

ARTICLE

Author

Carolina Brandao Nobili
Moody's Analytics

Contact Us

Americas
+1.212.553.1658
clientservices@moodys.com

Europe
+44.20.7772.5454
clientservices.emea@moodys.com

Asia (Excluding Japan)
+85.2.2916.1121
clientservices.asia@moodys.com

Japan
+81.3.5408.4100
clientservices.japan@moodys.com

The Australian Business Securitisation Fund in a Nutshell

Highlights

In face of the current status quo, where the big four banks in Australia account for over 80% of small business lending, often charging higher rates and imposing tougher conditions to grant these borrowers access to credit, the Australian Business Securitisation Fund comes as an alternative to facilitate the non-bank lenders' participation in this market and to promote more competition/liquidity and therefore better conditions for SMEs to secure a loan.

The creation of the fund is in early stages and the characteristics of the pool of assets and structure of the warehouses/securitisation deals that will be accepted/prioritised in the investment decisions are still not clear. In this report, Moody's Analytics presents a summary of what the new policy represents and what it entails.

Moody's Analytics markets and distributes all Moody's Capital Markets Research, Inc. materials. Moody's Capital Markets Research, Inc. is a subsidiary of Moody's Corporation. Moody's Analytics does not provide investment advisory services or products. For further detail, please see the last page.

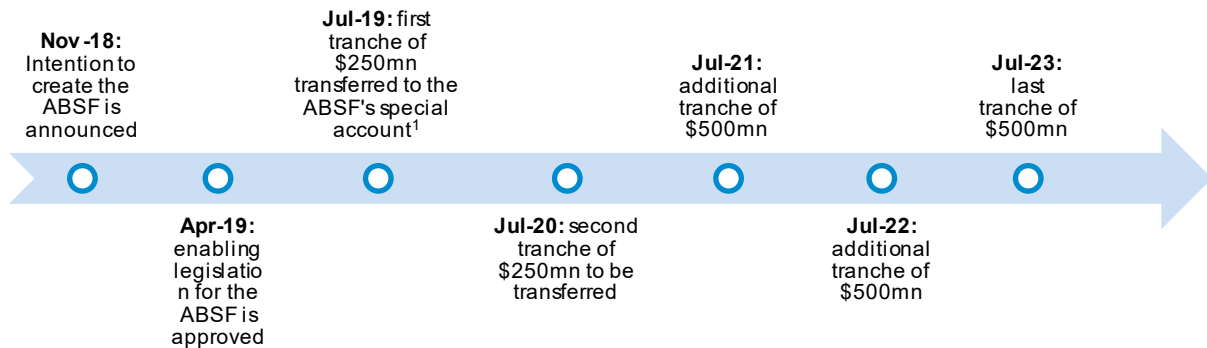
Table of Contents

- Australian business securitisation fund** 3
- Chronology** 3
- Definitions** 3
 - Authorised Debt Securities 3
 - Investment Decision-Making Strategies and Criteria 3
 - Investment Risk and Return 4
- Guidelines** 4
 - How Assessments Will Work? 4
 - Principles for ABSF Investment 4
- Conclusion** 5
- References** 5

Australian business securitisation fund

The Australian Business Securitisation Fund (ABSF) is a \$2 billion taxpayer-backed fund aiming to boost competition in the small to medium enterprises (SMEs) lending market – in other words, increase the availability and/or reduce the cost of credit provided to small business owners. It will be administered by the Australian Office of Financial Management (AOFM) and will target investments in securitisations of loans made by SME eligible lenders, via warehouse facilities or term deals. The expectation is that the development of market infrastructure to nurture the securitisation of SME loans can become an important component to attract additional (private) capital to the sector over the longer run.

Chronology



¹ Although \$250 million is already available for investment in the current financial year, AOFM is still to call for proposals. The transaction assessment process is not yet finalised as an Investment Manager for the purpose has not been hired.

Definitions

Authorised Debt Securities

As stipulated by law, the fund can only invest in authorised debt securities:

- » Issued by: (i) a trust or (ii) a special purpose vehicle.
- » Expressed in Australian dollars (AUD).
- » Related to secured or unsecured credits of a maximum of \$5 million each provided to debtors wholly or predominantly for business purposes – loans should not predominantly relate to businesses with a primary purpose of investing, such as superannuation funds.
- » Related to credits not provided by: (i) a major bank or (ii) a subsidiary of a major bank, being a major bank a deposit-taking institution subject to the Major Banking Levy Act 2017.
- » Not related to first loss securities – avoiding investment in first loss securities reduces risk and moral hazard for the Fund.
- » Compliant with any other requirements or restrictions to be prescribed by the rules.

Investment Decision-Making Strategies and Criteria

Investment decisions will follow the below priorities:

- » Investments in underdeveloped sectors of the SME securitisation market – there is a lot of confusion on what “underdeveloped sectors of the SME securitisation market” means. Some market participants assumed this is likely to mean focus on loans coming from industry sectors representing a bottleneck to production and/or productivity. Others understood that it might refer to the number of products available or players with capacity to lend for SMEs.
- » Investments that will help on the long term development of the SME securitisation market.
- » Investments that attracts the private sector into investing in the SME securitisation market.
- » Investments that are likely to promote competition between providers of credit to small and medium enterprises.

- » Investments in debt securities that do not relate wholly or predominantly to credit provided for investments in financial assets or residential properties.

In addition to the priorities listed, the following must be considered:

- » Whether an investment in a security whose rate of return expected is lower than the market rate is really required.
- » Whether the investment will affect the ability of the Fund to exit the SME securitisation market in the long-term without significant market disruption.

Investment Risk and Return

The financial return on the investments of the ABSF is the net return which is the return after management costs and any credit losses have been deducted and the Fund should:

- » Have an acceptable but not excessive level of risk.

Achieve over the medium term (5-10 years) a net financial return not lower than the AusBond Treasury 0-1 Yr Index.

Guidelines

Due to the heterogeneous nature of the market, the AOFM will be taking a principles-based approach to act as assessment criteria against which investment proposals will be evaluated. The principles are grouped under two categories: **market impact** and **risk management** and will serve as a reference for initial assessments in order to produce a shortlist for investment decisions.

How Assessments Will Work?

AOFM will provide more detailed instructions once it calls for proposals. This is likely to include both an invitation to proponents to directly address the investment principles and a request for a description of the lender's operating model, product range and market coverage, including both qualitative and quantitative information regarding loans under management, such as loan book size, historic arrears and loss rates, the range of interest rates charged and a breakdown of security types. Shortlisted proposals will undergo a comprehensive due diligence and credit risk analysis.

Principles for ABSF Investment

Market Impact

- » Sustainable impact: How the proposed investment will impact the SME lending market and associated capital markets?
- » Transparency: Is the proponent willing to enhance data reporting and disclose certain aspects of the transaction to give potential investor a better visibility of the market?
- » Additionality/additivity: Related to sustainable impact, how will the proposed investment help attract non-ABSF investments to the SME lending market?
- » Competition: How would the proposed investment increase competition for SME lending generally?

Risk Management

- » Institutional quality: Is the proponent a reputable institution and is its operating model and business strategy aligned with the longer term objectives of the ABSF?
- » Lending practices: Can the proponent demonstrate good governance and how it models good practice in lending assessment, servicing and collections?
- » Social responsibility: How does the proponent manage ESG risks? This includes unfair contract terms, AML/CTF and reputational risk.
- » Transaction risk profile: What is the risk profile of the structure of the transaction? And the credit quality of the underlying assets? Is the pool diversified?
- » Compliance: Does the proposed transaction comply with the ABSF Act, ABSF Rules and ABSF Investment Mandate Directions? Can the proponent demonstrate its ability and willingness to comply with these as well as additional, transaction-specific reporting requirements over the life of the transaction?

Conclusion

The available documents on the ABSF are high level and more detailed, operational documents should be issued to provide clarification on the specifics of how the fund will operate. The AOFM has committed to provide next steps on the submission and assessment process. The role of the above listed ABSF Investment Principles in filtering proposals should also be explained, and there will be a discussion of the information that SME lenders are likely to be asked to provide as part of their submissions.

It is clear that carefully developed eligibility criteria will be critical to the effectiveness of the legislation. Moody's Analytics and our team of securitisation experts are engaged in working with our clients to understand the criteria and how our solutions can contribute and help proponents in gathering the necessary information/data to participate in the assessment process.

References

The Australian Government Treasury and Australian Office of Financial Management websites:

- » <https://treasury.gov.au/consultation/c2018-t349315>
- » <https://www.aofm.gov.au/absf>

Policy documents from the Australian Government:

- » Exposure Draft Legislation
- » Explanatory Memorandum
- » Investment Mandate

© 2020 Moody's Corporation, Moody's Investors Service, Inc., Moody's Analytics, Inc. and/or their licensors and affiliates (collectively, "MOODY'S"). All rights reserved.

CREDIT RATINGS ISSUED BY MOODY'S INVESTORS SERVICE, INC. AND/OR ITS CREDIT RATINGS AFFILIATES ARE MOODY'S CURRENT OPINIONS OF THE RELATIVE FUTURE CREDIT RISK OF ENTITIES, CREDIT COMMITMENTS, OR DEBT OR DEBT-LIKE SECURITIES, AND MATERIALS, PRODUCTS, SERVICES AND INFORMATION PUBLISHED BY MOODY'S (COLLECTIVELY, "PUBLICATIONS") MAY INCLUDE SUCH CURRENT OPINIONS. MOODY'S INVESTORS SERVICE DEFINES CREDIT RISK AS THE RISK THAT AN ENTITY MAY NOT MEET ITS CONTRACTUAL FINANCIAL OBLIGATIONS AS THEY COME DUE AND ANY ESTIMATED FINANCIAL LOSS IN THE EVENT OF DEFAULT OR IMPAIRMENT. SEE MOODY'S RATING SYMBOLS AND DEFINITIONS PUBLICATION FOR INFORMATION ON THE TYPES OF CONTRACTUAL FINANCIAL OBLIGATIONS ADDRESSED BY MOODY'S INVESTORS SERVICE CREDIT RATINGS. CREDIT RATINGS DO NOT ADDRESS ANY OTHER RISK, INCLUDING BUT NOT LIMITED TO: LIQUIDITY RISK, MARKET VALUE RISK, OR PRICE VOLATILITY. CREDIT RATINGS, NON-CREDIT ASSESSMENTS ("ASSESSMENTS"), AND OTHER OPINIONS INCLUDED IN MOODY'S PUBLICATIONS ARE NOT STATEMENTS OF CURRENT OR HISTORICAL FACT. MOODY'S PUBLICATIONS MAY ALSO INCLUDE QUANTITATIVE MODEL-BASED ESTIMATES OF CREDIT RISK AND RELATED OPINIONS OR COMMENTARY PUBLISHED BY MOODY'S ANALYTICS, INC. AND/OR ITS AFFILIATES. MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS DO NOT CONSTITUTE OR PROVIDE INVESTMENT OR FINANCIAL ADVICE, AND MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS ARE NOT AND DO NOT PROVIDE RECOMMENDATIONS TO PURCHASE, SELL, OR HOLD PARTICULAR SECURITIES. MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS DO NOT COMMENT ON THE SUITABILITY OF AN INVESTMENT FOR ANY PARTICULAR INVESTOR. MOODY'S ISSUES ITS CREDIT RATINGS, ASSESSMENTS AND OTHER OPINIONS AND PUBLISHES ITS PUBLICATIONS WITH THE EXPECTATION AND UNDERSTANDING THAT EACH INVESTOR WILL, WITH DUE CARE, MAKE ITS OWN STUDY AND EVALUATION OF EACH SECURITY THAT IS UNDER CONSIDERATION FOR PURCHASE, HOLDING, OR SALE.

MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS, AND PUBLICATIONS ARE NOT INTENDED FOR USE BY RETAIL INVESTORS AND IT WOULD BE RECKLESS AND INAPPROPRIATE FOR RETAIL INVESTORS TO USE MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS OR PUBLICATIONS WHEN MAKING AN INVESTMENT DECISION. IF IN DOUBT YOU SHOULD CONTACT YOUR FINANCIAL OR OTHER PROFESSIONAL ADVISER.

ALL INFORMATION CONTAINED HEREIN IS PROTECTED BY LAW, INCLUDING BUT NOT LIMITED TO, COPYRIGHT LAW, AND NONE OF SUCH INFORMATION MAY BE COPIED OR OTHERWISE REPRODUCED, REPACKAGED, FURTHER TRANSMITTED, TRANSFERRED, DISSEMINATED, REDISTRIBUTED OR RESOLD, OR STORED FOR SUBSEQUENT USE FOR ANY SUCH PURPOSE, IN WHOLE OR IN PART, IN ANY FORM OR MANNER OR BY ANY MEANS WHATSOEVER, BY ANY PERSON WITHOUT MOODY'S PRIOR WRITTEN CONSENT.

MOODY'S CREDIT RATINGS, ASSESSMENTS, OTHER OPINIONS AND PUBLICATIONS ARE NOT INTENDED FOR USE BY ANY PERSON AS A BENCHMARK AS THAT TERM IS DEFINED FOR REGULATORY PURPOSES AND MUST NOT BE USED IN ANY WAY THAT COULD RESULT IN THEM BEING CONSIDERED A BENCHMARK.

All information contained herein is obtained by MOODY'S from sources believed by it to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, all information contained herein is provided "AS IS" without warranty of any kind. MOODY'S adopts all necessary measures so that the information it uses in assigning a credit rating is of sufficient quality and from sources MOODY'S considers to be reliable including, when appropriate, independent third-party sources. However, MOODY'S is not an auditor and cannot in every instance independently verify or validate information received in the rating process or in preparing its Publications.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability to any person or entity for any indirect, special, consequential, or incidental losses or damages whatsoever arising from or in connection with the information contained herein or the use of or inability to use any such information, even if MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers is advised in advance of the possibility of such losses or damages, including but not limited to: (a) any loss of present or prospective profits or (b) any loss or damage arising where the relevant financial instrument is not the subject of a particular credit rating assigned by MOODY'S.

To the extent permitted by law, MOODY'S and its directors, officers, employees, agents, representatives, licensors and suppliers disclaim liability for any direct or compensatory losses or damages caused to any person or entity, including but not limited to by any negligence (but excluding fraud, willful misconduct or any other type of liability that, for the avoidance of doubt, by law cannot be excluded) on the part of, or any contingency within or beyond the control of, MOODY'S or any of its directors, officers, employees, agents, representatives, licensors or suppliers, arising from or in connection with the information contained herein or the use of or inability to use any such information.

NO WARRANTY, EXPRESS OR IMPLIED, AS TO THE ACCURACY, TIMELINESS, COMPLETENESS, MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE OF ANY CREDIT RATING, ASSESSMENT, OTHER OPINION OR INFORMATION IS GIVEN OR MADE BY MOODY'S IN ANY FORM OR MANNER WHATSOEVER.

Moody's Investors Service, Inc., a wholly-owned credit rating agency subsidiary of Moody's Corporation ("MCO"), hereby discloses that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by Moody's Investors Service, Inc. have, prior to assignment of any credit rating, agreed to pay to Moody's Investors Service, Inc. for credit ratings opinions and services rendered by it fees ranging from \$1,000 to approximately \$2,700,000. MCO and Moody's investors Service also maintain policies and procedures to address the independence of Moody's Investors Service credit ratings and credit rating processes. Information regarding certain affiliations that may exist between directors of MCO and rated entities, and between entities who hold credit ratings from Moody's Investors Service and have also publicly reported to the SEC an ownership interest in MCO of more than 5%, is posted annually at www.moody.com under the heading "Investor Relations — Corporate Governance — Director and Shareholder Affiliation Policy."

Additional terms for Australia only: Any publication into Australia of this document is pursuant to the Australian Financial Services License of MOODY'S affiliate, Moody's Investors Service Pty Limited ABN 61 003 399 657 AFSL 33 6969 and/or Moody's Analytics Australia Pty Ltd ABN 94 105 136 972 AFSL 383 569 (as applicable). This document is intended to be provided only to "wholesale clients" within the meaning of section 761G of the Corporations Act 2001. By continuing to access this document from within Australia, you represent to MOODY'S that you are, or are accessing the document as a representative of, a "wholesale client" and that neither you nor the entity you represent will directly or indirectly disseminate this document or its contents to "retail clients" within the meaning of section 761G of the Corporations Act 2001. MOODY'S credit rating is an opinion as to the creditworthiness of a debt obligation of the issuer, not on the equity securities of the issuer or any form of security that is available to retail investors.

Additional terms for Japan only: Moody's Japan K.K. ("MJKK") is a wholly-owned credit rating agency subsidiary of Moody's Group Japan G.K., which is wholly-owned by Moody's Overseas Holdings Inc., a wholly-owned subsidiary of MCO. Moody's SF Japan K.K. ("MSFJ") is a wholly-owned credit rating agency subsidiary of MJKK. MSFJ is not a Nationally Recognized Statistical Rating Organization ("NRSRO"). Therefore, credit ratings assigned by MSFJ are Non-NRSRO Credit Ratings. Non-NRSRO Credit Ratings are assigned by an entity that is not a NRSRO and, consequently, the rated obligation will not qualify for certain types of treatment under U.S. laws. MJKK and MSFJ are credit rating agencies registered with the Japan Financial Services Agency and their registration numbers are FSA Commissioner (Ratings) No. 2 and 3 respectively.

MJKK or MSFJ (as applicable) hereby disclose that most issuers of debt securities (including corporate and municipal bonds, debentures, notes and commercial paper) and preferred stock rated by MJKK or MSFJ (as applicable) have, prior to assignment of any credit rating, agreed to pay to MJKK or MSFJ (as applicable) for credit ratings opinions and services rendered by it fees ranging from JPY125,000 to approximately JPY250,000,000.

MJKK and MSFJ also maintain policies and procedures to address Japanese regulatory requirements.