



# 1H18 Results Presentation

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17 April 2018

FOR THE HALF YEAR ENDED 28 FEBRUARY 2018  
Bank of Queensland Limited ABN 32 009 656 740. AFSL No 244616.

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## Results Overview

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Jon Sutton  
Managing Director & CEO

## Financial Detail

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Anthony Rose  
Chief Financial Officer

## Summary & Outlook

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Jon Sutton  
Managing Director & CEO

## 1H18 HIGHLIGHTS



- 1 — Improved lending growth
- 2 — Retail and BOQ Business delivering on Group four-pillar strategy
- 3 — Asset quality remains sound
- 4 — Investing in transformation while maintaining expense discipline
- 5 — Strong capital position provides flexibility

Good morning, I would like to begin with the highlights of the result.

Our strategy to grow the right way, together with our deliberate approach of building our niche businesses, is delivering.

We have proactively sought to diversify our lending across the Group over the past five years and we are seeing good results.

I am pleased to report that lending growth has improved. This was supported by our commercial niche segments, as well as home loan growth through the Virgin Money, BOQ Specialist and BOQ Broker channels.

Both Retail Bank and BOQ Business are delivering against the Group's four pillar strategy. This half, we have introduced a new segment reporting structure to align with the way we manage the business day to day. More detail will be provided as we go through the presentation.

Our asset quality remains sound, which is evident across a range of metrics. We are not seeing any areas of concern arise across the portfolio.

We have maintained discipline in expense management. This has allowed us to

continue investing for the future.

Our capital position remains very strong, providing us with options to enhance shareholder returns for the long term.

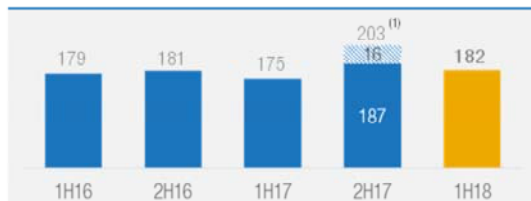
These results were achieved against a backdrop of changing regulatory and market conditions.

Today we have also announced the sale of our St Andrew's business. Anthony will provide some detail on the transaction in his section.

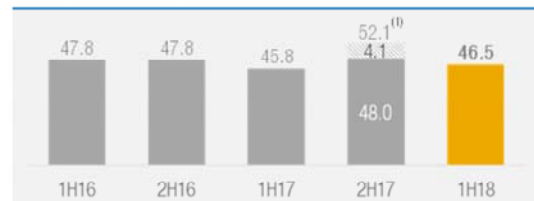
# KEY ELEMENTS OF THE RESULT



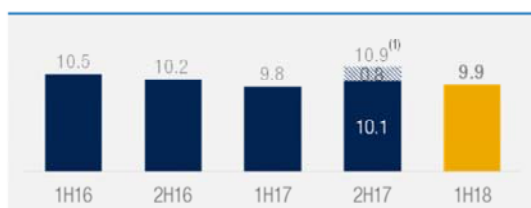
## CASH EARNINGS AFTER TAX (\$M)



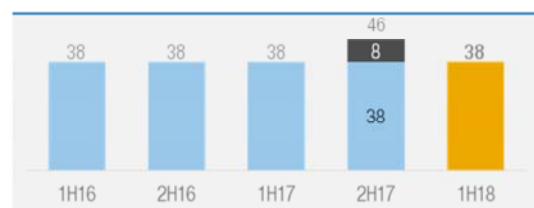
## EARNINGS PER ORDINARY SHARE (CENTS)



## RETURN ON EQUITY (%)



## DIVIDENDS PER ORDINARY SHARE (CENTS)



Looking at the key financial elements of the result.

Cash earnings after tax of 182 million dollars increased four per cent on 1H17.

Earnings per share of 46.5 cents. This represents an increase of two per cent on 1H17.

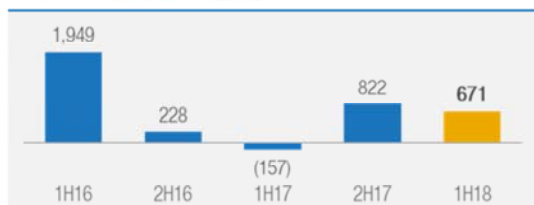
Return on equity increased 10 basis points to 9.9 per cent.

The ordinary dividend has been maintained at 38 cents per share.

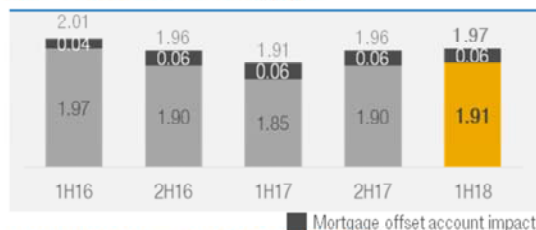
# DRIVERS OF THE RESULT



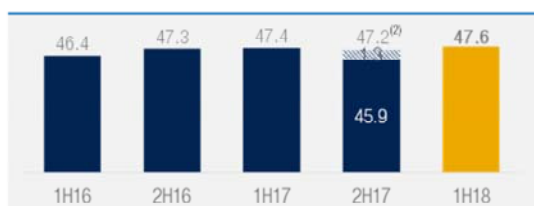
## LENDING GROWTH (\$M)



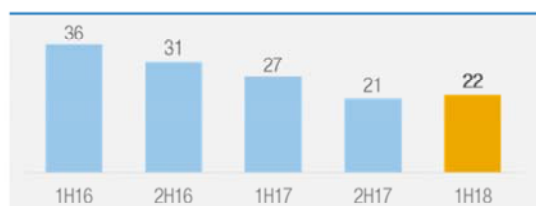
## NET INTEREST MARGIN (%)<sup>(1)</sup>



## COST TO INCOME RATIO (%)



## LOAN IMPAIRMENT EXPENSE (\$M)



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(1) NIM net of mortgage offset accounts has been shown to align with industry practice  
 (2) 2H17 includes the benefit of a \$16m profit on disposal of a vendor finance entity

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Slide 6 provides an overview of the drivers of these results.

Total lending growth of \$671 million in this half represents an uplift of more than \$800 million compared to the contraction of \$157 million in the first half of 2017.

Net interest margin increased one basis point from last half to 1.97 per cent against a backdrop of intensified price competition for lending and deposits.

Our cost to income ratio was 47.6 per cent, with operating expense growth of just one million dollars on the prior half.

Our loan impairment expense decreased five million dollars or 19 per cent compared to the same period in 2017.

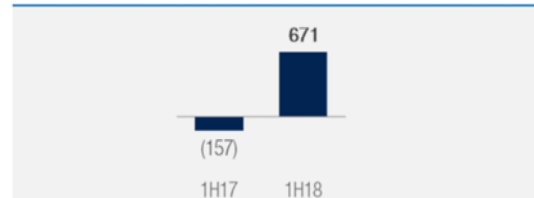
# IMPROVED LENDING GROWTH



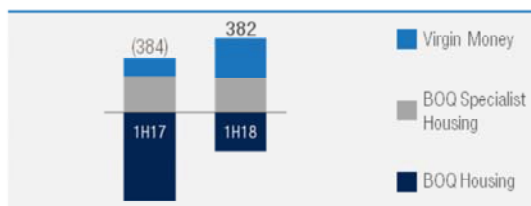
## SUMMARY

- Strong home loan growth through Virgin Money Australia & BOQ Specialist continuing
- Mortgage broker volumes building
- Strong growth in commercial loans driven by niche segments
- Branch network run-off slowing
- Historically, second half has been seasonally higher growth period

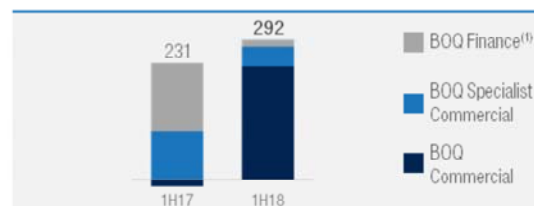
## TOTAL LENDING GROWTH VS PCP (\$M)



## HOUSING LOAN GROWTH (\$M)



## COMMERCIAL LOAN & LEASING GROWTH (\$M)



Moving to slide 7.

We are seeing improvements in both housing and commercial loan growth.

In housing, BOQ Broker, Virgin Money Australia and BOQ Specialist have all made strong contributions.

We have also seen improvement in the branch network as branch numbers stabilise. As we have previously stated, it will take more time for the branch network to return to lending growth.

Our niche segments have delivered very good results, supporting commercial loan growth of 1.6 times system.

The first half has traditionally been a lower growth period. We are pleased with the steady rate of growth since the prior corresponding period.



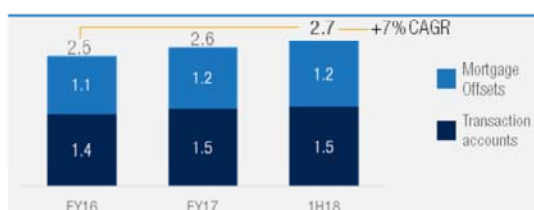
# RETAIL BANKING FOCUS ON CHANNELS & DEPOSITS



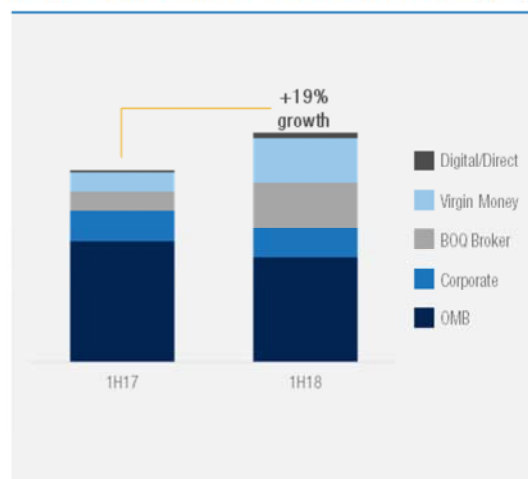
## SUMMARY

- Retail expanding distribution channels through BOQ Broker, Virgin Money Australia and Digital
- Settlement volumes improved on PCP basis
- Strong relationship deposit growth in branch network driven by Balanced Scorecard

## RETAIL RELATIONSHIP DEPOSIT BALANCES (\$B)



## RETAIL HOUSING SETTLEMENTS BY CHANNEL (\$M)



Turning now to our Retail Bank and BOQ Business divisions.

Retail Banking has continued to diversify its channels. BOQ Broker and Virgin Money Australia contributed 40 per cent of Retail's home loan settlements in the first half of 2018.

Overall, housing loan settlements increased 19 per cent compared to the same time last year. This was achieved while continuing to fulfil our responsible lending obligations to our customers.

Virgin Money continues to perform ahead of expectations. Since the launch of the Virgin home loan product just under two years ago, the portfolio has grown to 1.2 billion dollars.

Even though it will take some time before our branch network returns to growth in lending, we have seen continued improvement through the network during this half.

Our branch network remains a key driver for deposit gathering and is crucial in funding BOQ's future growth aspirations.

Pleasingly, transaction account deposit growth has been strong at ten per cent since first half 17.

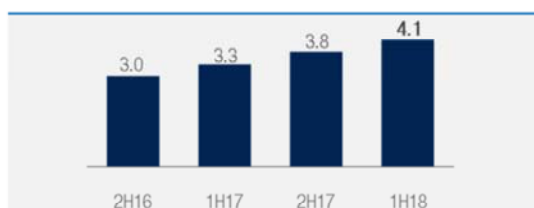
# BOQ BUSINESS GROWING NICHE SEGMENTS



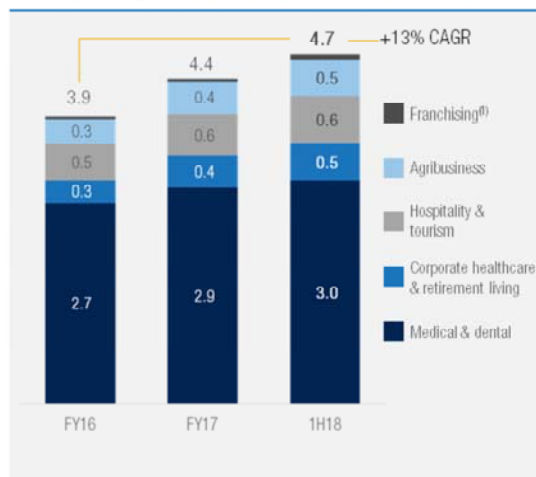
## SUMMARY

- BOQ Business focus on growing niche segments of agribusiness, corporate healthcare & retirement living, hospitality & tourism
- BOQ Specialist mortgage growth remains strong – building future pipeline of commercial loan customers
- BOQ Finance focused on improving mix, growing in higher margin segments

## BOQ SPECIALIST MORTGAGE BALANCES (\$B)



## BUSINESS BANKING NICHE SEGMENT BALANCES (\$M)



The BOQ Business division has continued to benefit from maturing its niche strategy across commercial customer segments. It achieved commercial loan growth of nearly 300 million dollars.

This has been delivered across target segments that seek a real relationship banking proposition and industry expertise. These include medical & dental, corporate healthcare & retirement living, hospitality & tourism and agribusiness.

BOQ Specialist has delivered another strong period of housing loan growth. Total mortgage balances of this portfolio have grown to 4.1 billion dollars in just three and a half years.

BOQ Finance has remained focused on margin and mix and successfully growing its structured vendor programs.

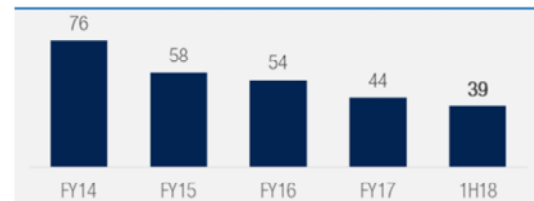
# ASSET QUALITY REMAINS SOUND



## SUMMARY

- Impaired assets continue to reduce
- Arrears levels remain benign
- QLD and WA showing signs of improvement
- Prompt implementation of prudential practice guides

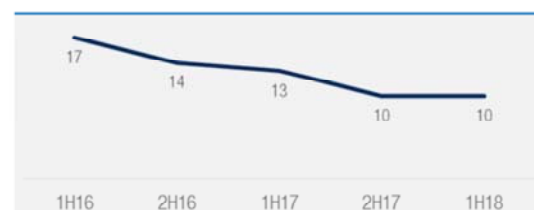
## IMPAIRED ASSETS % OF GROSS LOANS (bps)



## 30-DAY ARREARS (bps)



## GROUP IMPAIRMENT EXPENSE / GROSS LOANS (bps)



Our asset quality remains sound, which is clearly evident across a number of metrics.

Impaired assets have reduced to 39 basis points of total loans.

Impairment expense has remained steady at 10 basis points of total loans.

Our arrears trends remain benign, with the exception of the usual post-Christmas uptick. In March we have seen these levels reduce again.

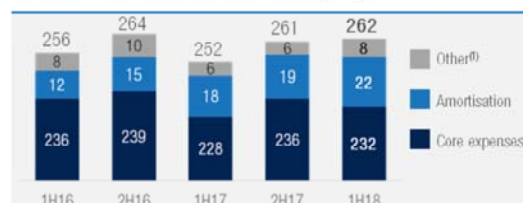
# INVESTING IN TRANSFORMATION WHILE MAINTAINING EXPENSE DISCIPLINE



## SUMMARY

- Cost savings enabling investment in technology and growth businesses
- New web experience platform now utilised across BOQ, Virgin Money Australia, BOQ Finance and BOQ Specialist
- 10 capex projects delivered in FY17; 18 delivered in 1H18 and 66 in progress

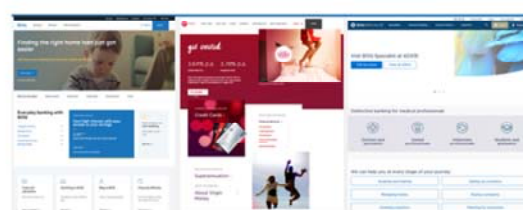
## CORE EXPENSES REDUCING (\$M)



## CAPITAL EXPENDITURE PROJECTS

Strategic/Longer term	Regulatory & maintenance
Tech infrastructure modernisation	New Payments Platform
Financial Markets digital platform	Cyber Security
Customer engagement platform	Cheque digitisation
API gateway & service fabric	PEXA
Web Experience Platform	Treasury & market risk systems

## NEW WEB EXPERIENCE PLATFORM



We have continued to search for and extract efficiencies across the business. This has enabled us to reduce core expenses by four million dollars compared to last half.

At the same time, we have been investing for the future with a large number of transformation initiatives underway across the group.

We've completed the rollout of our new web experience platform which enhances our customer connectivity. BOQ and BOQ Finance brands have now joined Virgin Money Australia and BOQ Specialist on the new platform. Since launch, we have seen positive feedback and engagement from customers.

This is an important step in our journey to lift the standard of our digital assets to better meet our customers' expectations.

There is still a lot more for us to do in this regard. Our internet and mobile banking offerings are high on the list to be refreshed into modern and more flexible platforms.

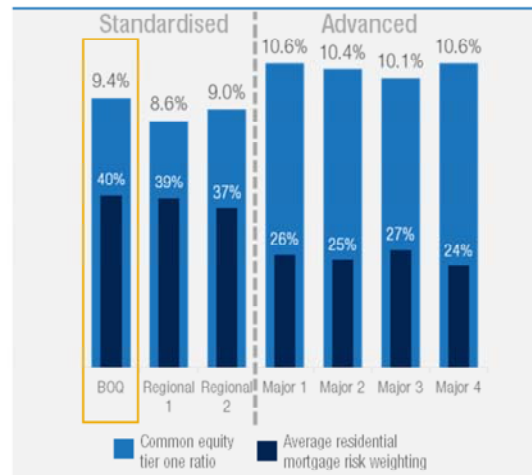
# STRONG CAPITAL POSITION PROVIDES FLEXIBILITY



## SUMMARY

- CET1 position remains very strong for a standardised bank at 9.42%
- Interim 9.25% CET1 target remains in place
- Basel & APRA announcements<sup>(1)</sup> suggest BOQ's position remains very comfortable relative to peers
- Capital management initiatives under active consideration

## CET1 CAPITAL VS PEERS<sup>(2)</sup>



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(1) <https://www.bis.org/chs/publ/d424.pdf>

<http://www.apra.gov.au/ad/PrudentialFramework/Documents/Revisions%20to%20the%20capital%20framework%20for%20ADs.pdf>

(2) Peer data based on most recent half or full year disclosures

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Our capital levels remain very strong.

Following the Basel and APRA papers released in the past few months, we remain comfortable with our position. Relative to our peers, we are in a very strong position as a standardised bank at 9.42 per cent CET1.

Our interim CET1 target of 9.25 per cent remains in place until there is further certainty from the regulator.

Therefore, our capital management options remain under active consideration.

I will now hand over to Anthony to discuss the financials in more detail.



# Financial Detail

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Anthony Rose  
Chief Financial Officer

## FINANCIAL PERFORMANCE



	1H18	1H18 v 1H17	1H18 v 2H17	1H18 v 2H17 adjusted <sup>(1)</sup>
Net interest income	\$475m	5% ▲	0%	0%
Non interest income	\$75m	(6%) ▼	(21%) ▼	(5%) ▼
<b>Total income</b>	<b>\$550m</b>	<b>3% ▲</b>	<b>(3%) ▼</b>	<b>(1%) ▼</b>
Operating expenses	(\$262m)	4% ▲	0%	0%
<b>Underlying profit</b>	<b>\$288m</b>	<b>3% ▲</b>	<b>(6%) ▼</b>	<b>(1%) ▼</b>
Loan impairment expense	(\$22m)	(19%) ▼	5% ▲	5% ▲
<b>Profit before tax</b>	<b>\$266m</b>	<b>5% ▲</b>	<b>(7%) ▼</b>	<b>(2%) ▼</b>
Income tax expense	(\$84m)	8% ▲	0%	(1%) ▼
<b>Cash earnings after tax</b>	<b>\$182m</b>	<b>4% ▲</b>	<b>(10%) ▼</b>	<b>(3%) ▼</b>
Cash basic earnings per share	46.5c	2% ▲	(11%) ▼	(3%) ▼
Return on average tangible equity	12.9%	(10bps) ▼	(140bps) ▼	(30bps) ▼

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(1) 2H17 adjusted for the \$16m profit on disposal of a vendor finance entity

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Thanks Jon. I'll start with the P&L on slide 14. I'll focus on comparisons with 1H17 given the day-count impact and seasonal factors mean this is the most appropriate point of comparison.

Total Income increased by three per cent or 18 million dollars compared to 1H17. The primary driver of this was Net Interest Income growth of five per cent or 23 million dollars, which is the result of growth in average interest earning assets of two per cent and a six basis point increase in net interest margin.

Non interest income contracted five million dollars or six per cent, which I'll discuss later.

Operating expenses increased ten million dollars or four per cent, driven by an increase in software amortisation as well as some seasonal timing differences between the periods, mainly around marketing activity.

This meant underlying profit increased by eight million dollars or three per cent.

Loan impairment expense reduced by five million dollars or 19 per cent.

Allowing for a tax rate of 31.4 per cent due to the non-deductibility of interest on



hybrid capital instruments, this meant that cash earnings increased four per cent or seven million dollars.

The comparisons with the second half of 2017 are not as clear. The prior half included a 16 million dollar benefit from the disposal of a vendor finance entity, which is obviously non-recurring in nature. Given this, we have provided an adjusted column for a more like-for-like comparison.

Even after adjusting for this, it is important to point out the impact of differential day count as well as general seasonality in our earnings between the first and second halves.

Day count alone has an impact of eight million dollars or two per cent on net interest income. The key take away is that we grew assets and did increase margin by one basis point compared to the prior half, so the result demonstrates an improved underlying position as we enter the second half.

We also kept our operating and loan impairment expenses largely stable, which further supports that the underlying trajectory is better than these numbers illustrate.

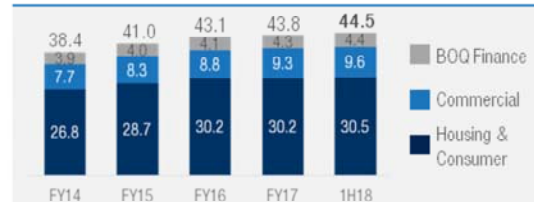
# LOAN PORTFOLIO AND GROWTH



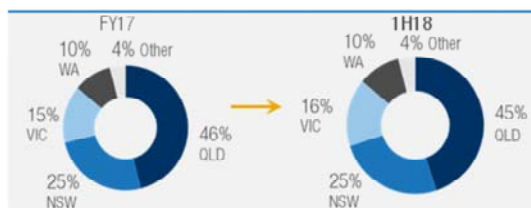
## SUMMARY

- Growth across all portfolios
- Total lending growth at 0.7x system; Housing 0.5x; Commercial 1.6x
- Strongest growth in niche commercial segments and new housing channels
- Growth being driven outside of QLD, improving geographic diversification

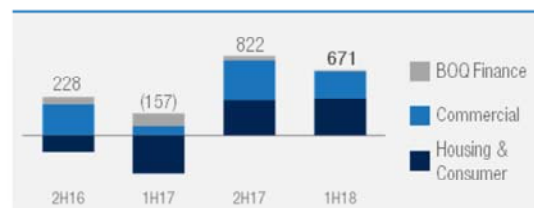
## GROSS LOANS & ADVANCES (\$B)



## TOTAL LENDING GEOGRAPHIC MIX



## HALF YEARLY GROWTH COMPOSITION (\$M)



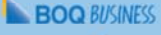

Now moving on to business momentum and I'll start with the loan portfolio on slide 15. We did achieve growth across all product portfolios. Total lending growth was 0.7x system, with housing loan growth tracking at half system and commercial loan growth at 1.6x system.

Our strongest growth has been achieved in our niche commercial segments as well as our new housing loan distribution channels.

We have also continued to diversify the loan portfolio geographically, with Queensland exposure down to 45 per cent.

## BOQ REPORTING SEGMENT OVERVIEW



	Retail Banking	BOQ Business
Brands	 	  
Summary	<ul style="list-style-type: none"> <li>Housing loans and deposits originated through the branch network, direct channels, Virgin Money Australia and mortgage brokers.</li> <li>Excludes home loans originated by BOQ Specialist and SME loans originated through branches.</li> </ul>	<ul style="list-style-type: none"> <li>Commercial loans, SME loans, housing loans, asset finance and deposits originated through BOQ Business, BOQ Specialist and BOQ Finance.</li> <li>Includes SME loans originated through the BOQ branch network.</li> </ul>
Balance sheet	Housing loans: \$25bn Deposits: \$17bn	Housing loans: \$5bn Commercial loans: \$10bn BOQ Finance: \$4bn Deposits: \$13bn
Cash earnings	\$75m	\$107m

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Note: The Other segment includes Treasury, head office functions and St Andrew's

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On slide 16 we have provided an overview of our new reporting segments, which reflect the way we manage the business day to day.

Retail Banking incorporates housing loans and deposits originated through the branch network, direct channels, Virgin Money Australia and our mortgage broker distribution. This covers around 25 billion dollars in lending assets and 17 billion dollars in deposits.

For clarity, it excludes home loans originated by BOQ Specialist and also excludes SME loans that may have been originated through branches.

These sit with BOQ Business which also comprises our BOQ branded commercial loans as well as BOQ Specialist and BOQ Finance.

This covers around 19 billion dollars in lending assets and 13 billion dollars in customer deposits originated through our BOQ Business relationship managers, finance brokers and through BOQ Specialist.

The third segment 'Other' comprises our St Andrew's insurance business, as well as a number of head office activities.

## FINANCIAL PERFORMANCE: RETAIL BANKING



	1H18	1H18 v 1H17	1H18 vs 2H17
Net interest income	\$227m	5% ▲	(1%) ▼
Non interest income	\$33m	(3%) ▼	(6%) ▼
<b>Total income</b>	<b>\$260m</b>	<b>4% ▲</b>	<b>(2%) ▼</b>
Operating expenses	(\$141m)	4% ▲	2% ▲
<b>Underlying profit</b>	<b>\$119m</b>	<b>3% ▲</b>	<b>(6%) ▼</b>
Loan impairment expense	(\$10m)	(9%) ▼	233% <sup>(1)</sup> ▲
<b>Profit before tax</b>	<b>\$109m</b>	<b>5% ▲</b>	<b>(11%) ▼</b>
Income tax expense	(\$34m)	6% ▲	(11%) ▼
<b>Cash earnings after tax</b>	<b>\$75m</b>	<b>4% ▲</b>	<b>(12%) ▼</b>

Turning to the performance of the Retail Banking segment specifically on slide 17, and the Retail division's performance largely mirrors the group results in terms of the 1H17 comparison.

Margin improvement supported income growth, while operating expenses increased due to higher software amortisation and some timing of expense spend, mainly related to marketing activity. Loan impairment expense improved and the net result is a four per cent increase in cash earnings to 75 million dollars.

The comparison with 2H17 is hindered by day count and seasonal factors. Loan balances and margin were largely flat compared to 2H17, while operating expense growth was contained to just two per cent. There was an increase in loan impairment expense but this was from a very low base of just three million dollars last half, which benefited from a six million dollar reduction in collective provisions in the transition to the Bank's new provisioning and reserving model that was implemented during the half.

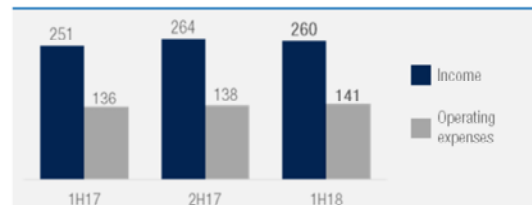
# RETAIL BANKING



## SUMMARY

- Focus on channel diversification and MFI customer growth
- Virgin Money Australia housing loan growth remains strong, contributing 20% of Retail housing settlements
- BOQ Broker volumes driving 20% of Retail housing settlements
- Branch network run-off improving
- Deposit growth focused on transaction and savings to improve funding costs

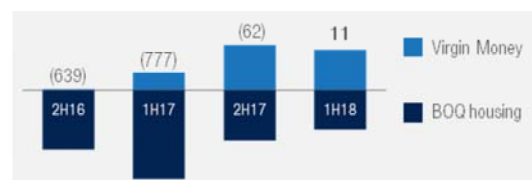
## INCOME AND EXPENSES (\$M)



## RETAIL TRANSACTION ACCOUNT GROWTH VS PCP



## HOUSING LOAN GROWTH BY CHANNEL (\$M)



The Retail division is delivering on its strategy of diversifying its origination channels and we are seeing good results in this regard.

Virgin Money Australia and BOQ broker channels each contributed 20 per cent of Retail's settlement volumes.

The branch network is still seeing run-off after a significant, multi-year reduction in branch numbers but this rate of run-off is slowing as branch numbers stabilise.

Pleasingly, the branches have been very successful in growing relationship deposit balances, particularly transaction accounts, with the Retail business delivering 10 per cent growth in these balances from 1H17.

The Retail team led by Matt Baxby is focused on enhancing our digital customer offerings, while continuing to mature our new distribution channels and growing the Virgin product suite.

## FINANCIAL PERFORMANCE: BUSINESS BANKING



	1H18	1H18 v 1H17	1H18 vs 2H17 adjusted <sup>(1)</sup>
Net interest income	\$251m	7% ▲	1% ▲
Non interest income	\$30m	0%	(6%) ▼
<b>Total income</b>	<b>\$281m</b>	<b>6% ▲</b>	<b>0%</b>
Operating expenses	(\$112m)	5% ▲	(1%) ▼
<b>Underlying profit</b>	<b>\$169m</b>	<b>8% ▲</b>	<b>1% ▲</b>
Loan impairment expense	(\$12m)	(25%) ▼	(33%) ▼
<b>Profit before tax</b>	<b>\$157m</b>	<b>11% ▲</b>	<b>5% ▲</b>
Income tax expense	(\$50m)	14% ▲	9% ▲
<b>Cash earnings after tax</b>	<b>\$107m</b>	<b>10% ▲</b>	<b>4% ▲</b>

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(1) 2H17 adjusted for the \$16m profit on disposal of a vendor finance entity

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Turning to BOQ Business on slide 19, and it may surprise some to see that it actually contributes a higher proportion of earnings than the Retail division. Given the majority of its assets are 100 per cent risk weighted though, we do allocate more capital to BOQ Business than Retail Banking.

Given the stronger growth we are seeing in commercial loans and BOQ Specialist housing, there has been better top line growth in BOQ Business. Expense growth has been managed in line with revenue growth so underlying profit growth has been positive, particularly compared to the same period last year.

Seasonality is particularly prevalent in commercial lending, with stronger asset growth and fee income typical in our second half relative to our first half. I'm not trying to provide guidance here, but simply providing an observation on recent historical trends.

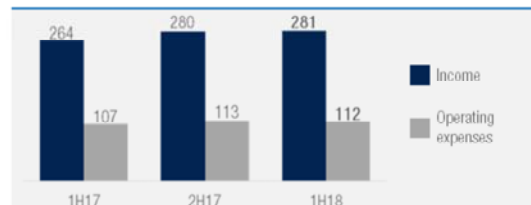
# BUSINESS BANKING



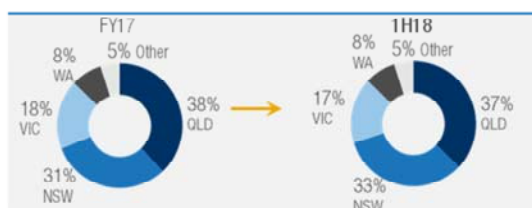
## SUMMARY

- Focus on quality and growth in niche segments, delivering \$281m in commercial loan growth
- BOQ Specialist mortgage growth remains strong
- BOQ Finance focus on margin and mix
- Delivering through consistent and superior industry specialist relationship offering

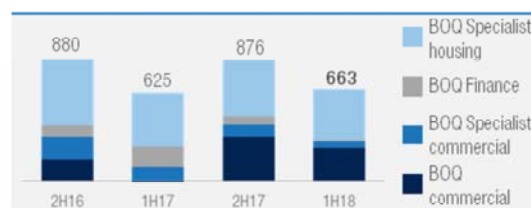
## INCOME AND EXPENSES (\$M)<sup>(1)</sup>



## COMMERCIAL LOAN GEOGRAPHIC MIX



## LOAN GROWTH BY CHANNEL (\$M)



The BOQ Business strategy is very much focused on growing in our target niche segments including medical & dental through BOQ Specialist, corporate healthcare & retirement living, hospitality & tourism and agribusiness.

The business has demonstrated good success in these segments in recent periods, delivering growth of 281 million dollars in 1H18.

BOQ Specialist has been very strong in growing its housing loan book, although commercial loan growth has slowed as competitors become more aggressive in that market. We remain confident that BOQ Specialist business will be able to defend its strong market share position in the medical segment, and continue to grow its mortgage book by targeting professionals at the early stages of their career, which provides a good pipeline of potential future commercial lending customers.

BOQ Finance also traditionally sees slower growth in the first half compared to the second, but this business has been successful in growing its structured vendor programs which do tend to be higher margin than more commoditised equipment leasing.

Overall, the BOQ Business team led by Brendan White has also been successful

at diversifying its portfolio geographically, with QLD exposure down to just 37 per cent.



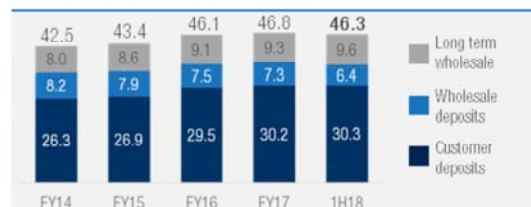
# FUNDING MIX



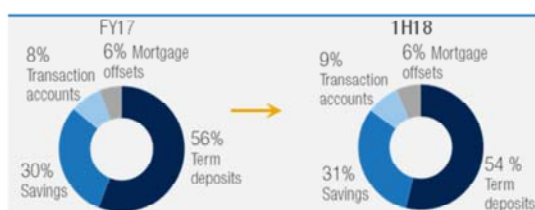
## SUMMARY

- Focus on growing lower cost deposits, diversifying funding base and improving mix
- Long term funding profile built out through senior unsecured
- Pricing analytics tool deployed to enhance term deposit retention levels
- Capital Note issuance to refinance redemption of CPS

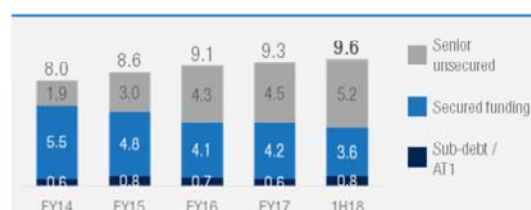
## OVERALL FUNDING MIX (\$B)



## CUSTOMER DEPOSIT MIX



## LONG TERM WHOLESALE FUNDING (\$B)



Moving to funding now on slide 21 and the story here is also one of diversification and improvement in mix.

We have continued to build out our stable wholesale term funding sources, while also focusing on improving our growth in stickier and better margin transaction deposits.

This is where having a strong branch network is key and an area where our Owner Managers have excelled in recent periods.

# NET INTEREST MARGIN



## NET INTEREST MARGIN MOVEMENTS 2H17 TO 1H18<sup>(1)</sup>



### 1H18 CONSIDERATIONS

- Front book vs back book impact ongoing given increased industry wide discounting for new business
- Deposit funding spreads improved for the half
- Hedging cost headwind emerging given current cash-bills spread

### SUMMARY OF KEY MOVING PARTS

Element	1H17	2H17	1H18 <sup>(2)</sup>
Asset pricing benefits	+6bps	+6bps	+4bps
Front book pricing & mix	(4bps)	(4bps)	(5bps)
Funding costs & mix	(3bps)	+5bps	+2bps
Hedging costs	-	-	+2bps
Capital & LCDs	(3bps)	(2bps)	(1bp)

Bank of Queensland Limited Results Presentation 1H18

(1) NIM has been adjusted for Mortgage Offset balances to align with industry practice. Average Mortgage Offset balances were \$1,447m in 1H17, \$1,565m in 2H17 and \$1,728m in 2H18.

(2) Other moving parts in 1H18 include the -1bp impact due to increased proportion of Third Party Costs

22

Getting into the detail of net interest margin on slide 22, and I'll point out that we have now moved in line with the rest of the industry in reporting our NIM net of offset accounts. This has an impact of around six basis points, which means our adjusted starting position from 2H17 is 1.96 per cent.

We did deliver an improvement of one basis point over the half to 1.97 per cent.

Stepping through each of the moving parts here, and we saw a benefit of four basis points from asset repricing that was completed during 2017. This was fully offset, though, by the ongoing front to back book pricing dynamic we see in the market which means that new business is written at rates lower than the average of the portfolio. This dynamic has increased in some parts of the book, as competition for certain segments of home loans has intensified. This also included a mix related impact as the flow of higher spread interest only mortgage lending slowed down dramatically to 16 per cent, from 37 per cent in the prior half.

We did see a benefit from improved funding costs, as the overall term deposit spreads improved compared to the prior period. This improvement was not as strong as we had hoped, given spreads did widen for a couple of months throughout the middle part of the half.

There was also a benefit of two basis points from the reduction that has occurred in the three month bank bills relative to the cash rate, which impacts the costs of hedging this element of the interest rate risk in our portfolio. The average cost of hedging reduced from 29 basis points in 2H17 to 23 basis points in 1H18. This trend has reversed recently and I'll cover this in the outlook.

Our NIM was reduced by one basis point due to the lower yield on the 4.2 billion dollar capital and low cost deposits replicating portfolio.

With the increased mix of business being originated through third parties as well as an increase in payments to owner managers due to strong performance against the Balanced Scorecard, largely related to deposit gathering, the third party cost component decreased NIM by one basis point.

In terms of the outlook, it is always very difficult to forecast margin but I can take you through some of the moving parts as we see them.

We have not made any significant asset pricing changes since August 2017 so there are no benefits coming through for this element as we sit here today.

The front to back book pricing dynamic is ongoing, so we would expect a headwind of around five basis points in the second half from this element.

Funding costs can go either way depending upon competition and market conditions, but at this stage, on balance, we could see a reasonable benefit in the second half if rates stay consistent with where they are at the moment.

Capital and low cost deposits will continue to be a drag of around a half a basis point in the second half if current rates implied by the forward curve prevail.

We don't expect there to be any impact from third party costs.

The final element is hedging costs, which is looking like it will become a headwind in the periods ahead if current bank bill rates are sustained. This could hit margin by between five to seven basis points over the next two periods, with a drag of three basis points likely in the second half of 2018 if rates remain at current levels. This is a theoretical analysis, as this part of the yield curve has recently been quite volatile. We have been sheltered from most of this impact to this point through the term hedging strategy that we employ.

As always, industry pricing levels and general market conditions can impact product rates achieved on both assets and liabilities. It is difficult to provide clear guidance on the likely NIM outcome. But it is fair to say that the various moving parts are larger than they've been more recently and the outlook is less certain.

To give some perspective, our underlying NIM for the month of March was a

couple of basis points higher than the 1H18 level, largely due to improved term deposit spreads.

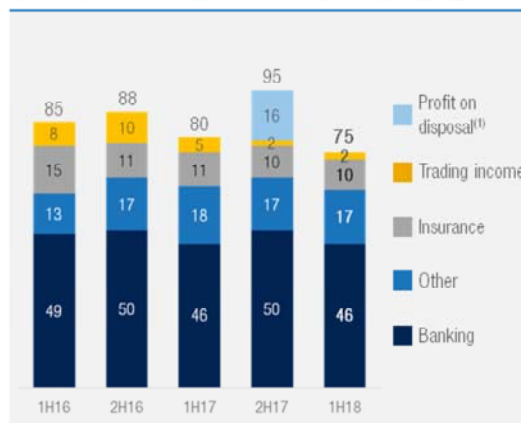
# NON INTEREST INCOME



## SUMMARY

- Banking fees remain under pressure
- ATM fee impact \$0.6m for the half
- St Andrew's income stabilised
- Trading income opportunities diminished

## NON INTEREST INCOME BREAKDOWN (\$M)



Moving to non interest income on slide 23.

As we have been saying for a number of periods, non interest income is a very challenging line to grow and we have to work very hard to even keep this line flat. That has been evident in this half with a five million dollar reduction.

Banking fees continue to face pressure and we see limited opportunities to generate trading income or other fee income.

Given this and the outlook for the second half, 75 million dollars would be a our expectation of a good result.

That's before the impact of the St Andrew's disposal that I'll discuss later.

# EXPENSES



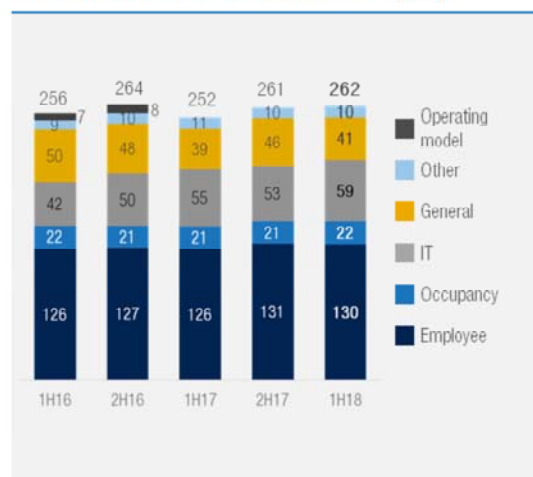
## SUMMARY

- Flat cost profile from 2H17
- IT expenses increased due to higher software amortisation
- Efficiency programs delivered targeted savings, allowing investment in growth businesses

## CARRYING VALUE OF INTANGIBLE ASSETS (\$M)



## OPERATING EXPENSE BREAKDOWN (\$M)



Operating expenses have been closely managed. We continue to work on identifying opportunities to digitise and find efficiencies across the business.

We must do this in order to provide the headroom for investments we to set the business up for the future.

We have a number of strategic transformation projects in progress but also a number of mandatory regulatory or maintenance projects that simply must be done.

Absolutely key to our success will be delivering our transformation program. However, we remain conscious of managing cost growth in light of the revenue growth profile.

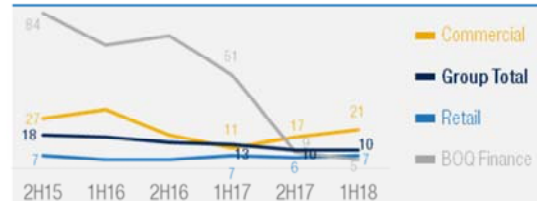
# ASSET QUALITY



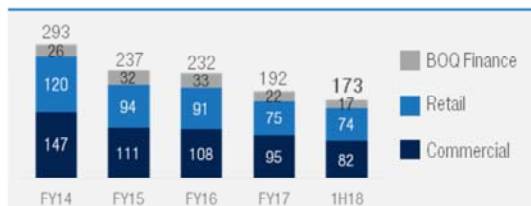
## SUMMARY

- Loan impairment expense flat at 10bps of GLA
- Impaired assets reduced a further 10% from 2H17
- New impaired asset volumes also reduced to lowest level since pre-2012

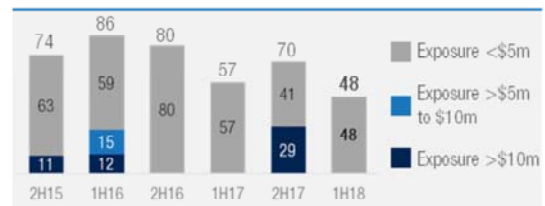
## LOAN IMPAIRMENT EXPENSE BY PRODUCT (bps)



## IMPAIRED ASSETS (\$M)



## NEW IMPAIRED ASSETS (\$M)



Turning now to asset quality, and there's no doubt that our loan book is in very good shape.

Loan impairment expense of 10 basis points and impaired assets of 173 million dollars or 39 basis points of gross loans are great numbers for the portfolio mix we have and given the journey we have been on since 2012.

Of course current economic conditions also play a role, with low interest rates, low unemployment, property price increases and reasonable levels of business confidence all contributing to low arrears and impairment results across the industry.

# PROVISION COVERAGE



## SUMMARY

- Specific provision coverage increased to 57%
- Provision coverage compares favourably with peers
- Total provision coverage remains strong

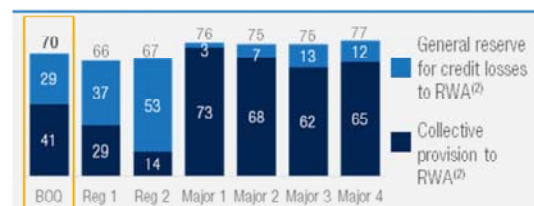
## SPECIFIC PROVISIONS / IMPAIRED ASSETS (%)



## TOTAL PROVISION & GRCL<sup>(1)</sup> / IMPAIRED ASSETS (%)



## PROVISIONING COVERAGE VS PEERS (bps)



We have also maintained strong provisioning coverage levels. Given the improvements in the underlying portfolio trends, we have been able to reduce absolute provisions, but our coverage ratios have remained consistent.



# ARREARS



## SUMMARY

- Arrears levels remain low across all portfolios
- Usual seasonal uptick apparent in February quarter

## COMMERCIAL ARREARS (bps)



## HOUSING ARREARS (bps)



## BOQ FINANCE ARREARS (bps)



Arrears levels remain benign. We have seen the usual seasonal increase in the post-Christmas period, but this has generally been at or below prior period levels.

The spike that is most evident in the BOQ Finance portfolio in the 30 day arrears bucket. I'm pleased to say that's improved since the end of February and is now back to the low to mid 60s.

## COMMON EQUITY TIER 1 MOVEMENTS



### SUMMARY

- 9.42% Common Equity Tier 1 (CET1) ratio
- 1H18 benefits of +26bps from APS 120 & GRCL reduction
- Capital management initiatives announced last half reduced CET1 by 29bps
- Other non-underlying items reduced CET1 by 7bps

### CAPITAL MANAGEMENT

- 9.25% interim CET1 target
- Capital utilisation options under consideration:
  - Organic growth
  - Accelerating digital transformation
  - Future returns of capital to shareholders

Turning to capital on slide 28 and there are a number of moving parts to discuss this half.

Firstly, we have the capital management initiatives announced at the full year 17 results, namely the eight cent special dividend and DRP suspension. These initiatives reduced common equity tier one by 29 basis points.

As we also flagged at the last result, we expected benefits to come through due to the implementation of APS 120 and a reduction in our general reserve for credit losses. The former, involving a reduction in risk weights on some of our housing loans that were previously risk weighted at 100 per cent, contributed 18 basis points to CET1. The reduction in GRCL following the implementation of our new collective provisioning model added a further eight basis points to CET1.

We did see a reduction of 5 basis points relating to a lower proportion of capital relief qualifying securitisation, that is funding the mortgage portfolio.

The net outcome of this was a CET1 ratio of 9.42 per cent. This remains well above our interim target of 9.25 per cent.

With the recent APRA consultation paper on the risk weighting framework

released, and more water to go under the bridge, we feel that we are in a very strong position.

As such, we continue to consider the best way to deploy excess capital to deliver enhanced shareholder returns into the future.

# SALE OF ST ANDREW'S



## SUMMARY

- Sale to Freedom Insurance for total proceeds of \$65m<sup>(1)</sup>, inclusive of a \$35m pre-completion reinsurance arrangement
- Entry into a three-year exclusive life insurance distribution partnership
- Indicative after tax profit on sale of ~\$8m<sup>(1)</sup>
- CET1 uplift of ~20bps following completion
- Customers to benefit from Freedom's specialised industry focus
- Subject to regulatory approvals and conditions – expected completion in second half of calendar year

## ST ANDREW'S HISTORICAL CONTRIBUTION (\$M)

	1H17	2H17	1H18
Non interest income	10	10	10
Direct operating expenses	4	4	4
Profit before tax	6	6	6
Income tax expense	2	2	2
Statutory net profit after tax	4	4	4

Today we have also announced the sale of our St Andrew's insurance business to Freedom Insurance Group.

BOQ acquired St Andrew's in 2010 and since that time it has made a very strong contribution to the group.

In recent years, however, the business and industry dynamics have changed dramatically, to a point where we believe Freedom is better placed to support St Andrew's future aspirations. This will also ensure BOQ can continue to deliver the best product solutions for our customers.

Subject to completion adjustments, the profit on sale will be approximately eight million dollars.

The sale will improve BOQ's common equity tier one ratio position by approximately 20 basis points, once the sale is completed.

Going forward, the absence of St Andrew's will reduce non interest income and expenses. In FY17, St Andrew's contributed 20 million dollars to non interest income and eight million dollars to operating expenses, with an after tax profit contribution of eight million dollars.

With that, I will hand back to Jon.



# Summary & Outlook

---

Jon Sutton  
Managing Director & CEO

### Industry

- Intense regulatory & public scrutiny
- Conduct, culture & trust critical
- Structural changes likely

### Economic

- Conditions supportive of small business
- QLD & WA showing signs of improvement
- Slowing credit growth

Thank you Anthony.

As I turn to the outlook, it makes sense to consider the external environment we are operating in. With increased regulatory and public scrutiny of the banking sector, there is no doubt that conduct and trust remain a core focus for the industry. At BOQ we are very aware of these challenges. We have worked hard and will continue to work hard to look after our customers to ensure their needs are met and respected.

There has been a heavy load of regulatory change with 57 external inquiries or reviews at a Federal level since 2007. BOQ has been and will continue to be an active participant in these processes. Together with a number of regional banks, we have also been calling for competitive neutrality.

We expect there will be structural changes to the industry as a result of this scrutiny. However, we encourage the regulators to consider how any changes could unintentionally impact the competitive landscape of the sector.

In terms of the economy, we remain cautiously optimistic. Although credit growth has been slowing, the other macro indicators are mostly heading in the right direction.

There are signs of improvement in the Queensland and Western Australian economies, while New South Wales and Victoria continue to perform well. In regional Queensland, the unemployment rate has declined in Mackay, Toowoomba and Townsville. The participation rate has risen across most regions, a sign that workers are becoming more confident about getting a job.

Over the past year, stronger business conditions are being reported across all sectors. This combination of strong residential activity and the infrastructure boom has boosted the construction industry.

Although system growth for commercial lending has been slower, we continue to find good opportunities in our niche segments which tend to be in higher growth sectors of the economy.



# STRATEGIC FOCUS



Strategic pillar	Customer in charge	Grow the right way	There's always a better way	Loved like no other
Goals	<ul style="list-style-type: none"> <li>Achieving minimum digital parity and meeting more of our customers' digital needs</li> <li>Delivering a seamless customer experience across channels</li> </ul>	<ul style="list-style-type: none"> <li>Improving deposit gathering and lifting MFI penetration across all business lines</li> <li>Growing assets with pricing based on risk profile and holistic relationship</li> </ul>	<ul style="list-style-type: none"> <li>Overhauling key processes to align to our relationship proposition</li> <li>Creating capacity to invest by Bringing the Future Forward</li> </ul>	<ul style="list-style-type: none"> <li>Delivering a differentiated service offering</li> <li>Investing in an engaged and capable team</li> </ul>
FY18 priorities	<ol style="list-style-type: none"> <li>Upgrade customer facing digital platforms</li> <li>Expand Virgin Money Australia product offering</li> <li>Increase frontline staff to support BOQ Business growth</li> </ol>	<ol style="list-style-type: none"> <li>Refocus distribution channels towards deposit gathering and MFI</li> <li>Close key product gaps that support deeper relationships</li> <li>Implement new FX digital platform</li> </ol>	<ol style="list-style-type: none"> <li>Operating model refresh and establish centres of excellence</li> <li>Delivery of key transformation initiatives</li> <li>Continuous improvement focused on productivity and customer experience</li> </ol>	<ol style="list-style-type: none"> <li>Delivery of the 'Customer Heartbeat' program</li> <li>Improve employee engagement</li> <li>Implement a program to increase advocacy across key business partnerships</li> </ol>

In this environment, our long term strategy remains the right one. We are building out our business bank and opening up new retail channels.

We remain focused on improving user experience in our digital offering. To do this, we are upgrading our online platforms and partnering with fintechs to deliver better solutions for our customers.

We will expand our product offering with a focus on increasing deposit gathering. This includes the rollout of an improved merchant capability and the launch of our partnership with a digital payments provider. These two products will make it easier for our SME customers to receive payments.

One of the key transformation projects we are commencing in the second half is moving our technology infrastructure into a modern cloud environment. This will improve the speed of project delivery and reduce costs.

There are also a number of initiatives underway across the group that will bring us closer to our customers and enable us to provide them with a differentiated service offering.

- 1 — Niche segment strategy delivering growth
- 2 — Virgin Money Australia continues to exceed expectations
- 3 — Structural changes in the industry provides opportunities
- 4 — Expense and investment discipline remains a priority
- 5 — Strong capital position provides flexibility

In summary, since 2012 BOQ has consciously evolved.

In the retail space, we have gone from being a mono-line distribution business to a diversified multi-channel retail bank. On the commercial side, we are now a niche specialist business bank with a focus on higher growth sectors of the economy. Across the Group, we have also expanded our geographical reach and have a national presence.

Underpinning this expansion is our commitment to growing the right way. Meeting our responsible lending obligations remains core to our operating model.

Our niche segment strategy is delivering in an ever changing operating environment. We are getting back to a steady rate of growth, with very solid results in our business bank.

Virgin Money continues to exceed our expectations. We firmly believe this business will become a significant contributor to the overall Group in the future.

We anticipate there will be structural changes in the industry given the issues that are emerging from the Royal Commission.

We believe competition and stability must co-exist. For the past decade, the default regulatory position has been focused on safety and stability. This has contributed to the emergence and maintenance of a concentrated market structure in retail banking. We have been advocating for regulatory settings to better balance the needs of both stability and competition.

Maintaining discipline around how we invest and spend remains a priority. Given the pace of change, this is essential so we can continue to invest for the future with a strong focus on improving customer experience.

Our capital levels position us favourably to many others in the industry. This provides us with the flexibility to consider options to utilise excess capital in a way that will enhance shareholder returns.

Finally, we are well positioned to deliver on our core strategic priorities over the medium to long term.

Thank you for your time. Now I will hand back to Tanny to moderate Q&A.



# Appendices

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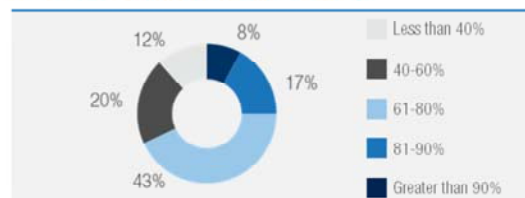
# HOUSING PORTFOLIO



## SUMMARY

- Broker settlements increased to 30% including Virgin Money
- Interest only settlements trending to less than 30%
- Room for growth under 10% investor cap
- Owner occupied P&I loans represent 49% of portfolio

## HOUSING PORTFOLIO LVR BANDS



## PORTFOLIO METRICS

Metrics (%)	1H17	2H17	1H18
Owner occupied	59	59	59
Investment	41	41	41
Interest only	39	37	32
Broker originated <sup>(1)</sup>	9	11	13
Weighted avg LVR	67	67	67
Line of Credit	8	8	7
Avg loan balance	\$265k	\$269k	\$275k
Variable rate	74	72	71
Fixed rate	26	28	29

## SETTLEMENT METRICS

Metrics (%)	1H17	2H17	1H18
Owner occupied	70	63	61
Investment	30	37	39
Interest only	38	37	16
Broker originated <sup>(1)</sup>	15	28	30
Weighted avg LVR	67	69	68
Line of Credit	2	1	1
Avg loan balance	\$370k	\$381k	\$394k
Variable rate	72	72	72
Fixed rate	28	28	28

# LIMITED EXPOSURE TO HIGH RISK SECTORS



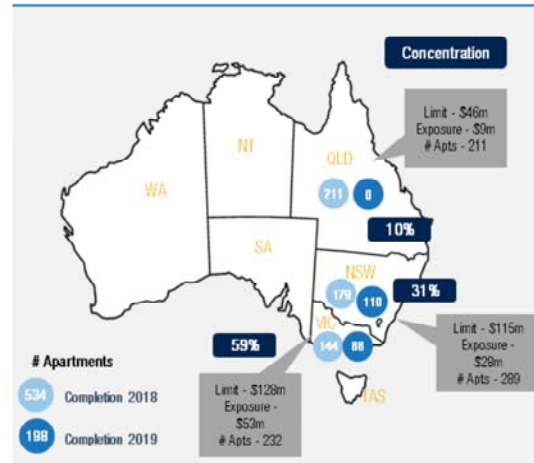
## APARTMENT CONSTRUCTION EXPOSURES

- \$90m current exposure to residential construction
- 16 developments across 3 states, completing 2018 through 2019
- Well diversified intra-state

## OTHER HIGH RISK SECTORS

- No material regional housing exposures
- No systemic issues emerging
- Direct mining industry exposure ~\$100m

## LENDING TO RESIDENTIAL APARTMENT CONSTRUCTION



# ABBREVIATIONS



1H: First half of financial year	EPS: Earnings per share
2H: Second half of financial year	FY: Financial year
30DPD: 30 days past due	GLA: Gross Loans & Advances
90DPD: 90 days past due	GRCL: General Reserve for Credit Losses
APRA: Australian Prudential Regulation Authority	LCD: Low cost deposit
APS: ADI Prudential Standards	LOC: Line of Credit
Apts: Apartments	LVR: Loan to valuation ratio
AT1: Additional Tier One	MFI: Main Financial Institution
Avg: Average	NIM: Net Interest Margin
BDD: Bad & Doubtful Debt Expense	OMB: Owner Managed Branch
bps: basis points	P&I: Principal & interest
CAGR: Compound annual growth rate	PCP: Prior corresponding period
CET1: Common Equity Tier 1	ROE: Return on equity
cps: Cents per share	ROTE: Return on tangible equity
CPS: Convertible Preference Shares	SME: Small and Medium Enterprises
CTI: Cost-to-income ratio	TD: Term deposit
DPD: Days past due	VMA: Virgin Money Australia
DRP: Dividend Reinvestment Plan	