Question and Answer

Matthew Davison
BofA Merrill Lynch, Research Division

It's Matt Davison from Merrill Lynch. And firstly, congratulations, Peter on your career. My question, related to APEA. You're starting to see pretty good growth in the underlying earnings number and the NPAT number. But you're still seeing very strong growth in risk-weighted assets, up 35% year-on-year. So I'm just interested in the outlook in terms of that return on risk-weighted asset, whether there's a bit of an abnormal issue with the growth in that balance. And just a related question, the Institutional NIM is down 30 bps x markets year-on-year. Peter, I think you've alluded to that being more Australia. But just interested if that is really in line with expectations or came in more disappointing than what you thought 6 months in there?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Okay. On the RWA growth in Asia-Pacific, that has been primarily as a result of driving the trade book. So it's high-quality assets and also short term. And that was done for a very deliberate reason in terms of the funding requirements. So it's much easier to fund that sort of short-term up. But the quality is very good. That meant a slightly lower return on that -- on those assets. In terms of -- what was the second part of the...

Peter Ralph Marriott
Former Chief Financial Officer

The next part of that, the Institutional NIM. The comment in terms of the ROE because it certainly was obviously a focus of discussion the last trading -- the last results announcement. And if you really got a look at the average risk-weighted assets and you're going to bring in all the deductions, it's a hard number to derive from the results announcement itself. But if you look at the ROE of the Asia business -- Asia-Pacific business, on a regulatory capital basis, it's improved about 1% since the last half. It's floating at the moment around about 11% on a regulatory capital basis. And when you drill in into that, the Retail business is around 12%. Now there's some one-off positives in that number but the Retail business is a long-term outlook business. So, in that, you shouldn't be expecting strong returns in the short term. Partnership is running about 11% and the star performer in there is the Institutional business, which runs about 16%. Now obviously, in terms of capital consumption, because the risk-weighted assets are growing so fast that you have a lot of capital, but we are, on a regulatory capital basis, getting reasonable returns and improving returns on that, and that is the ongoing focus for the business.

Michael Roger Pearson Smith
Former Non-Executive Advisor

In terms of the NIM. I have to say that the adjustment in NIM in the global loans area was the real surprise. I mean, I think the competitive pressures that came through there, that wasn't expected. Well, the scale of the adjustment wasn't expected. And it was on both sides of the balance sheet. It's incredibly competitive on the asset side, particularly -- this is Australia in particular, but also on deposits. And that, of course, is across the board. That moves also into Commercial and to Retail. Anything you want to add?

Peter Ralph Marriott
Former Chief Financial Officer

Yes, I'll just echo what I said in the presentation, that I think, at the time, at the end of the first quarter, yes, it was off a little bit, but we sort of saw it broadly stable, we knew a couple of basis points of that was just capital and there's always timing issues around fees and these sorts of things. But, no, the trend continued, and so that's -- and yes it was "surprise" compared to where we were 3 or 4 months ago.

Michael Roger Pearson Smith
Former Non-Executive Advisor

Maybe we should tell you what we're doing about that, Alex. Would you like to, I'll through you the line? On the NIM, yes.

Alexander Vincent Thursby
Former CEO of International & Institutional Banking and Member of Management Board

Just broadly on the NIM, we have a number of actions which we'll use some of our liquidity from offshore to try and restrict the margin compression from the liability side. So we're looking at opportunities that, frankly, are arbitrage opportunities. We're also looking at moving our book more towards the short term, which, I think, while it won't fix the NIM issue per se, it will give us a lot more flexibility in the balance sheet. So similar to what we did in Asia 1 year ago -- 1.5 years ago, we'll bring much more short term nature. We also feel that that's probably got an easier ability to price up in some of the terms stuff at the moment where the market seems to be just very, very -- in Australia and in New Zealand, very, very tight and not moving at all. And we have a number of other activities as well. But the fundamental thing is that the NIM in Australia in the Institutional side has come under a lot of pressure from both sides of the balance sheet.

Jill Craig
Former Group General Manager, Investor Relations

Do we have another question from Melbourne? Doesn't look like it at the moment. So Graham, I might go to Sydney. Questions from the floor there, please.

Graham Kennedy Hodges
Former Deputy Chief Executive Officer

Yes, we've got about 500 here. Well start here and we'll move across the room. So well just pass the mics around so...

Jonathan Mott
UBS Investment Bank, Research Division

John Mott form UBS. A question about the margin in Australia. And I can understand all the moving parts there that Peter has highlighted as always. But if you step back and look at it, the Australian mortgage business is growing twice system levels and you did have found it with pretty expensive deposits. And at the end of the day, the margin has gone down from relative to peers, 2.58 to 2.54 is still substantially higher than where the rest of your competitors are in Australia. So in reality, this is just the case of the Australian margin re-basing down to more realistically levels with where the competition is in Australia and this couldn't be an ongoing structural issue rather than anything more symptomatic of a few moving parts in deposits?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes, I think, John, that we can do more to manage the margin. You've seen those 2 out-of-cycle increases. That's going to have a flow-on effect as it moves through. The growth of 2x system in mortgages was the guys got a little excited when they got behind system growth at the beginning of the year and probably pressed the throttle a bit too hard. So what we're still aiming for there is growth over that system, just over the system, at which I think is appropriate, because as you rightly say, the issue with mortgage is how to fund that and the liquidity aspect around it. But in terms of the question about the structural change, I think the structural change that's coming through is on the deposit side and deposit cost. Quite clearly, with the situation in global credit markets remaining pretty uncertain and very volatile at best, all banks are going to be looking at deposits, domestic deposits, to fund their operation. And frankly, that's good banking, actually. So I don't actually see that as a major issue. What we have to do is to manage that margin and we've got to take some tough decisions around that. Phil, do you want to add something to that?

Philip Wayne Chronican
Former Chief Executive Officer of Australia

Just add the point Mike made that the deposits is important piece of that, and it's been core part of our strategy that we grow at better than market and the household deposit sector which we have consistently done. It is true we do get a bit ahead of ourselves in terms of the mortgage growth and we certainly never intended to grow 2x system and will be coming back from that. But we do see that the longer-term strategic positioning is more driven by our ability to continue to grow household deposits faster than the rest of the banks, which we've done that for a number of years, because that gives us the feedstock in a sustainable way to be able to build share on the asset side of the balance sheet. So the margin issues, I think will -- yes, it's hard to see that we're materially different from what the rest of the sector has gone through. The composition of our deposit growth is such that it's less concentrated on term deposits, so we would expect that to have more of a muted affect on margins than perhaps some of our competitors as well.

Jill Craig
Former Group General Manager, Investor Relations

Thanks, Graham. We'll go to the next question.

James Freeman
Deutsche Bank AG, Research Division

James Freeman from Deutsche Bank. Mike, having heard everything you just said, I was just wondering, is there anything that you can do actually on the deposit side to perhaps improve that spreads there? Obviously, you've since been focusing on the assets, I'm just wondering if there's anything that you can do to help improve deposit spreads. And just one for Phil, just trying to get a bit of an idea as to the run rate cost savings for your business moving into the second half of the period, obviously, 3% growth in the first half, probably a little bit disappointing given the revenue growth. Just a bit of an idea what we can expect in the second half?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes, James. So I think the key there is to really push CASA on both Retail and Commercial and Institutional business. And of course, the investment we've made in our cash management system is completely aligned to that. So there are things we can do and we do need to become more competitive in that lower cost area, which I think you'll see the results of that coming through in the next couple of years. Yes.

Philip Wayne Chronican
Former Chief Executive Officer of Australia

In terms of the costs, Peter had a chat earlier on that showed our first half cost growth had been 3% last year and the second half of 1%. We have 3% growth this year in the first half. It's hard to be specific about these numbers but it would be fair to say with the headcount reductions we're going through, it's likely that our second half cost growth will be below the 1% of the previous year. So broadly speaking, we'll be looking to flat if not declining nominal costs in the second half.

Peter Ralph Marriott
Former Chief Financial Officer

Yes, it's also important to appreciate because of the terms of the exits later in the half, slightly beginning into the next half. So the full momentum won't come through until 2013.

Michael Roger Pearson Smith
Former Non-Executive Advisor

Over the headcount reductions that we've announced, I think there are only a couple of hundred had gone by the end of March. There's a number, I believe, during April, May and June. So as Peter said, there will be a benefit in the second half from that but there was obviously then a kick on benefit into the first half of next year.

Jarrod Martin
Crédit Suisse AG, Research Division

Jarrod Martin from Crédit Suisse. Continuing on the theme of margins, maybe across to APEA. Six months ago, we saw a gapping down of margins in the region for the second half. And at the time, I think the outlook for margins into FY '12 was one more of optimistic rebound driven partly by trade finance margins yet in the first half we've seen APEA margins come down again. And I think Peter's outlook statement was for a small decrease in margins into the second half. I just wanted to know what changed from the outlook back at the full year '11 results and what the competitive dynamic is in Asia at the moment?

Peter Ralph Marriott
Former Chief Financial Officer

I might start and Alex may want to make some comments but APEA is a complex based from a margin point of view because there's very higher margin businesses like the credit cards business and lower margin businesses like trade. And so you get massive mix effects. Certainly, I think everything we said, was going to happen happened and the margins in trade were very, very strong in that month -- in the period. But the growth mix meant that the growth was in the lower margin business and less growth in some of the higher margin business because Alex has been rebalancing the portfolio, reducing some of the high risk parts of those credit card portfolios, for example. So you're always going to have this mix effect coming through. It didn't flow through into having an impact on the group margin in it was more what it did to the APEA's margin in isolation. So there was no surprises in really and it's a question ultimately around whether it's a mix effect in that business.

Michael Roger Pearson Smith
Former Non-Executive Advisor

I would say, Jarrod, there was quite a big change in the market and what had happened to trade margin, it had increased quite significantly because of the lack of -- the lack of availability. As the European banks have pulled back at the time, the first business they pulled back on was trade finance because that was short term, it was running off, they didn't get back into it. The LTRO changed all that, they're back with a vengeance. So there has been a fundamental shift in the market.

Ben Koo
Goldman Sachs JBWere Pty Ltd, Research Division

Ben Koo from Goldman Sachs. Just in regards to the Institutional division, can we get a sense of the cost levels in that business. I mean there's always been a very high level of investment embedded in that cost base already. We've seen over the last half the cost growth was actually quite slow despite the quite strong rebound in the markets related income. Could we just get a sense, with the cost outlook for that, there's talk about some restructuring benefits that has been benefiting in this half? Is that just something that we continue to expect relatively lower levels of cost growth compared to what we've seen previously, which we saw much, much higher cost growth in the Institutional business in the past periods?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Okay, so it's a question of priority. It's an issue of where we should be putting our investment dollar. And basically, we should be putting those in the areas that actually create biggest return for us. The cost initiatives and productivity initiatives that were undertaken in Institutional at the end of last year obviously came into -- started to benefit the business. And I think we shouldn't be seeing huge cost growth in that business. But I think it's probably fair to ask Shayne who was responsible, at that time, for initiating this issue, how you see it play through. And he's here of course, he's now turned gamekeeper.

Shayne Cary Elliott
CEO & Executive Director

There is a chart in the page that showed the cost growth was coming down from 10%, to 8%, to 5%, to 3%, so there's been a focus on driving down the cost growth over that period of time. And that's really driven by a couple of things. One, the big-ticket investment programs that we've had whether they're around remediation or whether they're around investment and investment being primarily in transacted end markets. The big kind of weight of those investments are behind us and so the ongoing business will be lower. And we start to get the benefits through of those investments over on the revenue side or on the cost side. Plus secondly, there has been a -- now that we've simplified the business within Institutional and made a more focused about where we have competitive advantage, we start to drive that productivity much greater. So just in terms of core BAU business absolutely, there's productivity coming through in the business. So I would expect those businesses to continue to trend down to be very, very low single digit.

Peter Ralph Marriott
Former Chief Financial Officer

Going back to what you said there have been as well as, I think we undertook this to you as not allowing the business to re-spend the rebound. You got to look through the rebound in the Trading and Sales business. And then even within the 3% cost growth in the first half was $15 million of restricting spend, so -- which will source through in the benefits in the future periods. So a lot has happened in that business after. I guess to be fair a lot of growth in cost got ahead of a lot of growth in revenue. So pulling it back into line now.

Victor German
Nomura Securities Co. Ltd., Research Division

Victor German from Nomura. Throughout the presentation there is a theme around deposits and your relative position or relative stronger position on deposits, which I guess is, no one will argue, is not a positive. The question that I have is that your deposits are relative to peers over weight in the Institutional space. And as we all know, not all deposits are created equal and particularly as we go towards 2018, albeit it's a long time away in net stable funding ratio environment Institutional deposits we give lower weighting. I'm interested to hear your thoughts about your strategy around deposit growth, whether there is more, more focus on more stable deposits. And also if you could give us a split in terms of margin pressure in Institutional business whether it's coming from lending or deposit side, what the split is?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Victor, it sounds like you want to apply for a job with APRA. But yes, you're right. There is always a difference in quality of deposit and we're well aware of that. But this is -- again going back to the issue of our cash management business. Once you pick up cash management mandates from corporates and from other financial institutions, it is a much stickier deposit than actually many Retail deposits would be. So I wouldn't accept that all corporate or institutional deposits are not as sticky as retail. Having said that, we do accept that the retail deposit base is very important for our future. And as you saw, we grew retail deposits by 6% in the half, which is a good outcome. We're also continuing to build up the retail deposit base in Asia. Now we accept that, that is a small business now and is something we have to continue to invest in. But at some stage, it is going to be an important part of our funding and that will be -- that is a long-term goal. So I take your points, but I don't think we are -- we are positioned badly. In fact, I still think we have a competitive advantage around our liability mix. And we will continue to watch that and build as much sticky deposit as we can.

Peter Ralph Marriott
Former Chief Financial Officer

And then within APRA, obviously, is a focus on Transaction Banking and grant more and more transactional-type accounts. I think your other question was around the split between...

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes, yes. [indiscernible]

Peter Ralph Marriott

Former Chief Financial Officer

Can I answer the NIM question?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes, go ahead.

Peter Ralph Marriott
Former Chief Financial Officer

There's a split between -- I'm safe now. The split between -- the split in the margin reduction within Institutional between what was there from deposit side and what was the asset side. And if you look at the waterfalls we've given you within the slides, in there, it actually shows that it's all funding and deposits. It's not asset. But's that's our problem. On the average, it's not assets. But within assets, it's a small factor, but it's actually from a margin point of view, the competitive pressures on the global loan side are meant that there was, that cost the business through fees mainly 5 basis points. But they made up 5 basis points on Transaction Banking so net-net, our assets was 0 but the Transaction Banking did very well but there was 5 on the asset side coming out of fees and loans.

Richard E. Wiles
Morgan Stanley, Research Division

It's Richard Wiles from Morgan Stanley. Mike, you said in your presentation that you're continuing to actively manage the Asian partnership portfolio. Could you expand on that statement? Could you comment on the prospects for change in your ownership interest in Indonesia and Malaysia? And could you also let us know how you think you're going in terms of building the Asian Retail franchise more broadly?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes, I'll give you some broad comments and then I'll throw it over to Alex. But we managed the partnerships as we always have in the last 4 years, which is basically as a strategic initiative into the country, which when possible, moves into an organic business. And when those partnerships no longer give us strategic value, for example, Sacombank in Vietnam, we'll dispose of them. If we can find ways to increase our ownership to a controlling stake, then of course that's also something we would look at. The difficulty in a couple of the cases you mentioned is that quite clearly, the other shareholders have to be at the dance with you. And of course, the regulatory impositions may restrict us from moving to larger stakes than we ought to move into larger stakes that we would like. But we're very pleased with the relationship we have with AmBank in Malaysia. And with Panin in Indonesia. As I say, Sacombank, we exited from. And of course, the holdings we have in the 2 banks in China are restricted by regulatory limits. Thank you -- sorry, what was the -- on the Retail. The Retail side, that's going relatively well. Really, it is -- it's being built off the base of the RBS business or the old ABN AMRO business that we bought in Asia. We have restructured it somewhat and it's much more based on affluent and wealth type product. It is not pretending to be mass-market business. The cards business slightly separate, but again we're focusing that more on the affluent side as well. But that build, as I said earlier, is a long-term build and really the value of that is to create a deposit base, a sticky deposit base. And we have to accept that our competitive advantage as ANZ in this market, really is geared to people who have a connection or an interest in Australia or New Zealand or perhaps somewhere else in the Pacific. But so far, the strategy is on track but I'll pass it over to Alex.

Alexander Vincent Thursby
Former CEO of International & Institutional Banking and Member of Management Board

Yes, just in regards to the partnership question, the only thing I would add, with some of the partnerships, we have very good interconnectivity of business flows, particularly with AmBank on the market side and also introduction of clients from both sides. We have also just recently announced the introduction of clients but also the -- on the retail side, but also the establishment of signature priority within Malaysia as well as they start to bank on the affluent side and we help them with that and obviously that, with our business in Singapore helps our businesses in Singapore develop. Relative to your question on the retail side, I would class it as we've now got our head above water very well. We have, for the first half, we've now acquired more customers than those that we have deliberately exited. And I'm quite happy to go through that with you when I next see you. We have continued to grow deposits in Wealth Management products. The growth in both of those areas have been strong, some 20% growth in deposits from the Retail side. And our mortgages business, which is becoming an important product relative to the affluent space, the larger mortgages is now starting to get off the ground and starting to get momentum. Counter to that, as we move segments, our Consumer Finance business, which includes cards, is changing quite dramatically. And we are specifically focusing now on the card side at the affluent and emerging affluent and slowly moving out people below that -- those levels. You're seeing that revenue is flattening off in those areas as we do that, as we change more from a model of revolvers to a model of actual utilization of a card. So you can expect, going forward, that to be a slow growth business, while the other 3 components that I spoke about in terms of product groups will be more bigger in growth as we start to acquire -- continue to acquire more and more customers and the dilution of the exit slowly walks away. But I would agree with Michael that it is a longer-term business for us.

Brian D. Johnson
CLSA Limited, Research Division

Brian Johnson, CLSA. 2 questions if I may. What is the dollar value in U.S. dollars that's been strained down the excess deposits from Asia into Australia? And the second question is on Slide 29, and I think I asked this question the last time around, but I never get my head around it, is why is the Institutional margin higher than the group margin given that that's a business when you think about a bank's -- we don't have a competitive advantage over the corporates themselves. Why is the APEA margin, which has excess deposits, why is it actually lower than the Australian margin given that when you speak to the rating agencies, they'll tell you that Asian portfolio ratings overall are lower than the Australian. So you've got an excess of deposits, you've got a higher credit risk, and yet you've got a lower margin overall? So the streaming and just an explanation of the Institutional margin and the APEA margin relative to the group?

Peter Ralph Marriott
Former Chief Financial Officer

Yes, okay. Brian, in terms of the streaming there, I can't give it to you U.S. dollars -- well because it would be the same, $11 billion bottom line. Slightly down on what I think it was when we last said that. And essentially what's happened is there was very strong deposit growth up through Asia and Europe and America as you would've seen in the numbers. And that was largely invested into liquid assets, because within Australia, we did so much in term funding, well ahead on that term funding program that the funds weren't required bank into Australia so the moneys were kept in liquid assets boosting our liquid assets offshore. In terms of the margin comparisons, remember the other thing you've got to put in their as well as that Institutional carries a higher amount of capital. There's more earning here more -- more risk based allocation of earnings to Institutional, which pushes the margin up. And then you've got also there's the corporate book in there as well as the true institutional end, which pushes the margin up. APEA, while you've got such a mixture of credit cards which really drags the average up because you have margins there, which are very, very high single-digit even occasionally won't get the double-digit but certainly, very, very high single-digit, which pulls the margin up and a write-down to lower risk. So it's so much driven by the mix question that I was mentioning before.

Unknown Executive

Just one thing, Brian. If you look at Page 67 and 84, at a macro level you're probably absolutely right, but in our book, the risk levels relative to grades is actually higher quality in our APEA book relative to the total Institutional book. And that's being quite clear we've stated the very top end of the market on our Institutional business both within the corporations and also within the financial institutions space.

Michael Roger Pearson Smith
Former Non-Executive Advisor

So you have to very careful of what rating agencies you talk to Brian.

Michael Wiblin
Macquarie Research

Mike Wiblin from Macquire. My question is just referring to Page 120, where we've just got a view of the watch and control lists. You can see the watch list ticking up there. I suppose first question is, is that should we be concerned about that? And second is, where are you seeing the sources of stress and I guess just a general view on the outlook for the economy given we've just had a jumbo sized rate cut?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Right. In terms of the watch list. I mean as you'd expect, most of this is in the Commercial book. It's really skewed actually to the agri sector within that Commercial book. And perhaps unsurprisingly in terms of where the economy is, if you think x resources sector, the economy is still struggling, and indeed, the resources sector themselves are putting a lot of projects on hold, which then flows through into the suppliers et cetera, et cetera, et cetera. So it's perhaps not really surprising that there has been a little bit of pain in that in what I'll call the middle market. Having said that, in terms of actual losses, that hasn't come through because of course that sector is generally more highly secured then we see at the top end of town. But in terms of a 50 basis point cut in the RBA, well, obviously, that will help in terms of getting the economy moving along. But will it actually address the real issue of confidence? I think we need some real stability and consistency to actually create business confidence. And I think that that's probably more an issue. But I might ask Nigel to just talk about the credit book.

Nigel Henry Murray Williams
Former Chief Risk Officer

I don't think there's anything new in terms of the credit issues that the book's facing. It's in the retail sector, manufacturing sector, those areas of -- those companies that have largely fixed-price revenue that are exposed to much higher costs. And some of those companies you're seeing exposed to higher cost because the cost structure is going through resource sector and contractors. So those areas aren't new and neither is the risk that we're seeing in Queensland. So I don't think there's anything new issues we've seen in the last 6 months.

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

Brett Le Mesurier, BBY. A couple of questions. First on that flow back of deposits to Australia. What are the accounts imply that they actually go to New Zealand that's in the intersegment elimination, the bottom of the average balance sheet? And then secondly, I want to understand how the change in average interest earning assets in APEA are fitted in with your strategy because they increase by $14 billion in a 6-month period, $4 billion of that, was line assets, $10 billion of that was investments in -- or deposits with the U.S. Fed and other government entities, which looks odd in the context that deposits increased by about $7 billion.

Peter Ralph Marriott
Former Chief Financial Officer

First of all, yes, you're right. One, congratulations, there's a lot of people who do their average balance sheet are very pleased that you raised a question on it. Two, the money which comes into Australia from Asia has been channeled into New Zealand, that's correct. It's been used fundamentally to finance the securitization -- not the securitization, the branch program I should really say. We have their assets securitized occurred across New Zealand into the branch. So that is why that shows up on the average balance sheet. In terms of the rest of the average balance sheet questions there. As was said before, there's been very strong growth in the deposits. And they were funded, as you identified, into very high-quality assets, liquid assets, Central Banks and so forth because the management weren't required back in Australia. So there's additional funds, which are available there that give us more flexibility.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Scott Manning from JPMorgan. Peter, you talked about a few mix factors that are going to offset each other to the margin going into the next half. I just wanted to see whether those margin comments included the mechanical re-basing of the margin outlook for the 50 basis point rate cut, specifically the lower return or free funds and the deposit compression that will come through that?

Peter Ralph Marriott
Former Chief Financial Officer

Well, as I said in my comment, I was talking about the outlook on margin, there are a lot of variables. And yes, the whole BBSW cash spread is a key one that's hard to forecast exactly how that's going to play out so depends upon expectations. And you're right we identified the other one, which isn't a big impact in the second half, it becomes more of an issue going forward is the effect of the lower rate environment on earnings on capital and MBIs. I think a lot of the commentary I've been reading about people focusing on the spread and not thinking about the MBI impact. There's not much for the second half but it is a bigger issue for us all going into 2013. So we literally, as you can imagine, have been running scenarios and there's a whole range of scenarios depending on how exactly it plays out, what the reserve bank does, what the market anticipates, et cetera. So yes, they had regard for that but with a pretty wide distribution, positively and negatively.

Scott Robert Manning
JP Morgan Chase & Co, Research Division

Sorry, just a second question, a follow-on from that, with the 50 basis point rate cut. I know it's the economists saying a bit down on the world with 4% credit growth expected for that [indiscernible] business in the next year, just your thoughts on whether you think that rate cut will see those system rates or credit growth go higher or whether you think it's just basically keeping people in the game for now?

Graham Kennedy Hodges
Former Deputy Chief Executive Officer

I think it's a bit of both. And I think there's probably -- it will certainly stimulate interest but I think that the market already discounted probably $0.25 of that cut in. And I think that, yes, there will hopefully be some stimulation as a result. But is it going to dramatically change things? No, I don't think so.

Jill Craig
Former Group General Manager, Investor Relations

I think we've got 1 more from the floor in Sydney then we'll go the phones.

T.S. Lim
Bell Potter Securities Limited, Research Division

It's the TS from Bellpotter. You referred to the pig in a python effect a couple of years ago and did you think this reflects the state of the economy right now the 2 speed economy where good thing is going but nothing ever gets out. And how do you actually manage -- in terms of practical banking, how do you manage, I think the side effects of this of this phenomenon?

Graham Kennedy Hodges
Former Deputy Chief Executive Officer

Well, I think it is a multi-speed economy. There's no doubt about that. And when you think about it that's normal, it should be normal. We just got used to a situation precrisis where everything was firing on all cylinders. And that's actually not how a normal economy does operate. So I think that we do make to -- or we have to be a bit cleverer in really making sure that, that we can support the growth from businesses that are going to do well in this environment. And of course, there will be, there will be many. And banks included. Banks have to adjust themselves to realize their potential in this sort of environment. And I think this is not sort of rocket science, there has to be a lot of common sense applied. But I am still pretty positive about where the banking industry lies at the moment. I still think whilst it's coming through this turbulent time, there's not -- there's nothing there that can't be managed.

Jill Craig
Former Group General Manager, Investor Relations

If we take the first question from the phone, please?

Operator

Your questions comes from the line of Craig Williams from Citigroup.

Craig Anthony Williams
Citigroup Inc, Research Division

A couple of questions, please. Firstly, the Australian businesses looking at a bit like the big ugly sister in the family portrait this half. Are you concern with the operating trends of this business despite the across the board market share gains or should we also assume that the business has been hit with a liberal dose of corporate overheads and high funding costs of recent. I do note a bit of interest income performance for the group centered this half. And second question related to capital, your Core Equity Tier 1 is now 8.9% or I think 7.8% on a Basel III basis. Are you -- where you need to be yes or does your different strategy in Asia so you're needing to build capital higher than peers and certainly, higher from here?

Michael Roger Pearson Smith
Former Non-Executive Advisor

On the ugly sister, Phil is actually -- he's -- I think he's well positioned to take advantage of some of the tasks that we've actually set ourselves have been done in this half, that will flow through the benefits, that will flow through in the second half of next year. And also the different pricing mechanism we've now introduced is going to be much easier I think to manage our margin more effectively, Craig. So I think we've got the building blocks in place there to actually bring that -- the performance back. In terms of the capital, I wish I knew. Every time we seem to get to the place that we want to be, our regulators say we require more capital. It is an issue for this -- for the industry. How much is enough? I mean if you look at what we -- how much capital we are holding now compared to precrisis, we're actually holding double the amount of capital that we had in 2007 to support the same size business on a like-for-like basis. That is all been at the behest of regulators. And we continue to be told that we require more capital for this more capital for that. So it is a difficult situation we're in and it is still not very clear. All I can tell you is that capital requests never seemed to go down. It appears to be one way. But at some stage, this has to stop because it's going to have an effect on the underlying economy. You cannot keep going and forever increasing capital requirements. So I think some of these regulators have no natural predators, that's the problem and therefore, they are -- there hasn't been I think, not all of the dots have been joined so we are where we are. We're in a good position in terms of our competitors that's all I could say.

Operator

The next question comes from the line of Andrew Lyons from RBS.

Andrew Lyons
RBS Strategy

Your domestic Commercial lending book in a lot of recent comments actually grew by a fairly respectable 7% year-on-year. Can you perhaps just talk about the extent to which ANZ is picking up share in this space? And which segments of the market are providing them, some better balance sheet momentum for the division?

Peter Ralph Marriott
Former Chief Financial Officer

We give you a breakdown on Page 52 of the results announcement. So that 7% growth you see it's particularly coming out of business banking is the main one was 9% and 13% coming out of Small Business banking, that's us trying to reclaim some of the ground in those parts of the business. Tougher in Regional and Commercial, obviously, because that's economically a tough environment and I think only 4% but still quite respectable and Esanda sitting at about 4% as well with Leasing business. So it's particularly us making more and more inroads into some of our traditional territory in the business banking and small business customers.

Jill Craig
Former Group General Manager, Investor Relations

Phil, did you want to add anything?

Philip Wayne Chronican
Former Chief Executive Officer of Australia

I'll just add that it's a very deliberate strategy to rebuild the ANZ presence in that small and medium-sized business markets. We think it's a very natural place. We think that medium term profitability there is more secure than it is likely to be in the consumer side of the business. The brand works there. Our capabilities in institutional and in the region play well particularly for those businesses that are focused in on import or export, therefore our trade finance capability has got leverage as well and it supports the foreign exchange business. So we see taking what is very strong market position we've had in Institutional and then trying to recalibrate our Commercial and middle markets positioning in line with that is a very natural thing for us to do. And gives us a much better and more stable source of earnings within the overall Australian business.

Jill Craig
Former Group General Manager, Investor Relations

We've got 1 last question from the phone, please.

Operator

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

Unknown Analyst

Just to take Craig's point further on capital. How does operational risk sort of fit into the picture, because if I triangulate a couple of points, you're clearly the most critical Australian bank CEO with respect to Basel III. CBA's new CEO suggests that a key reason for not offshoring is the elevated operational risk that you face in Asia. So therefore, could you sort of take us through a couple of points, one, what is the nature and extent of your offshored operations? Has APRA audited those functions. And if operational risk is elevated from offshoring, what are the implications for capital and how do you sort of trade off that cost versus capital equation?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Yes. I don't think there is any difference in your operational risk profile. It doesn't matter where you actually put your operational centers. I would dispute the fact that there's any difference. In fact, what matters is how you run them. It is the efficiency and the talent that you have actually running them. And yes, APRA do inspect our operational hubs as a matter of course.

Unknown Analyst

Okay. Perhaps a cheeky question, but given the renewed emphasis on cost management in the organization, will you have to give up the corporate jet?

Michael Roger Pearson Smith
Former Non-Executive Advisor

Well, I wish I had one.

Jill Craig
Former Group General Manager, Investor Relations

Matt, just to add, the banking personnel in those offshore -- they maybe, like headed offshore but they are ANZ personnel. So I think one of the points, if I recall it correctly, that [indiscernible] was making, was that quite often, in offshoring, you're actually putting your operations outside of your company and that you lose some control over risk that way, whereas it's a different outcome for us.

Peter Ralph Marriott
Former Chief Financial Officer

Plus it provides a geographic diversity as well rather than everything being in Melbourne, or everything being in Sydney, it means we're spread across 3 additional locations with the backup that, that provides.

Jill Craig
Former Group General Manager, Investor Relations

Thanks. And I think with that, I know there is a couple of questions in Sydney, but we might follow those up after the presentation. We've been going for quite a while now. So with that, Mike, did you have any closing comments.

Michael Roger Pearson Smith
Former Non-Executive Advisor
No -- well yes, I will. Thanking you for coming along today. As I said, I think this is a pretty strong result in what are fairly difficult operating environment. And I think again, this is another clear example where we can see that the benefits of our strategy are now beginning to come through in terms of real result. So with that, thank you for -- thank you for attending. Many thanks.