New Zealand's banks report lending growth, but profits are down

Banking Perspectives

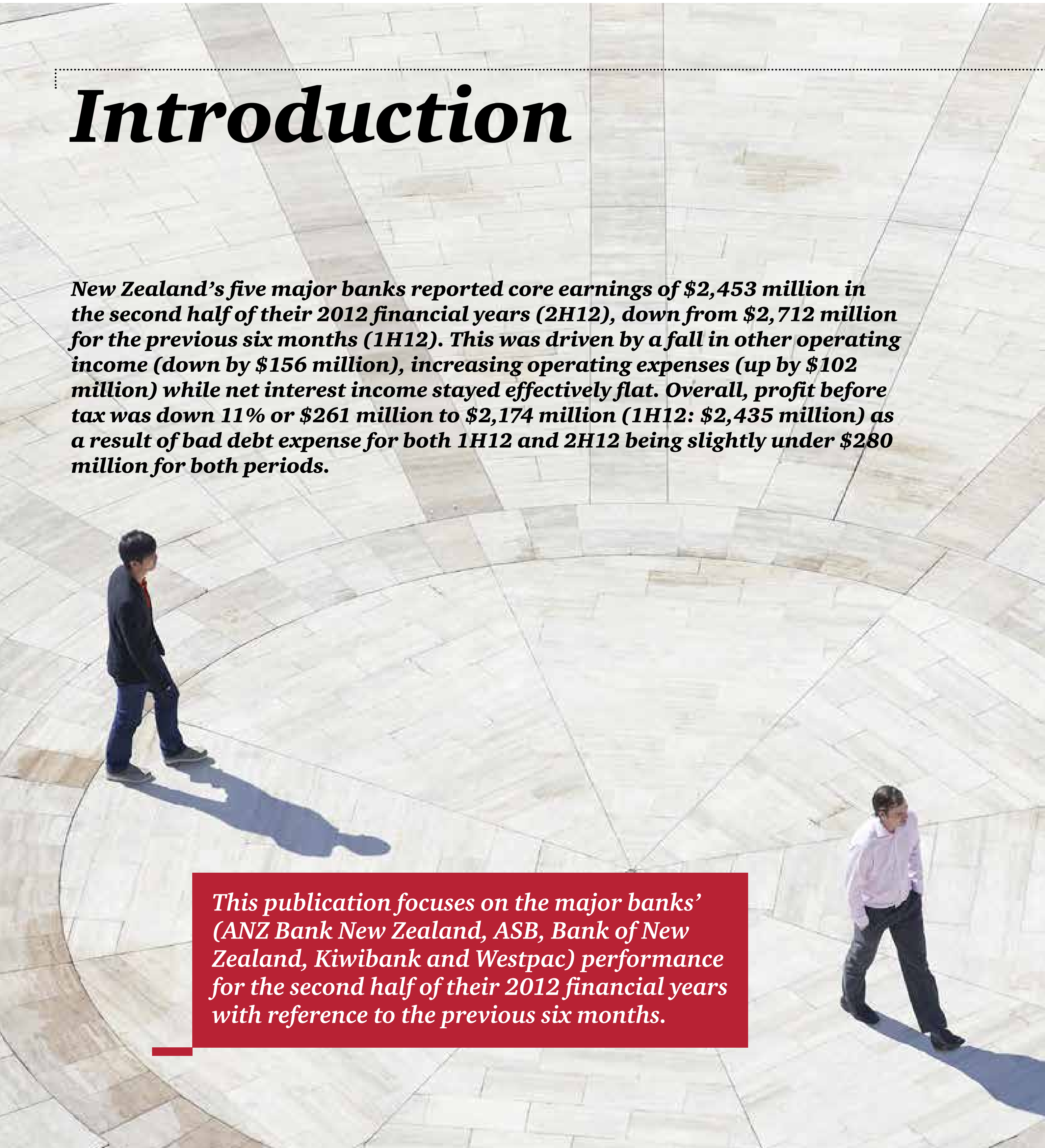
Major banks analysis February 2013

PwC analysis of the major banks' results for the second half of their 2012 financial years

pwc

Introduction

New Zealand's five major banks reported core earnings of $2,453 million in the second half of their 2012 financial years (2H12), down from $2,712 million for the previous six months (1H12). This was driven by a fall in other operating income (down by $156 million), increasing operating expenses (up by $102 million) while net interest income stayed effectively flat. Overall, profit before tax was down 11% or $261 million to $2,174 million (1H12: $2,435 million) as a result of bad debt expense for both 1H12 and 2H12 being slightly under $280 million for both periods.



This publication focuses on the major banks' (ANZ Bank New Zealand, ASB, Bank of New Zealand, Kiwibank and Westpac) performance for the second half of their 2012 financial years with reference to the previous six months.

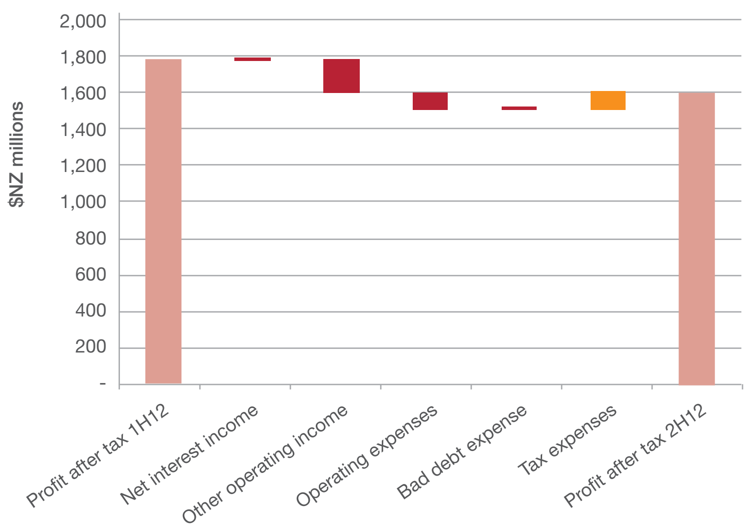
This fall in profit before tax was in spite of the major banks' lending books posting their biggest lending growth in 2H12 since 1H09, increasing 1.9% or $5.2 billion to $287.1 billion. So what went wrong?

Well, actually, not a lot. Net interest margin is down, but is still near a high since 2006; fee income remains stable; bad debts have stabilised, but operating expenses are continuing to increase and other operating income is noticeably down. The volatility of the financial markets continues to bring variability to the banks' other operating income through financial instruments held at fair value (up one period, down the next), but if these instruments are held to maturity this should only be a timing difference.

One observable change since the previous six months is the banks are locking in some fixed rate household lending. There has been a noticeable switch to fixed rate mortgages in the period with 22% of the banks' residential mortgage lending portfolio fixed for greater than a year at September 2012 compared with 15% at March 2012.

The strong performance by the major banks is supported on a year-on-year basis, with profit before tax showing a 6% or $253 million increase on their 2011 financial years (FY11) to $4,609 million in their 2012 financial years (FY12).

Figure 1: New Zealand major banks' change in profit after tax



The fact the banks are performing well is reflected by all five of the New Zealand majors (or where relevant, their Australian parent banks) appearing in the Global Finance Magazine's World's 50 Safest Banks list for 2012. The New Zealand banks continue to be seen positively by the financial markets when funding is required.

The Reserve Bank of New Zealand (Reserve Bank) seems committed to maintaining this position. As with the liquidity requirements that came in a few years ago, the Reserve Bank is one of the first regulators to implement the new Basel III capital ratio requirements. While their supervisory regime differs from the Australian Prudential Regulation Authority (in Australia) or the Financial Services Authority (in the United Kingdom), they remain one of the most proactive in terms of implementing new prudential requirements.

This regulation obviously comes at a cost. It is one of the drivers that has forced operating expenses up 16% since the first half of 2010, a cost which is ultimately borne by the banks' borrowers and shareholders through a higher net interest margin for borrowers and a reduction in dividend yields in the case of shareholders.

It is not the only thing that has driven up the net interest margin since the GFC though. The losses seen around the world caused the New Zealand banks to reassess their views on credit risk. As often happens after significant events, the views on credit risk swung towards more conservative lending practices. As discussed in previous editions of Banking Perspectives, we have seen the pendulum slowly swinging back again. The willingness of the banks to compete on interest rates for new lending reflects this.

Whether the pendulum has swung too far the other way remains to be seen, but the attitude seen over covenants at the top end of town is softening. One thing is for certain, the pendulum is still moving.

As well as reinforcing the security of the New Zealand banking sector, the other positive for the early implementation date for the Basel III capital ratios is that the New Zealand banks have resolved any potential concerns over their capital base before the overseas banks' rush for capital begins. Even with the downward revision of global growth expectations, many overseas banks are currently well short of capital requirements and there is a potential capital shortage on the horizon. The fact that the New Zealand banks and their Australian parents (where applicable) are well capitalised under the new rules and thus well ahead of the rest of the world, should mean less pain for the New Zealand major banks' shareholders further down the track, which will benefit the New Zealand economy as a whole.

Operating expenses are up

16%

since 1H10

The make-up of the major banks' funding continues to change, with the proportion of customer deposits continuing to strengthen. This continues to lower the risk held by New Zealand Inc as it reduces the reliance on offshore markets and signals the continuation of customers deleveraging. This continued change to the funding profile of the New Zealand banks has not impacted interest expense, which has remained relatively consistent with 1H12 ($5,743 million for 2H12 v $5,765 million for 1H12), due to the banks' cost of funding reducing over the period.

The other major source of long-term funding for the banks, other than the money markets and their customers, is their shareholders. Shareholders' equity has continued to grow from just under $19 billion in 2H07 to just over $25 billion at the end of 2H12. The main driver for this is the Basel accord and we have seen equity issuances of $450 million during FY12 to ensure the Basel III requirements will be met.

The returns from the New Zealand majors on this increased equity have been robust, albeit still below those produced by the Australian majors. As can be seen in figure 2 below, the New Zealand majors return on equity (ROE) has fallen post GFC, but only by circa 2% compared with a 5% drop in Australian ROEs and a massive 13% drop in global ROEs from 20% to 7% as a result of the GFC which also caused government bail-outs, tightening in prudential regulations and sovereign debt crises.

One of the dominating factors for the results of the New Zealand majors since 2007, both negative and positive, has been bad debt expense. Bad debt expense from households has now returned to the level seen in 2007, although the non household bad debt expense is still 5.5 times the level seen in 2007. While we do not expect any significant change to bad debt levels in the household sector, we do expect the non-household sector to continue its downward, if still volatile, trajectory, giving further upside to the banks' results.

Figure 2: Banks' shareholder value

	Pre GFC (2007)			Current (2012)		
	Global	**Aus**	**NZ**	**Global**	**Aus**	**NZ**
Leverage	31x	17x	15x	19x	15x	15x
Return on Equity	20%	20%	16%	7%	15%	14%

We have seen a massive

13%

drop in global ROEs as a result of the GFC

Five majors' combined performance

Annual results

On an annual basis, a 12% increase in statutory profit from $3,019 million in FY11 to $3,378 million in FY12 has been driven by the major banks increasing their interest margins in the first half of the year and reducing their bad debt expense.

The 24% improvement in bad debt expense from $734 million in FY11 to $556 million in FY12 was due to Christchurch earthquakes not having the expected negative impact on the quality of the banks' lending books, as well as general improvements in the economic environment in New Zealand.

Tax also decreased year-on-year through the reduction of the corporate tax rate.

Offsetting these positive moves was a 7% decrease in other operating income to $2,264 million in FY12 as market movements forced losses to be recognised on financial instruments held at fair value, and a 3% increase in operating expenses to $4,430 million in FY12 as one-off expenses combined with continued costs associated with regulatory pressure.

Bad debt expense has improved

24%

year on year

The fall in statutory profit was caused by market volatility resulting in financial instruments held at fair value to be marked down.

Semi-annual results

Comparing 2H12 with 1H12 we see a 9% fall in statutory profit from $1,766 million in 1H12 to $1,612 million in 2H12.

Net interest income was consistent between the two halves, slightly moving from $3,666 million in 1H12 to $3,665 in 2H12 with growth in the lending books being offset by a fall in the average net interest margin of the New Zealand majors.

The fall in statutory profits was caused by the market volatility resulting in financial instruments held at fair value being marked down, reducing other operating income by 13% from $1,210 million in 1H12 to $1,054 million in 2H12, and by continued upward pressure pushing operating expenses up 5% half-on-half to $2,266 million in 2H12.

Partially offsetting this fall was the reduction in tax expenses which fell due to the lower profit before tax as well as a lower effective tax rate in 2H12. The effective tax rate dropped from 27.1% in 1H12 to 25.5% in 2H12.

Figure 3: New Zealand major banks' combined performance ($NZ millions)

	2H12	1H12	2H12 V 1H12	FY12	FY11	FY12 v FY11
Interest income	9,408	9,431	0%	18,839	19,345	-3%
Interest expense	(5,743)	(5,765)	0%	(11,508)	(12,390)	7%
Net interest income	3,665	3,666	0%	7,331	6,955	5%
Other operating income	1,054	1,210	-13%	2,264	2,422	-7%
Operating expenses	(2,266)	(2,164)	-5%	(4,430)	(4,287)	-3%
Core earnings	2,453	2,712	-10%	5,165	5,090	1%
Bad debt expense	(279)	(277)	-1%	(556)	(734)	24%
Profit before tax	2,174	2,435	-11%	4,609	4,356	6%
Tax expenses	(552)	(660)	16%	(1,212)	(1,315)	8%
Outside equity interest	(10)	(9)	-11%	(19)	(22)	14%
Statutory profits	1,612	1,766	-9%	3,378	3,019	12%

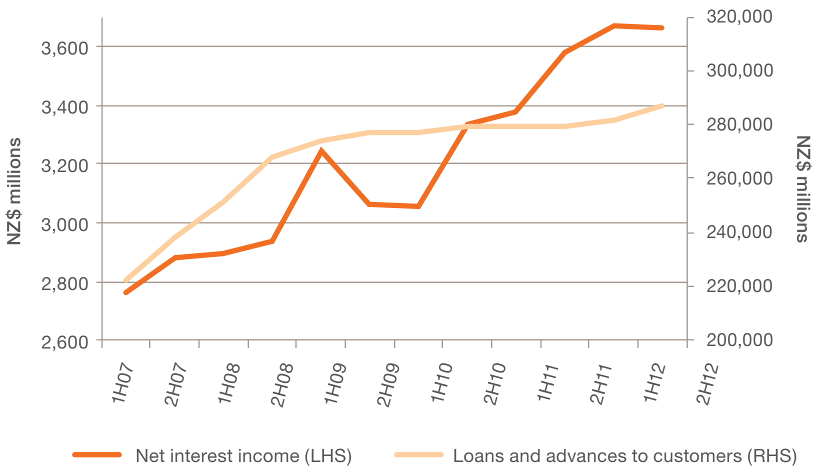
Net interest income

Net interest income for the five majors is broadly consistent between 1H12 and 2H12, down only $1 million to $3,665 million for 2H12.

Interest income has dropped by $23 million to $9,408 million for 2H12 and the interest expense has dropped by $22 million to $5,743 million for 2H12.

However these figures do not tell the story of what has been a testing but generally positive six months for the five majors. As can be seen in figure 4, the loan books of the major banks have experienced their first noticeable increase since the GFC but have experienced stabilisation in their net interest income, which translated into a contraction in their net interest margin.

Figure 4: Net interest income of NZ major banks in relation to loans and advances to customers



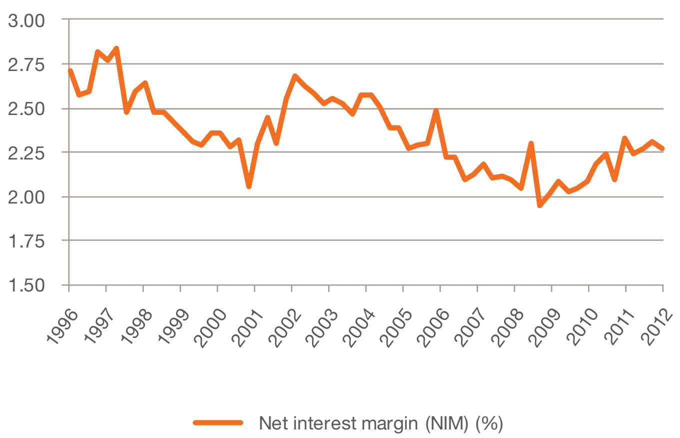
Margin

With interest rates for lending dropping and interest rates offered on deposits flat, we have witnessed a tightening of net interest margins (NIMs) in the current six months back to 2.24% from the semi-annual high (since 2006) seen during 1H12 of 2.27%.

Figure 5 shows the historical NIMs for the New Zealand banking sector based on Reserve Bank data. In this we can see the impact of the pre-GFC competition on the banks NIMs with a reduction from 2.68% in the quarter ended September 2002 to 1.95% in the quarter ended March 2009. The average NIM has been increasing since this time but has recently (since the quarter ended June 2011) stayed within a narrow range.

This narrow range has been driven by strong competition in a low growth market offset by a greater awareness of risk. We expect the banks to continue to navigate within this range, even with the recent growth seen in the banks' lending books. We feel it is important that it does (rather than decreasing as it did during the previous credit growth phase) if we wish New Zealand to retain its global reputation as having a financially sound banking environment.

Figure 5: New Zealand registered banks' net interest margin



Source: Reserve Bank of New Zealand

In contrast, Australian NIMs increased through 2008 and 2009, held steady through 2010 and 2011 but have reduced significantly during 2012, falling from 2.27% during 2H11 to 2.14% during 2H12. This recent fall has been precipitated by a deposit war amongst the Australian banks as they seek to prepare themselves for the liquidity regulations being implemented, similar to what we experienced in New Zealand in 2010.

New Zealand NIMs now sit above those of the Australian majors. The expectation of PwC Australia is that further degradation of the Australian NIMs will occur over the coming periods which may lead to the widening of this gap.

Lending

Much of the talk of the last six to nine months has been on lending interest rates. Households have been focusing on them due to press reports suggesting customers should renegotiate borrowing rates, even in the middle of a fixed rate period.

The banks have generally played ball, especially with the more secure lending, paying out break fees and extending credit at rates significantly below carded rates.

Extending this scrap for market share was the announcement in September 2012 that the National Bank brand was being dropped. Widely expected, this resulted in bank campaigns being run, ranging from advertising to interest rate specials.

This pressure on lending rates was not isolated to the household market. As a result of the confidence from having stronger balance sheets from recent deleveraging coupled with the media activity in the household market, many corporates have also taken the opportunity to renegotiate their borrowings packages. At the top end of town this has even seen the relaxing of covenants given the general improvement in the financial conditions of many corporate borrowers.

This is the typical activity we would expect in a flat market with the banks actively competing for what share of the market is available. This manifested in gross lending increasing by $5.2 billion or 1.9% in 2H12 to $287.1 billion, the highest six month increase since the first half of 2009.

As can be seen in figure 6, this growth has come from the corporate sector growing by 2.2% or $2.3 billion in 2H12 to $106.5 billion supporting the household sector's continued growth (growth of 1.7% or $2.9 billion in 2H12 taking gross lending to $180.6 billion). This is the first time the corporate sector has recorded two consecutive periods of growth since 2009.

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The growth witnessed in the corporate sector has been driven by the agricultural sector (4.0% increase) and the property sector (3.4% increase). The agricultural sector is particularly encouraging as this is the backbone of the New Zealand economy and generally has been under significant pressure from the banks to reduce leverage. This turnaround, with lending increasing from the $47 billion mark (seen since 2010) to $49 billion, is a good indicator of improved confidence in the economy.

While the household sector has continued to grow, we have seen interesting changes in this lending portfolio. There has been a move to fixed rates during the period, as can be seen in figure 7, with only 58% of the portfolio floating at September 2012 compared with 63% at March 2012. Furthermore, 22% of the portfolio is fixed for greater than one year at September 2012 compared to 15% at March 2012.

This also represents a positive sign for the economy with households beginning to hedge against increases in residential mortgage interest rates, typically a sign of a growing economy. We will have to see whether this heralds an actual improvement in the economy or is more of a false dawn, with key indicators such as GDP from the first half of 2012 being revised downward.

Also, this refixing represents the beginning of households reconsidering how to restructure their borrowings. We expect the competition in interest rates to continue as banks attempt to lock-in market share over the coming months.

Figure 6: Changes in NZ major banks' lending portfolios

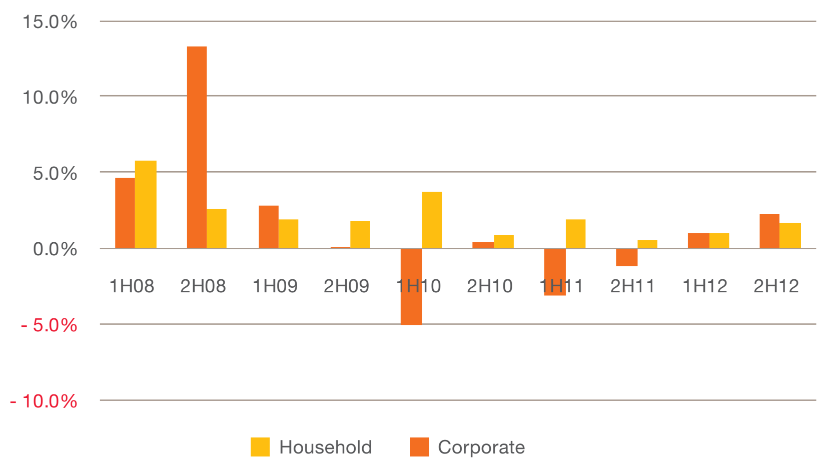
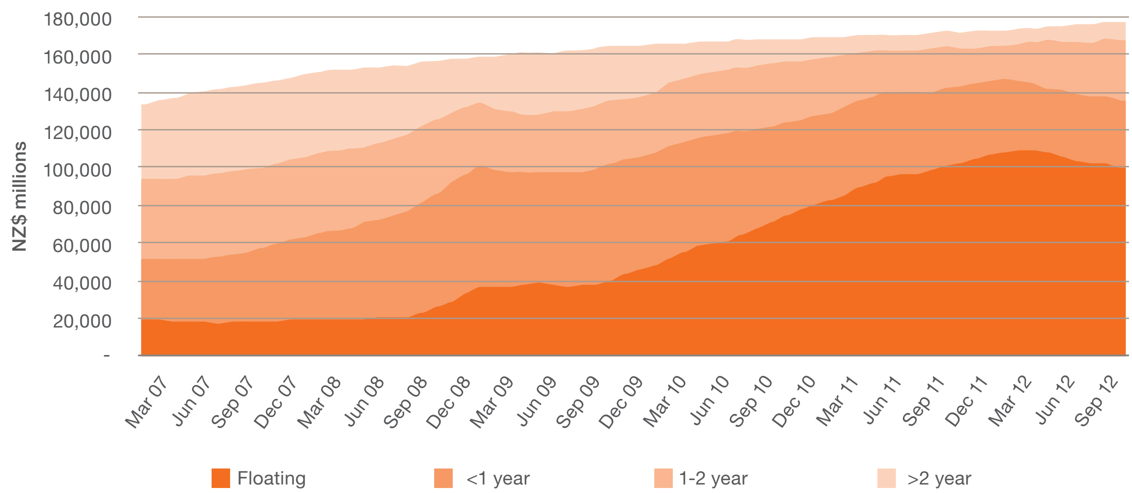


Figure 7: Maturities of residential lending performed by New Zealand registered banks



Source: Reserve Bank of New Zealand

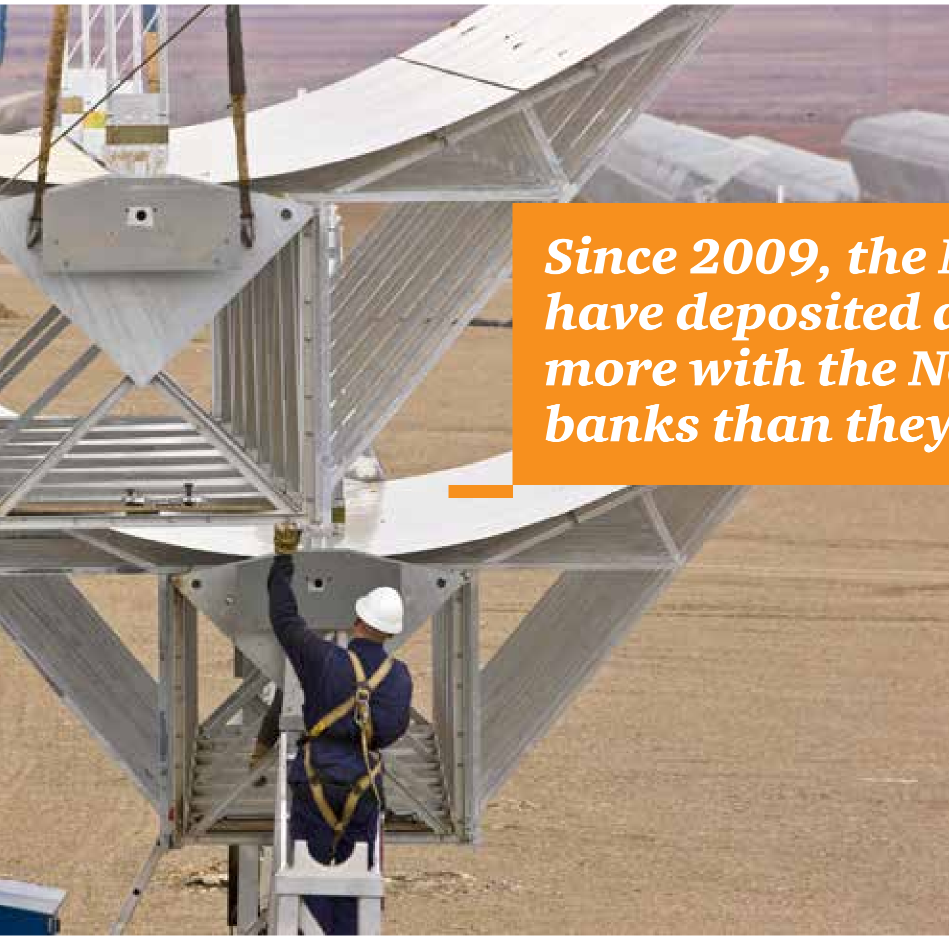
Funding

In order to meet the increased lending seen in the period, the New Zealand majors' funding has grown from $306.3 billion at the end of 1H12 to $307.8 billion at the end of 2H12.

This is smaller than the $5.2 billion increase in lending as the improvement in overseas conditions has allowed the banks to use some of their liquid assets held in case of a dislocation in the wholesale funding markets in the Northern Hemisphere.

The major banks' exposure to these overseas concerns is still significant but reducing. Since 2009, the New Zealand public have deposited more with the New Zealand major banks than they have borrowed. If this continues, even with the restarting of credit growth, this will reduce the risk of the New Zealand banks and of New Zealand Inc to overseas events. Albeit volatile, figure 8 shows that the New Zealand public have deposited almost $29 billion more than they have borrowed since 2009.

This behaviour has also changed the funding structure of the five majors (see figure 9). The percentage of the five majors' funding which is obtained from deposits from customers has increased from 52% or $155 billion in 2009 to 64% or $196 billion at the end of 2H12, including a $7.8 billion increase in the current period. This has allowed the five majors to reduce their reliance on wholesale funding, reducing it from 48% of total funding, or $145 billion to 36% or $112 billion over the same timeframe.



Since 2009, the New Zealand public have deposited almost $29 billion more with the New Zealand major banks than they have borrowed.

This change in funding composition has been driven in part by the liquidity ratios brought in by the Reserve Bank in 2010. From 1 January 2013 the core funding ratio, which measures long-term funding against loans and advances, has increased to 75%. While this increases the regulatory minimum, and hence the safety of the banking system, we understand that the banks have been funding in excess of this level due to concerns abroad.

However these overseas concerns reduced during the period, especially with the financial restructuring of Greece being agreed, which has lowered the banks' incremental funding costs. The financial issues of the Northern Hemisphere are far from over though, with concerns remaining for Spain, Italy and Greece in the Eurozone in particular and the United States continuing to walk along the edge of the fiscal cliff.

Figure 8 : New Zealand major banks' net cash flows with customers

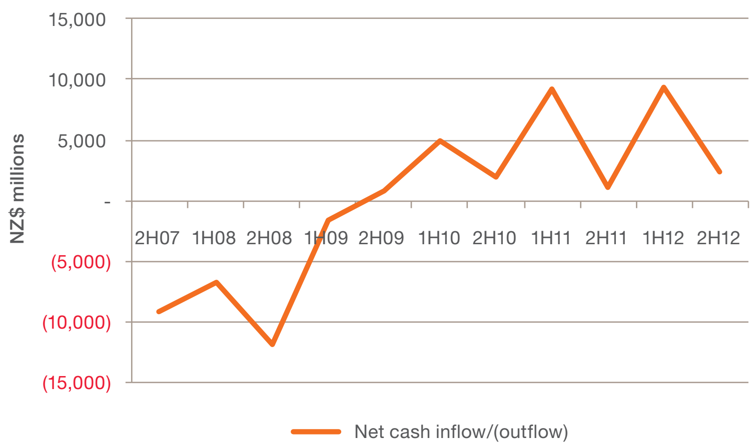
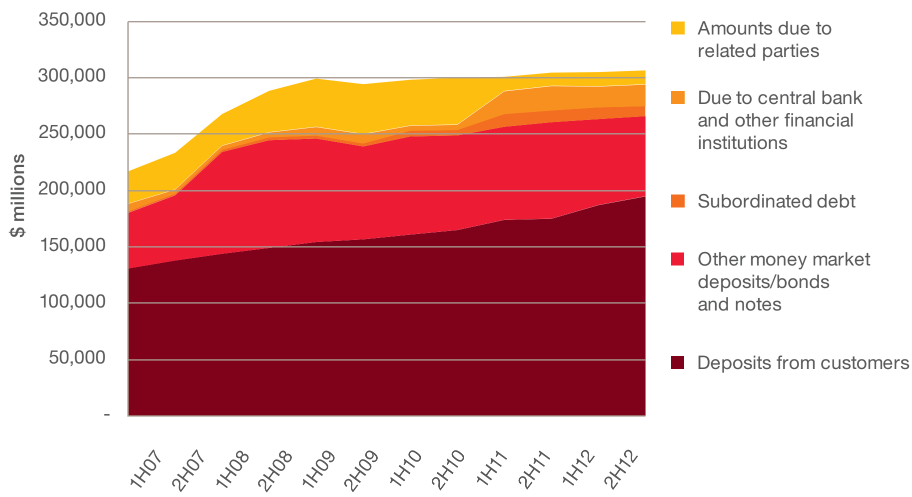


Figure 9: New Zealand major banks' funding books



The financial issues of the Northern Hemisphere are far from over in the Eurozone in particular and the United States continuing to walk along the edge of the fiscal cliff.

Other operating income

Other operating income has fallen 13% or $156 million in 2H12 to $1,054 million, furthering the 7% fall seen in 1H12.

Both of these falls have been driven by the repricing of financial instruments held at fair value with a small increase in fee income being wiped out by significant valuation losses arising from marking these financial instruments to market in the current period.

Due to reduced half year disclosures we can no longer see a breakdown of this movement on a six monthly basis but on an annual basis we can see:

- Fee income virtually flat, down $6 million from FY11 to $2,048 million in FY12.
- Trading income down 0.9% or $4 million to $460 million in FY12.
- Losses on financial instruments held at fair value up $216 million from FY11 to $396 million in FY12.
- Other income increasing from $2 million in FY11 to $69 million in FY12.

The volatility in the losses on financial instruments held at fair value is hard to predict going forward, but if the banks continue to compete on interest rates rather than fees then the fee income for the banks should continue to remain solid around the $2 billion mark, as it has since FY08.

If the banks continue to compete on interest rates rather than fees then the fee income for the banks should continue to remain solid.

Expenses

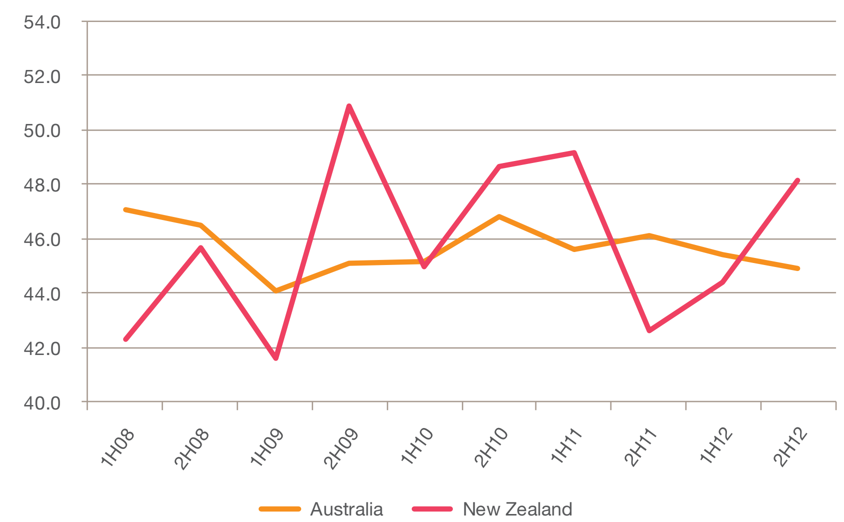
Operating expenses have increased a further 5% from 1H12, standing at $2,266 million for the current period compared to $2,164 million for 1H12. Given the lack of growth in the balance sheets of the major New Zealand banks, costs continue to be an area of focus.

While costs remain a focus for the banks, IT upgrades, regulation and significant internal changes (such as the decommissioning of the National Bank brand) continue to place upward pressure on the costs that the major banks face.

These pressures combined with the reduced other operating income in the current period have driven the cost-to-income ratio for the New Zealand majors back up to 48.1%, compared to a reduction in the Australian majors' to 44.9%. Australia's ratio is more stable than New Zealand's reflecting their larger proportional size and diversity and the greater impact on our results of movements in the financial markets.

The tax expenses have decreased in the current period, due to both a reduction in the profit before tax but also in the effective tax rate from 27.1% in 1H12 to 25.4% in 2H12.

Figure 10: Cost to income ratios of the New Zealand and Australian major banks



With the Reserve Bank responding to the global regulatory environment, banks have faced additional regulatory-driven changes. What sets the current environment apart is the sheer volume of significant new regulation being introduced. Indeed, the regulations require banks to address the way they do business and so it commands a significant part of their annual budgets.

Asset quality

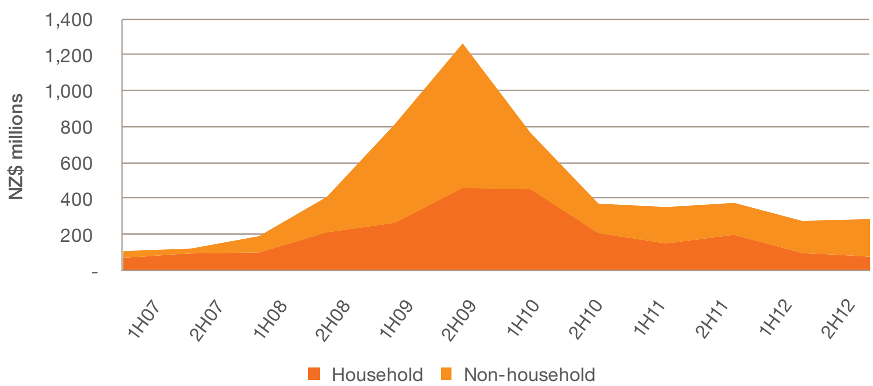
The bad debt expense for the New Zealand majors has levelled out, at $279 million for 2H12 compared with $277 million for 1H12. As illustrated in figure 11, this has come from a $25 million reduction in the household sector to $72 million in 2H12 offset by a $27 million increase in the non-household sector to $206 million.

With historically low interest rates, we do not expect to see any increases in the household bad debt expense due to borrowers not being able to repay their loans.

With the New Zealand property market flourishing again, particularly in Auckland, and the Christchurch rebuild beginning there could be further improvements in the bad debt expense due to the increasing value of the underlying security.

With the majority of the non-household sector also largely reliant on property for security (either farming or property companies), this buoyant property market will also aid the non-household sector. However there still remains significant uncertainty, with the possibility for significant 'lumpy' losses to be incurred by the banks.

Figure 11: New Zealand major banks' composition of bad debt expense



The predicted long, dry summer won't help the dairy sector with the possibility of a drought on the cards. The question is will global demand improve prices enough to offset the impact of a dry summer? The latest forecast is still below the 2012 pay-out even without a possible dry summer. The banks push for deleveraging over the last few years will no doubt alleviate some concerns in this area.

The major banks' provisioning levels have continued to drop in the current period in both absolute terms and in comparison to the underlying lending books. Household provisions dropped from $966 million at the end of 1H12 to $857 million at the end of 2H12, a drop from 54bps to 47bps when compared to the gross household lending. Non-household provisioning still remained significantly higher than household provisioning but dropped from $1,575 million to $1,476 million during the period, or from 151bps to 139bps when compared to the gross non-household lending.

This buoyancy can be seen in the other figures reported by the major banks in 2H12 with the 90 day past due assets dropping from 36bps at the end of 1H12 when compared to the gross lending to 32bps at the end of 2H12, levelling slightly but still continuing the fall from the high of 51bps seen at the end of 1H09. The impaired assets figure continues to reduce, falling to 103bps of the gross lending books at the end of the period, as more confidence is obtained and problem loans continue to be worked through and are rehabilitated or written off. We expect to see continued improvement in these figures, although we expect the impaired assets to stabilise out well above 10bps of the gross lending book, the level seen at the end of 1H07.

The early indicators for bad debt expense show positive signs of improvement.

Figure 12: New Zealand major banks' asset quality and bad debt expense

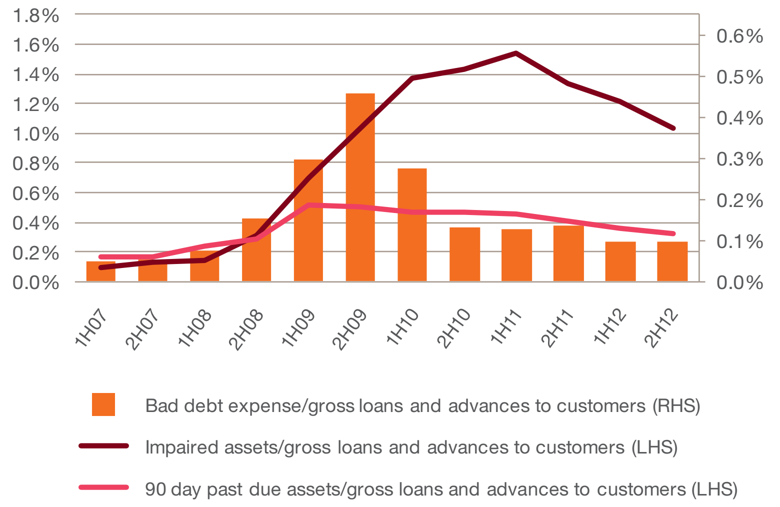
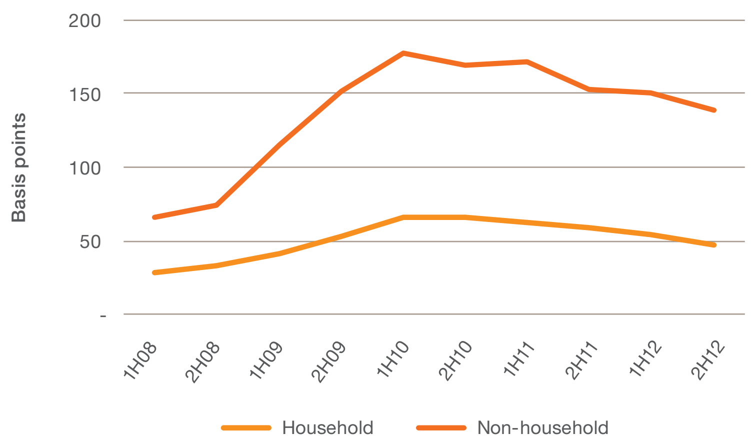


Figure 13: New Zealand major banks' basis point loan loss provisions



The major banks' provisioning levels have continued to drop in the current period.

Capital

The major banks have continued to prepare for Basel III in the current period with subordinated debt unable to qualify in the long run as tier 2 capital under the new rules being redeemed. In its place, the New Zealand banks continue to accumulate more tier 1 capital by retaining more earnings than are being paid in dividends and from further issuances of ordinary share capital.

In the current period the major banks shareholders' equity has increased from $23.9 billion at the end of 1H12 to $25.2 billion at the end of 2H12. This has continued the trend seen in recent years.

Capital adequacy

As at 2H12 the average tier 1 capital ratio was 11.2%, up from 10.8% as at 1H12, while the total capital ratio was unchanged at 12.7%.

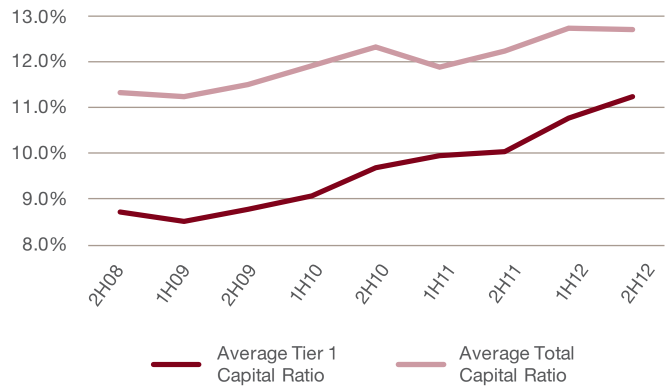
The convergence of tier 1 capital to total capital illustrates the greater importance placed on pure shareholders' funds (i.e. share capital, retained earnings) rather than other innovative capital instruments.

From 1 January 2013, the banks need to comply with the new Basel III capital ratios as defined by the Reserve Bank. As with the liquidity requirements, the Reserve Bank has implemented these ratios before the majority of the rest of the world, helping reinforce New Zealand's reputation of having a safe banking environment. However this does continue to place regulatory pressure on the New Zealand banks.

There is no change to the treatment of the regulatory overlays in the new regulations. This means that the New Zealand banks continue to have their regulatory overlays included as part of their capital ratios (decreasing the ratios), as opposed to globally where overlays are not included in their capital ratios.

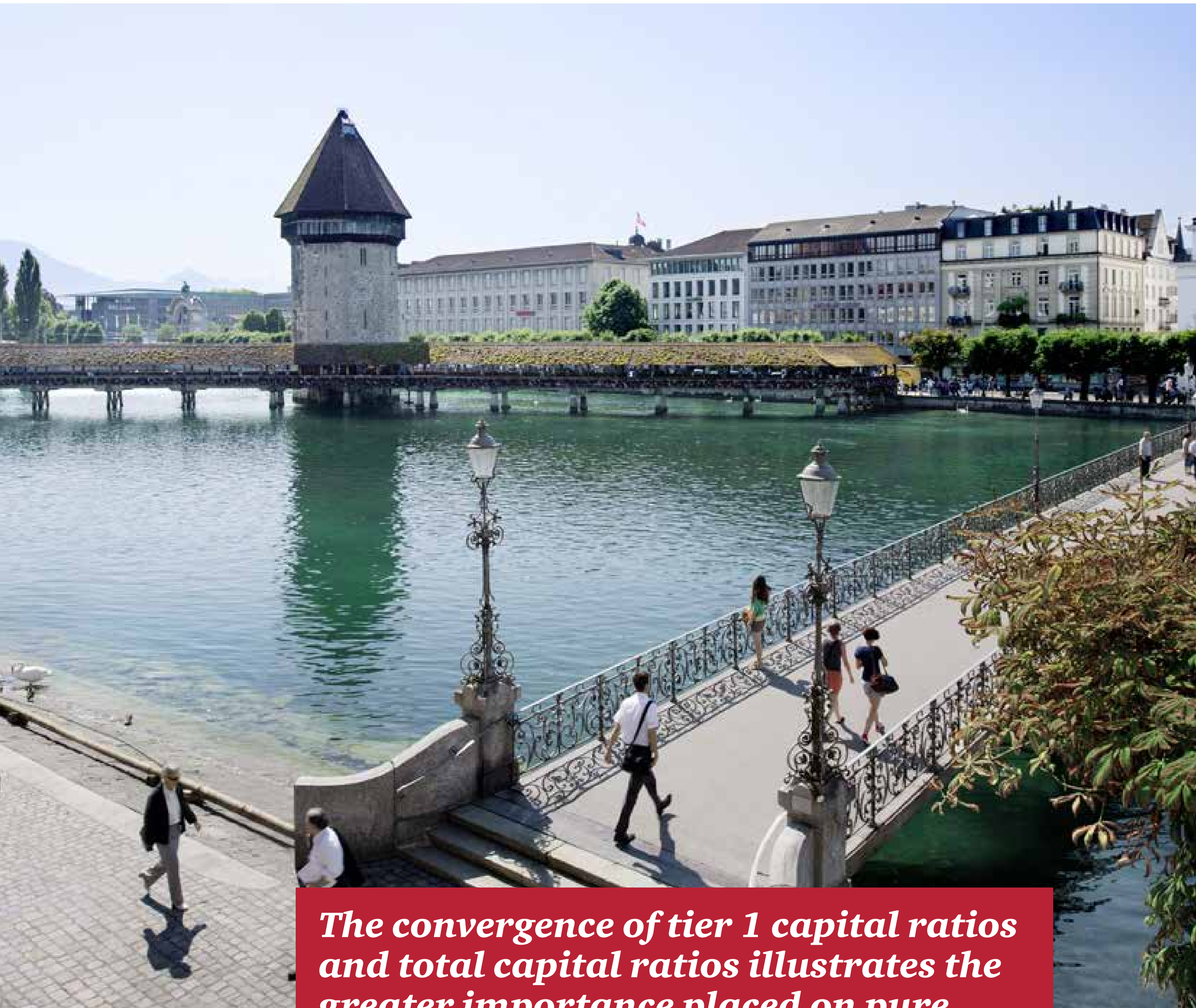
This means that New Zealand's banks' capital positions will continue to be conservatively reported when compared to their international peers. This does not seem to be causing problems in the global debt markets at the moment as New Zealand is in favour, and the New Zealand banks are proactive in recognising the different approaches and presenting their ratios as they would appear in different jurisdictions.

Figure 14: Average capital ratios of the New Zealand major banks



However, with many overseas banks currently well short of the Basel III capital requirements, especially in Europe, New Zealand may have beaten the rush by implementing this regulatory change early. Globally it is anticipated that there will be a capital shortage and many investors' continued reluctance to have an increased weighting in banks will not help solve this.

This shortage is likely to lead to increases in the cost of capital. With New Zealand already complying with the requirements and the Australian parents (where applicable) well capitalised, the New Zealand majors should be sheltered from the majority of these increases.



The convergence of tier 1 capital ratios and total capital ratios illustrates the greater importance placed on pure shareholders' funds rather than other innovative capital instruments.

Return on equity

With reduced profit and increased equity levels to comply with Basel III, the New Zealand majors' average return on equity has fallen from 15.3% in 1H12 to 13.0% in 2H12. This means that it has averaged around 14% for both of the last two years, down two percentage points from the pre-GFC level of 16%. When compared internationally, this reduction is actually a good result for the New Zealand major banks albeit with them coming from a low base.

While New Zealand's return on equity is still behind Australia's, the New Zealand majors have only dropped two percentage points since the GFC as opposed to Australia which has dropped five percentage points. While the owners of the New Zealand majors will be looking for improved return on equity, this may be an unlikely scenario in the current environment of regulatory change and the competition that comes with limited growth in the top line.

Figure 15: Banks' shareholder value

	Pre GFC (2007)			Current (2012)		
	Global	Aus	NZ	Global	Aus	NZ
Leverage	31x	17x	15x	19x	15x	15x
Return on Equity	20%	20%	16%	7%	15%	14%

While the owners of the New Zealand majors will be looking for improved return on equity, this may be an unlikely scenario.

Key Banking Statistics – Second Half Year 2012 $NZ millions

	BNZ			WBC *(i)*			CBA *(ii)*			ANZ *(iii)*			Kiwibank		
	6 months	6 months	6 months	**6 months**	6 months	6 months	**6 months**	6 months	6 months	**6 months**	6 months	6 months	**6 months**	6 months	6 months
	2H12	1H12	2H11	**2H12**	1H12	2H11	**2H12**	1H12	2H11	**2H12**	1H12	2H11	**2H12**	1H12	2H11
Income statement															
Interest income	**1,905**	1,885	1,881	**1,975**	1,990	2,118	**1,844**	1,899	1,911	**3,292**	3,276	3,304	**392**	381	372
Interest expense	**(1,149)**	(1,138)	(1,169)	**(1,199)**	(1,241)	(1,278)	**(1,193)**	(1,213)	(1,302)	**(1,944)**	(1,915)	(1,989)	**(258)**	(258)	(270)
Net interest income	**756**	747	712	**776**	749	840	**651**	686	609	**1,348**	1,361	1,315	**134**	123	102
Other operating income	**(16)**	157	337	**290**	292	262	**237**	238	236	**462**	442	434	**81**	81	81
Operating expenses	**(408)**	(386)	(393)	**(445)**	(427)	(422)	**(393)**	(355)	(383)	**(880)**	(863)	(778)	**(140)**	(133)	(124)
Core earnings	**332**	518	656	**621**	614	680	**495**	569	462	**930**	940	971	**75**	71	59
Impairment losses on credit exposures	**(31)**	(30)	(57)	**(90)**	(94)	(107)	**(42)**	(32)	(62)	**(99)**	(103)	(105)	**(17)**	(18)	(48)
Total operating profit before income tax expense	**301**	488	599	**531**	520	573	**453**	537	400	**831**	837	866	**58**	53	11
Income tax expense	**(73)**	(136)	(183)	**(150)**	(143)	(187)	**(130)**	(144)	(122)	**(182)**	(222)	(259)	**(17)**	(15)	(5)
Net profit to minorities	**0**	0	0	**(2)**	(1)	(2)	**(8)**	(8)	(9)	**0**	0	0	**0**	0	0
Net profit attributable to shareholders	**228**	352	416	**379**	376	384	**315**	385	269	**649**	615	607	**41**	38	6
Balance sheet															
Net loans and advances to customers	**58,919**	57,834	56,661	**59,892**	58,689	58,114	**57,109**	56,680	56,419	**96,094**	93,817	93,613	**12,445**	12,068	11,495
Total assets	**73,111**	71,716	74,085	**77,854**	75,661	78,293	**69,515**	71,337	68,674	**130,868**	124,738	129,083	**14,745**	14,386	13,875
Deposits from customers	**37,090**	33,883	31,354	**41,967**	39,424	38,019	**39,391**	39,056	34,178	**66,051**	64,179	61,994	**11,565**	11,716	10,586
Total shareholders equity	**5,277**	4,673	4,349	**5,515**	5,178	4,761	**4,497**	4,309	4,182	**9,177**	9,002	8,465	**747**	699	608
Asset quality & provisioning															
Gross loans and advances to customers	**59,376**	58,296	57,099	**60,499**	59,370	58,779	**57,347**	56,907	56,675	**97,357**	95,164	94,927	**12,536**	12,160	11,582
Gross other individually impaired assets	**459**	529	659	**868**	899	919	**301**	264	269	**1,242**	1,626	1,772	**84**	100	106
Gross impaired assets as a % of loans and advances	**0.77%**	0.91%	1.15%	**1.43%**	1.51%	1.56%	**0.52%**	0.46%	0.47%	**1.28%**	1.71%	1.87%	**0.67%**	0.82%	0.92%
Gross other assets under administration	**20**	14	10	**0**	0	0	**53**	27	38	**0**	9	6	**0**	0	0
90 day past due assets	**250**	214	202	**184**	226	256	**219**	257	336	**226**	295	307	**36**	25	33
Allowance for impairment losses on individual financal assets	**132**	138	170	**277**	283	266	**101**	77	84	**461**	511	511	**41**	48	37
Individual assessed provision as a % of impaired assets	**28.76%**	26.09%	25.80%	**31.91%**	31.48%	28.94%	**33.55%**	29.17%	31.23%	**37.12%**	31.43%	28.84%	**48.81%**	48.00%	34.91%
Allowance for impairment losses on groups of financial assets	**172**	198	207	**366**	438	437	**149**	165	185	**620**	639	672	**50**	44	50
Bad debt charge as a % of loans and advances	**0.05%**	0.05%	0.10%	**0.15%**	0.16%	0.18%	**0.07%**	0.06%	0.11%	**0.10%**	0.11%	0.11%	**0.14%**	0.15%	0.41%
Other key data															
Other operating income (% of total income)	**-2.2%**	17.4%	32.1%	**27.2%**	28.0%	23.8%	**26.7%**	25.8%	27.9%	**25.5%**	24.5%	24.8%	**37.7%**	39.7%	44.3%
Expense/income ratio *(iv)*	**55.1%**	42.7%	37.5%	**41.7%**	41.0%	38.3%	**44.3%**	38.4%	45.3%	**48.6%**	47.9%	44.5%	**65.1%**	65.2%	67.8%
Tier 1 capital ratio *(v)*	**11.3%**	9.6%	9.0%	**12.0%**	11.7%	10.5%	**11.7%**	11.2%	11.2%	**10.8%**	11.3%	10.5%	**10.4%**	10.1%	9.0%
Total capital ratio *(v)*	**13.3%**	12.4%	11.8%	**14.1%**	13.7%	13.0%	**12.6%**	12.9%	12.8%	**12.2%**	12.6%	13.0%	**11.3%**	12.1%	10.5%

(i) Represents the aggregated results of the New Zealand banking operations of Westpac Banking Corporation including Westpac New Zealand.

(ii) Represents the aggregated results of the New Zealand banking operations of Commonwealth Bank of Australia including ASB Bank.

(iii) Represents the aggregated results of the New Zealand banking operations of Australia and New Zealand Banking Group including ANZ Bank New Zealand.

(iv) Recalculated from the banks' disclosure statements based on net interest income, other operating income and operating expenses.

(v) Taken from the relevant locally incorporated bank's disclosure statements, in relation to Basel II.

Notes:

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