AUSTRALIAN BANKERS' ASSOCIATION INC.

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Mr Paul Morris
First Assistant Secretary
Agricultural Competitiveness Taskforce
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Dear Mr Morris,

Agricultural Competitiveness Issues Paper

The Australian Bankers' Association (ABA) appreciates the opportunity to provide comments on the Federal Government's *Agricultural Competitiveness Issues Paper*. We note this is the first phase of consultation, with a white paper and green paper to follow this year. Therefore, our comments are intended to provide some initial high level input and insights into aspects of access to finance from the perspective of the banking industry. We anticipate that we will provide more substantive input into this consultation process as it progresses.

Opening remarks

The ABA supports the Federal Government's efforts to develop a platform for enhancing the contribution of the agriculture sector to economic growth through increased innovation, productivity, employment, investment and trade. We recognise the importance of the agriculture sector to our economy, and more broadly our community.

The banking industry has been a critical component of the agriculture sector since the late 1800s working with primary producers and farming businesses in rural and regional Australia. Banks take a long term view in managing agribusinesses through commodity price, business and seasonal cycles and managing their customers in these circumstances sensitively and supporting them through the challenging times. However, there are instances where banks are no longer able to support a business due to the adverse impact on the borrower and the bank in prolonging an unavoidable situation, and in these instances alternatives are needed. Banks are critically aware of the impact on farming families of their businesses becoming unviable.

Due to the volatility of earnings in the agriculture sector, agribusinesses require a greater level of equity relative to other industries. When agribusinesses do require debt, this is used to support short falls in working capital as well as finance investment in high cost assets (mainly land and machinery plant and equipment) that improves scale and productivity. Earnings from the agriculture sector available to service debt commitments are typically variable due to the vagaries of global market forces combined with more local influences, such as seasonal conditions, weather and climatic impacts, and risks of regulatory interventions.

Agri-sector loan contracts often have longer loan terms than other business sectors. However, not all agri-sector loans have long terms. For example, the agriculture sector also has a high level of use of overdrafts that are revolving facilities and not set for an extended term and a high level of equipment financing where the loan term is determined by the asset being financed. Borrowing large amounts of capital, whether it is to invest in increased scale, new technology or to implement a financial, business or succession plan can leave an agribusiness financially vulnerable to circumstances they cannot control. Banks' lending decisions take into account the fact that agribusinesses are susceptible to circumstances beyond their control. However, this is no different to other business sectors.

Having said that, the underlying value of loan contracts in the agribusiness sector are at risk from variable earnings and cash flows due to seasonal conditions, such as increased demand around the festive season or decreased production due to weather conditions. The underlying value of loan contracts is also at risk from indirect and direct regulatory intervention, such as direct regulatory risk including changes that affect the enforceability of loan contracts and indirect regulatory risk including regulation of the use of natural resources (land, water, vegetation and access to minerals and gas) and other interventions, such as animal welfare issues (live trade) and changes in industry policy (deregulation of industries).

When a bank assesses a loan application for an agribusiness customer, they take into account all available sources of income to meet loan commitments and all available assets that can be used as security for a loan. Every loan is assessed and reviewed on an individual customer basis. Focusing only on changes in rural debt to total receipts from a farm business will not tell you whether the debt level of individual farmers is either productive or sustainable, especially if that debt is supported by off-farm income and off-farm assets.

Delivering banking products and services to the agriculture sector is expensive due to the types of products and services demanded by the sector. However, the agriculture sector does provide a great opportunity to produce tailored banking products and services. Banks employ agribusiness and industry experts who travel to their customers to do business and provide face-to-face support. These bank staff have local knowledge and industry experience and provide specialised services to agribusiness customers, including financial insight and support needed to help manage the business effectively. For example, agribusiness bankers assist their agribusiness customers find the right products, understand how to manage agribusiness risk, create solid financial and business plans, and access specialised products. Having said that, the industry recognises that not all farmers have access to specialist bankers and industry experts.

Agriculture sector – Access to finance

Appendix 1 provides a snapshot of the agriculture sector in Australia.

The following provides some statistical highlights about lending and financing the agriculture sector, farm debt levels and future growth prospects:

- Lending from banks to the agriculture sector is approximately $61 billion (RBA).
- ABS data shows that 32% of agribusinesses sought debt finance over the two years to June 2011. In comparison, the average across all industries is 17% (Appendix 2, Table 1).
- The agriculture sector contributes a small amount of deposits (approximately $3.5 billion in FMDs) relative to its borrowings. (However, some farmers have indicated they prefer to maintain deposits in standard bank accounts.) This means that the high demand for debt from the agri-sector must be met by funding provided from other sectors, including industries, investors and households. Households in particular are paying down their own debts, which contributes to the scarcity of capital.
- The growth in credit outstanding in the agriculture sector from banks has averaged 1% over the last 4 years, while the average for all industries has been around 1.9% (RBA).
- ABS data shows that compared to other industry sectors, the agriculture sector has the lowest proportion of borrowers seeking finance who are unable to obtain it (Appendix 2, Table 2).
- Largest growth in debt has been businesses with turnover in excess of $500,000.
- Since 2007, debt for businesses with turnover less than $500,000 has decreased. Approximately half the debt taken on since 2004 has been to finance property purchase, followed by working capital, machinery plant and equipment, and reconstructed debt.
- Debt per hectare has increased consistent with increases in areas operated per farm and farm cash income per hectare increasing in real terms for farms with annual output in excess of $400,000.

- Around 70% of the broadacre sector debt was held by 12% of farms which produced 42% of total production at June 2012. 68% of broadacre farms were estimated to have equity greater than 90% at June 2012. Broadacre farms with equity less than 70% and negative cash incomes are around 4%.
- Bank Pillar 3[1] reporting indicates that impaired loans, including 90 days past due are estimated by the ABA to be around 3% of bank loans outstanding to the agriculture sector.

The ABA acknowledges that rural debt has grown significantly over the past 10 years in Australia. However, we do not believe there is a systemic problem facing rural Australia (albeit some industries and areas are facing greater challenges than others). We consider there are a number of reasons why rural debt has increased significantly in recent times, including:

- Adjustment pressure to achieve economies of scale that produce higher returns on capital;
- Adjustment pressures to change from livestock to more capital intensive cropping enterprises;
- Relatively low interest rates;
- Adoption of new technologies that improve labour productivity;
- Increased reliance on off-farm income to support financial sustainability, especially for small farms; and
- Financing cash flow shortfalls in some industries and some areas under financial pressure.

There have been changes in the agriculture sector. Some people will have left industries and some people will be new borrowers. However, overall the data indicates that there has been a significant reduction in the number of borrowers that had viability issues (1007) in 2009 and there is a significant improvement in the number of borrowers viable under any circumstance (4439) in 2011 (Appendix 2, Table 3 and 4).

Confidence – growth and future prospects

The ABA believes that the long term outlook for the Australian agriculture sector is positive with strong growth prospects. Australian farmers are well placed to benefit from domestic population growth, national prosperity and changing consumer diet preferences and food demands as well as economic growth that is forecast for the Asian region.

The opportunities for the Australian agriculture sector to respond to domestic and international demand are favourable. In October 2012, Port Jackson Partners and ANZ published a report "Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand" [2] indicating that Australia could capture up to $1.7 trillion in additional revenues from agricultural exports up to 2050. For example, as global concern increases about food security and demand for agricultural produce increases it is likely that there will be a significant increase in demand, particularly from China, for high-end agricultural products like fruit, dairy, high-grade meat, and seafood. However, expanding existing and encouraging new trade agreements, improving the efficiency of the agri-sector supply chain, and promoting innovation across the sector will be critical.

Broadly, the competitiveness of the Australian agriculture sector generally is also favourable in a global context, a position that has underpinned a prominent role in global trade over the years. However, the agriculture sector needs to look at broader factors to maintain its global competitiveness in a changing export landscape and increasingly competitive marketplace. In April 2014, Rabobank's Food and Agribusiness Research team published a report "Competitive Challenges"[3] identifying the challenges affecting the global competitiveness of the Australian food and agribusiness sectors and what local industries can do to compete for future growth. For example, the focus should be on developing into high-value markets where Australian agribusinesses can compete on quality and other sought after attributes where consumers have capacity to pay.

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[1] APRA Prudential Standard APS 330 Public Disclosure (APS 330).
[2] Part Jackson Partners and ANZ, ANZ Insight Series. Greener Pastures: The Global Soft Commodity Opportunity for Australia and New Zealand. October 2012. http://media.corporate-ir.net/media_files/IROL/24/248677/ANZ_insight_3_Greener_Pastures.pdf
[3] Rabobank Food and Agribusiness Research and Advisory. Agriculture in Focus 2014: Competitive Challenges. April 2014. http://www.rabobank.com.au/News-and-Events/Media-Releases/2014-News-Archive/Pages/media-release-20140407.aspx

NAB's Agribusiness quarterly survey[4] conducted in December 2013 indicated that agribusiness conditions have risen significantly late last year with all three indicators in the conditions index – trading, profitability and employment – recording positive results. The conditions index recorded its highest level in nine years (+17). Despite traditionally more positive seasonal factors during this period with increased domestic and international demand for fresh and processed foods, the results suggest a strengthening in underlying fundamentals and a number of economic developments supportive of business conditions. Trading conditions increased (+24) with the depreciation of the Australian dollar (falling 3% in November and December), stronger asset prices and sustained low interest rates. Profitability conditions improved (+16) with better sales margins and cash flows. Employment conditions improved (+10) (and 15 points above the five year average of -5) with increased trading activity.

Rabobank's quarterly rural confidence survey[5] conducted in March 2014 indicated an easing in rural confidence since December 2013 (to near neutral levels) on the back of continued dry seasonal conditions in many parts of the Australia. However, 73% of farmers still expected the same or better incomes compared to last year with 80% expecting to maintain or increase their level of investment in their farm business over the next 12 months.

Challenges and issues facing the Australian agriculture sector

The ABA identifies a number of challenges and issues for the Australian agriculture sector:

- *Improving supply chains and addressing rising production costs on-farm and beyond the farmgate*: Declining performance and increasing costs for major supply chains is putting competitiveness of local industries at risk. The key will be to create, or recreate, contestable supply chains that are aligned with the interests of the producer, fostering greater trust and coordination.
- *Investing in infrastructure*: Inefficiencies in logistics infrastructure need to be addressed to lift competitiveness. Higher on-farm costs and slowing productivity growth in many sectors in Australia relative to global peers have increased the importance of driving efficiencies in alternate parts of the supply chain.
- *Improving innovation*: Farms perform at substantially different levels with many delivering poor yield and profit outcomes. Closing the performance gaps means reinvigorating public and private extension systems in order to build farmer confidence and to encourage investment in new technologies and best practices.
- *Sourcing capital and addressing capital constraints*: Farmers face challenges in raising sufficient capital to fund growth and support farm turnover. New structures for owning and operating farms will need to be encouraged to attract investment from domestic and foreign investors and capital markets.
- *Attracting skilled labour*: Labour force shortages have intensified across the agriculture sector. Widespread skill shortages across supply chains and succession concerns associated with an ageing farmer population will need to be addressed by attracting new workers, enhancing education platforms and promoting the performance of the agriculture sector.
- *Accessing international markets and targeting key markets*: Further work is needed to understand consumer requirements and explore more innovative ways to access new markets. In addition to free trade agreements, strategic agreements should be explored, particularly in return for capital investment. There will also need to be efforts taken to capture premium market opportunities.
- *Focusing research and development*: National agricultural R&D programs will need more focus and coordination to drive long term growth, especially by identifying and pursuing the highest potential opportunities.
- *Accessing land and water*: Land-use conflicts are an ongoing issue and many regions lack clear and efficient water markets. As natural resource inputs become increasingly scarce, resource management should be improved by optimising land use and making better use of water.

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[4] http://business.nab.com.au/wp-content/uploads/2014/03/q4-nab-agribusiness-survey-2013.pdf
[5] http://www.rabobank.com.au/research/pages/rural-confidence-survey.aspx

- *Addressing regulatory pressures*: Barriers to local production need to be removed and further work is needed on engagement across governments and industries to reduce the likelihood of direct and indirect regulatory interventions which risk fragmenting sector performance and disrupting local production and export opportunities, particularly without prior consultation and management.

The ABA believes that ensuring Australian primary producers and farmers can make the most of their opportunities and address these challenges will require support from Federal Government. Support includes opening up trade opportunities, supporting research and development that improves productivity, promoting the opportunities of working in the agriculture sector, investing in regional services and infrastructure, removing and avoiding unnecessary regulation, and where intervention is deemed necessary, minimising the impact on costs through the agri-sector supply chain.

Furthermore, regardless of the fact that drought is an ongoing feature of the Australian agricultural landscape, seasonal conditions remain one of the critical issues that affects farmer confidence, at all levels (regardless of whether they hold bank debt or not). Therefore, in light of recent droughts in Western Australia and more recently in Queensland, we consider that it may be timely for the Federal Government to again review the effectiveness of changes made to drought programs and assistance.

The ABA believes that given the volatility of earnings and cash flows and the time it takes for weakened balance sheets of agribusinesses to recover, a multifaceted approach is needed to restore momentum in the Australian agriculture sector, including:

- Continuing Federal Government support for Farm Management Deposits;
- Harmonising and implementing a nationally consistent farm debt mediation process;
- Continuing Federal and State/Territory government funding and support for rural financial counselling services;
- Assisting primary producers and farmers manage financial difficulty through dedicated loans and grants programs (including specifically for those impacted by prolonged drought); and
- Adopting strategies to selectively reinvigorate stalled industries with growth potential, sustain and strengthen existing high growth industries, and foster new and emerging agricultural industries around high growth opportunities (i.e. new varieties of oilseeds, advanced biofuels, etc).

Banking products and services

Australian banks provide various mainstream banking products and services for agribusinesses, including accounts to make money management easier, loans and finance solutions for new equipment, property and business expansion, investment options to smooth cash flows and interest bearing accounts, and risk management and advice to assist manage business risks and prepare for the future. Banks also provide additional support services and assistance, including financial literacy for agribusiness customers seeking additional information and advice and financial hardship for agribusiness customers who may be experiencing financial difficulties.

Agribusiness accounts

- Farm management accounts – transaction accounts provide flexibility for everyday banking needs with access to electronic banking, cheque book, deposits. Some accounts are interest bearing accounts.
- Farm management deposits – fixed term and fixed interest rate investment accounts for eligible primary producers. This account receives tax benefits to protect earnings from the risk of poor seasonal and economic conditions.

Agribusiness loans and finance

- Farm management overdraft – an overdraft account provides flexibility for managing seasonal cash flow. This account allows access to funds up to an agreed limit.
- Farm equipment finance – a loan for a range of products, including vehicle, equipment and plant financing needs. Options include rent, hire to purchase, purchase outright or sell and lease back.

- Farm loan packages – a package can offer concessions, benefits and discounts on a range of products. These loans are usually tailored by an agribusiness banker and their customer.
- Domestic and international trade finance – finance options allows easier management of payments to suppliers and sales cycles. Maturity and interest rate options assist manage cash flow and interest rate risk.

Risk management

- Risk products – commodity price risk management offers a range of strategies, tailored to the agribusiness to assist protect the business from the risk of commodity price changes; foreign exchange risk management offers a range of products to manage risk linked with foreign currencies; and interest rate risk management offers products to offset the impact of adverse interest rate movements, and take advantage of favourable ones.
- Insurance products – insurances to cover agribusiness assets and continuity, such as in relation to a natural disaster and loss of production.

Financial planning

Banks have agribusiness financial planners to assist agribusiness customers plan for their financial future. These advisers work with producers and farmers to identify a financial, business or succession plan that suits the business now, and prepares for future challenges and opportunities.

Agribusiness market research

Some banks have agribusiness market research analysts preparing reports and surveys for agribusiness customers to get a better understanding of their business, sector, industries, trends, economic growth prospects, case studies, etc.

Financial literacy

At an industry level, the ABA has published a number of fact sheets for small business, such as "Dealing with Debt: How banks can help if you are experiencing financial difficulties", "Applying for a loan" and "Refinance your business debt" (prepared with CPA Australia). These resources provide guidance to small business customers about finance and management and information about financial hardship assistance.

At an individual bank level, banks have financial literacy programs to assist their customers with money management, business planning, financial and estate planning, etc. Specifically, banks have resources to assist agribusiness customers, including dedicated areas of their bank websites. Agribusiness specialist bankers are also essential in helping their customers build their knowledge about their financial and business circumstances, including legal, accounting, financial, environmental and social considerations. For example, Rabobank has developed two unique programs – the Executive Development Program for farm owners and decision makers and the Farm Managers Program designed specifically for the next generation of farmers. These programs are financially subsided by Rabobank. Additionally, NAB has introduced an Agribusiness Traineeship Program providing one-on-one mentoring for agribusiness analysts to assist build their capacity to provide additional support services for their agribusiness customers.

Financial hardship

At an industry level, the ABA has released the financial hardship package[6]. This initiative reflects the banking industry's commitment to assist their customers who may be experiencing financial difficulty. The package consists of an industry guideline and consumer fact sheet on financial hardship and the 'DoingItTough' consumer website, which provides information about financial hardship assistance offered by banks and contact numbers for banks' dedicated financial hardship teams[7].

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[6] http://www.bankers.asn.au/Consumers/Are-you-experiencing-financial-difficulty-

[7] http://www.doingittough.info

At an individual bank level, banks have implemented a number of industry commitments to make information about financial hardship assistance more prominent in their branches and on their bank websites. Banks have also been making changes to their dedicated financial hardship teams to ensure staff are better trained and equipped to deal with the unique situations of their customers[8].

Australian banks are committed to assisting their customers who may be experiencing financial difficulties. Banks understand that agribusiness customers face additional challenges with their businesses and livelihoods and their dedicated financial hardship teams are committed to negotiating or meditating agreed solutions to problems faced by their agribusiness customers in meeting their loan commitments.

Banks have a long history of working with farmers through business and seasonal cycles, and put in place special arrangements to address financial needs during times of financial hardship. Banks are aware of the physical and mental stress that farmers endure at times of financial hardship. It is industry practice to try and resolve the repayment of debt without relying on the legal rights of loan contracts that enable banks and other lenders to enforce loan agreements. The financial impact on industries of extended drought, natural disasters, and interruption to trade takes time to work through as weakened balance sheets are vulnerable to further volatility in earnings and cash flows due to alterations in production and commodity prices. Banks have found that farm debt mediation has generally delivered more positive (i.e. higher equity) outcomes for borrowers. It is only when agreed solutions or arrangements fail or are unable to be sustained that enforcement action is taken on agri-loans.

It is rare for farmers to become over-indebted. However, in these instances, the stress placed on the borrowing family can be significant. In contrast to many other types of businesses in financial difficulties, this stress is compounded for the family because it is not just the continuity of their business that is at risk, but they also face the very real possibility of losing their family home and property. We acknowledge that there are farmers in specific areas and industries that are under financial pressure. For example, in the case of northern beef cattle producers, their position has been obviously exacerbated by disruptive events, such as the live export ban, and more recently, drought. Banks have supported their agribusiness customers through the 'decade of drought' on the east coast and the prolonged drought period in the west coast grains industry. These areas have been recovering and rebuilding equity.

Banks have supported their agribusiness customers through extended drought, natural disasters, and the loss of trade and continue to do so by providing special arrangements to deal with financial hardship of individual agribusinesses as well as emergency relief packages for communities. Banks also work with governments providing assistance at these times. Banks also encourage their agribusiness customers to use rural financial counsellors and independent mediators to help reach agreements on the repayment of farm debt.

Innovations in finance and initiatives to foster investment and growth

The ABA and the banking industry is interested in exploring alternative and innovative finance solutions, opportunities for fostering investment, growth and sustainability of agribusinesses, and strategies for promoting farm performance and productivity. Ultimately, alternative financing models will likely require a combination of different business structures, government funding and support, and investment incentives for private investors.

Some options may include:

- *Tax treatment*: Existing tax incentives could be supplemented with investment allowances, accelerated depreciation, revising restrictions on tax losses, and revisiting the ban on negative gearing of farms when off-farm income is more than $250,000.

[8] Industry initiatives include: website disclosure industry commitment – button on homepage and click-through to revised webpage content on financial hardship to help customers find information more easily about hardship assistance and relevant emergency relief packages; branch disclosure industry commitment – branch display (e.g. poster, TV presentation, counter card and brochures based on minimum content standard) on financial hardship and getting access to hardship assistance; and staff training industry commitment – review of relevant staff training programs and changes implemented to improve frontline staff and relevant specialised staff (i.e. financial hardship and debt collections team) awareness of financial hardship.

- *Alternative lending products and management approaches*: For example, agricultural management firms may provide benefits for dealing with smaller farmers where the management firm is able to introduce economies of scale across separate agribusinesses. Income contingent loans are loans against which repayments are only made if and when the borrower can afford to make repayments. These products could make it easier for primary producers and farmers to manage volatility in cash flows due to seasonal conditions and would assist manage default risk. Lending terms and interest rates would need to be commercially negotiated and government funding and support (i.e. guarantees, protections) would likely need to minimise lending risk, which in the absence of government guarantees or protections may be cost-prohibitive for agribusinesses.
- *Alternative investment vehicles*: For example, customised financial agreements or managed investment schemes are solutions to provide specific purpose funding, such as land acquisition, start-up and operation. Managed investment schemes have been used in Australia due to the tax incentives available on these schemes, however, community or cooperative arrangements are less familiar in Australia. Community or cooperative arrangements are similar to joint venture arrangements and could benefit from investment subsidies to attractive private capital. Alternative investment vehicles can provide diversified access to capital, however, there have been some high-profile failures of managed investment schemes and investor losses have made these options less attractive to private capital. Importantly, a well constructed managed investment scheme remains a good investment tool and when the scheme is based on solid business grounds (and based on other benefits in addition to tax incentives), schemes have a role in financing for the agriculture sector.
- *Risk sharing strategies*: For example, shared equity arrangements or equity partnerships are options to assist agribusinesses access mainstream finance. A shared equity loan scheme involves the co-ownership of the property by government and/or private equity investors with the agribusiness owner. Structures could include equity partnerships, modern variants of share farming and use of off-take agreements, as in the mining sector.
- *Farm management bonds*: A specialised bond (or similar debt instrument) could be developed which embeds better business and operational management, increases in productivity and innovative production techniques, and accountable structures. These debt instruments enable investment risk to be shared across public and private investors and leverage capital markets (i.e. innovation within financial service providers, capacity of investors, expertise of service providers, etc). The Federal Government's strong balance sheet could sensibly be used to channel private capital into the agriculture sector as an alternative to bank lending and enhance the investment proposition for private investors. The underlying assumption of cost-effective government credit enhancement would be fundamental to the commercial viability of these debt instruments and the ability for bonds to raise adequate levels of capital.

The ABA believes the Federal Government should look to investigate regulatory and market barriers, assess risks and opportunities for establishing alternative financing and support models and appropriate risk sharing strategies (i.e. shared equity arrangements, tax incentives, investment subsidies, protections or guarantees, credit enhancements), and determine parameters needed for financing arrangements (debt and equity) and for successful private investment (i.e. alternative investment vehicles and farm management bonds).

Other supportive programs will be needed, including tax treatment (i.e. investment allowances, depreciation, negative gearing, etc), initiatives to build investment (i.e. expansion of the finance market to include second and third tier financiers (e.g. rural stores)), expansion of visa programs for rural workers (i.e. revised 457 visa requirements and restrictions), attraction of foreign investment into new and existing developments, harmonisation of state-based legislation (i.e. farm debt mediation, water securities, etc), and prioritisation of infrastructure projects to support continued rural and regional growth (i.e. irrigation projects, dams, etc).

The ABA also believes there continues to be an essential role for Federal Government in supporting agribusiness education programs and a need for increased focus on the investment in human capital in farming.

The ABA supports the adoption of a partnership approach between the Federal Government and the banking industry to look for alternative financing and support models and economic strategies as part of an overall approach to fostering investment and growth in the Australian agriculture sector.

Government assistance (including the Farm Finance Program)

The ABA and the banking industry endorse the Federal Government's Farm Finance Program. The program consists of four measures that seek to build the ongoing financial resilience of farm businesses:

- Concessional loans – short term financial assistance for productivity enhancement projects or debt restructuring.
- Farm Management Deposit (FMD) accounts – the scheme has been increased from $65,000 - $100,000 for non-primary production income and allows consolidation of existing FMD accounts.
- Financial counselling – funding for an additional 17 full-time rural financial counsellors.
- Farm debt mediation – establishment of a nationally consistent approach to farm debt mediation.

Concessional loans

The Concessional Loans Scheme is available in Victoria, Queensland, South Australia, Western Australia, the Northern Territory and Tasmania (noting applications for loans in 2013-14 have closed in New South Wales). Types of loans (productivity enhancement or debt restructuring), loan terms and loan amounts differ between each jurisdiction and tailored to meet the needs of each jurisdiction's farming sector.

On 13 November 2013, the Minister announced a reallocation of scheme funds[9]. There is now also a $40 million reserve fund for 2014-15. Under the scheme, farmers can apply for loans between $50,000 and $200,000 at the concessional rate of 4.5%. The interest rate will be reviewed every 6 months and may be adjusted in line with prevailing economic conditions. The concessional rate of interest will apply to the five years of the loan only. At the end of the five year period, the loan funds need to be repaid, such as via obtaining commercial refinance.

The ABA notes that the scheme offers loans not dissimilar to existing mainstream loans, which may be a reason for why there has been low uptake of the loans. In practice, the Government's lending decisions are based on eligibility criteria[10] similar to commercial lending decisions (i.e. evidence of the ability to meet repayments and future viability of the farm), and therefore, unlikely to be different to commercial lending decisions. (It should be noted that banks are subject to responsible lending obligations and agribusiness lending is based on debt serviceability and evidence of the ability of the borrower to meet repayments and cash flows.) Additionally, farmers will generally need to take out a second loan and renegotiate with a financier after the five year period.

The ABA supports the Concessional Loans Scheme. However, we believe that the policy should focus on growing the 'high performing' agricultural sector in order to improve productivity and global competitiveness. (We note that recent ABARES analysis demonstrates a large portion of the agricultural sector is 'low performing'. Appendix 2, Table 3 and 4.) We consider that the low performing agricultural sector should receive government funding and support via specific debt relief initiatives, such as drought concessional loans, debt relief packages and/or grants program. Furthermore, we believe that the Federal Government should consult with the banking industry about the concessional loans scheme to ensure that these loans are targeted and do not have adverse consequences for borrowers or their banks and other lenders. For example, closer attention should be given to the transition between a concessional loan and obtaining commercial finance after the five year period.

[9] http://www.daff.gov.au/agriculture-food/drought/assistance/farm-finance/concessional-loans
[10] The eligibility criteria requires that agribusinesses: (1) Can demonstrate their need, their ability to repay a loan and can provide sufficient security; and (2) Are experiencing debt servicing difficulty but are considered commercially viable in the longer term.

Farm Management Deposits

The ABA supports the extension of this scheme and the increase in the income threshold due to take effect on 1 July 2014. FMD accounts assist primary producers deal with fluctuations in cash flows. The scheme allows eligible primary producers to set aside pre-tax income from primary production in years of high income, which they can draw on in years of low income. Income deposited into a FMD account is tax deductible in the year the deposit is made and becomes taxable income in the year in which it is withdrawn.

The ABA supports the Farm Management Deposit scheme. FMDs are one of the cornerstones of drought planning and building resilient farm businesses. However, we consider a number of changes could be made to maximise the benefit of the scheme for farmers, including further increasing the upper limit of FMDs and extending the range of operators eligible to use these accounts, such as trusts. We also believe that further investigations by the Federal Government and the banking industry into related issues needs to be undertaken, for example, implications of the unclaimed monies regime for farmers and possibilities of a mortgage offset account using a FMD. Federal budget and taxation issues will need to be resolved.

Financial counselling

The ABA supports the increased funding for an additional 17 full-time financial counsellors for rural and regional communities. The banking industry and individual banks have recognised the importance of financial counselling and have been working closely with the financial counselling sector on improving banks' practices and approaches in dealing with customers who may be experiencing financial difficulties and identifying ways to improve interactions between banks and financial counsellors on behalf of their clients.

At an industry-level, clause 28 of the 2013 Code of Banking Practice sets out enhanced obligations regarding customers experiencing financial difficulties. In addition, the ABA's financial hardship package was released on June 2013 (as previously detailed).

At an individual bank level, banks have been making changes to their internal policies and procedures, customer information and staff training. Banks have been working closely with the financial counselling sector to make improvements to their internal systems and practices. Banks have also been providing financial and in-kind support to the financial counselling sector in a number of ways, including project funding and partnerships.

The ABA notes that financial counselling can have the greatest impact at time of crisis and when people can put into practice an educational intervention to help them overcome their financial difficulties. Rural financial counsellors provide a free and confidential service and can assist their clients identify financial and business options, negotiate with their bank or other lender, develop a plan, provide information about government assistance schemes, and refer their clients to other services, including legal, accounting, agricultural advisers, and other assistance, such as personal and social counseling.

Research indicates that financial counselling has a significant impact on addressing financial hardship, including:

- Resolving financial difficulties in 66% of cases;
- Helping avoid legal action in 74% of cases;
- Improving their skills in prioritising debt and better able to budget in 75% of cases; and
- Improving their health, mental and emotional wellbeing in 63% of cases (and around half of respondents worried and felt less anxious about their money)[11].

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[11] Brackertz, N (2012). I Wish I'd Known Sooner! The impact of financial counselling on debt resolution and personal wellbeing. Salvation Army, Swinburne University, Westpac. http://www.salvationarmy.org.au/Global/News%20and%20Media/Reports/2012/00099-I-wish-I-had-knownsooner-Oct-2012.pdf

Research also indicates that financial counselling in Australia is underfunded and lacks a coherent whole-of-government approach to addressing financial hardship and financial stress[12]. Currently, demand for financial counselling services in Australia means that it can be between two and eight weeks for a client to be able to see a face-to-face financial counsellor, and in some areas, such as rural and regional Australia, the wait can be longer.

> The ABA supports enduring government funding and support for rural financial counselling as critical in assisting farmers experiencing financial difficulties and in financial crisis, and especially farmers in regions or industries experiencing debt stress and where natural disasters have had the greatest impact on their businesses. We consider that Federal Government funding for the Financial Management Program, including funding for financial counselling, should be retained and increased in the upcoming Federal budget to expand these essential public services.

Farm debt mediation

The ABA supports the implementation of a nationally consistent farm debt mediation model across Australia. Farm debt mediation is a mechanism to facilitate a discussion between a farmer and their bank or other lender so they can better negotiate their financial position.

The ABA believes that farm debt mediation can deliver positive outcomes for all parties, however, currently the process varies across jurisdictions. Importantly, the process can identify workable solutions when all parties engage with a genuine desire to try and find a solution. Unfortunately, there have been some examples when borrowers have used the process as a means to prevent debt enforcement, which serves little purpose other than potentially expose the borrower to a higher risk of loss if the asset value falls during mediation.

> The ABA supports a harmonised and national approach to help farmers and their financiers adopt consistent, simple and fair approaches. We support the working group established by the Federal Government comprising of representatives from the banking industry, agricultural groups, the rural financial counselling service, and State/Territory governments to develop a nationally consistent approach to farm debt mediation, drawing on the various farm debt mediation models currently in place across Australia. We note that the working group is aiming to have an agreed model developed by the end of 2014.

Summary

The ABA believes the Federal and State/Territory governments should support the agriculture sector through the Farm Finance Program. The four elements of the program are important to support improved performance and productivity in the agriculture sector – providing and improving concessional loans, supporting farm management deposit accounts, continuing and increasing support for rural financial counselling services, and harmonising farm debt mediation across Australia.

However, other supportive programs will also be needed across the agriculture sector, including loans and grants for special purposes or reasons (i.e. drought concessional loans, low performing sector adjustment), advancement of free trade agreements and agricultural exports (i.e. expansion of market access for Australian agricultural products), promotion of opportunities of working in modern agriculture (i.e. skills, training, education, jobs growth and human capital, strategies to shift market returns to the farm gate), promotion of research and development, investment in regional services and critical infrastructure projects, and removal of unnecessary regulation throughout the agri-sector supply chain.

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[12] Livingstone, C, Bruce, E, Kotnik, E and King, S (2009). Comparing Australian and International systems to address consumer financial stress. Monash University. http://www.financialcounsellingaustralia.org.au/getattachment/Corporate/Publications/Reports/Comparing-Australian-and-International-Systems-to-Address-Consumer-Financial-Stress.pdf

Foreign investment and trade agreements

The ABA believes that encouraging improved terms of trade for the Australian agriculture sector is critical to improved performance and productivity. Trade opportunities should be pursued via multilateral and bilateral arrangements.

Free trade agreements (FTAs) are a useful mechanism to encourage improved trade outcomes (tariffs and quotas) for the agriculture sector. Australia has seven FTAs in place – New Zealand, United States, Chile, Thailand, Malaysia, Singapore, and the Association of South East Asian Nations (ASEAN). Trade with these countries accounts for 28% of Australia's total trade. Additional FTAs have just been agreed, but not yet in force, with Japan and South Korea. Australia is currently negotiating FTAs with China, India and Indonesia as well as the multilateral Trans-Pacific Partnership, with 12 countries including Australia. There has also been memorandum of understanding approaches between industries, such as the Western Australian Livestock Exporters Association and Chinese companies' representatives.

In addition to trade negotiations, there is currently strong foreign investment into the Australian agriculture sector, which demonstrates the sector's growth prospects.

> The ABA believes that the Federal Government should consider introducing a register for foreign investment into the Australian agriculture sector as a way to build public confidence. The Federal Government should continue to pursue trade opportunities via multilateral and bilateral trade agreements concentrating on countries where our largest trade opportunities exist and negotiating 'most favoured nation' status for Australia's food and agriculture suppliers in key markets. Additionally, certain industries, such as Australia's beef industry, should invest in strengthening relationships and knowledge exchange frameworks with their foreign peers.

Reconstruction and Development Board

The Australian Reconstruction and Development Board (ARDB) has been proposed as a mechanism for the Reserve Bank of Australia to take over certain debts and manage rural adjustment programs, including loans at a low interest alternative.

The ABA does not support the ARDB. Despite there being limited detail about how it would operate, there is an assumption that it would require financiers to sell off their loans at a discount and for the Government to take over lending. There are a number of consequences which could have adverse implications for farmers (in terms of property valuations) and the Government (in terms of credit risk associated with low performing or unviable businesses).

The ABA notes that the *Rural Adjustment Act 1992* currently exists for the specific purpose of enabling the Federal Government to provide direct or indirect assistance, such as grants and loans to farmers, for purposes related to rural adjustment. We consider this approach more appropriate.

The ABA made a submission to the Senate inquiry into the *Reserve Bank Amendment (Australian Reconstruction and Development Board) Bill 2013*[13].

> The ABA supports the Farm Finance Program and other strategies and initiatives to address the low performing sector. Policies to reconstruct the rural sector by building financial viability and resilience should not replicate the role of the mainstream banking industry or result in unintended consequences for property valuations, credit growth (over lending) and legacy issues.

[13] Submission 109. http://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Economics/RBA_Amendment_2013

Concluding remarks

The ABA and the banking industry acknowledge the difficulties faced by agribusinesses, especially those agribusiness customers enduring prolonged drought conditions, other extreme climatic and weather events, including floods, and the loss of trade throughout Australia.

Australian banks have continued to support their agribusiness customers through providing special arrangements to deal with financial hardship of individual businesses as well as emergency relief packages for communities. Importantly, banks recognise the financial impact on the agriculture sector as a result of these unforseen events, and recognise that agribusiness customers can take time to work through and resolve their financial difficulties. These events have left some agribusinesses with weakened balance sheets and more vulnerable to volatility in earnings and cash flows. However, the banking industry believes that the long term outlook for the Australian agriculture sector is positive with strong growth prospects.

The ABA believes that the Federal Government should adopt an approach across the whole agri-sector supply chain. Primary producers, farmers and other components in the agriculture sector, including governments, banks and other lenders, and rural and regional representatives, need to work together to capitalise on these economic growth opportunities. To this end, the ABA has been engaging regularly with the National Farmers' Federation (NFF) and State farming organisations and governments to discuss issues impacting on the agriculture sector. We consider that the agriculture sector needs some barriers removed and a national plan for enabling agri-sector growth. The role of the Government in facilitating economic growth opportunities will be critical.

The ABA looks forward to engaging further with the Federal Government and other stakeholders throughout this consultation process. For further information or to discuss aspects of this initial submission, please contact Diane Tate, Executive Director – Retail Policy on (02) 8298 0410: dtate@bankers.asn.au.

Yours sincerely,

Steven Münchenberg

Appendix 1: Snapshot of Australian agriculture sector

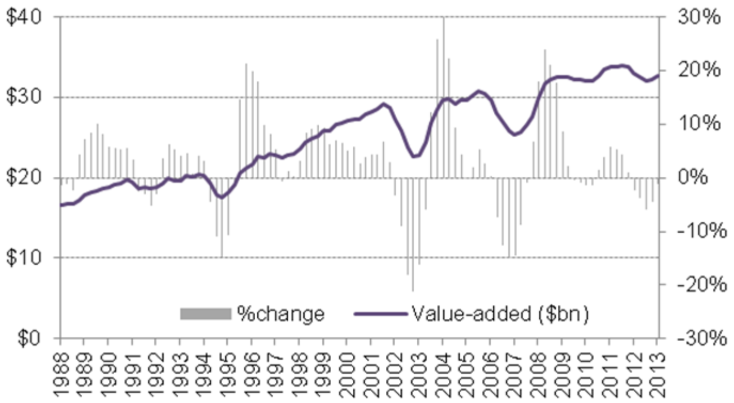
Contribution to economy

Over the year ending September 2013, industry value-added for the agriculture, forestry and fishing industry was $32.6 billion. It has almost doubled over the past quarter of a century.

In comparison, industry value-added for the largest industry in economy, the mining industry, was $152.0 billion over the year ending September 2013. For the finance and insurance industry, the second largest industry, value-added was $123.0 billion and for the construction industry it was $115.6 billion.

Value-added for the agriculture, forestry and fishing industry is roughly in the same order as the electricity, water and gas industry and the accommodation and food industry.

Industry value-added for the Agriculture, forestry and fishing industry



Source: ABS

The contribution of the agriculture, forestry and fishing industry to the economy has generally been within a tight range over the past 25 years. Over the past 10 years, the average contribution has been 2.4%. There have been noticeable dips to low points of around 2.1% contribution during times of drought or the impact of changes in commodity prices (such as the early 1990s).

Over the past year, the agriculture, forestry and fishing industry contributed 2.3% to the Australian economy, drifting slightly downwards from a 2.5% contribution over the last two years.

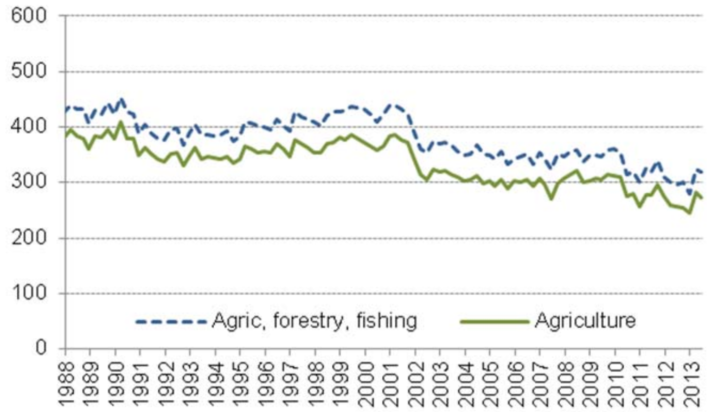
Contribution the agriculture, forestry and fishing industry to the economy

Source: ABS

Employment

Over the past 10 years, employment for the agriculture industry subdivision has averaged 87% of employment for the wider agriculture, forestry and fishing industry. It is now at 86%. The chart below shows that employment levels for the agriculture industry were close to 300,000 for much of the period from 2008 to 2010 after which there has been a fall in employment to 273,600 in February 2014.

Employment for the agriculture industry



Source: ABS

As a proportion of total employment in the economy, the contribution from agriculture has halved over the past 25 years, averaging around 5.0% at the end of the 1980s to 2.4% in 2013.

Agriculture industry employment as % of total employment

Source: ABS

In a recent research project from KPMG, initiated by Rabobank, into the past developments and expected trends of rural demographics, it was found that the agricultural workforce has suffered a steep decline. Over the period 2001-2011, while Australia's total workforce had grown by 21%, the agricultural workforce declined by 30%. This is particularly pronounced in Western Australia and Queensland where the growth of the workforce was respectively 32% and 31% (relative to 21% nationally) and the decline of the agricultural workforce was 36% and 26% respectively (relative to 30% nationally).

Production

The 2010-11 Agriculture Census shows that just over one-fifth (21.4%) of agriculture production is cereals used for grain while cattle and calves make up 17.0% of agricultural production.

Livestock products, such as milk, eggs and wool, account for 15.6% of production.

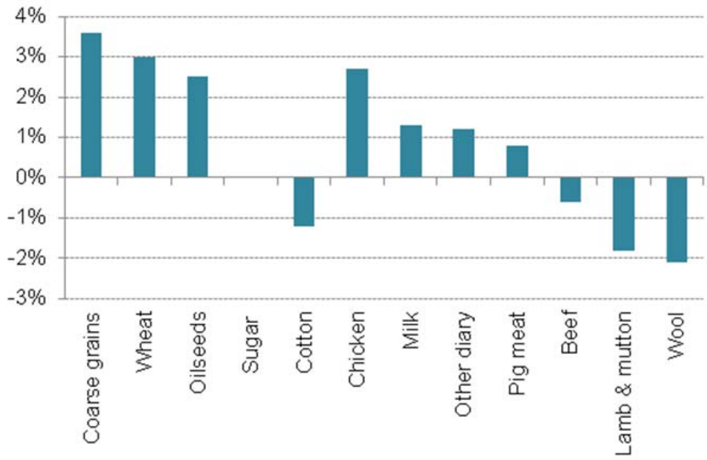
Agriculture production

Activity (2010-11)	Production $bn	%contrib
Agriculture	$46.0	100.0%
Crops	$25.0	54.4%
Cereals for grain	$9.8	21.4%
Cattle and calves	$7.8	17.0%
Livestock products (milk, eggs, wool)	$7.2	15.6%
Fruit	$3.7	8.1%
Vegetables for consumption	$3.3	7.3%
Other crops	$3.1	6.8%
Sheep and lambs	$2.9	6.2%
Poultry	$2.1	4.5%
Oilseeds	$1.3	2.9%
Nurseries, cut flowers, turf	$1.3	2.7%
Hay	$1.1	2.3%
Legumes for grain	$1.0	2.1%
Pigs	$0.9	2.0%
Nuts	$0.3	0.6%
Vegetables for seed	$0.1	0.3%
Goats	$0.1	0.2%

Source: ABS

Agricultural production forecasts from ABARES[14], averaged over the next three years ending 2015-16, show that the strongest performance will be seen across the coarse grains, wheat, oilseeds and chicken industries.

Agriculture production forecast average 3 years to 2015-16



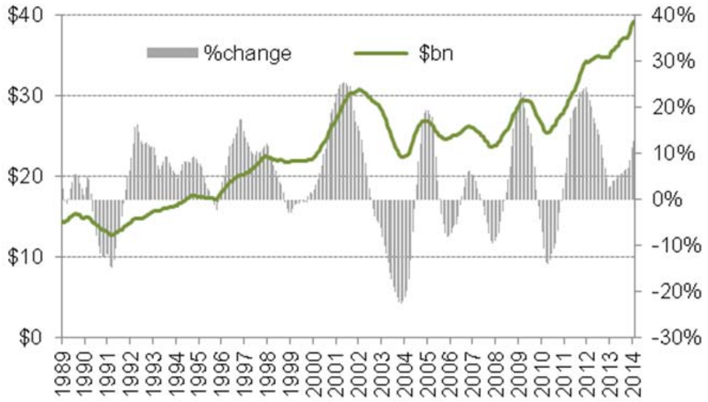
Source: ABARES

[14] ABARES is a research bureau within the Department of Agriculture.

Rural exports

Over the year ending February 2014, the value of rural exports was $39.2 billion, increasing by 12.7%. There has been a strong upward trend in rural exports for almost four years, which has seen the value of rural goods exported increase by 54%.

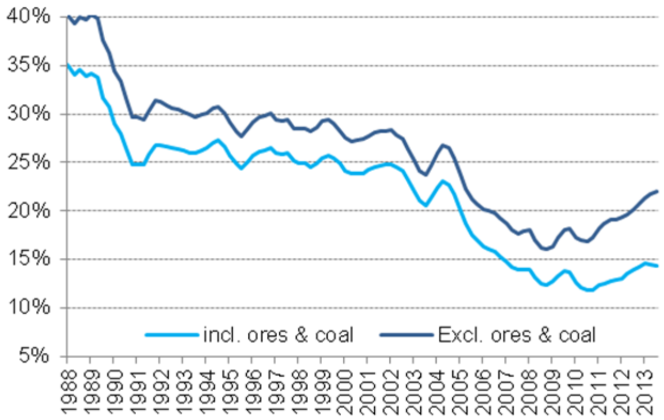
Rural exports



Source: ABS

Rural exports accounted for 14.4% of total exports in 2013. Removing the impact of two categories of mining exports (metal ores and minerals and also coal) shows rural exports at 22.0% of total exports. In either case, the past three years has seen a sizable increase in contribution from rural exports to total exports.

Rural exports as a percentage of total exports

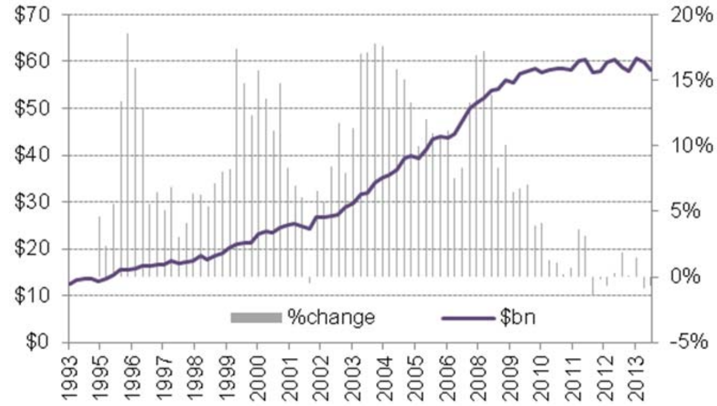


Source: ABS

Bank lending to the agriculture industry

At the end of 2013, bank loans to the agriculture, forestry and fishing industry were at $58.3 billion. This has changed little over the past four years.

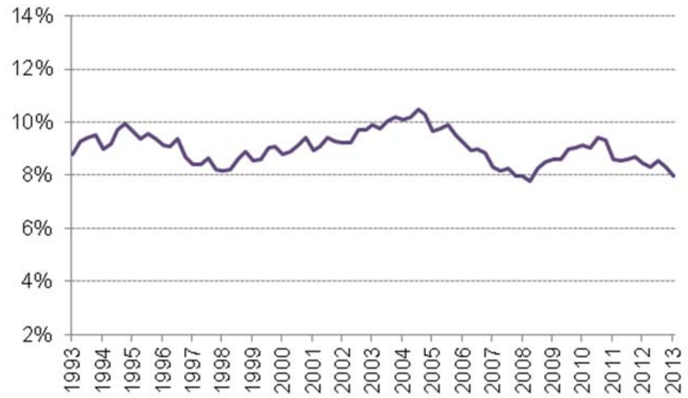
Bank lending to the agriculture industry



Source: RBA

Over the past 20 years, bank loan outstandings to the agriculture, forestry and fishing industry, as a proportion of total business loan outstandings, has been in the range of 8% to 10%. At the end of 2013, this was at the lower end of the range (8.0%).

Bank lending to the agriculture industry



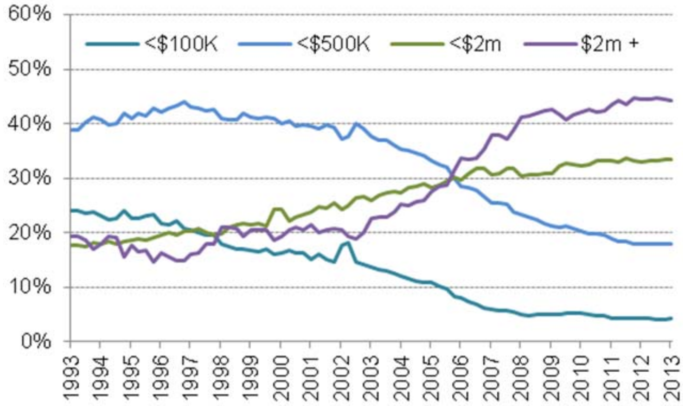
Source: RBA

Twenty years ago, loans under $500,000 accounted for 65% of loan outstandings to the agriculture, forestry and fishing industry. This is now 22%.

In particular, the past 10 years has seen a significant fall in the proportion of loan outstandings where the loans are of value less than $500,000 for the agriculture industry. This also coincides with a consolidation in the number of agribusinesses. That is, while the total business population increased by 11% of the past 10 years, the number of businesses in the agriculture, forestry and fishing industry fell by 13%.

Loans of $2 million and over have increased from 20% of loan outstandings for agriculture, forestry and fishing over the several years to 2003 to 44% of outstanding over the past two years (2012 and 2013).

Agriculture – loan outstandings by size of loan

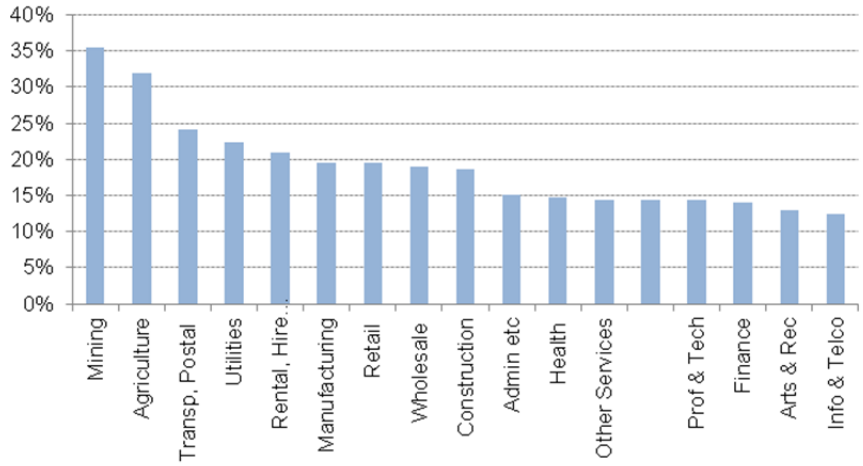


Source: RBA

Businesses seeking finance

The agriculture, forestry and fishing industry has a relatively high likelihood to seek either equity or debt finance. Over the three years ending June 2012, on average per year, 32% of businesses in the agriculture, forestry and fishing industry sought finance.

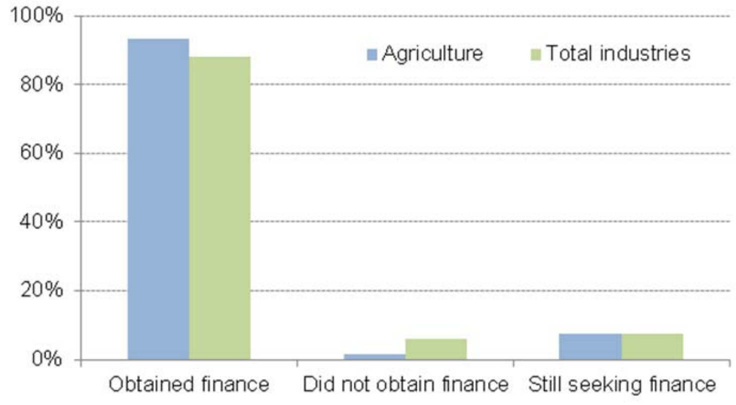
Businesses that sought debt or equity finance over average over three years to 2011-12



Source: ABS

Of all businesses which sought equity or debt finance over the three years ending June 2012, 88% were successful. At 93%, the agriculture, forestry and fishing industry was the highest of all industries.

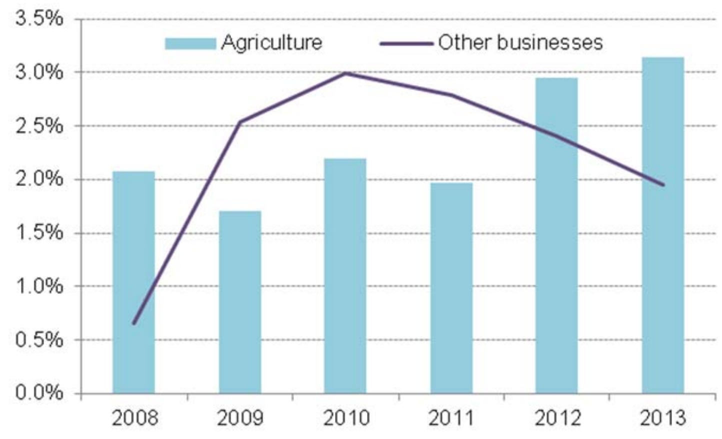
Businesses that sought finance over three years to 2011-12 and whether obtained



Source: ABS

Estimates of arrears on loans for the agriculture, forestry and fishing inducts show that arrears for these loans have exceeded that of all business loans over the past two years (2012 and 2013).

Arrears on business lending



Source: RBA/Banks Pillar 3

Appendix 2: Agriculture sector and debt

Table 1

Proportion of businesses seeking debt finance		
	2010-11	2009-10
Industry	%	%
Agriculture, Forestry and Fishing	31.6	32.1
Mining	21.8	22.6
Manufacturing	15.5	19.4
Electricity, Gas, Water and Waste Services	21.0	21.2
Construction	15.4	19.3
Wholesale Trade	18.3	18.2
Retail Trade	20.0	15.9
Accommodation and Food Services	13.4	14.2
Transport, Postal and Warehousing	20.9	23.4
Information Media and Telecommunications	14.8	13.6
Financial and Insurance Services	12.7	13.0
Rental, Hiring and Real Estate Services	17.0	17.6
Professional, Scientific and Technical Services	12.4	12.4
Administrative and Support Services	15.5	12.0
Health Care and Social Assistance	13.3	13.0
Arts and Recreation Services	11.1	11.2
Other Services	13.4	14.0
Total	**16.6**	**17.2**

Source: ABS 8167.0 - Selected Characteristics of Australian Business

Table 2

Proportion of businesses seeking debt finance that was not obtained		
	2010-11	2009-10
Industry	%	%
Agriculture, Forestry and Fishing	0.7	2.0
Mining	9.7	5.3
Manufacturing	11.3	6.6
Electricity, Gas, Water and Waste Services		
Construction	8.2	5.2
Wholesale Trade	9.1	8.6
Retail Trade	11.2	8.2
Accommodation and Food Services	3.6	3.3
Transport, Postal and Warehousing	8.2	9.9
Information Media and Telecommunications	12.4	6.3
Financial and Insurance Services		
Rental, Hiring and Real Estate Services	9.8	19.7
Professional, Scientific and Technical Services	6.8	2.7
Administrative and Support Services	4.6	5.6
Health Care and Social Assistance	5.0	
Arts and Recreation Services	11.0	3.7
Other Services	6.6	1.4
Total	**7.1**	**5.8**

Source: ABS 8167.0 - Selected Characteristics of Australian Business

Table 3

Family farm business performance estimates by size of business, broadacre farms, 2009-10 to 2011-12				
Average per business / household				
Size of farm business				
Size of farm operation expressed in sheep equivalents	**Receipts of farm business (total business income)**	**Rate of return on total capital used**	**Farms ranked in top 25% of population by return on total capital used**	**Share of disposable income earned from non-farm sources**
no.	$	$	%	%
889	64,189	-2.9	3	100
1,734	85,942	-1.5	6	97
2,413	113,750	-1.0	9	85
3,125	157,388	-0.6	15	66
3,920	191,456	-0.5	20	78
4,711	234,244	0.4	24	48
5,486	262,253	0.6	22	58
6,335	297,192	0.8	27	43
7,253	345,560	1.3	35	33
8,436	392,610	1.3	39	39
9,850	431,880	1.6	39	40
11,526	558,517	2.3	51	23
13,282	606,683	2.0	46	23
15,650	699,155	2.3	52	23
18,441	740,868	2.5	54	20
22,463	996,333	3.0	59	18
27,761	1,132,531	2.9	62	22
37,158	1,534,036	3.4	64	15
53,334	1,884,856	3.1	58	13
106,820	3,872,193	3.7	69	12

Source: ABARES Australian Agricultural and Grazing Industries Survey (AAGIS)

Table 4

Estimates for farms ranked by rate of return on total capital used, 2007-08 to 2011-12,						
all broadacre industries							
average per farm							
		Top 25%		**Middle 50%**		**Bottom 25%**	
Size of operation							
Total area operated	ha	11 500	*(4)*	5 300	*(5)*	4 700	*(7)*
Area sown to crop	ha	1 000	*(2)*	300	*(3)*	200	*(6)*
Beef cattle	no	600	*(3)*	400	*(2)*	100	*(6)*
Sheep	no	2 300	*(3)*	1 000	*(3)*	500	*(6)*
Financial performance of farm business							
Total cash receipts	$	896 200	*(3)*	313 800	*(2)*	137 500	*(4)*
Total cash costs	$	605 100	*(3)*	248 000	*(2)*	152 600	*(4)*
Farm cash income	$	291 100	*(3)*	65 800	*(4)*	- 15 200	*(23)*
Farm business profit	$	219 800	*(4)*	- 12 400	*(19)*	- 90 900	*(4)*
Farm business debt and equity at 30 June							
Farm business debt	$	1 045 700	*(3)*	408 400	*(4)*	211 900	*(7)*
Net business worth	$	4 830 400	*(2)*	3 713 100	*(2)*	1 661 700	*(3)*
Equity ratio	%	83	*(1)*	90	*()*	88	*(1)*
Liquid assets available to farm business at 30 June							
Farm management deposits	$	74 900	*(6)*	28 200	*(9)*	6 300	*(21)*
Other liquid assets	$	148 500	*(6)*	121 800	*(6)*	97 500	*(13)*
Debt servicing							
Interest paid to receipts percentage	%	8	*(3)*	9	*(3)*	11	*(6)*
Debt to receipts percentage	%	123	*(3)*	137	*(3)*	169	*(6)*
Household income of owner-manager and partner a							
Household off-farm income	$	28 200	*(4)*	32 700	*(5)*	40 300	*(6)*
Total net household income	$	186 400	*(3)*	58 700	*(4)*	10 600	*(33)*
Share of net household income earned off-farm	%	15	*(5)*	56	*(4)*	100	*(31)*

Figures in parentheses are standard errors expressed as a percentage of the estimate provided. a Owner-manager and partner's share of net farm income (farm cash income less depreciation) plus off-farm income.

Source: ABARES Australian Agricultural and Grazing Industries Survey (AAGIS).