MAJOR AUSTRALIAN BANKS

The calm before the storm?

Full Year 2022 Results Analysis

November 2022

Contents

Full Year 2022 Results Snapshot

REVENUE

Operating income increased by 1.6% to

↑ $80.7 billion

Net interest income increased by 2.9% to

↑ $65.8 billion

EARNINGS

Cash profit after tax increased by 6.5% to

↑ $28.5 billion

Average net interest margin decreased by 9.5 bps to

↓ 178 bps

SHAREHOLDER RETURNS

Average return on equity[1] increased by 0.7% pts to

↑ 10.6%

Average dividend payout ratio remained steady at

– 71.0%

EXPENSES

Average cost to income ratio decreased by 2.0% pts to

↓ 50.2%

Share of risk and compliance of total investment spend decreased by 6.1% pts to

↓ 45.0%

ASSET QUALITY

Average credit impairment provisions (as % of GLA) decreased by 11 bps to

↓ 0.66%

Write-back of credit provisions of

$925 million

BALANCE SHEET

Average CET1 capital ratio decreased by 102 bps to

↓ 11.7%

Deposit to loan ratio decreased 0.1% pts to

↓ 86.1%

Lending assets increased by 7.0% to

↑ $3 trillion

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*Comparisons are to the 2021 financial year, unless otherwise stated and adjusted for restatements as applicable

[1] Includes notable items

At a glance

	ANZ		CBA[1]		NAB		WBC	
	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21
Ranking								
By profit before tax	2	3	1	1	3	2	4	4
By total assets	2	2	1	1	3	4	4	3
By total equity	3	3	1	1	4	4	2	2
By market capitalisation	4	4	1	1	2	3	3	2
By CET 1 capital ratio	1	3	3	1	2	2	4	4
Financial Performance – P/L (continuing operations)								
Operating Income – cash basis ($ million)	18,547	17,447	24,896	24,156	18,296	16,806	19,001	21,038
Profit before tax – statutory basis ($ million)	10,079	8,936	13,684	12,375	9,744	9,068	8,469	8,501
Profit after tax – statutory basis ($ million)	7,138	6,179	9,673	8,843	7,060	6,471	5,699	5,463
Cash profit after tax ($ million)	6,515	6,198	9,595	8,653	7,104	6,558	5,281	5,357
Performance Measures – P/L (continuing operations)								
Net interest margin – cash basis (basis points)	163	164	190	208	165	171	193	206
Cost to income ratio – cash basis (%)	49.7	52.3	46.7	47.0	45.2	46.5	55.1	62.7
Basic earnings per share – statutory basis (cents)	250.0	215.3	561.7	499.2	219.3	196.3	159.9	149.4
Basic earnings per share – cash basis (cents)	228.8	216.5	557.1	488.5	220.7	199.3	148.0	146.3
Return on average equity – cash basis (%)	10.4	9.9	12.7	11.5	11.7	10.7	7.5	7.6
Credit Quality Measures								
Impairment charge/(benefit) (statutory basis) ($ million)	(232)	(567)	(357)	554	125	(217)	335	(590)
Impaired loans to loans and advances to customers (%)	0.21	0.31	0.33	0.42	0.15	0.20	0.20	0.30
Collective provision to credit RWA (%)	1.1	1.2	1.2	1.4	1.3	1.4	1.2	1.2
Financial Position								
Total assets ($ million)	1,085,729	978,857	1,215,260	1,091,975	1,055,126	925,968	1,014,198	935,887
Total equity ($ million)	66,400	63,676	72,838	78,688	59,032	62,779	70,452	72,092
Capital Measures								
Capital Adequacy Ratios (%)								
- Total	18.2	18.4	17.6	19.8	18.2	18.9	18.4	18.9
- Tier 1	14.0	14.3	13.6	15.7	13.1	14.6	13.4	14.7
- Common Equity Tier 1	12.3	12.3	11.5	13.1	11.5	13.0	11.3	12.3
Market capitalisation ($ billion)[2]	68.1	78.7	153.6	177.0	90.8	91.3	72.3	95.4

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[1] CBA reported as at 30 June 2022. All other majors reported as at 30 September 2022.
[2] Market capitalisation as at the respective reporting date of each Major Bank.

RESULTS SUMMARY

Executive summary

The 2022 full year results of the Australian major banks (the Majors) saw an increase in aggregate cash profit after tax of 6.5 percent. The results highlighted continued improvements in portfolio quality as well as the initial benefits of an increasing interest rate environment.

> "After over a decade of ultra-low rates weighing on bank profitability, the recent rapid rises in interest rates are starting to provide some initial margin relief for the Majors."
>
> **STEVE JACKSON**
> KPMG AUSTRALIA'S HEAD OF BANKING AND CAPITAL MARKETS

Highlights

The Majors reported a combined **cash profit after tax** from continuing operations of $28.5 billion, up 6.5 per cent from FY21. This result reflects strong growth in housing credit, with improved asset quality leading to reductions in provisions (including $925 million of write-backs) and increasing net interest margins compared with that of 1H22 on average across the four Majors.

The average **net interest margin** (cash basis) increased by 3 basis points compared to that of 1H22, although it is 10 basis points lower than FY21. As such, the Majors' FY22 results include early indications of the positive impact of increased interest rates.

The **average ratio of impaired loans** continued to decrease in FY22, down by 8 basis points from that of FY21 to 0.23 per cent. This is a result of a decline in delinquencies to the lowest levels since 2018 and may also reflect the natural lag in the impact of interest rate increases on mortgage holders.

Cost-to-income ratios decreased modestly from an average of 52.2 per cent in FY21 to 50.2 per cent. Excluding notable items, operating costs increased by 1.3 per cent to $39.2 billion, reflecting lower remediation and provisioning costs, although offset by an increase in personnel costs and investment spend.

On average the Majors' **Common Equity Tier 1 (CET1) ratio** decreased 102 basis points to an average of 11.65 per cent as all Majors completed share buy-backs during the year and, simultaneously, lending growth has driven higher Credit Risk-Weighted Asset (CRWA). The Majors' CET1 ratio remains comfortably above APRA's 'unquestionably strong' benchmark of 10.5 per cent.

Dividend pay-out ratios remained steady compared to that of FY21 at 71 per cent on average, which resulted in improved dividend yields of 5.57% (up from 4.38% in FY21). Both the yield and dividend per share were up across all four Majors.

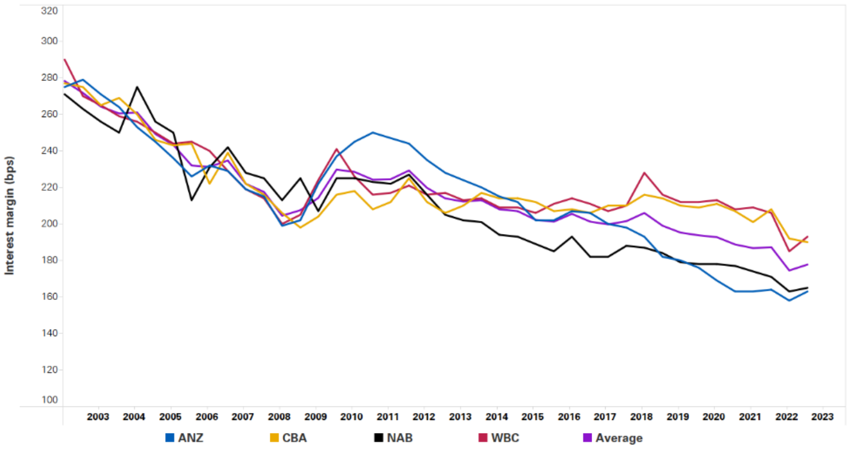
The growth in earnings has seen **Return on Equity** (ROE) increase by an average of 66 basis points from that of FY21 to 10.6 per cent, returning to the double-digit standards experienced prior to the pandemic.

Observations

Margins showing early signs of improvement

The Majors realised more normalised and positive results in FY22, driven by the post-Covid stability seen across the Australian economy. The FY22 results show the first indications that net interest margins (NIM) may have passed their low point, with the average NIM increasing by 3 basis points compared to that of 1H22, though 10 basis points lower than FY21. This is largely the result of 5 successive rate increases by the RBA from May through to September 2022 (the period covered by this report), taking the cash rate from 0.10% to 2.35%, with two further increases in October and November 2022. The Majors, as well as their competitors, have largely passed the increases on to their borrowers.

Diagram 1. **Net Interest Margins**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Stubborn costs

The Majors have worked hard throughout the year to address their cost bases, but overall costs have increased marginally, with the average increase across the Majors being 1.3%. All the Majors have signalled that their cost targets will either be adjusted or abandoned as these inflationary pressures continue. The average cost-to-income ratio decreased from FY21 by 300 basis points to 49.2%. Several factors including continued regulatory compliance requirements, ongoing customer remediation (albeit declining) and increased labour and FTE costs are putting pressure on the overall cost-to-income ratios.

> "What will prove interesting is how the costs will play out, with inflation putting further pressure on the pace of transformation. With the backdrop of a tight labour market, competition for skilled resources will place pressure on staff costs as banks respond to attract and retain the right skill sets."
>
> **MARIA TRINCI**
> KPMG BANKING PARTNER

Re-pivoting provisioning

The significant Covid related provisions raised by the Majors in 2020 have now been effectively released. Underlying credit quality of the Majors' lending portfolios have returned to pre-pandemic levels, with 90+ day delinquencies decreasing to their lowest levels since 2018.

Though credit quality remains strong at this point, the Majors are signalling a likely economic slowdown, leading to increased unemployment, falling house prices, and increased interest rates into 2023. These factors are expected to lead to raised provisions in the years ahead.

Outlook

Despite the Australian economy's strong rebound from the height of the pandemic, the global economic outlook remains uncertain amidst inflationary pressures, geopolitical unrest, and an expected global economic slowdown. Kicking a historic decade long trend, the RBA's seven successive interest rate rises during 2022 are yet to materially impact domestic demand.

Whilst the increasing interest rate environment is likely to continue to support a recovery in the Majors' net interest margins, inflation is likely to also continue to place pressure on the majors' cost bases and, should interest rate rises continue at pace, the potential economic slowdown, increase in unemployment and falls in house prices could present a more challenging landscape for the majors.

The outlook for growth is therefore uncertain, particularly in the context of recent divestments and the majors' concentration on mortgage and business lending and with transformation activities and new tech-enabled business models yet to generate significant returns.

The economy appears strong at present, and the RBA has pointed to improved resilience in households to withstand the effects of higher rates as supportive macroeconomic measures over the course of the pandemic have resulted in significant savings buffers. However, these buffers may be tested in the coming months as the impact of rate rises begins to impact borrowers.

The big question is how far and how fast interest rates will rise as this will determine for the economy and for the majors, whether this is the calm before the storm.

> "Banks are signalling challenging times ahead for the economy and the big question is whether a 'soft landing' will be achieved that avoids the harsher potential outcomes."
>
> **STEVE JACKSON**
> KPMG AUSTRALIA'S HEAD OF BANKING AND CAPITAL MARKETS

Income

Margins continued to tighten across the Majors during the year, although there are signs in the FY22 results that they may have passed their low point. While down compared to that of FY21, net interest income increased slightly in the second half of FY22.

Diagram 2. **Net interest incomes**

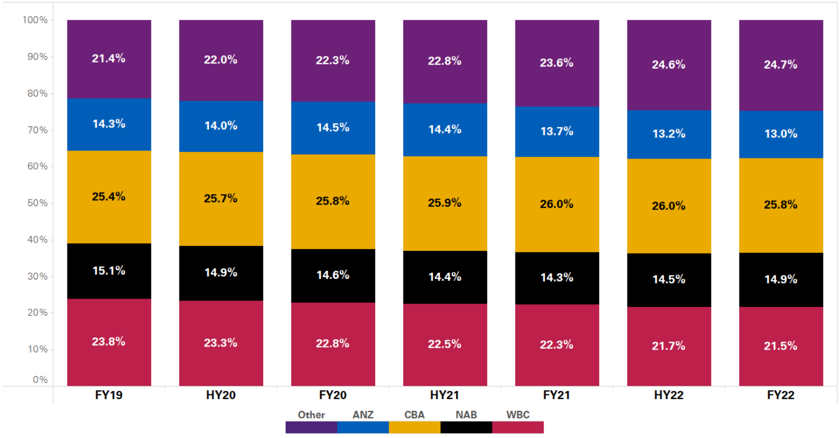
Cash Basis	FY22	FY21	Movement
Net Interest Income ($million)			
ANZ	14,874	14,161	5.0%
CBA	19,473	19,302	0.9%
NAB	14,852	13,797	7.6%
WBC	16,605	16,714	(0.7%)
Aggregate	**65,804**	**63,974**	**2.86%**
Net Interest Margin (basis points)			
ANZ	163	164	(1)
CBA	190	208	(18)
NAB	165	171	(6)
WBC	193	206	(13)
Average	**178**	**187**	**(10)**

Net interest margin

Net interest margins across the Majors rose during the second half of FY22, although it was still 10 basis points lower than that of FY21. While the increase in the second half is a benefit to the Majors because of increasing interest rates, margin pressure remains due to these key drivers which were consistent across the Four Majors:

- Increased competition both amongst the Majors and from challenger banks and non-bank lenders, particularly impacting home lending margins. The combined Majors' home lending market share has decreased from 78.6% at the start of 2019 to 75.3%(see Diagram 3);
- Refinancing activity within mortgage lending competition as customers took advantage of lower margin fixed rate loans; and
- Continued growth in lower yielding liquid assets to replace Committed Liquidity Facilities as required by the regulator (APRA).

Diagram 3. **Mortgage lending market shares**



Source: APRA Monthly Authorised Deposit-taking Institution Statistics

Interest earning assets

Average interest earning assets increased by 9.3 per cent from FY21 to $933.6 billion with all four Majors reporting increases. This was primarily driven by growth in non-housing credit which includes business and personal lending.

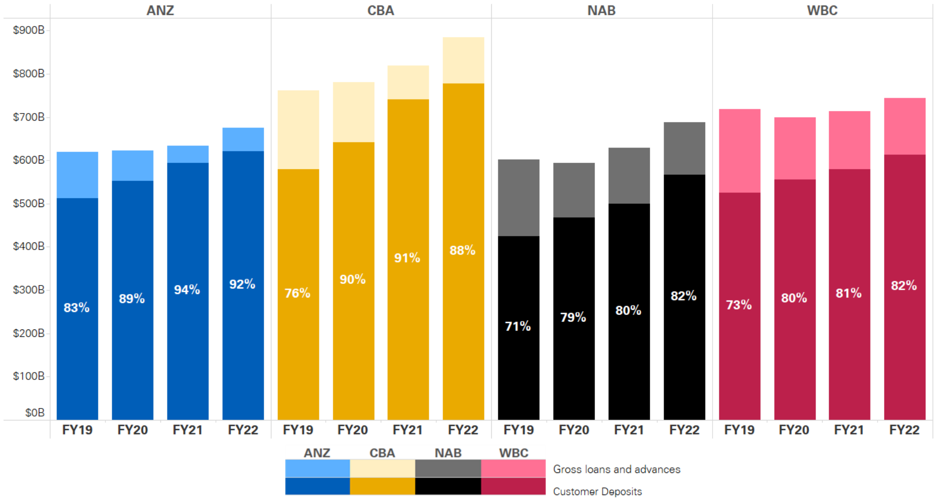
Mortgage lending saw an average growth of 5.7 per cent across the Majors in FY22 to a total of $1.91 billion. The growth was predominantly driven by stronger demand for credit and overall system growth across the Australian market.

Funding Mix

Customer deposits remain the primary source of funding for the Majors. The average proportion of customer deposits to total gross loans and advances across the Majors has decreased by an average of 0.2 per cent in FY22 to 86.1%.

The rate of growth in customer deposits (6.7% in FY22) has slowed compared with the 7% rate of growth seen in FY21, and was exceeded by the growth in gross loans and advances during the year.

Diagram 4. **Deposit funding ratios**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Costs

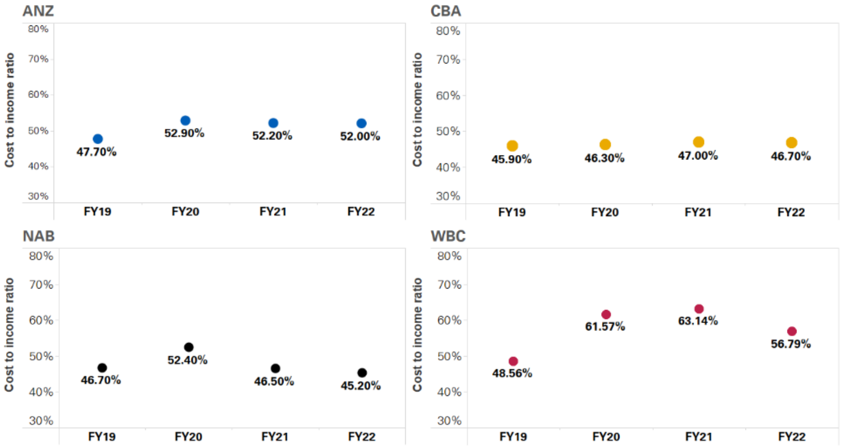
The Majors have maintained their focus on cost reduction initiatives with lower costs and improved cost-to-income ratios realised during FY22.

Operating expenses

Operating expenses have decreased by an average of 2 percent from FY21 to $40.7 million, although this was not consistent across the Majors.

While there was an overall reduction in operating expenses, there were increases compared to FY21 in staff costs driven by an increased headcount, investment spend, inflation and the tight employment market.

Diagram 5. **Costs to income ratios**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Investment spend

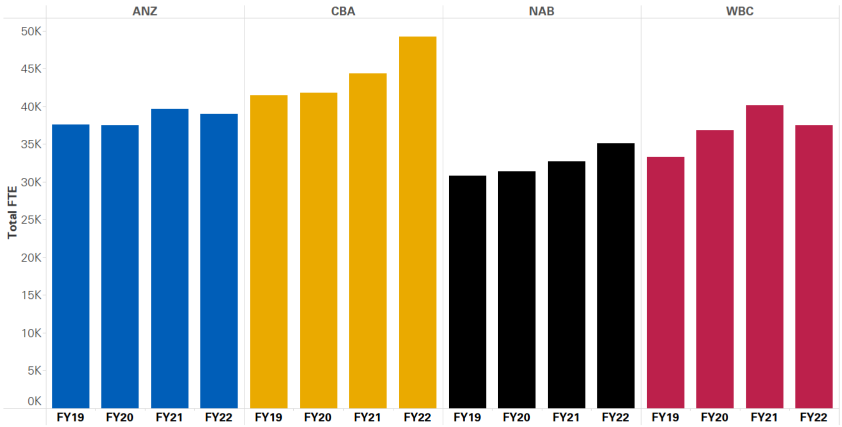
Aggregate investment spend across the Majors increased by $534 million to $7,431 million in FY22. There is a shift across the Majors compared to previous years with higher investment in growth and productivity and a reduction in risk and compliance as remediation programs start to wind down.

Technology expenditure has decreased by $488 million to $6,262 million, primarily due to lower amortisation and a slowdown in productivity initiatives, partly offset by higher software licensing and infrastructure costs including increased cloud computing usage and investment in cyber security capabilities and system resilience.

Personnel

The aggregate number of Full Time Equivalent (FTE) staff employed by the Majors has increased by 3,893 during FY22 to 160,836. This was primarily driven by additional operational staff required in processing higher lending volumes and financial crime assessments. Notably CBA increased their FTE by 4,870 (11 per cent) with an increased focus on frontline and technology resources in relation to cyber security capabilities, while Westpac reduced their FTE (down 2,667 or 6 per cent) because of changes in the organisational structure, sale of additional business and cost reduction steps.

Diagram 6. **Total FTE**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Capital

Strong balance sheets have positioned the Majors well for growth, with each of the Majors executing share buy-backs during the year.

Capital adequacy

The Majors continue to maintain strong capital positions at the end of FY22 as they continue to exceed the ‘unquestionably strong’ thresholds set by APRA.

The average CET1 ratio across the Majors decreased by 102 basis points to 11.65%. This has mainly been driven by the completion of share buy-backs, payment of final FY21 dividends and higher total risk-weighted assets (RWA) due to growth of the lending portfolio and interest rate risk in the banking book. The Majors collectively completed $15.4 billion in share buy-backs during the period:

- ANZ completion of $1.5 billion on-market share buy-back as well as a $3.5 billion Share Entitlement issue;
- CBA completion of $6.0 billion off-market share buy-back and $468 million on-market share buy-back.
- NAB completion of $3.9 billion on-market share buy-back; and
- WBC completion of $3.5 billion off-market share buy-back.

Diagram 7. **Capital adequacy ratios**

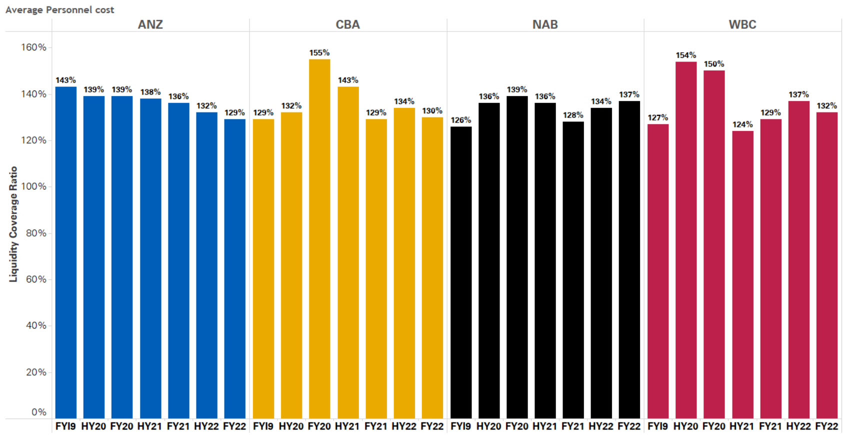
	ANZ		CBA		NAB		WBC	
	FY22	FY21	FY22	FY21	FY22	FY21	FY22	FY21
Common Equity Tier 1 (%)	**12.3**	**12.3**	**11.5**	**13.1**	**11.5**	**13.0**	**11.3**	**12.3**
Tier 1 Capital (%)	14.0	14.3	13.6	15.7	13.1	14.6	13.4	14.7
Tier 2 Capital (%)	4.2	4.1	4.0	4.1	5.1	4.3	5.0	4.2
Total Regulatory Capital ratio (%)	**18.2**	**18.4**	**17.6**	**19.8**	**18.2**	**18.9**	**18.4**	**18.9**

The average APRA leverage ratio across the Majors decreased by 51 basis points to 5.32%. This remains well above APRA's minimum requirement of 3.5% for internal ratings based ADIs. The movement was consistent across the Majors, driven primarily by higher loan growth.

Liquidity

Across the Majors, liquidity ratios appear to have peaked, with the average liquidity coverage ratio (LCR) increasing by 150 basis points to 132 per cent, largely driven by action taken because of APRA's announcement of a sector-wide phased reduction in the reliance on the Committed Liquidity Facility (CLF). The RBA expects there will be sufficient High Quality Liquid Assets (HQLA) for ADIs to meet their LCR requirements without the need to utilise the CLF by the end of 2022, subject to market conditions.

Diagram 8. **Liquidity coverage ratio**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Asset quality

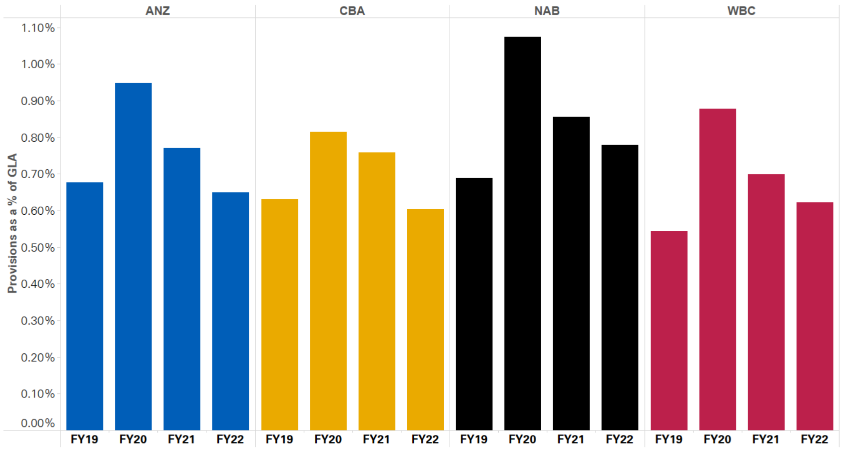
The Majors had lower impairment charges in FY22 by $691 million compared with that of FY21, although this includes $925 million of write-backs. There is uncertainty on the horizon from the forecast impacts of inflation and interest rate rises on borrowers.

As a result of the Australian economy's strong recovery, the Majors continued to write-back their Covid provisions during FY22. The overall increase in GDP, being around 4.5 per cent above its pre-pandemic level, and the decrease in unemployment have both evidenced and promoted optimism in the wider economy. Notwithstanding, there are uncertainties due to inflationary pressures and interest rates, which are expected to continue to rise in the short to medium term.

Though credit quality remains strong at this point, the Majors are signalling a likely economic slowdown, leading to increased unemployment, falling house prices, and increased interest rates into 2023. These factors are expected to lead to raised provisions in the years ahead.

The overall impact of these factors was positive in FY22 with an improvement in credit risk, favourable changes in portfolio composition, and the return to normalised provisioning, resulting in a decreased ratio of impaired loans to Gross Loans and Advances (GLA) by an average of 12 basis points compared to that of FY21. A similar decrease is seen in the average provisions compared to GLA which have returned to pre-Covid levels.

Diagram 9. **Provisions as a percentage of GLA**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

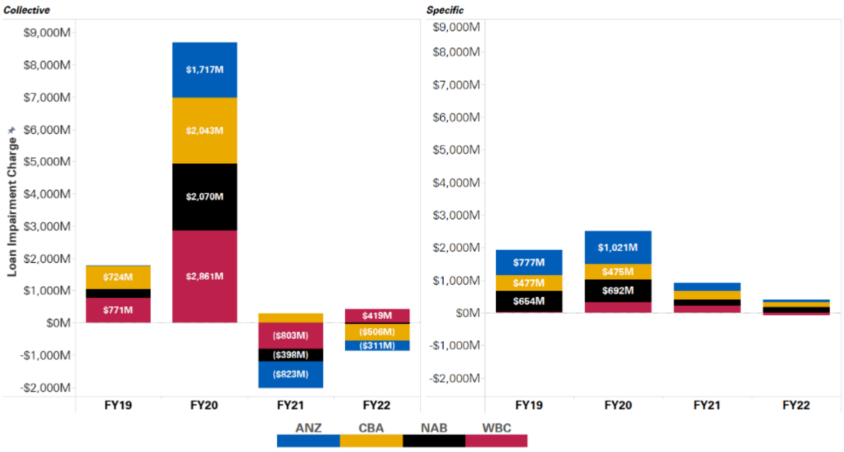
Loan impairment

The Majors recorded net loan impairment write-backs of $129 million during FY22, although this was driven by write-backs of Covid provisions amounting to $681 million across the Majors.

The Majors released $444 million in collective impairment charges in FY22. This has primarily been driven by improved economic conditions in Australia as the economy adjusts to a “post lockdown” economic scenario and increasing asset quality. Significant uncertainties in the economic outlook remain, such as the geopolitical unrest between Ukraine and Russia, supply chain disruptions, higher interest rates and increasing inflation. The Majors have incorporated these uncertainties into their forward-looking assumptions of expected credit losses (ECLs).

Specific impairment charges of $315 million were taken during FY22 compared to $917 million in FY21. This reduction is a result of decreases in underlying delinquencies and impairment flows, as well as a return to normalised levels of impairment after the Covid-impacted comparative period.

Diagram 10. **Loan impairment charges**

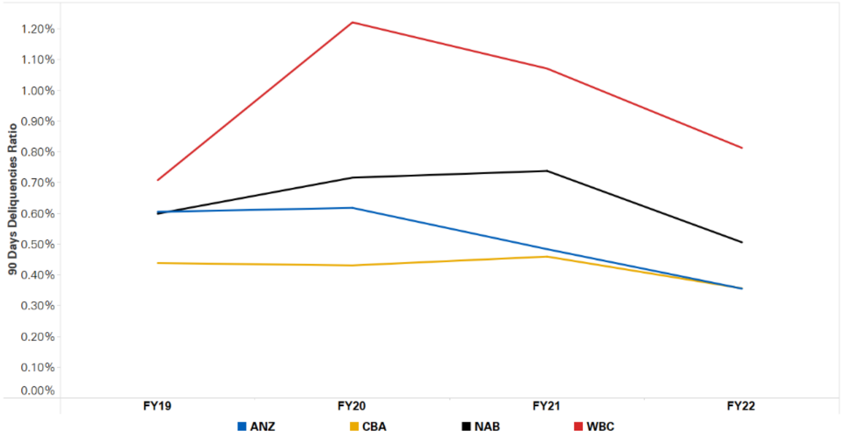


Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Delinquency

Delinquencies (90+ days past due) have seen a general reduction because of improving economic conditions, a strong property market, and the effect of government support provided during the pandemic. Average delinquencies as a proportion of GLA across the Majors decreased by 18 basis points compared to FY21 to an average of 0.69%, levels not seen since 2018.

Diagram 11. **90 days delinquency ratios**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Notable items

Divestments continue to be a key feature across the Majors as well as provisions for customer remediation costs.

Divestments

The Majors have continued their simplification journey, with sustained divestment activity in FY22 with all four banks reporting asset sales. Key transactions during the year included:

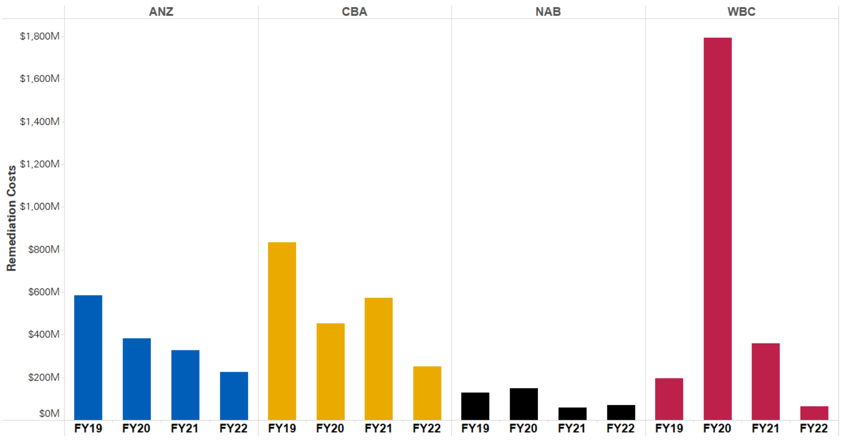
- ANZ completed the sale of its merchant acquiring business to ANZ Worldline Payment Solutions, resulting in a pre-tax gain of $307 million. ANZ also completed the sale of its financial planning and advice business to Zurich Financial Services Australia Ltd recognising a $62 million loss.
- CBA completed its sale of a 10 per cent shareholding in Bank of Hangzhou resulting in a post-tax gain of $299 million. CBA also completed its transfer of the Commonwealth Financial Planning business recognising a post-tax loss of $73 million.
- NAB completed the disposal of BNZ Life, recognising a gain on disposal of $197 million.
- Westpac completed its sale of Westpac Life Insurance Limited, recognising a loss of $1.1 billion. Additional expenses and revaluations associated with asset sales, including of Advance Asset Management, totalled $125 million.

Customer remediation

Customer remediation charges have remained a prominent, although declining, theme for the Majors in FY22. Across the Majors, costs related to remediation totalled $609 million for the year, down from $1,321 million in FY21.

The remaining provisions on the books of the Majors for remediation continued to decrease in FY22 to a total of $2.8 billion (37.3 per cent lower than at the end of FY21).

Diagram 12. **Customer remediation costs**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Other notable items

Other notable items during the year included:

- ANZ entered into an agreement to purchase Suncorp Bank for $4.9 billion, subject to regulatory approval. Completion is expected in the second half of calendar year 2023.
- ANZ also recognised restructuring expenses of $68m relating to operational changes across multiple divisions.
- CBA invested an additional $47 million into Klarna as part of their US$800m capital raise executed during the period.
- NAB completed its acquisition of the Citi consumer business for a provisional cash consideration of $3.14 billion.
- NAB also completed the acquisition of 100% of the issued share capital of Lantern Claims, recognising software of $40 million.
- Westpac recognised a loss of $129 million due to the write-down of assets and costs associated with the consolidation of branches.

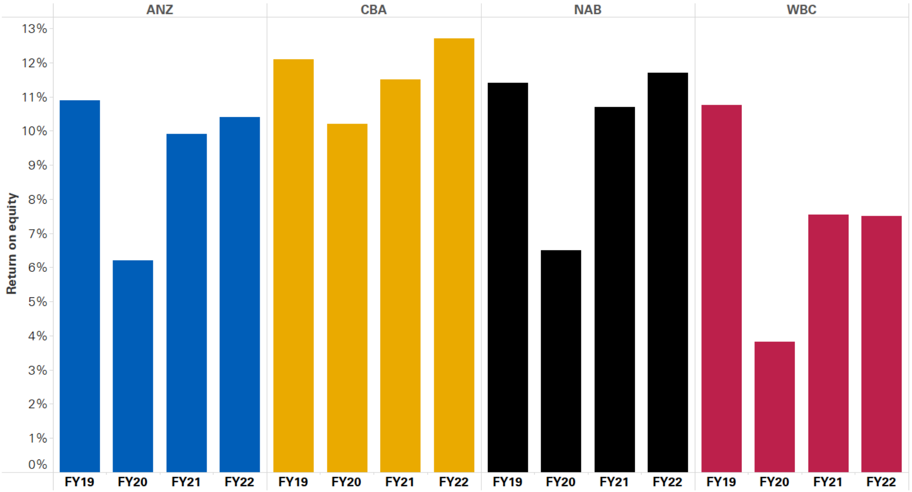
Shareholder returns

Stronger returns and an increase in dividends.

Return on Equity

ROE has continued an upward trend in FY22 across the Majors. Average ROE increased by 66 basis points compared with FY21 to 10.6% continuing the momentum from last year's return to double-digit ROE. This has been driven by the impact of higher cash profit and the share buy-backs completed by each of the Majors.

Diagram 13. **Returns on equity**

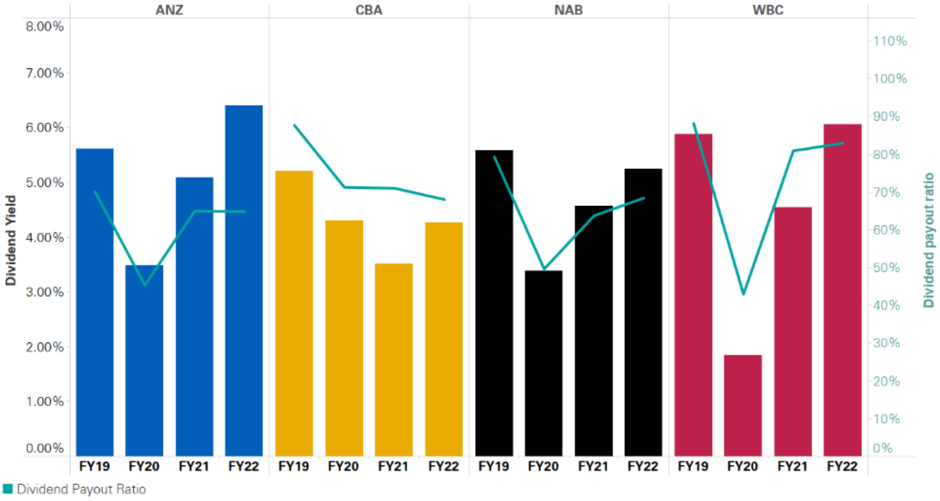


Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

Dividends

The Majors declared higher dividend payments in FY22 with an increase in the average dividend per share of 9.5% per cent compared to FY21, resulting in an increase of 1.1% in dividend yields. Despite the increase in dividend payments and yield across the Majors, the average dividend payout ratio has remained steady at 71%.

Diagram 14. **Dividend yields**



Source: KPMG analysis from ANZ, CBA, NAB, WBC Full Year Results Announcements

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