



SME lending in Australia

Australian Banking Association
Economic Report



Australian Banking
Association

August 2019

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Foreword

Small business¹ is the engine room of the Australian economy. Accounting for more than 40 per cent of all jobs or around 4.7 million people, their success is an integral part of the ongoing prosperity enjoyed by all Australians. From your regular coffee shop, to your friendly tradie, primary producer, beautician, pet walker or local greengrocer, small businesses are everywhere, in our cities, country towns and regional and remote Australia.

Lending to small businesses is essential for the growth and ongoing success of the Australian economy. It is the springboard by which small businesses can prosper. With borrowed funds, small businesses can grow their businesses, purchase and replace machinery, employ new staff and move into new markets.

Australian banks are open for business. Despite a decrease in the number of business loan applications being received, banks are still approving business loans at the same rate they always have. The cause of the recent decline in loan applications by small businesses in Australia is a question that the banking industry is keen to address.

This report provides an analysis of present trends in small business lending and aims to provide a basis for further discussion about what the banking industry can do to make it easier for small businesses to access finance.

A handwritten signature in blue ink, reading "Anna Bligh". The signature is fluid and cursive, with a long, sweeping underline that extends to the right.

Anna Bligh

August 2019

1. In this report small businesses are defined as businesses with less than 20 employees, including sole traders.

9 million

Australians have dreamed of starting their own business

60%

cited “access to money” as the reason holding them back

YouGov research, April 2019

Figure 1: YouGov research - ‘What type of business would you like to start?’ (%)*

		Men	Women	18-34	35-49	50+
Food / hospitality	24	20	28	26	20	25
Retail / clothing	23	17	31	28	21	18
Professional services	17	18	16	20	16	14
Technology / IT	16	24	7	18	19	8
Arts / sports / recreation	15	15	15	15	13	15
Educational	10	7	14	13	10	7
Healthcare	10	7	13	13	9	6
Accommodation	9	9	8	8	9	11
Trades / construction	8	12	5	10	9	6
Agri / horticulture	7	9	4	7	7	6
Finance	6	7	5	8	6	3
Other	10	8	13	9	6	18

Figure 2: YouGov research - ‘What is holding you back from starting your own business?’ (%)*

		Men	Women	18-34	35-49	50+
Access to money	60	55	65	67	59	51
Life circumstances	42	41	43	40	44	44
Lack of experience	36	31	42	43	40	21
Desire for income certainty	34	35	32	35	37	27
Lack of time	26	24	29	35	28	10
None of the above	6	6	5	1	3	16

*YouGov research conducted for the ABA, 3-5 April 2019.

Introduction

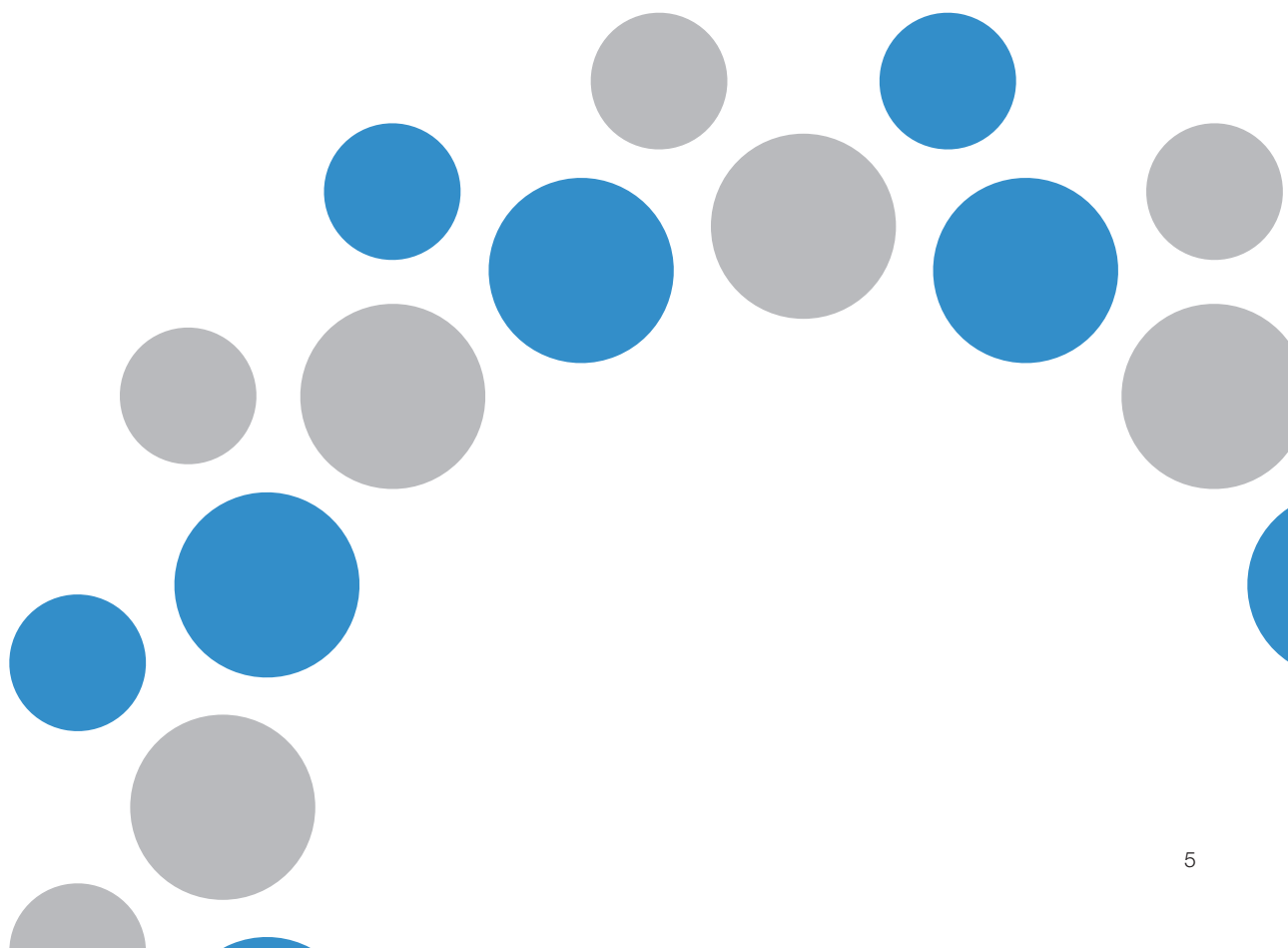
Most businesses in Australia are small businesses. Nearly two-thirds of all businesses are sole traders and around one-third employ less than 20 people. Small businesses have a lower chance of survival than larger businesses, with only 60 per cent of all sole traders and 70 per cent of businesses employing less than 20 people remaining in business after four years. In contrast, the survival rate for larger businesses hovers around 80 per cent.

Recent YouGov research estimates that nine million Australians have dreamed of working for themselves and starting their own business. However 60 per cent of these Australians (5.4 million) cited “access to money” as the reason holding them back.

The data in this report shows that many small businesses wait until the last minute to access credit. In 2017-18 nearly 1 in 3 small businesses sought credit to ensure the survival of their business, while 1 in 4 sought credit to replace equipment. Compared to large businesses, small businesses were much less likely to seek credit to upgrade or purchase new equipment.

At the same time, interest rates for loans to small businesses are at an all-time low, and bank approval rates for business loans remain steady. Yet fewer small businesses are approaching banks for credit. Only just over half (57 per cent) of small businesses employing 0-4 people who sought credit in 2017-18 approached a bank.

ABA member data shows a 33 per cent decline in business loan applications over the past five years, while approval rates remain at around 94 per cent.



Profile of small businesses in Australia

There are 2.31 million businesses in Australia - most of which (2.3 million or 98 per cent) are small businesses. Nearly two-thirds of all Australian businesses are sole traders, a quarter employ 1-4 people and one in twelve employ 5-19 people. Only a fraction of businesses employ more than 20 people.

The industry with the largest number of small businesses is construction, followed by professional, scientific and technical services and rental, hiring and real estate services.

Figure 3: Australian businesses by employment size, 2018 (%)*

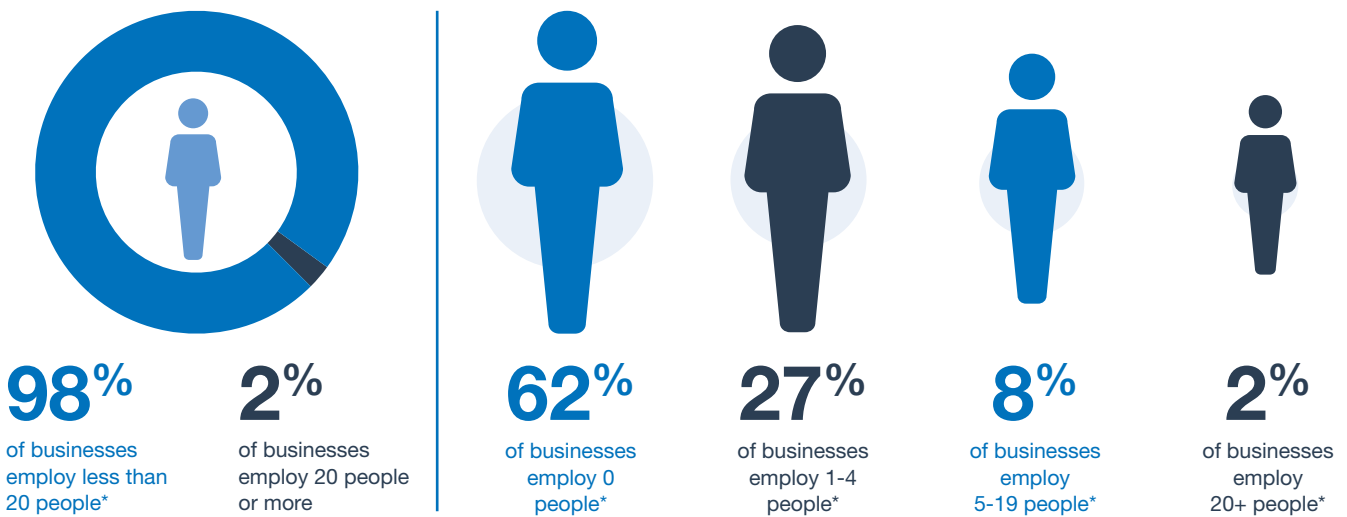
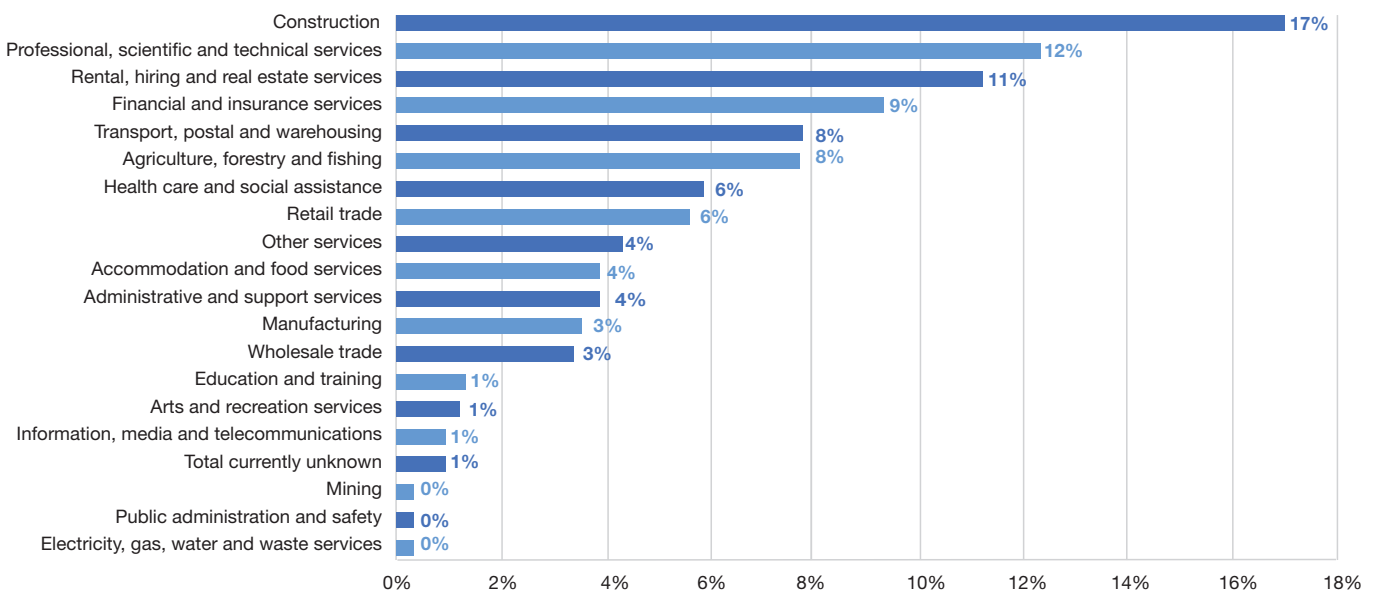


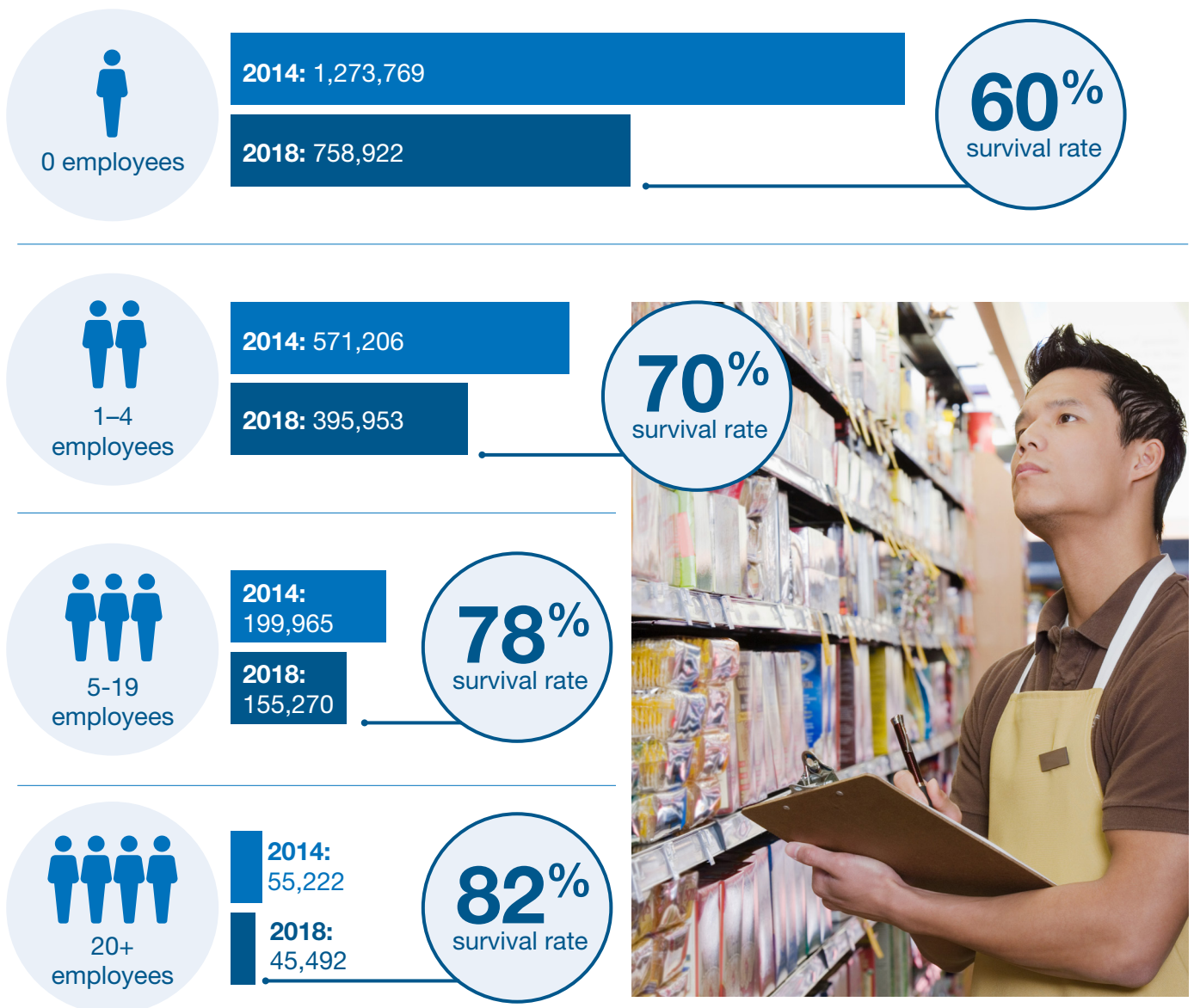
Figure 4: Distribution of businesses employing less than 20 people, 2018 (%)*



*Source: ABS, Counts of Australian businesses, including Entries and Exits, June 2014 to June 2018, Cat. No. 8165.0

Operating a small business can be difficult. More than half a million sole traders operating in June 2014 were no longer operating in June 2018, a survival rate of only 60 per cent. Chances of survival are greater for larger businesses.

Figure 5: Businesses operating in June 2014 still operating in June 2018, by Employment Size, 2014 - 2018 (#)*



*Source: ABS, Counts of Australian businesses, including Entries and Exits, June 2014 to June 2018, Cat. No. 8165.0

Small business access to finance

In 2017-18 only 12 per cent of businesses with less than five employees sought finance, compared with 20 per cent with 5-19 employees, 23 per cent with 20-199 employees and 34 per cent with 200 or more employees. The majority (86-87 per cent) of small businesses who seek finance are successful.

Figure 6: Business finance sought, by type and status, by employment size (%)*

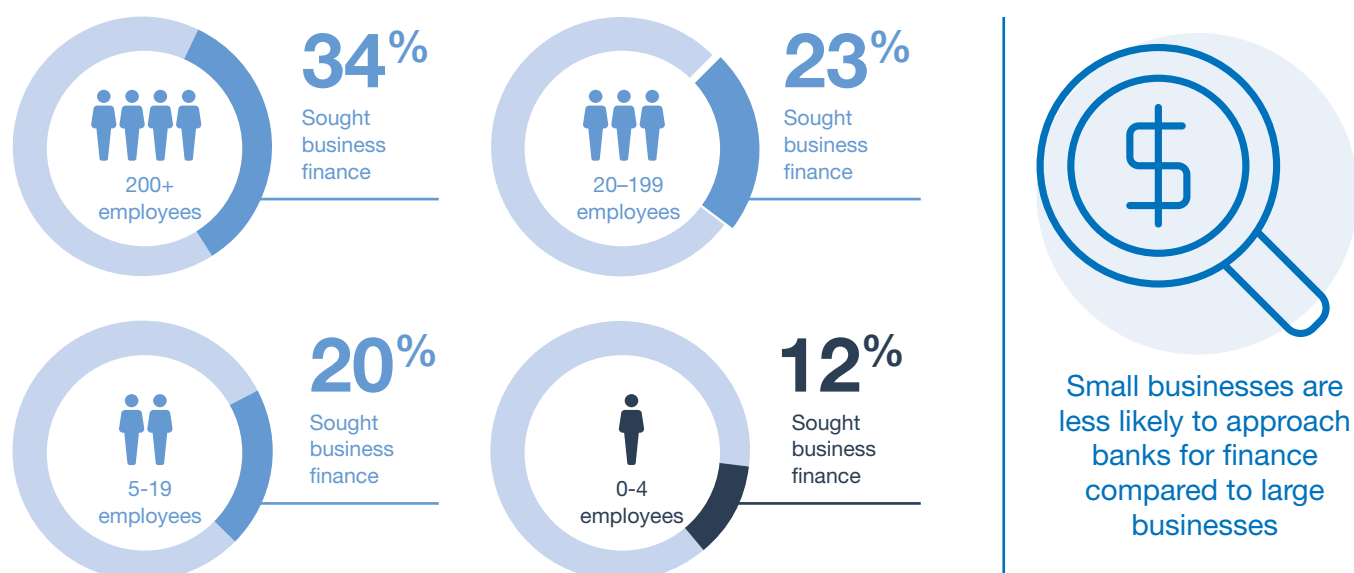
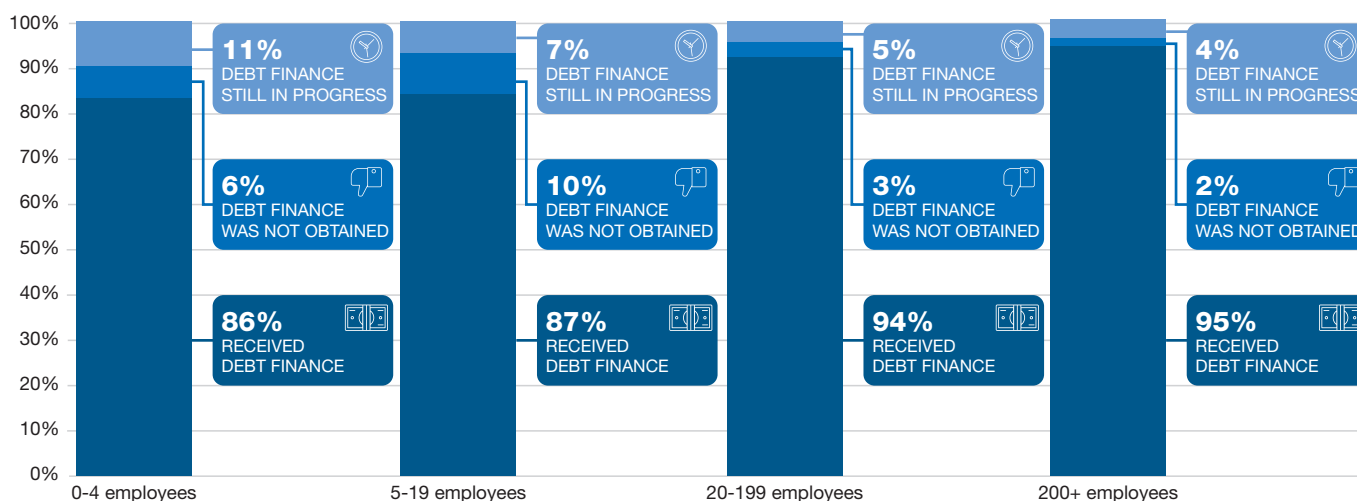


Figure 7: Businesses that obtained debt finance by employment size, 2017-18 (%)**



*Source: ABS, Characteristics of Australian Business 2017-18, Cat. No. 8167.0

#Note: numbers add up to more than 100 as question is multiple response

The most common types of credit obtained by small businesses were new credit cards and bank overdrafts.

Table 1: Type of finance obtained by employment size, 2017-18 (%)*

	0-4	5-19	20-199	200+
New loan with a term of more than one year	40.4	35.1	41.6 [^]	41.1 [^]
New capital/finance lease or hire purchase agreement	31.2	35.4	46.5 [^]	48.5 [^]
New loan with a term of one year or less	16.0	15.5	9.0	21.8
Increase in amount of existing credit facilities or limits	15.9	15.7	21.5	24.4
New bank overdraft	11.0	20.2	20.4	8.9
New credit card	10.8	12.2	16.9	29.8*
New mortgage loans	8.0	7.4	7.1	1.7
Other	3.1	1.8	4.5	12.1



*Source: ABS, Characteristics of Australian Business 2017-18, Cat. No. 8167.0

[^]Estimate has a relative standard error of 10% to less than 25% and should be used with caution

Small businesses are less likely to approach banks for finance compared to large businesses, and more likely to approach finance companies. Small businesses are also more likely to approach friends and family for finance than big businesses.

Figure 8: Businesses who approached banks for finance, by employment size 2017-18 (%)*

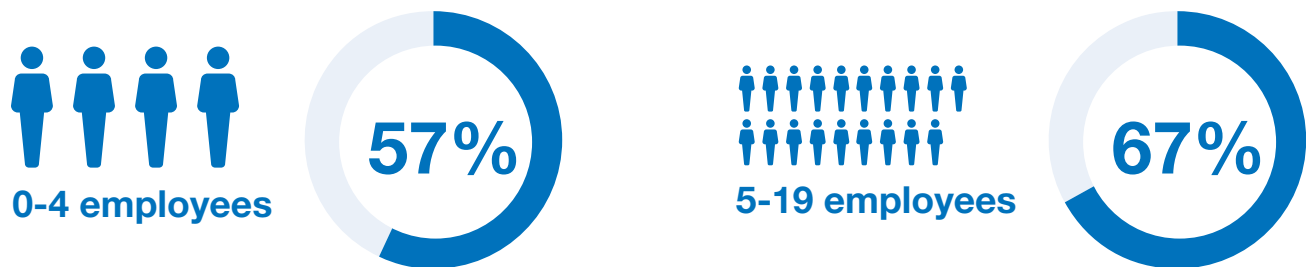


Table 2: Who was approached for finance, by employment size 2017-18 (%)*

Industry	0 to 4	5 to 19	20-199	200+	Total
Banks	56.6	67.1	83.4	83.5	64.0
Finance companies	42.4	33.4	31.7 [^]	21.0	37.4
Existing owner(s)	13.7	13.8	11.7	18.7	13.6
Friends or family existing owner(s)	12.3	8.5	2.1	0.0 [^]	9.5
Other individual(s)	2.8	2.1	0.0 [^]	0.9	2.3
Other businesses	3.2	2.0	4.3	3.4	2.8
Other	0.7	1.8	2.2	4.3	1.4

*Source: ABS, Characteristics of Australian Business 2017-18, Cat. No. 8167.0

[^]Estimate has a relative standard error of 10% to less than 25% and should be used with caution

Small business purpose for seeking finance

Of those businesses that accessed finance, many did so to replace equipment and machinery, regardless of size. Yet small businesses are less likely to seek finance to upgrade and purchase additional equipment. Instead, for many small businesses, finance is accessed as a last resort.

Figure 9: Top 3 reasons for seeking finance, businesses employing 0-4 people, 2017-18 (%)*

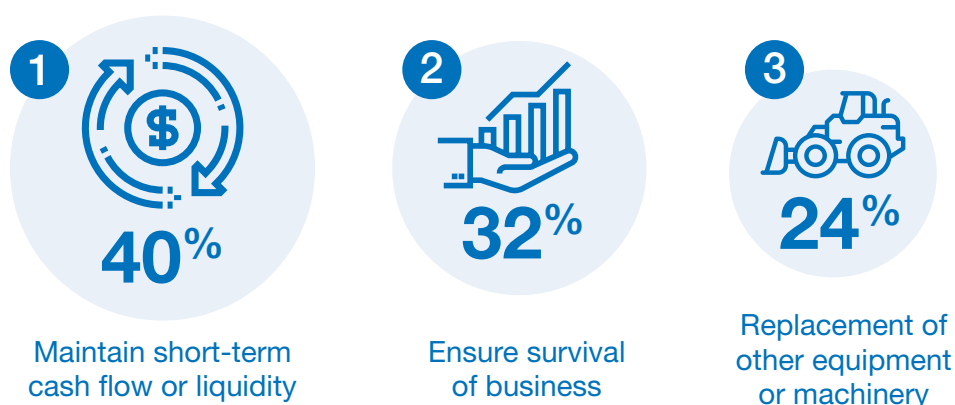


Table 3: Reasons for seeking finance, by employment size, 2017-18 (%)*

Industry	0 to 4	5 to 19	20-199	200+
Businesses that sought debt or equity finance	11.9	20.2	22.5	34.2
Ensure survival of business	31.5	29.9	11.7	3.9
Maintain short-term cash flow or liquidity	40.1	42.7	39.4	43.7 [†]
Replacement of:				
– IT hardware	3.1	4.5	5.4	13.4
– other equipment or machinery	24.2	30.7	31.9 [†]	31.1
Upgrade of:				
– IT hardware or software	2.7	5.9	7.6	15.5
– other equipment or machinery	13.3	15.2	19.8	20.1
Purchase of additional:				
– IT hardware or software	0.8	4.8	7.4	14.8
– other equipment or machinery	16.4	20.9	30.3 [†]	25.8
– assets not related to expansion	6.2	5.7	8.6	9.8

*Source: ABS, Characteristics of Australian Business 2017-18, Cat. No. 8167.0

[†]Estimate has a relative standard error of 10% to less than 25% and should be used with caution

Most small businesses are spending money on innovation.[^] For those small businesses that are innovation-active, the greatest barrier to further innovation is lack of access to funds.

Figure 10: Spending money on innovation, by employment size, 2016-17 (%)^{*}

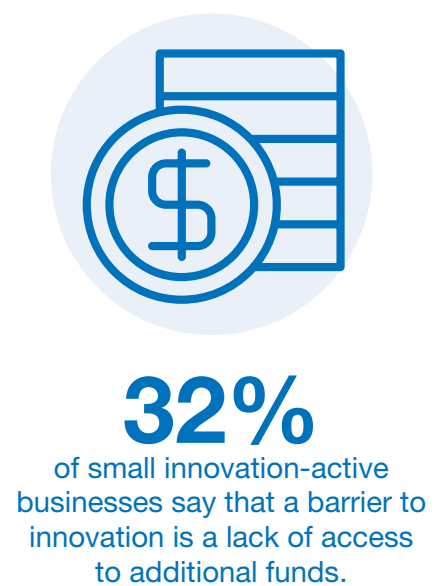
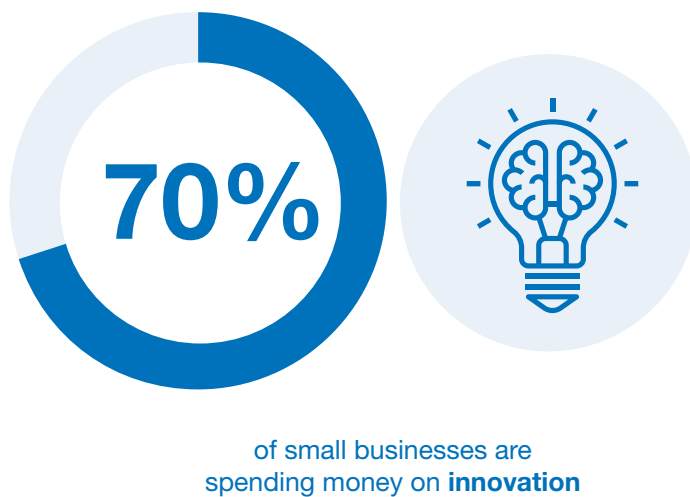


Table 4: Barriers to innovation for innovation-active businesses, by employment size, 2016-17 (%)^{*}

Industry	0 to 4	5 to 19	20-199	200+
Lack of skilled persons in any location	21.6	27.8	24.7	18.0
Cost of development or introduction/implementation	20.7	19.3	20.6	18.0
Uncertain demands for new goods or services	17.8	15.1	17.1	8.3
Lack of skilled persons within the business	17.3	19.9	16.0	14.1
Government regulations and compliance	11.5	11.4	8.7	12.8
Lack of skilled persons within the labour market	8.7	18.3	15.1	8.4
Lack of access to knowledge or technology to enable development or introduction/implementation	6.2	6.8	6.7	8.4
Adherence to standards	3.2	4.7	3.7	4.1

^{*}Source: ABS, Innovation in Australian business, 2016-17, Cat. No. 8158.0

[^]ABS defines innovation as new types of goods or services, operational processes, organisational/managerial processes, or marketing methods

SME demand for credit over time

The current credit environment should be facilitating small business borrowing. Business confidence outlook is in line with the long-term average, while interest rates on small business loans are at generational lows.

The weighted-average interest rate for small business loans (under \$2 million) has seen a long and sustained fall since June 2011. For most of the past 20 years the weighted-average interest rate has been between seven and eight per cent.

Figure 11: SME business confidence next three months (Index)*

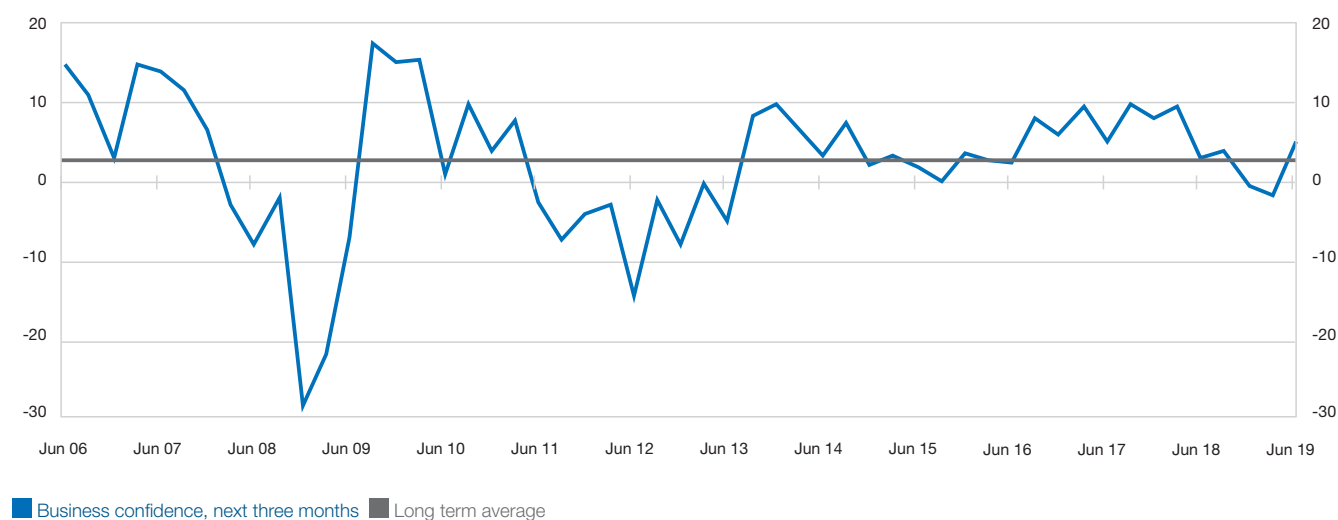
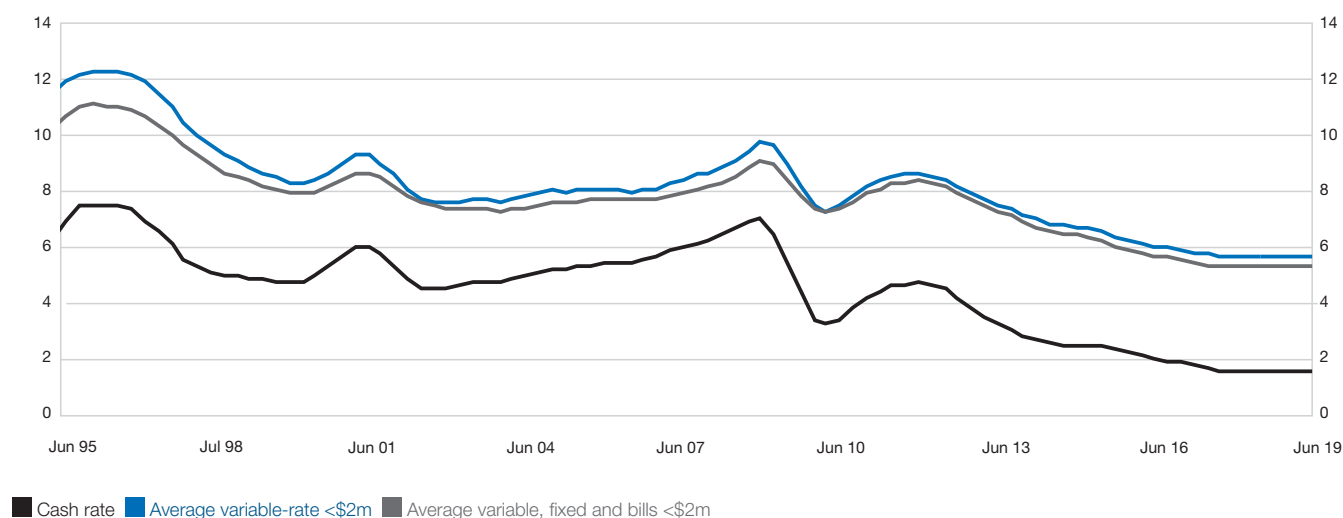


Figure 12: Average interest rate on business loans which are less than \$2 million (%)^



*Source: NAB Business survey, ABA analysis; NAB defines small enterprise as having a turnover of \$100,000 - \$5m; medium enterprises are defined as having a turnover of \$5m - \$10m

^Source: RBA Bank lending to business, March 2019; Data refers to weighted-average interest rates

New business loan approvals from banks have risen strongly over the 2018-19 year to the March quarter. New lending commitments have been driven by a surge in lending to larger businesses. The value of <\$2 million loan approvals has declined to \$283 billion, though there are early signs of improving demand for new SME loans.

Since 2014 there has been a 33 per cent decline in demand, or applications, for SME loans (loans <\$2 million). The rate at which banks approve small business loan applications has actually improved slightly over the past 18 months, at around 94 per cent. As a result, trends in loan approvals have tracked in line with changes in loan applications. There has been an encouraging lift in applications over the June quarter. Applications for new SME loans rose by 23% in the June quarter 2019, a much stronger rise than the average 15% increase over the previous 5 years.

Figure 13: New business loan commitments (rolling annual total), \$b*

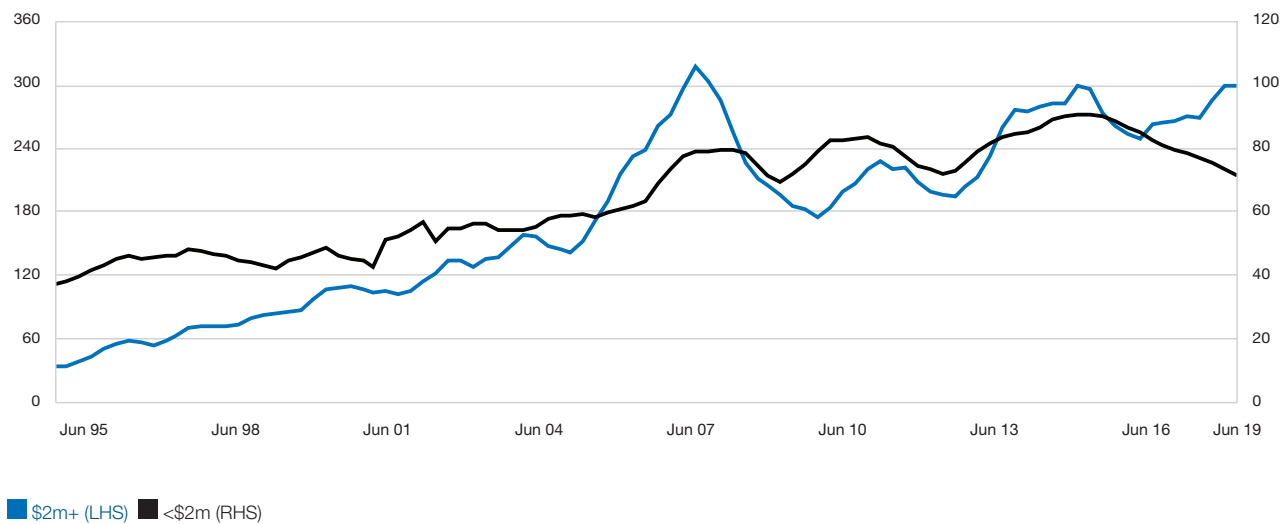
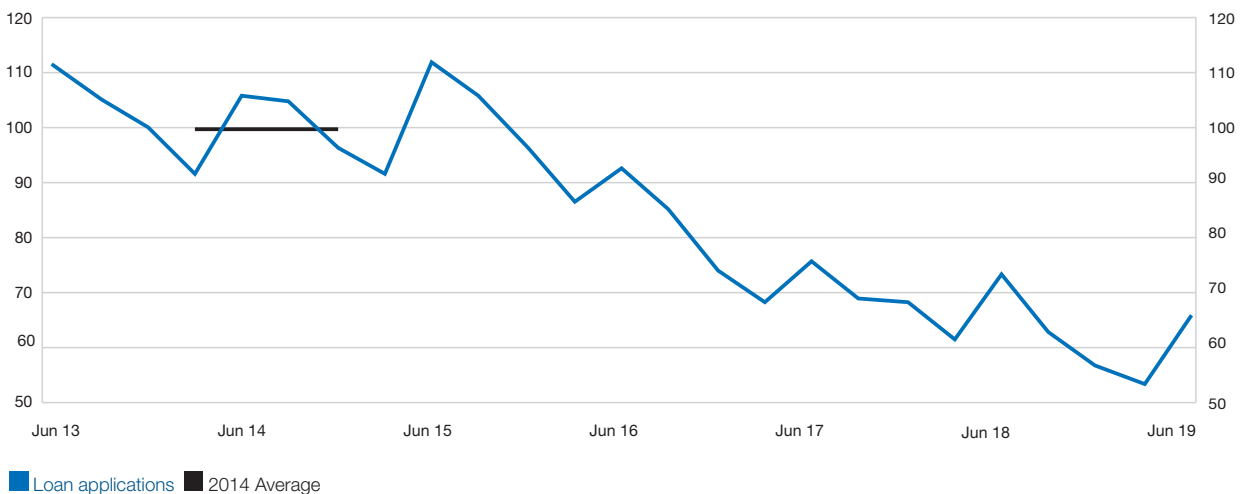


Figure 14: ABA surveyed banks – Small business loan applications, <\$2m (Index)^



*Source: RBA, Bank lending to business – New credit approval by size and purpose

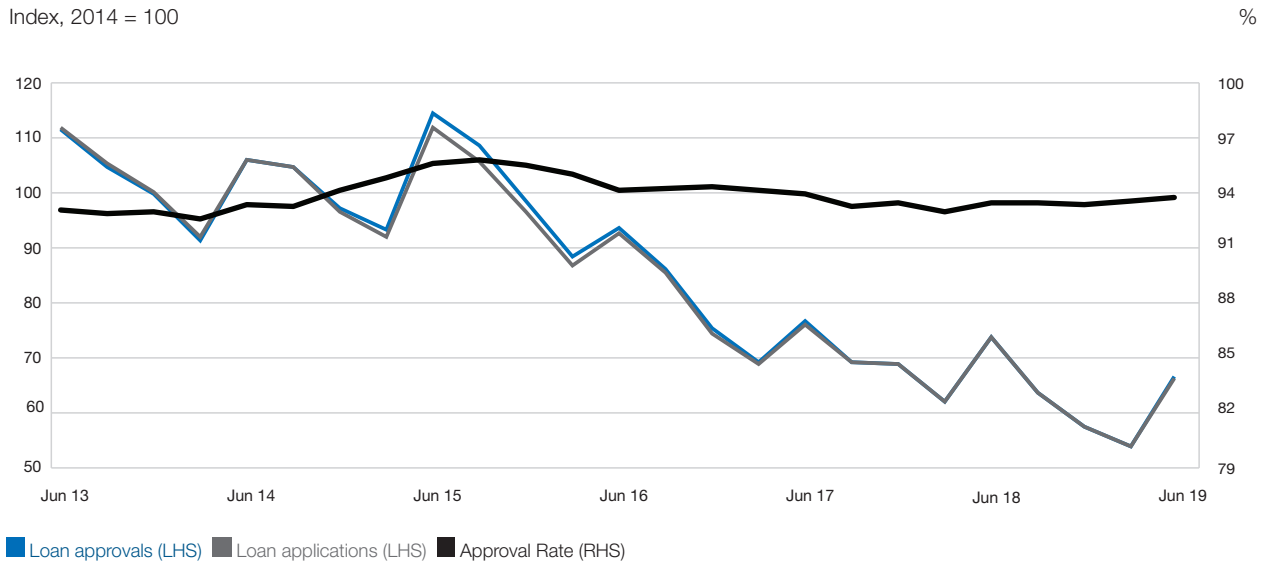
^Source: ABA member bank data, Note: Applications Index, 2014 = 100

With low interest rates, and sustained approvals, there remains a question of why there is subdued interest in new borrowing by small businesses.

The ABA, together with COSBOA and CPA Australia, have recently launched a website to assist small businesses considering applying for a loan with a bank.

For more information, visit www.financingyoursmallbusiness.com.au

Figure 15: ABA surveyed banks – Small business loan trends, <\$2m (Index, %)*



There has been a
33%
drop in loan applications since 2014



Banks have approved
94%
of small business loans

*Source: ABA member bank data. Note: Approvals and Applications Index, 2014 = 100; % = Approvals as percentage of applications



Australian Banking Association

Australian Banking Association Inc.
ARBN 117 262 978
(Incorporated in New South Wales)
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For more information contact:

James McIntyre
Principal Economist

Michelle Jakubauskas
Director, Research
and Data Management

(02) 8298 0417
reception@ausbanking.org.au

www.ausbanking.org.au