

Media statement
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Strategies for growth help to secure momentum for BNZ

Strong underlying performance has seen the Bank of New Zealand (BNZ) report a statutory net profit for its banking group¹ of NZ\$451 million for the half year to 31 March, 2016.

“Our results reflect a clear focus on delivering our strategy and implementing it against a backdrop of a competitive environment and increased funding costs from offshore market volatility,” said CEO Anthony Healy.

“We have seen real momentum in our priority segments of housing and SME, with particularly robust volume gains in the important Auckland market. Progress has been made in customer satisfaction due to a clear focus on key end-to-end customer experiences and increased investment in our digital platforms and simplification agenda,” he said.

Key financial results:

(Note: comparisons are with six months ending 31 March, 2015, unless otherwise stated for both BNZ banking group and New Zealand banking operations)

BNZ banking group¹

- **Statutory net profit¹** of NZ\$451 million.
- **Cash earnings²** decreased by NZ\$22 million or 4.5% to \$461 million reflecting increased collective provisions mainly due to the outlook for the Dairy industry.
- **Common Equity Tier 1, Tier 1 and total capital ratios¹** of 10.41%, 11.03% and 12.58%, respectively.

New Zealand banking operations³

- **Underlying profit³** increased by NZ\$9 million or 1.4% driven by improved revenue partially offset by an increase in expenses.
- **Cash earnings²** decreased by NZ\$14 million or 3.3% to \$404 million, reflecting increased collective provisions mainly due to the outlook for the Dairy industry.
- **Net operating income³** increased by NZ\$17 million or 1.6% driven by growth in lending and deposit volumes partially offset by lower deposit and lending margin.
- **Net interest margin³** decreased by fifteen basis points to 2.31% largely driven by lower deposit and lending margins and higher funding costs from heightened offshore market volatility.
- **Operating expenses³** increased by NZ\$8 million or 2.0% mainly due to growth in personnel to support priority growth segments, the investment programme to support those segments as well as regulatory spend.
- **Charges for bad and doubtful debts³** increased by NZ\$38 million or 82.6% as a result of increased collective provision charges, mainly due to the outlook for the dairy industry.
- **Average customer deposits³** increased by NZ\$2.7 billion or 6.0%, driven by a focus on higher quality personal deposits and managing deposit growth in line with asset growth.
- **Average lending volumes³** grew by NZ\$4.4 billion or 6.8%. Average housing volumes were up by NZ\$1.7 billion or 5.3% and business lending by NZ\$3.0 billion or 9.1%.

1. “Banking Group” means Bank of New Zealand’s financial reporting group, which consists of Bank of New Zealand, all of its wholly owned entities and other entities consolidated for financial reporting purposes.

2. Cash earnings is a common measure of financial performance which excludes items introducing volatility and one-off distortions that are unrelated to BNZ’s ongoing financial performance. Cash earnings is based on statutory net profit which is adjusted to exclude fair value movements, hedging gains/(losses) and the disposal of subsidiaries. These items are excluded from cash earnings as they introduce volatility and/or distortions and are shown in the cash earnings to net profit reconciliation included on the final page. Cash earnings is calculated in accordance with Group (NAB) policy.

3. “BNZ’s New Zealand banking operations”: excludes BNZ’s Group Capital Management and BNZ Markets operations (previously known as Wholesale Banking) from the “Banking Group” and includes the Insurance operation in New Zealand for management reporting purposes.

Commentary – Anthony Healy

AGRIBUSINESS

“While there’s no question that it is a difficult time for many dairy farmers and their families, BNZ is well placed to continue supporting our farming customers with thoughtful advice and financial support.

“Our approach is a prudent one. BNZ’s agri book is diversified, and asset quality remains sound. We commenced reviewing our dairy portfolio 18 months ago, working with customers as we took a ‘lower for longer’ view of the sector. We have also doubled our collective provision for dairy to reflect this.

“We have been working with our customers to plan for a range of scenarios and the majority of our farmers are enacting those plans now. From a financial management perspective, they’re adjusting well, removing costs and, if they have to, selling non-core assets.

“We recently announced an investment in cloud-based farm accounting software provider Figured Limited, making it easier for farmers to work with their accountants, farm consultants, and rural bankers.”

HOUSING

“While demand, in part driven by continuing strong migration, is still high and the supply response is lagging, there will continue to be upward pressure on Auckland house prices.

“We have arrested our declining market share in housing. We attribute this to our increased focus on growing our share of the housing sector through a range of channels. We re-entered the broker market last year, supported by BNZ’s broker hub and we significantly expanded our mobile mortgage workforce. The success of this strategy is reflected in the volume gains we’ve achieved. Last month we announced a second broker partner, Mortgage Express, keeping us well-positioned to continue building momentum.”

AUCKLAND

“Our Auckland growth strategy has delivered strong volume growth within our existing risk appetite. We’ve targeted the SME and housing segments in Auckland and both have seen strong volume increases compared with last year.”

CREDIT CARDS

“The decrease in our market share for credit cards represents the tail end of our shift from Global Plus to BNZ Advantage. The majority of losses have been card-only customers who prefer Airpoints as a reward. Our BNZ Advantage proposition, which is wider than just credit card rewards, is resonating well with customers who prefer broader rewards and recognition. This includes the choice of cash back or Fly Buys at an accelerated rate, and being able to choose from a range of additional, exclusive rewards. We have enjoyed a 30% increase in retention of this high-value retail customer segment.”

BUSINESS AND SMALL BUSINESS

“Our strength in SME, a sector integral for BNZ and the New Zealand economy as a whole, continues. We have hired 50 new small business bankers, including 20 people in a new hub in Hamilton, 10 people in Christchurch and the remaining 20 in Auckland. These strategic moves will ensure BNZ is well placed to maximise its strengths in a growing sector.”

DIGITAL INVESTMENT

“Digital is now the number one way our customers choose to bank with us, online and through the BNZ app. Around 86% of transactions in our own channels are digital, adding up to 11.6m sessions per month. Digital sessions increased 23% in 2015, mobile by 36%.

“We recently completed migrating all our customers to You Money, our award-winning digital banking platform. This has been well received by our customers.”

INITIATIVES FOR A HIGH-ACHIEVING NEW ZEALAND

“Our initiatives to support a high achieving NZ continue to roll out.

“Our community finance programme helps low income New Zealanders be good with money and we are working with our partners to expand the scheme. We estimate that our \$500,000 of community finance lending over the past 18 months has saved our clients more than \$280,000, compared with borrowing costs through alternative lenders.

“Our commitment to offer lending of more than \$1 billion to small and medium business owners looking to grow, expand or export remains in place. This is in addition to our hiring of 50 more small business bankers.

“Housing affordability is an issue of immense social and economic importance, particularly in Auckland. BNZ has been busy working on housing affordability initiatives, including supporting housing development in areas such as Hobsonville and the Special Housing Areas, and working with Auckland Council and Beca to launch the *Affordable Housing Development Guide*. We are also funding a number of developers building affordable accommodation such as at the McClellan development in Takanini, and the Waimahia development in Weymouth. “

CAPITAL AND FUNDING POSITION

BNZ maintains a robust capital structure, with a strong balance sheet that is well funded through diversified and stable funding sources. BNZ has been active in the domestic and offshore bond markets, issuing in JPY, USD, HKD and NZD currencies during the first half of this financial year. On 17 December 2015, the Banking Group issued \$550 million of subordinated unsecured notes (Subordinated Notes) to the New Zealand public. The Subordinated Notes are treated as Tier Two capital under the Banking Group’s regulatory capital requirements.

BNZ’s Core Funding Ratio (CFR) of 86.6% exceeds the Reserve Bank of New Zealand minimum requirement of 75% as at 31 March, 2016. BNZ’s Common Equity Tier 1, Tier 1 and Total capital ratios of 10.41%, 11.03% and 12.58%, respectively, as at 31 March 2016 were well above the RBNZ minimum capital ratio requirements of 7.00%, 8.50% and 10.50%, respectively. Collectively, BNZ’s funding and capital position is supportive of BNZ’s long-term senior unsecured issuer credit ratings of AA-/Aa3/AA- (S&P/Moody’s/Fitch).

Ends

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Note for editors

IFRS9

IFRS9 is a new accounting standard that will replace IAS39 and will be compulsory for all banks from 1 January, 2018. BNZ, in line with its parent NAB, has made the decision to early adopt IFRS9 with 1H15 and FY15 results reported on this basis.

BNZ Banking Group

Income Statement Summary

	Half Year to			Mar 16 v	Mar 16 v
	Mar 16	Sep 15	Mar-15	Sep 15 %	Mar 15 %
	NZ\$m	NZ\$m	NZ\$m		
Net interest income	882	885	850	(0.3%)	3.8%
Gains less losses on financial instruments	55	189	133	(70.9%)	(58.6%)
Other operating income	194	193	182	0.5%	6.6%
Total operating income	1,131	1,267	1,165	(10.7%)	(2.9%)
Operating expenses	(434)	(445)	(420)	(2.5%)	3.3%
Total operating profit before impairment losses on credit exposures and income tax expense	697	822	745	(15.2%)	(6.4%)
Impairment losses on credit exposures	(79)	(81)	(47)	(2.5%)	68.1%
Total operating profit before income tax expense	618	741	698	(16.6%)	(11.5%)
Income tax expense on operating profit	(167)	(205)	(196)	(18.5%)	(14.8%)
Net profit attributable to shareholders of Bank of New Zealand	451	536	502	(15.9%)	(10.2%)

Balance Sheet Summary

Spot Balances (NZ\$m)	Mar-16	Sep 15	Mar-15	Mar 16 v	Mar 16 v
				Sep 15 %	Mar 15 %
Total assets	90,078	86,787	82,083	3.8%	9.7%
Total liabilities	82,719	79,745	75,466	3.7%	9.6%
Total shareholders' equity	7,359	7,042	6,617	4.5%	11.2%
Ordinary shareholder's equity	6,709	6,392	5,967	5.0%	12.4%
Contributed equity – perpetual preference shareholders	650	650	650	0.0%	0.0%
Total shareholders' equity	7,359	7,042	6,617	4.5%	11.2%
Performance Measures²					
Net profit on average assets (Annualised)	1.02%	1.25%	1.26%	(23 bps)	(24 bps)
Net interest margin	2.23%	2.32%	2.31%	(9 bps)	(8 bps)
Cost to income ratio	38.4%	35.1%	36.1%	(330 bps)	(230 bps)

Capital Adequacy Ratios¹

	Mar 16	Sep 15	Mar 15	Mar 16 v	Mar 16 v
	Basel III	Basel III	Basel III	Sep 15 %	Mar 15 %
Common Equity Tier One capital ratio	10.41%	10.70%	10.79%	(29 bps)	(38 bps)
Tier One capital ratio	11.03%	11.69%	11.85%	(66 bps)	(82 bps)
Total qualifying capital ratio	12.58%	12.67%	12.90%	(9 bps)	(32 bps)

1. Based on the RBNZ's Capital Adequacy Framework.

2. Performance measures are based on the BNZ Banking Group which excludes the Insurance operation in New Zealand and includes BNZ's Group Capital Management and BNZ Markets operations. Performance measures are calculated on a net profit basis.

New Zealand Banking operations

	Half Year to					
	Mar 16	Sep 15	Mar 15	Mar 16 v	Mar 15 v	
	NZ\$m	NZ\$m	NZ\$m	Sep 15 %	Mar 15 %	
Net interest income	812	820	804	(1.0%)	1.0%	
Other operating income	239	238	230	0.4%	3.9%	
Net operating income	1,051	1,058	1,034	(0.7%)	1.6%	
Operating expenses	(415)	(419)	(407)	1.0%	(2.0%)	
Underlying profit	636	639	627	(0.5%)	1.4%	
Charge to provide for bad and doubtful debts	(84)	(88)	(46)	4.5%	(82.6%)	
Cash earnings before tax	552	551	581	0.2%	(5.0%)	
Income tax expense	(148)	(146)	(163)	(1.4%)	9.2%	
Cash earnings (NZ Banking) ¹	404	405	418	(0.2%)	(3.3%)	
Reconciling items to statutory net profit (BNZ Banking Group)						
Structural differences between NZ Banking and BNZ Banking Group ²	57	78	65	(26.9%)	(12.3%)	
Fair value movements and hedging gains/(losses) ³	(14)	73	27	(119.2%)	151.9%	
Taxation on reconciling items	4	(20)	(8)	(120.0%)	(150.0%)	
Net profit attributable to shareholders of Bank of New Zealand ⁴	451	536	502	(15.9%)	(10.2%)	
Average Volumes (NZ\$bn)⁵						
Gross loans and acceptances	69.4	66.7	65.0	4.0%	6.8%	
Interest earning assets	70.4	67.5	65.6	4.3%	7.3%	
Total assets	72.5	69.5	67.7	4.3%	7.1%	
Customer deposits	47.5	45.0	44.8	5.6%	6.0%	
Performance Measures⁵						
Cash earnings on average assets	1.11%	1.16%	1.24%	(5 bps)	(13 bps)	
Net interest margin	2.31%	2.42%	2.46%	(11 bps)	(15 bps)	
Cost to income ratio	39.5%	39.6%	39.4%	10 bps	(10 bps)	

1. BNZ's New Zealand Banking operations are reported as a separate division and include the Retail, Business, Agribusiness, Corporate and Insurance businesses. It excludes BNZ's Group Capital Management and BNZ Markets (previously known as Wholesale Banking) operations reported at a Group (NAB) level.
2. BNZ Banking Group excludes the Insurance operation in New Zealand and includes BNZ's Group Capital Management and BNZ Markets operations.
3. Includes unrealised fair value gains or losses on economic hedges that do not qualify for hedge accounting and ineffectiveness of designated hedge accounting relationships. Fair value movements are mainly driven by changes in interest rates, credit spreads and volatility on cross currency swaps.
4. Statutory net profit has been prepared in accordance with Generally Accepted Accounting Practice in New Zealand ("NZ GAAP"). It complies with New Zealand equivalents to International Financial Reporting Standards ("NZ IFRS") and other applicable Financial Reporting Standards.
5. Average volumes and performance measures are based on BNZ's New Zealand Banking operations. Performance measures are calculated on a cash earnings basis.