How Good Were the Covid Loan Support Schemes?

During the covid crisis the Australian government introduced several measures to ensure the availability of credit to the small and medium sized business sectors (SMEs) which were expected to suffer badly from lockdowns and reduced demand.

Did they work? We don't really know since there has been no accounting for the policy's performance. Ideally, governments should be publishing post-audits of the schemes' performance to provide guidance on what works and what doesn't, should future crises demand similar action.

But looking at the small amount of publicly available data, it would be hard to escape the conclusion that, if nothing else, the banks did pretty well out of the schemes.

There were two main components of the government support. One was the SME Loan Guarantee Schemes initially announced by the government on 22 March 2020 and which closed on 30 June 2022. There were several iterations, with loans made by banks to SMEs being initially 80 per cent guaranteed by the government, and with the guarantee being reduced to 50 per cent for loans made after January 1, 2022.

The other component was the Term Funding Facility (TFF) , announced in March 2020 whereby banks could borrow funds from the RBA for three years at an interest rate of initially 25 basis points, with the interest rate being reduced to 10 basis points on borrowings after November 2020. Ability to access the TFF was related to lending to all businesses but with incentives for lending to SMEs. The TFF closed for new drawdowns on 30 June 2021.

What might one have expected to happen as a result of these policies? First, lending to the SME sector should have been higher than it otherwise would have been over the period from March 2020 till mid 2022. Unfortunately, we don't know what the counterfactual (what otherwise would have occurred) is. If the crisis was otherwise going to cause a massive decline in lending to SME's, then an outcome in which lending did not decline may have been a good outcome.

And that may have been the case, although figures on loans granted each month don't appear to be publicly available. Figures on loans outstanding are however available (from Reserve Bank Statistical Table D14). Small enterprise loans outstanding were relatively constant between March 2020 and June 2021 (but fell somewhat for the year after that). Loans outstanding for medium sized business were also relatively constant between March 2020 and June 2021 but grew relatively strongly after that.

Loans outstanding to Large (Non-Financial) businesses actually declined by around 6 per cent over the year after March 2020 and did not return to the March 2020 level until near the end of 2021. If one makes the (big) assumption that SME and large business loans would have experienced similar declines in the counterfactual then the relative stability of SME loans suggests the schemes may have been somewhat successful in protecting SMEs.

But what about the loan interest rates? With the government absorbing much of the default risk via the guarantees, it might be expected that banks would reduce substantially the credit spread component of the interest rates charged. Or did they not adjust interest rates for lower risk and capture the benefits of the guarantees for themselves? (And this is not to mention the benefits of cheap TFF funding).

Again, data available (Reserve Bank Statistical Table F07) is patchy, but not indicative of any bank largesse! In the half year before March 2020 (when the schemes began) new variable rate loans to small enterprises averaged 179 basis points higher than those to big enterprises. From March 2020 to June 2021, that gap increased to 191 basis points. A similar story holds for rates for medium enterprises where the margin over loans to large enterprises increased from 37 to 57 basis points.

Many of the small enterprise loans are secured by residential property, but even so the gap between the small enterprise loan rate and the residential mortgage rate increased from 20 to 27 basis points over the periods being considered.

These numbers (as rubbery as they are) are not consistent with a story that the government schemes led to lower interest rates for SME borrowers, but rather with the banks maintaining credit spreads and keeping the benefits of lower risk lending due to government guarantees. (They also got the benefit of a lower risk weighting for their capital requirements).

Supporting the banks, as well as businesses, during a crisis period is good policy. But the recent high profit rates of the banks suggests that the benefits got somewhat skewed towards the banks. More analysis is warranted, and it should be incumbent on our policy makers to either produce such analysis or make public the data needed for others to do so.

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