MOODY'S
INVESTORS SERVICE

CREDIT OPINION
7 March 2022

Update

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RATINGS

Macquarie Group Limited

Domicile	Sydney, New South Wales, Australia
Long Term CRR	Not Assigned
Long Term Debt	A3
Type	Senior Unsecured - Fgn Curr
Outlook	Positive
Long Term Deposit	Not Assigned

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Macquarie Group Limited

Update following rating affirmation, outlook changed to positive

Summary

On 14 February, we affirmed the A3 long-term rating of Macquarie Group Limited and changed its outlook to positive from stable, reflecting the group's strong and improving profitability as its franchise matures across a number of business lines, including the significant growth in MBL's retail banking franchise, which has seen its market share of residential mortgage lending in Australia rise to 4.2%. The strong overall credit profile also balances the risks of the group's continual evolution against the strength of its earnings profile and the group's strong capitalization and liquidity metrics. The rating also includes two notches of uplift to reflect our view that depositors and senior bondholders would benefit from systemic support, if needed.

Moody's also maintains ratings for the group's banking subsidiary, Macquarie Bank Limited (MBL, A2/A2 positive, baa1), and an intermediate holding company housing its non-bank operations, Macquarie Financial Holdings Pty Limited (A3 positive). For the rating factor grid applicable to MBL, please refer to MBL's Credit Opinion.

In particular we note:

» MGL maintains a solid balance sheet position, with high levels of capital and very strong liquidity metrics. As at 31 December 2021, its banking subsidiary reported an APRA Basel III Common Equity Tier 1 (CET 1) ratio of 12.2%. The banking subsidiary had a quarterly daily average Liquidity Coverage Ratio of 177% for the quarter ending 31 December 2021. Management's focus on maintaining a resilient balance sheet is key to maintaining the firm's strong credit profile.

» MGL's risk management is very strong with tight risk controls, cognizant of market, regulatory and reputational pressures both on an individual unit and on a portfolio basis. The well-embedded risk culture reflected in the firm's earnings performance are positive. Maintaining its disciplined risk culture remains a challenge as the group grows larger, or pursues further growth opportunities through acquisitions.

» A high probability that MGL would receive systemic support in case of need, as a consequence of its significant presence in Australia's financial markets. We continue to view the regulatory and political framework in Australia to be favorable to the interests of senior bank creditors, in contrast to many developed markets. As a result, we incorporate two notches of systemic support uplift into the ratings of MBL, and, by extension, MGL.

Credit strengths

» A diversified business profile, constrained by exposure to non-lending risks.

» Conservative risk management is key to MGL's credit profile.

» Capital levels remain supportive; future positioning is a key credit consideration.

» Strong liquidity profile.

Credit challenges

» Exposure to volatile capital markets businesses, albeit declining.

» Complex and diverse nature of MGL's operations, requiring disciplined and proactive risk management.

Rating outlook

The ratings outlooks for MGL are positive, reflecting the outlook for the group's main operating company, Macquarie Bank Limited.

The positive rating outlook fro Macquarie Bank Limited reflects the potential improvement in the bank's asset risk profile with the significant growth in the bank's retail banking franchise, which has seen its market share of residential mortgage lending in Australia rise to 4.2%. We consider the rise in mortgage lending, which has historically been a low loss asset class, as providing an offset to the group's trading and investment banking activities. The outlook also reflects the group's strong and improving profitability as its franchise matures across a number of business lines.

Factors that could lead to an upgrade

MGL's ratings could be upgraded if Macquarie Bank Limited's ratings are upgraded.

Factors that could lead to a downgrade

With the ratings on positive outlook a downgrade is unlikely. However, the outlook could return to stable if Macquarie Bank Limited's outlook returns to stable.

As the ratings of MGL, MBL and MFHPL incorporate the potential for systemic support, any signal from the regulator or government that suggests a less creditor-friendly stance on bank resolution could create downward pressure on the supported ratings. In particular any signs of a reduction in the degree of a support available to, or expectation of greater loss absorbency by, holding companies could lead to downward pressure on the ratings of Macquarie's holding company, MGL.

We view the Macquarie legal entities as closely intertwined, with a high degree of operational and financial linkages. However, should in the medium-to-long run there be a sharpening of the boundaries between the group's bank and non-bank entities, it could lead to greater divergence of their credit profiles and rating outcomes.

Key indicators

Exhibit 1
Macquarie Group Limited (Consolidated Financials) [1]

	09-21[2]	03-21[2]	03-20[2]	03-19[2]	03-18[2]	CAGR/Avg.[3]
Total Assets (AUD Million)	274,103.0	227,270.0	211,982.0	185,595.0	180,291.0	12.7[4]
Total Assets (USD Million)	197,998.4	173,100.1	129,743.9	131,837.1	138,291.8	10.8[4]
Tangible Common Equity (AUD Million)	19,729.4	18,684.8	17,122.7	14,846.3	14,519.0	9.2[4]
Tangible Common Equity (USD Million)	14,251.5	14,231.3	10,480.0	10,546.0	11,136.8	7.3[4]
Problem Loans / Gross Loans (%)	1.0	1.9	2.1	2.5	1.1	1.7[5]
Tangible Common Equity / Risk Weighted Assets (%)	18.5	21.8	19.3	20.5	16.4	19.3[6]
Problem Loans / (Tangible Common Equity + Loan Loss Reserve) (%)	6.0	10.2	11.0	12.6	5.3	9.0[5]
Net Interest Margin (%)	1.3	1.2	1.2	1.2	1.4	1.3[5]
PPI / Average RWA (%)	3.9	3.8	3.4	3.0	2.9	3.4[6]
Net Income / Tangible Assets (%)	1.6	1.3	1.3	1.6	1.4	1.5[5]
Cost / Income Ratio (%)	71.8	72.1	76.4	78.2	74.6	74.6[5]
Market Funds / Tangible Banking Assets (%)	41.7	36.0	40.5	39.9	44.4	40.5[5]
Liquid Banking Assets / Tangible Banking Assets (%)	32.4	37.2	31.1	33.5	32.9	33.4[5]
Gross Loans / Due to Customers (%)	130.1	126.1	141.1	139.4	152.9	137.9[5]

[1] All figures and ratios are adjusted using Moody's standard adjustments. [2] Basel III - fully loaded or transitional phase-in; IFRS. [3] May include rounding differences because of the scale of reported amounts. [4] Compound annual growth rate (%) based on the periods for the latest accounting regime. [5] Simple average of periods for the latest accounting regime. [6] Simple average of Basel III periods.
Sources: Moody's Investors Service and company filings

Profile

Macquarie Group Limited (MGL) is the non-operating holding company of the Macquarie Group. The group offers asset management; finance, banking, advisory services and risk and capital solutions globally. As at 30 September 2021, the group reported consolidated assets of AUD 348.6 billion.

MGL was formed in 2007 when Macquarie Bank Limited (MBL, established as Hill Samuel Australia Limited in 1969, renamed MBL in 1985, and listed in 1996) was reorganized under a holding company structure. Since 2007, MGL's shares have been listed on the Australian Securities Exchange (Ticker: MQG).

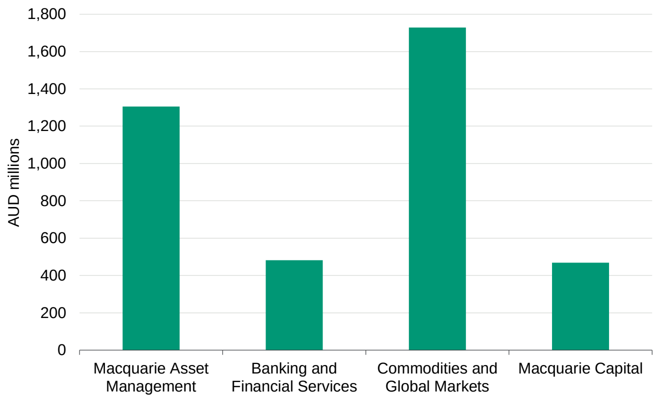
Detailed credit considerations

A diversified business profile, with strong earnings potential

MGL's earnings are highly diversified by product and geography. MGL's activities are carried out through four primary business lines: Macquarie Asset Management (MAM), Banking and Financial Services (BFS), Commodities and Global Markets (CGM) as well as Macquarie Capital (MacCap).

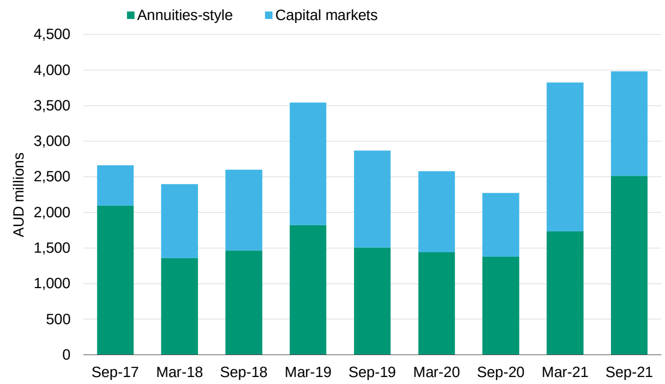
MGL benefits from a highly diverse business profile, with a history of strong earnings contribution from its more stable lines of business, including asset management, asset finance and banking. This provides the group with a base of stable earnings, enabling it to better absorb earnings shocks that may arise from market volatility that would affect its markets facing businesses (Exhibits 2 and 3).

Exhibit 2
Net profit contribution by division
For the year ending 30 September 2021



Source: Company disclosures

Exhibit 3
Strong earnings built on a base of stable businesses
Half-yearly profits excluding Corporate Centre costs



Source: Company disclosures

Underlying earnings trends are:

» Strong contribution to earnings from Commodities and Global Markets ("CGM") and Macquarie Asset Management ("MAM") in first half of fiscal 2022 (Exhibit 4), respectively contributing 43% and 33% of net income for the period.

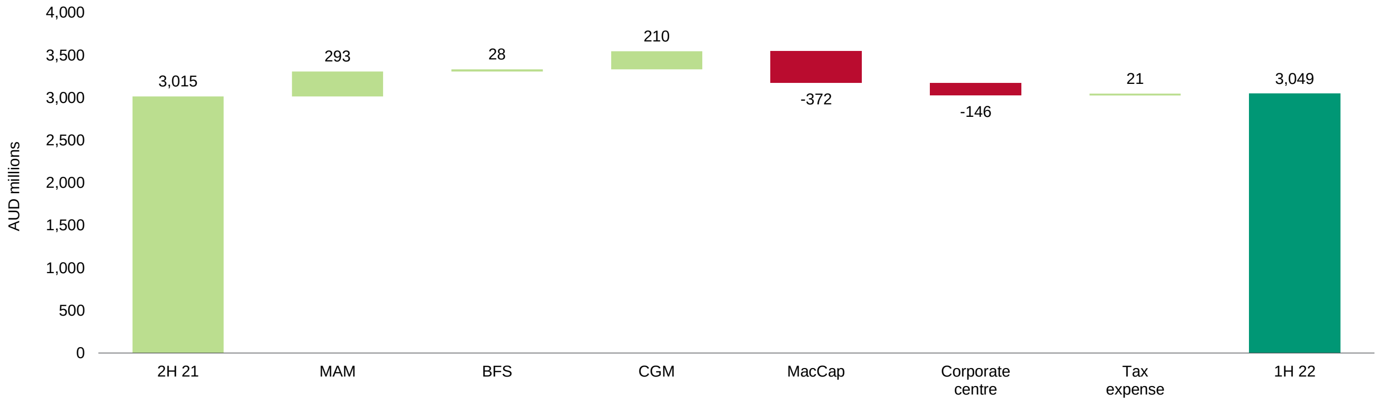
» CGM's net profit was up 14% half-on-half to AUD1.7 billion. This business increased revenue across Commodities, with strong risk management income from Gas and Power, Resources, and Agriculture, and the partial sale of UK meter assets.

» MAM's net profit was up 29% half-on-half to AUD1.3 billion, driven by income related to the disposition of Macquarie Infrastructure Corporation assets. AUM was up 31% to AUD 736.0 billion as at 30 September 2021, primarily from the acquisition of Waddell & Reed Financial, Inc.. Base fees were up 44% to AUD 1.5 billion (Exhibit 5), and we consider the base fee stream generated by MAM to be the key contributor to the group's profitability. Performance fees for the group tend to be cyclical and are dependent on timing of asset realisations. While these were down 57% to AUD 177 million during the period we still expect performance fees will be a large contributor to profits on a through the cycle basis.

» Macquarie Capital reported a net profit contribution of AUD 468 million, which declined half-on-half but was up significantly from a net loss in the prior corresponding period. The result reflected higher fee and commission income which was driven by mergers and acquisition and debt capital markets income, and material asset realisations.

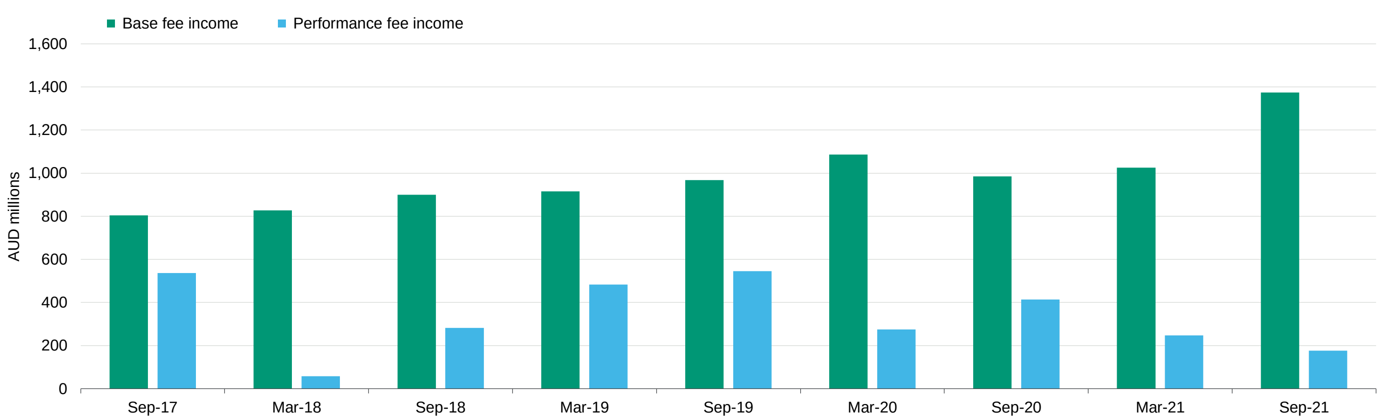
» Banking and Financial Services' net profit contribution increased to AUD482 million as decreased credit impairment charges partially offset by increased headcount and investment in technology. The home loan portfolio was up 14% and the business banking portfolio up 8% for the September half. We expect intense competition for Australian mortgages, combined with the very low interest rate environment will result in margin pressure in 2022.

Exhibit 4
Profit growth waterfall
2H21 compared to 1H22



Source: Company disclosures

Exhibit 5
Macquarie Asset Management base and performance fees



Source: Company disclosures, Moody's Investors Service

Conservative risk management is key to MGL's credit profile

The benefits of MGL's global scope and diversification also raises the level of operational complexities and risk management challenges. In addition it exposes the firm to and risks associated with the evolution of the group's business model. As a result, we adjusted MBL's financial profile negatively by one notch.

We consider MGL's ability to maintain a conservative risk culture as being one of the firm's most difficult tasks. The diversity of MGL's business requires tight risk controls, cognizant of market, regulatory and reputational pressures both on an individual unit and on a portfolio basis. To date, management has been focused on containing its markets exposure through a combination of tight risk management oversight and an emphasis on less volatile streams of trading revenue.

MGL has a well-embedded risk culture and the firm's track record and ability to limit earnings volatility are positive. Maintaining its disciplined risk culture remains a challenge as the group grows larger, or pursues further growth opportunities through acquisitions.

Macquarie's asset risk profile is improving

Macquarie asset risk profile is improving with its deliberate strategy of growing its retail bank by focusing on residential mortgage lending in Australia. This has asset class has proven track record of stability, with inherently low loss rates given the structure of the mortgage market where lenders have full recourse to borrowers in the event of default and with the bulk of new origination done with loan-to-value ratios (LVRs) below 80%. The bank has increased its share of the Australian mortgage market from 1.8% at the end of 2017 to 4.2% at the end of 2021, making them the 5th largest mortgage lender in the country behind the 4-major banks.

Non-lending risk is well managed and risk management is a relative strength of the group. Macquarie has a well-embedded risk culture and the firm's track record and ability to limit earnings volatility are positive. The group is active in capital markets; however, the risk is well managed through the use of netting and collateral arrangements and a strict adherence to trading limits. Macquarie sets a Global Risk Limit that constrains the group's aggregate level of risk. The Global Risk Limit references to capital and earnings and is an input to the group's risk appetite statement and used to quantify the group's aggregate risk appetite.

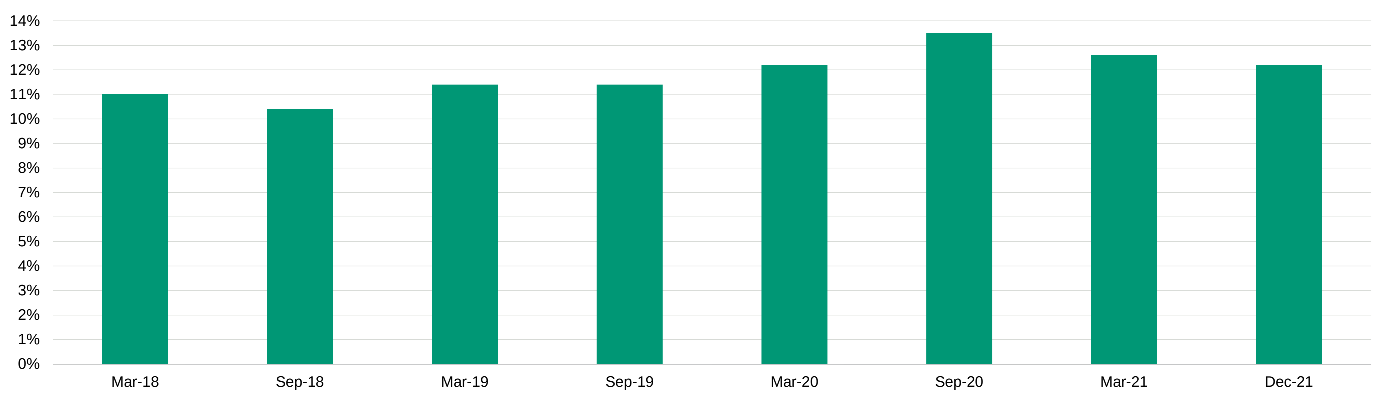
Capital levels remain supportive; future positioning is a key credit consideration

The firm's capital requirements are a combination of Basel III capital requirements for its banking operations contained within MBL and additional capital requirements in respect of its non-banking operations calculated on the basis of an economic capital adequacy model (reviewed by the Australian Prudential Regulation Authority).

As at 31 December 2021, MBL, MGL's banking subsidiary, reported a Common Equity Tier 1 (CET 1) ratio of 12.2%, calculated with APRA's capital methodology (Exhibit 6) and a self-reported "Harmonized" Basel III ratio of 15.4%. On an overall group basis, as at 31 December 2021, Macquarie had AUD 11.5 billion of surplus capital and buffers relative to APRA's requirements, assuming a minimum Tier 1 ratio of 8.5% of the banking group's risk-weighted assets.

Exhibit 6

Common equity Tier 1 ratio of Macquarie Bank Limited



Source: Company disclosures, Moody's Investors Service

Strong liquidity profile

On a consolidated level, MGL's liquidity metrics remain strong. As at 30 September 2021, the group's cash and liquid asset portfolio stood at AUD 57.9 billion and at 31 December 2021, MBL's quarterly daily average Liquidity Coverage Ratios was 177%. MGL's standard liquidity policy is to ensure that at least twelve months' maturities can be met from internal sources. This is reflected in MBL's very high `a1' Liquid Resources score.

The group's external wholesale funding is chiefly raised by MBL. The bank has also successfully grown its deposit base, up 9% in the half ending 30 September 2021. Factors we would view to support the stickiness of such deposits are the fact that they are transaction accounts with relatively small average balances, such that there would be a high degree of coverage by Australia's Financial Claims Scheme (a form of deposit insurance).

The group's funding structure remains exposed to high levels of wholesale funding. However, the weighted average maturity of the firm's long-term wholesale funding is 4.7 years, mitigating some of these concerns. Deposits rose to AUD 91.7 billion, up from 84.2 billion at 31 March 2021.

MGL's rating is supported by Australia's strong operating environment

Australia's Strong+ Macro Profile reflects the country's very high degree of economic robustness, institutional and government financial strength, and low susceptibility to event risk. Australia's economy grew uninterrupted for 28 years before the pandemic, and unemployment remains low. Our baseline scenario projects a recovery in the country's real GDP growth to be 3.3% in 2022.

The government's economic support package has provided financial assistance to companies and individuals, effectively mitigating the negative impact of reduced activity caused by the pandemic. Fiscal measures and partial government guarantees have provided credit to small and medium-sized enterprises, while wage subsidies and debt rescheduling efforts by banks have relieved the immediate pressure on borrowers and minimized a potential wave of bankruptcies.

Government wage subsidy payments and bank loan forbearance expired at the end of March 2021, which will highlight the underlying impact of the pandemic on residential mortgage quality and small business loans. Household debt is high, with household debt/annualized disposable income at 185% as of September 2021. However, employment growth, low interest rates, rebounding house prices and low LVRs on home loans, and small business loans that are typically secured by residential properties should provide buffers to asset quality.

Australian banks' very strong pricing power has historically been supported by the high level of concentration in the banking sector. While loan loss charges increased during the pandemic and loan volumes declined, rebounding economic conditions are once again supporting demand for credit. To date, banks have successfully preserved their NIMs as lower funding costs, assisted by low-cost funding facilities from the RBA, offset the impact of the low interest rate environment on interest income.

Australia's structural reliance on external financing remains a key vulnerability. However, Australian banks have been extending the term structure of their wholesale market funding for a number of years and pre-funding upcoming maturities well in advance. The RBA's committed liquidity facility, combined with its bond purchases and term-repo operations, has boosted system-level liquidity. A temporary reciprocal swap line arrangement between the RBA and the US Federal Reserve has facilitated access to US dollar liquidity.

ESG considerations

Macquarie Group Limited's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 7
ESG Credit Impact Score

CIS-2

Neutral-to-Low

For an issuer scored CIS-2 (Neutral-to-Low), its ESG attributes are overall considered as having a neutral-to-low impact on the current rating; i.e., the overall influence of these attributes on the rating is non-material.

Source: Moody's Investors Service

MGL's ESG Credit Impact Score is neutral-to-low (**CIS-2**), reflecting the limited credit impact of environmental and social risk factors on the ratings to date, and low governance risks.

Exhibit 8
ESG Issuer Profile Scores

ENVIRONMENTAL	SOCIAL	GOVERNANCE
E-3	S-4	G-2
Moderately Negative	Highly Negative	Neutral-to-Low

Source: Moody's Investors Service

Environmental
MGL faces moderate exposure to environmental risks, in line with peers, primarily because of its portfolio exposure to carbon transition risk as a diversified bank. In response, MGL has developed climate risk management strategy and reporting frameworks, incorporating environmental considerations in its strategy and lending policies, including policies related to financing of coal-related businesses.

Social
MGL faces high industrywide social risks from customer relations (regulatory risk, litigation exposure and high compliance standards), and the area of data security and customer privacy. While the Australian regulators' focus on mis-selling and misrepresentation have identified weaknesses in some policies and procedures, extensive remedial actions are well progressed at addressing these deficiencies. The bank also faces industrywide moderate social risks related to societal trends – in particular, digitalization --- and the extent to which such measures could hurt earnings.

Governance
MGL faces low governance risks. The bank's risk management, policies and procedures are in line with industry's practices and are suitable for its risk appetite. While the bank has incurred regulatory capital add-ons for operational risk, its track record on execution highlights the strength of the group's risk management and control capabilities.

ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moodys.com. In order to view the latest scores, please click here to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Support and structural considerations

Government Support
We believe the probability that MGL would benefit from systemic support in case of need to be high. In contrast to many crisis-hit economies, we view the regulatory and political framework in Australia to continue to be favorable to bank creditor interests. We also note that, to date, the regulatory focus in Australia has been heavily on the preservation of systemic stability and that the Macquarie group as a whole has a significant presence in Australia's financial markets.

Within the group, we believe that the chief beneficiary of support would likely be MBL, and accordingly we incorporate two notches of systemic support in its A2 rating. We note that during the global financial crisis in 2008-10, only MBL was eligible under the government's guarantee programme for debt and large deposits.

Nevertheless, considering the high degree of operational and financial integration between MGL and its operating subsidiaries, we view their credit profiles to be closely linked. In particular, although there is a global regulatory trend towards “pre-positioning”, such as requiring separate, or easily separable, IT systems for different legal entities; we view the probability that, in a crisis, the Macquarie group could swiftly be unbundled to be relatively low and, consequently, we believe it increases the probability that the group would be supported as a whole.

MGL'S relationship to the ratings of its operating subsidiaries
MGL's A3 rating is positioned one notch below the A2 rating of MBL. MBL dominates the group both in terms of assets and earnings. MGL's rating is positioned in line with Moody's usual notching practice for holding companies, which recognizes the structural subordination of MGL's creditors to those of its principal operating subsidiary.

We assign the following ratings to MGL's principal operating subsidiaries:

» Macquarie Bank Limited has a baseline credit assessment of baa1. The bank's A2 / P-1 for deposit and debt ratings incorporate two notches of uplift for potential systemic support.

» Macquarie Financial Holdings Pty Limited is an intermediate holding company for some of the group's non-bank's entities. MFHPL's operations are closely interlinked: one of the group's four business lines cross over the boundaries between MBL and MFHPL. MFHPL's issuer rating incorporates uplift for systemic support as a result of its close integration with the bank.

We continue to view the Macquarie businesses as closely intertwined, with a high degree of operational and financial linkages. However, should in the medium-to-long run the transfer serve to sharpen the boundaries between the group's bank and non-bank entities, it could lead to greater divergence of their credit profiles and rating outcomes.

Ratings

Exhibit 9

Category	Moody's Rating
MACQUARIE GROUP LIMITED	
Outlook	Positive
Issuer Rating	A3
Senior Unsecured	A3
ST Issuer Rating	P-2
Other Short Term	(P)P-2
MACQUARIE FINANCIAL HOLDINGS PTY LIMITED	
Outlook	Positive
Issuer Rating	A3
ST Issuer Rating	P-2
MACQUARIE INTERNATIONAL FINANCE LIMITED	
Outlook	Stable
Issuer Rating	A3
ST Issuer Rating	P-2
MACQUARIE BANK LIMITED	
Outlook	Positive
Counterparty Risk Rating	A1/P-1
Bank Deposits	A2/P-1
Baseline Credit Assessment	baa1
Adjusted Baseline Credit Assessment	baa1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
Issuer Rating	A2
Senior Unsecured	A2
Subordinate	Baa3 (hyb)
Commercial Paper	P-1
Other Short Term	(P)P-1
MACQUARIE BANK LIMITED, LONDON BRANCH	
Outlook	Positive
Counterparty Risk Rating	A1/P-1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
Senior Unsecured	A2
Pref. Stock Non-cumulative	Ba1 (hyb)
MACQUARIE BANK LIMITED, SINGAPORE BRANCH	
Counterparty Risk Rating	A1/P-1
Counterparty Risk Assessment	A1(cr)/P-1(cr)
Senior Unsecured MTN	(P)A2
MACQUARIE FINANCE LIMITED	
BACKED Pref. Stock Non-cumulative -Dom Curr	Ba1 (hyb)

Source: Moody's Investors Service

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