ANZ

News Release

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Transcript of podcast with ANZ Chief Risk Officer Kevin Corbally, ANZ Acting Chief Financial Officer Shane Buggle and ANZ Head of Investor Relations Jill Campbell

Jill Campbell: Hi everyone, I'm Jill Campbell the Head of Investor Relations for ANZ. Welcome to all of you listening to today's podcast which accompanies ANZ's release of a trading update for the first quarter of financial year 2021. We've released a number of materials today including a slide pack and we'll refer to that at points during this podcast. The materials were lodged with the ASX, they're also available on the ANZ website in the shareholder centre.

I'm speaking today with our Chief Risk Officer Kevin Corbally and our acting CFO Shane Buggle covering some areas of interest to those of you looking to delve a little deeper into the update.

I'll start with you Kevin. Let's talk a little about credit quality and provisions. ANZ announced a $A173 million release of collective provision today. Can you walk us through some of the aspects of determining that?

Kevin Corbally: Jill, look thank you. There are a number of things to think about here. We came into this financial year in a strong position. We're very well positioned from both a capital and a provisioning perspective at 11.7% Common Equity Tier 1 ratio and also we had $A5.6 billion of total provisions. And, included within that there was about $A4.8 billion in collective provision balances at the end of that first quarter.

So if you think about it this way, we put on roughly about $A1.7 billion in provision charges essentially in 6 months last financial year and what we've done is we've released about 10 per cent of that uplift today. And the outcome was a mix of some portfolio reductions together with the release of some of the build-up in the provision balance as the economic conditions have improved since last year.

If you think about it, the economic outlook has really improved relative to what were pretty dire estimates that we had last year and also both Australia and New Zealand, I think have really handled COVID better than almost every other country in the world. If you think for example that at September last year, we were forecasting a contraction in housing prices of nine per cent this year. Now what we're saying in this update is that we're forecasting growth nationally of about five per cent. And similarly we're expecting GDP to return to pre-COVID levels a year earlier and we're also forecasting a much lower unemployment level than we were last year.

At the same time though, this is still a delicate period for the economy as evidenced by recent issues in Queensland, NSW, Western Australia

and even more recently in both Victoria and in Auckland. We are also mindful that there's still quite a bit of support in the system – from government in the form of JobKeeper, JobSeeker etcetera. And also that banks through things like mortgage and commercial loan deferrals have also supported the system and it's sort of unclear what happens when all of that support falls away.

So, if I was to step back and think about where the economy is at especially relative to last year, how we're set up with less customers on deferral than many of us thought was going to be the case last year – we've got roughly about 1% of our home loan customers in Australia and New Zealand that are still on deferrals – but also counter that with the level of volatility and uncertainty that still exists, we feel that our current provision levels are prudent and are appropriate and we are comfortable with what is a relatively small release.

Jill Campbell: Ok, thanks. So when you think about that total provision charge that's obviously a combination of whatever the outcome was for the IP or individual provision and the CP, collective provision outcome. The IP in the first quarter finished at $A23 million and that's substantially lower obviously than the average for, if I think back over the last couple of years. So how should we think about that? Is it timing, is it something else, have we struck a new normal?

Kevin Corbally: Look if we step back, it's worth remembering that the Individual Provision charge is actually an aggregate of new impaired charges, increased impaireds and any write backs and recoveries that we might have. So essentially in the first quarter what we saw was write backs and recoveries were broadly in line with the average of second half of last year. And new individual provisions and write backs and recoveries largely sort of offset each other and in addition the increased impaireds were actually lower across the portfolio.

So in terms of your question, 'is this the new normal?' I think we're some way off normal conditions and we haven't really had a normal quarter for some time right? So I don't think we are yet to see the impact of the removal of the support that I mentioned earlier from government and the banks. We do expect that that will start to flow through in the second half of this financial year and also into 2022 and we will therefore see an increase in IP. But I think it's important to remember that during the course of last year we built up a large collective provision balance and that was built up with an expectation that we would ultimately then release that as credit quality deteriorated or, alternatively some of our customers became delinquent. And the other point I'd make too is that the lower Individual provision charge for this year also reflects the fact that our larger customers are in a much better financial position and it's important to bear in mind that's a bigger impact for us because our Institutional business is a bigger element of our book than maybe some others. But it's also a reflection on the fact that there's been unquestionably a lot of work on reducing our risk profile and improving the credit quality of our book, not just within Institutional actually, over the last number of years.

Jill Campbell: Ok, thank you. You mention deferrals as part of one of your answers there. When you think about the deferral cohorts today, what are the kinds of things you're thinking about?

Kevin Corbally: What we've seen and what people will have seen in the trading update is that we've had an 84% reduction in our Australian mortgage deferral cohort from the peak to the end of January. We've also had an 88% reduction in our Australian commercial customers that were on deferral and a 92% reduction in New Zealand Mortgage deferrals. Or another way to think about it actually might be that approximately 1% of our home loan customers in Australia and New Zealand remain on deferral and there's a meaningful portion of that - those that are remaining on deferral - that are due to roll off in February.

So that backs up part of the initial view that in large part, and we've been saying this throughout, these were customers who just needed time … given the impacts of COVID, customers who were performing well prior to the lockdowns etcetera and would highly likely return to performing once they emerged from these lockdowns.

And it's important to remember, I think this is really important, that we have been in regular dialogue with these customers throughout the deferral period and will again contact them several weeks out from the end of their deferral period to discuss how they're tracking. And the indications are that those that need more help will be relatively small and therefore it will be manageable. Now we'll obviously have to work really closely with those customers and look at what options are available to them and that includes the ability if we want to restructure those loans without capital penalty right up until the end of March.

Jill Campbell: Ok, so when you think about, sounds like most of these (deferrals) are going to be gone before the end of March but there will be some customers who remain. When you think about that tail, how do you deal with that, how do you think about that?

Kevin Corbally: If you look at those remaining on deferral post the end of January, there's probably not really many surprises in terms of the composition – so where they are geographically, what businesses they're in - 60 per cent of our commercial loans that are on deferral are from Victoria. And if you combine our exposure in cafes and restaurants and retail trade that's about 44 per cent of those that are left.

So as we approach the end of March, the tail, as you described it, then is likely to be small, we think it will be manageable particularly relative to the level of provisioning that we've already taken to date.

And maybe the key point is that delinquency trends for the sector, more generally have been favourable and they've been favourably impacted by the deferral cohort because basically anyone who was on deferral is treated as current. Having said that we've, as I said earlier, we've been in regular dialogue with all of our deferral customers throughout the deferral period. We are going to do so again a few weeks before their end date. And our experience has been that in almost all instances those saying that they will resume payment have actually done just that.

Jill Campbell: Right, thanks for that. We're going to move on now to talk to you Shane about margins, I think that will be a bit of a hot topic today. So the Group margin up 5 basis points, can you walk us through the components of that?

Shane Buggle: Thanks Jill. We've included within the trading update support pack a slide (slide four) which provides a useful step through of the movements in the margin. And you can see that the Group net interest margin or NIM increased 3 basis points, on what we call the underlying basis, that excludes the Markets balance sheet activities. Pleasingly the margin grew in each of our divisions which will be the first time in quite a while.

The impacts from low rates on our replicating portfolio and liquidity books did come through as we said it would and competition continues to remain intense.

The relative improvement arose from improved wholesale funding and deposit pricing. Some improvement in the mix which was came from stronger growth in our mortgages book relative to our Institutional lending book and some benefits from asset pricing and that's where we repriced the Institutional front book in the second half of 2020 and we see that flowing through.

Jill Campbell: So when I look at that waterfall chart that you've talked about, there's four basis points of funding cost and deposit pricing and another two basis points of asset pricing. Is that now in the NIM or is there more upside from here?

Shane Buggle: I think essentially it's embedded in the NIM now. We may see some further upside on deposit pricing as TD rates and savings might come down. But they're also asset competition headwinds and we expect those to continue.

If you think about the home loan market there are incredibly sharp fixed rate offers in the market now and we expect to see customer switching and back-book repricing to persist. The front book/back book margin differences and higher margin maturities will also be a headwind.

Jill Campbell: So when you think about all of that, and this is the impossible question, but how are you thinking about where margins will be at the end of the half?

Shane Buggle: Well Jill, as you know we don't provide forecasts. But you could think about it this way.

On volumes the mix benefit of the faster growing retail and commercial book vis-a-vis our Institutional book is likely to continue given the momentum we have particularly in the mortgages book. On pricing, the benefits as I mentioned from funding and deposit pricing are largely embedded. So offsetting that we continue to have the lower rate environment and that impacts our replicating portfolio and impacts our

liquidity book and competition continues to remain persistent.

So thinking about all of that we would expect that on an underlying basis margins to be slightly up compared to the second half of 2020. How much depends on customer behaviour.

Jill Campbell: So that's slightly up on the 159 basis points?

Shane Buggle: Measuring by reference to the underlying 159 (bps 2H20), yes.

Jill Campbell: Last question which is one for you Shane still, on expenses, another flat cost outcome. How should we think about expense management in the quarter?

Shane Buggle: Well I think it's been a consistent story from ANZ on expense management for the last five years. Our position hasn't changed and we aim to continue to reduce cost in absolute sense. That comes from seeking productivity improvements on our business as usual costs and also to invest in the future of the business and partially through the savings from the productivity benefits and partially through our investment spending.

We have - and I just want to remind you – said many, many times that the journey is unlikely to be linear and that we will not go into underinvest just to hit a number. So we might see some bumps along the way but it continues to be a very tight focus on business as usual and productivity.

Jill Campbell: Right and it's been quite a few quarters in a row now so I think we can definitely say there's a theme.

So that was all the questions I had for both of you. I think we've covered most of the main topics. There will be a transcript of this podcast available online if you want to check back on any of the things that we've talked about and of course the Investor Relations team is available to have a conversation with you as well. So with that, thank you to everyone who has listened. Thanks to Shane, thanks to Kevin.

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