



ASX/Media Release

MACQUARIE GROUP ANNOUNCES \$A1,248 MILLION HALF-YEAR PROFIT

Key points

- 1H18 net profit of \$A1,248 million, up 19% on 1H17 and up 7% on 2H17
- 1H18 net operating income of \$A5,397 million, up 3% on 1H17 and up 5% on 2H17
- Annuity-style businesses' combined net profit contribution¹ up 28% on 1H17 and up 30% on 2H17
- Capital markets facing businesses' combined net profit contribution down 18% on 1H17 and down 25% on 2H17
- International income 62% of total income² in 1H18
- 1H18 operating expenses of \$A3,693 million, down 1% on 1H17 and up 5% on 2H17
- Assets under management of \$A473.6 billion at Sep 17, down 2% from Mar 17
- Financial position comfortably exceeds regulatory requirements³
 - Group capital surplus of \$A4.2 billion
 - Bank CET1 ratio 11.0% (Harmonised: 13.3%); Leverage ratio 6.1% (Harmonised: 6.9%); LCR 153%; NSFR 109%
- 1H18 earnings per share (EPS) \$A3.70, up 19% on 1H17 and up 7% on 2H17
- Annualised return on equity (ROE) 16.7%, up from 14.6% in 1H17 and up from 15.8% in 2H17
- Interim ordinary dividend of \$A2.05 per share (45% franked), up on 1H17 interim ordinary dividend of \$A1.90 (45% franked) and down on 2H17 final ordinary dividend of \$A2.80 (45% franked)
- To provide additional flexibility to manage the Group's capital position going forward, the Board has approved an on-market buyback of up to \$A1 billion, subject to a number of factors including the Group's surplus capital position, market conditions and opportunities to deploy capital by the businesses

SYDNEY, 27 October 2017 – Macquarie Group (ASX: MQG; ADR: MQBKY) today announced a net profit after tax attributable to ordinary shareholders of \$A1,248 million for the half-year ended 30 September 2017 (1H18), up 19 per cent on the half-year ended 30 September 2016 (1H17) and up seven per cent on the half-year ended 31 March 2017 (2H17).

Macquarie Group Managing Director and Chief Executive Officer (CEO) Nicholas Moore said: "1H18 highlighted the strength of Macquarie's global platform, the diversity of its business mix and its ongoing ability to adapt to changing conditions.

¹ Where referenced in this document, net profit contribution is management accounting profit before unallocated corporate costs, profit share and income tax.

² Where referenced in this document, total income is net operating income excluding earnings on capital and other corporate items.

³ Where referenced in this document, Group capital is calculated at 8.5 per cent Risk Weighted Assets (RWA) including capital conservation buffer (CCB), per APRA ADI Prudential Standard 110. The APRA Basel III Group capital surplus is \$A5.6 billion calculated at 7.0 per cent RWA, per the internal minimum Tier 1 ratio of the Bank Group. 'Harmonised' Basel III estimates are calculated in accordance with the BCBS Basel III framework. CET1 refers to the Common Equity Tier 1 ratio. LCR refers to the Liquidity Coverage Ratio. Where referenced in this document, average LCR for the September 2017 quarter is based on an average of daily observations. NSFR refers to the Net Stable Funding Ratio. APRA released final NSFR requirements at the end of 2016. The NSFR and associated changes to APRA ADI Prudential Standard 210 will be effective from 1 January 18.

“Macquarie’s annuity-style businesses (Macquarie Asset Management (MAM), Corporate and Asset Finance (CAF) and Banking and Financial Services (BFS)), which represented approximately 80 per cent of the Group’s 1H18 performance⁴, generated a combined net profit contribution of \$A2,094 million, up 28 per cent on 1H17 and up 30 per cent on 2H17.”

“Macquarie’s capital markets facing businesses (Commodities and Global Markets (CGM) and Macquarie Capital) delivered a combined net profit contribution of \$A568 million, down 18 per cent on 1H17 and down 25 per cent on 2H17.”

Net operating income of \$A5,397 million in 1H18 was up three per cent on 1H17 and up five per cent on 2H17, while operating expenses of \$A3,693 million were down one per cent on 1H17 and up five per cent on 2H17.

Mr Moore noted: “During the half-year we continued to build on the strength of our Australian franchise, while international income accounted for 62 per cent of the Group’s total income.”

Macquarie’s assets under management (AUM) at 30 September 2017 was \$A473.6 billion, down two per cent from \$A481.7 billion at 31 March 2017, largely due to net asset realisations in Macquarie Infrastructure and Real Assets (MIRA)⁵ and unfavourable currency movements in Macquarie Investment Management (MIM), partially offset by positive market movements.

Mr Moore said: “The Group remains well positioned, with a strong and diverse global platform and deep expertise across a range of products and asset classes. This is built on the foundation of a strong balance sheet, surplus capital, a robust liquidity and funding position and a conservative approach to risk management which is embedded across all operating groups.”

Macquarie also announced today a 1H18 interim ordinary dividend of \$A2.05 per share (45 per cent franked), up on the 1H17 interim ordinary dividend of \$A1.90 per share (45 per cent franked) and down from the 2H17 final ordinary dividend of \$A2.80 per share (45 per cent franked). This represents a payout ratio of 56 per cent. The record date for the final ordinary dividend is 8 November 2017 and the payment date is 13 December 2017.

Board and management changes

Macquarie advised today that Glenn Stevens will be appointed to the Macquarie Group Limited and Macquarie Bank Limited Boards as an independent director, effective 1 November 2017. Mr Stevens worked at the highest levels of the Reserve Bank of Australia for 20 years, most recently as Governor between 2006 and 2016. He led policy decisions through the global financial crisis, Australia’s mining boom, and an extended period of low interest rates and developed Australia’s successful inflation targeting framework for monetary policy.

After 25 years of service, Stephen Allen, Macquarie’s Chief Risk Officer and Head of Risk Management Group (RMG), has announced his intention to retire and will step down from Macquarie’s Executive Committee on 31 December 2017.

Mr Moore said: “I would like to thank Steve for his enormous contribution to Macquarie over many years and wish him all the very best for his retirement. In addition to a successful career establishing and growing some of our operating businesses, Steve has built a powerful legacy, overseeing Macquarie’s risk management activities at a time of significant change in the financial services industry and rapid expansion in regulation.”

Effective 1 January 2018, Macquarie’s Chief Financial Officer and Head of Financial Management Group (FMG), Patrick Upfold, will succeed Mr Allen as Chief Risk Officer and Head of RMG.

Effective the same date, Alex Harvey, Global Head of Principal Transactions in Macquarie Capital, will succeed Mr Upfold as Chief Financial Officer and Head of FMG and will join the Executive Committee. Mr Harvey joined Macquarie in 1999.

⁴ Where referenced in this document, Group’s performance is based on 1H18 net profit contribution from operating groups.

⁵ Includes divestment of Thames Water by MIRA-managed funds and ceasing asset services to consortia investors (\$A25 billion).

Outlook

Macquarie currently expects the combined net profit contribution from operating groups for the year ending 31 March 2018 (FY18) to be slightly up on the year ended 31 March 2017 (FY17).

The FY18 tax rate is currently expected to be broadly in line with 1H18.

Given substantial performance fees were recognised in 1H18, Macquarie expects the 2H18 result to be down on 1H18 and broadly in line with 2H17.

Accordingly, the Group's result for FY18 is currently expected to be slightly up on FY17.

The Group's short-term outlook remains subject to:

- market conditions
- the impact of foreign exchange
- potential regulatory changes and tax uncertainties.

Mr Moore said: "Macquarie remains well positioned to deliver superior performance in the medium-term due to our deep expertise in major markets, strength in diversity and ability to adapt the portfolio mix to changing market conditions, the ongoing benefits of continued cost initiatives, a strong and conservative balance sheet and a proven risk management framework and culture."

Half-year result overview

Net operating income of \$A5,397 million for 1H18 was up three per cent on 1H17, while total operating expenses of \$A3,693 million were down one per cent on 1H17.

Key drivers of the change from 1H17 were:

- A one per cent increase in combined net interest and trading income to \$A1,892 million, up from \$A1,874 million in 1H17. The movement was mainly due to volume growth in the loan and deposit portfolios and improved margins in BFS, and a reduced cost of holding long-term liquidity in Corporate. This was partially offset by reduced interest income from Macquarie Capital's debt investment portfolio and higher funding costs associated with an increase in principal investments, including the acquisition of Green Investment Group (GIG), as well as lower trading income in CGM as a result of lower market volatility.
- A 17 per cent increase in fee and commission income to \$A2,568 million, up from \$A2,203 million in 1H17, due to increased performance fee income in MAM and higher fee income from the US debt capital markets business in Macquarie Capital due to increased client activity. This was partially offset by reduced Life Insurance income in BFS after Macquarie Life's risk insurance business was sold to Zurich Australia Limited in September 2016; lower mergers and acquisitions fee income in the US and Asia in Macquarie Capital; and reduced CGM brokerage and commissions income, mainly in equities due to continued low volatility across global equity markets and reduced brokerage commission rates due to the trend towards lower margin platforms.
- A one per cent decrease in net operating lease income to \$A469 million, down from \$A476 million in 1H17, due to improved underlying income in CAF from the Aviation, Energy and Technology portfolios offset by foreign exchange movements.
- Share of net profits of associates and joint ventures accounted for using the equity method of \$A103 million in 1H18 increased from a loss of \$A8 million in 1H17, primarily due to the improved underlying performance of investments held in Macquarie Capital.
- Other operating income and charges of \$A365 million in 1H18, down from \$A673 million in 1H17. The primary drivers were lower principal gains in Macquarie Capital and CGM and the non-recurrence of the gain on sale of Macquarie Life's risk insurance business to Zurich Australia Limited in 1H17 by BFS, partially offset by lower charges for provisions and impairments across most operating groups.

- Total operating expenses of \$A3,693 million in 1H18 decreased one per cent from \$A3,733 million in 1H17, mainly due to reduced project activity in BFS, reduced employment expenses from lower average headcount, partially offset by transaction, integration and ongoing costs associated with the acquisition of GIG in Macquarie Capital.

Staff numbers were 13,966 at 30 September 2017, up from 13,597 at 31 March 2017.

The income tax expense for 1H18 was \$A448 million, a two per cent increase from \$A438 million in 1H17. The increase was mainly due to higher profit before tax. The effective tax rate of 26.4 per cent was down from 29.4 per cent in 1H17 and broadly in line with the 2H17 rate of 26.9 per cent, reflecting the geographic mix and nature of earnings.

Strong funding and balance sheet position

Chief Financial Officer (CFO) Patrick Upfold said “Macquarie remains well funded with a solid and conservative balance sheet and we continue to pursue our strategy of diversifying funding sources by continuing to grow the deposit base and accessing a variety of funding markets.”

Total customer deposits⁶ increased three per cent to \$A49.4 billion at 30 September 2017 from \$A47.8 billion at 31 March 2017. During 1H18, \$A8.2 billion of new term funding⁷ was raised covering a range of tenors, currencies and product types.

Capital management

Macquarie’s financial position comfortably exceeds APRA’s Basel III regulatory requirements, with Group capital surplus of \$A4.2 billion at 30 September 2017. This surplus was down from \$A5.5 billion at 31 March 2017, following payment of the FY17 final dividend and FY17 Macquarie Group Employee Retained Equity Plan buying requirement, the ECS⁸ buyback and business growth, partially offset by 1H18 profit and movement in reserves. The Bank Group APRA Basel III Common Equity Tier 1 capital ratio was 11.0 per cent (Harmonised: 13.3 per cent) at 30 September 2017, down from 11.1 per cent (Harmonised: 13.3 per cent) at 31 March 2017. The Bank Group’s APRA leverage ratio was 6.1 per cent (Harmonised: 6.9 per cent), LCR was 153 per cent and NSFR was 109 per cent at 30 September 2017.

Regulatory update⁹

The Basel Committee has delayed the finalisation of proposals to amend the calculation of certain risk weighted assets under Basel III. Any impact on capital will depend upon the final form of the proposals and local implementation by APRA.

APRA has delayed until at least 1 January 2019 the implementation of a new standardised approach for measuring counterparty credit risk exposures on derivatives (SA-CCR) and capital requirements for bank exposures to central counterparties. APRA has also announced that it does not expect to finalise a new market risk standard¹⁰ until at least 2020, with implementation from 2021 at the earliest.

APRA provided guidance around CET1 capital ratios for Australian banks to be considered ‘unquestionably strong’ and intends to release further details on how the new requirements will be implemented later this year. APRA has indicated¹¹ that the implementation of the proposal will incorporate changes to the prudential framework resulting from the finalisation of Basel III. Based on existing guidance, Macquarie’s surplus capital position remains sufficient to accommodate any additional requirements.

⁶ Total customer deposits as per the funded balance sheet (\$A49.4 billion) differs from total deposits per the statutory balance sheet (\$A59.0 billion). The funded balance sheet excludes any deposits which do not represent a funding source for Macquarie.

⁷ Issuances cover a range of tenors, currencies and product types and are AUD equivalent based on FX rates at the time of issuance and include undrawn facilities.

⁸ Exchangeable Capital Securities.

⁹ The Basel Capital Framework applies to the Bank Group only.

¹⁰ Also known as the Fundamental Review of the Trading Book.

¹¹ APRA’s information paper published July 2017: ‘Strengthening banking system resilience – establishing unquestionably strong capital ratios’.

Share buyback

To provide additional flexibility to manage the Group's capital position going forward, the Board has approved an on-market buyback of up to \$A1 billion, subject to a number of factors including the Group's surplus capital position, market conditions and opportunities to deploy capital by the businesses. This buyback has received the necessary regulatory approvals.

Operating group performance

- Macquarie Asset Management** delivered a net profit contribution of \$A1,189 million for 1H18, up 39 per cent from \$A857 million in 1H17. Performance fee income of \$A537 million, from Macquarie European Infrastructure Fund 3 (MEIF3), Macquarie Atlas Roads (MQA) and other MIRA-managed funds and co-investors, was up from \$A170 million in 1H17. Base fees of \$A795 million were broadly in line with 1H17 as investments made by MIRA-managed funds, growth in the MSIS Infrastructure Debt business and positive market movements in MIM AUM were partially offset by asset realisations by MIRA-managed funds, net flow impacts in the MIM business and foreign exchange impacts. Investment-related income was broadly in line with 1H17 and included gains from sale and reclassification of certain infrastructure investments. Assets under management of \$A471.9 billion decreased two per cent on 31 March 2017.
- Corporate and Asset Finance** delivered a net profit contribution of \$A619 million for 1H18, up 19 per cent from \$A521 million in 1H17. The increase was mainly driven by increased income from prepayments, realisations and investment-related income in the Principal Finance portfolio and lower provisions for impairment, partially offset by lower interest income as a result of the reduction in the Principal Finance portfolio. The Asset Finance portfolio continued to perform well. CAF's asset and loan portfolio of \$A35.5 billion decreased three per cent on 31 March 2017.
- Banking and Financial Services** delivered a net profit contribution of \$A286 million for 1H18, up 10 per cent from \$A261 million in 1H17. The improved result reflects increased income from volume growth in the loan and deposit portfolios and improved margins. 1H17 included the gain on sale of Macquarie Life's risk insurance business net of expenses including impairment charges predominately on equity investments and intangible assets, and a change in approach to the capitalisation of software expenses in relation to the Core Banking platform. BFS deposits¹² of \$A46.4 billion increased four per cent on 31 March 2017 and funds on platform¹³ of \$A78.9 billion increased nine per cent on 31 March 2017. The Australian mortgage portfolio of \$A29.9 billion increased four per cent on 31 March 2017, representing approximately two per cent of the Australian mortgage market.
- Commodities and Global Markets** delivered a net profit contribution of \$A378 million for 1H18, down 23 per cent from \$A490 million in 1H17. The result primarily reflects reduced income from the sale of investments, mainly in energy and related sectors, and lower volatility across the commodities platform resulting in reduced client activity and trading opportunities. This was partially offset by strong client flows and revenues from interest rates and foreign exchange, improved results across the equities platform, and lower operating expenses reflecting reduced commodity-related trading activity, reduced average headcount and associated activity, and realisation of benefits from cost synergies following the merger of Commodities and Financial Markets and Macquarie Securities Group. Macquarie Energy improved its Platts ranking to become the No. 2 US physical gas marketer in North America¹⁴.
- Macquarie Capital** delivered a net profit contribution of \$A190 million for 1H18, down seven per cent from \$A205 million in 1H17. The result reflects reduced investment-related income and lower M&A fee income in the US and Asia, partially offset by higher fee income from debt capital markets in the US and lower provisions and impairment charges. During 1H18, Macquarie Capital advised on 152 transactions valued at \$A73 billion including being defence adviser to DUET Group in response to the \$A13.4 billion acquisition by Cheung Kong Infrastructure; acquisition of 100 per cent ownership interest in RES Japan, a Japanese subsidiary of Renewable Energy Systems Group, rebranded as Acacia Renewables and

¹² BFS deposits exclude corporate/wholesale deposits.

¹³ Funds on platform includes Macquarie Wrap and Vision.

¹⁴ Platts Q2 CY17.

focused on developing a pipeline of onshore wind energy projects; and financial advisor and equity investor in the restructuring and acquisition of the 907MW Norte III combined cycle gas plant in Juarez, Mexico. During 1H18, Macquarie completed the acquisition of the UK Green Investment Bank plc from HM Government for £2.3 billion. The Green Investment Bank, rebranded as Green Investment Group, is one of Europe's largest teams of green energy investment specialists, with expertise in project finance and development, construction, investment and asset management of green energy infrastructure.

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