Question and Answer

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Thanks very much, Jon. We're going to take questions from the floor first in Sydney. Can I ask you to please wait for microphones so that our participants on the webcast can hear and then we'll take questions from the phones. And I also ask you to please stand up so our microphone attendants can see you. I might start here with you, Jon.

Jonathan Mott
UBS Investment Bank, Research Division

Jon Mott from UBS. Quick question. One of the comments that had towards the end is that you want to grow in Retail, but there was a big definitive no change in pricing or risk, and especially on the broker channel. I just wanted to explore that a little bit. You're seeing a lot of your competitors, one regional bank in Queensland that's not yourselves, in particular, putting the upfront broker commissions up to 80 basis points, and other competitors are aggressively putting prices up for brokerage rates as well to try and tap into that market, especially if the banks that don't have the same exposure to Sydney and Melbourne commercial property. So can you comment on will you be able to do it if you do see -- and continue to grow that channel, if you do see competitors continue to push up their pricing there? And also on the risk side, you have mentioned that you've don't have as much exposure to Sydney or Melbourne on investment property, can you just give us a bit of a breakdown on how much investment property you have versus owner occupied at the flow and anything you do have on Sydney and Melbourne that would be great.

Jon Earle Sutton
Former MD, CEO & Executive Director

That's a nice way to kick off, Jon. I think you've asked about 4 questions in 1, so I might start off with how we're going to compete in the broker market and talk about some of the pricing metrics that we see there. I'll hand over to Anthony to talk a little bit about what we're seeing in flows. But let me say at the outset, we've had a very, very definitive strategy with the brokers. We, first of all, went to AFG in Western Australia, a market that we're underrepresented in for a long period of time. And the feedback that we've got from the 4 broker groups that we're now with at the moment was that they welcome to have BOQ on the panel. They wanted to have more competition. Where we are competing in that particular channel is that we're using a Clear Path product. It has a -- it's not a switch and bait product like a lot of other banks, actually it has a very low transparent interest rate, very low fee. What you see is on the tin[ph] is what you exactly get, and we're seeing some enormous uptake with that. As always, we review what our commission model should be with the brokers, but we are finding that they are supporting us well. Now we're moving that out through the Eastern Seaboard, and each month we're seeing incremental gains on the amount of broker volumes that are coming through. And just on credit quality, it's early days. We don't have great, detailed vintage analysis because we've only just been there for a little while, but the majority of the proportion of what we're seeing is PAYG, which actually goes further to diversify our book. And the early indications of the credit metrics are very good. Do you want to talk about the other?

Anthony Rose
Executive Officer

Sure. Just to pick up on a couple of the points. Obviously, our portfolio in the retail spaces look a little bit different to our traditional portfolio. We've been over weight lock and we've talked about that at length. We have also had a high proportion of investor than probably a traditional bank. The new business metrics that we're actually writing today are trending much more like a traditional banking operation. In fact, a greater than 80% lending would be slightly below on our numbers what the average of the rest of the industry would be. And in fact, if you look at our investor exposure, the LVRs on that portfolio average around 65%. It does tend to be slightly lower LVR than owner occupied for obvious reasons, just the nature of the property. And yes, so I think -- hopefully that catches your question.

Jon Earle Sutton
Former MD, CEO & Executive Director

Just to add on Sydney, Melbourne. I think last month, the settlements invested for our total loan portfolio was 6.1% in Sydney, so it's negligible; and Melbourne was slightly higher. So we're not over indexed there at all. Sorry, I can't see with the lectern. I'm very short.

Richard E. Wiles
Morgan Stanley, Research Division

Rich Wiles, Morgan Stanley. I think in Slide 30 you referred to the difference in capital. It seems almost inevitable that the majors will be forced to lift risk weightings on their mortgages, but do you believe that you should get a reduction in your mortgage risk weightings? What are you actually doing to convince APRA that you should have lower mortgage risk weightings? Can you give us an update on your efforts to get to advanced accreditation?

Jon Earle Sutton
Former MD, CEO & Executive Director

I might just make some opening remarks on that. I would never make a comment about any discussions that I have with APRA, but what we have -- do have were very much on the public record through the FSI and what we're advocating. And we would be advocating lower risk weightings, particularly in that band of low risk mortgages, less than 8%. And Anthony can talk to some more detail on that.

Anthony Rose
Executive Officer

Sure. There's obviously a number of factors, and it's interesting in the overall discussion around macroprudential levers how does the regulator actually deal with the Sydney and Melbourne investor piece. Now currently, they've got a countercyclical capital buffer, that if they were to apply that, it would apply to all lending, which is a fairly blunt instrument. Clearly, one of the things we've been advocating is a more transparent capital regime. We currently have a standardized suite of banks and we have advanced banks that operate with bespoke[ph] black box models, which lack, I think, the transparency to provide the resilience to the system that we would, I think, benefit the broader economy. And our view would be that the advanced banks should all be reporting on a standardized basis as well and that the advanced outcomes are calibrated with maximum deviation from the standardized element so that there is transparency. There still needs to be appropriate incentive for advanced risk modeling capability. Clearly, the gap is too large. I think that framework adds significant resilience. What I would also would do in a macroprudential sense is you could put increase in risk weights on investor loans in Melbourne and Sydney post codes on standardized banks and you immediately recalibrated the entire industry if you had advanced calibrated to standardized. As far as our path towards advanced accreditation, we don't have a characterized advanced accreditation program as such, but the steps that we're putting in place at the moment, the digitization, is absolutely the foundation building block to that path. We clearly have made a lot of progress in the market risk space, and I don't think our gap to advanced accreditation is significant here. We are expanding in the operational risk piece, and we've got a lot to do in that regard. And then in the credit modeling piece, we've made a lot of progress as well. So I think it's mainly getting that foundational digital environment. It's pretty hard to sit down with the regulator and prove validation when you have to then go and pull security packets to do so.

Jon Earle Sutton
Former MD, CEO & Executive Director

I'd endorse those comments that Anthony's made. Peter and his risk team have been on a tremendous journey in a very, very short period of time. And having been through 2 advanced accreditations at 2 other institutions, the bar, over the years, has been materially lifted higher by the regulator in terms of what's required. But we have a term within the bank we always use is well-run bank, and a lot of the work that Peter and his team has done have laid the foundation stones for us to get advanced accreditation. And we'll continue to pursue improvements in our risk and our risk culture and our systems and processes.

Richard E. Wiles
Morgan Stanley, Research Division

So can I just clarify, at this point, there is no target date for submitting an advanced accreditation application to APRA?

Jon Earle Sutton
Former MD, CEO & Executive Director

We don't have at the moment. We're not going to put a date out there, but we are well and truly on the journey for putting the foundation stones and the layers needed for advanced accreditation. We're going to continue to watch very closely of what the outcome is with the FSI inquiry as well.

Richard E. Wiles
Morgan Stanley, Research Division

Well, Bendigo Bank started this journey a couple of years ago, it looks like it will take them 2.5 years to get to the point where they have submitted an application to APRA. Do you think that's a reasonable time frame for a regional bank of your size?

Jon Earle Sutton
Former MD, CEO & Executive Director

I couldn't possibly comment on what Bendigo has done or hasn't done. I'll come back to the comments that I just made before is that we're doing a lot of work around ensuring that the systems and processes -- Peter, do you want to add something to that?

Peter Deans
Former Chief Risk Officer & Group Executive

It is a really good question, and we've pondered particularly as the FSI has rolled through this year. Historically, the regional banks have adopted what I call a one-size approach. You have to do the full program for all 3 pillars: credit, market, operational risk. I think in the discussions that sort of been held in the public domain a little bit, meaning the submissions we put forward, we did put forward the option which say delinking the 3 pillars. And I think that's sort of -- we've had encouraging feedback that that's one of the options being considered, so you may not need to do the full program. And I think with -- our sort of firming view that there will be some benefit to the regional banks come out of the FSI, hopefully. We thought it will still need to put in place an extensive program which requires significant capital investment over what you've pointed out is a long period of time. If there may be a shorter path to get the benefits of advanced accreditation without the full 5- to 7-year program, I would just echo Jon's point, we had actually been doing a lot of the work that you'd normally see with a Basel II program to get us to well-run bank. So even though we don't call it a program as such, I think we're well placed to hopefully come up with a revised plan next year once this clarity around the regulatory settings.

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Okay. We might go down the back. Yes?

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

It's Ed Henning from CLSA. Just going back to the retail and the growth there. Can you just run through the issues in the owner-managed branches and also with the change in the commission structure, is the worst behind you there? And just lastly on that, with the Line of Credit product, how much is remaining of that legacy to roll off?

Jon Earle Sutton
Former MD, CEO & Executive Director

Okay. Look, I'll make some overall comments around our branch network and then hand to Anthony. He can talk to the specifics around the Line of Credit product and what we're seeing there. Look, when I think about distribution for a bank, be it -- whether it's a regional bank or a big 4, you've got to start with the customer first. Customers choose how and when they want to deal with you. Customers may start online, they may do some investigative work there, they may then move to -- straight to a branch, or they may actually then choose to go to an item -- they may choose to go to a broker and then ultimately they'll end up with a branch, again, opening up an account. So what we're doing is looking at what the macro themes are and we're always evaluating what are the appropriate channels of distribution. Now I want to go back to my opening remarks. This is a bank that has largely ignored the broker channel for the best part of its -- since its inception. It was in it for a little while. And 43% of all lines now come through a broker. So you ignore that channel at your own peril. So what we have done is opened up our growth -- distribution growth through that particular channel. We stand by our Owner-Managers. I was recently at the Owner-Manager conference a few weeks ago, it's the third one I've attended, and I'll have -- absolutely have to say, it's the most amount of confidence I've seen from our Owner-Managers in the period of time that I've been at BOQ. We've had a reduction of 18 branches. A lot of those -- some of those come down to Owner-Managers deciding to amalgamate and actually grow their business and offer better servicing. Some have decided to retire. And some we've actually taken back, but not a lot. And it still remains dynamic, and we will continue to look at those distribution channels. It's a work in progress, but we're happy with where we are at the moment.

Anthony Rose
Executive Officer

Just on the LoC question, we had $700 million of runoff this year. We don't expect it to be as large next year, but it will still be a headwind for us going forward and it will be not a significant -- not a major reduction on that $700 million number. We were 21% of the portfolio, it's down to about 13% now, which is clearly back more towards risk appetite. If I look at the arrears position on the LoC product, it's still more than double our traditional Home Lending, and that is where the bad debt expense has been overweight. So you look at our bad debt expense for Housing, it's in the 12 sort of region. We would like to see that single digit, and if you actually just strip the Line of Credit product out, you'd be pretty much there. So it is a focus for us, but again, it comes down to the pricing discipline and the risk discipline of maintaining that focus. And we've got a new product in the market, which is writing Line of Credit products for the right customer base, but there are still elements there that we'll continue to roll off.

Jon Earle Sutton
Former MD, CEO & Executive Director

We didn't sort of answer your questions on commissions, so the thing I would say about commissions, the commissions that we're currently paying our Owner-Managers and what we also pay to our brokers are very, very, very similar. There's not very much difference. And in fact, as we roll out the new balanced scorecard that we talked about in my earlier remarks, that will also drive further cost sales across the network and also greater health in the OMB network as well.

Anthony Rose
Executive Officer

And the main thing is the digitization piece, because as an organization, we talked about before, we've got one arm tied behind our back in relation to capital. Our Owner-Managers and the corporate branch managers have got one arm tied behind their back in relation to the systems that they have to operate within. You go to a branch and you have to dodge the filing cabinets.

Jon Earle Sutton
Former MD, CEO & Executive Director

I'm Toll's [ph] best customer.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Just back on the owner-managed branches, do you think...

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Come in just right for the mic, Ed.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Just back on the owner-managed branches, do you think -- from now, do you think you're going to see a happier mob moving forward from where you're sitting?

Jon Earle Sutton
Former MD, CEO & Executive Director

Very much so. I'd just go back to the remarks I made previously, I went to the Owner-Manager conference and it is materially different in terms of how they feel about where we're going. It's a true partnership. I attended the national advisory committee along with Matt. Matt and his team has done a wonderful job in reinvigorating the Owner-Manager network. They love the new branding that we have. They're on board with the products that we currently have. They're on board with the new commission model. There are already score cards and letters out there. And in fact I had the chance to be at one of the branches the other day where an Owner-Manager got absolutely all greens on all of his audits and was genuinely excited. If I took you out to Parramatta, you're probably -- you're going to meet one of the most enthusiastic bankers you're ever going to see. He's got a lot of experience and really is a leader with his own community at Parramatta. So we're very committed to the Owner-Manager network.

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Craig?

Craig Anthony Williams
Citigroup Inc, Research Division

Craig Williams from Citi. There's obviously a lot going right at the bank at the moment and the financial results are showing that, and some good progress on processes and that sort of thing. You're calling out a wish to be Australia's most loved bank. Your Net Promoter Score, 16.8, and the major banks are flat to negative on this score. So I look at your retail loan growth, it's 0.1x system[ph], your retail deposit growth I think is 1.8% this year, excluding the acquisition of the Investec book. So can you explain the relevance of the net promoter measure? And what benefits being a more loved bank[ph] are in fact providing?

Jon Earle Sutton
Former MD, CEO & Executive Director

Look, that's a great question, and it's a journey that we're going on. It's a repositioning of the bank. And it's not only for external, for customers, it's also -- it's very much internal as well. So it's the way we approach everything we do within the bank itself. It's getting close to our customers, being less bureaucratic, getting our time to yes down. So it's something that I've been really close to over the last 2 years is this whole digitization. And it's just an understatement to say that we've got so much paper, we have mountains of paper. And sure we have been underweight this year in terms of our retail growth, but if you sat down with one of our Owner-Managers and saw what he had to go through to get a home loan application entered into the system and -- as opposed to what you'll have starting in April, it's just chalk and cheese[ph]. So we've been fighting with one hand behind our back. And it's a fairly emotive statement to say it's possible to love a bank, but it's something that everyone comes to work every day to try and do and live and eat and breathe. So I'm confident that we have the right strategies in place to actually get our retail distribution growth back towards system or slightly above system. And look, I want to say again, it's this executive team that is sitting here today that devised the strategy and is executing on that strategy, and we are making progress on that.

Craig Anthony Williams
Citigroup Inc, Research Division

So how are shareholders...

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Craig, can you just...

Craig Anthony Williams
Citigroup Inc, Research Division

So how should shareholders actually see the benefits of this strategy being executed effectively over the next couple of years?

Jon Earle Sutton
Former MD, CEO & Executive Director

Well, I think they see the significant benefit today in the results that was announced. There's been an increase in earnings per share. There's been a healthy increase in the dividend. And when you sit and look at running a financial institution, and I'll look at the history of this organization as well, is we want to make sure that we have got sustainable earnings per share growth, that we've got sustainable dividend growth and then we have the right risk settings so that we don't have periods of volatility and that we can actually get through the cycle, each cycle. And that's really, really important. And everything you've heard here today is really building and bridging towards that and that's what it's all about. It's not about short-term massive increases in profit. It's really about getting that EPS on a sustainable growth path, getting the dividends on a sustainable growth path and executing what is, I believe, is a quite simple strategy. There is an absolute place for us that customers are crying out to come away from the big 4 banks. Small example, particularly in the Business Bank, we talked about a lot the retail bank, but in the Business Bank, the people that can make a decision can be pretty much convened with a phone call. And we did that recently with a leasing deal which involves some helicopters for the rescue service in Queensland. And that was quite a complex deal, it was cross-border, but the decision-makers were put on the phone around the table and we gave the customer the answer they needed, and the other banks involved still had to go to their credit committees. That, to me, is a competitive advantage that we have.

Anthony Rose
Executive Officer

If I could just maybe add, just to give you an example of how we -- you called out 1.8% deposit growth, absent BOQ Specialist. If you actually look at what we considered to be relationship deposits and the growth in that underlying part of the portfolio, we've actually had system growth there. What we've been doing is reducing the reliance on the high cost, and that cost component where we, in fixing the balance sheet post GFC, paid up for the real hot money and we've just being unwinding that progressively as we go. So I think the residents[ph] of the model is still working, and we're staring into some of the constraints operationally but also the turnover of the portfolio into a new top customer going forward that I think this we're in at the moment. And also being out of the market in brokers, which has been obviously significant growth for other participants and less exposed in the areas that have had the higher system growth, Queensland still below half of national system average.

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Andrew?

Andrew Triggs
Deutsche Bank AG, Research Division

It's Andrew Triggs from Deutsche Bank. Just following on from that response, Anthony, how far do you think you are through that hot money TD rolloff? And your comments on the margin, did they relate to further -- I guess further to come on that? Or is it more about the counter rates? And second question, just in the Business Banking, despite obviously there's been very good growth, what sort of appetite is there at the moment for commercial property?

Anthony Rose
Executive Officer

So in relation to the deposit space, you manage both sides of the balance sheet. So clearly, we've had a year where we haven't grown in the asset side any way as fast as we wanted. And as we look forward, we aspire to higher rates of growth. And I think the foundations that we've built in this year, do put us in a position to grow at an accelerated rate in 2015. So your capacity to play those levers on the deposit side really depend upon what does the other side of the balance sheet actually do. So there are a number of moving parts to that. We still do have a significant presence in that more price-sensitive part of the market. Every bank plays in that space. Again, it just depends upon what pace of growth do we want the aggregate balance sheet to look like as to how much we're going to rely upon on that element going forward. In relation to appetite on Commercial Lending, I think one of the significant changes that we've got is -- our executive credit committee, we seek with our portfolio metrics of understanding by geography and postcode where our appetite actually sits and we regularly monitor that. We didn't have that capability and it was just using the gray matter of the people around the table, whereas, now we've got a much more considered approach to the front line can then go and leverage in the areas that they choose to spend their time and target new customer acquisition, with the knowledge base as to where our broader appetite actually sits.

Jon Earle Sutton
Former MD, CEO & Executive Director

We're very disciplined about that. Again, having been through a couple of cycles and having a deep understanding of development finance and commercial property, we're all about a well-diversified book. And Brendan and the team are doing that. In fact, if you looked at one of the strategies that we've been involved in with Agri. We're currently well underway in delivering growth in Agri, but we've also actually declined quite a lot the businesses as well. So it's quite a disciplined approach to what we're taking. But the key takeout is diversification.

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations

Nicole?

Nicole Mehalski
BofA Merrill Lynch, Research Division

Nicole Mehalski from Merrill Lynch. Just going back to the movement of the paper-based system, you described it as one of the biggest transformation projects you've taken on. You're talking about starting the pilot in April, and I assume hoping to get everything rolled out by the end of the year, how much of a constraint could that be on your capacity to write mortgages next year, for example taking on the BOQ Specialist book, and how do we think about that? And then just another one on the runoff of the book, you talked about the Line of Credit, I understand there's been some sort of concentrated runoff in some other parts of the book and how do we think about that in terms of next year?

Jon Earle Sutton
Former MD, CEO & Executive Director

I might just start with how we're going to write mortgages and Anthony, because he loves the Line of Credit, he can talk to the Line of Credit. BOQ Specialist has its own systems and process. And it's testament to the dexterity of that organization that they were quickly able to see how they could actually put those mortgages on balance sheet on those systems. So again, I'll go back to my earlier comments that this -- they've been writing $1 billion of mortgages with third parties. We would like to see us writing 50% of that over the next coming 12 months. And they're well on their way. As far as BOQ goes, we've had to take, as we go through this transformation program, we've had to have a bit more of an intensive approach to servicing the broker mortgages at the moment through additional people on the ground to help us do that. But also, that's around making sure we get the right servicing. So as we actually move through FY '15 and deploy our lending system, that will start to free up resources as well.

Anthony Rose
Executive Officer

I think I -- we covered the LoC.

Nicole Mehalski
BofA Merrill Lynch, Research Division

So I was meaning the other parts of runoff. You talked about sort of around the Victoria book and issues around there, and how we think about that next year.

Anthony Rose
Executive Officer

Look, the way we think about what we're doing with the -- and there's been quite some compositional change in the branch network that you will note. There is a macro driver which says customers are changing the way they interact. And the branch looks very different today than it did 10 years ago and it will look very different going forward than it looks today. And we're obviously cognizant of those changes. In addition to that, there are a number of our branches that are relatively poorly located. So as we go through whether that's a change or whether there's an end of lease term or whether it is a retirement of an Owner-Manager event, it is a horses for courses decision at each individual branch, just what do we do with that. Do we consolidate that? Do we turn it into a corporate branch? That's the exercise we've been rolling through at the moment, with the overlies that I talked about around customer preference and the recognition that we're not going to renew a lease in a location that we think is suboptimal, and we're taking a different approach to where we want to locate branches going forward to get full traffic.

Jon Earle Sutton
Former MD, CEO & Executive Director

I think really good example of that is some of that dexterity that we're talking about. If you got to Macquarie Shopping Centre, that is a shopping center that has a footwall of 10 million or more people, and that is increasing as they expand that center. Now we've just recently opened up an icon branch, and the past experience I've had when you go into these shopping centers is you've got to actually get the right macro location. And we did a lot of work to understand footfall traffic, branch design and got what I believe is one of the best locations in the Macquarie Shopping Centre. The thoroughfare through the food court all the way to through the dining chains. And it's very, very early days yet, but we've seen some really nice results come through in our icon branch. So again, it's horses for courses around the branch network.

Anthony Rose
Executive Officer

In relation to your question around the rollout of the new system, if you think about a traditional bank that, let's call it, is growing at system growth rates and I have a preexisting digitized platform and you're changing them onto a new system, they will naturally be some indigestion training, learning, shifting to new systems. To be honest, whilst we have to go through that exercise, the processes that they have to go through today are that manual and that archaic that, that degree of impact that you would naturally see in a change over of systems for a frontline, given what we're going from and to, I think means that we're probably not going to see the same degree of slowdown that you otherwise would see. Not to say that we won't be immune to any of that, clearly there's a training requirement as we roll this out. But again, it will be progressive, so you'll have some parts of the network that will be on the new system reinvigorated, ready to go, whilst others are still on the old and will be a transition over that course of the rollout.

Karyn Munsie

Former Group Executive of Corporate Affairs, Investor Relations & Government Relations
Okay. Any more questions on the floor? No, I don't think we have any questions on the phone. Last chance for question? No? In that case, we will leave it there. Thank you very much, everyone.