MOODY'S
INVESTORS SERVICE

CREDIT OPINION

24 February 2022

Update

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RATINGS

ANZ Bank New Zealand Limited

Domicile	Wellington, New Zealand
Long Term CRR	Aa3
Type	LT Counterparty Risk Rating - Fgn Curr
Outlook	Not Assigned
Long Term Debt	A1
Type	Senior Unsecured - Dom Curr
Outlook	Stable
Long Term Deposit	A1
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.

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ANZ Bank New Zealand Limited

Update to credit analysis

Summary

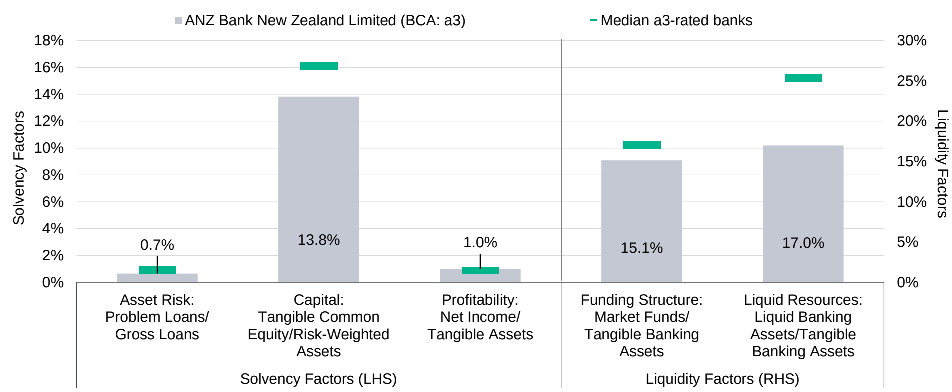
ANZ Bank New Zealand's (ANZNZ) A1 senior unsecured and deposit ratings includes two notches of uplift on top of its standalone baseline credit assessment (BCA) of a3. This reflects the very high probability of support from its Australian parent, the Australia and New Zealand Banking Grp. Ltd. (ANZ), rated Aa3, as well as the potential for systemic support from the Government of New Zealand (Aaa stable).

New Zealand's strong economic rebound since the peak of the pandemic has eased risks to asset quality - reducing the likelihood of material credit losses. That said, the latest Omicron outbreak presents some uncertainty although any rise in credit losses are likely to be manageable in the context of the bank's strong balance sheet buffers - ANZNZ's common equity tier 1 (CET1) ratio was 13.4% at 30 September 2021. ANZNZ's funding and liquidity profiles remain healthy and remain supported by access to the Reserve Bank of New Zealand's (RBNZ) Funding for Lending Programme and repo facility.

Whilst likely rate rises will support the bank's net interest margin (NIM), an unlikely repeat of provision releases in 2021 as well as ongoing competition for home loans are headwinds for profitability.

Exhibit 1

Rating Scorecard - Key Financial Ratios



Source: Moody's Financial Metrics

Credit strengths

» Strong market position as New Zealand's largest bank

» Capital provides a strong buffer against ongoing coronavirus-related uncertainty

» Strong asset quality but rising house prices remain a concern

» New Zealand's strong operating environment

Credit challenges

» Competition and rising funding costs to challenge banks' NIM

» Sensitivity to wholesale funding market conditions

Outlook

ANZNZ's ratings have a stable outlook.

Factors that could lead to an upgrade

» An upgrade of ANZ's BCA

ANZNZ's BCA could face positive pressure if the bank's Tangible Common Equity ratio rises above 14%.

Factors that could lead to a downgrade

» A downgrade of the parent's (ANZ) BCA

ANZNZ's BCA could face negative pressure as a result of:

» Uncertainty surrounding the economic recovery remains a key risk for New Zealand banks' asset quality. A material increase in non-performing loans would be negative

Key indicators

Exhibit 2
ANZ Bank New Zealand Limited (Consolidated Financials) [1]

	09-21[2]	09-20[2]	09-19[2]	09-18[2]	09-17[2]	CAGR/Avg.[3]
Total Assets (NZD Million)	178,509.0	174,523.0	161,549.0	152,257.0	145,902.0	5.2[4]
Total Assets (USD Million)	123,144.5	115,359.6	101,299.2	100,938.7	105,472.3	3.9[4]
Tangible Common Equity (NZD Million)	13,431.0	12,359.0	10,833.0	9,487.0	9,158.0	10.0[4]
Tangible Common Equity (USD Million)	9,265.4	8,169.3	6,792.8	6,289.4	6,620.3	8.8[4]
Problem Loans / Gross Loans (%)	0.5	0.9	0.5	0.4	0.4	0.6[5]
Tangible Common Equity / Risk Weighted Assets (%)	13.8	12.1	11.2	11.5	11.2	12.0[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	5.5	9.0	6.4	5.3	5.5	6.3[5]
Net Interest Margin (%)	2.0	2.0	2.1	2.2	2.1	2.1[5]
PPI / Average RWA (%)	2.6	2.4	2.8	3.4	2.9	2.8[6]
Net Income / Tangible Assets (%)	1.1	0.8	1.1	1.3	1.2	1.1[5]
Cost / Income Ratio (%)	38.9	42.1	39.1	35.6	37.0	38.6[5]
Market Funds / Tangible Banking Assets (%)	15.1	16.5	18.9	18.0	18.9	17.5[5]
Liquid Banking Assets / Tangible Banking Assets (%)	17.0	18.6	12.5	12.1	12.3	14.5[5]
Gross Loans / Due to Customers (%)	112.6	110.1	121.7	121.9	126.2	118.5[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

ANZNZ is a New Zealand bank headquartered in the city of Wellington. The bank is a fully owned subsidiary of ANZ, making up 18% of the parent's total assets and 30% of net income at 30 September 2021.

Together with its subsidiaries and associate companies, ANZNZ offers a range of banking and financial services. The bank caters for all customer segments, including retail, business banking, rural, corporate and institutional customers. As of 30 September 2021, ANZNZ was New Zealand's largest bank by reported total assets of NZD184.8 billion.

ANZNZ was created as a result of the October 2003 acquisition by ANZ Banking Group (New Zealand) Limited of NBNZ Holdings Limited and its consolidated subsidiaries, including The National Bank of New Zealand Limited (NBNZ).

Please refer to the Issuer Profile to read about ANZNZ and the New Zealand Banking Sector Outlook to read about the New Zealand banking system.

Detailed credit considerations

Strong market position as New Zealand's largest bank

ANZNZ is the largest of New Zealand's four major banks with a 29% market share of total loans. Similar to its peers, ANZNZ has looked to support its competitive position through ongoing investment in digital and core IT systems, which has become increasingly important given the rising need for digital banking solutions during the pandemic.

Despite the dominance of the four major banks, competitive pressures remain high, particularly for fixed-rate mortgages which typically make up the largest part of bank portfolios. Competition for mortgages with low loan-to-value (LTV) ratios is also strong as a result of macro-prudential measures introduced by the RBNZ. Under the current settings, residential property investor loans with LTV ratios of greater than 60% are restricted to 5% of a bank's new residential property investor mortgage lending, while for owner-occupiers, loans with LTV ratios of higher than 80% cannot exceed 20% of a bank's new owner-occupier mortgage lending.

Healthy capital position provides a strong loss absorbing buffer

ANZNZ's capital position remains very strong, with a CET1 ratio of 13.4% as of 30 September 2021. In fiscal 2021, the bank's CET1 ratio improved by 170 basis points. We expect the bank will continue to maintain high levels of capital despite the potential for increased capital consumption as dividend payouts normalise.

We expect New Zealand bank capital to continue to strengthen as the RBNZ's dividend restrictions, which constrain payouts to 50% of earnings, will remain in place until July 2022. This also coincides with the introduction of higher regulatory capital ratio requirements, which also come into effect in July 2022, but grants banks a six year transition period to meet the higher targets.

Under the RBNZ's new capital rules, the CET1, Tier 1 and Total Capital requirements for New Zealand's four largest banks will rise to 13.5%, 16.0% and 18.0% of risk weighted assets (RWA) respectively. This represents a significant increase from the current requirements of 7%, 8.5% and 10.5%.

Since 1 January 2022, the RBNZ has also required the major banks to report both IRB and standardised capital calculations and the output floor on IRB exposures was set to 85%. The derecognition of non qualifying AT1 and Tier 2 instruments also commenced at the start of 2022 and will be fully derecognised by 1 July 2028. From 1 October 2022, the IRB scalar will increase from 1.06 to 1.20.

Economic recovery to limit significant asset quality deterioration

We expect ANZNZ's asset quality to remain strong and the impact from the pandemic to be modest, supported by a residential mortgage portfolio which has demonstrated low loss rates over time. As at 30 September 2021, the problem loans ratio (proportion of Stage 3 loans) stood at 0.55% of gross loans. That said, there is some potential for asset quality to weaken as some customers who continue be impacted by current economic disruptions transition from banks' hardship programs to becoming non-performing. Furthermore, there remains some uncertainty given ongoing restrictions in relation to the latest Omicron outbreak. Conditions for sectors such tourism and hospitality are also likely to remain challenging until international borders are reopened.

Asset quality pressures could also emerge as expansionary monetary and fiscal policy settings during the peak of the pandemic have pushed up the already high levels of household leverage and house prices. This raises the sensitivity of households to an economic shock which could drive a rapid decline in house prices and pressure on asset quality as more loans fall into negative equity. That said, limits on high LTV mortgage lending that have been in place since October 2013 have helped mitigate risks in the housing market. As of 30 September 2021, ANZNZ's proportion of lending at LVRs above 80% was 5.7%, the lowest amongst the major banks who reported an average of 6.8%.

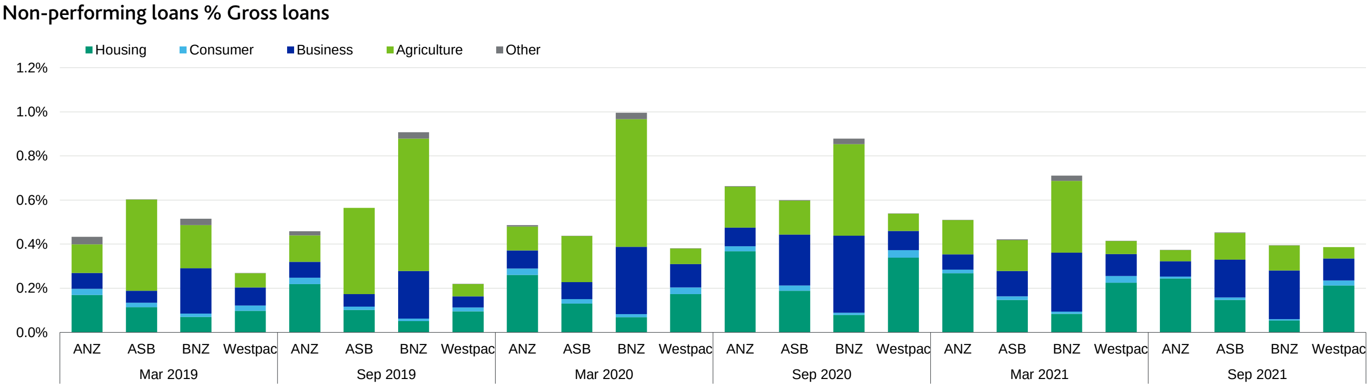
Highly leveraged farms, particularly in dairy, also remain a risk. At 30 September 2021, ANZNZ's exposure to the agriculture sector, of which dairy is the largest component, was at 11.3%, compared to an average of 11.2%. This has declined in recent years as the bank has sought to reduce this concentration risk.

These risks from the housing and rural sectors underpin our `asset risk' adjustment in our scorecard.

Exhibit 3

Asset quality remains strong

Non-performing loans % Gross loans



Source: RBNZ

Despite the challenges noted above, any rise in credit losses are likely to be manageable for the bank, given its robust loss absorbing buffers. Provision coverage of gross loans declined in 2021 but they still remain higher than pre-COVID levels.

Receding asset risks have reduced credit costs, but margins under pressure

ANZNZ's profitability rebounded strongly during the fiscal 2021 with net profit after tax rising 41% to NZD1.9 billion. The result was underpinned by a NZD114 million credit impairment benefit, compared to the NZD403 million impairment charge in fiscal 2020 and reflects New Zealand's strong economic recovery since the peak of the pandemic. The bank's return on average assets ratio rose to 1.1% for 2021, up 30 basis points from fiscal 2020.

Looking ahead, robust housing loan growth and access to low cost funding from the RBNZ's Funding for Lending Programme should continue to support net interest income. Further cash rate rises in 2022 will also provide support to the bank's NIM, although the timing of such benefits will be impacted by the skew of housing loans towards fixed-rate mortgages, albeit at relatively short maturities of one to two years.

These positive pressures will be partially offset by ongoing downward pressure on NIM which, despite rising 2bps during FY2021, will be challenged from ongoing and intense competition for mortgages and a rise in funding costs as banks' start to normalise their wholesale funding issuance. Investment in technology will also continue to be a key focus for banks, although subsequent ongoing maintenance costs from these projects should be lower, and partially offset by a gradual benefit from efficiency gains. Additionally, the sizable benefit to the 2021 result from provision releases is unlikely to be repeated in 2022. This is because further provision releases will be dependent on the ongoing health and economic outlook which faces some uncertainty given the most recent Omicron outbreak.

Sensitivity to wholesale funding market conditions

New Zealand's major banks, including ANZNZ, remain exposed to wholesale funding conditions and in particular, offshore funding markets. That said, ANZNZ's funding and liquidity metrics improved during the outbreak due to the surge in system liquidity from both monetary and fiscal policy actions taken in response to the pandemic. These trends have started to reverse, in line with the wind back of government stimulus and a recovery in household consumption. Accordingly, customer deposit growth slowed in fiscal 2021, growing 3.5% compared to 10.6% in fiscal 2020, resulting in a slight deterioration in the loans to total deposits ratio of 111.0% at fiscal 2021.

New Zealand banks also benefit from access to the RBNZ's Funding for Lending Programme, established in November 2020 in response to the economic downturn from the pandemic which serves as an additional source of low-cost funding, and the central bank's repo facility, allowing ANZNZ to rapidly monetize its large mortgage book. As of 30 September 2021, the bank held NZD9,647 million self originated residential mortgage backed securities (RMBS) on its balance sheet that are readily available to be pledged with the RBNZ.

To reflect this additional source of liquidity, we apply a positive adjustment to this section of our scorecard, assessing Liquid Resources in the `baa' range.

In addition to local requirements, New Zealand's four major banks are required to meet the Australian Prudential Regulation Authority's (APRA) liquidity coverage ratio and net stable funding regime, given that the banks are subsidiaries of the four major banks in Australia.

ANZNZ's rating is supported by New Zealand's strong operating environment

New Zealand's Strong+ Macro Profile reflects the country's high economic strength, very high institutional and government financial strength, and low susceptibility to event risk. While the global coronavirus outbreak presents unprecedented challenges to New Zealand's economy, the government has promptly deployed its fiscal capacity to buffer the impact of the shock. Overall, strong institutions and policy effectiveness mitigate external and domestic vulnerabilities related to high reliance on external financing and elevated household debt.

We expect real GDP to grow 5.5% in 2021 and 3.3% in 2022, after contracting 1.1% in 2020. Substantial economic support package from the government will provide financial assistance to companies and individuals, which will likely mitigate the negative impact of reduced activity because of the coronavirus outbreak.

While New Zealand banks' current asset quality is very strong, coronavirus-related economic disruptions will lead to increases in problem loans. While the performance of housing and dairy loans, the two largest segments of New Zealand banks' loan portfolios, remains strong, high indebtedness makes borrowers vulnerable to an economic downturn. In particular, a rise in unemployment will hurt the quality of housing loans, which, at about 63% of the system, make up the largest part of banks' loan portfolios.

New Zealand banks have been lengthening the term structure of their market funding for a number of years, and this will greatly offset the risk of New Zealand banks' relatively heavy dependence on wholesale funding, especially from offshore markets.

ESG considerations

In line with our general view for the banking sector, ANZNZ has a low exposure to Environmental risks. See our Environmental risks heatmap for further information.

We consider banks to face moderate social risk. The most relevant social risks for banks arise from the way they interact with their customers. Social risks are particularly high in the area of data security and customer privacy which is partly mitigated by sizeable technology investments and banks' long track record of handling sensitive client data. Fines and reputational damage due to product mis-selling or other types of misconduct is a further social risk. Societal trends are also relevant in a number of areas, such as shifting customer preferences towards digital banking services increasing information technology cost, aging population concerns in several countries impacting demand for financial services or socially driven policy agendas that may translate into regulation that affects banks' revenue base.

Governance is highly relevant for ANZNZ, as it is to all players in the banking industry. For example, in May 2019, the RBNZ required the bank to use the standardised approach for operational risk, following the discovery in April 2019 by ANZNZ, that the bank had not been using an approved model since December 2014 for operational risk. An external review of ANZNZ's compliance with the RBNZ's capital adequacy requirements highlighted a number issues that led to the use of unapproved credit and operational risk capital models. ANZNZ is working with the RBNZ to rectify these issues.

In June 2019 the RBNZ requested a review of ANZNZ's Director's Attestation and Assurance framework. The report highlighted areas of weakness and made a number of recommendation which the bank is required to implement by the end of 2021.

Support and structural considerations

Affiliate support

ANZNZ's ratings incorporate a very high probability of support from its Australian parent, in light of its significance to the overall group's operations, and the close regulatory and political ties between Australia and New Zealand.

Loss Given Failure analysis

There is currently no statutory bail-in in New Zealand. As a result, we do not consider New Zealand to have an operational resolution regime (as defined in our methodology). We apply a basic loss-given-failure (LGF) approach in rating New Zealand banks' junior securities.

In determining whether New Zealand has an operational resolution regime we take into account both the current resolution framework and the New Zealand policymakers' public stance. Whilst the New Zealand authorities have developed a framework to imposes losses on creditors through its Open Bank Resolution (OBR) Policy we view this framework to be a policy tool for responding to a bank failure, rather than a statutory bail-in regime. Furthermore, the RBNZ acknowledged that the OBR is not intended to be the only option in the event of a bank failure and that there may be circumstances in which a private sector solution is available.

Under the basic LGF approach we currently apply in New Zealand, ANZNZ's dated subordinated debt is rated A3, one notch below the bank's adjusted baseline credit assessment (BCA) of a2. Its undated subordinated debt is rated two notches below its BCA, at Baa1.

Government support considerations

The likelihood that systemic support would be extended to the bank in a systemic crisis is viewed as moderate, given the expectations that ANZNZ's parent will be the primary source of support. Our assessment of systemic support also reflects the importance of ANZNZ, like its major bank peers, in funding New Zealand's net external liabilities, and the complexity of their resolution, if required.

Counterparty Risk (CR) Assessment

ANZNZ Bank's CR Assessment is Aa3(cr)/Prime-1(cr)

We consider New Zealand 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)

ANZNZ Bank's CRRs are Aa3/Prime-1

We consider New Zealand 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 Bank Scorecard

Our Scorecard is designed to capture, express and explain in summary form our Rating Committee's judgment. When read in conjunction with our research, a fulsome presentation of our judgment 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 4

ANZ Bank New Zealand Limited

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	0.7%	aa2	↔	a1	Expected trend	Sector concentration
Capital						
Tangible Common Equity / Risk Weighted Assets (Basel III - transitional phase-in)	13.8%	a2	↔	a2	Risk-weighted capitalisation	Stress capital resilience
Profitability						
Net Income / Tangible Assets	1.0%	a3	↔	a3	Expected trend	
Combined Solvency Score		a1		a2		
Liquidity						
Funding Structure						
Market Funds / Tangible Banking Assets	15.1%	a3	↔	a3	Extent of market funding reliance	
Liquid Resources						
Liquid Banking Assets / Tangible Banking Assets	17.0%	baa2	↔	baa2	Additional liquidity resources	
Combined Liquidity Score		baa1		baa1		
Financial Profile				a3		
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				a2 - baa1		
Assigned BCA				a3		
Affiliate Support notching				-		
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	1	Aa3	Aa3
Counterparty Risk Assessment	1	0	a1 (cr)	1	Aa3(cr)	
Deposits	0	0	a2	1	A1	A1
Senior unsecured bank debt	0	0	a2	1	A1	(P)A1
Dated subordinated bank debt	-1	0	a3	0		(P)A3

[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 5

Category	Moody's Rating
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
Senior Subordinate	(P)A3
ST Issuer Rating	P-1
Other Short Term	(P)P-1
PARENT: 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
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

Source: Moody's Investors Service

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CLIENT SERVICES

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

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