

Aus Major Bank Latest Results - Calendar 2013, Current Pricing & Outlook – Draft Dec 2013

BANKS Strategy & Pricing

The Sector has been clearly over-priced, but for obvious reasons. There ain't that much else in Aus of Quality; And I believe quite categorically, Aus Major Banks are now Quality Businesses with Quality Management; Pricing has unwound a little in the last week but basically Aus Bank Investors are paying too much for the Assets @ generally 2x and up to 2.7x Book Value when ROE is 14%-18% and could easily be $\leq 14\%$ average, implying 1.5xBV. However I don't see this in itself as a Sell Signal. Dividend, lack of alternatives and excess system liquidity, remain supportive. Although maybe not so the Monetary "Tapering Effect" and rising long term interest rates. I prefer those Major Banks that have been under-rated.

Key Sector Operational Issues appear to be a) Superannuation, whereby I don't think the diversion of Consumer assets / deposits to Super is a Banking Horribillius. There is a temptation for the Banking Industry to Cry Poor, and opportunity through the Finance Sector Inquiry for a Review of Banking & Finance Intermediation. Banks can access these funds through Wealth Management operations, Super Fund Deposits to Banking, and Participation in Infrastructure Investment related Lending or Debt:Equity exposure; and b) Wealth Management operations, whereby none of the Australian Banks has found the WM Holy Grail. CBA has Size and Branding but not necessarily Profitability. Maybe the key will be Operating Efficiency - Cost/Income, with ratios of 60%+ approaching something like current Aus Banking practice of 40%-45%, I expect primarily through Cost reduction. In 1992, Don Argus (NAB, BHP) suggested Banking Cost/Income would approach 45%. At the time it was in the range 55%-60%. Don, God Bless Him, made this exceptional Prophecy, but he did also acquire NAB UK at peak margins.

The main Question In Aus Banking Stock selection to me Is: Do you think CBA & Ian Narev know Secrets to Irreplicable Banking Success that Cameron Clyne, Craig Drummond and Michael Smith etc don't?

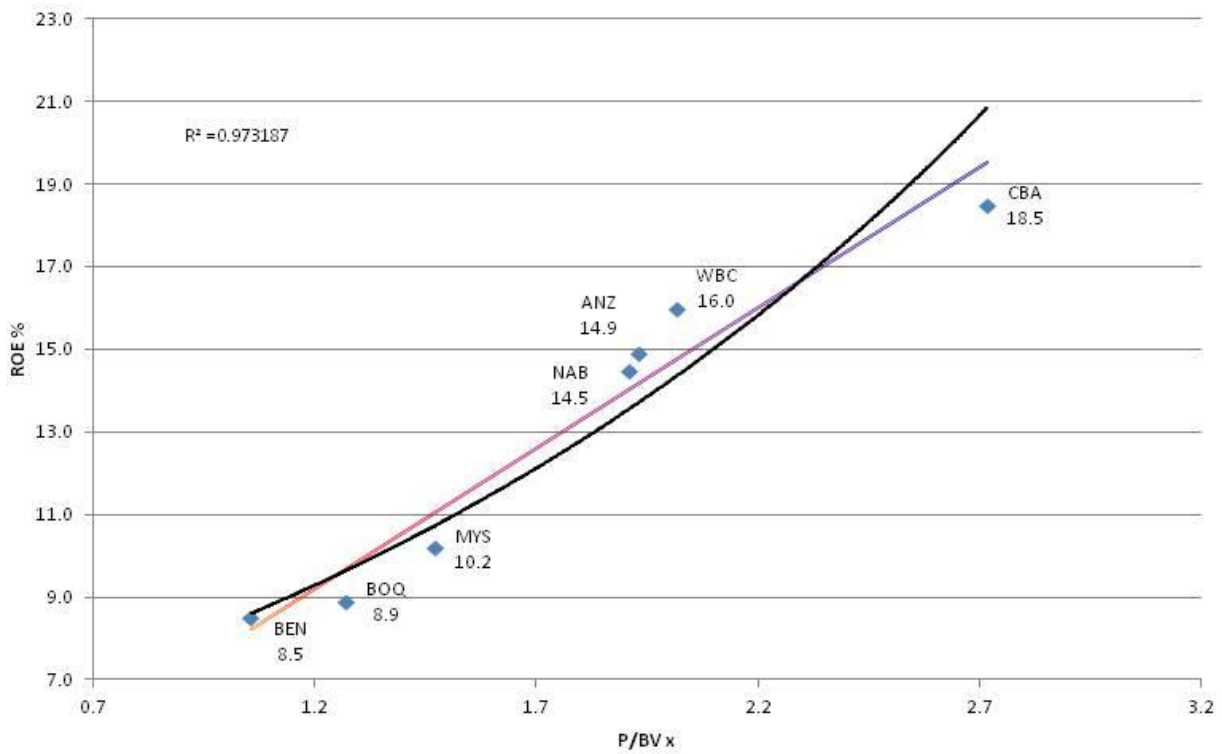
The answer is they don't. It is unlikely they would in what is essentially an Oligopoly. In any event On my New & Preliminary Review, NAB appears to have Rebuilt Pre-eminent Size ($\geq 10\%$ bigger by Assets) and in all but UK (\$78B = the +10% Assets), Profitability.

Sector :	Modest Overweight
ANZ	Overweight
CBA	Modest Underweight. Look for opportunities to Reduce
NAB	Overweight. Major Sector Position
WBC	Market to Underweight

NAB Commentary

- **Business Lines** The thing about NAB is just how severely the Group and its Profitability is impacted by the UK Operations - in both Banking and the separated Commercial Real Estate. The UK is on the improve and so too should be NAB-UK but it has a long way to go. I think most other parts of NAB - Aus, NZ, GW-US, show impressive if not leading Profitability.
- **Strategy** Low and behold GW-US has turned out to be highly Profitable albeit small. It stands as an ongoing attractive proposition. NZ is strong and Aus Business and General Banking appear to have been Rebuilt. Main Question is how quickly UK Recovers, is Divested or just Down-sized. The other question is how any Asian Strategy feeds in beyond natural Aus-Asia connections. NAB also has the = highest proportion of earnings from a rapidly improving NZ.
- **Stock Pricing** NAB has been priced close to fair-value (P/BV) particularly compared to CBA and WBC. In the context of UK Recovery, Rising Profitability, PE Discount and Dividend Yield advantage, it represents the most attractive sector exposure.

Australian Banks P/BV v ROE - 2013 Full Year



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Aus Banks

Major Banks Valuation Summary - Price:Book & Relative PER

Sunday, 15 December 2013		ANZ		CBA		NAB		WBC	
		H2 2013	FY r2013	H2 2013	Fyr 2013	H2 2013	Fyr 2013	H2 2013	Fyr 2013
ROE	%	15.3	14.9	18.8	18.5	14.3	14.5	15.7	16.0
P:Book	x		1.9		2.7		1.9		2.0
P:Nta	x		2.2		3.6		2.3		2.8
Rel PER (v Market)	%		78		95		80		88
Rel PER - Target	%		82		90		85		85

Regional Banks Valuation Summary - Price:Book & Relative PER

Sunday, 15 December 2013		BEN		BOQ		MYS	
		H2 2013	FY r2013	H2 2013	Fyr 2013	H2 2013	Fyr 2013
ROE	%	8.6	8.5	7.0	8.9	10.5	10.2
P:Book	x		1.1		1.3		1.5
P:nta	x		1.7		1.6		2.0
Rel PER (v Market)	%		82		88		90
Rel PER - Target	%		80		90		90

Aus Major Bank Results - 2013

ANZ	P&L	Reported Profit		Cash Profit		Revenue		NIM		Expenses		88:00 Charge \$m		
		\$b	%Ch	\$b	%Ch	\$b	%Ch	%	%	\$b	Exp/Inc %	\$b	\$b	
	F Yr	6.27	11	6.50	11	18.40	4	H2	2.20	4.20	45.2	H2	600	
	H2/H1	9.88	18	9.82	4	9.50	7	H1	2.24	4.08	44.1	H1	598	
	Balance Sheet	Imp Ass \$b		Prov / IA %		C Prov / Cr RWA %		Kapital %		Loans \$b	Assets \$b	Deposits \$b	Equity \$b	
	H2	4.88		H2	94.4	H2	1.00	Tier 1 APRA	9.5	47.5	708	968	45.6	
	H1	4.70		H1	92.9	H1	1.01	Tier 1 Int'l	10.8			0.775	0.065	
CBA	P&L	Reported Profit		Cash Profit		Revenue		NIM		Expenses		88:00 Charge \$m		
		\$b	%Ch	\$b	%Ch	\$b	%Ch	%	%	\$b	Exp/Inc %	\$b	\$b	
	* Q1 2013-14 Profit \$2.1b	F Yr	7.68	9	7.78	10	21.84	7	H2	2.17	4.85	44.6	H2	466
		H2/H1	4.02	10	4.02	7	10.81	8	H1	2.10	4.75	44.8	H1	616
	Balance Sheet	Imp Ass \$b		Prov / IA %		C Prov / Cr RWA %		Kapital %		Loans \$b	Assets \$b	Deposits \$b	Equity \$b	
	* Q1 2013-14 T1 Int'l (10.7%)	H2	4.88	H2	97.6	H2	1.46	Tier 1 APRA	9.2	59.2	722.2	448.5	45.5	
		H1	4.81	H1	48.8	H1	1.50	Tier 1 Int'l	11.0			0.791	0.063	
NAB	P&L	Reported Profit		Cash Profit		Revenue		NIM		Expenses		88:00 Charge \$m		
		\$b	%Ch	\$b	%Ch	\$b	%Ch	%	%	\$b	Exp/Inc %	\$b	\$b	
	Group Cost/Inc 44%	F Yr	5.50	84	5.94	9	20.58	2	H2	2.02	4.20	49.5	H2	842
		H2/H1	2.88	16	9.02	4	10.87	2	H1	2.08	3.97	41.7	H1	1082
	Balance Sheet	Imp Ass \$b		Prov / IA %		C Prov / Cr RWA %		Kapital %		Loans \$b	Assets \$b	Deposits \$b	Equity \$b	
		H2	6.35	H2	92.0	H2	0.94	Tier 1 APRA	8.4	52.8	808.4	966	46.6	
		H1	6.10	H1	90.8	H1	0.98	Tier 1 Int'l	10.4			0.701	0.058	
WBC	P&L	Reported Profit		Cash Profit		Revenue		NIM		Expenses		88:00 Charge \$m		
		\$b	%Ch	\$b	%Ch	\$b	%Ch	%	%	\$b	Exp/Inc %	\$b	\$b	
		F Yr	6.80	18	7.10	8	18.88	4	H2	2.12	3.91	41.2	H2	408
		H2/H1	9.51	6	9.57	1	9.48	1	H1	2.18	3.78	40.6	H1	488
	Balance Sheet	Imp Ass \$b		Prov / IA %		C Prov / Cr RWA %		Kapital %		Loans \$b	Assets \$b	Deposits \$b	Equity \$b	
		H2	3.40	H2	97.8	H2	1.46	Tier 1 APRA	9.1	59.8	696.6	424.5	47.5	
		H1	4.28	H1	95.2	H1	1.56	Tier 1 Int'l	10.6			0.786	0.068	