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APRA-TREASURY LIAISON MEETING

Date:	Monday, 10 December 2018
Time:	2:30 pm - 4:30 pm
Location:	APRA offices, Level 12, 1 Martin Place

Agenda items

	Item for discussion
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5.	Update on the Business Growth Fund – post Treasurer roundtable (Treasury)
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5 Update on the Business Growth Fund (Treasury)

- **Note** that NAB has agreed to lead a working group of banks (and potentially a superannuation fund and general insurer) to progress the development of the Business Growth Fund (BGF). Treasury has agreed to support the working group and the regulators have agreed to engage with the group as required. The working group will aim to report back to the Treasurer on progress in February 2019, with the first working group meeting organised for the week beginning 10 December 2018.
- **Seek** APRA agreement to clarify the conditions it is seeking the BGF adhere to so that banks participating in the working group have some certainty on the regulatory arrangements. This will allow the participants to begin development of a business model for the BGF.

Background

- The Government announced on 14 November 2018 that it was endorsing the creation of the private sector-owned Australian Business Growth Fund to provide equity finance to SMEs. The Fund is based on a model that has been adopted in the United Kingdom and Canada.
 - The fund offers equity investments (holding minority stakes of between 10-40 per cent) and mezzanine debt of greater than \$2 million, targeting businesses in the scale-up phase.
- On 6 December 2018, the Treasurer chaired a roundtable with key stakeholders to secure private support for the Fund. In attendance at this roundtable was the Governor of the Reserve Bank of Australia and representatives from the major banks, a superannuation fund, key regulators, the Council of Small Business of Australia, the Australian Banking Association and the Australian Small Business and Family Enterprise Ombudsman.
 - APRA provided the roundtable with an update on their view of the capital treatment of the fund and the conditions needed to enable a concessional capital treatment, a critical component of the banks commercial consideration to participate.
- To differentiate the BGF from other funds, APRA has proposed the Treasurer write to the Chair of APRA, stipulating certain conditions on the BGF. The letter is to include:
 - that the Government appoint the inaugural chairperson. Future chairpersons will be required to be independent of the shareholder entities in the fund;
 - the fund will be required to have broad participation, being open at least, to all ADIs with no APRA regulated institution having a controlling interest;
 - the fund will be required to be governed, and its investments managed, independently of its shareholder entities; and
 - the fund will have an annual reporting obligation to disclose publicly its investment activities.
- APRA have also provided Treasury with a list of conditions for the participating shareholders and the BGF more broadly. These conditions include:
 - ADI investment of up to 2 per cent of its common equity tier 1 capital in the BGF;
 - BGF has a clear purpose and is not for routine business lending purposes; and
 - The BGF must not be allowed access to leverage and must be wholly equity funded.

TREASURY MINISTERIAL SUBMISSION

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PDR No. MS18-003055

Treasurer

THE BUSINESS GROWTH FUND

Timing: You have requested information on the Business Growth Fund ahead of your meeting with s22 on Tuesday, 18 September.

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s22 APRA is currently considering the proposal and has informally indicated it is not opposed to making accommodations for the BGF.

Laura Llewellyn
Senior Adviser
Financial System Division
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Contact Officer: s22

Consultation: s22 Australian Prudential Regulation Authority, s22

The Australian Business Growth Fund

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APRA is currently considering the proposal and has informally indicated it is not opposed to making accommodations for the BGF, subject to certain risks being mitigated.

SUPPORT FOR SMEs - NARRATIVE

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- APRA is currently considering its treatment of a BGF type fund, and has informally indicated it is not opposed to making accommodations on the regulatory treatment of banks' equity in a BGF.
 - APRA's capital requirements have "risk weights" because different types of loans have different risk profiles. The more risky a loan is, the higher the risk weight, and the more capital the bank is required to hold with respect to that loan.
 - From a bank's perspective, a higher risk weight means that the bank must charge slightly more interest to the borrower, or accept a slightly lower return, with respect to the loan.
 - : For example, the average risk weight for standard residential mortgages is around 25% for the major banks. The risk weight for reverse mortgages is 100% (where LVR > 60%). The risk weight for "margin loans" is 400%.
 - Certain types of exposures (such as shares in an entity such as the BGF) are materially more risky than loans. Under APRA's long-standing capital rules, where a bank makes an equity investment, this is treated as a "capital deduction" (also known as a "regulatory adjustment").
 - : A good "rule-of-thumb" is that a deduction is roughly equivalent to a risk weight of 1250%.
 - In practical terms, this means that if banks' funding to the BGF were structured as an equity investment, it may not be economical for the banks unless APRA were to determine an alternative capital treatment were applicable, or the banks were to accept a materially lower rate of return.

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- APRA is currently considering its treatment of a BGF type fund, and has informally indicated it is not opposed to making accommodations on the regulatory treatment of banks' equity in a BGF.

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Secretary Meeting Brief

11.30am, Friday, 19 October 2018 — Treasury

Meeting with Kate Carnell, Australian Small Business and Family
Enterprise Ombudsman

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: Treasury has facilitated discussions between APRA and NAB about the alternative capital treatment of such a fund.

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Australian Business Growth Fund – Working Group Meeting

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If agreement is reached, APRA is currently contemplating a risk weight of 250% for ADIs equity exposures to the fund.

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AUSTRALIAN BUSINESS GROWTH FUND – STAKEHOLDER MEETING AGENDA - DRAFT

Date: Thursday 6 December 2018

Time: 10:30 – 11.30am

Location: TBC

Item	Agenda item	Report by	Format	Time
1.	Opening remarks	Treasurer	Verbal	10:30am
1.1	Introductions and apologies			
1.2	Role of a Business Growth Fund in improving access to finance for Australian businesses			
2.	Update on small business lending conditions	RBA Governor	Verbal	10:40am
3.	Update on regulatory issues - APRA representative on capital treatment of equity investments into an Australian BGF	APRA	Verbal	10:45am
4.	Update on international experience - experience with the BGF in the UK and Canada	HSBC	Verbal/Slides	10:50am
5.	Questions on BGF and international experience	All	Verbal	10:55am
6.	Views on an Australian BGF	All	Verbal	11:05am
7.	Next steps	All	Verbal	11:15am
8.	Closing remarks	Treasurer	Verbal	11:25am

AUSTRALIAN BUSINESS GROWTH FUND

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APRA is currently considering the proposal and has informally indicated it is not opposed to making accommodations for the ABGF, subject to certain risks being mitigated.

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ATTACHMENT A – AGENDA AND ATTENDEES

Australian Business Growth Fund – Stakeholder Meeting Agenda

Date: Thursday 6 December 2018

Time: 10:30 – 11.30am

Location: MG.63, Parliament House

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6.	Views on an Australian BGF	All	Verbal	11:05am
7.	Next steps	All	Verbal	11:15am
8.	Closing remarks	Treasurer	Verbal	11:25am

Roundtable Attendees

The Hon Josh Frydenberg MP	Treasurer	
Senator the Hon Michaela Cash	Minister for Small and Family Business, Skills, and Vocational Education	
Dr Philip Lowe	Governor	RBA
Ms Leigh O'Neill	Customer Executive, Small Business and Business Direct	NAB
Mr David Lindberg	Chief Executive Officer, Business Bank	Westpac
Mr Adam Bennett	Group Executive, Business and Private Bank	CBA
Mr Dean Firth	Head of Business Banking	Macquarie Bank
Mr James Chew	Global Head, Regulatory Strategy	HSBC
Mr Noel McNamara	Chief Risk Officer	HSBC Australia
Mr Stuart Wilson	Portfolio Manager	AustralianSuper
Mr John Lonsdale	Deputy Chair	APRA
Mr Scott Gregson	Executive General Manager, Merger and Authorisation Review	ACCC
Ms Diane Brown	Deputy Secretary, Markets Group	Treasury
Ms Kate Carnell	Ombudsman	ASBFEO
Ms Anna Bligh	Chief Executive Officer	ABA
Mr Peter Strong	Chief Executive Officer	COSBOA

ATTACHMENT B – ANNOTATED AGENDA

1. Opening Remarks

Introductions and apologies

- Thank you all for joining myself and Senator Cash today for this roundtable to discuss the establishment of an Australian Business Growth Fund.
- Around the table we have senior representatives from the major banks, AustralianSuper, the Australian Small Business and Family Enterprise Ombudsman, the Australian Bankers Association and the Council of Small Business of Australia.
- I am particularly grateful to James Chew who has flown all the way from London to join us today.
- We are also joined by the Governor of the Reserve Bank, key regulators, and of course my own department.
- I would like to start by saying that I see this roundtable as an opportunity to gauge interests, raise concerns and agree on the next steps for establishing the BGF in Australia.

Role of Business Growth Fund

- As you know, on 14 November I announced that the Government was endorsing the creation of an Australian Business Growth Fund to provide equity finance to SMEs.
- There are over 2.2 million SMEs in Australia, accounting for around two-thirds of private sector employment and creating a substantial proportion of new jobs
- Ensuring that these businesses have access to finance is important for their growth and the creation of jobs in the economy.
- Overall, SME conditions and confidence continue to be strong and a significant majority of SMEs are able to access suitable finance, particularly when using property as security.
- However, there are ongoing concerns and gaps about the price of that finance. The proportion of small businesses that perceive it to be relatively easy to access finance has recently declined.
- Equity is an alternative to debt finance and may well be more suitable for businesses without access to collateral looking to scale up, but SMEs find it difficult to access equity beyond family and friends.

- While private equity and venture capital financing is sometimes available, its supply is limited, terms can be restrictive and control of the business can be lost.
- To help SMEs accessing equity finance, we are encouraging the establishment of the private sector-owned Australian Business Growth Fund.
- The creation of the Australian BGF follows the establishment of a BGF in the UK in 2011 and more recently in Canada this year.
- These Funds are making a real difference – with the UK BGF having a financing capacity of around 4.5 billion Australian dollars and the Canadian BGF on track to grow to over 1 billion Australian dollars.
- I have convened this roundtable today so we could all work together to reach agreement with the banks and regulators to progress the development of a similar Fund in Australia.
- Of course, I accept that this is a very complicated proposal and there will be a number of issues to sort through.
- What I am looking for at the conclusion of this meeting is a clear way forward, where this group can develop a proposal that draws on all the experience in this room and delivers real results for Australian small businesses.

2. Update on small business lending conditions

- I would now like to invite Dr Phil Lowe, the Governor of the RBA to give a brief update on small business lending conditions in the Australian economy.

5 minute presentation

- Thank you Dr Lowe for that update. It is clear that small businesses' perception of their ability to access finance has declined in recent years and the Government sees the Business Growth Fund as a vehicle to improve the flow of finance to those businesses.
- I should at this point acknowledge the excellent work of Kate Carnell who also identified the BGF as a key priority in her June 2018 report *Affordable capital for SME Growth*.

3. Update on Regulatory issues

- For the BGF to succeed, the Government recognises the importance of the involvement of the major banks. Their participation in the fund will deliver a

strong flow of referrals, generating scale, keeping costs down and reducing risk via diversification.

- We recognise that the regulatory treatment of banks' equity investment into the fund is critical to their commercial consideration to participate.
- I would like to invite Mr John Lonsdale, Deputy Chair of APRA to provide us with APRA's views on the capital treatment of the fund and the conditions needed to enable a concessional capital treatment.

5 minute presentation

- Thank you Mr Lonsdale for that update. We look forward to working with APRA to accommodate this concessional regulatory treatment.

4. Update on international experience

- I now would like to invite Mr James Chew, Global Head of Regulatory at HSBC to share his experience of the BGF in the UK and Canada.

5 minute presentation

- Thank you Mr Chew. We appreciate you flying to Australia to share your experience with us. It is clear that the BGF has been successful in the UK and Canada and I look forward to similar success in Australia.

5. Questions on BGF and international experience

- I now open the roundtable for general discussion and questions on the international versions of the BGF.

Allow 10 minutes for open discussion

6. Views on an Australian BGF

- Thank you for that insightful discussion. I would like to go around the room now and seek everyone's views and concerns regarding the development of the Australian BGF. [Note: You may wish to ask Ms Leigh O'Neill from NAB to speak first, given NAB have indicated informally that they would be prepared to lead a working group to develop a proposal for an Australian BGF.]

Allow 10 minutes for participants to share their views

7. Next steps

- Thank you all for your views on the development of the Australian BGF. It is clear to me that there is a lot of support for this idea and that there are a range of issues that needed to be ironed out before we can establish the BGF in Australia.
- [As suggested by NAB] I would like to propose the establishment of a Working Group to take this idea forward. I think NAB are in a great position to lead the Working Group, and of course my department can provide assistance as needed.
- It's probably best if the Working Group includes the private sector members to begin with, noting that the regulators are available to meet with the Working Group as required.
- I would like to suggest that this group reconvenes in the sitting weeks in February to discuss the progress that has been made.
- I now open the roundtable to seek views on this proposal.

Allow 10 minutes for discussion

8. Closing remarks

- I would like to thank you all for your attendance and participation in the roundtable today. The discussion was insightful and comprehensive.
- I want to reiterate the Government's endorsement of the Fund. We see the Fund as a vehicle to improve the provision of finance to SMEs that will benefit the Australian economy more broadly.
- I look forward to meeting with you to discuss progress with the implementation strategy of the Working Group in the new year.

AUSTRALIAN BUSINESS GROWTH FUND – AGENDA AND ATTENDEES

Stakeholder Meeting Agenda

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Location: MG.63, Parliament House

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Dr Philip Lowe Ms Leigh O'Neill	Governor Customer Executive, Small Business and Business Direct	RBA NAB
Mr David Lindberg	Chief Executive Officer, Business Bank	Westpac
Mr Adam Bennett	Group Executive, Business and Private Bank	CBA
Mr Dean Firth Mr James Chew	Head of Business Banking Global Head, Regulatory Strategy	Macquarie Bank HSBC
Mr Noel McNamara Mr Stuart Wilson Mr John Lonsdale Mr Scott Gregson	Chief Risk Officer Portfolio Manager Deputy Chair Executive General Manager, Merger and Authorisation Review	HSBC Australia AustralianSuper APRA ACCC
Ms Diane Brown	Deputy Secretary, Markets Group	Treasury
Ms Kate Carnell Ms Anna Bligh Mr Peter Strong	Ombudsman Chief Executive Officer Chief Executive Officer	ASBFEO ABA COSBOA

Australian **BGF** – Conditions for In-principle Commitment

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- We assume that APRA will deliver on the 250% risk-weight as outlined by John Lonsdale in the meeting on 7 December and set out in further papers from APRA.

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HELPING SMALL BUSINESS GROW PACKAGE

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AUSTRALIAN BUSINESS GROWTH FUND

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APRA is currently considering the proposal.

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23 October 2018

PDR No.MS18-003577

Treasurer

cc: Assistant Treasurer

MEETING WITH APRA CHAIRMAN

Timing: You are scheduled to meet APRA Chairman, Mr Wayne Byres, on 24 October 2018.

KEY POINTS



- Background information on other agenda items proposed by Mr Byres are covered in Section B. s22



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Senior Advisor
Financial System Division

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- APRA continues to engage with relevant private sector parties regarding the capital treatment relevant to the proposed business growth fund;

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ACCESS TO FINANCE FOR SMALL AND MEDIUM BUSINESSES

FOI 3246
Document 14

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COALITION ACTION:

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- The Government is also in consultation with APRA and a number of financial institutions in regard to the establishment of an Australian Business Growth Fund that would provide longer term equity funding to small businesses. s22

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QTB Number:	QB18-000349	Adviser:	s 22
Contact Officer:	s22	Contact Number:	s22
Division responsible	Financial System Division		
Office Responsible	Treasurer		