

TRANSCRIPT OF ANALYST BRIEFING

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MR GENTRY: Good afternoon, and welcome, everyone, both those analysts with us here in Martin Place and those on the phone. The purpose of the discussion this afternoon is really just to provide an opportunity to extend the question and answer session from the results last Thursday and also to provide a bit more context around some of the more common questions we have had in the last few days.

The format of this hour or so is shortly I will hand over to John, who will spend five or 10 minutes just addressing two or three of the major issues and the more regular issues that have come up in recent days, and then we will open it up for Q and A. If we have time at the end, we will also take a few questions on the phone. The conversation is being recorded and will be posted on anz.com in due course.

John, perhaps I could hand over to you to kick things off.

MR MCFARLANE: We were conscious that post the result a number of points of questioning, because of media comment, engineered further questions in the minds of shareholders and the minds of analysts. So we thought it would be appropriate, therefore, just to extend the Q and A session so that everybody at least had a chance to get their own perspective on these issues.

I just want to deal with the general environment and then deal with two specific issues. One is Asia - that seems to feature prominently, but in substance is not as material - and then the second is personal banking strategy. So I will give an introduction to those issues and then we can extend into anything else anybody wants to talk about.

In the general situation, we have had an environment over the last decade where ANZ and nearly all the banks, to that extent, have really gone through three phases - phase one, which was getting out of trouble; phase two, consolidating their position; and then phase three is transforming the organisations and creating higher shareholder value.

In this third phase, we were blessed with a very buoyant Australian economy at the same time as we were able to engineer quite massive productivity gains in the business because of inefficient starting positions. Then at the same time the elimination of concentrations of risk, mainly arising from overseas but also arising from investments in non-traditional businesses that weren't core, and that led to mid-teens compound earnings growth. It led to a decline in costs - flat costs and then a slight rise in costs - and it's led to a lower cost of capital, a change in the business mix towards a more sustainable business mix from a lower sustainable business mix and has given us a relatively strong position.

It's resulted in us being able to outperform the average of our three major domestic peers in each of the last four years, notwithstanding all the noise around 2003. The year to date I think we're broadly neutral to the average of those, although I think one of the players is, on balance, higher than the others, and that would be Westpac. But we are roughly around the average this year.

Looking forward, the environment is a little different. We are likely to see a more subdued mortgage environment. I mean, the strength of the mortgage environment is pretty unexplainable, really. It has surprised us on the upside constantly and, therefore, I wouldn't regard us as a superb forecaster of what this is likely to be going forward. Our track record in this has not been very good. In fact, it's all been better than we expected on the way. So in that respect we do think that an attenuation of this is perfectly reasonable.

At the same time there is an argument that business investment should actually be reasonably buoyant over the period, and we can't find any arguments against that. So we expect Australia to do reasonably well.

Nominal GDP is likely to be in the 5.5 to 6 per cent range. The productivity gains that might have been available previously are probably not available because people are more efficient - we are certainly more efficient - and there's a need to invest in the propositions going forward which will soak up some of the spare capacity in any event. The risk reduction possibilities are, again, of course - all the banks are, I think, relatively modest.

That said, I can't see anything to change the paradigm that financial services will grow, on balance, faster than nominal GDP. In that respect, therefore, all other things being equal, a major financial company in Australia should be able to produce nominal GDP's worth of earnings. In other words, if you don't produce nominal GDP, all other things being equal, then you know there are issues around you.

Given that financial services are probably going to be slightly stronger than nominal GDP, there is an argument that says, look, on balance if you are performing really well you should do better. For that reason we have set the industry at a sort of 6 to 8 per cent earnings environment, which should, in theory, also be an EPS range if capital management is managed effectively. The organisations that do well will be high in the range - perhaps even a nudge above - and someone who is weaker will be at the lower end of the range. Anyone respectably performing should be able to do reasonable levels of earnings over this year and the next few years.

My own instinct is if I were setting the bonus program for our own executives in advance and not changing it, I would set it at 8 per cent as being a good performance level where you get a normal bonus, and anything below that I would actually probably discount bonuses. It is just an intuitive feel that I think that that is where - as the CEO I would place it there.

It is in that context we have said, look, you know, all other things being equal, we would like to be at the upper end of that range and get normal bonuses. So that is the essence of the thing. The bonus is not material, I just use it as an indication of my own feeling of where the centre of gravity of ANZ's performance should lie if we're respectable.

Now, dealing with two issues that actually came out strongly post the result, but actually were not a material feature of the result. They happened to exist but were amplified during this period. The first is Asia. I want to throw a little bit more colour to that. It is based upon some work we did with McKinsey in 2000, which is still valid today. Basically, we asked McKinsey to tell us the implications of globalisation on the Australian banking scene, and on ANZ in particular.

It was a very comprehensive report, but it ended with three points. The first is that globalisation is real and particularly vulnerable to two types of competitors - one is very large competitors who are a multiple of the market cap of the Australian banks; and, secondly, people who were global specialists in certain areas of financial services.

The first would have a competitive advantage in that the acquisition of assets, given their scale against ourselves, would mean that an asset acquisition by an Australian bank would be relatively dilutive relative to a larger player were they to be interested in the same space.

Secondly, in the areas of globalisation, the whole of the Australian business is not subject to globalisation unless a global player found an Australian bank to be accretive or not materially dilutive and where it was high on their list to acquire an Australian bank. We have not seen any evidence of that. But over long periods of time I think the concept is still valid.

With respect to the businesses themselves, they'll fall into two broad categories - those that are not inherently subject to globalisation other than through brute force, and that is the domestic banking franchises that are not easily assailed by a new competitor entering the market. An example of that is the personal banking business where there have been some international players who have tried to break into that market in a broad way and actually have not succeeded domestically, and they have withdrawn as a consequence.

Niche players have managed to move in - for example, ING Direct is a good example, where they have actually gone for a niche positioning which is essentially a deposit-raising positioning, then investing the assets in unique asset classes such as mortgages, appealing to a particular niche of the market.

But it is true that investment banking would be classically an area subject to globalisation, as would certain aspects of insurance and funds management. It is for that reason that we were not inclined ourselves to own a funds management company outright - there was a domestic company - because we felt that it wasn't sustainable in a globalising business.

For that reason, therefore, you do one of two things generically: you either sell the business before it declines in value or you partner with a global player who is keen to get into your market and are able to attract them at a premium, either as a sale and/or as a partner if you want to stay in the business, in that having a share in a global partner's business is respectable in a globalising scenario, particularly if it is synergistic to that partnership where we, through our domestic franchise, can bring value to that entity. So that is the inward threat scenario.

But there was an outward scenario, and the outward scenario is that where we have real capabilities that we can leverage in other markets potentially globally, they are likely to be niche positions rather than broadly based positions. It would be intelligent for us to do so, providing they are low risk and provided that our competitive advantage was relative to the other potential players and/or there were barriers to entry that would give us a privileged position.

So the first thing that we looked at was whether there were any global niches that we could potentially dominate that would be very, very thin niches, and the answer is no, we can't come up with any of those, at least for ANZ at this point in time. We did, though, come up with the prospect that we may be able to engage in investments in the region, rather than globally, that would be niche investments, leveraging some capability here.

The classic type of investment would be, for example, the deal that we are looking at with the Metro Bank in the Philippines where we clearly have an advantage in running credit card operations. They have the number 1 banking franchise domestically, but the number 5 credit card franchise and are struggling on their own to leverage it. So, therefore, leveraging a known capability that we have by getting the franchise of another partner and the two of us creating a better outcome together than they could on their own.

There is an argument that is made by investors that they can get these type of investments themselves and they can get an investment in us themselves and therefore they can hold those investments and don't need us to do it. That is very a respectable position. That is not what we're arguing. We are arguing that you cannot get that proposition without us inside it, because that proposition doesn't exist unless we leverage it. So we are really offering a synergistic proposition. So that is what that is about.

Now, there is another attribute with respect to that, and I said if you can access it such that you have a competitive position against all players and/or there were barriers to entry, that would give you a privileged position. It just so happens in this particular case, or in similar cases, the other players who could leverage such a scenario tend to be already competing in those local marketplaces with these potential partners and, therefore, they are not regarded as partners, they are regarded as competitors. Therefore, the extent of potential competition to enter these spaces is narrower than you might imagine.

It might actually happen in another way. If you take China, for example, where licences are scarce and the licences are granted semi-politically. Therefore, it isn't an open, free market and you are therefore given a restricted access to a marketplace, which is a competitive advantage.

Now, going beyond that, to the extent where we would take stakes in domestic banks in Asia is stretching the proposition a little. Therefore, that would not be hard core to the proposition that we have as a core to our strategy, and anything on that has largely been either opportunistic, and therefore of a lower value and lower probability.

The Panin situation was partly of necessity and it was partly opportunistic. As you know, Panin needed recapitalisation and we already had a joint venture with Panin in Indonesia 85/15 and we needed our partner to be healthy, so there was a protection of our existing franchise built into our helping recapitalise Panin.

We went in with loans and options and, as it turns out, the value of our initial capital injection in Panin at no stage had been under water, even in the decline in the value of that franchise. The only time it went under water was when we acquired additional equity in the marketplace to bring us up to 29 per cent.

So in that respect, that second stage wasn't as smart as the first stage. The first stage has played out almost impeccably. So you can see that.

Now, that isn't the case with any new venture going forward. The other point about this is that we wanted it to be diversified, given the risk of Asia, and therefore we didn't want large concentrations of risk and we didn't want to put all our eggs in one basket. Therefore, we were looking at smaller investments, principally Horizon 3 or Horizon 2 type investments rather than current investments.

So in a sense I'm giving you a signal of the probabilities of certain things happening, because some are quite clearly congruent with the space that we are trying to engineer and others are less clear in that space.

We did not intend to put \$1 billion immediately on the table. What we tried to give was a boundary that over this whole strategy being executed we would likely increase the amount of capital in Asia by 2.5 per cent of our capital incrementally up to 7.5 per cent of our capital incrementally if the whole strategy was unveiled in the way that it had the potential to, but the mean of that would be lower than the ceiling.

QUESTION: John, is that ACE capital?

MR MCFARLANE: ACE. So in other words you're essentially talking about a total capital invested in Asia - east Asia, I'm talking about - as between \$500m and \$1 billion. But you have to get there, so it never jumps to the maximum position.

Let me clarify that we are already in Asia. We have already paid the price of being in Asia and learning about Asia. We have been there a long time. We generate 5 per cent of our profits from Asia from 2.5 per cent of our capital. It is actually a productive investment. And we generate another 4 per cent of our returns from the Pacific. So Asia Pacific is already 9 per cent of our profits and it is a disproportional return to our capital investment in those franchises. Therefore, doing more is inherently sensible because we have a platform to take it from.

Secondly, we are nervous if you take longer time frames of being constrained to domestic - Australia/New Zealand - principally because we feel that the economies of Asia and Australia/New Zealand will become more interdependent rather than less interdependent over long periods of time.

The third point I make is there is a big difference between the Grindlays investment and the strategy that we have in the Pacific and the strategy that we have in Asia. Our previous strategy in Asia was lending to corporations in Asia and being a foreign bank in south Asia. We have withdrawn from the first. We don't want a domestic lending and a cross-border lending position to Asian companies in Asia. We don't want to do that. We want to do international trade, foreign exchange and essentially leverage our position with our core customers in Asia and in other parts of the world. That is what that existing strategy now is.

The strategy we are aiming to unfold is, rather than be a foreign bank in these marketplaces where you, in essence, operate upscale in the corporate scene or have a struggle to compete in the domestic market with domestic players - we want to partner with domestic players rather than be a foreign bank in these areas leveraging their domestic franchises with a real capability that we will build. That is not the case with Grindlays. We were not the natural owner of Grindlays. There were no synergies between Australia and that part of the world and therefore it was perfectly possible that it was more valuable to someone else than it was valuable to us and the right thing for us was to sell it to somebody to whom it was more valuable than us. That is exactly what we did.

So we played out that third part of the globalisation thing, which was that investment for us was non-strategic, it was non-core. We were the wrong owner and there were other global players wanting to move into that because of their size, ala the major global banks - better leave them nameless, but they were bidding for it - and the other was Standard Chartered, who already had the same positioning as we had there and the doubling up was synergistic and allowed them to have the dominant position in the region. So that is all I'll say about Asia.

I'll now say something about personal banking. One of the strengths of ANZ has been our ability to maintain our strength on the corporate side of the business and we haven't changed that. The other is in a position where we haven't had traditional strengths on the consumer side to find specialisation of leveraging it. So one of the things that came out of the McKinsey work was this specialists are going to win, and that it is more important to run a great business than to build your business based on synergies between businesses. That was a principal of that strategy work. And so we decided that we would run specialised businesses, inherently product led, and they were in asset finance, credit cards and mortgages, and there was one potential of wealth management but that's a different point. I'll leave that one aside and if you ask a question I'll deal with it.

In that respect by giving specialist focus and building specialist capability in those areas, we managed to generate either leadership positions or positions where we were able to grow the business faster than nominal and to gain market share and market position. And so in that respect in the cards business we actually leveraged direct marketing and third party brands to grow our positioning beyond our own brand and we did not need to leverage what was a relatively weaker distribution paradigm in that area. So we have run a successful cards business, despite having a relatively weaker network distribution paradigm.

The same is true of mortgages. Our mortgage capability was constrained by our ability to leverage our distribution. So what we did was freed up our mortgages to leverage third party distribution, and providing it is an acceptable risk on return, that is an acceptable paradigm. In fact, the return on third party mortgages, all other things being equal, is relatively neutral with respect to our own originated mortgages. It is transparent to everybody. It is better to originate your own mortgages through your own network because it is a fixed cost overhead that you put more business through, but if you can't get the business in the first place, then it is academic and you might as well get the revenue at the margin, so we then went for that strategy. It has been incredibly successful for us. It has paid off for us in having a very robust mortgage position. On average over the last few years we've fought well above our weight.

Now, the final frontier though is this personal banking proposition which is not a traditional strength of ours. We have an under weight position in it and we have not until now been able to build a differentiated position and a distinctive strategy in there. In order to fix that, I am not arguing to you that we'll get the leading position in this, but I am arguing that we have no choice but to be in this because it's interdependent with our other propositions. Our customers, whether they are corporations, actually do business through our branches. Our branches distribute wealth management and other products, and our customers believe that the branch network is our window on the world. So there is no way that we could not be in this. We have to be in it.

Finally, in order to grow the whole franchise we need to raise customer deposits and therefore growing the consumer part of our business is actually core to us growing our whole enterprise. So we have to make this successful but we have to find a way of making it sustainably successful. In that respect the first thing we had to do was to - we had an uneconomic proposition on our hands. It was making a profit but was not generating the right amount of return. So the first thing we did was radically improve the productivity by cutting the branch network and pruning its costs, improving its performance. That took us to a base level that we have now.

The second thing we did was try and engineer a point of difference by trying to take advantage of what the regional banks have taken advantage of which is a different image to the large banks who are on balance disliked as a paradigm but nevertheless liked by their clients. And so if we could get a softer edge on our larger competitors and perhaps replicate some of the image aspects of the regional players, we could then start to - in customer differentiation mixed with the human face characteristic through the restoring customer faith program and that was in essence a localisation passing - the response to the marketplace in the hands of the local people rather than a centrally driven approach to local marketplaces. So we started that some time ago and again that's getting some traction.

The third point was that we had to improve the service in the branches and gain respectable service such that we didn't lose clients. I'll come back to that in a minute.

The final point was when we added it up, the package of benefits that we offered has to have a sustainable advantage in the eyes of our clients, and unfortunately there was something missing in that package of benefits. The thing that was missing was unlike all our other propositions we had leading products, and what was also missing was something that was a package of benefits that was sufficiently tangible in the eyes of our clients to warrant them moving their business to us and/or staying with us.

In that respect we hit upon the idea that at a relatively modest cost and erosion of profits we could afford to develop leading priced products in the transactional space that did not erode the profits of the whole enterprise because most of the profits are made on liabilities not on transactions. And so we could engineer a real competitive advantage in the current account space by having something that was tangible in the eyes of customers that did not erode the total returns of the sector other than tactically in the transaction space.

We hired First Manhattan to help us with this proposition and they argued that the leading product thing was absolutely fundamental. It was actually core to ANZ and it was one of our strengths and we needed them. So we sprung out the transaction product business which we could then have taken on the characteristics of the other specialist businesses and potentially leverage third parties if we choose to. They haven't actually decided to do that but they are looking into that now so that running a successful product business is the first pillar of this.

Second is having leading products in that business and that meant simplifying the current account structure. We've taken nine transaction accounts I think it was and created two transaction accounts, one which is the \$5 account for a month then no transactions cost, the other is a pay-as-you-go account.

On reflection in having run through those paradigms we are winning market share but there are really, as we see it now, three paradigms in operation rather than two - the first one is fine in that we had a debate as to whether it should be five, six or \$7 a month. But we decided that the long term positioning would end up at \$5 rather than \$7 and therefore we might as well take it to \$5 now and really differentiate, take a bit of pain short term. The second proposition, which was the pay as you go one, actually was tactically a better proposition for customers because we gave free transactions as well as being pay as you go whereas the free transactions were not geared to people like us. They were geared to those elements of the community that couldn't afford banking that we needed to subsidise for social and other reasons. Therefore our first proposition, the \$5 a month one, was not as successful as it should have been because we were subsidising the second bundle and so some time in the future we will probably try and engineer a clearer separation between the paradigms than we have now and get the first paradigm to be more successful because it's being eroded by the very competitive aspects of the second.

Now it is not a discounting strategy. What it is is recognising that in order for us to have a differentiated position in this industry, we have to price to give the most benefits in aggregate for any price in this space, and/or for a given level of benefits to be marginally priced below the competition as an attacker play. So we have to have an attacker but it is not a discounting strategy, as it only applies to the transactional product and it is uniquely related to customer acquisition.

I would also make a very important point. We are talking about a business that generates 12.5 per cent of ANZ's profits, not 30 per cent, 12.5 per cent, and we are only talking about part of that proposition. I am not talking about the liability part that will benefit from more accounts because there is no price change in that.

As it's turned out we now have a package of benefits that work. Now the final one was service in that if you then have this bundle, it was quite transparent that we could not have a premium priced and/or a premium service model. It had to be a service model that was consistent with the price that we were tackling. It could be neutral on liability but it had to be a service which was essentially a reliable service at low prices, the woolworths type positioning, not discounting.

Therefore the price erosion or the margin erosion that we are actually sustaining and potentially sustaining as a consequence of this is actually only in the transaction space and it's only temporary and is not going to lead to a wholesale price war across the industry, across the liabilities because it is not related to pricing of liabilities. It is only related to pricing of transactions. So I think I will stop there.

MR GENTRY: Thanks, John. Perhaps just to let so that people are aware, we've got about 15 or 20 minutes where we can take some questions. Could I ask that the questions, if you have questions on the detail of the financial results could you save those for later and direct them to either Steve Higgins or myself. Let's just confine our questions perhaps to the areas that John has touched on or any other major strategic issues that people want to discuss. Let's start in the room.

QUESTION: John, why do you say the margin erosion is only temporary?

MR MCFARLANE: Because the amount of profit - well, clearly we will erode marginally transaction margin - but if you take the total margins in that whole business you're talking about marginal reductions in revenue relative to expenses in aggregate.

Secondly, I don't believe that the competitors will try and replicate that because their bundle, the strategy bundle is different to ours. It is my sense that Westpac and NAB's strategy is up scale positioning and therefore this is inconsistent with that positioning; and secondly, the Commonwealth Bank's strategy, without putting words in their mouth, they are really Australia's most convenient bank and therefore what they should be extracting is a higher margin for convenience. They don't have to have the premium, a low priced product. So I don't actually think that this is going to be an industry effect at all. I actually think it is an ANZ effect and is essentially the cost of us having a sustainable position that we could never get otherwise.

QUESTION: John, how do you protect yourself against though ING. I do my deposit account with ING, do my transaction account with you, do my home loan with whoever is the cheapest? By creating yet another discount product in one particular segment that is not linked into anything isn't that a major risk that you just get a lot of the crappy product?

MR MCFARLANE: It is not because the positioning of this segment for us is not up scale. It is not mass affluent, or in your case very affluent!

QUESTION: I'm not quite as affluent as yourself.

MR MCFARLANE: It is actually a middle positioning but not trying to get the bottom end. So it's a middle positioning and therefore - and the propositions you're talking about are not aimed at that middle segment. This is absolutely aimed at this middle ordinary Australian who has a job.

QUESTION: Looking at that long term perspective, John, how do you see yourself extracting profit and value out of those customers?

MR MCFARLANE: But we are now. I mean, the earnings in that segment, although they were a little flat in the half because of margin erosion and liabilities, if you take it over a year earnings were up 11 per cent. So you can't actually complain that we're not extracting value from this proposition now. We are extracting it. The problem is the value extraction is not sustainable without actually a reshaping of the strategy, and so what we have engineered is a sustainability for a short term cost.

QUESTION: John, you mentioned the first paradigm eroding the second. Are you effectively saying there is more cannibalisation than you first estimated, so more of your own customers are moving to that 60 bucks a year account than you thought?

MR MCFARLANE: No, less of our customers than we wanted - than we thought moved to the 60 bucks a year because the pay-as-you-go product was so competitive. So for example one of the things that we did that in essence was done as a pilot, and probably slightly hastily, was to eliminate the charges on Internet because if it's classically pay as you go, then if you go you should pay, basically. I mean, that's the principle of it. Then so in essence why - the concept of a lost leading strategy, well, you charge nothing for this, but then you get all this stuff over here, isn't actually what we're trying to achieve here. We're actually trying to make sure that this business stand alone, other than the synergies that you can get from these customers through cost signing on the other products. Forget that for the moment. That is a bonus, and we believe that will be there by the way. But we want to make this business actually sustainable economically in and of its own right.

In that respect the returns from this transaction segment are high at the moment because it actually hasn't got very many assets. It doesn't therefore have much capital other than operational risk capital and we can afford therefore to give up some of that return on equity at the margin. So we're not actually giving up something that is actually going to hurt us economically. We're giving up return.

QUESTION: That's only on the assumption that your competitors don't adjust.

MR MCFARLANE: Well, on the assumption that they won't adjust but we've seen the evidence of that in that we've actually seen a competitor respond. Immediately we announced this - remember it was about a year ago since we announced these - and the response was they matched the \$5 account but left fees, if you remember. So it's demonstrating that they're not matching. They've had the chance to match. They've never matched.

QUESTION: Is it like the Aussie Home Loans from six, seven, eight years ago? They wait until it becomes a material movement of customers and then they adjust?

MR MCFARLANE: That may be the case. In fact, what's happened associated with this bundle of benefits in the Victorian pilot is that there's quite a lot of customer attrition in banking but a lot more than you would probably assume there was. It's principally associated with us causing a service issue with a customer, upsetting them in some tangible way and therefore them looking over the shoulder to try and move because they're dissatisfied with something we've done rather than a price point somewhere else necessarily. So we've stopped the erosion of our customers and our bundle of benefits has actually been an attack of play that we've actually brought new customers in, getting an exponential growth in customers. I think we've had something like - I think the cost was about \$9m in the half, in terms of the costs of this whole approach and we got 200,000 extra customers. I mean, boy, if you can get 200,000 customers for \$9m!

QUESTION: But that's from a flat revenue base. The industry has grown that fee line six, seven per cent in the last year, so it's more than nine of your current balance.

MR MCFARLANE: Yes. But I'm sort of arguing the point that I actually genuinely think that the secret to this isn't just pricing. It's actually not screwing up. And if we can get our service proposition to reliable without upsetting our customers, then your revenues are going to rise anyway because you eliminate the attrition that everybody is currently experiencing now. You may be right, if the customer attrition is sufficiently material then that might engineer a response. However, the response is less likely for the upscale players than it is for the general market player. The problem with the general market player is the price of matching is enormous because you have to reprice your existing customers as well as your attractiveness to new customers. We've actually seen that the largest players in any market have never become the price leaders as a consequence of that because the price is too high and you can't rely on that. But that - just if you reflect on it, it's an intelligent assumption.

QUESTION: You're still 15 per cent of the market, so you're not small.

MR MCFARLANE: No, we're still material, but in all the other businesses we have been able to get market shares much higher than that. We really would like to get into the space.

There are two products that matter more than anything else to cross-selling and your ability to have a deeper relationship with your client that is sticky - one is a mortgage; the other is a current account.

I don't know about you guys, but moving my current account, you know, I just don't have time to even think about that even though I'm really upset with my bank - which I better not be because it's ANZ - but you know what I'm saying, it's just too hard. It's in the too-hard bucket. You've really got to be very upset, in a sense, to move that and/or perceive that you want to move it for positive reasons. It's not just about pricing, it's about this human face, it's about all sorts of other --

QUESTION: John, haven't you just announced the biggest risk of this strategy?

MR MCFARLANE: I don't think there's any risk in this strategy.

QUESTION: Just that you're basically sacrificing margin on the transaction account.

MR MCFARLANE: At the margin. We are reducing a strong return on equity for a strong return on equity, because there's virtually no equity in the business.

So you might ask the question why can you get away with these prices at the moment. They can't compare because the industry is inherently profitable.

I personally don't think there's material risks to this. Oh, and there's another part to it, by the way, and that is that we believe that specialist sales forces are going to win over generalist sales forces and that general distribution networks are actually only going to work in rural communities and suburbia. They are not going to work in the 80/20, they are not going to work in the big cities and the big branches. In those big branches you're going to need specialists and, therefore, what we should have in the branches is transaction banking specialists who do nothing else; mortgage specialists who do nothing else or are in a bank or wherever; wealth specialists and auto specialists and whatever other specialists - small business specialists, whatever makes sense, but not generalists.

In that respect, if there is an 80/20 in this business, if you strip the rural out it's a very different paradigm. The 80/20 is - the core of this is actually specialisation, not price. It is a sales specialisation.

QUESTION: You talked about 200,000 additional customers. How many more are you expecting to get from the strategy?

MR MCFARLANE: The trouble is it's not easy to model this. It is easier for us in Victoria to win because it is our natural domestic marketplace. It is a little harder for us to win in the natural marketplace of the other players. So in that respect I have to slightly attenuate my assumptions there.

What we would really like is to fight in the high teens across all our businesses and given that there is some synergy between the businesses, then providing we can engineer high teens market shares generally, which will take a while, as you can imagine, then there is no reason why it can't be in this space, but I don't think it will be soon.

MR GENTRY: We have got time for one question on the phone.

QUESTION: You were just talking about how many customers you were hoping to get. I suppose the difficulty with ever putting out a target is that you are going to be held to it.

MR MCFARLANE: That is why we didn't do it.

QUESTION: Well, it was August 2001 --

MR MCFARLANE: Not because we didn't want to be held to it --

QUESTION: It was August 2001 that Peter Hawkins said that over the next two or three years you would get a million extra customers net. 50,000 customers for the next six months suggests 10 years down the track rather than two to three years down the track. I suppose, before you mentioned that --

MR MCFARLANE: That is only Victoria, remember.

QUESTION: The 50,000?

MR MCFARLANE: Remember that's where the pilot was run. You have to take the rollout across Australia and New Zealand.

MR GENTRY: It was also across all products, it wasn't just personal banking. It was personal financial services at the time, which included SME, cards, mortgages, as well as this business.

MR MCFARLANE: I wouldn't be surprised if that is still a reasonable target. He was a little unspecific on the timing, but you're right, it was more what you said than 10 years.

QUESTION: One of the points you made before about your own circumstances was it is put in the too-hard basket to move. What customers are you going to get if for most of us shifting from one bank to another is in the too-hard basket? CBA seems to have a fairly strong grip on the youth market. Does that mean you are chasing those customers who are willing to go to that effort for \$1 or \$2 a month?

MR MCFARLANE: I'll be honest with you. It is more to do with the fact that there are so many dissatisfied customers in banks, and that is the fertile ground rather than attracting them who are satisfied. It is the customers who have just been absolutely upset, walked out and then said, "where do I go?" what we're hoping is that the sort of positioning of the bank with a human face is what encourages them to say, "Okay, ANZ seems to be the sort of bank I want to bank with." That's a sort of leading attractor.

MR GENTRY: It is early days and we can't say that it is across the board yet, but the profile of customers attracted so far has not been dissimilar to the existing profile of customers.

MR MCFARLANE: I would make another point: I would do this even if all we did was held our position, because we have to have this to be successful.

QUESTION: Does it require the cross-sell story? Will you get enough funding and liability side benefits to make this pay its way over a period of time?

MR MCFARLANE: It doesn't require it now. In other words, this business standalone is successful from an earnings and an ROE standpoint without the cross-sell. The cross-sell is the synergistic aspect. We would like to make this business standalone successful and then engineer greater synergy cross-sell. We believe that building great businesses is the foundation for synergy rather than trying to get cross-sell.

MR GENTRY: I'm afraid we have run out of time for questions. There are obviously questions that people do have, and we can help in answering some of those over the days and weeks ahead.

We will be having a strategy day probably in late July in which this will be laid out in a lot more detail. The purpose of today was not to answer everything, but simply to start giving you a flavour of the thinking. Hopefully we have at least made a step in that direction. Thank you all for joining us.

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