

## News Release

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### **Transcript of bluenotes video interview with ANZ Chief Financial Officer Farhan Faruqui**

BRETT FOLEY: Farhan, thanks for joining us on the morning of the result. Both you and Shayne talk about the benefit of a diversified portfolio. With the CFO lens, how has that diversification specifically contributed to this result?

FARHAN FARUQUI: Well, I would say, Brett, that diversification has probably been never as, or the benefits of diversification, have actually never been as evident as they were this year. And I think in particular this half as well. Basically, when we think about diversification, we think about it in the context of taking advantage of the benefit of the scale of each of our businesses. The mix of geography and customers, and our ability to capture opportunities that come across each of those businesses. And I think that's particularly relevant in a time when we've seen very different trends across our four businesses in this year. We've seen an Australia Retail business, which has been intensely competitive and has seen drags on margins, et cetera. But at the same time, we've seen the benefits of our large Institutional business because of its geographic and customer mix and product mix, benefiting greatly in this diversification, through this period of uncertainty and volatility. So, you sort of have the ability to balance your portfolio, how you allocate capital, how you manage the investment during this period of time, and how you can actually create opportunities to either offset any part of our business, which is potentially going through a difficult cycle, through capturing opportunities in other parts of the portfolio which are benefitting. So, we've had that benefit this half and for the full year, and we've seen our Commercial business doing really well, our Institutional business doing really well, our New Zealand business performing well and some challenges around the Australia Retail business. But the portfolio mix actually provides great impetus for getting great return outcomes and growth as well.

BRETT FOLEY: So Farhan, the Institutional business is a fundamentally different business today in terms of how it makes its money and where, can you tell us a little bit about that transformation?

FARHAN FARUQUI: No, absolutely, Brett, I will talk about, the earnings profile is very different to what it used to be, but I think it's important to state upfront that it is a demonstrably less risky business than it used to be seven, eight years ago. It is a higher returning business and a far more resilient and sustainable business as we look forward. And the reason for that, is that when we started the journey about seven years ago around transforming the Institutional business, the first order of work was to look at our customers, and understand the riskiness of those customers, and understand the value that we were delivering to them and the value that they were attributing to what we were delivering to them in terms of our product, in terms of our network. And that led us to effectively reshaping our customer portfolio. So, over the period of time between then and now, we have reshaped the customer portfolio to be, to have gone from 27,000 customers now down to about 7,000 customers, with a skew towards higher investment grade, higher proportion of our customers in financial institutions and sovereigns, which are less risk in terms of long run loss rates relative to some of our corporate customers. And within corporate, a much greater degree of investment grade, shorter tenure, more secured. So, it's a much, much better quality portfolio, and that has happened over years, so it's not something you do overnight. So that's one big change that's happened to that business

and that discipline is still continuing. The second thing that we did while we were reshaping, is that we invested in the business and we invested in particular around technology. We looked at cash management, our payment systems, our FX and rates platforms, and we made sure that we built effectively what was a seamless, connected experience for our customers – no matter which part of our geographic network you were operating in. And that is what we call a digital backbone. So, whether you're sitting in Hong Kong or you're in Singapore or you're in India or you're in Australia, or New Zealand, you effectively face into the same system and you're able to operate seamlessly across the network because many of our customers do use us in multiple countries and they want that seamless experience. And I think that's just been a long journey to get there and I think that's really helped us to reshape the quality of our business. Where the outcome has been, that we now have three parts of the Institutional business all equally weighted. So, we have our lending activity, which is roughly about \$2 billion of revenue. We have our transaction banking product suite, which includes trade and cash management and payments, which is also about \$2 billion. And then we have our markets platform, which is FX, rates, commodities, capital markets, et cetera, also roughly about \$2 billion. That's the first time that we've achieved that outcome, and that's been driven by the reshaping of our portfolio and the investment that we've had in our technology. And as a result of that, it is sustainably a higher returning business, well above cost of capital, across all three products, as well as across all three geographies – Australia, New Zealand and our international business. And we are very confident that this is something we can sustain going forward.

BRETT FOLEY: You spoke about the investment in Institutional. We're also now seeing investments in ANZ Plus and into the Commercial division – are there greater synergies kind of emerging from the investments in all those different areas?

FARHAN FARUQUI: Yes, there are. So, if you think about the payments business, we actually had great success with the payments business because we sort of... the lesson we learned was that we basically took that business and built it centrally, i.e., in a centre of excellence, and to serve the entire bank to provide a reliable service that had a great customer experience associated with it. And we invested appropriately in it to ensure that it aligned with our intent and ambition. And as a result of that, that business today serves the Institutional bank, the Commercial bank, as well as retail capabilities around payments. So, it's built as an enterprise function rather than as an Institutional product capability. So, an example of that, Brett, is the fact that today 70%, near 70%, of the users of our cash management platform are actually Commercial bank customers. So, it is an investment that we've leveraged across the enterprise. Now, there are other things obviously, that we're looking at in terms of building out similar sort of capabilities. ANZ Plus, which is a great example, which is our now new retail, digital retail bank is actually building incredible capability, including things like onboarding or product management. And we want to take some of those learnings and apply them on an enterprise-wide basis as well, so that we have a common service approach to our entire set of customers across the enterprise. And those allow us then to be efficient, in terms of cost, but it allows us to deliver a really good experience to our customers and equally importantly, if not more, by virtue of creating that uniformity of common services, it allows us to reduce non-financial risk in our business. So, this is an important focus for us and one that we will continue to come out with new common service platforms going forward.

BRETT FOLEY: So, we've seen some pretty extreme movements in interest rates and inflation in the last 12 to 18 months. How do you think about that and how did ANZ sort of navigate those trends?

FARHAN FARUQUI: Yeah, so look, I mean, I think there is obviously a human side of this issue as well because obviously there are, there is stress in households across the country in terms of the challenges we're facing with inflation and rising cost of interest. But the experience that we've had from a portfolio standpoint is that our customers have actually

been a lot more resilient facing into this. Now, you would argue that four to five per cent rates are not particularly high in the context of history, but it is the speed with which that acceleration took place, which I think is causing a little bit of imbalance between the abilities, ability of the households to reorient themselves to the higher level of rates after having enjoyed a lot of low rates, a long period of low rates for some time. So, I think that there is that human element which of course, the country and households are adjusting to, but they're coming off a strong, resilient base, which is why we haven't seen any portfolio, significant portfolio degradation as a result of the rising rates. But having said that, Brett, we said about a year and a half ago when rates first started to rise that look, you know, typically what happens in these environments is that your cost as a bank gets impacted first, because you pay your people and you have to pay them in line with the sort of inflationary challenges that they're facing into, just as households are. So, there's wage increases, which of course puts pressure on cost. The benefits of revenue coming from higher rates do come through, but we also said that those benefits do get competed away and we started to see that in the course of this year with some of the benefits of raising rates have sort of gotten competed away. And then the third, is a period when there will be some more risk and credit losses simply because of the fact that households are having to face into a tough time and those who are not able to make that transition in time to the higher rate environment from a cost of living perspective will face into some challenges. So that's sort of the normal history of how these things operate. It's no different this time, and we've seen costs rising. We've seen rate benefits sort of starting to fade. And while we haven't seen risk play out yet, there will be a time when, you know, in the next 12 months or 24 months when there'll be some increases in the cost of credit. Our focus in the context of this, is A) support our customers to get through any hardships that they might be facing, B) manage our cost. I don't think this is a one-off issue. I think the banking industry as a whole has to continue to make itself more efficient. And that's a journey we've been on, and we've shown a long track record of having delivered on productivity and cost out ambitions, and we're just going to continue doing that as well as we have done in the past. And the third thing, of course, is to make sure that we are using that diversified portfolio to get the benefits on the revenue side by counteracting where there might be pressures and where there might be opportunities in certain other parts of our portfolio.

BRETT FOLEY: ANZ tends to talk about risk adjusted margin, can you talk us through why that's such an important metric?

FARHAN FARUQUI: So, risk adjusted margins versus net interest margins, which is where I think there's a lot of focus across the world from an industry standpoint. You know, it's an interesting question because, you know, I think NIM is important. I think it's important to measure net interest margin. But the reality is that net interest margin, from a correlation point of view to return on equity, there is almost no correlation. You can actually grow your net interest margin without having an impact on ROE. In fact, you can degrade your ROE while you're expanding net interest margin, and that's because net interest margin doesn't measure risk. It also doesn't measure operating expenses. So, to some extent, it is an important measure to look at, but it simply does not tell the whole story. And with the risk adjusted margin, you are able to benchmark the return you are generating in the context of the risk you're taking. And I think that's a really, really important measure for banks, particularly as we enter into the uncertain environment that we are facing into. And we've actually seen our risk adjusted margin expand continuously over the last six, seven years, over the net interest margin. And that actually shows that we are performing and delivering returns on a risk adjusted basis, which is really what our shareholders care about, that we are not taking undue risk and we are getting paid appropriately for the risks that we are taking. So, we think that risk adjusted margin actually helps us measure our real performance, and it also helps us to make sure that we are driving the right behaviour, in terms of the kind of risk and returns we're generating in our business.

BRETT FOLEY: Farhan, thanks very much for your time.

FARHAN FARUQUI: Thank you very much, Brett.

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