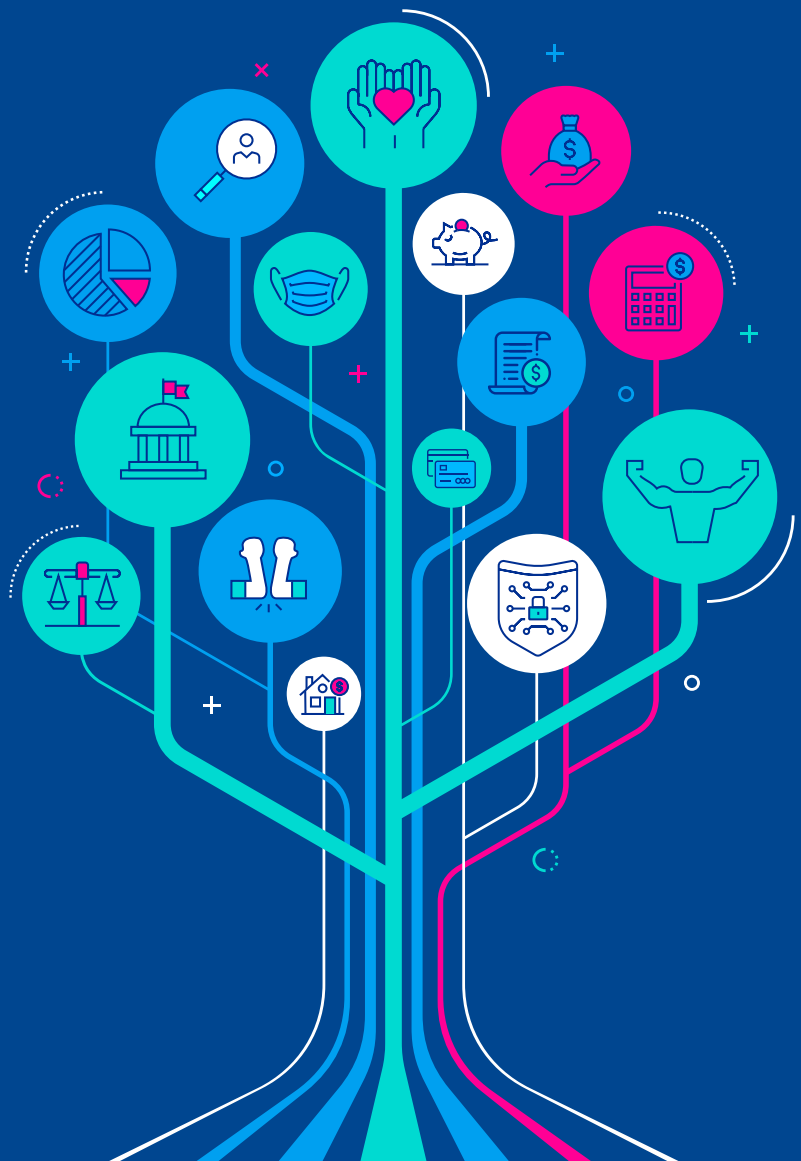
KPMG

Mutuals industry review 2020

Maintaining a resilient, trusted Mutual sector



November 2020

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Introduction

The 2020 year saw the Mutuals increase net assets by 4.6 percent to $9.8 billion (2019: increase of 6.4 percent). However, overall operating profit before tax fell by 19.1 percent (2019: decrease of 3.6 percent) to $494.3 million (2019: $611.0 million). The fall in operating profit before tax was due to a continued squeeze on net interest margins, increased loan loss provisioning and increased technology and people costs.

The 2020 financial year will be summarised as a challenging year for business, communities and individuals.

The consequences of bushfires, floods, and the COVID-19 pandemic, along with the continued competitive pressures and low interest rate environment, were all reflected in the results of the Mutuals for 2020.

In our discussions with many market participants over the past twelve months (and particularly the latter part of the financial year) there were a number of key factors exercising the minds of Board and executive team members. In particular, those that are impacting on the Mutuals include:

Operational

The COVID-19 pandemic required organisations to shift quickly to firstly protect the health and well-being of their people. This saw all organisations move to a remote working environment, thus testing the resilience of systems, processes and controls. In particular, the robustness of information technology systems was tested. While the sector withstood the impacts of this shift, as the pandemic has progressed organisations have now shifted their thinking to how they can continue to retain some of the initiatives that have been developed (and in some cases, institutionalised) over the past 6 months.

Financial

The past year has been categorised by low interest rates, and hence a flow on impact to net interest margins – essentially the life-blood of the Mutuals' financial performance. This issue is one that has been exercising the minds of participants for the past few years, however it was exacerbated as a result of the pandemic. This saw many Mutuals take advantage of access to the Reserve Bank of Australia's Term Funding Facility (TFF) which enabled the Mutuals to access lower rate funding – as a mechanism for additional liquidity and capital. While these funds have principally been invested in investment securities at present, this funding positions the Mutuals well to continue to grow their lending portfolios as the markets return to a growth phase in future periods.

The pandemic also saw Mutuals experience an increase in provisioning levels. Previously, the Mutuals have maintained relatively stable levels of provisioning – a reflection of their focus on sticking to their core competencies of residential lending. However the broad financial and social impacts of the pandemic have impacted the Mutuals (like most financial services entities). While there are a number of government stimulus packages currently in place, the uncertainty in the market has seen the Mutuals incorporate revised economic assumptions and model overlays in their provisioning models. This has had a flow on impact to the bottom line of many market participants.

Strategic

Previously we have discussed many strategic focus areas for the Mutuals, including technology, automation, alliances, and operational resilience – all with the backdrop of continuing to maintain a focus on "what the customer wants".

Positively we have seen the Mutuals continue to maintain a focus on all of these areas during the past year. However, the pandemic has escalated the need for change as customers preferences shifted to online banking and interaction with their financial services provider. There is no question that technological change that was originally thought to take 2-3 years to achieve, was – in many cases – achieved in less than 2-3 months and at lower cost.

Going forward the challenge will be to continue to maintain this cultural change, both with respect to retaining the changes made (ie. not returning to old ways of working) and identifying and transforming additional aspects of the organisation.

Of course, while the above considerations are paramount for the Mutuals, the pending regulatory agenda can also not be forgotten.

Now, more than ever, Mutuals must consider current and future implications from these key factors as they plan for the future – **how you grow matters**.

Ultimately Mutuals can no longer just rest on the customer trust / bond that they have built up over many years. They must continue to identify ways to invest and transform in a cost efficient manner whilst building a resilient organisation into the future.

As we look towards the next 3-5 years, we have identified a number of core topics which must remain front of mind for Boards and Executives as they continue "**maintaining a resilient, trusted Mutual sector**". These topics are:

1. Regulatory resilience - Race to compliance
2. Operational Resilience
3. Transformation and Simplification
4. Cost Optimisation
5. Trust Agenda in unprecedented times
6. Evolving Customer Behaviours
7. ESG key themes, including:
   - Climate risk and sustainable finance models
   - Modern Slavery
   - Sustainable development goals

These topics represent a strategic imperative for all financial services institutions. However, the Mutuals are well positioned to meet these challenges. In times of uncertainty, customers look to their financial institution to provide them with clear solutions and support. The success of Mutuals lies in their strong customer bond and affiliation as "purpose-driven organisations", providing value to the community and members alike.

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

Brendan Twining
National Sector Leader, Mutuals
KPMG Australia

Year in review – 2020 highlights

36bps

Average capital adequacy ratio decreased by **36bps** to **16.67%**

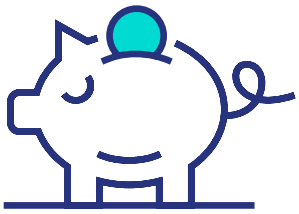
19.1%

Operating profit before tax decreased by **19.1%** to **$494.3m**

13bps

Net interest margin dropped **13bps** to **1.79%**

7.0%



Deposits grew by **7.0%** to **$108.4b** (2019: **$101.3b**)

3.65%

Non-interest income decreased by **3.65%** to **$421.8m**

5

5 mergers completed (2019: **2**)

3.0%

Residential lending increased by **3.0%** to **$100.2b** (2019: **$97.3b**)

8bps

Impairment expense increased by **8bps** to **0.12%** of Loans to members

Deferrals

$5.65b of COVID-19 related loan deferrals (**5.5%**) of loans and advances[1]

7 Current and emerging topics

1 Regulatory resilience - Race to compliance

How can Mutuals reprioritise efforts to respond to amendments to the regulatory change agenda? What are the different strategies to respond?

2 Operational Resilience

How do Mutuals remain operationally resilient in the face of a global pandemic, and other challenges?

3 Transformation and Simplification

What are the next steps and priorities in the Mutuals growth and transformation journey? Where should Mutuals focus in order to simplify the customer experience and enhance core capabilities?

4 Cost Optimisation

What levers are available for Mutuals to pull to optimise their cost base, whilst remaining agile? When should these levers be pulled to remain resilient?

5 Trust Agenda in unprecedented times

How can Mutuals use their existing bond with the customer and community to navigate challenges together and with the customer?

6 Evolving Customer Behaviours

How are customer behaviours and preferences evolving during COVID-19 and which features will persist beyond the pandemic?

7 ESG key themes

1) Climate risk and sustainable finance models
   What are some of the learnings from emerging climate risks and what sustainable finance models can be used by market participants?

2) Modern Slavery
   Are Mutuals captured under the new legislation? What are the learnings that are transferrable regardless of the size of the Mutual?

3) Sustainable Development Goals
   How can Mutuals leverage goals set by other financial institutions and what expectations will cascade through the sector?

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.

Preface

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). This is the 33rd year of the Report.

It includes the financial results of 47 Mutuals for the 2020 financial year (2019: 44 Mutuals), which represents over 97 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 the industry being exposed to.

Certainly 2020 has been a year of unprecedented challenge for the sector with bushfires, floods and COVID-19 in particular impacting on the results and operations of all market participants. Despite this, we had a fantastic response rate this year of 91 percent. This reflects the Mutual sector's eagerness to come together, leverage experiences and operate in unity, and building towards resiliency in a highly competitive 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, support and contribution to this report.

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

- **Webinar**: An overview of the key findings from our report. This includes analysis of the financial results for the sector, and incorporating key responses to our qualitative survey. A recording of the webinar is also available.
- **Mutuals insights dashboard**: Interactive charts and graphs of the financial data collected, which can be filtered based on preferences.
- **Spark Videos**: These short video clips provide highlights of the key themes from our report. Please watch our report contributors speak to their respective observations in the Mutuals sector as well as the broader banking sector. We hope these spark your interest.
- **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.

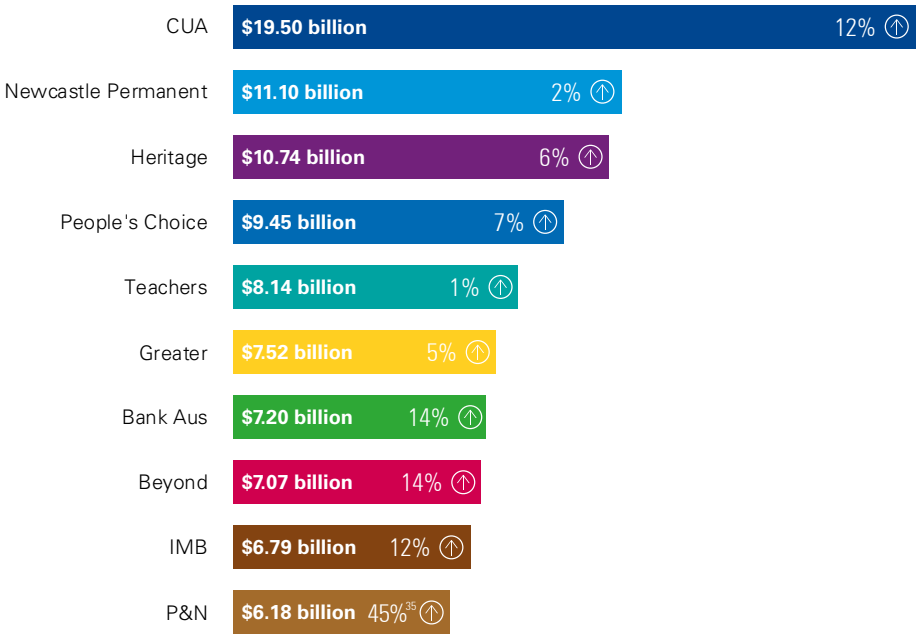
2020 financial results

In a challenging environment, the 2020 financial year saw the Mutuals record consistent growth in total assets, relative to previous years, as the sector continued to focus on their 'customer-centric' approach and brand loyalty within their community. The sector also took the opportunity to access cheaper funding via the federal funding facilities. Access to the funding facility was for a limited time and sector participants utilised the opportunity to reshape balance sheets from a liquidity perspective and replace existing higher cost funding facilities. 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, have continued to maintain their presence in the Top 10 since 2016, with all the Top 10 Mutuals retaining their respective rankings in 2020 (compared to 2019).

Top 10 by total assets ($) – 2020



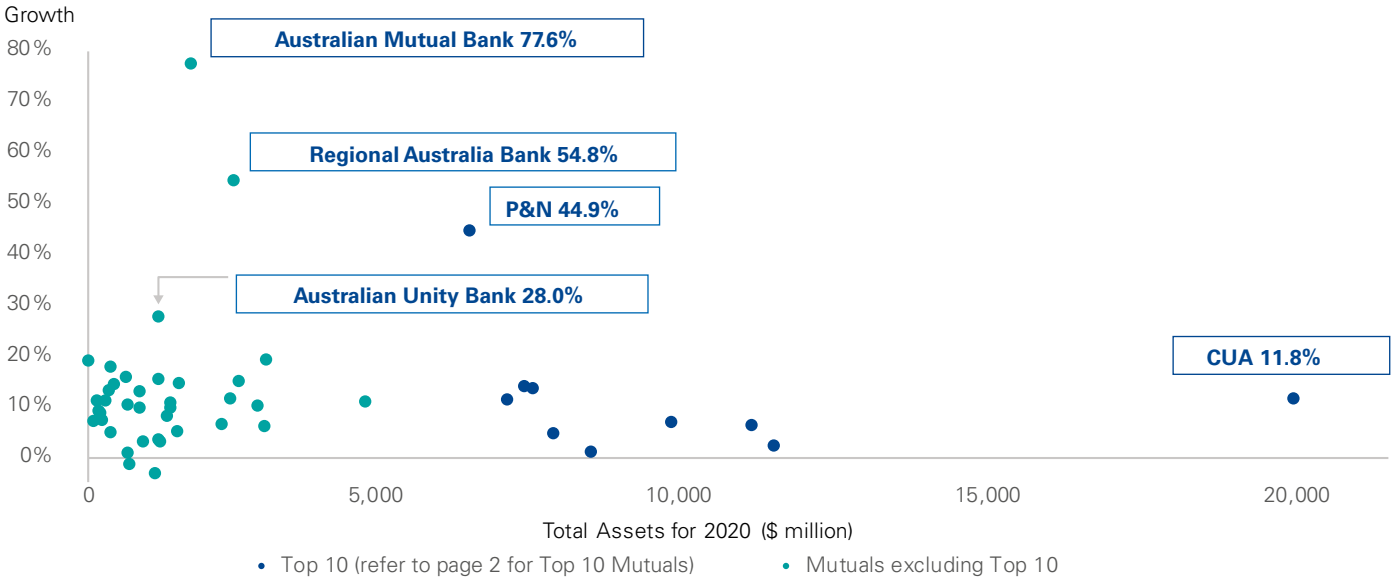
Total assets for the Mutuals increased by 8.2 percent (2019: 9.5 percent) to $138.0 billion in 2020 (2019: $127.6 billion), despite a year of extraordinary challenges, including pressures on margins from fiscal easing measures, competitive pressure from the majors and new entrants, and an economic environment facing unprecedented levels of uncertainty.

As the Australian economy looks towards the recovery phase, following the adverse impacts of COVID-19, building a resilient, and trusted Mutual that meets customer's needs remains a priority. Success will ultimately involve navigating through this economic recovery to build sustainable growth.

Mutuals comprised 2.6 percent (2019: 2.6 percent) of total assets across all authorised deposit-taking institutions (ADIs) in Australia at 30 June 2020. The maintenance of this market share points to the fact that the Mutuals continue to be seen as an attractive proposition for customers that want to 'support local' in their communities as evidenced by the continued growth in residential lending and total assets.

The sector has also continued to maintain a positive outlook in the face of ongoing market and economic uncertainty, with 70 percent of survey respondents revealing they feel confident in their three year growth prospects, a notable increase from 63 percent in 2019.

Growth in Total Assets (%) – 2020



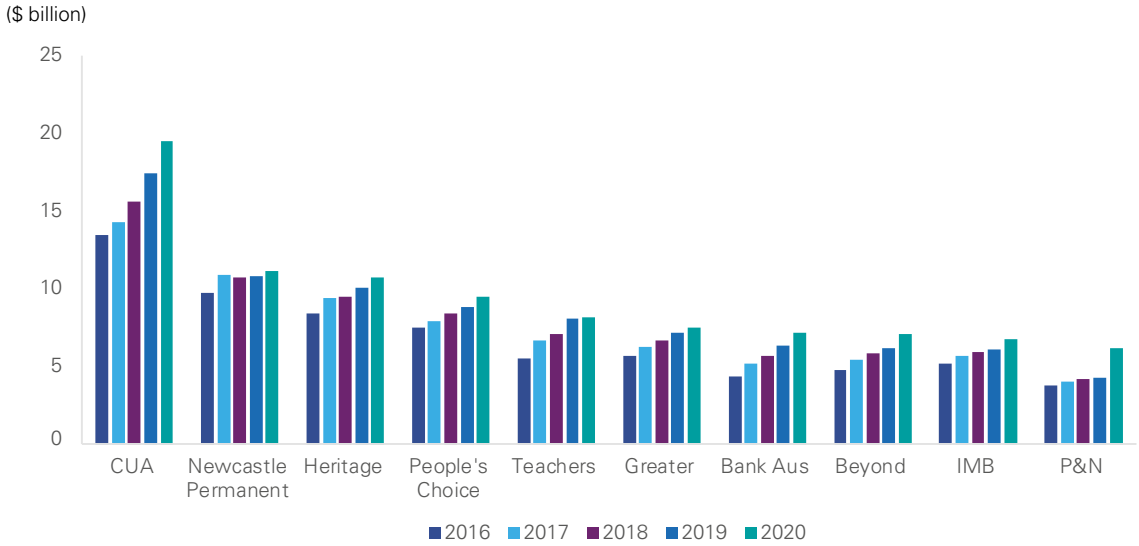
Total asset growth across the sector was partly driven by participants accessing the RBA's Term Funding Facility (TFF) as a means to manage liquidity and capital in the short to medium term. Excess funds from the TFF (i.e not used for lending purposes) were invested into investment securities in the intermediate term. This extra liquidity also provides the sector with sufficient funding to take advantage of growth opportunities as confidence returns to the lending market.

The Top 10 individually, and as a collective, experienced strong growth in Total Assets at an average rate of 9.9 percent, which outperformed the Majors who grew 3.3 percent (2019: 3.0 percent).

The highest level of growth in the sector was experienced by Australian Mutual Bank who undertook a merger during the year. The highest level of organic growth in the sector was experienced by Australian Unity Bank who saw strong mortgage portfolio performance attributable to leveraging broker networks, and simplifying product offerings for their customers[2].

Further, the impact of the initial adoption of *AASB 16 Leases* from 1 July 2019 led to a nominal increase in Total Assets of the Sector of $372.6 million (representing 0.3 percent of Total Assets).

Top 10 Total Assets (2016 – 2020)



Loan portfolio

The total loan portfolio for Mutuals in 2020 was $106.9 billion (2019: $103.9 billion), a 2.9 percent increase from 2019 (2019: 8.5 percent).

However, it is important to note that the loan growth for the Mutuals was consistent with the banking sector as a whole (including the Majors) whereby the overall banking industry reported growth of 2.5 percent (2019: 4.5 percent). This performance continues to reflect the Mutuals disciplined approach to building their customer bond and community focused lending, a topic which 40 percent of the respondents to our survey consider is one of their top three success factors.

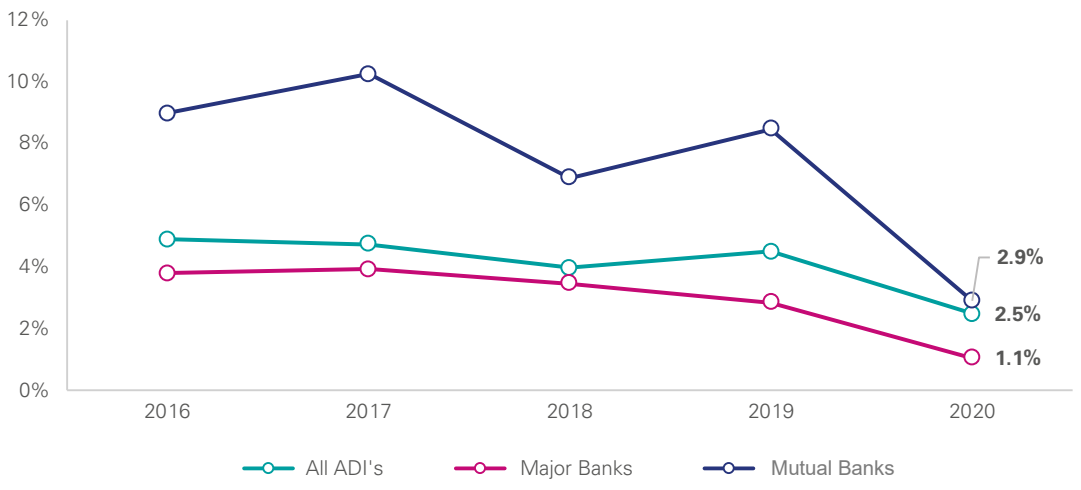
This was an unprecedented year, with bushfires, floods and the impacts of COVID-19 from March 2020 onwards which impacted the financial services sector (and the broader economy in general). However, there were also other forces that impacted on the sector's ability to grow their loan books. This included increased competition in the banking market, offset by fiscal stimulus measures which were introduced to promote lending and economic recovery. We analyse these opposing forces further below.

Residential lending market and government stimulus

The Mutuals' loan book remained concentrated on residential lending with 93.7 percent (2019: 93.6 percent) of their portfolio comprising residential loans at 30 June 2020. This is a core area of strength and expertise of the sector. Previously we have commented on the sector continuing to be focused on their core skill set and expertise, and there is no more important time than now. This is particularly due to the various headwinds facing the economy - albeit in some ways offset by government support packages. Some of these impacts include:

- Average property price increases observed at 6.2 percent in 2020 enabled more favourable residential lending appetite from an LVR perspective (per ABS data) however, different regions in Australia experienced different growth rates. Further, average prices fell by 1.8 percent in the final quarter of fiscal year 2020 – driven by the impacts of COVID-19.
- Treasury's economic response to COVID-19 which led to various initiatives to promote residential lending. One such incentive was the HomeBuilder Scheme to encourage new home builds and renovations. A grant of $25,000 was offered to eligible owner-occupiers (including first home buyers) to build a new home or substantially renovate an existing home. The impact of these schemes will hopefully contribute to loan portfolio growth in the upcoming year.

Loan Portfolio Growth (2016 – 2020)



Interest rates and availability of funding

Historically low interest rates (10bps) together with the RBA's Term Funding Facility (TFF) have assisted to create higher than normal levels of liquidity for ADIs. The aim of establishing the TFF was to assist with reducing the funding costs of ADIs and as a result, potentially reduce the interest rates for borrowers. As a result, we observed a number of Mutuals utilising the increased liquidity provided by the TFF. With this build-up of excess cash and liquidity on balance sheets the key will be managing the medium-term investment return profile in order to maintain net margins.

Impact of competition on pricing and innovative responses

The 2020 fiscal year saw strong competition in the banking market. The Mutuals were resilient in the face of this competition as they sought to grow market share through sustained competitive pricing. In fact, 21.8 percent of our survey participants indicated that competitive pricing was one of the main contributors to their financial performance and market share growth in 2020.

While the sector continues to compete on price with the broader financial services market, it is also adopting new and innovative initiatives, such as alliances with fintech companies. One such example was Athena Home Loans (Athena) and Newcastle Permanent striking a $300 million home loan funding deal to utilise Athena's innovative digital home loan platform to continue to attract and service new borrowers, resulting in a continued strengthening of the customer 'centric' experience.

Another example of innovation was Regional Australia Bank collaborating with fintech 'Basiq' to approve a loan application end-to-end in under six minutes. This was the first loan provided in Australia under the newly implemented Open Banking regime and shows the strength of innovation possible within the Mutual sector.

Loan deferrals and road to recovery

Maintaining trust with customers has involved understanding the impact of COVID-19 on their ability to make repayments. In the initial response period, several ADIs granted temporary relief to impacted borrowers, allowing them to defer loan repayments for a period of time.

Did you know…?

2020 Canstar Award winners include:

- Customer Owned Institution of the Year – Teachers Mutual Bank
- Institution of the Year (Customer-Owned) – Everyday Banking – Qudos Bank
- Customer Owned Bank of the Year - Online and Mobile Banking – Beyond Bank
- Institution of the Year (Customer-Owned) – Savings Award – CUA

Overall, the banking sector's total loan deferrals have increased. As at June 2020, APRA data reported $263.4 billion worth of all loans were deferred, and of this, $5.6 billion were Mutuals related[1]. In keeping the customer front of mind, the Mutuals have responded proactively through developing assistance packages to support pandemic impacted members. This level of deferral led to a stagnation of repayments and a slower decline in outstanding balances.

We note that the Mutuals customer bond is a strength of the sector. The ability of the Mutuals to respond quickly, and in a one-to-one manner with respect to loan repayment deferrals, has been, and continues to be, a strength of the sector in these challenging times. Clearly, prolonged exposure to deferrals is not sustainable and assisting customers return to a repayment plan will be an important focus for the Mutuals as the sector shifts from 'response' to 'recovery' following COVID-19.

Asset Quality

With COVID-19 impacting the financial services sector in the second half of the fiscal year, the sector also experienced an increase in the 'doubtful debts expense to average gross receivables' ratio (bad debt expense ratio) in 2020 to 0.12 percent (2019: 0.04 percent). The rate of increase across all ADIs was 21 bps (2019: 1 bps). While a number of customers have returned, or are returning to repayment programs, the longer, more prolonged impact of the pandemic on asset quality is yet to be determined and will be driven by the speed with which the various state economies move to recovery and then a growth phase. As noted earlier in this report, the ongoing interactions with customers during the current payment pause period will be critical to understanding the full impact on the individual loan portfolios of the Mutuals, particularly in light of some of the various (not a complete list) economic impacts noted below:

- Savills June 2020 data indicated that despite the current economic climate, strong investor demand for real estate was still apparent in Australia. This provided a backbone for investors to remain in the residential market throughout the financial year.
- The various Government assistance programs such as JobKeeper Payments, temporary access to non-taxed superannuation, increased income support and HomeBuilder programs all contributed to household income for Australians, despite the on-going COVID-19 pandemic.

Coupled with these government intervention schemes to maintain customer spending power, the risk of a price bubble in the Australian residential property market remains. In addition, during the 2021 financial year, temporary government stimulus measures will unwind and as a result, a focus on asset quality and credit risk must remain front of mind.

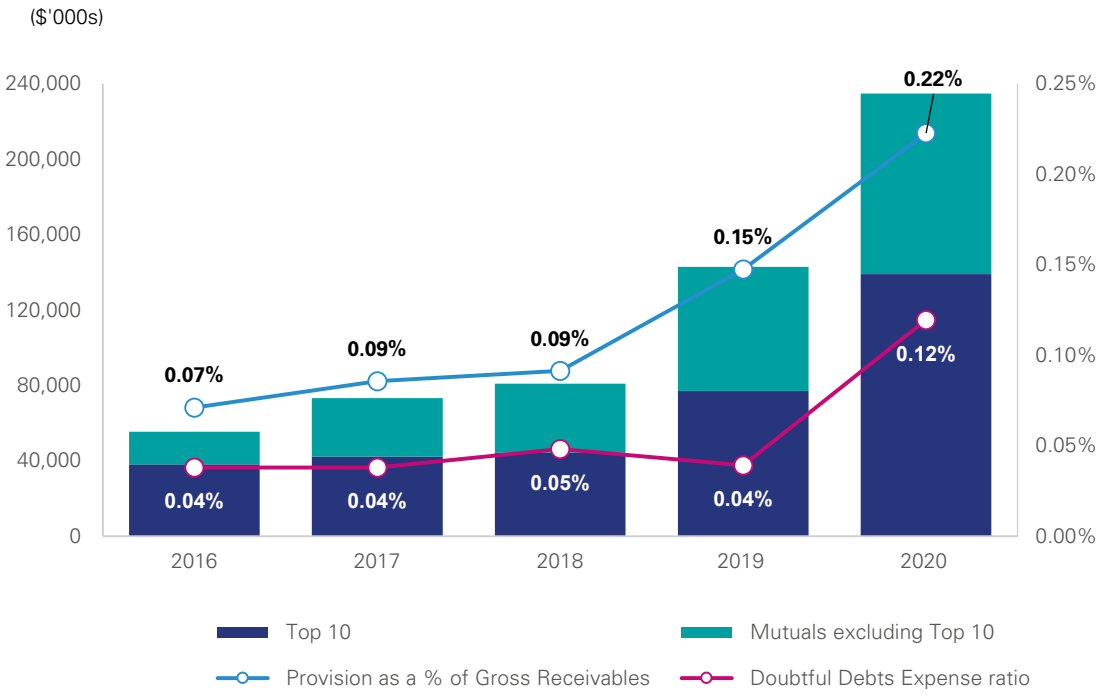
Provisioning and asset quality

Accounting standard *AASB 9 Financial Instruments* became effective during the 2019 financial year which resulted in a change in the approach to calculating the provision for impairment. In addition to any specific provisions, the standard requires estimation of a general provision called the 'expected credit loss' (ECL). The ECL requires the incorporation of forecast macroeconomic factors in assessing the appropriate provision to apply against the loan portfolio. As a result of the uncertainty associated with the COVID-19 pandemic, provisions across the sector increased by 64 percent (2019: 77 percent increase). The total provision for doubtful debts to gross receivable ratio also increased by 7 bps to 0.22 percent (2019: 0.15 percent).

A closer look at the collective provisioning for the Top 10 highlighted a 113 percent increase in collective provision to $123m (2019: $57m). In a year where bushfires and floods were only the beginning of the challenges faced by Australians, the states most impacted were Victoria and NSW which saw a proportional increase in provisions of 60 percent from the previous year. These states were significantly impacted by COVID-19 related factors including lockdowns, increased unemployment rates, and border closures.

Further, the accounting standards require Mutuals to classify their loans into stages with respect to expected recovery. Based on publicly disclosed information of a sample of the larger Mutuals, we observed that collective impairment charges formed 89 percent of the total provisioning at the end of 2020. For the same sample, 54 percent of the loan provisions were classified into stage 1 (2019: 53 percent) whereas stage 2 and 3 were 26 percent and 21 percent respectively (2019: 21 and 26 percent). With the continued uncertainty associated with the impacts of COVID-19, border closures and the second lockdown in Victoria from July 2020, Mutuals provisioning levels were heavily influenced by the inclusion of significant macro-economic assumptions and model overlays.

Impairment provisions (2016 – 2020)



Deferrals

Analysing asset quality and deferrals together is also important. In response to the COVID-19 pandemic, the Federal Government together with guidance and oversight from APRA introduced a temporary mortgage deferral scheme which gave customers the option to defer mortgage repayments for up to 6 months. This also partially contributed to the rise in provisions for the residential loans.

As at June 2020, APRA data reported that a total of $5.6 billion in loan facilities were subject to the temporary repayment deferral in the Mutual sector, 92 percent of which constitutes mortgage loans. The loan facilities under the temporary repayment deferral plan totalled 5.5 percent for the sector as at 30 June 2020. This number is expected to reduce in the coming months as customers continue to return to repayment schedules. However, the second lockdown in Victoria which commenced in July 2020, along with other potential second wave outbreaks, may impact on this positive trend. Hence, communications with customers will be critical to understanding the impact on repayment terms, and the areas of largest exposure.

Capital

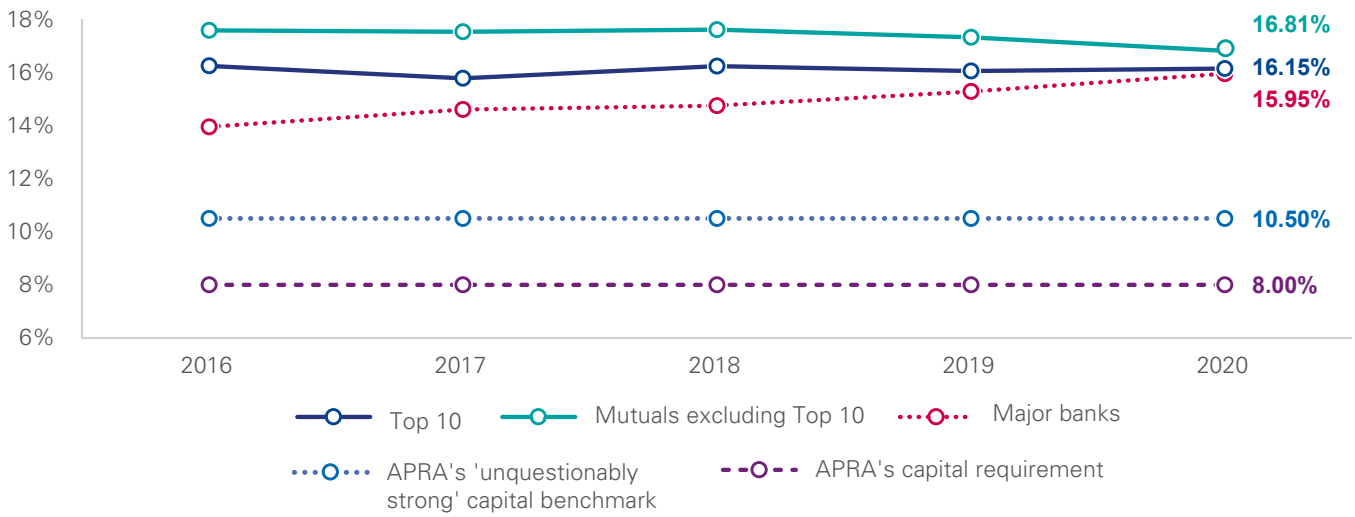
Current position

The Mutuals' average capital adequacy ratio decreased by 36 bps to 16.67 percent[3] (2019: 17.03 percent). This was primarily attributable to the increase in impairment provisions leading to lower profits. This impact has been felt by Mutuals excluding the Top 10 whose average capital ratio decreased by 46 bps to 16.81 percent (2019: 17.27 percent).

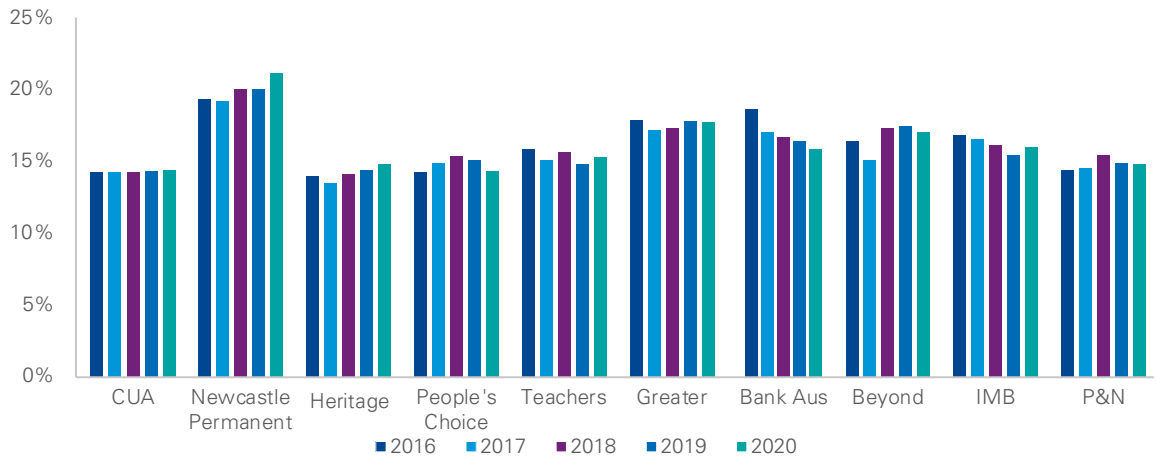
The Top 10 Mutuals experienced a slight increase in the average capital ratio by 8 bps to 16.15 percent (2019: 16.07 percent).

We highlight Regulatory Updates for the revised APRA implementation schedule for Basel III at page 18.

Average total capital adequacy ratio (2016 – 2020)



Top 10 capital adequacy ratio (2016 – 2020)



Deposits

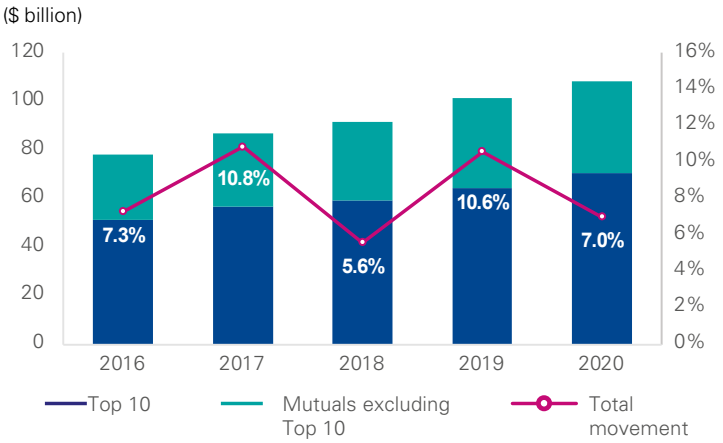
Deposits continued to be the most significant source of funding for Mutuals, followed by other capital sources (including the TFF issued by the RBA). Despite the challenges presented by COVID-19, deposits continued to grow steadily in 2020 amid RBA cash rate cuts. This is reflective of changing customer behaviours as the COVID-19 pandemic caused households to rethink discretionary spending.

Total deposits grew by 7.0 percent (2019: 10.6 percent) which is below the growth experienced by the major banks (8.7 percent). This brings total deposits to $108.4 billion (2019: $101.3 billion) for the Mutuals sector.

Total deposit growth reflected the Mutuals continued efforts to establish customer and community centric experiences to enable them to remain resilient amidst strong competition.

Our survey respondents ranked deposits as their third biggest driver of growth, with the other two being greater focus on increasing residential lending and the digitisation of banking services.

Total deposits and growth in deposits (2016 – 2020)



Net interest income (NII)

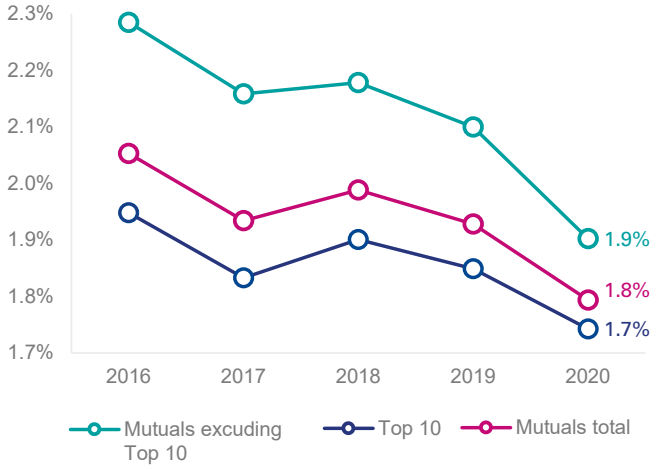
In 2020, the Mutuals reported an increase in net interest income of 0.6 percent to $2,475.3 million (2019: $2,459.8 million), driven by underlying growth in the loan book. Of this, 66.0 percent was earned by the Top 10 (2019: 63.5 percent).

Net interest income (2016 – 2020)

Net interest margin (NIM)

Pressure on margins becomes apparent in a sustained low interest rate period and a highly competitive market. The pressure on NIM has never been more pronounced, with the RBA considering quantitative easing measures and public pressure on financial institutions to 'pass on' rate cuts in full to customers. The NIM for the Mutuals, excluding the Top 10, continued to decrease with a NIM of 1.9 percent (2019: 2.1 percent). The Top 10 experienced a decrease in NIM of 9 bps to 1.7 percent (2019: 1.8 percent).

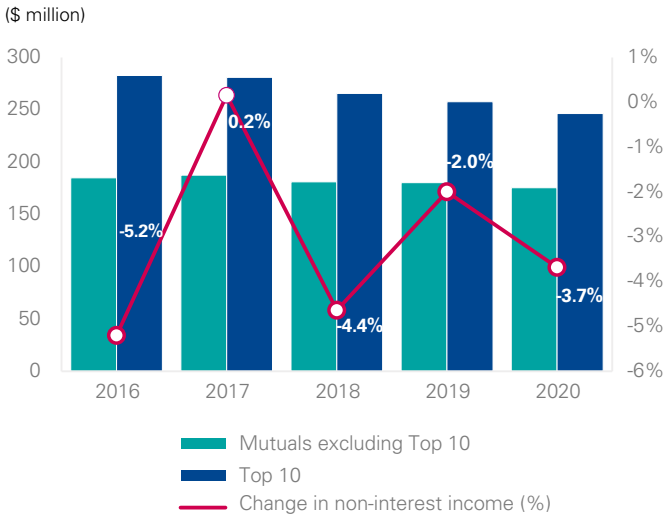
Net interest margin (2016 – 2020)



Non-interest income

In 2020, total non-interest income decreased by 3.7 percent (2019: decrease by 2.0 percent) to $421.8[4] million (2019: $437.8 million). The Top 10 reported a decline of 0.5 percent (2019: decrease of 6.6 percent). This drop is consistent with the drop observed by the majors as the banking sector continues to face competitive pressure and increased scrutiny from regulators and customers on fees and commissions. However, the decrease in non-interest income has been partly offset by government grants of approximately $8.17 million in the form of incentives like JobKeeper payments. Further, Mutuals, excluding the Top 10, reported a decrease of 7.8 percent (2019: decrease of 4.6 percent).

Non-interest income (2016 - 2020)



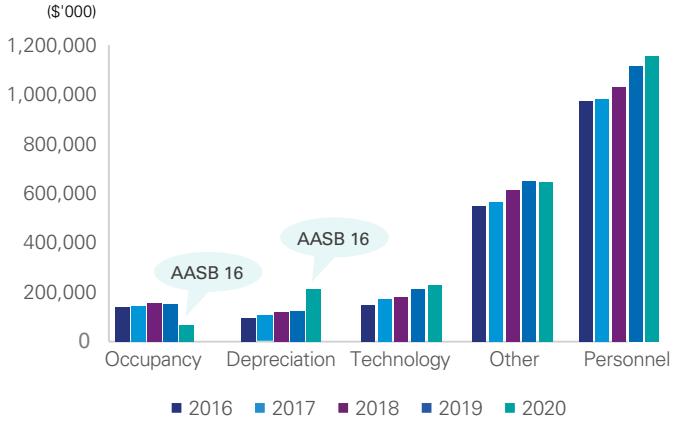
Costs

2020 saw total operating costs for Mutuals rise by 3.0 percent to $2.32 billion (2019: $2.26 billion). This increased the cost-to-income ratio to 79.7 percent (2019: 77.7 percent), driven by increased spend on technology and personnel primarily by the Top 10. While the Majors experienced a significant increase in their cost-to-income in 2020, this was mostly due to large and ongoing customer remediation and regulatory programs. In contrast, the Mutuals saw remediation costs decrease by 60.3 percent (from $15.8 million in 2019 to $6.3 million in 2020).

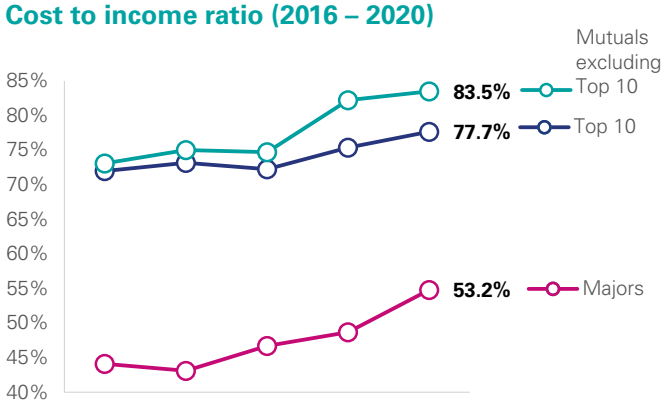
In the past few years, we have commented on the Mutuals strategic focus of shifting towards a more agile operating model, embedding resilience throughout the organisation by focusing on reducing `points of friction' at the customer level, simplifying products and digitising their workflow. While actively pursuing this resilience agenda, Mutuals also continue to focus on executing their longer term transformation strategies.

With the impact of COVID-19, almost overnight organisations were forced to reimagine the way they deliver products and services, the platforms they used, the way they worked and their means of engaging with customers. Pivoting to online channels proved to be a fast and cost-effective solution for many services that were previously delivered face-to-face.

Total Costs (2016 – 2020)

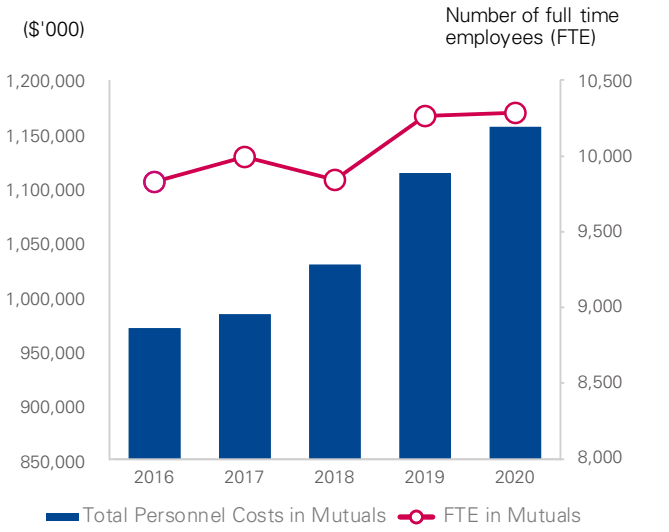


Cost to income ratio (2016 – 2020)



Personnel expenses continue to account for a major part of operating costs for Mutuals at $1.16 billion in 2020 (2019: $1.12 billion). While employee numbers increased marginally by 0.2 percent (from 10,326 in 2019 to 10,348 in 2020), personnel expenses increased by 3.8 percent (2019: 8.2 percent). We consider this highlights the need to shore up operations in the face of COVID-19, as well as the continued trend towards higher skilled, more expensive labour as the sector continues to transform its operations and pursue a broad-based digital services agenda.

Personnel expenses (2016 – 2020)



Other expenses, mainly consisting of administration costs, marketing and communication fees, and transaction and distribution costs, was the next major cost. This fell by 0.1 percent to $647.2 million (2019: $648.2 million).

In addition, $231.1 million was spent on technology expenses, which rose by 7.9 percent in 2020, again reflecting the continued investment in technology across all Mutuals. Based on our survey, the largest contributors to technology spend in 2020 were projects related to: cyber security, mobile banking and technology changes to meet new regulatory requirements.

AASB 16 lens on costs

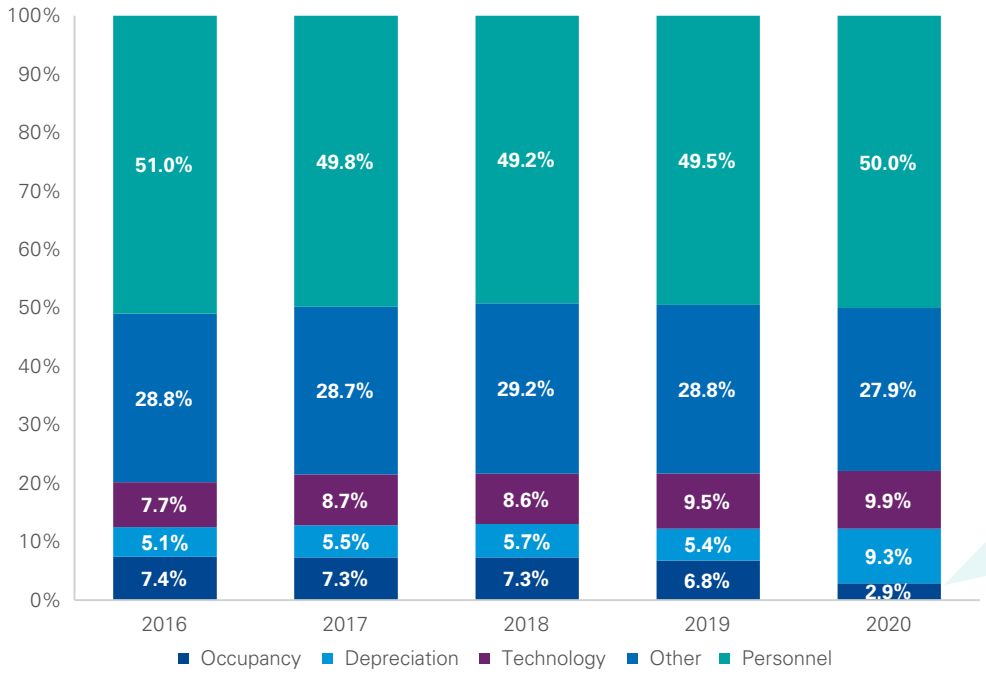
The impact of AASB 16, effective from 1 July 2019, saw a shift away from 'occupancy' and 'other operating expenses', which have traditionally included any head office and branch leases.

Under AASB 16, these costs are now reflected in amortisation/depreciation charge and interest expense. The graph below reflects this, with the 3.9 percent drop in occupancy costs in 2020, offset by a 3.9 percent increase to depreciation.

Consistently, the majors reported an expected shift in their cost composition as noted in KPMG's Major Australian Banks Full Year 2020 research analysis.

AASB 16 also resulted in a gross up of right-of-use lease assets and lease liabilities on the Mutuals' balance sheets. This did not have a significant impact on net assets or capital adequacy ratios.

Composition of costs (2016 – 2020)



This reallocation from occupancy costs to depreciation is a result of the adoption of AASB 16. On adoption, the shift in expenses had no significant impact on total costs for the year.

Profits

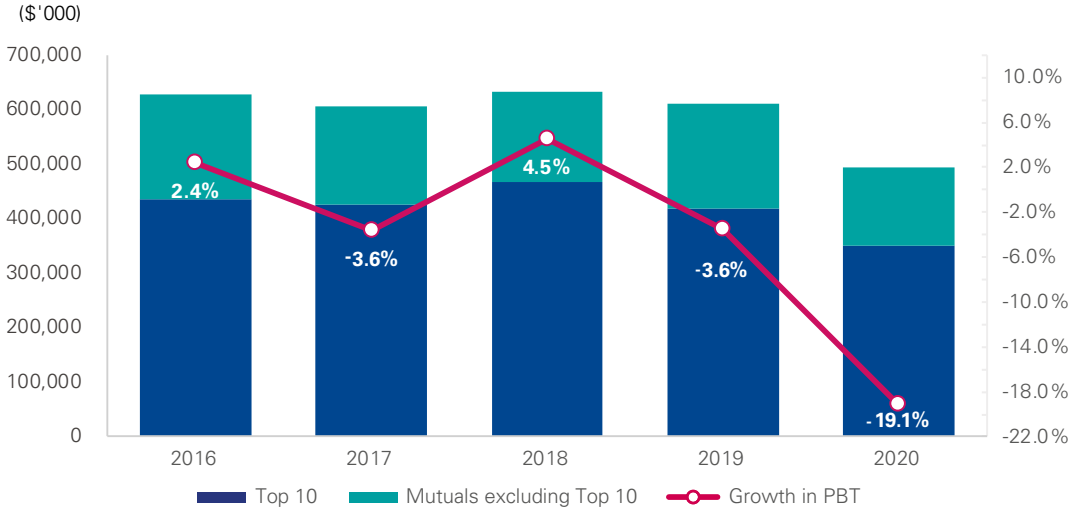
Profits before tax (PBT) fell by 19.1 percent (2019: fell by 3.6 percent) to $494.3 million (2019: $611.0 million), while the majors saw profits fall by 33.8 percent (2019: fall by 12.6 percent). This was a result of the heightened margin pressure, as the sustained low interest rate environment impacted on net interest margins, and costs increased as the Mutuals sector continued to spend on innovation, operational resilience and responding to working remotely in a COVID-19 environment.

Another key driver of the fall in profits before tax was an increase in impairment expense from $38.0 million in 2019 to $126.1 million in 2020 across the loan portfolio.

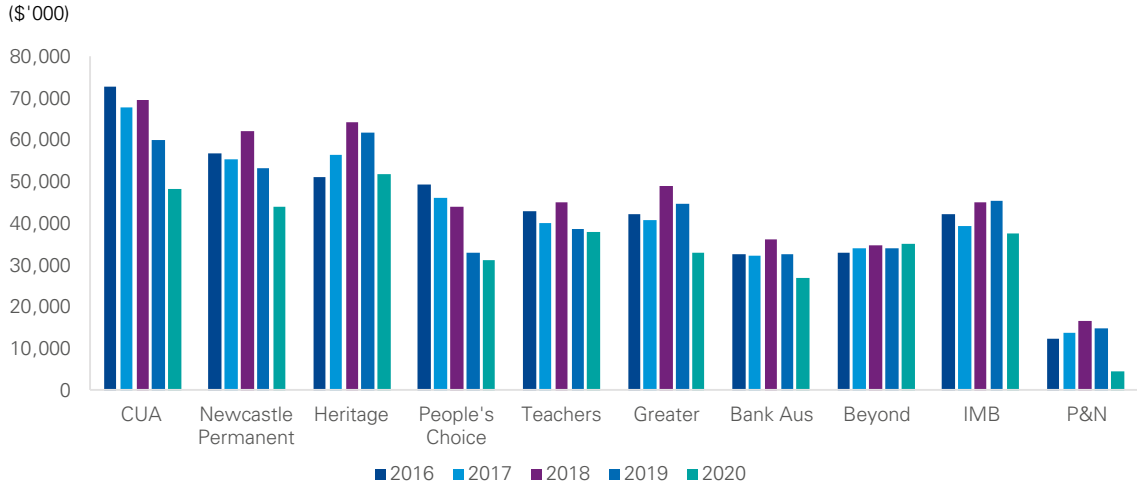
The Top 10 Mutuals experienced a significant decrease in PBT in 2020 of 16.1 percent (2019: 10.4 percent decrease). This was driven by impairment provisions, along with an increase of 17.0 percent in technology expenses and an increase of 8.7 percent in personnel expenses. Collectively, these expense increases are aimed at supporting the Top 10 to increase operational resilience in the current environment, process automation and agility in chasing opportunities focused on the customer.

The impact of low interest rates will continue to be a major factor on profits, with 52.3 percent of survey respondents ranking the low interest rate environment as the number one risk for their organisation.

Profit before tax (2016 – 2020)



Top 10 total profit before tax (2016 – 2020)



Did you know…?

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

1. Technology and transformation of business (40.9 percent)
2. Improving efficiency – doing more with less (27.3 percent)
3. More collaboration with peers (13.6 percent)

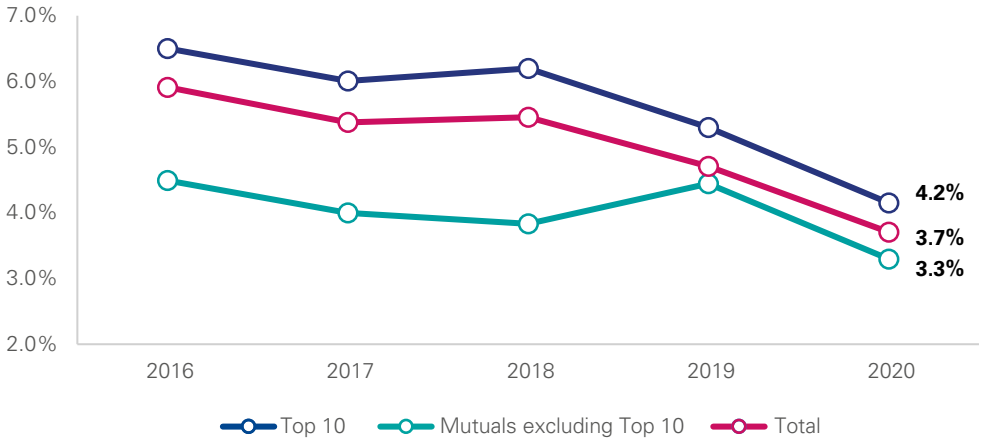
"Profitability, growth and safeguards against existential risks are crucial to strengthening a company's long-term prospects. But if these three factors constitute a company's 'hard power', firms also need 'soft power': public trust and acceptance, won by fulfilling a company's social responsibility."

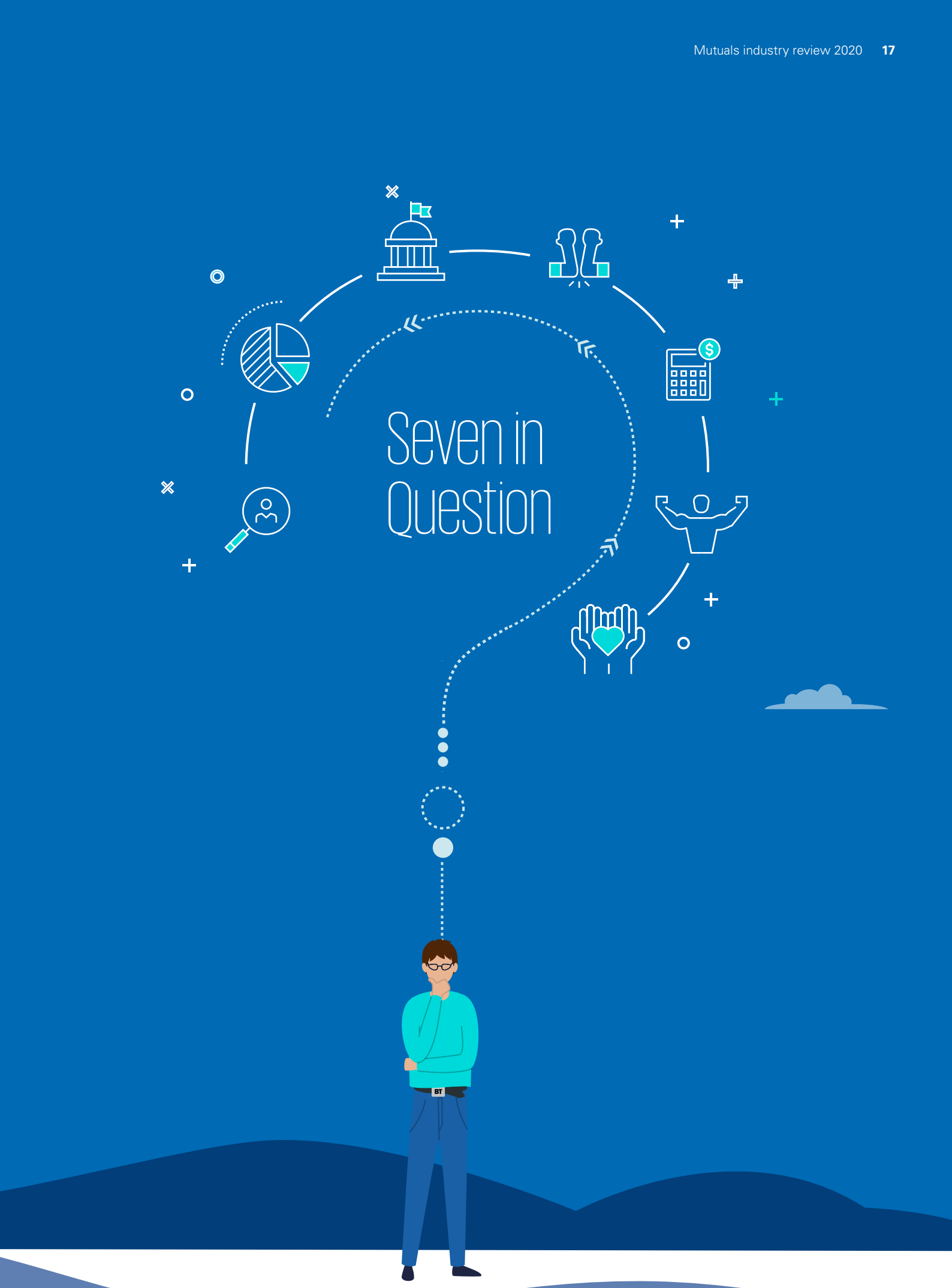
Klaus Schwab
Executive Chairman,
World Economic Forum

Return on equity (ROE)

While not a key metric for the sector, total ROE decreased by 101 bps (2019: fell by 75 bps) to 3.7 percent (2019: 4.7 percent). The ROE of the Top 10 remained stronger than the overall sector, where the decrease in ROE for the Top 10 in 2020 was 90 bps. This led to the Top 10's ROE falling to 4.2 percent (2019: 5.1 percent). For the remainder of the sector, the ROE fell by 118 bps to 3.3 percent (2019: 4.5 percent).

Return on equity (2016 – 2020)





Regulatory resilience – Race to compliance

Quang Dang, Director, Audit, Assurance and Risk Consulting
Luke Gower, Associate Director, Audit, Assurance and Risk Consulting

PLAY VIDEO

Due to COVID-19 APRA has announced a deferral in the implementation of the Basel III reforms by one year for each prudential standard. A timeline of upcoming changes and key actions for Mutuals to consider and respond to is summarised below.

June 2020	January 2021	January 2022	January 2023	January 2024
Open Banking Phase One	APS 220 Credit risk management →	APS 220		
	APS 222 Related entities →	APS 222		
	Open Banking Phase Two	APS 110 Capital adequacy →	APS 110	
		APS 112 Standardised approach to credit risk →	APS 112	
		APS 115 Standard measurement approach to operational risk →	APS 115	
		APS 117 Interest rate risk: Banking book (IRRBB) →	APS 117	
		APS 330 Public disclosures →	APS 330	
			APS 116 Market Risk →	APS 116

Today

July 2020

January 2022

Open Banking for the Mutuals

July 2020: Product data on accounts

February 2021: Product data on accounts, mortgages, and CDR data on accounts

July 2021: Product data on all products, and CDR data on mortgages

February 2022: CDR data on all products

How to respond?

— Decide and implement chosen strategy to comply, compete or innovate

— Identify how to build or gain access to the new capabilities through partnership or innovation based on the chosen strategy while balancing capital budgets

APS 220 Credit Risk Management

What's new?

— Changes to the credit standards allows for a scalable and flexible approach to assess credit risk of the borrower

— Valuation of collateral does not require the ADI to predict 'external events' that are likely to occur. Stronger focus on fair value (highest and best use)

— Simpler classification for assets. Mutuals can classify exposures as 'performing' or 'non-performing' and as 'past-due' and 'restructured'

How to respond?

— Assess gaps against revised standard and implement changes to model

Want to know more?

See the link here for the KPMG newsletter on how Mutuals are responding to APS 220.

APS 222 Related Entities

What's new?

- New standard will include a broader definition of related entities
- Revise limits on the level of an ADI's exposure to related entities and minimum requirements for ADIs to assess contagion risk

How to respond?

- Consider levels of current exposures and limit against prescribed levels

APS 110 Capital Adequacy

What's new?

- Introduce a minimum capital floor
- Simplify frameworks, improve transparency and comparability of capital framework

January 2023

APS 112 Standardised Approach to Credit Risk

What's new?

- Simplify credit risk management by removing the requirement to have credit rating grade for counterparty default and replaced with risk weights only
- Revising risk weights for standard mortgages and a flat risk weight of 100% to be applied to all non-standard residential mortgages. Additional due diligence requirements are also included
- Limiting the use of internal models for certain credit portfolios. Introduction of standardised approach for CVA
- Ability to get capital benefit where lender's mortgage insurance is adequate (previously, required adequate collateral)

APS 115 Standard Measurement Approach to Operational Risk

- Replacing existing approaches with a new standardised approach
- More prescription around when Mutuals are required to reduce operational risk or hold additional capital if APRA considers ADI's operational risk regulatory capital is not proportionate with ADI's operational risk profile

APS 117 Interest Rate Risk – Banking Book (IRRBB)

What's new?

- The standard is, for the first time, applicable to all ADIs
- Active participation of senior management in the implementation of IRRBB framework and policies
- A stress testing program incorporating sudden changes in interest rates for both economic value and net interest earnings
- Integrate internal reporting of IRRBB exposures with day-to-day risk management

Want to know more?

See the link here for KPMG webinar on how Mutuals are responding to APS 117.

APS 116 Market Risk

What's new?

- APRA will allow Mutuals to disregard back-testing exception for volatile months in determining a plus factor when calculating market risk exposures

How to respond?

- Consider reducing back testing to the extent not required for internal decision making

January 2024

2024 & Beyond

APS 330 Public Disclosures

- Introduction of "Net Stable Funding Ratio" (NSFR) in addition to Liquidity Coverage Ratio
- All ADIs will be required to fill out ARF 210.6 as a new reporting form

How to respond?

- Identify data inputs and governance measures

The success for a Mutual to navigate through these upcoming changes will stem from their ability to be adaptive, responsive, innovative and agile.

Mutuals would need to consider stronger board engagement for determining frameworks and policies, placing greater focus on capital management strategies, with a consideration of various risk factors and a focus on developing and improving data governance measures to produce accurate reports for decision making.

COVID-19, Operational Resilience and Remaining Agile

Anthony Donohoe, Partner, Audit Assurance Risk
Mark Tims, National Leader, Technology Risk and Cyber
Campbell Logie-Smith, Associate Director (Operational Resilience), Management Consulting

PLAY VIDEO

Impacts and Learnings from COVID-19

Since January 2020, businesses across the globe have experienced significant disruption to their operations due to unforeseen circumstances. In Australia, the business continuity and resilience of organisations has been regularly tested by several events including a perilous bushfire season, floods, increasingly complex cyberattacks and, most significantly, the COVID-19 pandemic.

While the potential effects of a pandemic were relatively unexplored by prior business resilience planning practices, this new disruption risk has demonstrated unprecedented and widespread impacts across all key components of a business. This impact has forced a significant re-think of resilience arrangements and how customer impacts and tolerances need to be managed.

Impacts on the Banking Sector

Within the banking sector, COVID-19 acted as a catalyst for the digital transformation of traditional banking processes and challenged the notion of permanent physical branches. Lockdown restrictions drove changes in consumer behaviour, with the accelerated shift to digital channels within the banking sector. Following this shift, the banking sector pushed forward with the innovation journey to stay competitive, with a fast realisation that products and services can continue to be delivered without the need for face to face interactions (i.e. mortgage lending).

In the broader business context, the impacts of COVID-19 highlighted that traditional resilience practices concentrated on short-term disruptive risks and did not consider such extensive staff and supply chain impacts, or the sustainability of response strategies, from days to months. Business continuity plans often became obsolete due to their lack of guidance, with response teams being stretched to adapt to the rapidly changing scenario, whilst upholding the balance between managing staff fatigue and maintaining service delivery.

In some instances, resilience was further tested through cyberattacks, concurrently to the pandemic.

To continue to survive and adapt to a changing risk landscape, a resilient organisation must establish Operational Resilience at its core, in order to respond to all threats, not just to the problem at hand.

Advantages of Remaining Agile

The effects of COVID-19 re-emphasised that being attuned to customers' needs is key in upholding a strong reputation and ongoing service demand. Organisations who adopted flexible and agile operating models were better positioned to maintain continuity and this trend is likely to continue going forward. The pandemic has given rise to key learnings that are being considered by businesses in their future risk management practices.

What is Operational Resilience?

During the pandemic, the maturity of resilience arrangements largely determined organisations' ability to effectively navigate the uncertainty, with many being forced to quickly activate their response plans and teams to manage disruption impacts. With the frequency of such disruption events likely to increase going forward, more organisations are recognising the importance in utilising resilience as an enabler to continue the delivery of their services.

Learning from COVID-19

1. Business disruptions are no longer non-frequent, short-term events
2. Business has embraced flexibility and remote working arrangements
3. Managing effectiveness and providing support in remote environments has become a focus for businesses
4. Business has a significant reliance on Information and Communication Technology as well as a focus on:
   - Security and continuity of business activities
   - Business resilience planning and exercises to include third parties
   - Understanding most vulnerable customers and providers

86% of our survey participants now consider themselves to be **very resilient** in the face of COVID-19 and any future outbreaks.

As customers become less tolerant to service interruptions, organisations need to pivot towards becoming inherently resilient to minimise the occurrence of operational disruptions. This construct is known as 'Operational Resilience' and aims to ensure that end-to-end critical business services can continue no matter the event. Resiliency must be ingrained in the design of systems and processes, be simple and easy for all staff to follow, and must assume disruptions will invariably occur going forward.

Mutuals can harness Operational Resilience to focus on limiting the impact and 'harm' that operational disruptions can cause customers by improving their ability to absorb disruptive impacts of incidents, while continuing to deliver their critical services. The pillars of Operational Resilience extend beyond business continuity and IT disaster recovery, and focus on IT Resilience; Cybersecurity; People Resilience; Third Party Resilience; Continuity and Incident Management; and Asset Resilience, creating a cohesive approach and integration within Business As Usual operations.

Key Benefits of Operational Resilience

Operational Resilience is a major shift in the approach to business continuity but in doing so, brings valuable benefits to organisations including:

Operations	Reduction in operational risks and costs of disruptions
Synergies	Cross-functional synergies and establishment of industry engagements
Market	Resiliency in the wider Mutuals sector and market
Resources	Efficient and effective allocation of resources
Customers	Enhancement of customer trust and loyalty

Key Challenges to Operational Resilience

Mutuals face challenges which differ from the rest of the banking industry, potentially including limited investment capacity, geographic concentration stemming from their community focus, and reliance on manual processes. For example, 70.5 percent of respondents to our survey have over 50 percent of their IT budget allocated to Business as Usual operations, which limits their capacity to invest in technology enhancements and innovations.

APRA's Commitment to Resilience

APRA's 2020-2024 Corporate Plan has reiterated and recommitted to previous plans and focused on the following objectives:

1. Maintain financial system resilience;
2. Improve outcomes for superannuation members;
3. Transform governance, culture, remuneration and accountability across all regulated institutions; and
4. Improve cyber resilience across the financial system

Due to the magnitude of economic impacts and prevailing uncertainty in the external environment, APRA has chosen to prioritise the first objective of maintaining financial resilience in the coming 12-18 months. This includes a commitment to foster operational resilience during a period of significant disruption and enhancing contingency plans for adverse events.

Within the Banking Sector specifically, APRA has committed increased attention to protecting the stability of the financial system by utilising operational resilience and risk management practices to:

- Respond to key risk areas that could impact regulated institutions and industries;
- Analyse loan repayment deferral impacts and consult with other relevant stakeholders to determine appropriate regulatory responses; and
- Provide data and insights on the Australian banking sector, thereby promoting transparency so organisations can identify emerging trends and proactively adjust their operating models.

How well did the Mutuals survey participants respond to COVID-19?

Flexible work arrangements
Responded very well – all branches remained open, most back office staff working remotely with key services and offerings not disrupted. Staff are a lot happier with flexible working arrangements post COVID-19.

Extended service for customers
We responded very well. Continuity of service was maintained and member support was even enhanced through extended hours to assist those in hardship.

Proactive planning
Effective response with BCP planning and Crisis Management team. Effective use of remote working activities

What does a Resilient organisation of the future look like?

Banking organisations that put the customer first and incorporate operational resilience into their day-to-day operating models will be better positioned to proactively and effectively manage future disruption risks. Successful organisations will be those that design operational resilience around the customer and focus on protecting brand and reputation.

Mutuals have the ability to implement resilience measures quicker than competitors due to their agile business structures. This needs to be balanced with pressure on budgets and concentrated reliance on limiting the number of third party service providers who may have knock-on effects across the industry.

Key themes to embed into culture:

1. Operational Resilience must be **driven from the Board**, with clear ownership and accountability to drive differentiated investment decisions.
2. Resilience should be established **for end-to-end** business services by considering resilience arrangements in respect to five key pillars (i.e. technology, data and information, people, property and supplier).
3. Boards should set clear impact tolerances and enterprise-wide resilience thresholds that are **measured**, tracked and reported against set tolerance limits.
4. Establish rigorous **testing** programs to challenge the Mutual's ability to provide critical business services within the set impact tolerances in scenarios.
5. Embed 'resilience' as a key criterion across all management decisions and business activities. This should be core in the organisation's **culture**.
6. A **recovery-centric** mind-set should be adopted to demonstrate adaptability or substitutability, assuming major disruption will occur.
7. Establish a multi-channel, enterprise-wide **communications** approach, to manage disruption across internal and external stakeholders.

Conclusion

The various disruptions experienced throughout 2020 have demonstrated the importance for organisations to embrace the concept of operational resilience and transition to proactive response planning sooner, rather than later. COVID-19 has shown us that traditional business resilience approaches are no longer sufficient to control such large-scale disruptions and organisations need to expand their resilience thinking to consider the wider business eco-system.

Need to chat?

KPMG's Business Resilience Team possesses deep technical resilience skillsets and they have worked to help build and review resilience arrangements for numerous clients, ranging from small community organisations to large global institutions. Our team can help you to navigate the complexities of the constantly evolving risk environment and stay ahead in the market through the deployment of KPMG's Enterprise-wide Operational Resilience framework. Our Framework consists of 12 key components that assist to create, design and embed an operational resilience model, and subsequently prepare, assess and action resilience arrangements to enhance your organisation's overall resilience capability.

Building resilience through transformation and simplification

Hessel Verbeek, Partner, Banking, KPMG Strategy
John Critchley, Director, Banking, KPMG Strategy

PLAY VIDEO

Efficiency is key to delivering member value and financial resilience for the Mutuals

The Mutuals have long had their unique challenges that set them apart from other banks. In addition to specific advantages, issues including limited scale and high cost bases have impacted the financial resilience of the Mutuals. In the current operating environment with low interest rates, low margins and high investment return requirements, several new issues have emerged which particularly challenge the sector. For the Mutuals to be resilient and recover, they need to demonstrate cost discipline and an ability to transform.

Financial performance is key to strategic resilience

The strategic context for the Mutuals is evolving, due to technology-driven shifts in customer expectations and new industry norms for business performance. For many Mutuals, transformation will be required, but difficult to prosecute, where investment funding is limited.

These challenges are recognised by sector leaders, where nearly three-quarters say that maintaining profitability and sustainable growth is their top priority over the next three years.

Addressing the cost base to improve financial performance clears a path to optionality, including the option to transform service and competitive pricing.

Our survey participants identified the following as the biggest drivers of growth:

1. **Increase in residential lending**
2. **Digitisation of banking**
3. **Deposits**

Underlying performance trends continues to highlight challenges facing the Mutuals

The Mutuals have been dealing with long-term performance challenges that fall into three patterns:

1. **Sustainability of growth** of the 47 Mutuals analysed[5], 34 added to their cost-to-income (CTI) over the five-year period, of which nine are in the group of ten largest Mutuals (by total assets; see Exhibit 1). Conversely, only eight Mutuals reduced their CTI while also growing total assets.

2. **Extracting scale advantage from mergers** has been a theme for the sector for some time; however, 11 of the 14 Mutuals that went through a merger since 2012 have subsequently added to their CTI over a period of five years (FY2016-20).

3. **Finding the capacity to invest** as margins have tightened and the technology gap has widened, approximately 20 percent of sector leaders say funding capacity is the biggest challenge to digitisation; the Mutuals are limited in the access to funding (no dividend pay-outs to cut, limited access to capital markets).

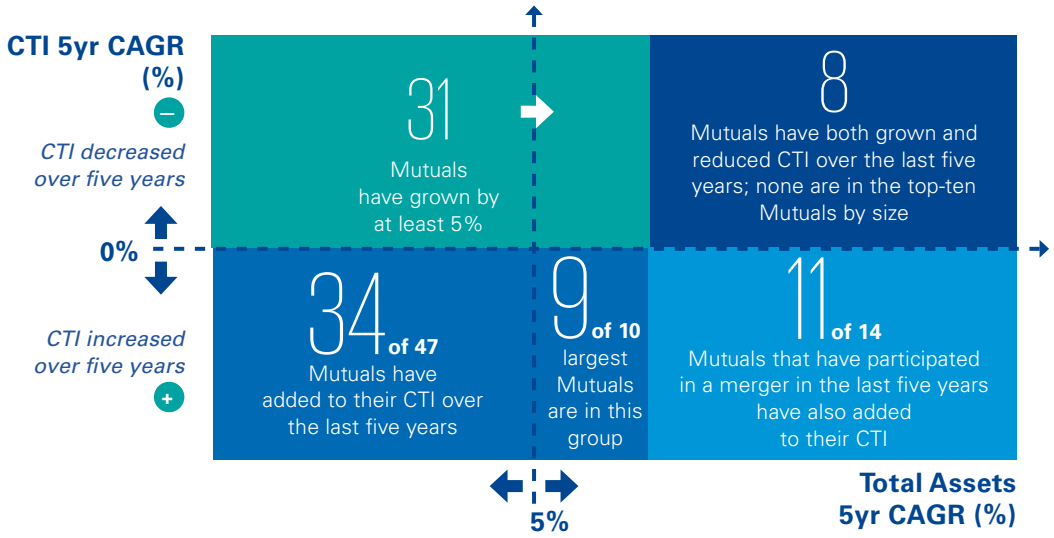


Exhibit 1:
CTI 5-year compound growth vs. total asset 5-year growth highlighted key performance insights across the Mutuals

The Mutuals are also facing new challenges to their performance and resilience

The events and economic conditions of 2020 have added new challenges for the Mutuals, amplifying the effects of the underlying long-term challenges.

Sector exposure to rising household mortgage stress

The Mutuals are exposed to a trend of rising household and investor mortgage stress, particularly in regional economies impacted by COVID-19 (e.g. the tourism economy of Queensland, student accommodation investors in university suburbs).

Despite government support (e.g. JobKeeper), the industry has seen a slight increase in the rate of default and doubtful debts across the sector (i.e. rate of defaults increased from 14 bps to 24 bps), with rates potentially to increase once COVID-19 government support schemes are withdrawn (currently anticipated to be March 2021).

Low levels of investment in technology is catching up with sector players

Overall IT expense increased by 8 percent, based on our quantitative survey. Nearly half of our survey respondents indicated that 50-75 percent of their current IT budget is allocated to IT operations to just run and maintain their business. Conversely, well over half indicated that 0-25 percent of the IT budget was allocated to improving and transforming the business.

This sentiment reflects a pattern of low levels of investment in technology for the sector, which has avoided short-term capital expense that is now resulting in stark operational inefficiencies and a widening gap to competitors (major banks and challengers).

With vendor competition at high levels and increasingly cheaper options available (e.g. cloud-based solutions), now is a good time for technology transformation in the sector. The opportunity cost of doing nothing is also mounting.

On-going pressure on margins in a long-term low-interest economy

The Mutuals have traditionally offered competitive home lending rates compared with the major banks. However, in a low-interest economy, the price differential is smaller, making the Mutuals less price-competitive, and the impacts of lower margins are heavier on a sector comprised of lower scale banks.

A recent study by KPMG found that the low-interest environment encourages borrowers to seek cheaper home loans through refinance in a competitive market; over 70 percent of mass affluent borrowers indicated they would renegotiate or switch lender as regularly as five years or less[6].

Tighter margins for the Mutuals translates to less capacity to pass value on to members, either by investing in service or reducing price. This is consistent with over half of the Mutuals leaders citing the low interest rate environment as the top risk for their organisation.

There are four practical steps to address costs, opening a path to transforming for future member value

By focusing on cost discipline, the Mutuals will have more margin to invest in better customer experience or to give back to members through competitive pricing.

Building on the theme from last year's Mutual Industry Review, where we focused on simplicity as a key strategic theme, we have identified four non-exclusive actions that the Mutuals can take to practically address costs in challenging times.

The yield from these practical steps will lead to tangible cost reduction and capacity to invest in enhancing member value, from exploiting data for an intimate customer experience at scale, to transforming products and services to meet the needs of a new target segment.

1 Address the cost base with a focus on member value

- Engage with your members to understand what they value and what they do not; reallocating costs to match member value can free up capital
- Break down the cost base to identify key drivers and isolate those that are controllable – which of these will rapidly return the most value to members (e.g. streamlining application processing by eliminating double-handling)?
- Reinforce with staff a focus on returning value to members through cost discipline; this can lead to a cultural shift, with individuals conscious of their role in driving member value

2 Drive for simplification

- Products – keep products simple and focused on the specific needs of the target membership; rationalise the back book
- Distribution – incentivise the distribution network for cost efficiency and customer effectiveness; digital is not a panacea – it adds to existing distribution costs and is only as effective as the holistic distribution strategy allows it to be
- Operations and Technology – nearly 40 percent of sector leaders indicated that the limitations of current IT systems is the biggest challenge to digitisation; this is often driven by customisation decisions to align technology to 'the way we do things', while industry leaders use the opportunity to digitise and automate inefficient and cumbersome manual processes into a simpler digital operating model

3 Adopt a programmatic approach to cost transformation; piecemeal can erode value

- Avoid the haircut – indiscriminate cost cutting can lead to unintended (and negative) consequences
- Taking the member-value focus (above), group and prioritise addressable cost drivers; identify interventions in terms of immediate, medium and long-term
- Prioritise cost initiatives that will return value to the bottom line (not just redeploy costs) to demonstrate intent, and then use the momentum to drive longer-term cost initiatives
- Coordinate and report centrally, prioritise resources to deliver, and empower leaders to make local decisions within a whole-of-enterprise decision framework for transformation

4 Invest wisely and follow-through on realising benefits from investment

- Focus on metrics that drive valuable investment decisions (e.g. ROI, NPV)
- Follow through on benefit realisation, such as stripping out the legacy and enforce standardisation
- Do not hesitate to lean on partnerships to leapfrog capability development and avoid the cost of non-differentiating functions (even for micro services)

Cost Optimisation

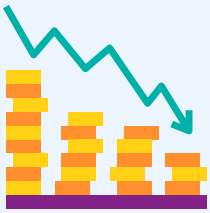
Hilda Carmichael, Partner, Financial Services Sector, KPMG Technology
Bruce Sweeney, Partner, Financial Services Sector, KPMG Enterprise

Where member growth and sustainability used to be the primary business drivers, cost optimisation and long-term resilience represent a new focus for the Mutuals.

Cost optimisation is more than just cost cutting and belt tightening, as these short-term tactics alone will not lead to sustained business success. As a result, it is necessary to consider the effectiveness of your operating model and if your products, channels and markets still make sense in the current environment, and potential future state.

Whilst ensuring sustained profitability is key to maintaining the Mutual sector's resilience, our financial results analysis highlight cost-to-income ratios have continued to increase for Mutuals (2020: 79.7 percent), and remain high when compared to the major banks (2020: 53.2 percent).

Our Mutuals survey participants ranked cost reduction as the fourth key challenge in the next three years – following Cyber security, Productivity improvement, and Digitisation of product channels.



Cost is key in economic response and recovery

The Mutuals continue to face the challenges of shrinking net interest margins and increasing competition.

Amidst a crisis, such as the 2019 bushfire season and the current pandemic, the immediate priority for your business is the safety of your people and members, however long-term resilience also needs to be considered during this economic crisis.

Year-on-year, the Mutuals have focused on delivering value to their members through service and pricing where customer centricity and a community focus has contributed to higher customer satisfaction ratings compared to their competitors. Increasing the member experience by designing products that are centred around customers and getting these to market quickly requires the Mutuals to configure and customise product design. This has brought with it an increase in costs. When balancing the cost vs customer drivers in a growth market, the management of costs and capital is an enabler rather than the driver to achieve sustainable growth. In this economic crisis, cost is key.

COVID-19 has been a catalyst for tactical digital transformation. The Mutuals have had to react quickly to enable remote working, shift to digital channels and transform products and services to meet the changing demands of members. The pandemic has forced financial services organisations to urgently leverage new technologies and ways of working, implementing digital projects in mere weeks that would previously have taken months, if not years, and at significantly greater costs.

Reducing 'points of friction' at the customer, or front office, was nominated as the top cost and customer experience improvement strategy amongst our Mutual survey participants.

Based on the Harvey Nash KPMG CIO Survey 2020, 71 percent of respondents anticipated automation would increase. Businesses want to make their product supply chain and member engagement frictionless, increase velocity and lower cost. Automation is a key enabler of that.

In the short term, the Mutuals will remain focused on supporting their customers and the economy in their recovery. In the medium to longer term, they will have to continue to enhance the member experience (with a focus on digital channels) at the same time as addressing their profitability by accelerating their cost, simplification and operational resilience efforts.

Matching response to your circumstance

To optimise costs, the Mutuals need to ensure achieving cost reduction does not impede growth. Our experience has shown that organisations that invest more time to improve processes can create value more sustainably.

KPMG Connected Enterprise

At KPMG, we work with our clients to first develop a Connected Enterprise view of every aspect of their operations, from the front, middle and back office functions, to technology and fixed and variable costs associated with any outsourcing arrangements. Only then can a cost optimisation strategy be built around each cost category to determine the best cost lever to use. A successful cost optimisation initiative starts with gathering your current cost base and performing a spend analysis. This will help inform your needs and sets a baseline to measure and track success. Using KPMG's Connected Enterprise, banking industry trends and self-diagnostic tool, benchmarking data and access to industry or functional experts may help to improve the identification of the right cost opportunities. A future-ready, Connected Enterprise can drive competitive advantage with an agile supply chain, an improved customer experience (CX), and an aligned and resilient organisation.

What is the KPMG Connected Enterprise?

The KPMG Connected Enterprise is built on a foundation of eight integrated capabilities that help banks unlock costs and value for members and employees. Members passing through complex journeys can use multiple channels to interact, making the tracking and measurement of costs difficult. Becoming a connected enterprise gives banks greater visibility on the end-to-end cost to serve the customer and helps identify points across the enterprise to be strengthened against ever-changing and heightened expectations, whilst also creating resiliency.

How you can identify the right cost optimisation opportunities?

As the Mutuals enter into a period of lower revenue growth, they will need to optimise their cost bases in order to manage profitability. Every business is unique, however, there are common levers any Mutual can identify and pull to optimise costs. These include:

Lever 1: Simplify the Product Portfolio

This requires a member-centric strategy. First, the Mutuals need to evaluate which products are important to maintaining their current member base. And then, using the same assessment criteria, determine which of their products will help expand on that member base. This approach will help differentiate products that deliver actual value to customers.

Cost optimisation through stronger product management requires Mutuals to analyse products from the perspective of members, revenue, and also costs in order to determine which products represent clear differentiators and which are legacy products.

The strategic importance and regulatory obligation of each product will then allow the Mutuals to determine if the product can be removed from the suite of products.

Significant product and systems simplification and rationalisation, including customer migration from, and permanent closure of, backbook products will drive downstream simplification across the Connected Enterprise with the processes, workflow, policies, workers, data and systems required to support it translating into reduced costs.

Cost Optimisation strategy characteristics	
Short Term	– Establish control of miscellaneous spending – Stop or put on hold non-critical projects – Stop or freeze non-critical external spend – Take overdue actions: rationalise your underperforming assets, freeze recruitment – Slow or stop discretionary spend
Medium Term	– Reduce wastage within the supply chain – Develop organisation-wide operational improvement programs – Identify simple process automation opportunities – Resolve unfinished business that can generate or release capital
Long Term	– Rethink the core business and operating models – Develop new service offerings, utilising excess system capacity – Identify 'low cost to serve' markets and develop plans to grow market share – Review the target operating model

Our experience has shown that successful businesses

Consider the business and the **connected enterprise** operating model in delivering digital transformation and cost savings

Understand trade-offs between costs, revenue, impacts on member service and continued regulation compliance and risk

Adjust or eliminate underperforming operations or product portfolios

Prepare to invest in certain cases to get a better outcome

Embed a culture of high performance and cost leadership

Lever 2: Optimise Banking Channels

Acceleration of realignment of branch networks, to bring the branch numbers, hours and staffing in line with current customer needs and behaviour, can have a dramatic impact on costs.

Additionally, members are expecting to be able to use the engagement channel they prefer as an entry point into a process and to have a seamless experience irrespective of the channel they choose. This requires a greater focus on digital origination and customer self-service, coupled with member incentives to use mobile and online banking post-COVID-19. These initiatives, instead of returning to branches and call centres, can go a long way towards helping the Mutuals reduce their cost to serve.

The Mutuals can drive cost optimisation by influencing the channels that customers use. Optimising the lower cost, self-service channels for lower value transactions can allow branches to handle higher value traffic, therefore allowing the branches to engage on more impactful member services, driving greater revenue to the Mutual.

Channel convergence for the Mutuals means that they need to be present intelligently on devices, offer converged channels and revisit ageing call centre infrastructure that is incapable or inefficient in supporting the convergence. They must also refocus their attention on legacy processes and procedures that are a hindrance to enable channel cross selling and improved customer experience.

Lever 3: Alleviate Built-in Waste

The Mutuals, like all banks, need to find ways to shift the burden of routine transactional tasks away from branch staff and into lower-cost channels, such as call centres and quality member self-service.

Common but decentralised back-office activities performed in the branches creates a cascading set of problems such as increased branch work, inflated staffing levels, low value customer needs being over-serviced and low-value activities with error-prone data entries.

A cost optimisation strategy to redesign the branch processes and centralise routine tasks and transfer these from the branch to the back office can result in benefits requiring no new technology (or cost thereof). This includes new and clearly-defined roles, improved support operations both in the branches and the back office, an increase in the customer experience and setting a target increase in processing capacity.

Lever 4: Optimise IT Cost Structures

The effects of COVID-19 have caused many organisations to reconsider the design of their traditional core IT services. In this context, three options are outlined below, all of which can have a significant impact on cost as well as positioning for future resilience.

Option 1 Re-designing core IT
Cloud computing to reduce operating costs, data analytics to personalise member offerings, deploy mobile channels to reach your member, and offer open APIs to other fintech companies to plug into their back-office infrastructures are all technology opportunities to optimise cost by re-designing the core.

Option 2 Optimising your Cyber costs
Cyber cost optimisation capability is designed to analyse capabilities, identify efficiencies, savings, cost re-distribution, and re-investment opportunities across the Cyber Security function. It solves some of the typical challenges driving cost and complexity such as: underutilised or overlapping security tools, and an abundance of security project, inefficiencies and increasing third-party security spend.

Option 3 Re-defining the IT Service Delivery model
Utilising outsourcing and offshoring delivery models have become a part of most companies' IT service delivery model. In the current pandemic environment, it has also meant reviewing contracts to ensure a more resilient future. Within your service delivery model, there are many areas to consider, including location strategy, outsourcing agreements and resource productivity.

Looking ahead to become more resilient

The Mutuals that take a proactive approach will emerge from this crisis stronger and better equipped to adapt and leverage their organisational agility.

In these testing times, operational resilience and an ongoing focus around cost optimisation will be imperative. Cost optimisation, though, does not necessarily mean cost control and cost reduction. A one-off cost saving approach or mindset is unlikely to achieve sustainable value and could result in the Mutual losing its competitive edge. It is important to manage through the entire lifecycle of this crisis – not just the event.

Now is the time for a renewed focus on costs.

Trust Agenda in unprecedented times

Richard Boele, Partner in Charge, KPMG Banarra Human Rights and Social Impact Services
Rita F., Associate Director, KPMG Banarra
Dr. Nicole Gillespie, KPMG Chair in Organisational Trust; Professor of Management at UQ Business School

PLAY VIDEO

It is during heightened periods of crisis and disruption when trust is most needed. However, it is also at this time that trust is most under threat.

Last year, we highlighted that Mutuals have not suffered the crisis of confidence which impacted other parts of the financial services sector in the wake of Hayne's Royal Commission on trust in the broader financial services industry.

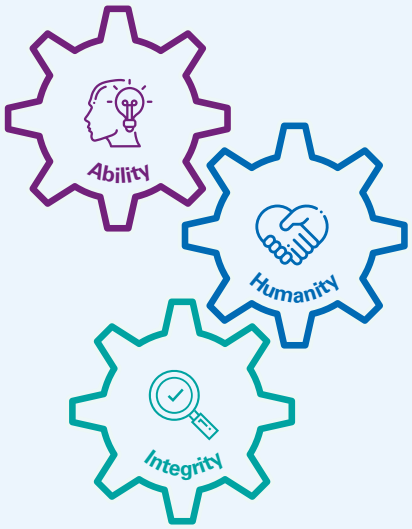
Being customer-owned, Mutuals have been able to consistently position themselves to leverage their strong relationships with customers, and their deep alignment with customer needs, to maintain a reputation for trust through that period of increased public scrutiny. Building a resilient organisation cannot happen without first fostering trust – both with members externally and with staff internally.

Trust within the organisation

The COVID-19 pandemic is an altogether different type of crisis, creating unprecedented uncertainty and unpredictability at a very fast pace. It has forced business leaders, employers and policy makers to make rapid and large-scale changes to meet stakeholders' needs and stay financially viable as they react and respond to the crisis. Most of these changes have directly impacted workers across Australia, many of whom have unfortunately faced reduced pay, limited work hours or lay-offs.

While Mutuals continue to have higher than average customer satisfaction ratings and are maintaining the loyalty and trust of their members, trust within the organisation will be critically important to continue to navigate and emerge from the disruption caused by the pandemic.

Employees in particular, are at their most vulnerable during this unprecedented period and need reassurance that their trust in their employer continues to be warranted. Employees play a critical role in enabling the organisation to navigate through the crisis and continue to adapt to the new normal.



Ability relates to the collective knowledge skills, and competencies that enable the organisation to function reliably and effectively in delivering its products and services and meeting its goals and responsibilities.

Humanity is about exercising benevolence and a 'duty of care' to those affected by the organisation's operations, products and services, and at a minimum 'doing no harm'. Humanity involves having a positive orientation towards stakeholders, beyond profit motives.

Integrity is about an organisation's consistent adherence to commonly accepted ethical principles and moral values, such as honesty, fairness, promise fulfilment, taking responsibility for one's actions, and operating within the law.

For a deeper dive into this model from our 2019 report, click here.

Clearly, trust fostered within the organisation will drive better customer outcomes outside the organisation as employees are empowered to generate positive customer experiences especially during a time of crisis.

Our Model of Organisational Trust

Research shows that stakeholders trust organisations they perceive to have three key characteristics of trust worthiness: '**Ability**', '**Humanity**' and '**Integrity**' – see image on page 31. Proactively demonstrating and role modelling these characteristics during disruption is particularly important for reassuring employees and reducing their feelings of uncertainty and vulnerability.

Lessons learned on preserving trust during times of crisis

Research on organisations that successfully preserved trust during the 2008 Global Financial Crisis highlights three key practices that help organisations reassure and maintain the trust of their internal stakeholders.[7]

1 Build a bridge to the future founded on core values and purpose

Demonstrating integrity by adhering to the organisation's core values and shared purpose throughout the disruption is critical.

Mutuals can draw on and leverage established foundations of trust – their strong values and purpose – to help reduce uncertainty for employees.

This involves communicating openly and transparently with employees about how the crisis is affecting the organisation, what changes are required and how these changes will affect employees.

Developing a shared understanding of what the organisation needs to do to navigate through the crisis, and building a vision for the future which reinforces values and purpose gives employees hope and focus.

This lesson can also apply to a Mutual's customers, given their ownership of the organisation and their personal connection to its purpose and values. A crisis not only can provide an opportunity to deepen and refresh a Mutual's purpose for its employees, but also for its members.

2 Care for and continue to support employees, emotionally and practically

Showing humanity, through empathy and caring for employees enhances engagement, wellbeing and acceptance of change, whether that is as a result of consolidation to gain economies of scale or the COVID-19 crisis.

Mutuals can use simple, authentic actions to show they care for their employees and help them to cope emotionally through the disruption. Acknowledging challenges, having accessible leaders, and protecting jobs, help shore up trust and build resilience amongst employees.

Supporting wellbeing and flexibility in unprecedented times benefits employees and has a flow-on positive impact for members. These initiatives include dedicated time set aside for family and community.

3 Empower employees and treat them fairly

Fostering a sense of empowerment and control amongst employees helps maintain their trust – during disruptive periods. Proactively consulting and involving people in decisions and changes that affect them is critical to empowerment and fair treatment, as is clearly and openly explaining how decisions are made – especially the difficult ones.

This will be particularly important as the economy recovers and Mutuals continue to invest in their capability and technology in order to digitise, consolidate, and transform in multiple ways.

COVID-19 and accelerated uptake in new technologies

The COVID-19 pandemic has accelerated the uptake of advanced technology and investment in artificial intelligence has continued to grow significantly.

As the Mutuals navigate the use and impact of artificial intelligence, they can demonstrate all characteristics of trustworthiness – ability, integrity and humanity – by investing in upskilling and retraining employees – ready for a digitised future. This will help strengthen the organisation's capability and preserve trust.

Artificial intelligence can ***strengthen ability*** and deepen trust with members – through enhanced cyber-security, fraud detection and regulatory compliance, as well as increased customer experience and agility. This framework is not unique to just within the organisation. Mutuals can continue to use this in order to drive trust in all decisions around the customer and community.

Australian Insights on Trust in Artificial Intelligence (AI)

KPMG recently partnered with the University of Queensland to survey Australia's Artificial Intelligence. It is the first survey of its kind to take a deep dive into the public's trust towards AI and expectations of how it is used and governed.

Mutuals can reflect on the implications of these insights for their employees, their members and the public as they continue to adopt new technologies[8].

1 We found that Australians have low trust in AI systems but generally accept or tolerate AI. Only one in three Australians reported that they are willing to trust AI. Only about a quarter of Australians have high confidence in commercial organisations to develop and use AI.

2 We learnt that Australians feel comfortable with some, but not all uses of AI at work. Most Australians (65-79 percent) are comfortable with AI use for the purposes of monitoring organisational security, and task automation and augmentation.

3 But they are less comfortable with the use of AI for monitoring and evaluating employees, or in recruitment and selection processes.

4 Of particular relevance to maintaining trust during unprecedented times, most Australians (59 percent) disagree with the notion that AI will create more jobs than it will eliminate.

5 In the event that their jobs are automated, Australians expect advance notice (93 percent), retraining opportunities (92 percent) and redeployment (89 percent).

Evolving Customer Behaviours

Carmen Bekker, Partner, Customer, Brand & Marketing Advisory
Benjamin Kilpatrick, Director, Management Consulting

PLAY VIDEO

As Australia cautiously emerges from the restrictions caused by COVID-19, it is worth considering what lasting changes we may have to learn to live with. Learning from our experiences and digging deeper into the current situation, below are four changes which we believe have the potential to endure well beyond the pandemic, and which Mutuals and all ADIs will need to respond to. These changes have emerged in a post COVID-19 reality, and Mutuals, and ADIs more broadly, must consider how to leverage these changes to differentiate themselves and grow.

> *"At the moment I am often asked when Corona 'will be over' and when everything will return to normal. My answer is: never. There are historical moments when the future changes direction. We call them bifurcations or **deep crises**. These times are now. The world as we know it is dissolving. But behind it comes a new world, the formation of which we can at least imagine."*
>
> **Matthias Horx** – Futurist

1 Community
Supporting local businesses as purpose driven organisations

2 Back to Basics
Simplify products and consider the genuine 'must haves'

4 Trust
Embed trust in your organisation's purpose

3 Technology
Invest in tools and platforms for tangible value

1 Supporting local community

One of the earliest changes to our behaviour necessitated by the pandemic related to heavy restrictions on movement to comply with various types of 'self-isolation' guidelines. With the sudden closure of many Australian businesses, the social and economic impact of the pandemic has been felt at a very personal and local level.

Many customers responded by supporting local businesses and brands – doing their bit to ensure every dollar spent reasonably went to those nearby. What started at local coffee shops and retailers has ultimately become a larger movement. Customers are posing the question: 'How do I support local business and do the right thing?'

In a recently released KPMG study entitled *Consumers and the New Reality* – 96 percent of Australians said they would be willing to pay more where their spending has a noticeable impact on the local economy. In a COVID-19 world, promoting local takes on a sliding scale at three levels: a local community, a state and a national level.

Community – Mutuals must consider:

- How can we leverage our existing community orientation to broaden our customer base and attract new types of customers?
- How else can we support our local communities and deepen our reputation as purpose driven organisations?

2 Back to basics

In many ways, the pandemic has been a great leveller. Lockdown has broken many long-standing habits, as individuals have been forced to reconsider what is a genuine 'must have'.

Since COVID-19, people are prioritising their basic needs and being mindful of what represents value for their hard-earned dollars. A recent KPMG survey found that 43 percent of customers are now more selective with purchases, and 41 percent feel financially overwhelmed or vulnerable[9].

In this new paradigm, value for money, and its corollary price, is the single most important factor in decision-making, with nearly half of respondents saying that it is more important now than pre-COVID-19. This is closely followed by a greater appreciation for organisations who can get the customer basics right, even in a crisis.

Post lockdown, we expect new customer segments will emerge, separated by their need to group products and services into categories of necessity, due to the psychological impact of COVID-19. This may span from individuals where financial strains will dictate more savvy spending, to others where the unpredictable and sudden lockdown measures may increase opportunistic spend when restrictions are relaxed.

Basics – Mutuals must consider:

- Being customer-owned, are there other ways we can create and deliver 'value for money', aside from competing on scale and price?
- Where do we expect to see vulnerable cohorts emerge from our membership, and how might we ensure their financial well-being?
- How can we accelerate efforts to simplify our products, pricing, and introduce more self-service?

3 Acceleration of technology

Beyond the intimate personal use of technology, the disruption caused by COVID-19 has accelerated digital transformation agendas across the globe. Pre-COVID-19, digital transformation was the top concern among executives[10]. Fast forward and almost overnight organisations were forced to reimagine the way they delivered products and services, the platforms they used, the way they worked and their means of engaging with customers. Pivoting to online channels proved to be a fast and cost-effective solution for many services that were previously delivered face-to-face.

With banking services, across all age groups, we have seen a shift in preferences towards online, with 32 percent of people who previously preferred face-to-face interactions now preferring digital channels. People are telling us that even after current restrictions are lifted, they will continue to use digital channels, especially for interactions related to everyday banking. Consistent with our Mutuals Survey, respondents indicated digitisation of banking as one of the biggest drivers of growth in 2020.

As organisations compete for the customers' attention, what will be the winning strategy?

Customers are telling us they want convenience and availability. This means offering 24/7 support through mechanisms like webchat, call-back options, and providing an omni-channel experience. However, when taking out high-value products, the role of the branch across all ages is still seen as crucial. From our Mutuals survey, we observed a negligible decrease in the number of branches this year.

Moving forward, organisations will need to reassess their channel mix, and balance their digital investments with a persisting physical footprint. Successfully re-tuning the digital experience is important, with one in ten individuals considering switching banks as a result of COVID-19, and of those, over half (53 percent) exploring digital bank alternatives[9].

Technology – Mutuals must consider:

- Has the purpose that each channel serves changed, and how might we re-purpose our call centres and branch networks?
- Are there opportunities to partner with fintechs to level the technology playfield and leapfrog competitors?
- What investments can we make to build a more tangible sense of value in our digital experiences?

Our Mutuals Survey respondents believe that the Top 3 key technological challenges in the next 3 years are:

1. Cyber security
2. Productivity improvement
3. Digitisation of product channels

4 Nurturing Trust

The speed of change at the onset of the pandemic was unsettling for most, and created fear in many. The tension of the individual vs the collective has never been more palpable. For some, fear has been demonstrated through stockpiling. For others, fear drives protectionism, cocooning and risk-averse purchase behaviour, while also extending the decision making and purchasing process for many businesses.

Trust is the fundamental basis of counteracting this fear and uncertainty.

We are seeing trust become increasingly multidimensional and contextual, with customers now paying more attention to what brands stand for and their sustainability, in terms of both environmental impact and whether they will 'act in my best interests'. There is now more questioning: Can I trust my bank to put my well-being before profit? Will my data be safe? Will they behave credibly when it comes to support of the local community and 'the greater good'?

On balance, banks have fared reasonably well with creating trust during the COVID-19 pandemic. Organisations have re-geared their operations to improve responsiveness, and many have proactively communicated the effect of COVID-19 on their service offerings. As a result, the majority of customers trust their bank at least as much as before COVID-19 (87 percent), with 19 percent indicating they now have more confidence in their banking institution.

Successful Mutuals will need to maintain their trust with customers by transitioning cautiously back into 'normality' and persisting with broader community obligations. We are seeing a shift towards customers 'buying into companies' rather than simply 'buying from them'. This means focusing on digital security, personal safety, and prioritising vulnerable cohorts – with commitments that are not 'over-reaching' and can be successfully fulfilled.

Mutuals have always focused on enhancing their bond with the customer and positioning themselves as a trusted brand in their community.

Trust – Mutuals must consider:

— How might we maintain customer trust as COVID-19 support programmes like re-payment holidays, wind back?

— Do all our products, services and operations (and their social impact), support our purpose and engender trustworthiness?

Thinking ahead

As Australia continues to emerge from the COVID-19 crisis – one thing is almost certain, customers will change. We're seeing customers leaning into brands that are providing them with a sense of security and stability – essentially brands that they trust to 'act in their best interests'.

Trust has always been an area of differentiation for the Mutuals. This is an opportune time for Mutuals to take advantage of their unique market positioning and expand their customer base. Moving forward it will be important for Mutuals to:

— Align their inherent strengths and **community** reputation, with what the broader consumer base is now valuing post COVID-19, to attract members outside of their existing base.

— Get the **basics right** consistently. This means setting expectations, delivering on commitments, and delivering simpler more accessible member experiences.

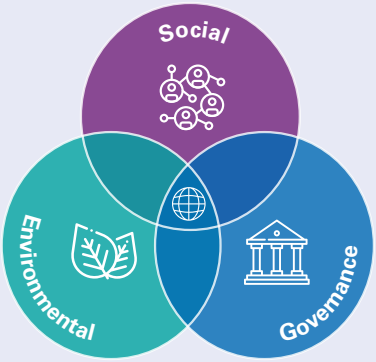
— Pin pointing investments in **technology** tools and platforms that will improve convenience and availability, to ensure that value feels tangible to customers.

— Embed **trust** and be guided by your organisation's purpose, in all levels of decision making and customer interaction.

Increasing focus on Environmental, Social & Governance (ESG) - Summary

The ESG space has evolved significantly in the span of twelve months since the last Mutuals industry review in 2019. The World Economic Forum released its Global Risks Report and for the first time ever, environmental risk has been identified as one of the Top 5 global risks in terms of likelihood. Environmental and societal risks have been identified as fourth out of the Top 5 global risks in terms of impact. The subsequent economic shocks from COVID-19 serve as a stark reminder of the external non-financial threats that can significantly impact on portfolio performance and loan book.

The limbs of ESG can be defined as follows:

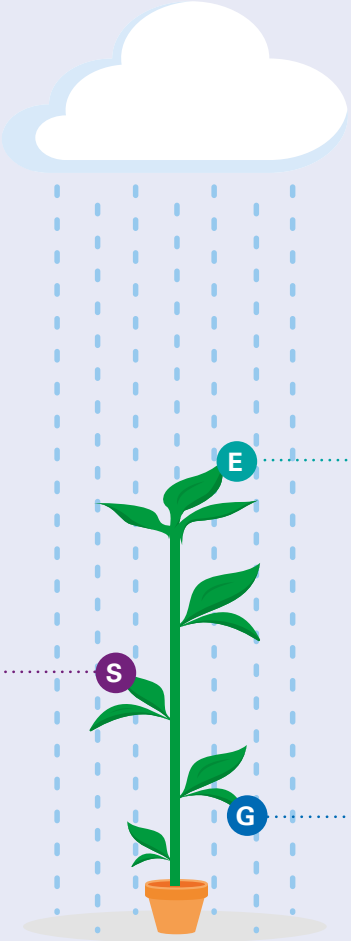


Environmental
criterion looks at how an investee company performs as a steward of the natural environment.

Social
criterion examines how a company manages relationships with its employees, suppliers, customers and the communities in which it operates.

Governance
criterion is concerned with a company's leadership, executive pay, internal controls, externals audits and shareholder rights.

Each of the ESG areas are diverse and continually evolving with the rapidly developing global environment. However, there are **key themes** that have continued to evolve. In our report, we have highlighted key themes across each of the three limbs of ESG, and how Mutuals can be best positioned to understand and adapt to manage the risks these pose to the organisation, ensuring these don't take over.



Environmental – Climate risk and Australian Sustainable Finance Initiative (ASFI)
Understanding how Mutuals can drive sustainable finance through responding systematically to initiatives, including products. Further, understanding how the loan books may be exposed to climate-linked risk and reporting on Mutuals' actions to respond. See Page 39 for further details.

Social – Modern Slavery
Understanding the risk of Modern Slavery like conditions that can exist in supply chains. Navigating how Mutuals can proactively respond to the 'risk to people' this can pose, and opportunities to demonstrate trust built in the community. See Page 41 for further details.

Governance – Sustainable Development Goals (SDGs)
17 Goals set by the UN to achieve by 2030 for all nations including Australia. Understanding the vital role Mutuals can play in responding and positioning the Australian economy for success. See Page 43 for further details.

Increasing focus on Environmental, Social & Governance (ESG)

Mark Spicer, Head of ESG and Responsible Investment, Sustainability Services
Julie Vasadi, Associate Director, Sustainability, Audit, Assurance and Risk Consulting
Samantha Bayes, Manager, Sustainability, Audit, Assurance and Risk Consulting

PLAY VIDEO

Consumer demand for ESG and alignment to their values – a deeper look

The misconduct findings from the Royal Commission into Banking and Finance have seen an increase in the scrutiny of financial services providers and the wider stakeholder outcomes they are responsible for, both positive and negative, rather than the simple binary of profit or loss. The combination of better communication over these outcomes and actionable measures to remediate and prevent future instances will lend confidence to an organisation's claims of responsible and ethical practice. For Mutuals, this is a roadmap showing the growth of responsible investing and the future of investment at large.

Within this context, ESG is being increasingly seen as a sound management framework with its founding principles, focus on broader stakeholder expectations – not just shareholder returns - and longer-term horizons. These principles are synonymous with business resilience, enabling future proofing against external shocks.

A recent joint report in Responsible Investment Association Australasia (RIAA) highlighted key areas and statistics that Mutuals should consider and respond to.

Key themes and Statistics from RIAA	Impacts on Mutuals
Customer values, beliefs and specialisations **87 percent** of Australians expect the money in their bank accounts to be invested responsibly and ethically.	Customers want to invest their money with institutions that are purposeful and aligned to what they believe is just, responsible and ethical, an area of historical strength for Mutuals. Mutuals must continue to listen, understand and respond to their customers in order to deliver on financial products that are aligned with customer values, beliefs and specialisations.
Propensity to act **74 percent** of Australians would consider moving their banking, super or other investments to another provider if they found out their current provider was investing in companies engaged in activities not consistent with their values.	With the imminent changes to Open Banking, customers will be able to more quickly and easily switch banks and find better-suited products in line with their values and interests, a process which was longer and more complicated in the past.
Transparency **4 in 5** Australians would like their super fund and their bank/s to communicate the impacts – positive and negative – their money is having on people and the planet.	Mutuals should continue to develop their ESG reporting in order to evidence relatable and tangible outcomes for their stakeholders. Increasingly, financial institutions are aligning their reporting to broadly accepted frameworks such as the Sustainable Development Goals (SDGs), Taskforce on Climate related Financial Disclosures (TCFD) and Modern Slavery.
Providing options **72 percent** of Australians believe there is a lack of credible ethical and responsible banking options to choose from.	Mutuals can demonstrate that their funding is ethically managed through RIAA certification for their wholesale products to distinguish responsible, ethical and impact investment products and services in Australia and New Zealand. For example: Teachers Mutual Bank Limited (TMBL) has its $1 billion wholesale products certified by RIAA.

Clearly, these are an opportunity for Mutuals to respond and further distinguish their core capabilities and deep community roots. Using these broadly accepted frameworks gives Mutuals the ability to map their loan portfolios against the material ESG themes to measure and target greater positive impact to their stakeholders.

What's changed in 12 months...?

Australian Sustainable Finance Initiative (ASFI)

Since our last Mutuals Review Report in November 2019, the ASFI released its progress report in December 2019 that identified six critical challenges that the Australian financial services sector response must address. These areas continued to reflect the increasing focus on aligning the financial services sector to better support and contribute to sustainability.

1. Leadership, culture and institutional structures;
2. Decision-making and valuation;
3. Policy, regulation and supervision;
4. Frameworks, tools and standards;
5. Unlocking sustainable finance and allocating capital to where it is needed; and
6. Community and consumer interest and expectations.

Mutuals response to ASFI

Given the increasing opportunities open to the financial sector to adopt sustainable finance initiatives and responsible investing practices, the following should continue to be prioritised:

- Consider becoming a signatory to the UN Principles of Responsible Banking or UN Principles of Responsible Investing (UNPRI).
- Develop a systematic approach to ESG that will better inform financial decision-making, manage investment risks and enhance disclosures and transparency.
- Disclose non-financial risks across your business and its activities including climate but also culture, social licence, reputation and trust.
- Continue to innovatively develop sustainable finance solutions. For example: A number of green personal, car or home loans are available providing discounted rates or cash back incentives for green initiatives to customers.
- Sustainability linked loans have been issued recently by Australian banks with the interest rate charged linked to performance against specified ESG criteria.

What's changed in 12 months...?

Climate risks and opportunities

As Australia recovers from the 2019 bushfires, our realisation that risks posed by a changing climate are present, systemic and accelerating is stark. Investors, regulators, customers and communities are increasingly scrutinising the activities of Australian corporates as the financial risks and opportunities related to climate change are becoming more apparent. Prudent corporates are now beginning to assess the risk and opportunities presented by the socio-economic responses to climate change in order to anticipate and mitigate their impacts.

Climate risk reporting is increasingly a focus area for many financial regulators (including ASIC and APRA) as they push regulated entities to consider their exposure to climate risk and report under The Task Force on Climate-related Financial Disclosures (TCFD) framework. Since our last Mutuals Review Report, even more financial regulators are referring to and endorsing, the TCFD framework as the prominent and accepted disclosure framework for addressing and reporting organisations' exposure to climate-related risks and opportunities.

Mutuals response to climate risk

Given the risk that climate change poses to the financial services sector, the following should be front of mind:

- Adopting the TCFD's recommendations and progressing towards alignment of climate-related risk reporting.
- Consider exposure of the mortgage portfolio to:
  i) Regions that are heavily dependent on emissions intensive industries
  ii) Physical risks of climate change
  iii) Develop socially responsible climate risk strategies that support vulnerable customers through climate transition.
- Consider how loan portfolios could be better positioned to mobilise capital to support emerging climate-related opportunities.

Responding to Modern Slavery Legislation

Richard Boele, Partner in Charge, KPMG Banarra Human Rights and Social Impact Services
Mark Lyster, Director, KPMG Banarra
Jean-Louis Haie, Director, KPMG Banarra
Meg Brodie, Director, KPMG Banarra
Ellen Lenczner, Manager, KPMG Banarra

PLAY VIDEO

What is modern slavery?

Modern slavery refers to a range of serious human rights violations, which are also crimes in Australia. The term is used to describe situations where coercion, threats or deception are used to exploit people and deprive them of their freedom. Modern slavery includes trafficking in persons, slavery, servitude, forced marriage, forced labour, debt bondage, the worst forms of child labour, and deceptive recruiting for labour or services.

Did you know?

An estimated 40.3 million people globally – about 70 percent of whom are women and girls - were living in modern slavery in 2016. Closer to home, the Global Slavery Index 2018 estimates that on any given day in 2016[11], there were 15,000 living in conditions of modern slavery in Australia.

Modern slavery risks are not necessarily direct instances of these conditions, but impact can also be captured through use of services and partnerships. Modern slavery risks that Mutuals can be exposed to include:

- Procurement of high-risk goods and services (e.g. cleaning, security services and IT equipment);
- Business lending that may facilitate modern slavery (e.g. construction, labour hire and agriculture);
- Retail banking customers (e.g. child sexual exploitation and domestic violence related payments); and
- Financial activity (e.g. managing bank accounts on behalf of individuals involved in the exploitation and enslavement of workers)

Are Mutuals captured?

The *Modern Slavery Act 2018* (Cth) requires entities with consolidated revenue of $100m or more to submit an annual modern slavery statement on what they are doing to identify and manage modern slavery risk in their operations and supply chain. The New South Wales Government also passed legislation in June 2018 to implement a modern slavery reporting regime in the State for entities that meet specific criteria. Following an inquiry, the Government has committed to seek greater harmonisation with the Commonwealth reporting requirement[12]. In response, many Mutuals need to proactively address issues of harm to people in their operations and supply chain. From the sector, 15 Mutuals have revenue greater than $100m.

Under the Commonwealth reporting requirement, statements are published on a central government registry and require approval of the Board (or equivalent)[13] and the signature of a Director or a responsible member of the entity. Mutuals that fall outside the threshold can demonstrate good practice by reporting through a voluntary 'opt in' mechanism.

Given investment and lending activity is explicitly included in the scope of the Act, and public and investor scrutiny is increasingly directed towards financial actors, Mutuals need to respond, beyond basic minimum compliance. Below, we highlight some risks, yet opportunities in responding.

Risks of not responding

Risk to business

Changing stakeholder expectations has seen the mainstreaming of ESG risk management guidance, improved company disclosures and the advance towards best practice. Investor action also contributed to an increase in ASX 200 companies reporting on sustainability at a 'leading' level and lobbying to introduce mandatory human rights due diligence measures.

With this additional scrutiny, lenders themselves increasingly need to demonstrate that they follow the same rigorous ESG

principles that they ask of investees and borrowers. While scrutiny over human rights risks was once only directed at a few 'ethically-leaning' financial actors, the reporting requirement is now likely to make this common practice[14].

Mutuals have always been able to clearly link their value proposition to align with both their customers and community through their trust agenda. Protecting that trust from violations of 'good conscience' behaviour such as modern slavery becomes vital.

A loss of trust in the banking sector was particularly evident following 2018's Banking Royal Commission where the industry faced scrutiny into unethical practices. It reiterated the importance of public trust, as well as Board and executive accountability.

Risk to people

Legislative developments have been driven and informed by the 2011 *United Nations Guiding Principles on Business and Human Rights (UNGPs)*[15] which confirmed the importance of human rights due diligence frameworks. A key difference with human rights due diligence is that it focuses on risks to people rather than risks to business. Taking a risk to people approach asks the risk question in a different way – how might people be harmed as a result of this business activity, decision or purchase?

Modern Slavery Risk Factors	
Vulnerable Populations — Migrant workers — Base-skill workers	**High Risk categories** — Service procurement — Goods not for resale — Raw materials
High Risk Business Models — Labour hire and outsourcing — Franchising — Seasonality — Aggressive pricing	**High Risk Geographies** — Conflict — Weak rule of law — Corruption — State failure to protect human rights

Where multiple high-risk factors co-exist, there is a higher likelihood that actual harm is experienced, and additional controls are required to ensure that risk does not become harm. Considerations around the level of influence, alongside the severity and ability to remediate potential impacts, can help ADIs guide mitigation actions and response.

While the legislation looks specifically at modern slavery risks, considering the full spectrum of human rights risks will enhance the credibility of modern slavery responses and statements, and will support Mutuals to meet this increasing stakeholder expectation and potentially reduce reputational damage.

Opportunities of responding

While poor ESG risk management can erode public trust, demonstrating integrity through transparent reporting, and taking responsibility for human rights impacts will enhance perceptions of trustworthiness[16]. Mutuals already have a strong community bond with their customers, and there is an opportunity to further distinguish.

Making a public commitment to addressing modern slavery practices in operations and supply chains can be an opportunity for companies to rebuild public trust. For many companies, addressing modern slavery also aligns with their purpose, culture and values, an alignment that is often important for employees and customers alike and especially so for Mutuals and their alignment of organisational purpose with customers' interests.

Road map

The modern slavery legislation requires Mutuals to report on the risks of modern slavery across both supply chains and operations. Critical for the financial services sector is that the broad definition of 'operations' intends to cover financial lending and investments.

Applying the UNGPs framework to addressing modern slavery, or human rights more broadly, depending on the Mutuals risk appetite and level of ambition, could see it follow the below steps:

Step 1: Policy commitment

— Commit to respecting human rights

— Establish policy to respond

Step 2: Due Diligence

— Identify, prevent, mitigate and account for how the business addresses human rights risks

— Map operations and supply chains

— Implement measures

— Monitor measures and report with annual Modern Slavery statement

Step 3: Remediation

— Respond to instances of harm

— Respond without jeopardising safety of victims

— Establish trusted grievance mechanisms

— Early warning system

Responding proactively through leveraging human rights frameworks to highlight risks can provide Mutuals opportunity to further distinguish themselves from peers and protect trust.

Sustainable Development Goals for Mutuals

Donna O'Neill, Associate Director, Corporate Citizenship

PLAY VIDEO

The Sustainable Development Goals (SDGs) are 17 goals set by the United Nations General Assembly as a universal call to action to end poverty, protect the planet and ensure all people enjoy peace and prosperity by 2030. This is applicable to all nations and people, seeking to address inequality and leave nobody behind.

The third limb of ESG (Governance) has grown significantly in prominence in the last decade. So much so that customers are starting to embed these considerations when selecting their financial service provider.

The increased focus on governance has been crucial for the financial service sector to appropriately service their customers by fulfilling their immediate and future financial goals. A top down approach has been taken by the wider banking industry, including the Mutuals, where the focus on governance has been implemented throughout their entire organisation down to the individual products and services that they offer.

There is no doubt that the Mutuals play a vital role for the customer, and this role extends beyond just making a positive contribution in the community (an area where the Mutuals have been able to distinguish themselves).

Mutuals have always positioned themselves as 'community- centric' with a number of new community initiatives (see page 46 of our report for Community highlights in 2020).

There is now also an increasing need for the Mutuals to be transparent and clear on how their products and services will help achieve global SDGs. Each entity has a part to play, with more vital organisations playing bigger roles to empower and drive change.

Delivering on the SDG targets

The 17 SDGs are integrated, acknowledging that action in one area will affect outcomes in another. The achievement of the SDG targets requires a significant investment of time and resources. To date there has been mixed success in Australia, and globally. Referencing the 'Transforming Australia: SDG Progress Report' released in 2018, Australia is performing relatively well in health (SDG 3) and education (SDG 4). However, the results for reducing inequalities (SDG 10) and climate action (SDG 13) are notably poor. There is a considerable way to go in achieving the other goals and Australia will not fulfil its commitment to achieving the Sustainable Development Goals without a major change from the current business as usual approach.

> *"There's strong progress in the areas of health and education, but poor performance in addressing inequality, tackling climate change and housing affordability. The 'Transforming Australia' report also highlights challenges in achieving Australia's economic goals with relatively low investment in research, development and innovation, increasing underemployment and high levels of household debt"*
>
> **Professor John Thwaites** – MSDI Chair

The 17 Sustainable Development Goals

Source:https://www.un.org/development/desa/disabilities/envision2030.html

Opportunities for the broader FS industry overall and how Mutuals can respond

Many Mutuals are asking themselves how they can make an impact on the SDGs. Due to their size and agility in operations, Mutuals are well positioned to respond and contribute. Delivering on any of the 17 goals cannot be achieved without a wider Financial Service sector response to fuel change and drive value. The Financial Services industry is a vital enabler for the real economy. It supports improved economic well-being which is then translated into enhancing the ability of families and Governments in achieving better social outcomes. The biggest opportunity for the Mutuals is to be a catalyst for change, and to drive value, aligned with the following four themes[17]:

1. Access

Increasing financial inclusion for individuals, small and medium sized enterprises and Governments. This includes access to secure payment and remittance facilities, savings, credit and insurance. These core financial services facilitate secure payment for goods and services, including regional and international trade, and enable smoothing of cashflows and consumption over time. This helps to provide financial protection and support more efficient allocation of capital.

2. Investment

Invest in, finance and insure renewable energy and other infrastructure projects. There is an opportunity to partner and service stakeholders in the renewable sector by providing people working in these industries new and innovative green products and services, such as those offered by Police Bank for solar hot water systems, rainwater tanks and green vehicles.

3. Risk management

Leveraging risk expertise to directly influence customer behaviour and to create more resilience in the economy. Mutuals can develop innovative pricing models which incentivise more sustainable living and production, share non-proprietary risk data, risk analysis and risk management expertise to inform public policy and practice.

4. Stakeholder influence

Positively influencing the ESG practices of corporate clients and investee companies by adopting good practice principles, policies and risk frameworks to guide business transactions and investments – particularly on sensitive sectors or issues; pricing to reflect ESG risks and opportunities; and promoting active investor stewardship.

In realising these shared value opportunities, multi-stakeholder partnerships and collaborations will become increasingly important. Many solutions will include blended finance (e.g. combining a financial institution's finance with third party concessional funds), innovative financing mechanisms such as development and climate bonds, and application of new technologies.

Financial Inclusion Action Plan (FIAP)

The Financial Inclusion Action Plan (FIAP) program is an initiative for organisations from diverse sectors to collaboratively work towards providing more opportunities for greater financial inclusion and resilience in Australia.

Since the program's implementation in 2016, the FIAP program has been able to create a platform that has encouraged over 40 organisations to join, committed to over 630 action to realise greater inclusion and obtained a completion or progression on 87 percent of these actions. The ongoing efforts are aimed towards assisting the millions of Australians who are severely, or completely excluded from, access to financial institutions.

Continual success of the FIAP program will be driven by expanding the footprint to new sectors and then integrating the actions which promote greater financial inclusion to the industry norm for the wider community. Having a member and community focused framework, Mutuals have already begun and are in a strong position to adopt this initiative.

2020 was noted as the beginning of the 'decade to deliver'. There is critical momentum of activity and the Sustainable Development Goals are accelerating a convergence in societal demands across corporate and government action, and the recognition that market potential is wider than pure economics and financial benefit.

Community highlights

Growing a healthy, resilient community

12
Mutuals operate their own charities or foundations

$21.5m
In donations and fundraising raised for 2020

$1.1m
Pledged for bushfire appeals

60%
Of Mutuals in our survey believe community involvement is a key differentiator to their business

578
Community events and organisations supported

Environmental & Social

Bank Australia integrated Indigenous Land Management to their customer-owned Conservation Reserve through an Indigenous trainee program. This saw the implementation of traditional cool burns – a gentle practice of cultural importance for the traditional Owners and Elders used to reduce pests and fire risks.

Qudos Bank continues to offset carbon emissions of one fleet per employee and all work-related air travel with Greenfleet. This year, 3,803 native trees were planted to establish a biodiverse forest and offset 1,019 tonnes of CO2-e emissions.

Greater Bank commemorated their 75th anniversary through planting 75,000 trees across areas where its customers and communities reside in order to tackle climate change.

Financial Literacy

Beyond Bank continues to promote financial literacy through 'Beyond Money', a program which encourages students in Years 5 – 7 to gain an understanding of earning, saving and spending money by earning spare fictional income that can be converted to a reward at the end of the program.

The Mutual Bank's Bank@School program promotes the importance of saving amongst students by sending representatives to schools once a week to collect Bank@School deposit books and deposit envelopes.

Newcastle Permanent Building Society incentivises savings habits from a young age by offering children award-winning bank accounts featuring relatively high interest rates.

Disadvantage

CUA collaborated with Australian Red Cross and Infoxchange, in launching 'Connected Future', a program that seeks to improve the digital and financial capability of vulnerable community members – including older Australians who are digitally isolated, low income households, people experiencing unemployment as well as those living in remote areas.

Regional Australia Bank has supported BackTrack since the organisation's inception in 2006 to provide guidance and education programs for at-risk youth from regional communities, to help them develop work-based skills and broaden their employment prospects.

Heritage Bank opened branches early to create a safe banking environment for the elderly in the community during COVID-19.

Credit Union SA was the major sponsor for Zahra Foundation's 'Women on the Run 2020', a run that created awareness and raised funds for women and children fleeing domestic or family violence.

Professional Legacy

Teachers Mutual Bank empowered the regional and rural teaching community by providing 30 teachers from regional, rural and remote schools with accredited professional learning opportunities through the Bell Shakespeare Regional Teacher Mentorship - an initiative that seeks to give teachers equal development opportunities and enrich student learning.

P&N Bank sponsors Nine News WA Police Excellence Awards and WA Nursing & Midwifery Excellence Awards to celebrate the exceptional dedication and service excellence of the community-serving professional groups.

Defence Bank cares for the Australian Defence Force Veterans by funding 'Defence Community Dogs', a program that rescues abandoned dogs and trains them as assistance animals. These assistance animals are then provided to improve the lives of serving and veteran members suffering from post-traumatic stress disorder and related conditions, free of charge.

Going Digital

RACQ created an online competition to continue celebrating Queensland's proud motoring heritage following the cancellation of MotorFest 2020 due to health concerns surrounding COVID-19.

People's Choice Credit Union's Community Lottery is going 100 percent digital in 2020 - replacing the previous arrangement to physically sell, count and return tickets, and effectively accommodating social distancing requirements.

Coastline Credit Union launched a digital marketing package giveaway initiative to three Coastline business customers in each of the valleys they operate in (Hastings, Macleay & Manning) in efforts to support the local business community who have faced difficulties including bushfires and COVID-19.

Appendix

Financial results: 2020 survey participants

The following table contains key financial data[18] of the Mutuals included in our report.

Company Name	Period[19,20]	Net Assets[21] $'000	Total Assets $'000	Total Deposits[22] $'000	Operating Profit Before Tax[23] $'000	Capital Adequacy Ratio[24] %	Return on Equity[25] %	Cost to Income Ratio[26] %
Australian Military Bank Limited	**Jun-20**	**98,201**	**1,461,121**	**1,311,949**	**3,510**	**15.11%**	**2.5%**	**83.5%**
	Jun-19	95,783	1,387,315	1,239,955	5,845	15.21%	4.4%	79.8%
Australian Mutual Bank Ltd[27]	**Jun-20**	**175,921**	**1,658,624**	**1,458,238**	**116**	**21.53%**	**0.1%**	**97.9%**
Endeavour Mutual Bank[27]	Jun-19	87,648	645,654	548,675	2,575	26.74%	2.2%	85.9%
Sydney Mutual Bank[27]	Jun-19	87,369	933,985	833,583	2,192	17.33%	1.8%	88.3%
Australian Unity Bank Limited	**Jun-20**	**75,005**	**1,133,863**	**1,055,989**	**2,667**	**14.43%**	**2.6%**	**87.9%**
	Jun-19	65,148	886,022	811,160	3,602	16.07%	3.9%	84.8%
Bank of us	**Jun-20**	**75,298**	**1,148,823**	**902,196**	**3,754**	**14.54%**	**3.8%**	**79.7%**
	Jun-19	72,511	993,179	753,985	3,167	15.87%	3.2%	84.4%
Bank Australia Limited	**Jun-20**	**554,601**	**7,201,302**	**5,917,585**	**27,111**	**15.81%**	**3.6%**	**73.5%**
	Jun-19	533,218	6,332,262	5,275,948	32,778	16.39%	4.4%	72.8%
Bank First	**Jun-20**	**233,070**	**2,858,727**	**2,604,343**	**13,341**	**15.62%**	**4.1%**	**79.3%**
	Jun-19	221,432	2,690,195	2,448,483	15,522	15.90%	5.2%	75.0%
BankVic[28]	**Jun-20**	**195,721**	**2,308,025**	**2,030,854**	**14,000**	**18.10%**	**5.3%**	**70.5%**
	Jun-19	185,636	2,062,823	1,850,261	16,054	18.50%	6.2%	71.1%
Beyond Bank Australia[29]	**Jun-20**	**549,438**	**7,072,124**	**5,318,909**	**35,292**	**17.09%**	**4.7%**	**77.7%**
	Jun-19	509,127	6,196,006	4,672,672	29,322	17.43%	3.9%	80.6%
Nexus Mutual[29]	Jun-19	19,599	348,335	325,139	1,589	13.95%	6.1%	77.6%
Coastline Credit Union Ltd	**Jun-20**	**44,206**	**623,884**	**568,403**	**4,345**	**14.08%**	**7.3%**	**75.6%**
	Jun-19	41,063	537,962	490,669	4,505	14.09%	8.3%	70.3%
Community First Credit Union	**Jun-20**	**96,087**	**1,137,889**	**1,006,146**	**1,169**	**14.90%**	**1.1%**	**94.3%**
	Jun-19	92,810	1,097,498	994,652	1,433	15.10%	1.3%	94.0%
Credit Union Australia Limited	**Jun-20**	**1,026,323**	**19,497,108**	**11,078,692**	**48,187**	**14.38%**	**3.7%**	**76.7%**
	Jun-19	983,084	17,435,211	10,587,500	59,845	14.30%	4.0%	75.7%
Credit Union SA Ltd	**Jun-20**	**108,795**	**1,471,494**	**1,072,056**	**3,044**	**18.49%**	**2.2%**	**85.8%**
	Jun-19	105,788	1,281,111	1,065,309	5,327	17.98%	3.7%	82.2%
Defence Bank Limited	**Jun-20**	**188,979**	**2,759,930**	**2,204,707**	**14,322**	**13.90%**	**5.5%**	**73.3%**
	Jun-19	179,243	2,500,301	2,092,438	14,346	14.30%	5.8%	73.1%
Family First Credit Union Limited	**Jun-20**	**12,919**	**172,089**	**151,417**	**912**	**15.30%**	**5.3%**	**79.0%**
	Jun-19	12,290	157,329	139,564	1,022	15.80%	6.3%	79.4%
G&C Mutual Bank Limited	**Jun-20**	**116,528**	**1,294,383**	**1,124,736**	**8,531**	**16.91%**	**5.5%**	**70.3%**
	Jun-19	110,480	1,193,999	1,022,537	9,316	17.11%	6.1%	64.7%
Gateway Bank Ltd	**Jun-20**	**107,458**	**1,091,349**	**797,948**	**3,866**	**19.84%**	**2.7%**	**72.8%**
	Jun-19	104,849	1,122,905	858,182	3,011	19.10%	2.0%	78.3%
Geelong Bank[30]	**Jun-20**	**11,105**	**161,419**	**146,034**	**500**	**14.75%**	**3.5%**	**82.5%**
	Jun-19	10,690	144,889	132,709	509	15.30%	3.6%	84.5%
Greater Bank Limited	**Jun-20**	**570,678**	**7,519,960**	**6,449,234**	**33,168**	**17.71%**	**4.1%**	**79.2%**
	Jun-19	548,264	7,161,631	6,141,175	44,740	17.77%	5.9%	73.8%

Company Name	Period[19,20]	Net Assets[21] $'000	Total Assets $'000	Total Deposits[22] $'000	Operating Profit Before Tax[23] $'000	Capital Adequacy Ratio[24] %	Return on Equity[25] %	Cost to Income Ratio[26] %
Heritage Bank Ltd	**Jun-20**	**610,593**	**10,738,948**	**8,423,323**	**51,672**	**14.83%**	**6.1%**	**77.3%**
	Jun-19	575,726	10,085,055	7,738,886	61,708	14.42%	7.8%	71.5%
Horizon Credit Union Ltd	**Jun-20**	**27,419**	**429,639**	**388,945**	**1,692**	**14.02%**	**4.7%**	**86.0%**
	Jun-19	26,210	375,148	344,165	1,868	14.53%	5.4%	84.2%
Hume Bank Limited	**Jun-20**	**85,142**	**1,341,934**	**1,240,544**	**5,700**	**14.38%**	**4.7%**	**76.1%**
	Jun-19	80,848	1,208,275	1,112,521	6,913	14.38%	6.4%	77.6%
Illawarra Credit Union[31]	**Jun-20**	**45,951**	**651,884**	**588,083**	**827**	**15.96%**	**1.4%**	**94.6%**
	Jun-19	45,322	644,412	593,043	1,638	17.73%	2.6%	89.0%
IMB Limited[32]	**Jun-20**	**411,677**	**6,786,590**	**5,871,469**	**37,685**	**16.00%**	**6.8%**	**70.1%**
	Jun-19	362,708	6,077,077	5,266,418	45,401	15.50%	9.0%	66.1%
Hunter United Employees' Credit Union Ltd[32]	Jun-19	24,623	333,350	306,752	284	14.62%	0.8%	96.4%
Lysaght Credit Union	**Mar-20**	**8,893**	**94,715**	**82,594**	**316**	**19.78%**	**2.6%**	**82.0%**
	Mar-19	8,683	88,142	78,608	404	19.77%	6.7%	78.0%
Macarthur Credit Union Ltd	**Jun-20**	**25,649**	**282,529**	**254,557**	**357**	**18.64%**	**1.0%**	**93.9%**
	Jun-19	25,317	253,844	225,869	195	20.03%	0.6%	95.3%
MOVE Bank[33]	**Jun-20**	**67,068**	**663,748**	**579,384**	**2,011**	**21.17%**	**2.2%**	**84.7%**
	Jun-19	65,508	671,203	603,904	2,348	20.66%	2.7%	79.0%
The Mutual Bank[34]	**Jun-20**	**53,081**	**840,164**	**688,975**	**4,660**	**14.97%**	**6.6%**	**74.4%**
	Jun-19	49,678	764,494	647,308	6,491	15.17%	11.0%	72.2%
Newcastle Permanent Building Society Ltd	**Jun-20**	**1,018,386**	**11,101,344**	**8,773,603**	**43,966**	**21.20%**	**3.6%**	**76.6%**
	Jun-19	982,670	10,832,330	8,478,794	53,178	20.10%	3.7%	71.7%
Northern Inland Credit Union Ltd	**Jun-20**	**40,622**	**355,250**	**303,955**	**1,689**	**19.83%**	**3.2%**	**81.8%**
	Jun-19	39,357	313,542	267,586	1,417	22.85%	2.7%	86.9%
Orange Credit Union Ltd	**Jun-20**	**27,042**	**230,024**	**201,516**	**330**	**23.18%**	**0.9%**	**92.3%**
	Jun-19	26,916	213,868	185,396	887	22.75%	2.5%	87.6%
P&N Bank[35]	**Jun-20**	**445,041**	**6,182,148**	**4,964,141**	**4,500**	**14.84%**	**0.7%**	**85.3%**
	Jun-19	290,645	4,268,098	3,176,461	14,907	14.93%	3.6%	82.1%
Bananacoast Community Credit Union[35]	Jun-19	151,036	1,702,734	1,531,396	14,700	15.64%	7.3%	73.2%
People's Choice Credit Union[36]	**Jun-20**	**638,182**	**9,447,487**	**6,743,585**	**31,206**	**14.32%**	**3.5%**	**84.2%**
	Jun-19	618,829	8,810,188	6,421,521	33,126	15.07%	3.5%	85.4%
Police Bank Ltd	**Jun-20**	**204,600**	**2,154,200**	**1,789,600**	**800**	**18.27%**	**0.2%**	**93.3%**
	Jun-19	203,300	2,016,500	1,690,600	4,300	19.12%	1.2%	90.2%
Police Credit Union Limited	**Jun-20**	**88,831**	**1,173,912**	**1,042,726**	**7,335**	**14.00%**	**6.0%**	**70.6%**
	Jun-19	83,314	1,135,104	1,039,990	6,931	14.04%	6.0%	76.0%
Q Bank	**Jun-20**	**82,519**	**886,041**	**722,883**	**2,557**	**20.77%**	**2.3%**	**86.2%**
	Jun-19	80,656	857,887	730,571	3,579	20.71%	3.3%	82.2%
Qudos	**Jun-20**	**284,913**	**4,486,494**	**3,993,780**	**21,993**	**14.61%**	**5.6%**	**63.5%**
	Jun-19	268,337	4,038,284	3,606,457	24,931	14.99%	6.7%	66.2%
Queensland Country Credit Union	**Jun-20**	**179,466**	**2,872,031**	**2,114,032**	**7,820**	**15.73%**	**3.1%**	**90.1%**
	Jun-19	174,525	2,403,600	2,003,706	7,451	16.16%	3.1%	89.5%
RACQ Bank	**Jun-20**	**184,414**	**2,445,627**	**2,102,654**	**(14,101)**	**15.81%**	**(6.1%)**	**125.2%**
	Jun-19	159,419	2,121,755	1,791,379	(15,793)	15.36%	(7.8%)	133.2%
Regional Australia Bank[37]	**Jun-20**	**173,903**	**2,348,652**	**2,146,122**	**10,887**	**15.37%**	**4.4%**	**83.2%**
	Jun-19	124,821	1,517,596	1,372,558	12,539	15.82%	7.4%	73.8%
Holiday Coast Credit Union[37]	Jun-19	45,340	631,459	578,771	2,295	14.66%	3.6%	88.6%
South West Slopes Credit Union	**Jun-20**	**22,443**	**192,164**	**168,318**	**622**	**22.24%**	**1.7%**	**90.3%**
	Jun-19	22,070	176,226	151,938	889	26.60%	3.0%	86.2%

Company Name	Period[19,20]	Net Assets[21] $'000	Total Assets $'000	Total Deposits[22] $'000	Operating Profit Before Tax[23] $'000	Capital Adequacy Ratio[24] %	Return on Equity[25] %	Cost to Income Ratio[26] %
Southern Cross Credit Union	**Jun-20**	**58,974**	**639,290**	**572,864**	**3,720**	**18.40%**	**4.7%**	**71.5%**
	Jun-19	56,243	578,014	515,770	4,321	19.00%	5.9%	67.1%
Summerland Credit Union	**Jun-20**	**63,861**	**847,832**	**762,555**	**2,936**	**15.28%**	**3.3%**	**83.1%**
	Jun-19	61,567	748,489	653,836	4,550	16.47%	5.3%	79.0%
Teachers	**Jun-20**	**574,465**	**8,140,525**	**6,863,284**	**37,995**	**15.30%**	**4.6%**	**76.0%**
	Jun-19	548,549	8,041,748	6,570,030	38,649	14.81%	5.0%	76.9%
The Capricornian	**Jun-20**	**26,702**	**365,672**	**335,112**	**2,278**	**14.71%**	**6.4%**	**75.4%**
	Jun-19	25,137	348,084	319,676	2,267	14.03%	6.8%	77.8%
Traditional Credit Union	**Jun-20**	**5,421**	**17,642**	**11,493**	**551**	**117.23%**	**7.9%**	**89.8%**
	Jun-19	5,008	14,804	9,125	527	126.22%	15.3%	90.8%
Unity Bank	**Jun-20**	**115,050**	**1,344,194**	**1,162,652**	**3,035**	**16.13%**	**2.0%**	**85.2%**
	Jun-19	109,855	1,222,335	1,073,067	5,909	16.50%	4.0%	80.7%
Warwick Credit Union	**Jun-20**	**26,748**	**366,782**	**324,980**	**1,455**	**14.40%**	**1.5%**	**83.6%**
	Jun-19	25,987	310,755	264,345	1,088	15.42%	2.7%	86.4%

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

Endnotes

1. Loan deferrals calculated based on APRA's Temporary loan repayment deferrals due to COVID-19, June 2020.
2. Australian Unity Bank's credit growth outstripping rest of market, Australian Broker, 12 March 2020. Link here.
3. Average capital adequacy ratio excludes a Mutual as an outlier.
4. For non-interest income, one-off items for a Mutual has been excluded.
5. Scope of analysis was limited to the forty-seven largest of sixty mutual banks; full list of banks included in the analysis has been provided in the appendix.
6. The evolving mortgage market, KPMG, October 2020. Link here.
7. Gillespie, N., Searle, R., Gustafsson, S., Hope, Hailey, V., 2020. Preserving employee trust during crisis. Behavioural Science & Policy. Link here.
8. Lockey, S., Gillespie, N., & Curtis, C. (2020). Trust in Artificial Intelligence: Australian Insights. The University of Queensland and KPMG Australia. doi.org/10.14264/b32f129
9. Consumers and the New Reality, KPMG, September 2020. Link here.
10. Digital transformation top CEO concern for 2020, KPMG, December 2019. Link here.
11. International Labour Organization and the Walk Free Foundation in partnership with the International Organization for Migration, Global Estimates of Modern Slavery, 2017. Link here.
12. NSW Government, 'Modern Slavery', October 2020. Link here.
13. Under the Modern Slavery Act 2018 (Cth), s 13(2)(c) the entity's principal governing body must approve modern slavery statements.
14. For further commentary on the role and perspective of investors in this regard, see Australian Council of Superannuation Investors, 'Modern Slavery: Rights Risks and Responsibilities – A Guide for Companies and Investors, February 2019, link here, and Responsible Association Australia, 'Modern Slavery Reporting – Guide for Investors', November 2019, link here.
15. Guiding Principles on Business and Human Rights, United Nations, 2011. Link here.
16. A practical guide to organisational trust, KPMG, November 2019. Link here.
17. SDG Industry Matrix, United Nations Global Compact, KPMG, September 2015. Link here.
18. 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 case, KPMG has adjusted a number of balances to reflect a significant one-off event.
19. All figures for the current and prior year are reported under AIFRS and in Australian dollars.
20. All of the results in the report were for a 12-month period.
21. Net assets include other equity interests.
22. Total Deposits is taken from the balance sheet and includes all deposits, such as retail, non-retail and other deposits.
23. Operating profit before tax is before outside equity interests.
24. Capital adequacy ratio has been calculated under the APRA's risk based measures.
25. Return on equity has been calculated as profit after tax as a percentage of average net assets.
26. Cost-to-income ratio has been calculated as operating expenses as a percentage of operating income.
27. In October 2019, Sydney Mutual Bank merged with Endeavour Mutual Bank Ltd to form Australian Mutual Bank Ltd.
28. Registered name is Police Financial Services Limited.
29. In March 2020, EECU Ltd (trading as Nexus Mutual) merged with Community CPS Australia (trading as Beyond Bank Australia).
30. Ford Co-operative Credit Society Ltd. trading as Geelong Bank
31. Community Alliance Credit Union Limited trading as Illawarra Credit Union.
32. In April 2020, Hunter United Employees' Credit Union merged with IMB Ltd.
33. Railway Credit Union Ltd trading as MOVE Bank.
34. Maitland Mutual Limited trading as The Mutual Bank.
35. In November 2019, Bananacoast Community Credit Union merged with Police & Nurses Ltd.
36. People's Choice Credit Union, a trading name of Australian Central Credit Union Ltd.
37. In July 2019, Holiday Coast Credit Union merged with Regional Bank Australia.

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