Moody's INVESTORS SERVICE

CREDIT OPINION
31 August 2023

Update

Send Your Feedback

RATINGS

Australia and New Zealand Banking Grp. Ltd.

Domicile	Melbourne, Victoria, Australia
Long Term CRR	Aa2
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	Aa3
Type	Senior Unsecured - Fgn Curr
Outlook	Stable
Long Term Deposit	Aa3
Type	LT Bank Deposits - Fgn Curr
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

Contacts

Letitia Wong +61.2.9270.8128
Associate Analyst
letitia.wong@moodys.com

Patrick Winsbury +61.2.9270.8183
Associate Managing Director
patrick.winsbury@moodys.com

Australia and New Zealand Banking Grp. Ltd.

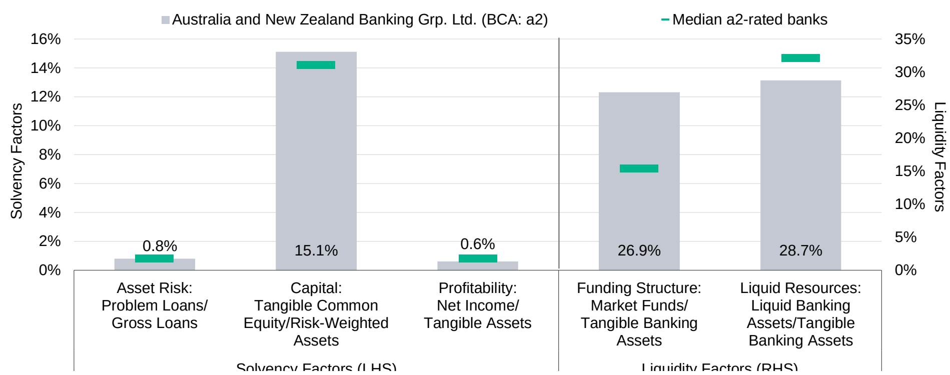
Update to credit analysis

Summary

The Aa3 senior unsecured debt and deposit ratings of Australia & New Zealand Banking Group Limited (ANZ) reflect the group's strong capital levels, robust asset quality and a sound funding and liquidity position. ANZ's Aa3 rating incorporates two notches of uplift from ANZ's standalone financial strength of a2, in recognition of the bank's systemic importance and the traditionally supportive approach of Australia's bank supervisors.

We expect a moderate deterioration in asset quality over the next 12 months as high inflation and high interest rates may put households and businesses under financial strain. Despite a slowdown in system deposit growth and the maturity of central bank funding in 2023-2024, ANZ's funding and liquidity position remain sound and is supported by its good access to a well-diversified range of funding sources.

Exhibit 1
Rating Scorecard - Key Financial Ratios



Source: Moody's Financial Metrics

Credit strengths

» High levels of capital.

» Very high levels of loss absorbing reserves.

» Funding and liquidity position is strong, with additional support from the Reserve Bank of Australia.

Credit challenges

» Asset quality may deteriorate as rising interest rates and high inflation leads to a rise in loan delinquencies, albeit from very low levels.

» Underlying revenue growth expected to be constrained by competition and slowing credit growth.

Rating outlook

The outlook on ANZ's ratings is stable. Despite an uncertain outlook as the economy recovers from the pandemic amid inflationary pressures, these risks are partly mitigated by the bank's resilient balance sheet settings.

Factors that could lead to an upgrade

» Problem loans ratio (measured as Stage 3 loans as a % of gross loans and advances) falls to below 0.5%.

» Moody's capital ratio (measured as tangible common equity as a % of RWA) increases to above 16%.

Factors that could lead to a downgrade

» Return on assets, as measured by Moody's, falls to 0.5%.

» Problem loans ratio (measured as Stage 3 loans as a % of gross loans and advances) rise to above 1.8%.

» An increase in the level of wholesale funding such that market funds as a % of tangible banking assets rises to 40%.

Key indicators

Exhibit 2

Australia and New Zealand Banking Grp. Ltd. (Consolidated Financials) [1]

	03-23[2]	09-22[2]	09-21[2]	09-20[2]	09-19[2]	CAGR/Avg.[3]
Total Assets (AUD Million)	1,069,053.9	1,002,323.0	943,391.0	907,848.0	860,542.0	6.4[4]
Total Assets (USD Million)	716,001.0	644,443.9	681,458.7	650,698.5	580,392.4	6.2[4]
Tangible Common Equity (AUD Million)	65,876.0	64,765.8	58,924.0	55,562.0	54,998.0	5.3[4]
Tangible Common Equity (USD Million)	44,120.6	41,641.2	42,563.8	39,824.0	37,093.4	5.1[4]
Problem Loans / Gross Loans (%)	0.6	0.6	0.8	1.1	1.1	0.9[5]
Tangible Common Equity / Risk Weighted Assets (%)	15.1	14.2	14.2	12.9	13.2	13.9[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	6.0	6.4	8.4	11.6	11.4	8.8[5]
Net Interest Margin (%)	1.7	1.6	1.6	1.6	1.7	1.6[5]
PPI / Average RWA (%)	2.3	2.2	2.1	2.1	2.3	2.2[6]
Net Income / Tangible Assets (%)	0.7	0.7	0.7	0.4	0.7	0.6[5]
Cost / Income Ratio (%)	49.6	50.4	50.4	51.3	49.3	50.2[5]
Market Funds / Tangible Banking Assets (%)	28.4	26.9	25.7	27.6	28.8	27.5[5]
Liquid Banking Assets / Tangible Banking Assets (%)	24.0	28.7	29.8	28.1	24.2	27.0[5]
Gross Loans / Due to Customers (%)	106.6	108.6	106.6	112.5	120.8	111.0[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.

Sources: Moody's Investors Service and company filings

Profile

The Australia and New Zealand Banking Group Limited (ANZ) is the fourth-largest bank in Australia in terms of total deposits and loans, with a market share of 13% each as at 31 May 2023. The bank had a consolidated asset base of AUD1,112 billion as of 31 March 2023.

ANZ provides a range of financial products and services, including retail, commercial and private banking to retail, small business, corporate and institutional clients. ANZ's primary markets are Australia and New Zealand, supplemented with Institutional banking services across Asia-Pacific, Europe, America and the Middle East.

Please refer to the Issuer Profile to read more about ANZ, and the Australian Banking System Profile to read about the Australian banking system.

Detailed credit considerations

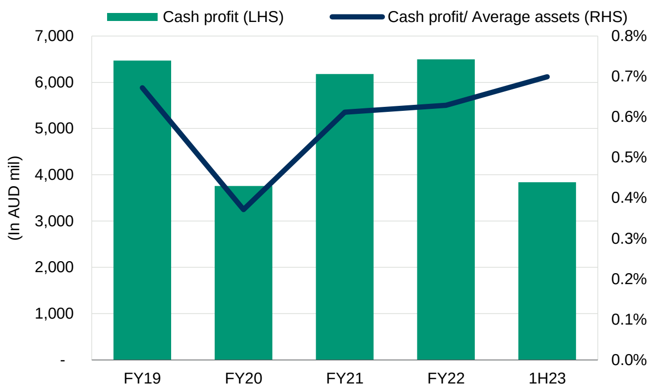
Profitability underpinned by rising interest rates and increased lending volumes

ANZ's cash profit rose 24% to AUD3.8 billion for first-half 2023 compared with the prior corresponding period, growth was broad based across all four core businesses from volume and margin expansion. The two biggest profit contributing segments, institutional and retail reported a 97% and 10% growth in cash profits respectively.
The group's reported net interset margin (NIM) on a cash basis rose to 1.75% for 1H 2023, up 7 basis points (bps) compared with 2H 2022 and up 17 bps compared with 1H 2022, as the spread between lending and deposit rates widen along with gains from its replicating portfolio. NIM is expected to have peaked for Australia Retail due to heightened competition in both the mortgage frontbook and backbook as banks offered aggressive discounts to retain existing customers, rising funding costs will squeeze margins as depositors shift back towards higher-yielding term deposits. However, ANZ's business structures offers geographic and product diversification benefits, strong momentum in its Institutional ex-Markets and International businesses will help offset some margin headwinds in the Australia and New Zealand residential mortgage market.

ANZ had net releases on its specific provision, but that was more than offset by much larger collective provision charges, it took a credit impairment charge of AUD133 million for 1H 2023, this compared with AUD87 million of provisions writeback in the previous corresponding period. The potential normalization of credit costs, given elevated asset risks, could limit further improvements in earnings during the second half.

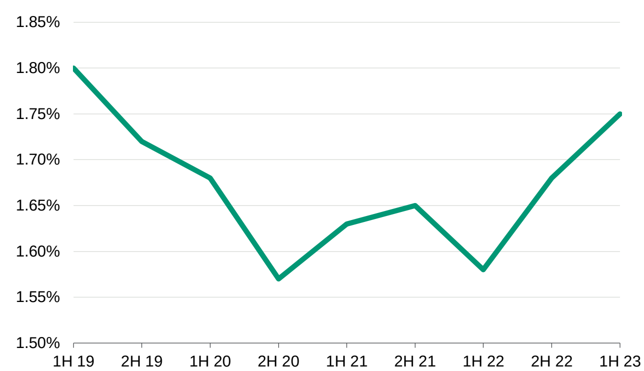
We expect earnings to be directly impacted by rising inflation through higher operating expenses. The bank's operating expenses was up 4% in 1H23 from the prior corresponding period, driven by personnel expenses and technology investment spend, which was partially offset by benefits from simplified network infrastructure and reduction in regulatory and compliance related costs.

Exhibit 3
Profitability supported by margin expansion and volume growth



Cash profit/ Average assets for 1H23 is annualized.
Source: Bank disclosures, Moody's Investors Service

Exhibit 4
Rising interest rate boosted margins



Source: Bank disclosures, Moody's Investors Service

Strong balance sheet fundamentals and conservative underwriting to withstand rising asset risks

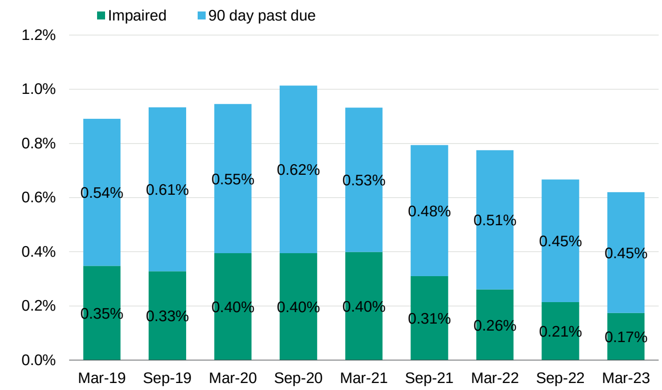
Non-performing loans, classified as Stage 3 under the accounting standards, fell 15bps to 0.6% as of March 2023 from a year earlier (Exhibit 5), following the end of pandemic-related restrictions and a rebound in economic activities.

We expect a pick up in loan delinquencies in the next 18 months from the current low base as persistently high inflation and the resultant high interest rate constrain household finances. In particular, 22% of Australian mortgage borrowers are on fixed rate as of March 2023, they will face a repayment shock when they reprice onto higher variable mortgage rates in the second half of 2023 and 2024. That said, we believe the uptick in home loan arrears will be modest given strengthening in household savings during the pandemic and a still strong labour market, the proportion of the bank's borrowers ahead of mortgage repayments remained largely stable at 70%. In addition, ANZ has been tightening its underwriting standard in recent years, the average dynamic loan-to-value ratio (including offset) across its home loan portfolio reduced to 43% in 1H 2023 from 49% two years ago.

Business loan arrears will come under greater stress as households cut down on discretionary spending in response to higher living costs and mortgage repayments. Small and medium enterprises (SME), construction and retail sectors are likely to be vulnerable as economic conditions weaken, although ANZ's exposures to these sectors is relatively small.

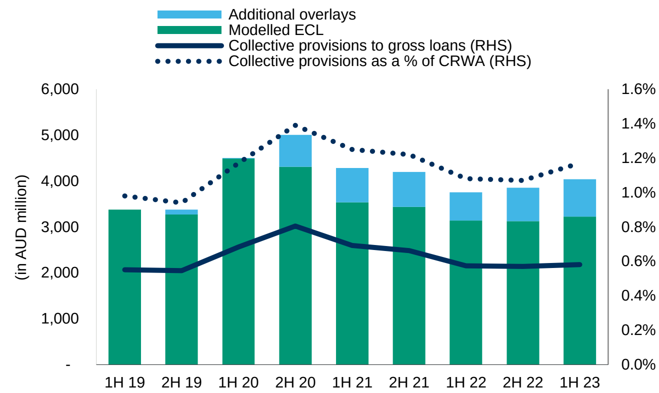
Despite these risks, the bank's healthy levels of loan loss provisions and solid capital position make it well placed to absorb potential increases in credit losses. Its provisioning coverage ratio measured as collective provisions as a share of credit risk-weighted assets remains elevated above pre-pandemic levels at 1.17% as of March 2023, providing a strong buffer against credit losses.

Exhibit 5
Problem loans have fallen



The data refers to that of ANZ Group Holdings Limited
Source: Bank disclosures, Moody's Investors Service

Exhibit 6
Collective provisions remain elevated than pre-pandemic period



Source: Bank disclosures, Moody's Investors Service

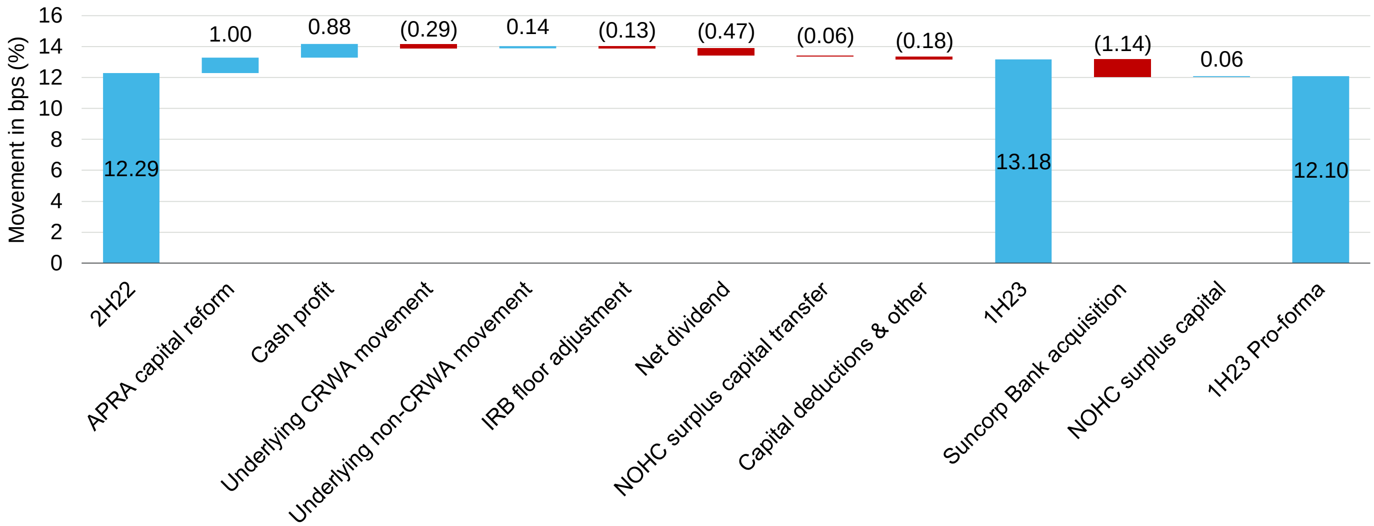
Capital position remains strong as new capital rules come into effect

ANZ's capitalization remains strong, the bank's Level 2 Common Equity Tier 1 (CET1) ratio rose 89 bps to 13.18% during the March 2023 half. The implementation of the regulator's revised capital framework at the start of 2023 lifted the CET1 ratio by 100 bps because of a reduction in credit risk-weighted assets mainly from the bank's institutional book. High cash earnings also contributed to the increase in the ratio, but this is partially offset by dividend payout and robust lending growth. ANZ also reported lower non-credit risk weighted assets and lower interest risk in the banking book (IRRBB) risk-weighted assets, the latter declining by AUD6.2bn.

The CET1 ratio of 13.18% included AUD3.5 billion equity raised to partially fund the potential acquisition of Suncorp-Metway Limited (SML, A1/A1 Ratings under review, baa1) and the surplus capital in Non-operating Holding Company (NOHC), the ratio would come down to 12.1% on a pro-forma basis excluding these adjustments. We expect ANZ to continue to operate above APRA's new benchmark of 10.25%.

Australian regulatory capital ratios are calculated on a conservative basis, understating their risk absorption capacity relative to Basel requirements. Fair value movements in trading and investment securities are refected in CET1 capital either through retained earnings or through equity reserves. Investment securities accounted for on an amortised cost basis, where fair value movements are not refected, are immaterial in size. Credit risk weights are higher than Basel requirements on a wide range of assets, while Australia is the only country to include interest rate risk in the banking book as a Pillar 1 capital requirement. As such, Australia's largest banks hold capital against the risk of losses due to interest rate movements.

Exhibit 7
Capitalization remains solid
Movement in CET1 ratio



Source: Bank disclosures, Moody's Investors Service

Funding and liquidity profile continues to benefit from pandemic stimulus

Australian banks have benefitted from the surge in system deposits as supported by significant government stimulus during the pandemic. ANZ's funding profile has improved with its use of deposits rising to 56% of total funding sources as at 31 March 2023. Customer deposits grew 8% in 1H 2023 compared with a year ago, outstripping the 6% loan growth, although we expect deposit growth to moderate in the next 18 months as households grapple with higher cost of living pressure.

Similar to the other Australia's major banks, ANZ has a structural reliance on wholesale funding, with an important offshore component close to 50%. In particular, ANZ has drawn AUD20 billion from the Term Funding Facility (TFF), which is central bank's low-cost funding introduced during the pandemic. While this substantially reduced the need for the bank to access wholesale funding markets, it creates a sizable refinancing task and exposes the bank to market funding conditions when the majority of the funding matures in the second half of 2023 and fiscal 2024. This also comes at a time when investor sentiment is fragile due to the recent stresses at some offshore banks. That said, we expect this refinancing risk to be mitigated by ANZ's strong access to wholesale markets, as well as the diversity of its funding by product, currency and geography. It has proactively pre-funded its maturities and completed 80% of its fiscal 2023 term wholesale funding target by the first half of 2023.

ANZ reported a Net Stable Funding Ratio (NSFR) of 119% as of 31 March 2023 and a half-yearly average Liquidity Coverage Ratio (LCR) of 128%. Regulatory liquidity rules ensure that liquid assets are of a very high quality relative to other banking systems. The banks also have capacity to generate additional central bank repo-eligible assets through self-securitisation of their high-quality residential mortgage books.

Rating is supported by Australia's strong operating environment

Australia's Strong+ Macro Profile reflects the country's robust economic strength, institutions and governance strength, and low susceptibility to event risk. Our baseline scenario projects real GDP growth slowing to 1.5% in 2023 as higher interest rates constrain growth, before improving to 2% in 2024.

The Australian economy has continued to perform strongly after a period of fiscal and monetary stimulus provided to combat the dampening economic effects of the pandemic-related health measures. Very tight labor markets and strong economic growth, boosted by strong household consumption and high levels of public and private investment, have resulted in the unemployment rate falling to very low levels of below 4%. Rising interest rates, in response to high inflation, are likely to temper growth in 2023. High levels of household debt, combined with an increase in debt burden as interest rates rise, are key economic vulnerabilities. Household debt relative to income remained high at 187.8% as of December 2022, and rising interest rates led to national average house prices falling 9.1% from April 2022 to February 2023, although they have since stabilized and increased modestly from the February trough. Further improvement in banks' asset quality is unlikely as rising interest rates could reduce buffers built by borrowers or put some borrowers under financial pressure. However, low unemployment, and low LVRs on home loans and small business loans, which are typically secured by residential properties, should provide buffers against asset-quality risk.

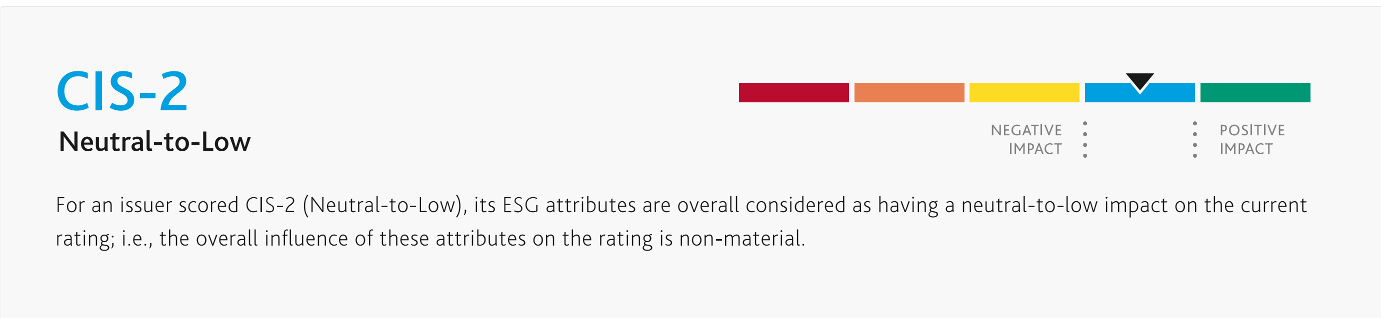
Australian banks' very strong pricing power has historically been supported by the high level of concentration in the banking sector. Net interest margins are expanding as interest rates rise, however, funding costs, will rise as banks begin to repay cheap funding provided by the central bank from 2023 onwards. This could constrain further net interest margin gains in 2023.

Australia's structural reliance on external financing remains a key vulnerability. However, Australian banks have been extending the term structure of their wholesale market funding for a number of years and pre-fund upcoming maturities well in advance.

ESG considerations

Australia and New Zealand Banking Grp. Ltd.'s ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 8
ESG Credit Impact Score



Source: Moody's Investors Service

ANZ's ESG Credit Impact Score is neutral-to-low (**CIS-2**), reflecting the limited credit impact of environmental and social risk factors on the ratings to date, and low governance risks.

Exhibit 9
ESG Issuer Profile Scores

Source: Moody's Investors Service

Environmental

ANZ faces moderate exposure to environmental risks, in line with peers, primarily because of its portfolio exposure to carbon transition risk as a diversified bank. In response, ANZ is actively engaging in developing its climate risk management and reporting frameworks by incorporating environmental considerations in its strategy and lending policies, including policies related to financing of coal-related businesses.

Social

ANZ faces high industrywide social risks from customer relations (regulatory risk, litigation exposure and high compliance standards), and the area of data security and customer privacy. The group also faces industrywide moderate social risks related to societal trends - in particular, digitalization - and the extent to which such measures could hurt earnings. Significant investment places ANZ in a strong position to meet rising digital expectations from customers. While the Australian regulators' focus on mis-selling and misrepresentation have identified weaknesses in some policies and procedures, extensive remedial actions have been taken to address these issues.

Governance

ANZ faces low governance risks. The bank’s risk management, policies and procedures are in line with industry best practices and are suitable for its risk appetite. While the bank has incurred significant charges for customer remediation and regulatory capital add-ons for operational risk, which have hampered our assessment of financial strategy and risk management, significant investment has strengthened the bank’s risk management and controls capabilities.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations

Loss Given Failure Analysis

Australia’s resolution framework is based on contractual loss absorption for capital securities and we currently apply a basic Loss Given Failure approach in rating Australian banks' junior securities.

APRA’s requires domestically systemically important banks (D-SIB) to maintain minimum total loss absorbing capital equivalent to 18.25% of risk weighted assets by 1 January 2026. This can be met through a combination of Common Equity Tier 1 capital (minimum 10.25%) and Additional Tier 1 and Tier 2 capital. Additional Tier 1 and Tier 2 capital securities have contractual bail-in provisions at the point of non-viability. As an interim measure banks are required to have minimum total loss absorbing capital equivalent to 16.75% of risk weighted assets by 1 January 2024.

Government support

Potential for government support remains very high. ANZ's Aa3 global-scale local currency deposit and senior debt ratings incorporate two notches of uplift from the bank's Baseline Credit Assessment of a2, reflecting a very high probability that, as a consequence of its size, it would receive systemic support in case of need.

Counterparty Risk (CR) Assessment

ANZ's CR Assessment is Aa2(cr)/Prime-1(cr)

We consider Australia to be a non-operational resolution (non-ORR) regime. For non-ORR countries, the starting point for the CR assessment is one notch above the bank's Adjusted BCA, to which we then typically add the same notches of government support uplift as applied to deposit and senior unsecured debt ratings.

Counterparty Risk Ratings (CRRs)

ANZ's CRRs are Aa2/P-1

We consider Australia to be a non-operational resolution (non-ORR) regime. For non-ORR countries, the starting point for the CRR is one notch above the bank's Adjusted BCA, to which we then typically add the same notches of government support uplift as applied to deposit and senior unsecured debt ratings.

About Moody's scorecard

Our scorecard is designed to capture, express and explain in summary form our rating committee's judgement. When read in conjunction with our research, a fulsome presentation of our judgement is expressed. As a result, the output of our scorecard may materially differ from that suggested by raw data alone (though it has been calibrated to avoid the frequent need for strong divergence). The scorecard output and the individual scores are discussed in rating committees, and may be adjusted up or down to reflect conditions specific to each rated entity.

Rating methodology and scorecard factors

Exhibit 10

Australia and New Zealand Banking Grp. Ltd.

Macro Factors							
Weighted Macro Profile	**Strong +**	**100%**					

Factor	Historic Ratio	Initial Score	Expected Trend	Assigned Score	Key driver #1	Key driver #2
Solvency						
Asset Risk						
Problem Loans / Gross Loans	0.8%	aa2	↔	aa3	Quality of assets	Expected trend
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	15.1%	aa3	↔	a1	Stress capital resilience	Access to capital
Profitability						
Net Income / Tangible Assets	0.6%	baa2	↔	baa1	Return on assets	Expected trend
Combined Solvency Score		a1		a1		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	26.9%	baa2	↔	baa1	Term structure	Market funding quality
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	28.7%	a3	↔	a3	Quality of liquid assets	Additional liquidity resources
Combined Liquidity Score		baa1		baa1		
Financial Profile				a2		
Qualitative Adjustments				Adjustment		
Business Diversification				0		
Opacity and Complexity				0		
Corporate Behavior				0		
Total Qualitative Adjustments				0		
Sovereign or Affiliate constraint				Aaa		
BCA Scorecard-indicated Outcome - Range				a1 - a3		
Assigned BCA				a2		
Affiliate Support notching				0		
Adjusted BCA				a2		

Instrument Class	Loss Given Failure notching	Additional notching	Preliminary Rating Assessment	Government Support notching	Local Currency Rating	Foreign Currency Rating
Counterparty Risk Rating	1	0	a1	2	Aa2	Aa2
Counterparty Risk Assessment	1	0	a1 (cr)	2	Aa2(cr)	
Deposits	0	0	a2	2	Aa3	Aa3
Senior unsecured bank debt	0	0	a2	2	Aa3	Aa3
Dated subordinated bank debt	-1	-1	baa1	0	Baa1 (hyb)	Baa1 (hyb)
Junior subordinated bank debt	-1	-1	baa1	0		Baa1 (hyb)

[1] Where dashes are shown for a particular factor (or sub-factor), the score is based on non-public information.

Source: Moody's Investors Service

Ratings

Exhibit 11

Category	Moody's Rating
AUSTRALIA AND NEW ZEALAND BANKING GRP. LTD.	
Outlook	Stable
Counterparty Risk Rating	Aa2/P-1
Bank Deposits	Aa3/P-1
Baseline Credit Assessment	a2
Adjusted Baseline Credit Assessment	a2
Counterparty Risk Assessment	Aa2(cr)/P-1(cr)
Issuer Rating	Aa3
Senior Unsecured	Aa3
Subordinate	Baa1 (hyb)
Jr Subordinate	Baa1 (hyb)
Commercial Paper	P-1
Other Short Term	(P)P-1
AUSTRALIA AND NEW ZEALAND BNKG GRP LTD, HK BR	
Outlook	Stable
Counterparty Risk Rating	Aa2/P-1
Counterparty Risk Assessment	Aa2(cr)/P-1(cr)
Senior Unsecured MTN	(P)Aa3
Other Short Term	(P)P-1
AUSTRALIA AND NEW ZEALAND BNKG GRP LTD, SG BR	
Counterparty Risk Rating	Aa2/P-1
Counterparty Risk Assessment	Aa2(cr)/P-1(cr)
ANZ BANK NEW ZEALAND LIMITED	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Bank Deposits	A1/P-1
Baseline Credit Assessment	a3
Adjusted Baseline Credit Assessment	a2
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Issuer Rating	A1
Senior Unsecured -Dom Curr	A1
Subordinate	A3 (hyb)
ST Issuer Rating	P-1
Other Short Term	(P)P-1
ANZ NEW ZEALAND (INT'L) LTD, LONDON BRANCH	
Outlook	Stable
Counterparty Risk Rating	Aa3/P-1
Counterparty Risk Assessment	Aa3(cr)/P-1(cr)
Bkd Senior Unsecured	A1
Bkd Other Short Term	(P)P-1
ANZ NEW ZEALAND (INT'L) LIMITED	
Outlook	Stable
Bkd Senior Unsecured	A1
Bkd Commercial Paper	P-1
Bkd Other Short Term	(P)P-1
AUSTRALIA AND NEW ZEALAND BNKG GRP LTD, NY BR	
Outlook	Stable
Counterparty Risk Rating	Aa2/P-1
Counterparty Risk Assessment	Aa2(cr)/P-1(cr)
Senior Unsecured	Aa3
AUSTRALIA AND NEW ZEALAND BNKG GRP LTD, LDN	

Pref. Stock Non-cumulative	Baa2 (hyb)

Source: Moody's Investors Service

REPORT NUMBER 1373763

CLIENT SERVICES

Americas	1-212-553-1653
Asia Pacific	852-3551-3077
Japan	81-3-5408-4100
EMEA	44-20-7772-5454

MOODY'S INVESTORS SERVICE