Commonwealth Bank of Australia

Transcript – 2021 Half Year Results Briefing

For the half year ended 31 December 2020

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Melanie Kirk: Hello and welcome to the Commonwealth Bank of Australia's results briefing for the half year ended 31 December 2020. I'm Melanie Kirk and I'm Head of Investor Relations. Thank you for joining us.

For this briefing we'll have a presentation from our CEO, Matt Comyn, with an update on the business and an overview of the financial results. Our CFO, Alan Docherty, will provide details of the financial results and Matt will then provide an outlook and summary. The presentations will be followed by the opportunity for analysts and investors to ask questions. I'll now hand over to Matt. Thank you Matt.

Matt Comyn: Thanks very much, Mel and good morning to everyone. The last six months have clearly been a very challenging period for many Australians and individuals right around the world. From our perspective we're starting to see a marked turn in an improvement in economic conditions, which is of course on the back of very effective management of the pandemic and very significant stimulus packages from both the Federal Government, the monetary supply settings from the Reserve Bank and a whole range of different business support measures that have been in place.

From our perspective, we've been very focused on making sure that we're continuing to support all of our customers and communities through the pandemic. We've been focused on very strong operational excellence, which I think is well reflected in our volume growth through the half. We've continued to strengthen our balance sheet to ensure that we're well prepared for a range of economic scenarios and we also thought it was an appropriate time to refresh our strategy and set a more ambitious agenda for the future.

One of the things that's really stood out to me during the half has been the commitment and discretionary effort from all of our people to support our customers and communities. During the course of the pandemic, we've added 1,000 people into our financial assistance solutions team. We've also relied very heavily on technology to support our customers during that time. We saw more than 6.3 million people come to our coronavirus support page, which provided the latest information for all of our customers.

On the back of the investments that we've been making in technology, we're able to stand up our BizExpress product and originate more than 50% of SME loan guarantees through the course of the year. We've also used technology to supplement a very large operational process to support the payment deferrals. We've made more than 250,000 calls to customers, but we've also supplemented that with 730 million messages across our mobile app in particular, but also email, a synchronous chat, to make sure that we could work very closely and constructively with our customers to deliver them the best possible outcomes.

The repayment deferral outcomes that are seen on this slide are certainly a good reflection of the way that we and the broader industry have been able to make an orderly transition through the various stages of the pandemic. When we look at the home lending deferrals firstly, 84% of customers are now have exited from their home loan deferral and of those 84%, 92%, as you can see on the slide, have returned to their pre-deferral levels. On top of that, we've seen about 3% switching to interest only, 4% requiring further assistance and about 1% impaired.

From a business lending perspective, the numbers are even stronger with 98% of customers who went into a repayment deferral now exiting and of those, 96% returning to their repayment levels and we're seeing of that remaining 4%, 2% requiring further assistance and 2% in impaired.

Clearly, as we go forward, we'll continue to work with customers who are still in deferral and we do anticipate, even though the numbers are getting much smaller, that there will be customers during the course of the year that will require ongoing assistance and we're seeing that reflected in the areas that are most impacted by the pandemic at this stage.

As I said, we've had a big focus on just operational excellence and making sure we're serving our customers' day-to-day banking needs very well. This has being reflected in strong volume growth across all of our core businesses. In home lending, as you can see, fundings were up strongly in the half and we grew well above system at 1.5%. Particularly coming into the last quarter of the calendar year and the month of December was a strong month with balanced growth of more than $3 billion.

Again, we've seen a strong deposit performance, growing above system in household deposits, but our transaction account balances, which as you know is a key measure that we watch very closely, increasing by 30% and 400,000 new transaction accounts, notwithstanding we do suffer some impact from the lack of migrants, which is obviously a segment that we traditionally do very well in.

Our business bank performance has been strong over the half. If we look at our business lending, we've seen a balance growth of 7.4%. That would be the strongest balance growth we've seen in about four years. It's obviously against the backdrop of a weaker system growth, which is why you see that reflected in a system number of more than three times the market rate of growth. We've seen those balances grow across a diversified range of sectors, from agriculture, to healthcare, to manufacturing.

Importantly, it hasn't come at the expense of either margin or of increasing our risk exposure. We look at the weighted average of probability of default of new originations and during that period, they've actually been one notch higher or better than the portfolio.

As you can see, that strong business performance is also reflected in our business deposits, growing almost 20% and our business transaction accounts up 41% for the period. We also grew strongly in our New Zealand business in ASB, with home lending growing at 1.3 times system and on business lending, growing about 130 basis points of share over the period.

As I said, home lending, both fundings but also approvals, have continued to grow strongly during the period. As I said, December was a strong month and as we look at January, certainly versus the prior corresponding period, it was again a strong month of applications.

As we look across a couple of areas of our business that have been more challenged than the pandemic, I think credit cards is a good example of that. We saw balance growth over the course of the calendar year down about 16%. Actually sequentially, so up about 2% in terms of balances.

One of the key factors of that has been obviously the substantial fiscal stimulus that has been in place and people repaying those balances and you'll see that reflected in one of the slides Alan will take you to, where there's been a substantial reduction in credit card 90-day arrears.

Importantly we're starting to see now though an improvement in our application volumes coming back towards pre-pandemic levels and our new CommBank Neo card represents more than a third of our new applications.

As you'd expect during the period, it's been another very strong performance from CommSec, well reflected in our new trading accounts, up more than 130%. Our active accounts have increased on the prior corresponding period by about 83% and we've seen about a 150% increase in contract note volumes, which is reflected in our other banking income, which Alan will refer to later.

Overall, we feel that we've been able to deliver strong performance to a variety of our stakeholders. We're very pleased to see, for the first time, get to number one in our Net Promoter Score across all of our businesses.

Unfortunately we finished at number two in our retail bank at the end of the calendar year and whilst it's pleasing to be at number one across NPS for many months of that first half, we'd be the first to acknowledge that we want to see a significant increase in our absolutely Net Promoter Scores.

Our people have taken a lot of pride and motivation in being able to play an important role supporting our customers and broader economy. I think that's best reflected in our people engagement score of 80, which was the highest for more than five years. We've also seen improvements in our RepTrak, which is our measure of reputation tracking, it's an external survey that we subscribe to.

We're at number one for the first time in five years. We've seen similar improvements in many of our brand metrics, but again, we recognise there is more work to do to restore our standing in the community. Overall, that consistent performance and execution of our strategy has enabled us to deliver consistently for our shareholders.

Our balance sheet has never been in a stronger position. Our deposit ratio has now increased to 75%. As you can see, up 20 percentage points since 2008. Our provisioning level, total provision is now at $6.8 billion, peer leading provision coverage at 181 basis points to credit risk weighted assets and our capital, measured on a Common Equity Tier 1 Level 2 basis, at 12.6% for the half and another 32 to 42 basis points that we're anticipating from previously announced divestments.

Thought I'd spend just a moment on our strategy. Over the last 2.5 years we feel that we've made good progress on improving and becoming a simpler and better bank. But we also thought it was an appropriate time to refresh that strategy and set a more ambitious agenda for the future. There are four key strategic pillars. The first is leadership in Australia's economic recovery and transition. The second, reimagined products and services. The third, global best digital experiences and technology. The fourth, building on our simpler better bank is simpler and better foundations. I thought I might just briefly move through some of the key highlights from each of these strategic priorities.

The first, to play a leadership role in Australia's economic recovery and transition, starts by making sure that we continue to provide the right support to our customers and communities when they need us most, which will be required throughout the course of the pandemic. But looking forward, we see that there are real opportunities for the Commonwealth Bank to participate and allocate capital to those sectors of the economy that need it most.

One of the key drivers looking forward is going to be a pick-up in business investment to see Australia recover. We saw quite sluggish business investment even pre-COVID, which is why we want to play a bigger role in our business banking and making sure that we're allocating, as I said, capital to the areas of the economy where we think we can drive the most productive improvements and the Australian economic outlook.

We also think that it's really important to make sure that we're participating again from an institutional perspective and providing access to pools of liquidity, both domestically and internationally. Our institutional bank were able to do that in the half to about $159 billion. We also saw strong performance particularly in our markets trading business.

Our reimagined products and services is all about our customers, understanding and anticipating what we believe their needs will be and then making sure that we understand what sort of problems there are and how we can best resolve those. I think many people see banking as a commoditised product. We take a different view and we intend to be able to deliver a number of distinct customer propositions to really set banking with the Commonwealth Bank apart from some of our competitors.

A few quick examples, one would be the CommBank Neo card, which as I said, is now playing quite a significant role in our credit card applications. This enables customers for a fixed fee to have access to the benefits of being able to pay on credit. We see that customers really want to take more control. They want to see more simplicity and they also want to have help in and around their budgeting needs. We've recently launched AdvancePay which enables customers to access a small portion of their income which has been earnt but not yet paid, we're currently trialling and anticipate rolling that out a little later this year.

A third example might be our Bill Sense product, which is really about helping our customers to budget and anticipate what expenses are going to be upcoming. We're able to do that by processing more than 16 billion transactions across 17 million accounts and then making about 60 million bill predictions for our customers looking forward.

As we think about having the best products and services for our customers, also an element of that is making sure that we're integrating additional external services. We recently announced that we'd applied to be an accredited recipient of data under the Consumer Data Right. We see that as an important piece of legislation, not just for the banking industry, but more broadly.

There's a number of ventures that we're scaling in X15, which we anticipate will integrate some of those external services into a richer and more differentiated banking proposition for our customers. We recently announced the acquisition of Doshii, which is a point-of-sale provider in technology that we want to add in to further augment our merchant service offering.

We've talked quite a bit about digital and technology and the importance of that. I think that's very much been part of the Commonwealth Bank's success for the last 20 years. I think it's really important that we continue to innovate and to invest. That starts, particularly at the moment with the best-in-market digital experience. We've got more than 7.5 million digitally engaged customers, we've seen significant increases during the course of 2020.

We peaked at more than 10 million daily logins into our CommBank app during 2020. We're recognised as the number one mobile banking app, both locally and internationally by Forrester, but our aspiration has to be to set the best possible digital experience for our customers across their broader lives so that we can really be at the centre of their relationship and a trusted relationship with the Commonwealth Bank.

To be able to provide that personalisation to our customers, we've talked about our customer engagement engine. Simply we're analysing 157 billion data points across 400 machine learning models in real time. That enables us to make about 35 million decisions each day across our customer base.

As we look forward, there's going to be a number of capabilities that we're investing into to both ensure that we continue to innovate, but also that we're able to increase the velocity of change inside the organisation.

Some of that is about reconfiguring and decoupling some of the systems into micro services, some elements of that are about moving those services onto the cloud. Of course that starts with having best-in-class engineering capability. We already have a very large IT engineering team, but we're certainly looking to continue to expand and making sure that we're attracting the best talent in market.

Then our fourth strategic priority and as I said, very much building on the last 2.5 years of simpler, better foundations. We've invested heavily to ensure that we are becoming a simpler and better bank, particularly around the management of non-financial risk which has been a key focus for us over the last 2.5 years. Pleasingly this was recognised during the half by APRA with the return of half of the capital or $500 million.

From here and we're also during the course of today, released the latest Promontory reports and whilst we've completed a significant number of the milestones, as you would anticipate, the remaining milestones are the most challenging and it's really incumbent on us to be able to demonstrate that all of the changes that we've made are sufficiently embedded in the organisation and are sustained before we can reasonably expect any further capital releases.

We've continued to make good progress across our portfolio with the divestment being completed of BoCommLife during the period, which clearly contributed to our Common Equity Tier 1 capital. We remain committed to disciplined management of capital and costs. Our approach to costs remains unchanged. We very much look at each period with an intention to reduce costs. But we also retain the flexibility where we see opportunities to invest in our business, to either, as we have in this period, deliver above system volume growth or to further enhance our competitive offering and positioning, then we're prepared to make that.

Now turning to the result. Firstly starting with statutory profit which is, as you can see, is down 20.8%. About two-thirds of that is driven from the one-off gain in the last period from the sale of our CFS Global Asset Management business. That broadly reconciles statutory to the cash net profit after tax.

Of course the main drivers that saw the cash NPAT come down were the remediation and COVID-related costs and impairment. If we were to exclude those for a moment, our cash net profit after tax would be broadly flat. Alan's going to go through more of the drivers of those in a minute.

The capital result, as I said, is very strong at 12.6% and about $10 billion above APRA's unquestionably strong 10.5% benchmark. That, coupled with the strong operating performance and that surplus capital position, has allowed the Board to declare a fully franked dividend of $1.50 for this period and we will be neutralising the dividend reinvestment plan.

Now if I look sequentially, actually our profit sequentially is up 32% on higher income of just under 2%. Our expenses are down 2.2% period on period and notwithstanding an $882 million loan impairment expense in the half, compared with significant provisions that we took in the sequential last half, our loan impairment expense fell to 22 basis points. I'm now going to hand over to Alan, who's going to talk you through the result in more detail.

Alan Docherty: Thank you, Matt and good morning. In summary terms, this result again demonstrates that notwithstanding the current economic environment, a combination of our competitive advantages and a disciplined execution of our strategy can deliver industry leading outcomes for our customers and our shareholders.

Obviously, our economic environment today is characterised by historically low rates. We're recovering from our first recession in nearly 30 years and we're seeing a period of elevated economic uncertainty due to coronavirus.

So there are certainly some challenges there. However, in comparison to most other advanced economies around the world, Australia has so far delivered globally leading health outcomes, a very strong rebound in economic activity and a strongly capitalised banking system that supports the continued flow of credit to the economy.

We can't be complacent but we should have confidence in our ability to collectively manage through this uncertain period.

In this context, CBA has continued to perform strongly. Customer behaviours have continued to change in ways that deepen our existing competitive advantages with a broadening of our base of digitally engaged customers; a scale advantage that attracts more customers to the Commonwealth Bank during uncertain times; a strong rebound in the housing market that provides additional moment to our core home lending portfolio; and a balance sheet mix that helps us consistently generate structurally higher levels of organic capital.

We have continued to build upon those competitive advantages through supporting our customers and building stronger levels of advocacy. A consistent operational execution across all of our core banking businesses and instituting better risk and capital disciplines across the Group.

This is reflected in the delivery of a strong set of outcomes in this half year result with market share gains in all core products, peer leading provisioning levels, a significant capital surplus and a growing dividend.

Now, onto the detail and let me start off as usual with a reconciliation of total statutory profit to cash profit from continuing operations. Statutory profit was $4.9 billion for the half year, largely due to those one-off gains on the sale of our various wealth management businesses, most notably the completion of the sale of BoCommLife in December.

After adjusting out discontinued operations and the usual non-cash items, we delivered continuing cash profit of $3.9 billion for the six-month period. As Matt has described, while that cash profit is up strongly against the prior half, it's 11% lower than the equivalent period last year.

With operating income down 0.5%, operating expenses up nearly 7%, leading to that decline in operating performance and loan impairment expense significantly higher than the levels we were reporting pre-COVID. I'll unpack these P&L items in a bit more detail before drilling into the balance sheet, capital and dividend considerations.

Looking firstly at our first half operating income. It was only slightly below the $12 billion that we achieved in the first half of the previous financial year and that was despite the impact on our margins of a much lower cash rate environment.

That stabilisation of our top line performance was largely a function of continued strong growth in home lending and business lending volumes with both products growing well above system.

By contrast, Institutional lending balance were lower as utilisation levels dropped in an environment of very strong corporate liquidity. Other banking income was lower due to some unavoidable headwinds from COVID-19 on credit card and retail FX fees and impairments on aircraft, although that was somewhat mitigated by a very strong performance in both our CommSec and global markets businesses.

Funds management and insurance income increased due to lower general insurance claims this period versus the first half of last year, which of course included the impact of the bushfires.

As you can see on the right-hand side of that chart, revenue has increased 1.9% on the sequential half due to that strong market's performance as well as day count. Though net interest margins were lower over the sequential half, as you can see here, margins fell three points to 201 basis points.

The drivers of our net interest margin are well known. First of all, we are carrying higher liquids balances due to the stimulatory effects of fiscal and monetary policy on domestic money supply. That turns up on our balance sheet as higher deposit liabilities and higher cash and liquid assets.

While there is little to no yield to be earned on the marginal dollar of extra liquidity, the two basis point dilution of reported margins from higher liquids has a very minimal effect on our level of net interest earnings.

Asset pricing changes cost us two basis points due to the continued competitive pressures on home loan margins and lower revolve rates on credit card balances.

The low-rate environment continued to feed through into lower deposit margins, though are replicating portfolio and lower wholesale funding costs, provided some protection there.

Portfolio mix was flat with the benefit of the deposit funding mix offset by continued decline in consumer finance balances and we've seen a one-off three basis point benefit of the bottoming out of basis risk.

Looking ahead, our expectation remains that we'll encounter a seven basis point headwind over the course of this financial year as a consequence of low rates.

Operating expenses increased 6.9% on the comparative period. This was mostly driven by higher remediation costs which were up $241 million, largely due to top-up provisioning for historic wealth management-related issues.

Excluding that, underlying costs were up 2.3%. The biggest driver of the cost increase was a decision we made this year to re-base our investment spend envelope upwards from around $1.4 billion last year to an annualised run rate of around $1.7 billion this year.

We believe that additional spending is necessary to strengthen and extend our digital capabilities and continue to innovate for future growth, which we believe is crucial to the long-term health of the franchise.

This added 2.4% to our underlying cost growth this period, our ongoing business simplification initiatives resulted in incremental productivity savings of $193 million. Those savings have offset both the growth and volume-related expenses related to a strong performance in home and business lending and other inflationary cost increases. That has helped bring the net underlying cost growth down to 2.3% against the comparative period.

Over the sequential half, total costs are 2% lower and we have reaffirmed our strategic focus is on long-term cost reduction in a low earnings environment.

Turning to our balance sheet settings and looking first at credit risk, during the half we further increased our forward-looking adjustments to collective provisioning of our exposure to specific business sectors. This resulted in our corporate loan loss rates remaining elevated in the current half.

Our usual leading indicators are trending positively with consumer arrears trending lower and reductions in troublesome and impaired exposures. However, these indicators are still being heavily insulated by the government, central bank and regulatory support measures.

From here, we would expect to see these rates increase in the second half of this financial year as the deferral programs come to an end and the income support measures are tapered. So given that uncertainty, it's too early at this point to unwind the collective provisioning on our consumer portfolio.

The increase in our level of collective provisioning during the half was driven by specific business sectors of concern. Aviation remains our key sector of concern given the likelihood of an extended period of restrictions on travel. Around half of our exposures in this sector are to airports and the other half are to airlines and you can see we have significantly increased provisioning coverage here as well as taken additional impairments to the carrying value of our aircraft.

Provisions have also been increased on other vulnerable subsectors, including hotels and other businesses that were reliant on international tourists and business travellers and commercial office property and student accommodation.

So while the top-down macroeconomic numbers are improving, the uncertainties around the outlook and our judgment mean that it's still too early to be releasing collective provisions. As a result, over the last six months, we further increased collective provisions in the consumer portfolio by 6% and in the corporate portfolio by 17%.

That takes our total provisions to $6.8 billion and our coverage to credit risk rated assets to over 1.8%.

We are very well positioned for the future. Our current level of provisioning is now $1.8 billion higher than the level of provisions that we calculate would be required under our central economic scenario. Certainly, the macroeconomic trends are continuing to point in the right direction.

Our funding settings are in good shape with a customer deposit ratio of 75% and short-term wholesale funding levels remaining at historical lows.

We have so far accessed $19 billion of three-year funding from the Reserve Bank's term funding facility and there's a further $22 billion available under that facility at a fixed interest rate of 0.1%.

The size of our allocation is of course a function of the strong growth in lending to our small and medium sized business customers over the past year.

On capital, we've delivered the level 2, common equity tier 1 capital ratio of 12.6%, which is up 100 basis points since June. The good progress made on our wealth management divestments added 42 basis points this period and we delivered 43 basis points of organic capital generation.

Level 1 parent entity capital is higher again at 12.8% and our capital levels will be further strengthened when we finalise the majority sale of our Colonial First State business.

The interim dividend of $1.50 represents a cash payout ratio of 67%. This is a little below our target dividend payout range, reflective of a period of economic uncertainty and is in accordance with the latest APRA industry guidance released in December.

The Board has also reaffirmed that our dividend payout guidance remains that long-term target range of between 70% and 80%. Given our significant surplus capital position, the Board has also decided to neutralise the interim dividend reinvestment plan.

That's the fourth occasion in the last five halves that we have avoided inflating our share count via the DRP. That accords with our long-term focus on managing our share count and is underpinned sector leading total shareholder returns for the last two decades.

Looking ahead, there are three key factors that will determine the timing and extent of future capital management initiatives. Firstly, a greater level of certainty around the domestic economic outlook. Secondly, our ongoing assessment of credit quality and likely level of forward loan losses. Thirdly, the prudential regulatory guidance on capital management activities.

We will keep the market updated as this situation continues to evolve throughout 2021. Matt will now take you through the outlook and a closing summary. Thank you.

Matt Comyn: Thanks very much, Alan. Look, overall as we turn to the economic outlook, our base case for global growth is about 5%. Clearly, there's going to be some uneven distribution of that during the course of the period ahead. What we think has really been demonstrated during calendar 2020 is the resilience of the Australian economy. We believe both Australia and New Zealand are relatively well positioned and of course, that starts with very effective management of the pandemic.

There's also a number of support measures or tail winds that we think are going to drive improving economic outcomes during the course of the year. One of those is the significant accumulated household savings which we think is more than $150 billion.

We've seen a strong recovery in the labour market with an unemployment rate now of 6.6%, the RBA forecasting at the end of the calendar year of about 6%. Clearly that's a strong improvement but of course, there are risks to that. We've seen consumer confidence now at seven-year highs.

Business confidence is high, but it isn't quite translating into increased levels of business investment, understandably. And of course, the housing market has been very resilient, having fallen only 2% during the course of calendar 2020, and our economics team forecasting house prices to increase by approximately 8% during the course of the calendar year, about 9% in houses and 5% in apartments.

Overall, our base case is very similar to the Reserve Bank's latest forecasts and their statement of monetary policy last week, but as Alan has said, we want to make sure that we are prepared for a number of different risks to that scenario and ensure that the Bank and our balance sheet is well prepared for that range of economic scenarios.

Of course, as we look forward, a number of risks, some of which are going to be directly a function of the ongoing successful management of the pandemic, the vaccine rollout. I think particularly as we're seeing the tapering of some of the very substantial income support and some of the other measures that have been put in place, how effective are they at continuing the strong labour market recovery and a pick-up in business investment.

Now turning lastly to just a very quick summary. Overall, we'd say during the six months we've been very focused on making sure we're supporting our customers, which has been greatly assisted by having a highly engaged team of people and great technology to be able to rely upon.

Our operational focus has seen us deliver strong volume performance across all of our core businesses. We've been able to further strengthen our balance sheet and we're now very focused on ensuring that we continue to do all three of those and execute a more ambitious strategy for the future.

I'll now hand over to Mel for Q&A.

Melanie Kirk: Great. Thank you, Matt. For this briefing we'll be taking questions from analysts and investors. Please follow the prompt on the phone to ask your question. I will then call the name for the next question; the phone line will open. Please state your name and the organisation that you represent, and to give others the opportunity, please limit your questions to no more than two questions.

We'll now take the first question from Andrew Lyons.

Andrew Lyons: (Goldman Sachs, Analyst) Thanks, Mel. Andrew Lyons from Goldman Sachs.

Matt, just a question on expenses. For a long time now, CBA has been willing to grow costs above peers and it has certainly delivered a better outcome for shareholders via better revenue growth. Your commentary today would suggest that that strategy will likely continue, where you've said cost reductions are there but it's a long-term goal and you will continue to invest.

However, I'm just wondering, how flexible do you think the organisation's performance on costs can be if the revenue environment is such that even if you're still outperforming peers on revenue, that's driving a flat or a declining outcome on revenues over the medium term?

Matt Comyn: Thanks for the question. From our perspective, there's a lot of work that goes into our cost management and the initiatives that we're going to deliver during the period, and not just this year but into future years. I think what we've indicated and very consistent with our approach for a number of years is we believe that the best interests of the ongoing success of the Commonwealth Bank is having a degree of flexibility around that.

We start each period with the intent to reduce our operating costs, but as you said, we've seen opportunities in the last - certainly the last several periods, either to respond in the way that we're supporting customers with some of the substantial resources we've put into financial assistance solutions, but also in this period $88 million of expenses in volume growth from operations to business bankers, which has delivered strong above-system growth. Clearly, we're comfortable with that. We want to continue to invest in our technology. We believe that that's critical to the ongoing success of CBA.

I think we see that reflected, the technology actually assisting again in that above-volume growth, but we also have to be cognisant of that external environment. As you mentioned, it's a softer revenue environment, particularly given where low rates are.

So, between Alan and I and the rest of the team, we're always just trying to get the optimal outcome and from our perspective, each period talking about what we've done, the choices that we've made, because we're comfortable with those choices, but we have to be able to retain sufficient flexibility to be able to continue to deliver the best overall outcome.

Andrew Lyons: (Goldman Sachs, Analyst) Thank you.

Melanie Kirk: Great. Thank you, Andrew. We'll take the next question from Jon.

Jon Mott: (UBS, Analyst) Thanks, Mel. It's Jon Mott here from UBS. I've just got two questions, if I could.

The first one actually relates to the second quarter, and you did give us a very detailed first quarter trading update back in November where you said revenue was flat in particular at around just under $5.9 billion dollar level.

So, if you backsolve out the revenue in the second quarter, especially if you add back some of the aircraft leasing, which technically is like an impairment charge, you saw extremely strong revenue growth in the second quarter, somewhere around 5% to 6% depending on what exactly that flat number is, but very, very strong. That came through a stronger NIM, better fee income, better trading income.

Given that you've come out with your opening remarks that you've seen a marked turn in economic conditions, why shouldn't we be extrapolating the stronger December quarter out for - the outlook from here, providing you've got the assumption that the economic conditions continue to improve? Then I've got a second question, if I may.

Matt Comyn: Why don't I start and Alan, you add. You're right, Jon, insofar as second quarter was stronger, and a number of different drivers for that, many of which you've mentioned. Stronger volume growth across a number of businesses; home lending, as I said, December with a net balance growth of just over $3 billion, very strong month. Similarly, business was strong throughout the half but certainly in that second quarter.

As you said, fee income. CommSec delivered a very strong performance and as you would expect during the periods of ongoing volatility, again higher markets and trading income as well was significant, particularly in our commodities area, and that trading performance obviously very hard to replicate period on period. They would be the main drivers from my perspective.

Alan Docherty: Yes. The only thing I'd add to that, Jon, is there was some element of the aircraft impairment that we took in the first quarter of the financial year, so that wasn't all weighted towards the same quarter. We continually look at on a month-to-month basis how those discounted cash flow assumptions across that portfolio look and so we did take some provision, which would have held the first quarter revenue back a little bit relative to second quarter. Yes, other than that the momentum was strong in the same quarter.

Jon Mott: (UBS, Analyst) Thank you. Just a second question, if I could. On slide 36, and this one is probably not as update. This is one of the charts we've been talking about for many years, which is your MFI by age bracket. Providing that the colour scheme is right, and I presume it is, it looks like you're seeing a sharp decline in your MFI over the last 12 months, especially in that youth and up to the age of 35 bracket. You're back to where you were in December 2015.

I wanted to make sure is that correct, and what's happened over the last 12 months, especially given your investment in technology, all the positive talk you had through the presentation that your MFI market share in the youth generation X and generation Y has fallen back so dramatically over the last 12 months?

Matt Comyn: Thanks, Jon. As you might anticipate, we've looked pretty closely at the results, which are provided by an external provider. The best causal explanation I've got is a significant reduction driven by migrants. We do extremely well in migrants, and obviously there's been far fewer, so let's say we're probably about a 40% share. I'm not entirely convinced that there's enough of a reduction in flow to impact the stock but it's a survey-based result, so I don't have a better answer. Certainly, we can't see anything beyond that that would indicate any degradation.

If we look at the way we're - in terms of share around both deposits, everyday banking and the way people are banking with us, home lending share, strong growth right across all of the ways that our customers bank with us.

I think the reasonable next question would be well, on that basis we'd like to see some recovery in that, certainly as international borders are open, which unfortunately is probably still some time away. We'll certainly be looking for that. I don't have a better explanation, but there's certainly nothing else other than that that we can see.

Melanie Kirk: Great. Thank you, Jon. We'll take the next question from Brian.

Brian Johnson: (Jefferies, Analyst) Brian Johnson, Jefferies. First off, congratulations on a fantastic operational result. Two questions. The first one is that when we have a look at basis risk, which was three basis points better over the period, can this actually get better going forward, or should we be thinking that’s now a neutral?

Alan Docherty: Yes. It was a big benefit in the sequential half, three basis points, and there was a couple of things going on there. Obviously, we had the, if you like, the bottoming out of the bill OIS spread that was around minus two basis points averagely over the six-month period. The other dynamic that's going on in there is a volume dynamic. Effectively, because of that very strong growth in the at-call deposit portfolio, we've effectively got much less structural exposure to basis risk.

So, that reduction in the size of the balances that we're paying the bill rate on meant that there's a volume benefit embedded in that three basis points, so that was around half the benefit, rate was the other half of the benefit. I'd see that that sort of structural change, there's been a large move in it. I don't see a whole lot left in that move and obviously, at minus two basis points we'd see that from a rate perspective that's bottomed out. So yes, I'd say very much that's a temporary insulation in terms of the sequential move.

Brian Johnson: (Jefferies, Analyst) Alan, the 7 basis points down is before any adverse movement that comes through on basis risk?

Alan Docherty: Yes. That excludes basis risk, yes.

Brian Johnson: (Jefferies, Analyst) Okay. I've got a lot of questions but just the second one if I may. When we have a look at slide 71, the housing growth, we can actually see that from slide 76 we can see that the average drawdown for home lending is actually shrinking, but I think what is more concern is when we have look at slide 71, we can see new funding drawing down $65 billion but people repaying back $63 billion.

If I annualise the $63 billion, it's telling me your book is only now lasting about 3.8 years, which when you think about it is telling us the front book/back book accelerates. Could you just run through what's - those dynamics that are coming through? Why are you getting such paltry growth, what does it mean for the margin, and what does it mean for basically holding the dominant market share?

Alan Docherty: In terms of the weighted average life, actually we're seeing - that's actually held up very well in the context of lower rates and faster repayments, so we're seeing that flow to fixed-rate home loans, actually, leading to an overall lengthening, a marginal lengthening in this period of the overall home loan behavioural term. For many years we've talked about home loan behavioural terms of weighted average of six years.

Our expectation is that that's going to actually increase marginally over the next six to 12 months due to that greater share of flow into fixed-rate home lending. Partly in terms of the dollar rise in it, it's just a much larger stock of home loans that you're looking at that $63 billion run-off in the context of.

So, if you look at the $63 billion in the context of the larger stock, relative to the last six-month period, the run-off is only marginally higher than the rate that you would have seen six months ago, due to that strong fixed-rate flow.

Matt Comyn: Just to add to that, BJ. As you would expect, as rates have come down - there was a couple of rate cuts during that period - the book does amortise more quickly. As Alan said, one of the things that we've looked at - because as people have switched across the market to fixed-rate loans, you do get a NIM compression from that, but actually, the offset to that is actually the duration as we're looking out is improving.

We're certainly not seeing any change in and around the behavioural term. I think it's unlikely we'll see the repeat of what we've had in the last period, which is if you break down how the housing market has actually grown, there's definitely been more refinance splits going into fixed-rates, just as rates have come down and we've moved across the industry more people into fixed-rate loans. We probably would have peaked in the early 40% in terms of flow of fixed-rate, which would be more than double what we would have otherwise seen in prior periods, but I think that's starting to slow.

Then compositionally, strong growth in first-home buyer, owner occupier, investor still weak, and of course a couple of those segments are segments that we do well in. We've seen run-off, repayments; we've looked at that, they’ve grown, but actually fundings have grown more.

As Alan said, it's a very large book so it does run off and so there is absolutely an element of funding to be able to continue to grow. Our balance growth during that period and particularly in the second quarter was very strong.

Melanie Kirk: Great. Thank you, Brian. We'll take the next question from Richard.

Richard Wiles: Good morning, Matt. Good morning, Alan. I'd like to ask questions on a couple of topics. The first is the dividend. I think you've explained pretty well why the payout ratio is below the long-term target rate of 70% to 80%, but could you comment on whether you think your long held practice of having a 45/55 first half, second half skew is still appropriate?

Could you also talk about the pros and cons of using your surplus capital for a multiyear increase in the dividend rather than a multibillion dollar buyback? In other words, why couldn't you - with so much surplus capital, why couldn't you push your target payout ratio even higher for several years if you chose to use the capital that way rather than doing a buyback?

Then I've also got a question on business banking which I can come back to.

Matt Comyn: Sure. Why don't I start and Alan, you add. I mean look, on the dividend, overall our principle to the dividend insofar as target payout ratio between 70% to 80% remains. As you know, typically that's meant that we've paid in around that 75%. There's been a slight differential between the first and second half.

I mean broadly speaking, we're not intending on changing that. As you said, we're slightly below for the reasons that I think Alan well covered in terms of just some conservatism and being just cognisant of the risks that we face over the next period.

Then I guess on the capital side, I wouldn't like to - I'm not going to speculate on the differential between those. As you've seen in terms of the way we think about capital and certainly share count is an element that we think has been an important contributor, to DPS growth over a sustained period of time but there's a range of different capital options. That's clearly a discussion with the Board and we'll go through a variety of different choices at the appropriate time and therefore make the announcement on that basis.

Richard Wiles: Okay, thanks Matt. Then on slide 12, you talk about the - one of your strategic priorities being to build Australia's leading business bank. How are you going to measure that success? What does leading business bank mean? Is it net promoter score? Is it size of the business bank? Is it profit at a business bank? How will you measure that objective?

Matt Comyn: Yes look, I mean there's a range of different factors and trying to make the link in terms of where I think it's important economically for a pick up in business investment. I think financial institutions clearly have an important role to play there. We have a strong customer franchise in business banking.

We've got I think the strongest share of business deposits in areas like merchants and in payments. Typically we've lagged in lending. We're not going to measure success based on a volume metric as you'd expect. Obviously volume, pricing, credit quality - all important through the cycle.

You know in terms of in this period, we saw as I said diversified growth across a range of different sectors. We've added business bankers. We've broadened our sector and geography segmentation. We've improved the service offering, particularly some of the digitisation and speed decisioning.

Ultimately, we'd be looking very much at a balanced set of metrics that's an aspiration for us over the medium term and we're pleased with the performance that we've had in the six months but it's just that, it's one period. We're very much going to measure our success or otherwise over multiple years across a number of the measures that I just mentioned.

Melanie Kirk: Great, thank you Richard. We'll now take the next question from Andrew Triggs.

Andrew Triggs: (JP Morgan, Analyst) Thanks Mel. Question relates firstly to - I've got two questions. The first one relates to investment spend, that the half of annualising at $1.7 billion for the year. Is this the new level we should expect for the near term, noting that much of the pickup came from productivity and growth?

The second question relates to credit risk migration. So you actually saw tailwind to capital in the half from positive credit risk migration. Can you perhaps update us on the thinking? I think previously you've said that the central peak estimate in the base case was a 70 basis point impact which clearly things are turning out much more favourable than that.

Alan Docherty: Yes, thanks Andrew. Yes so on the investment spend, yes I mean we took a decision this year to rebase upwards that overall level of investment spend. I mean you've seen a slight decline in the proportion of risk and compliance spend in terms of the overall envelope although the dollar amount of that spend is still relatively consistent on the same period last year and given the amount of work that we wanted to do around continue to invest in the franchise and a technology agenda and digitising the Bank, we rebased the spend upwards.

That's the annualised run rate of around 1.7 and I think that's, you know, a rebased level of investment spend commensurate with the changed program that we've got across productivity, growth and obviously continue to invest from a risk and compliance perspective.

On the provisioning assumptions and credit risk weighted asset migration, we've obviously been very pleased with the improvements and the risk weighted asset intensity of the portfolio over the period. One of the side effects of the very strong support that we've seen is growth and mortgage offset accounts. People have got further ahead averagely in the repayments. That along with there's other improvements in the broader economy have helped reduce the risk weighted asset intensity relative to the level that we've seen back in June.

So we revised our assumption in terms of what happens to credit risk weighted assets through a central scenario, another central scenario now we wouldn't expect to see any material negative migration and credit risk weighted assets.

We're retained a pretty cautious downside scenario and so you can see in the disclosures, we've continued to assume a negative credit risk weighted asset migration in the assumption that you see, you know, a pretty punitive downside scenario but under a central scenario we wouldn't expect to see any material deterioration in credit quality from here.

Melanie Kirk: Great, thank you Andrew. We'll take the next question from Jarrod.

Jarrod Martin: (Credit Suisse, Analyst) Jarrod Martin from Credit Suisse. Just a follow up on capital and just particularly around the dot points on slide 30 about when your decision-making and that's greater certainty regarding domestic economic performance and the ongoing assessment of the portfolio credit quality.

Could you give it a bit more detail around what you're looking for there? Assuming that you know, you're wanting to see the policy support measures come off such as JobKeeper and how that flows through to the economy. What - and what sort of timeframe do you need to see those things come off before you feel that you have enough certainty to make that decision? Is it one month, three months, six months, 12 months?

Matt Comyn: Yes no, thanks Jarrod. Look, I mean it's a little hard to be specific on the timeframe because realistically there's a number of variables which still need to play out. Certainly as you said, that's one of the keys from our perspective, is we think there's a lot of resilience in households with that surplus savings but clearly some of the income measures are going to be tapering over the next few months. How effective will some of the other stimulus measures in terms of creating continued recovery in the labour market and investment?

So we certainly want to see that play through into the midyear at least. I guess one part of that would be how the economy continues to perform during that period and so I mean as we look domestically, even the continued management of the pandemic, a critical enabler of that, any interruptions in terms of a vaccine or broader impacts from any constraints placed on the economy.

So I think from our perspective we can safely say that we'll be looking into that April-June quarter, but between now and then there's also a number of other things that we'll be looking for and we may change that view.

Alan Docherty: Just to add to that, the - we're obviously also looking at very particular sectors of the economy and particular exposures that we have in our portfolio that are going to be under - you know, they're under significant stress. So aviation we've called out specifically and a number of other vulnerable subsectors.

So again, part of the - one of the moving parts I guess in terms of how we think about our level of provisioning credit quality in the outlook is how those sectors perform and what the outlook is for those sectors and you know, each quarter that passes, we'll obviously have more information around how they're likely to fare over the period ahead so that, you know, as well as the macro factors, we'll obviously be looking at those particular sectors that we've called out.

Melanie Kirk: Great. Thank you, Jarrod. We'll take the next question from Victor.

Victor German: (Macquarie, Analyst) Thank you, Mel. It's Victor German from Macquarie. I had two questions as well, one on expenses and one on margins. So the first question, following up from what's been discussed before on expenses, Matt when you originally outlined your strategy around expenses, you had that chart which I think at the time you kind of indicated that you're probably going to regret putting in, but that chart indicated that you were hoping, excluding divestments, to achieve a reduction in the cost base and at that point it would have implied a cost base of less than $10 billion.

With currently annualising around $11 billion, I'm just interested in sort of your thoughts. We appreciate the fact that you're obviously seeing great opportunities to continue investing in business, but do you think sort of vis-à-vis where we were sort of two years ago, that uplift in cost base is enough to absorb those opportunities or do you still feel that you need to see that cost base to continue to go up to capture all those opportunities that you want to do in the next two to three years?

Matt Comyn: Yes no thanks, Victor and look, I don't recall expressing regret at the time. I do recall you trying to work out what our core and non-core cost base. Look as you said, if we looked at including divestments, our cost base has gone down but that's a very low bar.

As we look at sort of our continuing operations of expenses, all of the expense growth over that period has been driven by risk regulation and compliance spend. We think that that's been necessary investments. Obviously in the management of non-financial risk it's been critical around the remedial action plan responding, you know we've added significant FTE to our management of financial crimes compliance. So probably in the order just in that area alone of about 2000 people over that time.

Then if I look at the rest of the expense base, we're flat on a nominal basis, which means we've absorbed both inflation and volume related costs. So yes, our commitment and our approach remains unchanged. You know certainly, we accept the higher, an elevated risk and compliance over that period and as I said earlier, in each subsequent period, we start with an intent to reduce our cost base but have some flexibility where we can see that there's opportunities to increase costs if it's in the best interests of creating value for our shareholders.

Melanie Kirk: Great. Thank you, Victor. We'll take the last question from Brendan.

Brendan Sproules: (Citi, Analyst) Good morning. Brendan Sproules from Citi. I've just got a couple of questions on Group margin on slide 23. You've shown some asset price discounting evident in the half. I was wondering if you could talk to what is the competitive environment at the moment and do you expect that discounting to increase over the next six months given some of the pretty sharp deals that are available in the market?

Then secondly on the deposit side, obviously transaction saving and investment were all drags in this particular period but we've obviously seen TD and high interest savings account rates come down in the market. So I was wondering if you can talk about what we can expect in the next half on those?

Matt Comyn: Well why don't I talk broadly about the housing market and then Alan, if you want to add something either to that or on deposits. I mean as you'd expect, the housing market remains very competitive which is obviously great news for customers. So I do think that we're going to continue to see a lot of price based competition.

Margins are still quite good so as I said, we would expect that to continue. You do see some pressure from switching from variable to fixed rates, so there's a compression effect there. So I think it's hard to imagine that that really abates anytime soon.

Alan Docherty: Yes and on the deposits side, we've seen obviously the sort of lower rate environment feed through and to those deposit margins. We've done some repricing in the period, although swap rates have been falling as well, so net - net term deposits have still been a little bit of a drag of one basis point as you can see on that slide.

Then looking ahead, there's potentially some offset to the headwind that we can see through broader liability repricing, albeit within that guidance that we provide around the seven basis point headwind year-on-year. You've obviously got the forward effect in each subsequent period of that continued run-off of the reduced tractor rate on the replicating portfolio on the non-rate sensitive deposits and also the continued roll-off of the equity hedge.

So those headwinds remain and to your point, I mean we'll look at other actions we can do to try and offset some of that headwind, although those headwinds are structural.

Melanie Kirk: Great. Thank you, Brendan. That brings our briefing to a conclusion. If you have any follow up, please come back to CBA Investor Relations and thank you for joining us for the briefing.