Bank of Queensland Limited
ABN 32 009 656 740
Level 6, 100 Skyring Terrace, Newstead QLD 4006
GPO Box 898, Brisbane QLD 4001
Telephone (07) 3212 3333
www.boq.com.au

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Managing Director and CEO Address
2018 Annual General Meeting

Thank you Roger and good morning ladies and gentleman. I will start with the highlights of the results.

The strategy we have been implementing in the past few years has transformed BOQ into a resilient, multi-channel business that is geographically diverse. This evolution of BOQ has continued throughout this financial year.

In FY18, we delivered a good underlying result in what has been a significantly difficult operating environment. We have achieved consistent lending growth in our commercial niche segments. Asset quality across our loan portfolio has improved further and remains a key strength. Our strong capital position provides us with options to invest in the future and enhance shareholder returns for the long term.

Cash earnings after tax decreased two per cent over the year to $372 million. Excluding the $16 million one-off profit on disposal of a vendor finance entity, which occurred in FY17, cash earnings increased three percent.

While earnings per share decreased three per cent on a headline basis, it did increase one per cent on an adjusted basis. Return on equity decreased 50 basis points to 9.9 per cent, or 10 basis points on an adjusted view. The ordinary dividend has been maintained at 38 cents per share, bringing the full year dividend to 76 cents per share.

Turning to the drivers of the result. We achieved lending growth of $1.5 billion. This was close to $800 million more than in 2017. We also delivered an improvement in net interest margin to 1.98 per cent. Our cost to income ratio was 47.5 per cent, an increase of 20 basis points from the underlying level of 2017. Loan impairment expense reduced $7 million to $41 million, or just 9 basis points of total loans.

There has been a significant shift in our business mix. Our strategy to diversify our channels has delivered material benefits. Noticeable improvements in the business mix, channel and geography, positions BOQ to be more resilient over the long term.

Loans originated through Virgin Money Australia and BOQ Specialist now account for 20 per cent of the loan portfolio. Since acquiring these businesses, both have delivered consistent organic growth which we expect will continue into the future.

BOQ Business increased cash earnings by 10 per cent this year with revenue growth of five per cent. It now contributes close to 60 per cent of the Group's cash earnings. Since FY14, it has delivered an average uplift in lending balances of six per cent per year. In addition, we have made good progress in digitising our back office as well as our systems and operations. This evolution is continuing, particularly in the technology space.

While the business continues to grow, we have maintained focus on delivering results. There is no doubt that 2018 has been a tough year for the banking sector. Public scrutiny and regulatory change, slowing credit growth and changing customer expectations have all had an impact.

Despite this, we have delivered underlying revenue growth of two per cent. This result was supported by an improvement in net interest margin. Lending growth was almost fully funded by customer deposits. There was also an improvement in the funding mix. Expense growth was prudently managed at three per cent with core expense growth of just one percent. This was achieved while still investing in the business.

The performance of our commercial niche business segments has been a stand-out again. We achieved lending growth of $623 million across these segments which include the health sector, retirement living, hospitality and agribusiness. In the housing loan portfolio, Virgin Money Australia and BOQ Specialist continued to deliver strong levels of growth. These businesses contributed to $653 million of total housing loan growth.

BOQ Finance had a particularly strong year with growth of $250 million. The prospects for this business remain strong. In the new financial year we established a new partnership with Harley-Davidson to provide finance through their 46 Australian dealerships. This demonstrates our capability in delivering finance solutions to iconic global brands.

The loan book in the branch network contracted. This is in line with the expansion of our channels and corresponds with a 27 per cent reduction in branch numbers from FY14 to FY18. Despite this, we have seen an increase in deposit balances, with deposits per branch increasing 43 per cent over that period. This shows the important role that our branches continue to play in our distribution footprint and the overall funding of the group.

The improvement in our asset quality metrics is very pleasing. Impaired assets and loan impairment expense both reduced 15 per cent from FY17. Our bad debt expense was just eight basis points of total loans in the second half. Arrears levels remain low and steady, comparing favourably with peers. These metrics are the direct result of the very deliberate approach we have taken to risk management. We have a clear risk appetite with responsible and robust lending practices.

Our capital position remains strong with a common equity tier one ratio of 9.31 per cent as at 31 August 2018. Customer expectations are rapidly changing when it comes to digital experience. We have therefore decided to take advantage of our strong positon and invest for the future. We plan to increase capital expenditure in FY19 to focus the business for future success. This will involve utilisation of seven basis points of additional CET1 to enhance our digital banking platforms and improve customer experience.

Turning to the outlook, and looking at the broader picture, there are a number of long term trends that are shaping the sector. These will create a host of challenges, but also opportunities, especially for BOQ. The economic landscape is changing. Slower housing credit growth, elevated basis risk, lower house prices and stagnant wage growth are having an impact on revenue across the industry.

Given system credit growth is slowing, we continue to see fierce competition for new business with discounts at historical highs. There are both supply and demand issues at play here as many banks have been tightening lending standards and housing prices have been falling sharply in some markets.

Regulators and government understand the important role that the availability of credit has on the economy. We remain focused on growing commercial lending in our target niche segments, as well as supporting SMEs. In retail lending, it is important that all participants have clarity on responsible lending, particularly with respect to requirements for validation.

Customer digital needs remain a key focus, and we recognise increased investment is required. We remain in a highly competitive environment and as a result value chain disruption continues at pace. In addition, banks face ongoing public scrutiny and the likelihood of further regulatory change. We believe BOQ is well positioned because of its simpler business model and risk based approach.

Our strategy to diversify lines of business is the right one. An example of this is the growth of Virgin Money Australia, BOQ Specialist, BOQ Finance and our niche commercial segments. Progress has been made with improving our technology.

We have successfully implemented a number of projects utilising our API gateways, allowing us to partner with third parties to deliver better solutions. For example the new Virgin Money Australia credit card app and a digital financial markets platform which is scheduled for launch in the second half of FY19.

In 2019, work will continue on modernising our technology infrastructure, simplifying our core banking platform and shifting towards a hybrid cloud environment. These initiatives will help us deliver improved digital banking platforms that meet the changing needs of our customers.

Importantly, we know digitally active customers are more engaged, more profitable and are increasing in numbers. We recognise that there is work to do so that we meet the needs and expectations of these customers.

We are also accelerating a series of targeted investments to fast track our digital strategy. This will include upgrading our digital banking and customer engagement platforms and modernising our call centre systems. These initiatives will be leveraged across all of our brands.

The proven success of Virgin Money in Australia across multiple products gives us great confidence in this brand's future. Our aspiration remains for it to become a full service digital bank. We are looking closely at new technologies which will significantly enhance the customer experience and develop the potential for this strong brand.

In summary, the environment remains one of change but we firmly believe that our strategy is the right one. What is particularly pleasing is the acceleration of growth we have seen across our niche business segments and Virgin Money Australia.

We continue to deliver results while managing the business for the long term. Our asset quality metrics demonstrate our portfolio is resilient. We are taking advantage of our strong capital position to invest for the future.

While the likelihood of further regulatory change is high, we remain committed to delivering positive customer outcomes. We will also continue to advocate for competitive neutrality. Our future focus will be on enhancing the digital capability across the Group.

Finally, we are confident that BOQ has a key role to play in servicing the needs of retail and commercial SME customers, now and in the future.

Thank you.

Jon Sutton

Jon Sutton
Managing Director & CEO