CEO'S REPORT

Dear shareholders,

This has been a year like no other. COVID-19's impact has been profound and has created challenges for many individuals and companies. The sharp decline in economic growth, low interest rates and higher impairment charges have materially impacted the sector's and our earnings.

At the same time, our own issues, including responding to our shortcomings in risk management – particularly in financial crime – have contributed to lower earnings. These factors saw dividends and the value of your investment fall.

You expected more from Westpac and we apologise for letting you down. I recognise the distress lower dividends caused to many shareholders, especially retirees. I assure you that while it will take some time, we are doing everything we can to fix things and rebuild Westpac.

I do not underestimate the importance of leading Australia's oldest company at such a pivotal moment – it is a great privilege. Having spent the best part of my career at Westpac, I know this Company has strong foundations and deeply committed people, and so I am confident we will **fix** our issues, **simplify** our business and **perform** for our stakeholders.

Turning things around

On 20 November 2019, AUSTRAC commenced civil proceedings against Westpac in relation to alleged contraventions of the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth). This had a major impact this year, highlighting weaknesses in our management of financial crime. We have taken responsibility for our failings and in September this year, we reached an agreement with AUSTRAC to resolve the proceedings. As part of the settlement, Westpac agreed to pay a civil penalty of $1.3 billion, which the Court has approved.

While this is a significant cost for shareholders, the overall settlement is an important step forward, allowing us to direct our energy to getting back on track.

We have investigated the underlying issues, and we know we need to do better. We carried out a number of internal reviews including an assessment of management accountability in relation to the issues raised in the AUSTRAC proceedings and the adequacy of Westpac's financial crime program. We also established an independent Advisory Panel to review Board governance and Board accountability in relation to the issues raised in the AUSTRAC proceedings and reassessed our 2018 Culture, Governance and Accountability self-assessment program. The recommendations and findings of these reviews were published on 4 June and 17 July 2020 respectively.

Complexity has been at the heart of our issues – in our systems, processes, and businesses. Accountability was often not clear, and the right skills and capabilities were lacking in some areas. We didn't have the right culture and we were too reactive and slow to respond when issues emerged.

For change to be effective it must start at the top.

There has been significant change at the executive level with the team renewed. We have sharpened our focus on Australia and New Zealand and are moving back to core banking, with our Specialist Businesses division bringing our non-core businesses together.

We have enhanced our operating structures by implementing a Lines of Business model which aligns our businesses to our major customer offers such as mortgages, everyday banking, or business lending. Individuals are now responsible for each Line of Business, including financial performance, risk management and customer outcomes. This model aims to improve decision making, creates clear end-to-end accountability for our activities, streamlines management and speeds up decision making.

These changes are complemented by our new purpose and values and will help guide our cultural change.

We have also made changes in risk management, including the creation of a new role – Group Executive, Financial Crime, Compliance and Conduct, and added significant skills and resources to our risk management areas. Fixing our management of risk is a key priority.

We have made good progress in improving our financial crime program and are making Company-wide changes through our Customer Outcomes and Risk Excellence program. This program deals with the source of our issues, seeking to strengthen non-financial risk management and improve our risk culture.

I am confident that these changes are steering Westpac in the right direction, towards becoming a simpler and stronger bank. The turnaround will take some years, but we are determined to rebuild value and importantly, your trust.

Helping customers when they need it most

Against this backdrop, I am very proud of how our people stepped up to support customers through COVID-19, and the bushfires and floods that affected large parts of Australia this year. We worked hard to support customers through this time, changing our operations to remain open, diverting resources to areas of most need and providing a range of tailored support packages.

With the bushfires, in addition to the many employees working on the front line, our teams worked tirelessly to ensure customers could access their funds while also providing emergency grants to those most affected. Around 2,000 relief packages were provided.

With COVID-19, our focus was doing everything we could to keep our people safe while supporting customers. We kept as many branches as we could open while enabling around 22,000 employees to work from home. We provided customers with special interest rates, certain fee waivers, and temporary loans and supported over 215,000 consumer and business customers with repayment deferrals.

While there were a few setbacks through the year, such as increased wait times and delays to loan processing, we have (and will continue to) supported customers through this uncertain time.

Performance

Our financial performance this year was disappointing. The Group's reported profit was $2,290 million down 66% (or $2,608 million in cash earnings, down 62%), partly a result of our operating environment including low interest rates, materially higher impairment charges and higher costs from navigating COVID-19. The AUSTRAC settlement, further remediation costs, asset writedowns and high risk and compliance costs also contributed. The larger impacts on results included:

— Impairment charges of $3,178 million, reflecting an increase in provisions for expected credit losses due to COVID-19 impacts;

— $1,442 million after tax in provisions for AUSTRAC proceedings including a civil penalty of $1,300 million; and

— Additional provisions for customer refunds, repayments, associated costs and litigation items of $440 million after tax.

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Despite the strength of our franchise, lending stalled over the year. While demand was lower, we did not keep pace with the market – particularly in our core mortgage portfolio. Net interest margins were also down due principally to low interest rates and a highly competitive market.

However, our balance sheet remains strong. Key liquidity and funding ratios are above target, and our CET1 capital ratio was 11.13% – the highest level for at least the last 20 years. This strength made possible the payment of the final dividend, albeit reduced, and allows us to continue supporting customers and the economy through this challenging time.

We remain comfortable with our current capital ratios and have buffers to absorb a potential further deterioration in asset quality. Capital will also be generated as we exit activities in our Specialist Businesses division.

Looking ahead

In the near term, growth is already benefitting from the reopening of the economy. Next year we expect that to continue, albeit at a slower pace. Risks around the containment of the virus, the gradual unwinding of support measures, and prospects for the global economy emphasise the high uncertainty we will continue to experience.

Growth in financial services will also be challenged, particularly in a persistent low interest rate environment. Impairment charges are also likely to remain elevated as consumer and business defaults rise following stimulus measures unwind.

With our three priorities of fix, simplify and perform we are becoming a simpler and stronger bank focused on our core consumer, business and institutional segments. Through our program of change we are implementing our new Lines of Business operating model, strengthening our risk management capability, finalising customer remediation, enhancing our risk culture and simplifying where we operate.

Finally, I want to thank our people. I know how deeply many have been affected by our issues this year. Despite the challenges our people have worked incredibly hard and always maintained their passion to help each other and customers.

Importantly, we move ahead with a strong balance sheet and the financial resources and commitment to continue supporting customers and shareholders through this difficult time.

Yours sincerely,

Peter King
CEO