FIPS

Financial Institutions Performance Survey

March 2023 Quarterly Results

Overview

Information current as at 20 June 2023

“What the Budget delivered was approximately $19 billion in new operating expenditure over the next four years.

The results of the banking sector for the March 2023 quarter showed an overall decrease in net profit compared to the previous quarter driven mainly by some major banks preparing for future expected credit losses by increasing their provisions on loans. The sector’s net profit decreased by 13.0% from $1.77 billion in the quarter ended December 2022 to $1.54 billion in the quarter ended March 2023.

Key moments in the March 2023 quarter included the Government releasing Budget 2023 and the Reserve Bank of New Zealand (RBNZ) releasing its latest Monetary Policy Statement. These documents showed that the Government was not intending to reduce spending by as much as anticipated by most economists, while the RBNZ indicated that the interest rate cycle had peaked despite strong net migration figures adding fuel to inflation.

Inflation, interest rates and the cost of living

In the lead up to the release of Budget 2023, Prime Minister Chris Hipkins was keen to emphasise that it would be ‘no-frills‘, reflecting the times and addressing cost of living pressures for New Zealand households, whilst also funding the recovery and rebuild from the second costliest natural disaster New Zealand has seen. He hoped to do this in a way that wouldn’t further stoke inflationary pressures.

What the Budget delivered was approximately $19 billion in new operating expenditure over the next four years. However, Minister of Finance Grant Robertson was eager to emphasise that this was mostly to enable core spending to keep up with inflation. While there were some signals pointing to a future focus, the Budget appeared very much focused on “let’s get through today”[1].

Headlines from Budget 2023 which focused on the cost of living included:

- $1.2 billion for extending 20 hours of childcare to include two year olds (in addition to the current funding for three to five year olds) from March 2024;
- $618 million to remove the $5 co-payment for prescriptions;
- $402 million for expanding Warmer Kiwi Homes to subsidise 100,000 heating and insulation installations, 7,500 hot water heat pumps and 5 million LED light bulbs; and
- $327 million for free public transport for under 13 year olds and half price public transport for under 25 year olds.

Other key areas of spending included:

- $1 billion for the previously announced Cyclone Recovery Package;
- $71 billion over five years for new and existing infrastructure projects;
- $3.6 billion to address cost pressures in the current public housing build programme and a further $3.1 billion for 3,000 more public housing places by the end of June 2025[2].

KPMG’s reflections on the 2023 Budget announcement can be found here.

In late May, the RBNZ’s Monetary Policy Committee increased the Official Cash Rate (OCR) from 5.25% to 5.50%[3]. Industry expectations for the announcement were largely pointing towards the OCR going up to 6% over the next few months.

“In March 2023 alone the biggest monthly migrant arrivals estimate ever creating a net gain of

65,000

for the year ended March 2023.

> The inflation rate has fallen from **7.2%** for the year ended December 2022 to **6.7%** for the year ended March 2023.

This was on the back of Budget 2023 along with strong net migration data which saw 21,400 migrants arrive in March 2023 alone. This is the biggest monthly migrant arrivals estimate ever, creating a net gain of 65,000 for the year ended March 2023 compared to the prior year's net loss of 19,300[4]. In contrast to expectations, the RBNZ indicated that it still sees 5.50% as the peak and anticipates cuts to the OCR from the third quarter of 2024[5].

RBNZ Governor Adrian Orr had previously admitted that the RBNZ was deliberately engineering a recession in order to rein in inflation[6]. While the latest Monetary Policy Update noted that Treasury now forecasts that New Zealand will avoid recession as the rebuild from the flooding and cyclone events support activity along with stronger tourism, the latest figures from Stats NZ showed that New Zealand had entered a technical recession. Gross Domestic Product (GDP) has fallen for two consecutive quarters in a row, 0.6% in the December 2022 quarter and 0.1% in the March 2023 quarter[7].

The inflation rate has fallen from 7.2% for the year ended December 2022 to 6.7% for the year ended March 2023. This is attributed to an improved level of supply and a decrease in consumer demand as interest rates increase, both of which are helping to push down the Consumer Price Index (CPI). Petrol prices and airfares have been large contributors to the lower CPI.

While almost all CPI groups have seen a decreasing rate of inflation, the rate of inflation for food was still increasing[8]. We are yet to see the full inflationary impact from the additional spending on the recovery from Cyclone Gabrielle, with the Government announcing a $1 billion Cyclone Recovery Package.

The Monetary Policy Update also touched on unemployment which continued to sit at 3.4% for the quarter ended March 2023 due to the ongoing labour shortages in a number of sectors. This level is unchanged from the previous quarter.

Housing market

Increases to interest rates are continuing to impact demand for housing. Since the housing market peak in November 2021, house prices have fallen by 15.3% according to the RBNZ[8]. Auckland saw further falls over the first quarter as its average house price dropped $43,000 to $1.29 million although Northland, Otago, and the West Coast experienced increases to their average prices[9]. With the OCR expected to stay at 5.5% before decreasing, the housing market prices could be close to bottoming out. ANZ is predicting exactly that[10].

There continues to be a significant number of houses listed for sale, with property website realestate.co.nz showing 26,685 residential properties available for sale at the end of May, the highest number for the month of May since 2015. Stock levels were also up 81% compared to May 2021 when the market was approaching the peak of the recent boom. However, new listings are at their lowest level ever, indicating that the high level of properties available for sale have been sitting unsold with vendors expecting higher sale prices than the market is offering[11].

Lending

New mortgage lending for the March 2023 quarter was down 28.3% on the previous quarter at $12.6 billion. It was also down 24.5% on the March 2022 quarter which had new mortgage lending of $17.6 billion[12].

> Since the housing market peak in November 2021, house prices have **fallen** by **15.3%**.

> **New mortgage lending for the March 2023 quarter was down 28.3% on the previous quarter at $12.6 billion.**

Mortgage lending was down across all categories; however, the degree of the falls varied. New lending to first-home buyers decreased by 9.2% from the December 2022 quarter to the March 2023 quarter to $2.7 billion, while lending to other owner occupiers decreased by 32.6% to $11.3 billion and lending to investors decreased by 32.7% to $3.1 billion in the same period (see Figures 2–4).

2 – 4 See Figures 2–4 – page 10

The RBNZ confirmed on 26 May 2023 that rules around the loan-to-value ratios (LVR) imposed on banks would be loosened slightly. From 1 June 2023, the percentage of a bank's new mortgage lending that can go to owner-occupiers with a deposit of less than 20% was increased from a 10% cap to 15%. The changes also lowered the minimum deposit most investors needed to have from 40% to 35% of the value of the property[13].

Loan impairment and provisions

When compared to the previous quarter, the three months ended March 2023 have seen a significant increase to impaired asset expenses as the banks start to increase their loan provisions.

Among the major banks, impaired asset expense has increased 191.9% from the December 2022 quarter to the March 2023 quarter, rising to $320.2 million. Driving this change are significant increases to both individual and collective provisions[14]. See **page 11** for further analysis on this breakdown.

The major banks impaired asset expense as a percentage of operating expenses now sits at 20.55%[15]. Outside of the pandemic, this quarter is the highest the ratio has been since 2011 when we faced the Christchurch earthquakes and the fallout from the Global Financial Crisis. Former Westpac treasurer, Jim Reardon, is of the mind that as more and more people refix their mortgages at higher interest rates, further indicators of financial stress will start to show[16].

There are a few potential reasons for the increase in provisions on loans:

- Each of the major banks have reported an increase in both the percentage of loans which were impaired and the percentage of loans which were past due. These movements will likely feed into the expected credit loss models and produce a higher provisioning requirement. See Figures 5–7 for further information on the increases in these percentages.

5 – 7 See Figures 5–7 – page 12

- The economic environment has been uncertain since the Covid-19 pandemic, and this has meant that it has been difficult to rely solely on the expected credit loss models, which require a range of economic inputs. This is particularly the case for inputs such as unemployment, which has remained near historic lows despite other metrics indicating a tougher economic environment. Banks may be revising their models or adding overlays to better reflect the current economic environment, driving increases in the level of loan provisioning.
- Banks may be looking towards the future and acknowledging in their provisioning figures that it is likely going to remain a difficult economic environment for households for the foreseeable future, with an increase in defaults and losses on their lending.

> **Impaired asset expense has increased 191.9% from the December 2022 quarter.**

“Total provisions on loans of the major banks **rose** by **10.4%** from **$2.69** billion in December 2022 to **$2.97** billion in March 2023.

According to RBNZ data, total provisions on loans of the major banks rose by 10.4% from $2.69 billion in December 2022 to $2.97 billion in March 2023. The largest increases in total provisions on loans were seen by Westpac with a 27.5% increase and ANZ with a 12.9% increase[17].

It will be interesting to see whether the trend of increasing past due loans continues as households refix their mortgages onto higher rates, and how this translates into the banking sector's loan provisioning figures. It might be a lead indicator as to whether the RBNZ's OCR changes to date, and to come, have been on target for a mild recession or whether they over or undershoot the target.

Banking performance

Quarterly net profit after tax (NPAT) decreased by 13.0% from $1.77 billion in the December 2022 quarter to $1.54 billion in the March 2023 quarter[17].

Net interest decreased by 2.8% from $3.69 billion to $3.58 billion, driven by a slight reduction in the net interest margins of some of the major banks[17].

The usually volatile non-interest income was relatively flat compared to the prior quarter, as was operating expenses[17].

As discussed above, the largest contributor to the decrease in banking sector profits were the impairment charges taken, with impaired asset expense increasing by 192.9% from $109.7 million to $320.2 million[17].

The bank which has made headlines for its falling profit is Westpac, reporting that its net profit after tax for the six months ended 31 March 2023 was down by a third. It is important to note that part of this is due to the gain from last year's sale of Westpac Life, which was not repeated in the latest result. Westpac also took a large impairment charge against a backdrop of the financial impacts of severe weather in the North Island[18].

On 20 June 2023 the Government asked the Commerce Commission to launch an inquiry into competition in the banking sector to ascertain whether New Zealanders are "getting the best deal possible" from their banks.

This inquiry is focused on personal retail banking, specifically the competition for "personal loans, mortgages, credit cards and other banking services".

There will be an initial paper released in August 2023 which will give early indications of the nature of competition and set the direction for the study with the full report due in August 2024[19].

Concluding remarks

In summary, the March 2023 quarter's banking sector results showed a reversal to the general trend of rising profits before and during the pandemic (except for the volatile period at the start of the pandemic). There are indicators that banks are expecting more losses on their loans in the future through impairment charges taken to increase loan provisioning levels.

While the RBNZ has indicated that interest rates have peaked, which will come as a relief to borrowers, this is dependent on inflation continuing to reduce. In turn, this will be dependent on factors such as net migration and Government spending.

“Quarterly NPAT **decreased** by **13.0%** from **$1.77** billion in the December 2022 quarter to **$1.54** billion in the March 2023 quarter.

> With an overall fall in profits in the March 2023 quarter, we are seeing a reversal to the general trend of rising profits in recent years.

There will also be a large number of borrowers who have yet to roll onto higher interest rates, which has the potential to lead to an increase in arrears in the future.

Looking forward, it will be interesting to see whether banks continue to provide for future expected credit loses, and the degree to which these losses eventuate.

As we potentially come to the end of the interest rate rising cycle, it will be interesting to see if the rises have stopped in the right place and at the right time. With the recently released figures showing a 0.1% decline in our GDP meaning that New Zealand is in a technical recession, we will need to wait until the next quarter's results to determine whether this is the start of a mild recession that will put a break on inflation, or whether the steps taken overshoot the target and cause greater economic slowdown in the form of a more severe recession, or whether the steps taken end up short of the target and the economy takes off again. There are more questions than is desirable.

Commerce Commission banking sector inquiry

What is it?

The Government has asked the Commerce Commission to launch an inquiry into competition in the banking sector to ascertain whether New Zealanders are "getting the best deal possible" from their banks.

What is covered?

The inquiry will focus on personal banking services, meaning those "ordinarily acquired for personal, domestic, or household use" and could include:

- the structure of the industry and the nature of competition;
- the conditions for entry by potential competitors and the conditions for expansion;
- any barriers to consumers comparing bank offers or switching banks, including the extent to which products or services may be tied or bundled;
- any impediments to new or innovative banking products or services; and
- comparative indicators of bank financial performance (including profitability).

Timing

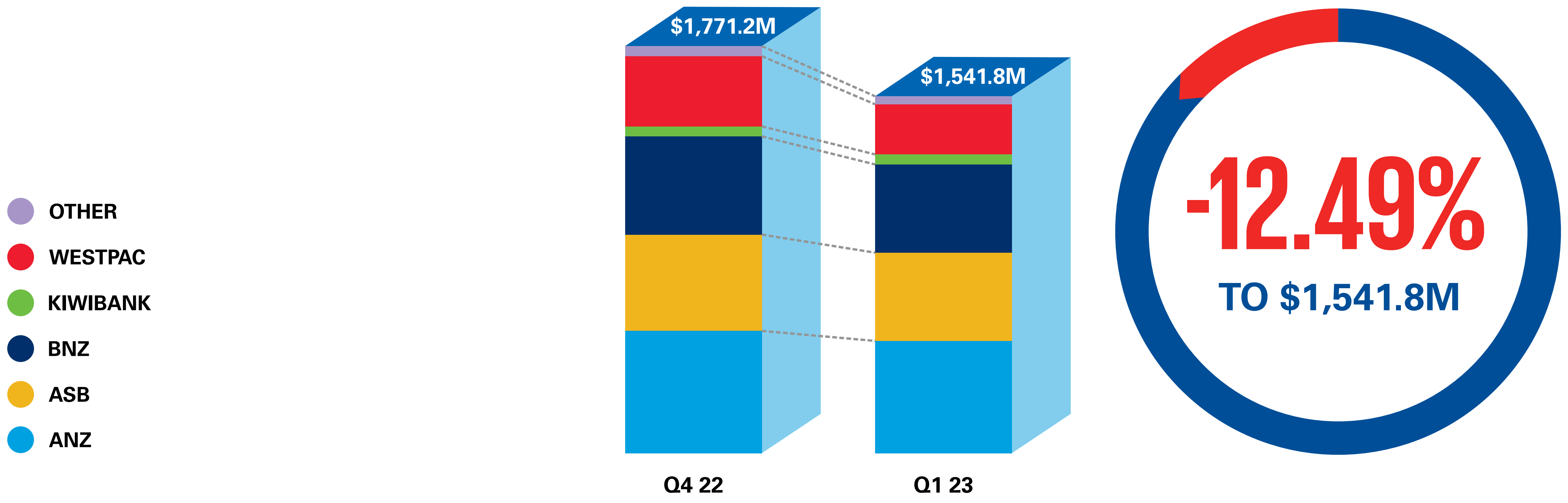
The Commission is expected to release a preliminary issues paper in August 2023, with the full report due in August 2024.

Net profit after tax

Q4 22–Q1 23 | Q1 22–Q1 23 | Q1 21–Q1 23 | Q1 18–Q1 23

HOVER over the button to see the comparisons over time, 1 quarter, 1, 2 and 5 years

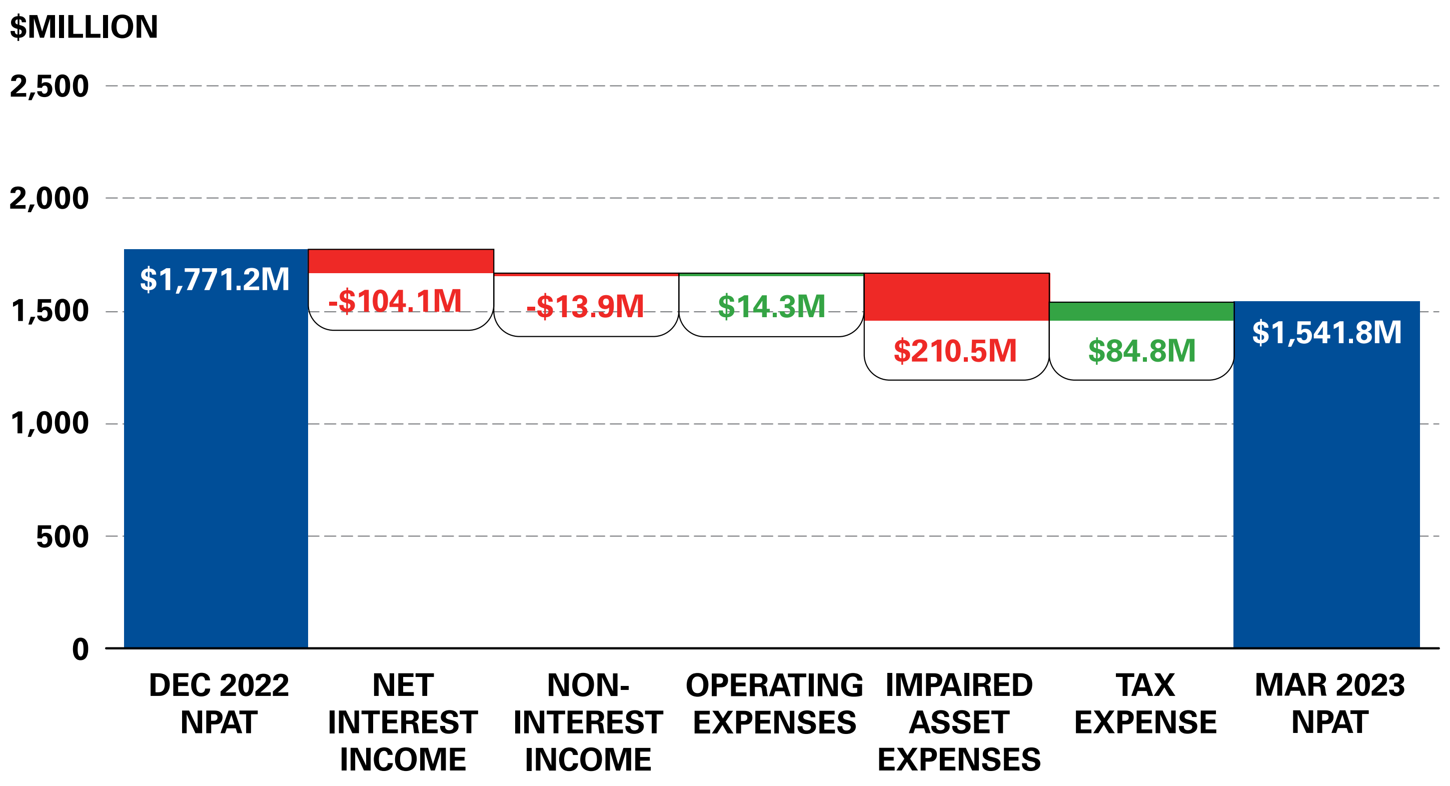
Movement in net profit: Breakdown



Hover over the button to see historic quarterly results

Q1 23 | Q1 22
Q4 22 | Q4 21
Q3 22 | Q3 21
Q2 22 | Q2 21

MOVEMENT IN NET PROFIT FOR THE QUARTER ENDED 31 MARCH 2023



Q4 22–Q1 23 | Q3 22–Q1 23 | Q2 22–Q1 23 | Q1 22–Q1 23

HOVER over the button to see the movement in each quarter

Net interest income

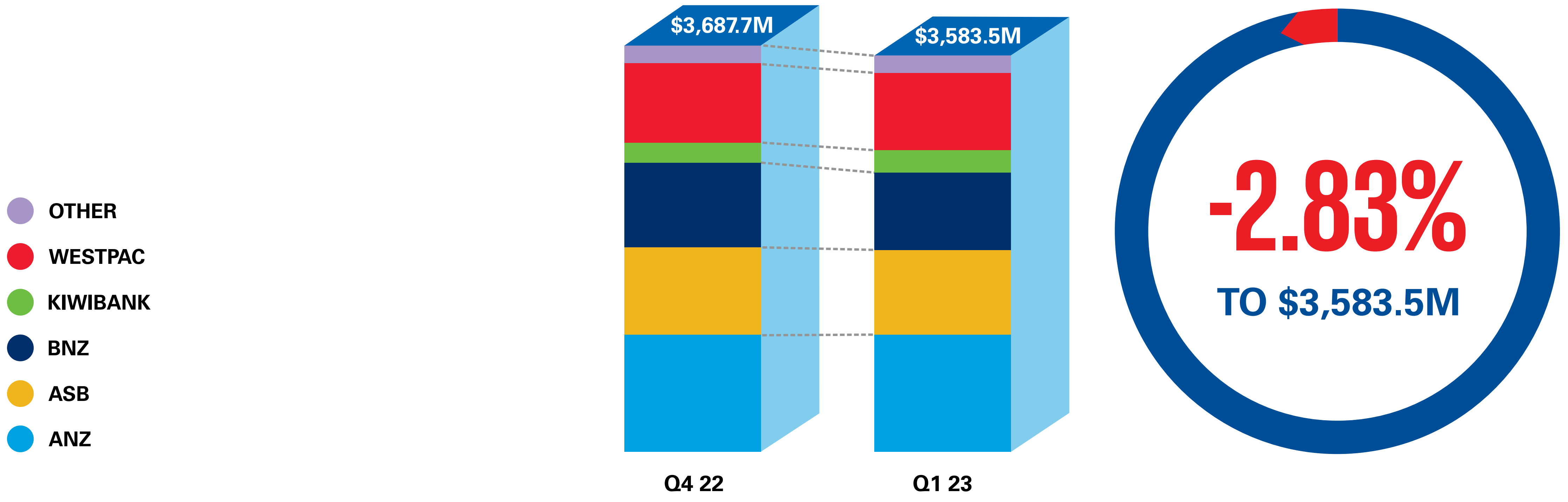


TABLE 1: Movement in interest margin

Entity[20]	Quarter ended 31 Mar 23 (%)	Mvmt. during the quarter (bps)	Mvmt. for the 6 months (bps)	Mvmt. for the 12 months (bps)
ANZ	2.4	0	10	30
ASB	2.5	0	0	40
bnz	2.4	-10	0	30
HEARTLAND BANK	4.1	-10	0	-20
Kiwi bank.	2.5	0	10	40
sbs	2.5	-20	-10	-10
TSB	2.1	-10	0	20
The Co-operative Bank	2.6	0	-10	30
Westpac	2.3	0	10	30

Net profit after tax

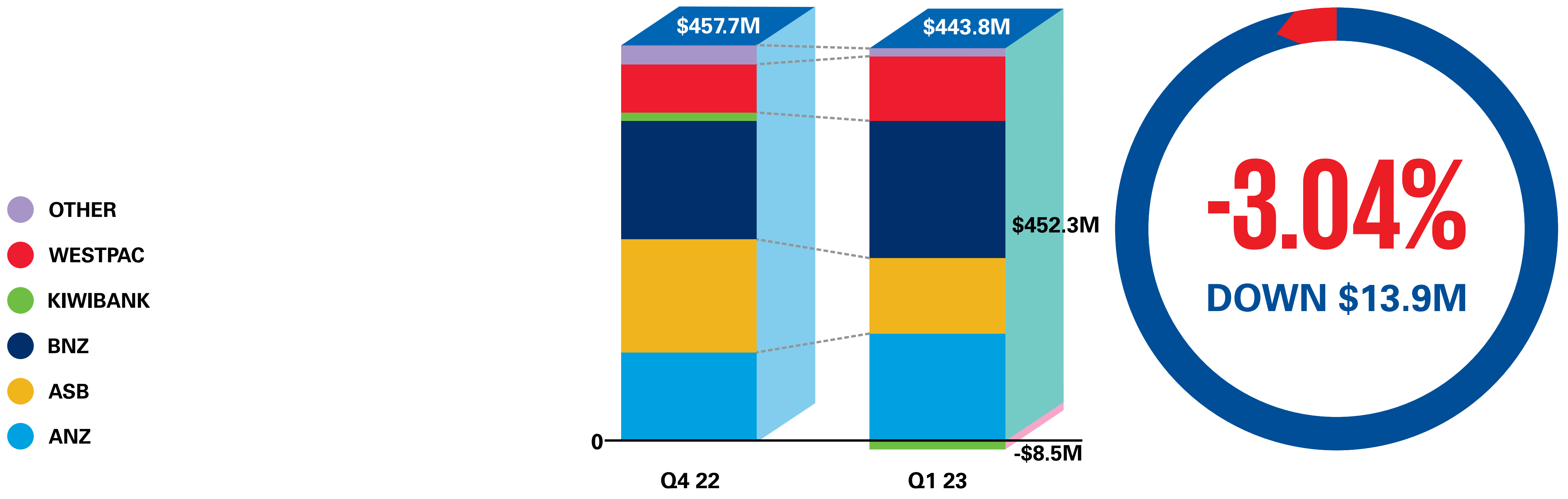
Q4 22–Q1 23 Q3 22–Q1 23 Q2 22–Q1 23 Q1 22–Q1 23

HOVER over the button to see the movement in each quarter

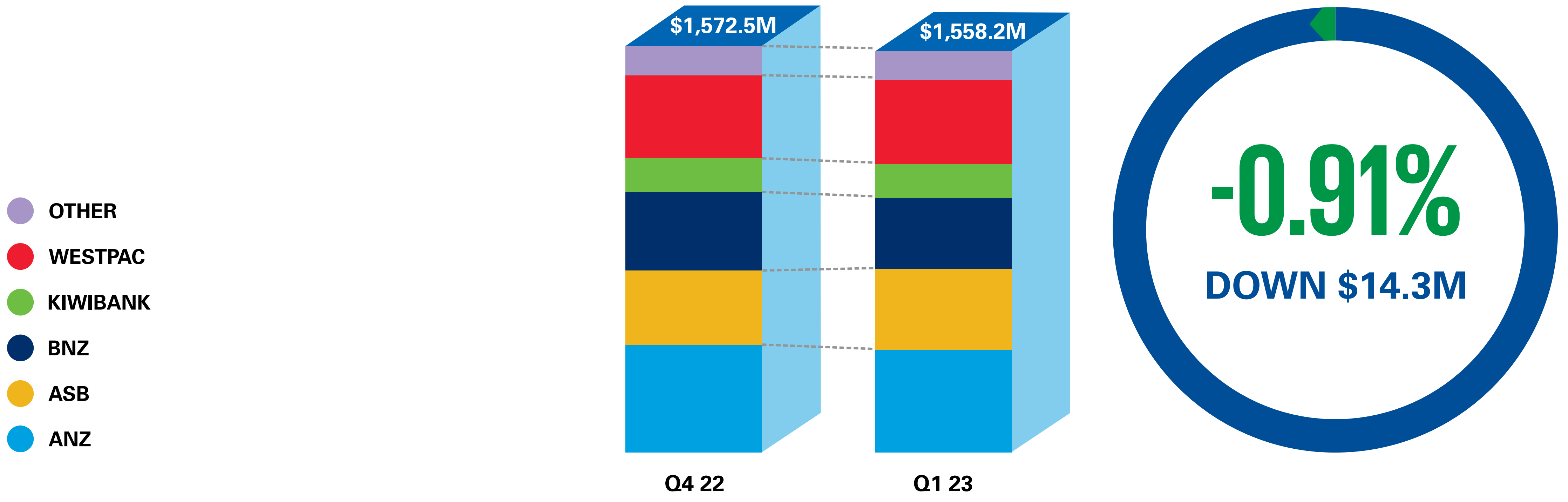
Q4 22–Q1 23 Q3 22–Q1 23 Q2 22–Q1 23 Q1 22–Q1 23

HOVER over the button to see the movement in each quarter

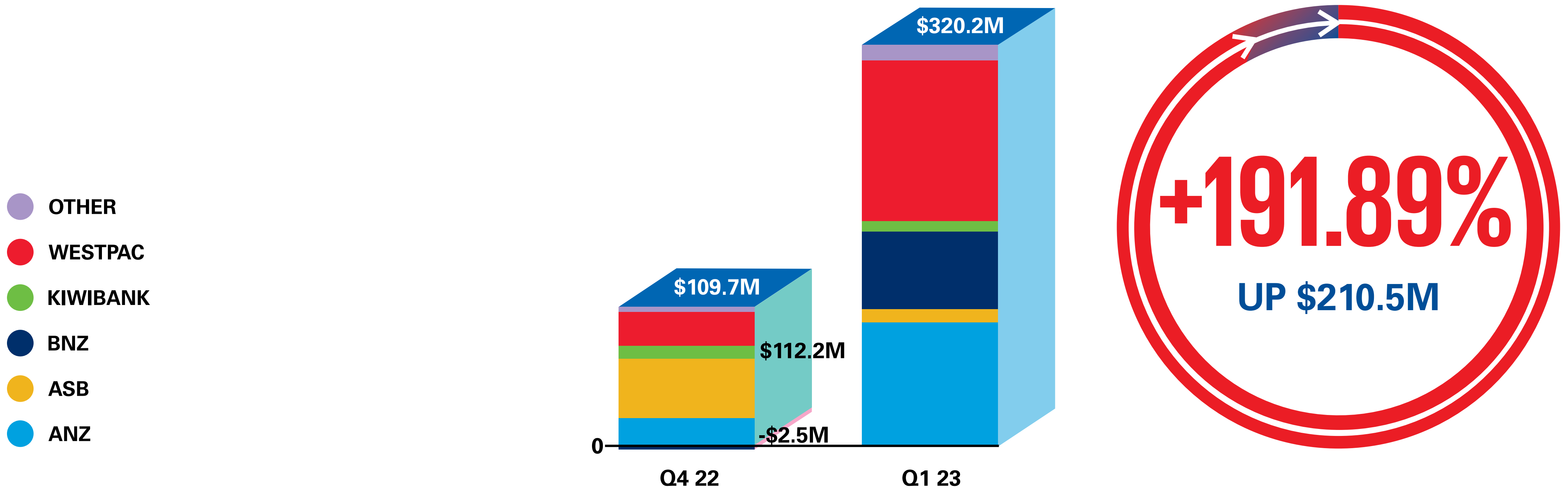
Non-interest income



Operating expenses



Impaired asset expenses (writebacks)

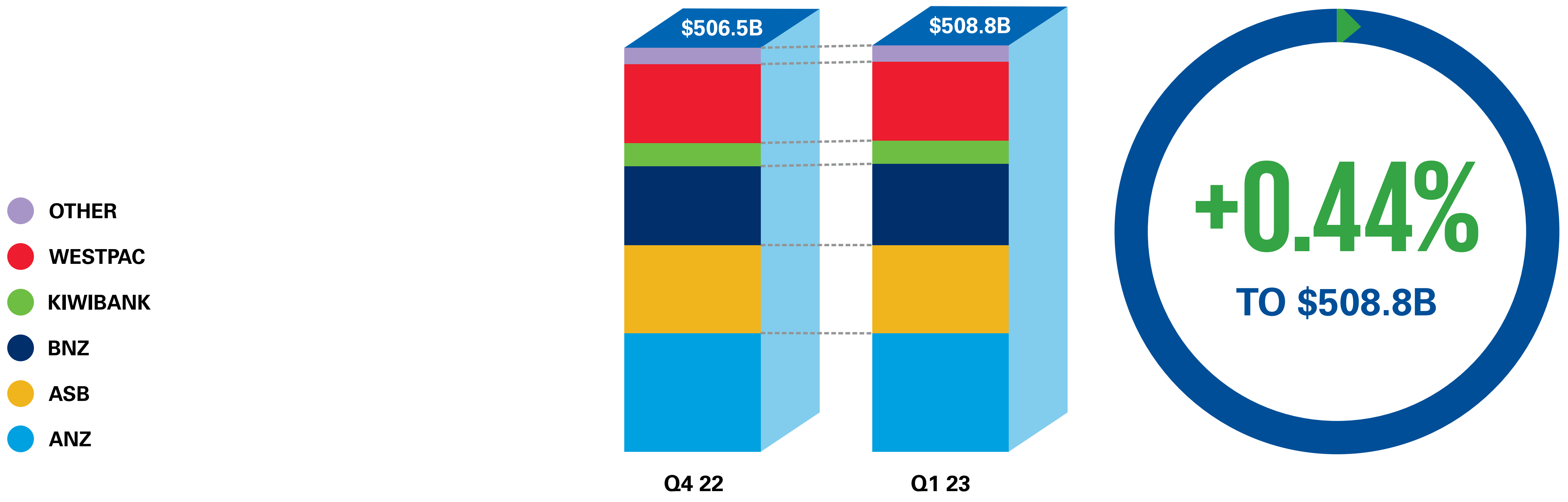


Lending

Q4 22–Q1 23 | Q3 22–Q1 23 | Q2 22–Q1 23 | Q1 22–Q1 23

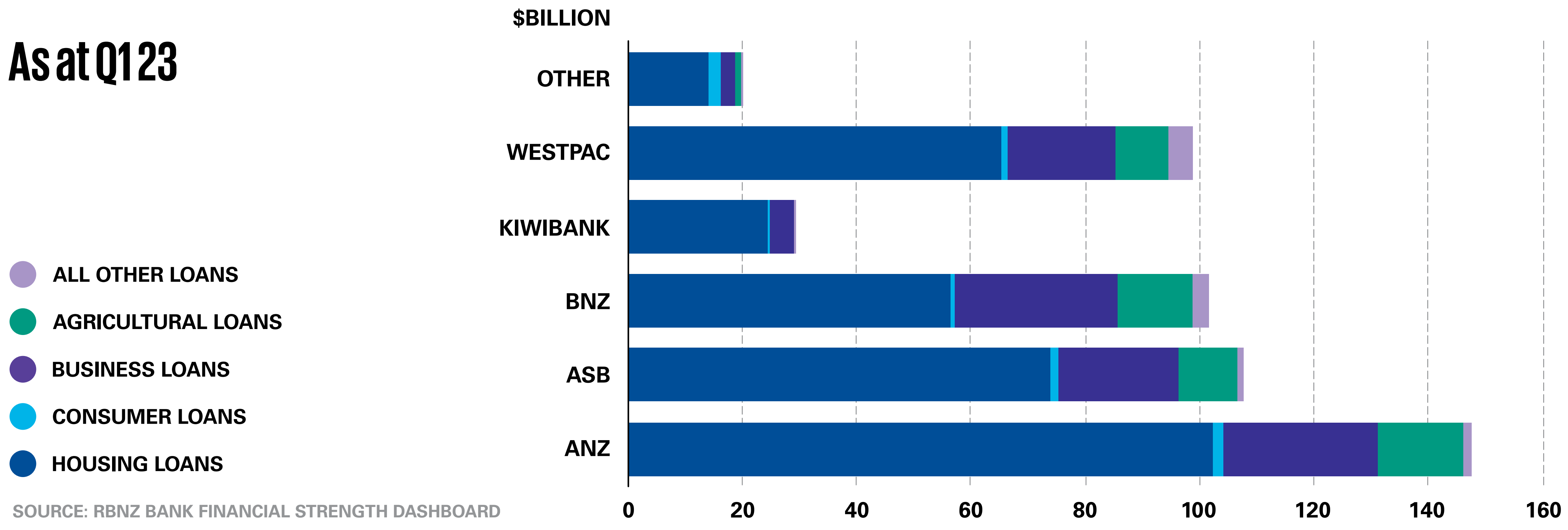
HOVER over the button to see the movement in each quarter

Gross loans



Breakdown by bank

As at Q1 23



SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

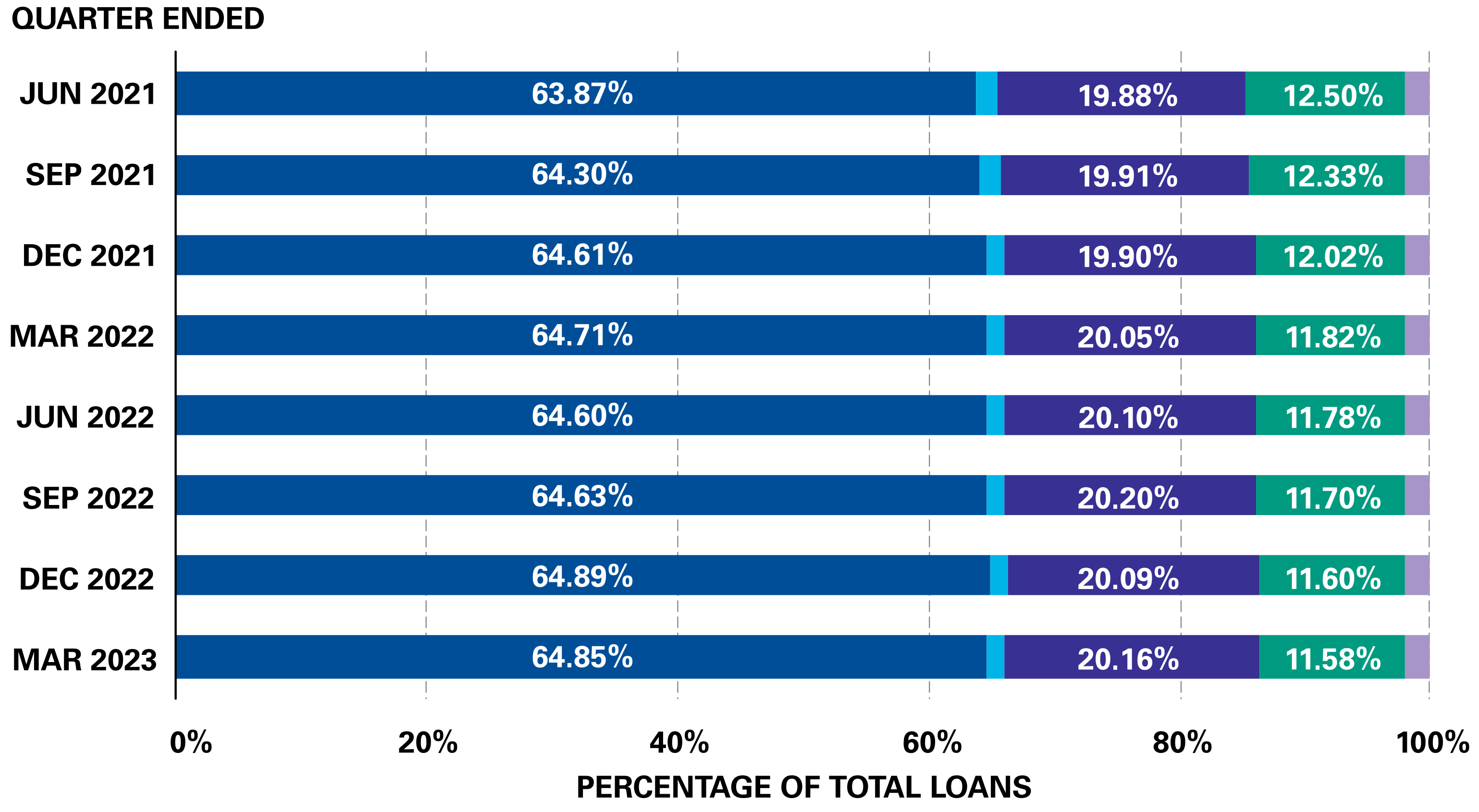
TABLE 2: Analysis of gross loans

Entity[20] Quarterly analysis	Quarter ended 31 Mar 23 $Million	Quarter ended 31 Dec 22 $Million	% Increase (Quarterly)
ANZ	148,173	147,870	0.21%
ASB	110,284	110,458	-0.16%
bnz	101,994	101,313	0.67%
HEARTLAND BANK	4,851	4,714	2.91%
Kiwi bank.	29,342	28,976	1.27%
sbs	5,059	4,948	2.26%
TSB	7,076	7,035	0.57%
The Co-operative Bank	2,897	2,906	-0.30%
Westpac	99,163	98,329	0.85%
Total	508,799	506,547	0.44%

Entity[20] Annual analysis	Quarter ended 31 Mar 23 $Million	Quarter ended 31 Mar 22 $Million	% Increase (Annual)
ANZ	148,173	146,971	0.82%
ASB	110,284	107,456	2.63%
bnz	101,994	98,791	3.24%
HEARTLAND BANK	4,851	4,310	12.56%
Kiwi bank.	29,342	27,468	6.82%
sbs	5,059	4,433	14.13%
TSB	7,076	6,700	5.60%
The Co-operative Bank	2,897	2,704	7.13%
Westpac	99,163	94,872	4.52%
Total	508,799	493,705	3.06%

Lending

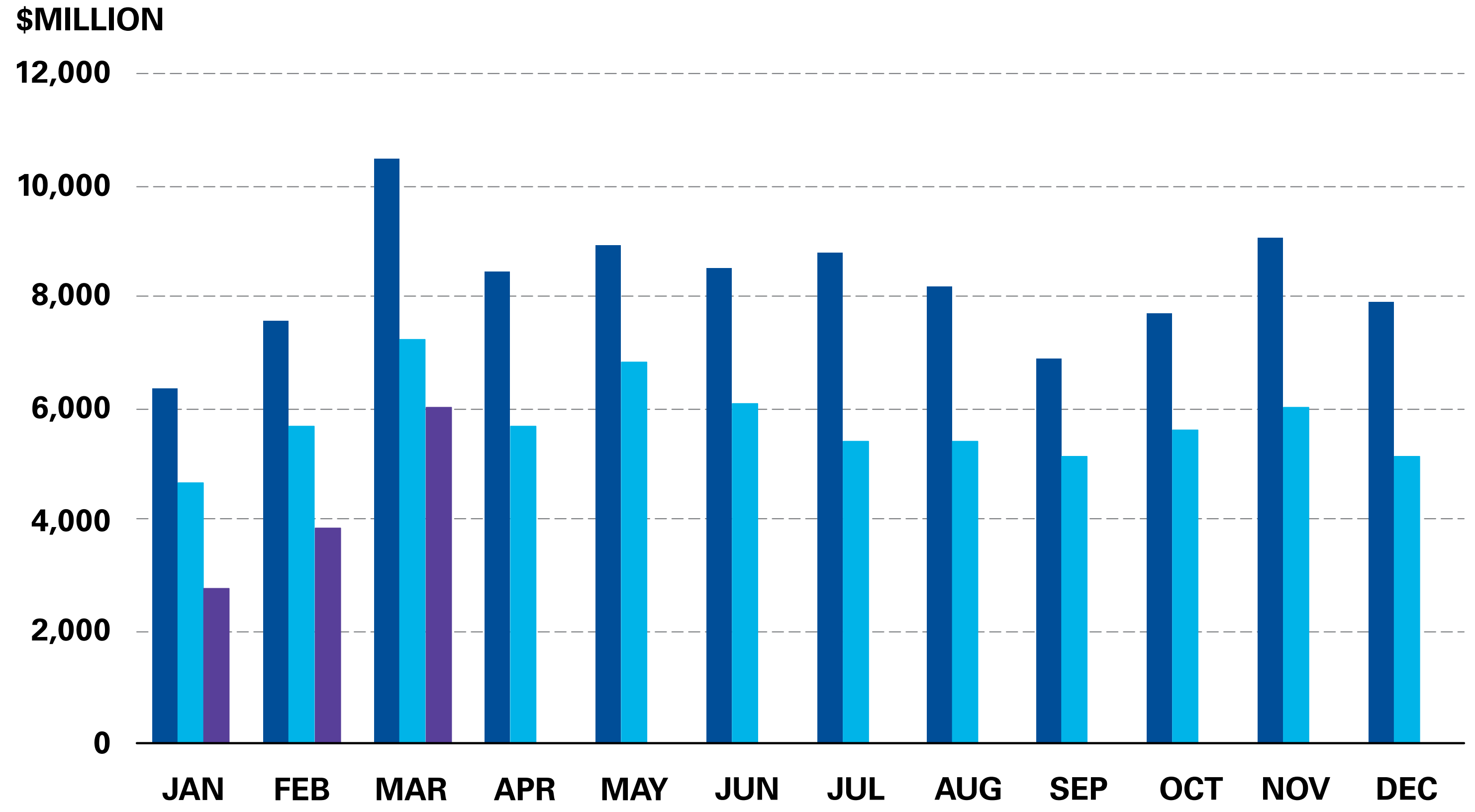
1 NZ BANKS PORTFOLIO COMPOSITION BY QUARTER



- ALL OTHER LOANS
- AGRICULTURAL LOANS
- BUSINESS LOANS
- CONSUMER LOANS
- HOUSING LOANS

SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

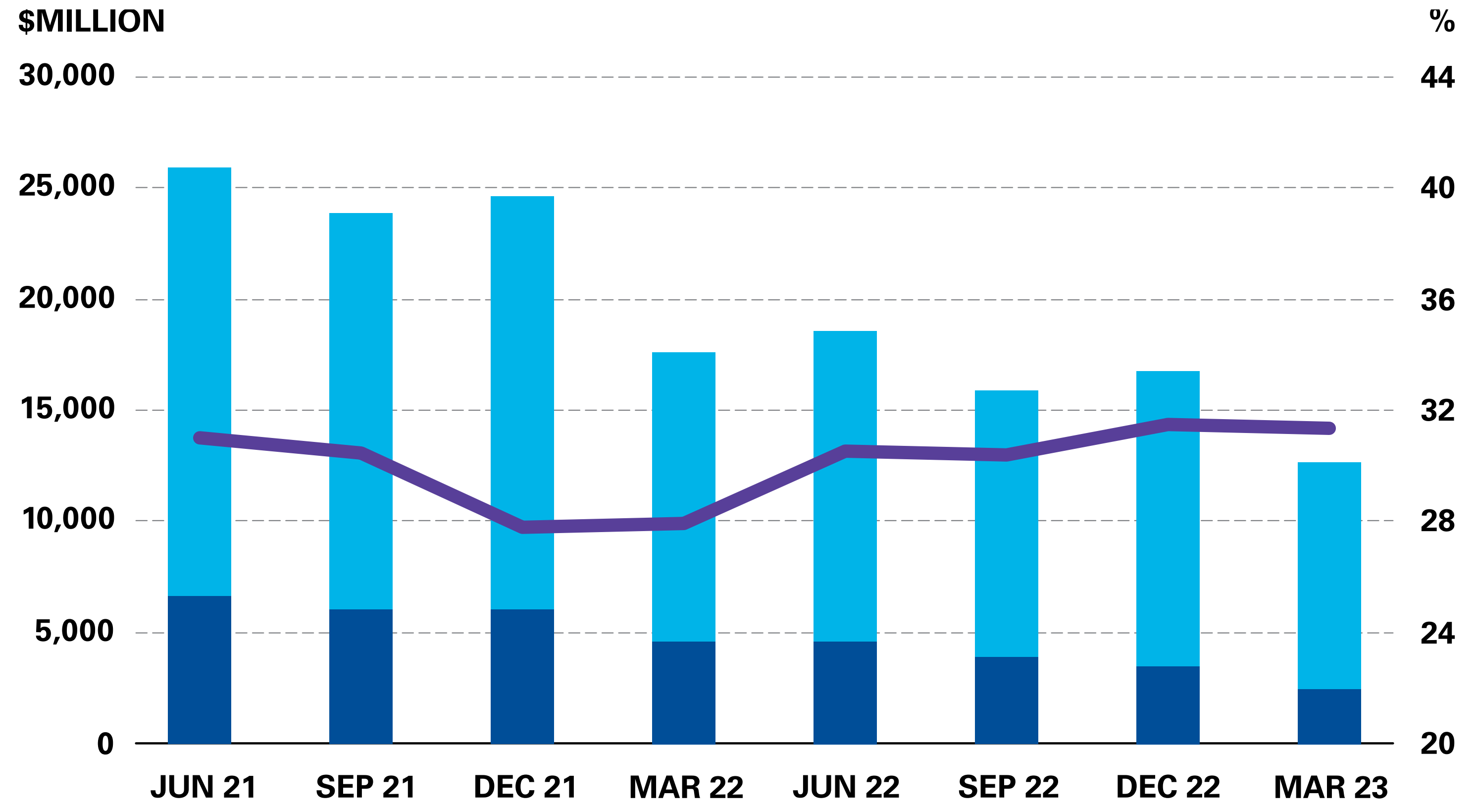
2 TOTAL MONTHLY MORTGAGE LENDING



- 2021
- 2022
- 2023

SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

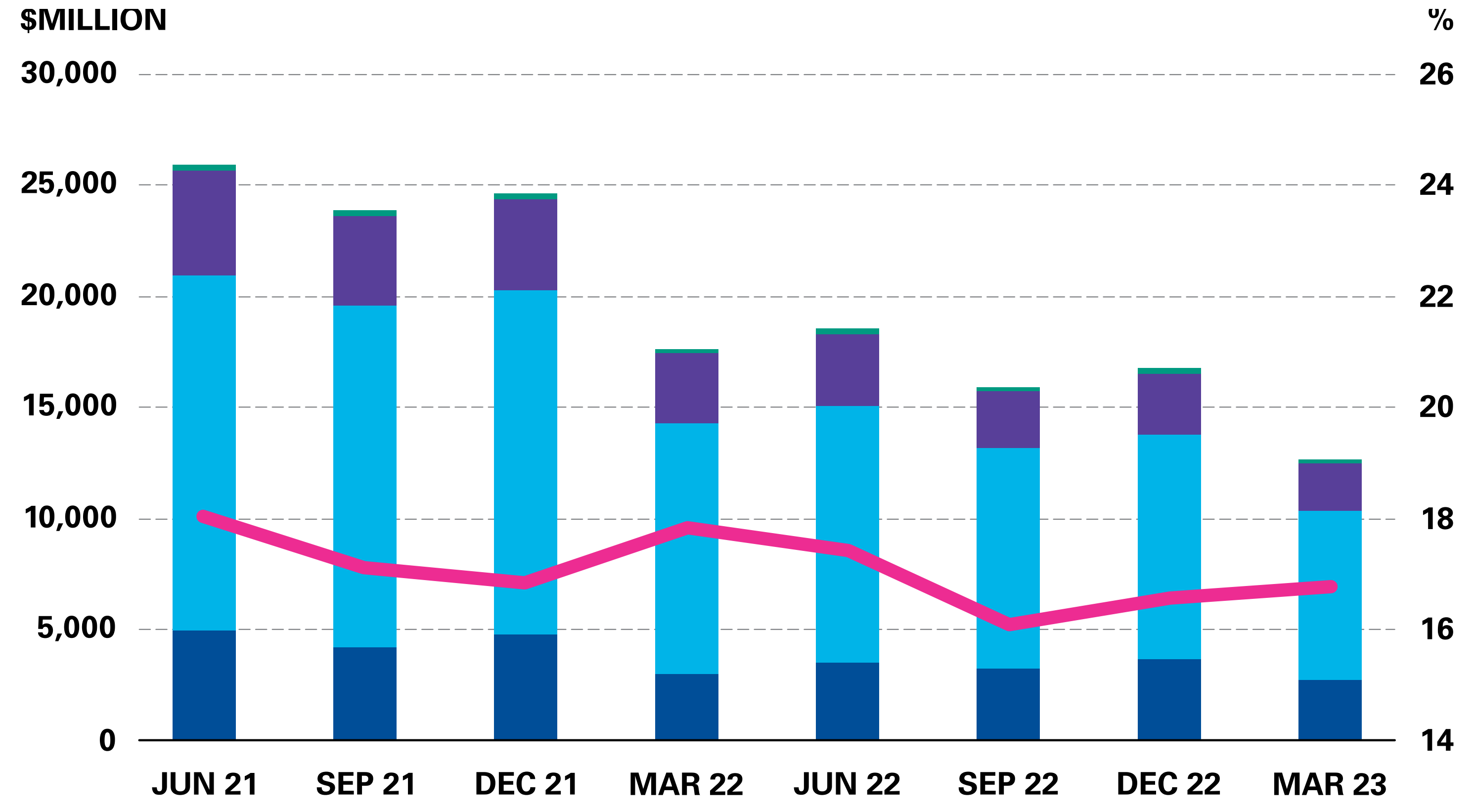
3 NEW MORTGAGE LENDING BY PAYMENT TYPE



- INTEREST ONLY (INCLUDING REVOLVING CREDIT) (LHS)
- PRINCIPAL AND INTEREST (LHS)
- PROPORTION OF NEW LENDING INTEREST ONLY – INVESTOR (%) (RHS)

SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

4 NEW MORTGAGE LENDING BY BORROWER TYPE



- FIRST-HOME BUYER (LHS)
- OTHER OWNER OCCUPIER (LHS)
- INVESTOR (LHS)
- BUSINESS PURPOSES (LHS)
- INVESTOR LENDING (%) (RHS)

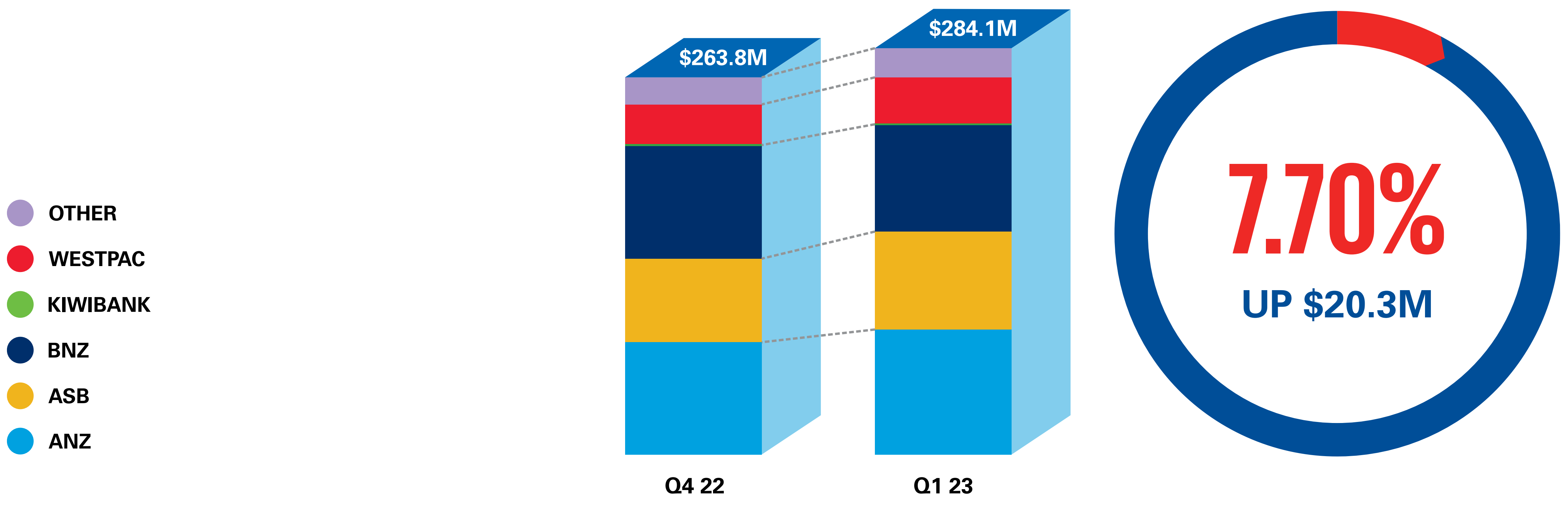
SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

Asset quality

Q4 22–Q1 23 | Q3 22–Q1 23 | Q2 22–Q1 23 | Q1 22–Q1 23

HOVER over the button to see the movement in each quarter

Individually assessed provisions



Collectively assessed provisions

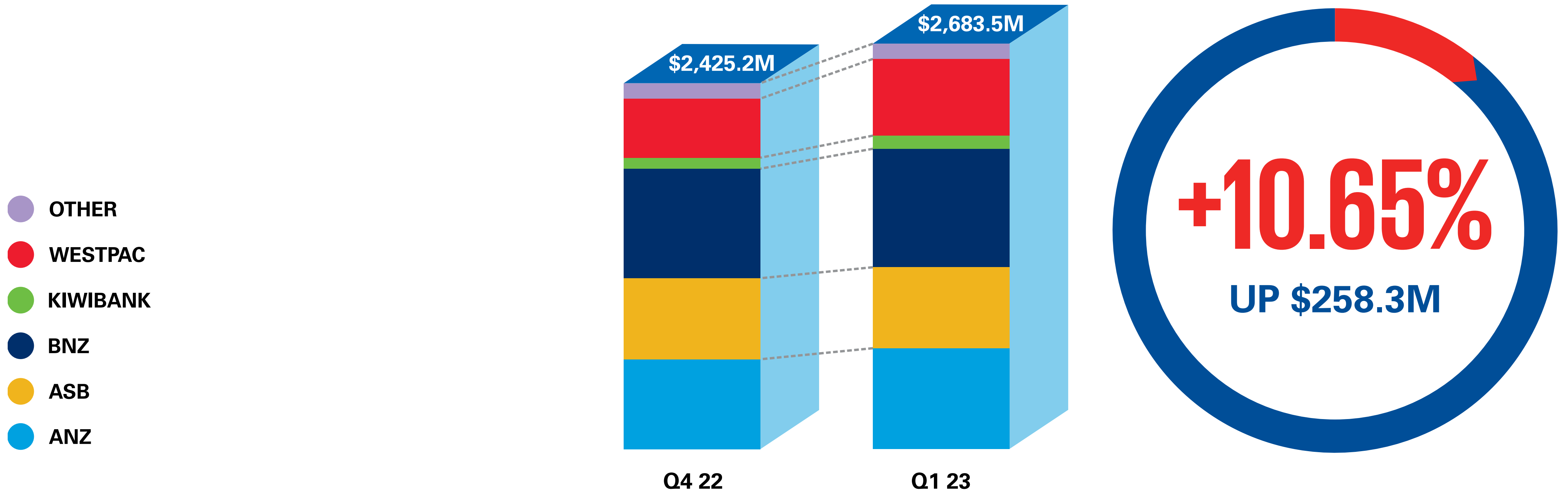


TABLE 3: Impaired asset expenses

	$Million
March 2023	$320.2
December 2022	$109.7
September 2022	$114.3
June 2022	$52.2
March 2022	$52.7
December 2021	-$35.0
September 2021	-$29.2
June 2021	-$70.7

TABLE 4: Movement in impaired asset expense/Average gross loans

Entity[20]	Quarter ended 31 Mar 23 (%)	Mvmt. during the quarter (bps)	Mvmt. for the 12 months (bps)
ANZ	0.27%	21	30
ASB	0.04%	-14	-2
bnz	0.25%	26	11
HEARTLAND BANK	0.55%	13	19
Kiwi bank.	0.12%	-2	10
sbs	0.30%	8	27
TSB	-0.17%	0	-15
The Co-operative Bank	0.06%	2	6
Westpac	0.52%	41	49
Average	0.25%	16	21

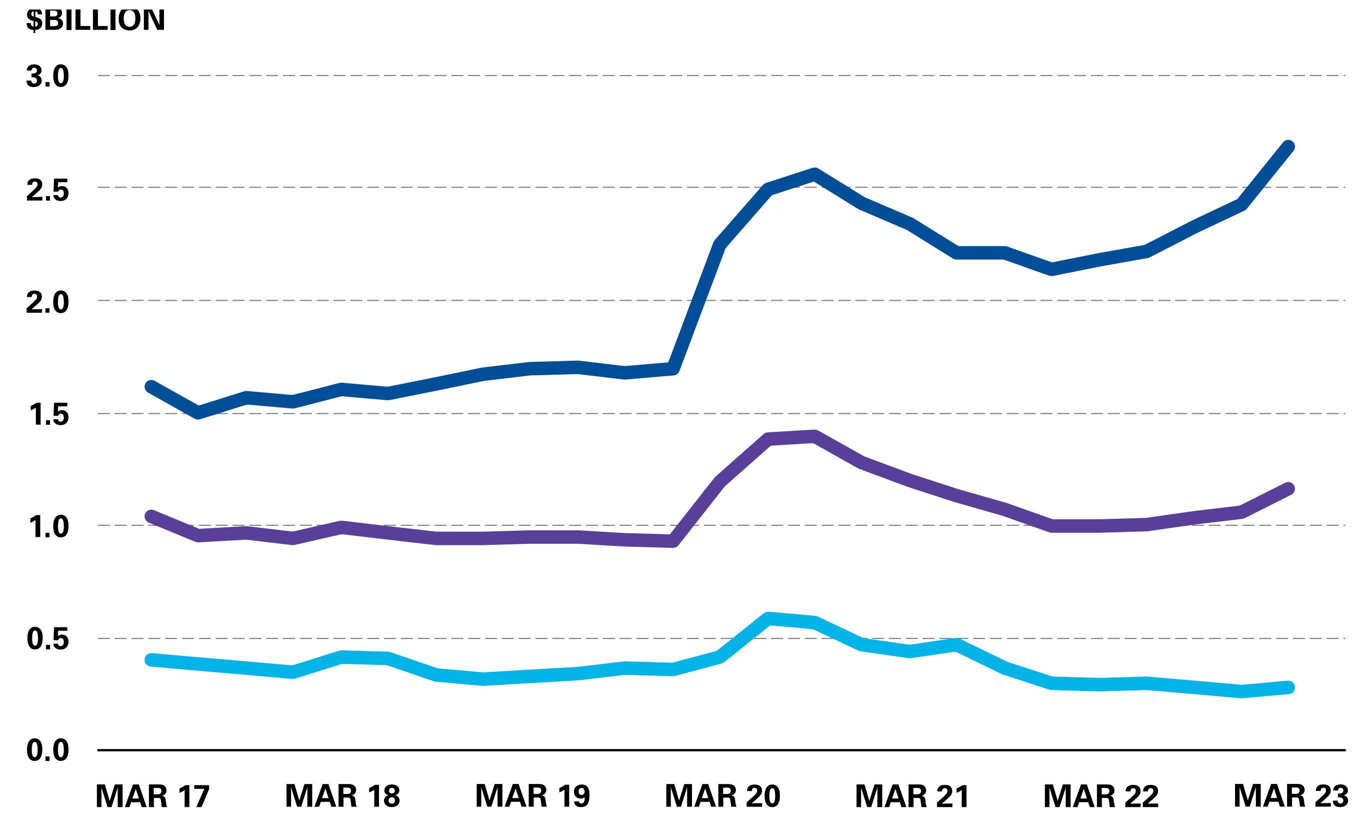
The results for the quarter ended March 2023 showed the trend of increasing collective provisioning picking up pace. There have now been five consecutive quarters of increases since it bottomed out in the December 2021 quarter. Individual provisions increased by 7.70% from $263.8 million in the December 2022 quarter to $284.1 million in the March 2023 quarter, while collective provisions increased by 10.65% from $2,425.2 million in the December 2022 quarter to $2,683.5 million in the March 2023 quarter.

The coverage ratio for the quarter (Total provision for doubtful debts/Gross loans and advances) increased from 0.53% in the December 2022 quarter to 0.58% in the March 2023 quarter (see **Figure 5**), after a low of 0.50% in December 2021. Although this is a steep increase for one quarter, we must remember that we are still a way off from the peak (in hindsight slightly inflated) coverage ratio of 0.70% in September 2020 seen as a result of the Covid-19 pandemic.

These provision increases are an indication that the banking sector is expecting deteriorating economic conditions, including lingering high inflation, increased cost of living and a tight labour market to adversely impact customers. These factors are driving banks to increase provisioning in response to the increased likelihood of customers not being able to meet their repayments, and we would expect this trend to continue throughout 2023.

Asset quality

5 **MOVEMENT IN PROVISIONING**

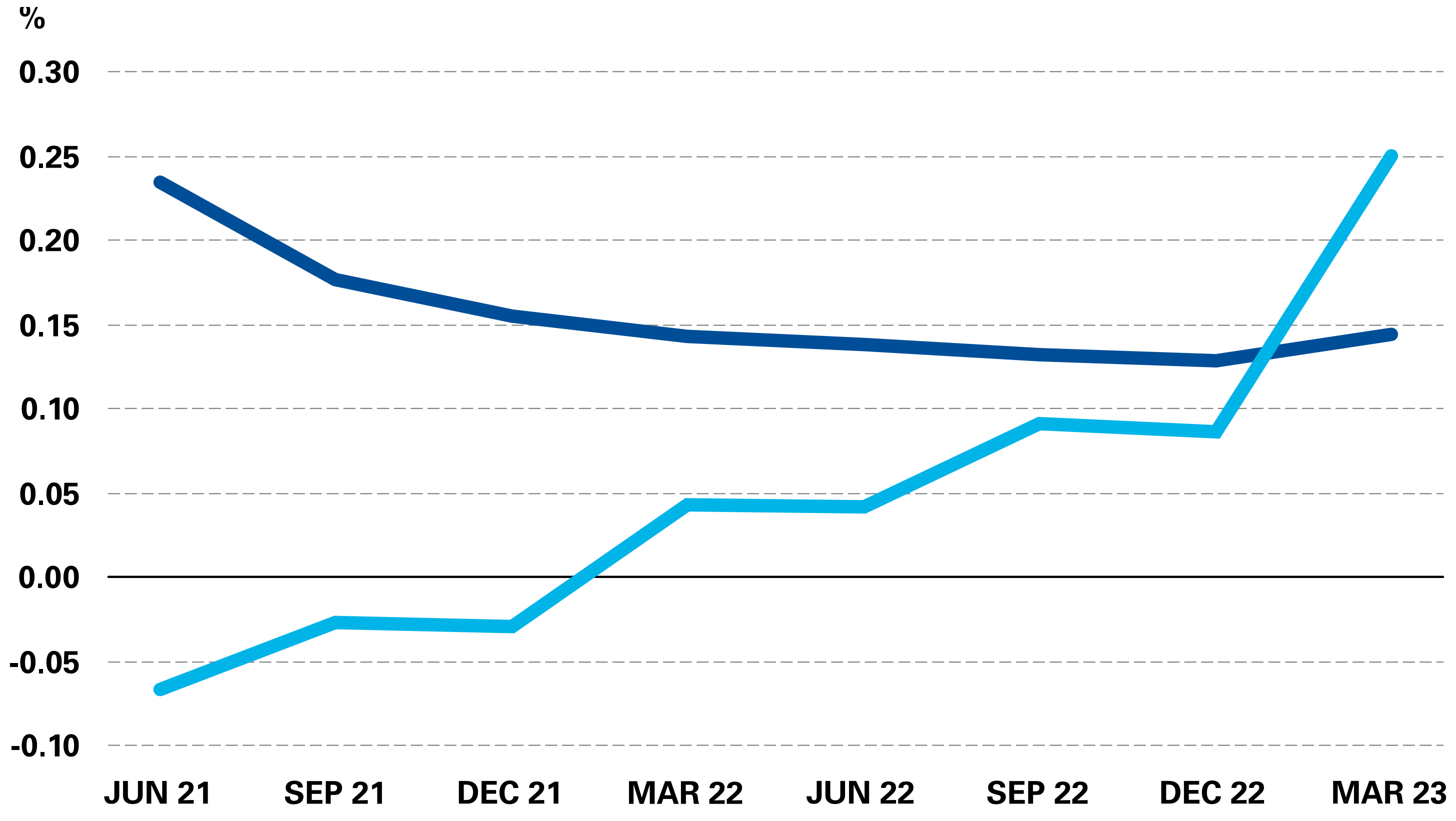


COLLECTIVELY ASSESSED PROVISIONS (LHS)

INDIVIDUALLY ASSESSED PROVISIONS (LHS)

TOTAL PROVISION FOR DOUBTFUL DEBTS/ GROSS LOANS AND ADVANCES (RHS)

6 **MAJOR BANKS: GROSS IMPAIRED VS. IMPAIRED ASSET EXPENSE**



GROSS IMPAIRED LOANS/ GROSS LOANS AND ADVANCES

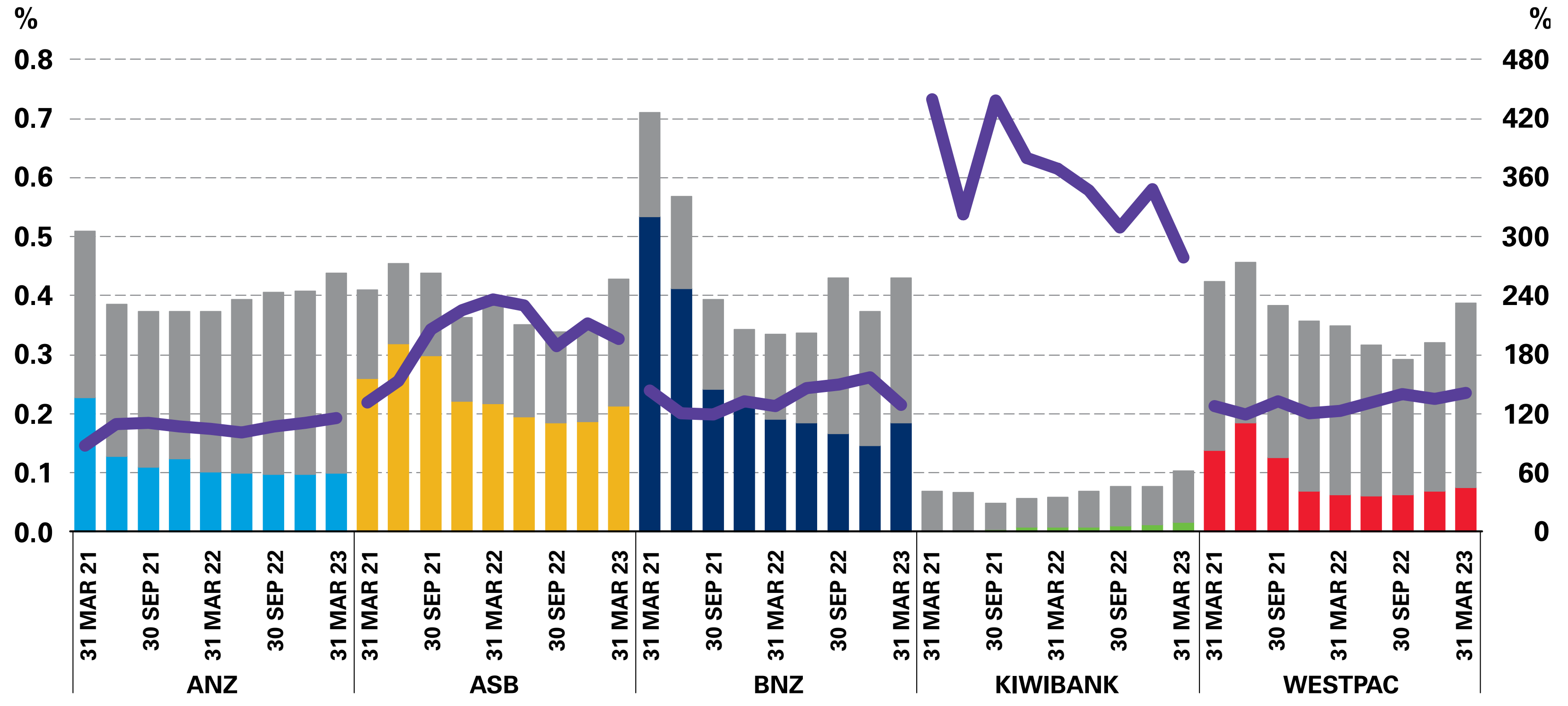
IMPAIRED ASSET EXPENSE/ AVERAGE GROSS LOANS AND ADVANCES

7 **MAJOR BANKS: PAST DUE AND GROSS IMPAIRED ASSETS VS. GROSS LOANS AND ADVANCES**

GROSS IMPAIRED/ GROSS LOANS AND ADVANCES (LHS)

PAST DUE/GROSS LOANS AND ADVANCES (LHS)

TOTAL PROVISIONS/ PAST DUE AND GROSS IMPAIRED ASSETS (RHS)



Major banks – Quarterly analysis

Size & strength measures

Entity[20]	30 Jun 21	30 Sep 21	31 Dec 21	31 Mar 22	30 Jun 22	30 Sep 22	31 Dec 22	31 Mar 23
Total assets ($Million)								
ANZ	187,064	185,072	190,636	190,720	193,335	201,439	195,852	189,253
ASB	120,810	120,230	121,030	123,365	125,838	128,437	128,426	128,191
BNZ	118,549	119,122	123,038	124,060	126,852	131,420	130,242	126,460
Heartland Bank	4,419	4,484	4,703	4,857	5,159	5,264	5,409	5,476
Kiwibank	28,230	29,379	30,970	30,589	31,547	32,017	33,368	33,505
SBS	4,789	4,889	5,024	5,220	5,421	5,519	5,771	6,005
TSB	8,725	8,780	8,934	8,961	8,925	8,942	9,124	9,145
The Co-operative Bank	3,171	3,194	3,239	3,194	3,189	3,261	3,331	3,344
Westpac	116,786	119,848	122,382	125,026	129,385	135,780	134,315	132,735
Total	592,543	594,998	609,954	615,991	629,651	652,078	645,838	634,114
Increase in gross loans and advances (%)								
ANZ	1.41	0.93	1.81	1.91	0.75	-0.03	-0.10	0.21
ASB	2.79	1.94	0.88	1.31	1.28	0.79	0.69	-0.16
BNZ	2.78	1.64	2.19	0.92	1.07	0.65	0.82	0.67
Heartland Bank	3.11	2.54	5.19	3.35	5.20	1.83	2.09	2.91
Kiwibank	2.51	3.49	3.87	0.85	1.27	1.84	2.28	1.27
SBS	0.23	2.00	3.78	2.59	2.82	3.87	4.50	2.26
TSB	2.32	1.53	1.70	-0.49	-0.23	1.96	3.21	1.01
The Co-operative Bank	2.05	-0.13	-1.36	-0.65	2.03	2.70	2.54	-0.30
Westpac	2.13	0.15	0.81	0.65	1.40	1.65	0.55	0.85
Average	2.20	1.30	1.63	1.25	1.13	0.81	0.64	0.44

Entity[20]	30 Jun 21	30 Sep 21	31 Dec 21	31 Mar 22	30 Jun 22	30 Sep 22	31 Dec 22	31 Mar 23
Capital adequacy (%)								
ANZ[21]	15.50	16.90	16.40	15.10	15.60	16.40	16.40	15.20
ASB[21]	15.10	14.50	14.60	13.40	15.00	15.00	15.50	15.70
BNZ	16.50	16.90	16.40	15.30	15.00	15.40	15.30	15.70
Heartland Bank	13.90	14.00	14.00	13.10	13.40	12.90	13.10	12.60
Kiwibank	13.20	12.80	13.70	13.80	13.60	13.60	13.40	13.40
SBS	16.20	16.30	16.00	15.40	15.00	14.60	13.90	13.60
TSB	14.20	14.10	13.70	13.50	13.60	13.40	13.10	13.30
The Co-operative Bank	16.80	16.10	16.90	16.90	16.60	16.70	16.70	16.60
Westpac[21]	18.80	18.60	19.00	14.50	14.80	13.90	14.20	13.70
Net profit ($Million)								
ANZ	487	503	496	600	620	583	531	491
ASB	317	367	382	349	356	438	420	383
BNZ	318	344	356	353	377	328	424	381
Heartland Bank	20	20	21	19	30	17	20	18
Kiwibank	31	32	32	36	32	55	44	41
SBS	13	11	10	11	8	10	11	10
TSB	13	12	9	5	13	7	10	3
The Co-operative Bank	4	5	4	-1	3	4	5	-3
Westpac	249	219	305	373	290	331	307	219
Total	1,452	1,512	1,614	1,744	1,728	1,773	1,771	1,542

Major banks – Quarterly analysis

Profitability measures

Entity[20]	30 Jun 21	30 Sep 21	31 Dec 21	31 Mar 22	30 Jun 22	30 Sep 22	31 Dec 22	31 Mar 23
Interest margin (%)								
ANZ	2.10	2.00	2.00	2.10	2.20	2.30	2.40	2.40
ASB	2.00	2.00	2.10	2.10	2.20	2.50	2.50	2.50
bnz	2.00	2.00	2.00	2.10	2.20	2.40	2.50	2.40
Heartland Bank	4.90	4.80	4.50	4.30	4.60	4.10	4.20	4.10
Kiwibank	2.10	2.10	2.00	2.10	2.30	2.40	2.50	2.50
sbs	2.90	2.80	2.70	2.60	2.60	2.60	2.70	2.50
TSB	1.80	1.80	1.90	1.90	2.10	2.10	2.20	2.10
The Co-operative Bank	2.40	2.30	2.20	2.30	2.50	2.70	2.60	2.60
Westpac	2.00	1.90	2.00	2.00	2.10	2.20	2.30	2.30
Non-interest income/Total assets (%)								
ANZ	0.40	0.53	0.54	0.65	0.71	0.43	0.21	0.26
ASB	0.55	0.67	0.48	0.53	0.55	0.51	0.41	0.28
bnz	0.50	0.66	0.61	0.51	0.53	0.39	0.41	0.49
Heartland Bank	0.39	0.39	0.33	0.29	0.45	0.18	0.35	0.15
Kiwibank	0.15	0.22	0.19	0.09	0.32	0.45	0.14	-0.10
sbs	0.74	0.71	0.66	0.49	0.83	0.85	0.59	0.52
TSB	0.22	0.28	0.19	0.21	0.67	0.37	0.25	0.25
The Co-operative Bank	0.62	0.65	0.57	0.60	0.43	0.53	0.55	-0.28
Westpac	0.33	0.42	0.40	0.65	0.64	0.51	0.16	0.22
Average	0.43	0.54	0.49	0.56	0.61	0.45	0.28	0.28

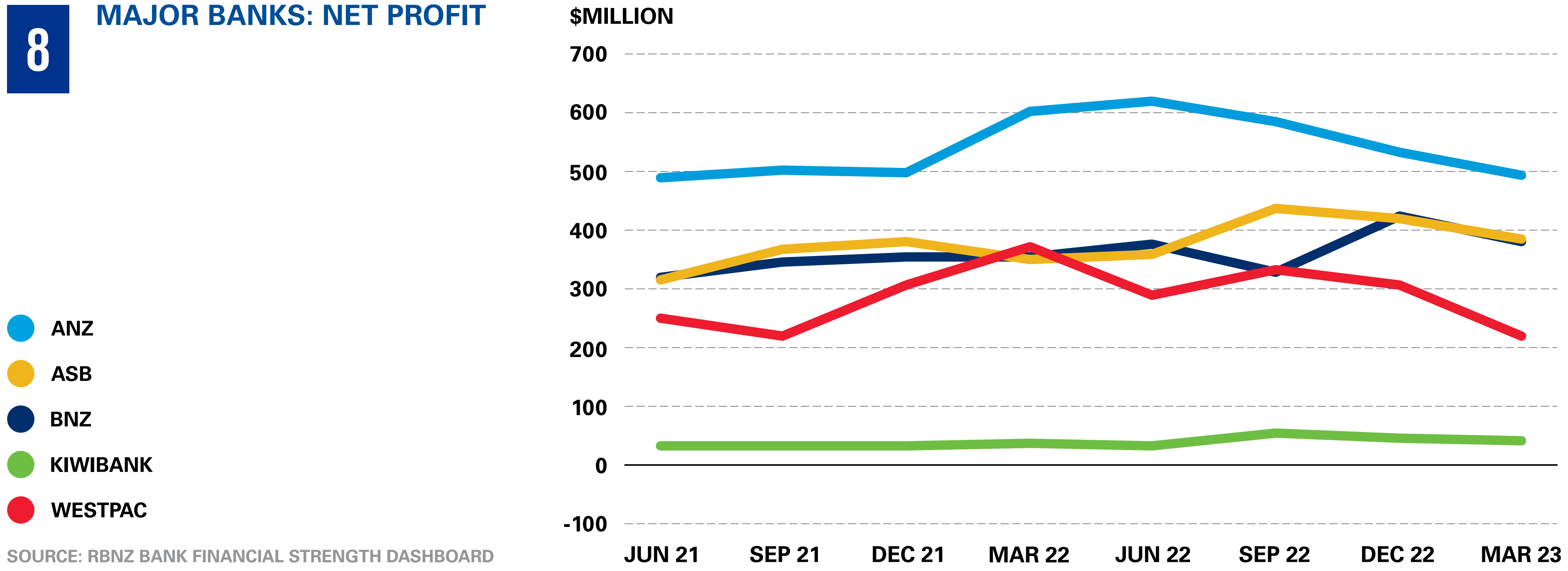
Entity[20]	30 Jun 21	30 Sep 21	31 Dec 21	31 Mar 22	30 Jun 22	30 Sep 22	31 Dec 22	31 Mar 23
Impaired asset expense/Average gross loans and advances (%)								
ANZ	-0.10	-0.03	-0.03	-0.03	0.03	0.13	0.06	0.27
ASB	-0.07	-0.04	-0.02	0.06	0.14	0.00	0.18	0.04
bnz	-0.06	-0.07	-0.03	0.14	0.00	0.26	-0.01	0.25
Heartland Bank	0.54	0.46	0.40	0.36	-0.37	0.37	0.42	0.55
Kiwibank	-0.31	0.05	0.06	0.02	0.11	0.03	0.14	0.12
sbs	0.06	0.28	0.22	0.03	0.31	0.24	0.22	0.30
TSB	-0.12	-0.31	-0.04	-0.02	-0.05	-0.09	-0.17	-0.17
The Co-operative Bank	0.06	-0.06	0.01	0.00	0.03	0.07	0.04	0.06
Westpac	0.04	0.02	-0.09	0.03	-0.02	-0.03	0.11	0.52
Average	-0.06	-0.02	-0.03	0.04	0.04	0.09	0.09	0.25
Operating expenses/Operating income (%)								
ANZ	38.88	39.25	39.19	32.19	32.76	32.08	35.26	33.70
ASB	44.62	37.77	32.43	37.51	38.03	34.68	31.42	36.62
bnz	38.23	39.02	35.31	29.70	34.67	37.28	33.80	31.88
Heartland Bank	42.93	42.53	43.40	42.00	39.29	48.91	43.98	43.66
Kiwibank	84.38	70.88	70.67	68.78	71.77	62.10	64.82	65.27
sbs	56.21	57.51	62.23	59.74	64.46	61.48	61.28	61.11
TSB	65.02	74.84	74.23	85.71	68.63	88.55	80.37	83.37
The Co-operative Bank	71.86	72.41	72.65	105.26	79.91	76.68	73.44	120.65
Westpac	44.98	49.95	41.15	38.40	43.00	40.05	41.29	43.26
Average	43.97	43.07	39.69	37.10	39.03	38.15	37.93	38.71

Major banks – Quarterly analysis

Q1 23 Q1 22 Q1 21 Q1 20

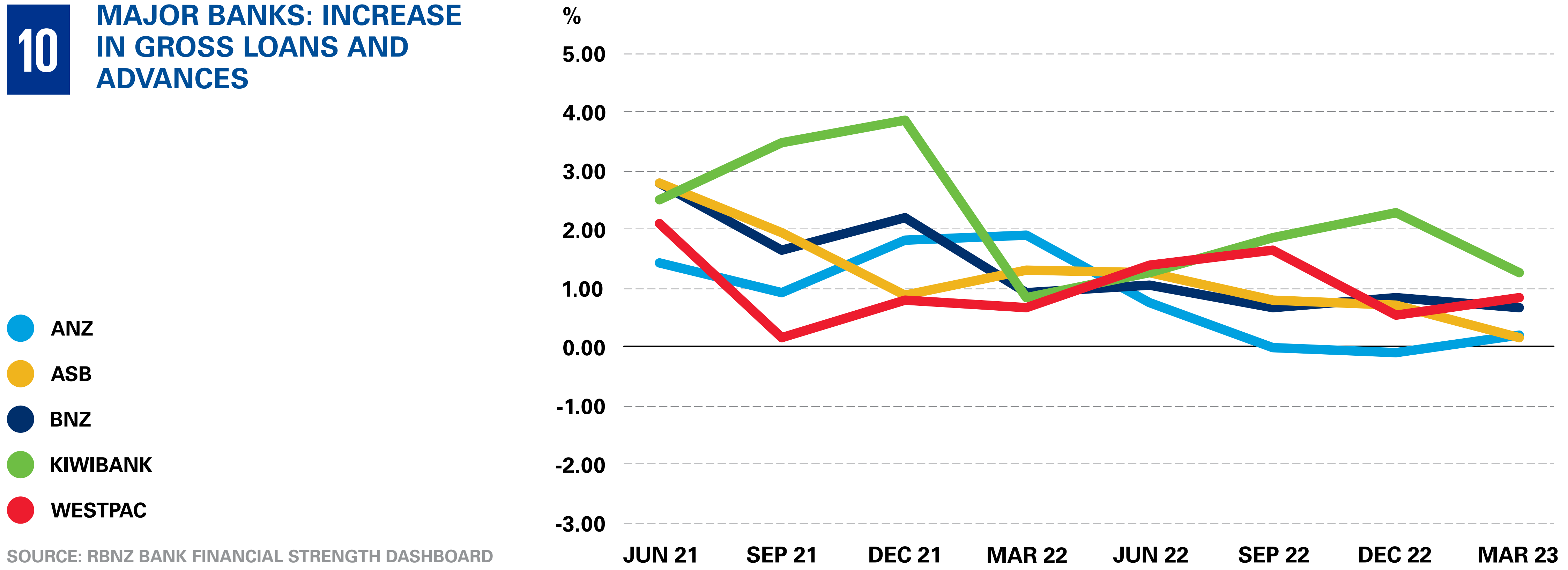
HOVER over the button to see the results for each quarter

8 **MAJOR BANKS: NET PROFIT**



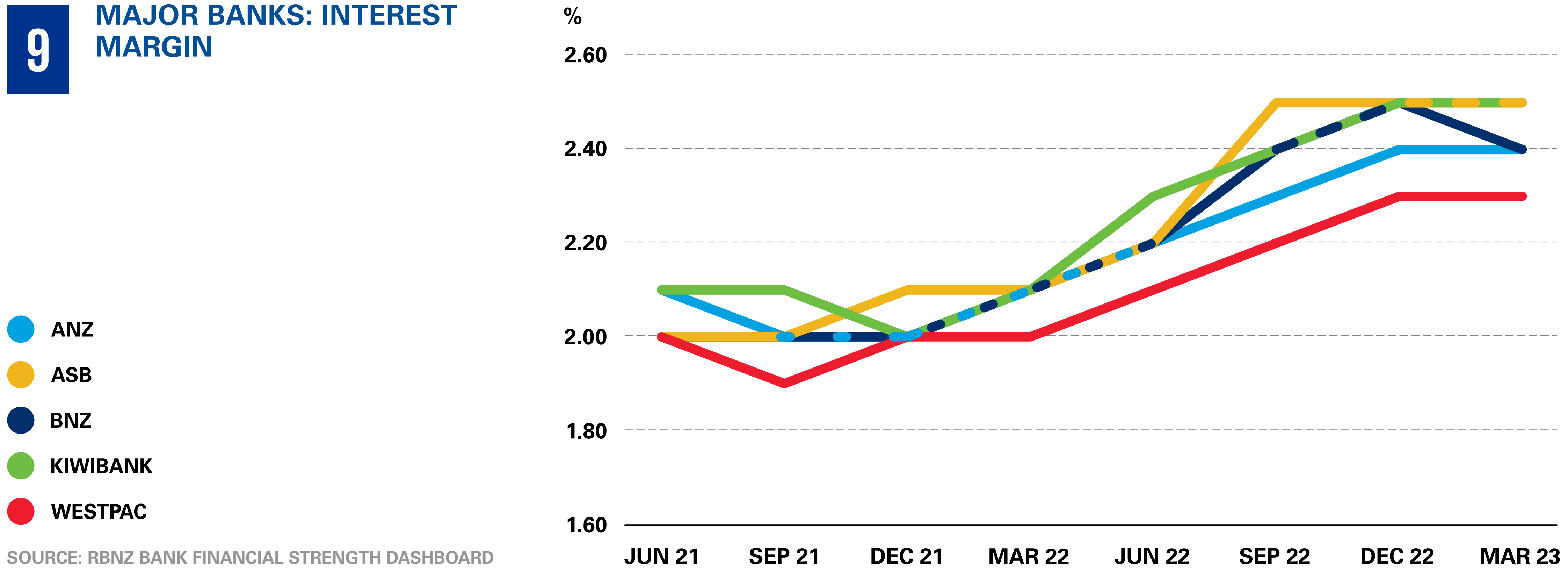
SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

10 **MAJOR BANKS: INCREASE IN GROSS LOANS AND ADVANCES**



SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

9 **MAJOR BANKS: INTEREST MARGIN**



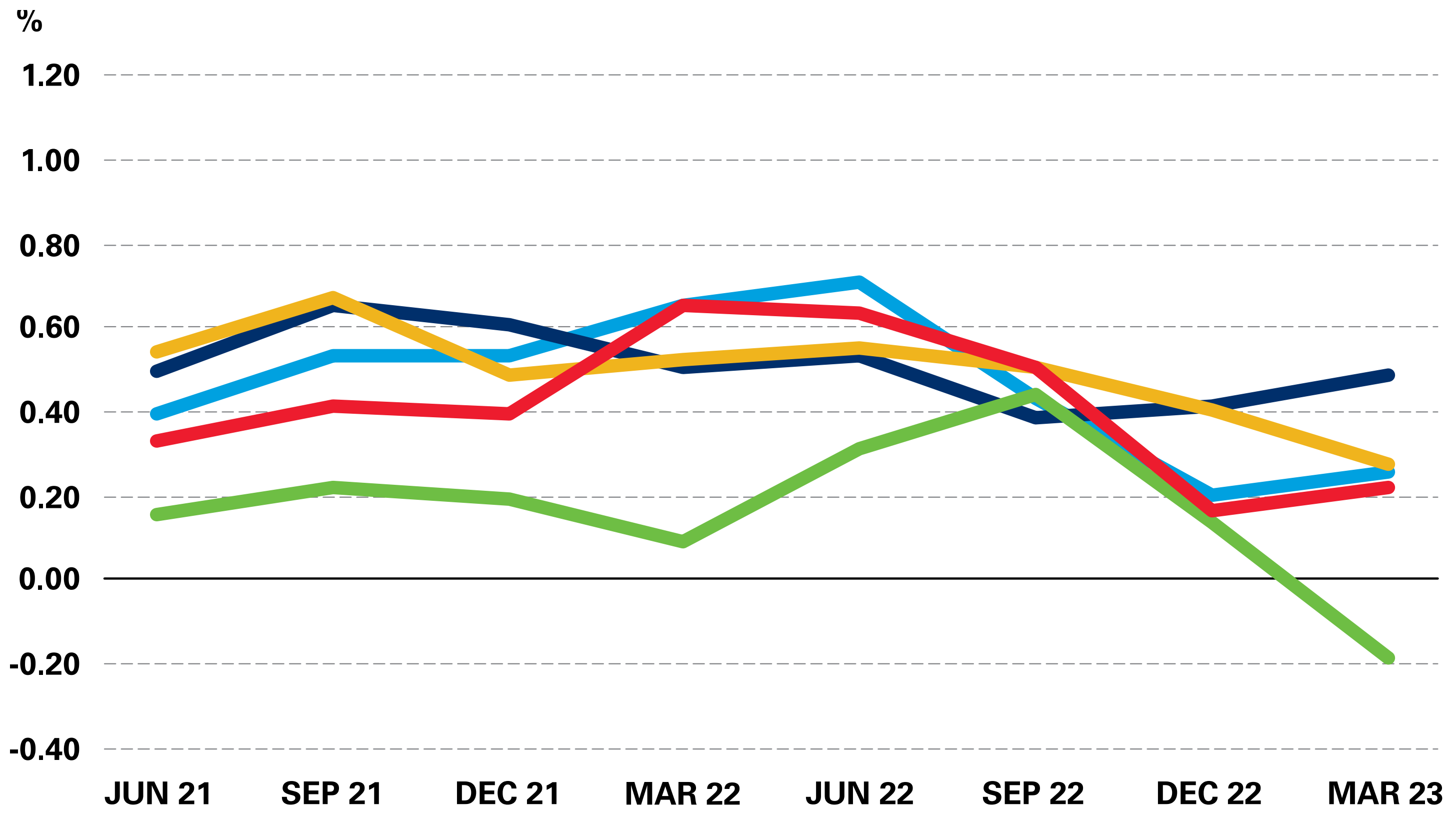
SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

Major banks – Quarterly analysis

Q1 23 | Q1 22 | Q1 21 | Q1 20

HOVER over the button to see the results for each quarter

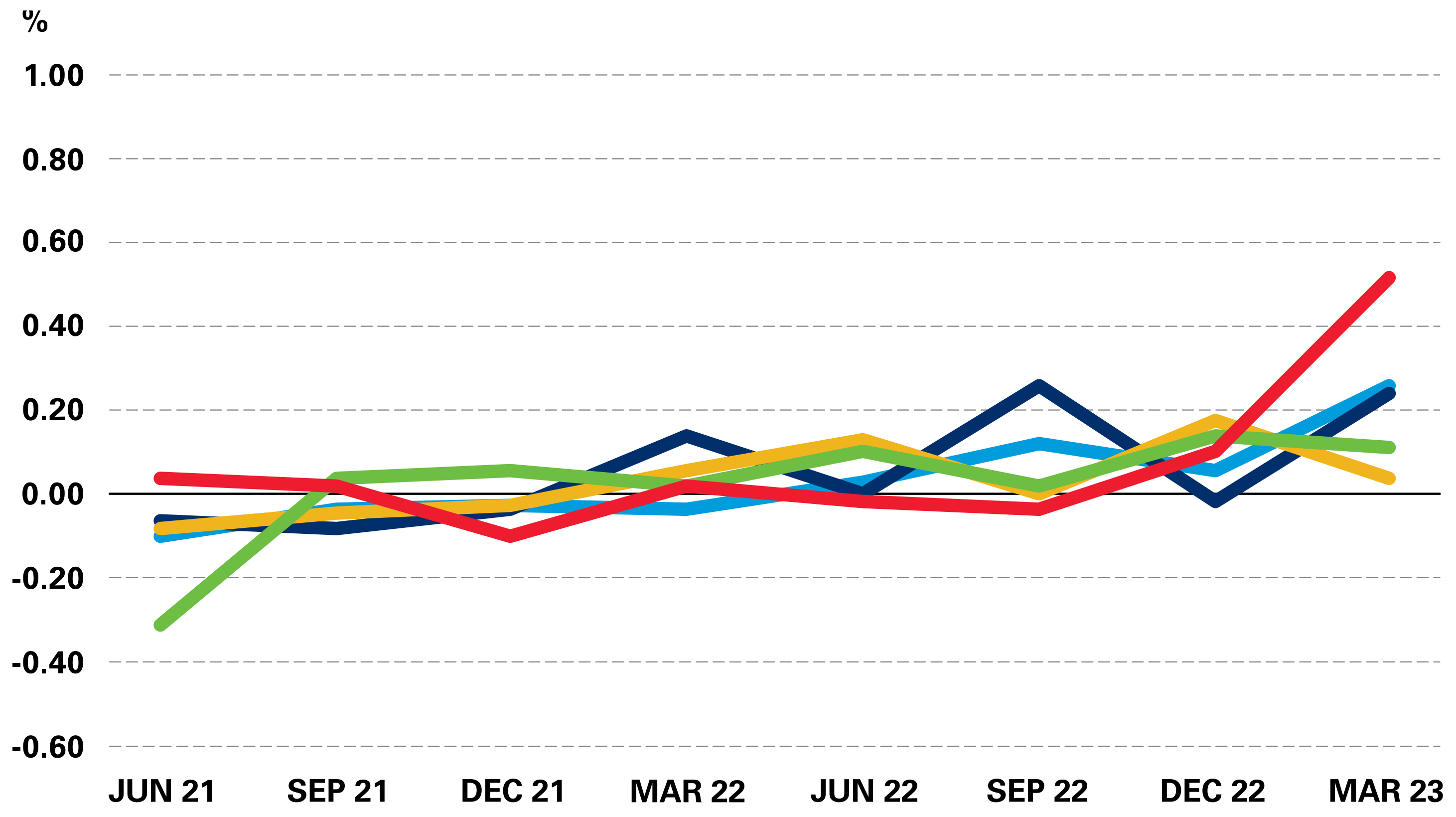
11 MAJOR BANKS: NON-INTEREST INCOME/ TOTAL ASSETS



- ANZ
- ASB
- BNZ
- KIWIBANK
- WESTPAC

SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

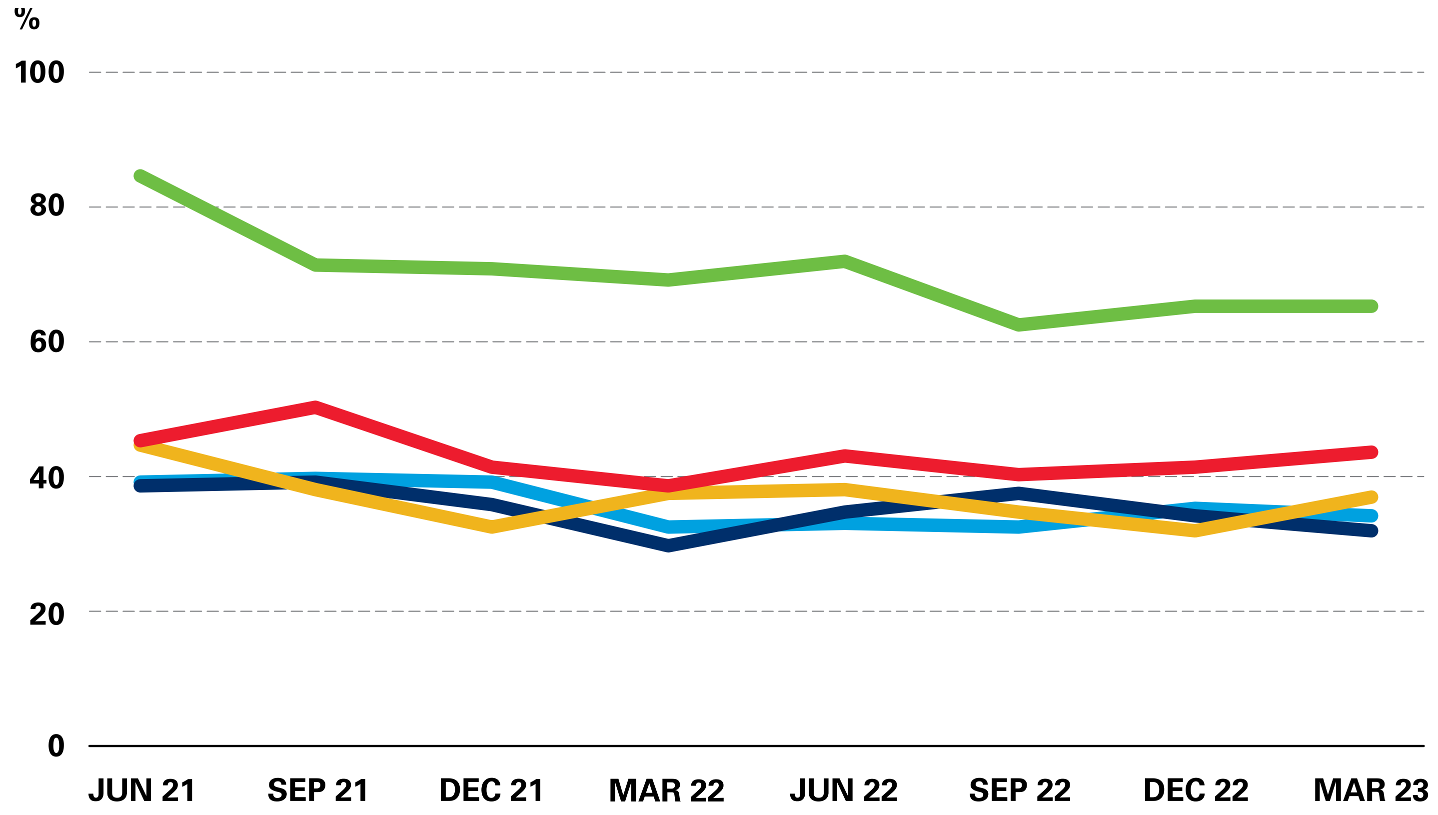
13 MAJOR BANKS: IMPAIRED ASSET EXPENSE/AVERAGE GROSS LOANS AND ADVANCES



- ANZ
- ASB
- BNZ
- KIWIBANK
- WESTPAC

SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

12 MAJOR BANKS: OPERATING EXPENSES/ OPERATING INCOME

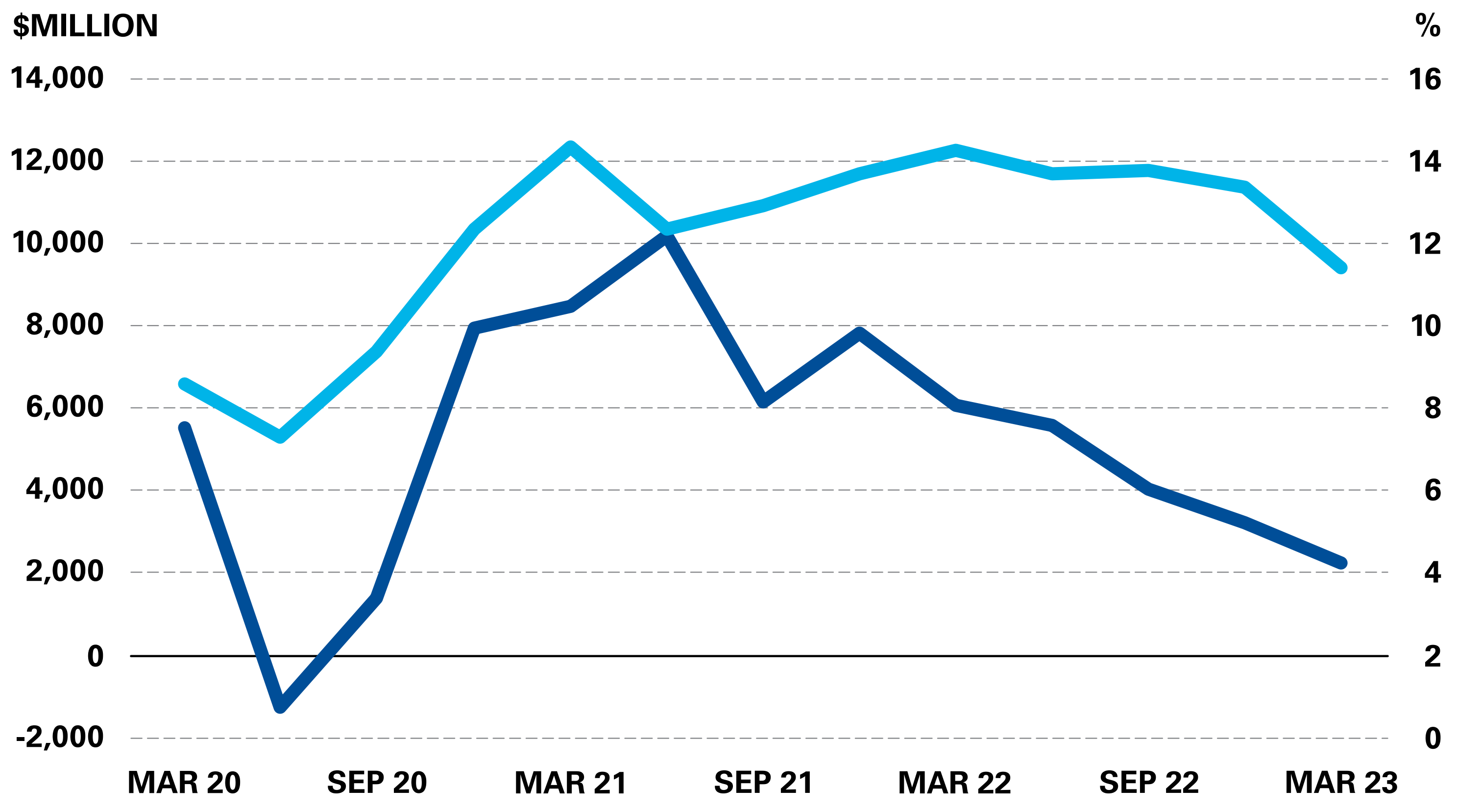


- ANZ
- ASB
- BNZ
- KIWIBANK
- WESTPAC

SOURCE: RBNZ BANK FINANCIAL STRENGTH DASHBOARD

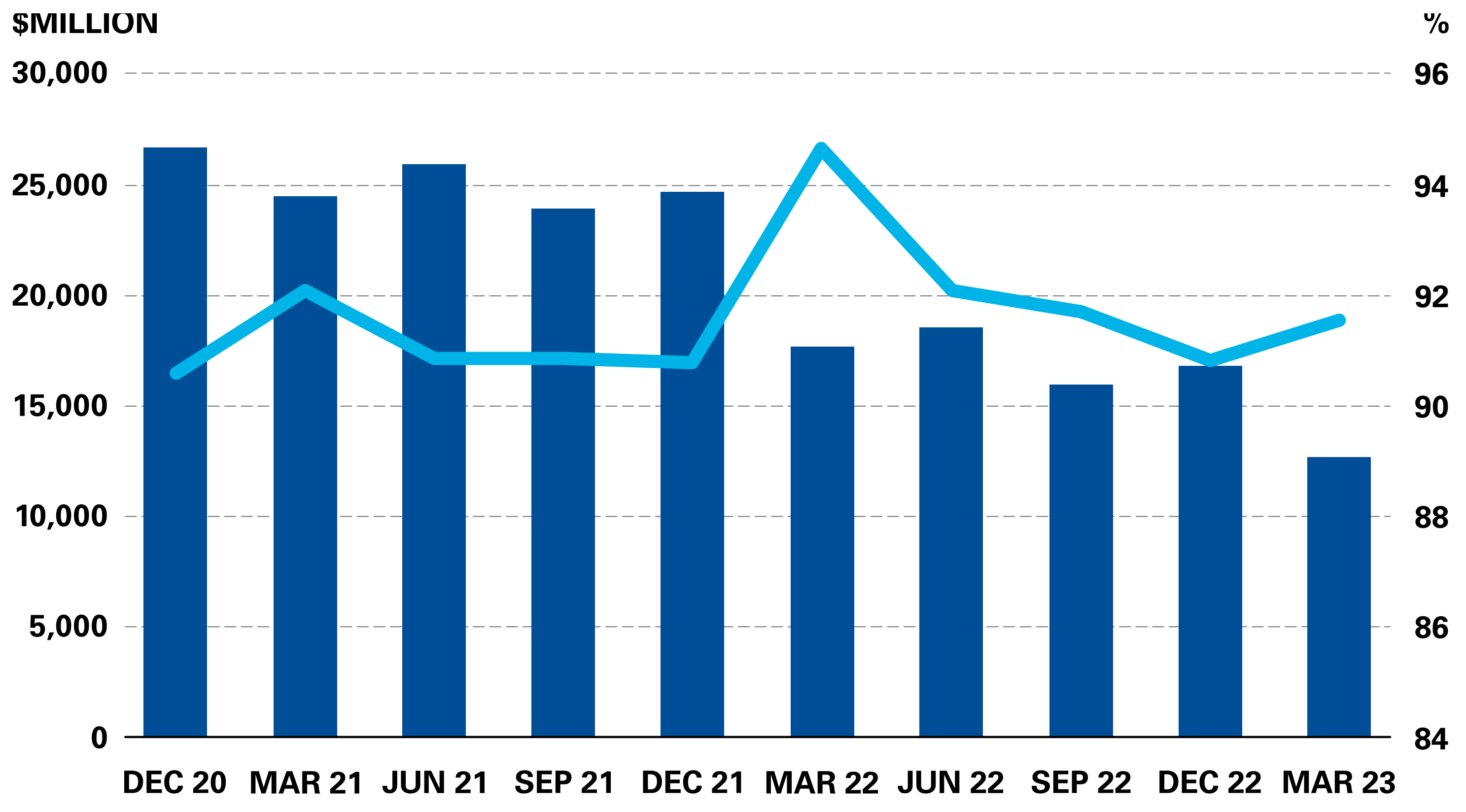
Quarterly analysis

14 GROWTH IN GROSS LOANS AND ADVANCES VS. RETURN ON EQUITY



GROWTH IN GROSS LOANS AND ADVANCES (LHS)
RETURN ON EQUITY (RHS)

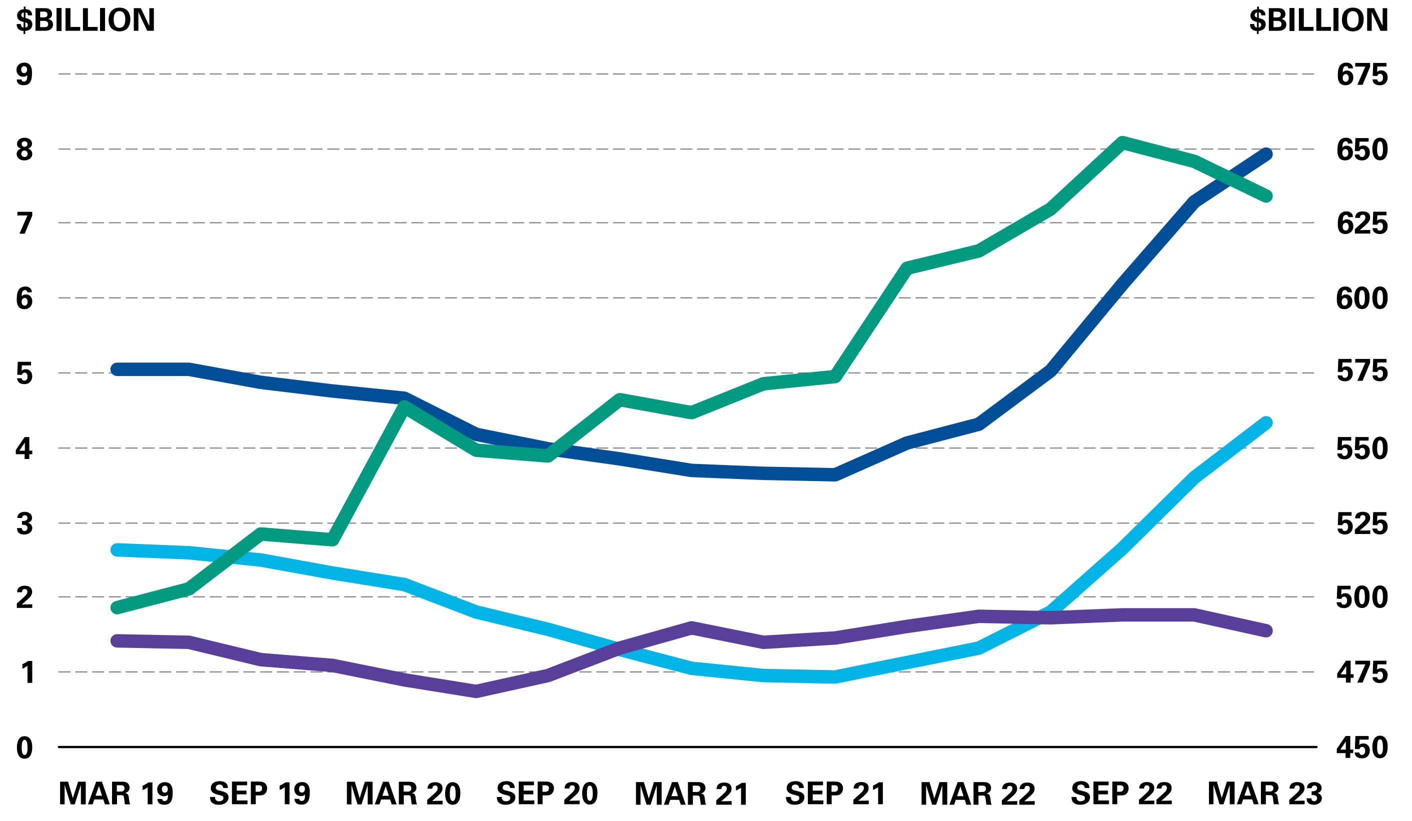
16 LVR ANALYSIS OF RESIDENTIAL MORTGAGES



NEW MORTGAGES (LHS)
PROPORTION OF NEW MORTGAGES WITH LVR OF 80% OR BELOW (RHS)

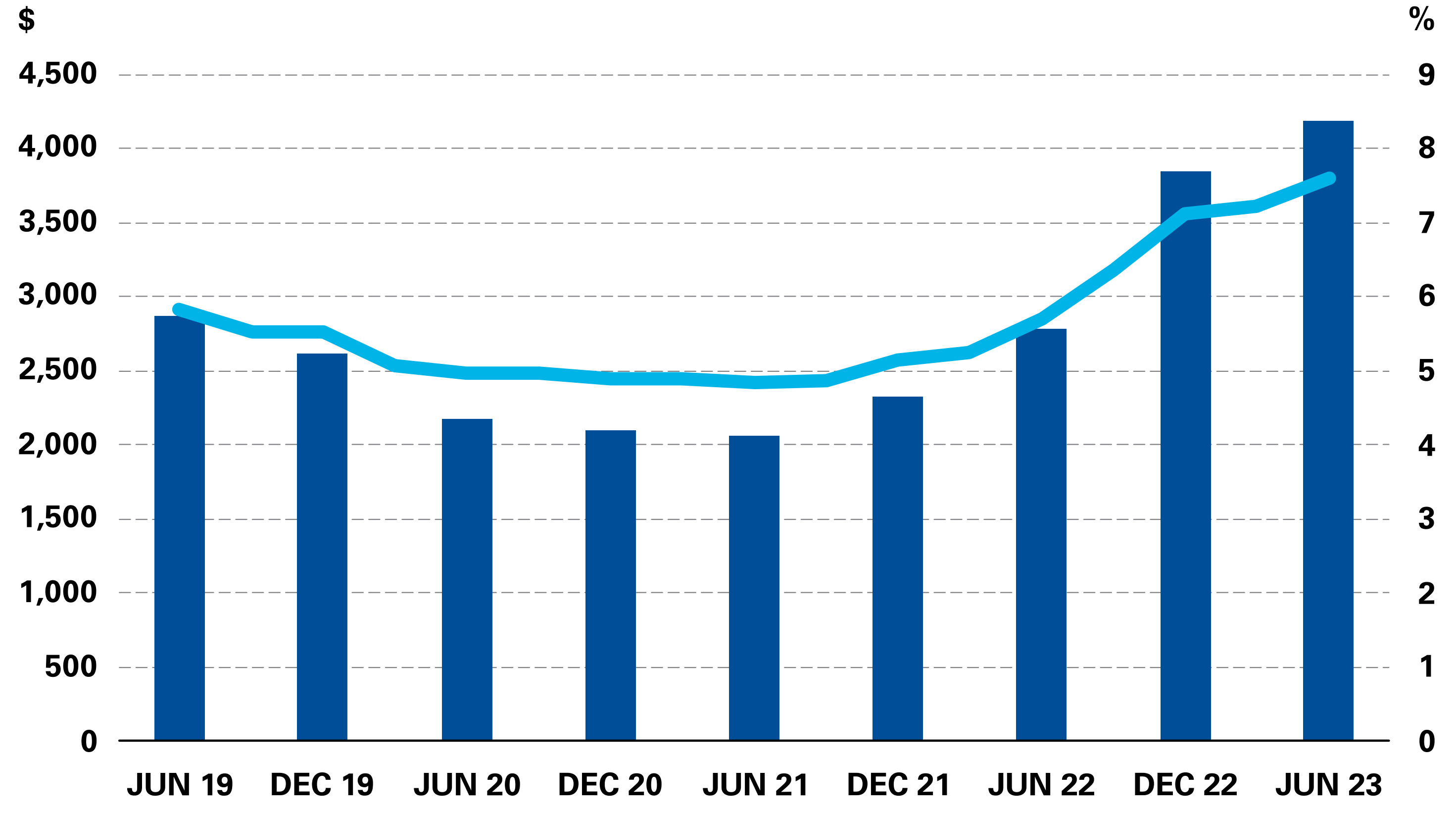
SOURCE: RESERVE BANK OF NEW ZEALAND STATISTICS

15 MAJOR BANKS: INTEREST EARNING ASSETS COMPARED TO INTEREST INCOME AND EXPENSE



INTEREST INCOME (LHS)
INTEREST EXPENSE (LHS)
NET PROFIT (LHS)
TOTAL ASSETS (RHS)

17 MONTHLY MORTGAGE REPAYMENTS BASED UPON AVERAGE BANK FLOATING MORTGAGE INTEREST RATES ON A 30-YEAR $500,000 MORTGAGE



MONTHLY MORTGAGE REPAYMENTS (LHS)
AVERAGE BANK FLOATING MORTGAGE INTEREST RATE (%) (RHS)

SOURCE: INTEREST.CO.NZ

Peak interest rates and the long road ahead

> Around a third of households have a home loan, the sharp rise in the cost of borrowing will have a huge impact.

Roger Beaumont
Chief Executive
New Zealand Banking Association

New Zealand Banking Association
Te Rangapū Pēke

The New Zealand Banking Association – Te Rangapū Pēke (NZBA) is the voice of the banking industry. Roger leads NZBA's commitment to support a strong and stable banking system that benefits New Zealand households, businesses and the economy.

Roger joined NZBA in January 2019. Prior to this role, Roger spent seven years in executive leadership roles in the banking industry in New Zealand and Australia. The earlier part of his career was pre-dominantly in the broadcast and digital media industry.

With interest rates rising sharply to combat inflation and the cost of living, combined with severe flooding and cyclone damage in the North Island, the first half of 2023 has been eventful to say the least. While some commentators are saying the cost of borrowing appears to have peaked, what lies in store for consumers in the second half of the year, and how are banks helping?

In October 2021 the Official Cash Rate (OCR) started rising from its historic low of 0.25% to its current setting at 5.5%, with a sharp increase of 3.5% over the last year. The Reserve Bank of New Zealand (RBNZ) meant to make an impact on inflation by targeting consumption and there are signs it has done exactly that. The tricky part is getting the balance right – not going too hard or too soft. Initially RBNZ was aiming for a shallow recession to slow down spending and rein in inflation. At the recent Budget, the Treasury announced that it no longer saw New Zealand heading into a recession, with growth of 1% forecast for the next 12 months. That's good news from a macro-economic perspective.

That doesn't mean households are having an easy time. If you consider around a third of households have a home loan, the sharp rise in the cost of borrowing will have a huge impact. And because New Zealanders generally prefer fixed interest rate mortgages to floating interest loans, RBNZ's efforts to dampen demand in the economy might take a while to filter through. While the OCR may have peaked at 5.5%, the question now is how long it will stay there? RBNZ has indicated that it will stay at the current level for the 'foreseeable future'. Some commentators see it staying at the current peak for at least a year before slowly starting to taper down. That makes sense because it will take some time for the full impact of the raised OCR to take effect. It's fair to say there's likely more mortgage pain to come, especially when

you consider around half of fixed interest rate mortgages will come up for renewal within the next year.

Our six-monthly data insights to December 2022 show that many people with home loans had prepared well for the current financial storm. At that stage 45% of home loan customers were ahead on their loan repayments. They likely retained their repayments at the same as they had been before interest rates hit historic lows, which helped repay their loans faster and save on the overall cost of the loan. It also meant that nearly half of the people with home loans had built in a buffer that effectively cushioned the impact of higher interest rates, which we're now seeing. It was a double win for them.

As well as mortgagors helping themselves, banks have been there to support customers doing it tough. Banks will work with customers experiencing financial difficulty to find a way through on a case-by-case basis. Depending on the circumstances involved, options may include temporarily moving to interest-only repayments or restructuring the loan over a longer term to reduce regular repayment amounts.

In addition to helping customers through the current economic conditions, banks have also shown they can step up in an emergency. When the floods and cyclone hit the North Island, the banks responded quickly as events unfolded, making $1.4 billion available in low-cost lending, and donating $6.5 million to disaster relief funds. They also provided loan repayment relief and access to term deposits without penalties, and worked with RBNZ to get cash to impacted areas.

The banks know that they also have a part to play in helping communities recover over the longer term following the devastating impact of these events. Banks will work constructively with the government, insurers, and other parties to help get affected customers back on track.

New Zealanders are well served by their banks, and that will continue to be the case as we navigate the current economic headwinds. Our banks are well capitalised and regulated, and profitable. That helps make them resilient, which is important at times like this.

Banks also contribute their fair share to New Zealand. Last year banks made a net profit of $7.18 billion. They also spent $9.1 billion running their businesses and paying taxes here. That's a net positive contribution of $1.92 billion – before you take into account the contribution banks make in funding household and business needs, to the tune of around $540 billion.

While interest rates may have peaked, we'll be living with a higher cost of borrowing for some time yet. The good news is that many mortgage holders prepared well for the current economic environment, and our resilient banks are also there to help customers through these challenges.

“New Zealanders are well served by their banks, and that will continue to be the case as we navigate the current economic headwinds.

Bad debt – Could increased borrowing spell trouble for bank profits?

Keith McLaughlin
Managing Director,
Centrix Group Limited

CENTRIX
Credit Bureau of New Zealand

Keith McLaughlin is the Managing Director of Centrix Group Limited, New Zealand's only locally owned credit bureau. A highly experienced senior executive and director, Keith started Centrix with a vision to offer New Zealand businesses a superior and cost-efficient credit offering, with a focus on long-term relationships. Previously the founder and Managing Director of Baycorp Holdings Limited, his strengths include strong leadership skills with an emphasis on empowerment, and a proven ability to forge and sustain high performance teams.

In 2022, we saw bank profits hold near-record high levels. In the three months ended December 2022, industry profits were 9.7% higher than the same period a year before. Collective industry profits for the year ended December 2022 were a record $7.2 billion.

Despite this, many economists and financial commentators have said the strong performance of the banking sector in 2022 may have peaked, with banking sector net profits anticipated to slow as Kiwi households swing into more borrowing to get through the current economic climate.

Increases in credit impairment – or bad debt expense – can be attributed to the financial impacts of the severe weather events and the weaker economic outlook, including things like the recession and the rising cost of living, squeezing household cash flows.

For example, in May 2023 ANZ posted their half-year results (for the six months ended 31 March 2023) with net profit down 9% compared to the same period last year. Furthermore, Westpac reported net profits down 33% down compared to last year, with both organisations reporting an increase in bad debt provisions.

In the first four months of 2023, credit arrears have climbed as the reality of the current financial situation puts more pressure on Kiwi households meeting their repayment obligations.

Delinquencies by the numbers

Looking at the data, we can start to see some trends emerging.

18 – 21 See Figures 18–21 – page 21

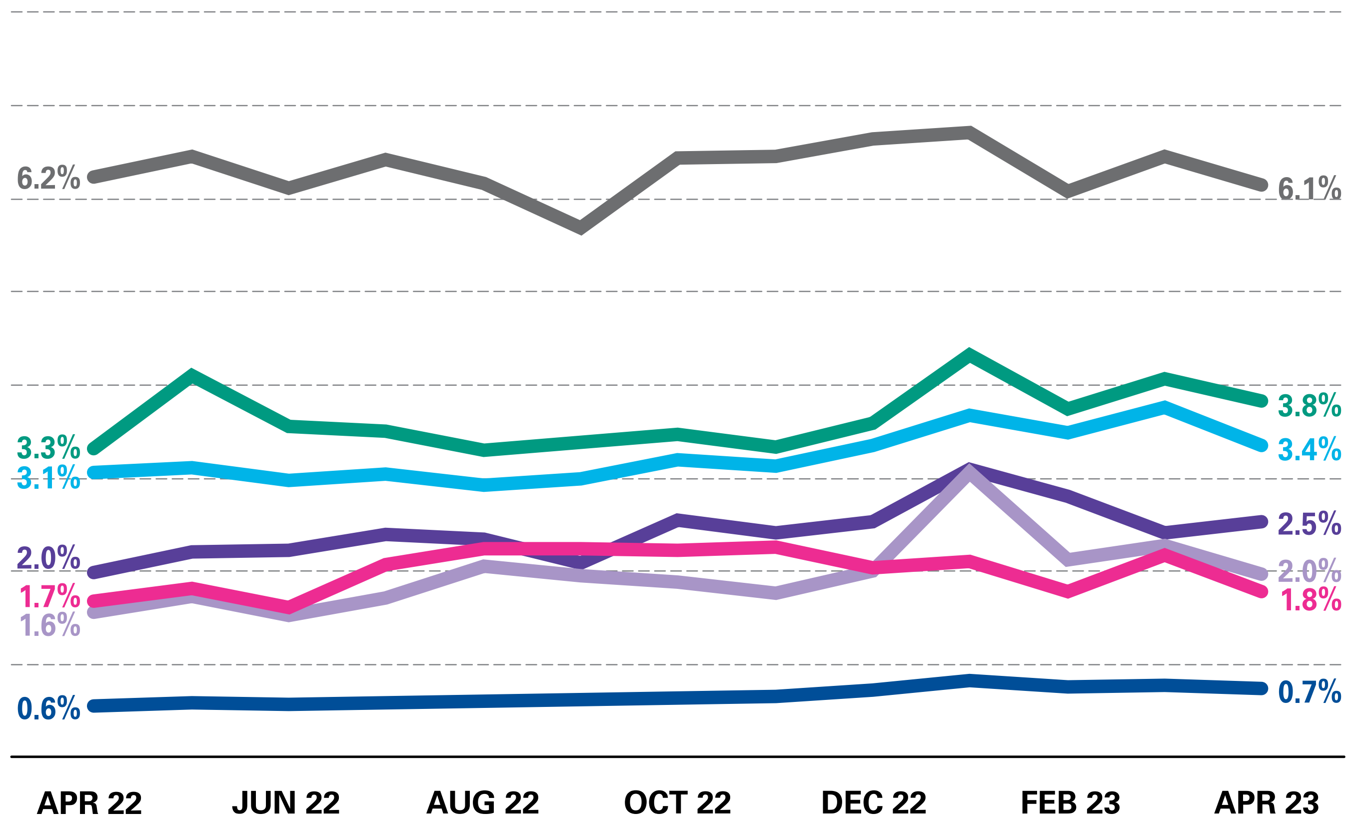
Year-on-year, the percentage of personal loans overdue by 30 – 59 days rose from 1.4% of accounts in April 2022 to 1.9% in April 2023.

“In the first four months of 2023, credit arrears have climbed as the reality of the current financial situation puts more pressure on Kiwi households meeting their repayment obligations.

18 1 – 29 DAYS DELINQUENCIES

- MORTGAGES
- CREDIT CARDS
- AUTO LOANS
- PERSONAL LOANS
- BNPL
- TELCO
- UTILITIES

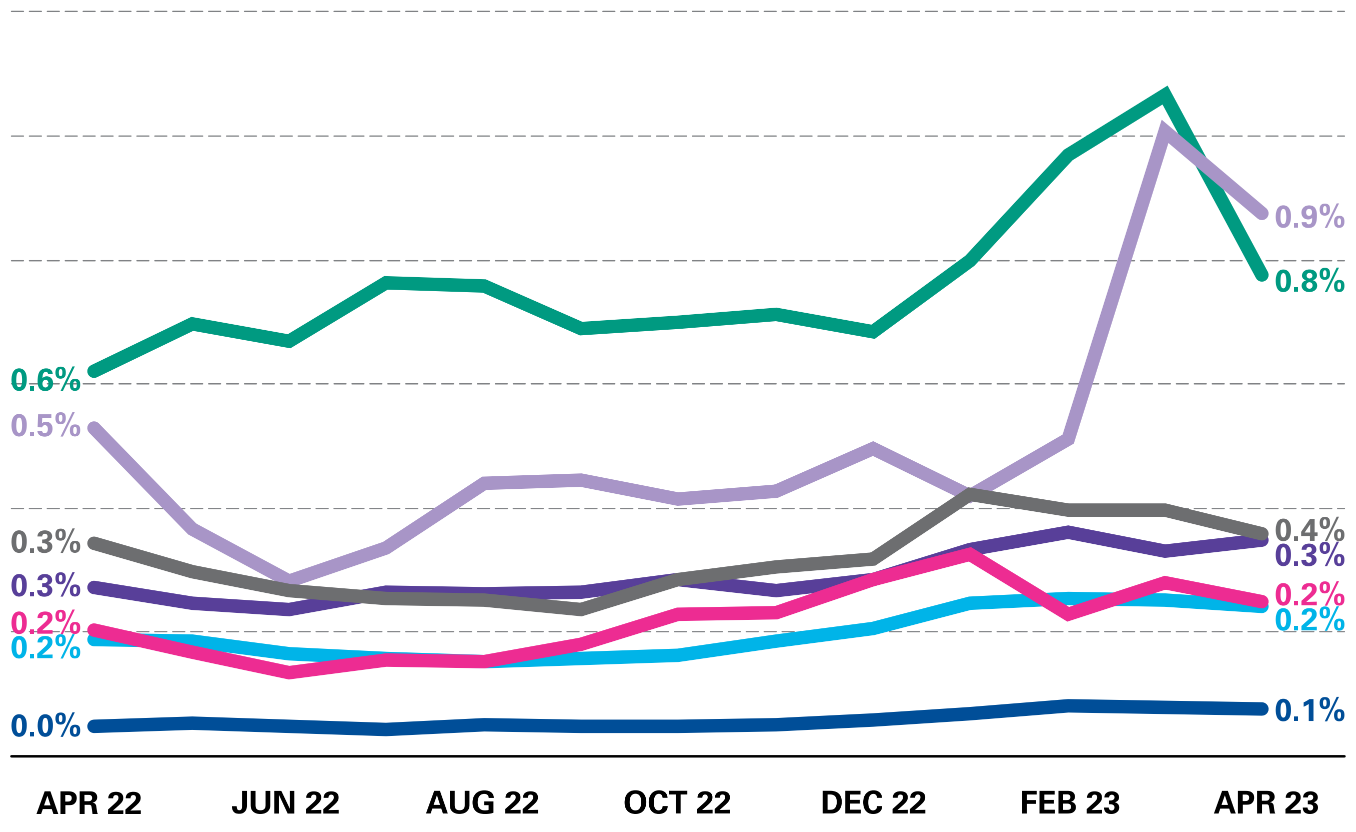
SOURCE: CENTRIX



20 60 – 89 DAYS DELINQUENCIES

- MORTGAGES
- CREDIT CARDS
- AUTO LOANS
- PERSONAL LOANS
- BNPL
- TELCO
- UTILITIES

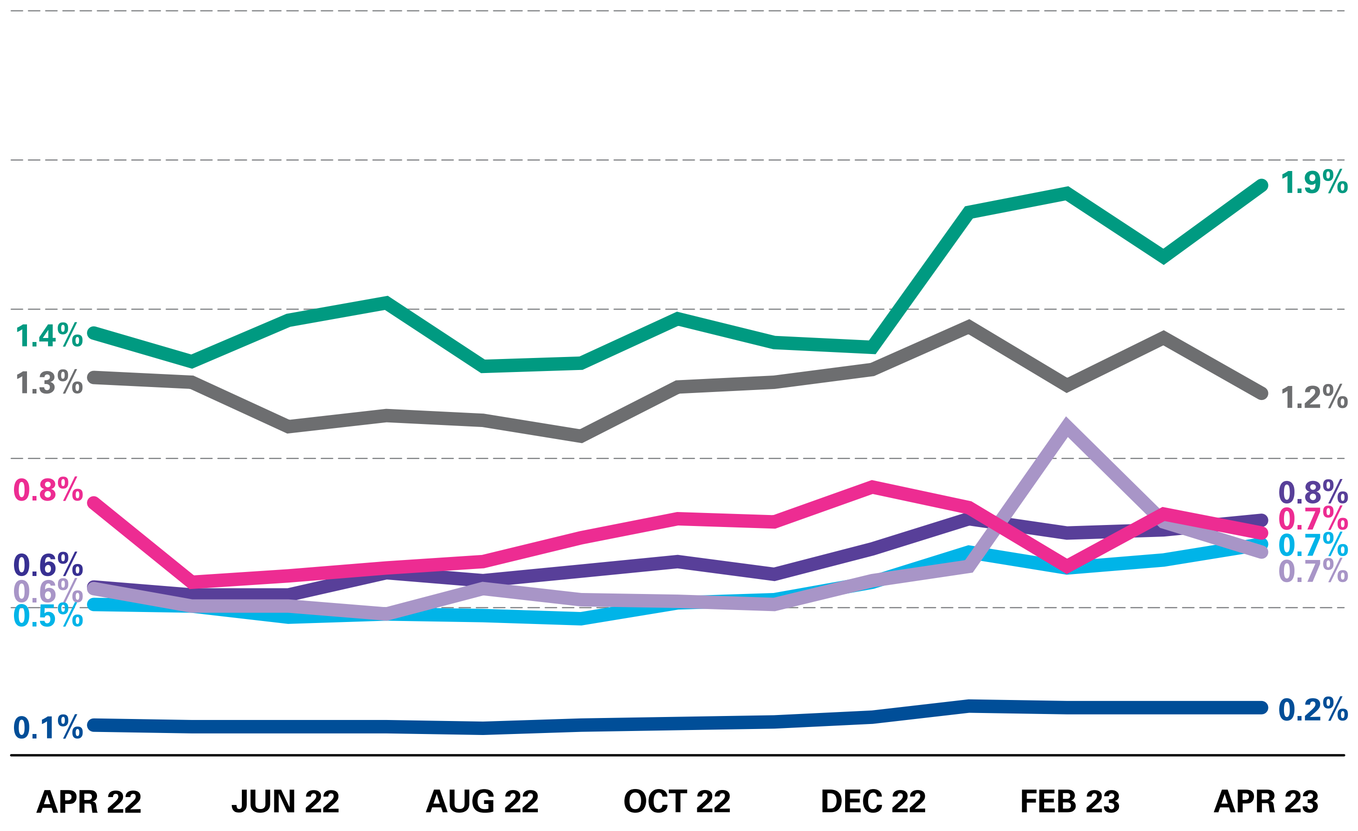
SOURCE: CENTRIX



19 30 – 59 DAYS DELINQUENCIES

- MORTGAGES
- CREDIT CARDS
- AUTO LOANS
- PERSONAL LOANS
- BNPL
- TELCO
- UTILITIES

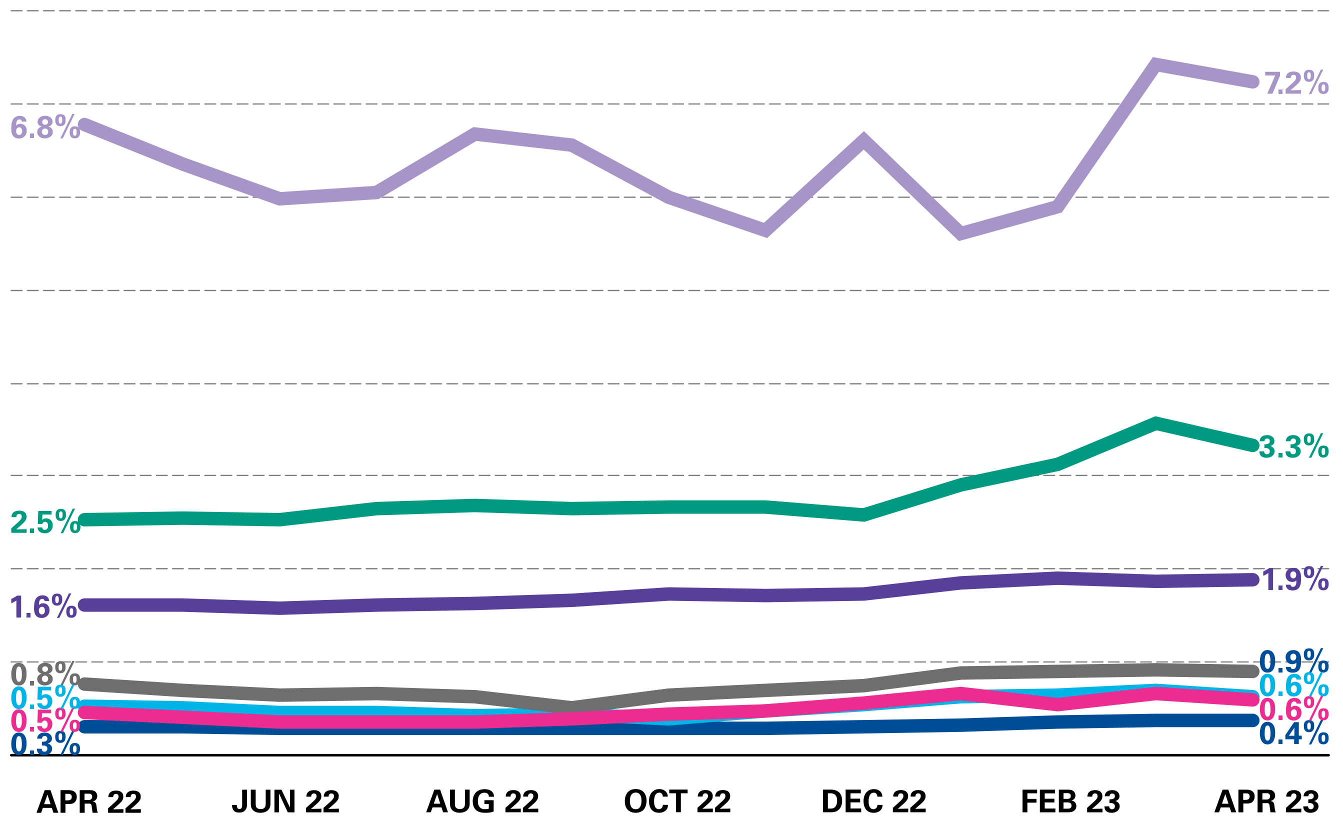
SOURCE: CENTRIX



21 60+ DAYS DELINQUENCIES

- MORTGAGES
- CREDIT CARDS
- AUTO LOANS
- PERSONAL LOANS
- BNPL
- TELCO
- UTILITIES

SOURCE: CENTRIX



“This upswing began in January 2023 and has been steadily climbing throughout the year, dipping slightly in April 2023 – a trend which can be attributed to the overall financial challenges facing many Kiwi households at the moment.

Furthermore, personal loan delinquencies over 60+ days climbed from 2.5% in April 2022 to 3.3% in April 2023, and the percentage of personal loans with 90+ days delinquencies climbed from 1.9% in April 2022 up to 2.6% in April 2023.

22 See Figure 22 – page 23

This upswing began in January 2023 and has been steadily climbing throughout the year, dipping slightly in April 2023 – a trend which can be attributed to the overall financial challenges facing many Kiwi households at the moment.

Furthermore, Buy Now, Pay Later (BNPL) product delinquencies have also climbed. While arrears for these products remain below personal loan arrears in the short term (1 – 29 days, 30 – 59 days), we very quickly see an upswing in delinquencies as the period of time for missed payments grow.

Year-on-year, 60+ days delinquencies climbed from 6.8% of BNPL accounts in April 2022 to 7.2% of accounts in April 2023. Ninety plus days delinquencies also climbed slightly from 6.3% in April 2022 to 6.4% in April 2023.

Short-term delinquencies (1 – 29 days) for auto loans have climbed year-on-year as well, up from 2.0% in April 2022 to 2.5% in April 2023.

However, the longer-term delinquencies remained relatively stable, which could indicate that people are prioritising getting these particular repayments organised in lieu of the smaller, more discretionary lending.

Additionally, credit card delinquencies have followed a similar pattern. While 1 – 29 days delinquencies have climbed slightly (3.1% in April 2022 compared to 3.4% in April 2023), longer-term delinquencies have remained low and steady throughout 2022 and into 2023 thus far.

It is encouraging to see long-term delinquencies for mortgages and utilities remain relatively stable since April 2022.

However, there is a creep beginning for mortgage delinquencies when we look at the year-on-year growth. For example, 1 – 29 days delinquencies have risen 33%, while 90+ days delinquencies are up 19%.

23 See Figure 23 – page 23

What’s in store for the remainder of 2023?

In May, the Reserve Bank of New Zealand (RBNZ) increased the Official Cash Rate (OCR) another 25 basis points, reaching the forecast 5.50%, with many believing this will be the level the RBNZ holds the OCR at for the remainder of the year in order to rein in inflation and avoid a recession.

This begs the question – how will Kiwi households manage the remainder of 2023 with the cost of living and interest rates set by this new benchmark?

Many have seen new interest rates push their mortgage repayments up by hundreds – if not thousands – of dollars a month, while budgets remain stretched thin. This in turn could cause issues for banks in the medium-to-long term, especially if delinquencies continue to slowly climb and Kiwi households begin defaulting on their repayments.

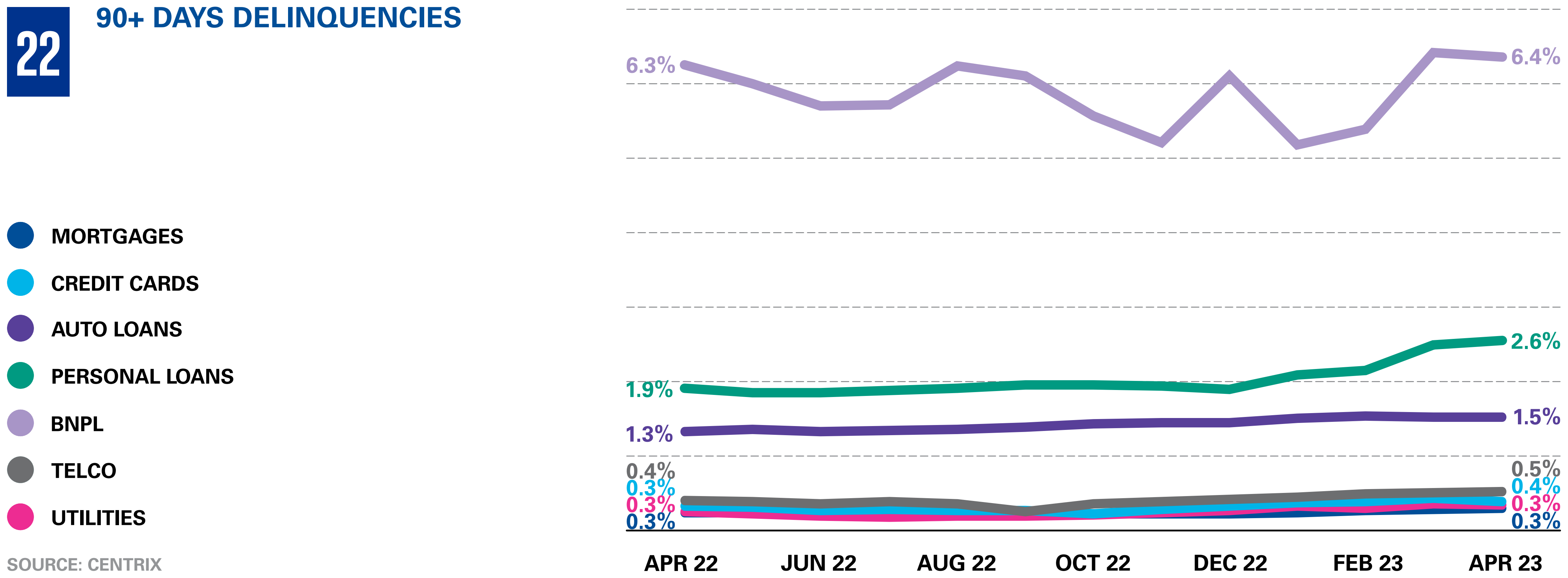
“A rise in bad debt spurred on by the challenging economic climate could see an overall increase in the number of defaults and written off debts.

A rise in bad debt spurred on by the challenging economic climate could see an overall increase in the number of defaults and written off debts.

If the OCR remains steady, the economic stage for the remainder of 2023 has been set. Only time will tell if households begin adapting to this new normal and what this means for delinquencies – and for banking sector profits this financial year.

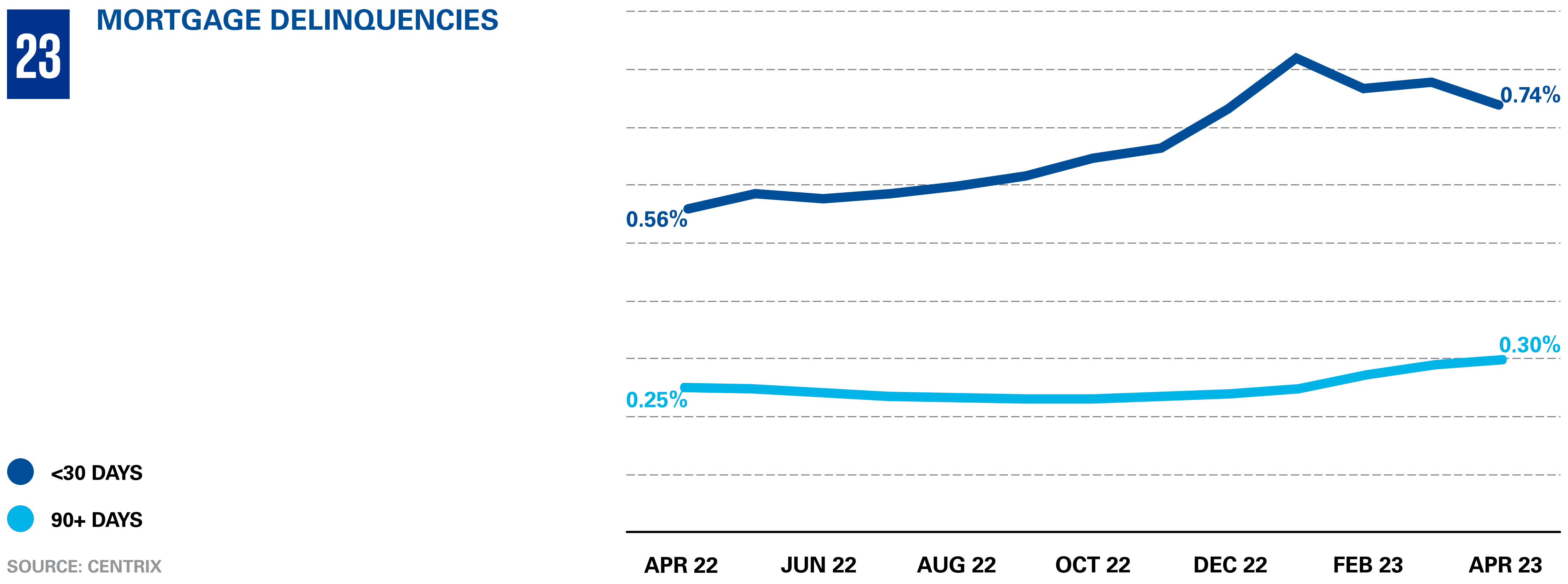
If the job market begins to suffer in greater numbers, we could be staring down the barrel of substantially increased credit impairments or bad debts in 2024.

22 90+ DAYS DELINQUENCIES



SOURCE: CENTRIX

23 MORTGAGE DELINQUENCIES



SOURCE: CENTRIX

Banks need to step up to meet new reporting challenges

Sanel Tomlinson
Principal, Impact Measurement, Assurance & Reporting
KPMG

Sanel is a Principal in KPMG's Impact team, supporting clients in navigating the various financial and broader corporate performance reporting requirements.

If you want more information on the topics discussed in this article then please reach out to Sanel.

About 200 entities in New Zealand are now busily getting ready to present their first mandatory climate financial statements. We acknowledge that several entities have already prepared voluntary reports over the last couple of years, but it is surprising that a limited number of banks feature as part of this reporting group. We look forward to seeing whether this statistic will be turned on its head as part of the 2023 reporting cycles.

One question we get asked a lot is about what is happening in the rest of the world. In this article we provide an overview of our findings in the first phase of our annual survey of 35 global banks' climate-related disclosures, including comments about progress in different parts of the world[22].

The overarching messages are simple: Banks need to step up to meet new reporting challenges; and those banks reporting their climate-related disclosures under heightened regulation are powering ahead, leaving behind those in jurisdictions with less of a climate-related regulatory focus. New Zealand is one of the forerunners when it comes to regulation of climate-related disclosures. Our survey did not include any New Zealand reports, but we will endeavour to provide a comparison as part of next year's survey if New Zealand banks step up to the challenge and provide voluntary climate statements during the 2023 reporting cycle.

Observations across jurisdictions

UK banks continue to take the lead

- In 2021, the Task Force on Climate-related Financial Disclosures (TCFD) recommendations became mandatory for UK premium listed banks on a comply or explain basis (which includes a statement in the annual report on whether or how they have complied with the TCFD recommendations). This is reflected in the nature and extent of climate-related disclosures of UK banks.

> "Banks need to step up to meet new reporting challenges; and those banks reporting their climate-related disclosures under heightened regulation are powering ahead, leaving behind those in jurisdictions with less of a climate-related regulatory focus.

- UK banks appear to be ahead in the following areas:
  – All banks included in our analysis publish climate-related disclosures (including those in other standalone reports) on the same date as their financial statements.
  – Continued progress is generally observed in climate-related disclosures made as part of 2022 annual reports – including:
    - although still limited, UK banks have started to disclose climate-related impacts within their financial statements;
    - they provided more clarity on the TCFD recommendations they have disclosed verses not disclosed (with explanations); and
    - they show continuing progress on the more challenging areas – e.g. quantification of financed emissions for certain loan portfolios, sharing insights from scenario analysis to date, and development of initial transition plans, which are already released or will be released in 2023.

Other banks continue to make progress in 2022

- Continuing progress is seen in jurisdictions with heightened regulation or where regulators have emphasised the importance of climate-related disclosures.
- Although disclosures are not (yet) at the same level as the UK banks, the banks in Australia and Europe have generally continued to make progress – e.g. some have started to disclose impacts in the financial statements.
- A few banks in Australia and Europe disclose judgemental adjustments to their expected credit losses (ECLs) due to extreme weather events or country-specific regulation.

Some banks lagging behind

Banks in jurisdictions with few or no climate-related regulations generally provide less climate-related information in their annual reports. No significant year-on-year progress is noted for such banks, with the nature and extent of disclosures being consistent with 2021.

Key findings

Our analysis also highlighted three key findings.

- Location and timing of climate-related disclosures make it challenging to understand the big picture – improving connectivity with the financial statements and between different parts of the information in climate-related disclosures remains key.
- Data challenges including availability, reliability and time lags are impacting the scope and extent of scenario analysis and the disclosures on metrics and targets. Going forward, banks will need to improve their data collation or estimation methodologies (and the accompanying systems, processes and controls) to enable them to report the required information at the same time and for the same period as the financial statements.
- Credit risk remains the focus followed by the impacts on reputation and operational risk. In 2022, notably, more banks identify litigation or liability risk as an area impacted by climate-related risks – sometimes mentioned together with greenwashing. However, a limited number of banks disclosed how they identified and assessed material risks and opportunities related to climate, and therefore, what they needed to disclose.

In next quarter's article we will explore in more detail our findings in respect of the four thematic areas of the disclosures: governance, risk management, strategy, and metrics and targets.

What about greenhouse gas (GHG) emissions disclosures?

Globally, many banks currently disclose a target to achieve a committed amount of sustainable financing (usually by 2030) and net zero in operational emissions (usually by 2030). Generally, these banks detail how they plan to achieve these goals through their climate-related strategy.

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For financed and facilitated emissions, banks often disclose an overarching target to achieve net zero by 2050. Some banks disclose quantitative details on financed and facilitated emissions, which are then provided for a section (or sub-section) of a bank's loan portfolio. Banks do not yet disclose the total financed and facilitated emissions across their full lending and investment activities. This means it's generally not easy to understand how much of the banks' total operations are captured – i.e. whether a bank is on track to achieve its net-zero targets in 2050 – or to make comparisons between banks.

> Credit risk is the most common note in the financial statements in which banks mention climate-related impacts.

Also, in many cases it is challenging to understand how absolute or intensity-based financed and facilitated emissions metrics are calculated (if these are quantified).

We also note that some banks use climate-related or Environmental, Social and Governance (ESG) factors to set variable remuneration. However, financed and facilitated emissions often do not yet feed into the specific climate-related or sustainability metrics and targets used to determine variable remuneration.

More mentions of climate in financial statements

The word 'climate' is starting to appear more frequently in financial statements; however, the disclosures are limited. Many of the banks that mention climate in their financial statements do so in the context of disclosing climate-related impacts on their financial statements. In most cases, these banks note that the quantitative impact on the financial statements is not considered material, either at this time or in the short to medium term.

Credit risk is the most common note in the financial statements in which banks mention climate-related impacts. Some banks disclose how these risks are managed, and/or how these are factored into their measurement of expected credit losses (ECLs). Notably, in the 2022 annual reports, there are a few banks that disclose judgemental adjustments to their ECLs due to extreme weather events or country-specific regulation.

We expect that the quality and sophistication of climate-related disclosures should improve under the forthcoming reporting standards, which in turn will enhance the ability of companies to make connections and identify climate-related impacts in the financial statements.

Also, the focus on connectivity between climate-related disclosures in and outside of the financial statements will become more prominent with the new project recently started by the International Accounting Standards Board on climate-related risks in the financial statements.

This aspect is particularly relevant for New Zealand climate reporting entities given that climate statements are required to be made available at the same time as financial statements and New Zealand financial statements are prepared using the same international accounting standards.

Leaving you with an interesting finding…

There is an emerging focus on biodiversity. Globally, 74% of banks include biodiversity disclosures as part of their 2022 annual reports. These banks acknowledge its importance when it comes to climate change. Biodiversity may impact climate change – at the same time, climate change may also affect biodiversity. These banks disclose how they have started to address biodiversity loss through their sustainability strategy. More details to follow soon…

> We expect that the quality and sophistication of climate-related disclosures should improve under the forthcoming reporting standards.

Customer trust: Key to unlocking sustainable business growth?

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If you want more information on the topics discussed in this article then please reach out to either Cathrin or Anna.

The Covid-19 pandemic has fundamentally changed customer behaviours in ways that look set to endure. Digital, mobile and social trends are gaining momentum and a new type of consumer has emerged worldwide. This consumer is financially restricted, highly proficient in the use of digital technologies and significantly more driven by a set of newfound values.

As the banking sector becomes more competitive, and products and services more homogenised, customers increasingly make decisions and evaluate organisations through the lens of their own core values. Banks are therefore faced with the fundamental challenge of earning and maintaining customer trust.

But customer confidence in the financial services industry has been steadily declining because of unfair banking practices coming

> "Consumer NZ recently reported that New Zealanders' trust in banks has been diminishing over the last two years sitting at an all-time low of **39%**.

to light in a number of countries, triggering our own review of conduct and culture in New Zealand retail banks. While the review by the Financial Markets Authority and the Reserve Bank of New Zealand has not found evidence of widespread or systemic issues, it certainly prompted banks to scrutinise their own practices, processes and culture.

New Zealand banks have taken good strides towards trying to ensure unbiased and fair treatment of customers, but it will take more time and effort for trust to be regained.

Consumer NZ recently reported that New Zealanders' trust in banks has been

> A focus on building trust is therefore not just a safeguard; it is the key to unlocking sustainable business growth.

diminishing over the last two years sitting at an all-time low of 39%, with the country's big four banks seeing the worst results[23].

KPMG's own customer research identified that integrity is increasingly driving customer buying decisions and advocacy[24]. Organisations that are perceived as trustworthy have reported higher Net Promoter Scores (NPS) and customer loyalty results. A focus on building trust is therefore not just a safeguard; it is the key to unlocking sustainable business growth.

The trust imperative: Going beyond transactional and regulatory trust

At the core of banking is transactional trust. Do I trust my bank to keep my money safe and deliver on their promises? 20th century customers were comforted by fancy stonework branch facades and imposing looking vaults. Fast forward to the 21st century and the threats are increasingly more complex and digital. As banking is changing, New Zealand regulators maintain a watchful eye on the industry and financial market as a whole to ensure financial stability and to protect customers from unfair treatment. The imminent Conduct of Financial Institutions (CoFI) legislation is a recent example of regulator intent to address potential conduct weaknesses in financial institutions.

Historically, banks have always been good at complying with changes in regulatory requirements, working hard towards earning regulatory trust. Indeed, their licence to operate depends on being compliant and working within the boundaries of the law.

Earning and maintaining customer trust will require banks to go beyond what is mandated by the regulator. Are banks genuinely invested in me and my community? Are they serving my needs in a way that suits me and my circumstances, or are they just going to add more complexity to my already complex financial query? And what am I really getting for my money, tenure and loyalty?

The trust issue that banks face stems from New Zealanders questioning what banks are often perceived to be – powerful, intimidating and an institution they'd rather not deal with if they don't have to. Customers are humans, and most of us don't like the unknown or complex, and how that makes us feel.

Customers want transparency and full visibility of the end-to-end process. Take loan applications for example, customers fill in pages of information (information that banks often already have) just so their form ends up in a black hole of 'decision making'. What happens during that time? Should I be worried? What will they think about my last excessive shopping trip? Will that influence the decision to approve or decline my application? This is a nerve-wracking experience for many customers that's usually driven by a lack of visibility, communication and customer engagement.

While one could argue that certain processes are the result of banks trying to meet complex regulatory requirements, which in some instances have created unintended consequences to customers, the opportunity exists for banks to be more open at every step of the customer journey.

> Earning and maintaining customer trust will require banks to go beyond what is mandated by the regulator.

> Fortunately, the pandemic has pushed many banks to elevate their processes and interactions with customers to provide greater visibility and control.

Fortunately, the pandemic has pushed many banks to elevate their processes and interactions with customers to provide greater visibility and control. For example, there is an ongoing strong focus on improving Kiwi financial wellbeing with many mobile banking apps now showing customers where and how to reduce debt or shave years off their home loan tenor. These insights help customers make financially smart choices that are easy to understand and follow. This level of transparency, openness and ease will help legacy banks to regain customer trust and drive business value.

Unlocking sustainable business growth

Offering intuitive, transparent and frictionless products and solutions is not only going to help banks to restore customer confidence, it can solidify their role as trusted financial advisers.

Looking at the next generation of potential customers, they are turning to social media platforms like TikTok for advice on how to manage their personal finances. It even has a name: 'FinTok'.

Creating trust and finding ways to engage with customers in a meaningful, personalised way will ensure banks remain relevant for this and the next generation of customers, and help reap benefits that span innovation, growth and cost optimisation.

- **Innovation:** Often there is a disconnect between what customers want and what banks are offering. Customers will question the relevance and value-add of a product or process if it appears too complex or irrelevant. Removing this disconnect by co-creating with customers not only demonstrates genuine care for their needs, it enables banks to innovate products and services that existing customers really want and might attract future customers.
- **Growth:** The arrival of 'Open Banking' in New Zealand will make it easier for customers to move their business and in a crowded landscape of similar products and services, customers will gravitate to those they know and trust. Growing customer trust leads to customer loyalty, which can in turn boost profits as well as lead to happier and more productive employees. Developing a deep understanding of what drives value for customers and delivers experiences that meet those needs will improve bank-customer relationships, while impacting the bottom line.
- **Operational excellence:** Trust is based on customers having superb interactions with an organisation every single time. Each time, and as trust grows, customers share more about themselves, their motivations and unmet needs. These insights are powerful. They show banks what drives value for customers and help them prioritise and reallocate resources and capacity to areas with the most potential for value creation and lower cost to serve.

Grabbing the opportunity

Customers are facing into headwinds of rapidly rising cost of living and worldwide economic uncertainty. This is the opportunity for banks to step up, work with their customers and demonstrate why they are deserving of their customers' trust.

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End notes

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21. The capital adequacy ratios reported are for the local bank.
22. More detail are provided here: Banks' climate-related disclosures – KPMG Global
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