TRANSCRIPTION

MACQUARIE GROUP LIMITED RESULT ANNOUNCEMENT

FOR THE HALF YEAR ENDED 30 SEPTEMBER 2022

28 OCTOBER 2022

[START OF TRANSCRIPT]

Operator: Thank you for standing by and welcome to the Macquarie Group Limited 2023 half year result. All participants are in a listen-only mode. There will be a presentation, followed by a question and answer session. If you wish to ask a question, you will need to press the star key followed by the number one on your telephone keypad. I would now like to hand the conference over to Sam Dobson, Head of Investor Relations. Please go ahead.

Sam Dobson: Well, good morning, everybody, and welcome to Macquarie's first half 2023 result presentation. Before we begin this morning, I would like to acknowledge the traditional custodians of this land, the Gadigal people of the Eora Nation and pay our respects to their Elders past, present and emerging. For those in the room, if you could please mute your phones before we start, that'd be great.

As discussed we'll hear from both our CEO, Shemara Wikramanayake and our CFO, Alex Harvey on the results, and there will be an opportunity for you to ask questions following that. We'll start in the room and then we'll go to the lines. With that, I'll hand over to Shemara to go through the result. Thank you.

Shemara Wikramanayake: Thanks, Sam, and welcome, good morning, everyone, from me as well. As usual, we'll kick off our half-year results by just noting the footprint of the business that we have and as we've shared many times, we have a very good, diversified portfolio of businesses across four Operating Groups. We have two annuity-style businesses, Banking and Financial Services (BFS), our Australian Banking and Financial Services business, and our global asset manager, Macquarie Asset Management (MAM). Then we have two global –markets- facing businesses in our Commodities and Global Markets (CGM) and our Macquarie Capital business.

These businesses give us good diversification through the cycle and resilience. In the environment we just had, we had an equal contribution from each of the annuity-style and the markets-facing activities. Now, those operating businesses are supporting by four important support groups: our Risk Management Group, our Legal and Governance Group, our Financial Management Group and our Corporate Operations Group.

All of our Group heads, I think, are represented either in the room here today or dialled in. So if you have questions, they will be here to speak to you.

So turning to the results for the first half, as you can see, we delivered a result of $A2.305 billion. That was up 13 per cent on the first half of last financial year and down 13 per cent on a very strong second half last financial year. The return on equity was 15.6 per cent, which is commendable in this environment.

Looking at the contribution from the Operating Groups, in terms of the result versus the first half last year, they were up 15 per cent and that was principally due to contribution from the markets-facing groups, which were up 35 per cent on that period. Looking at them versus the strong second half, as I mentioned last year, they were down 17 per cent with the annuity-style and the markets-facing being down on that very strong period.

Indeed, if we look at it over a longer period, and that's the last five halves, you can see the operating income and the profits and the earnings per share kept stepping up until the second half last year in which we had some very strong realisations and asset sales. So the result for this half is down slightly on that.

Our assets under management, as you saw at the beginning of this financial year, stepped up quite a bit with the two large acquisitions we did in the public investments area. In this half to September, they're up 3 per cent. The main driver there is investments being made in the private markets business and the benefits of foreign exchange movements, partially offset clearly by the movement in markets, particularly equity markets.

Then looking at the diversification of our income by region, you can see there the Americas were 38 per cent of our income, EMEA 24 per cent, Asia 10 per cent and Australia 28 per cent. You may recall last year the Americas had stepped up to 48 per cent, because of some very large one-off gains in the Americas, but I think this is showing a trend that we've been foreshadowing for a while, which is that the percentage contribution from the Americas and the EMEA region will continue to grow, particularly relative to Australia.

That's while Australia, as you can see on this slide, continues to grow in absolute terms, but the fact is we're quite mature in a small market here, whereas in North America and EMEA – or in the Americas more generally and EMEA, we are a small representation at the moment in very big markets. As we grow a little bit there, the percentage grows more materially than the Australian.

Now, looking at each of our Operating Groups and their contribution through this period at a high level, Alex will take you through more detail in a minute, but the asset management business, Macquarie Asset Management, contributed 31 per cent of our income in this last half year at $A1.402 billion. That is up 28 per cent on the prior comparable half.

Some features to note are in the private markets business, the equity under management is now at a record $A188.5 billion, having raised also a substantial record raising of over $A20 billion in this half, $A22 billion. We have dry powder of $A30 billion as we go into the next period. I'd also note that the Green Investment Group was brought over into the asset manager last year, as you may recall. That integration is going well. We've launched our offshore wind platform, Corio, in this period.

In the public investment side, the assets under management at $A520.7 billion are down 3 per cent. The main driver there, as we said, is market movements partially offset by foreign exchange. So a good contribution from the asset manager. Also, the Banking and Financial Services Group, 13 per cent of our income, up 20 per cent on the prior comparable period at a $A580 million contribution.

You can see there that every line of the business has continued its organic growth with our home loan portfolio up 13 per cent now at just over $A101 billion. Business banking, up 7 per cent at $A12.3 billion and we had inflows into our funds on platform, but they were down slightly due to market movements.

Now, I note also the quality of the book there in terms of the LVR at which we're able to grow our home loan portfolio also remains very strong. All of that growth is supported by, again, a big step-up in deposits, where we've had – the deposits grown now to $A116.7 billion.

Turning then to the market-facing businesses, commodities and global markets. The largest contributor in this half, 43 per cent of our income, and a result of $A1.996 billion, which was up 15 per cent on the prior comparable period. We had good solid contributions in the asset finance business, even though you may recall at the end of last year we divested the UK industrial and commercial Meters business, which took the book from $A6 billion down to $A5.7 billion, but a solid contribution there.

Then in our financial markets and our commodity markets businesses, we saw volatility driving increased client need and activity, an opportunity for us to step up and support our customers. So in financial markets that drove good results in increased earnings in foreign exchange, also futures and the financing activities in equity, derivatives and trading. In the commodity markets, we had an increase in terms of our revenue from risk management across all of power and gas, resources, global oil.

In the inventory management and trading income area, we did see gains from the gas and power business, but that was offset by the timing of income recognition in storage and transportation contracts.

Then Macquarie Capital contributed also 13 per cent of our income in this last half, down 12 per cent at $A595 million. The big factor there obviously is that activity levels are much lower in this environment and that's meaning that fee revenue is lower across areas like mergers and acquisitions, advice and capital markets advice. Having said that, our principal investment book has continued to grow, sitting now at $A18 billion. Particularly in private credit we've grown that book now to $A15 billion and we're having increased income from the credit side and we had some good realisations in this first half, particularly in real estate and in our digital infrastructure businesses.

So that's the contribution from the four Operating Groups. That was supported as ever by a strong funding and capital position, and you can see here that our funded balance sheet remains strong with our term funding still comfortably exceeding our term assets. We were able to raise $A15.4 billion of term funding in this half on top of the over $A48 billion that we raised in the last half. So we're well-positioned with our term funding. As you can see, we're sitting now with all of that funding over $A100 billion of cash and liquids.

In addition to that, I mentioned our customer deposits, the BFS team, have been growing very well and we're at $A122 billion now of deposits, up 20 per cent. So, good funding position and, also in terms of capital, a strong position where our Basel III surplus has gone from $A10.7 billion up now to $A12.2 billion.

Drivers of that clearly were the earnings in the first half offset by the dividend that we paid, a hybrid issuance that we did, contributing $A800 million and then the net absorption of capital in the businesses, which as you can see was not massive in this period. So in Macquarie Asset Management, there was $A400 million going into ongoing supporting the organic growth of that business; either seed assets for funds or co-investment into the new funds.

BFS continued to absorb capital in the growth of its mortgage book, its business banking book. In CGM, we had a release of capital and that's really counterparty credit capital that we're holding and driven by market movement. Then in Macquarie Capital, we had some investments; I mentioned we're growing the credit book in principal finance, and also some digital infrastructure investment.

Now, the large absorption of capital was in FX movements, which is offset by our foreign currency translation reserve. We also are sitting with strong regulatory ratios, well above the Basel III minimums, as you can see there. Given that result and where we're sitting with capital and funding, the Board has declared an ordinary dividend of $A3.00 for the half year. That is a 50 per cent payout ratio.

So with that, I'll hand you over to Alex to take you in more detail through the performance of the businesses and come back to talk about our outlook.

Alex Harvey: Thanks, Shemara, and good morning, ladies and gentlemen. As Shemara said, I'll now take you through more of the detail on the financial results for the first half and then talk about some other aspects of the Group over the last six months.

So starting now with the income statement, you can see here operating income for the half up 11 per cent from where we were in the first half ended 30 September 2022. Key drivers there, a 39 per cent increase in net interest and trading income, reflecting the growth in the loan books across the Group, together with the strong trading conditions that we saw.

You can see a 56 per cent increase in investment income and that reflects disposals that we saw across our green energy portfolio, the real estate assets within Macquarie Capital and the digital infrastructure assets. Those were partially offset by a reduction in fee and commission income, down $A420 million and a lower contribution from the share of joint ventures and associates.

Operating expenses were up 11 per cent also for the half, versus the first half of last year, and the key drivers there really were the increase in employment expenses reflecting higher average headcount in this half versus the first half of last year, wage inflation coming through together with higher profit share expense and share-based payments expense reflecting the underlying performance of the Group.

The income tax effective tax rate for the half was up at 24.3 per cent, so the bottom line, just over $A2.3 billion, up 13 per cent from where we were in the first half of FY22.

Turning now to more of the detail for the individual Operating Groups. Starting with the asset management business, you can see profit for the half up at $A1.4 billion, up 28 per cent from the first half of last year. Key driver there was the increase in investment-related income coming through largely from the disposal of the assets in Green Investment Group that we transferred into Macquarie Asset Management during the half, net of the gains that we saw in the first half from the disposal of the Macquarie Infrastructure Corporation (MIC) assets in the first half of last year. So a step-up in investment-related income on a net basis.

Expenses were down during the period, largely reflecting the fact that we have one-off costs associated with the acquisitions, particularly Waddell & Reed in the first half of last year. You can also see base fees up $A16 million. There's a couple of things that are worthwhile highlighting there. The private markets-based fees were up 12 per cent. We obviously had favourable foreign exchange movements coming through. They were partly offset by the market moves across our public investments business, together with outflows across some of our equity portfolios and the public investments component of that business.

In terms of the underlying drivers, our assets under management are obviously key. On the left-hand side there, you can see the private markets space. A really good period of investing, nearly $A23 billion of additional assets under management through the investment activities across the platform in the first half.

Favourable FX, so pushing up the assets under management by $A36.9 billion. On the right-hand side there you can see the market moves over the first half offset or mostly offset by the FX effect that we had coming through on the public investment side as well.

Turning now to the banking and financial services business. Obviously a really strong result, $A580 million, up 20 per cent from the first half of last year. That really reflects the growth in the loan books. It also reflects the recovery in margins that we're seeing coming through that business. In terms of the segments, personal banking up $A119 million. That reflects an average – a 30 per cent average growth in loan volumes in our mortgage business.

Although we did see a moderation of the growth in those loan volumes towards the second half of the first half in FY23, a really strong result from the mortgage perspective. On the business bank, up $A55 million, so we saw a growth in the loan books. We also saw a growth in the deposits. We had better margins and better margins on the deposits coming through that business.

Wealth management income up $A76 million, reflecting the growth in deposits and improved margins on deposits coming through that business. Then you can also see the step-up in expenses. We've talked about this for a while now. The team in BFS is investing heavily in the platform, increasing headcount to support the growth that we're seeing coming through there, increased investment on the technology side to make sure the platform supports the digital business that Greg Ward and the team are running down there and obviously, investment that we're making across our regulatory obligations and compliance obligations. So you saw that coming through for the first half as we foreshadowed.

In terms of the underlying drivers of the business, home loans are up, business loans are up, deposits are up. We saw a partial reduction in the platform. Assets, obviously that's mainly market moves coming through over the first half. You can see the fall-off in car loans there, remembering that we sold obviously the dealer finance book in particular in the second half or we completed the sale of the dealer finance book in the second half of FY22.

So turning now to the first of the markets-facing businesses. The commodities and global markets business, up just under $A2 billion worth of contribution for the half, a really strong result. Obviously we had strong conditions across most of the platform in CGM for the first six months of the year.

Turning to the component parts, you can see commodities up $A635 million, about 50 per cent up on where they were for the first half of last year. Pleasingly, we saw a step-up of $A547 million in the contribution from the risk management aspect of that business. That's where we're providing derivative solutions to clients. We've had an expanded client base there. Obviously we saw strong conditions, lots of volatility, lots of transaction activity in the first half.

We particularly saw good contributions across gas and power and that's obviously become much more of a global business, so we saw contributions across all regions in the gas and power business. We saw an increased contribution from the resources segment there together with global oil.

On the inventory management and trading, up $A20 million from the first half of last year. We saw good trading gains, particularly through the North American gas and power business, offset by that timing of income recognitions associated with the transport and storage assets that are used in that business, both in North America and also in Europe.

We had pleasing results from the financial markets perspective, up $A263 million, just over 70 per cent increase from that business last year. And that's obviously FICC, futures, credit markets - that sort of business in our CGM business. Up $A263 million, a 70 per cent increase.

Obviously we saw lots of transaction activity through the first half. The other thing we saw and I think would be very familiar to people is volatility in FX markets and interest rates.

We saw a lot of volatility particularly through the first half of the year in that business and the business was able to provide solutions to help clients manage that risk over the course of the first six months of our year.

Investment income down $A523 million. That largely reflects the gain that we saw in the first half of FY22 from the disposal of the industrial and commercial meters business in CGM.

And you can see expenses up over the period. Again, reflecting an increase in - slight increase in head count. In average terms, the head count is up about 5 per cent. We also saw - we see the investment that the team has made in the technology platform to support the business together with the investments being made in regulatory and compliance obligations in that business.

In terms of the underlying drivers, again, a chart hopefully that's familiar to people. You can see in the top right-hand side there. You know, the key driver to this business obviously is client numbers. Actually being able to provide services to more clients in more regions more often. And we see that continuing through the first half of FY23.

You can see that reflected in the underlying operating income. The underlying client business driving the big step up in operating income for CGM for the first half.

And from a capital perspective, I'm sure people recall, March 2022 was quite an elevated level of capital in CGM. That's remained pretty consistent from period to period. Although we did see a spike in capital usage, particularly in the middle part of the half with energy markets across the world.

In terms of Macquarie Capital, a more subdued period. Not surprising obviously with transaction volumes. So if you look at where we are for the first half, $A595 million of contribution. And you can see the component parts there. Fee and commissioning come down 23 per cent from the first half of last year. And that's both from an M&A perspective together on the capital market side.

Operating expenses up through the period. Again, the investment that the team is making in the platform to support the growth of the business going forward. And those two are partly offset by an increase in investment related income. And it was good to see the disposals coming through. the real estate assets that Macquarie Capital have on their balance sheet together with the digital infrastructure assets that the team has been working on and building over the last couple of years. We also saw an increased contribution from the principal finance portfolio, up $A89 million in terms of the contribution for the first half of FY23.

As I mentioned, one of the key things for Macquarie Capital is the capital we have alongside our clients there. And you can see what's going on in this chart. Up from $A3.6 billion to $A4.1 billion at 30 September 2022. And the primary mover there I guess is the increase in debt that you see coming through, together with the increase in digital infrastructure and the team has found some additional investment that they've been able to make in Philippines Tower portfolio over the course of the half. So it was good to see that coming through and obviously that capital partnership should pay off into future periods.

So that's the operating groups. I might now turn to a couple of other aspects of the financial result for the half. One of the things that we have been doing over the last few years is investing significant amounts in the platform to support the type of organisation we want to be, to support our ability to grow going forward, and obviously to meet the obligations that we have across the Group.

So we set out a couple of slides here which illustrate some of where that expenditure is occurring. And firstly, maybe to start with the regulatory compliance slide. Up 41 per cent from where we were in first half of FY22.

There's a couple of aspects there. You can see an increase in regulatory change and project expense is up 60 per cent from the first half of 2022. Some key programs of work there. We're doing end-to-end capital and liquidity transformation across the Group.

We're obviously working on our APRA remediation program that we talked about before. And we're continuing to uplift the focus on non-financial risk across the Group.

Now, some of that finds its way into business as usual spend. And so you can see that up 33 per cent from the first half of FY22. Obviously there's an ongoing obligation to meet our obligations.

Also some of that project spend that we see, that translates into ongoing business as usual expenditure, coming through our regulatory compliance efforts.

Then on the bottom part of the chart, you can see the technology spend over the last few years. Up an annual growth to 12 per cent over the last four or so years.

A significant investment is being made to support the growth for business. In particular, and there's obviously lots of activity here, but in particular, the team is making a significant investment in data and in data analytics, in end-to-end straight through processing, and all the way to cyber. And of course, increasing the use of cloud capability across the Group.

Now in terms of the central support areas, another area we've been investing heavily over the last few years. You can see here the expense is up FY22, nearly $A2 billion in the first half of FY23. $A1.26 billion of expenditure across corporate operations.

And what COG is doing, apart from running the operations of the Group, particularly focused on data, data analytics, automation, machine learning, helping us actually meet our obligations but also position ourselves to grow.

From a financial management perspective, modern financial management. Thinking about real time analytics to support the Groups. And then from risk management perspective, you can see the focus around non-financial risk and uplifting our capability to manage risk across the organisation.

So these are very significant investments that we're making to support the platform, further embed and strengthen the foundations of the Group, enable better risk management. And of course the other thing that's very important is enabling the groups actually to nimbly move towards new opportunities to actually change and adapt and actually see opportunity coming forward. All these investments that we're making in the central support groups are important to do that.

During that period of time of course, what we've been able to do is deliver an average return on equity over that same period of time of about 16 per cent. So we were able to continue to deliver despite the increase in costs. And of course what we think we're doing is setting up the business to be well positioned for the future.

In terms of the balance sheet, and Shemara mentioned it obviously, very consistent story. Solid, conservatively positioned balance sheet. Pleasingly we saw the opportunity to raise $A15.4 billion worth of term funding over the course of the half.

That was split pretty evenly between term funding for the Bank and term funding for the Group. The diversity of issuance is something we've talked about before.

We continue to look for new pockets of funding to support the efforts of the Group. Obviously from weighted average life, the term funding is quite long dated, supporting the activities of the Group.

In terms of the deposit story, up at $A122 billion worth of deposits. Up 19 per cent from the half and I think what's really pleasing about this story in particular is what's happening in BFS. Expanding the product portfolio, tailoring products to meet the customer demand. And over the course of this half, we saw a really good step up in our transaction and savings account.

That account actually is something we introduced I guess about two and a half years ago. So that's now growing nicely. The other thing we saw is the opportunity to grow our retail term deposit portfolio.

In terms of the loan and lease portfolio, up 11 per cent. You can see the key drivers there. Home loans at the top of the page, really driving the step-up. And the other thing we've seen during the half is the increase at the bottom of that stack really in the corporate and other lending which is the private credit business - largely the private credit business that Macquarie Capital has been growing over the last few years.

From an equity perspective, up $A1 billion on where we were for FY22. I guess the main thing to point out there probably is the use by MAM, the asset management business, of the balance sheet putting their foot on seed assets that will ultimately make their way into new mandates and new products for customers in that private market business.

In terms of the regulatory update, lots of things going on. I mentioned that obviously previously. A couple of things to point out here firstly. In relation to the new capital standards, they obviously become enforced at 1 January 2023.

Been a long time coming. We're obviously pleased that that process is now complete. We're obviously well advanced in terms of our preparation for that and have been holding capital aside for those changes for some time.

The other thing I might point out is just the work that we're doing with APRA in relation to the MBL remediation program. A really important piece of work.

Obviously the end result of the program is improved processes, improved systems, improved frameworks and plainly, we think it will further strengthen the risk culture across the organisation.

In terms of the Bank capital ratio, it’s very strong at 12.8 per cent. As is the liquidity position in terms of the LCR itself but also the unencumbered liquid assets and cash that we have on the balance sheet, over $A75 billion.

And finally from me, in terms of capital management, just a couple of things to mention here. During the period out of the Group, we were able to issue a new hybrid, raising $A750 million.

We were also able to do a tier 2 issue out of MBL, raising $A850 million so we appreciate the support that we get from investors across each of those areas.

And the final thing to mention for me, in terms of the interim dividend, the Board has resolved that no discount will apply for the first half FY23 dividend reinvestment plan and that we intend to apply shares on market to satisfy any applications under that plan.

So with that, I'll hand over to Shemara. Thanks.

Shemara Wikramanayake: Thanks, Alex. So I'll take you through the outlook now. Starting as usual at the short-term outlook, and as you know, we look at this by each of our operating groups.

So first of all, Macquarie Asset Management. We're expecting the base fees in this business to be broadly in line with last financial year and that's because the investing that we're doing in the private market and the acquisitions that we've done on the public investment side are substantially being offset by the market movements that we've had over this financial year so far.

In terms of net other operating income, we expect that to be significantly down on last financial year because we won't have the repeat of the large contribution we had from Macquarie Infrastructure company, despite the higher performance fees we expect which will partially offset that.

And similarly with the Green Investment Group. We had some very large realisations last financial year. So we expect this year's contribution there to be significantly down, again despite the material gains and realisations we had in the first half of the financial year, we don’t expect that to recur in the second half.

Then with banking and financial services, we expect growth in the loan portfolio, deposits and platform volumes to drive earnings. But as Alex mentioned, we're seeing a slowing in the rate of growth there.

We also expect market dynamics to continue to drive margins and we also expect higher expenses as we continue to invest in areas like volume growth, technology, and regulatory requirements, and we will have ongoing monitoring of provisioning in that business.

Macquarie Capital, subject to market conditions as we noted. Transaction activity is expected to be substantially down on a record year last financial year with market conditions, as we've seen, weakening in this financial year.

Investment related income we expect to be broadly in line due to the increased revenue from the growth as we mentioned in our private credit book in principal finance, but offset by lower revenue from asset realisations.

And again, Alex and I mentioned we had some good realisations in the first half of that business but we don’t expect that to recur in the second half of the financial year. And as we both mentioned, we're continuing to deploy the balance sheet in that business in credit and equity.

And then in commodities and global markets, we expect increased income from the commodity business compared to last financial year after taking account of the impact of timing, of income recognition in our gas and power transportation and storage contracts.

And we also expect an increased contribution from financial markets across our client and trading activities. And you've seen that in the first half as well. And then continued contributions from the asset finance business.

At the corporate level, we expect a compensation ratio and the tax rate to be in line with historical ranges and outcomes.

Now, that short-term outlook as ever, remains subject to a number of factors and some of the ones that apply at the moment are clearly the market conditions which include global economic conditions, inflation and interest rate outcomes, significant volatility events, and the impact of geopolitical events we're seeing playing out.

It also is subject to the completion of period end reviews and the geographic composition income, the impact of foreign exchange, and potential tax and regulatory changes and other uncertainties.

And so we continue to maintain, as you've seen, a cautious stance with our conservative approach to capital funding and liquidity which we thinks positions us well for all environments but particularly the current environment.

And turning to the medium term. We continue to believe that we're well positioned through, as I mentioned at the beginning, the diversification of our footprint across business lines, across geographies.

Supported by our ongoing investment in our platform but in a disciplined way in terms of managing our cost base, our strong and conservative balance sheet, and our proven risk management framework.

And you can see that play out in terms of the returns we've delivered. Alex mentioned a 16 per cent average over the last five years across the Group. In our annuity-style businesses over the last 16 years, we've delivered an average 22 per cent ROE and have done that again in this first half.

And in our markets-facing businesses, we've delivered an average 16 per cent over the last 16 years and 20 per cent in this most recent half. And even after our $A12.2 billion surplus capital, as we mentioned, we've delivered a 15.6 per cent ROE in this half.

So with that, I will hand back to Sam to take questions.

Sam Dobson: Great. Thanks Shemara. So as I said, we'll start with questions in the room and then we'll go to the phone lines. John? Just at the front. Thanks.

Jonathan Mott: (Jonathan Mott, from Barrenjoey) Question on slide 30. On the commodities business on the left hand side it shows really good growth coming through. Especially seeing it come through from the commodities risk management side continue to grow period after period.

I understand the volatility has been very good for that business in the last little while but given the environment's unlikely to reduce volatility given global events that you called out, as well as the decarbonisation leading to some pressure on sustainability of energy over the next little while, why wouldn’t we see that continuing to grow?

You tend to always try to be a conservative and say how it's a great period. But you can see the light green box there has continued to grow. It's hard to see why that would turn around any time soon.

And then a following question is if you then look at the inventory and management trading, I understand the box at the very top. It goes up and down and there's timing, we've heard about that many times.

But it tends to be very seasonal and you're coming off a very low period in the first half. Why is it so seasonal? And why wouldn't that recover into the second half which would potentially offset some reduced volatility that's coming through from other parts of that business?

So it seems like this business is pretty well set up.

Shemara Wikramanayake: Yes. Thanks John for that couple of questions. And I think you're right that ultimately medium-term we're growing a franchise here where we're increasing the markets in which we operate for customers, producers, consumers, et cetera, that we support.

And as you've seen, we've grown from North America into our franchise growing in Europe into Asia. So over time, that's what we're focused on, is patiently adjacently growing the franchise.

Having said that, we call it a markets-facing business because in any particular period, it's going to be impacted by the activity levels and the volatility persisting.

Now, that may look seasonal when you look at the last two financial years. But actually, it can vary completely. And we had a very active first half of our financial year this year with the issues. For example, if you look at the European gas and power market, what went on there.

TTF went up to 350, unheard of, with the curve having sat at 20 to 30. That's now abated a lot. Germany is sitting with 96 per cent storage as we now go into the winter. We're having slightly warmer temperatures.

So things have come off a lot. In fact, the price spot was negative. So ultimately, the level of market activity within any period, it's not really seasonal, can really impact both our risk management service income but also our inventory management and trading.

But medium-term, we're looking to really keep growing those franchises as you say, especially with energy transition et cetera. With the inventory management and trading, we did highlight - Alex mentioned as well, that the storage contract in European gas and power do mean that we had basically timing of income recognition impacts that should come back this financial year.

Nick is sitting in the front row. I might let Nick add to that. Nick, if you have anything you want to elaborate on? But I guess my overall comments are medium-term, growing a franchise. Short-term, environment impacts.

Nicholas O'Kane: Thanks Jonathan and Shemara. Yes, look, I'd reiterate what you're saying there, Shemara, in terms of the focus that we've had over times in terms of investing and growing the franchise. Particularly in terms of the clients servicing nature of the business.

And we do think that over time, the services that we provide will be important for the client base, particularly as we work through the transition.

And we're establishing the business to be able to adopt - to evolve and adapt to the needs of the customers as they change. And indeed, a lot of the conversations that we have with our clients on a daily basis are about these types of subjects. So we'll continue to invest in that.

In terms of the inventory management question, to Shemara's remarks earlier. Whilst it may appear at times that this can be seasonal, what we have seen over the course of the last half is truly exceptional conditions and they have subsided.

So not only what we've seen in Europe but we've also seen something similar happen in the US. Where if we just look at the benchmark price for natural gas in the US, which is Henry Hub, we went all the way up to $US10 and back down to $US5 twice.

And heading into the US winter, inventory levels are very healthy and also our production levels. So, the market seems to be well placed going into the Northern Hemisphere winter.

Sam Dobson: Brian at the front.

Brian Johnson: (Brian Johnson, Jefferies) Perhaps I could ask that same question a slightly different way, perhaps some numbers around it. If we have a look at the difference between the economic accounting and the accounting, it periodically seems there's a big gap that widens which unwinds over the subsequent periods. I'd just be interested in the total size of that unrecognised balance sheet asset and the timing that we should think that it unwinds over, because like a hidden reserve, I'm guessing it unwinds over two years?

The second one if I may is that when we have a look at the bank balance sheet, it is extraordinary how much liquidity you've got there. So, we can see the LCR is not really 175 per cent, it's 180 per cent something because you guys take out the CLF, your peers don't. You've got a massive balance of unencumbered balance sheet liquidity, everything you see, it's long duration funding. Shall we be thinking that this is an opportunity just to raise more deposits or it's telling us about future growth? Or is it in fact telling us something about what happens to global liquidity going forward?

Shemara Wikramanayake: I'll briefly comment and then hand over to Alex. But the accounting versus economic impact, Alex can take you through the details, but the timing of the reversal of that can vary depending on whether it's storage in Europe, transportation contracts in Americas et cetera. So, Alex can give you a bit more colour on that. In terms of the liquidity, we are sitting with big liquidity at the moment, but as you know we run prudent balance sheets throughout the cycle and we're in very uncertain economic times at the moment. So our view is if we can be returning a 15.6 per cent ROE and sit with the surplus capital we have in the prudent termed out funding we have, we think it behoves us through this next cycle to be positioned for upsides and downsides with sitting with that particularly strong balance sheet.

Alex Harvey: Thanks, Shemara. Just on the timing, the income recognition on the storage and transport, there's a lot of variables in that. I mean obviously spread moves are one thing, so that obviously is a factor, then how those spread moves over time, those spread move over time and so that's not something that - and then I guess the third thing is there's a portfolio of contracts that we have access to pipelines or storage facilities , we have access to and we're often doing new deals, new powerlines or new transmission capabilities.

So, there's a lot of variability in that particular line. What we've done obviously Brian, is try to, without sharing, because there's a lot of moving parts there, without sharing the details of all those moving parts because some of them are obviously future forecasts of what happens with prices. Just put all that together from our viewpoint with all that we know and saying look if you look at the commodities income, we expect it to be up including the impact of what's happening with income recognition around gas and storage and transport contracts.

We think that's a better way to think about it. They're obviously an important part of the business, we have really strong businesses based on both our physical presence and our financial presence, it gives some accounting versus economic mismatches, but overall when we look at it, we think that the full year guidance is a better way for you guys to think about how that might mean from a Group perspective.

I think Shemara covered the liquidity point very well obviously and I agree with what she said. A few things, your market conditions through last year obviously very supportive, so if you looked, we raised over $A48 billion of funding last year. Just to put that in perspective, ordinarily you would have seen us raise $A25 billion to $A30 billion of term funding a year, so there were opportunities for us to, because of the market conditions both length and the maturity of the balance sheet and also take advantage of the conditions that we found, we obviously continued that over the first half. That seemed to make economic sense anyway to do it.

There's a few other things that are happening, you need to look at the growth of Greg's business obviously essentially deposit growth funding that business and we're getting in front of that deposit growth or the growth of the mortgages through raising the deposits. You've got the TFF that needs to be refinanced in a couple of years' time, so getting in front of that exercise makes sense. You've got the CLF being withdrawn from the market, Brian, so I think I'd put it in the context of the broader story, which is from a Group viewpoint, the underlying philosophy is conservative, strong balance sheet, be prepared for I don't know what the future holds but make sure you try to get in front of it. So I think it's probably that.

Operator: Andrei?

Andrei Stadnik: (Andrei Stadnik from Morgan Stanley) Morning. I wanted to ask two questions, maybe I'll ask them together just in the interests of time. In terms of MAM and the Green Investment Group in particular, there was almost towards $A1 billion investment related income in this half, but it doesn't look like there were a lot of major green fund launches to offset this. How are you thinking about changing the mix of revenue in that business down going forward? Are you doing enough in terms of green fundraisers?

Then my other question of course, how are you thinking about cost flexibility in case revenues do stay subdued a little bit longer? We note that Waddell & Reed and capital integration costs will fall away, but are there any other cost factors you're thinking about?

Shemara Wikramanayake: Thanks, starting Andrei first with the question on the Green Investment Group, we moved it over to the asset manager last year as you know, at the end of last year, and there's several billion of balance sheet there which we will continue to either run off and realise principal gains or bring over to be seed assets for funds. So, you'll see some realisations but gradually we'll shift much more to base fees and performance fees. Now in MAM we already had the growth series of funds, the global renewable energy funds, so we'd done Fund 1 and Fund 2. What we found by bringing Green Investment Group across is the deployment stepped up a lot because the pipeline of investments they access by doing this has stepped up a lot. So, MGREF2 has got invested a lot quicker and hence we launched into MGREF3 which is a more mature energy fund. In addition to that we're raising an energy transition fund, the acronym for that is MGET and so that's out on the road and that's going very well, meeting good demand. What we intend to do as we do with all our asset management business is be very disciplined about the size of these funds.

So, we've seen others raise very big energy transition funds. I think we're going to pace ourselves and keep raising, reflecting our ability to get really well invested, because for us that's the biggest thing is to be delivering superior return to investors on each of these funds and gradually build a very big franchise there. So, I think the team have very good capacity to invest, but we don't want to go beyond their capacity while they're also realising assets. Then in terms of cost, we do say that we're disciplined on costs, and we thought it was important to share that we are still investing a lot in our cost base, even though we say we're disciplined, we want the business to be really strong and resilient.

As Alex mentioned, we're investing in areas like automating our end-to-end processes and making them more robust in non-financial risk responses, regulatory compliance. But at the same time in our businesses, we're constantly looking at how we can be most efficient. So, as you say, there's big cost savings from the integration of Waddell & Reed and also AMP happening in the investment bank, we're constantly looking at where we position the business to drive efficiency. Greg's sitting here in the front, and I know you're investing a lot, Greg, in BFS, but at the same time both you and Nick sitting there are constantly looking at how we can do things more efficiently.

I don't know if you have a couple of examples you might want to share in terms of those you grow? Could we just give Greg a mic as well, just to give you, Andrei, a sense of everybody is owning return on not just capital but OpEx investment.

Greg Ward: Thanks, Shemara. As you say, big investments in regulatory compliance and all the emerging rules there and that's super important for a business like this. Enormous investments in cyber and fraud management and so forth and we've seen just how important that is, so we continue to invest. But in the business bank an origination platform and our online banking capabilities to the business bank, and of course we're upgrading the platform on the wrap side as well, so more solutions, so there's a lot of investments.

Shemara Wikramanayake: I think your cost to income ratios are actually improving.

Greg Ward: They're gradually improving, particularly in some areas, but offset by some of these investments and of course we're not building for the business to be the current size, we're trying to build and scale this business to be much, much bigger.

Shemara Wikramanayake: Thanks.

Operator: John?

John Storey: (John Storey, UBS) Thanks very much. Appreciate the detail on the costs, so thanks for that slide. Got a question on FX sensitivities and just trying to understand what the results would look like on a constant currency basis? Obviously you provide what the revenue is and where it comes from, but would be interested just to get a sense on bottom line cost and currency earnings. Then the second question I have is around capital allocation, BFS obviously continues to grow very strongly. Wanted to get a sense obviously that BFS ROE is a little bit lower, so just get some insight into the ROE and how the Group thinks about continuing to support that division, thank you.

Shemara Wikramanayake: I might answer the first question and then I'll hand over to Alex for the second. Basically the way we look at ROE, we have hurdles for every business line we're in, not just at the operating group level but underlying in the operating groups for each division we're in. So, if we're doing private credit in Macquarie Capital as opposed to private equity, we will have benchmark returns that we think we need to reward us for the risk. If we're hitting those benchmarks then we're happy to support those businesses. So, for BFS we have a hurdle if BFS is beating that hurdle which is happening comfortably, we're happy to deploy more capital.

Now in MAM, which is a low capital-intensive business, we have much higher ROE. So the Group ROE is a blend of all of those ROE into the various businesses. We're not prescriptive about what mix and weighting we want. We try to invest in all of them so they're all growing together, but ultimately the Group ROE is a result of where the mix is across those businesses, but in each of them we're very disciplined in what do we need to put a dollar in, not just MAM but in public investments versus in real estate versus in private credit.

Alex Harvey: Thanks, John for the question on FX. Obviously as you've seen from the slides previously, if you look at 70 per cent of the income being our offshore, then there's a relationship – 10 per cent depreciation one way or appreciation, we'll talk about 7 per cent so that's the general rule. The first half was relatively unaffected from an FX viewpoint, because if you think about it, it's a bit of a mixed story, the Aussie's obviously depreciated against the US, but the Pound's been pretty weak, the Euro's been pretty stable. So, if you think about the diversity of the business, the FX story across the Group is a pretty muted one other than the US.

The other thing obviously is the FX generally from a revenue viewpoint, it's mainly affecting the flow type businesses, if you think about the asset management business, particularly the public investment side, it obviously affects that where you've got regular flow of income. Where we're doing transactions you obviously swap it back into Aussie dollars, effectively the day the transaction's done. So, relatively muted affect. It would have been less than a percent or two in terms of the bottom line, from an FX perspective.

We hedge our capital as Shemara talked about before, and you can see that movement coming through the other foreign currency translation of reserves, so where you got a depreciating Aussie against the US, you obviously want to make sure your capital's balanced in your risk weighted assets you go against your US portfolio, but other than that I guess that's the answer to the question.

Shemara Wikramanayake: I think as our foreign income grows, we try to match our funding as well in those currencies, but basically we haven't adjusted for FX rates and the Aussie's been up to parity and down to $A0.50 over the years, but we've still managed to deliver these mid-teens ROE through...

Alex Harvey: Should say 1 per cent to 2 per cent pre-profit share, pre-tax.

Shemara Wikramanayake: Yes.

Sam Dobson: Right, we've got a few questions on the line so we might go onto the phone line please.

Operator: Thank you, your first question comes from Andrew Lyons with Goldman Sachs, please go ahead.

Andrew Lyons: (Andrew Lyons, Goldman Sachs) Thanks and good morning, just a question on your outlook, you've noted that while realisations in MAM and MacCap were strong in the first half, they appear to be largely done for the year with certainly much lower levels expected in the second half. Therefore the divisional guidance would appear to imply a reasonable step down in NPAT for 2H versus the first half. So, to the extent that this is a fair characterisation, can you perhaps talk to the extent to which the expected step down in realisations in the second half is cyclical or structural and therefore what it might mean for looking into FY24 and beyond?

Shemara Wikramanayake: Thanks, Andrew for that. The realisations in both Macquarie Capital and Macquarie Asset Management are lumpy because basically we're realising assets at whatever the time is to get the best return for that asset. So, if we have to wait three years, we wait three years, if it's worth doing now we do it now. So, as you've seen historically there's been quite a bit of lumpiness. In Macquarie Asset Management we mentioned that the performance fees will probably be higher in the second half than the first, it's just the timing of when the assets are realised. But we had a big Green Investment Group realisation in the first half and when we look at the pipeline of when the best time is to keep running off that Green Investment Group balance sheet, we don't see things to that extent that we'd realise in the second half.

Same in Macquarie Capital, we had a real estate asset we held for I don't know how many years, I know Michael Silverton's on, but five years at least and this was the best time we've been working on it for a while that we've realised in a digital infrastructure a couple of assets as well. So, it really is driven by, I don't know that it's cyclical, it basically is when is the best time to realise the asset? We will take into account external market factors in that, but also very much what's happening with the business, and we've driven the change that we want to get it to the point where it makes sense for us to exit and let somebody else then own that business.

In terms of cyclical versus structural, the environment, we've had these environments before ups and downs. Macquarie Asset Management, Ben Way's on the line, I know it's early morning for him but I might let him speak briefly, but we're sitting with $A30 billion of dry powder and I think we're going to be, as we always have been, very disciplined about when we invest it, when we realise assets, all driven by long-term how do we get the best return for our investors in these funds and keep our franchise going?

But Ben, are there any cyclical points you want to comment on, or structural?

Ben Way: I think, Shemara, the point is that I think we all acknowledge that the environment will be a little bit, is a bit more challenging than it was 12 months ago, but I think as you can see from say our fundraising, there's still very strong support for people wanting to be allocated in terms of our size base, to things like real assets, so we continue to see very strong support for all our funds in the marketplace and we expect that to continue through to the rest of the year.

Equally, I think the way there's still significant investment opportunities for us despite the changes in the macro environment, particularly around energy transition and digitalisation. As a consequence of that there's also still strong demand for our assets. So, I think you've made the right point, Shem, we are disciplined, we do take a medium to long-term view, our job is to make sure that we get the best returns for clients. So, we remain optimistic about the market both in terms of deployment opportunities but we're at 8 per cent from a realisation point of view because there remains very good appetite for people to be allocated to particularly things like real assets.

Shemara Wikramanayake: Yes, and overall for the Macquarie Group, we don't put any pressure on Macquarie Capital or Macquarie Asset Management to be realising in a period, because the Group's diversified and as you can see in a time like this, the commodities business is contributing strongly, the banking business is contributing strongly, so we can empower them to be realising assets at the best time for the return on that investment.

Andrew Lyons: That's really helpful, thanks Shemara. Just a second one just despite a difficult in the MacCap business, I know you did continue to invest in the franchise, which was a bit of a drag on the profit contribution. I guess with Green Investment Group now out of that division, can you perhaps just talk in a bit more detail about where you see the opportunities within MacCap and where that elevated investment or the step up in the investment is being particularly focused on?

Shemara Wikramanayake: Yes, I'll let Michael Silverton, who's on, comment in a minute as well because he's dialled in from the US. But basically there's still a lot of opportunity to support the deep expertise of our bankers with balance sheet across Macquarie Capital. The private credit book we talked about that's now at $A15 billion and is investing principally in North America's about 58 per cent of that book and then Europe another big part, so Australia is just smaller. Then I think there's four areas in equities where we invest, we've got the tech venture style early-stage investing, which we've been doing for a long time as you know and had some excellent investments there.

There's the growth equity that we invest in in the Americas principally, which is government services type say for really revenue generating businesses, a little bit further along the growth curve that we have a great track record in and a DC expert team. We have our infrastructure and energy principal investments, we've done a few PPPs you've seen the Maryland DOT, the Pennsylvania DOT that we've done recently, and then in our private credit principal finance team we also do investments in more mature equity positions. So, Energetics was an example of that that we've done.

So, there are four areas. Basically we look for areas where we have some deep specialist expertise relative to the market and we support those people. They're very disciplined in their investing, a lot of what we're doing is bilateral proprietary investing, and the risk management team which Andrew Cassidy heads up, sits very strongly alongside them and we've had decades of investing in all these four areas. Michael, any comments you would like to add?

Michael Silverton: Thanks, Shemara. The only comment I would add is that offshore we're still relatively small in terms of our market share. So in those sectors that we focus there's a lot of opportunity and from a principal standpoint we're still seeing opportunities from a growth perspective and private credit is growing as a sector and our share of that market continues to be there. So we continue to see good opportunity across the board.

Then also as we become more international in these sectors there's cross-border opportunities as well that we can benefit from. But clearly the capital markets have been challenging for us over the last period. You can see that the reduction is smaller than what you would have seen in the broader market and that is in part because our scale is such that we can focus where we see the opportunities.

Shemara Wikramanayake: Those are all good points. Thanks.

Andrew Lyons: Thank you very much. Appreciate that.

Operator: Thank you. Your next question comes from Ed Henning with CLSA. Please go ahead.

Ed Henning: (Ed Henning, CLSA) Thanks for taking my questions. Just my first one, a little bit of follow-up just on the equity and investments. If you look at all the categories there on slide 39 can you just touch on where you're actually seeing pricing pressure on the market, where you've taken some impairments and also which categories you still have really strong demand if you were to realise them in the current marketplace? That's the first question.

Shemara Wikramanayake: Alex, did you want to take that one?

Alex Harvey: Yes, sure. So just a couple of things. Probably the most obvious area of pressure, not just for us but generally, has been in the technology sector. I think you've seen that has been pretty widely reported. That is probably the area where there's most pressure. That's the first thing. Secondly, most of these things, Ed, as you know, we hold at amortised cost. So we don't remark these things through the balance sheet. In many cases they're quite seasoned investments that are probably in the money in the first place. So the level of impairment that we saw coming through the first half was pretty modest.

I think I made the point there was, as is sadly often the case there's one or two positions that are underperforming their expectations and we take impairments, but it was a relatively light half in terms of impairments coming through. In terms of the underlying story, obviously I think Ben touched before on the infrastructure space. There really continues to be strong demand for infrastructure assets, particularly they tend to offer a higher yield and in some cases are inflation protected. I don't think we're seeing anything from a transport industrial infrastructure perspective. The PPP sectors that Shemara talked about before for the infrastructure space we're seeing good demand there.

Our digital infrastructure, I made the point that we obviously divested of a digital asset in Europe during the period and divested well. We obviously invested in a new digital asset over the period, so we feel good about where pricing is there. Green energy, we're not really seeing any sort of softness. So generally speaking, I think we're not seeing that many – we're not seeing impairments come through and, again, we don't mark these things to market on the way up, so we wait to invest generally speaking. So not seeing much impairment. As I said, probably the pressure more generally is on the technology side. But that is reasonably well telegraphed.

Obviously more generally, Ed, as you know, it's a pretty diverse book. So that's where we're at. What is happening to the capital market point that Michael made, with the capital market slowing down that tends to slow down transaction activity levels. Just financing to make the acquisition work tends to be harder to get. People are more cautious about proceeding and often, as you see a downturn obviously purchasers and vendors have a different view of price expectation. So it takes a while for that to normalise.

Ed Henning: That's great. Thank you. Then just a second one on GIG. Obviously you're having no issue raising money. Can you talk a little bit about the ability to deploy the money; are you actually seeing red tape being reduced for developments by governments or is that still talk? Then the other part of it is the new funds that you're raising, are you still taking all the development risk or are you going to start to see GIG actually in the funds, take some development risk and therefore take the profits with that as well?

Shemara Wikramanayake: So GIG, the investment environment is still huge. I think John Mott was talking earlier about the energy transition and we're seeing – ultimately what we need is massive investment in solutions if we're going to transition off the conventional ways we deal at the moment with energy, transport, agriculture, buildings, industry et cetera. The capital requirement is massive.

We are fortunate in that we have a team with very, very deep expertise to respond to some of that. We're seeing governments respond all over the world. You saw the Australian budget allowance for it. The US has introduced this new – they call it an Inflation Reduction Act that has a $US360 billion allocation to climate transition investments in addition to another $US110 billion that was allocated in the Infrastructure Investment and Jobs Act. So a huge scope of projects are now being developed in the US.

Here in Australia, for example, we've been involved in onshore wind, solar, hydrogen projects, EVs, EV charging. Offshore wind is now becoming a big area. So there is a massive pipeline of opportunity to respond that is getting government support to catalyse it in the developed and the developing world and a lot of interest from private sector investors either in the strategics to partner with us or financial investors to invest. So we're seeing a good pipeline.

If anything, the biggest constraint we have is the capacity of our team because, as I said, we're very disciplined about building out the scale of our business based on the scope of our expertise. So we are seeing with the green investment group, good opportunity to keep getting invested. Sorry, the second question as well; did I answer that as well in terms of GIG?

Ed Henning: Just about the development risk.

Shemara Wikramanayake: Oh, right. Yes, sorry. You did ask about that. We started out investing in operating assets. Then we moved to late-stage construction, then to earlier stage construction, then to development as the returns kept being brought in, in each part of the spectrum. So we did end up building up a lot of development skills. So Corio I mentioned as the offshore wind platform, we have a lot of deep development expertise there and we're finding that's where you are getting rewarded, but it's higher risk.

So what we've got for our investors is spectrum of offering where the more operational lower risk assets that command lower returns as well will be offered in one portfolio, the global renewable energy fund portfolio and series, and then the earlier stage assets which still won't be completely the beginning stage, we're doing in this MGETS offering. So as time goes on I'm sure that will get compartmentalised into other series as we respond to the market opportunity.

Ed Henning: So you will still be using a balance sheet in GIG to see some development gains to seed into funds as well as some funds taking that from scratch?

Shemara Wikramanayake: That's probably right. Basically if an investment falls in the mandate of the fund we will do it in the fund. The balance sheet will not compete with the fund mandate, but there will probably still be areas. For example, some of the early hydrogen projects we're doing here, Macquarie Capital is playing a role with the balance sheet as well as Macquarie Asset Management. So there will be areas that are still balance sheet areas as well, but probably the vast majority of the big balance sheet will move over to the fund. So we have several billion dollars at the moment in green investment group assets and over the next few years that will have run off to much smaller amounts.

Ed Henning: That's great. Thank you very much.

Alex Harvey: Obviously we will continue to put investments in the funds, Ed, themselves. So we will have an interest in those assets through our limited partner interest but less directly.

Shemara Wikramanayake: And in development stages, well the checks tend to be small. So that will probably be the trend.

Sam Dobson: We've still got a few more on the line.

Operator: Thank you. Your next question comes from Andrew Triggs with JP Morgan. Please go ahead.

Andrew Triggs: (Andrew Triggs, JP Morgan) Thank you. Good morning Shemara and Alex. The first question just relates to MacCap. It's a follow-up really on the private credit portfolio. There's an interesting comment that in MacCap it was actually quite subdued but was was referenced to some marked to market losses on underwriting positions. So firstly, keen to get an understanding of how big those are, those underwriting losses, and more generally I would assume that spreads have widened quite materially in the private credit market. So I'm keen to get some sense of what underlying growth in NII on the MacCap portfolio has been in the half.

Shemara Wikramanayake: I will give some comments and then hand over to Alex. But I think we need to distinguish between the private credit portfolio and the underwriting business, which is a debt capital market business. So the provisioning we did was in the debt capital market business where we do underwrite to syndicate for a short period, private credit we invest to hold and typically we're terming out the funding of that as well to match the term of the investments we make. So we will have fixed in the spread subject to credit. We've obviously been taking a lot of ECL provisioning on the private credit book as it grows and once it matures and stabilises we should see more stable income come through in that private credit book. But with that I'll hand to Alex to talk about that.

Alex Harvey: In terms of the margin, we talked before, Andrew, about – basically we've seen an NII margin of 4.5 to 5 per cent for the last few years. That continues to hold. You probably saw from the results, if you look at the $A3.6 billion I talked about, $A2.5 billion was invested in the first quarter. So the growth in the private credit book for the latter part of half was quite low. The reason for that was the point I was making before, that it takes a while obviously for markets to adjust to the new reality. What we are seeing – what we're starting to see is a bit of an expansion in the margin on the private credit side as credit more generally becomes harder to access. So that's obviously good in terms of the go-forward.

As Shemara said, we lock in the term funding against the asset anyway. So we've locked in the spread on those assets that we have on the balance sheet. In terms of the portfolio itself, you obviously create an ECL when you originate assets. Over time we've had – as I've said before, we've had a few assets that we've had to impair. They've been in idiosyncratic situations. Obviously you will recall the Covid story with the cruise line where we lost some money on that exposure. So there are some assets which underperform from time to time.

But generally speaking the credit profile of that book is strong and the underlying credits are performing well. We did see a deterioration in the macroeconomic outlook over the half. So we've stepped up our ECL provisioning for that. As you know, we hold an overlay in our ECL of about $A490 million. Some of that is obviously related to the principal finance book. Effectively that is us forming a view as to what that deteriorating macroeconomic outlook does to the loan portfolio across the group. But generally speaking, it is well provisioned and we feel good about the sectors where that book is exposed.

Andrew Triggs: Thanks, Alex. The second question just on the performance fee outlook, taking into account what has been said about the second half it would seem like the performance fee take as a percentage of EUM will probably run at half what it has been over recent years. Just keen to get your thoughts on maybe beyond the second half what 2024 might look like and whether we could realistically expect that to head back to the 55 basis point of the past or something closer to that?

Shemara Wikramanayake: Look, the performance fee is done as a percent of equity under management and the same for base fees. They have come down a bit since we shared information some years ago, five or six years ago. I think the big driver there is the diversification of where our equity under management is. So as we have more money in equity in businesses like private credit, real estate, the base fees on those are at a slightly lower level than the infrastructure funds and the performance fees as well in private credit, we don't have performance fees. So that is what is bringing the average down. But I think it's important to share that certainly in the infrastructure funds we're seeing no pressure on fees.

Our funds are closing at their hard caps oversubscribed and we're not getting challenge on the fee level. We are increasing the percentage of co-investment. That brings fees down a bit but we get more capital deployed more quickly. I think we will see both base fees and performance fees on EUM come down but it's not really because we're having to take lower fees per dollar of a EUM in each of the asset classes when we're just diversifying into adjacent asset classes that carry a lower fee per EUM on them, but we think that's worthwhile doing.

We're trying to broaden and diversify our franchise and go into adjacent areas patiently. On performance fees in the infrastructure funds, we are still seeing similar IRRs on the funds and rates of performance fees, et cetera, depending on the region and the mandate of the fund. We're also doing some slightly more core infrastructure funds which get performance fees on yield, but I guess my short point of view is we are not seeing pressure on the fee margin per product. It's the mix of the product and changing things.

Andrew Triggs: Maybe just to ask a little bit more generally Shemara, is 2024 likely to be a slightly stronger period for realisation just given timing of fund maturities?

Shemara Wikramanayake: Yes, we have MIP3 and MEIF4 going through their realisations at the moment and we have assets to be realised in those years. They're probably the main contributors, aren't they Alex and Ben is on the phone as well. As Alex has been saying and everyone has been talking about, the environment for realisations, we don't know what that will be like. We should still see good demand. There's a lot ofdry powder in infra funds. There's still a lot of interest from strategics buying our assets and the assets have improved a lot in terms of their results. So, we should see reasonable realisations in FY24 similar to this year, I think, possibly. Yes.

Andrew Triggs: Thank you.

Operator: Thank you. Your next question comes from Brendan Sproules with Citi. Please go ahead.

Brendan Sproules: (Brendan Sproules, Citi) Good morning. I have a couple of questions in the Asset Management business, specifically the movement in the assets under management that you show on slide 26 today. My first question is just in the public investments business. It does show that you had slightly positive net inflows over the half. I was wondering if you could talk about the drivers there. Obviously, Waddell & Reed had had significant outflows in the years prior to your acquisition. So, I'd like to understand how that business is faring and also some comments on the net inflows in the Delaware business please.

Shemara Wikramanayake: Yes. In the public investment business what we've been seeing is pretty much what the market has been seeing over these six months which is a rotation to fixed income from equity. We did have good inflows into fixed income but offset by outflows out of equity and the fact is that the fee margin in equities is higher than in fixed income so that has an impact on base fees. I think the much bigger driver of base fees obviously is that equity markets have come off about 20 per cent and that's as we've said in the results presentation here, the big driver of what has impacted assets under management and base fees in the business.

Waddell & Reed integration is going well, so we are on track, a little bit ahead of track, in terms of bringing that business together. The same with the AMP business here and the same with the CPG business. As you've said, Waddell & Reed was already in outflow and we are working with all our distribution teams as well as LPL in a backdrop environment where equity markets have come off and outflows from equities are increasing to try to bring down outflows in Waddell & Reed in line with our acquisition case. Does that cover it?

Brendan Sproules: Thanks. Yes, no, that's fantastic. If I could just ask a similar question in the private markets business. The interesting thing about the flows there is you show that investments are almost $A23 billion, which would be probably well above average of what you've shown in previous periods where divestments seem well below. I think as interest rates start to flow into valuations over time is it likely that we will see an expansion of equity under management and assets under management in private markets because it will be a lot easier to deploy given the flow that you've had for investors, that divestments will be a lot more challenging?

Shemara Wikramanayake: Yes, look, structurally I think Ben Way was saying that when he spoke, we are seeing institutional investors, being pension funds, insurers, allocate much more now to private markets. They used to in the very early days have a 60-40 fixed income equities public markets allocation but I think they're finding not only can they get better alpha but they can get better matching of duration, et cetera, for their liability by putting it more into private market assets.

We are finding that is creating an industry good demand for private market strategies. So, if you look at macro data will see flows and fees particularly going much more to private markets from public markets even though ETSs are growing in size, the fees are very low there, so I think private markets is where the fee flow is. For us specifically, as I've been saying, it's all about being able to bring superior expertise and results in each of the subsectors we're in.

Infrastructure, we're still the largest manager in the world. We have a good track record in the funds we're investing in so we should continue to see flows there. In terms of the interest rate backdrop and what that will have, I guess inflation is driving a lot of this interest rate movement and infrastructure, as Alex alluded to earlier, is an asset class where a lot of the assets have a natural inflation hedge in them as well.

So, we are finding the driver of interest rates, which is inflation, is leading to people also looking to allocate more through this cycle to things like utilities or transportation assets where you can pass on the infrastructure and have some sort of protection.

Brendan Sproules: Thank you. That's very helpful.

Sam Dobson: We've just got one more on the line.

Operator: Thank you. Your next question comes from Lara Tufegdzic with Bank of America. Please go ahead.

Lara Tufegdzic: (Lara Tufegdzic, Bank of America) Hi, thank you for answering my question. I was just wondering, having completed the Waddell & Reed acquisition earlier this year, would you consider further acquisitions of active asset managers and if so, what asset classes and geographies might be appealing? Thank you.

Shemara Wikramanayake: Thanks Lara. Yes, we hadn't done many acquisitions since 2009. I think we'd done small things like the Luxembourg ValueInvest team, et cetera, so we'd brought in boutique teams in areas where we saw a gap in our capability, but a large platform acquisition like Waddell & Reed we only did last year and that's because it's rare to be able to invest in those accretively, especially in the cycle we had with EBITDA multiples getting up to about 12 times.

Now they've come of clearly quite a lot and I guess I'd say high level in the US we have now a platform so we can do more in market acquisitions of other managers in public investments like we did in Waddell & Reed. In Europe, we don't have a presence so we would have to find a much more compelling case because we couldn't take that benefit of integrating the platform costs and getting the synergies. I think we'd be open to it. We're not present in the European market, we'd be open to something, but in our usual very, very disciplined way and that's why these inorganic steps are rare for us.

Lara Tufegdzic: Thank you.

Shemara Wikramanayake: Thanks Lara.

Sam Dobson: We're just going to go to the room and then we'll come back online.

Shemara Wikramanayake: Brian has been waiting patiently.

Brian Johnson: (Brian Johnson, Jefferies) Never patient Shemara. Brian Johnson, Jefferies. I have three quick questions which I suspect will not be answered but they've got to be asked. The first one and you've got to remember this comes in the context of a rather disappointing result yesterday that management were telling us was great that perhaps wasn't. If we have a look at your downside scenario in your ECL provisioning and it's refreshing to see someone where the provisions aren't effectively being written back from where they were in COVID.

Alex, the one number that you don't share which is really important, could we get the unemployment assumption in Australia that you're using in the downside scenario?

Shemara Wikramanayake: Having told you you're not going to answer the question, Alex.

Brian Johnson: Yes, I'm just saying that house prices falling don't create loan losses. Unemployment and the house prices falling create loan losses. I find that a reasonable question.

Alex Harvey: Brian, we're happy to be the economics forecast but I think we're probably in the mid-fours in terms of unemployment.

Brian Johnson: It says 4.6 per cent is the base case.

Alex Harvey: Yes.

Shemara Wikramanayake: Yes.

Brian Johnson: I'm interested in what the downside one is.

Alex Harvey: We will have to come back to you with an exact number.

Shemara Wikramanayake: We're happy to share it.

Alex Harvey: I think we should share it with everyone in our economics forecast anyway so...

Brian Johnson: Yes, yes, so...

Shemara Wikramanayake: We're happy to share it but I think Greg would endorse that unemployment is a driver. Sorry, Greg, did you have a comment?

Greg Ward: I can't remember either.

Alex Harvey: Yes.

Shemara Wikramanayake: Yes.

Alex Harvey: Yes. We're happy to give you the answer but we'll have to do it after.

Brian Johnson: Fantastic. Well don't give it to anyone else.

Alex Harvey: We will put it on the website.

Brian Johnson: Okay. My second one is that when we have a look at the legendary slide 39, we can see that there's $A1.1 billion of seed assets in MAM which includes Green

Investment Group, but down below it we can see there's green energy investments of $A1.3 billion. Could we understand what the difference between those two are? Is this where MacCap buys stuff and are speculating that it's going to go really well or what's the difference between?

Alex Harvey: No, the principal - I mean the green asset portfolio, the green energy portfolio there is principally what was in the Green Investment Group. That's now gone into MAM, so that's the Corio asset that Shemara talked about, Blueleaf, Cero, a few other platforms they've got. The investments acquired to see new private market assets, there will be a small component of green energy in there, but the team is actually out there putting their foot on, I don't know, in the past the national grid for the sake of an example in the UK. It will be those sorts of things that will find their way into, in that case, the Super Core Infrastructure Fund.

Here there's a range of secondary investments, there's a range of investments that will find their way into non-green assets. There'll be some small exposure to green but principally green is in the lines

Brian Johnson: That $A1.3 billion, that's destined ultimately for a MAM fund.

Shemara Wikramanayake: Well either - yes.

Alex Harvey: I guess what we're doing is - so what we saw during this half, there were some assets that were sitting on the balance sheet that you saw coming through the MAM P&L. Those assets have just been sold to third parties. There's still a portfolio of assets, one of which is the offshore wind asset that Shemara talked about and we've got a solar platform. The team are working their way through whether those assets are sold to third parties or whether they form seed assets in a new green energy fund.

The discussion Brian is a bit - if they're embedded with large profit then obviously the shareholders of the Group have taken the risk to get that large profit and so we want to get an adequate and proper return for that. We don't want to sell them into the funds at that elevated price because that conversation is a hard one to win. You either pay too much in the fund or you've sold them too cheaply for the Group. Where they're not invested with large profit, then typically they might form a seed asset for the fund.

Where they're invested with large embedded profit then maybe they will come off the balance sheet and go to third parties. That conversation is a live conversation and it will take, as we've said before, a few years to go from the balance sheet investing to that large scale fiduciary offering that Ben and the team are putting together on the MAM side, the MAM private market side.

Brian Johnson: The final question, I promise I'll shut up after this one, is we hear a lot about interest rates going up, asset values fall. In the private markets business, when Macquarie bought an asset 10 years ago for one of the funds, we know that the assets tend to be inflation protected and we know that we tend to term out the funding for the life of it. When you're terming out that funding, do you term that out with infrastructure linked debt rates or naked debt at the time?

Because it will have a radical difference on the end value of the asset as inflation comes through if you have termed it out with debt where it was. There's a gigantic capital gain as inflation comes through. Alex, could we just understand what it is predominantly?

Alex Harvey: Yes, I mean there's obviously 160 assets in the portfolio so there will be a - there won't be one answer to that question. Some of them will be inflation linked swaps that have been in place. Typically speaking what they will have done is they will have termed out the debt and they will have turned it into a fixed rate debt. They will have - it won't be an inflation linked debt. To the point you're making, you will obviously have an expansion to the top line and you might have the costs of the debt fixed for a period of time, but remember the buyers of the assets are obviously raising the funding in that inflationary environment.

So yes, they get the top line, their cost of capital is going up, so it's not as simple as saying you've got nominal growth to the top line and you've got this fixed cost there. That to some extent will be happening, you do that expansion, but equally you've got to obviously find a buyer market and the buyers have got to go and raise their funding and get their return for risk that they're taking as well. So there's not a simple answer to the question.

Shemara Wikramanayake: I think also our leverage across those assets is sitting at around 50 per cent, so we're pretty prudent on levering those assets. Having been through a cycle previously over a decade ago where you could actually turn good assets into risky ones through leverage, if you have to re-buy in a cycle where there's no liquidity. So we've been pretty prudent on the debt that we put in, and as a result the costs of debt are pretty, they're not egregious debt where you're spread for getting high.

Brian Johnson: Thank you very much, and congratulations.

Sam Dobson: Right, and we've got one more question on the line, so we'll go to the lines please.

Operator: Thank you. Your next question comes from Brett Le Mesurier with Perpetual. Please go ahead.

Brett Le Mesurier: (Brett Le Mesurier, Perpetual) Thanks very much, I'll make this quick. You commented that you were moving away from mature investments, more towards in development assets to improve the ROE. I'm interested to know whether the ROE you get on development assets now is better than the mature asset ROE investments that you were getting, say, five years ago? In other words, are you being compensated for the extra risk you are taking now, compared to the returns you were getting, say, five years ago on the mature asset?

Shemara Wikramanayake: Yes, thanks Brett. I just qualify, that that was just in the green investment assets that we were talking about, where we had moved up the risk curve more to development assets. I think the returns have come down across that space, because more and more capital is chasing it. So the returns for mature assets have come down, but even the returns for development assets, as people have got more familiar with it. But also as people are wanting to allocate much more to the space.

We, as I said, are pretty disciplined asset-by-asset. If we don't think the return is there for the development risk, we'll go and apply our skillsets in another area where there isn't as much compression of return for the development work you're doing. So as some of these development areas get de-risked we'll move to other development areas where we see the spread for the risk that we're taking. So hopefully that answers it.

Brett Le Mesurier: Just one more quickly on the ROE. You commented on your ROE hurdles by division and how they varied. But when you look at your incremental investment, do you look at the incremental ROE? Or do you, you're actually looking at the average division ROE when you're making your decisions?

Shemara Wikramanayake: No, we look at it investment-by-investment. So if we're looking at a new investment we won't subsidise it by superior ROE we may be having in a similar nature of assets already on the book. We are very disciplined about each particular investment operating like it's the only investment. It may get cost synergies and things from other investments, and we'll factor that in. But ultimately everything's got to stand on its own.

We don't feel any compunction to put money out the door. We're happy to sit on our capital in the funds and on the balance sheet if we're in an environment where there are no good opportunities, and wait for the right time.

Brett Le Mesurier: That concept applies to the smaller assets, the home loans, for example, that you have in BFS?

Shemara Wikramanayake: Yes, Greg's sitting here nodding in front of me. That's very much the case, that we don't need to put capital out of the door if there isn't a good return on putting that capital out of the door.

Brett Le Mesurier: Thank you, they're all the questions I have.

Shemara Wikramanayake: Great. I should say as well as Greg and Nick and Ben and Michael , we have also got Evie, our General Counsel, here in the front row, Nicole, our Head of Corporate Operations, and Andrew Cassidy, our Head of the Risk Management Group with us who didn't get to speak today. Stuart Green's not with us, but the rest of the Executive Committee are.

Sam Dobson: Great. All right, thanks Brett, and thanks everyone for your support and interest. We'll look forward to seeing you over the next couple of weeks. Thanks very much.

Operator: That does conclude our conference for today. Thank you for participating. You may now disconnect.

[END OF TRANSCRIPT]