

## Police Financial Services Ltd. (trading as BankVic)

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# Police Financial Services Ltd. (trading as BankVic)

## Ratings Score Snapshot

### Issuer Credit Rating

BBB+/Stable/A-2

SACP: bbb+

Support: 0

Additional factors: 0

Anchor	a-	
Business position	Constrained	-2
Capital and earnings	Very strong	+2
Risk position	Adequate	0
Funding	Moderate	-1
Liquidity	Adequate	
CRA adjustment		0

ALAC support	0
GRE support	0
Group support	0
Sovereign support	0

Issuer credit rating
<b>BBB+/Stable/A-2</b>

ALAC--Additional loss-absorbing capacity. CRA--Comparable ratings analysis. GRE--Government-related entity. ICR--Issuer credit rating. SACP--Stand-alone credit profile.

## Credit Highlights

### Overview

#### Key strengths

Very strong capitalization.

Sound asset quality, given an essential services member base.

#### Key risks

Exposed to price competition from larger banks due to small scale.

Susceptible to funding pressure.

**Police Financial Services Ltd. (trading as BankVic) will maintain very strong capital.** We estimate our risk-adjusted capital (RAC) ratio for the mutual bank remain broadly stable between 24.5%-25.0% over the next two years. Our forecasts assume loan growth slightly stronger than system levels and a marginal contraction in net interest margin (NIM) because of ongoing deposit market competition and likely Reserve Bank of Australia (RBA) interest rates cuts. As of June 30, 2024, our RAC ratio for BankVic was 24.8%.

**BankVic's low-risk residential lending to essential services personnel in Victoria supports its sound credit quality.** We expect credit losses to remain below 5 basis points (bps) over the next 24 months. This is lower than the systemwide average but in line with mutual peers.

**BankVic will remain a price taker.** We believe the scale and incumbency of Australia's major banks enable them to be price-setters on both sides of the balance sheet. Consequently, mutual lenders (including BankVic) are susceptible to price competition from these larger institutions.

*Australia's small financial institutions, including BankVic, are vulnerable to funding competition from the major banks.*

Despite this, BankVic's funding base is made up almost entirely of retail deposits and is comparatively stable.

## Outlook

The rating outlook on BankVic is stable. Australia's economic prospects over the next two years are sound, despite subdued GDP growth due to elevated interest rates and major trade partners' slowing economies. We forecast unemployment to increase somewhat but remain low in a historical context. We expect modest growth in house prices over the period. Strong immigration-driven population growth along with limited new housing supply should continue to support house prices.

We forecast BankVic's credit losses to remain low, at about 5 bps of customer loans, lower than the systemwide average. We expect the mutual bank will remain very well capitalized with a RAC ratio between 24.5%-25.0% over the next two years.

### Downside scenario

We see a low likelihood of a downgrade over the next two years. Nevertheless, we could lower our ratings on BankVic if, for example, systemwide risks rise due to rapid growth in Australian property prices or private sector debt.

### Upside scenario

An upgrade is highly unlikely over the next two years. This is because we consider it unlikely that BankVic will strengthen its franchise, market share, and business position to a level comparable to higher-rated domestic banks.

## Key Metrics

### Police Financial Services Ltd.--Key ratios and forecasts

	--Fiscal year ended June 30 --				
(%)	2023a	2024a	2025f	2026f	2027f
Growth in operating revenue	23.4	(0.1)	2.7-3.3	4.2-5.1	4.2-5.1
Growth in customer loans	15.8	8.3	5.4-6.6	5.4-6.6	5.4-6.6
Growth in total assets	6.8	2.5	5.4-6.6	5.4-6.6	5.4-6.6
Net interest income/average earning assets (NIM)	2.3	2.2	2.1-2.3	2.0-2.3	2.0-2.2
Cost to income ratio	69.5	72.0	71.6-75.2	71.2-74.8	71.2-74.8
Return on average common equity	6.8	5.9	5.0-5.5	5.0-5.5	5.0-5.5
Return on assets	0.5	0.5	0.4-0.5	0.4-0.5	0.4-0.5
New loan loss provisions/average customer loans	0.0	0.0	0.0-0.1	0.0-0.1	0.0-0.1
Gross nonperforming assets/customer loans	0.5	0.7	0.6-0.6	0.5-0.6	0.5-0.6
Net charge-offs/average customer loans	0.0	0.0	0.1-0.1	0.1-0.1	0.1-0.1

## Police Financial Services Ltd.--Key ratios and forecasts (cont.)

	--Fiscal year ended June 30 --				
(%)	2023a	2024a	2025f	2026f	2027f
Risk-adjusted capital ratio	24.2	24.8	24.1-25.3	24.0-25.2	23.9-25.1

All figures are S&P Global Ratings-adjusted. a--Actual. f--Forecast. NIM--Net interest margin.

## Anchor: Resilient Economy, Conservative Regulations, And Low Risk Appetite Mitigate Housing Risks

The starting point for our ratings on BankVic--similar to all other banks operating predominantly in Australia--reflects our assessment of Australia's macroeconomic environment.

*Australia has a wealthy, open, and resilient economy that has performed relatively well following economic downcycles and external shocks.* Low unemployment over the next two years should keep credit losses low, and close to pre-pandemic levels. Nevertheless, banks in Australia remain exposed to a jump in credit losses due to high household debt, elevated interest rates and prices, and global economic uncertainties. We expect the persistent gap between housing demand and supply to drive modest growth in property prices in the next two years.

*We consider Australia's prudential regulatory standards and supervision to be among the strongest globally.* In our view, an oligopolistic industry structure supports system stability. Sound earnings and solid interest margins should protect the banking system from unforeseen events, including a significant rise in credit losses. A material dependence on external borrowing exposes Australian banks to funding disruptions.

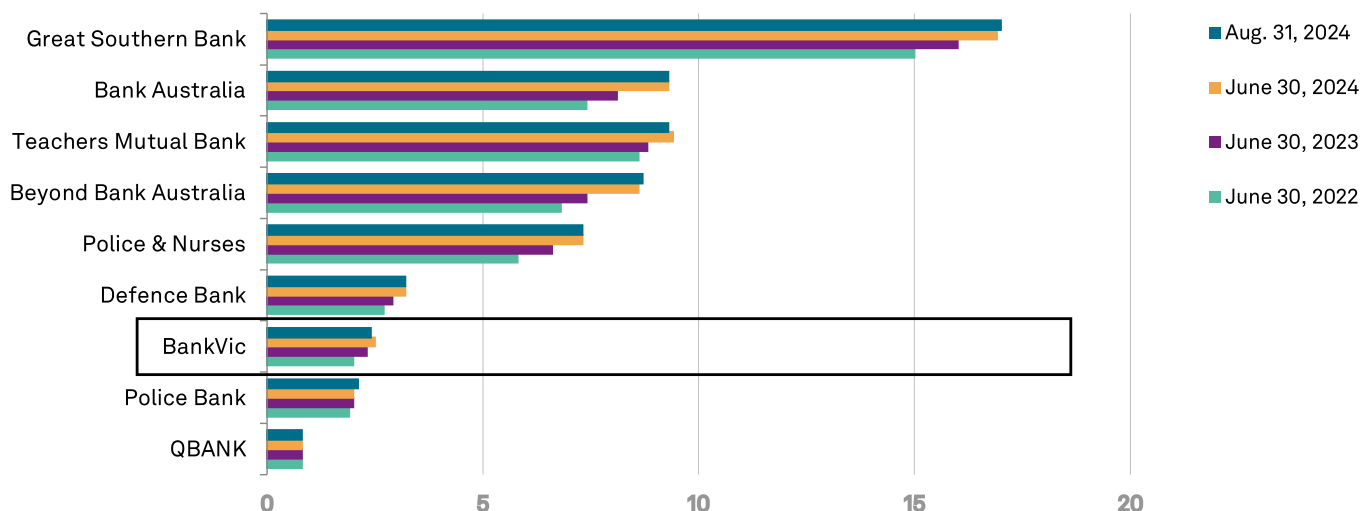
## Business Position: BankVic's Small Scale Exposes It To Price Competition

*BankVic's small market share in Australia constrains its competitive position.* Like its peers, the mutual bank is a price-taker in a banking system that four major banks dominate. The four large and diverse Australian major banks have a collective market share of about 75% of the residential lending and household deposit markets. As of Aug. 31, 2024, BankVic had a market share of only about 0.1% of total housing loans and 0.2% of total household deposits.

## Chart 1

**BankVic remains small among mutual banks we rate in Australia**

Total lending exposures (bil. A\$)



Source: Australian Prudential Regulatory Authority.

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***BankVic's increasing use of brokers will support growth.*** We believe brokers are an important source of growth for Australian financial institutions given they originate 60% of lending in the market. BankVic established its broker distribution channel in fiscal 2023 and originated about 15% of its new loan flow via brokers in fiscal 2024. This is lower than the mutual sector average of about 45%. We expect brokers to make up a growing portion to about 30% of BankVic's new lending over the next 12-24 months as the mutual bank targets police and emergency services members based outside of Victoria.

***We expect BankVic to retain its strong presence among Victoria's police and law enforcement personnel.*** In our view, the mutual bank has a good brand and reputation among these customers, who represent the foundation of its franchise.

We also expect BankVic to grow its small presence among Australian Federal Police personnel and retain its smaller but stable presence in the Victorian healthcare sector. Both of these customer segments are closely aligned with BankVic's essential services common bond.

We believe niches like this can help smaller lenders compete against larger institutions within a specific domain.

## Capital And Earnings: Very Strong

***BankVic's capitalization is a strength for its credit profile.*** We project our RAC ratio for the mutual bank will remain broadly stable between 24.5%-25.0% over the next two years. Driving our forecast is slightly stronger than system loan growth and a marginal contraction in BankVic's NIM, driven by an increase in deposit market competition and likely RBA interest rates cuts. As of June 30, 2024, our RAC ratio for BankVic was 24.8%.

***BankVic will manage regulatory capital well above the minimum prudential requirements.*** As of June 30, 2024, the mutual bank had a common equity Tier-1 ratio of 19.5% and total capital ratio of 20.3%. This compares with a minimum regulatory requirement for standardized banks of 6% and 8%, respectively.

***NIM will continue falling over the next two years as interest rates decline and funding costs remain tight.*** BankVic's NIM fell by 7 bps to 2.19% in fiscal 2024 as ongoing competition, rising funding costs, and the mutual bank's aggressive growth ate away prior year gains.

## **Risk Position: Mortgage Lending To Essential Service Personnel Supports Asset Quality**

***BankVic's risk profile is consistent with that of the broader Australian banking system.*** We believe we adequately capture the mutual bank's risk profile in the standard risk weights we applied in our capital and earnings assessment. BankVic's risk management practices are sufficient for an organization of its size and complexity, in our assessment.

***BankVic's residential mortgage book and essential-services membership base underpin its stable asset quality through the cycle.*** We view the repayment prospects of the mutual bank's members as more stable and predictable than the average borrower. This is because the mutual bank's members are employed in publicly-funded essential service roles, making their income largely independent of macroeconomic conditions.

We believe this adds a layer of through-the-cycle stability to the repayment prospects of BankVic's borrowers. Even amid high interest rates and cost-of-living pressures, we forecast the mutual bank's credit losses will remain below 5 bps over the next 12-24 months.

***Like most Australian mutuals, BankVic's portfolio is concentrated by product and geography.*** The mutual bank mostly extends residential mortgages to members in metropolitan Melbourne in the state of Victoria. This makes it more susceptible to localized economic pressures than more diversified mutual peers.

That said, Melbourne is Australia's second-largest city with a diversified economy. Likewise, the underwriting standards of Australian mutual lenders, including BankVic, are generally conservative in the face of rising economic uncertainties and lower customer serviceability prospects.

## **Funding And Liquidity: Retail Deposit Focus Supports Funding Stability**

***Australia's small financial institutions, including BankVic, are vulnerable to funding pressure from the major banks.*** We consider the mutual bank's funding strength to be broadly comparable with that of most of the regional banks and mutual lenders in Australia.

In addition, we assess the funding profiles of the four major banks and Macquarie Bank Ltd. to be stronger than all other banking institutions within Australia, including BankVic. This is because we believe the major banks could bring funding pressure on all other Australian financial institutions if they decided, or were forced, to compete more aggressively for domestic deposits due to a dislocation in overseas wholesale funding markets. Such a market event would be accompanied by some form of economic crisis, which would likely cause a flight-to-safety in domestic deposit markets, in our assessment.

***Deposits will continue to make up almost all BankVic's funding.*** As of Aug. 31, 2024, deposits made up almost 100% of the mutual bank's funding, compared with the mutual sector's average of 93%. We consider deposit funding to be a relatively stable source of funding.

Although deposits will continue making up the bulk of its liabilities, we expect BankVic to diversify its funding base via warehouse funding over the next 12-24 months.

***We expect BankVic to continue to manage down liquidity to support loan growth.*** The mutual bank's average quarterly minimum liquidity holdings ratio was 18.0% for the three months to June 30, 2024, down from 23.0% for the three months to June 30, 2023. Driving the decrease was BankVic's above-system growth and the repayment of its final RBA Term Funding Facility (TFF) maturities. We expect BankVic's liquidity ratio to remain well above the 9% regulatory minimum even as it continues to decrease its position over the next 12 months to fund new lending.

***BankVic holds sufficient on-balance sheet liquidity to meet at least 12 months of general market stress.*** The mutual bank had a short-term wholesale coverage ratio (which measures on-balance sheet liquidity cover for wholesale funding maturities within 12 months) of 32.6x as of June 30, 2024, an increase from 8.3x one year earlier. The significant increase is because BankVic no longer has short-term wholesale liabilities on its balance sheet following the repayment of the RBA TFF in March 2024.

In a longer-term stress scenario, BankVic could also draw on contingent liquidity from the RBA via repurchase agreements of internally securitized mortgages. As of June 30, 2024, the mutual bank had access to about A\$516 million under its internal securitization program. That said, we do not foresee any large or unusual liquidity needs for BankVic over the next 24 months.

## Support: Extraordinary Government Support Unlikely

As of Aug. 31, 2024, BankVic accounted for about 0.1% of total housing loans and 0.2% of total household deposits in the Australian banking sector. Given the mutual bank's small market share, we consider it unlikely that its failure would lead to a disruption in the larger financial system and the economy. Therefore, we believe it is unlikely the Australian government would provide extraordinary support, if needed.

## Environmental, Social, And Governance



*We see ESG factors for BankVic to be broadly in line with those for its industry and domestic peers.* In our view, the mutual bank's risk management and governance policies and practices are adequate for an organization of its size and complexity.

*Australian mutual lenders, including BankVic, maintain a sound social franchise in the community.* Their member-owned structure and an ethos of providing benefits to both their member base and the wider communities in which they operate support this. While BankVic's involvement with Victorian essential service employment groups (and their respective unions and community groups) provides an element of stability to its franchise, we see this as only being marginally supportive of the mutual bank's credit profile.

*We see environmental factors as less relevant (than social and governance factors) to the creditworthiness of BankVic.* The mining sector accounts for only about 1% of the total domestic lending by the Australian banking sector. Still, we believe BankVic is indirectly exposed to environmental factors because it operates in an economy where the commodities sector is significant.

Evolving domestic and global environment standards and legislation, and changing customer preferences leading to a transition to less carbon-intensive forms of energy, could weaken the broader economy. That could have a flow-on effect on BankVic's lending portfolio, even though the mutual bank does not directly lend to energy companies.

## Key Statistics

**Table 1**

Police Financial Services Ltd. (trading as BankVic)--Key figures					
	June 2024	June 2023	June 2022	June 2021	June 2020
Adjusted assets	3,096.6	3,020.5	2,827.6	2,663.9	2,307.8
Customer loans (gross)	2,481.1	2,290.4	1,977.4	1,766.4	1,733.1
Adjusted common equity	245.2	231.0	215.6	203.9	193.3
Operating revenues	73.8	73.9	59.9	53.9	56.1
Noninterest expenses	53.2	51.4	43.9	38.5	39.5
Core earnings	14.1	15.7	11.6	10.6	10.1

**Table 2**

Police Financial Services Ltd. (trading as BankVic)--Business position					
	June 2024	June 2023	June 2022	June 2021	June 2020
Total revenues from business line (currency in millions)	73.8	73.9	59.9	53.9	56.1
Commercial and retail banking/total revenues from business line	100.0	100.0	100.0	100.0	100.0
Return on average common equity	5.9	6.8	5.5	5.3	5.3

**Table 3**

Police Financial Services Ltd. (trading as BankVic)--Capital and earnings					
	June 2024	June 2023	June 2022	June 2021	June 2020
Tier 1 capital ratio	19.5	18.9	16.4	16.6	17.5
Adjusted common equity/total adjusted capital	100.0	100.0	100.0	100.0	100.0
Net interest income/operating revenues	90.3	89.3	87.3	86.0	82.8

Table 3

Police Financial Services Ltd. (trading as BankVic)--Capital and earnings (cont.)					
	June 2024	June 2023	June 2022	June 2021	June 2020
Fee income/operating revenues	9.5	10.5	8.9	8.8	11.0
Cost to income ratio	72.0	69.5	73.3	71.4	70.5
Preprovision operating income/average assets	0.7	0.8	0.6	0.6	0.8
Core earnings/average managed assets	0.5	0.5	0.4	0.4	0.5

Table 4

Police Financial Services Limited--Risk-adjusted capital framework data					
(Mil. A\$)	Exposure*	Basel III RWA	Average Basel III RW(%)	S&P Global Ratings' RWA	Average S&P Global Ratings' RW (%)
<b>Credit risk</b>					
Government and central banks	177.0	0.0	0.0	5.3	3.0
Of which regional governments and local authorities	0.0	0.0	0.0	0.0	0.0
Institutions and CCPs	426.5	128.5	30.1	69.7	16.3
Corporate	0.0	0.0	0.0	0.0	0.0
Retail	2,694	863	32.0	797.0	29.6
Of which mortgage	2,650	796	30.0	758.8	28.6
Securitization§	6.1	0.0	0.0	1.2	20.0
Other assets†	5.3	5.5	102.2	6.0	112.5
Total credit risk	3,309	996.6	30.1	879.2	26.6
<b>Credit valuation adjustment</b>					
Total credit valuation adjustment	--	0.0	--	0.0	--
<b>Market Risk</b>					
Equity in the banking book	0.0	0.0	0.0	0.0	0.0
Trading book market risk	--	0.0	--	0.0	--
Total market risk	--	0.0	--	0.0	--
<b>Operational risk</b>					
Total operational risk	--	99.7	--	110.8	--
	Exposure	Basel III RWA	Average Basel II RW (%)	S&P Global Ratings' RWA	% of S&P Global Ratings' RWA
<b>Diversification adjustments</b>					
RWA before diversification	--	1,096.2	--	990.0	100.0
Total diversification/ Concentration adjustments	--	--	--	376.4	38.0
RWA after diversification	--	1,096.2	--	1,366.4	138.0
		Tier 1 capital	Tier 1 ratio (%)	Total adjusted capital	S&P Global Ratings' RAC ratio (%)
<b>Capital ratio</b>					
Capital ratio before adjustments		213.5	19.5	245.2	24.8
Capital ratio after adjustments‡		213.5	19.5	245.2	17.9

Table 4

**Police Financial Services Limited--Risk-adjusted capital framework data (cont.)**

\*Exposure at default. §Securitization exposure includes the securitization tranches deducted from capital in the regulatory framework. †Exposure and S&P Global Ratings' risk-weighted assets for equity in the banking book include minority equity holdings in financial institutions.

‡Adjustments to Tier 1 ratio are additional regulatory requirements (e.g. transitional floor or Pillar 2 add-ons). RWA--Risk-weighted assets.

RW--Risk weight. RAC--Risk-adjusted capital. Sources: Company data as of June 30, 2024, S&P Global Ratings.

Table 5

**Police Financial Services Ltd. (trading as BankVic)--Risk position**

	June 2024	June 2023	June 2022	June 2021	June 2020
Growth in customer loans	8.3	15.8	11.9	1.9	3.9
Total managed assets/adjusted common equity (x)	12.6	13.1	13.1	13.1	11.9
New loan loss provisions/average customer loans	0.0	0.0	(0.0)	(0.0)	0.1
Net charge-offs/average customer loans	0.0	0.0	0.0	0.0	0.0
Gross nonperforming assets/customer loans + other real estate owned	0.7	0.5	0.6	0.8	0.5
Loan loss reserves/gross nonperforming assets	39.5	52.4	43.5	43.6	69.0

Table 6

**Police Financial Services Ltd. (trading as BankVic)--Funding and liquidity**

	June 2024	June 2023	June 2022	June 2021	June 2020
Core deposits/funding base	85.3	85.0	94.2	95.6	91.0
Customer loans (net)/customer deposits	103.2	97.4	80.5	75.3	90.2
Long-term funding ratio	86.5	86.1	96.2	99.5	94.1
Stable funding ratio	91.9	95.4	110.9	118.4	108.9
Short-term wholesale funding/funding base	0.3	1.5	2.3	0.5	0.8
Broad liquid assets/short-term wholesale funding (x)	32.6	8.3	6.9	35.0	19.0
Broad liquid assets/total assets	7.9	11.4	14.4	17.1	14.6
Broad liquid assets/customer deposits	10.2	14.7	16.6	19.5	17.6
Net broad liquid assets/short-term customer deposits	10.1	13.1	14.3	19.2	17.0
Short-term wholesale funding/total wholesale funding	1.8	10.0	39.5	11.9	9.3

**Police Financial Services Ltd.--Rating component scores**

Issuer credit rating	BBB+/Stable/A-2
SACP	bbb+
Anchor	a-
Economic risk	3
Industry risk	2
Business position	Constrained
Capital and earnings	Very strong
Risk position	Adequate
Funding	Moderate
Liquidity	Adequate
Comparable ratings analysis	0
Support	0
ALAC support	0
GRE support	0

**Police Financial Services Ltd.--Rating component scores (cont.)**

<b>Issuer credit rating</b>	<b>BBB+ /Stable/ A-2</b>
Group support	0
Sovereign support	0
Additional factors	0

ALAC--Additional loss-absorbing capacity. GRE--Government-related entity. SACP--Stand-alone credit profile.

**Related Criteria**

- Criteria | Financial Institutions | General: Risk-Adjusted Capital Framework Methodology, April 30, 2024
- Criteria | Financial Institutions | Banks: Banking Industry Country Risk Assessment Methodology And Assumptions, Dec. 9, 2021
- Criteria | Financial Institutions | General: Financial Institutions Rating Methodology, Dec. 9, 2021
- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

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**Ratings Detail (As Of October 16, 2024)\*****Police Financial Services Ltd.**

Issuer Credit Rating BBB+ /Stable/ A-2

**Issuer Credit Ratings History**

02-Apr-2024 BBB+ /Stable/ A-2  
20-Nov-2022 BBB/Positive/A-2

**Sovereign Rating**

Australia AAA/Stable/A-1+

\*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings' credit ratings on the global scale are comparable across countries. S&P Global Ratings' credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.

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