

**Speech to Trans-Tasman Business Circle
Michael Smith, Chief Executive Officer, ANZ**

Sydney, 27 November 2007

I have to say that I'm particularly pleased to be talking to the Trans-Tasman Business Circle today.

Wearing my Irishman's hat, I've decided it is not in any one's interest to spend time talking about that the one thing that binds and divides Australia and New Zealand... rugby union.

So let's quickly move on to business.

As someone who has only been in the job at ANZ for two months, I thought the most useful thing I could do today is give you a few personal observations on what's happening in the international financial environment

I'll then take a look at what those changes may mean for Australia and New Zealand, particularly for financial services.

Addressing these changes will be heart of ANZ's future strategy.

I believe they are also relevant more broadly, particularly as the new Rudd Labor Government turns its mind from Saturday's election success to the opportunities for further economic reform.

Fundamentally, I believe there is an urgent need for a fresh look at reforms to help create a more competitive, outwardly focused economy. But, I'll talk more about that later too.

First let me say that I understand anyone who feels confused right now.

Oil is looking longingly at \$100 a barrel.

Gold is looking just as longingly at \$1,000 an ounce.

Northern hemisphere banks, and lots of organizations that look like banks, are all racing each other for the gold medal for the biggest write down from losses in sub-prime lending.

So far US investment banks have provided nearly \$50 billion. For those of you who are confused by the terms write down and provision, they are bank speak for losses.

At the moment, write downs this year are equal to the annual Gross National Product of Kuwait.

It seems to me that the sub-prime experience is a classic example of financial institutions breaking one of the fundamental rules – not methodically addressing the question of a borrower's capacity to repay.

All the effort was on sales and analysis designed to reassure that sub-prime lending was sound. You don't need regulation or involved internal credit processes to know that servicing and repayment capacity, appropriately stress tested, lies at the heart of "sound banking".

To some extent this approach was also driven by the view that it didn't matter anyway because the assets would be quickly on sold to someone else.

Once again, this does not say much for good banking practice. And I believe, as regulators turn to look at the sub-prime experience, this will be one of the issues that comes under some scrutiny.

Now while I am wary of talking about history after Warren Buffet's remark that *'If past history was all there was to the game, the richest people would be librarians'*..... right now I will take the chance.

From an economic perspective, my view is the effect of the sub-prime crisis will be mainly focused in the US. Despite the significance of the US, I think 2008 will still be a pretty good growth year for the world economy – say about four and a half percent GDP growth. This result will largely be as a consequence of continued robust growth in Asia.

Now if you think sub prime is confusing, interest rates are equally confusing.

They are going up in Australia and New Zealand; down in the US; and are 14% in Iceland and 17% in Turkey just in case you were thinking of buying a home there.

Things have become so confusing that the Brazilian supermodel Giselle who earned \$35 million in the first six months of this year.... made an unusual request.

Just before the 27 year old.....who is already worth \$150 million signed a deal to promote Pantene hair products - she demanded to be paid in Reals, the currency of her native Brazil, not in US Dollars.

As it turns out Giselle is a better currency strategist than most. The Real has risen by over 20% against the Dollar this year, while the Euro gained just over 10%.

So you are right to be feeling confused and uncertain about the future.

However, some things never change.

Customer retention and deepening wallet share will remain the key to organic growth.

Now, I haven't heard many banks that say they don't want to focus on the customer ... and I would guess many of you might think that after some of the experiences you have had over the years ... but, actually being customer centric is a lot harder to deliver than to say.

For instance our customers expect that we know about all their transactions with us. For us, and many other banks, that is simply not the case.

At ANZ we have 24 businesses.

My job is to ensure that we don't act like 24 businesses to our customers. Our culture and systems need the customer as their centre of gravity, not the products we sell.

To my mind that means banks will have to be more like other successful businesses. More like those companies who live and die by their marketing and their ability to really understand and get close to their customers.

We have made good progress on this at ANZ. Our Personal Bank leads the major banks on customer satisfaction.

But to take this to the next level, and become truly customer-centric requires continual investment in technology and continual investment in people.

Conventional wisdom says the internet makes the customer relationship less personal.

I believe it allows you to get closer to both individual and corporate customers. What it does do is take the human element from routine boring tasks and gives people the tools and the skills to focus more on the customer and really add value versus taking orders.

It means the customer can handle routine tasks online which cuts costs for both the customer and the bank.

And it puts more power, more control in the hands of the customer.

In all aspects of society, more power is moving to the consumer.

Up to ten years ago if you wanted to buy or sell shares you had to know a stockbroker. Then he might have allowed you to open an account. If you wanted to buy some shares you rang up the broker and placed an order.

Later that day or even the next day the broker would ring you up and tell you what you paid for the stock and whether your order was filled.

Then you would get a form in the mail. You'd fill it out and a few weeks later you'd get your share scrip. If you wanted to sell you'd go through the same process.

Today you go online with E*Trade. You enter your order and in about 30 seconds you have the details of your trade, the money has been taken out of your account and the transaction is completed.

So you have controlled and executed the process. You have saved a lot of money and time. This is a model you will see banks apply to many more aspects of their business.

It cuts costs and saves time for the customer ... and time, and how you can save customer's time, is increasingly the new currency. It also reduces complexity.

But this doesn't mean less bank branches.

Successful companies will blend the digital world with the physical world. We want to increase traffic whether it's on anz.com or through our branches.

Successful companies also understand the market no longer rewards meeting expectations. It only rewards out performance.

That is very clearly in my mind as we look at how to reconceive ANZ as a customer-centric, marketing focused, technology based, performance driven organisation.

OK. That's the picture in banking, at ANZ and with our customers. What about the international environment.

I opened my speech today by describing my journey to Australia by way of China.

Of course, for the majority of the last 20 centuries, China has been the largest economy in the world.

In 1890 – over a century ago – a quarter of the globe was ruled from London.

Then we moved from the European century to the American century.

Today, we are at another turning point. One in which by 2015, China will once again be the world's largest economy.

Over the last two decades we have watched the industrialization and urbanization of China and to a lesser extent India. Over that time around 700 million people have moved from rural areas into the cities. This dwarfs what happened during the industrial revolution.

Last year in China, 67 million Chinese bought a mobile phone. The same sort of increases is true for everything from air conditioners, refrigerators, microwaves, cars and industrial equipment.

As a result Chinese growth is driving world materials demand. The Chinese steel industry is now 4 times the size of the US steel industry.

Let's put this another way: over 60 per cent of the world's population lives in Asia.

Asian GDP, led by China, is forecast to remain 3 to 4 times higher than OECD countries. The compound effect of this growth is that Asia accounted for just 20 per cent of global GDP in 1980. Today, it is close to double that.

This century is the Asian century.

For financial services firms the opportunity is immense. By the end of this year, 13 percent of China's urban families, or almost 25 million households, will be defined as middle class, with this proportion set to double in the next three years.

Until recently, Chinese consumers only paid cash for their purchases. With greater deregulation, consumer credit and credit cards are more available and, because of this, spending and borrowing are on the rise.

This is a huge and growing opportunity for financial services providers.

So where does Australia and New Zealand fit in all this?

First of all we are part of Asia, like it or not.

Australia is already the leading destination for the education of a new generation of Asian people. Australia is currently home to 90,000 Chinese students and 50,000 from India. To put this in perspective, Australia is currently helping to educate more Chinese students than the US.

Half of Australia's population growth is from migrants and Asia accounts for over 40 per cent of that.

At ANZ, we are already incredibly multi-cultural. Among our top ten surnames are five Asian names. Of course, I'm pleased to say Smith still tops the list.

Much of our wealth and economic growth is already coming from Asia. That's most obvious with the success of our resources industry.

Now as nations and as businesses, we can make a decision to sit back and see others in the region succeed and passively accept the indirect benefits, or we can decide to be part of Asia, part of the opportunity and share in creating the region's success.

To help us decide whether this is our new reality or just a fad, let me give you two facts and ask you a question.

Today, China represents 21 per cent of world population and 15 per cent of world GDP.

Do you believe these proportions will remain constant?

If you want some help, the Board of BHP Billiton have already answered that question in making the proposal to Rio Tinto to create a \$400 billion resources giant.

Interestingly enough no one has really questioned the logic of combining the two companies ... although the two companies have very different ideas on price!

Chinese banks and increasingly Chinese companies are also answering the question. They are using their size to look at strategic opportunities outside China.

To help us think about this, it is worth remembering that the largest bank in the world by market capitalisation is not Citibank; it's not Bank of America; and it's not HSBC.

As of July 2007, it was a Chinese bank - ICBC with a market capitalisation of \$360 billion and over 18,000 outlets including more than 100 overseas branches.

This month, the top 3 banks in the world by market capitalisation are Chinese.

And just the other week, ICBC opened its first branch here in Sydney.

At my first media conference two months ago, I talked about the ambitions of the Chinese banks and Australia's strategic importance to China.

Since then, we have seen ICBC's landmark agreement last month to acquire a 20 per cent stake in Standard Bank in South Africa, Africa's largest financial services group.

This approach highlights the new-found confidence among Chinese banks in looking beyond their domestic markets, a push encouraged by Beijing.

For Australia, I believe this will be the third wave of financial competition since deregulation.

The first was the opening up of the market to foreign banks in the late 1980s. In fact, that was my first role in Australia when HSBC opened here.

The second was the emergence of non-bank financial institutions such as mortgage specialist such as Aussie Home Loans, and finance companies like GE.

Now, it is the banks from Asia that will form the next wave of competition.

But global growth is not just about China. Put simply, developing economies are growing faster than developed economies.

Nor are our opportunities just about China's influence on our region.

India began its economic transformation almost a decade after China did but is rapidly creating world-class businesses in knowledge-based industries such as software, IT services, and pharmaceuticals.

The most efficient bank in the world today is India's ICICI.

ICICI's success is largely based on the innovative use of technology. It has enabled ICICI to serve close to 20 million customers today compared to just 100,000 in 2000.

The reason I use the example of a world class Indian bank is because it seems to me that Australia's Four Pillars policy has developed an inward looking culture within significant parts of the Australasian banking system.

While successive governments have done a great job at opening up the Australian and New Zealand economies, I believe consumers are increasingly disadvantaged by the Four Pillars Policy.

You see, I think the real question is not how we compare to our domestic competitors but rather; how does our internet banking compare with Wells Fargo's? How do our ATMs compare with Spain's Santander's? You can practically cook dinner with a French ATM - they sell insurance, approve mortgages. It's quite amazing.

But where is that perspective in Australasia?

This is about the central role technology can play in producing best-in-class solutions for our customers.

There is no doubt in my mind that productivity will be one of the keys to not only a company's success in a still globalising world, but to its very survival.

Why is it that India is a global leader in innovation, technology and cost?

Simply, because of the Indian education system.

In a number of technology and operational areas, Indians are some of the most skilled professionals in the world. These are skills which are in chronic short supply in Australia and New Zealand.

And it's not just in technology.

When the Indian economy liberalized ten years ago the growth of technology and outsourcing companies exploded. As a result there are now more than a thousand business schools in India.

Even with that many business schools competition for places is fierce. Two years ago 133,000 students applied to the Indian Institute of Management. One per cent were admitted.

The result is the growth of these technology driven companies, staffed by highly educated locals, has helped doubled GDP growth in India in just four years.

In less than eight years India will surpass Japan as the world's third largest economy.

India's pool of young university graduates - those with seven years or less of work experience – is around 14 million ... twice that of the United States.

Every year that huge number of young graduates is topped up by two and a half million new ones.

I was in Bangalore earlier this month visiting ANZ's technology and operations centre that one of my predecessors had the foresight to establish in 1989.

At ANZ, we are committed to keeping our call centres and customer facing roles at home in Australia and New Zealand..... but a significant part of our software development and technology support now goes on in Bangalore. We have almost 2,000 ANZ employees working there.

My intention is that we'll continue to develop Bangalore in the coming years, such that it becomes a strategic asset for ANZ in innovation, cost and service.

At ANZ, there's no question we are making progress but here's the question:

Is it good enough in the world I have described to have as your vision to be the best of four Australasian banks?

Isn't the real question and the real aspiration for our shareholders and our staff, to ask how can we be as good or better than the best financial services companies in the world in the areas in which we choose to compete?

Given the mature Australian and New Zealand economies and that the market rewards growth, it is clear that our banks face a fundamental problem.

They will eventually become ex-growth relative to the opportunities in Asia and increasingly marginalized as regional banks expand grow in Asia and ultimately in Australia.

The differential rates of growth between Asia and the OECD, including Australia, mean over the medium term the significant growth opportunities are in our region not at home.

But unless we become more outward looking now, the next wave of competition from Asian banks with best in class customer solutions will be formidable competitors.

Australian banks are increasingly sub-scale and potentially unable to fund and service the growth required by those Australian and New Zealand companies who have decided to be part of the Asian growth story.

Now is the time for us to be more outward looking, innovative and customer focused.

I believe it is in Australia's national interest to move beyond the Four Pillars Policy and allow the banking system to be subject to the same competition policy that all other Australian businesses face.

The election of the Rudd Government provides us with a fresh opportunity to examine this because I believe Australia's national interest requires us to allow the banks to ultimately grow to a size where they can compete as 'super regionals'.

Economic and social growth is not guaranteed to any country.

Like great rugby teams they take leadership, training, skill, depth and most importantly courage.

Now is the time for both Australia and New Zealand to make the decision about whether we want to be real players on the world stage but we must do this quickly ... the world will not wait for us.

Thank you.