Mutuals industry review 2018

Maintaining trust in turbulent times

November 2018

KPMG.com.au

Foreword

This report examines the performance and trends of Australia's mutual banks, building societies and credit unions (together, the Mutual sector) as regulated by the Australian Prudential Regulation Authority (APRA).

It includes the financial results of 48 Mutuals for the year ended 30 June 2018 (2017: 52 Mutuals), which represents over 90 percent of the Mutual sector by total assets and profit before tax.

The financial information, analysis and observations have been compiled from publicly available financial reports, APRA statistics and also includes information from the prior year. In certain instances, data has also been obtained directly from survey participants.

This report also includes the results of our qualitative survey, which asked Mutuals to share their views on the risks, challenges and opportunities they see facing the industry. We had a fantastic response rate this year of 100 percent (2017: 75 percent) which demonstrates the Mutual sector's enthusiasm to come together and leverage experiences and operate in unison in the highly competitive banking market.

For the purposes of preparing our charts and analysis, KPMG has disclosed the results of the Top 10 Mutuals by total assets (the Top 10) together with the results of the remaining Mutuals (Mutuals excluding the Top 10).

We have also made reference to the financial results of the Australian major banks (the majors).

We would like to thank the survey respondents for their time and contribution to this report.

Please visit our website for access to the following materials that accompany this report:

— Webinar: A preview into the key findings from our report. This covers both analyses of financial results, and of key responses to our qualitative survey. A recording of the webinar is available.

— Mutuals insights dashboard: Interactive charts and graphs of the financial data collected, which can be filtered based on preferences. An introduction into the dashboard's capabilities is included in the webinar recording.

— Financial datasheet: This details the financial information collected.

Contents

The KPMG Mutuals Insights Dashboard

The KPMG Mutuals Insights Dashboard which accompanies this report contains interactive charts and graphs that are underpinned by the financial data collected from Mutuals surveyed. This dashboard enables you to filter the data based on your own preferences and view the financial metrics for a particular year or segment of the Mutual sector. You can also view metrics for an individual Mutual in comparison to a peer group.

The dashboard can be accessed via our website at **KPMG Mutuals Insights Dashboard**

Year in review – 2018 highlights

30bps

Average capital adequacy ratio increased by **30 bps to 16.36%**

4.6%

Operating profit before tax increased by **4.6% to $634.8m**

1bp

Net interest margin increased **1 bp to 2.04%**

5.0%

Deposits grew by **5.0% to $ 91,933.9m**

1.9%

Non-interest income decreased by **1.9% to $555.9m**

4

5 mergers completed **(2017: 9)**

0.04%

Impairment expenses remained steady at **0.04%** of average gross receivables

6.6%

Residential lending increased by **6.6% to $89.5b**

5.7%

Technology spend rose by **5.7% to $182.9m**

10 current and emerging topics

1 The Trust Agenda

Why trust is important, and what framework to utilise to measure and foster trust.

2 Customer branding and loyalty

How to utilise existing branding of a Mutual to demonstrate trust.

3 Emerging technologies

What are the new upcoming technologies on the horizon for the banking sector? How can a Mutual leverage its size, relationships and often limited budgets to gain exposure to these new technologies?

4 New Payments Platform (NPP)

The progress of the NPP and its take-up in the Mutual sector. What will the current and future state of NPP look like?

5 Open Banking

How is Open Banking regulation world-wide shaping the current state of Open Banking in Australia and are the Mutuals prepared for this?

6 Workforce of the future

How robotics process automation (RPA) and artificial intelligence (AI) are currently shaping the workforce and how they may shape the workforce of the future.

7 Royal Commission

What were some of the key interim findings, how will they impact on trust in the financial services sector? What lessons can a Mutual learn from the Commission?

8 Banking Executive Accountability Regime (BEAR)

What are the right tools for building accountability in all facets of the business? This is in the presence of the sector campaigning for a '#MoreThan4' proportionate regulation.

9 Regulatory changes

How do we utilise the cybersecurity governance regulation to build resilience in our data governance & reporting processes? Further, how can a mutual utilise additional capital raised through Mutual Equity Interests (MEIs) effectively.

10 Tax developments

Managing expectation of all stakeholders, including communities that depend on government funding, the ATO and members in relation to tax.

These questions are here to stay and not addressing them head-on opens the opportunity for others to take the lead in the fight for growth, customers and returns.

Introduction

The year 2018 saw Mutuals perform well, with a balance sheet (net assets) growth of 5.6 percent (2017: 7.3 percent) to $8.9 billion. Overall operating profit before tax, grew by 4.6 percent (2017: fell 4.3 percent) to $634.8 million (2017: $606.7 million) while the squeeze on net interest margins (NIM) has started to stabilise.

The Mutuals' performance has been underpinned by their continued effort in streamlining operations, enhancing products and services, investing in technologies to enhance the customer experience, maintaining pricing discipline, and in some cases, merging to gain economies of scale.

Also impacting these results is a business environment characterised by low interest rates, strong competition, property price fluctuations and an industry being reshaped by a new wave of technological innovation and evolving customer preferences.

The industry is also facing unprecedented political, regulatory and media scrutiny and ultimately, challenges in arresting a decline in trust.

However, it's not just in Australia where trust in financial institutions has diminished - this is also occurring globally. APRA explains 'trust is the currency of banks'. However, this currency cannot be bought, sold or demanded, rather it is built over many years. And as we have observed, it can also be lost quickly.

Against this backdrop, there are many pertinent considerations for Mutuals to consider, in particular, the potential for, and extent, to which recommendations from the Royal Commission into Financial Services and the APRA Prudential Inquiry will impact the Mutual sector, as well as how, and when, to invest in new technologies to enhance the customer experience.

This report explores a number of similar considerations and aims to provide insight into what is on a Mutual's mind when it comes to '**maintaining trust in turbulent times**'.

Starting with trust, we explore 10 current and emerging topics for the sector, being:

1 The Trust Agenda

2 Customer branding and loyalty

3 Emerging technologies

4 New Payments Platform (NPP)

5 Open Banking

6 Workforce of the future

7 Royal Commission

8 Banking Executive Accountability Regime (BEAR)

9 Regulatory changes

10 Tax developments

Refer to page 5 for more details on the 10 topics.

These questions are here to stay and not addressing them opens the opportunity for others to take the lead in the fight for growth, new customers and value for members.

In these 'untrusting' times, Mutuals must take ownership of their customer advocacy and branding efforts and own the trust narrative through their interactions with all stakeholders. Their success lies in their ability to retain their strong branding as `community focused', and providing clear solutions to address the primary pain points and financial wellbeing of members.

Mutuals must also remain vigilant and respond proactively to the challenges of remaining simple, technology-focused, and meeting regulatory expectations, whilst always preserving alignment with member interest and values.

We hope that you find this publication insightful and we look forward to having further discussions with the sector in the coming year.

Brendan Twining
National Sector Leader, Mutuals
KPMG Australia

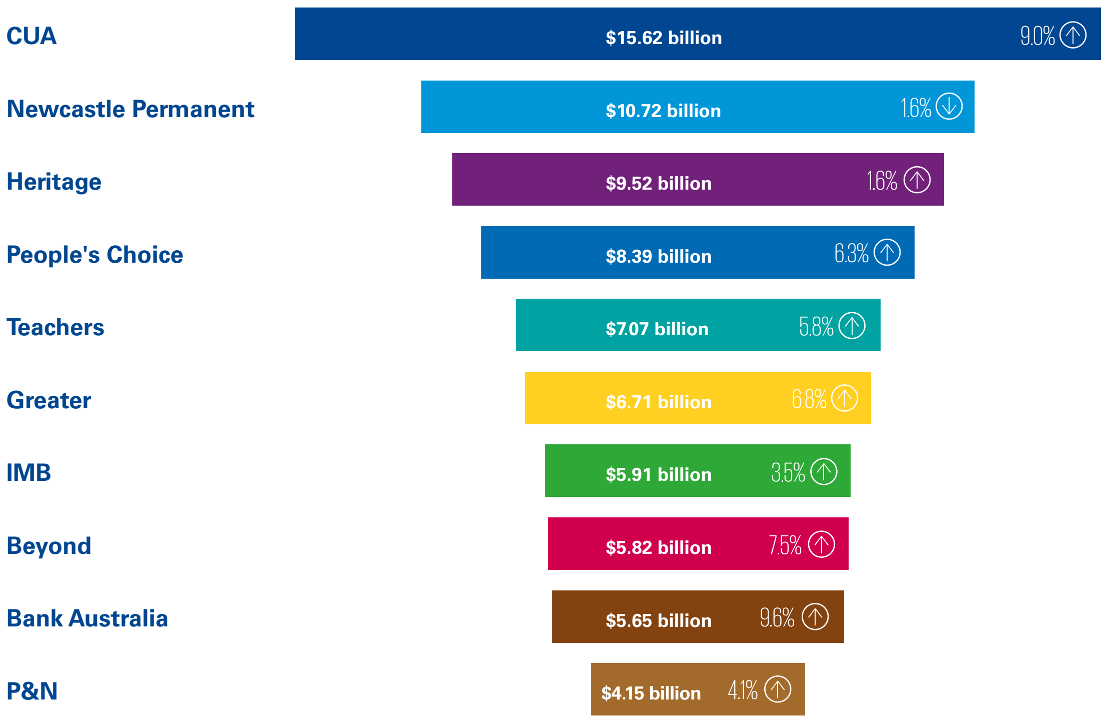
2018 financial results

The 2018 financial year saw the Mutuals record slower growth relative to previous years due to reduction in margins, rising funding costs and growing uncertainty in the current economic and regulatory environment. In the analysis below, we have highlighted some of the key financial results observed across the sector as well as the Top 10 Mutuals (by total assets).

Assets

The Top 10 Mutuals by total assets this year have continued to maintain their ranking since 2016.

Top 10 by total assets – 2018

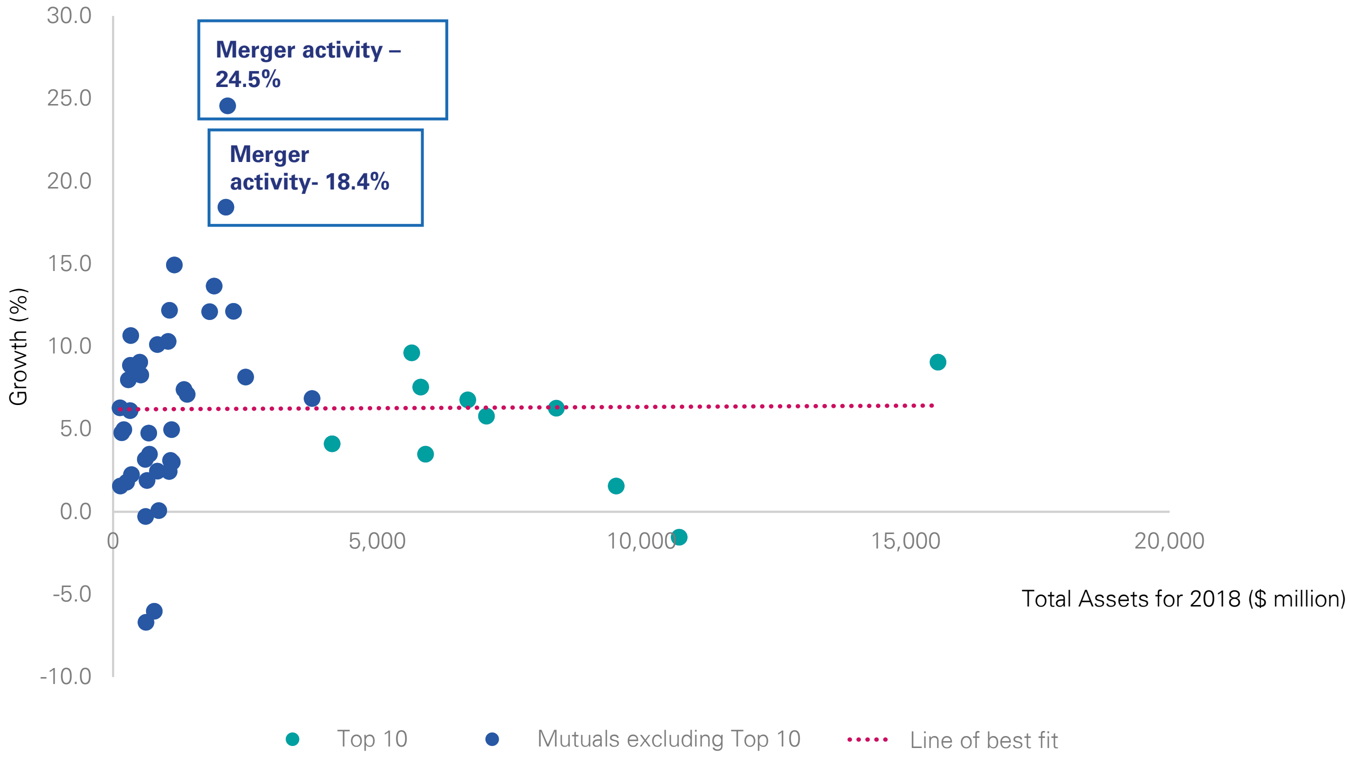


Total assets for Mutuals increased by 5.5 percent (2017: 10.1 percent) to $117.3 billion in 2018 (2017: $111.1 billion), despite a sustained low interest rate environment, an increasingly competitive market, heightened regulatory focus and a decline in trust in the financial services industry.

Despite these factors, Mutuals continue to be seen as an attractive proposition to consumers, with the sector comprising 2.4 percent (2017: 2.3 percent) of total assets across all authorised deposit-taking institutions (ADIs) in Australia at 30 June 2018. However, the majority of responses to our survey indicated the majors remain the dominant competitive force, albeit they too are facing substantial industry headwinds.

This is evidenced by the fact that while the Top 10 grew their combined assets by 5.1 percent (2017: 11.0 percent), the majors showed an increase of 2.6 percent, despite heightened regulator and community focus.

Growth in Total Assets (%) - 2018



Some Mutuals excluding the Top 10 exhibited double-digit growth, particularly through consolidation as Mutuals target achieving economies of scale in their operations. Examples include Queensland Country Credit Union, RACQ Bank and Credit Union SA.

Of the Top 10 Mutuals, only Newcastle Permanent experienced a drop in total assets in 2018 to $10,716.1 million (2017: $10,884.4 million). This was due to a decrease in value of its investment portfolio.

Top 10 Total Assets (2014 - 2018)

Factors driving growth in total assets is also analysed further in the following sections.

Loan portfolio

The total loan portfolio for Mutuals in 2018 was $96.0 billion (2017: $90.3 billion), a 6.3 percent increase from 2017 (2017: 10.3 percent). The lower growth rate was due to tighter APRA lending restrictions and increased competition, particularly from the majors and non-bank lenders.

The Mutual sector outperformed overall growth in the market of 4.0 percent across all ADIs, perhaps reflecting the Mutuals' focus on building their customer bond and community involvement, a topic which 63.8 percent of the respondents to our survey agree with.

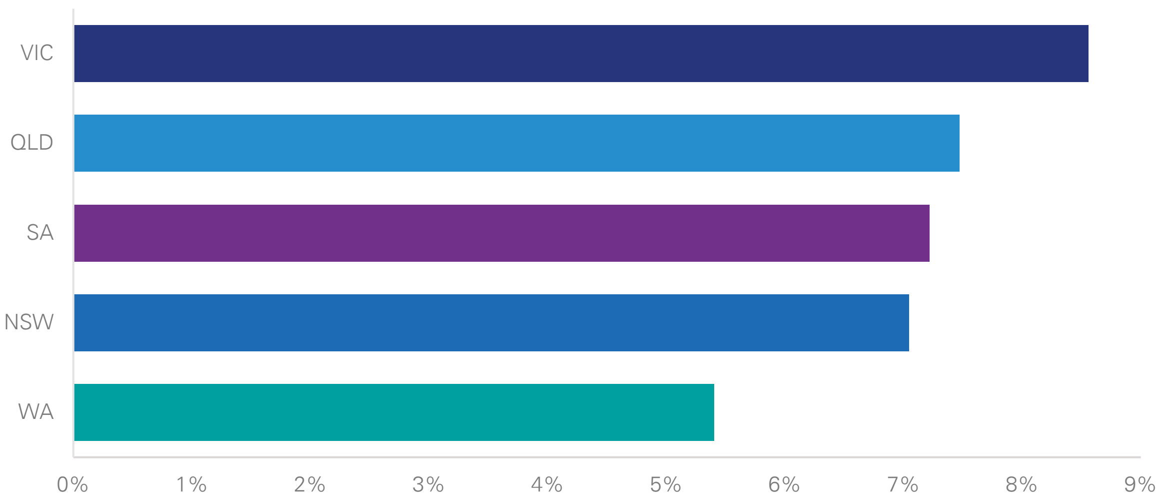
The Mutuals' loan book remained concentrated on residential lending with 93.3 percent (2017: 93.0 percent) of their portfolio comprising residential loans at 30 June 2018.

With the average property price decreasing by 0.6 percent in 2018 (per Australian Bureau of Statistics (ABS) data), compared to the strong growth in prior years, the risk of a market correction needs to remain front of mind.

The slowdown in the growth rate of residential loans reflects tighter lending standards in light of prudential reviews conducted by APRA, enhanced serviceability requirements, and an increasing number of Mutuals getting involved in mergers outside the sector, such as Novo Credit Union merging with Bendigo Bank.

Housing affordability is another factor that has affected the growth in residential loans. With a wage growth rate of only 2.1 percent in 2018, and a high amount of debt, Australians are considering alternatives to taking out loans.

Growth in residential loans split by state – 2018



Note: ACT and TAS were excluded from the data for the purposes of this chart

The ABS reports that Australia is experiencing a continued increase in population, reaching a milestone of 25 million people in mid-2018. This, coupled with a strong labour market, and economic policies to redirect and incentivise populations to inhabit various areas across Australia, are all affecting the increase in the residential loan portfolio.

The strong growth in residential loans in Victoria and Queensland is linked to the spike in population growth of 2.2 percent and 1.7 percent, respectively.

In the face of competition, Mutuals have aimed to grow market share by discounting new loans. 61.7 percent of our survey participants indicated that competitive pricing was one of the main contributors to their financial and market share growth in 2018.

Apart from pricing strategies, Mutuals have tried to differentiate the home loan experience through better customer service and product offerings, as well as increasing investment in technology.

Innovation has focused on areas such as websites that search and select properties. The next wave will need to focus on delivering a new customer 'centric' experience, disrupting the economics of under-writing mortgages or helping ADIs better manage risks and responsible lending obligations.

Did you know…?

2018 Canstar Award winners include:

- Customer-Owner Institution of the Year – Bank Australia
- Personal Lender of the Year – People's Choice
- Home Lender of the Year – Greater Bank
- Investment Lender of the Year – Newcastle Permanent

Asset Quality

Current view of Asset Quality

The Mutual sector continued to manage asset quality with the doubtful debts expense as a percentage of loans and advances (the doubtful debts expense ratio) remaining flat. Despite the fact that provisions as a percentage of gross loans and receivables have remained relatively flat at 0.07 percent, loan write-offs have increased by 33.9 percent to $39.4 million (2017: $29.4 million) mainly driven by write-downs in the personal loan portfolios.

Since the majority of the Mutuals' loan portfolio is comprised of residential loans, the Mutuals can potentially be exposed to macroeconomic factors impacting the retail sector.

Recently, there have been signs of pressure on household debt levels, combined with loans rolling from fixed to variable rates, and the potential for official interest rate increases in 2019 and beyond. Mutuals will need to keep a close watch on the performance of their loan portfolios going forward.

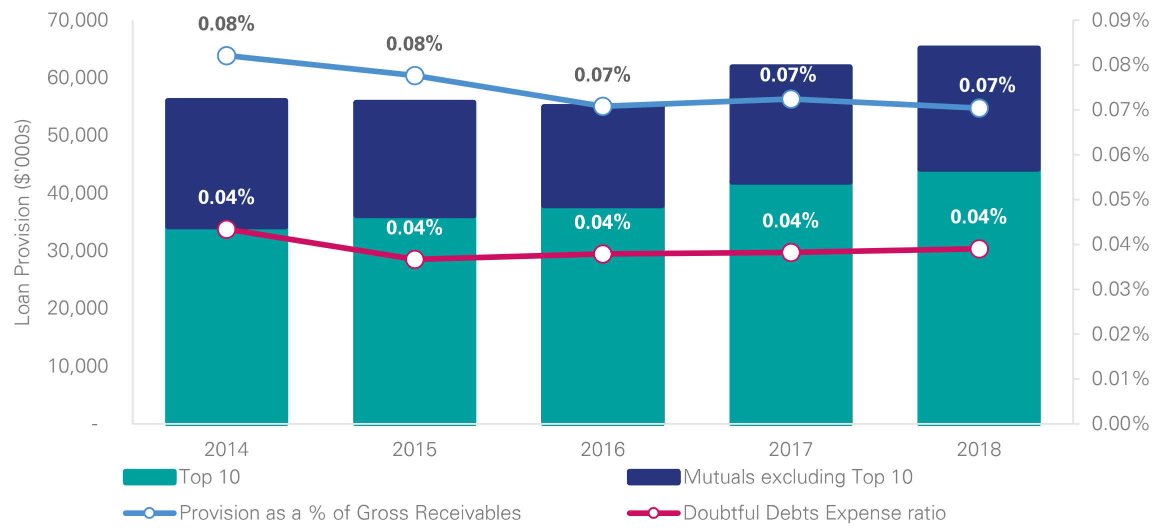
AASB 9 lens on Asset Quality

In the next financial year we expect to see larger provisions for loan impairment on balance sheets, as Mutuals implement an expected credit loss model in accordance with AASB 9 *Financial Instruments* which comes into effect for 30 June 2019 annual reports. Only a few Mutuals have been early adopters of AASB 9, but almost every Mutual in our survey has performed a preliminary assessment of AASB 9 on their loan provision accounts.

The impact of AASB 9 will be an increase in collective provisions. This is referenced by the fact that the majors have reported estimated increases of 31 percent for CBA, 27 percent for ANZ and 35 percent for Westpac, as noted in KPMG's Major Australian Banks Full Year 2018 Results Analysis.

This increase is consistent with the quantification performed by the Mutuals in their 30 June 2018 financial reports.

Impairment Provisions (2014 - 2018)



Capital

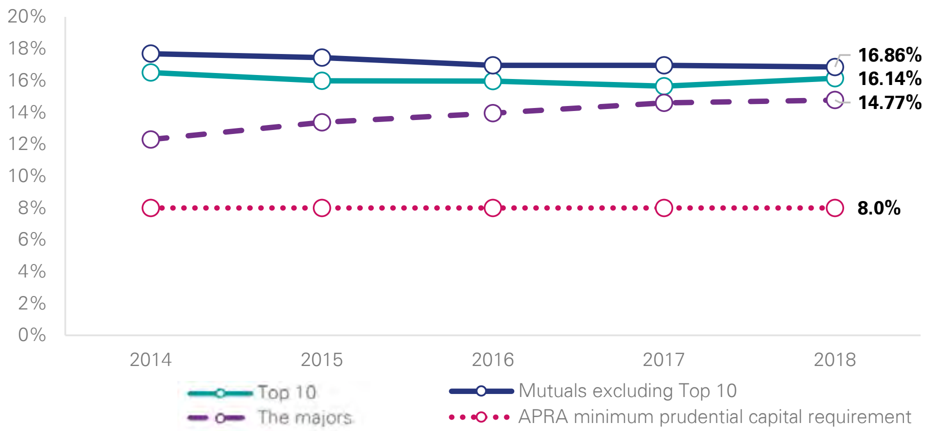
Current position

The Mutuals have increased their weighted average capital adequacy ratio by 30 bps to 16.36 percent (2017: 16.06 percent). This was largely attributable to the Top 10 who have increased their weighted capital adequacy ratio by 49 bps to 16.14 percent (2017: 15.65 percent). This was due to a slowdown in the growth of their residential loan portfolio and a significant increase in retained earnings driven by an increase in net interest income.

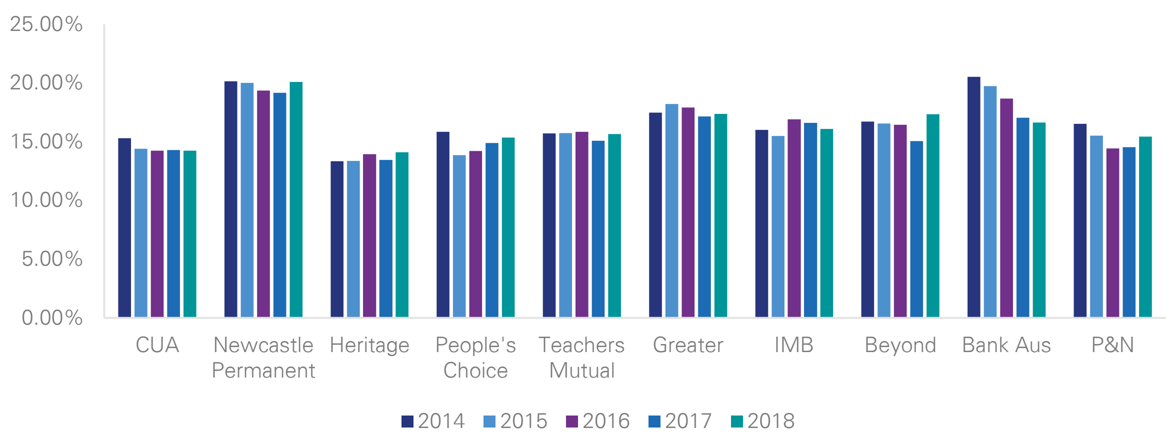
However, the weighted average capital adequacy ratio for the remaining Mutual sector dropped 10 bps (2017: increased by 0.4 bps) to 16.86 percent (2017: 16.96 percent) in 2018, representing a decline of 60 bps over the past 5 years.

The industry has maintained capital levels significantly in excess of APRA's minimum Prudential Capital Requirements of 8 percent, and the Mutuals are well positioned to meet APRA's 'unquestionably strong' benchmark CET1 ratio of 10.5 percent by 1 January 2020. This is consistent with the current position of the majors.

Average total capital adequacy ratio (2014 - 2018)



Top 10 capital adequacy ratio (2014 - 2018)



Capital journey ahead

Policy and regulatory developments in the Mutual sector and the banking industry more broadly have focused on building levels of competition in the banking industry more broadly and providing Mutuals with access to additional capital sources.

In November 2017, the Federal Government acknowledged four recommendations, in the Senate Committee Report on the *'Cooperative, Mutual and member-owned firms'* aimed at making it easier for Mutuals to raise capital.

In February 2018, APRA announced that it will include a risk-weighted asset floor for banks using the internal-ratings based approach in its revised capital framework, with a proposed implementation date of 1 January 2021. This will see the majors apply a mandatory minimum risk weighting to their loan portfolios thereby requiring them to increase their capital position to support their lower risk-weighted loans.

Another favourable change for the Mutuals is APRA's requirements for the major banks to recalibrate to a higher minimum capital requirement by approximately 150 bps compared to a lower increase of 50 bps for ADIs that utilise the standardised approach (including the Mutuals). These changes are required to be implemented by 2020.

In October 2018, the Australian Government issued a draft *Treasury Laws Amendment (Mutual entities) Bill* 2018, which would amend the Corporations Act definition of a Mutual entity and remove uncertainty for Mutuals seeking to raise capital without losing their Mutual status. If the Bill passes, it would assist Mutuals in issuing new capital instruments with reduced regulatory setback. This would enable the Mutuals to further compete against the majors in the lending markets.

91%

of the respondents have assessed their current position against APS 111

Effective from 1 January 2018, Mutuals can directly issue MEIs as Common Equity Tier 1 capital instruments. However this requires pre-approval from APRA along with legal documentation supporting that this will not trigger a demutualisation provision in the Corporations Act. Based on our review of the financial statements of the participants in our survey, we noted that no Mutuals have currently issued MEIs. Working through these provisions will effectively provide an additional source of funding beyond retained earnings as stated in the revised *APS 111 Capital Adequacy Standard.*

Together, these regulatory and legislative changes have been designed to increase the ability of the Mutuals to gain access to capital, and enhance their ability to compete in the market.

Deposits

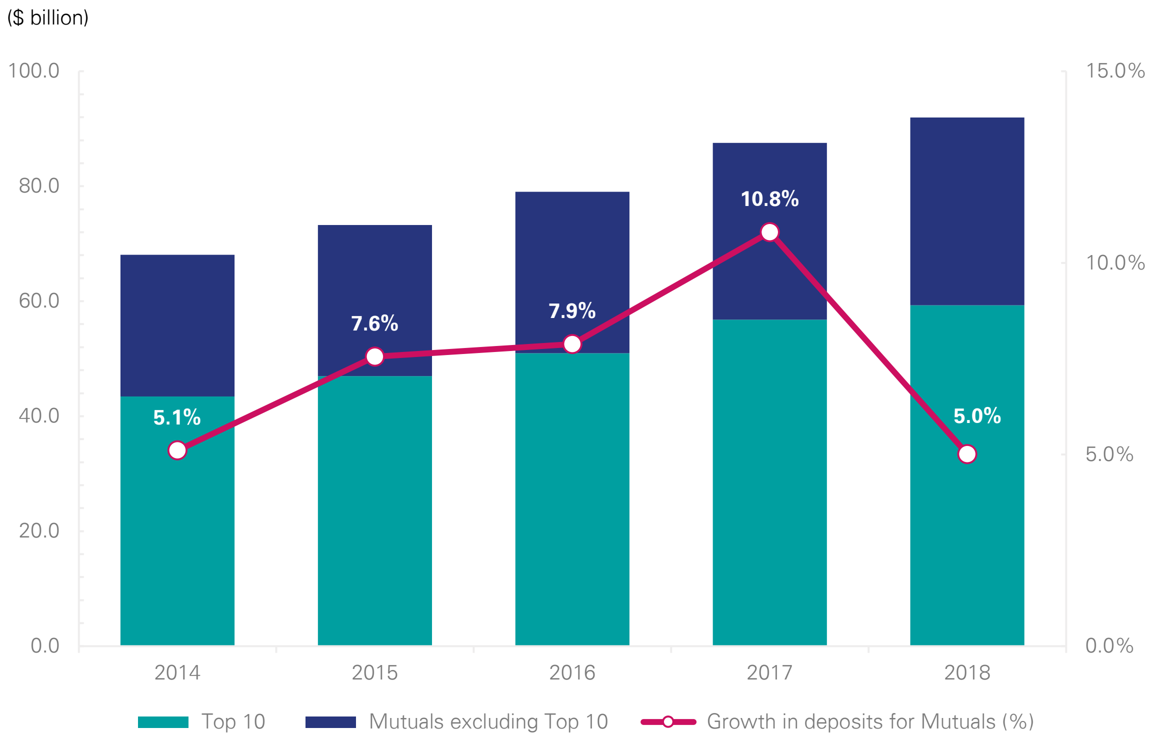
Growing deposits, as a source of funding, has been a challenge for the banking sector in 2018, with a system growth (being the growth observed across all ADIs in the banking sector) of 1.5 percent, and a decline in the household savings rate in Australia, which is currently at a 10-year low. The growth in total deposits has also been affected by the uncertainty and diminishing trust in the current period.

The Top 10 had a deposit growth of 4.4 percent (2017: 11.5 percent) while Mutuals excluding the Top 10, demonstrated a slightly stronger performance with a growth of 6.1 percent, albeit still below the prior year growth (2017: 9.6 percent).

Total deposits grew by 5.0 percent in 2018 (2017: 10.8 percent) which was above the majors' growth of 2.0 percent. This brings total deposits to $91.9 billion for 2018 (2017: $87.6 billion). This continues to reflect another year where Mutuals have focused on member acquisition, achieved through investments in technology, and a simplification of core product offerings.

Over the course of 2018, it was clear that as a 'member-owned, member-first' institution with a focus on community, Mutuals continue to position themselves in the market as an attractive banking alternative (to the majors).

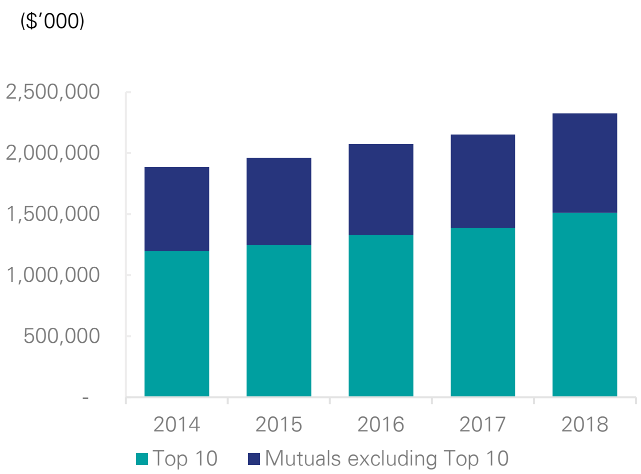
Total deposits and growth in deposits (2014 - 2018)



Net interest income

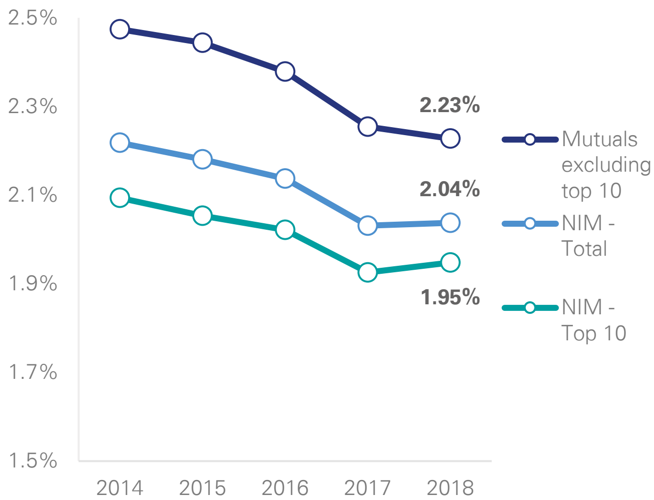
In 2018, Mutuals reported an increase in net interest income of 8.0 percent to $2,326.4 million (2017: $2,153.6 million). Of this, 65.0 percent was earned by the Top 10 (2017: 64.4 percent). This resulted from gross loans and advances outgrowing deposits by 1.3 percent during the year (gross loans and advances grew by 6.3 percent to $96,007 million and deposits grew by 5.0 percent to $91,933 million).

Net interest income (2014 –2018)



Pressures on margins become apparent in a low interest rate period and a highly competitive market. The NIM for Mutuals excluding Top 10 continued its decline with a NIM of 2.23 percent (2017: 2.25 percent). The Top 10 experienced a slight improvement in NIM of 2bps to 1.95 percent (2017: fell by 9bps to 1.93 percent).

Net Interest Margin (2014 – 2018)

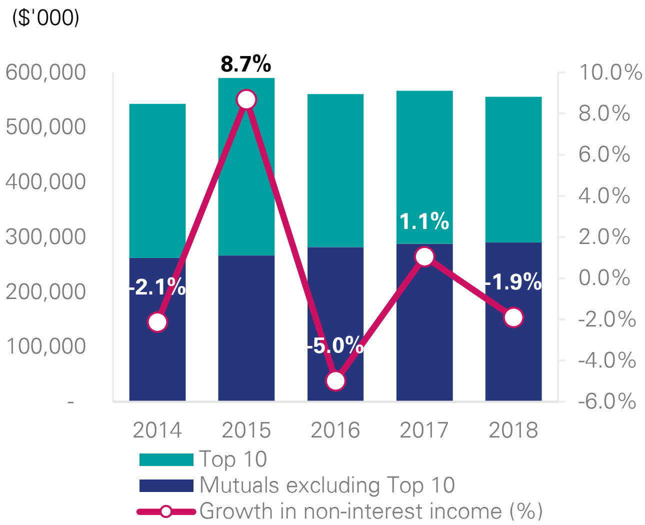


Non-interest income

In 2018, total non-interest income fell by 1.9 percent (2017: grew by 1.1 percent) to $555.9 million (2017: $566.7 million).

The Top 10 reported a steeper decline of 4.7 percent (2017: fell by 0.2 percent). This drop is consistent with a drop observed by the majors as the ADI market continues to face competitive pressure and regulatory scrutiny on fees and commissions and a more competitive environment. Mutuals excluding the Top 10 reported an increase of 0.8 percent, which was slower than the 2017 growth of 2.3 percent.

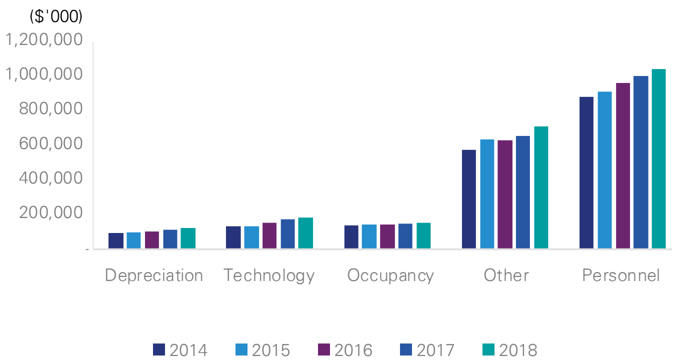
Non-interest income (2014-2018)



Costs

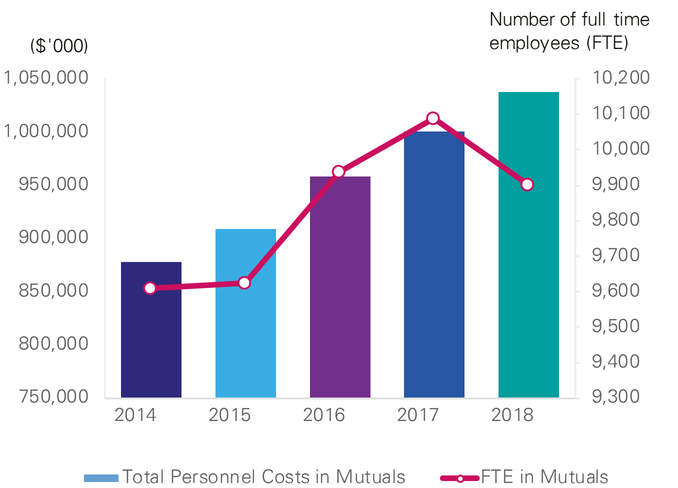
Total operating costs for Mutuals increased by 5.7 percent in 2018 (2017: 5.5 percent) to $2,201.8 million (2017: $2,083.4 million). With a consistent increase in income, cost to income marginally decreased to 76.4 percent (2017: 76.6 percent).

Growth in costs (2014 – 2018)



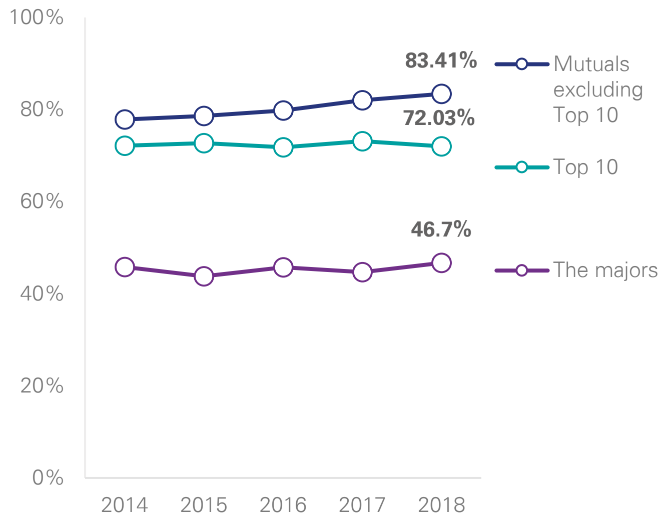
Personnel expenses continue to be the majority of the operating costs at $1,037.9 million in 2018 (2017: $1,000.6 million). This reflected an increase of 3.7 percent (2017: 4.4 percent) although the total number of employees decreased from 10,088 in 2017 to 9,902 in 2018, reflecting a continued rise in highly skilled employees in the workforce in a more technologically inclined industry.

Personnel expenses (2014 – 2018)



Other expenses, mainly consisting of administrative and distribution costs, is the next major cost, with its proportion to total operating expense increasing to 32.2 percent (2017: 31.4 percent). An emphasis on developing efficiencies and streamlining processes will assist in reducing these costs over time.

Cost to income ratio (2014 – 2018)



The Top 10 experienced an increased efficiency relative to the Mutuals excluding the Top 10, where they have been able to benefit from economies of scale and the implementation of their technology initiatives.

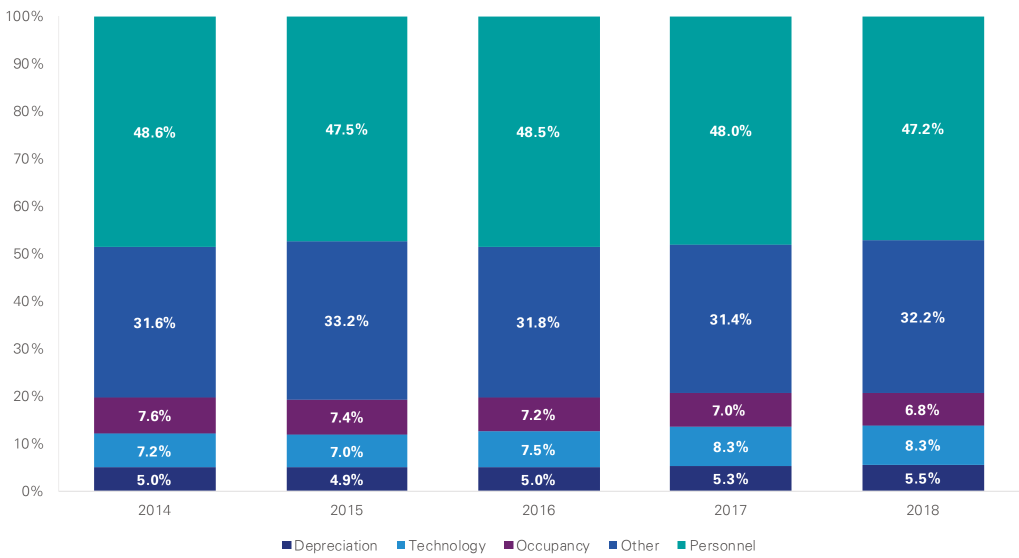
While consolidation, aimed at creating economies of scale and remaining competitive against other deposit-taking institutions, continued during 2018, new technology is another area whereby Mutuals can explore further cost efficiencies and productivity improvements. Mutuals will need to weigh the initial investment against the long term benefits that could be realised.

While total investment spend has increased, in most cases the proportion of investment spend on growth initiatives has decreased on a relative basis. During 2018, growth in technological investments for the Top 10 has significantly slowed to 4.2 percent compared to the growth of 20.6 percent in 2017.

Following the footsteps of the industry leaders, other Mutuals (excluding Top 10) in 2018 have continued to invest in technological innovation.

Digital transformation must be a core business strategy for the Mutual sector not only to improve customer experience but for better operational efficiency and removing complexity in operations. This is a consistent theme highlighted by our survey whereby survey participants observed that, doing more with less is the single biggest opportunity for the mutual sector to improve financial performance.

Composition of costs (2014-2018)



Profits

Profits before tax (PBT) grew by 4.6 percent (2017: fell 4.3 percent) to $634.8 million (2017: $606.7 million), while the majors saw profits grow by 0.9 percent. This was driven by the simplification of products and a continued focus on cost efficiencies, where 74.5 percent of our survey respondents say this was one of the main strategies implemented to improve customer experience.

The increase in total income of 6.0 percent (2017: 3.2 percent) is consistent with the continued focus of Mutuals towards their core products (residential loans). This is emphasised by the significant growth in net interest income at 8.0 percent, offset by non-interest income which fell by 1.9 percent.

Mutuals are also beginning to realise the benefits from planned mergers over the past few years as they move towards achieving economies of scale, especially during a period of substantially low interest rates.

With the introduction of MEIs (securities for the purposes of fundraising provisions in Part 6D.2 of Corporations Act) under the Hammond Review, Mutuals will be able to access and provide additional sources of capital, indicating a shift of focus from profit enhancements towards objectives such as investing in their customer journey experience.

Did you know…?

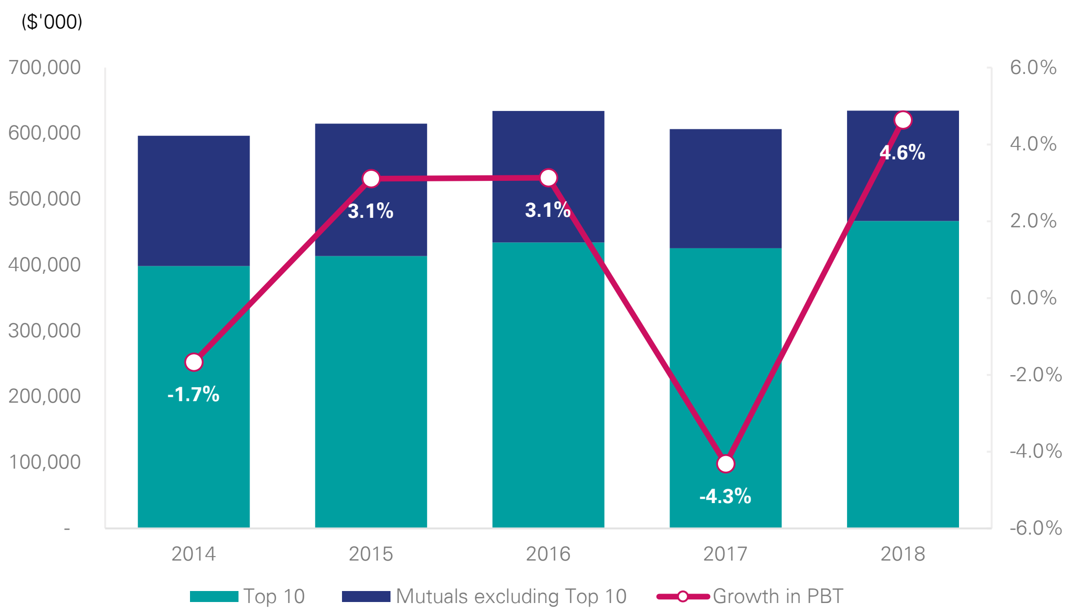
The three biggest opportunities identified by our survey for the Mutual sector to improve performance are:

1 Improving efficiency (27.7 percent)

2 More collaboration with alliance partners (23.4 percent)

3 More collaboration with peers (17.0 percent)

Profit before tax (2014 -2018)



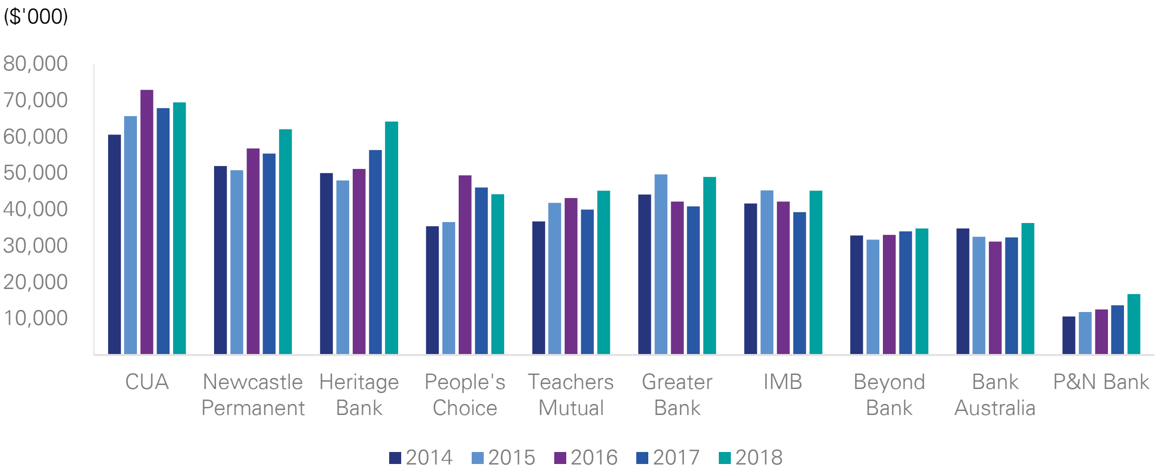
The Top 10 Mutuals have experienced a particularly large increase in PBT in 2018 of 9.8 percent (2017: 2.1 percent decrease), with Greater Bank experiencing the largest increase of the Top 10, an increase of $8.1 million in profit to $48.9 million (2017: $40.8 million), attributed to an increase in revenue in relation to loans and advances.

Although the Top 10 Mutuals are more profitable relative to 2017, the focus on broadening the target market should not be lost. With new and exciting opportunities such as MEI and digital banking, Mutuals should find it easier to target the next generation to be able to maintain a high profitability in the future.

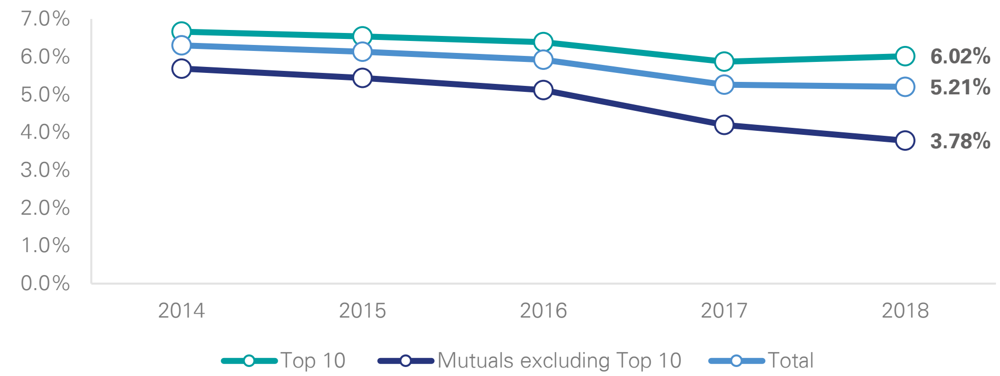
Return on equity (ROE)

Total ROE marginally decreased by 0.1 percent (2017: fell by 0.7 percent) to 5.2 percent (2017: 5.3 percent). The Top 10 performed better than the sector, with ROE of 6.0 percent (2017: 5.9 percent), while Mutuals excluding the Top 10 reported ROE of 3.8 percent (2017: 4.2 percent). This gap is due to the Top 10 experiencing better operating efficiency due to scale and cost efficiencies from investment in technology. Higher financial leverage also contributed to the result.

Top 10 Total Profit before Tax (2014 – 2018)

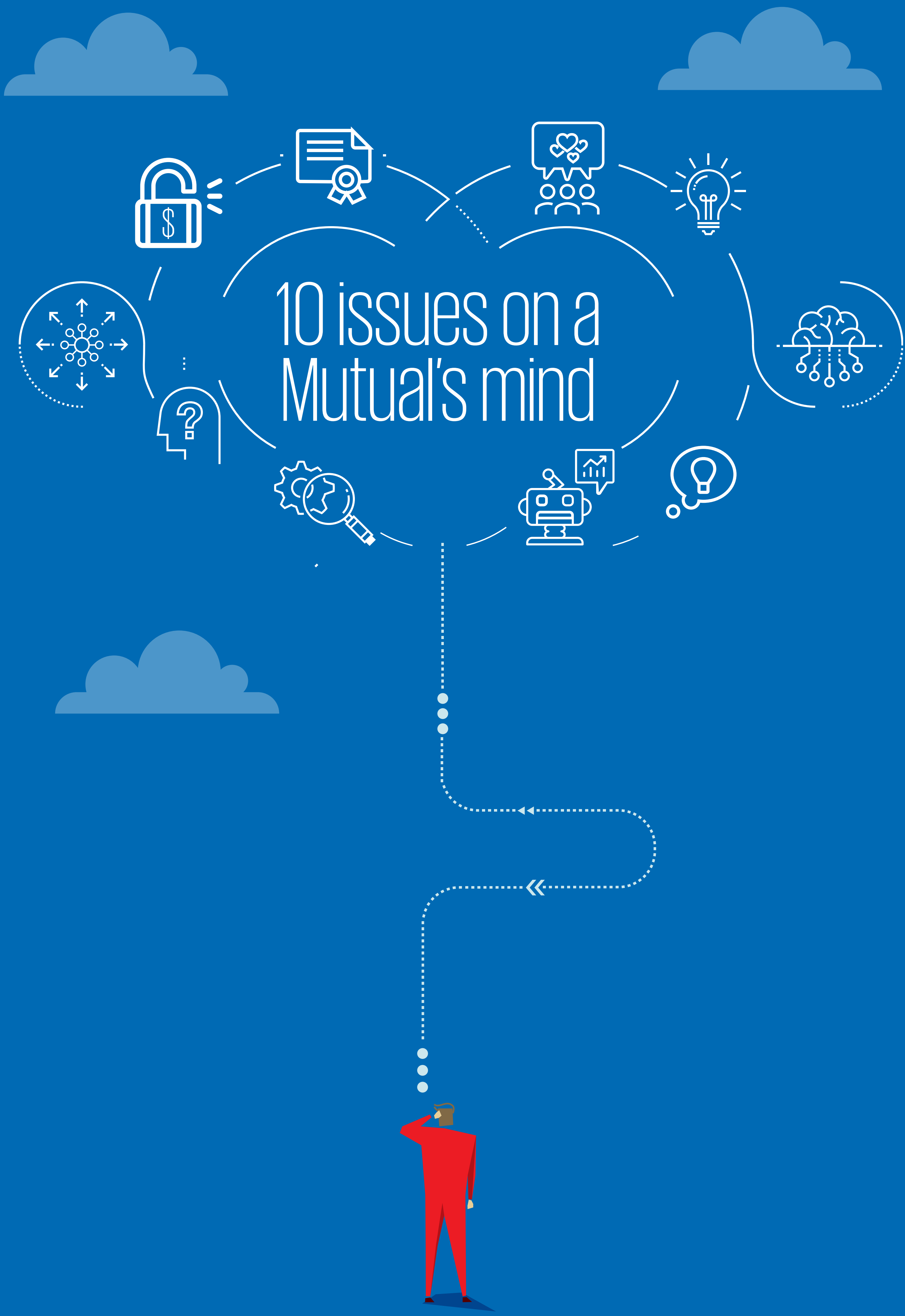


Return on equity (2014 - 2018)



> "Companies should not have a singular view of profitability. There needs to be a balance between commerce and social responsibility... the companies that are authentic about it will wind up as the companies that make more money."
>
> **Howard Schultz**
>
> Former CEO, Starbucks

10 issues on a Mutual's mind



01 The Trust Agenda

Richard Boele, Partner, Assurance and Risk Consulting
Rita Fentener van Vlissingen, Associate Director, Audit, Assurance and Risk Consulting

Trust in financial institutions has been significantly diminished globally, and in Australia. Hearings from the Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, and the recommendations emerging from the APRA Prudential Inquiry into the Commonwealth Bank of Australia, have led to multiplying conversations about corporate trust in boardrooms.

At the centre is the **harm done to customers**. As noted in the APRA report, "Trust is the currency of banks, and improper conduct that undermines confidence or causes harm to customers devalues that currency."

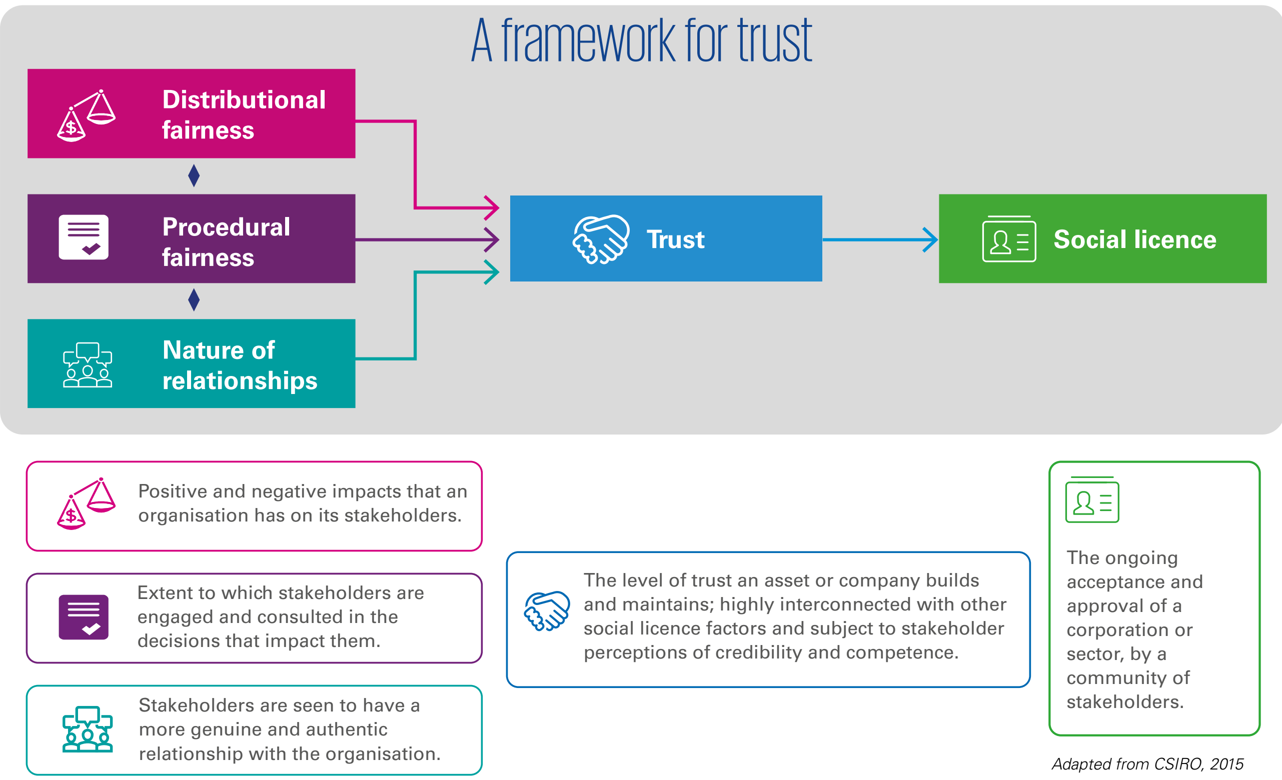
The lack of adequate processes to listen to and escalate customer voices – in particular complaints – and the existence of incentives that ignored customer outcomes, have had far reaching consequences for the lives of impacted individuals and their families.

Although Mutuals are well placed to maintain stakeholder trust, they must adequately identify and escalate customer issues and proactively listen to a broader range of stakeholder voices beyond their members.

Mutuals are well placed to maintain stakeholder trust in the current environment

Being customer-owned means that the nature and the quality of a Mutual's relationships with its customers is different to its other shareholder return focused competitors.

Mutuals should consider factors that contribute to trust and social licence, including how they impact their stakeholders, the level of perceived fairness in how decisions are made and the quality of their relationships with all their stakeholder groups.



Adapted from CSIRO, 2015

A reputation for integrity and fairness goes a long way in maintaining members' trust and their loyalty. It also supports existing members' word of mouth, which remains a key channel for Mutuals to attract new customers.

Mutuals haven't had a crisis of trust – why is this important?

Mutuals have not suffered significant breakdown of trust to date. However, the erosion of trust in the financial services sector can have a contagion effect across the broader industry.

An example is the regulatory change that results from a trust deficit, such as the BEAR, which are not necessarily aligned to the risk profile of the Mutual sector, but applies to all ADIs.

Another example is the 24 hour media cycle and social media, which are agnostic to the nature of the organisations that make up their headlines. Increased scrutiny and sensitivity around issues facing financial services customers can lead to the escalation of negative customer experiences, and lead to the perception of harm, regardless of intent.

Importantly, the fact that Mutuals are member-owned and not publicly listed does not mean they are immune. Even trust in other sectors that do not focus on profit is in decline (ref: Edelman Trust Barometer 2018) with many NGOs struggling to rebuild a reputation severely damaged by scandals involving their employees and contractors.

It is important for Mutuals to look internally as well as externally when thinking about trust, as an organisation's culture and the actions of its employees are essential to its integrity.

Mutuals can start with these three questions:

- How do we identify dissatisfaction amongst customers?
- How do we identify our most vulnerable stakeholders?
- How prepared are we for the impacts of technology and digitisation on our members and other stakeholders?

How do Mutuals identify dissatisfaction amongst their customers?

Mutuals are known to have some of the highest levels of customer satisfaction in the Australian banking market (according to the Customer Owned Banking Association or COBA).[1] These should not be interpreted, on their own, as an indicator of trust. The APRA Prudential Inquiry highlighted CBA's industry-leading customer satisfaction scores – these didn't prevent the customer voice being muted.[2]

Allocating enough time and resources to understanding the root causes of customer dissatisfaction, can be a source of meaningful insights.

An accessible and effective customer complaints and grievance mechanism is an important tool to identify existing and emerging issues negatively impacting customer experience. The customer information that call centre operatives or complaints mechanisms collect should be analysed alongside other sources of data.

Responding to customer complaints and stakeholder concerns transparently and in a timely manner helps to maintain trust but a focus on customers alone is not enough. A focus on 'listening' to stakeholders and identifying their emerging issues and concerns will be critical for mutual trustworthiness.

How do Mutuals identify their most vulnerable stakeholders?

Actively listening to customers, and in particular to a Mutual's most vulnerable stakeholders, will help identify red flags and can help Mutuals respond to issues before they are escalated, or prevent issues from occurring.

The most confronting examples of misconduct in the financial services sector have been actions impacting the most disadvantaged, or voiceless stakeholders (e.g. charging deceased people).

For a Mutual, vulnerable stakeholders can include customers in hardship, those living with a disability, those affected by a natural disaster, or those experiencing significant life changes. They needn't be customers – stakeholders can include potential customers, customers' families, their communities, as well as suppliers or contractors that are affected by the Mutual's business and its operations.

How prepared is a Mutual to manage the impacts of technology and digitisation on members and other stakeholders?

Offering a seamless customer experience via online and mobile platforms, as well as across borders, continues to be critical, in particular for the next generation customers who highly value convenience and access. It is an important contributor to trust as it demonstrates a Mutual's competence and ability to navigate the changing technological environment and evolving customer expectations.

However, Mutuals must also help ensure that digitisation and other transformations to their business model or processes do not disproportionately impact their existing member base or unintentionally discriminate against particular groups.

For example, the closure of branches in regional or rural areas may have a disproportionate impact on members who aren't digitally savvy or those who do not have suitable alternatives to access the financial services they need.

Access to value adding products, services, such as apps, tools and rewards, should be also **fair and inclusive**. Vulnerable members and potential customers must be taken into consideration when designing new products and services, or making significant changes to existing systems and processes.

Last but not least, keeping customer details private and managing their data appropriately is critical to building and maintaining trust and is one of the biggest risks facing Mutuals and their members.

Cyber security and data privacy can transform your average customers into vulnerable stakeholders within seconds. Recent cyber security and data privacy failures have had devastating consequences on the social licence of companies to operate, and the extent to which personal information can be trusted in a digital world.

Steps into developing trust without communicating how that trust is built, or what it represents, may not lead to intended outcomes. Without the right marketing or branding efforts, the key messages around what differentiates a Mutual from other ADIs may be forfeited. Branding and marketing, and keeping customers at the centre of decisions, is critical.

02 Customer branding and loyalty

Hessel Verbeek, Partner, Banking, KPMG Strategy
Michael Rowland, Partner, Customer, Brand and Marketing Advisory

In the current trust environment, companies must deliver quality services, respond to issues, and manage their customers' expectations by creating a customer-centric, connected enterprise. The way a Mutual markets itself and communicates its brand must align to its objectives. To deliver quality customer experiences, organisations must foster a strong connection amongst customers, business functions, employees, partners and the digital ecosystem.

Keeping the customer at the heart of decision making is one thing, but equally important is a Mutual being able to clearly articulate how they will add value to the customer, key stakeholders, and broadly the community. Without this clear communication, messaging around core principles may not be apparent.

Recently, there has been a shift towards Mutuals labelling themselves as a 'bank'. Mutuals need to consider how adopting a 'bank' name may impact on their current perception. For instance, branding the organisation as a 'bank' in the present trust landscape, may detract from the 'trusted' brand built from being a Mutual. This decision must be made by a Mutual after careful consideration.

Developing a customer-centric connected enterprise

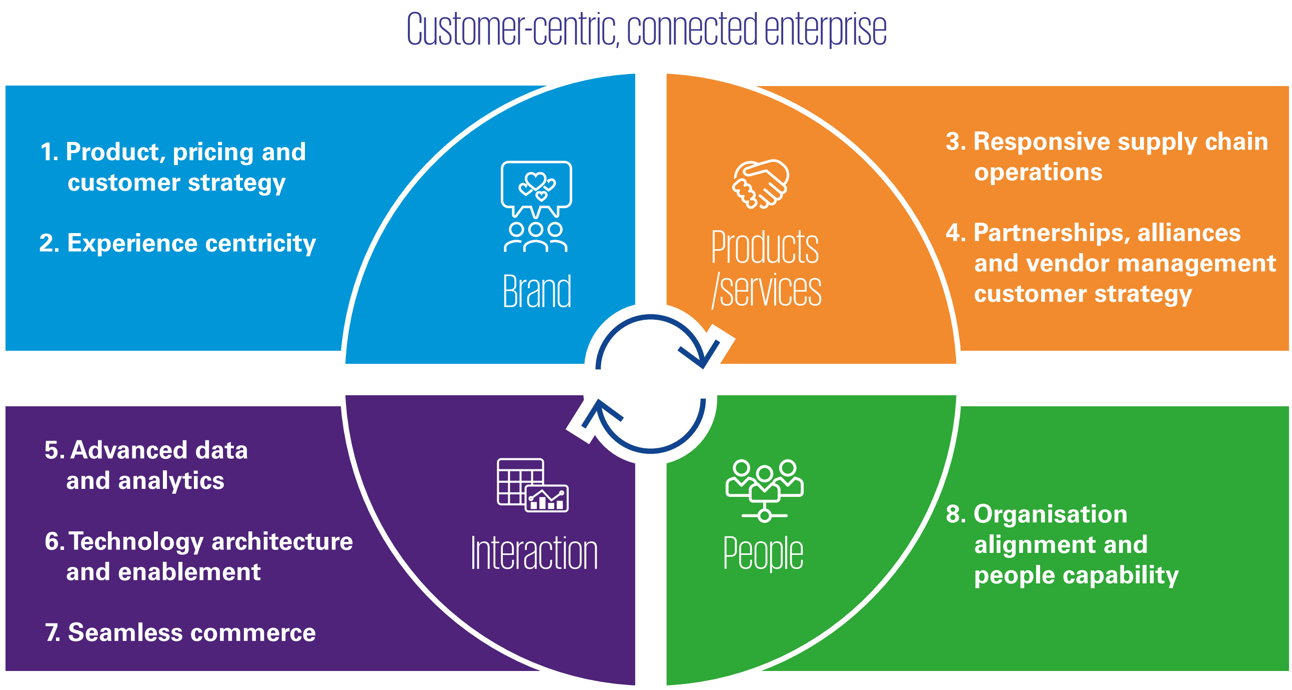
The target state for bank simplification is a 'connected enterprise', which is entirely organised around customer needs and is omni-channel, both with a digital focus. This bank is streamlined from front-to-back, with every process putting the customer at the core. It is not organised in product or channel silos, has no legacy restrictions, and is open to the outside world.

There are eight key connected enterprise capabilities that can help organisations understand customers' needs and values so as to consistently deliver the intended experience and customer promise. Hence, to achieve sustainable growth with customer demands evolving, it is vital to centre customer outcomes in every decision.

These eight capabilities align broadly to four categories: Brand, Product or Services, Interaction and People. These are illustrated on the next page.

Once a Mutual considers this connected enterprise model to brand and foster trust, a Mutual must consider how it can demonstrate this trust amidst customer needs for favourable products with favourable pricing. In essence, Mutuals must objectively build customer loyalty.

For further details about creating a customer-centric, connected enterprise please refer to the *Competing for Growth* publication. Also, for more advice to meet the needs of your current and future clients, or to facilitate transformational change experiences such as customer service performance, product and service development and marketing and brand management please reach out to the KPMG Customer, Brand and Marketing Advisory team.



Building customer loyalty

With technology making it easy for customers to walk away, and with challengers and start-ups hot on the heels, any bank that does not recognise loyalty will lose out.

Recognising customer loyalty appropriately is pertinent amid today's environment of customer dissatisfaction and digital disruption in the industry. The ACCC estimates that rates for existing mortgage customers are 32 bps higher than for new home loan customers. If Mutuals don't preference existing customers, they risk a significant loss in revenue as customers flee elsewhere.

Currently, Mutuals rely on their branding image to foster loyalty, i.e. aligning to their target customers' needs and to the broader community context. 63.8 percent of our survey participants believe community is a distinguishing factor.

But does this align to what customers are looking for?

A recent KPMG Acuity survey of over 500 Australian consumers about their attitudes towards their bank found evidence of the limited effectiveness of traditional loyalty programs, and the need for banks to find better ways to recognise loyalty as a priority.

Technology is allowing other ADIs to sign up customers, enquire and fulfil transaction accounts, deposits and loans, and offer competitive terms and pricing, all online. Currently, there are more than 20 companies that have applied for a banking licence, which will offer ease of transacting and new, attractive digital experiences. These start-ups will provide compelling customer experiences and lure customers away from Mutuals.

The good news is that Mutuals have the opportunity to take a new approach to recognising and rewarding the loyalty of existing customers through investing in their customer journey and making strategic partnership with service providers that can innovate the customer experience along the way.

Traditionally, Mutuals have remained simple and have not offered alternative unsecured products as a major component of their portfolio. They do not compete with the majors through providing increasingly attractive rewards and credit cards. Accordingly, Mutuals have the ability to invest in simple, appealing and relevant rewards for loyalty.

Is there any one best loyalty program? No. Successful loyalty programs require relevant, honest and believable engagement which is consistent across channels. This can take many forms, however the core attributes should include 'best offers' to existing customers; easy sign up and servicing; consistent experience across channels, and effortless complaint resolution.

Any bank, including Mutuals, that prioritise investment and transformation in a way which develops compelling customer loyalty will be well placed to turn around customer dissatisfaction, and avoid the significant reduction in returns that the new era of financial services beckon.

03 Emerging technologies

Nicholas Buchanan, Partner, Audit, Assurance and Risk Consulting

The emerging landscape for Mutuals is one of opportunities and threats. Wide ranging changes to the financial services industry are being felt with digital banks on restricted ADI licences entering the market, and a seemingly continuous line up of start-ups and Fintech players looking to make their mark. The outcomes from the Royal Commission are also already taking effect with a swift refocus to ensure that commercial outcomes are meeting the community's standard expectations. This revolution in financial services driven by Fintechs and changing regulations for data, privacy and trust, has meant technological change is moving at an unprecedented pace.

What is Future Tech bringing?

Technology such as Artificial Intelligence (AI), robotic automation, cognitive technology or the Internet Of Things (IoT) will shape the landscape for financial services. So what next? Distributed Ledger Technology (DLT) or Blockchain based encrypted databases, in particular have moved from idea to operational realities. The benefits from these types of systems being immutable, secure and efficient have the potential to unlock enormous benefits to a range of intermediaries.

What is the scale of investment – from Fintechs raising capital to banks investing directly?

The speed of future technology becoming available is not surprising, considering the amount of private investment over the last 5 years. KPMG's 2018 Fintech 100 report[3] outlines that - Aggregate capital raising has "rocketed over the past 12 months with the top four companies (in the selected 100) raising over US$1 billion in the last 12 months. The 'Top 50' have raised an aggregate A$38 billion over the past 12 months and A$70 billion over their lifetime while the next Emerging 50 have raised A$1.4 billion in the last year and just under A$3 billion since founding". These figures highlight the momentum of this sector.

KPMG's *The Pulse of Fintech H1 2018* report[4] notes the total global investment in Fintech companies for Q1-Q3 of the year has already a hit record of US$78 billion over 1500 deals. While the number of deal flows may be plateauing, the deal values are still significantly increasing. This indicates that the maturity of these deals and the technology underpinning them has moved from start-up stage to mature investments with long term real commercial applications.

According to *Forbes*, in 2017 the total value of equity backed investments in blockchain based companies in the US alone topped USD$4.5billion[5]. And depending on what stats you read this is much larger when you include raising capital through Initial Coin Offering (ICOs).

Blockchain based investment is still a drop in the ocean of total banking investment with overall global technology spend reported by the *Financial Times* to increase by 4.2 percent to over USD$261billion this year and JPM's investment an incredible US$11billion[6].

Despite significant global investment and large global bank budgets, the Australian investment appetite of the larger domestic banks still shows they want to be at the forefront of emerging technology. Each have a strategy in seeking to employ or invest in Blockchain or DLT, from forming global alliances with other banks such as in R3 (a distributed database company established in 2015 with over 200 firms in its consortium), or specific partner alliances with data science and tech firms to create their own bespoke working solutions.

These strategies come with significant budgets and commitments. It is a challenge for the mutual sector to determine what play to make and where to deploy resources.

How will Mutuals participate now and in the future?

KPMG's most recent global Fintech survey[7] suggests that there is no single best way to approach investment in Fintech, with financial institutions pursuing various avenues – from partnering and buying to sourcing and direct investment.

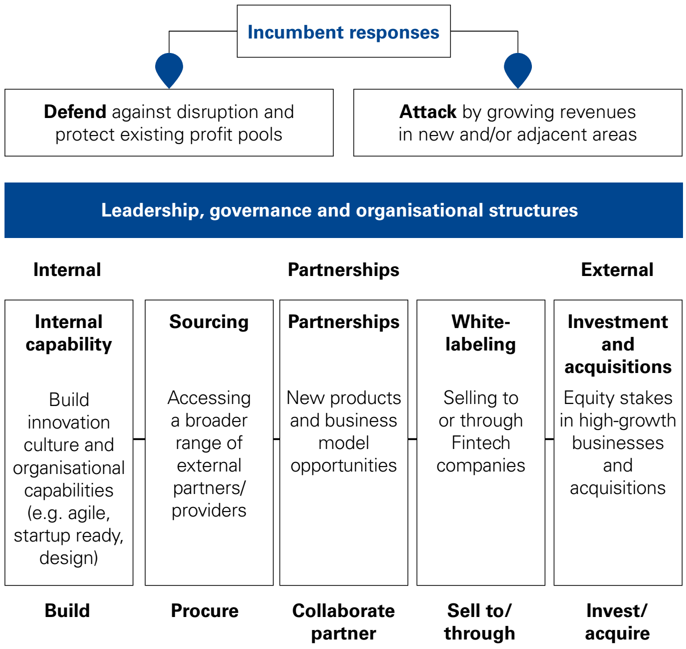
In the Mutual sector, 48.9 percent of respondents to our mutuals survey said they will invest in technology around Fintech in the upcoming year. Of this, half of respondents indicate this will be in payments and digital currencies or lending platforms.

In addition, 51.1 percent of *survey* respondents said that they aim to keep up with changes in their environment including regulation, Fintech, Open Banking and NPP.

The KPMG Global Fintech Survey in 2017 yielded similar results with the aim of technologies identified by Mutuals corresponding to the top three priorities across the banking sector.

Ranking of Fintech strategy objectives

Source: KPMG International Global Fintech Survey, 2017



The best practice underpinning any successful approach to Fintech however, is the definition of a focused strategy as outlined below.

This strategy should be no different whether there is a balance sheet of $10 million or $100 billion. But what might define the opportunities and threats is how strategy is executed as an incumbent in the mutual banking sector.

Mutuals will find the biggest challenges in areas of internal development and direct investment or acquisition, due to limited budgets and capital constraints.

Respondents to our survey mentioned Mutuals have spent less than $15 million on specific Fintech projects (other than NPP). Accordingly, a Mutual needs to consider collaboration. For example – participation in accelerators or incubators, investment via industry-based consortia either with new tech entrants or with the collective pressure on current industry platform providers. An example is SocietyOne, where 21 Mutuals have funded peer-to-peer lending initiatives.

Alliances are not always easy, either with each other or in attracting new market entrants for direct partnerships. It will therefore require sector wide acceptance of the need for an innovative culture, with mutual goals of investing for future member value.

No matter the strategy, a Mutual should utilise their competitive advantage over other incumbents (banks and non-ADIs) which stems from the origins of the sector itself – one that was founded on the premise of building commercial relationships for mutual benefit. As Mutuals are a traditional form of peer-to-peer lending, taking deposits from members and lending them to other members, they are not unlike some new Fintech entrants. The difference is in the deeper relationships that a Mutual has with its depositors and borrowers. These relationships should be nurtured and seen as a source of strength. We have seen in banking, and broadly in the financial services industry, just how quickly this relationship value can sour.

Mutuals will remain a genuine alternative to a big four and large regional bank, and whatever the strategy used to embrace future tech, Mutuals should take heed of the notions put forth by James P. Carse in *Finite and Infinite Games*, being that the goal should not be being number one within a finite game, it should be to stay in the game and play the infinite one.

04 New Payments Platform (NPP)

Kamal Kandasamy, Associate Director, Management Consulting

On 13 February 2018 the NPP was launched to the Australian market providing access to real time, data-rich payments and 24x7 availability.

The platform improves transaction flows and eases reliance on cash. Its capabilities include flexibility in nominating identifiers and removing limitations to BSB numbers and account numbers.

9 months after its launch the platform has the ability to reach the majority of Australians via more than 60 financial institutions, with banks also preparing their NPP offerings for institutional clients.

64% of survey respondents used NPP as a strategy to improve customer experience

42 of 48 survey participants are on the NPP

We have seen a large uptake of the NPP by Mutuals as they can leverage their smaller size and less complex operations to get it started. Customers of Mutuals, however, may find that they have to wait until all major players also fully migrated before they experience the benefits.

NPP service offerings from the banks have been limited to providing real time payments using online channels through the first overlay service called 'Osko'. The services represent the most basic functions of the platform. As the NPP ecosystem evolves it is envisioned to be a significant opportunity for banks and Mutuals to expand their product and service offerings.

Levelling the playing field

Today, the majority of payment transfers occur through the retail direct entry developed by the banking community decades ago. While technology has advanced, this process has hardly changed, meaning that banking customers have relied upon a payment service that was hosted within a single bank's closed ecosystem, providing little incentive to innovate, nor a level playing field.

The NPP opens up these closed ecosystems and provides equal access to modern payment services. Through the base infrastructure and future overlay services, the NPP will offer everyone the same ability to offer potential payment services. Overlay services offer a means for fintechs and other payment companies to develop complex payment services, and introduce innovative services.

The platform provides the opportunity for innovative banks to bring payment solutions to the broader industry by forming non-traditional partnership with Fintech and other providers of payment capability. Mutuals can collaborate with Fintechs and develop 'white label' products.

What Mutuals need to be aware of?

The NPP represents just one change that is disrupting the payment landscape with Open Banking, new legislation, and new technologies all changing the economics of banking and payments. All Mutuals should have a comprehensive payment strategy prepared to enable it to take full advantage of these trends as well as detailing how it plans to protect its existing revenue base.

As the NPP develops and banking customers demand access to the new products and services, Mutuals should ensure their core banking and payment systems remain up-to-date. They must push toward real-time processes in order to offer and process new overlay services, as well as possible future NPP functions. The ability to quickly adopt these payment services will enable Mutuals to remain competitive.

05 Open Banking

Ivan Vaptzarov, Manager, Management Consulting

Through the legislative push of the Consumer Data Right (CDR), the Australian government is empowering customers with the rights to own and direct the use of all data that organisations collect about them. The application of this legislation means customers will be able to authorise registered third party service providers access and use to their personalised data through a standardised Open Application Program Interface (Open API).

Open Banking, or CDR legislation in the banking sector, is intended to promote increased competition between banks by enabling smaller market players, such as Fintechs and challenger banks, to design and provide financial products and services leveraging on customer data traditionally held exclusively by banks. The open sharing of information is designed to promote greater transparency for customers and put the customer back in control of their data.

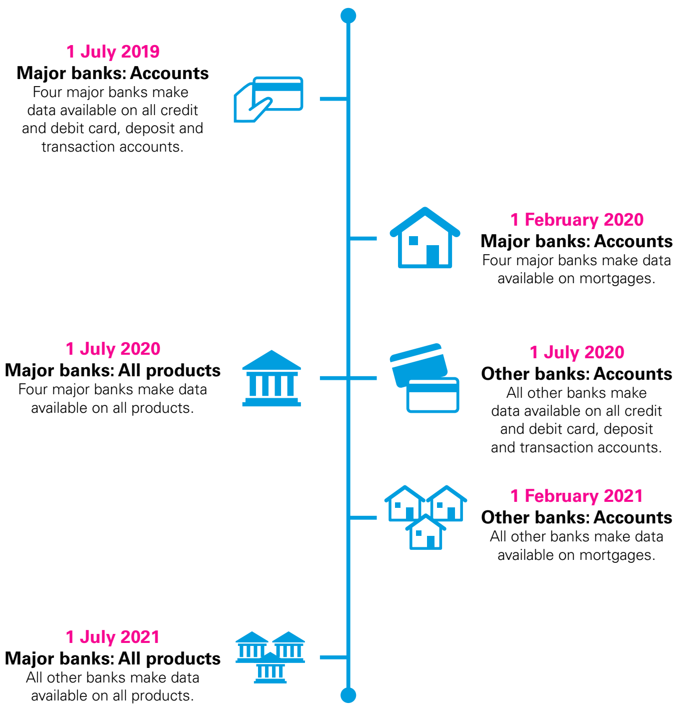
Open Banking in Australia

Open Banking will be the first application of the CDR regime in Australia. Through Open API access, financial institutions will be required to provide access to specific forms of customer banking data to an accredited third party given the appropriate customer authorisation.

The timeline of Open Banking is ambitious, with major banks required to be compliant by July 2019 and Mutuals by July 2020. The industry is currently in active consultation, utilising the open source platform GitHub, to reach consensus on industry standards.

There are a number of parties working on the implementation of Open Banking in Australia. APRA, RBA, ASIC and the ACCC share responsibility to support the reforms required to deliver Open Banking. ACCC is the lead regulator of the CDR and will develop the regulatory framework.

Open Banking Timeline



Source: https://www.kwm.com/en/au/knowledge/insights/open-banking-australia-consumer-data-right-energy-telco-20180510

What are the world-wide observations of Open Banking?

World-wide, Open Banking has observed contagion effects where learnings from one region have been leveraged to implement Open Banking in different regions. A summary has been illustrated on the following page:

Open Banking in practice – what are we seeing worldwide?

Europe

Two key pieces of legislation are being adopted across the European Union, which are key influences in spreading open banking legislation globally:

Payments Services Directive (PSD2) – banks required to provide read (view access) and write (payment initiation) access to third parties via APIs.

General Data Protection Regulation (GDPR) – sets out a number of universal data protection rights for European citizens.

UK

The UK government required its largest nine banks to meet the compliance requirements of PSD2 by 13 January 2018. All major banks have delivered on the minimum compliance objectives. However change is still in its early stages, with awareness and usage low but growing.

Compliance was the focus given the short timeline and the addition of the GDPR. Currently all nine major banks are implementing a version of Personal Financial Management (PFM) application.

Australia

Based on the legislation to date there is likely to be three types of data that banks are required to provide read-only access to:

Bank account data – customer's product information

Transaction data – granular information on a customer's transactions

Customer data – personally identifiable information such as the customer's (individual or business) name and address.

The initial concern for the major banks is compliance. Implementing tentative Open Banking standards by July 2019 while simultaneously dealing with the Royal Commission and the NPP will likely leave little room for innovation in the initial stage. This could result in Fintechs being the first to reach the market with new customer-focused propositions.

Unlike the EU's Payments Services Directive (PSD2), the launch of Open Banking in Australia will only include read-only access to customer data. For banks this means they will continue to be a central part of the customer's banking journey since banking aggregators will be limited in how they can enhance their existing service offering. This could change with write access (enabling third party payment initiation) highlighted as a possible addition to the standards in the future, where it would be possible for a non-bank third party (or an innovative bank) to become a customer's key banking contact.

Even read-only access could cause significant changes to the current competitive landscape as:

- Brokers and marketplaces will be able to collect product data and offer better deals for customers;
- PFM applications may identify where a consumer should store their deposits, how to minimise their interest repayments or structure their loans; and
- Banks will be able to use a competitor's banking data to validate loan applications or offer target marketing to win over customers.

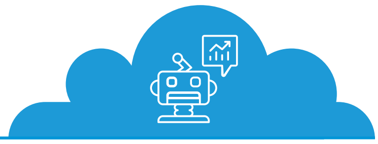
Banks need to consider not only how they can defend against innovative new solutions, but also how they can be the beneficiary of this evolving market. It is also important for banks to incorporate strategies for maintaining customer trust in light of the increased exchange of data.

What does this mean for Mutual banks?

For Mutuals, they will need to consider their strategic responses to Open Banking and decide when to participate. Some, hopefully many, will seize the opportunity to participate early and look to acquire new customers. This will undoubtedly require them all to work collaboratively with technology providers, as well as Fintech companies.

Mutuals must envision how to succeed in the Open Banking ecosystem. Technology capability uplifts will be unavoidable for Mutuals and in response, Mutuals can be proactive in seeking opportunities for collaboration. It is vital for the sector to ensure it can defend itself and retain its customers in an open data world.

06 Planning for the workforce of the future



Catia Davim, Partner, Management Consulting

Mutuals are experiencing unprecedented levels of change driven by technology, connectedness, globalisation, volatile economies, and shifting employee and consumer demand. The impact of these changes will be significant upon an organisation's operations and its workforce. Mutuals can either embrace the change or be changed by these external drivers. Developing people and sustainable operations strategies that address these changes is imperative.

Employment of the future will present a stark shift of an employee's skillset and job roles, than is present today. There is expected to be a significant impact on jobs, from significant job creation and job displacement, to heightened labour productivity and widening skill gaps. Developments in automation will see an increased requirement for 'soft' skills, including problem solving, critical thinking, communication and interpersonal skills, as well as some technical skills in science, maths, and advanced technology.

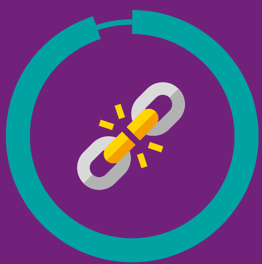
Mutuals will need to ensure that they are prepared for the workforce skills, occupations and ways of working needed for a sustainable future. The exploration of potential for, and application of, digital labour as well as ensuring that the relevant workforce capability exists is also critical while significant investments over the medium term are necessary to avoid the cost of obsolete workforces.

Transformations to operating models, the employment landscape and skills requirements will need attention in the realm of attracting, recruiting and retaining key talent.

Mutuals being smaller and agile should be able to implement new technologies quicker, albeit in the presence of cost and capital constraints.

Being community focused means Mutuals must effectively communicate that their future labour force does not necessarily mean reducing headcounts.

CEOs are embracing the digital agenda like never before



95% see technology disruption as an opportunity

71% are taking personal ownership for driving their organisation's transformation

Source: https://home.kpmg.com/content/dam/kpmg/xx/pdf/2018/06/frontiers-in-finance-issue-59.pdf

Lessons from first movers

Mutuals are also able to leverage from the experiences of first movers.

In 2017 KPMG ran a workshop for clients who were interested in governance of Intelligent Automation (IA). Attendees included global retailers, banks, insurance companies and aerospace manufacturers. The prominent lessons noted by these early movers were:

1 **Education is imperative:** It is important to up skill people involved in the IA program and retrain employees whose jobs are now automated. This will minimise automation anxiety.

2 **The right resource mix will help drive efforts forward:** There needs to be sufficient resources in place to support IA efforts including technical, functional, strategic and creative expertise.

3 **Start small:** Mutuals can begin with small, initial automation pilots to demonstrate quick wins to gain leadership support and for the workforce to build momentum.

4 **Require governance and coordination:** Financial Service organisations should focus on functional experimentation towards a more organised and managed approach.

5 **Get risk and Compliance functions involved early:** The right control mechanisms need to be in place to effectively manage bots. Risk and Compliance should be a key player to:

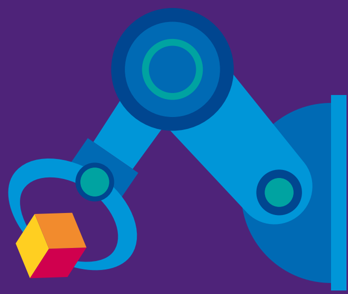
- provide the ethical compass to help the business guide automation decisions
- consider how core organisational values extend into technologies
- establish and track metrics that measure the residual effects of automation.

6 **Establish alignment between IT and the business:** Technology must be solving and driving the business's needs and growth. The IA journey must involve the entire organisation.

An engaged and proactive approach is key to implementing IA.

Next, Mutuals must also consider how this IA will evolve the way humans interact with the technology.

Many are still in the early days of their digital workforce journey.

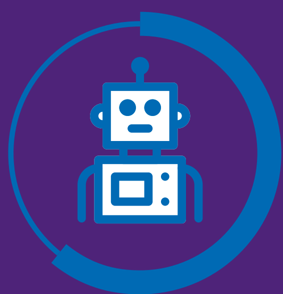


86% of respondents said they are either piloting or just starting to test out the value and benefits of AI and robotics.

Source: https://home.kpmg.com/content/dam/kpmg/xx/pdf/2018/06/frontiers-in-finance-issue-59.pdf

CEOs see new technology skills as critical to supporting the organisation's growth plans.

61% see AI and robotics as net job creators rather than job eliminators over the next 3 years.



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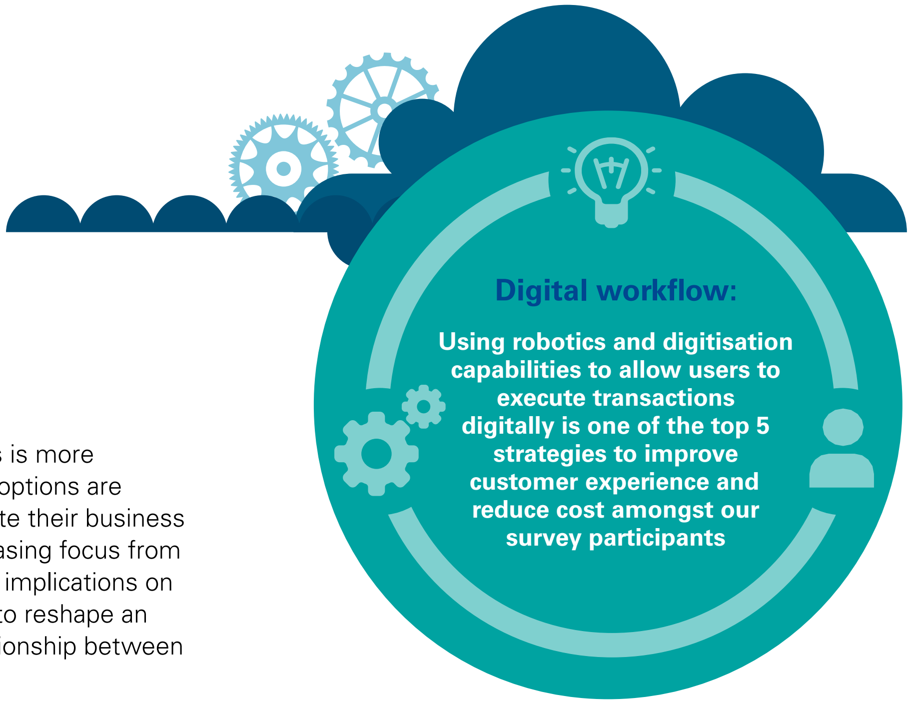

Intelligent interactions

The technology landscape for finance teams is more complex than ever. New and diverse digital options are being presented to organisations to automate their business processes and operations. There is an increasing focus from an organisation's perspective of RPA and its implications on the finance function. RPA is an opportunity to reshape an organisation and enhance the dynamic relationship between humans and technology.

The deployment of RPA is not only about software implementation, but also about an organisation's change management and identifying and keeping key stakeholders engaged.

Our survey showed that, 44.7 percent of respondents believe digital workflow and use of robotics are strategies to improve customer experiences and cost, and 61.7 percent intend to invest in robotics.

Applications for RPA within finance include:

- data entries, such as fill-in forms and posting transactions
- rule based tasks (follow 'if' decisions, making calculations)
- manage the approvals and checks
- extracting data and reformatting data into dashboards or reports
- loggin into system/applications, data import/extract between different systems or spreadsheets
- repetitive keyboard typing/mouse clicking
- opening emails and attachments, sending and archiving standardised emails and
- database creation/updates, merging data, copying and pasting data.

Robotics of the future will help reduce efforts further and move away from manual labour.

Success story

KPMG, in collaboration with Google, worked with a large retail bank in the US. This involved designing and implementing solutions to automatically categorise customer queries and match such queries with prepared and appropriate responses. This was implemented with a 97 percent success rate.

https://home.kpmg.com/us/en/home/insights/2018/05/kpmg-intelligent-interactions-google.html

Despite the positives of RPA, CFOs are still uncertain as to how RPA can benefit their finance teams. Mutuals are at the stage of deciding whether or not to adopt RPA in finance and began the RPA journey.

For more details on some of KPMG's client experience in RPA implementation, please refer to https://home.kpmg.com/au/en/home/insights/2018/10/robotic-automation-during-evolution-of-finance.html.

07 Royal Commission Interim Report

Astrid Raetze, Partner, Deals, Tax & Legal
Charlene Lee, Senior Manager, Deals Tax & Legal
Nicholas Alexander, Manager, Deals Tax & Legal

The Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry (Commission) released its Interim Report on 28 September 2018 (*Interim Report*). Interest has centred on the three areas of misconduct acknowledged by financial services entities, being:

a) **Fees for no service:** where licensees or advisers were charging fees to clients for financial advice that was not provided;

b) **Inappropriate advice:** financial advice that does not comply with the 'best interests' obligation, or that does not take proper account of a client's circumstances; and

c) **Improper conduct by advisers:** falsifying documents, misappropriating customer funds, and engaging in misleading and deceptive conduct in relation to clients.

In its *Interim Report,* the Commission identifies dishonesty and greed as the two main drivers behind the misconduct to date, declaring that the pursuit of short-term profit has been too often prioritised at the expense of basic standards of honesty.

The Commission sets out its initial observations and findings about the Australian banking and financial services sector under five broad categories, summarised in more detail here:

Consumer lending

1 **Intermediaries and confusion of roles:** The Commission examines the role of mortgage aggregators and mortgage brokers (along with other intermediaries) between lenders and borrowers. It concludes that, even if an intending borrower believes or expects an intermediary to be acting in their best interests, in most cases the intermediary owes no general duty to the borrower to seek out the best and most appropriate deal. Moreover, submissions indicate that, at least in the eyes of some lenders, the broker's task is to sell that lender's products.

2 **Communication with customers:** The Commission evaluates the conversations between financial services entities and their customers, observing that a 'conversation' with a customer is treated as an opportunity to sell, gather information about the customer, and too often involves the entity's representative telling the customer what they need.

3 **Responsible lending: The Commission observes that:**

a) lending was not treated as unsuitable if the customer was likely to default;

b) the banks make no inquiry about the customer's circumstances, requirements, or objectives (i.e. by relying on statistical benchmarks for expenditures to inform credit risk assessments); and

c) issues often classified as 'processing errors' by financial institutions amount to failures to deliver on the promised features of products sold.

Financial advice

This section contains some of the Commission's most consequential findings for the future:

1. **Conflicts of interest:** The Commission concludes that the conflict may be better seen as a conflict between the financial interests of the adviser or licencee, and the duty that each owes to the client. The Commission notes that the choice between interest and duty is too often resolved in favour of the adviser's self-interest.
2. **Conflicted remuneration, grandfathering and culture:** The Commission notes that, while the prohibitions on conflicted and other forms of banned remuneration may appear to be comprehensive, there are exceptions relating to general insurance, life risk insurance products, and basic banking products, along with provisions permitting grandfathered benefits. On this point, the Commission appears unequivocal in its acceptance of ASIC's position that "any exception to the ban on conflicted remuneration, by definition, has the ability to create misaligned incentives, which can lead to inappropriate advice". It also emphasises that, in an environment where the major banks have already begun to abolish grandfathered commissions, the onus is on the sector to demonstrate why the provisions should remain.
3. **Vertical integration:** In its commentary on the vertical integration of financial product manufacture with financial product sale and advice, the Commission observes that the internal efficiency of the 'one stop shop' does not necessarily produce efficiency in outcomes. It also acknowledges that, from the banks' perspective, vertical integration always promised the benefit of cross-selling financial products. This observation, coupled with the Commission's dismissal of past characterisations of what has occurred as a "few bad apples", indicates that the Commission may be contemplating a recommendation designed to address systemic issues associated with vertical integration. Mutuals are in a unique situation where vertical integration is not common – rather Mutuals focus on building strategic relationships with existing providers on innovative ways to expand customer experience and offerings.

Small and medium enterprises (SMEs)

1. **Multiple definitions of SMEs:** The Commission notes the wide range of statutory definitions of SMEs within the Australian regulatory landscape, and indicates that harmonisation of the existing definitions may both make the law easier to administer and understand, and reduce challenges in supervision and enforcement. This is being considered as part of the reforms planned with independent reviews done by Greg Hammond OAM last year. Feedback and further discussion with the industry has recently finished with Australian Treasury Department aiming to release results subsequent to compiling feedback.
2. **SME lending:** The Commission's commentary on SME lending brings into question the fact that the responsible lending provisions of the *National Consumer Credit Protection Act 2009 (Cth) (NCCP Act)* do not currently apply to lending for SME business purposes.
3. **Code of Banking Practice (Code):** The Commission observes that while the 2019 Code requires a bank to:
   a) consider the provision of a new loan or an increase in loan limit to exercise the care and skill of a diligent and prudent banker; and
   b) assess whether a small business customer can repay a loan based on their financial position and account conduct,

it does not resolve the bounds and content of these obligations.

4 Third party guarantors: In its discussion of voluntary guarantees, the Commission observes a disconnect between how the law, and lenders, treat third-party guarantors. This is instructive given the Commission's acknowledgement that most voluntary guarantors for SMEs are family members.

5 Dispute resolution: In assessing the outcomes of the Financial Ombudsman Service (FOS) and Australian Financial Complaints Authority (AFCA) proceedings, the Commission highlights that customers who were wholly or partly successful in their claims nonetheless failed to achieve what they believe to be a satisfactory outcome. The Commission questions whether AFCA should be empowered to award compensation for losses or harm caused.

Agricultural lending and remote communities:

The Commission draws attention to the following themes:

1 **Revaluation of securities:** There is a pattern whereby banks are revaluing land or other assets held as security, resulting in a decrease in the land-to-value ratio (LVR), which in turn is used as a non-monetary default allowing the bank to call up the loan.

2 **Difficulties obtaining access to services and support:** Farmers are having difficulty obtaining access to banking services and appropriate support for a number of reasons, including a failure by the banks to recognise ordinary seasonal variations in cash flow.

3 **Changes to lending conditions:** Submissions have indicated complaints about changes to lending conditions that are detrimental to the borrower, including increasing interest rates or altering the terms of overdrafts and other facilities.

4 **Enforcement by external administration:** In relation to the conduct of receivers or external administrators appointed by the banks, the Commission notes that a forced sale is rarely in the best interests of the customer, and that an appointment of an external administrator should be an option of last resort.

5 **Basic accounts, informal overdrafts and dishonour fees:** The Commission observes that:

a) lower cost 'basic accounts' are unnecessarily difficult to access in remote communities; and

b) informal overdraft arrangements and dishonour fees are not suitable in certain circumstances.

6 **Identification issues:** Aboriginal and Torres Strait Islander people may not always be able to readily assemble the documentary proof of identity that is required to comply with their *Anti-Money Laundering and Counter-Terrorism Financing Act (AML/CTF)* obligations, and bank employees should be trained to apply the Australian Transaction Reports and Analysis Centre (AUSTRAC) guidelines and assist such customers.

7 **Funeral insurance:** The Commission calls attention to ASIC's identification of inappropriate sales practices regarding the sale of funeral insurance products to Aboriginal and Torres Strait Islander people, and questions whether funeral life and funeral expense insurance policies might be better classified as financial products under Chapter 7 of the *Corporations Act 2001 (Cth).*

Regulation and the regulators

The Commission also evaluates the performance of ASIC and APRA:

ASIC: The Commission highlights ASIC's expressed preference for negotiated outcomes over civil proceedings, observing that ASIC's enforcement approach to date has not had the desired deterrent effect. The *Interim Report* questions whether ASIC's remit should be reduced or detached.

APRA & BEAR: The Commission notes that APRA's chief focus is governance and risk culture, and considers the impact of its report on governance, culture and accountability within the CBA group. The Interim Report also questions whether BEAR should be extended.

Next Steps

There will be a further round of public hearings to consider the matters raised and other questions that must be dealt with in the Commission's Final Report. The Commission's Final Report is due to be submitted to the Governor-General by 1 February 2019.

What did the Mutuals survey participants say about the Royal Commission?

Increased burden
"Mutuals will have to deal with more costs due to any regulatory changes implemented, and stringent oversight."

Opportunity for mutuals
"An increase in market share for mutuals is a possibility, by differentiating from the majors, and placing emphasis on members."

No proportionality
"Any changes in regulation will most likely be applied to all ADIs on an equal basis, which means larger ADIs have stronger resourcing to be able to tackle these effects."

Reduced differentiation in products
"Practices are most likely going to be restricted due to any increased regulation, creating homogenous products throughout the industry."

Increased trust
"Public trust will be restored in the sector as a whole if Mutuals can continue to demonstrate focus on the customer."

08 BEAR - the challenges and potential

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Banks including Mutuals have more work to do under the Banking Executive Accountability Regime, but it's also an opportunity to build a stronger culture of transparency.

The Royal Commission into Financial Services and APRA's Prudential Inquiry into CBA has highlighted the increasing focus on accountability in Australia, and follows the significant changes which have already occurred in the United Kingdom and Hong Kong.

the implementation of BEAR in July 2018 for large ADIs requires ADIs to consider who they identify as Accountable Persons (APs), and to analyse their roles and allocated responsibilities.

As a result, BEAR is changing how ADIs organise themselves and operate, given the specific focus on individual accountability.

What has changed?

This increasing focus on individual accountability has been driven by two main factors:

1. Following the global financial crisis, a drive to ensure that an ADI is managed prudently.
2. To hold individuals to account, either through the lever of remuneration and/or disciplinary action, when regulatory breaches and other failures do occur.

BEAR is explicitly focused on prudential matters. However, the level of attention on conduct in the current environment, along with the potential impact of conduct issues on financial institutions' financial standing, calls into question the boundary between conduct and prudential management.

What is the challenge?

Whilst individual accountability is a relatively easy concept to understand, in practice pinpointing the accountable owner in any situation is becoming increasingly difficult. Organisations are growing in size, becoming more siloed due to a need for specialisation, increasing their geographical distribution, offshoring parts of their processes, and using more third-party providers. Layering in the increased expectations of Board oversight, a strong regulatory requirement to have three lines of defence, and the expanding use of technology such as AI – it may seem like an impossible task. Or is it?

BEAR lessons to date

ADIs have had to ask themselves, 'What do we do and what risks are we facing?' They have then assessed 'how' they do what they do, and 'who' is doing what. This involves a significant amount of time by very senior people discussing, debating and ultimately agreeing who does what.

The exercise isn't sufficient to just 'tick the boxes' by identifying a list of APs, producing a set of individual responsibilities, and an overall mapping of governance arrangements. The large ADIs have made significant investment in getting it right, and engaged with the spirit of the regime. This isn't a one off compliance exercise, as the ADI has the ongoing challenge of notifying APRA when there are any changes to their APs and what they are doing. APs are also obliged to exercise reasonable steps in the execution of their responsibilities (and to be able to demonstrate this in relation to matters that may have taken place in the past). This requires a significant amount of internal control and awareness of their obligations. Through the recent hearings at the Royal Commission, it is clear that this is easier said than done – particularly giving notification to regulators in a timely manner.

The large ADIs have taken different approaches to implement BEAR, but the challenges they have faced are similar, namely:

- addressing current organisational structures and identifying accountabilities within a 'matrix management' structure
- variability in current operational processes across the ADI
- interpretation of reasonable steps.

BEAR is limited at this stage to the most senior management in the ADI. One of the key challenges for ADIs is how they leverage their accountability principles and cascade this throughout the organisation to ensure there is a consistent understanding of roles and responsibilities which can support effective and agile decision making.

So, where are the Mutuals now?

The BEAR timeline is tight and it will be a significantly onerous task for Mutuals due to time, cost and resource pressures. However, Mutuals have the advantage over larger ADIs of an additional 12 months for compliance, which they are currently utilising to implement BEAR. The implementation date for Mutuals (including other small/ medium ADIs) is set at July 2019.

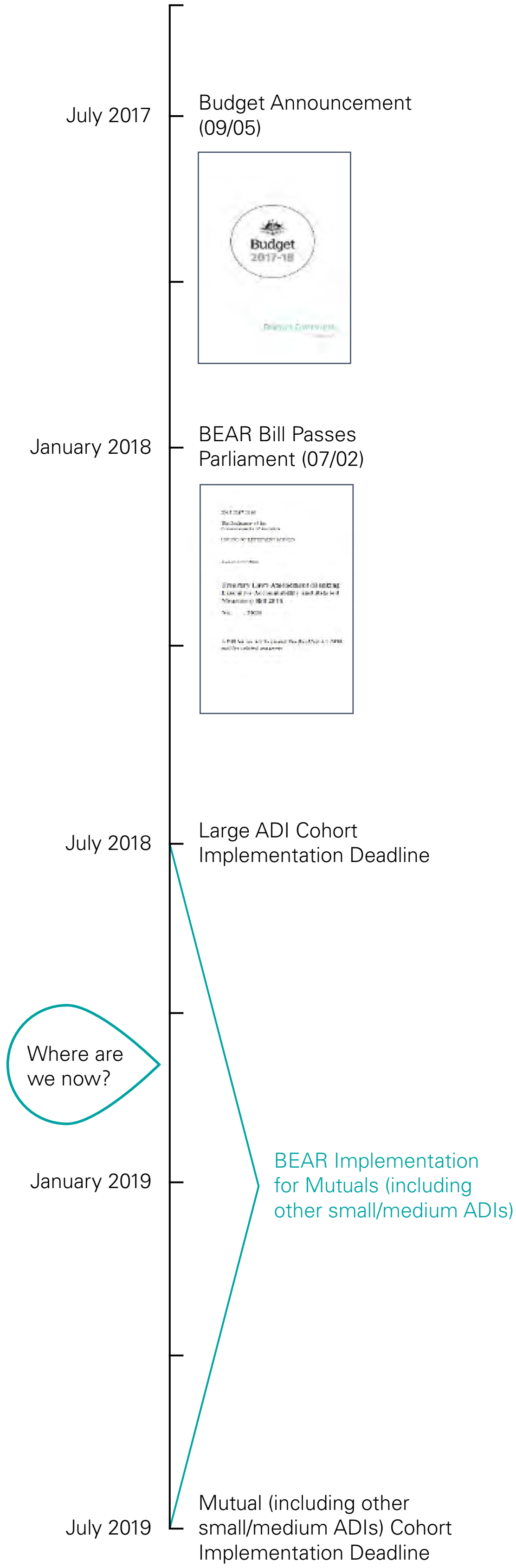
November 2018 update:
APRA has issued a letter in November 2018, requesting a draft of accountable persons, accountability statements and an accountability map by 21 January 2019. A brief summary of the timeline of adoption is as seen on the right.

Building a better culture

The introduction of BEAR has put significant pressure on ADIs. In the absence of prescriptive guidelines, Mutuals have also had to take their own view on how an AP can demonstrate that reasonable steps have been implemented. Where this isn't consistent issues tend to emerge.

The implementation of BEAR is only the start. The bigger challenge for organisations is how to maintain the focus on accountability and build a strong accountability culture. In considering this challenge, Mutuals should give consideration to how they articulate reasonable steps and guide AP record keeping.

Success for a Mutual would include: implementing these requirements quickly and efficiently; leveraging from learnings of the majors; and ensuring adequate monitoring measures. The broader challenge for mutuals remains consistent with other ADIs, i.e. how to maintain focus on accountability and build a strong accountability culture.



Did you know...?

Our survey highlighted that 89.4 percent of the Mutuals have assessed the requirements of BEAR.

09 Regulatory changes

The capital journey

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The Government's next steps on the capital journey ahead

Ever since the Senate Economics References Committee made four 'capital raising' recommendations to facilitate the ease for Mutuals to raise capital, there have been significant contributions from the Federal Government. The next step is to hopefully ensure that Parliament passes the Treasury Laws Amendment (Mutual entities) Bill 2018 to amend the Corporations Act to define the 'Mutual' as an entity and ensure that Mutuals can raise capital without triggering a demutualisation provision.

APRA's next steps on the capital journey ahead

By 1 January 2020, APRA is aiming that the major banks will raise their capital adequacy by 150bps compared to Mutuals raising 50bps. Finally, by 1 January 2021, APRA is aiming to provide revised prudential standards which includes placing a risk weighted asset floor for major banks. Both steps taken from APRA will help Mutuals compete against the major banks.

POTENTIAL

Amendment to the Corporations Act

JANUARY 2021

Release of final Prudential Standards to incorporate "floor on risk weighted assets" for major banks.

JANUARY 2020

Release of final Prudential Standards to incorporate – "Revised APRA Prudential Standards on 'Unquestionably Strong Standards'".

TODAY

OCTOBER 2018

All capital raising Senate recommendations, on advice on Greg Hammond were approved by the Australian Government.

MAY 2018

APRA agrees on the overall floor on risk weighted assets and would commence from 1 January 2021.

FEBRUARY 2018

APRA consultations open for an overall floor on risk weighted assets for Advanced ADI's.

NOVEMBER 2017

All capital raising Senate recommendations, on advice on Greg Hammond were approved by the Australian Government.

NOVEMBER 2017

APRA issued a revised APS 111 Capital Adequacy standard where Mutuals can raise CET1 capital instrument.

JULY 2017

Consultation for Mutuals to raise CET1 capital instruments – APRA Discussion Paper Released.

APRA information paper released, focusing on strengthening banking system resilience & establishing unquestionably strong capital ratios.

MARCH 2017

Treasurer announced Mr. Greg Hammond (OAM) to review recommendations.

MARCH 2016

Senate Committee Report announced 17 recommendations, of which 4 recommendations were to facilitate the ability for Mutuals to raise capital.

MARCH 2015

Senate Committee Report Senate Committee asked to review and report on the Mutuals industry.

Economic and Financial Statistics

Corporate trust not only means developing trust with customers, but also building trust by working with government stakeholders. This can be achieved by being more transparent and accurate in providing high quality insightful data to the APRA which can be used to enhance macro-economic analysis and enable better policy decision making. APRA has issued the final Economic and Financial Statistics (EFS) data definitions and reporting standards to build corporate trust through transparency and accuracy of data collection. The EFS data collection replaces the 'domestic books' data collection in three phases with the first phase commencing for the period ending 31 March 2019.

Building trust through transparency

New and more granular data is required to complete the new and revised ADI reporting forms (ARF). Mutuals will mainly be impacted by disclosing more details on lending to first home buyers, by purpose type, and significant changes regarding interest rate disclosures, profits and fees. A more granular and detailed data submissions such as investments and debt securities submitted by Mutuals would serve to increase the level of transparency in the industry and build trust with government agencies.

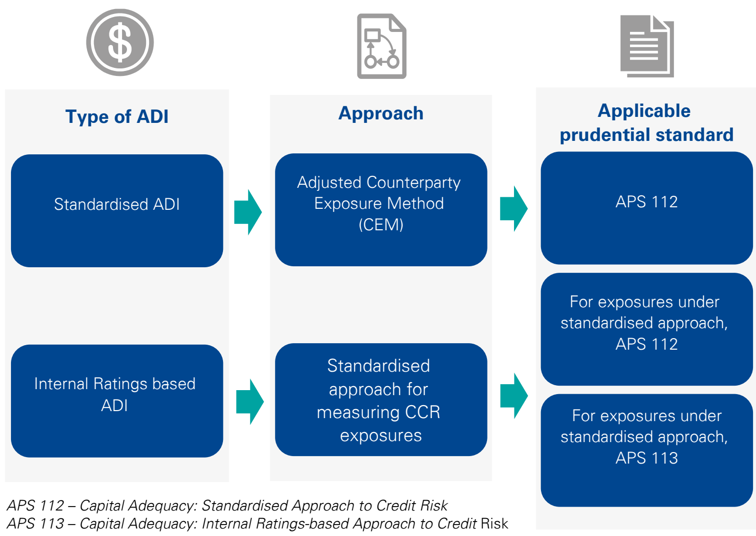
Building trust through accuracy

Over recent years, relatively high rates of resubmission for some forms in the EFS collection have led to concerns about the quality of data provided. In response, APRA has released new ARFs to improve the grouping of related concepts and revised the ADI reporting standards (ARS) to provide better guidance on data quality. APRA has released ARS 701.0 ABS/RBA Definition for the EFS Collection which provides a centralised glossary on all ARF reporting line items and ARS 702.0 ABS/RBA Data Quality for the EFS Collection which sets out the required level of accuracy and the relative priority attached to accuracy for different series.

APS 180 Capital Adequacy: Counterparty Credit Risk (CCR)

The revised prudential standard APS 180 Capital Adequacy: Counterparty Credit Risk will become effective after 1 January 2019. The revised prudential standard requires ADIs to hold capital for exposures to central counter parties (CCPs) in a manner consistent with the Basel Committee's Capital requirements for bank exposure to central counterparties – final standard. The primary objectives underlying the strengthening of the standard are **financial safety** and **financial system stability**.

The intention of the regulator is to find an appropriate balance between the objectives of financial safety and efficiency, competition, contestability and competitive neutrality, whilst promoting financial safety. It is the view of APRA that the revisions to the prudential standard will improve prudential safety outcomes.



APS 112 – Capital Adequacy: Standardised Approach to Credit Risk
APS 113 – Capital Adequacy: Internal Ratings-based Approach to Credit Risk

10 Tax developments

Natalie Raju, Partner, Deals Tax & Legal
Philip Beswick, Director, Deals Tax & Legal
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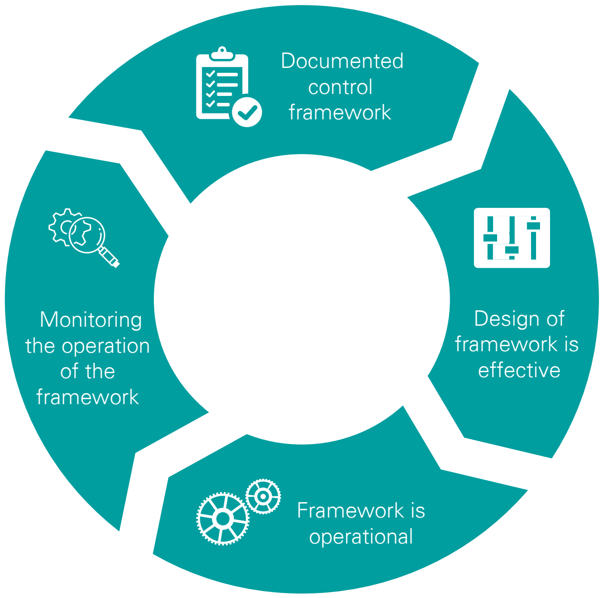
Tax governance and tax transparency measures

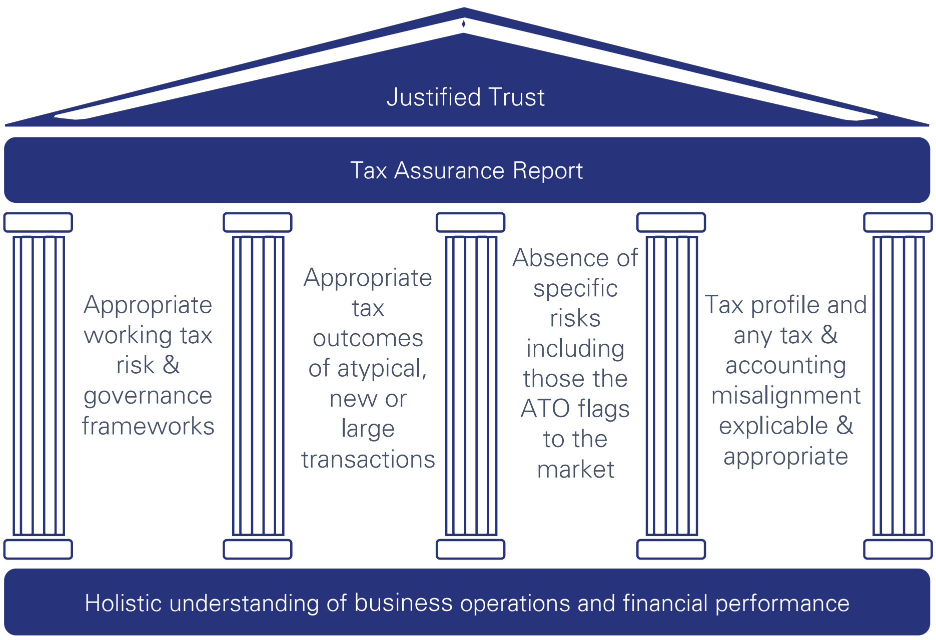
Mutuals have traditionally been viewed as 'low risk' entities in the eyes of the ATO. However, there is an increasing expectation from stakeholders for organisations to demonstrate that their tax policies and conduct align with the law, and meet public expectations. The ATO's Tax risk management and governance review guide assists taxpayers to understand what they believe better tax corporate governance looks like.

Generally, when demonstrating good corporate tax governance, a taxpayer should be able to provide a Tax Control Framework that effectively identifies and manages risk, and can provide evidence of its effectiveness and operation.



ATO's 'Justified Trust' model

The ATO's compliance program has also evolved with a renewed focus on tax governance, including the roll out of a number of initiatives to ensure that Australia's tax landscape is fair and equal. The Justified Trust initiative aims to improve transparency and governance, whilst building community confidence in the corporate tax arena. This initiative is based on the pillars to the right.



ATO's 'Justified Trust' model to tax governance

Streamlined Assurance Review

The ATO is currently targeting large companies with turnovers greater than $250 million to obtain assurance or identify areas of tax risk through a 4 month streamlined Assurance Review (SAR).

Taxpayers will have 28 days to respond to the ATO's initial request for information, which seeks to obtain assurance on the following:

- that appropriate tax risk and governance frameworks exist and are applied in practice
- that none of the specific tax risks the ATO have flagged in the market are present
- the tax outcomes of new or large transactions are appropriate
- any misalignment between tax and accounting results is explainable.

So how can you prepare for the ATO's SAR?

A good starting point is to undertake a gap analysis between your tax risk governance framework and the ATO's Guide.

Tax Transparency Code

Further in the spirit of good tax governance, the Board of Taxation has developed the Tax Transparency Code (TTC) which was endorsed by the Government in the Federal Budget 2016 -17. The TTC is a set of principles and minimum standards to guide medium and large businesses on public disclosure of tax information. Adoption of the TTC is voluntary, but companies that are medium (turnover between $100-500 million) to large ($500 million and over) businesses are strongly encouraged to adopt the TTC. Many Mutuals would fall within the 'medium' size requirement.

Businesses may elect to satisfy the minimum standard of the TTC by either publishing improved disclosures of tax information in their general purpose financial statements, or by publishing a separate TTC report. This includes disclosing information on effective tax rates and tax balances.

Although not mandatory, the ATO considers signing up for the TTC as a key component in its Justified Trust review.

Mutuals can use this as an opportunity to communicate to key stakeholders and the broader community their lower tax risk profile.

KPMG has developed Tax Control Room (TCR) digital technology to help clients undertake this assessment in the most efficient way. With the input of your tax/finance team and any nominated stakeholders, our TCR tool generates a tax maturity assessment of your organisation against KPMG's view of leading practice, and benchmarks it against peers and stakeholder perceptions'. The output also includes a 'gap analysis' against the 13 Board and Management Controls of the ATO's Guide. The reporting output from this technology has received positive feedback from the ATO and can be shared with the ATO under the SAR.

Tax transformation and outsourcing

As the business models across the Mutuals sector become more digitally enabled, there is a compelling case for the tax function to keep pace. Adding to this, the increased pressure from the ATO for improved governance and data integrity under the Justified Trust program, are driving a movement towards the transformation of the tax function.

Indeed, there is a compelling need to not only embrace new tax technology that is fit for purpose, but also implement better processes.

Mutuals are increasingly looking to engage with existing tax software providers to improve data integrity in their tax function, or alternatively considering the merits of a full outsource of key tax functions. This would enable Mutuals to focus on activities that add value to members.

The benefits of outsourcing include:

- access to a dedicated delivery team with specialists across each of the relevant taxes
- reduction in cost pressures
- access to market leading tax technology to enable greater efficiency and accuracy
- improved controls through automated extraction of data from core systems
- greater transparency and deeper insights through deployment of analytics that enable data-driven decision-making.

A well-executed transformation can help Mutuals improve tax governance through data integrity and transparency and also provide efficiency gains as they look to streamline and digitise their business models.

GST update

The Practical Compliance Guideline 2017/15 (PCG) issued in September 2017 continues to be the ATO's main strategy for practically administering the risk of incorrect reporting in the Mutual sector. Under the PCG, Mutuals are permitted to prospectively use a 'safe harbor' rate of 18 percent to recover Goods and Services Tax (GST) on certain costs. Where Mutuals have evaluated that their particular circumstances warrant the application of a rate higher than 18 percent, they are advised to take into account the ATO's draft GST governance and record keeping for financial suppliers (web guidance). The web guidance sets out the ATO's expectations for governance and record keeping and is part of the ATO's Financial Services and Insurance (FSI) strategy for GST.

Community highlights

Supporting a community from the roots up

11
Mutuals operate their own charities or foundations

$17.7m
In donations and fundraising raised for 2018

63.8%
of Mutuals believe community involvement is a key differentiator to their business

475
Community events were supported

888
Community organisations were supported

$ Financial literacy

Teachers Mutual Bank committed to a 3-year $177,000 investment, in collaboration with CUFA Education and Literacy programs, in Children Financial Literacy providing children living in poverty in Cambodia the opportunity to create brighter futures.

IMB launched a 'Financial Abuse Program' designed to increase awareness and understanding of financial abuse, particularly for older people in our communities who are particularly vulnerable.

Bank First launched 'Home First', a comprehensive home loan advisory platform to provide free information and advice for first home owners by harnessing the search power of Google, Domain and Yelp!.

Disability/disadvantage

Summerland is the first Far North Coast mutual to introduce a wearable payment device at no cost to customers. Summerland now also offers payWave terminals as part of The Salvos annual Red Door Knock Appeal, for ease of payment for community members.

P&N Bank's foundation Helping Hands have supported disabled or disadvantaged such as fixing the floor in the home of a wheelchair-bound individual and providing financial support to a family whose parents could not work and were supporting a newly paralysed son.

Bank Australia was the 1st bank to lend to customers who require specialist disability accommodation (SDA).

To date, Bank Australia has loaned $12.5 million for 43 homes across VIC, NSW, NT and QLD.

Beyond Bank supported initiatives such as 'Ride for Disability' for Raymond Terrace and Lower Hunter communities by funding specialist riding equipment and coordinating volunteering opportunities.

Health and wellbeing

People's Choice fund coordinates the annual People's Choice Undies Run and has raised more than $880,000 since inception. This has raised awareness of Australia's second largest cancer killer, bowel cancer.

Endeavour Mutual Bank donated $210,000 to its own foundation, the Australian Mutuals Foundation. A major recipient of the donations is Barnados Australia, which helps children and families suffering from disadvantage by creating safe and nurturing homes.

Defence Bank Foundation raised funds for the Defence Community Dogs program, which provides highly trained service dogs to serving and ex-serving ADF members to help deal with injuries and illnesses, including post traumatic stress disorder.

Rural support

Greater Bank donated $100,000 to Drought Angels, to support families, farmers and communities across NSW and South East QLD during a time of unprecedented stress and turmoil.

Newcastle Permanent's salary deduction scheme 'Community Assist', employees contributed $16,000 to the Thirsty Cow charity, which provides relief to farmers, graziers and their families, suffering from the effects of natural disasters such as severe drought, flood and bushfire.

Queensland Country Credit Union's Buy a Bale fundraiser has raised a total of $50,000 from staff and members donations to aid Farmers across Queensland.

Other community initiatives

Credit Union Australia continued its support of women gaining control of their finances through the CUAngles silent membership in collaboration with Micah Projects in Brisbane and are actively exploring affordable housing programs.

BankVic sponsored the 'Kids Day Out' as part of the Good Friday Appeal. Staff united and got behind the charity to raise $16,000 for the Royal Children's Hospital by creating the BankVic Ice Skating Wonderland.

Australian Military Bank continues to support Defence charities such as RSL DefenceCare, Legacy and Mates4Mates through its Military Rewards account.

Appendix

Financial results: 2018 survey participants

The following table details key financial data[8] of the Mutuals included in our report.

Mutual	Period[9,10]	Net Assets[11] $'000	Total Assets $'000	Total Deposits $'000	Operating Profit Before Tax[12] $'000	Capital Adequacy Ratio[13] %	Return on Equity[14] %	Cost to Income Ratio[15] %
Australian Military Bank Limited	**30-Jun-18**	**93,443**	**1,346,248**	**1,233,865**	**7,473**	**15.1%**	**5.7%**	**73.8%**
	30-Jun-17	88,076	1,253,724	1,109,037	7,598	14.9%	5.9%	76.2%
B&E Ltd[16]	**30-Jun-18**	**69,810**	**840,784**	**645,816**	**2,326**	**17.5%**	**2.3%**	**88.2%**
	30-Jun-17	68,223	763,603	615,299	4,856	19.1%	5.2%	75.4%
Bank Australia	**30-Jun-18**	**510,174**	**5,652,030**	**4,640,757**	**36,262**	**16.6%**	**5.2%**	**69.2%**
	30-Jun-17	484,894	5,157,005	4,169,704	32,306	17.0%	5.1%	69.4%
Bank First[17]	**30-Jun-18**	**205,689**	**2,509,173**	**2,281,609**	**17,014**	**15.6%**	**6.0%**	**72.6%**
	30-Jun-17	193,511	2,320,374	2,104,696	17,262	15.7%	6.4%	75.1%
BankVic	**30-Jun-18**	**177,632**	**1,830,317**	**1,595,735**	**17,909**	**19.7%**	**7.4%**	**65.3%**
	30-Jun-17	164,995	1,632,873	1,415,085	15,898	20.1%	6.9%	66.5%
Beyond Bank Australia[18]	**30-Jun-18**	**486,908**	**5,823,060**	**4,360,412**	**34,801**	**17.3%**	**5.5%**	**73.9%**
	30-Jun-17	431,184	5,415,141	4,268,837	33,977	15.1%	5.9%	74.3%
Big Sky Building Society Ltd	**30-Jun-18**	**62,603**	**777,441**	**708,593**	**3,932**	**17.6%**	**4.5%**	**67.5%**
	30-Jun-17	59,779	827,351	761,476	2,380	16.4%	2.8%	82.6%
Coastline Credit Union Ltd	**30-Jun-18**	**38,164**	**503,080**	**458,517**	**4,243**	**14.2%**	**8.5%**	**69.7%**
	30-Jun-17	35,061	461,319	420,980	3,407	13.7%	7.1%	72.0%
Community Alliance Credit Union Limited	**30-Jun-18**	**44,193**	**619,716**	**570,166**	**2,090**	**15.3%**	**3.3%**	**86.7%**
	30-Jun-17	42,738	664,178	615,574	788	14.2%	1.2%	94.1%
Community First Credit Union[19]	**30-Jun-18**	**88,843**	**1,066,278**	**966,072**	**2,932**	**15.4%**	**2.6%**	**88.4%**
	30-Jun-17	81,169	950,435	859,091	3,252	15.3%	3.1%	87.1%
Credit Union Australia Limited	**30-Jun-18**	**961,407**	**15,617,933**	**9,231,009**	**69,469**	**14.3%**	**5.6%**	**71.2%**
	30-Jun-17	907,257	14,323,091	8,760,229	67,871	14.3%	5.7%	71.6%
Credit Union SA Ltd	**30-Jun-18**	**100,583**	**1,160,080**	**945,510**	**5,676**	**18.8%**	**4.3%**	**81.4%**
	30-Jun-17	96,224	1,009,480	899,025	5,628	19.8%	4.5%	80.7%
Defence Bank Limited	**30-Jun-18**	**169,418**	**2,277,826**	**1,953,896**	**13,961**	**14.8%**	**6.0%**	**72.9%**
	30-Jun-17	159,624	2,031,528	1,741,142	13,176	15.4%	6.1%	73.0%
Endeavour Mutual Bank Ltd[20]	**30-Jun-18**	**82,724**	**639,250**	**545,366**	**3,061**	**25.8%**	**2.7%**	**83.0%**
	30-Jun-17	80,518	627,480	533,167	1,902	25.1%	2.4%	89.8%
Family First Credit Union Limited	**30-Jun-18**	**11,377**	**134,209**	**119,683**	**848**	**16.8%**	**5.6%**	**81.6%**
	30-Jun-17	10,759	126,287	112,834	605	16.2%	4.2%	85.1%
Ford Co-operative Credit Society Limited	**30-Jun-18**	**9,870**	**135,300**	**124,066**	**690**	**15.3%**	**4.1%**	**87.1%**
	30-Jun-17	9,469	133,232	120,867	690	15.3%	4.9%	80.4%

Mutual	Period[9,10]	Net Assets[11] $'000	Total Assets $'000	Total Deposits $'000	Operating Profit Before Tax[12] $'000	Capital Adequacy Ratio[13] %	Return on Equity[14] %	Cost to Income Ratio[15] %
G&C Mutual Bank	**30-Jun-18**	**104,760**	**1,120,680**	**957,737**	**6,804**	**18.2%**	**4.7%**	**69.4%**
	30-Jun-17	99,974	1,088,114	959,864	5,117	18.1%	4.0%	79.1%
Gateway Bank Ltd[21]	**30-Jun-18**	**103,544**	**1,064,121**	**746,395**	**3,692**	**20.4%**	**2.4%**	**78.5%**
	30-Jun-17	101,004	1,038,874	704,893	3,224	19.8%	2.3%	81.5%
Greater Bank Limited	**30-Jun-18**	**515,124**	**6,711,157**	**5,757,508**	**48,925**	**17.4%**	**6.9%**	**71.2%**
	30-Jun-17	481,233	6,286,212	5,375,917	40,845	17.2%	6.1%	74.0%
Heritage Bank Ltd	**30-Jun-18**	**533,399**	**9,524,363**	**7,149,791**	**64,213**	**14.1%**	**8.8%**	**70.6%**
	30-Jun-17	487,461	9,378,703	7,124,224	56,310	13.4%	8.5%	71.3%
Holiday Coast Credit Union Ltd	**30-Jun-18**	**44,145**	**607,657**	**556,556**	**3,196**	**14.5%**	**5.2%**	**81.9%**
	30-Jun-17	41,948	589,083	539,854	2,206	14.1%	3.8%	87.0%
Horizon Credit Union Ltd	**30-Jun-18**	**24,427**	**345,005**	**313,955**	**1,729**	**15.0%**	**5.8%**	**85.1%**
	30-Jun-17	22,415	337,427	312,161	1,648	14.6%	5.4%	85.1%
Hume Bank Limited	**30-Jun-18**	**75,776**	**1,104,110**	**1,016,352**	**6,013**	**14.5%**	**5.7%**	**79.9%**
	30-Jun-17	71,741	1,051,850	966,078	5,729	14.6%	5.7%	79.9%
Hunter United Employees' Credit Union Limited	**30-Jun-18**	**24,451**	**329,756**	**303,082**	**534**	**16.4%**	**1.6%**	**93.0%**
	30-Jun-17	24,071	302,950	276,995	422	16.9%	1.2%	94.7%
IMB Limited	**30-Jun-18**	**343,687**	**5,912,182**	**4,993,265**	**45,184**	**16.1%**	**9.4%**	**65.7%**
	30-Jun-17	330,248	5,713,681	4,795,283	39,252	16.6%	8.6%	67.9%
Macarthur Credit Union Ltd	**30-Jun-18**	**24,744**	**253,733**	**227,111**	**433**	**19.6%**	**1.2%**	**94.4%**
	30-Jun-17	24,449	249,279	233,033	723	19.3%	2.3%	91.7%
MOVE Bank[22]	**30-Jun-18**	**63,264**	**614,446**	**549,283**	**1,305**	**21.5%**	**1.5%**	**85.1%**
	30-Jun-17	62,331	616,223	552,070	1,721	20.8%	1.9%	85.5%
Newcastle Permanent Building Society Ltd	**30-Jun-18**	**954,293**	**10,716,100**	**8,242,302**	**62,041**	**20.1%**	**4.6%**	**67.5%**
	30-Jun-17	909,071	10,884,375	8,164,204	55,346	19.2%	4.3%	70.5%
Nexus Mutual	**30-Jun-18**	**18,515**	**323,252**	**301,618**	**1,715**	**14.3%**	**7.0%**	**75.0%**
	30-Jun-17	17,260	304,630	280,320	2,309	14.4%	9.6%	67.3%
Northern Inland Credit Union Ltd	**30-Jun-18**	**36,177**	**287,128**	**245,429**	**1,532**	**22.0%**	**3.0%**	**86.2%**
	30-Jun-17	35,102	265,919	226,502	1,720	21.8%	3.5%	84.2%
Orange Credit Union Ltd	**30-Jun-18**	**25,973**	**200,254**	**172,881**	**891**	**23.9%**	**2.6%**	**87.4%**
	30-Jun-17	25,318	190,795	164,028	985	24.2%	2.8%	85.3%
P&N Bank	**30-Jun-18**	**285,815**	**4,149,210**	**2,970,662**	**16,783**	**15.4%**	**4.3%**	**77.9%**
	30-Jun-17	273,493	3,985,492	2,837,251	13,667	14.5%	4.1%	80.3%
People's Choice Credit Union	**30-Jun-18**	**603,042**	**8,390,573**	**6,113,791**	**44,200**	**15.3%**	**5.5%**	**80.7%**
	30-Jun-17	570,754	7,895,914	5,802,013	46,018	14.9%	6.0%	79.4%
Police Bank Ltd[23]	**30-Jun-18**	**200,247**	**1,910,898**	**1,599,182**	**12,109**	**19.4%**	**4.4%**	**76.8%**
	30-Jun-17	183,699	1,681,290	1,368,936	12,122	18.7%	4.6%	75.9%
Police Credit Union Limited	**30-Jun-18**	**78,469**	**1,040,734**	**953,661**	**6,342**	**14.7%**	**5.9%**	**76.2%**
	30-Jun-17	73,156	943,636	856,091	7,097	14.9%	7.2%	79.1%
Q Bank	**30-Jun-18**	**78,255**	**839,711**	**735,298**	**4,607**	**19.9%**	**4.5%**	**79.0%**
	30-Jun-17	74,043	819,596	728,528	3,439	19.2%	3.3%	82.7%

Mutual	Period[9,10]	Net Assets[11] $'000	Total Assets $'000	Total Deposits $'000	Operating Profit Before Tax[12] $'000	Capital Adequacy Ratio[13] %	Return on Equity[14] %	Cost to Income Ratio[15] %
Qudos Bank	**30-Jun-18**	**255,949**	**3,763,343**	**3,363,502**	**2,053**	**14.4%**	**0.5%**	**96.7%**
	30-Jun-17	254,786	3,522,266	3,087,283	15,682	14.7%	4.5%	77.2%
Queensland Country Credit Union[24]	**30-Jun-18**	**245,187**	**2,167,525**	**1,881,212**	**7,893**	**15.8%**	**2.1%**	**95.2%**
	30-Jun-17	199,573	1,740,359	1,482,771	5,218	14.3%	1.0%	95.3%
RACQ Bank[25]	**30-Jun-18**	**166,139**	**2,136,356**	**1,475,377**	**-13,418**	**17.9%**	**-5.8%**	**131.2%**
	30-Jun-17	153,515	1,803,972	1,357,514	1,636	19.0%	1.0%	95.4%
Regional Australia Bank	**30-Jun-18**	**117,060**	**1,403,947**	**1,269,157**	**12,915**	**16.2%**	**8.2%**	**71.3%**
	30-Jun-17	107,182	1,311,010	1,176,723	11,755	15.8%	7.9%	71.0%
South West Slopes Credit Union	**30-Jun-18**	**21,285**	**164,661**	**142,028**	**883**	**26.1%**	**3.1%**	**86.1%**
	30-Jun-17	20,645	157,170	135,387	905	27.0%	3.1%	84.5%
Southern Cross Credit Union	**30-Jun-18**	**52,752**	**521,961**	**463,631**	**4,342**	**19.3%**	**6.0%**	**70.4%**
	30-Jun-17	49,689	482,090	427,006	4,217	19.6%	6.2%	69.9%
Sydney Credit Union Ltd	**30-Jun-18**	**80,659**	**867,529**	**771,619**	**5,385**	**16.9%**	**4.9%**	**78.7%**
	30-Jun-17	76,783	867,043	777,372	2,912	17.1%	2.8%	86.4%
Teachers Mutual Bank Limited	**30-Jun-18**	**525,385**	**7,068,765**	**5,813,647**	**45,211**	**15.7%**	**6.2%**	**71.7%**
	30-Jun-17	492,226	6,682,013	5,479,874	39,943	15.1%	6.0%	72.7%
The Capricornian Ltd	**30-Jun-18**	**23,902**	**333,437**	**306,555**	**2,000**	**13.9%**	**6.1%**	**76.3%**
	30-Jun-17	22,600	301,335	275,406	1,871	14.0%	6.0%	77.6%
The Mutual	**30-Jun-18**	**44,483**	**672,078**	**583,695**	**3,499**	**15.6%**	**5.7%**	**71.1%**
	30-Jun-17	42,034	641,600	573,384	3,399	15.2%	5.8%	70.9%
The Summerland Credit Union Limited	**30-Jun-18**	**59,094**	**689,150**	**598,864**	**4,235**	**16.8%**	**5.4%**	**79.5%**
	30-Jun-17	55,962	666,069	577,932	3,048	16.5%	3.9%	84.4%
Unity Bank Limited	**30-Jun-18**	**100,744**	**1,090,505**	**977,658**	**4,840**	**17.1%**	**4.2%**	**85.1%**
	30-Jun-17	96,920	1,057,749	932,210	3,162	17.5%	2.5%	87.7%

Footnotes

1 New figures show the leaders in banking satisfaction and advocacy, COBA, August 2018.

2 Prudential Inquiry into the Commonwealth Bank of Australia, APRA, April 2018.

3 2018 Fintech 100, KPMG, 2018.

4 The Pulse of Fintech 2018, KPMG, 2018.

5 Jonathan Ponciano, Blockchain Tops $4.5 Billion in private funding this year, but deal growth stalls, 2018.

6 JPMorgan's $11bn fintech bazooka, 2018.

7 Forging the Future, KPMG, 2017.

8 Information has been extracted from published annual reports (at a consolidated level where applicable). Parent numbers have been used in limited cases where they are a better reflection of results. In limited cases, KPMG has adjusted a number of balances to reflect significant one-off events.

9 All figures for the current and prior year are reported under AIFRS and in Australian dollars.

10 All of the results reported in the report were for a 12-month period.

11 Net assets include other equity interests.

12 Operating profit before tax is before outside equity interests.

13 Capital adequacy ratio has been calculated under the APRA's risk based measures.

14 Return on equity has been calculated as profit after tax as a percentage of average net assets.

15 Cost-to-income ratio has been calculated as operating expenses as a percentage of operating income.

16 Prior to November 2017, B&E Limited was registered under the name Bank of Us.

17 Prior to December 2017, Bank First was registered under the name Victoria Teachers Mutual Bank.

18 In February 2018, My Credit Union merged with Beyond Bank Australia, which is registered under the name Community CPS Australia Ltd.

19 In June 2018, Cape Credit Union merged with Community First Credit Union.

20 Prior to February 2018, Endeavour Mutual Bank was registered under the name Select Encompass Credit Union.

21 Prior to March 2018, Gateway Bank Ltd was registered under the name Gateway Credit Union.

22 Registered as Railways Credit Union Ltd.

23 In May 2017, Heritage Isle Credit Union (trading as: Banking of Heritage Isle) merged with Police Bank Ltd.

24 In April 2018, Queenslanders Credit Union merged with Queensland Country Credit Union

25 Prior to September 2017, RACQ Bank was registered under the name QT Mutual Bank.

For the complete datasheet compiled by KPMG, please visit **website**.

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