Bayside Business Network

Breakfast Function

7am, Tuesday, 1 September

I'm delighted to be here today talking about transformation. It's very timely, I must say, given it is the first day of Spring – and in addition to the usual changes Spring brings, we are also seeing real 'green shoots', to labour an already over-used phrase, in terms of optimism in business and in the Australian economy in general.

Recently RBA Governor Glenn Stevens indicated that Australia will not reach the 8.5% peak in unemployment forecast back in the May budget, nor the 0.5% contraction in economic growth in 2009 / 2010.

And Mr Stevens said that he didn't think that the rise in unemployment being smaller than expected is just because we're sharing the work around; but rather that the weakening in economic activity has not been as great as thought at one point.

In fact, most commentators are so convinced the economy is improving that that they are convinced the RBA will lift rates at their meeting today. But I wouldn't bet my house on it. Just last week, Reserve Bank board member Roger Corbett said that interest-rate increases will be determined by the strength of consumer spending and economic growth as government stimulus measures are withdrawn.

Regardless, if it's not today, there's no doubt it will happen soon, which is a sure sign the economy is in recovery, though perhaps won't be seen as wonderful news by all the mortgage holders among us.

Treasury Secretary Ken Henry also has some good news for us, saying in Canberra last month that the Australian economy may attract an even greater share of global capital flows as the world economy recovers.

So it turns out that not only has the Australian economy been more resilient than many economists had expected at this point, but that our recovery might be even quicker than anticipated.

This is all great news. Not only have we survived the economic downturn thus far, but the return to prosperity, or at least to a more confident and buoyant marketplace is closer than originally thought.

Does this mean that there won't be after-shocks? Of course not. But surely if we have survived the worst of the downturn, and not just by fluke, but by looking at the environment and reacting accordingly, then surely we can survive what's to come.

But I'm sure you already know that. The fact that you're all here today, still operating a small business in an unfriendly environment, means you probably took stock of the economic downturn and you did what you had to do to get through it.

And I guess that's what we're here to talk about today. About looking at your business, assessing the environment in which you're operating, and making decisions about the future of your business. And it's this constant review and assessment that I think is vital, and is in part what I'm here to talk about today.

In my experience, a lot of companies do not under-perform, or even fail, because of poor business decisions or because management acted in rash or foolish ways; it's their *failure* to act that is their downfall.

While I have always believed that persistence is absolutely fundamental to business success, I also believe that successful businesspeople are able to identify when change is required. These may seem mutually exclusive traits, but I assure you they are not.

And being able to determine when to persist and when you need to change your approach is even more important given the difficult times in which we have been operating for the past year or so.

Ray Kroc, the founder of McDonalds, said it well: “Nothing in the world can take the place of persistence. Talent will not – nothing is more common than unsuccessful men with talent. Genius will not – unrewarded genius is almost a proverb. Education will not – the world is full of educated derelicts. Persistence and determination alone are omnipotent.”

That is a great quote, and sums up the importance of persistence beautifully.

Like you, I have read many, many business and success books. You know the ones – “How to take over the world in 40 days with a calculator” and “How to become a millionaire by writing a book on how to become a millionaire”, and even “40 habits of successful people, by a previously unsuccessful person.”

There are a million of them.

One which you might not have read, but which is worth having a look at, is “Don’t die with the music in you” by outgoing Broncos coach Wayne Bennett.

Apart from the fact that I love a good quote, and so does Wayne, it is full of the sort of practical advice on life and business which you would only expect from rugby league’s most successful living coach, whose departure from the Brisbane Broncos brought a tear to many a Queenslander’s eye.

At this point I would love to make a crack about how his success has dwindled since he left our great state for those NSW based Dragons, but given the Dragons are top of the ladder and trounced the Broncos in their face-off at Suncorp Stadium earlier this year, I don't really think I'd have a leg to stand on.

Mind you, if I'm being honest I think it's a mugs game as I am a passionate AFL fan who is lucky enough to be involved closely with the Lions as a board member. I'm sure many of you here today are also more interested in what's happening with the top 8, and of course with the Grand Final.

The AFL fans here today would be loving the fact that the four top teams are all Victorian teams this year – but you never know there could be a bolter from the next four and no doubt Collingwood will get the wobbles again!

On another note, I'm sure you've all heard recently that the new Gold Coast team recruited Karmichael Hunt, a Brisbane Bronco, across to AFL. Those poor old Broncos can't seem to catch a break at the moment!

Which brings me nicely back to the great Wayne Bennett…

In his book Wayne has a chapter called "Keep going until the siren sounds" in which he outlines the value of perseverance in football, and in life.

In it he says, and I quote: "Almost every successful person could not remember doing anything great he or she had achieved without, at some stage, having wanted to tear it up and quit."

He goes on: “That is the difference between the success and the failure….those who won’t take risks and go for it, who won’t see things out, they’re the ones who come home early, never answering the challenge and never going anywhere.”

Good stuff. So, perseverance goes hand-in-hand with risk at times, because it is often all too easy to take the simple path, or give up when the going gets tough.

But Wayne also understands the importance of knowing when it’s time to change tack. His chapter about winning is titled “If you do what you always did, you’ll get what you always got”, and I think that sums it up perfectly.

The best example I can personally give you of this and of transforming a company is Bank of Queensland’s story.

So to talk about BOQ’s transformation, I’d like to look back to when I became Managing Director of the Bank, in 2001.

When I arrived, BOQ was doing OK.

We had one of the most identifiable brands in the State yet only six per cent of Queenslanders actually banked with us. And our branch network was smaller than any other bank’s despite the fact we were only in Queensland.

At the time I had many asking why I would I leave a senior position in a major bank I had been with for more than 30 years for the challenges which Bank of Queensland offered in 2001. It came down to one word – potential.

Bank of Queensland had enormous untapped potential, and still does in my opinion. I understood that there was a very solid base there, but I also knew that if we kept doing what we'd always done, we'd keep getting what we'd always got.

So, given the need for change, there were a number of paths I could have taken as a new Managing Director and CEO.

One was the tried and true path of new CEOs – slash and burn. Blame everything on the last guy, cut costs, and become a darling of the market through increased profit.

Usually when a banker talks about cutting costs it comes down to shutting branches and sacking staff. That is what is often expected of an incoming new executive in today's tough world of corporate business. After all, a low cost-to-income ratio means a happy market.

Or, I could take the other safe path of slowly building on the strengths BOQ had in the market, looking to leverage off a well-known brand through low-risk growth strategies which, while not as spectacular, would still have built value.
It means an easy story to tell to the market, and analysts can build a standard model in which to place Bank of Queensland.

Or I could take a more radical, riskier path. Well-managed risk combined with perseverance could perhaps win the day.

What if we built shareholder value through dramatically increasing revenue?

What if we built value through cutting costs without cutting people?

What if we came up with a new way to do banking in Australia, rather than following the pack?

Would we have the courage to see that new way through, even though it would be so different from the way the rest of the banking sector was doing it, and given it may be a while before others see the benefit?

Luckily I had a board of directors who understood the vision, and an executive team who were able to drive the changes.

We had confidence in our vision, and belief in our ability to execute it, but there were some dark days as we put up with the scepticism of the analysts, media and our competitors.

At one stage our largest shareholder, the Commonwealth Bank, sold its 11 per cent stake overnight and without any warning, driving our share price from what was then a high of $11 down to about $9.30.

But we stuck to our guns.

On another occasion Australia's most senior banking analyst said the BOQ model would not work, but we persisted and continued to push on.

And when our plan to replace our entire core banking IT platform created some heartache amongst our customers, many in the industry smirked quietly behind their hands and talked of our inability to manage our growth.

And even when we bought a couple of companies, one in ATMs and another in equipment finance, there was the claim that we had no integration experience and that the purchases could prove to be costly duds.

And then, when we announced that we would spread the BOQ story interstate, there were the claims that the brand would never work, and that the model was somehow distinctly Queensland, and couldn't possibly translate to the more sophisticated markets of Sydney and Melbourne.

Our competitor banks, which are all larger than us by the way, went on, often patronising our novel attempt to bring personal service and branch banking back to Australians.

While we undertook to open branches rather than close them, to drive more employment rather than less, our results showed a marked improvement, and the market began to respond, driving up our share price.

So, our net profit after tax has jumped from $24 million in 2001 to $155 million last year, and just a couple of weeks ago we successfully completed an approximately $230 million fully underwritten institutional equity raising. The fact that this equity raising was about significantly over-subscribed, and that we are expecting strong support through the retail component demonstrates how far we've come in terms of real and perceived shareholder value.

You could say we have been rewarded for our persistence…

So, perseverance, mixed with a little risk, paid off for Bank of Queensland, but it was perseverance in an entirely new business model, an innovative model, rather than persistence in the old model. And that is the key.

So the real question is, how did we combine innovation and perseverance and support our calculated risks?

Well first, to innovation.

In 2001 Bank of Queensland had 93 branches, in Queensland only, of which 35 were an agency model. Now, these agencies looked exactly the same as the corporate-owned branches, and provided full banking services.

The problem for the Bank was that these agencies had little incentive to actually drive value for the bank as they were remunerated on a transaction rather than a balance sheet basis.

Having worked and studied the banking system in America, I had, when I came to BOQ, a different idea of branch banking from many of my contemporaries.

In the US the branch was making a big comeback as a retail outlet, a viable sales channel, instead of the Australian perception of a branch by the big banks as a drain on profitability.

US banks were opening hundreds of new branches across the country, expanding their footprint and opening themselves up to literally millions of new customers.

Here in Australia, the banks were still closing branches.

I thought a small bank like BOQ could make its mark by being different, but, being small, we still faced issues around how to pay for a fast branch roll-out while also continuing to reduce our cost-to-income. The answer was the Owner-Managed Branch, or OMB. What we did was turn our agency model on its head, and at the same time, turned Australian banking on its head.

We turned the tired-old agency model into a thriving, value-driving machine by changing it into a franchise model, and attracting the very best banking entrepreneurs to come on board.

Rolling out a bank branch franchise network is unique to Bank of Queensland in Australia, and our model is actually unique in the world.

With our OMB model, we have created a very different culture, a franchise culture supported by rigorous banking controls.

Branch managers were now rewarded on performance – for increasing both lending and deposits – as well as for providing excellent service.

And we quickly discovered that as soon as people had ‘skin in the game’ their attitude and performance changed.

What we have seen is a service-driven model in which the bank branch managers bent over backwards to find out what their customers wanted, and then provide it.

It also led to an influx of brilliant bankers from our competitors and unearthed some serious talent from within our own ranks.

The bankers who migrated from other banks had, for many years, been top performers, but were often frustrated by their inability to build strong retail relationships with their clients.

Whenever they performed well as a branch manager, they were inevitably transferred somewhere else. Whenever they built up a strong client base in business or private banking, those clients were then shuffled off to call centres or to another banker.

The problem was that they had nowhere to go, except to another bank where the same problems would eventually occur.

They were actually becoming victims themselves of some of the problems that had been facing their customers over the previous decade as banks forgot that they were in a service industry.
As Mark Twain once said:
“A banker is a fellow who lends you his umbrella when the sun is shining, but wants it back the minute it begins to rain.”

Now their big bank employers were demanding the customers’ umbrellas back and they, the bank employees, were on the end of a wave of righteous customer anger.

Their options were to stick it out, leave the finance industry completely, or take up as a mortgage broker. Many found the idea of leaving a full banking environment to sell a single product less than appealing.

That’s where Bank of Queensland came in.

Our owner-managed branch model allowed these bankers to run a full-service branch with all the supporting bells and whistles, but in an old-fashioned, customer-facing, service-orientated way.

Consequently, we were flooded with offers by bankers in Queensland, and around the country, to take up the challenge of becoming a BOQ owner-manager. And we picked only the very best of them. Like Kate Merta, our Hampton Branch Owner Manager, who arranged for me to speak to you today.

The success of the roll out of owner-managed branches in Queensland through the variable cost model we developed, and the speed at which we were able to undertake the roll out, soon had us looking for new markets.

My plan all along was to ensure we attained the required reach and depth in the Queensland market. At 165 branches, we now match or exceed almost all the other banks' Queensland branch presence. We now have 201 Owner-Managed Branches, including 44 in NSW and ACT, 30 in WA, 26 in Victoria, and 4 in WA, NT and Tasmania. Our total network is around 270 branches.

We have obviously made some mistakes along the way, but we have learnt from these mistakes and have improved the way we manage our OMB network. And the results really do speak for themselves. We continue to outperform the market, growing at twice the pace of our peers in both lending and deposits, which is a significant achievement and is due in large part to our unique OMB model.
At the same time we were rolling out new branches, we were also opening new business banking centres, which have seen us return face-to-face banking to people running small and medium sized business, hopefully including some of you here today.

So, innovation has driven our success, our resurgence as a company, and our emergence as a confident, stand-alone regional bank in one of the country's most competitive industries.

But all this wouldn't have been possible without the ability to actually execute our plans.

And so I will speak briefly on execution, and how vital it is to any transformation.

As the old military axiom goes, no plan survives contact with the enemy, and so it is true that in business your plan is only as good as its implementation, or execution.

In Bank of Queensland's case, it didn't matter how revolutionary, how innovative we were, we had to make our plans, our vision, work. As they say, strategy's easy, it's the execution that's hard.
It is actually the part of the most recent BOQ story of which I am most proud.

As I alluded to earlier, before we began our Owner-Managed Branch rollout, many in the industry either did not realise we existed, or had quietly written us off as a force in banking.
It was one thing to come up with the OMB model, to realise we needed to dramatically improve business banking and expand into areas like debtor finance, introduce a new computer system, upgrade our ATMs, revamp our entire product suite – it was another thing to actually achieve the results we expected.

Not what others expected, but what we expected. The expectations of others were fairly low initially, now they are much, much higher.

So, to bring together a small team, inspire that team with the vision and the mission, and to see the results has been deeply gratifying.

As franchised bank branches had never been done before in Australia, we had to learn the execution side as well.

The key is to never forget your goal, the end game. Never let the details get in the way of the overall vision.

And don't form too many committees – that's particularly important. Sometimes the best committee is one person!

While we have had many overseas financial gurus ask us about our model, and whether it can be transported into an overseas market, the hardest thing for us to explain is that it is more than just the model.

It is knowing what works and what doesn't. It is knowing who will work, and who won't, in a franchised bank branch.

Franchising can be a tough game if you are selling fruit juice or sandwiches. It can be an even tougher game when you must be a talented banker as well as someone with the skills necessary to run a small business.

It limits the pool available. If you then take the uncompromising stance we have taken, it limits it even further.

But it is more than just the branches. While branches are the key to offering excellent service, modern banking and the extra functionality and convenience it offers is about much more.

So realising our ATM network in 2003 was limited to just one state and even then were pretty thin on the ground, we purchased ATM Solutions Australasia, a provider of convenience ATMs located where people need them.

Not only did this give us the most widespread ATM network of any Bank with more than 2,400 machines, it also allowed us to showcase our integration and entrepreneurial skills, as we expanded and sold the company less than two years later for a net profit of $15.5 million. ATM Solutions eventually morphed into Customers Limited, the second largest ATM provider in the country and their CEO, Tim Wildash, who is a close friend of mine and the founder of the old ATM Solutions business, is in the audience today.

As I mentioned earlier, we also aggressively grew our business banking operation, focusing on providing small and medium businesses with a level of personal service not available at other banks.

This strategy, in tandem with the opening of 16 dedicated Business Banking Centres throughout Australia and two strategic acquisitions — equipment finance company UFJ Finance Australia in 2004 and debtor finance company ORIX Capital in 2005 — saw us double our business banking portfolio in just two years.

Using the experience and hitting power gained by these highly successful acquisitions, we purchased Queensland-based Pioneer Permanent Building Society in late 2006, establishing the largest presence in Queensland of any bank.

And in December 2007, Home Building Society shareholders voted unanimously for a friendly merger with BOQ giving the Bank another 29 branches based in Perth.

Despite our earlier success with UFJ and ORIX, the nay-sayers doubted our acquisitional experience.

But you know what they say – success is the best revenge – and due to the dedication of my team, and our ability to never lose sight of the end goal, the vision, we have successfully integrated both Pioneer and Home Building Society. And even better, the cost synergies have been far in excess of what we originally anticipated.

Now this has all been a very positive story.

But let's not ignore the fact that the past twelve to eighteen months have drastically changed the environment in which we're operating.

The banking sector has not been a particularly friendly environment for Bank of Queensland over the past 18 months. The cost of funding has increased dramatically, pricing pressures have intensified, and consolidation in the sector has seen two of our regional competitors swallowed up by the big guys, and many were convinced that we were next.

As they say, when elephants dance, ants tend to die.

But once again, we looked at the environment, and realised that there were opportunities amongst all the gloom.

We recognised that there will always be some Australians who don't want to bank with the big guys. Who want a bank manager who knows their name, and a bank that's not so big it treats them like a number, nor too small not to know their stuff.

And the huge reduction in competition in the sector means they now have even fewer banks to choose from.

So what if we proved to these customers that we could give them the service everyone else just talks about. That we truly were a big small bank. A bank that is big enough to give them expert advice, but small enough to care about personal service.

What if we could be 'the fifth bank' in Australian banking?

But to do this, we realised that we need scale. So in December last year we announced Project Pathways, which was designed to help us achieve this scale through a number of programs.

The efficiency stream of Project Pathways will provide the Bank with estimated annual run-rate equivalent cost savings of approximately $50m in FY10, which should allow us to compete with the major banks on a Cost to Income (CTI) ratio basis (mid 40%), despite being only 1/20th their size.

We have also recently enhanced our direct channels and the OMB network to grow stronger ‘sticky’ retail deposits, and earlier this year we completed an organisation restructure to ensure we were the right ‘shape and size’ for the part of the economic cycle we were in.

We also performed a diagnostic of all of our current products and channels to see what we should stop doing and what we should focus on.

We have renewed and strengthened our focus on SMEs, which will hopefully please some of you here today, as we see SMEs as a natural fit for the Bank, in large part because the majority of our Branch Managers are also small business owners.

I know Kate would be happy to talk to anyone here today who isn’t happy with their banking and is looking for someone who actually understands the opportunities and challenges particular to a small business.

But I digress.

Last but not least on Project Pathways, we recently announced that one of our largest shareholders, a French bank called BRED Banque Populaire, will increase their shareholding from 10.48% to 12.5% as a cornerstone investor.

So I am delighted to tell you that we have now completed Project Pathways as part of our ongoing transformation, and believe that it has helped us position ourselves to take advantage of the opportunities coming out of this Global Financial Crisis.

Conclusion

So I hope you agree that persistence, innovation and execution have paid off at Bank of Queensland.

Obviously we're not without our trials, in fact, I'm sure many of you have read about some of the larger ones through the press, but I truly believe that BOQ is a great company, full of great people, and that's what will make us a success.

Because in business, it's all about people. No matter what it is you make, how you market it, you must never forget that it is all about people.

They are what make a company great; isn't that right, Kate?

The big banks forgot that for a decade or so.

But at Bank of Queensland, we know that we are only as good as the people who work for and with us, and that our entire strategy is based on getting more customers. Not more accounts, not more businesses, not more dollars.

More people, that's what we want, that is our goal.

So, as I started saying today, persistence, and the ability to know when to change your approach, are key to success in business. I once heard a great line that has stuck with me through the years – “you might be on the right track, but if you stay there long enough you’ll get run over”.

With the enthusiasm and dynamism that is so vital to small business and that is so obviously in the room here today, I know that won’t happen to you.

Thank you.