

ATB Financial response: February 12 Standing Committee on Public Accounts for FY2018-19 results

Thank you for the opportunity to respond to the six questions that arose during the Standing Committee on Public Accounts on February 12. Unfortunately, the committee overlapped with our ATB Board committee meetings in Calgary where we needed to attend to present our Q3 results, and we were confident in having Treasury Board and Finance speak to our FY2018-19 results as they have historically done at Public Accounts every year.

As the committee focused on FY2018-19 results, it is important to note that this was a highly unusual year due to the Alberta economy. As you know ATB Financial is based in Alberta. Our competitors, including the Big 5 and Canadian Western Bank respectively operate primarily in other provinces and jurisdictions around the world. The geographic difference plays a meaningful role in net income in years when the Alberta economy is struggling as was the case in 2019 with the Canadian GDP at 1.7% and Alberta's substantially lower at 0.4%. Simply by virtue of having economies of scale and the nature of operations (i.e., international activities, plus expanded service offerings such as wholesale banking & capital markets), the impact of the Alberta economy is felt differently by our competitors. A knock-on effect of a struggling provincial economy is ATB's loan loss provisions, and as should be expected, they are more variable than our competitors primarily due to our geographic concentration in Alberta. As reviewed by the Alberta Superintendent of Financial Institutions (ASFI), please be assured that ATB's small business underwriting is sound and following good industry practices.

In our view, the Alberta economy is slowly getting back on its toes, and we are seeing positive momentum building. In our FY2020 third quarter results, we achieved record net income, jumping almost 60% from the same quarter last year. Our income of \$81.7 million for the quarter ending December 31, 2019, meant a contribution of \$118.4 million to the Alberta treasury, an increase of \$16.1 million over the previous quarter and \$36.8 million more than the same quarter last year. Our year-to-date contribution to Alberta's revenue is \$294.8 million—an increase of \$21.3 million from last year. We reported \$35.1 billion in deposits and invested those back into Albertans, with more than \$4 billion in new lending during the third quarter. We are pleased to see an economic recovery moving forward and will continue to be here for Albertans and Alberta businesses as they help to create an incredible future for our province.



Curtis Stange, President and CEO, ATB Financial

Question 1: from Shannon Phillips (NDP) MLA for Lethbridge-West—*What is the difference in profitability between ATB's urban and rural branches?*

- ATB Financial is one of the largest financial institutions in western Canada and currently provides more than \$46 billion of credit to Albertans and Alberta businesses and employs more than 5,500 Albertans in over 300 locations across Alberta.
- With \$54.3 billion in assets, ATB Financial is an Alberta-built financial institution that is a catalyst for economic growth in our province. We got started in 1938 to help Albertans through tough economic times and are still the only financial institution in more than 100 Alberta communities providing personal, business, agriculture, corporate, investment banking, and wealth management services to more than 775,000 customers.
- Our customers spend nearly six hours on the Internet every day—and how they interface with it is changing. For example, about 40% of us use voice commands or voice search today. Combine that speed of computing with massive data sets and how companies like Google, Facebook, and Alibaba are connecting the world, and we recognize the importance of all distribution end-points and places where our customers access banking services, digitally and in person. With heightened competition, lower profitability, and shifting customer expectations, our service model must adapt to changing customer preferences, including more self-service offerings, to remain relevant and profitable.
- As it relates to profitability between ATB's urban and rural branches, the majority continue to be profitable and growing; however, with Alberta's population migrating from rural to urban and customer banking behaviour changing, a shift in stronger profitability and growth rate is occurring in urban communities.

Question 2: from MLA Jason Stephan (UCP) MLA for Red Deer-South—*There is a big difference between the amount of outstanding loans at ATB compared to CWB, and the opposite in relation to net income (loans of \$47B vs \$26B)(net income \$138M vs \$267M). Why is this the case?*

- When it comes to net income, ATB achieved the highest year-over-year growth in net income compared to the Big 5 banks in assessing Q4 2018 over Q4 2019. *(Note: quarter end is at October 31 of each year with ATB's results aligned for comparative purposes. While ATB grew 2.8%, most other banks had a decrease with the exception of Scotia that grew 1%)*
- As the question relates to the Canadian Western Bank (CWB), while ATB and CWB both have roots in Alberta, a number of differences exist between the two organizations. While ATB focuses on Alberta, CWB operates two-thirds of its business outside of Alberta. According to its 2019 annual report, only 32% of CWB loans were granted to Albertans last year, down from 53% about a decade ago. This geographic difference played a meaningful role in CWB's ability to maintain a higher net income in years when the Alberta economy was struggling.

- Our competitor's results are also impacted by the Canadian (and international) economy, compared to ATB, as we operate in Alberta. In 2019, while the Canadian GDP was 1.7%, Alberta's was substantially lower at 0.4%.
- In the course of prudently managing a safe and sound institution, ATB holds over \$5 billion in liquid assets and over \$5 billion in regulatory capital while maintaining strict Board guidance on the management of interest rate risk. Income generation is done with the utmost attention to risk management; ATB complies with top-tier global risk management regulatory guidance for capital and liquidity management including those from the Canadian banking regulator, OSFI.

Question 3: from MLA Jason Stephan (UCP) MLA for Red Deer-South—*ATB has a higher efficiency rate compared to CWB and RBC - and is forecasting an increase between 70-72% for next year. Why is ATB so much higher than these other banks?*

- ATB serves our customers through 315 branches and agencies in 247 communities, in contrast CWB has a presence in 60 locations but does not offer full branch services to their customers. By virtue of having a branch network and serving over 775,000 customers ATB has higher operating costs. With CWB being more focused on business clients they are able to charge higher interest rates on a larger portion of their portfolio compared to ATB. As a result of the difference in mandates, CWB has higher margins and lower operating costs which drives their efficiency ratio lower than ATB's.
- By virtue of having economies of scale and the nature of the Big 5's operations (e.g. international activities, plus expanded service offerings such as wholesale banking & capital markets) their efficiency ratio will inherently be lower than ATB's.
- Since becoming a provincial Crown in 1997, ATB has returned nearly \$4 billion directly back to the Province in earnings and multiples of that figure into the Alberta economy.

Question 4: from MLA Jason Stephan (UCP) MLA for Red Deer-South—*Why doesn't ATB provide any peer-comparative information in its annual report?*

- Including peer-comparative information in ATB's annual report is not a disclosure required by any accounting standards.
- It is important to note that TD, RBC and CWB do not disclose anything related to peer comparisons in their annual reports.
- Of note, ATB leads Alberta's small and mid-sized business banking space, with 22% market share. This is according to a recent report from the Canadian Federation of Independent Business (CFIB). ATB has maintained the number-one spot and widened the gap among the next most popular financial institutions, with RBC coming in second with 17%, TD with 14%,

and credit unions with 12%. Scotiabank rounded out the top five with just shy of 12% market share in Alberta.

Question 5: from MLA Jason Stephan (UCP) MLA for Red Deer-South—*ATB net income in 2018 was \$274M and in 2019 it was \$138M. CWB and RBC both went up year over year. Why is ATB losing money?*

- In 2019, while the Canadian GDP was 1.7%, Alberta's was substantially lower at 0.4%. While ATB is based in Alberta, CWB and RBC respectively operate primarily in other provinces and jurisdictions around the world. This geographic difference played a meaningful role in net income in years when the Alberta economy was struggling.
- ATB's loan loss provisions (LLP) are expected to be more variable than the Big 5 primarily due to our geographic concentration in Alberta.
- Our credit underwriting is periodically reviewed by the Office of the Alberta Superintendent of Financial Institutions (ASFI). The last review was in 2018 and was of our small business underwriting. The report concluded that ATB is following prudent lending policies, practices are consistent with the Board approved credit policies, and good industry practices.
- ATB implemented IFRS9 in April 2018. While we do not believe the implementation has impacted our total LLP, it has contributed to volatility in underpinning estimates.
- Of note, ATB's third-quarter results, released on February 12, reflect the Alberta economy, which is slowly getting back on its feet. In Q3, we achieved record net income, jumping almost 60% from the same quarter last year. Our income of \$81.7 million for the quarter ending December 31, 2019, meant a contribution of \$118.4 million to the Alberta treasury, an increase of \$16.1 million over the previous quarter and \$36.8 million more than the same quarter last year. Our year-to-date contribution to Alberta's revenue is \$294.8 million—an increase of \$21.3 million from last year. We reported \$35.1 billion in deposits—and invested those back into Albertans, with more than \$4 billion in new lending during the third quarter.

Question 6: from MLA Jason Stephan (UCP) MLA for Red Deer-South—*I am concerned about payment in lieu of tax at \$41M (2019) and \$81M (2018). CWB paid \$138M in dividends. Why is ATB returning less to Albertans than smaller banks?*

- ATB had the following impact on Provincial results for this past fiscal year:
 - ATB Net Income: \$138.9 million
 - Payment in lieu of taxes (PILOT) - Issued as sub-debt: \$41.6 million
 - Interest on sub-debt: \$9.2 million
 - Deposit guarantee fee (DGF): \$53.7 million
 - Total FY2019 Benefit: \$243.4 million*
- *in the fiscal year ending March 2020, this benefit is forecasted to grow to \$300 million*

- As a self-funded organization, there is no cost to the government for the operations of ATB.
 - ATB generates a profile that is 100% included in Alberta's budget.
 - ATB provides a PILOT.
 - ATB pays interest on its Wholesale Borrowings.
 - ATB pays at least a market rate for the deposit guarantee.
- Anything that ATB doesn't pay directly to the government (i.e. net income after all of those payments) shows up as earnings to the province in its consolidated financial statements.
- The difference between ATB and CWB's results is largely a function of our higher operating costs due to our community presence and our lower operating revenue due to our geographic constraints and limited access to funding through debt and capital markets.