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National Australia Bank Limited ASX:NAB

Company Conference Presentation

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Table of Contents

Call Participants

EXECUTIVES

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ANALYSTS

Zafar Aziz

Presentation

Zafar Aziz

My name is Zafar Aziz, Head of DR Market Solutions at Deutsche Bank's Depository Receipts Team. I'm pleased to note that our next presentation will be from National Australia Bank.

Before I introduce the speaker, a couple of points to note. Please remember that after the presentation, don't log out. You will automatically be transferred to the National Australia Bank booth where you can find contact details for company representative for questions and access additional investor material. On a final note, all of today's presentations will be recorded and will be available at the Deutsche Bank website, adr.db.com.

At this point, I'm very pleased to welcome Ross Brown, Executive General Manager, Investor Relations, from National Australia Bank. Over to you, Ross.

Ross Brown

Hello, and welcome to the National Australia Bank Investor Presentation. My name is Ross Brown. I'm Head of Investor Relations for National Australia Bank, and thank you for joining me today. I just want to talk briefly a little bit about who we are, and if we look at the -- this particular slide, it's a very brief overview of our corporate profile. You'll see we're one of the largest banks in the world. We have 12.7 million customers globally, predominantly within in Australia and New Zealand. We have about 42,000 staff, 1,700 branches, a little over 0.5 million shareholders. You can see in the bottom 2 charts on this slide that our earnings and assets are predominantly within Australia and New Zealand, and around 74% of our earnings are from Australia, around 10% from New Zealand, and the rest is either in the U.K. or U.S., Asia.

The sort of activities we conduct pretty traditional banking activities, range of banking products, retail and business, institutional customers. We have wealth management products, and we also have operations, if it's here in the U.K. We operate under the Clydesdale Bank and Yorkshire Bank brands, and we have a small U.S. bank called Great Western Bank.

Now just got a few key financial metrics here. Obviously, there's a lot more financial detail that I could talk to. You'll find all of that from our last set of results for the year, the 30 September, 2014, on our website. These -- I want to talk to these numbers in great detail. The things I'd highlight are that we are one of the few AAA rated banks in the world. You'll also see a description here of cash earnings. Cash earnings is uniquely, I think, Australian concept, particularly for the major banks in Australia that was adopted from years ago. It is relatively similar to the statutory earnings. It does exclude a few items, which I consider to be more in the accounting noise category, but a full description of what those items are is available on our website.

Now -- well, we wouldn't be a bank if I wasn't talking to about some of the balance sheet metrics that are pretty important. And on this particular slide, our Basel III capital ratios are described. In Australia, we're regulated by APRA, so our capital ratios are described a little bit differently. And you can see here a common equity Tier 1 ratio, our Tier 1 ratio. And our total capital ratios range from 8.63% for common equity. That varies. That's a slightly different metric to what you would see if we're reporting on an internationally comparable basis, in other words, on a Basel III basis. When we make those adjustments, our common equity Tier 1 ratio would rise from 8.63% to 11.58%.

In terms of funding, we use a metric called a stable funding mix to discuss our funding position, and you can see that in that bottom-left chart, we have around 90% of our funding is stable, and by that, it means, of all our lending book, 70% of it is funded with deposits; 20% of it is funded with term wholesale funding of more than 1 year; and the remaining 10% is funded either with equity or short-term wholesale funding. You can see that those have been an improving trend over the last few years.

And on the bottom right-hand chart, you will see our asset quality metrics. The one that we focus on is the 90-day past due plus EMT [ph] assets ratio. It's the same to gross loans and acceptances. You can see it's been a pretty pleasing trend, and that ratio has been outstanding at 0.88%.

I just want to talk a little bit more around about our strategy, and this slide really is a summation of what we're trying to achieve in the short to medium term and a particular focus for 2015. We're very much focused on a strong Australia and New Zealand franchise. And the underpinning to that, first and foremost, of their customer experience, and we're trying to deliver that by fixing a few pain points and making the digital experience for our customers better. We also are prioritizing the areas where we want to invest in Australia and New Zealand, and that is predominantly around the small to medium enterprise customers, our specialized business customers, the one such as agribusiness or health customers or our home loan customers.

Culture. Obviously important in any large organization, very much focused on accountability, performance and delivery. Underpinning that, the usual essentials in any bank, the balance sheet risk and technology. But also, what is more unique to us, we have some low-returning assets, which we are looking to accelerate the exit of. Hopefully, that'll come together in terms of better shareholder returns. And one of the key metrics that we are looking at is closing the return on equity gap we have with our peers in Australia.

Now just drilling down a little bit more into the returns piece. This is a summation of some key ROE metrics. And you can see our group ROE's 11.8%, but there were a number of lumpy items, what we call, specified items in the last result relating to the U.K. conduct charges, predominantly. When we stripped in our ROE, 14% -- 15.2%, but you can see within Australia banking, New Zealand and our wealth business the ROEs are at 17.2%. And it's our offshore assets, which are somewhat of a drag on ROE at 6.6%. We've got around 17% of that capital deployed in those other offshore areas with a fairly lower ROE. Now that's one of the key reasons -- one of our focuses for this year is to exit both positions to improve the overall ROE position.

Now just drilling down into those legacy asset positions. So we have 6.6% ROE businesses represent 4 key things for us. It's U.K. Bank, which I mentioned before as Clydesdale and Yorkshire Banks; U.K., Commercial Real Estate portfolio, which was placed in runoff about 3 years ago; our Great Western Bank, which is a Midwest U.S. bank; and the SGA assets, which -- with some runoff portfolios post the global financial crisis. Yes, we're making pretty good progress on exiting all those assets, change in the U.K. Banking, which is the largest one. We've restructured that business. The returns are improving. But we had said that we are looking to exit that business, and we are looking at a variety of options, including public markets.

Our full ROE portfolio in the U.K. has run down significantly. We ran off about GBP 3.4 billion to date. We have GBP 2.2 billion remaining. And following the portfolio of sale in December, that number has now fallen to GBP 800 million and for example, now the nonperforming [ph] portfolio. Great Western Bank, we IPO-ed 31.8% of that business late last year, and then we'll change to IPO the remainder over time. And the SGA assets, though, that portfolio of various assets post the GFC, we've already ran off 22 billion of risk-weighted assets with 4.1 billion left. And again, we're looking to accelerate the exit of the remainder of that.

Now turning to a little bit more to the core Australia franchise, and this chart with the bubbles really tries to explain why our focus is around the mortgage customers and our SME-specialized business customers. The bubbles represent -- the size represents the relative revenue contribution to net. And you can see, looking at the various axises [ph] on market attractiveness, which is effectively a proxy for ROE in a relative strategic position, which is a market share-type proxy, you can see that the businesses that are most important, they're in the right top part of the quadrant are our consumer businesses and our small business portfolios. The institutional and corporate ones are a little bit less attractive, and that's why our focus is very much on these priority segments [ph] it’s small to medium enterprise lending and mortgage lending in Australia.

Now in terms of what that means, Business Banking for us is a clear strength. We have the largest Business Bank out in Australia. We have 228 dedicated Business Banking centers on top of our normal branch network that's well ahead of competition. We have a little over 4,000 business bankers that includes 600 specialist agribankers. And we have a reputation within Australia for standing by our customers, and easy to say but a proof point of that was the -- just after the global financial crisis started in 2008, '09, we continue to be a lender to our customers, and we increased our market share in business in Australia by around 300 basis points.

You can see in the top-right chart, our relative market share position in Australia in those various segments in the small to medium enterprise lending. Micro, small, medium, we had between 20% and 29% share well ahead of our nearest competition, which is the other 3 major banks in Australia. And within the agri space, we are a very large player with 30% market share and it's those whose specialization such as agri, health, government and education where we have, we think, real competitive advantage in providing a much more insight to our customers.

The other aspect I'll tell you around our Business Banking performance would be reduction in risk profile, and the bottom-right chart just shows the proportion of Commercial Real Estate. We have the gross loans and acceptances in Australia, and we've been running that down over time, and obviously, we think that's a prudent thing to do.

Now how are we going to grow our Business Banking franchise? We have a bigger focus on adding to frontline business bankers related to 100. We're also adding mobile bankers, product sales specialists. We've tightened up some of our sales disciplines, and in aggregate, we're spending more than $40 million to improve the performance of that business. We've also invested in our new fulfillment model. That effectively means taking a lot of the banking and processing that business bankers do, such as documentation, consolidating that into 7 regional fulfillment centers. There have been some disruptions with the rollout of that, but we're well progressed in addressing that, and hopefully, the benefit of more time for our bankers in front of customers will come through over the next little while.

Technology is obviously a big part of any bank. We've got 3 big technology initiatives as described on this slide. One is NAB Connect. That's our Internet and mobile banking platform. We got a significant upgrade last year, which is providing some much better capability for our customers. NAB View. That gives our business bankers a genuine single-customer view of all the products that our customers hold. We're in the process of rolling that out to our business bankers, and we've seen some early signs of better sales conversations they are having with those customers. And finally, NAB Now. That's really a payments capability platform, a mobile payments capability platform for our small business customers, and now we're going to make and process the payment side of any of the business transactions in real-time online.

Now the other part of our business in Australia, which is the large Business Bank there also, a very sizable retail lender, which we call our Personal Bank, of which home lending is the dominant product. And we've also got credit cards, deposits and personal loans, but you can see on the top-left chart how many market shares have improved significantly over the last 5 years within agri, around 15.6% share in Australia. The returns in this segment are quite attractive, and it's an area where we continue to invest. A lot of our growth has come from better penetration of the mortgage broker channel in Australia. The mortgage brokers account for between 40% to 50% of all new mortgage flows. We've had some investment in that space. We've rolled out a One [ph] label product for mortgage brokers, which has been relatively successful. We're also investing in our own digital and direct [indiscernible] capability. So they're all being important factors in driving our consistent growth, and we're hopeful that we'll continue with these initiatives.

We also have a few key housing portfolio metrics there, given how many portfolio represents just under 60% of our total gross loans and acceptances, It's obviously a very large segment. And for the Australian housing portfolio, you can see around 64% of our customers are in advance of their monthly repayments. The average number of payments that are in advance is around 14, just under 14 monthly payments in advance. And in terms of the loan-to-value ratio, that mortgage book, the dynamic LVR, which includes current property process around 45% and other origination at around 75% of all the -- a little over 75% of all the loans that we originate had about [indiscernible] 80% or more than, so I think we're relatively prudent.

Now turning to our wealth business. So this is our wealth management business where we do insurance, life insurance lending for the life insurance sales, also superannuation products, which is a pension product, effectively asset management products. That's a business which has had some issues in recent past predominantly around fairly different claims environment in insurance. But the more recent earnings of that actually show the improvement of 13%. We've seen better pricing within the insurance business towards better claims management and retention and also try to really improve the cross-sell into our banking customer base of the various insurance and wealth products. And you can see in the bottom-left chart, sales through bank channels have been steadily improving. And on the top-right chart, super sales, superannuation sales or pension sales to our business customers have also been growing rapidly. Now while getting better returns and better earnings out of our wealth business, the return on equity is still below cost of capital, and a large part of that reason is the regulatory capital treatment we have in the bank owner of the wealth business. Now while we're committed to distributing wealth products, we are evaluating a number of options to improve the overall returns of that business.

Now the U.K. is obviously another business I referred to earlier on, and that was one of the businesses we're looking to exit. And I mentioned we're evaluating a number of options, including public markets. We've done a lot a work to improve the performance of that business and what has been, for those who follow the U.K. economy, a fairly difficult time in the U.K. and for the U.K. banks. There's been a number of issues, particularly around just a weaker economic growth but also combat in selling charges for the industry. We're pretty well positioned, we think, for growth over the medium term. We've got some very strong regional brands in Scotland, which is our Clydesdale brand, the Yorkshire Bank brand, which is also in Yorkshire in North England. But you can see in the top right what our market share positions are in those local markets, which equates to around 2% of the total U.K. market for mortgages and about 4% for SME lending.

We've been getting good growth within our mortgage business in the U.K., well above [indiscernible] utilization of the broker channel. While we do business lending, both SME and corporate, we're attaining to take away from the corporate lending, which has got lower returns, which focus more on the SME customer base, and we're obviously looking at some efficiency opportunities to migrate from that space to get to your customer directions.

Bottom-left chart just shows you where we see some growth potential in ROE in the U.K. 6.2% was the rough annualized number for the second half, but front book mortgage ROEs are around 14%, so hence our focus on mortgage lending. And in the bottom-right chart, you can see the benefits that have come from restructuring that business. We stripped out the Commercial Real Estate portfolio about 2 or 3 years ago, so the loan book now has sort of been 23% made out of Commercial Real Estate, which is 1%; and mortgages have gone from 37% of the loan book to 67%.

Now that sort of wraps up all I really want to say today. I think I'll just finish with the, I guess, the summary slide that was earlier around what our focus is for 2015. Big focus on improving our Australian dealer franchise. Again, that's around the customer experience dealing to various customer pain points, investment in digital to make the customer experience a little bit easier; very much focusing on our competitive advantage we have in SME, the specialized business customer segments such as agri and health; and also home lending customers are a big part of what we're trying to grow in Australia.

Culture. Again, it's important where you see how we started the middle of last year. We're very much focused on accountability, performance and being able to execute. And one part of that clearly is making sure we want within the NAB has a genuine passion for customers.

That's the Australia and New Zealand piece. The other aspect to that is, as I mentioned earlier, just running off those low-returning assets that account for that 17% of our capital would generate just a 6.6% return on equity. I've outlined where we are on those key components, and obviously, we're hoping to make progress over the next 12 months. And the aim for us is really to improve the shareholder returns by closing the ROE gap we have to our major bank peers in Australia. We have the lowest ROE, and we obviously want to be able to close that gap to the ANZ Commonwealth Bank and West Bank.
That pretty much wraps up all I had to say today. I really appreciate your interest, and hopefully, you've -- you're still on the line and you've been able to follow what I had to say. We obviously have a lot more

information on our website, details, financials are on much larger slide deck which kind of results in detail, a whole lot more information that I really don't have time to discuss today. But if you do have any questions, please feel free to email me, and thank you very much for listening today. Bye for now.