Question and Answer

Andrew Bowden
Head of Investor Relations

Let's start with James.

James Ellis
BofA Merrill Lynch, Research Division

It's James Ellis from Bank of America. Just a couple of questions. Firstly, in relation to the customer remediation provisions, which have been an ongoing contributor to the pressure on capital. Just to the extent of what you know, how confident do you feel around the adequacy of those provisions?

Brian Charles Hartzer
Former MD, Group CEO & Director

Well, James, we've provided for everything that we know and we can reasonably estimate. That's the short answer. In the sense, it's -- by definition, the unknown unknowns could be out there. This is something we've been working on though for a number of years. You might recall, I talked about get it right, put it right. It's been an initiative we've been running for a number of years. When I look at what we've dealt with this year, we've dealt with financial planning, we've dealt with issues in mortgages, we've dealt with issues in business bank, we've dealt with other issues in smaller [licks] last year or last couple of years. So I feel like we're getting through it. Our focus now is on paying customers back as quickly as we can because the time value money effect is significant, and that will affect what it ultimately ends up being. I guess the wildcard is probably around regulatory actions and whether there are other things that come at us that we need to deal with. But of course, we can never rule out that we might find something else.

James Ellis
BofA Merrill Lynch, Research Division

Just second question around the productivity aspiration. Acknowledging that you have stopped 40%, you have stopped with that target, your peers have got various iterations around absolute cost reduction. Not all of them are clear around the time frame, but deliberately. But can you just talk about, in an environment where there are pressures around revenues, which seem to be getting greater over time not less so, what's the efficacy of having a cost to income ratio target close to an absolute one?

Brian Charles Hartzer
Former MD, Group CEO & Director

Well, James, the way I think about that is we're trying to run the bank for the long term and we're trying to acknowledge with that target, which clearly has a revenue dimension to it. And so that's a bit of a wildcard. But we're trying to give an indication that we know we have to run the bank more efficiently to stay competitive, and that is about the relationship between cost and income. We don't feel that an absolute cost target necessarily leads you to making the right decisions along the way because we're really trying to, say, how do we drive more efficiency in these businesses. And as we grow, we may need to invest more in some areas. So I know it's a bit tricky particularly because in the last couple of years, we've had all the variation on the revenue line. But it's really a way of signaling that efficiency is incredibly important. It's a really important part of our priority, and we're driving that through simplification, automation, digitization. We'll continue to do that. I actually feel -- I know that there's a lot of noise in the result. I actually feel the productivity result this year is a really good one. We've worked really hard on this. And I think the absolute reduction of FTE by 5% a year is indicative of the fact that we're making real progress on this.

Andrew Bowden
Head of Investor Relations

Jarrod?

Jarrod Martin
Crédit Suisse AG, Research Division

Jarrod Martin from Crédit Suisse. Could you give a bit more color on the issues you've had in mortgage business and what has caused the slowdown in growth? I understand there was implementation of new HEM tables that didn't go well. And if I heard you correctly, most of this happened, in fact, in 4Q, and they're being fixed now. Why is it going to take an entire year to get back the system? Why wouldn't system growth come in the second quarter if applications takes sort of 3 months? Why is it going to take a full year to get back to system?

Brian Charles Hartzer
Former MD, Group CEO & Director

Well, Jarrod, I guess we're trying to give an indication of where we're headed. I mean there's a lot of -- we still have to make tradeoffs in terms of volume and margin and the like, and obviously, it's a really competitive market at the moment. The short answer to the delay is the lag effect as applications build up. It takes a while for them to flow in. And we've got work to do in a number of areas. So we feel like that's -- if we can get there faster, we will, but I don't want to be completely focused on volume growth because we still are making margin tradeoffs along the way. But as an indication, I think that's where we're getting. The way you characterize, it's a pretty accurate summary of what happened. We had new HEM tables plus the new HEM tables that we collect data, the expense categories at a more detailed level. And so there was a tool put out to the brokers in particular around how we needed to collect that data. The tool was, frankly, pretty clunky, so we've gone back and reworked that. It's a better experience now. And as I said, we're seeing the applications rise.

Andrew Bowden
Head of Investor Relations

Andrew?

Andrew Lyons
Goldman Sachs Group Inc., Research Division

Andrew Lyons from Goldman. Just 2 questions. Firstly, just on your margin. You've provided some commentary around the exit NIM versus the half NIM. Can you provide any more commentary around how the trajectory trended in October with the rate cut? And then just secondly, your economic profit disclosures highlight you've held on to your 11% cost of capital assumption. Just 2 questions. Have you had any consideration of reducing this given the rate environment? And then secondly, just given one of your domestic peers has been progressively reducing this over the last 12 months, have you seen any noticeable change in the competitive environment, particularly within institutional banking?

Brian Charles Hartzer
Former MD, Group CEO & Director

Why don't you talk about margin, and I'll do the second one?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

We've given what we can in terms of margins. So in particular, I'd highlight the new disclosure on low rate deposits in Australia on the margin slide. One of the challenge, I think, that you could see it in the half's result how volatile the different parts of the margin were, and we're just going to have to see what the first half looks like because we're dealing with movements in market rates, competitive impacts both in lending and deposits. So I wouldn't want to indicate something for October because I just think the whole half will be very different depending on how the industry navigates this future period. But I think we've given a lot of information so that you can hopefully understand the balance sheet piece. So no, I didn't want to add anything on October.

Brian Charles Hartzer
Former MD, Group CEO & Director

And on the cost of capital, this is a bit of an academic debate around what the cost of capital is. To be honest, it's not something we obsess about. Clearly, you would think that lower interest rates would be a contributor to that, but there are other debates. I think the important thing is how we manage the businesses around the allocation of capital to different businesses. We then expect them to make tradeoffs between margin and volume to optimize the value that they can create. We don't -- there's not a direct link in terms of us obsessing about a cost of capital and then how we feel we want to price in the market. It's an input, but there's lots of other things that we think about. And so I don't see it as a fundamental issue in terms of constraining our opportunity. We have -- you referred to WIB. We have prioritized return and managing margins in that business. That has meant some deals haven't met the hurdle, but it's typically not been a line ball issue. Really, we're continuing to back the customers that we believe in and then we think will generate long-term value. So I don't -- it's kind of interesting, this discussion, but I don't see it as a major driver for us in how we actually manage the business.

Andrew Bowden
Head of Investor Relations

Jon?

Jonathan Mott
UBS Investment Bank, Research Division

Jon Mott from UBS. Question on Slide 19, I think, Peter, you gave us quite a bit of detail on the tractor, and I just want to make sure the math is right as a headwind. If you look at and you get the ruler out, the tractor is currently yielding about 195 or 200 basis points; the 3-year swaps, about 75 bps, if that's right. And I think the RBA is saying we're going to be extended to a lower rate environment. Do we then use the capital hedge and the deposit hedge to that $90 billion, and you potentially got 120 basis point headwind over the next 3 years on that tractor rates that will...

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Yes. So that is the right -- so we're giving you the balances on the right-hand side and a pictorial of the right, and we'll have to wait and see what interest rates do and whatnot over time.

Jonathan Mott
UBS Investment Bank, Research Division

Sorry. It's about a $1 billion headwind over 3 years if rates stay at current levels.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Well, I'll let you do the modeling. That assumes an interest rate in the future, and we'll have to wait and see...

Jonathan Mott
UBS Investment Bank, Research Division

I think you said offsetting that, you had some flexibility on liquidity. What are you trying -- are you alluding you could release some liquidity to help you in NIM...

Peter Francis King
CEO, Acting MD of Westpac Group & Director

I'll just point out that we ended up a little bit more liquid at the end of the year, so we can time our wholesale funding in the next year.

Jonathan Mott

UBS Investment Bank, Research Division

And quick follow-up question. The interest rate risk in the banking book has fallen from 13 billion as a risk weighted asset to 500, and I think you said that embedded gains as rates have fallen. Can that go negative?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

No, I don't think so.

Andrew Bowden
Head of Investor Relations

No. The standard doesn't much go negative. It can go to 0, but not any lower.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

So I think it's hit 0 three times. This is the third time it's hit 0 in the last decade.

Andrew Bowden
Head of Investor Relations

Brian?

Brian D. Johnson
Jefferies LLC, Research Division

Brian Johnson, Jefferies. Two questions, if I may. And Brian, I suspect you'll try and dodge the first one, so I'd like to put a little bit of context in it. 2009, ANZ came out and did a capital raising that was underwritten. Also, more or less announced the big profit miss, share price fell, there was a shortfall. When we spoke to them on the evening, there was no discussion as to whether there's a shortfall. In fact, we were told the other way around. Could we get some -- could you tell us what is the protocol if the underwriters are left with a shortfall? Because I think it's something the market deserves to know. And then the second one is that when we have a look at the replicating portfolio, it seems to me that you're progressively becoming more unhedged as basically interest rates fall because that balance of interest rate and sensitive deposits goes up as rates actually fall. Do you need to top up the size of the tractor?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

I'm happy to take that.

Brian Charles Hartzer
Former MD, Group CEO & Director

Okay.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Brian, on the capital deal, we will make appropriate announcements. So I'll just leave it at that.

Brian D. Johnson
Jefferies LLC, Research Division

ANZ's disclosures are proper?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

I'm not going to comment on ANZ. On how we manage margins in a low rate environment, the concept behind the deposit hedge is you hedge in determinant 0 rate deposits. And for the rest of the deposit book, you're managing that against your assets. So that's how we think about it. Whether it makes sense or not to hit -- to lengthen the duration of the deposits, we'll increase the hedging, I'm not sure. And we'll more manage that through the asset liability mix than specifically hedging it.

Andrew Bowden
Head of Investor Relations

Victor?

Victor German
Macquarie Research

Victor German from Macquarie. If I just can follow up on costs and ROE. So in terms of costs, you're effectively telling us that you've got around $700 million of cost saves in the period, yet, effectively, it implies that the underlying cost growth is in the order of $800 million. There's $450 million or so explained by some of the drivers that you've highlighted. Is the rest simply inflation? And as we move into the following year, do you see a scenario where you can actually keep costs flat or reduce them? Because it sort of feels like every half, there is something extra that we find out that you need to spend on.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

So tell you, I haven't redone your calculations. But in terms of sort of the BAU cost growth, if you like, the one thing that I'd highlight is the new accounting standard change on credit cards. So remember that AASB 15 thing, that sees cost growth a bit impacted by what's happening in the cards portfolio on spends. That's some of that impact, and then the rest is really sort of activity and inflation. In relation to '20, I'm not going to go out that far because we've been pretty clear on what we're targeting for 2020.

Victor German
Macquarie Research

Maybe just to follow up on ROE question. Brian, obviously in the past, you've talked about ROE targets that you're trying to achieve. I've noticed today, you've announced 10x or 10 times, I don't know, whatever...

Brian Charles Hartzer
Former MD, Group CEO & Director

10x.

Victor German
Macquarie Research

10x, the partnership is, which is an interesting step for a very large incumbent to be looking to offer banking services. Just interested in your observation, how do you sort of look at the landscape of next 3 years? Do you see yourself as someone that in sort of a defensive position who needs to offer these sort of things for the fintech players to sort of thrive? And what does it do to longer-term ROEs for the industry?

Brian Charles Hartzer
Former MD, Group CEO & Director

I guess you can see it either as defensive or offensive. I mean it depends -- the way I think about it is if big banks like us did nothing, then there would be a vulnerability. But our strategy has been to get on the front foot about this stuff and see it as an opportunity that customers needs the way they want to bank is changing, the technology is creating new ways to deliver services. And we, for quite a number of years now, have viewed that as an opportunity and have been investing for that. The 10x opportunity is taking advantage of some new technology that's come along that's really globally leading, and we've built a good relationship with them. It's opened up some new opportunities for us to grow through partnerships and potentially through the creation of some new services. I don't want to go into too much detail about that at this point, but we're pretty excited about a new avenue that it opens up for us.

Andrew Bowden
Head of Investor Relations

Richard?

Richard E. Wiles
Morgan Stanley, Research Division

Richard Wiles, Morgan Stanley. Brian, I'd like to ask you some -- for some further comments on what you're thinking about with the dividend. Your outlook commentary implies that your average volumes will be flat next year. Your margins will probably be down, your noninterest income will be down and your costs will be up. So there's a challenging earnings environment facing you in 2020. And that could mean the dividend, if you hold the dividend at $0.80 per half next year, the payout ratio might well go above that 70% to 75% target range. So a couple of questions, did the Board consider what the FY '20 payout ratio could be when it cut the dividend to $0.80 this year? And what have you taken into account in terms of credit quality and sustainable levels of loan losses in setting that dividend?

Brian Charles Hartzer
Former MD, Group CEO & Director

Richard, I can't provide any guidance on what we're going to do over the next little while. I mean you'll obviously come to your own conclusions. I can say we certainly have considered carefully the level that we've changed the dividend to and feel comfortable with the decision that we've made at this point in time. And on credit, as I've said and I think Peter said as well, we feel that the book is in pretty good shape. With low interest rates, we continue to feel pretty good about the quality of the credit book, although it is probably about as low as it's going to be although we've been saying that for a while. But given where we're at with the capital is and the like, there's not much more I can say, I'm afraid.

Andrew Bowden
Head of Investor Relations

We'll take a call from the phone. Matthew Wilson, please, from Evans?

Matthew Wilson
Evans & Partners Pty. Ltd., Research Division

Matt Wilson, Evans & Partners. Just to further add to Richard's good comments on the dividend, what does the industry get in front of this issue and reset properly? It's pretty clear given the early comments you've made today that the dividend will again be under pressure in 2020.

And then secondly, a detailed question on Slide 25, properties in possession excluding WA and Queensland has jumped 30% in the half. Could you add some color to that movement, please?

Brian Charles Hartzer
Former MD, Group CEO & Director

I might do the second one, and then you want to go on the first one? On the second one, Matthew, the properties in possession number is up, but it is still a very, very small number. We're talking about fewer than 600 properties in possession on a mortgage book of well over -- I think it's about 1.2 million home loans. So these are very small movements in the scheme of things, and it really represents that it's taking a bit longer for people to clear properties in a slower moving housing market. So it's not anything that we're unduly concerned about.

Matthew Wilson
Evans & Partners Pty. Ltd., Research Division

Is there a state that stands out? Or...

Brian Charles Hartzer
Former MD, Group CEO & Director

We saw a bit more of an increase in Queensland. WA has continued to be a bit of an issue. But honestly, it's -- the numbers are pretty small in the scheme of things.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

And then, Matt, on your observation about next year, I'll just reiterate what Brian said, it's -- we've said what we can or we want to on the outlook. We're not providing detailed guidance on 2020, and the dividend decision is always one that you make based on what you can see at this time. And I think Brian set up pretty well how we thought about that at this time.

Matthew Wilson
Evans & Partners Pty. Ltd., Research Division

Okay. We will have a new chairman next year. Is that correct?

Brian Charles Hartzer
Former MD, Group CEO & Director

I don't think that's something that we've said at this stage.

Andrew Bowden
Head of Investor Relations

There's been no announcement on anything, any change.

Andrew Triggs?

Andrew Triggs
JP Morgan Chase & Co, Research Division

It's Andrew Triggs from JPMorgan. Two questions, please. Firstly on the term deposit portfolio. I'm just interested, I think I saw in the chart the average cost above the benchmark still rises. Just interested in your observations on the pricing environment and the term deposit book.

And then the second question, just to follow up again on dividend. I'm just interested to what extent the franking balance had a say in the sort of the setting of the dividend policy generally.

Brian Charles Hartzer
Former MD, Group CEO & Director

Short answer is it is still a very competitive market on term deposits as we've seen, and that's what that outcome reflects. And then yes, franking and the large franking balances, as I said in my talk, something that we consider very carefully, more conscious that the franking credits have value to shareholders that -- not value to us, and so we'd like to distribute them.

Andrew Bowden
Head of Investor Relations

I'll take a call from the phone again, please. Brendan Sproules?

Brendan Sproules
Citigroup Inc, Research Division

Look, I've just got a question on your cost guidance on Slide 29. When you announced the wealth restructure, you said there was one-off impacts, which you've talked about here today between $250 million, $300 million, you said that comes in the low end. You also talked about the ongoing impacts. Then back in March, you said that, that business in 2018 had operating cost of $260 million, and you said that most of those costs you expect it to be eliminated in FY '20. And secondly, the divisional restructure at the time, which is another $20 million, which you thought would start benefiting for FY '20, I was just wondering where that second component sit within your guidance.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Yes. Brendan, the $200 million that we're calling out for wealth reset is the majority of that $280 million that you referred to. We got a little bit this year, and there's probably a tiny bit left for the third year.

Brendan Sproules
Citigroup Inc, Research Division

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So the one-off impact is on top of that because they're not going to repeat?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

The one-off impact is in notables, which we haven't included in -- the FY '20 point is excluding notables.

Andrew Bowden
Head of Investor Relations

I'll take a question from Azib Khan on from Morgans on the phone.

Azib Khan
Morgans Financial Limited, Research Division

Andrew, can you hear me?

Andrew Bowden
Head of Investor Relations

Yes. You're right.

Azib Khan
Morgans Financial Limited, Research Division

So Brian, you've said that you're expecting system housing growth to lift from 3.1 to 3.5, but you think business credit growth will slow from 3.3 to 3. What do you see is driving the slowdown in business credit growth? Will it be more SME or the larger end of business lending?

Second question is are you now pretty much done with the RWA optimization in your institutional business? Or is there more to come on that front?

And the third question is can you please tell us what the magnitude of the investment is in 10x and what percentage shareholding this gives you on 10x?

Brian Charles Hartzer
Former MD, Group CEO & Director

I'll do those in reverse order. So no, I can't tell you. We're not disclosing that at this point in time. The RWAs on WIB, I think, is largely done.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Yes. Azib, I just say, the -- from here, RWA is really about restructuring of customer facilities, which you just do every time you roll a deal. It's not modeling or that type of thing.

Brian Charles Hartzer
Former MD, Group CEO & Director

And then on the system growth, there's not a huge amount of insight there. I would say it's reasonably well spread. The commercial credit demand has just been relatively weak, and that's partly been people paying down debt and probably been just a lack of business confidence to make further investments.

Andrew Bowden
Head of Investor Relations

Okay. I'll take a call from Brett Le Mesurier on the phone.

Brett Le Mesurier
Shaw and Partners Limited, Research Division

So firstly, we heard from ANZ that they were thinking about reducing their return hurdle on the institutional bank. I noticed you're using 11%. Do you have any plans to review any of your return hurdle?

Brian Charles Hartzer
Former MD, Group CEO & Director

Brett, we don't think of it in quite -- such a black and white way. We think about how we allocate capital across our different businesses and ask the businesses to then target generating as much value as they can, and that involves making tradeoffs between margin and volume. So no, we don't have a plan to make a fundamental change there, but equally, that's -- it's only one input into how we think about pricing deals.

Brett Le Mesurier
Shaw and Partners Limited, Research Division

The second question I had was you referred to -- in FY '20, you expect $100 million less income from wealth management, that's excluding the financial planning business, but there's a $50 million decline. To what extent are you confident that that's the end of the decline in revenue from that business?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Well, Brett, I think the -- just giving you a bit of insight into that particular drivers, it's things like the legislative change for Protect Your Super, lower interest rates that impact the returns out of the platforms, migrating some of our Super activity into lower spread products and then the repricing of BT Open flowing through. So they're the drivers. We can never work -- legislative change is not in our control as is cash rates will go wherever they go. So we'll just have to see.

Brett Le Mesurier
Shaw and Partners Limited, Research Division

The insurance income is declining. I've noticed that you've got increases in claims rate. You've also referred obviously to lapse rate having a significant incline. To what extent are you confident that the claims experience has stabilized?

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Well, I think that's something for you to decide. I can't predict storms into the future, unfortunately.

Brett Le Mesurier
Shaw and Partners Limited, Research Division

No, I'm actually referring to life insurance.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

Again, we haven't given any detailed guidance on claims in life insurance. So we've set out the historical trends in the report, and I'd refer to those.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Ed Henning from CLSA. Just a follow-up on growth and costs. Firstly on growth in business and you just -- you talked about the competitive environment you saw up here. Obviously, we talked about before around cost of capital. Do you anticipate -- and with your margin management, do you anticipate to be a [below] system in business and in scope at least in the next year? And then just again on costs, you talked about higher spending in '21 and the fall thereafter. Does that mean absolute cost up in '21 and down in '22?

Brian Charles Hartzer
Former MD, Group CEO & Director

I'll do the first bit, and you can do the cost bit. I think I'd separate the business division and WIB, WIB growth tends to really be a function of the transactions in the market, and the mix of customers that are doing things. And we've got a great customer franchise, and we're happy to support transactions from good customers and the returns are still pretty good on our portfolio and relationship basis. So I think what happens there will be a function of what our customers choose to do.

On the business side, I think we're very well positioned. We're #2 in market share and have a great distribution capability across all of our brands and segments. We've got leading customer advocacy in each segment of business, so I think we will continue to do very well there. And if growth comes back, I expect we'll benefit from that.

Peter Francis King
CEO, Acting MD of Westpac Group & Director

And then on the cost question, I'll just go back to what I've said. So we indicated 1% for '20, and then we expect reg and compliance costs to stay elevated into '21 before reducing.

Andrew Bowden
Head of Investor Relations
Okay. With that -- if you don't have other questions, so we'll call it a close. Thank you very much, and good morning.