies go down you will have suddenly lost two-thirds of your market.

These sorts of considerations became more important. At the beginning of 2009—I well remember it; I worked for a major bank at the time—we had very bleak expectations about what the economy was going to do, extremely bleak expectations.

In that environment, people were very nervous about accepting the same level of collateral, the same level of security quality, the same quality of information. Again, that is all improving, as people are coming through now. There are sectors of the economy that are still a problem—I am sure this will be close to the heart of your next witness. We have seen a large book chain, for example, get into difficulty just in the last week or so. We know that retail, for example, continues to be under incredible pressure. Because of the value of the dollar, we know that those businesses that are exporting or that are competing with importers are going to be under a lot of pressure. There is still a lot of uncertainty in the economy, so banks are still saying, ‘We probably do require more convincing today than we would have when the whole economy was going gangbusters back before the GFC.’ That is the way the banks perceive those situations—I can understand that a business will often perceive those situations very differently. But that is often what is driving the bank’s perception.

CHAIRMAN—Should that be a permanent change? Should that be something that banks do as a matter of course—just have that more stringent scrutiny? Or is it really about the market at that particular time—less scrutiny when the market is good and more scrutiny when it is bad?

Mr Munchenberg—To some extent I think that is appropriate, because it is driven by the level of risk. When an economy is going really strongly your risks are lower. To some extent we also feel we are in a bit of a bind—and this is not just an issue with small business clients but with clients across the board, including individual retail clients—because we are for a whole host of reasons asking more and more information of our customers. Some of it is driven by risk management; a lot of it is driven by regulation. But they find this annoying. There is a bit of a bind here as well. On the one hand, small business has a view that the banks should have better business expertise to make reasonable judgments of their businesses. On the other hand, that will require banks to understand their businesses more thoroughly and put more of an impost on them to provide the evidence to enable us to do that.

CHAIRMAN—One of the other issues that has been raised is the size of funds, the pie. Is this still a big issue for banks—to be able to access funds either overseas or internally?

Mr Munchenberg—Overseas we are not having trouble accessing. We are obviously a price taker in the sense that, whatever the international price is, we—

CHAIRMAN—So it is really just a cost issue, is it?

Mr Munchenberg—For the majors, in terms of their money overseas. The other element of this is the fact that there is a market where competition has surged considerably throughout the GFC, and that is in deposit taking. This benefits businesses as well as individual customers. While interest rates being moved higher than the RBA attracts a lot of attention in the mortgage market, it has been going on in the deposit market and for some reason does not quite get the same headlines—but that is by the by. But we are seeing strong competition there for deposits. That is great if you have savings and it is great if you have a business that has strong cash flows and everything, but it also adds to the costs of funding.

In terms of availability, the main missing piece is that the securitisation market, which was an important market for many non-major bank lenders, is still not operating as it did before. I am in no position to judge whether it will ever come back to that, but certainly we are strongly of the view that the government support for that market has been vitally important. We are seeing the banks themselves trying to push that market to become more active. We are also in that market selling residential backed securities, which were what—in another form, I hasten to add—triggered the GFC. It is a perceptional issue in that market as well. Money is just not as freely available as even many of the smaller banks would like it to be at this stage.

CHAIRMAN—Is the ABA liaising directly with other organisations such as people who have presented to us like Abacus and the Commercial Asset Finance Brokers Association of Australia and others? Is there any link between the different parts of the market? Do you guys get together and talk about the issues, as it were?

Mr Munchenberg—We certainly do not talk about prices. We do regularly get together. My view is that a lot of these issues are better talked about directly. We try to resolve them directly rather than through third parties, be that the media or other sources. We cannot always do that. Organisations like Abacus, to whom we do talk regularly, equally are competitors with my sector as well and will therefore take what opportunities they can in the public space to champion their own members, as I would in their shoes. But we do find that with virtually any organisation working on any of these issues we are able to have a dialogue. I would like to have more frequent dialogues. In part, that is my own failing in not having pushed that. But it has been rather a busy six months in the banking sector, if that is any excuse.

CHAIRMAN—You have also talked in your submission about demand for credit. Could you give us more information? Has that demand come off significantly? How is it coming back? What is the picture around demand and the quality of that demand?

Mr Munchenberg—It is hard to answer in broad terms. I suppose the starting point is that, given where the economy has been and the expectations around the economy, particularly through 2009, and even nervousness in some sectors today, it would be very surprising if demand did not come off. It would be very surprising if there were not businesses that in better times would have sought to expand but that have decided that it is better to adopt a more defensive approach. It is hard to quantify because a fall in demand means that people are not coming to the banks to talk to you about wanting a loan. So we cannot make real assessments of the extent to which it is a demand-driven thing, but it would be extremely surprising if demand were not a key part of it.

CHAIRMAN—Is that a reflection of the economy? Is it a reflection of the banking sector not being competitive enough in that area? Are people going elsewhere? Certainly there is growth in activity. The economy is picking up; there is growth back.

Mr Munchenberg—It varies. It is a very mixed set of circumstances. If you are a business that is somehow linked into the food chain of the mining resources boom, for example, even though you may be several businesses down the supply chain, you will be doing very well and you will be looking to expand your operations. If you are in retail at the moment—it varies, but certainly in areas where consumers are using discretionary spending—you might be very wary about expanding your operations. We do hear that part of the fall in demand is because people feel that there is no point in going to the bank because they will be turned away. Even if that were the case, circumstances are improving.

Mr Carroll—The growth in demand that is coming through in the $2 million and less loans is at the lower end. There is more growth in loan amounts of less than $100,000 than there is in, say, loan amounts of $500,000 to $2 million. So the growth that can be seen going on is in the smaller amounts. What that is reflecting, I cannot say. Maybe people are gradually getting more comfortable and taking on more debt in small amounts. That would be consistent with the pace at which the economy is starting to come back.

Mr Munchenberg—There are things that potentially could be done. If there are issues, I know that the committee will be looking at what can be done about them. Perhaps we should just touch on those. We have a strong view that the focus should be on the input end to the system, if you like. By that I mean that anything that can be done to help the funding of lenders—not just banks but of lenders—is going to flow through to better outcomes for small business, and in a way that is going to be less distortionary than trying to deal with the interface between banks and small business per se. I am not discounting that there are things that can be done in that space. The government, as part of its competition package, did announce some activities. The continuation of support for the RMBS market, the securitisation market, was good. Allowing major banks to raise money through covered bonds is good because they are a cheaper and more reliable source of funding. The government does have, as Treasury mentioned, a plan to wind down, slowly, over a long period, withholding tax. We think that more could be done in these spaces. We welcome what government has done. Just taking the withholding tax, for example, we have increasing activity from international banks here. They are not strong in small business relative to the Australian banks at this stage, but there is no reason why over time they would not move into those areas, and getting the withholding tax removed more quickly would encourage that level of activity, as well as adding to competition in retail lending.

Our view is that we need to be wary of things like guaranteeing small business loans, because that is a very complicated, potentially dangerous, exercise of moving risk around the system, even though it may seem superficially attractive. But the more we can do to pump more money into the system, the more competition we are going to get coming out of it, is basically what it boils down to.

CHAIRMAN—I thank you both very much for your submission.

[1.31 pm]

STRONG, Mr Peter James, Executive Director, Council of Small Business Organisations of Australia

CHAIRMAN—Welcome, Mr Strong.

Mr Strong—Thank you for this opportunity to appear before you. We did not put in a submission, mainly because of resources and time. The issues around small business and anything we get involved with these days are underpinned by two facts; one is that, according to the plentiful rhetoric around, we are an integral part of the economy, the backbone of the economy, the engine room of the economy. Everybody says it, but I am not sure people do much about it. The other thing is that we are people. A lot of the stuff that has happened to small business over the past 20 years has come from the fact that people seem to think we are like big businesses, only smaller. We are actually people. So our comments and our approach are underpinned by those two things. If something is impacting poorly, it is probably doing so because we are not treated like people.

In the banking area the best example I can give is information from the financial services ombudsman, who says that the Financial Ombudsman Service gets more complaints from small business about banks that have their small business loans capacity in their business division, and fewer complaints from small business about banks that have their small business loans placed in their consumer division. That quite simply means that, if you treat them like people, you get fewer complaints and, if you treat them like businesses, you get more. That is probably the most telling statistic I have seen for a while about small business and finance—treat us like people.

CHAIRMAN—Mr Strong, can you provide that to us? That is an interesting piece of information and we would love to have it as part of this inquiry. Following on that point, do you see any reason why that is the case? I raised this issue of the skills set earlier. Is it because the skills are different in those parts of banking?

Mr Strong—The skills are different and the attitudes are different. In business banking you expect the person to whom you are talking to know what you are talking about, and to deal with it and cope with it and give you the answers that you want, and off you go from there. In the consumer area you do not. You expect that the person to whom you are talking may have good knowledge, or bad knowledge, or whatever. So you spend more time explaining it, you tell them what is going on and, as a result, you get fewer complaints. It is attitude and skills. Better communications skills are in the consumer area, and a better attitude towards people.

CHAIRMAN—It may be a two-way street, you are saying, in terms of understanding what the products are and the requirements of lending and the terms and conditions and everything else that goes with it.

Mr Strong—That is right. I always say there is no such thing as 'small business'—that is an economist's description of an economic unit. There are owner-drivers, there are retailers and there are home-based businesses. It is such a diverse group that we should not think about them as one group. It is interesting with the brokers. About a year ago we got more involved with the brokers. All of my board members said the same thing—they had never thought of going to a broker for small business loans. Obviously, some sectors do. The commercial area is interesting; it is an area that we want to expand. A broker, often a small business, we will deal with in a separate way. They may get a product. It might even be a bit dearer than what you will get elsewhere, but the person he is dealing with will feel more comfortable with that product for other reasons. It might be ease of access, ease of exit—whatever the broker has brokered with them is something they need.

Not all brokers are not connected closely to banks; some are completely connected to banks. Other brokers, such as the Commercial Asset Finance Brokers Association, are very connected to the small business market and they understand the issues there. Point-7 in its submission talks about how some of the changes coming along will put more red tape on small business and make it much more difficult for them, again. That is the last thing we want. There is plenty of red tape out there, as it is. Most of them will not understand it anyway, being who they are.

CHAIRMAN—One of the strong complaints we have received from a number of small businesses—and it seems to be a theme—is that from their perspective, not only are less funds available and more difficult to get, but their ability to go to different financiers or lenders has shortened, basically. There is just less available. It is more difficult for them. Is that something you are hearing back through your organisation?

Mr Strong—There are a couple of things. I want to talk about the anecdotal information. Small business by its nature is very busy. Something like 47 per cent of them work more than 48 hours a week, or whatever it is. So to find time to go and look for new sources of finance is one of the issues, without a doubt. Some will. Some industries have that capacity. A lot of people do not have the time. So you just go back to the same old, same old. You deal with them. You cross your fingers and off you go. Again, they behave like people. They do not turn to their accountant and say, ‘Go and negotiate a loan for me’. They could do, but that would cost them $5,000 or something. They are limited by their lack of time and by their knowledge. One of the things we have to do better from the council’s point of view and from the point of view of a lot of people is to get more information on the different products and the different mechanisms out there. You have to get it out the right way. You do not communicate with small business in only the one way—you have to communicate with them to suit their particular needs. So we will be looking at that.

The other issue is the lack of real information on what goes on. Certainly we have had good conversations with the Australian Bankers’ Association about gathering better information. I can make any statement I want, and it is hard to prove or disprove in most cases. So we can say that small businesses are finding it harder to get loans, and there are some broad figures that show that. But why? I would like to know why. There might be very good reasons why. The last thing we want is some family to get a loan that they cannot service. Let us find out why they are being rejected. How many are being rejected? It might be a hundred. There might be 5,000. Nobody can tell me at the moment. The banks would know, but there are some commercial issues there. If we are going to have an informed debate about this, we need a lot more information on what is going on, even at the regional level. We could ask, ‘What is happening in the Illawarra?’—because they have specific types of small businesses there, probably more around transport than most other regions. So you go in there, have a look at it and say, ‘We can come up with a product that suits here'. We know the reasons they are not getting it. With a lot of them, English is their second language, perhaps. Then we start to develop products that suit the marketplace.

CHAIRMAN—Would you agree with the view of some that finance was too easy to get pre the GFC? There was too much available and competition was driving it. So long as you had a heartbeat, you got whatever you wanted.

Mr Strong—It was far too easy to get for big business. They just got it.

CHAIRMAN—What about small business?

Mr Strong—I do not think things changed. It was easy to get, but I would not call it a lot easier to get. Again, it comes back to that person going in, negotiating, talking, filling out forms, dealing with people. I think it is a big difference. Big business got it so easily—that is what caused the problem, in the end—whereas with small business I am only hearing now of people going belly-up, people going bankrupt and businesses closing. People are saying that that is due to the financial crisis; it is the ripple effect coming through. I am not sure about that, either. The internet has a lot of influence on that. As we know, retail is going through an evolutionary change. Bricks and mortar retailers have to reinvent themselves in many different ways—or whatever they have to do. That impacts on the landlords and it impacts across financing eventually, as well. Again, we need more information on the small business sector. Who is closing? Why are they closing? Is it GFC-related or something else?

CHAIRMAN—Given what you have just said, your membership's view is that it is harder for people to gain access to funds?

Mr Strong—Yes, definitely harder. Even little loans like $5,000, which some people might need to get a new laptop to take advantage of whatever is happening in the virtual world, are hard to get access to. I have heard that from a few people. They have gone looking to extend their credit card by $5,000 and they cannot do that.

CHAIRMAN—One of the issues we are looking at is, obviously, what the causes are—whether it is just the availability of funds, or just the banking sector and lenders deciding that maybe this is the equilibrium, this is where it ought to be. Has the pendulum swung too far and made it too difficult? Is it going to come back? We need to find some sort of equilibrium—

Mr Strong—My view is that it is a lot more profitable to give money to consumers in the home loan area. My understanding is that they are driven by the need for profit; they have gone off and done that and ignored the small business sector because there is not as much money in it. I was at an ASIC summer school the other day, where a fellow from NAB was saying exactly that. That has been coming out of a lot of banks—that it is more profitable to go into consumers; banks should be going in there. If they are going to maintain the economy and keep it growing, they have to look after that economic backbone. It is good for them to go in there, even though it might not be as profitable, because in the long term it works for them. The banks only look a couple of months ahead, as you can see by their technology at the moment—it is from the 1980s. I think they bought it from a second-hand IT salesman in Wollongong.

CHAIRMAN—Some banking sector change is on its way?

Mr Strong—It is. I know they are upgrading their technology now.

CHAIRMAN—Yours is a big organisation. Do you carry out surveys?

Mr Strong—We are not a big organisation. There is me, and we have a part-time secretariat. That is the nature of small business organisations. COSBOA was set up in 1979. We are a peak body of other bodies. The reason it was set up is that there was no single voice for small business. Various other bodies have big members and small members. When you have, say, a landlord as a member and a small business as a member, it is a bit hard to go out and attack the greedy landlords because they are members. So they set up an organisation that has none of those conflicts. We can attack whomever we wish, based upon the needs of small business. That being its nature, we do not have a lot of resources.

CHAIRMAN—You do not do an annual survey or something or have some way of gauging what the key issues are for small business right now? Is the biggest issue access to funds?

Mr Strong—No. I am glad you ask. ACCI does a very good small business survey. We work with a lot of organisations on that. Without a doubt the biggest issue we have is the two-speed economy. You have the big end going gangbusters and small business going backwards. Red tape, red tape, red tape is such an issue for us. It grows and grows and grows. People are working longer hours. You hear about lack of finance from certain sectors at certain times; then you will not hear about it for a little while and then you will hear about it again.

CHAIRMAN—Is that because they are busier dealing with the day-to-day issues? They are different issues. Finance might only come up once every five or 10 years in terms of what you are doing, or maybe once a year, but bureaucracy and compliance is something you do every day, every week, every month.

Mr Strong—It is there every month. It gets in the way of hunting for finance. If do you superannuation quarterly, it is a pain. You have to spend a lot of time doing that—chasing people if someone has not given you figures, whatever it is. It does take away a lot of your time and effort, which then impacts upon your time to go and seek finance, which is something we are working on much more closely with the brokers, to make sure that people have access to an 1800 number or whatever, that they have not had before. They might get better service that way. That is something we have to work on as we go forward.

We use figures from other people's areas, but we need better figures. We have been pushing this for a long time. The ABS needs to expand its SME data-gathering. I met with the Productivity Commission this morning around its retail review—and the same thing applies. If you are going to have informed policy and comment, you need a lot more information on small business than we have at the moment. That was taken out by the Howard government, for some reason I do not understand; let us bring it back in.

The brokers are one area. I did the banks—that is good. Treating small business like people is really important. If I go in there and use my home as collateral, that is fine if I am looking for a home loan or a loan for an investment property; but, when I use it for business, it is a totally different ball game. I understand the banks have their reason for that—it is due to some activities behind the scenes that I never understand—but it still seems wrong. It is the same house, the same person and the same business earning them money.

CHAIRMAN—Is this a banking policy difference or some other regulated difference in terms of how it is treated?

Mr Strong—You would have to ask the bank. There is a technical answer. They have told me several times. It just goes out of my head because it is too complicated, which probably means it is not true. You know how these things work. The other side of that is interesting. As you may know, I own a bookshop; the poor thing is suffering. If one of my workers goes to a bank to get a loan, they take their pay advice. The bank says, ‘You work for Smiths Alternative Bookshop; here is your loan’. If I go along, they say, ‘Oh, no; you are not viable’. You think, ‘Hang on a minute: one of my workers just got a loan for a business that you have just determined you would not lend to because there is a risk’. There is something odd going on there, too.

CHAIRMAN—Is that maybe because of the size of the loan, or are you saying it is right across the board?

Mr Strong—No; it is the approach of the banks. The rules are: check their pay; do not check the viability of the company.

CHAIRMAN—There is a real difference between the consumer and commercial. It is probably a bit deeper than we have understood, rather than just that commercial is treated generally as being riskier.

Mr Strong—And they are not. They are as risky as the home loan they are giving the worker, which always amuses me. That is another area where I scratch my head and wonder why there are different rules. The very first example I gave you is the best example—the banks that treat you like a person are the ones that get fewer complaints. They obviously explain it much better, and you move from there.

The other issue is the involvement of small business in a lot of these advisory groups. COSBOA is a peak body. Our job is to lobby and do things—not to get too heavily involved in everything. But a lot of our members have that capacity. We should have a lot more small business specific people involved in advisory committees and stakeholder committees, et cetera and, if possible, people who really do represent small business. Everybody claims to represent them. We all do. Every agency claims to represent them. It might only be a small group. CAFBA are members of ours. They are the group I talk to about small business financing issues because they understand it. We need to have that happening a lot more, as well.

CHAIRMAN—Is it your interpretation or your view that is it just too expensive to get loans, or is it that you just cannot get them in the first place?

Mr Strong—We cannot get them. The expense is another issue. Businesses sort that out; there is half a per cent here or one per cent there. Not being able to get them is the main issue. Or, if you can, it is a lot more expensive. We are talking four percentage points or 400 basis points, which is a lot, which means you do not go and get it. So they shop around. If we use brokers, they are the ones who will say, ‘This is 50 basis points more expensive but it is cheaper in these areas'. Brokers do not charge the small business because they are making their money out of what they are doing. They charge them for whatever it is, and the small business is aware of that and knows the value of it.

We are going to start pushing brokers a lot more than we have in the past. Maybe we will look at doing something for 12 months: working with brokers and really promoting them out there; not setting up more red tape for them, as we are doing at the moment, but taking away the red tape. That is one of the issues that I know CAFBA brought up as well—the extra red tape that will stop people seeking business loans and make them go into a bank. This happens a lot and is not anecdotal: I will go to the bank and say, 'I want a loan for my business'. 'Don't bother. I'll give you a line of credit against your house for investment purposes. It's cheaper and it's easier, and you probably won't get it for your business'. That is a very common solution that bank managers put into place.

CHAIRMAN—Is that because there is more money in doing it that way?

Mr Strong—It is easier, and they will get it. And it is cheaper.

CHAIRMAN—That is what I am asking. What is the difference? Is it because it is easier and they are guaranteed of getting it, so the bank is doing them a favour—

Mr Strong—That is right.

CHAIRMAN—by saying, 'If you just want to get the money, this is the easiest way of doing it'? Or is it a case that for the bank not only is it easier but also it is more profitable.

Mr Strong—I do not think it is more profitable for them. I think it is still more profitable in the business area. Again, that is my understanding. A good bank manager will work with the person. If you have a bank manager in a bank, they will sit down and say, 'This is what I think is best for you'. I hear that quite often. In many ways that is a good thing but it is, as I understand it, illegal as well.

CHAIRMAN—Which bit is illegal?

Mr Strong—Someone said it is illegal to give a loan that you know is a business loan and call it something else. Again, I am no expert in these areas; brokers were saying that. A bank manager is protected by being part of a big bank; whereas, with a broker, their licence is on the line.

CHAIRMAN—I would have thought that if you got a personal loan you could do whatever you liked with it.

Mr Strong—Exactly—

CHAIRMAN—including spending it on your business.

Mr Strong—An investment in the shop—

CHAIRMAN—I am not sure. I am not an expert in these areas.

Mr Strong—It is interesting that you go in and ask that. I had one fellow who was looking for $600,000 for six months and who could not find it. It was a good little business, too. Then the person he saw said, ‘I will give you a line of credit’, and he had it done within a couple of days. It has to be wrong that you have to fiddle to do that. That is what we all do to a degree, I suppose, but let us make it a bit more transparent.

Senator STEPHENS—I have one question. You made some remarks about banking technology. Is the extent to which the banks seek small businesses to use technology such as EFTPOS an issue for your members?

Mr Strong—It is a growing issue because of the change that is coming up. I am still getting my head around this change to EFTPOS payments. The fees are going to be increased quite a bit. Have you had a presentation from Tyro?

CHAIRMAN—No.

Mr Strong—That is an organisation. I might even get in contact with them. They are changing the fee structure potentially on EFTPOS, which means that small business will start to wear a lot more fees in the EFTPOS area. Big business can deal with that, of course, whereas for small business that is quite an impost. I am still reading the documents. I am no financier, but I do know that people are very concerned about it. We have to watch the way that works.

Senator STEPHENS—The impact of that will be that, where now there is a credit card surcharge, a surcharge will also be added to EFTPOS transactions?

Mr Strong—It will increase. I cannot go beyond that, except to say that I can send you some further information on that, which should inform that debate. I know an expert. Has the Australian Credit Payments Association put in a submission?

CHAIRMAN—No.

Mr Strong—They are another group that would understand that. That is one of the problems. This is about finance. Banks can get money from small business in many different ways. The online work with the banks is fantastic—that you pay online now is just fantastic. It is a lot easier than it ever was and will get better as time goes on, once the banks bring their technology up to date.

Senator STEPHENS—Yes, sure. It was put to me only a few weeks ago that a condition of a business loan for a small business was that they install the technology so that the sales money was coming through the bank account very quickly, rather than there being cash deposits and all of that kind of stuff. Is that an issue?

Mr Strong—I have never heard it. If that is what they are asking, I do not have a huge problem with that. Some businesses out there deal in the old ways, and good on them. Change is one of the hardest things to do, and I will not question that. But you have to go online when you come to banking, and those sorts of things. It is so much easier. It saves you time and money. If banks are asking them to do that, I think that is fair. The issue is if people miss out on money—even though they have a good idea—just because they cannot do that. It is hard to imagine someone who does not use online. That is an interesting thought. I have never heard that one.

Senator STEPHENS—Thank you very much.

CHAIRMAN—Mr Strong, thank you very much. We appreciate your appearance and your contribution.

Mr Strong—Sorry I did not put a submission in beforehand. I did not have time.

CHAIRMAN—That is okay. We would appreciate it if you could follow up on those couple of points.

Mr Strong—And I will contact the Tyro people.

CHAIRMAN—If you could do that, it would be of great help to the inquiry. Thank you very much.

Mr Strong—Thank you.

CHAIRMAN—I thank everybody for their assistance, including the committee secretariat, Hansard and the committee members.

Committee adjourned at 1.54 pm