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The Council of Financial Regulators

Via email: CFRReview@treasury.gov.au

Submission to the Council of Financial Regulators Review into Small and Medium-Sized Banks: **Multi-Seller Securitisation for Customer-Owned Banks**

Introduction

Laminar Capital is a structured finance firm with extensive experience in supporting customer-owned banks through securitisation. The firm has established the most securitisation programs for Mutual Banks in Australia, providing valuable insights into funding challenges and market dynamics. Laminar is a wholly owned subsidiary of Perpetual Corporate Trust, is the leading trustee in the Australian securitisation market. Given our experience, we are well-placed to contribute to discussions on improving funding access for small and medium-sized banks.

Executive Summary

This submission addresses the funding challenges faced by small and medium-sized customer-owned banks in Australia. It proposes a government-supported multi-seller securitisation model, with the government playing a market development role by providing mezzanine funding to a securitisation vehicle. This initiative would improve sector resilience, enhance funding efficiency, and support competitive neutrality in the financial system.

Key Funding Issues for Small and Medium Banks

Small and medium-sized banks, particularly customer-owned institutions, face several funding constraints that limit their ability to compete with larger banks:

1. **Higher Relative Cost of Wholesale Funding:** Smaller banks lack the scale and credit ratings of major banks, leading to higher funding costs in wholesale markets.
2. **Limited Access to Capital Markets:** Institutional investors and real-money investors often prefer larger more frequent issuers, reducing funding options for smaller banks.

3. **Securitisation Cost and Complexity:** Securitisation remains an important tool particularly for regulatory capital for Mutual Banks but is relatively expensive compared to on-balance-sheet funding particularly in the post GFC period.

4. **Challenges for Regionally Focused Mutual Banks:** Mutual Banks with regionally focused businesses tend to demonstrate stronger financial performance metrics than those seeking to compete nationally via mortgage brokers. However, these regional banks lack access to diverse funding sources and face challenges in attracting institutional investment at scale.

Overview of Multi-Seller Securitisation

Multi-seller securitisation is a structured finance mechanism that allows multiple smaller lenders to pool their assets into a common funding vehicle, enabling them to access capital markets on a scale comparable to larger financial institutions. This approach enhances funding efficiency, diversifies risk, and reduces costs by spreading transaction expenses among multiple participants. It also fosters market credibility by facilitating more frequent issuance and standardising documentation and structuring, making these transactions more attractive to investors.

Key advantages of multi-seller securitisation include:

- **Economies of Scale**: By aggregating loan portfolios from multiple lenders, the overall transaction size increases, allowing for more competitive funding terms.
- **Diversification of Risk**: A broader pool of assets reduces concentration risk, improving investor confidence.
- **Improved Market Access**: Smaller financial institutions gain entry to funding markets that would otherwise be inaccessible or prohibitively expensive.
- **Regulatory Capital Relief**: Properly structured transactions can help participating banks optimise capital efficiency along with liquidity management.
- **Support for Regional Mutual Banks**: Regionally focused banks gain access to securitisation markets which would otherwise be closed to them due to their geographic concentration risk.

History of Multi-Seller Securitisation in Australia

Multi-seller securitisation has historically been an important funding tool particularly for small customer-owned banks, though its usage has evolved over time. Several initiatives have been implemented, with varying degrees of success:

- **Cuscal's Integris Program**: Established in the early 2000s, this multi-seller securitisation program provided funding solutions for Mutual Banks until its closure in 2014.

- **Indue's Multi-Seller Warehouse**: Funded by Westpac, this program also supported Mutual Banks but was placed into run-off in 2014 and has since been fully wound up.

- **Australian Mutual Funding Platform (AMFP)**: Formed in 2012, AMFP is a user group that established a shared set of master program documents for mutual ADIs.

While it has facilitated several self-securitisation, each ADI operates its own trust, and the platform has not been used for external funding purposes.

- **Laminar's MTG Trusts Securitisation Program**: Established in 2014, this program has supported multiple self-securitisations as well as term RMBS and ABS transactions. However, these transactions have also been executed on a single-seller basis even while multi-seller securitisation has been a key goal of the program since inception.

Despite these historical initiatives, there remains no active multi-seller securitisation vehicle that enables customer-owned banks to efficiently access funding markets. This highlights the need for a new approach that ensures sustainable access to capital for the sector.

Lessons Learned from Previous Multi-Seller Securitisation Programs

While previous multi-seller securitisation programs have provided important funding avenues for Mutual Banks, they have also faced challenges that offer valuable lessons for designing a sustainable model:

- **Relative Cost of Securitisation**: Following the Global Financial Crisis, securitisation became a relatively more expensive way to fund loans compared to on-balance sheet funding for ADIs, reducing its attractiveness as a long-term funding strategy. However recent changes in the regulatory landscape for liquidity management for MLH banks have improved the relative cost effectiveness of securitisation. Further it continues to be the only proven tool for managing CET1 ratios beyond retained earnings for customer owned banks.
- **The Need for Commitment to Program Development**: Prior programs did not establish a consistent pipeline of transactions with regular access to the term RMBS market and diversifying the warehouse bank and real money investor base, leading to their eventual wind-down when regulatory change altered the economics of the existing structures.
- **Importance of Scale and Diversity**: Smaller programs struggle with investor confidence due to limited scale and asset diversity. A well-structured multi-seller model should address this by aggregating sufficient volume and frequency of issuance to attract broad investor support.
- **Operational Complexity**: Coordinating multiple sellers requires efficient governance and operational frameworks to avoid execution delays, as seen in earlier Mutual Bank initiatives.
- **Regulatory Considerations**: Ensuring alignment with evolving APRA regulatory requirements is crucial for long-term sustainability.

Steps Industry and Government Can Take to Improve Funding Access

To improve access to funding and enhance competition, the following steps should be considered:

1. **Government Support for Mezzanine Funding:** The Australian Government can play a market development role by providing mezzanine funding within a multi-seller securitisation warehouse or term RMBS vehicle. Several agencies currently have RMBS investment capability which may be considered as providers of this support including Housing Australia, the Clean Energy Finance Corporation, the Future Fund and the AOFM. Traditionally the junior AAA part of a securitisation has been the most challenging to place for securitisation issuers generally and this is particularly the case for inaugural issuing multi-seller programs.

2. **Regular RMBS Issuance Program:** Establishing a multi-seller program with regular term RMBS issuance would enhance market confidence and attract a more diverse investor base. Establishing this program with Government support during the development phase is likely to facilitate more widespread adoption by both issuers Mutual Banks and RMBS investors.

3. **Investor Education and Market Development:** Encouraging institutional investors to allocate capital to customer-owned bank securitisations would improve funding access.

4. **Regulatory Adjustments:** Ensuring that capital and liquidity requirements appropriately reflect the risk profile and business model of smaller banks would improve funding efficiency.

5. **Enhancing Regional Bank Competitiveness:** Facilitating multi-seller structures enables regionally focused banks to leverage diversified asset pools, allowing them to maintain their strong financial performance in their geographical niche while accessing competitively price funding at scale.

Conclusion

A government-supported mezzanine funding initiative within a multi-seller securitisation structure presents a viable solution to the funding challenges of customer-owned banks. By addressing market inefficiencies and fostering private sector participation, this initiative would strengthen the Mutual Banking sector, enhance financial stability, and promote competition in Australia's banking landscape.

We appreciate the opportunity to contribute to this review and welcome further engagement to refine and implement this proposal.

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