Question and Answer

Unknown Executive

[Operator Instructions] Jarrod Martin.

Jarrod Martin
Crédit Suisse AG, Research Division

Jarrod Martin from Credit Suisse. Andrew, you talk about closing the ROE gap with the peer group. Would you give us the ROE target?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Well, we've got to improve the ROE, Jarrod, address these legacy assets. You can see, the capital we've got, the returns that we're getting. And if we can deploy that back into the Australia and New Zealand franchise, you can see the ROE there. So we're going to improve the returns for the group.

Jarrod Martin
Crédit Suisse AG, Research Division

So I take that as the 17.2% ROE is the target for NAB under the current capital regime at least?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

At least. So our target here is -- what we're saying very clearly is to improve returns and close the ROE gap to peers. That's what our plan is. And we've got a plan to do it and that's what we intend to execute.

Jarrod Martin
Crédit Suisse AG, Research Division

But why isn't 17.2% the target? Your chairman surely should be asking you 17.2% at least and by when.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

So I'm going to repeat what I said. We don't give forecast...

Craig M. Drummond
Former Group Executive, Finance & Strategy

We don't give forecast to target, you know that.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

[indiscernible]

Unknown Executive

Jon?

Jonathan Mott
UBS Investment Bank, Research Division

Jon Mott from UBS. A question. You'd pointed out some good information, 2/3 of the revenue in the Business Bank is coming from the specialists and the SME, health, agri. And that's a real focus. But when we listen to a lot of the other major banks and regional banks, they say the same thing. 1/3 of the revenue is coming through from property, corporate, institutional and other areas. But when you look at Slide 16, that's where all the balance sheet growth is coming from. So is the challenge that you might end up being that you're continually focusing on an area which is very profitable or you're very good at, but really isn't growing much and is going to see ongoing margin pressure given the competition. And the areas which are growing, you've deemphasized and we'll just say further revenue pressure coming in the Business Bank, how do you match up the areas you're focusing on and the actual revenue growth opportunity?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Well, I'll kick off and then maybe Craig, you can add. So on the areas where we've got 2/3 of the revenue growth, you can see the revenue growth is positive. And whilst the system growth isn't significant and we expect lots of competition and limited growth going into the short-term future, I think if you come back, Jon, to the share of wallet slide. What we've got there is we've got 2/3 of the client's banking wallet. So we've still got a lot of room to grow in those. And that excludes, if you like, ancillary and other income from FX and interest rates and wealth products. So we still think that executing and focusing really well around the bits where we wish to excel and wish to be really strongly invest, we think there's opportunities to still expand returns.

Unknown Executive

Richard Wiles.

Richard E. Wiles
Morgan Stanley, Research Division

Richard Wiles, Morgan Stanley. Andrew, it's refreshing to hear NAB management acknowledge the weak performance of the business bank in the past year or so. It's also encouraging to see some stability in this result. I've got a few questions about the outlook. Firstly, Jon just mentioned that split of revenue. Do you think you can get some material growth in revenue? Or do you think that, that 1/3 of the business property, corporate, et cetera, remains a headwind? Secondly, Craig mentioned competition several times. What's the outlook for the margin? Do you think they can -- in the business bank? Does it continue to go down or is there some potential offset from funding? And thirdly, in this result, the loan loss charge in the Business Bank was relatively stable. Even though credit quality is improving, would you say that loan losses in Australian business banking have bottomed?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Thanks for the one question, Richard.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

2 or 3 questions, Richard. In relation to the institutional bank, I think that's where you're going, we weren't -- we're not looking to grow cash earnings per se. We're looking to grow returns that will be a combination of sensibly -- we're looking sensibly to deploy our capital from a risk return point of view, where we can get the optimal outcome. Now for some customers in institutional bank -- many customers in institutional bank, looking at a total relationship return, it does make a lot of sense. And as we've said before in, for example, commercial real estate, to some of the larger commercial real estate players in the institutional bank, we're very relaxed at a total relationship return. But we're not going to simply -- if there's no credit growth or minimal credit growth in the rest of business and there's very low ROE credit growth in the institutional bank, then we're going to be very selective. We're not simply going to go after a cash earnings number. We're going to go after an optimized return. In terms of the Business Bank margin, we won't give -- clearly, we won't give a forecast other than what we've said, and that is that in the past 6 months, the trends of what we've seen in the last 6 months, we expect broadly will continue. It's a competitive marketplace. But both on -- from a Wholesale funding point of view and from a deposit funding point of view, we are getting quite a lot of offset. So that 1 basis point decline we've seen in the Australian bank margin in the last 6 months is actually -- it's an encouraging number. It's certainly better than the 5 basis points we've seen previously.

In terms of the Business Bank loan-loss charge. It did tick up a bit, but I think we called out in the 6 months to March, we had a reasonably solid write-back. We had one write-back in the Business Bank that was meaningful. And so I would look through that and say we're actually not seeing a significant change. It's still reasonably benign environment in Australian BB. We've had 1 or 2 -- in the second half, we have 1 or 2 larger-than-normal charges well on BB. So I'd say net-net, it's a fairly -- remains benign, and not significantly different second half versus first half.

Unknown Executive

Okay. James?

James Freeman
Deutsche Bank AG, Research Division

James Freeman from Deutsche Bank. I just wanted to ask on the U.K. We've heard this a few times that the U.K. is a noncore asset. Just an idea on timing of the exit and just how you're going to manage the risks around that. I mean, you've now told the market you're exiting. You've told the customers, of course, that you're exiting. If this is a prolonged time period, you do run the risk that deposits start walking out the door well before you can match the lending and what point you can find a buyer. Can you just talk to us about the timing of this and how you're going to manage the risks around the exit of the U.K.?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Yes, so James, obviously, in coming to this point today we've done a lot of careful thought in management of understanding what those risks are and engaging with the relevant parties to make sure that we can make the statement confidently. We've obviously spoken to -- not just to the NAB Board, but the U.K. Board, the U.K. management, regulators, ratings agencies. So we've gone through a very thorough process to be able to make this statement today. And what I'm really signaling is clearly that's an intent to exit, but we've got to go through a very methodical and disciplined process. And once we do that and we can make an announcement, we will. But I can assure you, that's a priority. It's an absolute priority for us. And it will continue to be so until we can resolve the issue.

James Freeman
Deutsche Bank AG, Research Division

Sorry, Andrew, it's been a priority for over 5, possibly 10 years. I mean, are we talking about 5 to possibly 10 years?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

You're talking as long as it's going to take to get it addressed properly so that when exiting, we can manage the risk properly and we can get the shareholder the right return. So...

Craig M. Drummond
Former Group Executive, Finance & Strategy

James, I think the -- clearly, we have seen, to Andrew's point in his presentation, we have seen some significant changes in the environment, both in the markets environment, the economy, the underlying performance of the bank. I take your point and there are points that we've discussed internally. But the operating environment is completely different today for the U.K. than it was 3, 4, 5 years ago.

James Freeman
Deutsche Bank AG, Research Division

Has your price expectation changed?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Well, you can see the price that is in the market now for TSB [ph] as an example.

Unknown Executive

We might just check the phone for any questions.

Operator

[Operator Instructions] And your first question comes from the line of Craig Williams from Citigroup.

Craig Anthony Williams
Citigroup Inc, Research Division

You've demonstrated a degree of urgency in your efforts to clean up noncore assets, and I think that certainly is going to be welcomed by shareholders. When I look at your core business, the revenue growth is absent, particularly in the side of the business bank, where it's been flat to falling for 3 years now. Underlying cost outcomes look okay, but you've flagged a need for ongoing investment and have flagged rising amortization charges next year. And credit costs have probably surely improved, but they have also surely bottomed, given the adoption of IFRS 9. But my question is how much urgency do you give and can you give with all that you've got on your plate for the revenue performance of the core franchise and what sort of initiatives can we expect in the next 12 months in this respect?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Craig, Andrew Thorburn here. Thanks for your question. So really, we are indicating here that if you look at the Business Bank and where it's been in the last period, stabilizing in the last half, we are refocusing back on the segments which we believe are going to generate the right returns for us in the next year and beyond. So I think we're really focused on improving here, and we've got some efficiency opportunities. We're investing -- I've shown a few areas we're investing not just in people, but in technology and innovation. We're going to address the fulfillment centers, which I think are a drag on our performance and the experience in the short term. But obviously, we're not going to give a forecast about where we think this business is going to end up in 2015. I'm partly saying that I think there is some opportunities here with share of wallet and stabilizing people and capability and those fulfillment centers, which are going to enable us to get competitive growth. But it's a very difficult, challenging market, not just in terms of system growth, but in terms of all the domestic and offshore players who are in this market. So we do have some specific things that we're going to execute. They are on 4 -- 2 or 3 slides that I've mentioned. We will focus on those, and I think it's going to help the business get stronger in 2015 and is going to start to invest back in this business, which as we go forward in multiple years, is going to be a really important driver of returns for the bank.

Craig M. Drummond
Former Group Executive, Finance & Strategy

It's your namesake. You can't just -- can I add 2 or 3 things to what Andrew said? I did highlight an $80 million reduction in income in FY '14 from the legacy asset sales -- or legacy asset rundown, that's had an impact in the current year. I did also highlight $127 million reduction in markets income, which partly was CVA, FVA related. So I think that's one important message when you look at the current revenue outcome. I think another important message is we won't manufacture revenue for the sake of it. But Andrew had made it clear around maintaining credit standards where we need to maintain them. We spend a lot of -- the organization has spent a lot of time and effort in getting its asset quality, and there's more work to be done, but getting its asset quality into better shape. So the last thing we want to do -- go out and do is do something silly. And I think the third point is we're looking at about building something that's sustainable. So we are focused on where we have core advantage, investing where we have core advantage. And if there happens to be no revenue growth in the market in the short term, well, that's okay, we'll continue to look at market share opportunities, we'll continue to look at investing in those pieces of the business where we're really good.

Operator

Your next question comes from the line of Matthew Wilson from JCP.

Matthew Wilson
JCP Investment Partners Limited

Asset quality seems to be backward looking, therefore, could we look at one data point that has changed adversely? Or I have got an example of something that NAB has got advertised. I have seen [indiscernible] got a full-page advertisement in the Australian Financial Review highlighting those successful funding of the Roy Hill project [indiscernible] the iron ore price in Australia is $120 a ton or thereabout. Today, it's $77. However, mine researcher Wood Mackenzie has Roy Hill cash cost at $55. So that excluded freight, CapEx and other costs and, more importantly, debt. So what level of comfort can you give shareholders that we won't lose money from your [indiscernible] iron ore. And more generally, upon assuming the role of CEO, can you give us -- can you give shareholders some comfort or some color as to the nature of the credit file review you would have undertaken, where you're comfortable and where you're not?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Okay. Matthew, Andrew Thorburn here. Well, this is definitely going to be -- take 2 of us to answer, so I'll kick off. And obviously, we're not going to comment on individual customers or sectors. But we're a bank that has got a lot of skill and capability in assessing risks in all clients, including corporate clients. And yes, we bank lots of Australia and corporate Australia. And so we go through a very disciplined first, second and third line review of that. We, obviously, look at the risk in the business, look at the returns we need, and we're, obviously, making provisions as we go for the total book. So we're very focused on the right risk assessments. We're, obviously, very focused on the right returns, and that's what I can assure you of. And you would expect that, given the experience we've got and the size of our book, particularly in the corporate sector. And Craig is going to add if he wishes.

Craig M. Drummond
Former Group Executive, Finance & Strategy

I think you've covered them right.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

No, he's not going to add.

Ross Brown

Just one more final question.

Operator

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

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

Your recent disclosures mentioned that the U.K. regulator is conducting an enforcement process in relation to PPI mis-selling. Now that's usually code in legal circles for disciplined reaction. It's not clear what this enforcement process is about. Can you tell us what steps the regulator over there has taken and what the regulator is concerned about?

Craig M. Drummond
Former Group Executive, Finance & Strategy

I'm in danger of getting -- I'm looking at my legal counsel in the room here. He's giving me a bit of eye contact. Talking about enforcement issues are always a bit tricky, so I think the whole -- let me talk about it in an industry sense. The whole industry has been now providing for PPI for a number of years. So it's clear from that, that the industry has probably not done -- in the early days, not done the assessments that the regulator -- the right assessments that the -- in terms of the eyes of the regulator, may have assumed that we would have done. As a result, I think you'll see this is not an uncommon practice in the U.K. at the moment, where the regulator is looking at enforcement-related actions for a range of financial institutions as a result of those past attempted remediation actions. So in terms of giving any further quantity or whether it relates to fines or whatever, there's just a very high degree of uncertainty, but this is an industry-related issue and not a NAB-related issue.

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

So it's -- that's where it seems that this is still an investigation and no legal notices or fines are on the cards just yet?

Craig M. Drummond
Former Group Executive, Finance & Strategy

I think the investigation is ongoing as it is for the industry. And if we had anything to tell you, we would clearly have disclosed it.

Ross Brown

Okay, we'll go back. Andrew Hill?

Andrew Hill
BofA Merrill Lynch, Research Division

Andrew Hill from Merrill Lynch. Just a question again on the U.K. Presumably, you can't exit that business until you've addressed the issues around conduct. Can you maybe discuss what is on the cards there? And Craig, you mentioned TSB as one comparable there. We did see an indemnity provided by Lloyds Bank during that IPO process. Is that something you're contemplating through the exit of Clydesdale?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Andrew, let me take the second part of your question first. That's a good question, and Lloyds did provide an indemnity. Look, we -- it would be premature for me to make a comment on that. Conduct is clearly one of the -- you're right, it's one of the significant issues that we have with -- and you would expect that we are discussing those type of issues, both internally and with our regulators. So you would also note that we have made some substantial additional provisions for conduct in this release. So we think, as of today, we are appropriately provided. In terms of what we may have to do, if anything, in the future in relation to conduct, I just can't comment. It's not appropriate for me to comment at the moment. I'm sorry, the first part of your question was?

Andrew Hill
BofA Merrill Lynch, Research Division

Presumably, you had to address conduct before you can sell the business because, presumably, now it's going to take on that uncertainty.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Yes, I think that's fair to say.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

I think there's, obviously, a number of issues that we need to address to be able to exit this properly. That's one of them. And as Craig said, from what we know today, we've absolutely appropriately provided for that. But as we go forward and we get an exit, we have to work through a number of things and negotiate a number of things to be able to exit. So -- but until we get to that point, there's, obviously, nothing more that can be said.

Ross Brown

Mike Wiblin at the back.

Michael Wiblin
Macquarie Research

Mike Wiblin from Macquarie. My question, really, is just around Business Banking. It's obviously a focus. You're putting more bankers in, but your competitors are attacking, as you said. As an incumbent, NAB is, obviously, vulnerable to poaching. So is there a danger here that cost growth is higher than you expect as you defend the franchise? And do you have a sense as to whether NAB pays more or less than the competitors on The Street for business bankers? And as a result, is that going to cause you some trouble as well?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Yes, thanks, Mike. So yes, look, we are signaling this is an important franchise, and we need to invest not just next year but sustainably to build the franchise that continues to be competitive. On the cost piece, look, I think we've found -- one thing we have shown is that we can manage costs as a company and be disciplined around that. We're lifting the bar in the sense that we're saying that we want to get, within the cost increase we've got, productivity benefits of around $100 million to $150 million a year so that we have, then, the flexibility to be able to invest in opportunities not just in the Business Bank but be able to invest back in the company. And if we can start to build that and be more disciplined about deploying it into returns that are well above their cost of capital, we're going to get improvements. Now on the Business Bank itself, we are the #1 business bank, so we're obviously going to be under target. We have been, and we will be. And that's competition. And we want to be able to be good enough to retain the right people, hire them and retain them because they can see not just being paid competitively, which I think is in the case, but building a career and dealing with some great clients in Australia and being well waged having good products and services. So I think our proposition for our bankers is much broader than pay. People always talk about pay. It's usually a reason for them to leave if they get poached. But underneath it all, it's a symptom often of something else, which is their engagement, their training, their capability, their leadership, they've got the opportunities to work with much more streamlined processes and better technology. That's what we're working on. So I think we've got -- still the #1. We're being targeted, no doubt, because I think we've had some things which we probably -- we haven't implemented as well as what we should have. There's no doubt that's caused some friction and pain for our people, and competitors are targeting us. But our way to get back into this is not to panic and to deal with the cause of it and invest sustainably to continue to build the franchise so we're #1 well into the future.

Ross Brown

Andrew.

Andrew Lyons
Goldman Sachs Group Inc., Research Division

Andrew Lyons from Goldman Sachs. Just Slide 37, in your pack, you note that the ROE for your Wealth business is below the cost of capital, but that ignores the economies of distributing through the branch network. I guess, just in a light of that comment, can you perhaps make some further comments just on the extent to which you see banks, and particularly NAB, as natural loaners of wealth in particularly large businesses?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Thanks, Andrew. So we are saying some things here today that are important, and that is that this -- the business here, improving, and the products and services for us to win in the -- our segments that Michael was referring to earlier, that I've been talking about, is we have to have those 2 to sustain that, return and improve it, right, otherwise we're going to risk the core franchise if we don't have these products and services. But it's also clear, with the way capital is being treated and it's likely to continue to be treated, that we're not going to be able to see our way through to be able to get above cost of capital and the returns that our shareholders need. So all we're saying today is we are going to focus in, in a very disciplined, prioritized, methodical way to work out how we can address that issue. We're not saying today how that will happen or when that will happen, but we're saying that, internally, a few of us are clearly working through what that means. The goal is clear, but the goal is difficult, right? The goal is difficult because we need these products and services, yet we need to liberate some capital to get better returns. So there's the conundrum that we're going to work with. It's important because the capital issue is a material one. So it's a priority. It's going to be disciplined. And when we've got more to say, we will.

Ross Brown

Brian, you've been waiting patiently.

Brian D. Johnson
CLSA Limited, Research Division

Brian Johnson, CLSA. Andrew, the great tragedy of today is we haven't got a few of the other CEOs of the Year sitting on the stage or CFOs or board members or chair people. In the year 2000, which I think you'd agree was a long time ago...

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Yes.

Brian D. Johnson
CLSA Limited, Research Division

NAB made EPS of $2.15. Today, we sit here, and it's $2.16. I think under any measure, that is well short of woeful. If I had the time to -- and you did say we are going to have a very frank discussion. If I had the time to ask 2 questions, a sub-question I would ask, Wiles this is your approach, would be on Slide 21, you mentioned about how you might have put some more core capital into the U.K. You're talking about basically selling it. I'd like to understand how much that capital would be and whether you can actually fund that with debt. But that's not the question I wanted to ask. The official question is that when we have a look at Slide 37, you say that you're committed to wealth distribution, which sounds to me as though you're not so committed to wealth ownership. But more to the point, I can't say too much comment there on the life insurance company. On Slide 14, you say the ROE is 17.2% in Australia. Slide 18, you talk about how it's not impaired. But when I actually go through to the capital adequacy slide on Page 109 -- on Page 109 of the result, and I apologize for these numbers going to be a little bit out, but you've got to have something approaching $4 billion of tangible equity in there. I'm guessing around $300 million is the investments business, which is good, which means you got a bucket load of tangible equity invested in the life insurance company, which is bad. We add on to that, basically, the $4 billion of wealth management goodwill, we're giving an ROE of something like 4%, 5%. Even if you back out the goodwill, it's still well below it, and that's giving it the benefit of the investments business. So when you tell us that the goodwill is not impaired and that the value has actually gone up, it sounds kind of fanciful to me. And I'm just wondering, is this -- was this basically audited by the same person that said when NAB took the gigantic synthetic CDO write-off, that those tax benefits, you were bound to get the revenue in the future, so you didn't need to write it off? So if I could condense all of this, is there some degree of embarrassment at the board level about not really fessing up and taking what is probably the biggest hit of all time, which is writing down the life insurance business to what it is genuinely worth, what is genuinely realizable? Because I got to say, I for one, would actually flag that as being a very positive development because it means bugger all. But it means when we're talking about the 17.2% return on equity in the Australian business, it's a bucket load higher than that. Your response.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Thank you, Brian.

Unknown Executive

He really meant Frank.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

No, thank you, Frank [ph]. And this is definitely a CFO question.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Thank you, Andrew. Brian, can I make the point that the life earnings are at, arguably, but they are the cyclical low. And when you do the valuation, you don't do a spot valuation, as you know, on the current earnings with the discount rate. You do it on a -- looking out from -- for an extended period of time. And the discount rates really haven't moved. So the discount rate, what we're saying is the discount rate is essentially unchanged. Earnings are up and we're at a cyclical, arguably -- I agree, arguably, we're at a cyclical low in the earnings cycle. So when you do your NPV or, we accountants call it, value-in-use, there is no impairment. It I understand you're only working on the publicly available information, but we don't see an impairment at this point in time.

Brian D. Johnson
CLSA Limited, Research Division

So Craig, what you're really saying is we should expect the most gigantic rebound of all time in those life insurance earnings over the next few years?

Craig M. Drummond
Former Group Executive, Finance & Strategy

I can't give you a forecast, Brian.

Ross Brown

Scott.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

I'm not sure whether this cancels my question or not, but just following on from Brian. Some companies prefer to disclose sensitivities to a goodwill impairment. For example, future growth rates would reduce by X percent before impairment comes into question. Do you approve of it, allow to provide those sensitivities to the market?

Craig M. Drummond
Former Group Executive, Finance & Strategy

We haven't done historically. I think what I would say is -- Andrew said that we're looking at all options in relation to the capital intensity in the business. And one would hope through that, that we find a way in -- and I'm not going to put a time frame on it, but we find a way to liberate some capital.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

And that was -- so that was just -- finishing on Brian's question, my question is actually on executive remuneration.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Oh, so executive remuneration.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Yes, that's -- this is my question.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

You 2 shouldn't sit together.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

So if I revert back to your statements, when the write-downs were taken, there was a very clear indication that, that would be taken into account during compensation reviews. If I look at the compensation disclosures, the performance-based remuneration is actually up $50 million or 10% year-on-year. So can you talk through the transparency there, the accountability that you're so focused on and how that's ultimately been reflected in the remunerations period.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

All right, I'll kick off.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Yes, go for it.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

So yes, absolutely, I did say that. And you would expect that to be followed through on because it's clear that we have not met our goals, and we've had a material reduction in shareholder returns for this year. And today, we've announced inside the company that the bonuses going to paid to our people and, particularly, to the senior people. And particularly, the CEO, is going to be the lowest they've been for some time. So we're definitely following through on that. And when you see the annual report and the KMP, you'll be able to get that verified. So that's definitely the case.

Craig M. Drummond
Former Group Executive, Finance & Strategy

In relation to the statutory numbers, those statutory numbers, obviously, will include things like deferred compensation coming from one period or from a number of years ago into the current period. That will include the normal under and over accruals that you have on compensation decisions. So they have the right numbers, obviously, but they reflect a whole range of things. I think Andrew's point is when you see the remuneration report with the key management personnel, then I'm sure Andrew would be very keen and happy to have a conversation around the accountability that, that's indicating.

Ross Brown

Victor?

Victor German

It's Victor German from CBA Equities. Under the umbrella of changing time, I was hoping to clarify 2 points. First, on the NextGen program, it sounds like there's, obviously, this review that's taking place, and it sounds like it hasn't been finished yet. Your approach to investment appears to have changed. Should we expect to see, one, potential further reductions in capitalized software balances, and two, if you're out of the budget or original budget that was allocated to the program, should we see ongoing increases in expenses allocated to technology? And second, the changing tone is around business bankers. You were highlighting that service is, obviously, very important in that part of the business. And over the last few years, you've gone through quite significant change in addressing low growth environment, trying to reduce your cost base in that business. Why do think that model is appropriate going forward? And why shouldn't you have changes to that model, which, once again, will lead to significant increases in cost base in that part of the business?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Victor, I'll take the second one first, and then we'll go to Craig and comment on the cap software, and I'll do an introduction on NextGen. So we think the model we've got, Victor, in the Business Bank is the right model, and it's sustainable. We've got our business bankers working on broader portfolios, and we've got a series of specialists who work on things like agri and health, government, education, we've called them out. Also, we've got some other product sales specialists in the wealth and markets side. And we've invested a lot in getting that to work together, and I think it's increasingly working together. And we haven't seen the full fruits of that pay off. So I think the model is the right one. What we do need to get right is we need to make processes simpler. We need to build more bankers back into the front line because we've let them run off. And importantly, we're calling out the service and fulfillment center. We need to make sure it works. As I said, the vision is right, but we haven't executed it well enough. And today, it's not working any way near like what our customers and our frontline people need. And we're going to keep investing in technology. I talked about some of those innovations that we're going to do. So I think the Business Bank core, the model is right. We haven't executed parts of it well enough, and we haven't invested enough in it. But I certainly think within the cost envelope that we are indicating, total sort of investment spend of about $1 billion and about $8 billion in the bank for a year, within that, and within the productivity dividend that we're going to generate. We can invest back in a disciplined way back into the business, not just the Business Bank, into other parts of the bank. So I think the model is sustainable. I think we've got good management of costs. We're starting to generate more focus on productivity dividends, and I think that will be how we're going to execute the plan. On the NextGen piece, just a slight introduction. So we are going to focus on this Personal Bank origination platform, in addition to that NAB New in FTP. So what has changed is that we've learned that we can't run multi-year commitments of technology projects, and we can't get the sequencing of change incorrect. We've got to focus on a few things that are significant and do them well, right, because they pass through the process and affect all our frontline people. And we don't get that bit lined up right, which I don't think we've quite got that sequencing right in the past, it really causes some mayhem, right, and impact on our frontline people. So we're going to focus on the 3 things in the middle. That's what we're going to execute. We're going to land those. We can see clear line of sight on what we're going to spend, which we've already budgeted for, with some benefits, which we're going to bake in. We know who to hold accountable, we know what needs to be done, so we're going to focus on executing those. Now on the cap software piece and write-down question, Craig, perhaps you could answer.

Craig M. Drummond
Former Group Executive, Finance & Strategy

So on the cap software, the NextGen component of cap software currently is about $850 million. We, I think, historically, have given a target for a cap software to peak at about $2.5 billion. I'm not inclined to be talking about forecast on cap software because, frankly, who knows, in 3, 5, 7 years' time exactly, Andrew has talked about some of the priorities, we will look at -- we've got some priorities we need to do now and finish without -- personal use products is a good example on the transformation program. But we're going to be making other decisions based on the competitive allocation of our resourcing in 2017, 2018. So I think giving a forecast, I could give you a forecast, Victor, but I'm not sure how good it would be, frankly. But for all intents and purposes....

Victor German

Better than mine.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Sorry?

Victor German

Your view is better than mine.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Yes, but for all intents and purposes, the number that we have put out there of $2.5 billion, it's sort of there or thereabouts. But frankly, I'm not -- as I said, I'm not inclined to be putting my nasty -- nailing my name to a forecast on cap software, where there's just too much variability looking out over the next 5 to 7 years.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

But can I -- Victor, just to add, I think if we had or felt there was a need to have a write-down in NextGen, we would've done it, right? So what we've got in use, we see it being carried forward. And also, just a completely separate point, our change in policy, which is important, that we're putting everything above the line, right? So that was a decision we've made. We've restated some of it for -- back to 2013, and that's our policy from now going forward.

Victor German

Sorry, just to confirm your point about bringing this smaller project, delivering on smaller projects in time, does that change your budget at all in terms of what you...

Andrew Gregory Thorburn
Former Group CEO, MD & Director

No.

Victor German

So you still think that you will fit within your...

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Yes.

Victor German

Fits with your budget.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Yes. And that one's -- that Personal Bank origination platform is already well underway. And we're moving into final phase of preparation and execution. So that one's fully funded.

Ross Brown

Brett Le Mesurier, Sr.

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

So I've got 2 questions, actually, Craig, but they're simple ones. The additional regulatory methodology change, which led to the $591 million reduction in common equity Tier 1, could you tell us what that was?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Sure, a large component of that was, obviously, the level 2 changes that we had thrust upon us by the changing interpretation from APRA on capital. Secondly, there are a range of APRA methodology. We have conversations with APRA, as the other banks do, conversations with APRA all the time around bits and pieces on our capital base and interpretations from APRA. And that's really what they are. But that level 2 is the primary issue that you should focus on.

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

Is there a chance that there's going to be another chunk coming through in the next half?

Craig M. Drummond
Former Group Executive, Finance & Strategy

We're not expecting so. Look, the regulatory landscape, both at a global level and a local level, is always changing, but we're not expecting any adjustment. But as I've said, we put an 8.75%, 9.25% number out there, and we are comfortable that we're well on track to make that target.

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

And what is the split of capital between your investments and insurance business in wealth?

Craig M. Drummond
Former Group Executive, Finance & Strategy

The split of capital between our investments and insurance, I'll come -- we'll come back to you on that, Brett. I can give you a number, but I'd prefer to have it accurately stated.

Brian D. Johnson
CLSA Limited, Research Division

[indiscernible]

Craig M. Drummond
Former Group Executive, Finance & Strategy

Yes, it may not be. We'll come back to you. Same with you, Brian.

Ross Brown

I think we've got some more questions on the phone. Let's just check the phone, please..

Operator

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

Craig Anthony Williams
Citigroup Inc, Research Division

You've been -- I'm referring to Slide 31, the NextGen slide again, please. You've been going 6 years now on NextGen, and you've spent a lot of money on the project, investing, perhaps, wealth there of a couple billion dollars or so, so far. Yet when we look at what's slated for 2017 plus, it's the bulk of what shareholders, perhaps, would have been hoping this investment would bring to the table. And you've also indicated, I think, that this longer-term ambitions are fluid. But given the manner in which technology is changing and evolving, there's a strong likelihood that the bank ended up retaining significant legacy systems.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Craig, it's Andrew. Yes, we have been underway on this for some years, but it's a -- it was an ambitious and it's a complex task. And as I said earlier, I think we've actually built some things, which should not be dismissed. And actually, we believe the standing's in good state for many years to come. Having said that, I do acknowledge today, I suppose part of the message is that we have underestimated how difficult it was going to be. But on the point of benefits for shareholders, I disagree in part because if we deliver those thing -- when we deliver the things in the middle column, they will have significant improvements in the customer experience, in costs and productivity and, therefore, will be very important for returns to shareholders. So I think that is -- it's not into the future we're getting the benefits, we're getting them now. And when we nail the bits in the middle column, we'll get more. Coming to your end point, I am saying, we have to be flexible. I think one of the areas we've made is making major statements about it will take this long and cost this much, and we have got to be more realistic about that now, and I'm saying that. But on your point around legacy systems, no, eventually, we need to retire these and turn them off. So that's definitely going to happen. It's just a matter of when that happens and in what sequence. Because apart from -- well, the main reason will be that we will take not just complexity out of it, but we'll save money. So we'll definitely do it. But when we do it, I think we need a little bit of flexibility, and that's really what I'm indicating.

Operator

Your next question comes from the line of Matthew Wilson from JCP.

Matthew Wilson
JCP Investment Partners Limited

As Richard alluded to, the acknowledgment of issues and focus on the core Australian Bank is refreshing and welcome. But how do shareholders measure you and your team's success with its -- with your strategy and its execution when we continue to no longer understand the full profit and return performance of the critical business units that it comprises?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Matthew, it's Craig here. We've had -- I think we've had a conversation along those lines before. What we've aimed to do, we -- in the release that we -- you have in front of you, I'm not sure whether you had a chance to go through it, we have now provided our Business Banking revenue; we've provided Personal Banking revenue; we've provided Business Banking B&DDs, Personal Banking B&DDs; we've provided Business Banking -- sorry, business lending margins; we've provided housing lending margins. I think you can see -- and if you work through the slides, there are a range of other disclosures there that -- elevated disclosure on what we had at the first half. So I'm happy to have a conversation with you, as we did after the first half, to go through and address what additional things you've got. But we -- with managing, that's not the way we manage -- we're no longer managing the business to our Business Bank or to our Personal Bank, end to end. The Business Bank management has -- runs the customer relationships and the customer piece for the Business Bank. Gavin Slater runs the customer piece for the Personal Bank. Anthony Cahill runs the products and services that are provided into those businesses. But we do run one Australian Bank.

Matthew Wilson
JCP Investment Partners Limited

Given your emphasis on ROE, how do you assess the individual returns of those businesses? A simple, complete P&L would help shareholders tremendously.

Craig M. Drummond
Former Group Executive, Finance & Strategy

We have a simple, complete P&L, though, by the Australian Bank. If we look at the Australian Bank ROE, we also look at the ROE by products. So we know, for example, the ROE on the personal loans, on credit cards, on housing loans. So we know the products that Gavin and his team are selling, the returns that they're driving. We also know, by product in the Business Bank, what sort of return we're getting in the institutional bank, what we're getting in the SME part of the bank, what we're getting across a range of the Business Bank products. So that's the way we manage the business, rather than saying we want a specific Business Bank P&L, because there are so many interdependencies and relationships between each of these pods, that we think it makes much more sense to run it as one Australian Bank.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Matthew, [indiscernible].

Matthew Wilson
JCP Investment Partners Limited

Sorry?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Matthew, sorry, you're going to say something, but it's Andrew here. I just want to, I think, wrap that up and just land a couple of points, and that is that, firstly, the model is working and can work. And I've worked in a bank all my career and, like many people, have worked in different models. It's really not the model that makes the difference. It's the people in the model. And I think we've been through a lot of change in the last 18 months, and I think the bank is getting more settled, understanding it. And I think it actually could be a competitive difference for us as we go forward because of the flexibility it affords us. But I think the model is in, it's working, and I think we've got the team that really can nail it. So the other point I wanted to make is that we have tried to -- we have improved the reporting and the information we've given you this half. We heard that feedback, and I think we've changed it. And I think the improvements that Craig referred to are quite significant and numerous and, I think, should give you a very clear line of sight about the performance of not just the overall business but bits of it.

Ross Brown

I think we're done on the phone. Are there any more questions in the room? A couple more. Brian?

Brian D. Johnson
CLSA Limited, Research Division

I'll make this really quick. The sub-question that was never answered about the U.K. core equity Tier 1 that you're referring to in Slide 21...

Craig M. Drummond
Former Group Executive, Finance & Strategy

Yes.

Brian D. Johnson
CLSA Limited, Research Division

Craig, how much are we talking about? And is it really going to be real equity? Or can you turn debt into equity? And what happens if you sell it, so what does become equity then?

Craig M. Drummond
Former Group Executive, Finance & Strategy

So Brian, the numbers are yet to be determined, but we will need to -- the total exposure of NAB to the U.K. won't change, but we will need to swap some of the sub-debt into AT1 but also some common equity. So total dollar amount won't change, but within that, the -- compositionally, we will have a requirement to switch some of that some sub-debt into AT1 and equity.

Brian D. Johnson
CLSA Limited, Research Division

Will you have any more equity?

Craig M. Drummond
Former Group Executive, Finance & Strategy

Well, our exposure won't go up, but the common equity component will.

Ross Brown

Scott?

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Scott Manning from JPMorgan. Just a final question on capital allocations, ROE enhancement, that kind of thing. If you break down the businesses, you said you've got mid-single digit on a whole bunch of capital and good high-teens ROE on the rest of capital. Within that budget to get improving returns over time is, obviously, that you can redeploy the capital that gets released upon exit; whereas if I look at the sale in progress and potential sale of the U.K., it might be shipping back, call it, $5 billion, but you're also losing $400 million of earnings during the same course. If I then think of the headwinds to regulatory capital, you've got $2 billion against a level 2 wealth. If the minimum risk weight on the housing goes up to 20%, there's another $3 billion, you're at the bottom end of your range. So if you want to top that up, there's another $1 billion. So all the capital that gets released gets retained and is actually unable to be deployed, and you're still $400 million short because you sold businesses. So I'm interested in how -- the confidence that's extending from the ability to enhance ROEs over time.

Craig M. Drummond
Former Group Executive, Finance & Strategy

Well, I think you made a lot of assumptions there, Scott, some of which we may agree with, some of which we may not. But fundamentally, if we have $8 billion of equity generating 6% ROE, if we can deploy even half of that at a 20%, 25% ROE, we're going to have a material impact on the aggregate number. I take your point, though, that we're in a world were capital intensities has been increasing, so I can't give you a definitive yay or nay to your answer. All I know, though, is if capital intensity goes up and we've still got the 6% ROE businesses, our returns will go down.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

I suppose another way of asking the question is if there is net capital released above minimum capital requirements going forward, are you more committed to deploying that or returning it to shareholders?

Craig M. Drummond
Former Group Executive, Finance & Strategy

We will look at -- we will make that decision. I think it's premature to be making any sort of decision like that, but we don't want to run a lazy balance sheet. But equally, if we think we're in a world where you need to -- I'd prefer to run a slightly stronger balance sheet, slightly stronger capital position than a weaker one. That's ultimately where I want to get to.

Andrew Gregory Thorburn
Former Group CEO, MD & Director

And Scott, just any one thing, because I think you focused on bits around the legacy assets, which clearly we've indicated a priority. But in the Australia, New Zealand franchise, we've got capital deployed, and there is a spectrum of returns on that. And we're getting more granular around that. We're looking at 165 performance units. We got much more line of sight around that, and we are redeploying capital between -- in Australia and New Zealand now and I think in a lot more dynamic way, which is going to improve our returns and capability as we go forward.

Ross Brown

Okay, I don't see any more hands, so I think we're done on questions. So Andrew, do you want to make some concluding remarks?

Andrew Gregory Thorburn
Former Group CEO, MD & Director

Okay, so are we done?

Ross Brown

There's none on the phone, none in the room, we're done.

Andrew Gregory Thorburn
Former Group CEO, MD & Director
Yes, so everyone on the phones and in the room, if I could just thank on our team's behalf, particularly Craig and I, for being here and for your questions today. What we endeavor to outline is not just the numbers for 2014 but our plans and where we intend to execute going forward, to build a stronger -- not just a stronger business but better returns to shareholders. So thank you. And if you have any more questions, we look forward to receiving them and talking to -- you can talk to Ross and the IR team. So on that note, thank you. Enjoy the rest of the day.