Bendigo and Adelaide Bank Limited

2016 Annual General Meeting, 25 October 2016

MD's address

Good morning everyone.

As Robert has already outlined, the financial results for the company over the last twelve months were solid and, in the context of the operating environment, a testament to the hard work of our staff.

Low interest rates and slowing credit growth, coupled with new prudential regulation, mean that the market is very competitive at the moment. Compounding all that is a political environment where the banking industry finds itself at the centre of a campaign to pursue a Royal Commission.

As a bank, we have a privileged status in the community. We believe that it's important for the community to trust banks and feel confident that they will act fairly and transparently. Our Bank believes that our actions define who we are. It's in how we practise banking, in the culture we encourage for our people, and in our conduct with customers, that we are put to the test. We take our obligation to run the business for the benefit of all stakeholders seriously, understanding that the needs of our customer base, including both mortgage and deposit holders, are relevant and should be considered when we price our products.

We continue to focus on being Australia's most customer connected bank. That drives our desire to excel in customer service and help our customers achieve their financial goals. That focus, together with the implementation of our business strategies and diligent cost and margin management, underpinned these good financial results.

And those results have been achieved in a market where our key competitors have been given a number of free kicks in recent years that have enabled them to build their market dominance. The pricing of the Government Guarantee through the GFC and the implementation of the Basel II regulation saw them increase their market advantage at the expense of smaller players. There is no doubt customer choice has suffered.

However, with our capital, funding and credit positions being particular strengths for our Bank we are seeking to change that. With our Net Stable Funding Ratio at 115 percent we have already surpassed the new prudential requirement a year before it comes into place. This is testament to our retail brand and distribution network, with about 82 percent of funding provided by retail customers.

We are managing our business today as an advanced bank from a Basel II perspective. The investment of more than $80m we've made to move to advanced accreditation has increased our risk management capability, and this has become an important strategic asset for our Bank.

Additionally, we are pleased to see the positive outcomes of APRA initiatives that address the industry's uneven playing field; changes to risk weights on mortgages and a reduction in the capital advantage major banks have enjoyed. These outcomes will all serve to highlight the value proposition we offer customers and emphasise the benefit of choice in banking service providers.

We realise there is some community angst with regard to banks. There can be no hiding the fact that there have been some examples of poor behaviour in the industry. These examples have been acknowledged by those organisations who have undertaken them. But, it is apparent from the recent parliamentary hearings that there is no systemic issue across the industry. That is an important point to note.

In the recent past there have been 14 parliamentary inquiries into banks, the Murray inquiry into Australia's Financial System, three class actions against banks which were roundly unsuccessful and no finding of systemic wrong doing across the industry. Even so, a whole host of new regulation has been implemented to further ensure banks operate with the best interests of consumers in mind.

Given all that, it is very hard to see what substantive, tangible matters a Royal Commission would actually investigate. In my view, it would be a significant waste of taxpayer and shareholder money. We agree that there are some issues within the industry that should be addressed, but the most effective solution is the one in place; that banks and regulators will work even more closely to deal with the concerns that have been raised, while independently appointed parties will make sure banks are delivering. It's this action that will provide the best outcome for all Australians.

Let me be clear, I am not an apologist for the major banks. In fact, when one compares our performance with the majors across many of the indicators of good corporate citizenship, most people would conclude we are fighting well above our weight and perhaps we should be doing a lot more to call that out. Our brand advocacy, customer satisfaction, trust and community contribution are all market leading. Those attributes underpin our right to operate under the social licence that banks must earn. But, by and large, I believe all banks have the right intent.

So why is the industry under so much scrutiny? Much of this arises when banks don't pass on changes in the official cash rate to mortgage holders. But this is not a one-sided argument. Banks simply intermediate between depositors and borrowers and earn a margin for doing so. The rates bank set must be attractive enough for depositors to provide the funds that are then lent to borrowers. Without those funds there can be no borrowing, so when setting rates banks have to consider lots of stakeholders. We try to do this as equitably as we can.

Hopefully, Australians understand there is no direct link between changes in the cash rate and what happens to rates on loans and deposits despite some recent, opportunistic commentary to the contrary. It is a complex issue but even a simplistic understanding of why banks price as they do will go some way to easing the angst.

So let me try to assist. There is an expectation in the community that banks should pass on, in full, any rate cut that the Reserve Bank of Australia (RBA) makes to the official cash rate. As interest rates move lower this is not a realistic expectation for a number of reasons.

Firstly, banks do not fund all their loans at the official cash rate. The cash rate is the rate which banks pay to borrow funds from other banks in the money market on an overnight basis. It is the RBA's operational target for the implementation of monetary policy.

When the RBA Board decides that a change in monetary policy should occur, it specifies a new target for the cash rate. A decision to ease monetary policy is reflected in a new lower target for the cash rate, while a decision to tighten monetary policy is reflected in a higher target. It is simply an indication of where rates should head.

The fact is that banks fund their loans from lots of different sources at lots of different rates; business and consumer transaction accounts, term deposits, issuing short and long term paper in wholesale markets and through securitisation. Given interest rates are at record low levels, some of these funding sources are already at rates so low they can't be repriced further downward. This impacts the rates banks set on loans they provide for mortgages and businesses.

Which brings us to a second reason. Banks have a central role to play in market economies. They take deposits, generally for short terms, and use them to provide loans at much longer terms. This maturity transformation requires banks to manage liquidity and interest rate risk.

Banks also take the credit risk on the loans they make ensuring depositors always get their money back whether or not the loans are repaid. Of course they also facilitate payments domestically and overseas, provide credit and debit cards, ATMs, and meet many other customer needs.

To take that risk and provide the facilities they do, banks earn a margin by charging borrowers more than they pay depositors. That margin covers the cost of running the bank and provides a return to the shareholders who provide the capital. If banks don't do that profitably then there are no other institutions who will take on the credit, liquidity, interest rate and operational risk that allows depositors to earn an income securely and borrowers to buy houses and run businesses. People simply won't be able to borrow as banks won't attract the capital required to manage the risk of doing so or the deposits to allow them to lend.

Yes, banks make profits, but a strong banking industry is fundamental to the strength of a country's economy. Unprofitable banks in Greece, much of Europe and the UK have seen those economies struggle.

I hope that explanation helps.

In finishing I would like to talk a bit more about our bank.

Our organisation has a commitment to making it easier for our customers to do business with us. Our investments and activities align with our strategic aims, and we focus on taking advantage of the opportunities that are ahead of us. I believe we are doing these things better each day.

As a result, our Bank is very proud of our strong and valued brand, our commitment to great customer service and our role in the communities in which we operate. Our actions in delivering on this promise are real and there for all to see.

Most importantly, I would like to thank our people for their efforts in striving to achieve our vision of being Australia's most customer connected bank. Their efforts to deliver the amount of change that we have undertaken over the last few years, while continuing to deliver for our customers, is nothing short of amazing and is under rewarded to some extent because of the tight environment.

I would also like to thank our partners for assisting us in achieving our goals; our customers for their support and advocacy; and our shareholders for providing us with the capital to make it happen.

Thank you for your time today.