Financial Review - afr.com

Nov 25 2018 at 3:51 PM
Updated Nov 25 2018 at 3:51 PM

Bank of Mum and Dad fund 25pc of SME loans

by **Duncan Hughes**

Bank of Mum and Dad is being forced to fund more than 25 per cent of small and medium enterprise loans because of the credit crunch, which is being worsened by fall-out from the banking royal commission, according to small business Ombudsman Kate Carnell.

Falling residential property prices and rising rates are compounding the difficulty of getting loans because most lenders require SME bosses to put up their homes as collateral, Ms Carnell adds.

Borrowers with traditional lenders are being asked for deposits of up to 40 per cent and interest rates between 10 and 20 per cent, or up to nearly 10 times the rate of inflation, according to sector specialists.

"If we do not do something to make borrowing more affordable the engine room of the economy will run out of fuel," said Ms Carnell. "We are all the time hearing that small business cannot take the next step in manufacturing, retail, technology or tourism because they cannot access funding," she said.

SMEs employ about seven million and contribute nearly 60 per cent of gross domestic product, according to official numbers.

Brokers, who act as intermediaries between banks and small lenders, claim interest rates of between 10 and 20 per cent are being imposed for short term, unsecured loans of up to $50,000.

Most SME borrowers using their homes as security are facing unprecedented scrutiny of their domestic and business income and spending and much tougher property valuations, brokers claim.

"There is a bigger appetite for SMEs to work with non-traditional, second tier lenders who have faster processes; or they are seeking alternative forms of finance, such as debtor loans," said Neil Brennan, a director of business advisory for chartered accountants' William Buck. "Big four banks are lowering their thresholds since the royal commission."

Ms Carnell said Bank of Mum and Dad is also filling the finance vacuum by underwriting, or providing cash, for one in four SME business loans. This can create serious problems for families if the undertaking fails, or a child fails to repay the loan.

She expects the rate to increase in the absence of lower interest rates, easier borrowing terms or more government support.

Businesses are also being inhibited by terms and size of loans needed to take them to the next level, she says.

Bank of Mum and Dad, a term used to describe parents lending to their children for property purchases, is now the tenth largest lender, bigger than ME Bank, AMP Bank and the local operations of global banking giants like Citigroup and HSBC Australia.

Hamish Tagell, Australian equities portfolio manager for SG Hiscock, said the impact of falling prices on credit for SME and economic growth is an issue "we are monitoring closely".

The Morrison government is expected to inject $2 billion into the small business loan market in a bid to boost lending to cash-starved companies.

"Any move by the federal government to ease lending conditions will be welcomed," said Christopher Foster-Ramsay, principal of Foster Ramsay Finance, a finance broker.