Question and Answer

Nick Harris
Morgans Financial Limited, Research Division

Nick Harris from RBS Morgans here. Just a question, there's been some talk for a while about some systemically important banks, the major banks, potentially having to hold some more capital. Does that help you guys longer term as you sort of remove some of the funding -- sorry, balances some of the funding disadvantage you've had because you'll be able to hold a lower level of equity?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

I think it's still pretty much in the discussion area at the moment. I mean, we're holding a reasonable degree of equity at the moment. And I think if the banks are required to hold more equity, I'm not sure how they would react to that one way or another. And I don't believe that just by holding capital is in its own right one action. There'll be a reaction to that as well, and I think you'd have to ask the big banks as to how they would consider that. I think we should take any questions on the phone.

Operator

Your first question comes from the line of Jon Mott from UBS.

Jonathan Mott
UBS Investment Bank, Research Division

Firstly, well done on the great new disclosure. Much improved and very helpful, so we really appreciate that. Just got a question on dividend policy at the moment and now going forward. Has the board actually set a formal dividend policy on where you'd like the payout ratio to be going forward, especially if you move from what you'd say the restructuring phase into more of a sort of renewed business-as-usual phase over the next couple of years?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

We're actually still in a fairly transition zone. The way we are looking at it is the extent of capital that we hold, given the future growth prospects that we do have and what we see we require to hold internally. So we're still transitioning through that period and we haven't actually committed to any payout ratio targets.

Jonathan Mott
UBS Investment Bank, Research Division

So would it be fair to -- sort of until you get through that phase, you'd probably be still looking at trying to steadily grow the dividend? Or is this just a one-off reward to shareholders for their patience moving it up $0.02?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

I'm not sure what your model says, Jon. Look, we assessed it at the time when we got it and it's a board-based decision based on equity ratios. They want to maintain growth ambitions. I think once we get into a more stabilized environment, we'll be able to actually come out and outline clearly what the policy is.

Operator

Next question comes from the line of Andrew Triggs from Deutsche Bank.

Andrew Triggs
Deutsche Bank AG, Research Division

Perhaps a question for Anthony, if I could. Just with the disclosure on Page 15 of the presentation around the new impaired asset flow. I'm just interested in trying to get a sense of the underlying movements in new impaired. If I look at the $183 million and I exclude the Asset Quality Review loans, it seems like $142 million, but that seems quite elevated relative to both the previous half, if you exclude the 180-day mortgage reassessment and also second half '11 of $104 million. Can you perhaps give some guidance around -- I guess, it's the commercial loans that have seen that step-up. Is that fair to say?

Anthony Rose
Executive Officer

Yes, it is. So, I mean, if you look at the chart on the right-hand side of that slide, of the $22 million and the $42 million, the greater than $5 million buckets, I think we called out that $40 million of that we would consider to be the wash-through of the Asset Quality Review accounts. I mean, a number of these accounts were obviously quite difficult to determine the right realization strategy, complex exposures with several aspects to them. All of that work has now been completed and the valuations updated and in place, so that's the reason why that took some time to get done. That's -- that piece of work is now completed. If you exclude that $40 million, I do think you're getting a more normalized view of where it -- where the portfolio would normally expect to see turnover between new impaireds and realizations.

Andrew Triggs
Deutsche Bank AG, Research Division

And in terms of the guidance for full year bad debts, gross loans, does that assume any improvement in that flow of new impaireds or a steady state on that front? Because, obviously, during the half, you benefited from CP releases?

Anthony Rose
Executive Officer

I think we're very comfortable with those management targets that have been put out. We've always called out that we expected the profile from a credit quality's perspective to improve progressively over this period and it wouldn't be significant step down. That's exactly what we're seeing emerging. And we do see that those -- that profile is going to continue from where we are at the moment.

Operator

Your next question comes from the line of Andrew Lyons from Goldman Sachs.

Andrew Lyons
Goldman Sachs Group Inc., Research Division

Maybe just 2 questions. Firstly, one further due out to Jon's question, just around the capital position. Your absolute position looks pretty strong, as does your capital generation. I'm just -- I'm wanting to get your thoughts on just maintaining the DRP discount at 1.5%. And then just secondly, just around your Pillar 3 disclosures, just hoping to get a bit more data around Appendix A on Page 8 of the Pillar 3 disclosures, just understanding the reconciliation between the regulatory impaireds and the investor information impaireds, and just maybe a bit of a discussion on how the movement in your regulatory impaireds has looked over the last 6 months.

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

I'll pass that one to Anthony.

Anthony Rose
Executive Officer

So the first -- your first point was on capital generation. I'm not really sure I picked up the question in that point.

Andrew Lyons

Goldman Sachs Group Inc., Research Division

I just noted that you're continuing the...

Anthony Rose
Executive Officer

The DRP?

Andrew Lyons
Goldman Sachs Group Inc., Research Division

DRP discount at 1.5%. Just wanted to get your thoughts just around that.

Anthony Rose
Executive Officer

Well, we've obviously reduced it from 2.5% to 1.5%. I think it's important. One of the things this business, being a fully 100% domestic earnings stream, is we do generate a lot of franking credits. It's good to be able to provide those franking credits in the hands of our shareholders. And by enabling that DRP, it does enable us to generate additional capital to pay a higher payout ratio over that profile and put the franking credits in the hands where they're most valued. As far as your question on Appendix A to the Pillar 3, which is a new inclusion, given the changes that have happened in the Pillar 3 reporting through this period, which is a reconciliation of the impaired assets as we report them in our statutory accounts and the APRA definition of impaired assets, obviously, for APRA purposes, those impaired assets that's sitting off balance sheet trusts get excluded and there are other restructured facilities that were -- that meet specific APRA requirements that fit into the impaired asset definition. Those restructured facilities, a significant amount of those all would have been accounts that have come through the Asset Quality Review process and would have had restructured arrangements in place, but are obviously back to acceptable position from the bank's perspective.

Operator

Your next question comes from the line of Mike Wiblin from Macquarie.

Michael Wiblin
Macquarie Research

My question was just around the new commission structure. Can you just talk us through what you're doing there and any sort of financial implications in terms of revenue sharing on that front?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

We actually are working through it at the moment with the Owner-Managers, so we won't talk about it publicly until such time as we've socialized with the Owner-Managers in full about it, but the intent is not to, obviously, change the economics to the Owner-Manager substantially on the negative basis because that wouldn't make any sense. But it's more about balancing the behaviors of the Owner-Managers towards what we see as important, which is the balanced profile of deposits and loans. And at the moment, the commission structure is skewed very heavily towards the lending side rather than the deposit side, as well as bringing in quality aspects for origination and management, which proves the -- which do exist, but not to the extent that we like. So we're still working through that. And Matt Baxby and the team will be talking to the Owner-Managers out over the next few months.

Michael Wiblin
Macquarie Research

Just had a follow-up question on the impairment side. I mean, it sounds like you're talking about things improving sort of steadily, but there's a bit of a cautioned outlook. Can you give us a sense as to what you're actually seeing and what's driving some of the softness in those segments, and maybe where are you seeing them on a state-based sense?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Yes, and Queensland's still doing it reasonably tough. It's mainly in the small end of town. I think most of the surveys that we've seen indicate that the large businesses have a greater propensity to borrow at this point of time, whereas small businesses have been enduring a very tough market for a long period of time and are finding it difficult. And anecdotally, the tax office is -- has actually stepped up its activity in collections as well. And the caution we have around the book is that it's a lot more difficult to, I suppose, remedy and rectify commercial impaireds and residential, where sale of the property is quite instantaneous and working commercial does take a bit longer to get through. So I mean, we are being cautious because we are getting a mix of indicators across the board, and none of it provides a consistent approach to us that suggests confidence is rushing back that would give us some cause to say that things are picking up greatly.

Operator

Your next question comes from the line of Craig Williams from Citigroup.

Craig Anthony Williams
Citigroup Inc, Research Division

Can I echo Jon's praise for your attempts at improving disclosure up front? Could I ask a couple of questions as well, please? Can I confirm that your core equity Tier 1 capital position at the first half '13 of 8.7% will not have a dividend deduction in it, but the FY '12 core equity Tier 1 number of 8.58% will have been net of your $0.26, I think at the time, dividend announced at the time?

Anthony Rose
Executive Officer

The 8.72%, you're absolutely correct. The 8.58% starting position was a restated balance.

Craig Anthony Williams
Citigroup Inc, Research Division

Right. But that's prepared on sort of a like-for-like basis...

Anthony Rose
Executive Officer

Correct.

Craig Anthony Williams
Citigroup Inc, Research Division

Is what you're saying?

Anthony Rose
Executive Officer

Yes.

Craig Anthony Williams
Citigroup Inc, Research Division

Okay, great. And with the lift in your dividend, your payout ratio this period was 88%. Presumably, the message there is an expectation by the board of modest asset growth with sort of improved impairment and profitability trends going forward?

Anthony Rose
Executive Officer

That's correct.

Operator

Your next question comes from the line of Anthony Hoo from Nomura.

Anthony Hoo
Nomura Securities Co. Ltd., Research Division

I just wanted to ask about your commercial loan growth. It was mentioned that excluding the identified runoff, you had growth of 11.5% annualized. Could we get a better sense of where that is coming from, whether it's geographic or on an industry basis?

Anthony Rose
Executive Officer

There was -- as you said, the 11.1% is pure business bank. The 6.1% we referred to includes the BOQ finance book. And the BOQ finance book was flat to slightly negative, so that watered that down to 6.1%. We had reasonable growth out of the agribusiness portfolio, which I alluded to. And we've been growing, I suppose, a reasonable amount of business, but not rapidly, in that, I suppose, $10 million to $30 million borrowing requirement. And if you look on the slide, we showed the top 10. You'll see there's a few replacements in there, which are the new customers or size of customers that have been -- borrowed a bit more from us. And then on a state basis, we've probably diversified more into the New South Wales market for those exposures. And as we alluded to, it's developing more business, putting more business bankers into Sydney, Melbourne and Perth. We're looking to diversify further into the other states for quality borrowers, which we are funding.

Anthony Hoo
Nomura Securities Co. Ltd., Research Division

And if I'm looking at your arrears rate in commercial, as, I think, Anthony identified earlier, it seems to be still quite elevated and it's deterring slightly. What are the implications of that in terms of your focus on growing business banking, I mean, that would change your focus on what areas you wanted to target?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

You're correct in saying the arrears are quite elevated in the commercial. That is -- what we're focusing on is good business, which we are seeing. We are running through -- as we indicated at the second half of last year, we worked hard into the under $5 million borrowing. And what we're seeing are the implications of managing that much tighter than perhaps we might have in the past. We are working through those and we'd expect to see those arrears come down over time. As I indicated to you before, it's working out of a commercial exposure is a lot harder than working out of retail exposure. It does take time. But we recognize that those arrears are high on a comparative basis, and we will be working to get them down.

Operator

Your next question comes from the line of David Shi from Morgan Stanley.

David F. Shi
Morgan Stanley, Research Division

I've just got a question regarding Virgin Money. Online banking tends to be a pretty highly prized competitive sort of business in cases like UBank as being a loss-leading strategy. So I was wondering if you can just talk around how Virgin Money can be different through that?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Well, one of those things, it's got of fairly good brand to start with, which drags eyeballs to it and it's not necessarily just price that brings to it, as we can see through the 30,000 superannuation clients that have developed over time without a lot marketing. The eyeballs have just come. They're growing their customer. Customer acquisition is up around 20% to 25% per annum over the last 3 years. So they are growing customers at a very rapid rate of knots [ph]. And the mix of having an attractive brand name with a functional platform is a real advantage and it's been shown that while it has been losing money, we believe that it won't take long for that to turn around given that it's reaching scale very rapidly.

David F. Shi
Morgan Stanley, Research Division

Right. And just a follow-on question regarding your agribusiness lending. You mentioned in August last year that you're targeting for $1 billion over 3 years, and you alluded to the fact that, that's seen some growth over this half. Just wondering if you're able to provide an update on how far you're into that target.

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

We are $140 million into it. We've got a reasonably strong pipeline. The one thing that I would mention is parts of the agribusiness sector are experiencing some stress. So we've been a lot more cautious over the last 6 months as to which clients we are taking on. There's drought in the west. We're not really exposed there at all. A lot of exports have taken a bit of a hammering, and we really haven't gotten any of those clients on board. And cattle prices have come up as a result of that. So we are being selective about what we're taking on. We still think we can get to that number, but we're making sure that we're not taking unnecessary risks in order to achieve that target.

Operator

Next question comes from the line of Ed Henning from CLSA.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Just a first quick question on the costs. If you add back the restructuring, obviously, it was above inflation, can you just run through what was in the restructuring? And will this be ongoing because there was obviously a little bit of a restructuring charge below the line last period? And was there any capitalized software written off?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Sure. I'll pass it to Anthony.

Anthony Rose
Executive Officer

Yes. So obviously $11 million pre-tax is about $16 million. About $12 million of that were redundancies, just part of the spans and layers and shared services operations. That was a one-off, clearly. And the balance was a number of odds and sods that largely, with the shared services, we had to do some transfer of systems and technology. And it was a combination of that piece represented the balance. There was nothing material in there from an asset write-off perspective.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Okay. And will any restructuring be ongoing? Because, obviously, there was some last period, too, below the line, that is?

Anthony Rose
Executive Officer

There's no intention at the moment. I mean, obviously, that was a very significant transformational statement for the organization. We've got a new management team. We've got a new vision going forward. And I think it was appropriate to make sure that we had gone and set the fit and focus for what we needed to get, to use our internal vernacular.

Brian D. Johnson
CLSA Limited, Research Division

It's Brian Johnson. Could I just ask a question on the capital position? And my status is the most miserable bloke in the world. If you have a look at Slide 21, your capital position, you've paid out quite a big dividend in this period, which from a capital perspective, comes out in the next quarter, which we'll see in the next Pillar 3. So in this period, we had very low systemic asset growth. Is it unreasonable to think that we're going to see that core equity Tier 1 of 8.72%, prima facie, come back at peak, come back a hell of a lot in the next quarter? How far would you tolerate it slipping in the next quarter?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

With the impact of a dividend, absent anything else, we're where we would expect the DRP to participate, is about 20 points. And then obviously, by the time you get to November -- I'm sorry, by the time you get to May, should I say, you would have had the 3 months' worth of earnings to help offset that.

Brian D. Johnson
CLSA Limited, Research Division

Okay. So we've got a big [indiscernible] coming up next quarter. We've got a lower DRP clawback. We've got a higher asset growth. And the net result is simply that you don't think it actually declined in absolute percentage, is that right?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

You will see -- under the new framework, you will see a sawtooth approach to the movement in capital deploying a half and full year period as opposed to the Pillar 3 results. You will see a dropoff and then pickup again. But we think that the profile that we've got at the moment keeps the business over -- if you draw a line through that, at a steady state.

Brian D. Johnson
CLSA Limited, Research Division

Okay. The second one is -- and this is a great presentation, by the way. But one thing that's not there is talk about the balance sheet liquidity. Can you run us where you would be on the liquidity coverage ratio and what you did with liquidity for the period?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Yes. So the liquidity was conservatively managed. We hold liquidity around -- just over 15%. There is some coverage of that in the investor information pack. And as far as the liquidity coverage ratio is concerned, clearly, we've got the same issues that everybody else does around the composition of those assets. And clearly, if you were to turn them into qualifying assets, we would be at effectively the LCR level today. I think pretty much everybody is in the same spot there.

Brian D. Johnson
CLSA Limited, Research Division

And just the final one is in the results, the margin went up and it was this disciplined -- discipline on the deposit pricing. And yet in the outlook, Stuart, you were actually saying that there's quite a bit competitive pressure still building there. Can you give us a feeling for your expectation of deposit margins going forward?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

I think as the wholesale markets -- if the wholesale markets continue to open up and tighten up, I think that some of the pressure on the deposit margins will come off, but it's still competitive out there. And we look at the carded [ph] TD rates versus the noncarded [ph] TD rates. And the flows of business into TDs have actually started to reduce as people move more to online. So there's a lot more switching going on around it, when online, that typically is a tighter margin product for all banks. So while you can actually look at one sort of aspect of deposit market and trade it off against the others. So while we are seeing some, I suppose, improvement in margin in the term deposit market, it's being offset by a switch of people into online deposits.

Operator

Your next question comes from the line of Joseph Koh from Regal.

Joseph Koh

Just a question on -- again, on the Pillar 3 disclosure, the $145 million of restructured facilities. They don't seem to have been impaired at August 2012, is that right? And they only became impaired sort of during the period? It seems that the balance at August '12 between the Pillar 3 disclosure and your presentation is pretty similar. There was a slightly perfect $10 million, which is, I guess, securitization.

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Yes. They're retail accounts and it's a change in definition, if you like, of those facilities that now fit the new reporting framework for regulatory purposes. So they're a definitional change.

Joseph Koh

Okay. So due to definitional change, it became impaired during the period?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

For regulatory purposes. So they're not impaired in the way we think about the impaired exposures, but for regulatory purposes, they are reported under APS 220 as impaired. And they were not previously.

Joseph Koh

So no change in the actual fundamentals of those loans?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Correct. Right.

Operator

Your next question comes from the line of Brett Le Mesurier from BBY.

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

A couple of questions. Firstly, did I understand what you were saying before correctly as implying that this is the last time you'll reduce the collective provision without any improvement in asset quality?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

The answer to that is yes.

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

And secondly, the deferred expenditure increased from $107 million at August to $121 million in February '13. Could you give me some details about what that was about?

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

What are you referring to there, Brett, sorry?

Anthony Rose
Executive Officer

In the answer to capital.

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

Oh, in the Pillar 3 under the regulatory adjustment deferred expenditure increased from a 100 -- the deduction against capital for deferred expenditure increased from $107 million in August '12 to $121 million February '13.

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

I have to come back to you on the detail of that one.

Operator

Your next question comes from the line of Nicole Mehalski from Merrill Lynch.

Nicole Mehalski
BofA Merrill Lynch, Research Division

Stuart, you talked about the pilot project for the mortgage broker channel and the fact that around 5% of your originations are coming from this. I just wonder if you could talk a bit more about where you see that getting to and what the time frame is on that.

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

We haven't set any time frames. So as we said, it was a pilot and we're still early into it. We want to make sure our systems work and we can handle the volume and the flow. I would say we'd probably be able to make that determination probably in the 4- to 6-month period as to what are the next steps. But it was very much a "Well, let's get in there and see how it operates, see what systems of ours work and what the quality is like, most importantly," and then we can make a determination on that. As we've mentioned previously, WA is a key market for us, so we want to make sure we're successful there before we move out. But if you look at the firms that have been -- other banks that have been in that market for a lot longer than we have, the originations from brokers vary between 40% to 70%. So, I think it -- and that takes a long time to get there and we're very early days.

Operator

[Operator Instructions]

Stuart Ian Grimshaw
Former Chief Executive Officer, Managing Director and Executive Director

Okay. Well, thanks very much, everyone. I'm sure we will be talking to you over the next couple of days, but thanks very much for your attendance and your support.

Anthony Rose
Executive Officer
Thank you.