Question and Answer

Operator

[Operator Instructions] Your first question comes from Brendan Sproules from Citi.

Brendan Sproules
Citigroup Inc., Research Division

I just have a single question just around how this business will be managed. We've seen in Australia that a number of banks that have undertaken running multi-brands within the single organization has quite diverse product offerings across these brands, diverse IT and even diverse servicing offerings. I was just wondering how different ME Bank being managed within the Bank of Queensland umbrella will be.

George Frazis
MD, CEO & Executive Director

Thanks, Brendan. And you raised really important points in terms of -- the reason why we're particularly excited about this opportunity is that if you think about what we're developing in terms of our Temenos core banking platform within VMA, this is the latest version of that platform. It's cloud-based. There's no customization. And what it enables us to do then is to make sure that we've got an ongoing upgrade pathway to leverage their global investment in innovation. And what we've done is we've built that system in a multi-brand approach.

So we know the end state. It doesn't change that strategy. The beauty of the ME Bank acquisition is that because the data architecture is consistent and they're on version 18, we can easily schedule them into the transformational program. So the end state is known. It hasn't changed. We'll have all 3 brands effectively on one core banking platform, which is really exciting and very distinct.

Now there's a number of synergies that you had just laid out. But what we haven't actually talked about is at the end of 3 years, when we get to that point, we've got a banking platform that is really efficient and also able to be -- to add innovation for our customers. That puts us in a really strong position, which we're excited by.

Ewen Stafford
CFO & COO

Yes. Brendan, it's Ewen. I just might add a couple of things in terms of how we're thinking about it. So given it is clearly a multi-brand strategy, where we have our people close to the customer, close to the brands, we'll continue that. And that is entirely consistent with how BOQ operates as it is at the moment with the BOQ Blue brand and VMA on the retail side and similarly on the business side.

I think from there then, the way the Temenos platform, multi-brand platform is being built, it does allow for a simplified and consistent product offering, but then that can be configured and nuanced at a brand level. And from there, we certainly will be looking to -- and as the technology integration continues then, to achieve more consolidation and consistency in the middle office, which I think was your point about servicing, and then certainly, and as I mentioned, within the shared service functions, as soon as we can, and including the consolidation of those different technology platforms that support those areas.

Brendan Sproules
Citigroup Inc., Research Division

Can I just ask one clarifying question on that just in terms of product offerings? I mean, we have seen Westpac and St. George really align their products over time. Other banks have done slightly different. What's your planning around the different product offers across the brands?

George Frazis
MD, CEO & Executive Director

Brendan, the way we think about products is definitely simplifying our product set and also simplifying the end-to-end process and how we streamline those. So as you know, what's really important, let's say, our mortgages and our time to yes, that's something we've been able to do extremely well. And we'll continue down that path.

The way that the system enables -- these modern systems enable us to design is that effectively provides us the scope to have the different elements of differentiation by the different brands within the one product. So this is a very simplified approach to product, terms and conditions and also end-to-end prices.

Operator

Your next question comes from Brian Johnson from Jefferies.

Brian D. Johnson
Jefferies LLC, Research Division

I was just wondering, could you run through the differential in the NIM that we see between BOQ and then ME Bank? The NIM looks a lot lower. Bank of Queensland historically has had a much higher benchmark rate than perhaps even the peers. So I'd just be interested if we could get some kind of walk-through of the difference on the NIM between the 2.

Ewen Stafford
CFO & COO

Yes. Brian, it's Ewen. I'll take that one. So you're right. The numbers are different. Suppose if I start at the BOQ, 1.91%, the first thing we need to do is adjust out for business mix. So we have an advantage there of about 30 basis points because of the business banking operations that we run. But then you just need to slightly net off about 10 basis points because of our branch network, and particularly, our owner managers and payments to them. So that then gets you to apples for apples.

And from there, Brian, the key difference is really about funding costs. And sort of as we look forward, and as I mentioned, we've obviously modeled those cost synergies, and they're represented in those accretion statements, but we have not put through those models opportunity on the funding side. And that's about circa 20 basis points. And we would see that about half of that being of a retail nature, and then the other half, wholesale funding advantages that the BOQ business has.

So that's basically the walk. And we do see an opportunity certainly to improve that 1.56% on the basis of those funding costs for the 2 reasons I outlined.

Brian D. Johnson
Jefferies LLC, Research Division

Fantastic. Ewen, if I'd just push my luck with a second related question, if we were to break this down into the trading update versus the acquisition. On the trading update, you're talking that for the first half, the margin is up, but you've delivered multiple system credit growth in the Housing book. Housing has got a lower margin than the business book. We're also -- once again, we're starting off with a higher reference rate. How do you have your margin expanding in the first half when, by its very nature, you must be embedding a bigger discount?

George Frazis
MD, CEO & Executive Director

Brian, the thing to note is actually, on the business banking side, we've done quite a bit of work. Although we haven't grown balances net-net,given where the market's at, we have actually done a good job in terms of improving margin and return of the business that we've held. So that's the first point.

And I'll let Ewen cover off some of the other.

Ewen Stafford
CFO & COO

Yes. I mean, Brian, we'll provide the full detail and the usual walks on the 15th of April. But just to really summarize it, what we've experienced in the first half, some significant tailwinds on the funding cost side. Now when we spoke at the full year, we did signal that we have been late relative to the market to reduce term deposits, particularly. And so we benefited from the benefits of that as well as, obviously, the wholesale funding side of it in the first half.

And then really, we've had the usual front-to-back book drag that we've been consistently calling out. And hedging cost and the benefit of that hedging cost has broadly been awash with the capital and low-cost deposits. So that's kind of the dynamics that have played out there, and then a slight few basis points drag because of the higher liquidity. But as I said, we'll provide that full detail in a month or so.

Operator

Your next question comes from Richard Wiles from Morgan Stanley.

Richard E. Wiles
Morgan Stanley, Research Division

I'd just like to understand your thoughts around growth in a little more detail. ME Bank has been around for more than 20 years. It's got $27 billion of loans. So let's call it sort of 1% share, that sort of level. So it's hardly been a high-growth bank.

And then you're talking a lot about the multi-brand strategy. George, that didn't work particularly well at Westpac when you were there. So what makes you think multi-brand will be a success at BOQ? And why do you think ME Bank will suddenly turn into a high-growth bank than it's been in the past?

George Frazis
MD, CEO & Executive Director

Thanks, Richard. Just to correct you on the Westpac side, when I was running the St. George Banking Group with 4 brands, we actually grew it to more than 1.7x system and maintained margin. But we're not here to talk about them.

If I think about what we've achieved over -- if you go back 18 months ago, BOQ was going backwards in mortgages. In 18 months, we've been able to turn that around. As you can see, for this current half, growing at 1.2x system. And in fact, our exit rate is close to 2x system. And this has been fundamental improvements, which is the end-to-end process, getting time to yes down to below a day. So we know how to do that. That capability can be applied across all 3 brands, firstly.

The second thing to note is that we've also been able to achieve that turnaround, number one, in our own manager branches, which is traditionally the hardest place to achieve growth. But now we're also doing extremely well in our third-party broking channel. So again, we know how to drive growth, profitable growth that is, with margin improvement in our third-party channel, which is 75% of what ME Bank's channel is.

So we have the capability to grow all 3 brands, and we really understand this business. This is a simple business, which is core to ours.

And then the final point I would state is all 3 businesses have yet to tap into the opportunity that digital distribution has. The starting point of this is effectively the launch of VMA's new state-of-the-art mobile banking app. That will initially primarily be transaction, savings and credit cards. But the next phase of that is mortgages. And that gives us yet a totally new channel for us to actually drive profitable growth.

And then the final point I should state is -- I do want to emphasize that what we're talking about is 3 brands on a common core banking platform that really simplifies everything beyond that front facing.

Operator

Your next question comes from Andrew Lyons from Goldman Sachs.

Andrew Lyons

Goldman Sachs Group, Inc., Research Division

Just a question on CapEx. Your integration cost of $170 million to $180 million, when combined with the capital investment targets you provided last February, would suggest you're certainly investing quite heavily in the combined group over the course of the next few years. I just was hoping that you could maybe talk to how you're thinking about return on investment in relation to that capital investment. And also has the capital investment requirements of the combined group contributed to the reduction in the targeted payout ratio for the combined group despite the fact that you did have ROE -- you're getting ROE accretion from this deal?

Ewen Stafford
CFO & COO

There's probably about 3 questions in that one, Andrew. So let me start with the -- to talk about the investment program, and then we'll come to ROE, how we're thinking about that and the interplay with the dividend payout ratio.

I mean, you're right. We do plan to invest in this business heavily over the next -- and consistently over the next 3 years. I mean, the BOQ, as you point out, we're in the midst of a major transformation and delivering positively against that. But the way I'm thinking -- the way we're thinking about the combined envelope is that it could well be up over $0.5 billion, so $500 million over the 3 years.

But I think it's important, just on those $170 million or just on those costs -- integration costs. So we are thinking, as I mentioned, $130 million to $140 million. At the moment, our intent is not to capitalize those. So we will put those below the line in the years incurred, and some of those, out of organic capital. The -- notwithstanding, it will be part of the integrated funding envelope.

I think from how Craig and I are thinking about that funding envelope, there will definitely be CapEx synergies as we bring those together. We've already identified $15 million, again, which is not in these numbers. But once we can get further under the covers and refine the planning, we are quietly confident that there will be further. So that's really on the capital program and interplay with that $130 million to $140 million.

Just in terms of the payout ratio, the comment I'd make there is we really feel 60% to 75% is a sustainable payout ratio. And it just allows us the flexibility, depending on the different growth rates that -- and where that growth comes from and bearing in mind the business banking side of our operations as well. So we think that's an appropriate rate of payout, just to manage that carefully.

And then just on the ROE comment, I mean, we have clearly stated, it's greater than 100 basis points accretion. We are -- I'm not going to be drawing on the target today, but we are targeting peer level ROE outcomes peer-leading in the medium term.

Operator

Your next question comes from Jarrod Martin from Crédit Suisse.

Jarrod Martin
Crédit Suisse AG, Research Division

Question on distribution and how you see that going forward. You said 25% mortgage managers and 75% mortgage brokers. So on the mortgage managers, will they continue just to be ME Bank sort of focused? Or will they be able to offer a broader suite of products?

And also, part of the attraction that those mortgage managers pushed was that not only are you getting a cheap mortgage, but it's benefiting your super fund because of the ownership of ME Bank previously. And so does that proposition does change now with BOQ ownership?

Then on the 75% that are through brokers. I note that AFG flows over the last 12 months have particularly halved. Now there was an issue at the start of the pandemic. So how's that going to be managed? And how the differentiation between the brands is going to be able to still offer you some form of growth?

George Frazis
MD, CEO & Executive Director

Thanks, Jarrod, and all good questions. I mean, the starting point in terms of distribution is that at the actual BDM level or mortgage manager level, we will be leaving -- definitely leaving differentiation by brand. I think it's important that those bankers and BDMs really focused on growing their particular brand.

Now above that, in terms of management, particularly when it comes to leadership in third-party, we will look at how that operating model works. The thing I would say about the third-party distribution channel is that what makes success in terms of growth there, one is certainty, that you're going to approve alone that you've approved previously. The second thing is that you actually do that quickly. And the third thing is that you've got a distinctive segment that the brand is attractive to.

So all those 3 things, we do really well. And the 3 brands that we're offering have a different customer segment target. So there's very, very little overlap of that. And what we end up having is quite a compelling offering, providing choice to the aggregators and the brokers.

Just on the link to the members. And obviously, we will want to ensure we are providing a compelling offering to the industry members. But it only represents around about 10% of the flow today. So it's not a critical part of the growth going forward. We definitely know how to run mortgage lenders, and we definitely know how to grow in the third-party channel.

Operator

Your next question from Ed Henning from CLSA.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

I've got a couple of questions, but I'll stick to my one. If you look at ME Bank, can you just run us through the front book, back book pricing difference there? And will that be less of a drag going forward than BOQ on your NIM?

George Frazis
MD, CEO & Executive Director

Maybe I'll start off and then hand over to Ewen, Ed. And thanks for your question. I mean, dealing with the front book, back book issue is part of life in terms of running a retail bank, as you can see. And we've been able to increase margin and deal to that within BOQ. So we'll be applying those disciplines across the combined business. And I'm really pleased that we've got very good capability in our product to make those trade-offs in terms of the price volume trade-offs.

But I'll hand over to Ewen to give you a bit more color.

Ewen Stafford
CFO & COO

Ed, the front book, back book differential is quite consistent with BOQ on our average portfolio number. So it's in that early -- in that order of the early '40s. So it won't have any impact from that perspective. And their pricing has not been overly aggressive on that side either.

So I think perhaps where the bigger differentials from sort of market averages is more on the deposit side, as I referenced earlier in terms of those funding costs drag. But we're very comfortable, and I think, very aligned on that front-to-back book impact.

Operator

Your next question comes from Azib Khan from Morgans Financials.

Azib Khan
Morgans Financial Limited, Research Division

George, you mentioned earlier that you're bringing together 3 strong brands. The ME brand attracted quite a bit of negative publicity around last July when ME announced a freeze on withdrawals -- home loan withdrawals for certain customers. Has that resulted in more-than-usual customer attrition for ME over the last 6 months? And what level of customer attrition, if any, are you assuming as part of the combined financial targets that you've laid out today?

George Frazis
MD, CEO & Executive Director

Azib, thanks for your question. You're right in the sense that the redraw issue did create an issue for ME Bank and its branding. In fact, if you look at the behavior in terms of NPS, ME Bank roughly was in third position, fairly similar to where BOQ and Virgin Money was at. They then dropped from that position given the issue. They did quite a bit of work to recover and contacted all customers. And I think although slightly slow to the party, you might argue they did a very good job to recover, and then it's come back up.

But I'll hand over to Ewen just to give you a bit more color around that.

Ewen Stafford
CFO & COO

Yes. Azib, just a couple of other factors. On Slide 33, on the top right-hand corner, there's a -- we've just -- where we lay out an overview of ME Bank, we've included the home loan growth. And so you can see they had some outstanding years, where they put in '17, $2 billion on the balance sheet; $1 billion in '18; and $2 billion between '18 and '19. So we are -- and then it plateaus a little into '20. And that's sort of how we're seeing '21 as well.

I think importantly, though, with a strong growth and also the margin management from the ME team, it hasn't had a big impact on profitability. It's more asset growth and then a step off into '22 consideration. And obviously, through the due diligence that we have done and through the management discussions we've had, we've had extensive opportunities upon our own view on those forward-looking forecasts and make whatever adjustments we felt was appropriate today. And that's what's represented in the models that have driven those accretion statements.

Azib Khan
Morgans Financial Limited, Research Division

Just on the growth outlook, Ewen and George. George, you did mention earlier that the combination of the 2 businesses allows you to generate more capital-efficient growth. Can I take that to mean that you'll be targeting stronger home loan growth than business loan growth over the coming period?

George Frazis
MD, CEO & Executive Director

Yes. It's -- what it does for us is -- obviously, we're going to focus growth on both. But our weighting on business banking was higher than retail banking. What this acquisition enables us to do is to have a weighting of about 50-50. So in that sense, growing both sides just means that we're going to be able to generate better returns in terms of ROE and not drop as much risk-weighted assets and capital.

Ewen Stafford
CFO & COO

Yes, that's right. And just to put some numbers against that. So the ME risk weight intensity is at 39%, BOQ at 67% through this combination. And so that just illustrates George's point.

Operator

Your next question comes from Josh Freiman from Macquarie.

Joshua Freiman
Macquarie Research

I'll just ask the one question. Excluding the transaction, you guys guided to a slightly positive NIM over FY '21, while peers' results and quarterly updates are showing material margin benefits come through for deposit margins. Just when we do our channel checks, it highlights your retail deposit costs are typically higher than peers. So I just wanted to check to see how you see the trajectory of deposit margin benefits impacting your margins in FY '21 and beyond?

George Frazis
MD, CEO & Executive Director

Thanks, josh. Maybe I'll start off and then hand over to Ewen. I mean, the starting point is, as we announced today, basically our half-on-half NIM improves by 3 basis points. And what we're saying is our expectation for the full year is a flattish to slightly positive NIM with, I have to stress, a positive 1% in terms of jaws.

But I'll let Ewen give you a bit more color around that.

Ewen Stafford
CFO & COO

Yes. A few comments on that one from me, Josh. Firstly -- and I think when I was unpacking that a little bit earlier, we have -- well, firstly, we were later than the market on average to cut into our TD pricing. But we -- Chris and the team have now been working through a reset of that. And we've experienced considerable benefit in the order of about 7 basis points of positive NIM in the first half, and we will see some flow-through on that into the second half. So that -- we are getting that benefits, albeit, perhaps, a little later than some other parts of the market.

Secondly, and we've mentioned this for, I think, consistently for the last couple of halves. We have historically had a higher cost deposit base and we are structurally working to reduce that and making really good progress on that and in bringing that down to lower-cost deposits.

And the Virgin Money go live, the phase 1 of the digital bank, will really enhance that when that goes in, in March as well, and which is going to be laid out, both transaction and savings accounts as well. So there was a -- I guess, in summary, there was a structural issue which we are dealing to, and we'll continue to build out those lower-cost deposits.

And then secondly, we have now started to -- or have cut those rates and are seeing the benefits come through into NIM, and that will continue that tailwind into the second half.

Cherie Bell
General Manager of Investor Relations

Ladies and gentlemen, that concludes the Q&A session this morning. So I'll hand back to George for a closing comment.

George Frazis
MD, CEO & Executive Director

Thanks, Cherie, and thank you all for your participation. A game-changing day for BOQ, an acquisition which is compelling strategically and financially. This significantly improves our competitive position today, but importantly, creates a pathway to an innovative, leading digital bank with a personal touch for tomorrow. We are very much appreciative of your support and your time today. So hopefully, everyone, thank you, and have a great day.

Operator
Thank you. That does conclude our conference for today. Thank you for participating. You may now disconnect.