BELL POTTER

23 November 2017

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Bank of Queensland Capital Notes (BOQPE)

Fixed Income

Issue overview

Issuer	Bank of Qld
Issue ASX code	BOQPE
Face value	$100
Estimated offer size	$300m
Bookbuild margin	3.75-3.95%
Franking	100%
Dividend payments	Quarterly
First dividend payment	15 Feb 2018
Minimum application	$5,000
Call Date	15 Aug 2024
Mandatory Conversion	15 Aug 2026

Timeline

Lodgement of prospectus	22 Nov 2017
Bookbuild margin	29 Nov 2017
Announcement of margin	29 Nov 2017
AGM to approve buy-back	30 Nov 2017
Offer opens	30 Nov 2017
Offer closes	
Securityholder	15 Dec 2017
Reinvestment BOQPD	15 Dec 2017
Broker firm new money	21 Dec 2017
Issue date	28 Dec 2017
ASX listing (deferred settlement)	29 Dec 2017

Breaking a 5 year drought going the early refinancing route

Bank of Queensland's new $300m Capital Notes (BOQPE) has been launched as a Basel III compliant Additional Tier 1 replacement issue 5 months before the 16 April 2018 call date on the $300m BOQPD security. With BOQPE breaking BOQ's 5 year ASX hybrid issuance drought, the decision to refinance BOQPD early capitalises on the strongest hybrid market conditions in over 3 years.

The bookbuild margin range of 3.75-3.95% above 3 month bank bill for a security with an optional call date in Aug 2024 (6.75 years) reflects the market strength, and is consistent with the margins recently set on BENPG (3.75%) and SUNPG (3.65%).

We see the potential for BOQPE to be another successful issue when considering:

- **2017 redemptions currently exceeds new issuance by $4.1bn:** ASX listed debt & hybrid market redemptions for 2017 stand at $9.1bn vs issuance of $5.0bn.
- **Scarcity of new supply:** Issuance is increasingly allocated to the Reinvestment Offer on maturing securities, squeezing the amount available under the New Money Bookbuild and Securityholder Offers.
- **Strength in wholesale debt market:** The trading margin on 5 year major bank wholesale senior debt has firmed in from 1.10% to 0.75% since the start of 2017.

In the absence of an external shock event, we see a continuation of these factors supporting the hybrid market into the period of BOQPE listing in late 2017 / early 2018.

Figure 1: Trading margins on debt and equity securities

	Ranking (prior to exchange)	Security	Trading Margin over BBSW	Maturity / Mand Conv*	First Call
Higher Ranking	Senior debt	BOQ (OTC) senior	100bp	Nov 2021	
↑	Subordinated debt	BOQ (OTC) subordinated	165bp	May 2026	May 2021
↓	**Preferred equity**	**BOQPE (Additional Tier 1)**	**375-395bp**	**Aug 2026***	**Aug 2024#**
Lower Ranking	Equity	Ordinary BOQ Shares	~600bp	Perpetual	

WHERE NOT CONVERTED OR WRITTEN-OFF ON ACCOUNT OF A CAPITAL TRIGGER EVENT OR A NON VIABILITY TRIGGER EVENT. FIRST CALL DATE IS DISCRETIONARY.

SOURCE: YIELDBROKER, BELL POTTER

* MANDATORY CONVERSION IS SUBJECT TO SATISFYING THE MANDATORY CONVERSION CONDITIONS

BOQPE IS PERPETUAL AND MAY NOT BE EXCHANGED.

Key features

- **Initial grossed up coupon of 5.47-5.67% (3.83-3.97% fully franked):** Floating rate based on 3 month bank bill of 1.72% + 3.75-3.95% bookbuild margin.
- **BOQ option to exchange at year 6.75, mandatory conversion at year 8.75:** BOQ has the option to redeem or covert BOQPE at the Aug 2024 Optional Call Date, subject to APRA approval and BOQ being solvent, and a Capital Trigger or a Non-Viability Trigger Event not having occurred. BOQPE may not be exchanged on the scheduled Mandatory Exchange Date, and you may continue to hold BOQPE indefinitely.
- **Ordinary dividend restrictions:** Applies on the non payment of BOQPE distributions. BOQPE distributions are discretionary and subject to the distribution payment conditions being satisfied. Unpaid distributions are non-cumulative.

Bank of Queensland Capital Notes

Reinvestment Key Dates	Dates
BOQPD Ex Entitlement	16 Nov 2017
BOQPD Record Date	17 Nov 2017
Reinvestment Offer Open	27 Nov 2017
AGM to approve buy-back	30 Nov 2017
Reinvestment Offer Close	15 Dec 2017
BOQPD ex div (pro rata)	18 Dec 2017
BOQPD div paid (pro rata)	28 Dec 2017
BOQPD Reinvested	28 Dec 2017
ASX listing (deferred settlement)	29 Dec 2017

Reinvestment Offer for BOQPD

As the BOQPE offer is essentially a replacement issue for $300m BOQ Convertible Preference Shares (BOQPD), BOQ is offering the opportunity to reinvest BOQPD securities held at the 17 November 2017 record date into new BOQPE securities.

In order for BOQ to buy-back BOQPD under Reinvestment Offer or Redemption, it is seeking BOQ Ordinary Securityholder approval at its 30 November 2017 Annual General Meeting (AGM) in respect of the following resolutions:

⇒ Reinvestment Offer Resolution: Buy-back BOQPD under the Reinvestment Offer by a selective buy-back

⇒ Redemption Resolution: Implement an additional selective buy-back of BOQPD to facilitate a potential redemption on 16 April 2018.

If these resolutions are not passed at the AGM, BOQ will not be able to proceed with the Reinvestment Offer, and will remove the option for BOQ to redeem BOQPD at the 16 April 2018 call date. Given our expectation is for both these resolutions to pass, BOQPD holders essentially have three options:

- **Option 1: Participate in Reinvestment Offer:** For BOQPD holders that lodge their Personalised Reinvestment Application form by 15 December 2017, BOQ buy -back and reinvest participating BOQPD securities into BOQPE, subject to the Reinvestment Offer Resolution passing. Investors will receive a pro-rata dividend payment on 28 December 2017 of ~$0.98 fully franked for the 73 day period.
- **Option 2: Sell BOQPD on market**
- **Option 3: Do nothing:** BOQ has an option to exchange (redeem or convert) BOQPD on the 16 April 2018 call date. BOQ will consider exchanging outstanding BOQPD securities closer to the April 2018 call date, subject to satisfactory completion of the BOQPE offer, receipt of all required regulatory and Ordinary Securityholder approvals, and consideration of market conditions. If no exchange occurs at the 16 April 2018 optional call date, BOQPD could potentially remain on issue until the 15 April 2020 Mandatory Conversion date (subject to satisfying the Mandatory Conversion Conditions). This would result in BOQPD investors continuing to receive income at a margin of 5.10% over 6 month bank bill, which is higher than the likely 3.75% margin above 3 month bank bill on BOQPE.

Overall, BOQPD investors need to consider whether the likely 3.75% issue margin on BOQPE is sufficient to participate in the Reinvestment Offer. This is below the 5.10% issue margin on BOQPD, reflecting the market strength in both the ASX listed hybrid market and wholesale debt market. With year to date net redemptions in the ASX listed debt and hybrid market standing at over $4bn, there has been a diminishing supply of new issuance to reinvest into.

Broker Firm and Securityholder Offers

- **Broker Firm Offer:** Broker firm bids will participate in the Bookbuild to be held on 29 November 2017.
- **Securityholder Offer:** Available to investors in BOQ or BOQPD. Applications for investors holding these securities at the 17 November 2017 Record Date requires a HIN or SRN.

There is no Customer Offer or General Offer.

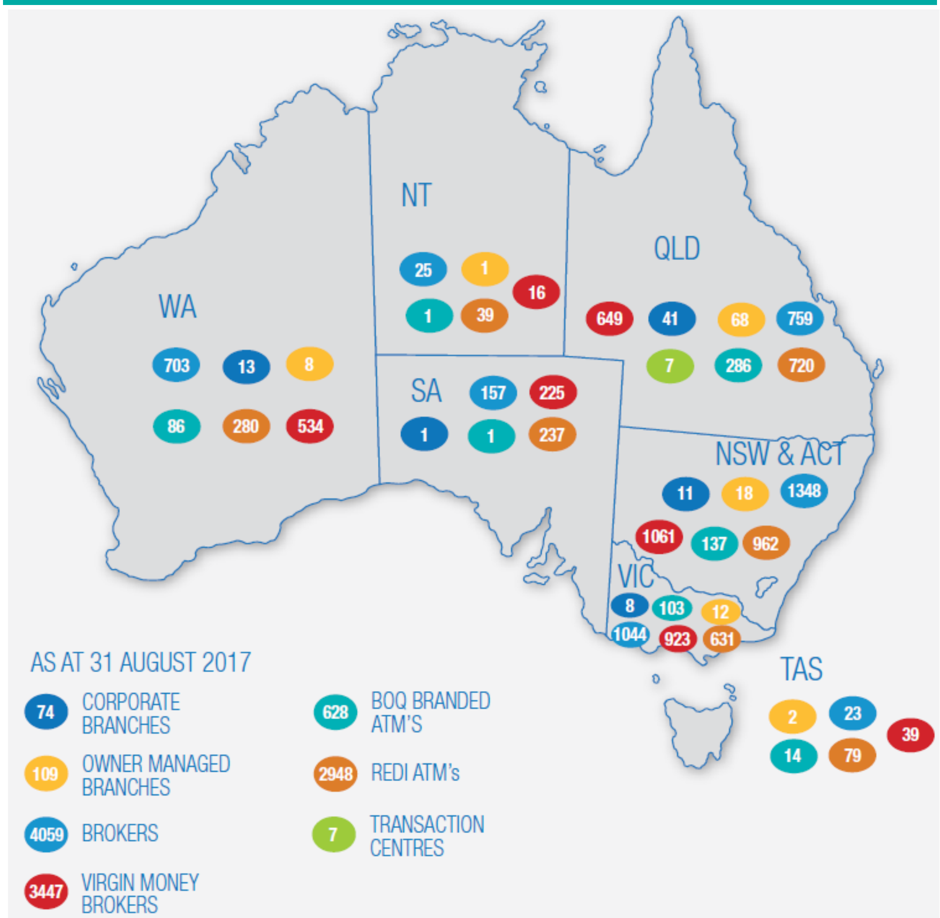
Bank of Queensland Capital Notes

Bank of Queensland Overview

With a history dating back to 1874, BOQ is today one of Australia's leading regional banks providing banking and insurance services primarily to retail customers and small to medium sized business. BOQ's operations span a network of 190 locations throughout Australia, including 109 Owner Manager Branches (OMB), 74 corporate branches owned and operated by BOQ, and 7 transaction centres. BOQ is currently ranked among the top 100 largest ASX listed companies (market cap $5.0bn) and operates four business segments:

- Banking - Retail: Banking and insurance services to households including deposit and lending products and credit cards. The distribution footprint has expanded to over 7,500 brokers following the 2013 acquisition of Virgin Money.
- Banking - Business: BOQ products include transactional accounts, treasury and FX risk management services, merchant services and lending products.
- BOQ Finance - BOQ is a provider of equipment and debtor financing, boosted by the December 2016 acquisition of Centrepoint Alliance Premium Funding (BOQF Cashlow Finance) to create a new Cashlow Finance team.
- St Andrew's Insurance - Acquired in July 2010, St Andrew's Insurance provides consumer credit insurance and life insurance.

Figure 2: BOQ branch network



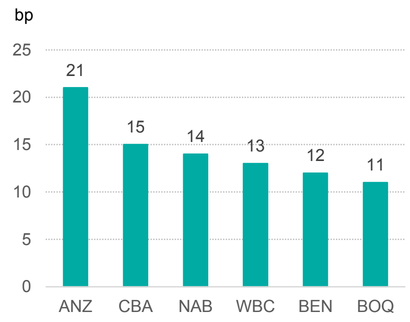
SOURCE: COMPANY

Bank of Queensland Capital Notes

BOQ strengthened & de-risked since BOQPD launch in 2012

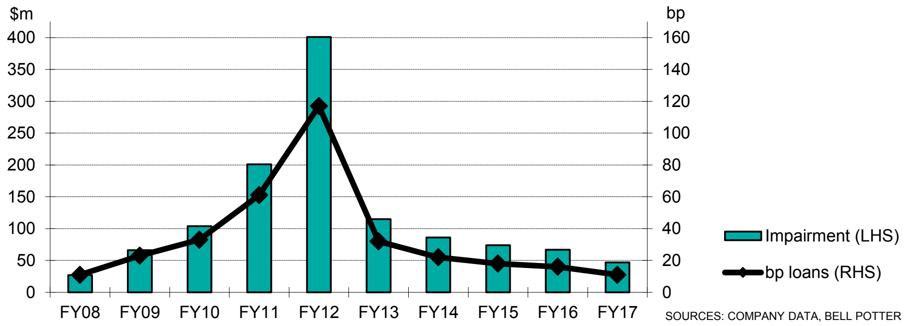
When compared with the environment when BOQPD launched in Nov 2012, BOQ in 2017 has significantly de-risked its operations. In 1H12, BOQ reported the first banking loss since 1992 after its impairment charge spiked to $328m (194bp of loans), driven by a continued decline in Queensland commercial property prices and weakness in the Gold Coast residential property market.

Figure 3: FY17 Impairment (bp loans)



SOURCES: COMPANY DATA, BELL POTTER

Figure 4: BOQ Impairment Charge FY08-FY17

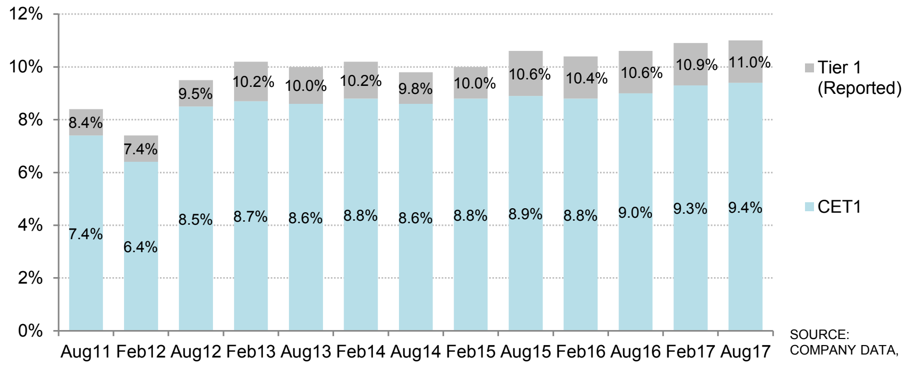


SOURCES: COMPANY DATA, BELL POTTER

BOQ's de-risking strategy has seen its impairment charge fall to $48m in FY17, equating to only 11bp of loans. This now places BOQ on the lowest impairment charge (on a bp to loans basis) of peers including the 4 major banks and BEN.

Post the $450m equity raising in March 2012, BOQ has steadily grown its Common Equity Tier 1 capital to a strong 9.4% at August 2017.

Figure 5: BOQ Common Equity Tier 1 Ratio - 2011 to 2017



SOURCE: COMPANY DATA,

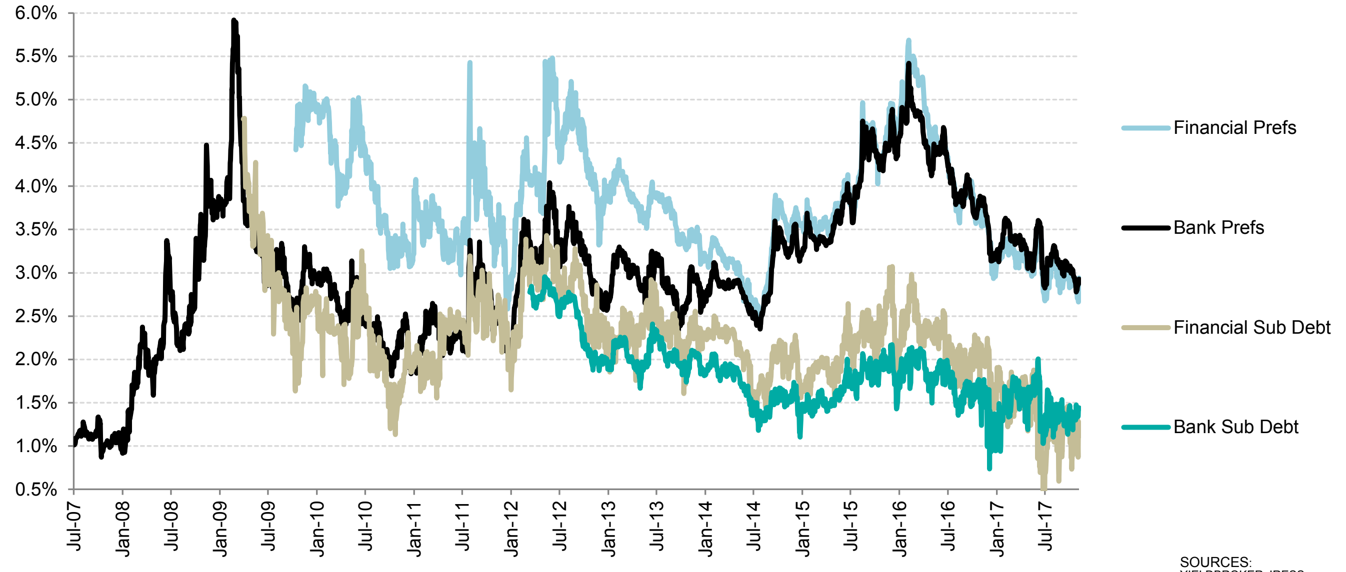
Bank of Queensland Capital Notes

Trading margins on bank and financial hybrids rally to 3 year lows

Figure 6 tracks the average trading margins split across 4 sectors:

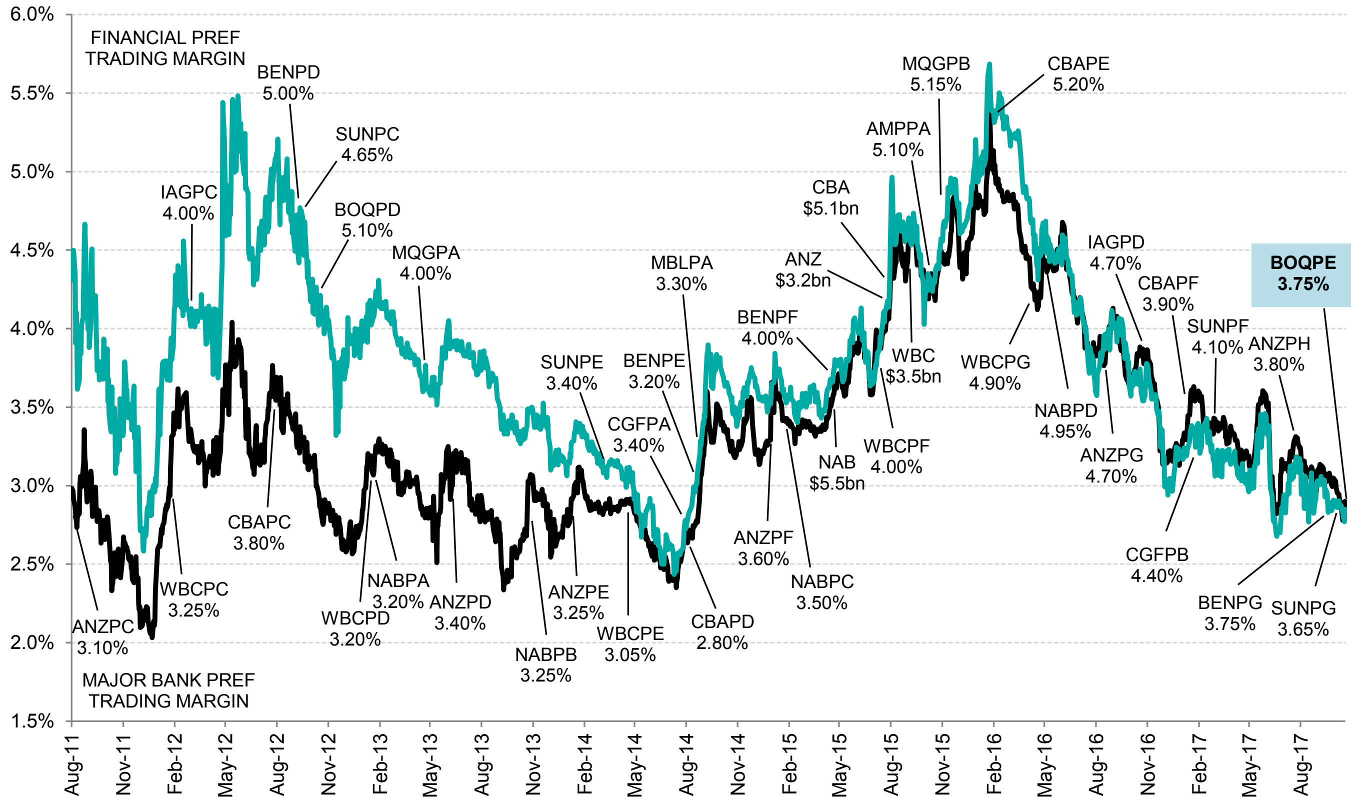
* Financial Prefs (AMPPA, BENPE, BENPF, CGFPA, CGFPB, IAGPD, IANG, MBLPA, MQGPA, MQGPB, SUNPE, SUNPF)
* Bank Prefs (ANZPD, ANZPE, ANZPF, ANZPG, ANZPH, CBAPC, CBAPD, CBAPE, CBAPF, NABPA, NABPB, NABPC, NABPD, WBCPD, WBCPE, WBCPF, WBCPG)
* Financial Subordinated Debt (AMPHA, SUNPD)
* Bank Subordinated Debt (NABPE, WBCHB).

Figure 6: Trading margins on ASX listed debt and hybrid sectors



SOURCES: YIELDBROKER, IRESS, BELL POTTER

Figure 7: Average trading margins on bank and financial prefs



SOURCES: IRESS, BLOOMBERG, BELL POTTER

Bank of Queensland Capital Notes

3.75% issue margin provides buffer between launch & listing

One key metric to consider when investing in a new hybrid issue is the attractiveness of the pricing compared with prevailing market pricing reflected by the average trading margin of the 12 financial prefs and capital notes. Attractive pricing to ensure a listing premium has been a key factor behind the last 11 bank / financial hybrids launched since AMPPA in Oct 2015 listing at a premium. This has been crucial for restoring investor confidence, and support for new hybrid issues.

Assuming BOQPE's issue margin is set at the bottom end of the bookbuild range at 3.75%, this represents a spread of 0.85% to the prevailing market of 2.90% on the 12 financial convertible prefs / capital notes. This is above the median new issue spread of 0.45% on the 37 major bank / financial hybrid issues since 2011.

This spread 0.85% reflects the extra duration on BOQPE with 6.75 years to its August 2024 optional call date, versus the average duration of the 12 financial hybrids of 3.4 years. It also provides a buffer for a modest adverse market move between BOQPE launching and listing.

Figure 8: Listing performance of Basel III Compliant Additional Tier 1 Hybrid Issues: 2011-2017

Security	Launched	Issue Margin	Trading Margin Index Bank / Financial	Issue Margin Spread vs Trading Margin	Listing Date	Opening Price	Trading Margin Index Bank / Financial	Trading Margin Index Change Since Launch
BOQPE	22 Nov 2017	3.75%	2.90%	0.85%	29 Dec 2017			
SUNPG	23 Oct 2017	3.65%	2.90%	0.75%	27 Nov 2017			
BENPG	16 Oct 2017	3.75%	2.90%	0.85%	14 Dec 2017			
ANZPH	16 Aug 2017	3.80%	3.30%	0.50%	29 Sep 2017	$101.10	3.12%	-0.18%
SUNPF	27 Mar 2017	4.10%	3.10%	1.00%	8 May 2017	$101.26	3.05%	-0.05%
CGFPB	28 Feb 2017	4.40%	3.25%	1.15%	10 Apr 2017	$101.20	3.17%	-0.08%
CBAPF	20 Feb 2017	3.90%	3.45%	0.45%	3 Apr 2017	$102.00	3.37%	-0.08%
IAGPD	21 Nov 2016	4.70%	3.60%	1.10%	23 Dec 2016	$103.00	3.18%	-0.42%
ANZPG	16 Aug 2016	4.70%	3.80%	0.90%	28 Sep 2016	$100.63	4.02%	0.22%
NABPD	31 May 2016	4.95%	4.40%	0.55%	8 Jul 2016	$100.50	4.32%	-0.08%
WBCPG	17 May 2016	4.90%	4.20%	0.70%	1 Jul 2016	$100.90	4.49%	0.29%
CBAPE	16 Feb 2016	5.20%	5.40%	-0.20%	31 Mar 2016	$100.00	4.80%	-0.60%
MQGPB	23 Nov 2015	5.15%	4.57%	0.58%	21 Dec 2015	$100.51	4.77%	0.20%
AMPPA	26 Oct 2015	5.10%	4.27%	0.83%	1 Dec 2015	$100.10	4.70%	0.43%
WBCPF	27 Jul 2015	4.00%	3.94%	0.06%	9 Sep 2015	$99.00	4.51%	0.57%
BENPF	27 Apr 2015	4.00%	3.47%	0.53%	16 Jun 2015	$99.10	3.91%	0.44%
NABPC	17 Feb 2015	3.50%	3.43%	0.07%	23 Mar 2015	$100.00	3.40%	-0.03%
ANZPF	27 Jan 2015	3.60%	3.63%	-0.03%	6 Mar 2015	$99.99	3.33%	-0.30%
MBLPA	16 Sep 2014	3.30%	3.20%	0.10%	9 Oct 2014	$98.00	3.62%	0.42%
BENPE	3 Sep 2014	3.20%	2.92%	0.28%	13 Oct 2014	$98.00	3.76%	0.84%
CGFPA	27 Aug 2014	3.40%	2.82%	0.58%	10 Oct 2014	$99.00	3.69%	0.87%
CBAPD	18 Aug 2014	2.80%	2.62%	0.18%	2 Oct 2014	$97.00	3.45%	0.83%
WBCPE	7 May 2014	3.05%	2.90%	0.15%	24 Jun 2014	$101.48	2.61%	-0.29%
SUNPE	31 Mar 2014	3.40%	3.11%	0.29%	9 May 2014	$101.19	3.11%	0.00%
ANZPE	11 Feb 2014	3.25%	3.12%	0.13%	1 Apr 2014	$100.75	2.89%	-0.23%
NABPB	12 Nov 2013	3.25%	2.78%	0.47%	18 Dec 2013	$100.25	2.88%	0.10%
ANZPD	3 Jul 2013	3.40%	3.19%	0.21%	8 Aug 2013	$100.00	2.88%	-0.31%
MQGPA	14 May 2013	4.00%	3.65%	0.35%	20 Jun 2013	$100.70	3.91%	0.26%
NABPA	13 Feb 2013	3.20%	3.20%	0.00%	21 Mar 2013	$99.75	3.15%	-0.05%
WBCPD	30 Jan 2013	3.20%	3.12%	0.08%	12 Mar 2013	$99.94	3.15%	0.03%
BOQPD	7 Nov 2012	5.10%	4.17%	0.93%	27 Dec 2012	$101.00	4.07%	-0.10%
SUNPC	25 Sep 2012	4.65%	4.61%	0.04%	7 Nov 2012	$101.48	4.17%	-0.44%
BENPD	24 Sep 2012	5.00%	4.49%	0.51%	1 Nov 2012	$101.00	4.26%	-0.23%
CBAPC	3 Sep 2012	3.80%	3.34%	0.46%	18 Oct 2012	$101.61	3.10%	-0.24%
IAGPC	19 Mar 2012	4.00%	4.11%	-0.11%	2 May 2012	$99.60	4.01%	-0.10%
WBCPC	16 Feb 2012	3.25%	3.19%	0.06%	26 Mar 2012	$99.75	3.24%	0.05%
ANZPC	23 Aug 2011	3.10%	2.98%	0.12%	29 Sep 2011	$100.00	2.80%	-0.18%
			Median:	0.45%				

SOURCE: COMPANY DATA, IRESS, BELL POTTER

Bank of Queensland Capital Notes

ASX listed debt & hybrid market net redemptions at $4.1bn

With net hybrid redemptions currently at $4.1bn, 2017 will be the first year of net hybrid redemptions since 2010. In addition, equity IPO volumes have been modest at $5.1bn, where 6 of the 10 IPOs over $100m have been Listed Investment Companies / Trusts. By contrast, Net Hybrid and Equity Issuance (including major bank raisings) in 2015 totalled $28.8bn. This 2015 spike in capital raisings coincided with weakness in the hybrid market, highlighted by the average trading margin on major bank prefs / capital notes jumping from 3.13% to 4.48% over the year.

Figure 9: Net Hybrid Issuance 2010-2017

Issuance ($bn)	2010	2011	2012	2013	2014	2015	2016	2017YTD	Cumulative
Hybrid Issuance	0.92	3.42	13.16	8.66	7.46	5.60	7.03	5.02	51.27
Hybrid Redemptions	1.10	1.68	3.09	2.42	5.90	1.07	5.68	9.12	30.06
Net Hybrid Issuance	-0.17	1.75	10.07	6.24	1.56	4.53	1.35	-4.10	25.32
IPOs	7.98	1.56	1.27	9.69	18.65	7.00	8.32	5.06	59.53
Major Bank Raisings	0.00	0.00	0.00	0.00	0.00	17.30	0.00	0.00	17.30
Net Hybrid & Equity Issuance	**7.81**	**3.31**	**11.34**	**15.93**	**20.21**	**28.83**	**9.67**	**0.96**	**102.15**
Bank Pref Avg Trading Margin (31 Dec)	1.92%	2.14%	2.76%	2.72%	3.13%	4.48%	3.22%	2.94%	
Bank Pref Avg Duration (years) (31 Dec)	3.6	3.0	3.2	3.9	5.1	4.4	4.1	3.9	
Bank 5YrSnr Trading Margin (31 Dec)	1.13%	1.54%	0.96%	0.94%	0.82%	1.07%	1.10%	0.75%	
CBA CET1 (30 June)	6.6%	7.3%	7.5%	8.2%	9.3%	9.1%	9.6%	10.1%	

SOURCES: ASX, AFR, BLOOMBERG, COMPANY DATA, BELL POTTER

2018 likely to be another year of net hybrid redemptions

If hybrid issuance aligns with refinancing maturing Additional Tier 1 hybrids in 2018, there may be as few as 3 new issues launched. The $1,189m WBCPC refinancing is likely to occur in early 2018, where the new money requirement appears to be reduced following Westpac raising US$1.25bn in its offshore Additional Tier 1 hybrid raising in September 2017. Refinancing issues for the $600m MQGPA in June 2018 and $2,000m CBAPC in December 2018 appear likely.

At this stage, it appears difficult to envisage a 2018 new issuance pipeline that exceeds the $7bn of expected redemptions for the ASX listed debt and hybrid market.

Figure 10: Refinancing considerations for ASX listed debt and hybrid securities with 2018 call dates

ASX Code	Security	Call Date	Issue Size	Replacement Issue Considerations
AQHHA	APA Subordinated Notes	31 Mar 2018	$515m	Redemption expected at call date, most likely funded out of bank debt facilities.
WBCHB	Westpac Subordinated Notes II	22 Aug 2018	$925m	Redemption expected at call date. Refinanced WBCHA at Aug 2017 call date.
CWNHA#	Crown Subordinated Notes	14 Sep 2018	$404m	Redemption expected at call date. Conducting on market buy-back. Unlikely to reissue.
SUNPD	Suncorp Subordinated Notes	22 Nov 2018	$770m	Redemption expected at call date. Expect wholesale Tier 2 subordinated debt issue.
AMPHA	AMP Subordinated Notes 2	18 Dec 2018	$325m	Redemption expected at call date. AMP has issued wholesale Tier 2 subordinated debt.
ASX Listed Debt Redemptions Pending			$2,939m	
WBCPC	Westpac CPS	31 Mar 2018	$1,189m	Likely replacement issue. New money requirement reduced by Sep17 US$1.25bn hybrid
BOQPD	Bank of Queensland CPS	15 Apr 2018	$300m	BOQPE
MQGPA	Macquarie Group Capital Notes	7 Jun 2018	$600m	Basel III compliant Additional Tier 1 replacement issue expected.
WHFPB	Whitefield Convertible Reset Pref	30 Nov 2018	$40m	Likely to be converted into WHF shares. Potential to undertake replacement issue.
CBAPC	CBA PERLS VI	15 Dec 2018	$2,000m	Basel III compliant Additional Tier 1 replacement issue expected.
ASX Listed Hybrid Redemptions Pending			$4,129m	
			$7,068m	

ON MARKET BUY-BACK HAS ACQUIRED $128m OF $532m CWNHA SECURITIES

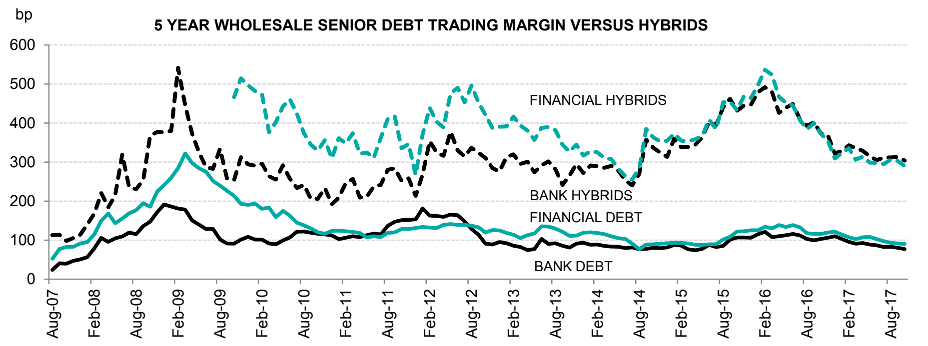
SOURCES: COMPANY DATA, BELL POTTER

Bank of Queensland Capital Notes

Hybrids still offer value relative to senior debt

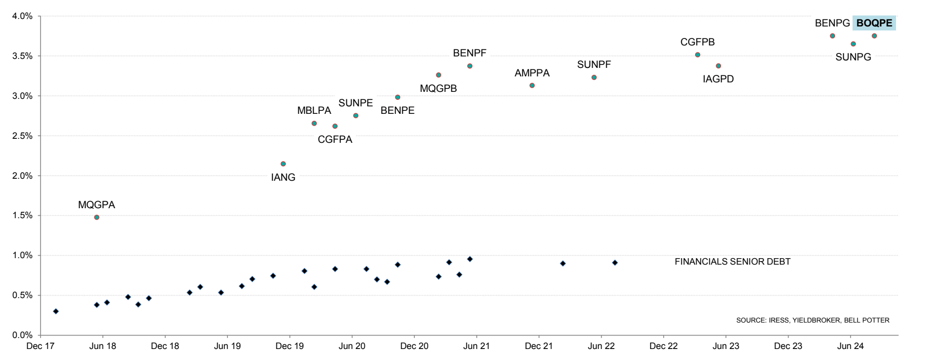
In strong hybrid markets since 2010, the spread between major bank senior debt and hybrids has compressed below 2.00%. Assuming BOQPE is priced at a margin of 3.75%, this represents a 2.75% spread above Nov 2021 (4 year) BOQ wholesale senior debt. After factoring in the yield curve impact of the extra 2.75 years duration on BOQPE (6.75 years to Aug 2024 optional call date) this 2.75% spread remains sufficient.

Figure 11: Average trading margins versus wholesale senior debt



SOURCE: YIELDBROKER, BELL POTTER

Figure 12: Trading margins on ASX listed financial prefs & capital notes: 22Nov17



SOURCE: IRESS, YIELDBROKER, BELL POTTER

BOQPD reinvestment likely to raise $135-180m

If the participation trend in recent reinvestment offers continues at a range of 45-60%, then we expect between $135m to $180m of the $300m BOQPD issue will be reinvested into BOQPE. Given the strength of the hybrid market and lack of new issuance, there is the potential for reinvestment participation to be at the upper end of this range, which will further squeeze the supply available for new money investment.

Figure 13: Participation in reinvestment offer replacement issues

Issue	Target	Bookbuild Completion	Reinvestment Offer	Securityholder Offer	Final Size	Securityholder Full Allocation Cap	Allocation Above Cap	Cornerstone (BNP Paribas Noms)
SUNPG	$250m	$300m	SUNPC undisclosed	$0m		No Offer		
BENPG	$300m	$260m	BENPD $124m (46.1%)					
ANZPH	$1,000m	$552m	ANZPC $682m (50.9%)	$248m	$931m	Full Allocation		
SUNPF	$250m	$300m	No	$75m	$375m	$300,000	28.5%	
CGFPB	$350m	$430m	No	$30m	$460m	$300,000	89.7%	
CBAPF	$750m	$1,450m	CNGHA undisclosed	$190m	$1,640m	$15,000	0%	$230m
IAGPD	$300m	$350m	IAGPC $224m (59.5%)	$0m	$404m	No Offer		
ANZPG	$1,000	$1,300m	ANZPA $900m (45.7%)	$322m	$1,622m	Full Allocation		
NABPD	$750m	$1,350m	No	$149m	$1,499m	Full Allocation		$300m
WBCPG	$750m	$1,450m	WCTPA undisclosed	$252m	$1,702m	$25,000	87.5%	$300m
CBAPE	$1,250m	$910m	PCAPA $260m (22.3%)	$540m	$1,450m	$15,000	95.0%	$285m

NOTE: ANZPH DID NOT CONDUCT A NEW MONEY BOOKBUILD. SOURCES: COMPANY DATA, IRESS, BELL POTTER

Bank of Queensland Capital Notes

Mandatory Conversion Conditions

In order for bank Convertible Preference Shares (CPS) and Capital Notes to qualify as Additional Tier 1 capital, APRA has imposed a maximum conversion number in order to limit the dilution of ordinary shares upon conversion.

This maximum conversion number represents the face value of the preference share divided by 50% of the volume weighted average price (VWAP) of the issuer on the 20 business days preceding the issue date (Issue Date VWAP). For example, if BOQ's 20 day VWAP was $12.65 before the issue date, the maximum conversion number would be 15.81 BOQ shares per BOQPE security (i.e. $100 / (50% x $12.65)).

To protect BOQPE holders from receiving less than face value at Mandatory Conversion, there are a number of Conversion Conditions to be aware of:

- First: VWAP of ordinary shares on the 25th business day before a possible Mandatory Conversion Date (13 July 2026) must be above 56% of the Issue Date VWAP. Using the BOQ price on 22 November 2017 of $12.65 x 56% = $7.08.
- Second: VWAP of ordinary shares during the 20 business days immediately preceding a potential Mandatory Conversion Date (20 July 2026 - 14 August 2026) must be greater than 50.51% of the BOQPE Issue Date VWAP (i.e. $6.39).
- Third: Continuous trading (i.e. No Delisting Event) prior to a possible Mandatory Conversion Date - to provide protection should investors wish to sell the ordinary shares they receive upon conversion. A Delisting Event occurs when BOQ is delisted or suspended, or there is an Inability Event.

If the Mandatory Conversion Conditions are not satisfied, conversion on the Mandatory Conversion Date will not occur. Under this scenario, the security will remain on issue and continue to pay distributions at the same margin. The Conversion Conditions will be tested on each subsequent future quarterly distribution date. The payment of BOQPE distributions is subject to satisfaction of the Distribution Payment Conditions.

Figure 14: Mandatory Conversion Conditions - Financial Prefs / Capital Notes

	BOQPE	AMPPA	BENPD	BENPE	BENPF	BENPG	BOQPD	CGFPA	CGFPB	IAGPD	MBLPA	MQGPA	MQGPB	SUNPC	SUNPE	SUNPF	SUNPG
Issue Date	28-Dec-17	30-Nov-15	1-Nov-12	10-Oct-14	15-Jun-15	13-Dec-17	24-Dec-12	9-Oct-14	7-Apr-17	22-Dec-16	8-Oct-14	7-Jun-13	18-Dec-15	6-Nov-12	8-May-14	5-May-17	24-Nov-17
Mandatory Conversion Date	15-Aug-26	22-Dec-23	13-Dec-19	30-Nov-22	15-Jun-23	15-Jun-26	15-Apr-20	25-May-22	22-May-25	16-Jun-25	24-Mar-23	7-Jun-21	18-Mar-24	17-Dec-19	17-Jun-22	17-Jun-24	17-Jun-26
Conversion Discount	1.0%	1.0%	2.5%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Issue Date VWAP	$12.65	$5.78	$7.98	$12.08	$12.09	$11.25	$7.11	$7.23	$12.30	$5.75	$57.93	$42.42	$81.33	$9.49	$12.92	$13.50	$14.05
50% Dilution Cap	$6.33	$2.89	$3.99	$6.04	$6.05	$5.63	$3.55	$3.61	$6.15	$2.88	$28.97	$21.21	$40.67	$4.75	$6.46	$6.75	$7.03
Max Conv No (Face Value/Dilution Cap)	15.81	34.60	25.06	16.56	16.54	17.78	28.15	27.67	16.26	34.78	3.45	4.71	2.46	21.07	15.48	14.81	14.23
Conv Test 1 - % Issue Date VWAP	56.00%	56.00%	57.50%	55.00%	55.00%	55.00%	56.12%	55.00%	55.00%	57.50%	56.00%	56.00%	56.00%	55.00%	55.00%	55.00%	55.00%
Conv Test 1 Security Price	$7.08	$3.24	$4.59	$6.64	$6.65	$6.19	$3.99	$3.98	$6.77	$3.31	$32.44	$23.76	$45.54	$5.22	$7.11	$7.43	$7.73
Conv Test 2 - % Issue Date VWAP	50.51%	50.51%	51.28%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%	50.51%
Conv Test 2 Security Price	$6.39	$2.92	$4.09	$6.10	$6.11	$5.68	$3.59	$3.65	$6.21	$2.90	$29.26	$21.43	$41.08	$4.79	$6.53	$6.82	$7.10
Conv Test 3 - Continuous Trading	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Parent Share Price - 22 Nov 2017	$12.65	$5.14	$11.25	$11.25	$11.25	$11.25	$12.65	$13.74	$13.74	$7.33	$99.50	$99.50	$99.50	$14.05	$14.05	$14.05	$14.05
Prem/Disc to Dilution Cap	100.0%	77.9%	182.0%	86.3%	86.1%	100.0%	256.1%	280.2%	123.4%	155.0%	243.5%	369.1%	144.7%	196.1%	117.5%	108.1%	100.0%
Prem/Disc to Conversion Test 1	78.6%	58.8%	145.2%	69.3%	69.2%	81.8%	217.2%	245.6%	103.1%	121.7%	206.7%	318.9%	118.5%	169.2%	97.7%	89.2%	81.8%

Bank of Queensland Capital Notes

Early Conversion Events: Capital Trigger and Non-Viability

The fallout from the Global Financial Crisis has seen the Basel Committee on Banking Supervision establish new capital reforms to be phased in between 1 January 2013 and 1 January 2019. The key objective of these new reforms is to ensure banks are adequately capitalised in the event of future crises. On 28 September 2012, APRA published its final Basel III prudential standards which include a number of changes to the eligibility criteria for capital instruments, including stricter criteria for instruments to qualify as Additional Tier 1 Capital.

These requirements include a Capital Trigger Event and a Non-Viability Trigger Event, where securities such as BOQPE must be converted into ordinary equity if the financial position of BOQ requires an immediate injection of capital. These prudential standards also require Australian banks to hold a minimum Common Equity Tier 1 Capital Ratio of 4.5% on 1 Jan 2013. This increased to 7.0% on 1 Jan 2016 after inclusion of the 2.5% Capital Conservation Buffer.

Capital Trigger Event

A Capital Trigger Event occurs when either BOQ determines, or when APRA notifies BOQ that it believes BOQ's Common Equity Tier 1 Capital Ratio has is equal to or less than 5.125%. Under this Trigger, BOQ must immediately Exchange enough BOQPE, and BOQPD securities to boost the Common Equity Tier 1 (CET1) Capital Ratio above 5.125%. BOQ's Basel III CET1 Ratio at 31 August 2017 stood at 9.4%, providing a buffer of $1.2bn. If we include BOQ's cash net profit for the 12 months to August 2017 of $378m, a breach of the Common Equity Trigger requirement appears very low, particularly as BOQ has options such as cutting ordinary dividends, divesting assets and undertaking equity raisings.

Non-Viability Trigger Event

In addition, BOQPE will be Converted if APRA determines that BOQ would be non-viable in the absence of an exchange or a public sector injection of capital. We note there are currently no precedents for a Non-Viability Trigger Event. Types of situations in which APRA may become concerned about non-viability include being insolvent, significant capital losses and financial stress, prolonged difficulties in raising funding in the public or private market, or maintaining sufficient liquidity.

Potential for Loss under Trigger Event if BOQ under $2.53

Conversion resulting from a Capital Trigger Event or a Non-Viability Trigger Event will be done at the VWAP of BOQ shares traded on the 5 Business Days immediately preceding the Conversion Date. While this is not subject to the Mandatory Exchange Conditions, it is still subject to the Maximum Conversion Number, which represents the face value of the preference share dividend by 20% of the issue date VWAP. If BOQ's 20 issue date VWAP was $12.65, the maximum conversion number would be 39.53 BOQ shares per BOQPE security (i.e. $100 / (20% x $12.65)). As such, BOQPE investors may be exposed to receiving less than face value if BOQPE is converted at less than $2.53. In practice this will only occur in the unlikely scenario that the issuer suffers severe impairment losses and does not raise equity to absorb those losses.

As it is likely that conversion under one of these Trigger Events would occur prior to a company Wind Up, BOQPE holders will hold ordinary shares and rank equally with other holders of ordinary shares (i.e. lose priority ranking).

Bank of Queensland Capital Notes

Inability Event

One additional risk is an Inability Event where BOQPE will be written off if BOQ is not able to issue ordinary shares from Conversion within five Business Days of the Trigger Event Conversion Date (i.e. Capital Trigger Event or Non-Viability Trigger Event). Scenarios under which this may occur include BOQ being prevented from issuing ordinary shares by circumstances outside of its control, including an applicable law or order of any court, or action of any Government authority from issuing shares.

Under an Inability Event, BOQPE holder's rights (including to distributions and face value) are immediately and irrevocably terminated, resulting in BOQPE losing its value and investors will not receive any compensation.

ASIC "Be wary of the risks" warning: Money Smart website

ASIC's Money Smart website provides information for retail investors who are considering investing in "Complex Investments" such as hybrid securities:

www.moneysmart.gov.au/investing/complex-investments/hybrid-securities-and-notes

Basically, hybrid securities (including subordinated notes and convertible preference shares) may be from well-known companies but they are very different from 'normal' corporate bonds.

Some hybrid securities make investors take on 'equity-like' risks. Some also have terms and conditions that allow the issuer to exit the deal or suspend interest payments when they choose. Some are very long-term investments (for example, more than 20 years).

Hybrid securities may be unsuitable for you if you need steady returns or capital security typically from a bank term deposit style of investment.

Bank of Queensland Capital Notes

Other investment risks

Investment risks

Key Security Risks include:

- BOQPE is not a bank deposit protected by the Government guarantee scheme
- BOQPE is subordinated and unsecured, and ranks behind deposits, senior debt and subordinated debt in BOQ.
- BOQPE distributions are non-cumulative and discretionary.
- BOQPE distribution payments are subject to the following Payment Conditions:
  - ⇒ BOQ, in its absolute discretion, making the Distribution;
  - ⇒ Payment not resulting in a breach of BOQ's capital requirements as they are applied to the BOQ Level 1 Group or the BOQ Level 2 Group or both under APRA's prudential standards;
  - ⇒ Payment not resulting in BOQ becoming insolvent; and
  - ⇒ APRA not otherwise objecting to the payment.
- Adverse movement in credit spreads as a result of a tightening in the availability and cost of credit.
- New issues may offer more attractive issue terms and margins, placing downward pressure on the security price.
- Adverse change in BOQ's and financial performance which combined with a major bad debt event could lead to the Common Equity Tier 1 Capital Ratio falling below 5.125%, resulting in automatic conversion under the Capital Trigger Event. Automatic conversion may also be required under a Non-Viability Trigger Event.
- BOQPE will lose its value and investors will not receive any compensation if BOQ is not able to issue ordinary shares within 5 business days from Conversion under a Capital Trigger Event or Non-Viability Trigger. Scenarios under which this may occur include BOQ being prevented from issuing ordinary shares by circumstances outside of its control, including an applicable law or order of any court, or action of any Government authority from issuing shares.
- Conversion of BOQPE at the 15 August 2026 Mandatory Exchange Date requires BOQ's share price at the time of Mandatory Exchange to be above certain thresholds. If these thresholds are not met in August 2026 or at future quarterly dividend payment dates, BOQPE may remain on issue indefinitely.
- BOQPE holders may receive $101.01 of ordinary shares for each BOQPE security held on the Mandatory Conversion Date, based on the 20 day VWAP. The VWAP may be higher than the market value of BOQ shares on Conversion

Key Business Risks of BOQ include:

- A material deterioration in global capital markets and the Australian economy.
- Weakening real estate markets in Australia.
- Adverse regulatory changes.
- Operational risks and trading errors.
- Increasing competition.
- Credit rating downgrades.
- Losses associated with counterparty exposures.
- Poor performance of acquired businesses.

Refer page 53 (Section 4) of the prospectus dated 22 November 2017 for further information on risks.

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Additional risks of hybrid securities

Hybrid securities are perpetual and do not constitute a deposit liability of the Issuer. They may be exchanged at the Issuer's discretion at the Optional Exchange Date (first call date) and then at the Mandatory Conversion Date if certain conditions have been satisfied. Hybrid securities pay discretionary dividends which are not cumulative if unpaid. Hybrid securities have complex terms of issue and each investment will differ in terms of conditions, time frame and interest rates. They often involve heightened risk and may not be suitable for all investors.

There are additional risks associated with this kind of investment as compared to a term deposit with the same issuer. These risks include:

- A 'trigger event' occurring leading to a deferral of interest payments or the Issuer repaying the hybrid early or much later than expected;
- Credit spreads widening making the return from the investment less attractive in comparison to other products;
- Additional new issuance at a higher margin;
- Market price volatility;
- Liquidity risk for hybrids is generally greater than shares in the Issuer company;
- Subordinated ranking;
- Distributions are at the discretion of the issuer;
- These products may be perpetual and can only be redeemed or exchanged for either cash or equity at the Issuer's option;
- Early repayment is at the Issuer's discretion

You should acquaint yourself with the specific returns, features, benefits and risks unique to any hybrid security before investing in them. If you do not understand, or have any concerns about a particular product you should talk to your Adviser. ASIC has published guidance, which may be relevant to your consideration of an investment of this kind, called "Hybrid securities and notes", under the heading 'Complex investments' at **www.moneysmart.gov.au/investing**

Disclosure of interest:

Bell Potter Limited, its employees, consultants and its associates within the meaning of Chapter 7 of the Corporations Law may receive commissions, underwriting and management fees from transactions involving securities referred to in this document (which its representatives may directly share) and may from time to time hold interests in the securities referred to in this document.

Additional disclosure:

Bell Potter Securities Limited has acted as Co-manager to the following issues: AMPHA, ANZPD, ANZPE, BENPD, BOQPD, CBAPC, CBAPD, CBAPE, CBAPF, CWNHA, IANG, MXUPA, MQGPB, NABPA, NABPB, NABPD, NFNG, SUNPC, SUNPD, TTSHA, WBCHB, WBCPF & WBCPG. Bell Potter Securities Limited received fees for these services.

ANALYST CERTIFICATION

Each analyst is primarily responsible for the content of this research report, in whole or in part, certifies that with respect to each security or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about those securities or issuers and were prepared in an independent manner and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed by that research analyst in the research report.