

2 September 2020

COSBOA Communiqué

The post COVID-19 ecosystem for SME finance

SYNOPSIS

COSBOA's COVID-19 roundtable seeks to engage SME representative industry bodies and related stakeholders in a discussion about current issues being experienced by SMEs in the wake of the COVID-19 economic downturn and the potential initiatives that could be progressed to support economic recovery and support job creation in the future. This latest meeting was conducted on **Friday, 28 August 2020**.

This particular meeting was the first in recent times where the discussion solely comprised COSBOA member organisations, facilitating the canvassing of somewhat 'routine' issues that were apparently constraining, or likely to constrain, the recovery of SMEs as the national economy commences the rebuilding process (albeit that Melbourne was still operating under Stage 4 restrictions and Regional Victoria remained subject to Stage 3 restrictions).

The subsequent conversation gave rise to a detailed conversation on two issues. The first related to the growing popularity of *Buy Now Pay Later* (BNPL) services and the second related to challenges associated with access to affordable finance products for SMEs.

A brief summary of these two themes is provided below.

KEY THEMES

- 1. Buy Now Pay Later (BNPL) products have a legitimate place as a merchant product but must be subject to the same regulatory oversight that applies to other payment/merchant services that are utilised and funded by SMEs.**
 - SMEs are reporting a significant growth in customer inquiries about BNPL options to accommodate product and service purchases in a post COVID-19 environment. Much of this inquiry appears to be generated from the Millennials cohort who are wary of building up unsustainable credit card debt.
 - One of the challenges of BNPL products, however, is the relatively high cost levied on the business when compared with traditional merchant services for debit card and credit card transactions. Essentially, BNPL is a consumer finance product (i.e. short-term loan) where the merchant is paying up to 7% of the transaction value in fees. This compares with an average between 1 and 2% for debit and credit card transactions.
 - BNPL providers suggest that the business will recover this cost as a result of being able to sell a greater volume of products and services via their electronic platforms, but this assertion is not supported by early SME experience. It is understood that most

businesses have entered into agreements with BNPL providers merely as a defensive mechanism to reduce revenue loss from this form of consumer payment – noting the growth in the use of these services from specific consumer cohorts.

- A secondary business benefit of BNPL mechanisms is that they minimise business exposure to *card-not-present* fraud which is an insidious and growing area of liability for merchants processing digital transactions (i.e. card not present fraud costs Australian businesses more than \$500M per year and accounts for around 85% of all credit card fraud in Australia).
- Roundtable participants agreed that BNPL solutions are a legitimate form of consumer payment to Australian merchants. As such, these solutions should be subject to the same transparency arrangements and regulatory requirements of the Australian Retail Payments (regulation) Act 1988 – as administered by the Reserve Bank of Australia – that are imposed on other merchant services (e.g. VISA and Mastercard systems, as well as EFTPOS).

2. Access to finance for SMEs is constrained at a time when SMEs need to be able to secure affordable finance to navigate the post COVID-19 recovery process. The cause for this constraint is likely due to multiple factors but must be addressed by the pursuit of coordinated actions to support SME recovery against a backdrop of extreme economic uncertainty.

- Numerous roundtable participants identified that their SME members are reporting substantial difficulty in accessing the financial products needed to support their recovery from the COVID-19 downturn, despite state/territory-government and Australian-government assistance with programs such as the Coronavirus SME Guarantee Scheme.
- This issue is being jointly pursued by COSBOA and ASBFEO with preliminary investigations suggesting that there appears to be a reduced appetite for SME lending, particularly among Tier 1 lenders. There appear to be multiple factors contributing to the lending difficulty being experienced by SMEs, including the legacy effects of the Hayne Royal Commission and the current interpretation of responsible lending laws by major banks and other Tier 1 financial institutions – leading to a decreased risk appetite. The practical issues associated with assessing an SME's capacity to repay a loan in the face of extreme uncertainty about the near-term economic outlook is also considered to be a significant factor.
- There appears to be an urgent need for all the actors in Australia's financial lending system (i.e. lenders, regulators, business and government) to work together to better understand the current impediments to SME lending and advance a solution to address this issues as a matter of priority.

-ends-