FitchRatings

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Fitch Affirms ANZ Bank New Zealand at 'A+'; Outlook Stable

Fitch Ratings - Sydney - 10 Oct 2024: Fitch Ratings has affirmed ANZ Bank New Zealand Limited's (ANZNZ) Long-Term Foreign- and Local-Currency Issuer Default Ratings (IDRs) at 'A+', Short-Term Foreign- and Local-Currency IDRs at 'F1', Shareholder Support Rating (SSR) at 'a+' and Viability Rating (VR) at 'a'. The Outlook on the Long-Term IDRs is Stable.

Key Rating Drivers

Support Prospects: ANZNZ's SSR and Long-Term IDRs reflect Fitch's assessment of a very high likelihood of support from the bank's Australia-based owner, Australia and New Zealand Banking Group Limited (ANZ, AA-/Stable/a+), if required. The anchor rating for ANZNZ's SSR and Long-IDRs is ANZ's VR as it is unclear whether qualifying junior debt buffers being built by ANZ will be pre-placed or effectively available to support ANZNZ's senior creditors.

Integral Subsidiary: ANZNZ's SSR reflects its position as a key and integral part of ANZ, offering products and services in the group's core market, New Zealand. A sale would be very hard to conceive and would noticeably alter the overall shape of ANZ, while any default of ANZNZ would constitute huge reputational risk for ANZ, damaging its franchise. Fitch expects the Australian and New Zealand banking regulators to allow support to flow as required.

Reduced Household Sector Risk: Fitch has revised the operating environment score for New Zealand banks to 'a+'/stable from 'a'/stable to reflect a sustained reduction in risks from the household sector over the last decade, due in part to a strengthened regulatory environment. However, household debt remains high relative to many other jurisdictions and we maintain the score below the implied 'aa' category score to reflect this.

The strengthened regulatory framework includes macro-prudential speed limits on riskier residential mortgages, which should reduce asset quality pressure as unemployment rises. The score also incorporates the small, open nature of New Zealand's economy, which leaves it susceptible to global shocks.

Market Position Underpins VR: ANZNZ's VR, which is in line with its implied VR, is supported by its large domestic market position. This allows for a simple business model, which underpins the financial profile. The 'a+' business profile score is above the implied 'bbb' category score to capture the strong market position. ANZNZ is New Zealand's largest bank, with market share of more than 20% across residential mortgages, agriculture loans and business loans, as well as deposits.

Robust Risk Management: ANZNZ manages risks well, benefitting from both regulatory oversight and access to expertise and policies from the parent. Credit risk remains ANZNZ's main risk and stems primarily from the loan book, which made up 77% of total assets at end-March 2024.

Peak Stage 3 Loan Ratio in 2025: We expect ANZNZ's stage 3 loan/gross loan ratio to peak in 2025 as the full effect of rapid interest-rate hikes in 2021-2023 and increased unemployment put pressure on some borrowers' repayment capability. The ratio rose by 30bp to 1.1% by end-March 2024. Provisioning levels will probably remain stable due to the utilisation of existing overlays raised for weaker economic conditions as impaired-loan balances rise.

Stable Profitability: We expect ANZNZ's operating profit/ risk-weighted assets (RWA) ratio to be relatively stable in the financial year ending 30 September 2025 (FY25), with a modest reduction in the net interest margin, driven by an easing rates cycle, offset by modest loan growth and cost control. Cost efficiency should remain strong, with the cost/income ratio likely to remain around 35%.

Capitalisation to Improve: We expect the common equity Tier 1 (CET1) ratio to continue to rise towards 14% from the 12.8% reported at end-March 2024 as the bank builds towards final implementation of the new capital framework in mid-2028. The framework is more conservative than global rules, and we take this into consideration when assigning the factor score at 'a', above the implied 'bbb' category.

Broadly Stable Funding: We expect ANZNZ's deposit growth to modestly lag loan growth over the next two years, but for the core metric, loans/customer deposits, to weaken only marginally. The loan/ customer deposit ratio was 112% at end-March 2024 and we expect it to remain below 115% through to FYE25. Liquidity is well-managed, with the bank reporting regulatory liquidity ratios well in excess of minimum requirements.

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/ Downgrade

Long-Term IDRs and SSR

Any downgrade of ANZ's VR is likely to result in a downgrade of the SSR and Long-Term IDRs assigned to ANZNZ; see Fitch Upgrades Australia and New Zealand Banking Group to 'AA-'; Stable Outlook, published on 27 May 2024, for the key drivers and sensitivities of ANZ's VR.

The Long-Term IDRs and the SSR may also be downgraded should we change our view on ANZNZ's importance to ANZ. This could be reflected in a partial or full sale of ANZNZ or a decision to significantly scale back operations within New Zealand. Weakening co-operation between authorities in Australia and New Zealand may indicate a reduced ability for ANZ to provide support in a timely fashion, and put pressure on the ratings. However, neither of these scenarios is likely in our view.

VR

The VR could be downgraded if deterioration in the economic environment results in a combination of:

- The four-year average of the stage 3 loan/gross loan ratio increasing significantly above 1.5% (FY20-FY23: 0.7%) for a sustained period;

- The four-year average of the operating profit/RWA ratio falling consistently and significantly below 2.0% (FY20-FY23: 2.6%);

- The CET1 capital ratio declining below 10.5% without a credible plan to return to above this level (end-March 2024: 12.8%).

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

Long-Term IDRs and SSR

An upgrade on ANZ's VR is likely to be reflected in ANZNZ's SSR and Long-Term IDRs, as long as there is no change to ANZ's propensity to support ANZNZ.

We may also change the anchor rating to ANZ's Long-Term IDR if qualifying junior debt or equity is pre-placed in ANZNZ to meet resolution requirements or ANZ's resolution plans identify ANZNZ as a beneficiary of intra-group resources. This would result in an upgrade of ANZNZ's SSR and Long-Term IDRs.

VR

An upgrade of the VR would require that ANZNZ maintain its strong business profile in combination with a sustained improvement in its asset quality, capital and funding metrics.

OTHER DEBT AND ISSUER RATINGS: KEY RATING DRIVERS

Short-Term IDR

The Short-Term IDRs of 'F1' are at the lower of the two options available at a Long-Term IDR of 'A+', as the parent's funding and liquidity score is below 'aa-'. This is the threshold for an 'F1+' Short-Term IDR.

Senior Unsecured

ANZNZ's senior unsecured debt is rated in line with its IDRs, in line with Fitch's *Bank Rating Criteria*.

OTHER DEBT AND ISSUER RATINGS: RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade:

Short-Term IDR

ANZNZ's Short-Term IDRs may be downgraded if the Long-Term IDRs are downgraded to 'A-' or below.

Senior Unsecured

ANZNZ's senior unsecured debt ratings would be downgraded if ANZNZ's IDRs are downgraded.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade:

Short-Term IDR

ANZNZ's Short-Term IDRs would be upgraded if the Long-Term IDRs are upgraded to 'AA-' or the parent's funding and liquidity score was raised to 'aa-'.

Senior Unsecured

ANZNZ's senior unsecured debt ratings would be upgraded if ANZNZ's IDRs are upgraded.

SUBSIDIARIES & AFFILIATES: KEY RATING DRIVERS

ANZNZ issues foreign-currency wholesale funding through its wholly owned subsidiary, ANZ New Zealand (Int'l) Limited (ANZIL). ANZIL is used for funding purposes only and is not rated by Fitch; Fitch only rates the debt that it issues. The debt ratings are aligned with ANZNZ's IDRs, as ANZNZ guarantees ANZIL's senior unsecured debt instruments and the guarantee ranks pari passu with ANZNZ's senior unsecured debt.

SUBSIDIARIES AND AFFILIATES: RATING SENSITIVITIES

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade:

The ratings of the guaranteed instruments issued by ANZIL would be downgraded if ANZNZ's IDRs are downgraded.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade:

The ratings of the guaranteed instruments issued by ANZIL would be upgraded if ANZNZ's IDRs are upgraded.

VR ADJUSTMENTS

The operating environment score of 'a+' has been assigned below the 'aa' category implied score for the following adjustment reason: level and growth of credit (negative).

The business profile score of 'a+' has been assigned above the 'bbb' category implied score for the following adjustment reason: market position (positive).

The capitalisation and leverage score of 'a' has been assigned above the 'bbb' category implied score for the following adjustment reason: leverage and risk-weight calculation (positive).

Sources of Information

The principal sources of information used in the analysis are described in the Applicable Criteria.

REFERENCES FOR SUBSTANTIALLY MATERIAL SOURCE CITED AS KEY DRIVER OF RATING

The principal sources of information used in the analysis are described in the Applicable Criteria.

Public Ratings with Credit Linkage to other ratings

ANZNZ's Long-Term IDRs are equalised with the VR of its Australian parent, given our view of potential support from ANZ. The ratings of the senior debt issued by ANZIL are equalised with ANZNZ's IDRs, as the parent provides guarantees for these instruments.

ESG Considerations

The highest level of ESG credit relevance is a score of '3', unless otherwise disclosed in this section. A score of '3' means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. Fitch's ESG Relevance Scores are not inputs in the rating process; they are an observation on the relevance and materiality of ESG factors in the rating decision. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/topics/esg/products#esg-relevance-scores.

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Rating Actions

ENTITY/DEBT	RATING			RECOVERY	PRIOR
ANZ New Zealand (Int'l) Limited					
• guaranteed	LT	A+	Affirmed		A+
• guaranteed	ST	F1	Affirmed		F1
ANZ Bank New Zealand Limited	LT IDR	A+	Affirmed		A+
	ST IDR	F1	Affirmed		F1
	LC LT IDR	A+	Affirmed		A+
	LC ST IDR	F1	Affirmed		F1
	Viability	a	Affirmed		a
	Shareholder Support	a+	Affirmed		a+
• senior unsecured	LT	A+	Affirmed		A+
• senior	ST	F1	Affirmed		F1

ENTITY/DEBT	RATING	RECOVERY	PRIOR
unsecured			

RATINGS KEY	OUTLOOK	WATCH
POSITIVE	⊕	⬘
NEGATIVE	⊖	⬙
EVOLVING	⊙	◆
STABLE	⊙	

Applicable Criteria

Bank Rating Criteria (pub.15 Mar 2024) (including rating assumption sensitivity)

Additional Disclosures

Solicitation Status

Endorsement Status

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The complete span of best- and worst-case scenario credit ratings for all rating categories ranges from 'AAA' to 'D'. Fitch also provides information on best-case rating upgrade scenarios and worst-case rating downgrade scenarios (defined as the 99th percentile of rating transitions, measured in each direction) for international credit ratings, based on historical performance. A simple average across asset classes presents best-case upgrades of 4 notches and worst-case downgrades of 8 notches at the 99th percentile. For more details on sector-specific best- and worst-case scenario credit ratings, please see Best- and Worst-Case Measures under the Rating Performance page on Fitch's website.

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