Liquidity Risk - including discontinued operations

Liquidity risk is the risk that the Group is unable to meet its payment obligations as they fall due, including repaying depositors or maturing wholesale debt, or that the Group has insufficient capacity to fund increases in assets. The timing mismatch of cash flows and the related liquidity risk is inherent in all banking operations and is closely monitored by the Group and managed in accordance with the risk appetite set by the Board.

The Group's approach to liquidity risk management incorporates two key components:

- **Scenario modelling of funding sources**

  ANZ's liquidity risk appetite is defined by the ability to meet a range of regulatory requirements and internal liquidity metrics mandated by the Board. The metrics cover a range of scenarios of varying duration and level of severity. The objective of this framework is to:

  - Provide protection against shorter term extreme market dislocation and stress.
  - Maintain structural strength in the balance sheet by ensuring that an appropriate amount of longer-term assets are funded with longer-term funding.
  - Ensure that no undue timing concentrations exist in the Group's funding profile.

  A key component of this framework is the Liquidity Coverage Ratio (LCR), which is a severe short term liquidity stress scenario mandated by banking regulators including APRA. As part of meeting LCR requirements, ANZ has a Committed Liquidity Facility (CLF) with the Reserve Bank of Australia (RBA). The CLF has been established to offset the shortage of available High Quality Liquid Assets (HQLA) in Australia and provides an alternative form of contingent liquidity. The total amount of the CLF available to a qualifying ADI is set annually by APRA. From 1 January 2019, ANZ's CLF is $48.0 billion (2018 calendar year end: $46.9 billion).

- **Liquid assets**

  The Group holds a portfolio of high quality unencumbered liquid assets in order to protect the Group's liquidity position in a severely stressed environment, as well as to meet regulatory requirements. High Quality Liquid Assets comprise three categories, with the definitions consistent with Basel 3 LCR:

  - Highest-quality liquid assets (HQLA1): Cash, highest credit quality government, central bank or public sector securities eligible for repurchase with central banks to provide same-day liquidity.
  - High-quality liquid assets (HQLA2): High credit quality government, central bank or public sector securities, high quality corporate debt securities and high quality covered bonds eligible for repurchase with central banks to provide same-day liquidity.
  - Alternative liquid assets (ALA): Assets qualifying as collateral for the CLF and other eligible securities listed by the Reserve Bank of New Zealand (RBNZ).

  The Group monitors and manages the size and composition of its liquid assets portfolio on an ongoing basis in line with regulatory requirements and the risk appetite set by the Board.

	Half Year Average			Movement	
	Mar 19 $B	**Sep 18 $B**	**Mar 18 $B**	**Mar 19 v. Sep 18**	**Mar 19 v. Mar 18**
Market Values Post Discount[1]					
HQLA1	**134.5**	137.0	131.8	-2%	2%
HQLA2	**7.6**	5.1	4.9	49%	55%
Internal Residential Mortgage Backed Securities[2]	**34.2**	38.9	37.8	-12%	-10%
Other ALA[3]	**12.9**	13.1	13.8	-2%	-7%
Total liquid assets	**189.2**	194.1	188.3	-3%	0%
Cash flows modelled under stress scenario					
Cash outflows	**176.3**	177.5	180.5	-1%	-2%
Cash inflows	**38.6**	41.2	40.4	-6%	-4%
Net cash outflows	**137.7**	136.3	140.1	1%	-2%
Liquidity Coverage Ratio[4]	**137%**	142%	134%	-5%	3%

1. *Half year average basis, calculated as prescribed per APRA Prudential Regulatory Standard (APS 210 Liquidity) and consistent with APS 330 requirements.*
2. *In accordance with APRA requirement, March 2019 NZD denominated liquid asset balances beyond that required to achieve 100% NZD LCR must be considered not transferrable and thus excluded from Level 2 LCR.*
3. *Comprised of assets qualifying as collateral for the CLF, excluding internal RMBS, up to approved facility limit; and any liquid assets contained in the RBNZ's Liquidity Policy - Annex: Liquidity Assets - Prudential Supervision Department Document BS13A12.*
4. *All currency Level 2 LCR.*

Funding - including discontinued operations

ANZ targets a diversified funding base, avoiding undue concentrations by investor type, maturity, market source and currency.

$15.3 billion of term wholesale debt with a remaining term greater than one year as at 31 March 2019 was issued during the half year ended 31 March 2019.

The following table shows the Group's total funding composition:

	As at			Movement	
	Mar 19 $B	**Sep 18 $B**	**Mar 18 $B**	**Mar 19 v. Sep 18**	**Mar 19 v. Mar 18**
Customer deposits and other liabilities					
Australia	**203.4**	202.7	204.2	0%	0%
Institutional	**205.4**	205.8	190.7	0%	8%
New Zealand	**85.4**	79.8	79.2	7%	8%
Pacific	**3.5**	3.5	3.4	0%	3%
TSO and Group Centre[1]	**(4.3)**	(4.5)	(4.7)	-4%	-9%
Customer deposits	**493.4**	487.3	472.8	1%	4%
Other funding liabilities[2,3]	**8.6**	8.6	8.5	0%	1%
Total customer liabilities (funding)	**502.0**	495.9	481.3	1%	4%
Wholesale funding					
Debt issuances	**113.4**	105.3	97.5	8%	16%
Subordinated debt	**16.3**	15.9	17.2	3%	-5%
Certificates of deposit	**43.6**	42.7	50.3	2%	-13%
Commercial paper	**14.7**	17.0	24.1	-14%	-39%
Other wholesale borrowings[4,5]	**100.1**	86.8	84.4	15%	19%
Total wholesale funding	**288.1**	267.7	273.5	8%	5%
Shareholders' equity	**60.0**	59.4	59.5	1%	1%
Total funding	**850.1**	823.0	814.3	3%	4%

1. *Includes term deposits, other deposits and an adjustment recognised in Group Centre to eliminate Wealth Australia investments in ANZ deposit products.*
2. *Includes interest accruals, payables and other liabilities, provisions and net tax provisions, excluding other liabilities in Wealth Australia.*
3. *Excludes liability for acceptances as they do not provide net funding.*
4. *Includes borrowings from banks, securities sold under repurchase agreements, net derivative balances, special purpose vehicles and other borrowings.*
5. *Includes RBA open repo arrangement netted down by the exchange settlement account cash balance.*

Net Stable Funding Ratio

The following table shows the Level 2 Net Stable Funding Ratio (NSFR) composition:

	As at			Movement	
	Mar 19 $B	**Sep 18 $B**	**Mar 18 $B**	**Mar 19 v. Sep 18**	**Mar 19 v. Mar 18**
Required Stable Funding[1]					
Retail & small and medium enterprises, corporate loans <35% risk weight[2]	**182.9**	183.9	184.0	-1%	-1%
Retail & small and medium enterprises, corporate loans >35% risk weight[2]	**189.1**	182.6	177.2	4%	7%
Other lending[3]	**23.2**	23.2	19.1	0%	21%
Liquid assets	**10.7**	9.8	9.7	9%	10%
Other assets[4]	**40.2**	36.6	38.4	10%	5%
Total Required Stable Funding	**446.1**	436.1	428.4	2%	4%
Available Stable Funding[1]					
Retail & small and medium enterprise customer deposits	**236.6**	231.7	233.4	2%	1%
Corporate, public sector entities & operational deposits	**91.5**	91.8	83.4	0%	10%
Central bank & other financial institution deposits	**6.1**	5.3	4.2	15%	45%
Term funding	**101.2**	96.3	94.0	5%	8%
Short term funding & other liabilities	**3.7**	1.3	2.7	large	37%
Capital	**73.9**	73.3	74.4	1%	-1%
Total Available Stable Funding	**513.0**	499.7	492.1	3%	4%
Net Stable Funding Ratio	**115%**	115%	115%	0%	0%

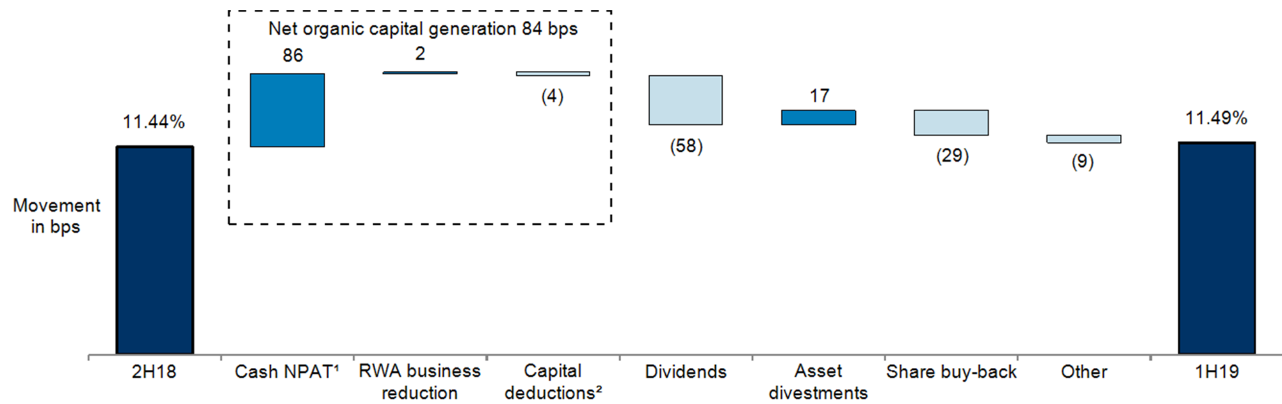
1. *NSFR factored balance as per APRA Prudential Regulatory Standard APS 210 Liquidity.*
2. *Risk weighting as per APRA Prudential Regulatory Standard APS 112 Capital Adequacy: Standardised Approach to Credit Risk.*
3. *Includes financial institution and central bank loans.*
4. *Includes off-balance sheet items, net derivatives and other assets.*

Capital Management - including discontinued operations

	As at					
	APRA Basel 3			Internationally Comparable Basel 3[1]		
	Mar 19	Sep 18	Mar 18	Mar 19	Sep 18	Mar 18
Capital Ratios						
Common Equity Tier 1	**11.5%**	11.4%	11.0%	**16.9%**	16.8%	16.3%
Tier 1	**13.4%**	13.4%	12.9%	**19.3%**	19.2%	18.7%
Total capital	**15.3%**	15.2%	14.9%	**21.7%**	21.6%	21.3%
Risk weighted assets ($B)	**396.3**	390.8	395.8	**310.9**	305.6	311.5

1. *Internationally Comparable methodology aligns with APRA's information paper entitled "International Capital Comparison Study" (13 July 2015)*

APRA Basel 3 Common Equity Tier 1 (CET1 ratio) - March 2019 v September 2018



1. *Excludes large/notable items for the purposes of Regulatory Capital Management attribution. Refer to pages 14 to 18.*
2. *Capital deductions represent the movement in retained earnings in deconsolidated entities, capitalised software, expected losses in excess of eligible provision shortfall and other intangibles in the period.*

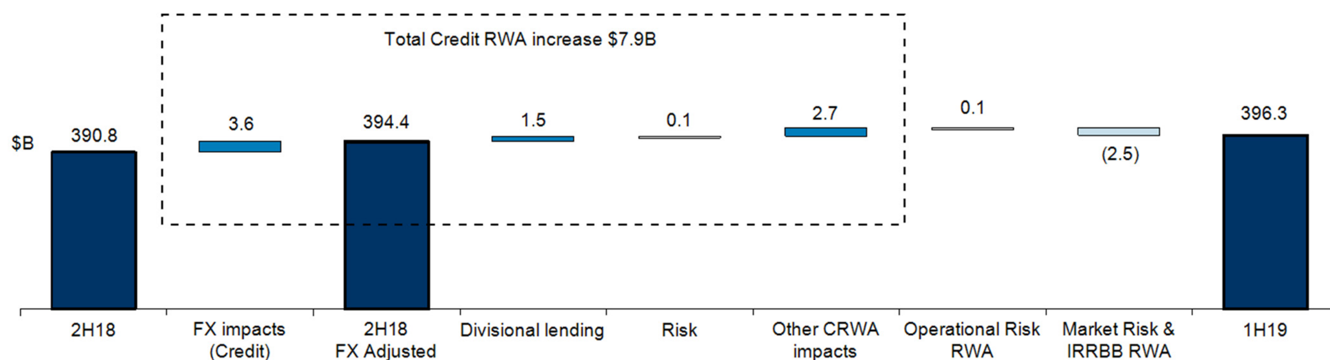
- **March 2019 v September 2018**

  ANZ's CET1 ratio increased 5 bps to 11.5% during the March 2019 half. Key drivers of the movement in the CET1 ratio were:

  - Net organic capital generation of 84 bps. This was primarily driven by cash profit (excluding large/notable items), a net reduction in underlying RWA (excluding foreign currency translation movements, regulatory changes and other one-offs), partially offset by growth in other business capital deductions.
  - Payment of the September 2018 final dividend (net of BOP issuance, neutralised DRP) reduced the CET1 ratio by 58 bps.
  - Capital benefits from asset disposals (OnePath Life (NZ) and Paymark) increased the CET1 ratio by 17 bps.
  - Group on-market share buy-back of $1.1 billion decreased the CET1 ratio by 29 bps.
  - Other impacts include RWA modelling changes, large/notable items affecting the March 2019 half cash earnings, movements in non-cash earnings, impact of AASB 9 transition and net foreign currency translation movements.

Total Risk Weighted Assets	As at			Movement	
	Mar 19 $B	Sep 18 $B	Mar 18 $B	Mar 19 v. Sep 18	Mar 19 v. Mar 18
Credit RWA	**345.5**	337.6	342.8	2%	1%
Market risk and IRRBB RWA	**13.1**	15.6	15.6	-16%	-16%
Operational RWA	**37.7**	37.6	37.4	0%	1%
Total RWA	**396.3**	390.8	395.8	1%	0%

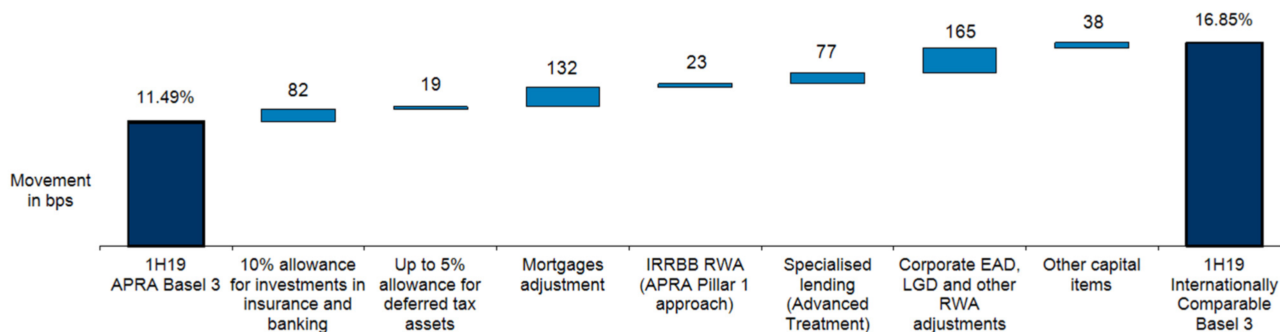
Total Risk Weighted Assets (RWA) - March 2019 v September 2018



- **March 2019 v September 2018**

  Total RWA increased by $5.5 billion. Excluding the impact of foreign currency translation movements and other non-recurring CRWA changes, underlying CRWAs (divisional lending and risk migration) increased by $1.6 billion, mainly driven by lending growth in the Institutional division. Other CRWA changes reflect net impacts from RWA modelling changes. The decrease in non-CRWA of $2.4 billion was mainly driven by a lower risk profile for Market Risk & IRRBB RWA.

APRA to Internationally Comparable[1] Common Equity Tier 1 (CET1 ratio) as at 31 March 2019



1. ANZ's interpretation of the regulations documented in the Basel Committee publications: "Basel 3: A global regulatory framework for more resilient banks and banking systems" (June 2011) and "International Convergence of Capital Measurement and Capital Standards" (June 2006). Also includes differences identified in APRA's information paper entitled "International Capital Comparison Study" (13 July 2015).

The above provides a reconciliation of the CET1 ratio under APRA's Basel 3 prudential capital standards to Internationally Comparable Basel 3 standards. APRA views the Basel 3 reforms as a minimum requirement and hence has not incorporated some of the concessions proposed in the Basel 3 rules and has also set higher requirements in other areas. As a result, Australian banks' Basel 3 reported capital ratios will not be directly comparable with international peers. The International Comparable Basel 3 CET1 ratio incorporates differences between APRA and both the Basel Committee Basel 3 framework (including differences identified in the March 2014 Basel Committee's Regulatory Consistency Assessment Programme (RCAP) on Basel 3 implementation in Australia) and its application in major offshore jurisdictions.

The material differences between APRA Basel 3 and Internationally Comparable Basel 3 ratios include:

Deductions

- Investments in insurance and banking associates - APRA requires full deduction against CET1. On an Internationally Comparable basis, these investments are subject to a concessional threshold before a deduction is required.
- Deferred tax assets - A full deduction is required from CET1 for deferred tax assets (DTA) relating to temporary differences. On an Internationally Comparable basis, this is first subject to a concessional threshold before the deduction is required.

Risk Weighted Assets (RWA)

- Mortgages RWA - APRA imposes a floor of 20% on the downturn Loss Given Default (LGD) used in credit RWA calculations for residential mortgages. The Internationally Comparable Basel 3 framework requires a downturn LGD floor of 10%. Additionally, from July 2016, APRA requires a higher correlation factor than the Basel framework.
- IRRBB RWA - APRA requires inclusion of Interest Rate Risk in the Banking Book (IRRBB) within the RWA base for the CET1 ratio calculation. This is not required on an Internationally Comparable basis.
- Specialised lending - APRA requires the supervisory slotting approach to be used in determining credit RWA for specialised lending exposures. The Internationally Comparable basis allows for the advanced internal ratings based approach to be used when calculating RWA for these exposures.
- Unsecured Corporate Lending LGD - an adjustment to align ANZ's unsecured corporate lending LGD to 45% to be consistent with banks in other jurisdictions. The 45% LGD rate is also used in the Foundation Internal Ratings-Based approach (FIRB).
- Undrawn Corporate Lending Exposure at Default (EAD) - an adjustment to ANZ's credit conversion factors (CCF) for undrawn corporate loan commitments to 75% (used in FIRB approach) to align with banks in other jurisdictions.

Leverage Ratio - including discontinued operations

At 31 March 2019, the Group's APRA Leverage Ratio was 5.4% which is above the 3.5% APRA proposed minimum for internal ratings-based approach ADI (IRB ADI) which includes ANZ. The following table summarises the Group's Leverage Ratio calculation:

	As at			Movement	
	Mar 19 $M	Sep 18 $M	Mar 18 $M	Mar 19 v. Sep 18	Mar 19 v. Mar 18
Tier 1 Capital (net of capital deductions)[1]	**53,075**	52,218	51,125	2%	4%
On-balance sheet exposures (excluding derivatives and securities financing transaction exposures)	**810,915**	785,405	780,272	3%	4%
Derivative exposures	**31,439**	30,676	32,747	2%	-4%
Securities financing transaction exposures	**37,287**	36,066	29,351	3%	27%
Other off-balance sheet exposures	**105,942**	102,810	99,921	3%	6%
Total exposure measure	**985,583**	954,957	942,291	3%	5%
APRA Leverage Ratio	**5.4%**	5.5%	5.4%		
Internationally Comparable Leverage Ratio	**6.0%**	6.1%	6.1%		

1. *Prior period numbers have not been restated for the impact of AASB 15 to align with previously reported regulatory returns.*

- **March 2019 v September 2018**

  APRA leverage ratio decreased 8 bps in the March 2019 half. Key drivers of the movement were:

  - Net organic capital generation of 10 bps from cash profit (excluding large/notable items) less dividends paid.
  - Exposure growth primarily from growth in liquids, trading securities, and securities financing transactions decreased the leverage ratio by 11 bps.
  - Benefits from asset divestments increased the leverage ratio by 7 bps (cash settlement of OnePath Life (NZ) and Paymark). This was offset by the impact of $1.1 billion Group on-market share buy-back during the March 2019 half (-12 bps).
  - Other impacts (-2 bps) mainly driven by non-cash adjustments (-3 bps), large/notable items affecting the March 2019 half cash earnings (-2 bps), offset by deferred tax asset benefits (+2 bps) and other (+1 bps).

Capital Management - Other Regulatory Developments

- **Financial System Inquiry (FSI)**

  The Australian Government completed a comprehensive inquiry into Australia's financial system in 2014 which included a number of key recommendations that may have an impact on regulatory capital levels. APRA initiatives in support of the FSI are:

  - In July 2017, APRA released an information paper outlining its assessment on the additional capital required for the Australian banking sector to be considered 'unquestionably strong' as originally outlined in the FSI final report in December 2014. APRA indicated that "in the case of the four major Australian banks, this equated to a benchmark CET1 capital ratio, under the current capital adequacy framework, of at least 10.5 percent. APRA also stated that the major banks should meet this benchmark by 1 January 2020 at the latest".
  - In February 2018, APRA released a discussion paper that commenced their consultation on the revisions to the capital framework that will produce 'unquestionably strong' capital ratios. The discussion paper summarises APRA's proposal regarding risk-based capital approach for credit, market and operational risk following finalisation of these requirements by the BCBS in December 2017. While the final forms of these proposals will only be determined later in 2020, the Group expects the implementation of any revisions to the current requirements will result in further changes to the risk weighting framework for certain asset classes and other risk types (such as market and operational risks). APRA has announced that it does not expect that the changes to the risk weights will necessitate further increases in capital for ADIs, although this could vary by ADI depending on the final requirements.
  - APRA released a discussion paper in August 2018 on adjustments to the overall design of the capital framework to improve transparency, international comparability and flexibility of the ADI capital framework. The focus of the proposals is on the presentation of the capital ratios to facilitate comparability whilst recognising the relative capital strength of ADIs and measures to enhance supervisory flexibility in times of financial stress. APRA's consultation for the above is currently taking place with final prudential standards planned to be made available by 2020.
  - In relation to Leverage Ratio, APRA released draft prudential standards in November 2018 proposing to set the Leverage Ratio minimum for Internal Ratings-Based (IRB) ADI at 3.5%, in addition to other changes to the calculation of the Exposure Measure. These changes are not expected to have a material impact to the Group.

  APRA's consultation for the above is currently taking place with target implementation by 2022 without any phase-in arrangements.

  On 8 November 2018, APRA released a discussion paper titled "Increasing the loss-absorbing capacity of ADIs to support orderly resolution". The paper is in response to recommendation three of the final report of the FSI. The paper proposes an increase in loss-absorbing capacity of between 4% and 5% of RWA for domestic systemically important banks (D-SIBs), and therefore includes ANZ. The Group is currently consulting with APRA on the proposals.

  Given the number of items that are currently open for consultation with APRA, the final outcome of the FSI including any further changes to APRA's prudential standards or other impacts on the Group remains uncertain.

- **Level 3 Conglomerates (Level 3)**

  APRA is extending its prudential supervision framework to Conglomerate Groups via the Level 3 framework which will regulate a bancassurance group such as ANZ as a single economic entity with minimum capital requirements and additional monitoring of risk exposure levels.

  In August 2016, APRA confirmed the deferral of capital requirements for Conglomerate Groups. This is to allow for the final capital requirements arising from FSI recommendations and from international initiatives to be determined.

  The non-capital components of the Level 3 framework relating to group governance, risk exposures, intragroup transactions and other risk management and compliance requirements came into effect on 1 July 2017. These have had no material impact on the Group's capital position.

- **The Reserve Bank of New Zealand (RBNZ) review of capital requirements**

  In December 2018, the Reserve Bank of New Zealand (RBNZ) released a consultation paper titled "Capital Review Paper 4". This paper relates to possible additional RBNZ capital requirements in relation to ANZ's New Zealand assets, which are separate to the Group's capital measurement and minimum requirements set by APRA. The consultation paper sets out amongst other things:

  - potential increases in the risk weighting applied to the assets of banks in New Zealand; and
  - potential increases to the percentage of capital held against those risk weights in New Zealand.

  The proposed implementation period is five years from the date the requirements are finalised. Based on the potential changes set out in the consultation paper, and ANZ Bank New Zealand Limited's (ANZ New Zealand) balance sheet as at 30 September 2018, the changes imply a potential capital increase in New Zealand of NZ$6 billion to NZ$8 billion (A$5.7 billion to A$7.7 billion). ANZ New Zealand currently has approximately NZ$12.5 billion of Tier 1 capital (A$11.9 billion).

  The overall impact on the Group depends on a number of factors. These include the outcome of the consultation, ANZ New Zealand's balance sheet at the time of implementation, and the outcome of other reviews currently underway by APRA.

  Responses to the consultation paper are due on 17 May 2019. ANZ will engage with RBNZ and APRA on these throughout the consultation period.

- **Revisions to the related entities framework for ADI (APS222)**

  In July 2018, APRA released a consultation paper and draft prudential standards on proposed revisions to its existing related entities framework, which also incorporated changes to its large exposures framework finalised and published in December 2017. APRA's proposals include revisions to:

  - The definition of related entities;
  - The measurement of exposures to related entities by aligning with requirements in the revised large exposures framework;
  - The prudential limits on exposures to related entities. APRA is proposing to align the capital base used in limit calculations to Level 1 Tier 1 Capital (capital base used in the revised large exposures framework) and to reduce the individual and aggregate limits of exposures to individual related ADIs; and
  - The extended licensed entity (ELE) framework by amending the criteria for a subsidiary to be consolidated in an ADI's ELE.

  APRA is currently consulting on the proposed changes. The impact on the Group and its subsidiaries will not be known until APRA finalises its review. APRA intends to have the revised related entities framework implemented by in the first half of 2020.