Box C

Use of the Reserve Bank's Term Funding Facility

The Term Funding Facility (TFF) was announced by the Reserve Bank Board in March 2020 as part of a comprehensive policy package to support the Australian economy in response to the COVID-19 pandemic. The facility has provided low-cost 3-year funding to banks operating in Australia (against high-quality collateral, as is the case for all central bank funding). The TFF had three overall aims:

1. to support the banking sector to continue to extend credit to households and businesses at a time when wholesale funding markets were significantly disrupted
2. to lower funding costs for banks and, in turn, lower borrowing rates for their business and household customers
3. to encourage banks to increase their lending to businesses, particularly small and medium-sized enterprises (SMEs).

While the facility closed to new drawdowns at the end of June 2021, it will continue to provide low-cost funding to banks for up to 3 years until final funding from the facility matures in mid 2024.

The amount each bank could draw upon under the TFF was the sum of three allowances:

- The 'initial allowance' was fixed at the start of the scheme to be equivalent to 3 per cent of each bank's total credit outstanding; banks could access their initial allowance until 30 September 2020.
- The 'supplementary allowance' was equivalent to 2 per cent of each bank's total credit outstanding; made available from 1 October 2020.
- The 'additional allowance' was available to any bank that managed to expand their business credit, particularly for SMEs. For every extra dollar of loans (relative to a pre-pandemic baseline) a bank made to large businesses, the bank could access one additional dollar of funding from the Reserve Bank. For every extra dollar lent to SMEs, it had access to an additional $5 of funding.

The cost of TFF funding was 0.25 per cent initially, and 0.1 per cent since November 2020 (in line with the reduction in the cash rate target at that time).

Banks accessed $188 billion of funding from the TFF

The TFF has provided $188 billion in funding to banks. This funding is equivalent to 4 per cent of banks' non-equity funding, or 6 per cent of credit. Drawdowns were concentrated over two periods of heightened activity in the lead up to expiry dates for allowances (Graph C.1).

Most banks took up most of their allowances

In aggregate, banks drew down 88 per cent of the total funding of $213 billion available over the life of the facility. By bank type, the major banks and mid-sized Australian banks took up all of their allowances in aggregate, while small banks and foreign banks took up a little over half of their total allowances (Graph C.2). By number, around two-thirds of banks accessed the TFF. Those that did not access the facility represented a very small share of allowances by value (Graph C.3). In large part these banks were small Australian banks and foreign banks, many with very small allowances, and some with larger allowances but with less ready access to collateral.

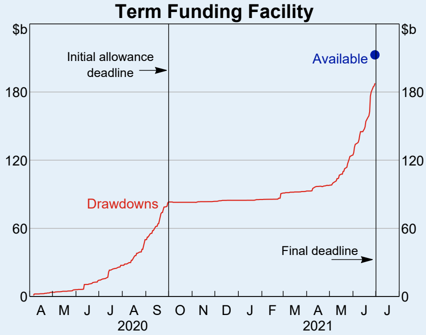
The top 10 largest users of the TFF account for almost 90 per cent of drawdowns from the facility (Table C.1). Differences in the amount drawn from the TFF within this group largely reflect differences in banks' total credit outstanding; this is consistent with each bank's initial and supplementary allowances having been based on its credit outstanding when the allowances were set in March 2020 and September 2020. However, for some of these banks the additional allowances they accumulated were significant, reflecting strong growth in their loans to businesses since early 2020.

The TFF has contributed to keeping bank funding costs low …

The TFF lowered banks' funding costs by providing a low-cost source of funds. In particular, the TFF provided funds for 3 years at a cost that has been well below the cost of wholesale debt for the same term. The estimated cost of sourcing 3-year unsecured funding in domestic wholesale debt markets for the major banks was around 0.6 per cent at the end of June 2021, compared with 0.1 per cent for TFF funding (Graph C.4). Taking into account the lower cost of funds and the share of bank funding provided, the Bank's estimates suggest that the direct effect of the TFF has been to lower major bank funding costs by a little more than 5 basis points. For smaller banks, the

Graph C.1

Term Funding Facility

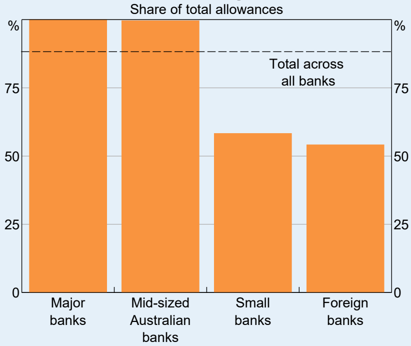


Sources: APRA; RBA

Graph C.2

TFF Usage

Share of total allowances

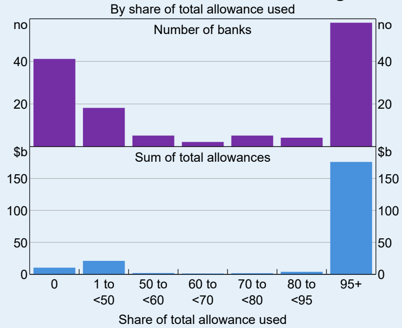


Sources: APRA; RBA

Graph C.3

Distribution of TFF Allowance Usage*

By share of total allowance used



* Includes 133 eligible banks as at the end of the drawdown period

Sources: APRA; RBA

Table C.1: Top 10 Largest Drawdowns of the Term Funding Facility by Bank

	Total Allowance		*of which*			
			Initial[(a)]		Supplementary and Additional[(b)]	
Bank name	Drawn-down ($ billion)	Share of allowance (Per cent)	Drawn-down ($ billion)	Share of allowance (Per cent)	Drawn-down ($ billion)	Share of allowance (Per cent)
CBA	51.14	100.0	19.15	100.0	31.99	100.0
NAB	31.87	100.0	14.27	100.0	17.60	100.0
Westpac	29.78	100.0	17.90	100.0	11.89	100.0
ANZ	20.09	100.0	12.00	99.8	8.09	99.9
Macquarie	11.26	99.1	1.72	100.0	9.53	98.9
ING Bank (Aust.)	5.42	100.0	1.87	100.0	3.55	99.9
Bendigo Bank	4.72	100.0	1.83	100.0	2.89	100.0
Suncorp	4.13	100.0	1.74	100.0	2.39	100.0
Judo Bank	2.86	33.1	0.03	99.8	2.83	32.9
BoQ	2.15	100.0	1.24	100.0	0.92	100.0

(a) Closed on 30 September 2020. More information on these allowances is available in the TFF Operational Notes.

(b) Closed on 30 June 2021. More information on these allowances is available in the TFF Operational Notes.

Source: RBA

difference between the TFF funding rate of 0.1 per cent and their cost of wholesale term funding is larger than for the major banks. Since the last of this low-cost funding is not due to mature until mid 2024, the TFF will keep bank funding costs lower than otherwise for a number of years.

The TFF has also had an indirect effect on banks' funding costs. As banks have drawn on the TFF, they have largely refrained from issuing new senior unsecured debt in wholesale funding markets, so the total stock of bank bonds has declined as existing bonds have matured. The lower supply of bank bonds has narrowed spreads on these bonds in the secondary market, and in turn contributed to narrowed spreads for other (financial and non-financial) institutions' debt, thereby reducing costs of new issuance for banks and other institutions.

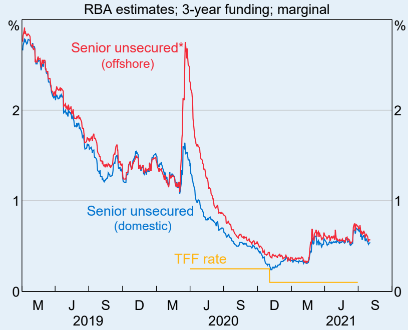
… and, in turn, contributed to lower lending rates

As a result of the Reserve Bank's policy measures, including the TFF, bank funding costs and lending rates are at historically low levels. On average, lending rates have

Graph C.4

Cost of Major Banks' Funding Sources

RBA estimates; 3-year funding; marginal



* Adjusted for cross-currency hedging

Sources: Bloomberg; RBA

declined in line with banks' overall funding costs, although the extent of reductions in interest rates has varied across different types of housing and business loans. Rates on outstanding variable-rate mortgages have declined by around 55 basis points since the end of February 2020, while interest rates on outstanding fixed-rate mortgages have declined by around 135 basis points. Since February 2020, interest rates on variable-rate loans to SMEs and large businesses have declined by around 95 basis points and 90 basis points, respectively. Interest rates on fixed-rate loans to SMEs and large businesses have declined by around 80 basis points and 55 basis points, respectively.

The TFF refinancing task that the banks will face is sizeable but manageable

Over the next 2 to 3 years, banks will need to repay the funding they have accessed from the TFF. The amount banks will source from wholesale debt markets over that period will depend on a number of factors, including their asset growth and the price and availability of other funding, including deposits. Liaison with banks suggests that their current plans are to raise a sizeable amount of funds to repay TFF funding (on or before maturity) from wholesale debt markets, thereby at least partly reversing the process whereby debt issuance declined as TFF drawdowns increased. There are a number of factors that suggest the banking sector is well prepared for this task. First, although TFF maturities in the peak quarters are sizeable compared with issuance over much of the past decade, banks have indicated in liaison that they plan to smooth out their issuance over a period of time, in amounts that would be in line with their issuance in the past. Second, the medium-term economic outlook is positive, which suggests that banks will be well placed to issue sizeable amounts on favourable terms. Third, Australian banks are highly rated by global standards, including because of continued profitability (see April 2021 *Financial Stability Review*).[1] The Reserve Bank will continue to monitor the situation going forward, along with APRA, which as usual will monitor banks' liquidity management.

Endnotes

[1] See RBA (2021), 'Chapter 3: The Australian Financial System', Financial Stability Review, April. Available at <https://www.rba.gov.au/publications/fsr/2021/apr/australian-financial-system.html>