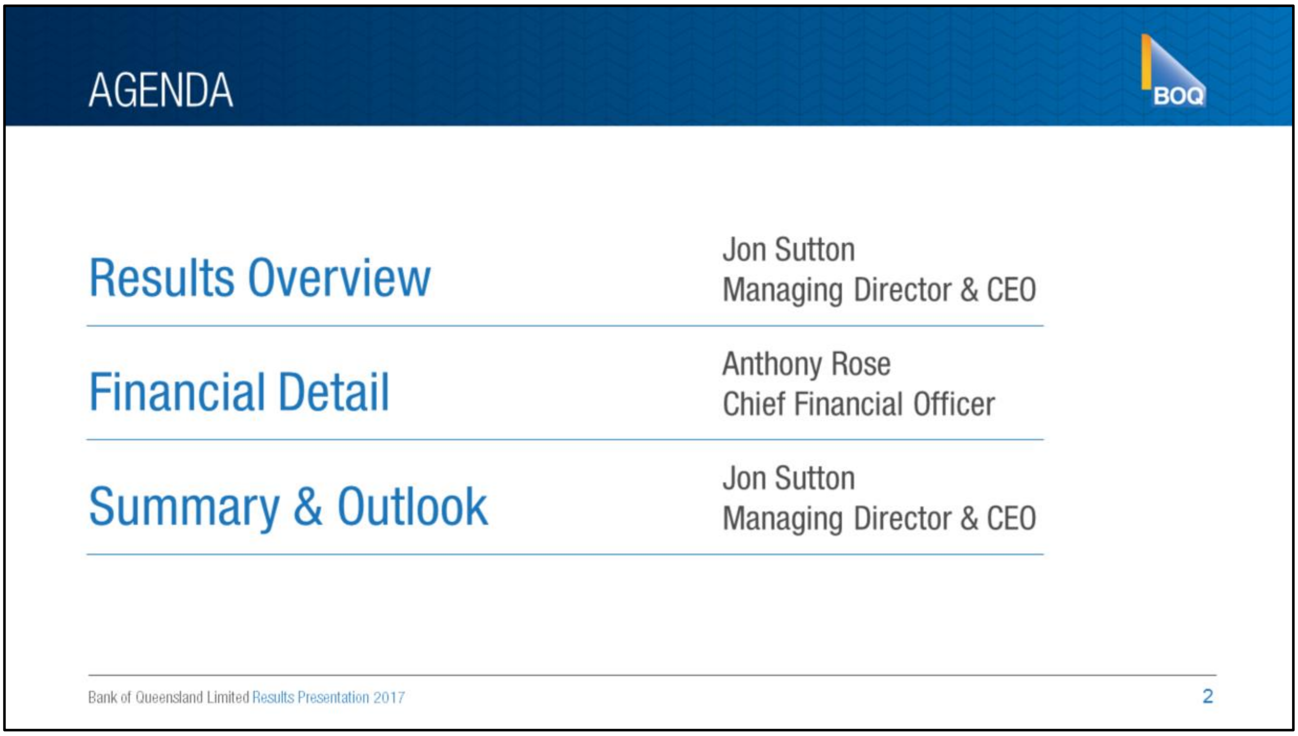

BOQ
FY2017
Results Presentation
12 October 2017
FOR THE YEAR ENDED 31 AUGUST 2017
Bank of Queensland Limited ABN 32 009 656 740. AFSL No 244616.

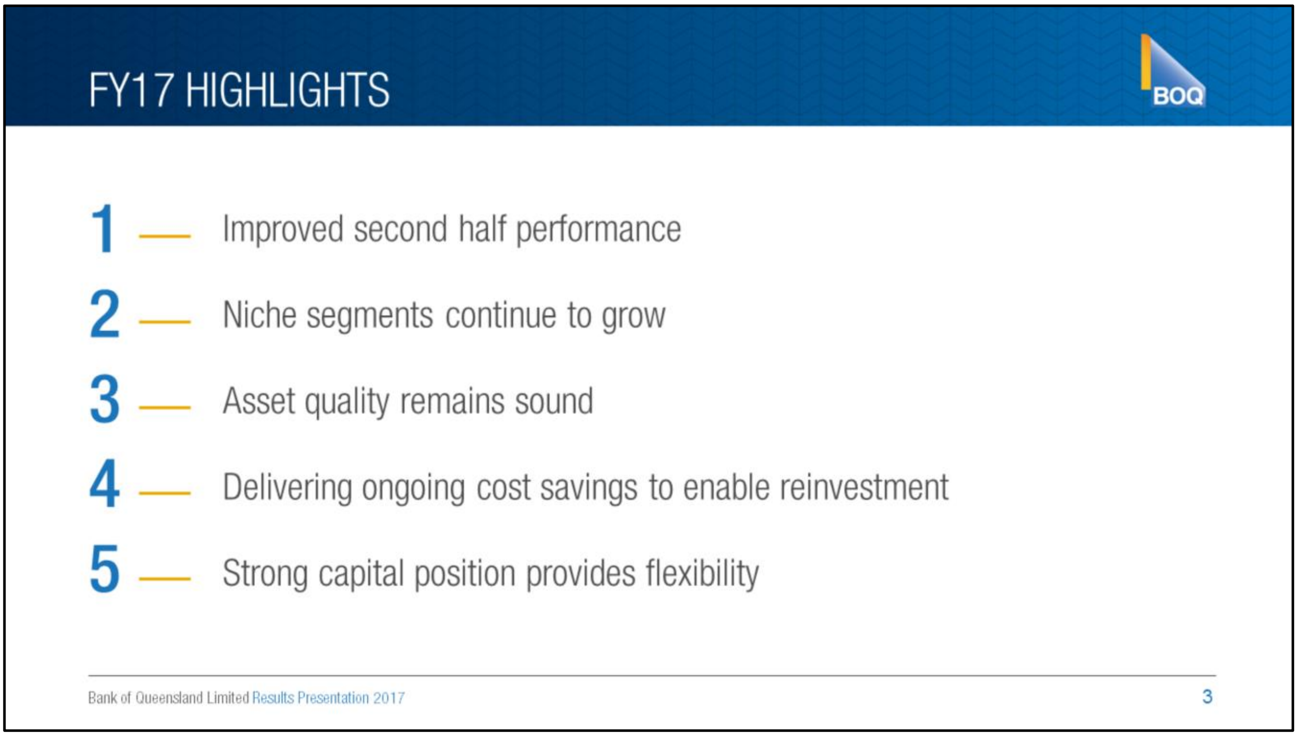



Ladies and gentlemen, welcome to BOQ’s full year financial result for 2017. My name is Tanny Mangos and I am the General Manager Corporate Affairs and Investor Relations.

Thank you for joining us today, in the room, on the phones and also by webcast.

For today’s presentation, Managing Director and CEO Jon Sutton will provide an overview of the result. Chief Financial Officer Anthony Rose will run through the numbers and then Jon Sutton will return to discuss priorities and the outlook for the period ahead. This will be followed by the opportunity for analysts and investors to ask questions.

I’ll now hand over to Jon.




Thank you Tanny and good morning.

I'll begin with the highlights of BOQ's full year result on slide 3.

We have delivered a sound result for 2017, with improved performance in the second half.

The improvement in both lending growth and margin is in line with the guidance we provided at our first half result.

This result has been achieved against a backdrop of industry challenges, including an ever changing regulatory and political landscape.

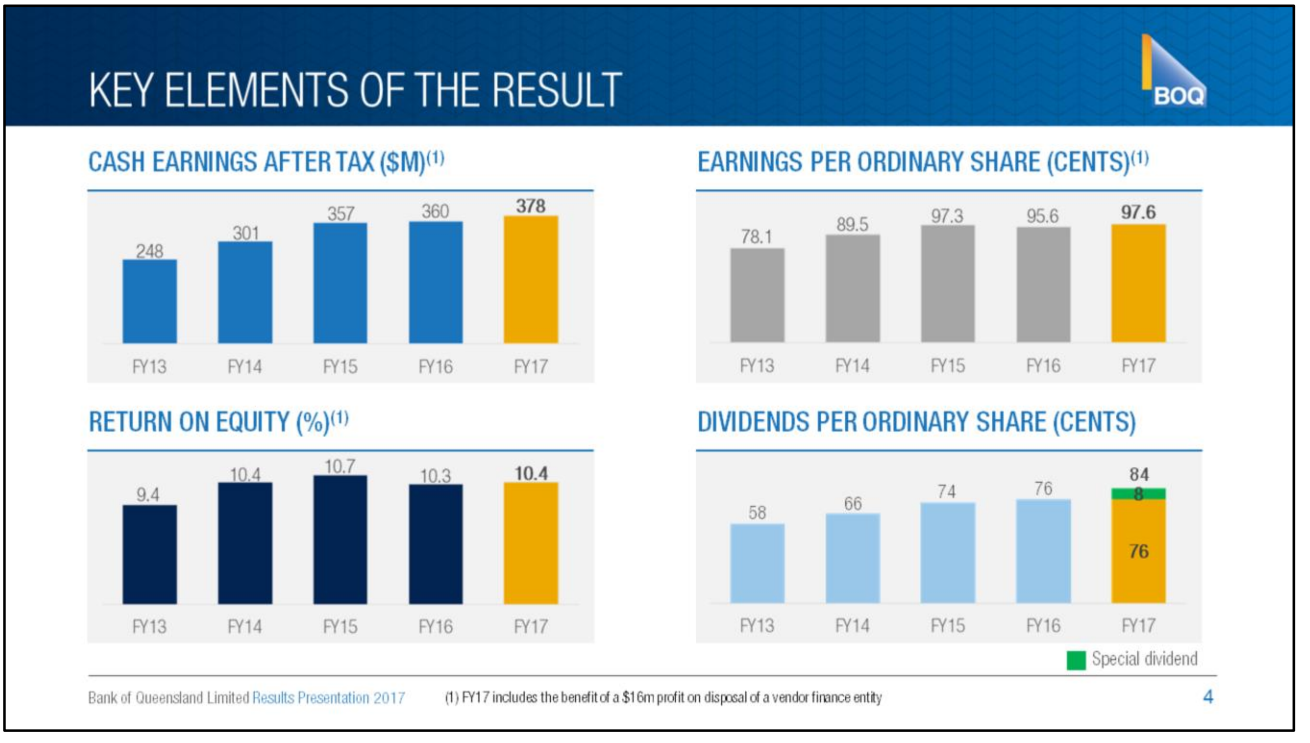
Our niche segments continue to grow. BOQ Specialist, BOQ Finance and our commercial lending segments have all delivered good results.

Virgin Money has also delivered ahead of expectations with growth in its home loan product.

Our asset quality remains sound, with further improvement across a range of metrics.  This is the outcome of a deliberate approach to improve risk management over the past five years.

I am also pleased to report that we have delivered on our expense targets. We have found savings throughout the organisation which have allowed us to reinvest in our growth businesses.

Our capital position is very strong. We are in an enviable position to consider capital management options to deliver long term shareholder value.




Turning now to the key financial elements of the result on slide 4.

Cash earnings increased by 5 per cent to 378 million dollars. This included a 16 million dollar profit on the disposal of a vendor finance entity. We will discuss this in further detail later.

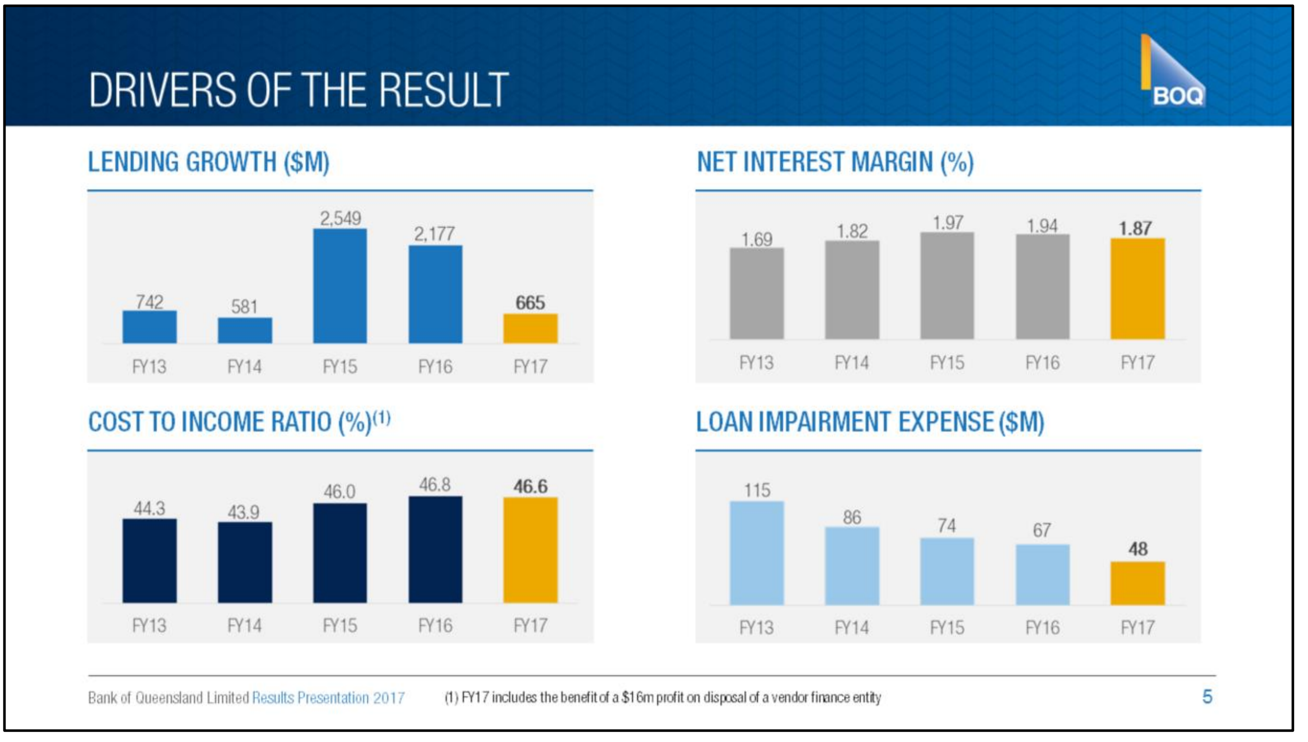
Excluding this one off item, cash earnings increased by 1 per cent to 362 million dollars.

Earnings per share which also includes the one off, increased 2 per cent to 97.6 cents per share. Return on equity increased 10 basis points to 10.4 per cent.

The Board has maintained the final dividend at 38 cents to bring the full year dividend to 76 cents per share.

The Bank's strong capital position is clear following the release of APRA's 'unquestionably strong' regulatory guidance in July. As a result, the Board has resolved to pay a special dividend of 8 cents per share.

Anthony will talk through our approach to managing capital and the rationale for this in more detail.

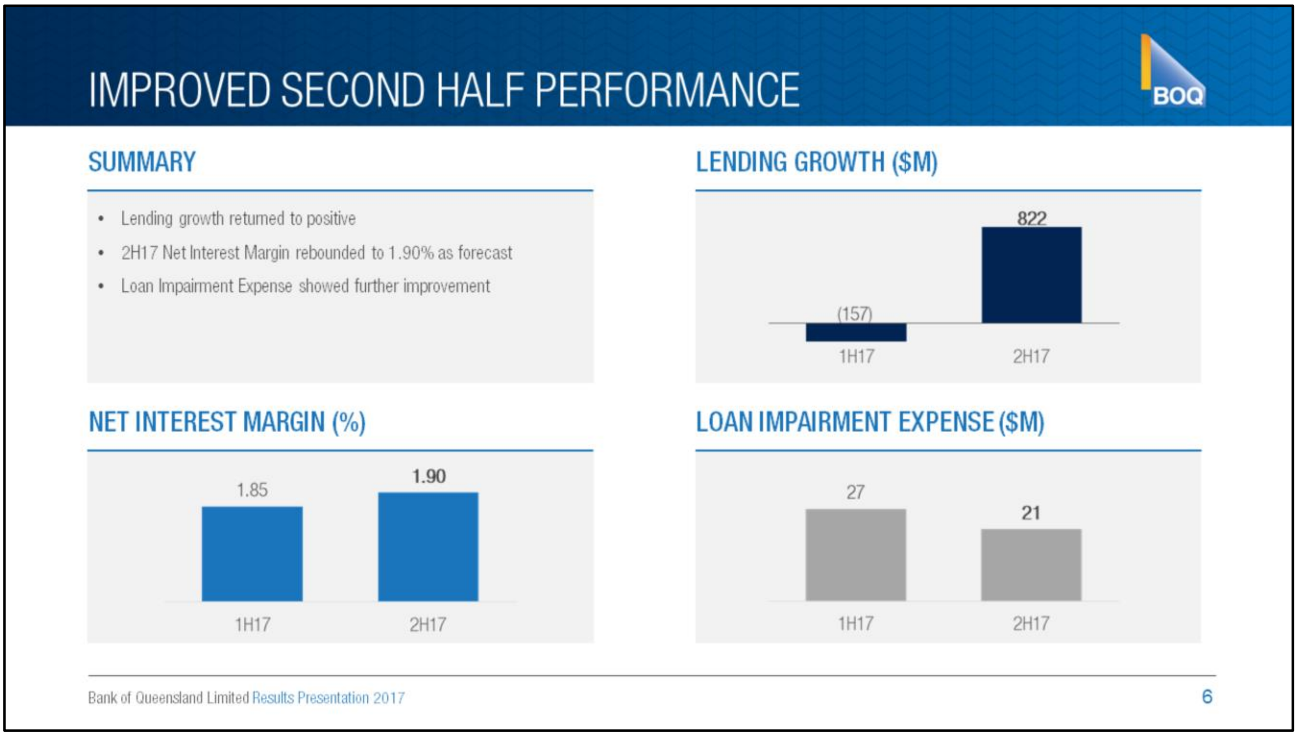



Moving to the key underlying drivers of the result on slide 5.

We achieved lending growth of 665 million dollars for the full year.

Net interest margin was down 7 basis points to 1.87 per cent.

Our cost to income ratio was down to 46.6 per cent and our loan impairment expense reduced to just 48 million dollars. This is a reflection of the continued improvement we have seen across the portfolio.



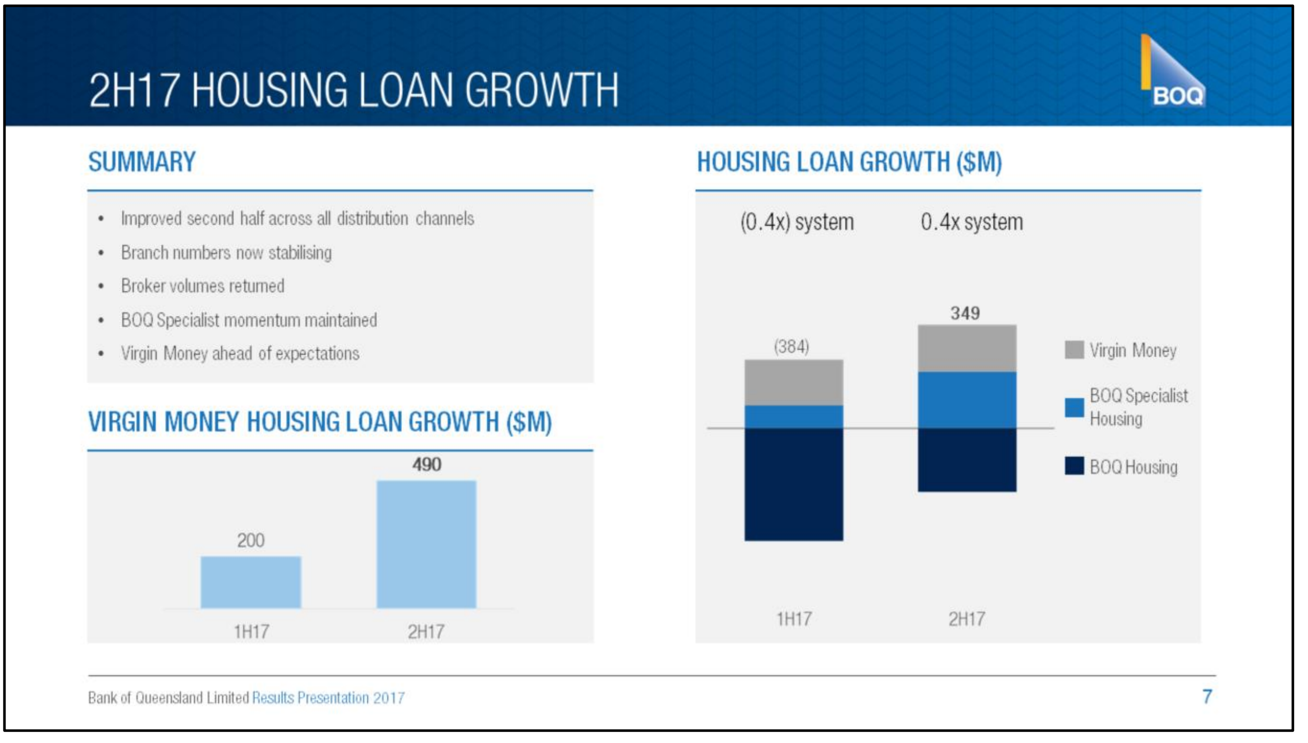

One of the most pleasing aspects of the result is the improved momentum in the second half as shown on slide 6.

The second half largely played out as we said it would at our first half result.

Lending growth improved significantly, in both the housing and commercial loan portfolios.

Net Interest Margin rebounded in the second half to 1.9 per cent. This was driven by a recovery in term deposit spreads, which we flagged at the first half result.

We also saw a further reduction in our loan impairment expense. I will talk more about asset quality shortly.




Slide 7 shows the improvement in housing loan growth across all channels in the second half.

The branch network remains a core part of our proposition for customers, not only in lending, but increasingly for deposits. We have been through a period of transition, improving the quality and compliance standards of the network. We have rebalanced the franchise commission model and increased the focus on customer retention and deposit gathering.

Although our branch numbers have reduced in recent years, we are now at a point where we expect our branch numbers to stabilise. We have focused on developing a good pipeline of quality new Owner Managers. This will help us manage succession planning and ownership transitions across the network.

The second half saw momentum lift in the broker channel across both the BOQ and Virgin Money brands. This included broker settlements nearly doubling for the BOQ brand in the second half compared to the first. We have been working hard to improve our processes and turnaround times. We are very focused on providing brokers and customers with a better experience when doing business with us. Feedback from brokers is that our turnaround times are no longer an issue. And that is not something we have been able to say in the past. I can also confirm we have been managing comfortably within our capacity under regulatory limits.

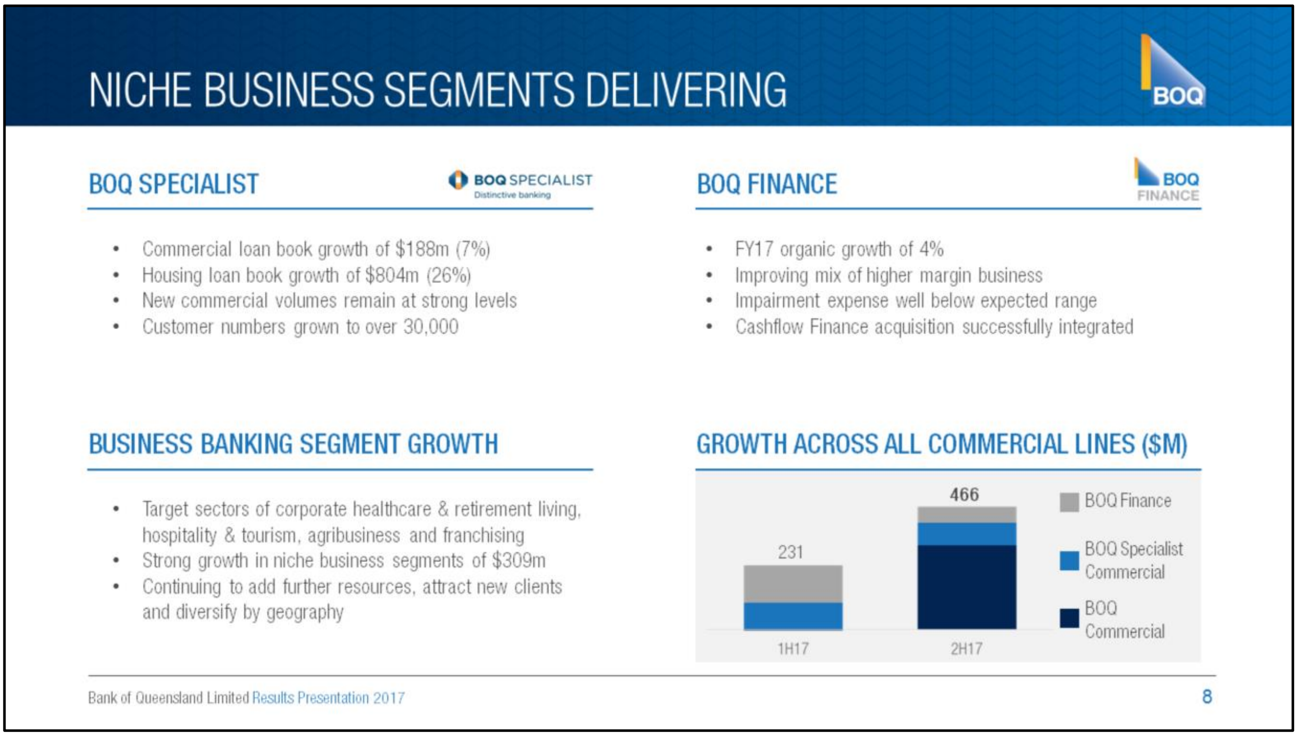
The increase in broker volumes has also been assisted by the convergence of serviceability tests, as well as income and expense validation requirements across the industry.  BOQ took a conservative approach to regulatory requirements and moved quickly to enhance practices in prior periods.  We are pleased to see that others are now moving in line with the practices we have been operating under for some time.

The Virgin Money Reward Me home loan portfolio has exceeded our expectations in terms of growth, delivering 700 million dollars in loan balances since its launch. We remain optimistic about the outlook for this business and are working on plans to expand its banking product offering.

BOQ Specialist has also continued to deliver strong mortgage volumes, with its portfolio growing to 3.8 billion dollars.  This is from a zero base when we acquired the business in 2014.  By meeting the needs of medical professionals early in their career, we are building a pipeline of future commercial and retail lending opportunities in this sector.

There is no doubt the macro prudential regulation is having an impact on the mortgage market.  We are seeing intense competition for owner-occupied principal and interest loans.

While we expect system and credit growth to moderate, we are confident in our diversified channel strategy.



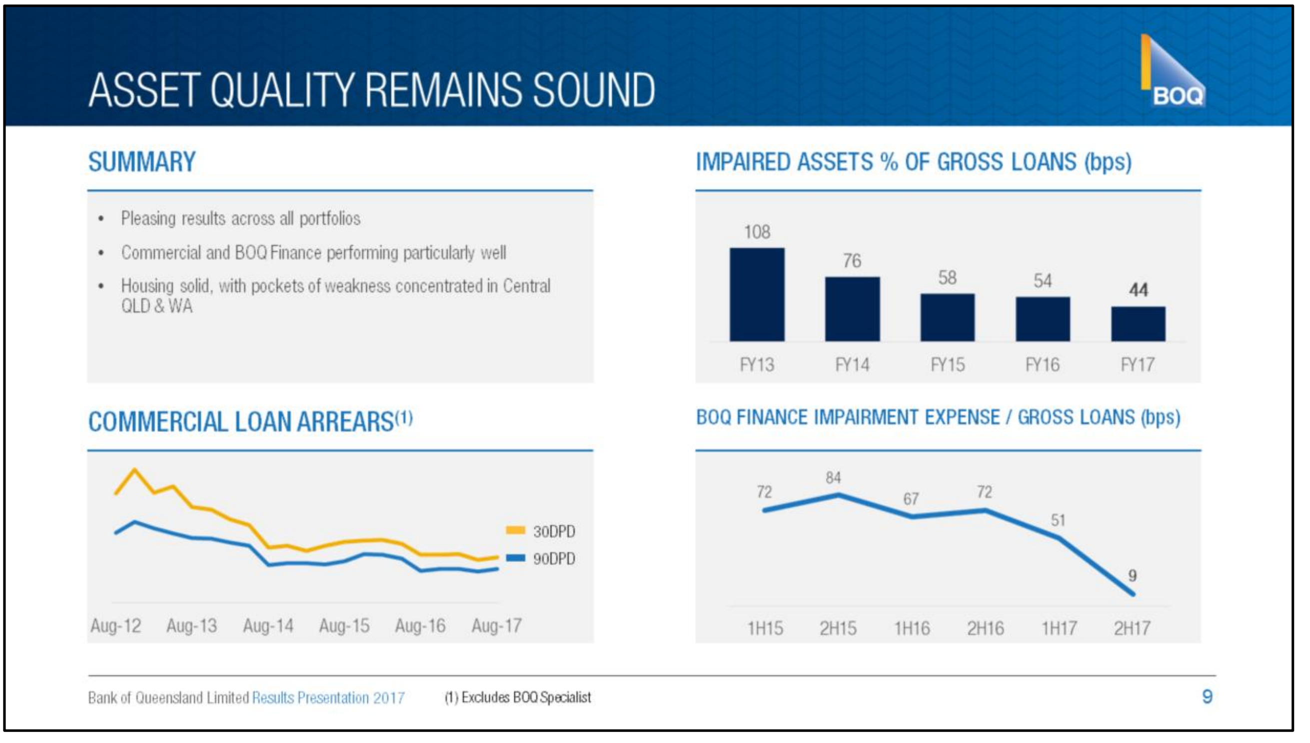

We have also made good progress in growing our niche businesses during the year.

BOQ Specialist delivered strong loan growth across both its housing and commercial loan books.  This business now serves more than 30,000 customers, which is up from around 19,000 when we acquired the business.

BOQ Finance made another strong contribution. Since its acquisition in December 2016, the Cashflow Finance business contributed revenues of 7 million dollars and a profit after tax of 2 million dollars. This is in line with expectations.

Our Business Banking target segments have continued to grow, albeit from a small base. Loan balances in the niche business banking segments of agribusiness, corporate healthcare & retirement living and hospitality & tourism have grown by 309 million dollars to 1.5 billion dollars.

During this period, we have built out capability in the niche segment of Corporate Healthcare, leveraging our industry expertise and contacts through BOQ Specialist.




Turning to slide 9.

The resilience we have built into the Bank is becoming increasingly evident.

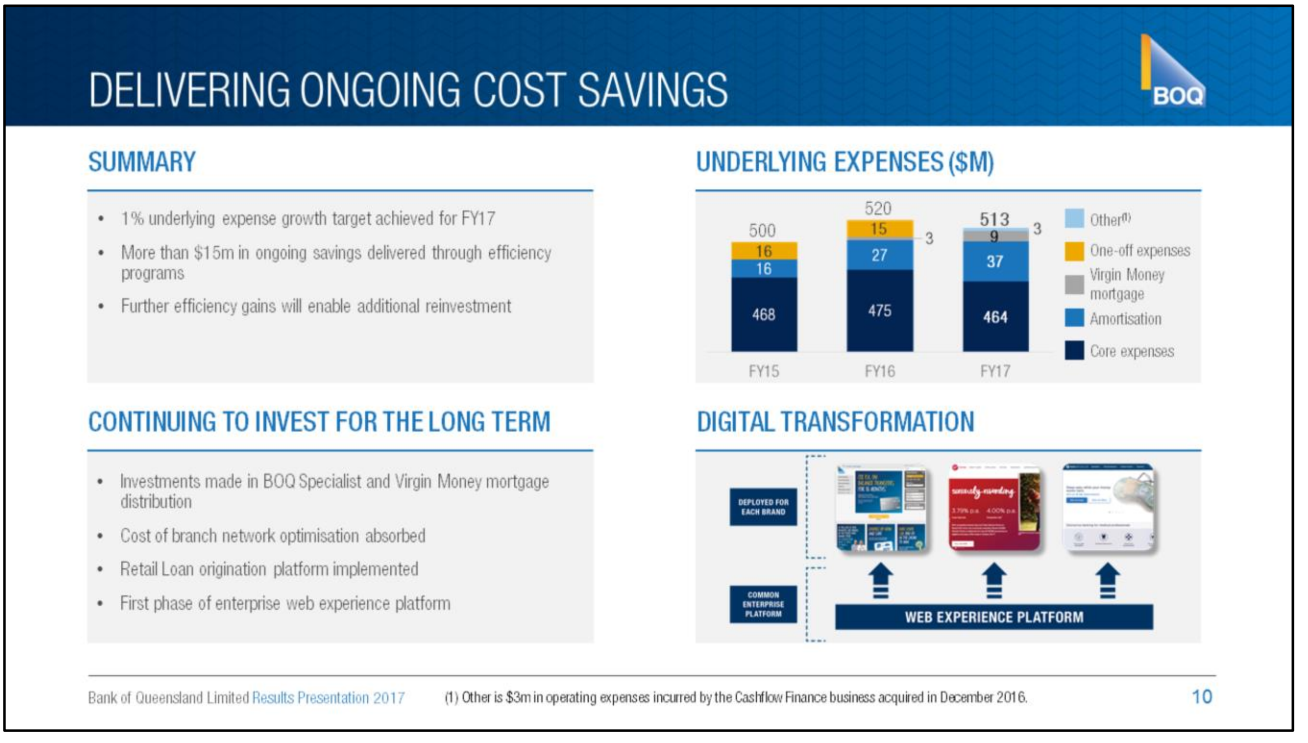
Impaired assets as a percentage of total loans is down to 44 basis points, while loan impairment expense was just 10 basis points of total loans in the second half.

The commercial loan portfolio is in very good health, which is evident in the long term arrears chart on this slide.

Meanwhile, the BOQ Finance portfolio recorded only 2 million dollars of impairment expense in the second half, or 9 basis points of total loans. This is an unusually low level which we expect will normalise in future periods.

The housing portfolio remains solid, although there has been a slight uptick in arrears, driven primarily by stress in central QLD.

Overall, we remain very comfortable with the health of the portfolio.  There are no signs of systemic stress emerging.




Another highlight of this result is our disciplined approach to cost management.

We have delivered on our 1 per cent underlying expense growth target, with underlying expenses of 510 million dollars.

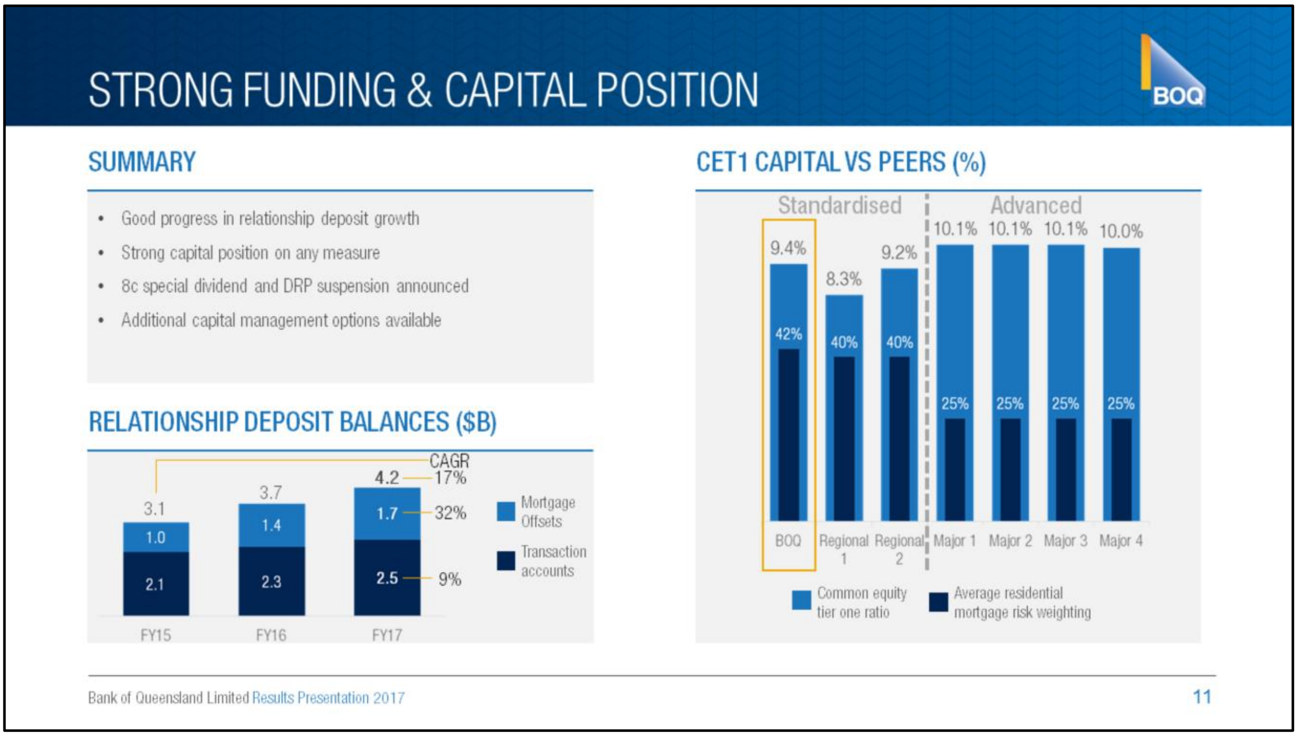
We achieved this target while still investing in the business.  Included in our underlying expenses are costs associated with the roll out of the Virgin Money mortgage product as well as the BOQ Specialist mortgage expansion.

We are also continuing to invest in digitising our processes, which will have the dual benefit of improving customer experience as well as improving efficiency.

In 2017 we established a mortgage hub bringing teams across the Group into a centre of excellence for mortgage processing. Supporting this is the retail lending origination platform which enables mortgages to be processed faster and at a lower cost.

The first phase of our enterprise web experience platform has been rolled out. Virgin and BOQ Specialist are currently operating on this new platform with plans for BOQ to join early in the new calendar year.

We continue to invest for the future, and I will provide some more information on this in the outlook section.




Moving to capital and funding on slide 11.

Our customer deposit growth has been pleasing. We have grown our at-call transaction account balances at a compound annual rate of 9 per cent since 2015. We have achieved even stronger growth in mortgage offset accounts, at a compound growth rate of 32 per cent.

This demonstrates growth in main bank relationships, which is important for the long term and is a very good result given our reduction in branch numbers. It is a good indicator of the improving performance of the network and our increased focus on deposit gathering.

Following APRA's clarity on 'unquestionably strong', we believe we are in a very strong capital position at 9.39 per cent common equity tier one.

Anthony will go through some of the tailwinds which would further strengthen this position by 20 to 25 basis points. This provides us with flexibility to consider capital management options.

In response to these changes and BOQ's position, the Board has determined that returning some of this additional capital to shareholders is the most appropriate course of action at this stage.

In addition to the determination to pay an 8 cent special dividend, the Board has suspended the dividend reinvestment plan.

# FY17 SCORECARD: STRATEGIC PRIORITIES

BOQ

| Strategic pillar | FY17 priorities | FY17 progress | Highlights |
|---|---|---|---|
| Customer in charge | 1. Expansion of mortgage aggregators for Virgin Money<br>2. Enhance digital customer experience<br>3. Ongoing branch network optimisation | Achieved<br>In progress<br>Achieved | Virgin Money mortgage growth of $700m |
| Grow the right way | 1. Optimise deposit pricing using data analytics<br>2. Develop specialist niche capability in franchising and hospitality<br>3. Focus investment in high margin businesses | Achieved & ongoing<br>In progress<br>Achieved & ongoing | Niche segment loan growth of $1.3bn |
| There's always a better way | 1. Complete roll out of new origination & leasing systems<br>2. Deliver return on investment in efficiency programs<br>3. Implement centralised mortgage hub | In progress<br>Achieved<br>Achieved & ongoing | >$15m in savings generated |
| Loved like no other | 1. Invest in leadership and talent<br>2. Build gender diversity towards 50% in senior management by 2020[1]<br>3. Complete ethics training roll-out | Achieved & ongoing<br>Achieved<br>Achieved | 39% of leadership roles held by women |

Legend: Achieved / Achieved & ongoing / In progress

Bank of Queensland Limited Results Presentation 2017 (1) 37% target for FY17 exceeded 12

Looking at our progress against strategy on slide 12, and I am pleased to report that we have delivered on our objectives.

We have expanded channels for customers to engage with us, including mortgage brokers as well as enhancing our digital capability.

We have continued to grow the right way, pricing for risk appropriately and targeting segments that value our relationship proposition.

We have found better ways to do things to keep our cost under control while also investing for the future.

And we continue to strive to be loved like no other, through ethics, diversity, leadership and our people.

I will return to talk about strategy and our focus going forward.

Anthony will now to take you through the financials in more detail.

# Financial Detail

Anthony Rose
Chief Financial Officer

# FINANCIAL PERFORMANCE: YEAR ON YEAR

BOQ

| | FY17 | FY17 v FY16 | FY17 adjusted[1] | FY17 adjusted[1] v FY16 |
|---|---|---|---|---|
| Net interest income | $926m | (1%) ▼ | $926m | (1%) ▼ |
| Non interest income | $175m | 1% ▲ | $159m | (8%) ▼ |
| **Total income** | **$1,101m** | **(1%)** ▼ | **$1,085m** | **(2%)** ▼ |
| Operating expenses | ($513m) | (1%) ▼ | ($513m) | (1%) ▼ |
| **Underlying profit** | **$588m** | - | **$572m** | **(3%)** ▼ |
| Loan impairment expense | ($48m) | (28%) ▼ | ($48m) | (28%) ▼ |
| **Profit before tax** | **$540m** | **3%** ▲ | **$524m** | - |
| Income tax expense | ($162m) | (1%) ▼ | ($162m) | (1%) ▼ |
| **Cash earnings after tax** | **$378m** | **5%** ▲ | **$362m** | **1%** ▲ |
| Cash basic earnings per share | 97.6c | 2% ▲ | 93.5c | (2%) ▼ |
| Return on average tangible equity | 13.7% | (10bps) ▼ | 13.1% | (70bps) ▼ |

Bank of Queensland Limited Results Presentation 2017

(1) FY17 adjusted for the $16m profit on disposal of a vendor finance entity

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Thanks Jon and good morning. I'll start on slide 14, which sets out our profit and loss.

On a headline basis our cash earnings after tax increased 5 per cent to 378 million dollars. This was driven primarily by a 28 per cent reduction in loan impairment expense.

On this slide we've also shown an adjusted result which strips out, the 16 million dollar profit on disposal, of a vendor finance entity - where the vendor partner exercised an option on the structured program. The profit on disposal came through the Non interest income line.

In addition, this profit was fully sheltered for tax against previously unrecognised capital losses.

Adjusting for this impact, our cash earnings after tax increased 1 per cent on the 2016 financial year. We did see a much improved performance in the second half which I'll take you through on the next slide.

# FINANCIAL PERFORMANCE: HALF ON HALF

BOQ

| | 2H17 | 2H17 v 1H17 | 2H17 adjusted(1) | 2H17 adjusted(1) v 1H17 |
|---|---|---|---|---|
| Net interest income | $474m | 5% ▲ | $474m | 5% ▲ |
| Non interest income | $95m | 19% ▲ | $79m | (1%) ▼ |
| **Total income** | **$569m** | **7%** ▲ | **$553m** | **4%** ▲ |
| Operating expenses | ($261m) | 4% ▲ | ($261m) | 4% ▲ |
| **Underlying profit** | **$308m** | **10%** ▲ | **$292m** | **4%** ▲ |
| Loan impairment expense | ($21m) | (22%) ▼ | ($21m) | (22%) ▼ |
| **Profit before tax** | **$287m** | **13%** ▲ | **$271m** | **7%** ▲ |
| Income tax expense | ($84m) | 8% ▲ | ($84m) | 8% ▲ |
| **Cash earnings after tax** | **$203m** | **16%** ▲ | **$187m** | **7%** ▲ |
| Cash basic earnings per share | 52.1c | 14% ▲ | 48.0c | 6% ▲ |
| Return on average tangible equity | 14.3% | 130bps ▲ | 13.2% | 20bps ▲ |

Bank of Queensland Limited Results Presentation 2017

(1) 2H17 adjusted for the $16m profit on disposal of a vendor finance entity

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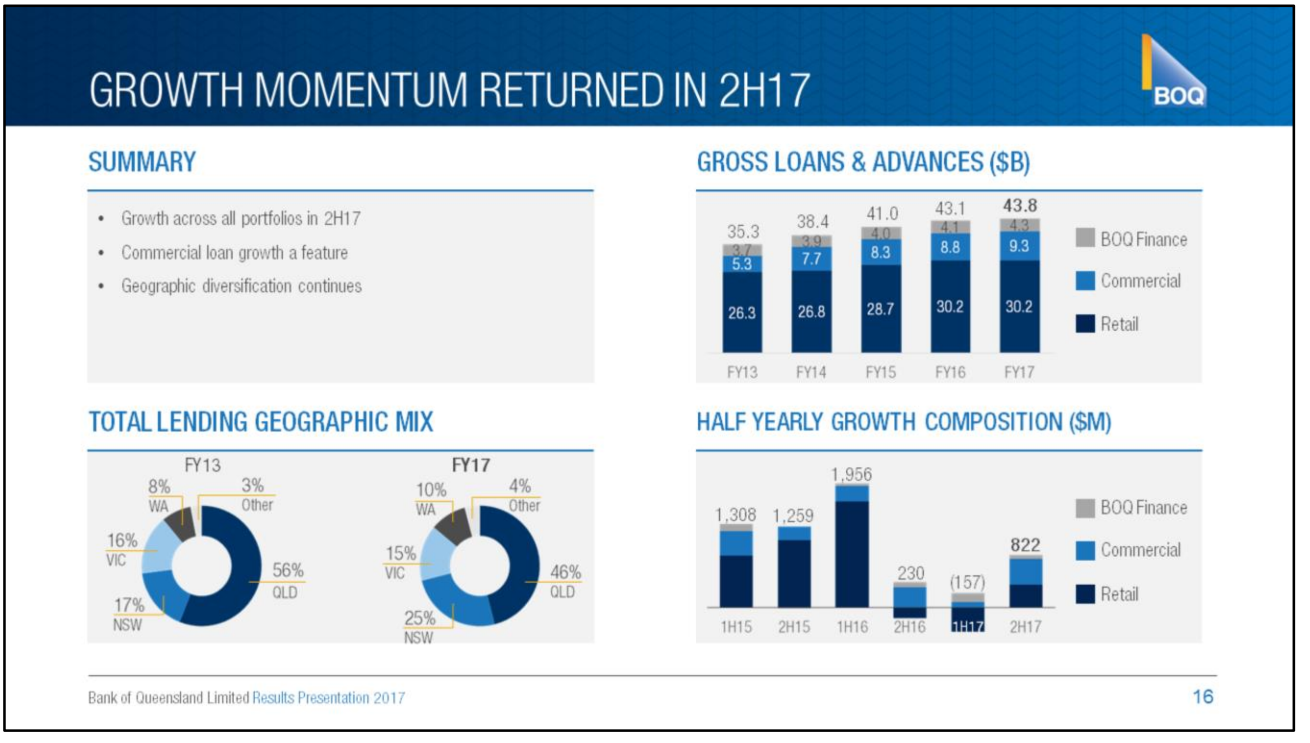
Again, we have provided adjusted figures here to strip out the 16 million dollar profit from the vendor finance entity disposal.

After adjusting for this, you can see the business has delivered a 7 per cent increase in earnings in the second half. This was driven by net interest income growth of 5 per cent and underlying profit growth of 4 per cent, as well as a 22 per cent improvement in loan impairment expense.

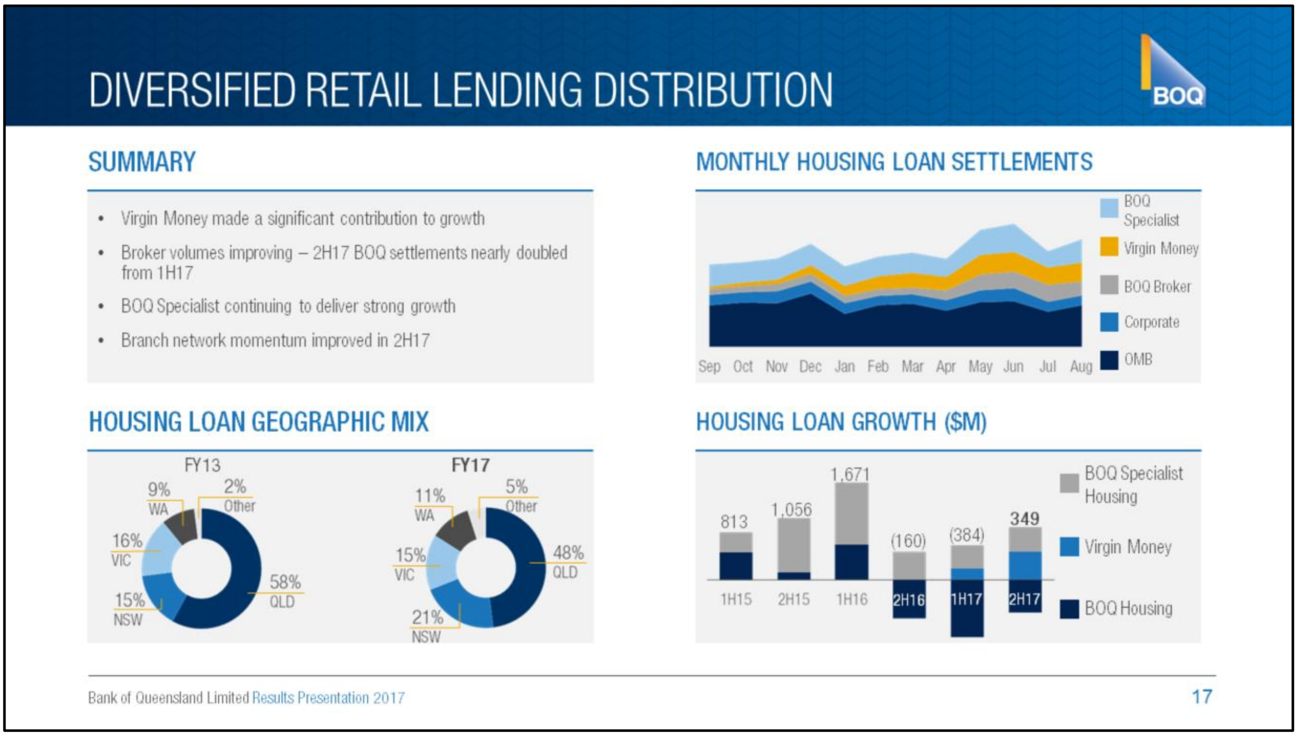
I'll now take you through the key drivers of each of these lines in more detail.




Starting with the loan portfolio on slide 16.

Following a contraction in the first half, we did see a return to growth in the second half of the year.

Pleasingly, the loan portfolio has continued to diversify geographically, with Queensland concentration now down to 46 per cent.



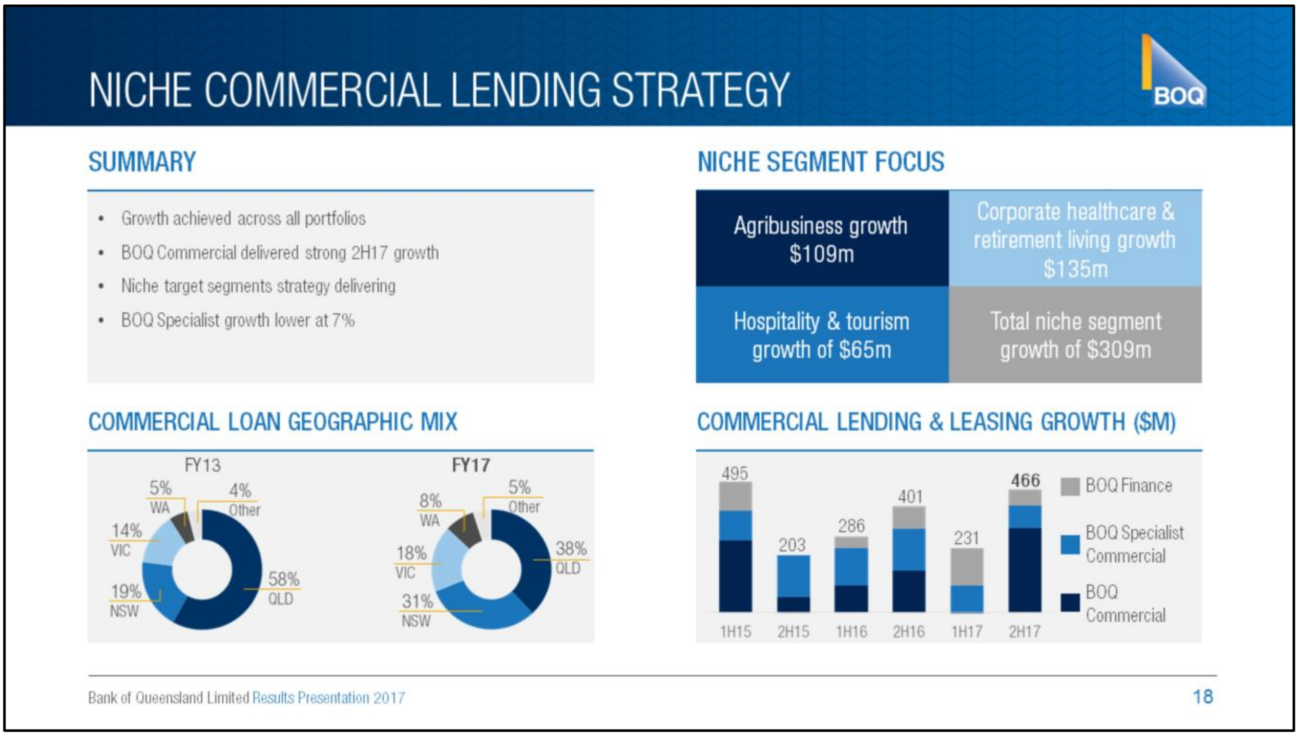

Digging into the retail portfolio on slide 17.

All distribution channels demonstrated improvement in the second half.

The chart on the top right, shows monthly housing settlements by channel, and as you can see, our owner managed branches are still our biggest contributor to our monthly housing loan settlements.

Overall we saw much better momentum in the second half as credit settings - particularly around validation requirements of customer income and expenses – became more aligned across the industry.

The uplift in broker volumes is the best evidence of this, with loans originated through brokers, including under the Virgin Money brand, contributing 28% of our home loan settlements in the second half.




Moving to commercial loan growth on slide 18, and as you can see on the bottom right, the portfolio grew strongly in the second half.

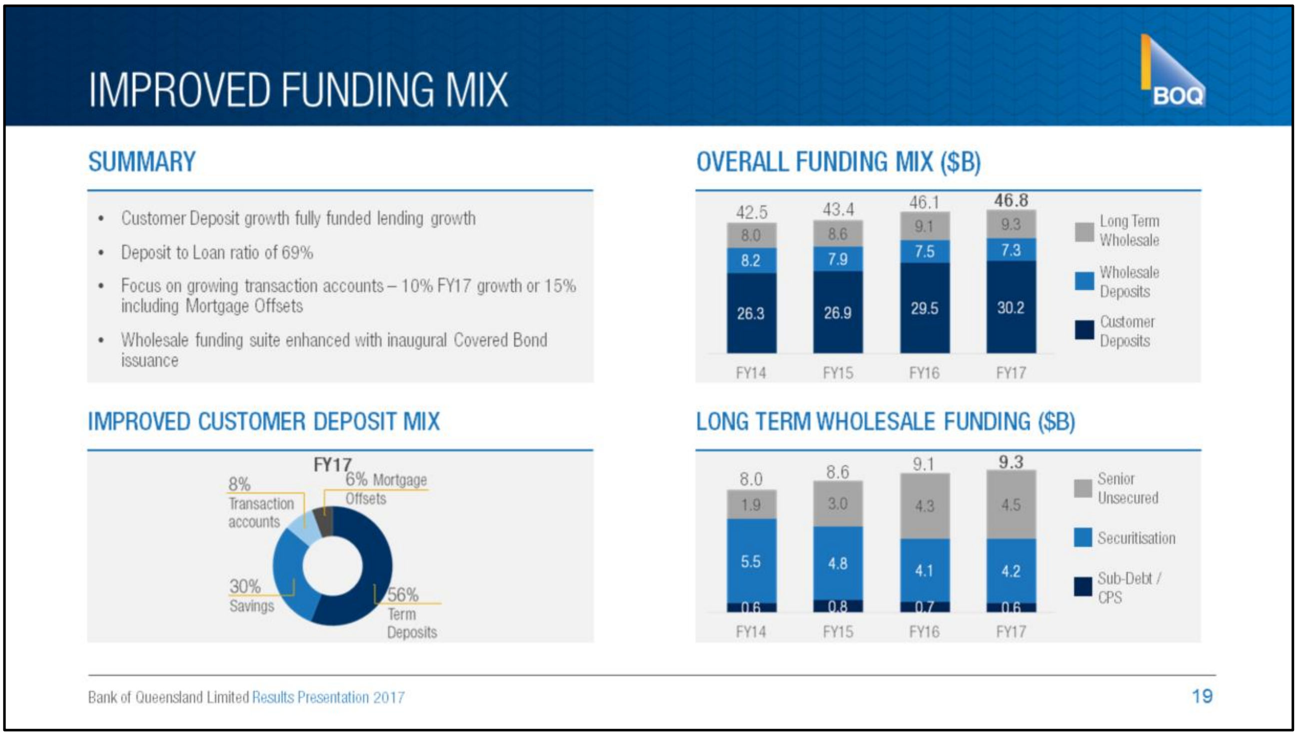
This followed a first half which was impacted by a small number of large customer paydowns.

Across the full year, we saw solid growth in the BOQ branded portfolio of around 300 million dollars. Our target niche segment strategy is delivering. We had strong new customer acquisition across agribusiness, corporate healthcare & retirement living, and hospitality & tourism.

BOQ Finance and BOQ Specialist also delivered solid levels of growth, with BOQ Finance particularly strong in the second half.

BOQ Specialist Commercial growth was slower in second half than in previous years. Settlement volumes have remained at consistent levels, but there was an uptick in run-off that slowed the rate of growth. We continue to see strong growth prospects for this business. Growth will be supported by the 'early life cycle' customer acquisition strategies that the BOQ Specialist team has been employing. Graduate customer acquisition success has been very pleasing and will deliver long term value.

Lastly, I'll point out that Queensland concentration in the commercial book is now down to 38 per cent, which we believe provides a good level of diversification. Changes in concentration levels going forward will now reflect underlying business opportunity.




Looking at the funding side of the balance sheet. And I'm now on slide 19.

Our 2017 lending growth has been fully funded by deposit growth. Our deposit to loan ratio finished the year at 69 per cent.

There has also been an improvement in the mix of deposit funding. As Jon has already touched on, we have good momentum in growing our main bank customer relationships that is evident by the growth in our transaction account and mortgage offset balances.

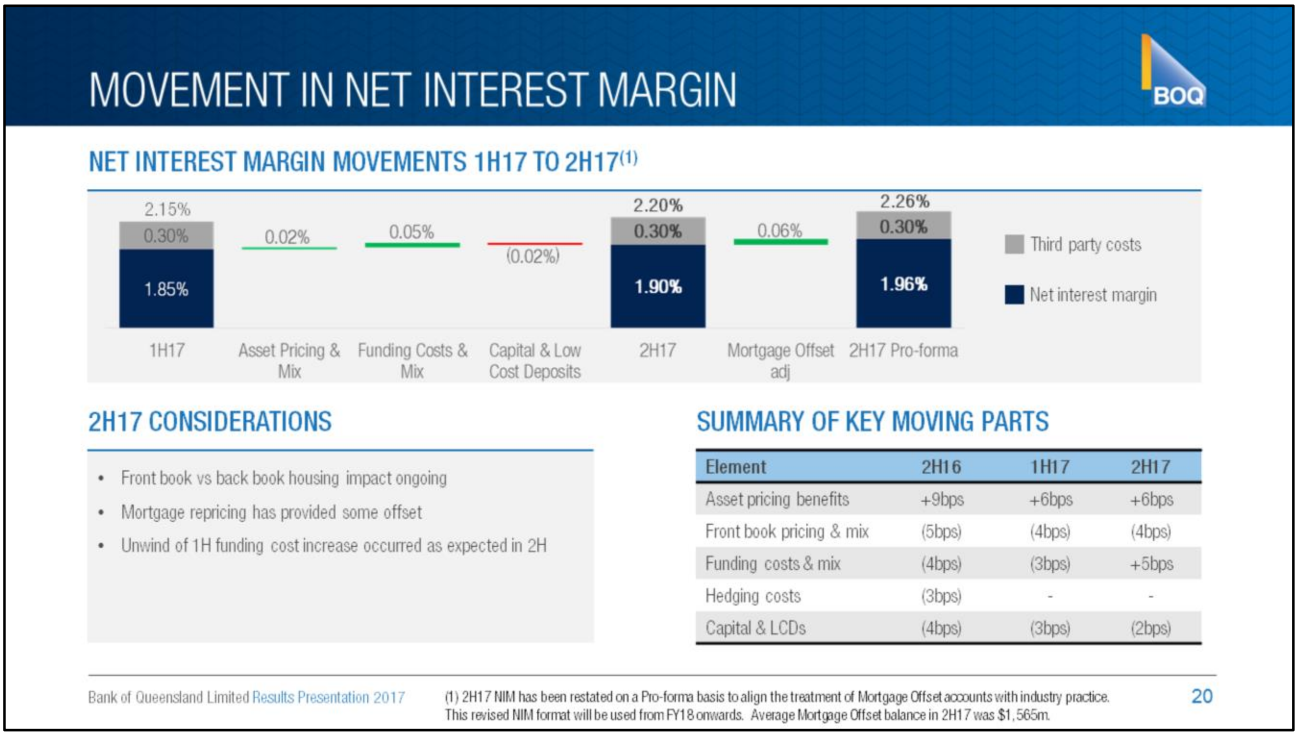
In May, we did see some noise as a consequence of the action Standard & Poor's took to downgrade 23 ADIs across the industry, including BOQ. This was based upon concerns with residential property prices and household debt levels, particularly in Sydney and Melbourne. I would highlight that BOQ is less directly exposed to this sector of the market and the relative outcomes across institutions in the industry were counterintuitive.

We did see some impact from this action in reduced credit lines and higher pricing in the more rating sensitive elements of the larger retail deposit and wholesale markets.

Moody's undertook a similar industry downgrade action in the month following, but pleasingly BOQ's rating was maintained at A3. Following this outcome, active work with the Bank's funding counterparties in these segments re-established limits to levels largely equivalent to those prevailing before S&P's action. We are now paying slightly more due to the split ratings position in this segment.

The split rating will also impact the pricing we are able to achieve in term funding markets, as our secondary spreads have widened.

In the term funding space, during the half, we successfully launched our inaugural covered bond issue. This is an important element of our forward funding armoury. It provides access to a deep pool of investors that we would otherwise be unable to access.




If we move on to the margin story - and I'm now on slide 20.

This was a story of two halves. In the first half, we experienced 5 basis points of margin contraction, which we thought would reverse in the second half. We did achieve that profile with a restoration of our margin to 1.9% - and conditions were largely in line with our expectations.

I have previously covered the ratings actions that played out during the half. If that had not occurred, the margin outcome would have been slightly better.

Looking at decomposing the movement for the half….
Loan repricing activity implemented through the year added around 5 basis points to our margin. We also benefitted by 1 basis point from the higher margin Cashflow Finance business we acquired during the year.

Meanwhile, the front to back book pricing dynamic continued to be a drag on margins, with a 4 basis point negative impact. This is driven by lower rates being provided on new loans and to retain existing customers, compared to the average of the portfolio. We expect this dynamic to continue.

The funding cost and mix changes improved margin by 5 basis points. This was driven largely by a retracing of spreads on term deposits that had widened significantly in the first half.

Capital and low cost deposits, or the return on our replicating portfolio, was a 2 basis point drag on our margin and consistent with our previous guidance. Looking ahead, we see a further 1 basis point impact from this element of the margin movement to come through in 2018, after which it will be largely neutralised. This profile is based upon forward interest rates implied by the yield curve.

The outlook for NIM, as always, is hard to predict. There are a number of variables that make forecasting the forward profile difficult, so we won't be providing guidance for overall NIM. However, we can provide some detail of the known or measurable elements that might make your own assessment of the forward profile somewhat easier.

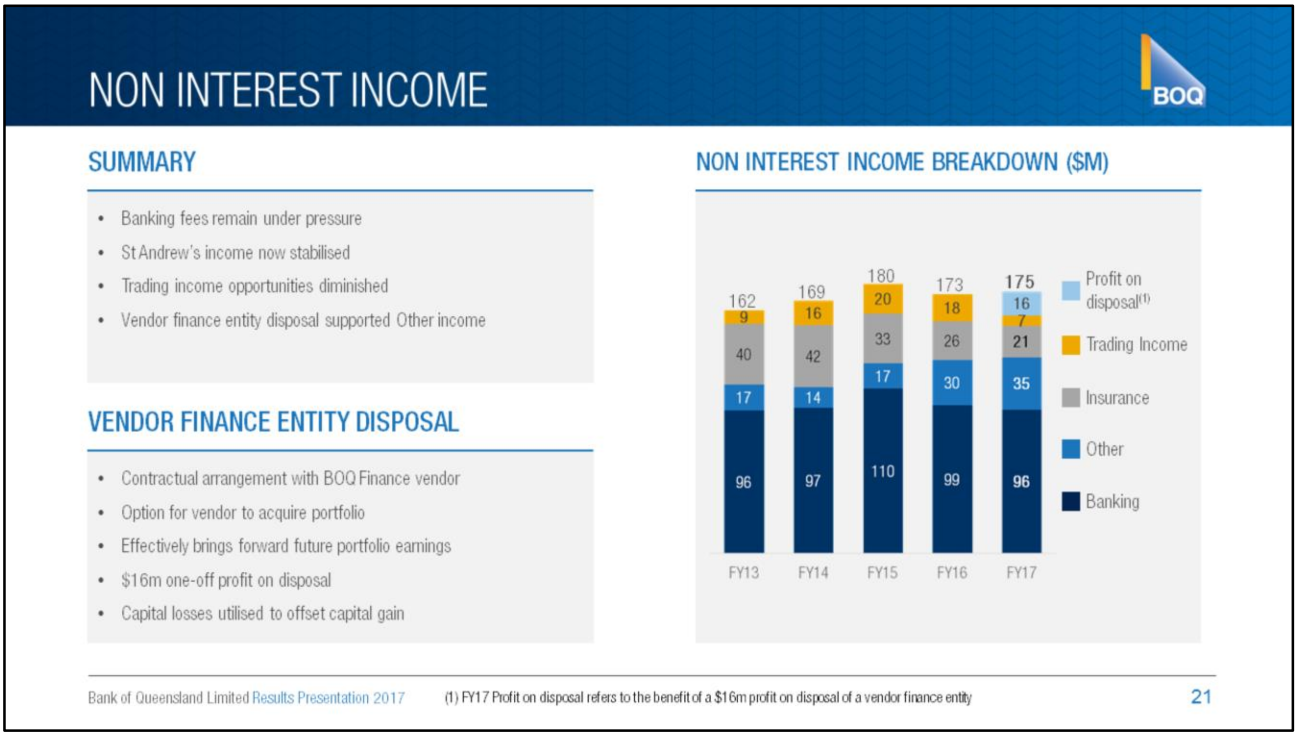
Looking at the half ahead…
The impact of repricing actions that have been taken to date will benefit the first half 2018 margin by around 5 basis points.

We would expect the front to back book margin impact to continue. We are also closely watching the level of competition in owner occupier principal and interest lending as well as the level of switching of our customers from interest only to principal and interest.

I've mentioned that we expect a further margin contraction caused by the capital and low cost deposit portfolio in 2018. We expect this to about half a basis point each half. We do, however, expect some benefit from hedging costs of about one basis point. Hedging costs have reduced. New hedges are being set at lower rates compared to those that have rolled off.

Now, the last large remaining element of the profile is funding costs and mix. That is a very dynamic item. The last half saw an improvement of 5 basis points. We think that level of improvement would be unlikely to be repeated in the next six months. However, as we sit here today, and if current dynamics remain, we would expect this to be a positive contributor to margin in the first half.

Lastly, we've also shown on this slide the impact of the netting of mortgage offset balances against interest earning assets in calculating net interest margin. This calculation methodology has emerged over recent periods as an industry standard. The impact of this is a six basis point difference in the calculation. We will commence reporting margin on this basis from 2018.




Moving to Non Interest Income on slide 21.

Although the headline result was fairly stable for this line, the 2017 result was supported by the 16 million dollar profit on disposal of the vendor finance entity that I mentioned earlier.

This transaction arose from a contractual arrangement with one of our BOQ Finance vendor finance partners. We had established a special purpose vehicle in 2015 to provide finance to the vendor's customers. The vendor partner had the option to acquire the financing entity and chose to exercise its option in the latest half.

I'll also reiterate that given we had some capital losses that were unrecognised, we were able to eliminate tax on the disposal profit. This is why we have a lower tax rate this year compared to more recent periods.

If we strip out the 16 million dollars, it was another tough year for this line, with reductions across most categories. Banking fees continue to reduce as customers opt for no or low fee products.

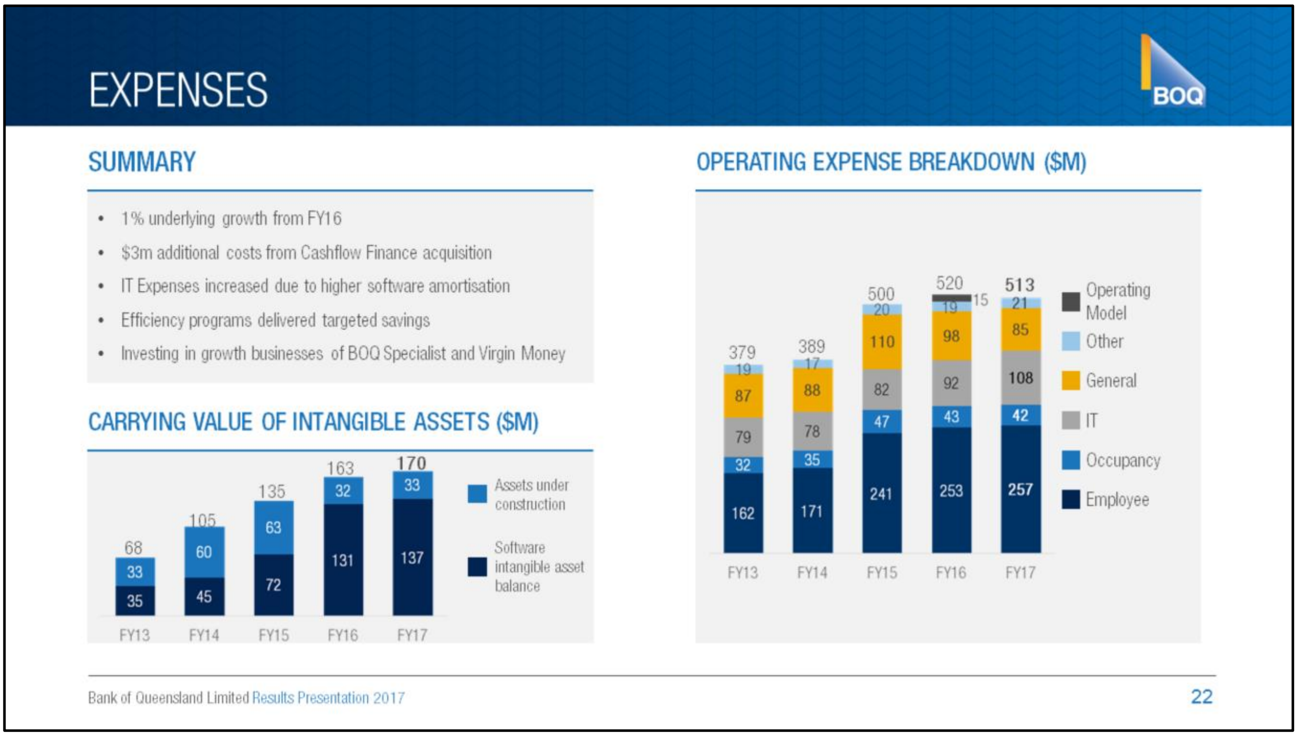
St Andrew's contribution reduced on the prior year, but the past three halves have stabilised at 10 to 11 million dollars per half.

Meanwhile, opportunities to generate trading income have also reduced significantly.

We expect the impact on the Bank’s owned ATM network, following recent industry fee changes, to be a further one and a half million dollar headwind in the 2018 financial year.

On the positive side, we are seeing some growth in our financial markets customer revenues, which we expect to continue, with further investment in the product suite and a digital delivery platform to be released over the coming year. And we have seen solid growth in our Virgin Money third party distribution business.

While we continue to explore all avenues to generate additional income, it’s fair to say that it will remain difficult to maintain non interest income averaging around 80 million dollars per half, but that’s what we’ll be aiming to do.

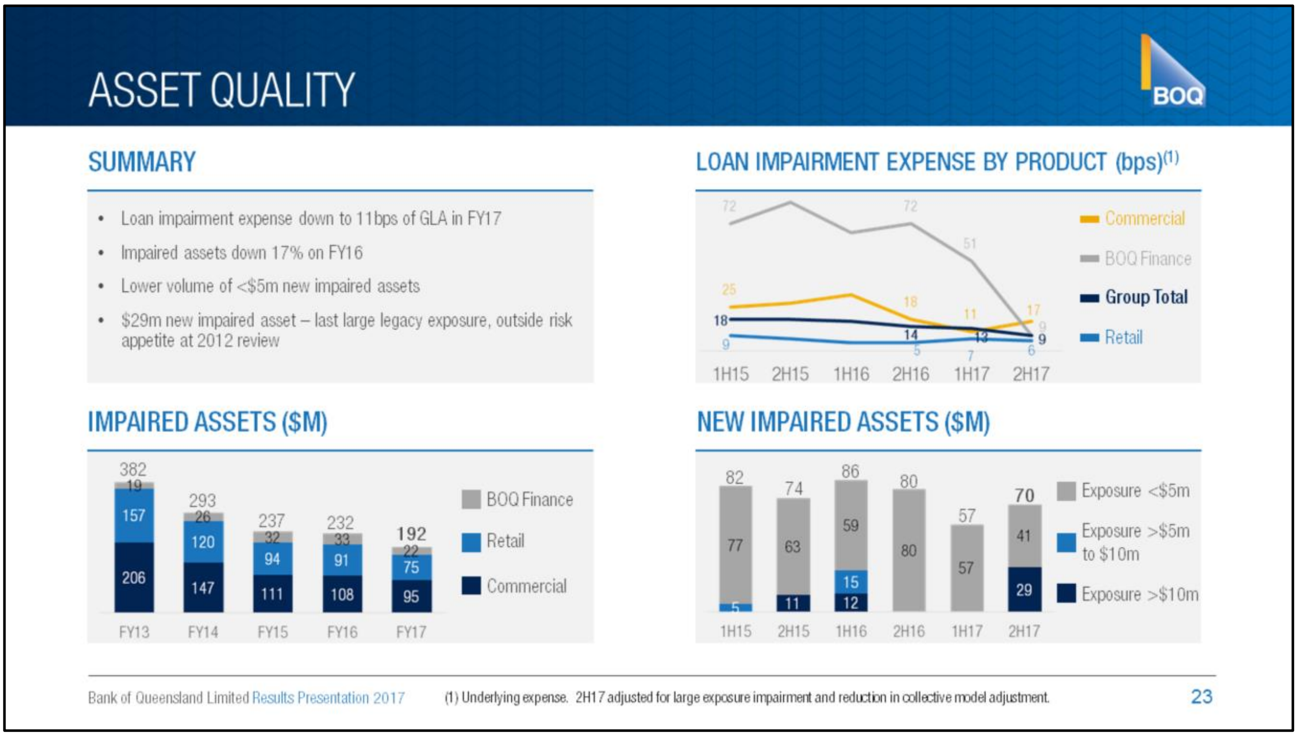



Shifting to expenses on slide 22 and we've been pleased with this result.

We've delivered the savings we needed to keep our underlying cost growth to 1 per cent this year. We've also achieved this while absorbing higher IT software amortisation and a full-year impact from the the roll-out of the Virgin Money mortgage product.

The Cashflow Finance business we acquired during the year added 3 million dollars to our operating expense base, which we would expect to be 4 million dollars on a full-year basis in 2018.

We continue to target a sub-inflation growth profile, while continuing to invest in transformation and supporting our growth businesses. We believe we can achieve this by delivering on our continuous improvement focus and harvesting the benefits of the transformation initiatives we are implementing.




Looking now at asset quality. I'm now on slide 23. This is a very pleasing story.

Loan impairment expense was down 28 per cent on the prior year, with reductions across all portfolios. Total impaired assets and the emergence of new impaired assets also decreased from 2016.

The housing portfolio continues to benefit from the record low interest rate environment and a strong residential property market.

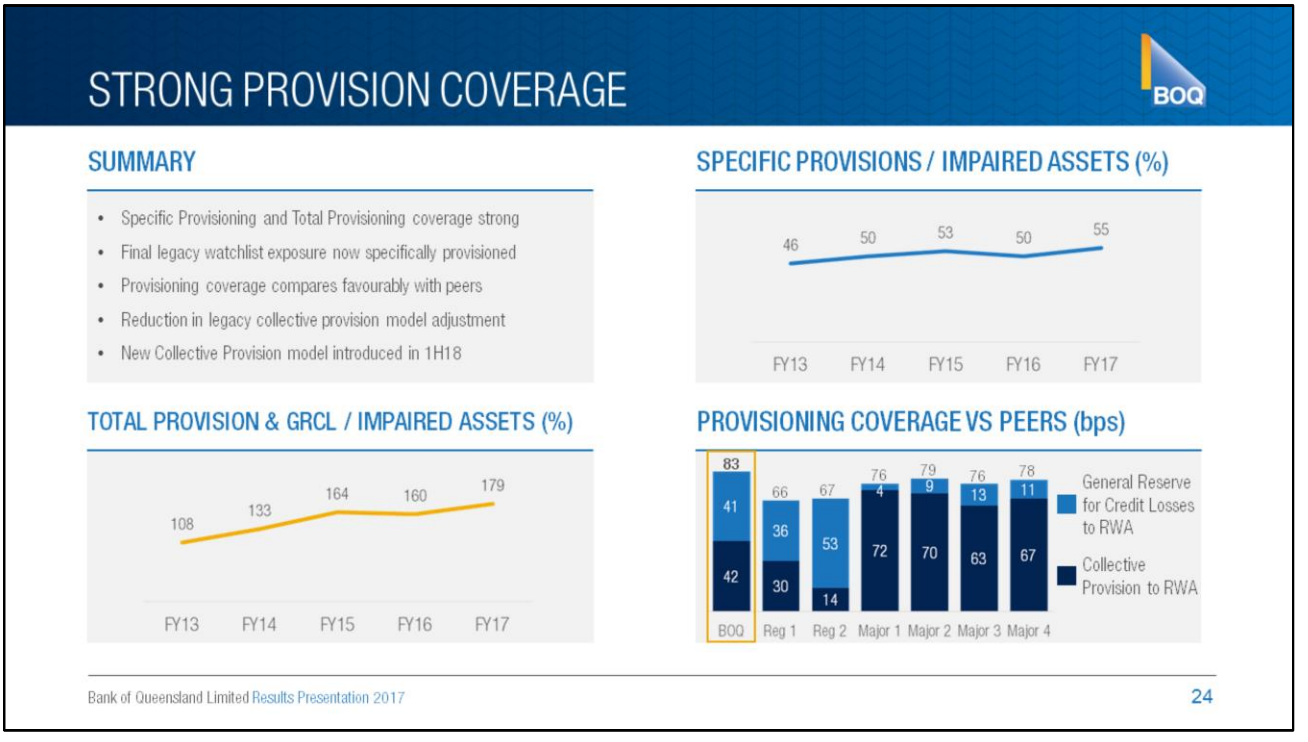
The BOQ Finance portfolio delivered an exceptionally strong second half result of just 2 million dollars. That represented 9 basis points of losses on that portfolio. We would not expect this to be sustainable. We believe this segment of the market should see 'through the cycle' loss experience of around 70 basis points. However, the very strong arrears performance in that portfolio, which I'll cover later, suggests there are no indicators it will return to those levels in the immediate term.

The commercial portfolio included one new impairment of an exposure greater than $10m. This exposure relates to a large Central Queensland property developer and investor totalling 29 million dollars. It was previously identified as outside of risk appetite under the revised settings established in 2012. It was being actively managed, with limited options for refinance, but moved to default in the half. Deterioration in collateral asset values in Central Queensland has resulted in a specific provision charge of 16 million dollars for this exposure.

In 2012, there was a significant portfolio of larger exposures identified as outside of risk appetite. At that time, a collective provision model adjustment was established which has been maintained without change until this half. This new Central Queensland impairment is the last remaining large exposure from the portfolio identified in 2012.

As a result, the collective provision model adjustment has been reduced accordingly. This had a 14 million dollar impact in the half.

The portfolio impairment data on the chart at the top right of this slide adjusts for these two items to provide a better view of underlying portfolio performance.

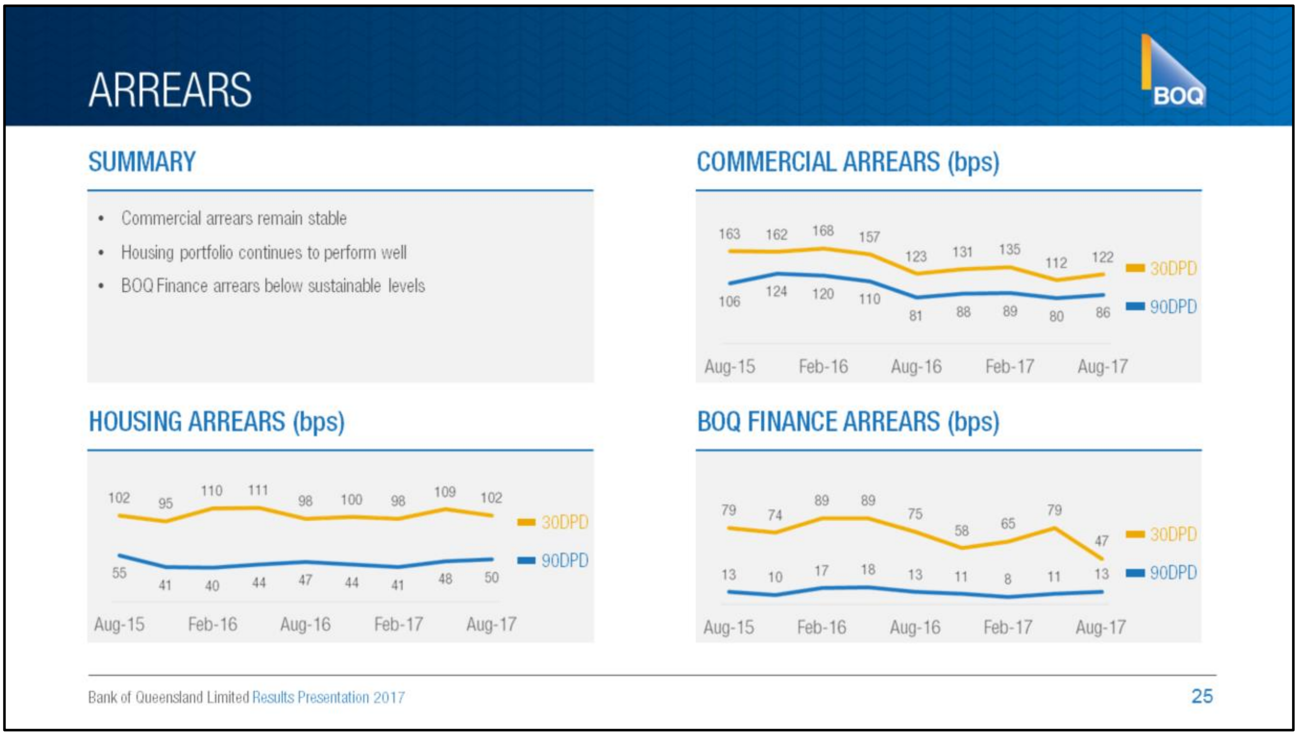



Although provisions reduced during the year, this was in line with improvements in credit quality metrics across the portfolio.

The Bank has been building a new collective provision model. The new model is in the final stages of validation and is expected to be adopted in the first half of 2018. The new model has been designed to address the requirements of IFRS 9 that is scheduled for adoption in the 2019 financial year. The introduction of the new model is not expected to have a material impact on collective provisions.

However, we do expect a likely reduction in the current level of general reserve for credit losses, the impact of which, I'll discuss shortly.

Our provisioning coverage continues to compare favourably with our peers when looking at collective provisions and general reserve for credit losses, relative to risk weighted assets.

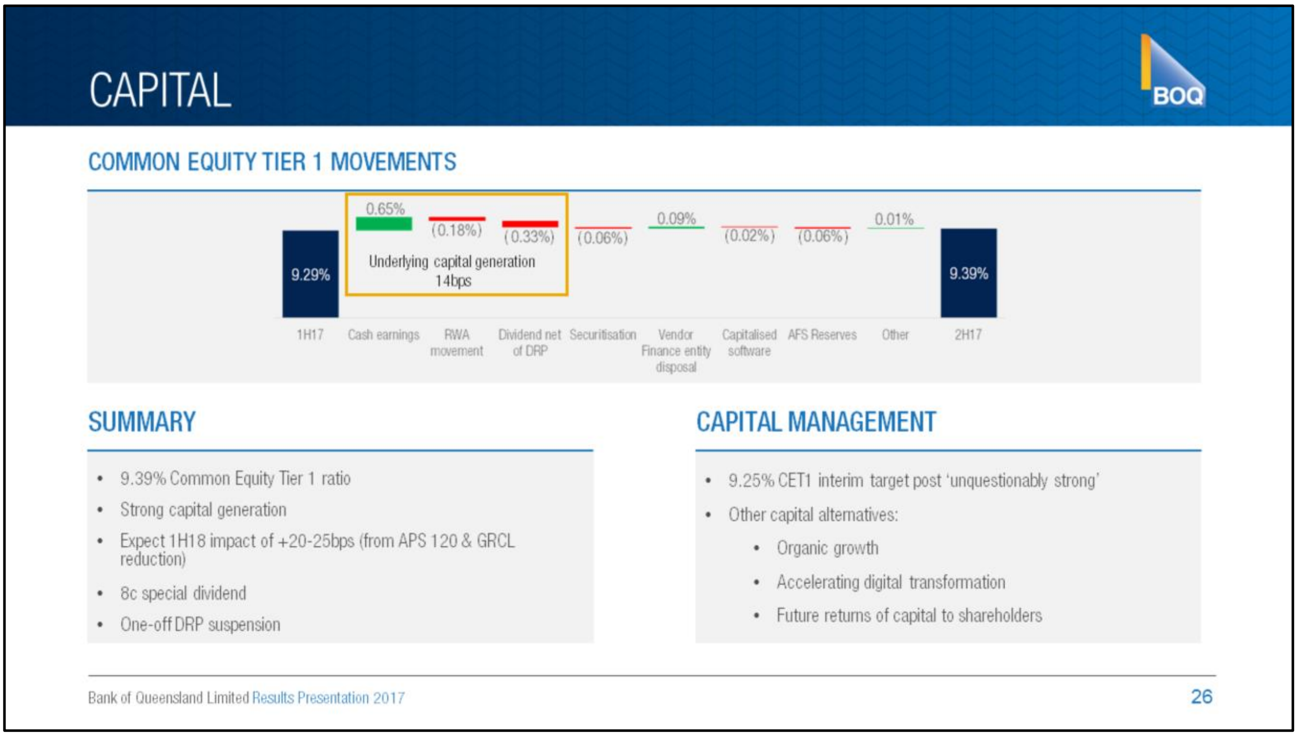



Looking at arrears, and all portfolios have performed very well.

In the housing book, 90-day arrears increased 9 basis points over the half and 3 basis points for the full year. We have seen some impact of continued softening in the Central Queensland economy, as well as a delayed effect of Cyclone Debbie in Queensland.

Commercial arrears continue to track at solid levels with no areas of concentrated stress evident.

BOQ Finance 30-day arrears have reduced significantly and at 47 basis points is at the lowest level we've seen for the last 6 years.  This is a direct leading indicator of near term impairment expense in this portfolio and points to a continuation of the low loss rates we've experienced.  But I will reiterate, we don't expect this level to be sustainable over the longer term.




Moving to capital on slide 26.

Our underlying capital generation was 14 basis points in the second half, which helped to boost our Common Equity Tier 1 ratio to 9.39 per cent.

There are 2 impacts expected in the first half of FY18 that will further improve the Common Equity Tier 1 ratio by 20 to 25 basis points.

The largest impact relates to changes being introduced to APRA's APS120 Securitisation standard that will be effective on 1 January 2018. For some time we have had higher average risk weights on our mortgage portfolio than some of our competitors. It appears as though we were applying a more conservative approach to our risk weighting calculations, albeit we did confirm with the regulator that we have been applying the technically correct approach. Changes being introduced to the standard will allow for more of our mortgages to qualify for concessional risk weighting treatment. Our ratios will now better align with our peers.

The remaining impact relates to an expected reduction in the general reserve for credit losses when the new collective provision model is implemented that I covered earlier.

We have been pleased with the clarity provided by APRA's guidance on unquestionably strong in July this year. Although there is still some uncertainty around the risk weighting framework, we believe it is appropriate that a conservative capital profile is maintained. Whilst it may be possible to target a lower capital level when the rules are finally clear, it may take some time to ensure all stakeholders are completely comfortable with a fully optimised target, given the headline ratios of the advanced banks.

In the interim, we believe a common equity tier 1 ratio of 9.25 per cent is appropriate.

In light of this, the Board has announced the special dividend and the suspension of the DRP for this dividend payment cycle. That equates to an impact of approximately 27 basis points, compared to not announcing those steps.

That leaves some additional excess capital that, together with our current profile of capital generation, provides optionality for us to consider how best that can be deployed for long term value creation.

It obviously provides some capacity to grow faster than we have been, but we will remain conscious of the return impact of using price to drive that outcome.

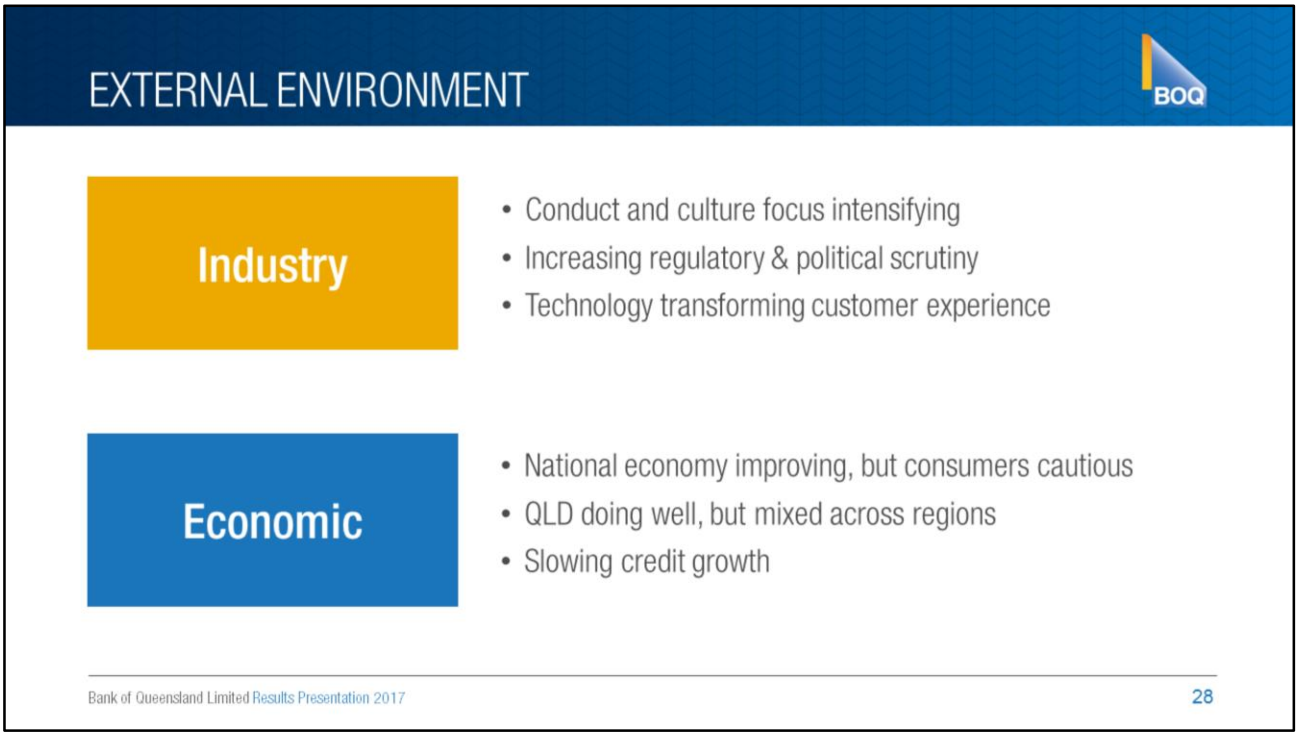
We are currently considering options for using some of that capital to accelerate our transformation and achieving digital parity in our customer fulfilment offerings. There is more for us to consider and if, or when, any decision is made, we would update the market accordingly.

Lastly, if we can't find appropriate opportunities to deploy capital excess to our target, it will be returned to shareholders.

With that, I'll hand back to Jon.

# Summary & Outlook

Jon Sutton
Managing Director & CEO




There is no doubt that the environment we are operating in is changing rapidly. Regulatory, legislative and political pressures require banks to be more focused and nimble than ever before.

Customers also expect more from their banks, particularly in terms of trust.

At BOQ, we take the issues of culture and conduct very seriously. We took a leadership position in signing up to the Banking and Finance Oath, established an Ethics Committee in 2015 and have completed the roll out of ethics training to senior staff and owner managers.

While the Financial System Inquiry made a number of positive recommendations, the playing field is still tilted in favour of the major banks. More needs to be done in this regard. Before any new regulations are introduced, greater consideration should be given to the impacts on smaller banks.

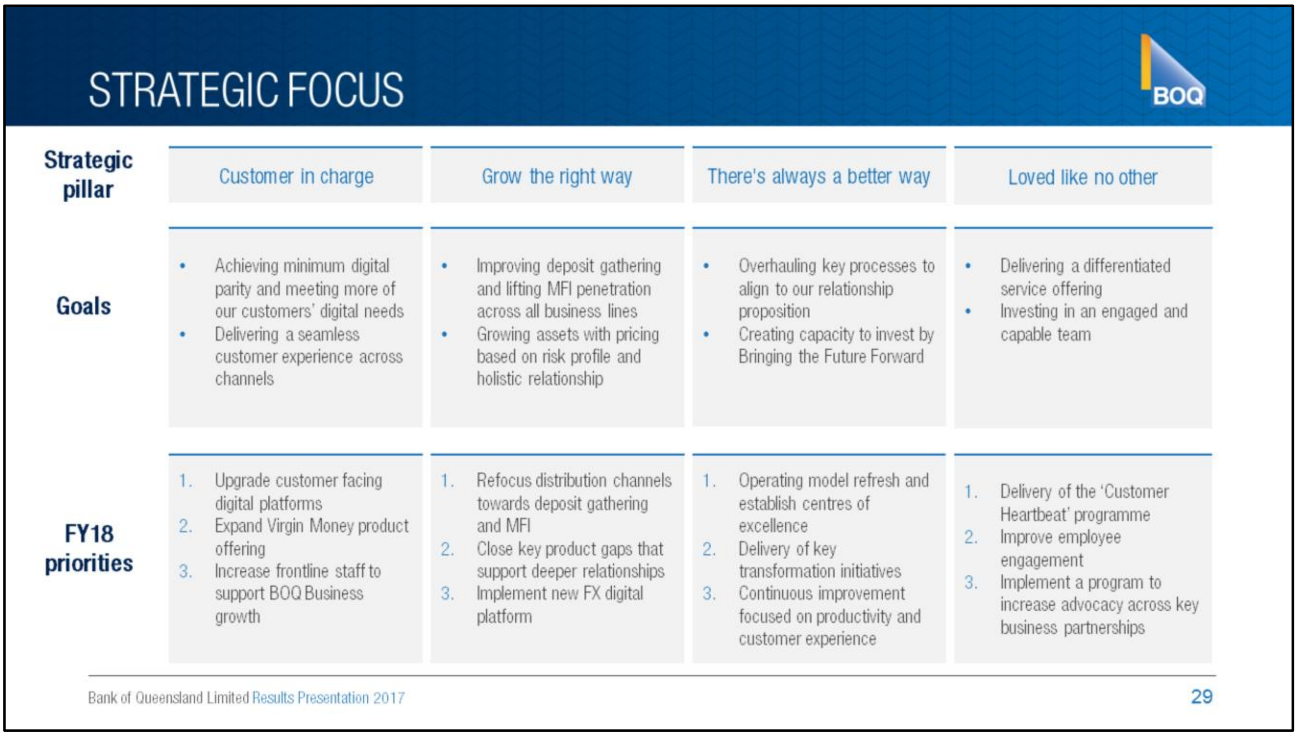
Meanwhile, technology development continues to move at pace, and with it customer expectations. For a bank to remain relevant in this environment, ongoing investment is required.

The economy is improving, albeit mixed. Business confidence is high, and jobs growth has been strong. With the unemployment rate around its decade average and interest rates low, loan losses have been minimal. But the consumer has been weighed down by stagnant wage growth, rising utility prices and high underemployment.

In Queensland, the South-East is performing well. Agriculture and tourism continue to support the state. Central Queensland is still doing it tough in its larger regional centres. Overall, though, we are positive about the outlook for the Queensland economy.

Given concerns about the housing market, particularly in Sydney and Melbourne, regulatory limits have been imposed to curb lending to higher risk segments. This is expected to have the effect of slowing credit growth across the economy. It has also meant that lenders are adjusting their rates and credit settings on a daily basis to manage volumes, margins and regulatory requirements.

We do see a more favourable set of operating conditions for our business bank, where opportunities have improved from 12 months ago. Our niche business areas of corporate healthcare & retirement living, medical, agribusiness, hospitality and tourism all have good momentum. Our leasing business provides valuable insights into the SME market and we are seeing growing momentum.




Turning to slide 30 and our strategy.

We remain committed to our strategy of targeting niche customer segments that value a more intimate relationship. The four pillars of our strategy remain relevant and unchanged.

Under the customer in charge pillar, we are seeking to achieve digital parity and deliver a seamless experience to our customers across channels. Our success in this pillar will be measured by the delivery of enhanced digital customer platforms.

We will focus on growing the right way by improving our deposit gathering capability and increasing our main bank relationships.  We will price for risk while considering the broader relationship with our customers.  Our MFI customer growth will be a key indicator of success for this pillar.

We continue to look for improvement in all our processes, removing friction points, with the aim of ensuring quicker time to yes to all of our customers.  To this end, we are targeting sub-inflation operating expense growth, while still investing to grow our businesses.

We remain committed to proving it's possible to love a bank.  We will demonstrate this by our continued focus on our customers and the value we can create for them.  This is a people business and to support our vision we are rolling out a Customer Heartbeat program across the group.  The purpose of this program is to ensure we consistently meet our customers expectations, through a unified service mission.

A key driver of our future success will be the delivery of our digital transformation. Initiatives we have in the pipeline include a new web experience platform for BOQ, as well as a new internet banking platform and mobile app.

Success on these initiatives will bring the bank closer to its customers.  Additional services will be provided that we have not had in the past, such as direct online foreign exchange. We do see good growth opportunities in our business bank.

We will continue to report back on our progress.


In summary, our niche strategy is delivering.

Our distribution channels of Virgin Money, brokers, BOQ Specialist and the branch network give us greater reach than we have had before.

We are cautious around the housing loan market, given that system growth is likely to slow. But, we are rolling out a range of initiatives that will improve the way we do business and serve our customers.

Our business bank has had an excellent second half. This has continued into the new financial year with a strong pipeline and settlements.

Our strong capital position provides optionality for long term shareholder value creation.

We have delivered a sound result at the same time as making significant progress on transforming the business.

While there is more for us to do, we are laying the right foundations for sustainable outperformance in the future.

Thank you and now I will hand back to Tanny to moderate the Q&A.

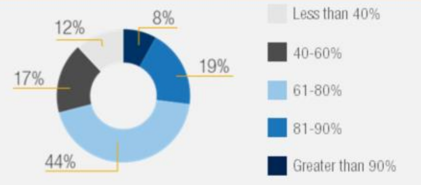
# Appendices

# HOUSING PORTFOLIO

## SUMMARY

- Broker settlements increased to 28% including Virgin Money
- Interest only settlements trending to less than 30%
- Room for growth under 10% investor cap

## HOUSING PORTFOLIO LVR BANDS




## PORTFOLIO METRICS

| Metrics (%) | 2H16 | 1H17 | 2H17 |
|---|---|---|---|
| Owner occupied | 58 | 59 | 59 |
| Investment | 42 | 41 | 41 |
| Interest only | 40 | 39 | 37 |
| Broker originated[1] | 8 | 9 | 11 |
| Weighted avg LVR | 67 | 67 | 67 |
| Line of Credit | 9 | 8 | 8 |
| Avg loan balance | $262k | $265k | $269k |
| Variable rate | 75 | 74 | 72 |
| Fixed rate | 25 | 26 | 28 |

## SETTLEMENT METRICS

| Metrics (%) | 2H16 | 1H17 | 2H17 |
|---|---|---|---|
| Owner occupied | 59 | 70 | 63 |
| Investment | 41 | 30 | 37 |
| Interest only | 39 | 35 | 31 |
| Broker originated[1] | 15 | 15 | 28 |
| Weighted avg LVR | 67 | 67 | 69 |
| Line of Credit | 3 | 2 | 1 |
| Avg loan balance | $376k | $370k | $381k |
| Variable rate | 69 | 72 | 72 |
| Fixed rate | 31 | 28 | 28 |

(1) Includes Virgin Money home loans

# EXPOSURE TO HIGH RISK SECTORS

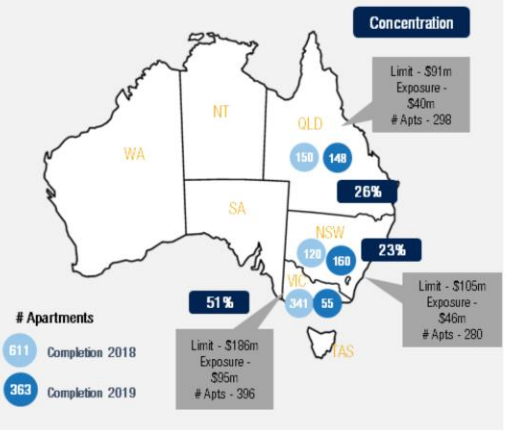
## APARTMENT CONSTRUCTION EXPOSURES[1]

- $181m current exposure to residential construction
- 28 developments across 3 states, completing 2018 through 2019
- Well diversified intra-state

## OTHER HIGHER RISK SECTORS

- No material regional housing exposures
- No systemic issues emerging
- Direct mining industry exposure ~$100m

## LENDING TO RESIDENTIAL APARTMENT CONSTRUCTION






(1) Projects over $5m. Data as at 31 August 2017

# ABBREVIATIONS

1H: First half of financial year
2H: Second half of financial year
30DPD: 30 days past due
90DPD: 90 days past due
ADI: Authorised Deposit-taking Institution
ALM: Asset & Liability Management
APRA: Australian Prudential Regulation Authority
APS: ADI Prudential Standards
Apts: Apartments
Avg: Average
BDD: Bad & Doubtful Debt Expense
bps: basis points
CET1: Common Equity Tier 1
cps: Cents per share
CPS: Convertible Preference Shares
CTI: Cost-to-income ratio
DPD: Days past due
DRP: Dividend Reinvestment Plan
EPS: Earnings per share
FX: Foreign exchange
FY: Financial year
GLA: Gross Loans & Advances
GRCL: General Reserve for Credit Losses
KPI: Key performance indicator
LCD: Low cost deposit
LOC: Line of Credit
LVR: Loan to valuation ratio
MFI: Main Financial Institution
NIM: Net Interest Margin
OMB: Owner Managed Branch
RBA: Reserve Bank of Australia
ROE: Return on equity
ROTE: Return on tangible equity
SME: Small and Medium Enterprises
TD: Term deposit
VMA: Virgin Money Australia

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