Question and Answer

Melanie Kirk

Great. Thank you. This morning, we will be taking analyst and investor questions. We would ask the media to hold their questions until their briefing this afternoon. We will start in the room and then we'll move to the phones and the web. In terms of protocol, could you please wait for the microphone and state your name and the organization that you represent. And please, to allow everyone the opportunity to ask questions, keep it to 2 questions.

We'll start with Jarrod Martin in the room.

Jarrod Martin
Crédit Suisse AG, Research Division

Jarrod Martin from Credit Suisse. Ian, a question on dividend and capital and all things good. So if you look at your capital ratio, first the $5 billion raising looks pretty good at 10.4% and everyone can pretty much understand the rationale for actually getting there. However, if I deduct things like the mortgage risk weights, you've called out, that's 95 basis points, and further roll off of your Colonial debt, that's around another 50 basis points over time. Pro forma-ing for that, that brings you back to circa 9%. If you look at your organic capital generation over the last 3 halves, you've gone from 9.3%, 9.2%, 9.1%. CBA hasn't been as good as it has been in the past in generating organic capital, and we know that there's further changes to come. The $5 billion rights issue, 4.3% additional shares on issue, maintaining a payout ratio. I'm just looking at that and it seems to me that this 9% really pro forma core equity Tier 1 is going to edge down to 8.5% and either you're coming back to the market for capital or you're changing your payout ratio at some point in the future. Something seems to me has to give for you to be able to actually continue to improve capital or payout what you want to payout going forward.

Ian Mark Narev
Former Executive

Well, Jarrod, I mean, everyone makes their own assumptions in terms of going 2 or 3 years out. And for example, in the Colonial loan recourse debt, we're talking about '17 and '18. And you've got to make your own assumptions about what risk-weighted assets growth is doing at that stage, what credit quality is doing at that stage. And it's up to investors and analysts to make their own assumptions on that in terms of how we think about it. Probably for the last couple of years, we've been sitting here saying 2 things. Number one is you've got to be flexible to your environment in terms of your capital decisions. And we've said that each time we, particularly at the interim and the full year, we look at outlook for risk-weighted asset growth, outlook for credit quality lease out effect as we make the decisions that we make and we have a dividend policy around that, we will continue to do that. So that's #1 thing that we said. The other thing we've consistently said is that we've had an environment where the financial system inquiry has been out there, where Bazel has been out there. And we've consistently said, probably for the last couple of years, the biggest single determinant of the external factors on us is going to be decisions made on Home Loan risk-weighting. Now interestingly, as David pointed out, the APRA decisions on that are not prudential standard-related. They're competition-related. The prudential standard-related metric is the one on global comparability, which we don't yet fully understand because they have said it doesn't necessarily mean it's within the top quartile, but we're clearly well within the top quartile. And that's actually the capital level that they have required. So when we add all those things up, we've seen exactly the same numbers as you have. We can quantify the impact of the Colonial debt, we can make our assumptions on risk-weighted assets, et cetera, we're very clear on what our dividend policy is and how important that is to our shareholders. And we've picked the $5 billion because we believe it's the right amount to respond to the changes we know about and to return to our normal transmission position as we watch the environment and we adjust capital in response to the environment. So there are scenarios under which your numbers might be right. There are scenarios under which I could give you other assumptions which would take the capital up to the top 9s and up to 10. We look at all those different scenarios, we model them and that's how we came up with a number that we had for the rights issue, and we're very comfortable with it.

Unknown Executive

All right. The next question we'll take it from Craig Williams.

Craig Anthony Williams
Citigroup Inc, Research Division

I guess I agree with a lot of Jarrod's math around that stuff, and I'm not sure how the current payout settings give you the capacity for balance sheet growth to absorb high credit costs as they probably likely come through and to absorb high regulatory capital requirements. As far as -- changing to my actual question now. If we talk about the global asset management business, I think there's been a recent restructure of that business, a dropping of the Colonial brand in part in the Edinburgh business. Can you talk about the significance or not of the restructure as it's been taking place?

Ian Mark Narev
Former Executive

Yes, the restructure, which was really between loosely described the Edinburgh-based team and the Hong Kong and Singapore-based teams was really solely driven by capacity and to making sure that the governance structure and the business structure of that was able to accommodate the trading strategies of both parts of the business, which all our investors will understand very well. That's all it stands for. I'm aware there's been all sorts of speculation about what businesses we might own, what businesses we might not own which is probably the subtext behind your question. So let me answer the question I think you wanted to ask, which is to say, from where we are on the capital raise, there is no divestment that we're going to contemplate for capital reasons. Now we've said consistently I had achieved to both buying and selling is we always look at businesses we own, that others own, and we say are we the best owner of it? We'll continue to do that for the next -- well, as long as I'm around and probably beyond. But there is no asset sale program that is going to be driven by capital requirements.

Unknown Executive

Great. We'll take the next one from Jon.

Jonathan Mott
UBS Investment Bank, Research Division

Jon Mott from UBS. A question for David, I could. And it's just a bit technical. Page 88, which goes through the risk-weighted assets, your profit announcement. You can see there the -- if you look at the advanced accreditation and you can see the 2 top lines there, corporate and SME corporate risk weights have both grown pretty aggressively over the last 12 months. So they're up by roughly 24% for the corporate and close to 14% -- I think, a 13%, 14% for the SME corporate. Obviously, the credit growth in those books are growing at about 4% or 5%. So can you run through why we're seeing such big growth in these risk-weighted assets? Is this a result of increased probability of default or have you been changing some model assumptions around that? And would that continue?

David Paul Craig

I might ask Alden to take that question.

Alden Louis Toevs
Former Group Chief Risk Officer

The basic answer here -- and I'm struggling to find exactly the page what you're looking at, is that -- oh, thank you. Yes, the -- there have been some model changes. They're required as we update models over time. That's the bulk of it. The -- there's been some migration downward in the top-rated credits. These are rated credits of BBB and higher. There's been very stable return of lower pass credits to higherperforming credits so that the bulk of it would be on the model change, but with some extra growth in the portfolio plus also some degradation of the higher-rated credits.

Jonathan Mott
UBS Investment Bank, Research Division

Can you just run through the model changes, why they came about, what was going on there?

Alden Louis Toevs
Former Group Chief Risk Officer

Well, this is the annual refresh of models. And you get some volatility, some extra modeling insight and some extra data on which you base your models.

Jonathan Mott
UBS Investment Bank, Research Division

And just following on, at the bottom of the page, you can see the interest rate risk in the banking book. I think David called out rate movements were one driver. But that's been pretty volatile going from $15 billion to $5 billion to $11 billion, which is quite a material change from half-to-half. Can you do anything to stabilize that given how aggressively that's jumping around? It can't all just be long ends to the yields and hope none of the U.S. bonds just start to get higher.

Alden Louis Toevs
Former Group Chief Risk Officer

We have taken some lien positions over the course of the year that would change these sorts of numbers. And then also we'll be bringing into account through accruals, interest rate risk banking book mismatches that just sort of come through. And the rates of long ago as they sort of mature drop into these kinds of numbers. So there's not been any massive or material change in the strategy. And the results have been actually quite productive for the group.

David Paul Craig

Yes, I think it's important to understand, though, that this is -- I mean, obviously, we're the only country in the world that has this measure. It is a volatile item. It moves with end markets when the markets are volatile that moves when the markets have been volatile. As you know, we've had -- we've made gains that are in -- that are within that book. And as those gains then amortize, then that reduces. So that's one part of it. So on Page 121, you can see the components very clearly. And then the other side of it, as I've pointed out, is that with rates in the long end of the curve going up then again the risk side of it goes up because rates are up. So it's a mixture of those 2 things that are the main movement. But it is going to be a volatile number. That's the nature of the beast.

Unknown Executive

We'll take the next question from Mike Wiblin.

Michael Wiblin
Macquarie Research

Mike Wiblin from Macquarie. Just a question on the capital raising. Obviously the point to highlight here is it's not a remedial action on capital. It's obviously bolstering the balance sheet. Have you thought a little bit about what some of the positive impacts might be of holding more capital? And maybe this is a question for Paulo [ph] on the debt rating, wholesale debt costs. The potential for further repricing and also the perceived safety of the institution because I think people tend to look at these things as being a little bit negative from the dilution perspective, but is that the case?

Ian Mark Narev
Former Executive

Well, one positive we'd hope for is we'd stop getting questions about capital. But I might just hand over to Paulo [ph] on that one as you suggested and get him to give you some sense of how it might play out in the market.

Unknown Executive

Yes, I think it's a good point that there will be likely some positive impacts from this. I think, certainly, it's protective of the rating. It's protective of our position as one of the best capitalized banks in the world. And we already benefit, I think, to some extent, from being differentiated in credit markets from both the other Australian banks, but viewed globally as one of the -- as one of the highest quality debt issuers, and I think this only protects that. Hopefully as the markets normalize and we've seen some volatility over the last few weeks, that will play through in terms of improvement in the cost of funding.

Michael Wiblin
Macquarie Research

And repricing?

Ian Mark Narev
Former Executive

That, as you know, is something we can't give any comment about.

Michael Wiblin
Macquarie Research

Sure. And I just had a -- just a quick follow-up question, just around APRA's 200 basis point number. I mean, is there anything else that you perhaps could shed on that? Is that capital ratio, is it core equity Tier 1 or is it total capital or is it something else?

David Paul Craig

I think, to be honest -- well, firstly, let's remember that was 200 basis points this time last year for the big 4 banks on average. So it clearly doesn't specifically apply to us. We've now disclosed to you all of our numbers, and we're in the top quartile on all measures of capital. So from our point of view, that's really an academic position.

Unknown Executive

We'll take the next question from Andrew Triggs.

Andrew Triggs
Deutsche Bank AG, Research Division

Just a question on a couple of areas of, I guess, stress that you called out in the -- on the asset quality side of things. New Zealand Dairy and personal lending in Australia, from memory, are reasonable areas of growth relative to system for CBA. Any sort of change in your assessment of the growth prospects or the attractiveness of those 2 markets please?

Ian Mark Narev
Former Executive

So sorry, it was New Zealand Dairy and...

Andrew Triggs
Deutsche Bank AG, Research Division

New Zealand Dairy and personal lending.

Ian Mark Narev
Former Executive

Personal lending. Well, I might just get Matt to talk about personal lending in a second. In terms of New Zealand Dairy, as I mentioned earlier, strategically an ASB growing in business banking including rule has been priority for a number of years. Number one, the size of the book relative to the Commonwealth Bank balance sheet frankly is completely immaterial. Number two, though, because we govern ASB very closely, it's got its own board there. As David mentioned there's an extra overlay being taken for the rural price. I mean, the issue I think in New Zealand Dairy is not just the fact that the milk price, Fonterra's milk price in particular, has gone below $4, but it's come down pretty quickly from $8 in a pretty short period of time. And that means you've just got to be very careful about farmers who were expecting $8 milk prices and how they're going to react to $4 milk prices. Those sorts of things are taken into account when we're advancing the money, obviously. But nonetheless in these sorts of charges, we've got to be careful. We're pretty comfortable about it. We're comfortable about provisions for it in particular. In all types of business banking, but in agri, in particular, you've got to make loans in a way that enables you to withstand the working capital problems, otherwise you just can't be in the business. So we take that view from the start. So I would expect in that book, yes, you'll continue to get a bit of weakening, but will it be material in terms of our results overall? Not at all. I might just get Matt to talk a little bit more about the personal lending.

Matthew Comyn
CEO, MD & Executive Director

So I mean the personal lending segment still remains very attractive. Obviously, we price for the risk that we take. As David mentioned, the majority of the increase in the arrears is actually driven out of WA in Queensland. To give you some precision around that, it's 32% of our balances, that contributes about 60% of the arrears deterioration. So we're very watchful of that on both a front book origination perspective as well as our management of that. But in terms of the credit quality in that product, we continue to see that as an attractive part of our business mix.

Andrew Triggs
Deutsche Bank AG, Research Division

And just a follow-up question, the other income line in other banking income, you mentioned some gains in sales and investments. Was that a material number for the second half?

David Paul Craig

No, there were no material sales. There were some sales, but they were small.

Unknown Executive

And we'll move to Scott Manning next.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Scott Manning from JPMorgan. Even though people might not ask about capital anymore, I think the more important question going forward that you'll still get is what are you going to do about it? Where are you deploying that capital? How are you going to get a return on it? So I'd imagine Matt's probably sitting there going off, thanks for an extra $4 billion to my capital allocation internally. So how are you actually going to offset this ROE drag? Because if I recall, you've always prided yourself on having an ROE differential relative to peers. You've effectively squashed that overnight. So you got to pedal twice as high to return that premium to market.

Ian Mark Narev
Former Executive

The number one thing you'll recall over -- and I can speak at least over the last 4 years for this very reason we have never given an ROE target. So I think the first time I sat here I was asked what is your ROE target, and my answer is we don't have an ROE target and you've got to play to the conditions. However, what we have said is that the ROE relativity to our peers has been an important part of why we think the Commonwealth Bank's done well. Now everyone's going to make their own capital decisions.

It's up to other banks to decide if they've got enough capital or not enough capital. Do we think that it is likely, given we're taking on extra $5 billion of capital, that the ROE will come down a bit? Sure we do. And some of the pro forma numbers are in the book. Do we think that, in light of the new conditions in the industry, we can still continue the outperformance that's made the business perform well? Well, that's absolutely what we're here to do. So the absolute number is going to be impacted by the capital but our ability to deploy it successfully and certainly an management aspiration more successfully than others remains as strong as it's ever been.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Was there any thoughts of high capital requirements going forward behind the decision recently to change the repricing on the investor book. And is that something that you think will increasingly be considered going forward?

Ian Mark Narev
Former Executive

I mean and we've said in the outlook overall credit quality of the sector has been good, but the banking sector and the regulators, the banking sector looked at the overall activity and said investor loans is something we as a sector have got to be more cautious about. When we were -- when Matt and his team were thinking about this for quite some period of time as they saw this coming, they've been saying the good news for Commonwealth Bank was for the reasons that you can see in here we were under the 10%. But the other fact that you have to take into account is when others are taking actions, there's just a flow effect of extra activity. And you've got to be very careful that even without changing your own settings, you don't suddenly get to a point where just by the virtue of others doing less, you exceed the 10% barrier. And the pricing was a direct response to that risk, and that's why we've made the decision.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

But surely that can be achieved with all the kind of whiz bang systems, surely that can be achieved on the front book, more selective pricing of the customers that you do want to attract lowering the OVRs. I don't understand the connection between the heightened risk outlook and repricing of the back book.

Ian Mark Narev
Former Executive

It can be achieved in a number of ways, but one of the interesting things you can see as you get under the numbers of investor loans is the number of investors who have got multiple loans. I think they were numbers released or commented by the reserve bank or somebody. These are big numbers. And often the people taking out investor Home Loans are people who already have investor Home Loans. So actually the impact of the repricing of the back book has a direct effect on that. There are all sorts of ways that you can or can't respond to this, but for us this was the right way.

Unknown Executive

We'll move to the phones now, and we have Brian Johnson on the line.

Brian D. Johnson
CLSA Limited, Research Division

Have 2 questions. The first one, just Slide 29, we can see that the CLF is actually coming down. Does this impose a constraint on growth and should we expect it to continue to decline each year by about the same quantum? My second question is that if I have a look at the mortgage slides at the back, I note that the low deposit premium disclosure has disappeared as has the low doc. But we can also see that, basically, in RBS, the mortgaging position's number looks to be flat. But when we have a look at the Australian book overall, it is up. Does that imply that the mortgaging position number is actually materially up for Bankwest?

Ian Mark Narev
Former Executive

No, but let me first let Matt talk to you about the mortgage numbers and then we'll go to David Tupelo [ph] on the liquidity number.

Matthew Comyn
CEO, MD & Executive Director

Brian. So low doc is unchanged. I think in the first half obviously it was 0.1%. In terms of stock of LDP, which we disclosed -- we've never disclosed flow, I think it was 7% for the half, it remains at 7% for the full year. I think the only reason we took it out is actually harmonized to get a Australian banking portfolio. And it's not relevant for Bankwest, which is why it's not there.

Brian D. Johnson
CLSA Limited, Research Division

Okay. And the low doc if I remember I thought it was 1.2% of the book?

Matthew Comyn
CEO, MD & Executive Director

No stock is about 6% and it's increased to 7%. I think it was 6% at June 14 and then you got 7%, it was 7% at the half, it remains at 7%.

Brian D. Johnson
CLSA Limited, Research Division

And then the second leg of it, the difference between the RBS numbers and the Australian numbers?

David Paul Craig

Well, Bankwest.

Matthew Comyn
CEO, MD & Executive Director

I don't have the Bankwest numbers. I can certainly say the retail bank numbers are not up. I don't believe the mortgaging positions are up materially at all from a Bankwest perspective.

Brian D. Johnson
CLSA Limited, Research Division

And what's the explanation for the difference between Slide 111 and 110?

David Paul Craig

Well, one of the slides is consolidated with Bankwest and one is not. So historically, we've only disclosed bank -- retail, and we thought the time had come to incorporate Bankwest in the numbers. And so we're including both slides this time so you can look back and see last time's slide. Going forward, we won't be separately disclosing RBS. Paulo [ph] can you cover the CLF question?

Unknown Executive

Just to cover the CLF point, the CLF requirement is down because when we go through the calculation, we're looking at the potential outflows as well as our investments, our liquidity investments. It's not a constraint on growth. It's down because we have increased the -- we've increased the amounts of term deposits that we have and we've reduced the outflows that we expect from -- in particular, from our retail deposit book. And that's consistent with I think the patterns you've seen around growth in transactional accounts and the stickier deposits. So it's not a constraint on growth.

Unknown Executive

And we'd take another call from -- another caller, Matthew Wilson.

Unknown Analyst

Most of the presentation spoke to the full year-on-year comparisons, which look quite satisfactory. As we look at the second half trends, which is the new information for the market today, most things seem to be heading in the wrong direction. Retail was down, Business Banking was down, [indiscernible] was down, wealth was down. New Zealand and Bankwest were both down. Bad debts are up 25%. And you have to have write-backs in the worst-performing state in the country to get you there. Can you talk more to the half-on-half trends? Have we really seen a change in momentum because I can't recall seeing second half trends so poor.

David Paul Craig

Yes, there are 2 aspects to this. The first one is, as you will recall, we have 3 fewer trading days in the second half than the first half. And so that weighs heavily on net interest income and those sort of aspects. And then the second one, which I tried to explain when we talked about expenses, is the expenses actually on an underlying basis were down 0.6%. So when you allocate that across the business, you will see the profitability on an underlying basis was reasonable. I mean, it's clearly been a time of intense mortgage competition. The impact of repricing that happened both the 5 basis points that went through in May and then the subsequent 27 basis points on investor loans which went through in July, of course, have had a negligible impact on that particular half. So in terms of momentum coming out of this financial year into the next financial year, we think that's pretty strong.

Unknown Analyst

I appreciate the days difference. But if we compare second half this year to second half over the last couple of years, there is a significant change in momentum up there.

David Paul Craig

Well, as I say, when you adjust out these one-offs, it doesn't appear that way to us.

Ian Mark Narev
Former Executive

I think -- if you look at momentum, these things have always got ebbs and flows. I think if you look at the economy in the second half and some aspects in the third quarter and you saw this right through the banking results, we're not as weak. And in the fourth quarter, I've mentioned that you'll start to see more business spending. You'll start to see more retail spending. You got the impact of the mortgage pricing. So the momentum aspect are all swings and roundabouts. I mean I think the numbers on the half are pretty clear. The key point to bear in mind from David's perspective -- as David emphasized, I think, on the expense line is the impact of some of the decisions we took in the second half.

Unknown Analyst

I think one other question if I could. How do you find the right balance between repricing in mortgages to recapture the ROE detriment for more capital and stretching the book because now arrears 90 days, 30 days seem to be tickling up.

Ian Mark Narev
Former Executive

Yes, well, first of all, if you look at home loan arrears, right across the book, they're very stable. Second, even with the investor repricing, Matt, and you'll know about this, you're only putting people back in the basic position there in a couple of months earlier before they got the last cast. And thirdly, you've got servicing criteria, which makes sure they can withstand about 5 or 6 or more rises. So it's a very good question. We think a lot about how to balance mortgage pricing and customer satisfaction in the long term that's very, very important in competition. In other circumstances, we need to be concerned about the link between an extra 27 basis points on mortgages and credit stress but that is not a major factor here at all.

David Paul Craig

I think if you have a look on the bottom left-hand corner of Slide 113, Matt, there's -- it shows you the arrears on the mortgage book for the last 5 years. And you can see that we're really pretty much bumping on the bottom an all-time low on arrears. So and that's obviously a function of very low interest rates. And as Ian said, even with the repricing that's occurred, it's still historic lows. 77% of customers, by the way, are paid in advance, in average 27 months in advance. So it's a pretty strong stable book at the moment.

Unknown Executive

Great. Next question from Brett.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

It's Brett Le Mesurier from APP Securities. Couple of questions. Firstly, on the Home Loan margin, David, you pointed out that there was no growth in the income relating to Home Loans from 2014 to '15, which would imply that the decline in margins is at the order of 12%, wouldn't it, because you've got 2% margin on Home Loans roughly and you got roughly 6% growth in the asset so to get no growth in income that would imply at the order of 12 basis points decline in margin. So it appears if that rate continues, in other words you continue to write at the same level of return that you currently get, that the increase in the margins, which you've put through in the last couple of months, would result in no margin decline in the year in which we're currently in. That would be a fair comment, wouldn't it, such that sitting here in 12 months' time, you would actually be able to report Home Loan income increasing at the same rate as loan growth. That's a fair comment?

David Paul Craig

Not quite. I'll ask Matt Comyn to answer that question.

Matthew Comyn
CEO, MD & Executive Director

Brett, so with -- I guess without giving you forward-looking guidance, I'd make 2 comments about margin for the half in particular. One is on the asset pricing perspective, which I guess is well documented and we've covered in some of the repricing more recently. I think the other piece which David called out which has had a reasonably significant impact is actually asset funding specifically the basis risk premium which is the switching between OIS and BBSW. That was larger in the half. So it's harder for you then to extrapolate out what the margin will be going forward.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

Is the a 3-year repricing such that, that decline in margin is almost eroded so that the, where you're currently writing is getting quite close to the average of your book?

Matthew Comyn
CEO, MD & Executive Director

As I'm sure you'll appreciate, it's very hard for us to make any comment around pricing.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

No, I mean, I'm not talking about changing your pricing. I'm saying whatever it was continuing at the level that you had for this year, is the gap between the average of the book and what you're writing at this year almost at an end?

Matthew Comyn
CEO, MD & Executive Director

So there's -- I mean, at the highest level, there's a couple of dynamics. One, there's an interest rate cut in February, right, which had an impact on margin. May, there was some repricing effect, it was more recently rate pricing. In August -- May and August virtually 0 impact. I think what we've seen in the market more generally is a stabilization in terms of flow level of discounting, which is because there's far less discounting in the investor side of the books than there was certainly 6 months ago and even 3 months ago. And so it's really going to depend on what level of competition plays out in owner-occupied, which I think is reasonable to anticipate there will be heightened levels of competition there.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

Just a question on Wealth Management. That's all right, Matt, you can step. A question on wealth management, the -- you highlighted the customer remediation costs and when we look at the disclosure that you've put in the announcement on Wealth Management, should we conclude that the increase -- that abnormally large increase that you show for Colonial First State in expenses, both volume expenses and operating expenses, is almost entirely due to that factor?

Ian Mark Narev
Former Executive

Not almost entirely, but it's clearly a significant factor. And bearing in mind that as David has said, the way we approach these issues is where we've got project costs that we can see ongoing, we recognize them as soon as we know what they're going to be.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

And does it include a provision for the future or...

Ian Mark Narev
Former Executive

Yes.

David Paul Craig

Yes, absolutely.

Brett Le Mesurier
Asia Pacific Prudential Securities Pty Ltd., Research Division

So we should expect to see a drop-off in the current financial year.

David Paul Craig

That's exactly, right.

Unknown Executive

We've received a web question from Richard Wiles at Morgan Stanley. His first question is on Slide 34 other banking income, what were the gains on sale that drove the increase in other income from about $200 million in the first half to $350 million in the second half? And his second question is around costs. So costs were up 7% in the second half. How much of the $350 million of compliance regulation program costs were in the second half and how much of the $150 million in the nonrecurring portion were in the second half?

Ian Mark Narev
Former Executive

Well, on the second point, firstly -- and David, you can take the other one. I mean on Slide 39, you can see there's the underlying expense growth in the second half as defined by what we think would recur is that the expenses were down about 0.6%. So what that tells you in terms of how you extrapolate back from the second half expense number is because we go through this process particularly year end of saying what do we think these things are going to cost and let's take all the costs now that, that's a significant factor in the second half expense result.

David Paul Craig

Yes so the majority -- by far the majority of the nonrecurring compliance and the FX was in the second half. In terms of the question of...

Unknown Executive

So the other banking income, the gains on sale that drove the increase in other income from $200 million in the first half to $350 million in the second half.

David Paul Craig

Yes, I'm not quite sure where those numbers come from. I think -- unfortunately, Richard, I can't answer the question. But I'm not quite sure where he's getting those numbers from. I suspect that if he's looking at disclosures in detail and profit and loss there'll be other types of gains on sale in trading income that would be in those numbers and are confusing it. But as I said, there is no individually material gain on sale within other banking income.

Unknown Executive

Andrew Hill.

Andrew Hill
BofA Merrill Lynch, Research Division

Andrew Hill from Merrill Lynch. Just looking at the asset quality disclosure on Page 72 of the result pack. Obviously, the impaired assets going down. But I'm just wondering if you could give a bit of color around the drivers within that, and particularly -- Page 72 of the pack, not the slides. So in terms of gross impaired assets, they're obviously down half on half, but the new increase is up and write-offs and recoveries are up as well. Whereas if you look at the full year picture, it tells you a slightly different story. So I'm just wondering if you can give a bit more color around the drivers of that.

David Paul Craig

I mean, to be honest, this is what you're looking at here is movements in provisions. And it's not a very good view of what's really going on underlying because there's certain net movements. Clearly what happens through a cycle is write-offs increase towards the end of the cycle as we finally write things off, so you provide for them upfront. And then you write them off at the back and then the net movements or otherwise. So the gross impaireds and the movement -- in aggregate movement in gross impaireds is a much more accurate view of what's really happening underneath it.

Andrew Hill
BofA Merrill Lynch, Research Division

Okay. Just checking, there's no seasonality at play in there in those numbers.

David Paul Craig

No, no seasonality at all. These are in -- no, none at all.

Unknown Executive

We'll take the next question from T.S.

T.S. Lim
Bell Potter Securities Limited, Research Division

T.S. from Bell Potter. Question for Ian. Can I get your views on the competition, your views on the disruptors coming in? And do you think CBS IT leadership relative to the other majors is now narrowing?

Ian Mark Narev
Former Executive

I think, look, a, our view on competition is very similar to what's always been, which is the other 3 major banks are well-managed institutions with terrific franchises. And we underrate them at our payroll and I think they consistently show that. Number two, in the next tier of banks, they have been specifically identified by the financial system inquiry as needing competitive support from policy, which they're getting. So we'd be crazy to discount them. And once we've stopped worrying about the major banks for the next year, we can then look at the existential threat posed by technology driven players. So what does all that add up to? From the point of view of the technology advantage going back probably 12, 18 months ago, I think when we first said, we're not going to get involved in the game of which bank has the best technology. What we are going to get involved in the game is showing you what we do with our technology and showing how that impacts on customer satisfaction and business results. And to me, probably the standout feature of the result is that we've got ongoing technology innovation leading to record customer satisfaction levels, leading to revenue growth while we're managing margin. And when you look at what technology is really designed to do from the revenue perspective, it's happening for us. That's A. B, we're doing some things, but the management team here all have a common view, we need to do a lot more actually in linking technology with productivity. But most importantly of all, even if we have this technology advantage however you measure it, it can go in an instant. And the key aspect of this is that the level of innovation, the driver simplicity has just got to keep going. I mean, that's why we often get asked about when is the investment in technology is going to stop, it's not. But what we are doing is building a management team and a culture which is going to enable us to keep these levels of innovation going. And if they can continue to produce results like you can see on this one, we'll be pretty happy.

David Paul Craig

And can I just add to that? Because I think that again, I want to call out the investment spend. And what you saw during the GFC was that we continue to invest where others didn't, and we believe that, that significant investment or out investment that we've made at that stage has underwritten some of the leadership that we've had since then. And we are continuing to invest now again in a tough time. And we think that from our point of view, we're caretakers for the future, and a lot of this investment that we're doing today won't score points necessarily for some years to come, but we think it's critical at this stage of the cycle to continue to invest and particularly with the opportunities that we see out there at the moment.

Unknown Executive

So we have another call or another question from Brian Johnson on the phone. Brian?

Brian D. Johnson
CLSA Limited, Research Division

Two if I may. Just on Slide 45, you say the overlay is 7 55 [ph]. Could we get that broken out between modeling our granularity and what is truly discretionary? And then the second one is the narrative today is the increase in the housing risk weighting is about competition. If we were to go back to November of last year APRA made a speech where they said all of the 4 major banks failed the mortgage stress test. In May, they basically came out and questioned the credit underwriting standards of all 4 of the major banks. By default is that telling us that we should expect a higher capital intensity going forward for those 2 sectors in housing?

Ian Mark Narev
Former Executive

Let me take Part B first, no. I think what APRA's made pretty clear is that there were 2 aspects of the combination of Basel and the financial system inquiry that will lift in their court. Number one explicitly was how to resolve the somewhat broad question of universally recognized -- globally strong, whatever the right term was, and they've done that. And number two was on housing risk weights and they've done that. There's no indication, Brian, anywhere from APRA that I've seen that there's more to do on either of those 2 levels. So certainly nothing that we've read or that's been said to us suggests there's more to come on that.

David Paul Craig

Can I just -- so you know the answer to the overlay, which is we don't break that out. If I can just come back to the mortgage stress test, though, which was actually a general stress test. I think frankly, your headline is pretty inflammatory. APRA didn't say all 4 banks failed the mortgage stress test. What that test was about and it was a normal stress test was if you take no action whatsoever, if you do not raise capital and take no action whatsoever for the entire period of a stress event, which was a 5-year stress event, what do your capital levels come down to and then do you breach your capital? No bank that I'm aware of, certainly CBA, in that test breached their capital at all. And that was with taking no action whatsoever for the entire period of the stress test. Then of course the second phase of the stress test is then what moderating -- what factors would you -- what would you do during the period of the stress test? And of course the answer certainly for CBA is that you can comfortably handle that stress event. So those were the findings. And I do think we've got to be careful with inflammatory statements like yours, Brian.

Brian D. Johnson
CLSA Limited, Research Division

Well, it's said that the advanced banks failed the stress test in the subscript, it's their words.

David Paul Craig

We'll disagree about what this subscript that you refer to is about.

Unknown Executive
Fantastic. Well, I think that draws us to an end. I think we've answered more questions. So thank you for attending, and we'll be speaking to you in the coming days. Thank you.