Question and Answer

James Ellis
Crédit Suisse AG, Research Division

James Ellis from Crédit Suisse. Just 2 questions. Firstly, the noninterest income, $84 million, for the half, just wondering whether you thought that it could hold there given your comments around insurance and what has been a fairly considerable contribution from trading income. And then secondly, in terms of the branch numbers, which have been declining steadily. Previously, that had been more concentrated in New South Wales, but in this results has been sort of spread more nationally to sort of -- if you could give us an explanation around what was happening there and whether the network there is rightsized. Noninterest income and branch numbers?

Jon Earle Sutton
Former MD, CEO & Executive Director

Thanks, James. Look, I'll talk to the branch numbers and Anthony can talk to the noninterest income line. Look, if you remember back to what I said at the last -- at our full year results presentation. The way we at BOQ think about branch numbers and customers is you've got to take the lens -- you've got to actually have a distribution network that actually allows customers to choose how and when they want to deal with the bank, and that's our first premise. And if you think about where we've been for the last few years, we have remained outside of one of the fastest-growing channels of distribution, and that's brokers. And this time last year, 4% of all of that settlements came through brokers. We're now at 14%. And if you look at the industry, it's closer to 50%. In terms of the branch number reduction, I think we're down 10 for this half. A number of those were consolidations, where Owner-Managers actually consolidated. A number of them were Owner-Managers that had been in the business for 7 to 12 years who decided to retire. And also, we actually opened up another icon branch as well. So we don't have a predetermined number of branches that we want to move or reduce to, but what we are doing is looking at all of our points of distribution, and it's through that lens of how consumers want to deal with us, that includes the digital channel.

Anthony Rose
Executive Officer

On the other income line, as you've called out, there are a number of moving parts to this. The St. Andrew's underwriting result with the claim's experience that it has had, we wouldn't expect that to occur in the second half. I mean, you can never predict those things accurately, but we do see it as a blip. Around the trading income, it's probably a little higher than we would expect to see it ongoing in the transition to the new liquidity requirements. We were conservative in the amount of liquid assets that we raised in advance. When we finally did our calculations as to what we were required, we didn't need as much as that. So as that -- we're fortunate during that period that those bonds had largely appreciated. As we sold them down, we got an extra bit of income out of that. Those 2 items, we think, largely probably offset themselves. But we have called out the continued pressure on this line and the reasonably low prospects for growth for some time, and we'd expect those to continue. And we're also flagging that the St. Andrew's transition of its business to regular premium policies is going to be a drain on that line going forward.

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

Okay, Jon, we might go to you.

Jonathan Mott
UBS Investment Bank, Research Division

Jon Mott from UBS. A question on the dividend. With you saying the divi got up by $0.02 per share now for 5 or 6 halves, and in the last half, had pushed the payout ratio up to 79%. To pay for it, you've had to lower the DRP discount on and obviously issuing new shares to pay for this. This can obviously become a problem when you're paying out, obviously, having to constantly issue shares to do it. So is it time that you actually consider pausing the dividend to let the earnings catch up? Or are you going to continue to increase the dividend at $0.02 per share and the payout ratio will keep rising?

Jon Earle Sutton
Former MD, CEO & Executive Director

Look, I might start with that, Jon. Look, we carefully consider, as a management team, what we recommend to the board in terms of our dividend payment. And obviously, the board takes careful consideration of that. And we always have one eye on to what our capital generation levels are, and I'll have Anthony talk to a little bit about that. We're not giving any guidance at all about what our future dividend growth will be. But the way I think about this is that we need to build a sustainable business that can go right through the cycle so that we can continue to reward our shareholders. And we're comfortable with the dividend that we've declared today.

Anthony Rose
Executive Officer

Right. Thanks, Jon. Look, a couple things I'd probably cover. Around capital and capital levels -- and I know there's been a lot of speculation about some institutions moving higher into the 9s area. I think we would -- our view on that is those institutions are the advanced banks. And that movement to those ratios, we would suggest, is in advance of impending changes to mortgage risk weights in that space. So as the denominated then gets adjusted for them, we would expect some readjustment back down as to where those levels sit. We believe that the target range that we've talked about for some time of 8.5 to 8.6 is appropriate for the organization. It's set to maintain our ratings position comfortably in the A- band with each of the agencies. And we take a view that the capital is better in the hands of our shareholders than it would be lazy on our balance sheet. Clearly, we've had a growth in dividends that's been in the 13% to 14% rate, and you would be heroic to suggest that, that's a rate of growth in dividends that would continue for an extended period of time. We continue to monitor this. At the moment, where we see the changes in the growth profile of our business going forward, we think the optionality of that dividend reinvestment plan is sensible for us today until we really see the benefits of the different levers we have to pull to have the business performance in the growth aspirations we have going forward.

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

Yes, okay, [indiscernible].

Michael Wiblin
Macquarie Research

Mike Wiblin from Macquarie here. Maybe if we just take a bit of a step-back and look at the strategy a little bit. If I look at Slide 10, underlying growth looks pretty weak, sort of down 2% half-on-half if I take out CRM and specialist, or maybe flat if I take out property. But then, you sort of talk about, on Page 24, investing significantly for growth which I think is fine. But to James' point, you then are sort of closing branches as well. So I mean, how do I reconcile those different elements? I mean, what, Jon, are you going to do with Bank of Queensland? What do you want to do? Do you want to grow or do you want to actually manage for returns? Or -- what are your plans?

Jon Earle Sutton
Former MD, CEO & Executive Director

Well, thanks very much for that. Look, our focus is to make sure that we've got a business that can actually withstand the various cycles that go through -- that the Australian economy goes through. And we are planning for growth. I'm kind of very happy with the way that we sit at the moment. When you include BOQ Specialist, we're at about 0.9x system, we've had good growth through our business bank, and we remain really focused on that. We're actually seeing good growth through the broker channel. And I think the announcement that we've made today about bringing Virgin to market over the next 12 months will again allow us to continue on our growth trajectory. So we're very focused on that. But we want to do it in the right way. And I've been in banking for 20 years, and I've been through a couple of cycles. And it's very, very easy to rush out and stick assets on the balance sheet and then pay for it dearly in 2 to 3 years inevitably when the cycle turns down. And we've got one eye on growth but actually the other eye very firmly on growing the right way.

Anthony Rose
Executive Officer

I might just add and just to reinforce that our strategy hasn't been about trying to compete harder in our established markets. It's actually been about extending into channels where we're opening ourselves up to customers to deal with us in different ways. We think that's a preferred strategy. Yes, it takes longer to execute that strategy than an alternative, but we actually think that's the right value for the long term. To the point of your question around earnings momentum, clearly, we had a very significant step-up in the underlying business in the last half. And the step-up in this business, which you called out as a contraction, is less pronounced. There is a bit of noise particularly when you look at the previous half. It had the free-funding benefit of the lazy capital in the net interest income line in that half. If you strip that out, if you also recognize that the net interest income half-on-half because of day count for us on 3 days is about $7 million, on a "strip out the noise" basis, our view is that the business did grow underlying profit by a small amount, in the order of 2% annualized. And it did have strong growth in earnings when you factor in the improvement in the impairment expense plus [ph] 8% to 9%.

Michael Wiblin
Macquarie Research

Just a quick follow-up question, just on broker. Do you think you can grow aggressively in the broker channel without it having an impact on margin? I mean, if every man and his dog is in there now and obviously competing very aggressively, so is that -- are you comfortable that, that's not going to have an impact on your margin?

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, look. We're very careful about how we look at the broker channel. It is a very, very -- it is a very competitive market out there. And obviously, we get to see some different things out there. And different banks change their commission rates. They change their trials. They try to attract different rates. So we've been very consistent in what we do. The go-to-market product that we have is a clear path home loan. It has great acceptance right throughout the brokers that we are using. Again, I'll come back to the fact that we're only -- the settlements 12 months ago -- well, last half of 4%, we're now at 14%. And a lot of our competitors are actually a lot higher than that. But we're reasonably happy with where we are at the moment. We're very happy with the commissions and the trial that we're currently paying. And to your point about margin, we fight for every basis point. It's not only just the front book, it's what we can do in the back book. And I think that over the last few halves, we've proven that we can effectively manage our liability book as well to help us with our front book acquisition.

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

Okay, we're going to take one more question from the floor, and then we're going to go to the phones.

Andrew Triggs
Deutsche Bank AG, Research Division

Andrew Triggs from Deutsche Bank. Just a question on asset quality, if I could. And just the, I guess, mixed signals that the impaired -- or the new impaired flow on the arrears rates are showing. I'd note your comments, Anthony, around some one-offs and some seasonal impacts in the arrears rates. And can I also just in that context check your comments, Jon, that you were seeing sort of bottom of the cycle levels now in terms of bad debt to gross loans. Just your feeling on the medium term for asset [indiscernible].

Anthony Rose
Executive Officer

Look, I think you got to be -- I mean, one exposure greater than $5 million in a portfolio of our size, and it is the only impaired asset greater than $5 million, is not a bad outcome, to be honest. So I think that's probably put down to the law of small numbers. And if there has been a seasonal uptick, and it's a little bit more pronounced than it was 12 months ago, at this stage, it's too early to call out whether that's a significant concern. There's nothing that we're seeing in the underlying portfolio that would suggest that, that is. And a lot of it will come down to the confidence, as Jon said, in the broader economy as we move forward to that. So you might comment about the cycle.

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, look, I think, my comments around the cycle is really -- it's based on the industry. And we all know that we've seen a fairly benign cycle for the last few halves. And obviously, with the lower interest rate environment, and maybe the prospect of it from further lower interest rates, that will shelter that. But there's a lot of forces out there in the economy at the moment. And if you look at the economies going through a major transition say from the heavy investment into mining, some of those projects are now coming onto stream. Yes, we see a little bit of that. We also see a little bit of it as well particularly in our BOQ Finance book where people are delaying their investments while all that inertia is increasing on a lot of, say, CapEx equipment. So it's more a comment about where the industry is at the moment, and we're probably getting close to the bottom of that cycle.

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

Okay, we're going to go to the phones now, and then we'll come back to the floor.

Operator

The phone question comes from Craig Williams from Citigroup.

Craig Anthony Williams
Citigroup Inc, Research Division

Now that you're back towards system growth in the Retail market, what would -- on the lending side, what will be the impact of asset spread on this new business versus the role of existing book? And where is the greater source of front book competition that you're seeing? And the second part, deposit balance growth has now slowed during the period. Will funding mix and cost reductions actually be able to offset asset spread conduction in -- contraction, sorry, in future periods as we've seen in the last half?

Jon Earle Sutton
Former MD, CEO & Executive Director

Well, thanks, Craig. Thanks for the 8-part question. I'll start with the competition around what we're -- around what we're seeing in the competitive market at the moment. There's no doubt that competition is red hot out there in the market at the moment. And probably the one thing that we do see is that most banks have a published SVR and ours are probably on the higher side. But most of the front book acquisition amongst the banks are actually a go-to product. So that go-to product is Clear Path. It's very -- it is competitively priced. It's not at the bottom of the market. It is probably towards the middle of the pack. But one of the features that we're actually seeing a lot in the market at the moment is significant under-the-counter discounting in particular. And we've also seen probably in the last 1.5 months increased competition amongst a couple of the very large competitors in the broker market as well. And look, it ebbs and flows week by week depending on whether people want to increase or decrease in what they're doing. And it also is very targeted at times to say lower LVRs, higher loan sizes. So we've been competing in this market for a long period of time, and we'll continue to do so but not cutting our price to the bare bone, and we don't want to do that.

Anthony Rose

Executive Officer

Just on your question on the deposit growth, we have taken the opportunity over this half, now that we've had all 3 credit rating agencies upgrade us to the A- category, to really build our senior unsecured credit curves. So we've now got a complete curve across the full 5-year spectrum. That has increased our duration and the resilience in the book and it's given us a greater access to that part of the wholesale funding market. And we've been using that, if you like, to pay down our reliance or reduce our reliance upon the higher cost, hot money retail. So that's largely been a neutral cost, but we think built us better resilience in the balance sheet. So from an absolute deposit growth perspective, you're probably seeing a negative outflow that's disguising an underlying growth in what we call relationship-based deposits from the business. So we're reasonably comfortable with how we're positioned in that regard.

Jon Earle Sutton
Former MD, CEO & Executive Director

I just want to add to that as well. Being a small and more nimble bank, both Anthony and I get the opportunity every week to sit down and look at where what's going on both sides of the balance sheet so that we can actually move quickly. And it's -- we're very focused on fighting for every basis point that we can get.

Anthony Rose
Executive Officer

And probably to that directional question around our margins going forward and whether the deposit spreads can shelter the asset spread repricing, we -- as I mentioned in the presentation, we have seen, I think, a reasonably disciplined approach to the repricing on the liability side that has been managing margins on an industry basis with some stability. You're correct that we'd need that to continue if asset spreads are -- and front book space is going to continue at where it is at the moment. And where I think, if you go back 12, 18 months ago, we had a lot more confidence that we had levers to pull given our reliance upon the higher cost component, what was much more pronounced. We don't have the same capacity in those levers today, and I'd suggest we're probably more in line with the rest of the market, absent Jon's comments about thinking that the ability for us to see what's directly happening in the balance sheet gives us, we think, a bit of an advantage.

Operator

The next question is from Richard Wiles from Morgan Stanley.

Richard E. Wiles
Morgan Stanley, Research Division

I just wanted to ask about your thinking on the guidance. As I understand it, at your previous update, you said consensus was at 3 62 [ph], less the $7 million for the CRM write-down brings you back to 3 55. Following today's result, that's implying that you've got to deliver about 5% growth in the second half, excluding the one-offs. And the way I look at it, you got to get much better trends in the second half to make that guidance than you've just achieved in the first half. Jon, given your comments in response to Craig's question around margin, given Anthony's comments on deposit pricing versus asset competition, what confidence can we have that you're going to make that guidance for the second half? Are you relying on better momentum from the Specialist business? Are you relying on better revenue in the core business? Or are you thinking loan losses can go lower again?

Anthony Rose
Executive Officer

The -- on the chart that we had on Slide 11, if you strip out the one-off noise, we delivered $178 million of earnings in this half. As I did flag before, we do have a day count difference, 181 versus 184 days, doesn't sound like a lot, but the net interest income line is the biggest line on our profit loss. It's about a $7 million kick. If you just roll that forward, that gives you, yes, a nice -- you're well into the low 180s to get to the 188 number that we need to achieve. So again, we would expect increased momentum in BOQ Specialist over and above that, and just general growth momentum in our business.

Jon Earle Sutton
Former MD, CEO & Executive Director

And I'll add to that as well. But all of our lines of business have had a very good first half in terms of performance. And if you look at -- we've talked a lot about BOQ Specialist, we talked a lot about the seasonality that they actually have in the second half. One of our unsung heroes is BOQ Finance, and it's actually growing ahead of where market is. And we've certainly got momentum back in the Retail banking, particularly through the broker channel. And again, just draw you back to our -- to the attention that we're relatively small in that particular part of the market. And there is still considerable scope for us to grow, and we're very mindful of our costs as well.

Richard E. Wiles
Morgan Stanley, Research Division

And, Jon, if we look at that core business -- forget BOQ Specialist for a moment which does seem to be going reasonably well. You're still growing below system in mortgages. It's quite possible that margins are down in the second half. We've got the resumption of the right cap cycle, we've got more competition in the mortgage business and you've got less confidence in levers to pull in deposits. So I fail to understand why you think there's such good momentum outside of BOQ Specialist and outside of the fall in the loan losses.

Anthony Rose
Executive Officer

The part of the technical answer to that argument is your growth in your net interest income is obviously a combination of your margin and the growth in your average balance sheet. In the FY '15 year, we will have a headwind, the business grew virtually nothing in the '14 year. And so that natural average balance sheet momentum is not helping on the revenue side. Given the growth trajectory is improving, that is going to start to come through over the future periods.

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, and look, I'll draw your attention to the fact that, in our business bank, we've actually grown at 1.2x system. And sure, look, if you just strip out and you just looked at BOQ x the brokers, we're at about 0.5. That's coming from a standing start. Some of the things that we're seeing is that our settlements are up in our owner-manager branches. And I think it's an industry-wide trend at the moment as well that there's probably not a great deal of growth coming out of branches for financial service institutions. But what you are seeing is this increasing growth by consumers to use brokers so, again, we remain confident around that guidance.

Operator

Next question is from Ed Henning from CLSA.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Anthony, just a quick question from you, and you touched on it before, just on the BOQ Specialist business and the really kind of high cost-to-income ratio there. Is there much [indiscernible] in the cost there that you guys can carve out there?

Anthony Rose
Executive Officer

Look, that business is -- has obviously performed really well. We're really comfortable with its momentum. And yes, it's one of those things that yes, you don't touch something that's not broken just for the sake of doing that. That business needs to continue on the path that it's been on. I'm sure, over time, there will be opportunities to explore ways in which we can collectively leverage the opportunities that the broader group provides to improve efficiency in that business. But it's not a high priority for us. It's driving that business in the way that it's being driven at the moment is the right outcome.

Jon Earle Sutton
Former MD, CEO & Executive Director

And I just want to add to that too, is when we flagged this acquisition last year, this time last year, one of the key attractive elements to this was the fact that not only was it a great business and it's got great people in it and who are leading it. But BOQ Specialist was originating about $1 billion worth of mortgages through third parties. And we gave some guidance saying that we'd like to be able to get to at least 50% of that on balance sheet by year end, and we're clearly ahead of the curve there. And part of that increased cost that you've seen there on BOQ Specialist was to allow BOQ Specialist to put staff on to actually originate those mortgages. And again, we remain very confident about that earnings guidance we've given for that business as well.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

Okay, just a second question on the commercial loan growth and just the BOQ business. Can you just talk about where that growth is coming from for this year?

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, look, we've been very, very deliberate about where we get our loan growth. And having had to rehabilitate a very large commercial book some time a few years ago, very attuned to ensuring that we actually are growing the right way. And what we've done through -- within our business bank is to be very targeted. We've targeted the rural lending there. We haven't seen a big increase in rural lending. We've largely stayed out of that during the drought, but very happy to say that the prospects there are improving with the recent rains. On the property front-end side, what we do, do is support our customers that we've known for a long, long period of time. And we've got some customers that are finishing some developments that are now looking at some developments. We're very judicious around the settings that we have around that and also in terms of the property development -- on the property development side but also the property investment side. Some of the growth has come through relationships that the senior management team have known for a long period of time and are very attracted to the fact that BOQ can actually provide very quick turnaround times and to service their needs. So quite comfortable with the settings and quite comfortable that we're growing at 1.2x system.

Edmund Anthony Biddulph Henning
CLSA Limited, Research Division

So -- and sorry, just is there any industry -- so there's a bit on the property side and some on the rural side, but is that like if you look at actual industries?

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, look, what we will be doing in the future is looking at specific industries, that's some work that we're currently thinking. We've got some very good capability around H care. And again, we're not being all things to all people. It's not a shotgun approach that we're taking. It's very much relationship-driven backed by strong risk fundamentals.

Operator

Last question comes from Victor German from CBA Equities.

Victor German
Nomura Securities Co. Ltd., Research Division

I was just hoping to also ask a couple of questions. One -- or just a few questions on my journal, so one question on risk-weighted assets. With respect to margins, are you able to remind us about your hedging policies for balance sheet purposes. I noticed there's about 3-basis-point reduction relating to lower interest rates, with further reductions as we've seen. Can you maybe give us your views as to how those are likely to evolve in the upcoming period?

Anthony Rose
Executive Officer

Sure. Look, we run a very conservative hedging approach to the entire portfolio. I think what you're alluding to is our capital and low-cost deposit portfolio. We have a replicating portfolio of derivatives we sort of overset that element of our free funding, if you like. That is on a net 2.5-year weighted average life, so it takes some time to come off. That just does reflect a drop in the yield curve. So yes, that is reasonably market standard and a reasonably conservative approach to managing that element. The rest of the hedging activities are largely risk neutral.

Victor German
Nomura Securities Co. Ltd., Research Division

And so we should expect a couple of basis points a half derived from that continue to come through, that's sort of the right way to think about it?

Anthony Rose
Executive Officer

With the reduction in the yield curve that we're seeing at the moment, yes.

Victor German
Nomura Securities Co. Ltd., Research Division

Yes, okay. The second question on margin, I guess following up from, I think, Craig's question, with respect to your funding mix, are you still expecting to continue to build the long-term funding as proportion of your total funding, or roughly the mix should stay where it is?

Anthony Rose
Executive Officer

I think we've done most of the heavy lifting in the diversification of our funding mix in the last half, so probably more close to maintaining the existing distribution.

Victor German
Nomura Securities Co. Ltd., Research Division

All right. And lastly just on risk-weighted assets, and thank you for providing additional disclosure on your mortgage book. If I look at the way the book is positioned, it -- I mean, it sort of sounds like it's a pretty standard book. You've got weighted average LVR of 65%. Can you maybe give us some little bit of an insight as to why your risk weighting relative to your exposure for mortgage book isn't sort of now mid-40s? Because if I look at high LVR lending bands, it doesn't seem like it should be particularly high numbers across your portfolio.

Anthony Rose
Executive Officer

Yes, look, there's probably a technical answer to that question that's beyond this forum. But a significant contributor to that relates to the way we have conducted securitization in the past, where there is shared collateral, and if you end up with a loan on your balance sheet, it ends up being 100% risk-weighted rather than 35% risk-weighted. That is legacy and it's created some noise. We don't have the, if you like, necessity to rely upon the RMBS funding in the same way as we had historically. So expectation would be that, that will gradually reduce over time.

Victor German

Nomura Securities Co. Ltd., Research Division

Roll off, right. And are you surprised that it hasn't sort of rolled off quicker because -- and you also made comments that you're reducing your risk in the housing portfolio as well, yet the risk weighted assets seem to be gradually stable or slightly rising, whichever way you look at it. Any sort of observations as to why we haven't sort of started to see this trending down?

Anthony Rose
Executive Officer

It's a question I'd have to take on notice and come back to you in more detail.

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

Okay. We might take final questions from the floor. Brian?

Brian D. Johnson
CLSA Limited, Research Division

Brian Johnson, CLSA. Jon, I had a few questions. The first one is that when you have a look at Slide 18, the IT that you have a lot of stuff with.

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes?

Brian D. Johnson
CLSA Limited, Research Division

The first thing that has to be stated is banks historically aren't very good at basically developing capitalized software. I'd just be interested when you have a look at it, the assets under construction number is going up. I think you wrote off $10 million during the half year. Can you just -- and I would have thought a new incoming CEO, that's the line you absolutely butcher. Can you just go through and make us feel that we shouldn't be worried about further impairments coming on that anywhere in there. And can you also reconcile for us how the CRM write off that you did during the period, did it go in the blue or the yellow bit? Because if not, it implies that the assets under -- the assets capitalized balance would have gone up -- sorry, the actual capitalized balance would have gone up a bucket load but for that. So if we could get some clarity on the movement in that?

Jon Earle Sutton
Former MD, CEO & Executive Director

Yes, certainly. Look, just at a high level, this is a bank, for a long period of time, that has not made significant investments. So we had to make some investments to grow. We're very committed to unclogging the arteries of the bank. We're world class at moving paper, as I said, I'm the best customer of Toll, I'm the best customer of snail mail still in Australia. What we have done is we are building -- and we're not building, we have actually taken off-the-shelf software from a vendor to allow us to be able to take our mortgage applications online with the customers, instead of filling out bits of paper. So we're not actually building it ourselves, we're actually adapting it. And we're well on the way to implementation, followed up by a digital process around settlement into the back office. So we're not actually constructing and we've got teams of programmers running around doing anything, it's really focused on the software and adopting it to what it is without radically changing in any way, shape or form. Comfortable with where we're at for the capitalized software. We went through a very rigorous process of reviewing all of those assets and I'm comfortable with where we've got to in terms of the write-off that we've announced on that particular asset. Anthony?

Anthony Rose
Executive Officer

Your point is valid. The $8 million that we called out as the increase in the assets under construction would have been $10 million higher if not for that writeoff. The growth in that line on the prior half was about $15 million, $16 million. We're at full capacity at the moment. The lending program that we've got in place, the Star HP transition program are very substantive pieces of work. And we are continuing to -- those teams are driving pretty much at that capacity. So I think it's fair to say that we'd expect that type of spend over the coming period. What we're not seeing at the moment is as those larger investments that we've undertaken hit and start amortizing, there isn't as much in the amortization coming through at the present time. We talked about the balancing of the benefits from the HP contract transition and the sheltering that, that will provide us to some of that amortization tail.

Brian D. Johnson
CLSA Limited, Research Division

The second one, Jon, great effort on capital, and you've always been a [indiscernible] stick at that capital. It's interesting, I think a lot of the narrative that you hear from the regional banks seems to me that it's very much still based on the interim report of the FSI rather than the final report. But if we go back to the 22nd of December, when I think most sensible people were enjoying a beer, the Basel committee actually came out with a paper that said standardized housing risk weightings probably need to go up. And it actually spoke about a grid which would actually see risk weightings basically more aligned to loan-to-income ratios and LVRs. And so that when you have a look in Australia on a global context, I would have thought the risk weightings could actually go up quite markedly. Could we get some commentary from you on what happens if the reverse of what you suggested is true? Is it the actual risk weighting on housing moves up markedly for the regional banks which is what that paper actually implied?

Jon Earle Sutton
Former MD, CEO & Executive Director

Well, Brian, I just want to reassure you that I was -- December 22, I was reading that report. And look, the way we think about that -- and look, that was a completely -- a different view to what we have all talked about from a regional bank perspective and anything that I talked about, there's a lot. And I still think there's a lot of water to go under the bridge before they finalize that. But if that counter view was to prevail, I think, what you have then is a rising tide for all banks in terms of capital. And look, that's a hypothetical at the moment. We need to keep a very close eye on how all this plays out and then we will -- we'll respond to that accordingly.

Anthony Rose
Executive Officer

I might add to that, Jon, if I can. I think it's important to put into context that there were 2 papers that Basel released at that point in time. And the first paper, the first paper was we want to bring largely -- the undertone was, we want to bring credibility to the advanced modeling system. Therefore, what we're going to do is come up with a framework for calibrating that to an enhanced standardized framework. So therefore, it moved to what's the standardized framework going to look like. Now many jurisdictions around the globe for mortgages simply have a flat 35% standardized framework. APRA already had a tiered structure, which is along the lines of what the Basel committee is putting forward. As Jon said, there's a lot of water to go under the bridge as to exactly how the different bandings are likely to play out on those different tierings. Whether serviceability ends up being part of the final equation again is going to be certainly up for debate and still up for discussion amongst the Basel community. So it's very hard to know where that is, but I'll reiterate Jon's comment that our view is the rising tide of capital clearly is coming in. The question is does it reach us, but we would suggest we're going to be the last and of the least impacted of the industry. And what it appears to be is an environment where the particularly in relation to residential mortgages, the gap in the risk weights is likely to significantly narrow. And we absolutely welcome an opportunity to compete on a much more level playing field than we have today. And we think that's going to go very well to our competitive position and our ability to return for shareholders.

Jon Earle Sutton
Former MD, CEO & Executive Director

Well, I think the other thing too is that some jurisdictions have already moved and some have increased their risk weightings and others are still considering what the Basel implications are. So again, we will be strongly advocating for a much more level playing field. If you think about this, the argument of you or I walking into any bank getting an 80% LVR loan as a PAYG and some banks have got 6% capital against it or 10% or 12% and us at 40%, it's got the same probability that follows. It's got the same LGD, it just doesn't make rhyme or reason. So I think there -- we're very strongly of the view that there has to be some sort of leveling of the playing field, but we also are not going to walk away from the fact that we'll continue to look at the benefits of getting towards advanced accreditation and how that plays out with all of this debate around capital levels. And I still believe that there is a lot more water to flow under the bridge, and it is very hard to make a definitive statement about where all this will end.

Brian D. Johnson
CLSA Limited, Research Division

Just a final related question. When you have a look, a lot of your rhetoric today is talking about the stark origination of home loans has been bad, and turning on the broker channel seems to be a solution. And so you spoke a lot today about increasing the broker representation. I'd just be interested to understand the math because when you actually have a look at a broker-originated loan, it's the worst capital-intensive loan you can possibly manage. Can you actually make us feel a little bit more comfortable that the deduction of the upfront commission doesn't actually hurt that core equity capital generation even further?

Jon Earle Sutton
Former MD, CEO & Executive Director

So just at a high level and I'll get Anthony to talk in some more detail about that. Obviously, the cost of origination of a broker loan is probably about the same as the cost of origination through an owner-manager when you talk in terms of the commissions that we pay the brokers or the commissions that we pay to our owner-managers. We're very careful about looking at that and we're very careful looking at what the return on equity is per channel, and we'll continue to monitor that.

Anthony Rose
Executive Officer

Look, I think the point is that we are in an owner -- we have an owner-manager channel where we pay commissions under the same framework today, so -- and it's not materially different moving into the broker space for us.

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

We might just take one last question from the floor?

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

Brett Le Mesurier BBY. Just back on the loan margin, they declined 6 basis points in the half. Should we deduce from that, that between the new business and the existing is at the order of 50 basis points?

Anthony Rose
Executive Officer

I'd have to take that question on notice.

Karyn Munsie
Former Group Executive of Corporate Affairs, Investor Relations & Government Relations
Okay. Thanks, everyone. We'll leave it there. Thanks very much for attending.