



Speech

A Review of the RBA's Term Funding Facility

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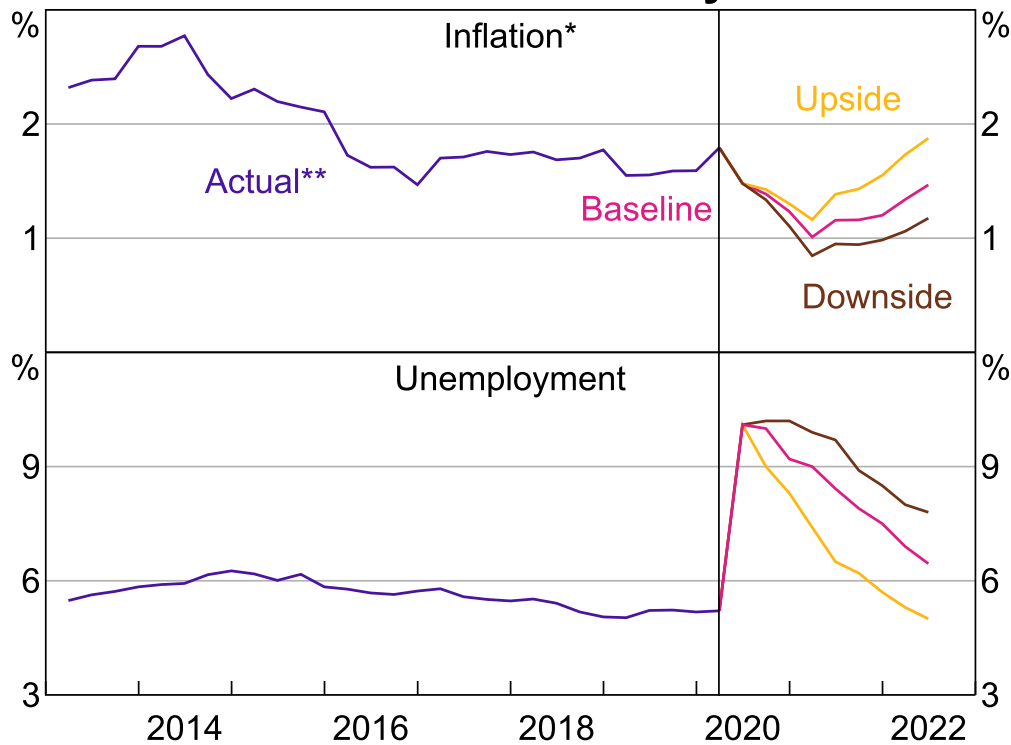
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Thank you for coming to the Reserve Bank's offices today. I will talk about a review we have published on the Term Funding Facility (TFF). [\[1\]](#) This is the fourth instalment of the series of reviews of unconventional policy tools the RBA used during the COVID-19 pandemic. [\[2\]](#)

In March 2020, the economic outlook was bleak and highly uncertain (Graph 1), financial markets were in turmoil, and there was limited scope to lower the cash rate further. In that environment, the RBA pursued a package of policies to support the economy. [\[3\]](#) The TFF review considers how that element of the package worked, whether it achieved its aims, and lessons for the future. I will cover the key points but there is a lot of detail in the review itself.

Graph 1

Forecast Scenarios as of May 2020 SMP



* Trimmed mean, year-ended.

** Outturn as at May 2020.

Sources: ABS; RBA.

What was the TFF intended to do?

The TFF aimed to:

- lower the cost of borrowing for businesses and households, by lowering lenders' funding costs, and to reinforce the benefits to the economy of the lower cash rate
- encourage banks to lend to businesses – particularly small and medium-sized enterprises (SMEs) – given that business credit tends to fall in downturns.

How did it work?

The TFF provided low-cost three-year funding to banks, which also indirectly helped to lower the cost of borrowing from wholesale markets.

Under the TFF, banks had access to cheap funding up to an amount that was based on the initial size and subsequent growth of their loan book. The interest rate was initially fixed at 0.25 per cent. This was lowered to 0.1 per cent in step with the reduction in the cash rate target in November 2020. A bank was able to secure additional TFF allowances if it increased its overall lending to businesses,

particularly smaller businesses. For each dollar of additional credit extended to large businesses, a bank was eligible for another dollar of TFF funding. For each additional dollar extended to SMEs, a bank had five more dollars added to its TFF allowance.

Banks could access their allowances up to the end of September 2020. However, by the time of the September Board meeting, the economy was still far from the RBA’s goals, and considerable downside risks remained. The Board decided to extend the facility and increase banks’ allowances; banks could access their new allowances for three-year fixed-rate loans until mid-2021. [\[4\]](#)

TFF funding was much cheaper than other sources of term funding. Unsurprisingly, banks took up most of their TFF allowances (Table 1). [\[5\]](#) The TFF ultimately provided \$188 billion of funding, which was equivalent to 6 per cent of the stock of credit outstanding at the peak of the TFF’s use. Banks repaid all TFF funds as scheduled by mid-2024 without incident.

Table 1: TFF Usage Across Banks

	Amount drawn \$ billion	Share of total allowances Per cent
Major banks	133	100.0
Mid-sized banks	24	99.6
Small banks	9	58.3
Foreign banks	22	54.2
Total across all banks	188	88.3

Sources: APRA; RBA.

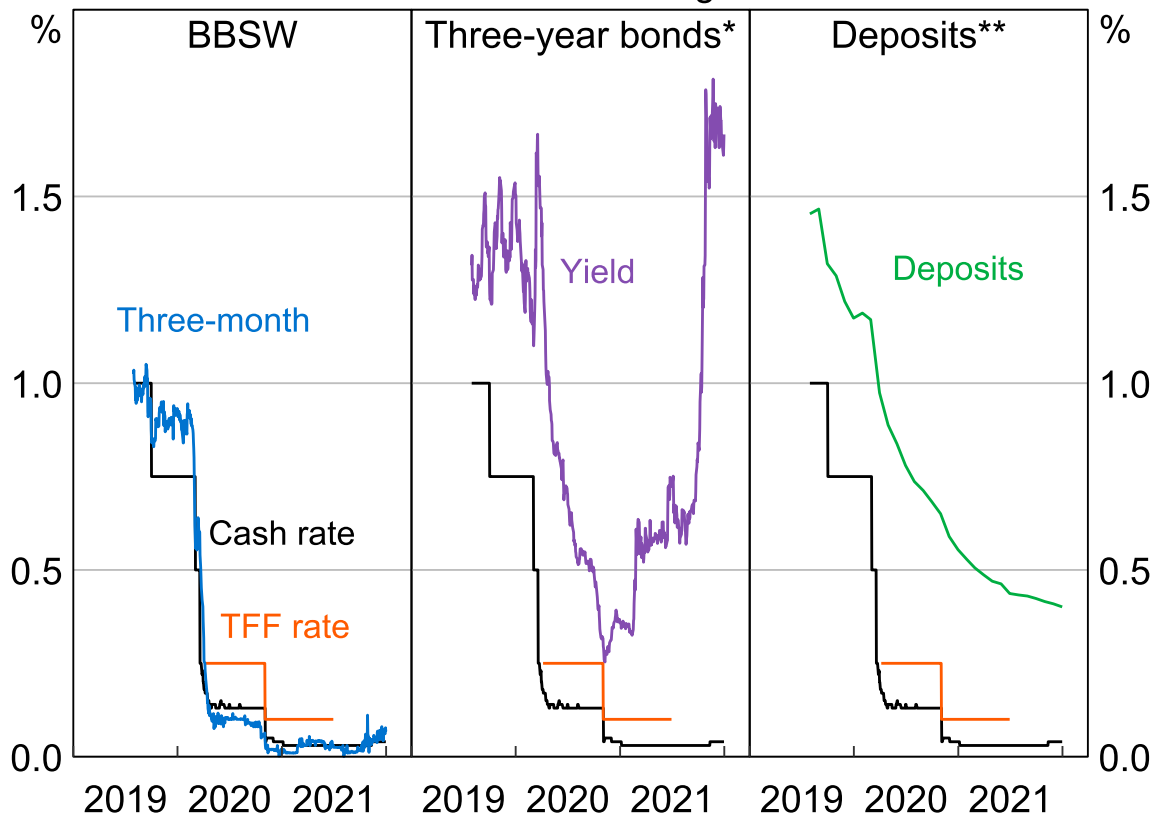
To summarise its effect on funding costs for banks and others with access to wholesale funding markets:

- The TFF lowered banks’ funding costs directly. For the major banks, the TFF was around 60 basis points cheaper than issuing bonds during the TFF drawdown phase (Graph 2). It lowered their average cost of funds by around 5 basis points. [\[6\]](#)

Graph 2

Major Banks' Funding Costs

For new funding



* Domestic issuance only.

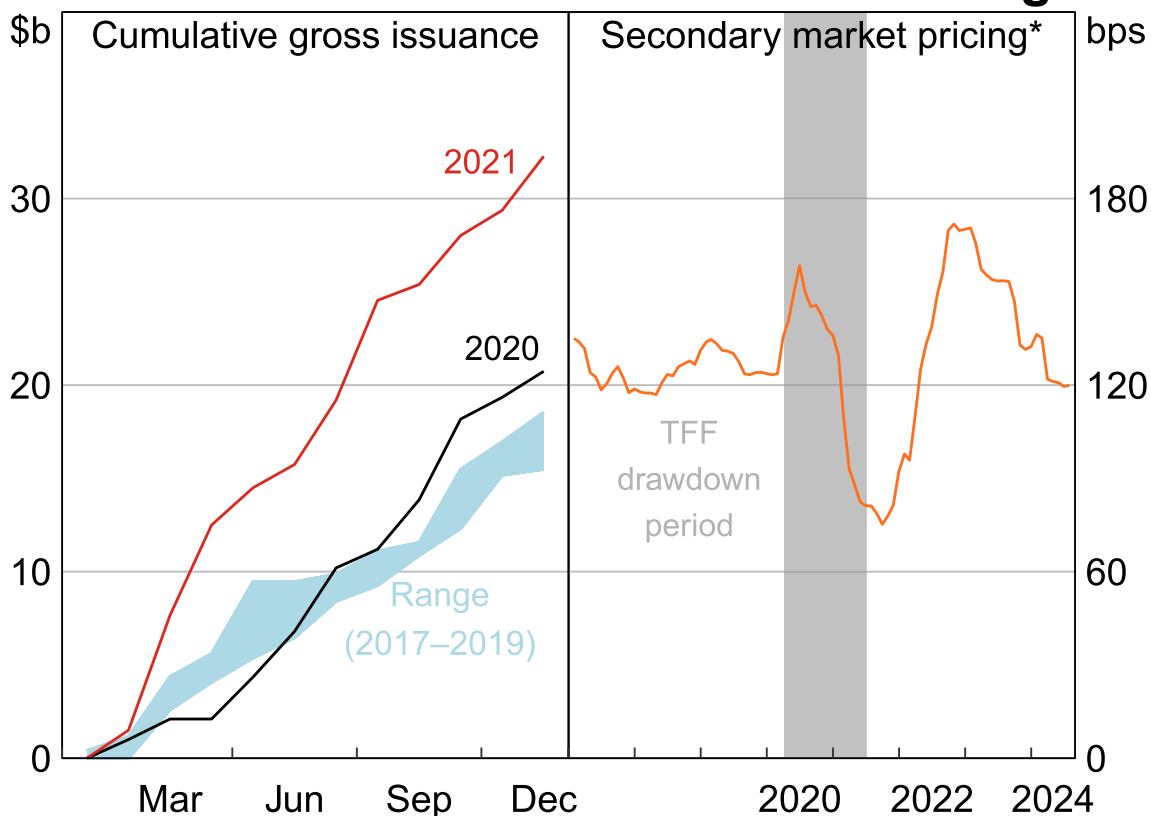
** Includes deposits in housing loan offset accounts.

Sources: APRA; ASX; Bloomberg; LSEG; major bank liaison; RBA.

- Together with other parts of the policy package, the TFF also indirectly helped to lower the cost of wholesale funding. With the TFF in place, banks had little need to issue bonds but investor demand for those and other similar securities remained strong. Strong demand coupled with a sharp fall in supply contributed to a decline in yields on a range of existing and newly issued securities. This included securities issued by non-major banks (which continued to issue bonds). Non-bank lenders also benefited significantly; their issuance of residential mortgage-backed securities (RMBS) – a key source of their funding – picked up significantly as the cost of issuance dropped sharply (Graph 3). [\[7\]](#)

Graph 3

Non-bank RMBS Issuance and Pricing



* Spread to one-month BBSW.

Sources: Bloomberg; ICE; KangaNews; RBA.

Did the TFF achieve its aims?

Banks passed lower funding costs through to retail lending rates for both households and businesses, on both new and outstanding loans. On average, outstanding lending rates fell by almost 100 basis points – a little more than the 84 basis point decline in banks’ overall cost of funding (Table 2). [8] The fall in business rates was comparable across variable- and fixed-rate loans, with larger reductions for SMEs than was the case for larger businesses. But the fall in mortgage rates was much more pronounced for fixed-rate loans; the decline in fixed rates was also large relative to the reduction in the cash rate compared with earlier episodes of monetary policy easing. Banks’ decisions to provide fixed-rate mortgages at very attractive rates was consistent with the low fixed-rate TFF loans as well as banks choosing to focus their competitive efforts in the fixed-rate mortgage market.

Table 2: Changes in Funding Costs and Outstanding Lending Rates

February 2020 – February 2022

	Change Basis points
Cash rate target	–65
Funding costs ^(a)	–84
Overall mortgage rates	–97
– Variable mortgage rates	–68
– Fixed mortgage rates	–152
Overall business lending rates	–105
– Variable business lending rates	–103
– Fixed business lending rates	–89

(a) Major banks.

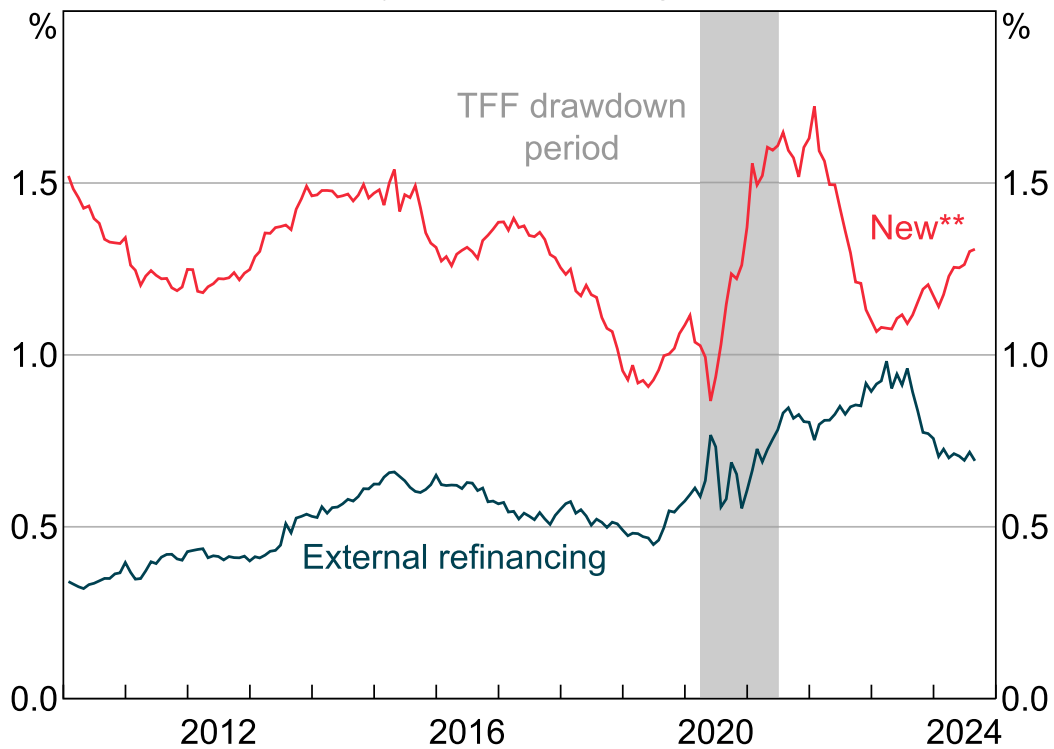
Sources: APRA; ASX; Bloomberg; LSEG; major bank liaison; RBA.

Households and businesses that took out fixed-rate loans benefited from the particularly low fixed rates on offer at the time. The share of new housing lending at fixed rates rose from around 15 per cent at the start of the pandemic to a historical high of over 45 per cent by mid-2021.^[9] Not only were existing borrowers switching from variable to fixed rates, but new mortgage lending also picked up noticeably through 2020 and into 2021 (Graph 4). In addition, lower rates contributed to a pick-up in disposable incomes of debtors. In these ways the TFF (together with other parts of the policy package) helped to support dwelling investment, the housing market more broadly, and other elements of aggregate demand.

Graph 4

Housing Loan Commitments

Monthly; share of housing credit*



* Seasonally adjusted and break-adjusted.

** Excludes refinancing.

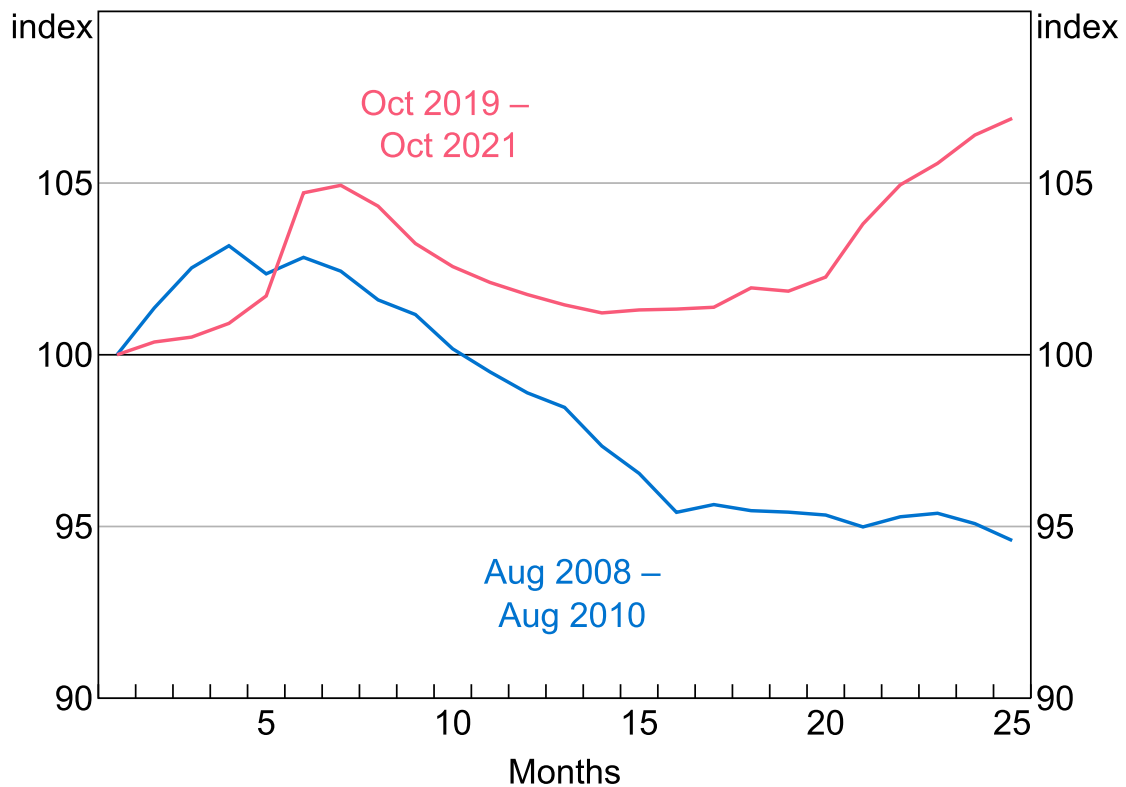
Sources: ABS; APRA; RBA.

The TFF was also intended to support the availability of credit. We were particularly concerned that banks might have been reluctant to continue to extend credit to businesses during such difficult times. The TFF is likely to have played a role in underpinning business credit. It encouraged demand by contributing to lower rates for borrowers. It also encouraged banks to expand lending to businesses to obtain additional low-cost TFF loans. Indeed, business credit held up better during the pandemic than in the global financial crisis (GFC) (Graph 5); such declines had also been evident in earlier downturns. Despite the supporting role of the TFF, total business credit may not have increased through 2020 and 2021 for several reasons, including a lack of business confidence and the reduced need for business credit given the sizeable government support to businesses' cashflows. And despite the considerable incentives in the TFF to expand SME lending, staff estimates found no statistically significant effect on total SME lending compared with large businesses.

Graph 5

Business Credit*

Pre-crisis levels indexed to 100



* Seasonally adjusted and break-adjusted.

Sources: APRA; RBA.

While not an explicit goal, one other benefit of the TFF was the indirect support it provided to the public sector balance sheet. By supporting stronger economic outcomes, the TFF – together with other monetary policy measures – contributed to higher tax revenues and lower support payments to households and businesses than would otherwise have been the case.

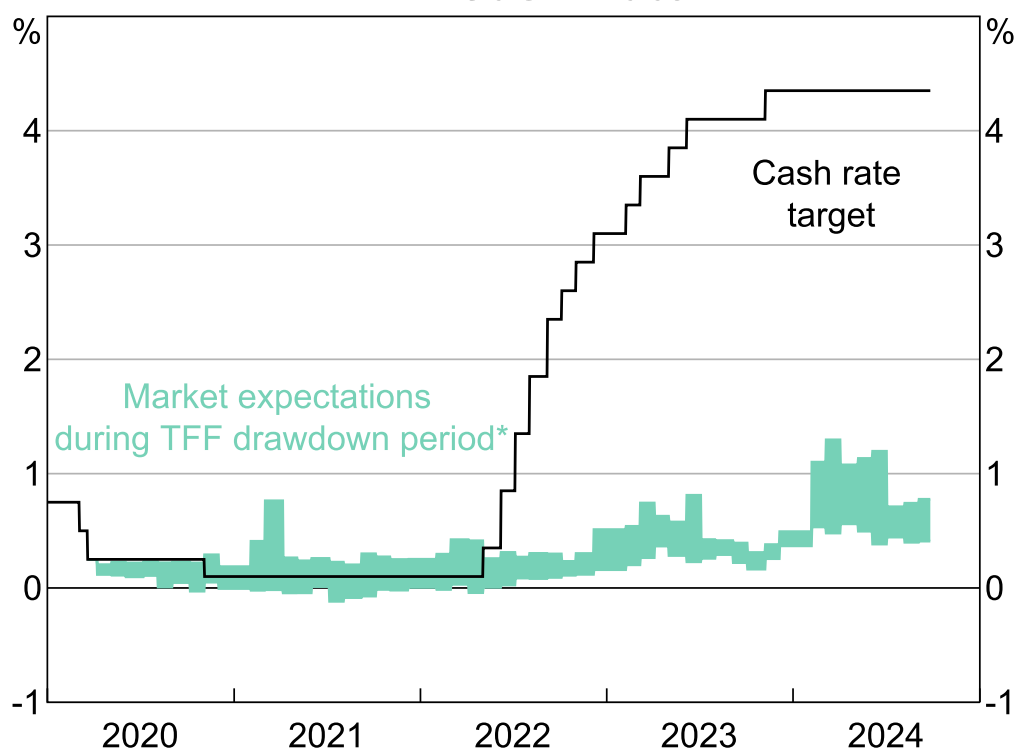
How much did the TFF cost?

The TFF was part of the insurance the RBA took out against a catastrophic economic outcome. While some of the TFF's design features underpinned its significant use by the banks – and hence its economic benefits more broadly – these were also associated with financial costs for the RBA. The total cost to the RBA is estimated to have been \$9 billion. There were several reasons for this cost.

First, the choice to supply funds at a fixed rate was intended to give banks and their borrowers certainty, thereby reinforcing the other elements of the policy package: notably the RBA's three-year yield target, and its forward guidance. But the economic recovery and increase in inflation turned out to be much stronger, and started much earlier, than the initial upside scenarios considered by most economists and the RBA. As a result, the Board ended up raising the cash rate target by much more

and much sooner than had been expected (Graph 6). While the TFF was profitable for the RBA until May 2022, once the cash rate increased, the RBA was paying banks more interest for the balances that they kept at the RBA than the low fixed rate the banks were paying on the TFF. Because the banks passed these lower funding costs in full, household and business borrowers who had locked in low fixed rates were the ultimate beneficiaries as interest rates rose.

Graph 6
RBA Cash Rate



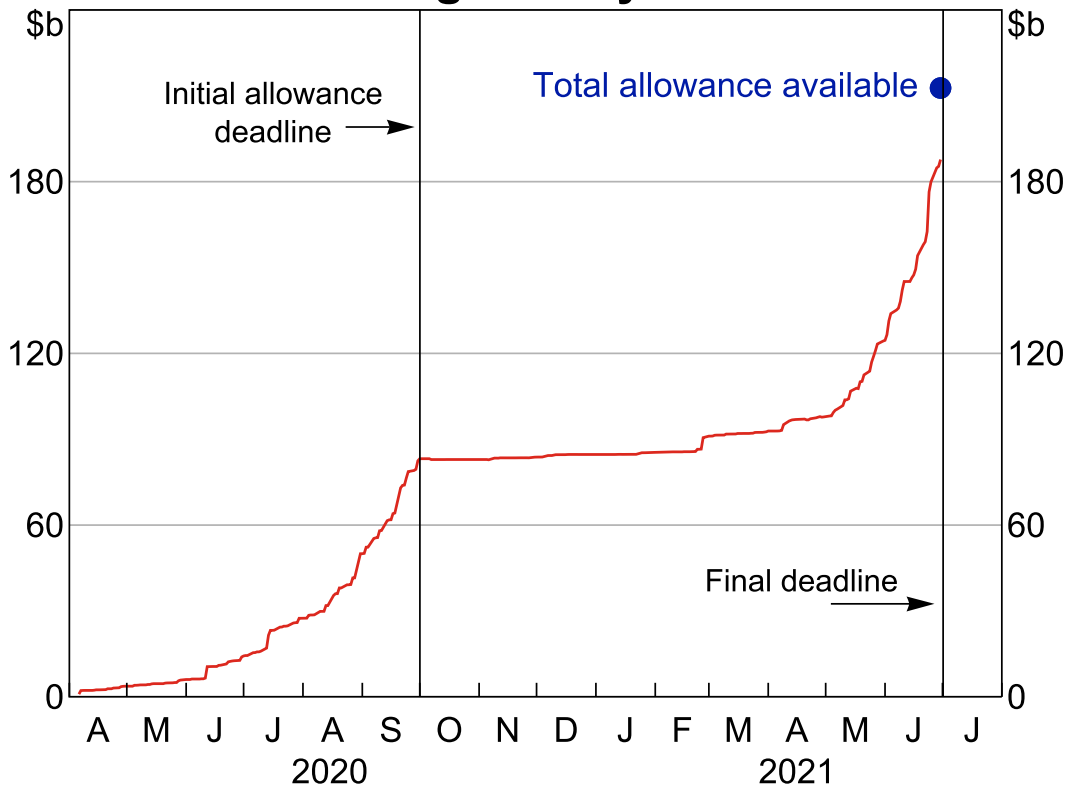
* Minimum and maximum cash rate path; implied by OIS from 19 March 2020 when the TFF was first announced to 30 June 2021 when the TFF was closed to new drawdown.

Sources: Bloomberg; RBA.

Second, around \$4 billion of this cost was the result of the Board's decision to extend the TFF in early September 2020. At that time, the banks had taken up just 60 per cent of their initial TFF allowances, with almost half of that occurring as late as August (Graph 7). This suggested that the banks did not need TFF funding to compete for, or satisfy, the demand for borrowing from households and businesses. Rather, the banks waited until as late as practical to draw down TFF funds because doing so extended the time the TFF would contribute to meeting regulatory liquidity requirements on the banks. [\[10\]](#) A similar pattern of late take-up was later observed with the second tranche of the TFF.

Graph 7

Term Funding Facility Drawdowns



Sources: APRA; RBA.

Some lessons for the future

The TFF delivered on its goals. It lowered borrowing costs for a range of borrowers, kept credit flowing to the economy, and supported aggregate demand. In addition, along with other measures – including the purchase of bonds in the early weeks of the pandemic – it helped to restore confidence in financial markets, which were significantly disrupted in the early days of the pandemic.

Based on the findings of the review, the Board judged that a term lending tool of this kind would be worth considering again if warranted by extreme circumstances. But there were valuable lessons we learnt along the way that could help to shape any future program of this type.

Degree of support for the economy versus flexibility

Central banks can choose between fixed- or variable-rate facilities. The fixed-rate option was chosen for the TFF in part to reinforce other policies: the yield target and forward guidance. Such policy packages can be particularly valuable when the standard interest rate lever is already near zero and significant downside risks to the economy remain. But the flipside to a fixed-rate facility is that it lacked flexibility. And given the large take up of the TFF at a very low fixed rate, it incurred a material

financial cost to the RBA when the economic recovery and pick-up in inflation turned out to be much stronger, and started much earlier, than had been expected.

Indirect effects

Many non-bank lenders were concerned that the TFF would undermine their competitive position vis-à-vis the banks. We had expected the TFF to help lower rates in wholesale funding markets to a degree. ^[11] But this effect was much stronger and more pervasive than we had anticipated. The TFF helped to lower funding costs significantly for a range of lenders and corporations that had no access to TFF funds. ^[12] It is hard to identify the specific contribution of the TFF to these lower funding costs separately from the effects of the wider policy package. But staff estimates suggest that these indirect effects caused yields on RMBS to be around 50 basis points lower than they would otherwise have been.

Open lines of communication between the RBA, other government agencies and industry

Another lesson is the importance of collaboration with other government agencies, and regular contact with industry participants. Collectively, this helped financial stability risks associated with the TFF to be well managed. This included monitoring and managing banks' refinancing and liquidity needs well ahead of the repayment of their TFF loans, although that task could have been more challenging under less favourable market conditions.

Similarly, for household and business borrowers, the RBA, the Australian Prudential Regulation Authority and the banks' close monitoring (and banks' prudent lending standards) helped to reduce the risks associated with the rise in borrowers' mortgage payments when their very low fixed rates rolled over to much higher variable rates. Only a very small share of borrowers struggled to meet the increase in their mortgage obligations when their low fixed rates expired.

Importance of contingency planning, risk management and governance

One of the important lessons is the value of planning ahead and being ready for a wide range of operational contingencies. We got the TFF up and running quickly in part by relying on existing, well-understood practices. But the speed with which the RBA designed and implemented the TFF also limited our ability to fully consider and manage the associated risks.

- Forward planning can expand the options available, help us to better weigh up the costs and benefits of each, and prioritise any pre-emptive operational work. On this latter point, for example,

floating-rate term-lending would have been challenging for both the RBA and the commercial banks to adopt in early 2020, because neither the RBA nor the banks were readily able to undertake floating-rate repos. The RBA and the banks have since upgraded systems and now have the capacity to easily undertake either floating- or fixed-rate repos.

- Design features could have competition implications. While RBA staff liaised with the Australian Competition and Consumer Commission during the TFF's setup, it would be helpful to consider competitive implications ahead of time for any future facilities.
- Finally, and perhaps most importantly, the Board has agreed to strengthen the way it considers risks, including by examining a wide range of economic scenarios when making policy decisions involving unconventional tools, and how to judge appropriate exit paths from such tools. In retrospect, a greater focus on potential upside economic outcomes could have led to a different calibration of the TFF, including deciding not to extend it in September 2020.

Summing up

The TFF met the objectives we set out for it at the start of the pandemic. It helped prevent dire economic outcomes at a time when the outlook was bleak and highly uncertain, and there was limited scope for further cuts to the cash rate. The TFF contributed to materially lower lending rates for households and businesses by reducing funding costs directly for banks, and indirectly for other institutions that borrow from wholesale funding markets. It kept credit flowing to households and businesses at a time when banks might have otherwise curtailed lending. In helping to prevent a much more severe economic downturn, the TFF also contributed to stronger public sector balance sheets than otherwise.

Would the RBA use a term-lending tool again in the future? The Board would consider such a tool in extreme circumstances when the cash rate target had been lowered to the full extent possible. But it would do so only after consideration of a wide range of scenarios and the associated risks, and with a broader range of operational options than were available at the time of the pandemic.

What's next?

In line with recommendations from the Review of the RBA, we will be publishing a framework for additional monetary policy tools next year. [\[13\]](#) The broader set of lessons learned from the combined use of a range of unconventional monetary policies will be considered as part of that framework.

Endnotes

- [*] I thank Susan Black, Iris Chan, Tekla Bastian, Venura De Zoysa, Siobhan Hutchings, Ben Jackman, David Meredith, Max Prakoso and Peter Wallis for their assistance in helping me to prepare this speech.
- [1] The full review is available at RBA (2024), [‘Review of the Term Funding Facility’](#), October.
- [2] The series of reviews are available at RBA, [‘Reviews of the Monetary Policies Adopted in Response to COVID-19’](#).
- [3] The package comprised a lower cash rate, a commitment by the Board to not raise the cash rate target until it was confident that inflation would be sustainably within the target range, the introduction of the TFF, bond purchases to address market dislocation, and a yield target on three-year Australian Government bonds: see Lowe P (2020), [‘Statement by Philip Lowe, Governor: Monetary Policy Decision’](#), Media Release No 2020-08, 19 March.
- [4] See Lowe P (2020), [‘Statement by Philip Lowe, Governor: Monetary Policy Decision’](#), Media Release No 2020-20, 1 September; RBA, [‘Term Funding Facility Increase and Extension to Further Support the Australian Economy’](#), 1 September.
- [5] TFF usage was high by comparison with similar schemes internationally.
- [6] The cost differential to obtain new funding through the TFF would have been even larger for non-major banks, which typically have higher issuance cost because of their lower credit ratings.
- [7] Securitisation markets were also supported by the Australian Office of Financial Management’s (AOFM) Structured Finance Support Fund (SFSF), which provided support to non-banks and smaller banks through public and private investments in structured finance market: see AOFM, [‘Background and Legislation’](#), available at <https://www.aofm.gov.au/securitisation-investments/background-legislation>.
- [8] Indeed, banks’ net interest margins declined over this period due to a range of factors, including strong competition and lower spreads-to-swap on fixed-rate loans.
- [9] Refinancing by households from variable-rate loans to lower fixed-rate mortgages was also elevated.
- [10] See RBA, n 1, for a detailed discussion of the TFF and banks’ liquidity requirements.
- [11] See, for example, Kent C (2021), [‘The Term Funding Facility, Other Policy Measures, and Financial Conditions’](#), Address to KangaNews, Online, 9 June.
- [12] In particular, non-banks that specialised in non-prime lending (and hence did not typically compete with the banks) benefited. However, some non-banks – particularly those that compete directly with banks in housing lending markets for prime borrowers – noted that non-banks did not receive the same level of policy support through the SFSF as banks using the TFF, which was significantly cheaper than issuing in securitisation markets.
- [13] See Australian Government (2023), [‘Review of the Reserve Bank of Australia’](#), Final Report, March.

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