

Auswide Bank Ltd

Update

Key Rating Drivers

IDRs Driven by VR: The Long-Term Issuer Default Rating (IDR) of Auswide Bank Ltd is driven by its Viability Rating (VR), which is in line with the implied VR under Fitch Ratings' *Bank Rating Criteria*. The IDR reflects a business model and risk profile that focuses on low-risk residential mortgages, which has resulted in relatively stable asset quality and earnings over a sustained period. These factors are offset by the bank's small franchise and market share.

Slowing GDP Growth: We expect the operating environment for Australian banks to remain stable and consistent with the 'aa-' factor score despite our expectation for slowing GDP growth through the remainder of 2023 following the sharp rise in interest rates throughout 2022 and three rate rises this year to tackle high inflation. Fitch believes that low unemployment, combined with conservative loan underwriting, should limit losses for the banks.

Concentrated but Stable Business Model: Auswide's national market share of around 0.2% for mortgages and household deposits remains a weakness for the VR. The small market position means it has limited competitive advantages and generally acts as a price-taker. Auswide's size and earnings would imply a 'bb' category score for business profile. However, Fitch believes the bank's low-risk and stable business model, which focuses on traditional banking activities, offsets the weaker market position, and supports the business profile score of 'bbb'.

Modest Weakening in Asset Quality: Fitch expects slowing GDP growth and rising interest rates to result in a manageable weakening in Auswide's asset quality over the next two years. Low unemployment and the bank's conservative loan underwriting focused on lower-risk mortgages should continue to support sound asset-quality performance.

Auswide has low exposure to interest-only and investor loans but a high reliance on a broker channel to drive growth. This risk is mitigated by centralised assessment of mortgage applications. The asset-quality factor score of 'a-' is below the category implied score of 'aa', as we apply a downward adjustment to reflect geographic and product concentration.

Stable Earnings: Fitch expects increasing earnings headwinds for the remainder of the year. However, the transition to the Australian Prudential Regulation Authority's new capital rules since the start of 2023 should support metrics at around current levels. We anticipate some pressure on net interest margin and for high investment costs to remain elevated.

The earnings and profitability factor score of 'bbb+' is below the implied 'a' category score, as we apply a downward adjustment to reflect low revenue diversification due to the heavy focus on residential mortgage lending.

Adequate Capital Position: We regard Auswide's capital as adequate for its ratings and believe the common equity Tier 1 (CET1) ratio – 10.7% at end-December 2022 (1HFY23) – will rise moderately following the bank's transition to the regulator's new capital rules. The capitalisation and leverage score of 'bbb+' is lower than the implied 'a' category score, as we adjust downwards for Auswide's small absolute size.

Modest Wholesale Funding Reliance: The core metric, loans/customer deposits (FYE22: 125%), may weaken modestly if strong loan growth continues, but we expect the ratio to remain supportive of the 'bbb' score. Auswide uses mainly deposit funding, but it is more reliant on wholesale funding than similarly rated domestic peers. Management of wholesale funding and liquidity appears sound. The 'bbb' funding and liquidity score is below the implied 'a' category score, as we adjust downwards for the bank's deposit structure and small deposit franchise.

Ratings

Foreign Currency

Long-Term IDR	BBB+
Short-Term IDR	F2

Viability Rating	bbb+
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Government Support Rating	ns
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Sovereign Risk

Long-Term Foreign-Currency IDR	AAA
Long-Term Local-Currency IDR	AAA
Country Ceiling	AAA

Outlooks

Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Foreign-Currency IDR	Stable
Sovereign Long-Term Local-Currency IDR	Stable

Applicable Criteria

[Bank Rating Criteria \(September 2022\)](#)

Related Research

[Global Economic Outlook – March 2023 \(March 2023\)](#)

[Fitch Affirms Auswide Bank at 'BBB+'; Outlook Stable \(December 2022\)](#)

Analysts

Jack Do
+61 2 8256 0355
jack.do@fitchratings.com

Nikkita Lok
+61 2 8256 0345
nikkita.lok@fitchratings.com

Rating Sensitivities

Factors that Could, Individually or Collectively, Lead to Negative Rating Action/Downgrade

IDRs and VR

The IDRs and VR could be downgraded if Auswide's risk profile were to deteriorate, possibly through a loosening of underwriting standards or risk controls in the pursuit of growth, although we do not expect this to occur.

Auswide's ratings could also be downgraded if there is a sustained deterioration of the bank's financial metrics, possibly reflected in a combination of:

- stage 3 loans/gross loans increasing to above 3% for a sustained period;
- operating profit/risk-weighted assets declining below 0.75% for a sustained period; or
- the CET1 ratio falling below 10% without a credible plan to increase it back above this level.

A downgrade of the Short-Term IDR to 'F3' would occur if the Long-Term IDR were to be downgraded to 'BBB' or below.

GSR

The Government Support Rating (GSR) is at the lowest point on the scale and no negative action is possible.

Factors that Could, Individually or Collectively, Lead to Positive Rating Action/Upgrade

IDRs and VR

An upgrade in Auswide's VR and Long-Term IDR appears unlikely, as it would require a significant improvement in the financial profile and business profile without a substantial increase in the risk profile.

While not probable, the Short-Term IDR could be upgraded to 'F1' if Fitch were to revise the funding and liquidity score to 'a', from 'bbb'.

GSR

Positive action on the GSR would require a significant improvement in market position such that the bank's market share is around 1%. An upgrade of the GSR is unlikely to affect the Long-Term IDR, which is driven by Auswide's standalone credit strength.

Other Debt and Issuer Ratings

Rating Level	Rating	Outlook
Subordinated: Long Term	BBB-	n.a.

Source: Fitch Ratings

Auswide's subordinated Tier 2 debt is rated two notches below its anchor rating, the VR, which is consistent with the base case in Fitch's *Bank Rating Criteria*. The two notches below the anchor rating are for loss severity, with non-performance risk captured adequately by the VR. None of the reasons for alternative notching from the anchor rating, as described in the criteria, is present.


The subordinated debt ratings will move in line with Auswide's VR.

Significant Changes from Last Review

High Inflation

Australia, like many countries globally, has experienced a rapid increase in consumer prices, with growth of 7% in the year to March 2023. This has resulted in the Reserve Bank of Australia increasing the cash rate by 375bp from May 2022 to 3.85%, although our current forecasts anticipate that rates are close to peaking. The high rate environment is likely to place some pressure on Australia's highly indebted households, but low unemployment, solid underwriting and buffers built up by households mean large losses are unlikely to result for Australian banks.

Ratings Navigator

Auswide Bank Ltd							ESG Relevance: 	Banks Ratings Navigator		
Operating Environment	Business Profile	Risk Profile	Financial Profile				Implied Viability Rating	Viability Rating	Government Support Rating	Issuer Default Rating
			Asset Quality	Earnings & Profitability	Capitalisation & Leverage	Funding & Liquidity				
	20%	10%	20%	15%	25%	10%				
aaa							aaa	aaa	aaa	AAA
aa+							aa+	aa+	aa+	AA+
aa							aa	aa	aa	AA
aa-							aa-	aa-	aa-	AA-
a+							a+	a+	a+	A+
a							a	a	a	A
a-							a-	a-	a-	A-
bbb+							bbb+	bbb+	bbb+	BBB+ Sta
bbb							bbb	bbb	bbb	BBB
bbb-							bbb-	bbb-	bbb-	BBB-
bb+							bb+	bb+	bb+	BB+
bb							bb	bb	bb	BB
bb-							bb-	bb-	bb-	BB-
b+							b+	b+	b+	B+
b							b	b	b	B
b-							b-	b-	b-	B-
ccc+							ccc+	ccc+	ccc+	CCC+
ccc							ccc	ccc	ccc	CCC
ccc-							ccc-	ccc-	ccc-	CCC-
cc							cc	cc	cc	CC
c							c	c	c	C
f							f	f	ns	D or RD

The Key Rating Driver (KRD) weightings used to determine the implied VR are shown as percentages at the top. In cases where the implied VR is adjusted upwards or downwards to arrive at the VR, the KRD associated with the adjustment reason is highlighted in red. The shaded areas indicate the benchmark-implied scores for each KRD.

VR - Adjustments to Key Rating Drivers

The business profile score of 'bbb' has been assigned above the 'bb' category implied score for the following adjustment reason: business model (positive).

The asset quality score of 'a-' has been assigned below the 'aa' category implied score for the following adjustment reason: concentration (negative).

The earnings and profitability score of 'bbb+' has been assigned below the 'a' category implied score for the following adjustment reason: revenue diversification (negative).

The capitalisation and leverage score of 'bbb+' has been assigned below the 'a' category implied score for the following adjustment reason: size (negative).

The funding and liquidity score of 'bbb' has been assigned below the 'a' category implied score for the following adjustment reason: deposit structure (negative).

Other

The Short-Term IDR of 'F2' is the lower of the two options available at a Long-Term IDR of 'BBB+', as the funding and liquidity score is not sufficiently high to support the higher option; the threshold is a score of at least 'a'.

Financials

Financial Statements

	31 Dec 22		30 Jun 22	30 Jun 21	30 Jun 20	30 Jun 19
	6 months - interim (USDm) Reviewed - unqualified	6 months - interim (AUDm) Reviewed - unqualified	Year end (AUDm) Audited - unqualified	Year end (AUDm) Audited - unqualified	Year end (AUDm) Audited - unqualified	Year end (AUDm) Audited - unqualified
Summary income statement						
Net interest and dividend income	31	46.5	82.0	78.2	70.5	63.2
Net fees and commissions	n.a.	n.a.	-4.5	-3.5	-2.3	-1.1
Other operating income	4	5.6	2.7	0.9	0.8	0.5
Total operating income	35	52.1	80.2	75.6	69.0	62.6
Operating costs	22	32.7	43.4	40.3	38.7	36.9
Pre-impairment operating profit	13	19.4	36.8	35.3	30.3	25.7
Loan and other impairment charges	-1	-0.8	-0.7	0.6	3.8	1.1
Operating profit	13	20.2	37.5	34.7	26.5	24.6
Other non-operating items (net)	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Tax	4	6.1	11.4	10.5	8.0	7.4
Net income	9	14.1	26.1	24.2	18.5	17.2
Other comprehensive income	-2	-2.4	12.8	1.0	-0.8	-0.2
Fitch comprehensive income	8	11.7	38.9	25.2	17.7	17.0
Summary balance sheet						
Assets						
Gross loans	2,728	4,084.0	3,832.4	3,561.1	3,212.6	3,090.7
- Of which impaired	3	4.0	5.9	10.2	13.5	13.1
Loan loss allowances	3	4.0	4.8	6.1	6.8	4.5
Net loans	2,725	4,080.0	3,827.6	3,555.0	3,205.8	3,086.2
Interbank	3	4.5	11.8	12.8	16.3	21.0
Derivatives	9	13.1	16.4	0.0	0.1	0.6
Other securities and earning assets	279	418.2	396.6	400.0	379.2	317.3
Total earning assets	3,017	4,515.8	4,252.4	3,967.8	3,601.4	3,425.1
Cash and due from banks	177	265.4	178.5	112.6	106.5	104.4
Other assets	48	72.4	73.7	75.4	81.6	73.9
Total assets	3,242	4,853.6	4,504.6	4,155.8	3,789.5	3,603.4
Liabilities						
Customer deposits	2,567	3,842.9	3,058.7	2,932.6	2,620.4	2,372.9
Interbank and other short-term funding	0	0.0	558.6	416.7	398.1	429.7
Other long-term funding	460	688.4	563.6	526.5	505.5	518.4
Trading liabilities and derivatives	1	1.0	0.8	2.7	2.1	1.3
Total funding and derivatives	3,028	4,532.3	4,181.7	3,878.5	3,526.1	3,322.3
Other liabilities	18	27.6	40.8	20.8	21.4	42.6
Preference shares and hybrid capital	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Total equity	196	293.7	282.1	256.5	242.0	238.5
Total liabilities and equity	3,242	4,853.6	4,504.6	4,155.8	3,789.5	3,603.4
Exchange rate		USD1 = AUD1.497	USD1 = AUD1.451589	USD1 = AUD1.330141	USD1 = AUD1.457089	USD1 = AUD1.425923

Source: Fitch Ratings, Fitch Solutions, Auswide

Key Ratios

	31 Dec 22	30 Jun 22	30 Jun 21	30 Jun 20	30 Jun 19
Ratios (annualised as appropriate)					
Profitability					
Operating profit/risk-weighted assets	2.0	1.9	1.9	1.6	1.6
Net interest income/average earning assets	2.1	2.0	2.1	2.0	1.9
Non-interest expense/gross revenue	62.8	54.1	53.3	56.1	59.0
Net income/average equity	9.7	9.7	9.7	7.7	7.3
Asset quality					
Impaired loans ratio	0.1	0.2	0.3	0.4	0.4
Growth in gross loans	6.6	7.6	10.9	3.9	5.8
Loan loss allowances/impaired loans	100.0	81.4	59.8	50.4	34.4
Loan impairment charges/average gross loans	0.0	0.0	0.0	0.1	0.0
Capitalisation					
Common equity Tier 1 ratio	10.7	10.6	10.8	11.1	11.8
Fully loaded common equity Tier 1 ratio	n.a.	n.a.	n.a.	n.a.	n.a.
Fitch Core Capital ratio	n.a.	n.a.	n.a.	11.7	12.5
Tangible common equity/tangible assets	5.1	5.2	5.0	5.1	5.3
Basel leverage ratio	n.a.	n.a.	n.a.	n.a.	n.a.
Net impaired loans/common equity Tier ¹	0.0	0.5	2.1	3.7	4.9
Net impaired loans/Fitch Core Capital	n.a.	n.a.	n.a.	3.5	4.6
Funding and liquidity					
Gross loans/customer deposits	106.3	125.3	121.4	122.6	130.3
Liquidity coverage ratio	n.a.	n.a.	n.a.	n.a.	n.a.
Customer deposits/total non-equity funding	84.8	73.2	75.7	74.4	71.5
Net stable funding ratio	n.a.	n.a.	n.a.	n.a.	n.a.
Source: Fitch Ratings, Fitch Solutions, Auswide					

Support Assessment

Commercial Banks: Government Support

Typical D-SIB GSR for sovereign's rating level (assuming high propensity)	a+ to a-
Actual jurisdiction D-SIB GSR	a
Government Support Rating	ns

Government ability to support D-SIBs

Sovereign Rating	AAA/ Stable
Size of banking system	Negative
Structure of banking system	Negative
Sovereign financial flexibility (for rating level)	Positive

Government propensity to support D-SIBs

Resolution legislation	Neutral
Support stance	Neutral

Government propensity to support bank

Systemic importance	Negative
Liability structure	Neutral
Ownership	Neutral

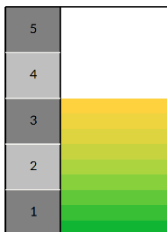
The colours indicate the weighting of each KRD in the assessment.

■ Higher influence
 ■ Moderate influence
 ■ Lower influence

The GSR of 'ns' reflects our expectation that there is no reasonable assumption of support being forthcoming from the state because of the bank's limited systemic importance.

Environmental, Social and Governance Considerations

Overall ESG

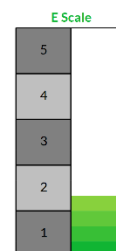


How relevant are E, S and G issues to the overall credit rating?

5	Highly relevant, a key rating driver that has a significant impact on the rating on an individual basis. Equivalent to "higher" relative importance within Navigator.
4	Relevant to rating, not a key rating driver but has an impact on the rating in combination with other factors. Equivalent to "moderate" relative importance within Navigator.
3	Minimally relevant to rating, either very low impact or actively managed in a way that results in no impact on the entity rating. Equivalent to "lower" relative importance within Navigator.
2	Irrelevant to the entity rating but relevant to the sector.
1	Irrelevant to the entity rating and irrelevant to the sector.

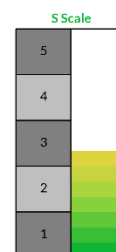
Environmental (E)

General Issues	Score	Impact	Sector-Specific Issues	Reference
GHG Emissions & Air Quality	1		n.a.	n.a.
Energy Management	1		n.a.	n.a.
Water & Wastewater Management	1		n.a.	n.a.
Waste & Hazardous Materials Management; Ecological Impacts	1		n.a.	n.a.
Exposure to Environmental Impacts	2		Impact of extreme weather events on assets and/or operations and corresponding risk appetite & management; catastrophe risk; credit concentrations	Business Profile (incl. Management & governance); Risk Profile; Asset Quality



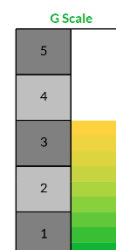
Social (S)

General Issues	Score	Impact	Sector-Specific Issues	Reference
Human Rights, Community Relations, Access & Affordability	2		Services for underbanked and underserved communities; SME and community development programs; financial literacy programs	Business Profile (incl. Management & governance); Risk Profile
Customer Welfare - Fair Messaging, Privacy & Data Security	3		Compliance risks including fair lending practices, mis-selling, repossession/foreclosure practices, consumer data protection (data security)	Operating Environment; Business Profile (incl. Management & governance); Risk Profile
Labor Relations & Practices	2		Impact of labor negotiations, including board/employee compensation and composition	Business Profile (incl. Management & governance)
Employee Wellbeing	1		n.a.	n.a.
Exposure to Social Impacts	2		Shift in social or consumer preferences as a result of an institution's social positions, or social and/or political disapproval of core banking practices	Business Profile (incl. Management & governance); Financial Profile



Governance (G)

General Issues	Score	Impact	Sector-Specific Issues	Reference
Management Strategy	3		Operational implementation of strategy	Business Profile (incl. Management & governance)
Governance Structure	3		Board independence and effectiveness; ownership concentration; protection of creditor/stakeholder rights; legal/compliance risks; business continuity; key person risk; related party transactions	Business Profile (incl. Management & governance); Earnings & Profitability; Capitalisation & Leverage
Group Structure	3		Organizational structure; appropriateness relative to business model; opacity; intra-group dynamics; ownership	Business Profile (incl. Management & governance)
Financial Transparency	3		Quality and frequency of financial reporting and auditing processes	Business Profile (incl. Management & governance)



Unless otherwise disclosed in this section, the highest level of environmental, social and governance (ESG) credit relevance is a score of '3'. This means ESG issues are credit-neutral or have only a minimal credit impact on the entity, either due to their nature or the way in which they are being managed by the entity. For more information on Fitch's ESG Relevance Scores, visit www.fitchratings.com/esg.

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