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Financial Institutions Performance Survey
Review of 2012

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UNIVERSITY OF NEW ZEALAND

A solid base camp – now onwards and upwards?

$125 incl. gst

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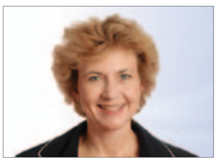

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A KPMG view from the Editor

John Kensington | Head of Financial Services | KPMG

Having been the editor of this Survey for the last three years, I have taken some time to reflect on the critical attitude some New Zealanders have to their banks.

I am not sure whether this reflects the classic Kiwi tall-poppy syndrome, or is a healthy sceptical view of anything controlled by our Australian neighbours. Or perhaps, more seriously and more concerningly, it reflects a general lack of financial literacy.

As a country we have tended to borrow beyond our means in order to fund the 'three Bs' lifestyle (Boat, BMW, and Bach). At the end of the Global Financial Crisis (GFC) we found ourselves with significant foreign borrowings and an economy that, while growing, was growing much more slowly than many of our trading partners. It was also an economy that was experiencing a 'warehousing' effect, with more and more jobs moving north to Auckland – before moving west to Australia.

The GFC caused all sorts of turmoil among world markets and economies. New Zealand never rose to the dizzy heights of Europe or the US. Maybe this was partly good luck. Or, perhaps, our banks hadn't had time to get into the collateralised debt obligation or derivatives markets that caused so much disruption to the banking systems of the US and Europe. Or maybe they were just more cautious. Whatever the reason, New Zealand banks have credit ratings amongst the highest in the world, borrowing rates that are at an all time low – and customers have access to banks that are keen to lend them money. "Our" financial crisis (the finance company episode), while heart-breaking, soul-destroying and a massive destruction of value for those affected by it, was fortunately only about 5-6% of our financial markets sector.

Whether through good luck, or good management, or a combination of both, the result is that our New Zealand banks have credit ratings as high as any in the world. This enables them to borrow to fund their customers' needs (which would appear still to consist of purchasing residential property), and to do so at rates that are amongst the best seen in New Zealand for twenty years – whilst still supplying a full range of services to their customers. When you also consider the 7.0 billion dollars worth of capital that has been invested into these businesses during and since the GFC, and the fact that they employ nearly 26,000 people, pay 1.3 billion-dollars of tax and spend approximately 2.0 billion dollars in the economy on rent, power, rates etc – is it not time to be a little less grudging of the profits that they make? Banking, like insurance, is a complex business; it has significant risks and as a result should be subject to reasonable returns. It is too easy to quote a bank's annual profit result or indeed the sector's quarterly result in the billions and say it is too much. It is easy to point out the number is large. But what is seldom recognised is that, taken as a percentage return on assets, that number is incredibly low. And even when considered as a return on equity it is no more than appropriate.

An interesting exercise would be to take a handful of the New Zealand Stock Exchange (NZX) listed entities and compare their profit figures as a percentage of assets or a return on equity. You would find that, given the additional risks and complexities a bank faces, its returns are not inappropriate. It is also worth remembering that around 20% of the shareholders in the Australian banks who make these profits are New Zealanders – and therefore 20% of the dividend that is paid by the New Zealand subsidiary to the Australian parent is ultimately returned here.

Perhaps another way to look at this would be; "How would our banking industry and economy look generally if our banks had made significant losses like many of their foreign counterparts?" The bailing out of South Canterbury Finance, a relative minnow when compared to any of the banks, put a significant dent in the Government's coffers. If the Government had been required to bail out one or more of the New Zealand banks the impact would have been catastrophic.

Consider if the banking sector, instead of making profits of around $2.0 - 3.5 billion over each of the last three years, had actually made losses. Credit ratings would be at much lower levels and the banks would have to borrow at much higher rates, if they could actually raise funds at all. New Zealanders currently enjoying mortgage rates of 4.9-5.2% would conceivably be borrowing at a rate of around 10%. Many people simply could not afford that level of additional interest and repayment. In addition to remain competitive jobs would have been cut and spending in the economy and tax payments would have reduced accordingly.

Our banks have credit ratings amongst the strongest in the world. Perhaps it is time to look at these global market leaders and treat them more as we would our winning sports teams or Olympic medallists. Rather than criticise them it might be more appropriate to reflect thankfully on what our strong banks allow us, as consumers, to do.

The Survey

Welcome to KPMG's 26th edition of the Financial Institutions Performance Survey

Our review of 2012 provides analysis on the performance of New Zealand's registered banks, major finance companies and savings institutions with balance dates between 30 September 2011 and 30 September 2012.

The range of balance dates that is captured in this review has changed from prior years, from a 31 December cut off to a 30 September cut off. The rationale for this is to make the information and analysis contained within the Survey more timely, particularly as the major banks have balance dates in June and September.

As a result registered banks with 31 December balance dates have their 31 December 2011 results included in this year's Survey once again as their most recent. The banks affected by this are Citibank, Deutsche Bank, The Hongkong and Shanghai Banking Corporation, JP Morgan Chase Bank, Kookmin Bank and Rabobank.

Two new registered banks are included in this year's Survey. We welcome The Bank of India (New Zealand) Limited for the first time as it has completed its first full year as a registered bank since obtaining its banking license on 31 March 2011. The Co-operative Bank has made the move from the savings institutions sector of the Survey to the registered banks sector, having obtained its banking license on 26 October 2011 and completing a full financial year as a registered bank on the 31 March 2012.

On 17 December 2012 the Reserve Bank of New Zealand (RBNZ) granted Heartland Building Society, a key subsidiary of Heartland New Zealand Limited (Heartland), its banking license and it was registered as a bank in New Zealand. However, as Heartland's most recent balance date was 30 June 2012, and it was a building society at that date, it has been included in the savings institutions sector analysis for this Survey. In the future it will be included in the registered banks section of our Survey.

For the non-banking sector participants, the threshold for inclusion in the Survey has remained at total assets of $75 million.

There has been very little movement in the number of participants in the non-banking sector. The Co-operative Bank has moved to the Banking section of the Survey, bringing down the number of savings institutions participants to 8. PGG Wrightson Finance Limited (PGGWF) was acquired by Heartland during the year and is now accounted for as part of Heartland in the savings institutions sector of the Survey, which brings the number of participants in the finance companies sector to 16.

As has been the case with previous FIPS Surveys, all information used in compiling our analysis is extracted from publicly available annual reports and disclosure statements for each organisation, with the exception of certain information provided by Survey participants. We wish to thank the Survey participants for their valued contribution, both for the additional information and for the time made available to meet with us.

Massey University continues to be a stakeholder of the Survey, assisting with the data collection and analysis, as well as drafting the forecasting section of this Survey. We thank them for their continued contribution.

Continuing the theme from last year, we are also delighted to have comments from the RBNZ and the New Zealand Banker's Association. We trust you find the content of this Survey of interest. If there are any issues or matters in the document that you wish to discuss in further detail, please do not hesitate to contact us.

TABLE 1: MOVEMENTS

	Who's out	Who's in
Registered banks 19 to 21		The Co-operative Bank Limited Bank of India (New Zealand) Limited
Finance companies 17 to 16	**Acquired by Heartland:** PGG Wrightson Finance Limited (PGGWF)	
Savings institutions 9 to 8	**Moved to Banking Sector:** The Co-operative Bank Limited	

Industry overview

The current year has seen profitability for many institutions improve to near record levels on the back of further reductions in impairment expenses, improvements in net interest margins and a return to lending growth. At the same time the Survey notes careful cost management, enhanced equity positions and the ever increasing burden of compliance with new regulations.

BANKING SECTOR

Performance of the banks

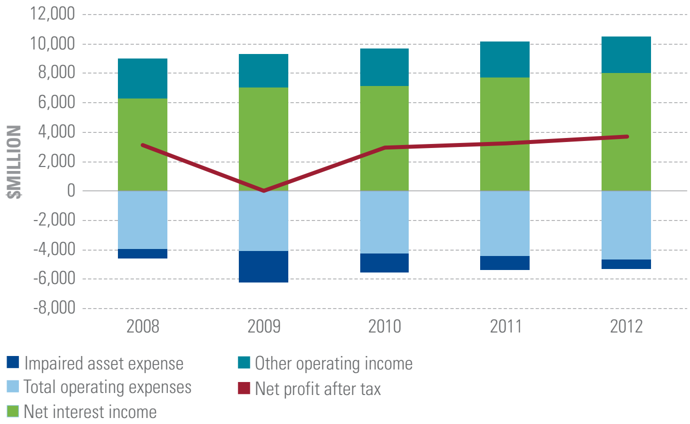
Driven by improved net interest margins, asset growth (an increase in gross loans and advances of 3.2%) and continuing reduced levels of impairment expenditure, the 2012 survey has seen sector profits increase by 13.6% on the prior year.

Deposits have increased by 9.8%, driven by attractive rates, competition by the banks for retail deposits and a continuation of the deleveraging trend. Net interest margins increased 3 basis points (bps) to 2.25%.

Regulatory changes in Reserve Bank of New Zealand (RBNZ) funding requirements has increased the demand for, and consequently the pricing of, retail deposits. This is still having a negative effect on margins although some easing of rates occurred toward the end of the survey period.

Overall funding costs have been lower with the major impact coming from the increasing stability of global debt markets. Some of the smaller banks with limited access to alternative debt markets are feeling increased margin pressure. When you consider the rates being paid for retail deposits (around 4% for six month term deposits), and what is able to be earned when monies are lent out in the competitive mortgage market (circa 5.3% for six month mortgages), this is not surprising.

1 REGISTERED BANKS: PERFORMANCE ANALYSIS



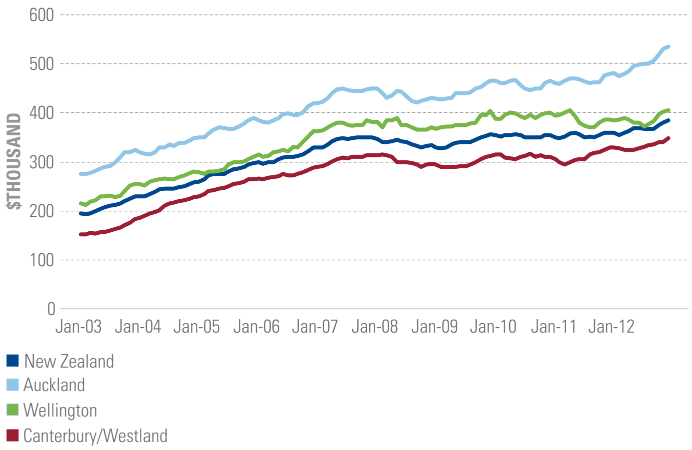
Credit quality

Credit quality has improved across the sector with past due and gross impaired levels reducing and an impaired asset expense 25.7% lower year on year. The impaired asset expense as a percentage of gross loans and advances is the lowest it has been since 2007, at 0.21%. These metrics indicate a recovering credit environment but banks are still cautious and mindful of the legacy issues of the Global Financial Crisis (GFC).

Interest rate environment

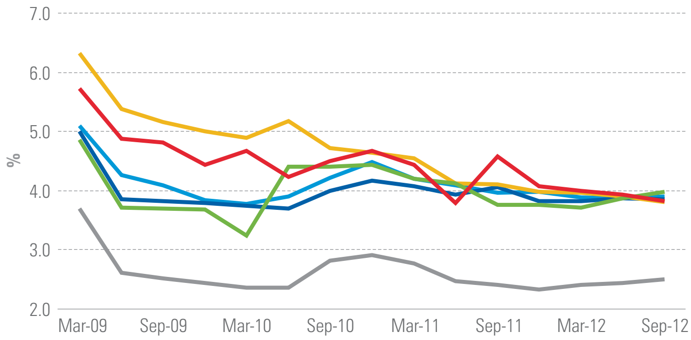
The Official Cash Rate (OCR) has remained at 2.5% since March 2011 and looks likely to

2 HISTORICAL TREND: MEDIAN HOUSEHOLD SALE PRICES (3 MONTH AVERAGE) IN NEW ZEALAND OVER 10 YEARS



Source: REINZ

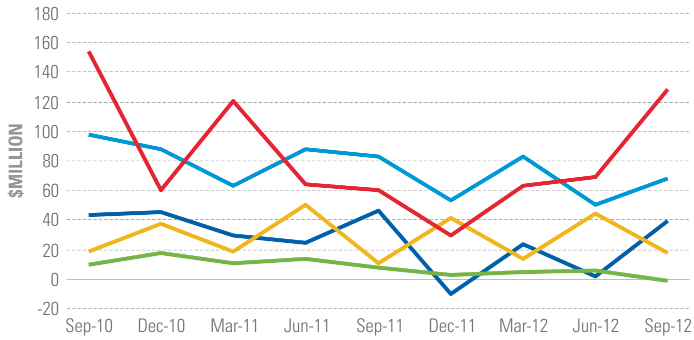
3 MAJOR BANKS: COST OF FUNDS VS OCR



■ ANZ BG ■ Kiwibank
■ Bank of New Zealand ■ Westpac
■ CBA + ASB ■ Average overnight interbank cash rate

Kiwibank data for September and December 2009 has been averaged to eliminate a change in methodology in their September reporting of interest income and expenses.

4 MAJOR BANKS: LOAN LOSSES



■ ANZ BG ■ Kiwibank
■ Bank of New Zealand ■ Westpac
■ CBA + ASB

Loan losses = Impaired asset expense less Collective provision movements

stay at this level for the majority of 2013. Together with stabilising global markets this has been a contributing factor to the low interest rates borrowers in New Zealand are able to access. These low rates are encouraging buyer demand in the property market, leading to rising house prices (figure 2). This is particularly noticeable in the Auckland region which has seen significant increases in house prices over the last 24 months.

The RBNZ announced on the 31 January 2013 that the OCR will remain unchanged at 2.5%. But it also mentioned that "house price inflation has increased and we are watching this and household credit growth closely". This could imply either an OCR hike, or that other tools such as a capital overlay may be considered to cool the housing market.

The low interest rate environment is having a less favourable effect for savers, and as the collapse of the finance company sector fades in the memory of savers they will be considering if there are returns out there better than in the bank deposit market. However, the relative safety that the New Zealand banking system provides, combined with a lack of alternative investments and little growth in the number of NZX-listed companies, have resulted in a 'flight to quality' and savers keeping deposit levels high. In fact deposits have risen significantly in 2012 due to this sentiment and banks are actively targeting this type of funding with competitive rates and products.

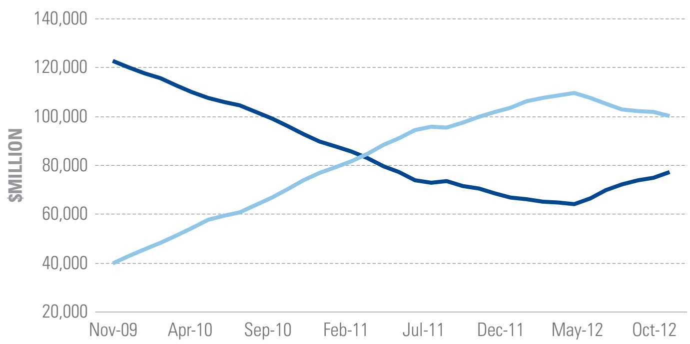
At the end of the period, we started to see a trend from floating mortgages back to fixed as customers consider a possible rate rise later in the year and as the banks offer competitive fixed rates which are below the current floating rates. Figure 5 illustrates this well, showing that from May 2012 the volume of floating loans starts to decline. The 1 to 2 year rate has seen the most defined increase in volume as customers switch from floating, as noted in figure 6.

Funding composition

In the aftermath of the GFC, market pressures and the introduction of new banking regulation, the banks have adjusted their funding composition. The composition has moved away from short-term wholesale deposit instruments such as commercial paper to instruments perceived to be 'stickier' such as retail deposits and long-term wholesale deposits. These are more expensive than short-term wholesale debt, but are "safe" in the current environment and contribute to the banks meeting their minimum core funding ratios.

The minimum core funding ratio, set by the RBNZ, increased from 70% to 75% on 1 January 2013. The ratio is calculated as core funding divided by total loans and advances. The criteria for meeting the core funding ratio have been among the factors contributing to increased competition for retail deposits in New Zealand and this is impacting margins of banks with limited access to alternative funding markets. The increased competition for deposits is illustrated in figure 7, which shows post the GFC the margin banks are paying for term deposits is

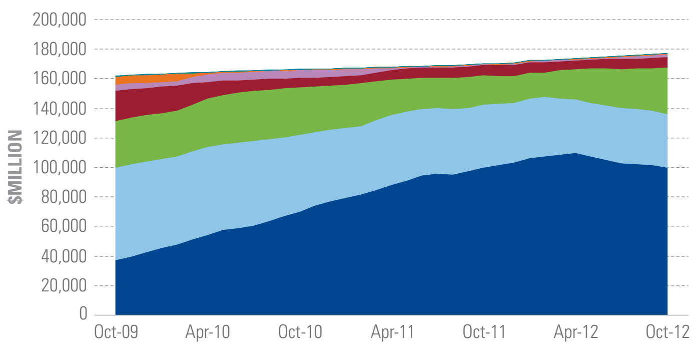
5 FIXED VS FLOATING MORTGAGES: VALUE OF LOANS



■ Residential mortgage loans – Fixed
■ Residential mortgage loans – Floating

Source: Reserve Bank of New Zealand Statistics

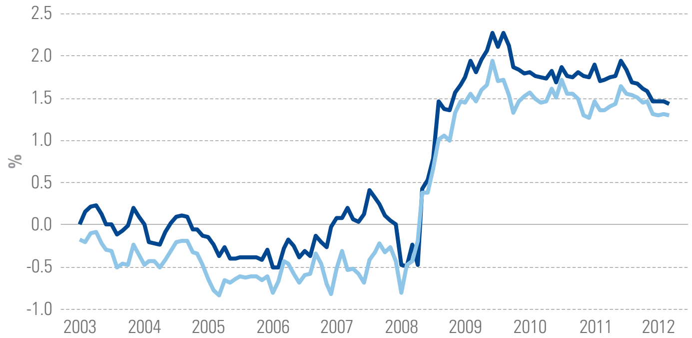
6 RESIDENTIAL MORTGAGE LOANS MATURITY PROFILE



■ Floating ■ 3>4 years
■ < 1 year ■ 4>5 years
■ 1>2 years ■ 5 years +
■ 2>3 years

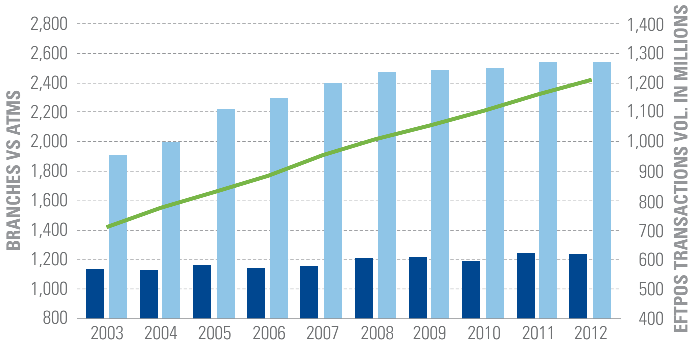
Source: Reserve Bank of New Zealand Statistics

7 TERM DEPOSIT RATE SPREADS (SIX MONTHS)



Source: Reserve Bank of New Zealand Statistics

8 REGISTERED BANKS: BRANCHES VS ATMS AND EFTPOS TRANSACTIONS



Source for EFTPOS transactions: Statistics New Zealand

well above the 90 day bank bill rate at currently around 130 basis points. However, pre-GFC banks were paying less than the 90 day bank bill rate as they could access alternative and cheaper funding on offshore markets.

Funding costs

The second half of 2011 and 2012 were marked by extreme volatility in overseas funding markets driven chiefly by the European debt crisis. The crisis saw funding costs soar due to concerns about sovereign and banking system credit worthiness. These concerns were interspersed with dramatic and short lived plunges of relief as policy makers floated proposals and central banks relaxed collateral requirements and injected huge amounts of liquidity to try to calm money markets and relieve liquidity pressures. The second half of 2012, and the final quarter in particular, saw these costs fall as confidence grew in the political will and capability to resolve the crisis and support the euro. This belief has continued into 2013 and should see the cost of overseas funding continue to fall.

This volatility meant that banks needed to be nimble in terms of their ability to choose to go to the wholesale markets for funding at short notice when conditions were favourable, and their capacity to maintain a sufficiently strong liquidity position to be able to afford to stay out of the market in times of stress when costs were high. Elevated costs also saw banks turn increasingly to covered bonds in order to access term funding at significantly cheaper rates than would have been available for traditional medium term notes. The thawing of debt markets in the last quarter of 2012 has extended into 2013 and, if it continues, should provide banks with a further benefit to their net interest margins.

Lending and competition

Lending volumes have increased by 3.2% during 2012, with increases occurring across all three major market segments of agriculture, business and total household. There is a broad recovery, with nearly all banks achieving increases. Comments from bank executives state that they are seeing growth in their business and mortgage portfolios but this growth is being partially offset by the continuing theme of deleveraging. And growth – or, indeed, retention of clients – is starting to cost margin.

Banks are offering quality customers discounts to reduce the risk they will shop for a new banker – which could result in a price war that could lose the bank further margin. Further competition in the mortgage market is impacting margins. Some banks are looking into new markets that they haven't entered into in a while, such as asset and lease financing, as they find credit growth difficult in their usual markets. The deleveraging economy is still a trend for many households and businesses. This is impacting banks' balance sheets and they are constantly looking for new lending to replace the runoff, whether that is through traditional sectors, new areas or extending maturities of existing customers.

Market participants have observed that the banking market has fallen back in love with the agricultural sector. While the period from 2009 to 2011 saw the banks taking a far more conservative and cautious approach to farm lending, 2012/13 appears to have seen a return to banks chasing deals and looking to secure the better credits. A number of farmers still need to continue to work through deleveraging strategies and improve productivity. The banks appear to be eager to grow their agri books, with an increased appetite to write deals at margins below those from the last year or two.

Economic situation

The RBNZ stated in their OCR announcement of 31 January 2013 that "global growth is set to recover in 2013 with economic indicators improving in many of our trading partners... Domestically, recent data on business confidence and construction activity suggests Gross Domestic Product (GDP) growth is recovering from the softness seen through the middle of last year."

The European crisis has been put off only until the next round of political talks, policy discussions resume and elections occur, or countries like Greece require additional funding to repay lenders. The US situation appears only to have been delayed, rather than resolved, as debt ceilings were raised and temporary measures put in place. The underlying issues that have lead Europe and the US to these fiscal situations are still festering in the minds of politicians, citizens and financial sector participants.

The appreciation of the New Zealand dollar (NZD) is a concern for exporters. Layoffs in this sector are increasingly common and a frequently stated factor is the high NZD. This ongoing bullishness of the NZD is leading businesses with foreign currency risk to reconsider their pricing and cost structures to remain competitive in the global market place.

Regulation change and challenges

Regulation and compliance departments in banks are increasing in size. As new regulation is rolled out and implemented, the banks are seeing their costs rising. These changes – instigated by the RBNZ and other financial system regulators – and policy

TABLE 2: REGISTERED BANKS: NON-PERFORMING LOANS	2009 %	2010 %	2011 %	2012 %
Past due assets to gross loans and advances	0.49	0.47	0.41	0.32
Gross impaired assets to gross loans and advances	1.06	1.55	1.46	1.18
Total	**1.55**	**2.02**	**1.87**	**1.50**

improvements are aimed at reducing the risk and impact of another GFC. Also, we are seeing increased compliance costs in relation to the Foreign Account Tax Compliance Act (FATCA) and the Anti-Money Laundering and Countering Financing of Terrorism Act. FATCA was issued by the US Internal Revenue Service (IRS) and requires financial institutions to comply with the Act and report to them information on US citizens so that the IRS can ensure US citizens are paying the appropriate amount of tax. Penalties are imposed on financial institutions that are affected and fail to comply.

Basel III is being implemented in New Zealand this year and will result in changes to the levels and type of capital New Zealand banks are required to hold. Already we are seeing some banks start to position for this with new capital structures.

The Open Bank Resolution policy is being worked through with the RBNZ and relevant banks. Its purpose is to put in place formal arrangements to manage a bank failure in an orderly fashion should one occur. While this is considered unlikely, the RBNZ believes it is necessary to have such arrangements in place as a safeguard to protect the financial system.

For more information on these topics, refer to the Regulatory changes and challenges section of this Survey.

Christchurch

The pace of the Christchurch rebuild has been slow, reflecting continued shakes and the task of working through town planning requirements – the rebuild has been a bit of a 'no show' in 2012. The rebuild offers definite opportunities for the banking industry and the economy as a whole – what remains to be seen is how long it will be before we really start to see the effects.

NON-BANKING SECTOR

The remaining non-bank Survey participants have survived the endurance test of the GFC, consolidated their positions in the market, and are now looking ahead to growing their lending portfolios by acclimatising to the current environment, checking over their existing practices and looking forward to the climb into new market segments.

Asset growth in the sector remains flat and competition for new lending is intense as sector participants compete with the banks in a deleveraging environment. With the intense competition from the banks being seen again in the sector, we expect to see pressure on margins over the coming 12 months.

Survey participants remain cautious after the GFC and are focused on maintaining good asset quality – but at a level that does not constrain the growth of assets through overly conservative lending practices. The failures of finance companies are stark reminders of the risks involved in this sector. The past five years have seen numerous receiverships as depositors fled and loan assets went sour. Receivers continue to seek to recover funds for depositors left out of pocket but asset recovery has proved difficult. The resilient have survived and are now preparing for the challenges to come, in a significantly more regulated and condensed industry.

A snap shot of sector performance can be taken as follows: asset growth is starting to recover as growth outweighs the deleveraging or run off of lending assets; profits have seen a healthy increase, fuelled by an improved net interest margin and substantially decreased impairment expense; participants are seeing improvements across all major credit quality measures as distressed assets of the past are exited, written off, or carefully managed – although management remain cautious about writing new business.

Margins and funding

In this Survey interest margins for the finance company sector improved as funding rates decreased, but lending rates remained stable. This resulted in an improved net interest margin, with the majority of participants enjoying increases.

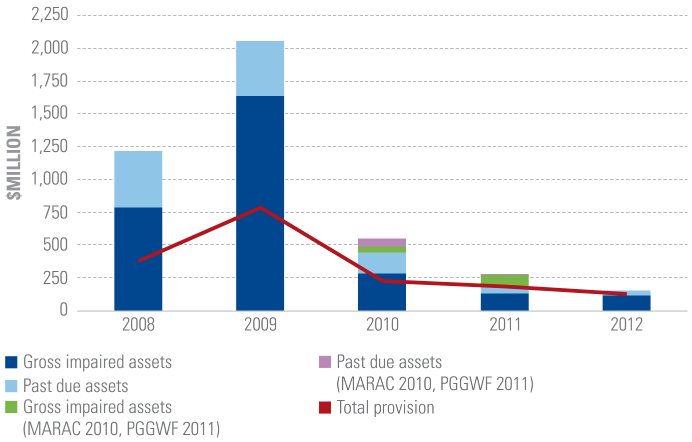
The savings institution sector did not enjoy the same improvement in net interest margin (when Heartland is excluded) as these entities are competing in the fiercely competitive mortgage market. The tough environment is leading to good deals for customers on mortgages, but smaller players like credit unions and building societies, without access to lower cost funding, are finding it harder to make adequate margins to cover rising costs.

Reduce cost structures and improve systems

Streamlining loan origination processes through better use of information technology and lean management systems is a focus this year. The pace at which technology develops requires participants to be in constant touch with the information technology environment. They need to ensure they have appropriately qualified professionals – in house or contracted – to help develop new systems that meet the ongoing information technology requirements, and to update systems to meet the ongoing regulatory amendments. Having adequate and secure internet based portals is becoming increasingly important as these are increasingly the most common medium through which financial institutions engage with their customers.

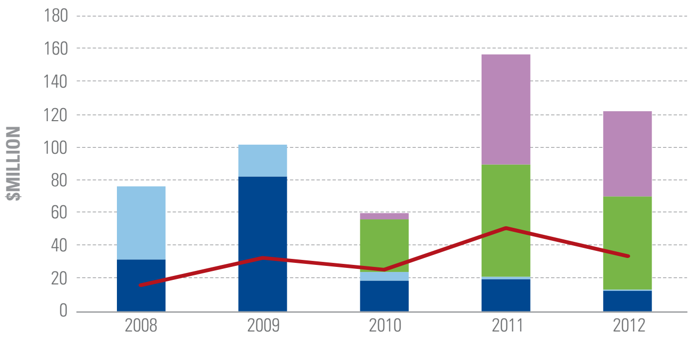
Some of the small players in the sector may find it difficult to get the critical mass required to sufficiently spread the increasing costs of updating information technology systems and regulatory compliance costs. This may lead to entities contemplating

9 FINANCE COMPANIES: GROSS IMPAIRED AND PAST DUE ASSETS



MARAC and PGGWF form part of Heartland New Zealand Limited, the results of which are included in the savings institutions section of our Survey. MARAC and PGGWF balances have been highlighted in the above merely to provide the reader with an understanding of the comparative figures for the entities included in the finance companies section of this year's Survey.

10 SAVINGS INSTITUTIONS: GROSS IMPAIRED AND PAST DUE ASSETS



- Gross impaired assets
- Past due assets
- Gross Impaired Assets – Quantum represented by Heartland (2010 comparatives being SBS/CBS, 2011 and 2012 being Heartland NZ Limited)
- Past Due Assets – Quantum represented by Heartland (2010 comparatives being SBS/CBS, 2011 and 2012 being Heartland NZ Limited)
- Total provision

merging to obtain sufficient scale to accommodate the costs of a being a participant in the non-banking sector.

Focus on core lending

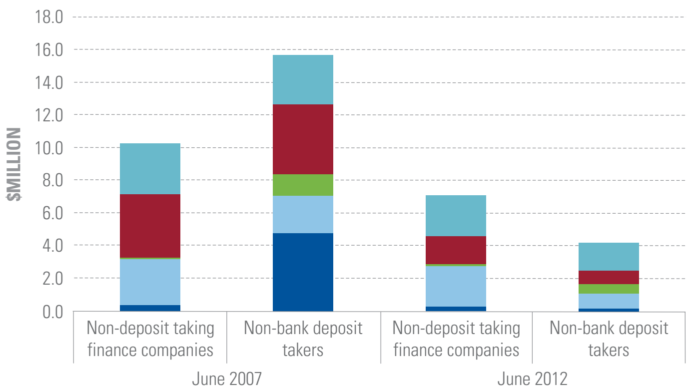
There is a common theme we have heard from executives we have met during the preparation of this Survey.

They have said that they are 'sticking to their core lending markets' and that 'what they know' has enabled them to avoid the pitfalls that some of the other finance companies have fallen into. The ratio of impaired asset expenses to average loans has fallen below 1% for the first time since 2008.

Also – for the first time since 2008 – total assets for the finance company sector have increased, albeit only by a 1.6%. Comments gleaned from executives indicate the writing of business has increased. But any new business is offset partially by the repayment of existing business, and this deleveraging trend continues from previous years as New Zealanders pay down debt on the back of historically low interest rates and a desire to reduce debt levels.

A theme indicated by several sector participants is that banks are starting to enter the territory of the non-banking sector. This indicates that banks are hungry for loan book growth and that the cycle has come back again to the point where banks are looking into other potentially profitable markets for which they have typically not had a risk appetite.

11 EXPOSURES OF NON-BANK LENDING INSTITUTIONS



- Property
- Other business
- Agriculture
- Housing
- Consumer

Source: Reserve Bank of New Zealand Standard Statistical Return, 'Financial Stability Report November 2012'
Note: 2012 figures exclude companies in moratorium or receivership.

Regulation change and challenges

Regulation and compliance are buzz words around the sector as participants work out who their new master is – the RBNZ or the Financial Markets Authority (FMA)? – and come to grips with the operational and reporting requirements of any new legislation about to be enacted. In our discussions with executives compliance is ironically referred to as the fastest growing part of their business. And where traditionally the compliance role could be filled adequately by a trained in-house staff member, a specialist in this area is now required.

The costs associated with hiring additional staff to meet the reporting and compliance requirements of legislation is proving costly and some smaller entities are left wondering how can they afford to hire additional staff to fill these roles. Further legislation such as the Anti-Money Laundering and Countering Financing of Terrorism Act can require amendments to existing information technology systems, as well as process changes to ensure frontline staff are obtaining and accrediting the necessary customer documentation to meet legislative requirements.

An exposure draft released outlining possible amendments to the Credit Contracts and Consumer Finance Amendments (CCCFA) Bill is causing a stir amongst sector participants. It appears to take some of the responsibility for the decision whether or not into enter a credit contract away from the borrower and to put it more squarely on the lender, ensuring the lender is practising 'responsible lending'. One of the primary intentions of the amendments to the Bill is to target 'loan sharks' and it is proposed in the exposure draft that entities that do not practise 'responsible lending' could be banned from the industry. How the Bill will be enforced in practice will be the FMA's responsibility and will ultimately be tried through the courts.

Merge and acquire

In this year's Survey The Co-operative Bank exited the non-banking sector and moved to the banking sector, PGG Wrightson Finance was acquired by Heartland Building Society and Manchester Unity Credit Union (a market participant, but not individually included in the Survey) merged with Credit Union Baywide. More recently, in December 2012, Credit Union North and First Credit Union merged. These mergers were arguably a result of the need to increase market share and achieve economies of scale, as well as to diversify their portfolio credit risk.

The future

The non-banking sector has undergone significant change over the last five years, as illustrated by figure 11 (extracted from the RBNZ November 2012 *Financial Stability Report*). It shows a dramatic decline in the size of the sectors' lending exposures. Gone are the property development exposures. One unanswered question, going forward, is – who will fund the mezzanine debt on new property development, particularly with the Christchurch rebuild on the horizon?

For participants to grow organically, they will first have to protect their traditional business. Then they will need to create innovative products to entice new customers – and to access new market segments – where they possess understanding and competency.

Timeline of events

January 2012

18th Kiwibank purchases Gareth Morgan Investments (GMI) – a late entry by the state-owned bank in the KiwiSaver market. GMI currently manages over $1.5 billion, of which $650 million is KiwiSaver related, on behalf of more than 57,000 clients.

26th Former National Finance director Trevor Allan Ludlow's prison sentence was extended in relation to Financial Markets Authority (FMA) charges for misleading investors and making false financial statements.

31st RBNZ Governor Alan Bollard announces he will not be seeking another term and will step down when his current term ends on 25 September 2012.

February 2012

1st Kiwibank's credit rating has been confirmed at AA- by international credit rating agency S&P. The outlook for the bank has been amended from stable to negative.

8th The US IRS issued proposed regulations with significant changes and clarifications to prior guidance for the Foreign Account Tax Compliance Act (FATCA).

27th Fitch downgrades CBA, NAB, Westpac Banking Corporation and their respective subsidiaries ASB, BNZ and Westpac NZ's long-term credit ratings by one notch to AA- bringing them in line with ANZ Bank which also had its rating affirmed. The downgrade brings Fitch's ratings for the big four banks in line with S&P.

March 2012

9th Westpac appointed Peter Clare as its new chief executive of the bank in New Zealand, replacing George Frazis, who will become chief executive of the Westpac subsidiary, St. George Banking Group in Australia.

13th RBNZ invites submissions on the Consultation document on the Non-Bank Deposit Takers Bill 2011. This Bill proposes the requirement for all non-bank deposit takers to obtain a licence and be subject to additional requirements.

April 2012

4th Member banks of Payments New Zealand have completed a major upgrade to banking systems costing millions, significantly speeding up bank to bank transfers. Instead of waiting for payments overnight, bank customers will now be able to access their payments within a couple of hours.

May 2012

17th New Zealand was removed from the European Union banking and corporate "White List" over concerns about the lack of money laundering and terrorism financing controls in place mostly related to the registration of shell companies meaning that EU financial institutions may increase measures to confirm the identity of customers from New Zealand.

22nd FMA proposed guidelines which will require entities who raise money from the public and use financial figures other than their profit and loss such as 'underlying profit' to explain why and ensure that the information is not misleading.

June 2012

5th Westpac and MYOB launch a new initiative "Getonline.co.nz" with the aim of making free websites available to New Zealand businesses for 12 months in order to help expose their products to the market.

6th New levies are introduced requiring the finance industry to fund the operations of the FMA. The imposition of the new levies will mean that the FMA is 60% funded by the industry. Commerce Minister Craig Foss believes this new levy will assist in funding a "well-regulated market".

29th The RBNZ published an update on the AML/CFT Act and provided further detail on the RBNZ's proposed supervisory approach. The date for full implementation is set for 30 June 2013.

July 2012

27th Carol Braithwaite, a director of failed finance company National Finance, is convicted for making untrue statements in the 2000 prospectus. National Finance went into receivership in 2006.

August 2012

2nd After a 3.5 year moratorium, Orange Finance is placed in receivership with 72 cents in the dollar of principal repaid.

17th Former Bridgecorp CFO Rob Roest's jail sentence increased for breaches of the Securities Act, Crimes Act and Companies Act brought by the FMA and previously the Securities Commission.

September 2012

1st The former directors of Capital + Merchant Finance have been sentenced to 7.5 years in prison. The directors loaned investor money for their own benefit which breached the company's trust deed. The company collapsed in 2007 owing $167 million to 7,500 investors.

7th The RBNZ and FMA announce that the NZClear settlement system has been declared a designated settlement system under the Reserve Bank of New Zealand Act. The designation of the system gives statutory backing to the finality of transactions and therefore in the event of a failure of a participant, the transactions cannot be undone.

10th Westpac and partner Lumley secure international reinsurance backing in order to offer new insurance policies to residents of Christchurch who are currently battling a lack of available insurance. The move hopes to open up the market for other financial institutions to follow. Home cover will be on a sum insured basis which is common overseas and likely to become standard in New Zealand due to changes in the country's reinsurance risk profile since the earthquakes.

21st Three members were struck off NZICA (two directors of failed finance companies, ex-Bridgecorp director Rob Roest and ex-Five Star Finance director Anthony Walpole Bowden, and a Tirau accountant Robert Philip Bell). Reasons for striking off these individuals relate to breaches of the Institute's Code of Ethics and bringing the accountancy profession in disrepute.

25th Former World Bank managing director Graeme Wheeler takes over governance of the RBNZ as incumbent Allan Bollard retires from the role.

26th Announcement that the ANZ Bank and The National Bank would be brought together.

October 2012

18th S&P affirms Heartland New Zealand's BBB- credit rating with a stable outlook which is seen as an important milestone in the company's quest to become a registered bank.

24th The US IRS released an advance copy of Announcement 2012-42 for the FATCA which provides timelines for withholding agents and foreign financial institutions to complete due diligence and other requirements.

27th The switchover of around 2.6 million National Bank customer accounts to the ANZ Bank brand begins.

30th Credit rating agency S&P cuts Kiwibank's and parent company NZ Post's credit rating to A+ with a stable outlook, one notch below the big four banks.

November 2012

19th S&P downgrades Rabobank New Zealand's credit rating one notch to AA- amid concerns about the home market of the parent company. The downgraded rating is in line with New Zealand's big four banks.

26th ASB Bank issues $250 million of ordinary shares to its parent company the Commonwealth Bank of Australia due to uncertainty to issue replacement tier 2 capital with the imminent arrival of the new more stringent Basel III capital adequacy standards.

December 2012

6th NZCU North amalgamated with First Credit Union.

11th The RBNZ releases the new Capital Adequacy Standards required under the Basel III capital adequacy framework which will be imposed from 1 January 2013 in a move aimed to strengthen New Zealand banks' capability to absorb losses.

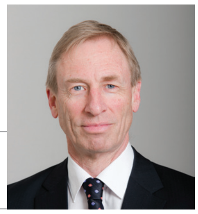
17th Heartland Building Society, the result of a merger between MARAC Finance and two building societies, was officially granted a banking licence from the RBNZ becoming the country's 22nd registered bank.

January 2013

9th Preparations are under way for the world's largest bank, China's ICBC "Industrial and Commercial Bank of China" to make an entry into the New Zealand banking market. An application for a banking licence was received by the RBNZ in late 2012 and is currently under consideration.

Reserve Bank to cement in regulatory changes in 2013

RESERVE BANK OF NEW ZEALAND
TE PŪTEA MATUA



Grant Spencer | Deputy Governor and Head of Financial Stability | Reserve Bank of New Zealand

After a period of significant regulatory change in recent years, 2013 could be characterised as a time of consolidation for the Reserve Bank's prudential regime. However, ongoing regulatory change will continue to be part of the scenery.

Most components of the Basel III framework are now in force, with new capital requirements taking effect on 1 January 2013. This means banks now have to maintain a common equity tier 1 ratio of 4.5 percent, a tier 1 capital ratio of 6 percent and a total capital ratio of 8 percent. In addition, from January 2014, banks will need to maintain a minimum 2.5 percent common equity buffer over and above these ratios, known as the conservation buffer.

The first day of 2013 also saw the further strengthening of liquidity requirements, with the Core Funding Ratio (our version of the Basel III Net Stable Funding Ratio) increasing to 75 percent. This puts New Zealand well ahead of the Basel implementation schedule. Remaining elements such as new counterparty credit risk and new disclosure requirements will be implemented in the first quarter of this year.

Another key micro-prudential regulatory development for the Reserve Bank will be making the Open Bank Resolution (OBR) policy fully operational later this year. OBR is a tool for allocating losses in the event of a bank failure, while minimising impacts on taxpayers and the wider financial system. Banks are required to implement their prepositioning of IT and other systems by 30 June 2013. This will make OBR a live option for the government and means New Zealand will comply with the main attributes for resolving failing banks as recommended by the Financial Stability Board.

This year should also see the introduction of a new regulatory framework for covered bonds. The Reserve Bank Covered Bonds Amendment Bill, which was introduced to Parliament in May last year, includes a register for covered bond issuances and will provide investors and depositors with greater legal certainty in the unlikely event of a bank failure.

Macro-prudential policy tools such as loan-to-value restrictions and capital overlays are being used increasingly around the world. In New Zealand we will have scope to implement the Basel III countercyclical capital buffer from January 2014 and the Reserve Bank intends to consult on an overall macro-prudential policy framework in March.

> **Another key micro-prudential regulatory development for the Reserve Bank will be making the Open Bank Resolution (OBR) policy fully operational later this year.**
>
> Grant Spencer

Meanwhile, the key development in the Non-Bank Deposit Taking (NBDT) sector for 2013 will be the review of the operation of the NBDT regulatory regime. This review, which is required by our legislation and involves a report to Parliament, will be completed by September this year. It will cover all aspects of the operation of this regulatory regime, which has been in place since 2008, and will draw on experiences to date, as well as lessons for improvement. The Reserve Bank will also introduce a licensing regime for NBDTs.

These prudential measures being progressed in 2013 will further strengthen our prudential requirements and support financial stability in New Zealand. But our work is not complete: global risk remains elevated and prudential regulation will need to continually evolve in order to respond to new challenges as they emerge.

So, while 2013 might be a year of regulatory consolidation, the Reserve Bank will continue to actively improve the regulatory framework as new vulnerabilities arise.

Regulatory change and challenges

Nicola Raynes | Senior Manager | Financial and Regulatory Risk Management | KPMG

Regulatory reforms remain prevalent in the banking sector, both globally and in New Zealand. Financial institutions need to stay proactive in dealing with these changes and they need to ensure their responses become embedded in their organisations as business-as-usual. Below we discuss some of the regulatory change topics which will have an impact on financial institutions in the near future.

Basel III capital reforms

At the outset of consultation by the Reserve Bank of New Zealand (RBNZ) on the revised Basel III capital adequacy framework, the RBNZ said it expected New Zealand banks to be relatively well positioned to meet the new requirements. This has proven true in most respects and in preparation for the introduction of the reforms, New Zealand banks have been reviewing the levels of regulatory capital held, their internal minimum capital requirements and the structure of their regulatory capital base to ensure they are compliant with the finalised rules at the implementation date of 1 January 2013. The RBNZ is yet to finalise its rules in respect of counterparty credit risk and disclosure requirements, but these are imminent.

The Basel III capital reforms have driven an expected change in the composition, quality and quantity of regulatory capital held by banks. This has also proven a necessity from a funding perspective; banks need to be seen in the eyes of the wholesale debt markets to have a high quality capital base.

There has been a greater concentration on the level of Tier One capital, through share issuance and retention of earnings, given the renewed emphasis on higher quality capital and loss absorption. During the Global Financial Crisis (GFC), hybrid instruments such as those recognised in banks' Tier Two capital under Basel II were found to lack the ability to absorb losses as they occurred. As such, these instruments are now highly unlikely to meet the enhanced criteria for recognition under Basel III. Institutions are choosing to withdraw them from the market rather than amending the terms and conditions to make them Basel III compliant. In the New Zealand market many of the locally incorporated banks called and repaid subordinated debt instruments during their respective 2012 financial years.

> **"The Basel III capital reforms have driven an expected change in composition, quality and quantity of regulatory capital held by banks.**

This non-common equity instrument market is yet to be fully tested in New Zealand. One bank did issue a new Basel III compliant subordinated debt instrument at the end of 2012 and we expect that others will follow suit in 2013 now that the recognition and loss absorption criteria are finalised. Banks may seek to use these instruments to replace existing Tier One capital or to supplement existing capital levels if growth in lending or changes in loan risk weightings lead to increased capital needs.

There are two additional areas of proposal that may also impact upon the levels of regulatory capital locally incorporated banks will need to hold.

- *Macro-economic policies* – The RBNZ has recently outlined additional measures they may look at which will dictate the level of regulatory capital required: (i) adjusting the risk-weighting of sector and product specific loans; and (ii) imposing limits on loan-to-value ratios in the residential mortgage sector. This is in addition to the introduction of the counter-cyclical buffer mechanism under Basel III reforms to help protect the banking sector from periods of extraordinary excess aggregate credit growth.

- Domestic Systemically Important Banks (D-SIB) Framework – following the development and endorsement of the global systemically-important bank (G-SIB) framework by the Financial Stability Board and G20, a smaller framework has now been finalised by the Basel Committee on Banking Supervision (BCBS) for D-SIBs. The framework outlines the principles national supervisors would use for identifying and monitoring D-SIBs and the higher loss absorbency principles that would be utilised by supervisory bodies (i.e. additional capital requirements). Given the four systemic banks within the New Zealand market are Australian-owned, it is expected that the RBNZ will wait before making any statements about its intentions until APRA – the Australian Prudential Regulation Authority – comes to a conclusion as to whether its existing risk assessment and oversight approach already meet the principles of the framework. This approach will be welcomed by the local branches and subsidiaries of the Australian banks. It is interesting to note that the International Monetary Fund in its recent working paper on New Zealand banks' capital adequacy (January 2013) stated that additional capital buffers for these banks – given high bank concentration and their large offshore wholesale funding needs – would be beneficial for times of market uncertainty.

Open bank resolution

Locally incorporated banks with retail deposits in excess of $1 billion must be pre-positioned for the RBNZ's Open Bank Resolution (OBR) policy by 30 June 2013. OBR aims to ensure that a bank has the ability to provide full or limited banking operations the next business day after being placed into statutory management, ensuring the ongoing immediate provision of liquidity to the economy. The policy also aims to instil confidence in the re-opened bank and avoid a 'run on the bank'. Once placed into statutory management, a prudent assessment of losses is required to be undertaken and a portion of depositor and unsecured creditor balances will then be 'frozen' to absorb the allocation of these losses. After the ultimate extent of losses is known and a solution for the bank has been determined any remaining portion of the frozen funds will be returned.

The RBNZ's OBR policy signals there is no Government support for a failing bank; however, there is still the option for intervention. The Government guarantees the unfrozen portion of customer / creditor balances and other new liabilities entered into by the 're-opened' bank. The only other time the Government will step in is if the original loss assessment and freezing of funds proves to be insufficient.

All banks required to pre-position for OBR are designing and testing, to the greatest extent possible, their proposed OBR solutions. Significant time and effort are required. The RBNZ has been engaging with banks bilaterally to ensure the scope and design of proposed solutions is robust and effective. A finalised policy handbook is in development.

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The AML/CFT Act has expanded requirements by setting up new standards on identity verification.

Non-bank deposit takers

The Reserve Bank Amendment Act came into force on 1 December 2010. This empowered the RBNZ to act as the prudential regulatory authority for non-banking deposit taking institutions (NBDT's). The key NBDT prudential requirements that are currently in force are credit ratings, governance, risk management, capital, liquidity and related party exposures. These requirements should be well embedded within NBDT's operations and should have prepared NBDTs for the next regulatory requirements that are imminent. Parliament announced a further Non-Bank Deposit Takers Bill in July 2011, outlining the remaining regulatory requirements (for example, minimum licensing requirements, change of ownership controls, RBNZ information gathering powers, etc) to be implemented for NBDT's (expected to come into force in June 2013).

The RBNZ still has a number of other areas of consultation underway – proposals for regulations under the Non-bank Deposit Takers Bill 2011 and the disclosure rules for NBDT prudential requirements.

AML/CFT

New Zealand enhanced its Anti-Money Laundering and Countering Funding of Terrorism (AML/CFT) regime by enacting The Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (The AML/CFT Act), which comes fully into force on 30 June 2013. The sector supervisors (the RBNZ, the Financial Markets Authority (FMA) and the Department of Internal Affairs (DIA)) expect reporting entities to be fully compliant from that date (not allowing for an assisted compliance period as seen in Australia). The AML/CFT Act has expanded requirements by setting up new standards on identity verification, monitoring activities (both internally and by an external advisor) and it has added criminal liability as a potential penalty.

Implementing these requirements is involving significant time, effort and cost (particularly IT investment) for New Zealand reporting entities, with severe regulatory and reputation risk for non-compliance. We understand a number of programmes are becoming increasingly time pressured in implementation and that costs are ramping up.

Reporting entities' obligations include:

- ➔ Assessing the AML/CFT risk they may reasonably be expected to face using a formal risk assessment and a robust auditable methodology;
- ➔ Developing and maintaining an effective AML/CFT compliance programme;
- ➔ Initial and ongoing customer due diligence which meets the requirements; and
- ➔ Reporting on suspicious transactions.

The Global Financial Action Task Force revised its 40 recommendations in February 2012, encouraging governments to enhance their AML/CFT regimes against financial crime, corruption and tax crimes. The New Zealand Ministry of Justice and sector supervisors have yet to assess these recommendations against the current regulatory framework.

Foreign Account Tax Compliance Act

The Foreign Account Tax Compliance Act (FATCA) is a law of the United States of America (US) aimed at preventing offshore tax abuses by US persons. This law is extra-territorial and requires financial institutions outside the US to:

- ➔ Identify US customers by following strict customer due diligence requirements; and

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FATCA is a law of the US aimed at preventing offshore tax abuses by US persons.

- ➔ Report various information to the US, including account balances, income earned and sale proceeds from debt and equity securities.

If a financial institution chooses not to partake in the regime it risks incurring a 30% withholding penalty on income from the US. There have been various delays to the implementation of FATCA but it is now expected to commence on 1 January 2014 with some of the customer identification and reporting requirements to be phased in over 2014 to 2017.

Intergovernmental agreements

Various governments, including New Zealand's, have announced an intention to enter an Intergovernmental Agreement (IGA) with the US which will provide an alternate basis to the US regulations for implementing FATCA in these jurisdictions. The US has recently announced that it is in IGA discussions with 50 other jurisdictions. Officials from New Zealand's Inland Revenue Department (IRD) have had initial discussions with their counterparts in the US. More formal negotiations commenced early 2013 with a signed IGA for New Zealand expected in the first half of 2013.

Under an IGA, New Zealand financial institutions such as banks and NBDT's will automatically be subject to FATCA's requirements. The IGA will eliminate FATCA withholding in most circumstances and facilitate FATCA implementation by providing concessions and exemptions from the customer due diligence and reporting requirements (though the impact of these is very limited). The IGA aims to overcome the legal impediments to compliance that had been identified with the regulations, such as privacy and discrimination concerns, with the IRD taking an integral role in the exchange of information with the IRS to overcome such concerns.

Financial institutions should be assessing FATCA's effect on their business by completing an impact analysis now and kicking off a FATCA project. Financial institutions waiting until the middle of 2013 for a signed IGA, domestic legislation and guidance may be leaving it too late to identify changes required to systems and processes and the design of new target operating models. This is particularly so given efficiencies can be gained as New Zealand implements similar customer due diligence processes for AML/CFT in the first half of 2013. This will enable organisations to react quickly and efficiently to the signing of the IGA and the release of local legislation/guidance.

Financial Markets Conduct Bill

The Financial Markets Conduct Bill (the FMCB) was first introduced to Parliament in October 2011, and will replace financial market conduct regulation contained in a number of statutes, including the Securities Act and the Securities Markets Act, to better align with Australian equivalent standards. The regime provided by the Bill aims to:

- ensure that investors are provided with understandable and accurate information to guide their decision making;
- ensure that governance arrangements in respect of financial products available to the public are robust;
- minimise unnecessary compliance costs for those raising capital; and
- promote innovation and effective competition.

The FMCB is extensive in coverage. It looks at the categorisation of financial products and the regulation and offer of these in the market; changes to the governance of financial products and services; prohibitions on misleading and deceptive conduct and the supervision of this; and changes to the liability regime in order to promote compliance. It is expected to be passed in early 2013 for progressive commencement during 2014. Issuers may register prospectuses for new offers under the current law for up to 12 months after the Bill's enactment, but all offers and existing products must transition to the new regime within two years of the FMCB being in force.

In December 2012 the Ministry of Business Innovation and Employment (MBIE) released the Financial Markets Conduct Regulations Discussion Paper, which outlines the regulations and registers that underpin the FMCB. Submissions on the paper close in early March 2013. An Exposure Draft is expected to be released around October 2013.

Financial Markets Authority developments

KiwiSaver guidance

Due to the rapid increase in the number of KiwiSaver providers, the FMA has released a guidance note outlining its interpretation of the laws and practices surrounding the KiwiSaver scheme. The guidance note focuses on the factors it will take into account when considering whether financial advice is given, and if so, what category of service has been provided (class or personalised). It also outlines the FMA's expectations in respect of compliance controls to ensure KiwiSaver scheme providers and salespersons are meeting their legal obligations (e.g. ongoing training, supervision of staff, formal documented procedures). For each distribution model, the FMA expects an adviser's processes and controls to deliver advice with care, diligence and skill to be appropriately designed and operating effectively, with similar obligations where third party distributors or agents are used.

> **"Due to the rapid increase in the number of KiwiSaver providers, the FMA has released a guidance note outlining its interpretation of the laws and practices surrounding the KiwiSaver scheme.**

Reviews of Financial Advisers Act compliance

In its licensing and supervision of Authorised Financial Advisers (AFA) and Qualifying Financial Entities (QFEs), the FMA is undertaking reviews of QFEs' compliance with the Code of Professional Conduct and other obligations to ensure they exercise the standard of care, diligence and skill required. We understand the FMA has raised concerns about inappropriate disclosure to clients, the effectiveness of the QFEs' monitoring activities and the robustness of the overall framework – is it actually working? There has always been a risk that implementing such frameworks would be seen as a 'tick the box' exercise. It is a timely reminder to all AFAs and QFEs that they need to ensure their overall framework and monitoring and compliance activities are still fit for purpose since their initial licensing and that these must be adhered to in all their activities.

Information risks today

Every financial institution's practical guide to data security

Philip Whitmore | Director | IT Advisory | KPMG

Security should be on every financial institution's agenda. Data security breaches now appear to be headline news almost on a weekly basis. This, coupled with the myriad of interconnected systems within and between financial institutions – often held together with "duct tape" – has resulted in the New Zealand financial sector often being seen as a soft target.

Recent high profile cases such as the ACC leak, the WINZ kiosk incident and Murray McCully's email being breached, show us that the threats to security in New Zealand are just as real as those overseas. We should not forget either that what we see in the media is just the tip of the iceberg. The consequences can be disastrous as businesses' bottom line and reputation are impacted.

So why are we seeing a rise in attacks? How has the enemy evolved? The recent spate of attacks is, in large part, a result of a changing cyber threat. Just five years ago, IT managers were fully engaged in protecting against the rather brutish forays of organised crime and cyber-hooligans. Their methods tended to follow the 'full frontal assault' approach: bash down the door, scoop up everything you can, and get out.

But the profile of traditional cyber attacks has changed. Today's cyber attacker is more likely to be a social activist with an axe to grind rather than one who is financially motivated. More troubling still has been the perceived rise of state-sponsored hackers who enjoy the luxury of time, funding and resources to patiently probe businesses' IT systems for high-value intellectual property and trade secrets.

The mode of attack has also become much more sophisticated. Many of the more recent cyber attacks have used publicly available information to 'lure' insiders into a trap. In an act now termed as 'spear phishing', hackers dig through public websites and social networks to identify specific high-value targets that may have access to secure computer systems or sensitive information.

And let us not forget the threat from the inside. With New Zealand organisations often struggling with the basics such as password management, it is not surprising that in a simulated attack by a staff member at a financial institution recently, full administrative access to the majority of the core systems was obtained undetected in less than half a day.

Despite the high profile incidents seen in New Zealand in 2012, instances of accidental data loss continue to occur, with one New Zealand financial institution recently unintentionally emailing out sensitive customer information to a range of third parties. KPMG's Data Loss Barometer has shown that globally, while the financial services sector has seen an 80% reduction in data loss by the number of incidents in the last five years, it is still the fifth worst performing sector in 2012.

Understanding the risk

Ensuring the continuity of business operations and protecting sensitive data is not just about how much you spend, but whether you understand your risk profile and spend effectively.

The looming potential threat of a security breach is clearly a Board-level risk that must be taken seriously. All financial institutions, regardless of their size and complexity, should ask themselves some hard questions such as:

- ➔ What have been the most serious security and privacy incidents that we have faced in the past 12 months, what have we learned from those experiences, and what are we now doing differently to prevent them from re-occurring?
- ➔ What key indicators are on our security dashboard, how is the business achieving those objectives, and how does this compare to our peers?
- ➔ What are we spending on security over the next three years, is it enough to appropriately respond to the threat?
- ➔ What are our regulatory and contractual requirements around security and privacy, and are we meeting those?
- ➔ What is our risk appetite for data loss and privacy incidents, how will we set our appetite level, and how are we tracking against that?

Turning challenges into opportunities

But managing the risk of a security breach does not have to be all about what will hit the Six O'clock news and Wikileaks exposures. More progressive organisations are starting to look at the management of risk as a way to unlock opportunity and competitive advantage.

The simple truth is that risk is often cited as a barrier to the adoption of new and valuable technologies. Take Cloud computing for example; the technology has the potential to reduce cost, increase efficiency and – in many cases – even enhance security. But many IT professionals believe that outsourcing to cloud providers will result in a net increase in risk for their business.

The prognosis for consumer devices such as smart phones and tablets is much more dire: A large majority of financial institutions fear that an increase in risk will accompany the use of these devices. With banks rapidly developing new mobile payment solutions, balancing the opportunities presented with the security risks will be fundamental to maintaining confidence and banks' success in the future.

Seeing an opportunity to turn risk into reward, many businesses are starting to think more clearly about the opportunity cost of security measures. Indeed, rather than backing away from innovation at the first sign of risk, businesses are focussing on balancing the cost of developing an appropriate response against the benefits that new technologies may provide. So with no respite from the constant threat of security breaches in the offing, financial institutions should expect to spend more and more time thinking about security.

Economic growth and regulation: a fine balance

NEW ZEALAND BANKERS ASSOCIATION

Kirk Hope | Chief Executive | New Zealand Bankers' Association

2012 could be described as a year in the balance, characterised by a huge volume of new regulation, a low but relatively stable credit growth environment, and strong competition across the banking sector.

Competition among New Zealand banks remains high. Barriers to entering the market are low and we have seen new entrants in the last year. New industry rules introduced in 2010 have made it easier for customers to switch banks, making an already competitive industry more so. We continue to see fiercely competitive interest rates for loans. Competition is also evident in high customer satisfaction ratings. Banks work hard to attract and keep their customers and the ratings reflect the quality of those relationships.

On the regulatory front banks have been preparing their systems for three new sets of regulation which come into force in 2013:

- The enhanced anti-money laundering regime which has the aim of helping protect New Zealand from financial crime, and meeting our international obligations;
- The Foreign Account Tax Compliance Act, which has been unilaterally imposed by the United States government on all foreign financial institutions in an effort to clamp down on tax avoidance by US citizens resident in other countries; and
- Prepositioning banking systems for Open Bank Resolution which is designed to keep a bank open in the unlikely event of a potential failure. The policy involves freezing a portion of depositors' funds to allow the bank to keep trading, and guaranteeing the unfrozen portion to discourage a run on the bank. Whether this would work in practice remains moot, and a number of outstanding policy questions remain. Nevertheless, banks have been required to preposition their systems in advance of having some of these questions adequately addressed.

Trends in our domestic banking regulation will continue to be driven by international developments, which aim to achieve and maintain financial stability, and includes the new Basel III capital rules. Consistent with this theme the Reserve Bank is also developing its "macro-prudential tool-kit".

This involves four tools, two of which are already in use and two under consideration:

In use

- Sectoral risk weights – the banking sector already has adjusted sectoral risk weights for farm lending.
- The core funding ratio – this requires 75 percent of bank funding to be sourced from domestic deposits or longer term offshore funding to ensure that the New Zealand banking system is less vulnerable to international funding shocks. Banks on average are at around 84 percent of the core funding ratio, so well above that threshold.

Under consideration

- The counter-cyclical capital buffer – this aims to reduce the effects of excessive credit growth. If the Reserve Bank becomes concerned that this is happening then it can require banks to hold more capital, with the idea of increasing the cost of borrowing or slowing the volume of lending, or both, in order to dampen credit growth. The key challenge with the buffer is defining the conditions under which it might be used by the regulator. Banks will want to know these conditions so that they can adequately prepare.
- A cap on loan-to-value ratios (LVRs) – this limits what consumers may borrow. There will always be challenges with LVR caps. Common questions which arise around LVR caps include when to use it. Would it lock out first home buyers or make it harder by increasing deposit requirements? What impact will it have on house and credit pricing? Would non-bank lenders be restricted in the same way?

Getting the regulation right, and striking a balance between new rules and the need to encourage economic growth in a sluggish environment, is critical. The industry will need to continue to engage with the Reserve Bank and other regulators as they develop rules to ensure that the right balance is struck.

New Zealand has a strong, stable and highly competitive banking industry which continues to perform well in challenging global conditions. We have seen the costs for economies which are not so lucky. As well as providing vital lending to businesses and households banks made a significant direct contribution to the economy of $6 billion in 2012 through employing around 26,000 New Zealanders and paying local businesses for goods and services supplied to them. This ongoing investment in New Zealand, as well as support for New Zealand business, will provide a strong platform for New Zealand's future.

Registered banks sector performance

Overview of results

Overall 2012 has been a good year for the registered bank sector, profits have increased by 13.6%, as interest margins improve slightly and impaired asset expenses reduce. We are seeing growth in lending assets of 3.2% with renewed emphasis from banks on key sectors including residential (particularly Auckland), business lending and an emerging re-emphasis on agricultural lending.

We are starting to see a switch back from floating rate mortgages to fixed as customers take advantage of attractive offers and expectations of rate increases occurring late in 2013 are rumoured.

Customer deposits have increased 9.8% during the year, as banks target this source of funding to meet regulatory and risk management requirements. We are also seeing a shift from reliance on offshore wholesale debt markets for funding, as the cost and regulatory requirement for these instruments becomes unfavourable.

In the media some commentators have asked whether later in the year we might see some increased competition for the maturing deposit money when, or if, the speculative list of IPOs and share issues occurs.

Asset quality has continued to improve in 2012, with a decrease in the impaired asset expense of 25.7% as credit quality and delinquencies improve. Legacy assets of the pre-GFC era remain, and continue to be actively managed – and exited where possible.

The banks have endured the turmoil of the GFC and are reporting increasingly healthy profits. They are achieving good loan and deposit growth during the year and have strengthened their balance sheets.

The following analysis of the registered banks is from the view of the top geographic entity in New Zealand for that banking group, unless stipulated otherwise. For example, when 'Westpac' is mentioned this is referring to Westpac Banking Corporation – New Zealand Division and not Westpac New Zealand Limited.

Net Profit after Tax

For registered banks in New Zealand Net Profit after Tax (NPAT) increased over the year by 13.64%, from $3,236 million to $3,678 million.

Since 2010 (refer to table 3), the banks have steadily returned healthy profits. We note the 2010 increase in net profit percentage is uncharacteristically high due to a low base level of profit in 2009.

In percentage terms in 2012, Kiwibank was the best performer of the major banks, experiencing an increase in profit of 272%. This was a movement from $21 million to $79 million. Looking into the detail Kiwibank's higher profit was largely driven by cheaper funding, and a lower loan impairment expense.

ANZ, CBA and Westpac also saw good increases in their profits from 2011 – 16.59%, 19.33% and 13.96% respectively.

BNZ saw a 13.56% decrease in profit. As discussed elsewhere in the Survey this is largely due to the movement in "gains less losses on financial instruments at fair value" between the years. This was also one of the drivers for the increase in profit in 2011, showing the levels of movement that

TABLE 3: REGISTERED BANKS: PERFORMANCE TRENDS

Year	Increase in total assets %	Increase in net profit after tax %	Net profit after tax/Average total assets %	Interest margin %	Operating expenses/ Operating income %	Impaired asset expense/Average gross loans and advances %
2012	0.31	13.64	0.93	2.25	44.47	0.21
2011	4.34	9.78	0.84	2.22	43.76	0.29
2010	-0.05	7,389.22	0.78	2.09	44.02	0.42
2009	5.03	-98.75	0.08	2.13	43.66	0.76
2008	12.84	-2.26	0.91	2.07	44.64	0.24
2007	16.10	9.70	1.08	2.15	43.30	0.10
2006	15.01	6.79	1.14	2.28	44.56	0.06
2005	8.74	-0.35	1.26	2.52	46.00	0.12
2004	7.25	8.74	1.25	2.64	44.51	0.14
2003	5.90	-10.50	1.23	2.65	44.70	0.36

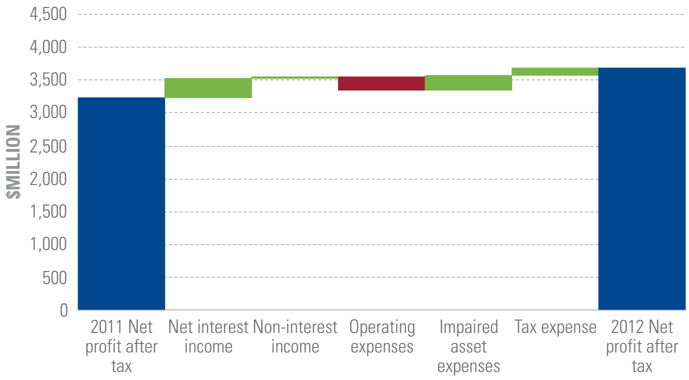
TABLE 4: ANALYSIS OF PERFORMANCE OF BANKS	New Zealand Incorporated Banks			New Zealand Branch Banks			All Banks		
	2012 %	2011 - 2012 Movement %	2011 %	2012 %	2011 - 2012 Movement %	2011 %	2012 %	2011 - 2012 Movement %	2011 %
Increase in total tangible assets	2.8	-2.4	5.2	-7.3	-5.8	-1.5	0.3	-4.0	4.3
Increase in operating income	4.8	-5.1	9.9	3.5	25.1	-21.6	3.2	-1.5	4.7
Increase in net profit after tax	16.3	-24.5	40.8	10.7	54.6	-43.9	13.6	3.8	9.8
Increase in gross loans and advances	5.7	5.1	0.6	-18.6	-17.5	-1.1	3.2	2.8	0.4
Net profit after tax/Average total tangible assets	1.0	0.1	0.9	0.7	0.1	0.6	0.9	0.1	0.8
Net profit after tax/Average equity	12.6	0.7	11.9	11.0	0.3	10.7	14.3	0.2	14.1
Net interest income/Average total tangible assets	2.2	0.1	2.1	1.0	-0.3	1.3	2.0	0.0	2.0
Non-interest income/Average total tangible assets	0.6	-0.1	0.7	0.5	0.4	0.1	0.6	0.0	0.6
Operating expenses/Average total tangible assets	1.3	0.0	1.3	0.4	0.0	0.4	1.2	0.0	1.2
Operating expenses/Operating income	45.2	0.0	45.2	25.6	0.0	25.6	44.5	0.7	43.8
Impaired asset expense/Average gross loans and advances	0.2	-0.1	0.3	0.3	-0.1	0.4	0.2	-0.1	0.3
Collective provision/Net loans and advances	0.5	-0.1	0.6	0.1	-0.2	0.3	0.5	0.0	0.5
Total provision for doubtful debts/Gross loans and advances	0.9	-0.1	1.0	0.5	-0.2	0.7	0.9	-0.1	1.0

profits are exposed to by volatile shifts in the fair value of financial instruments.

Overall, the profit increase can be broken down to the following, as shown in figure 12:

- ➔ An improved interest margin, which contributed $288 million towards the increased profit levels, which was largely driven by cheaper funding costs and a growth in loans and advances
- ➔ A small increase in non-interest income of $33 million. This figure was affected by losses seen in fair value movements reported by some entities
- ➔ Offset by an increase in operating expenses between years of $215 million
- ➔ Continued improvements in the quality of assets, which led to $225 million reduction in impairment expense in 2012
- ➔ A lower tax expense than 2011, a decrease of $94 million

12 **REGISTERED BANKS: MOVEMENT IN NET PROFIT AFTER TAX**



Net interest margin

Overall, banks were able to achieve a net interest margin (NIM) of 2.25% over the year, slightly up from 2.22% in 2011.

On an individual basis there was quite a variety of movements, with eight registered banks seeing an increase in margin, while nine banks saw a drop in their margin. However, as four of the eight banks that saw an increase were major banks, this weighted the overall change to an increase. Discussions with executives have indicated that late in the year and early in 2013 pressure on margins had increased as deleveraging and slow credit growth continued.

From the major banks, leading the increase in margin was Kiwibank with an increase in 34 bps, from 1.48% to 1.82%. Looking into the drivers of this movement, it is largely due to lower costs of funding rather than receiving higher incomes on lending and it should be remembered that Kiwibank came off the lowest base margin.

Looking into the factors that affect the net interest margin calculation, it can be seen that Kiwibank's interest income over the year grew 7.3% while interest earning assets grew by 6.0%. Interest bearing liabilities increased by 4.9% over the year, but interest expense for Kiwibank actually decreased by 2.5%. This shows that funding has become cheaper over the year, which will have improved the margin.

All of the other major banks saw an increase in their margins, with increases for ANZ, BNZ and CBA of 5 bps, 13 bps and 17 bps respectively. Except for Westpac, which saw a drop of 9 bps. For Westpac, while interest earning assets have grown over the year, interest income has actually decreased. This has offset any improvement in the cost of funding seen during the year.

Looking at all registered banks, the biggest improvers were Kiwibank and Citibank, which both saw an increase of 34 bps, and the largest drop in margin was seen by Deutsche Bank. However, the nature of Deutsche Bank is more that of an investment bank, thus interest margin would not necessarily be the best measure of its operating performance.

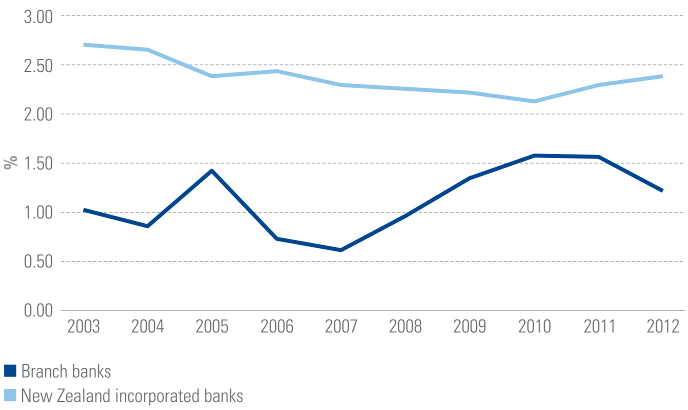
For TSB, 2011 saw its interest margin drop from 2.70% in 2010 to 2.02% as the impact of previous hedging contracts ran off. There has been a slight clawback in 2012, with an increase of 5 bps, bringing the interest margin up to 2.07%. This shows that TSB has adjusted lending and funding rates well in the tough competitive mortgage environment that has been seen over the year, as they have been not only able to maintain their margin, but to slightly increase it.

Newly registered bank, The Co-operative Bank, had a tough year with a 29 bps drop in interest margin, down to 2.78%. While there was a small decrease in the cost of funding, interest income dropped by 7.1% over the year, from $103.7 million to $96.4 million, while interest earning assets stayed flat. This demonstrates the competitive nature of the mortgage sector in the industry, which has been putting extra pressure on margins for all Survey participants, especially those that cannot operate on the same scale as the five major banks.

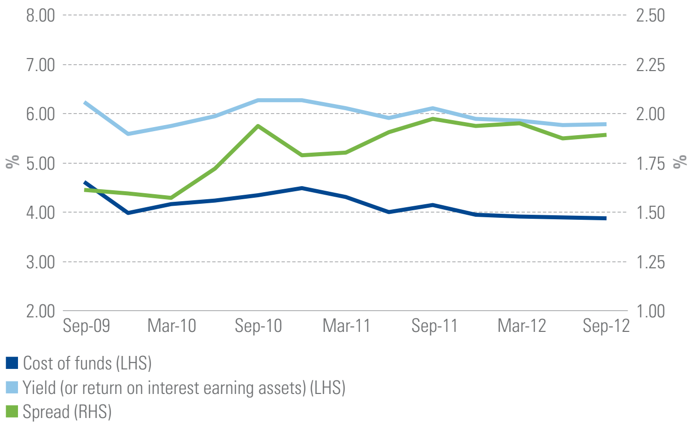
Return on assets and return on equity

The banks have continued to improve their returns as a whole over the year both on the basis of return on assets (RoA) and return on equity (RoE). However, returns

13 REGISTERED BANKS: INTEREST MARGINS



14 MAJOR BANKS: YIELD VS COST OF FUNDING



are still around the levels seen before the GFC. Return on assets improved from 0.84% in 2011 to 0.93% in 2012, while return on equity increased from the 14.10% seen in 2011 to 14.30%.

Significantly, Kiwibank lifted its RoE from 3.55% to 11.66%. This is partly a recovery from low level of profits seen in 2011.

Although Kiwibank's equity has increased from $608 million to $747 million the bank has been able to benefit from an increase in interest income from its growing loan book, decreasing interest expense resulting from a lowering cost of funding and improving asset quality. All of these factors have helped contribute to a significantly increased net profit, with only a small increase in equity.

Offsetting the increase in the overall sector RoE is BNZ, whose ratio has dropped from 16.07% in 2011 to 12.05% in 2012. Looking into the detail, this can be split into two components. Equity has significantly increased over the year, lifting $928 million to $5,277 million. This in itself will decrease the RoE. However, BNZ's profits also fell compared to 2011, dropping from $671 million to $580 million. Breaking the profit down, while there was a drop in expenses between years, this was offset by a large drop in other income, driven by a decrease in income from fair value movements.

Non-interest income

Non-interest income for the registered banks was fairly flat between years, with just a 1 bps decrease in the ratio of non-interest income to average total tangible assets. Non-interest income had a small increase from $2,431 million in 2011 to $2,463 million in 2012, whilst total tangible assets increased from $394.6 billion to $395.8 billion.

For the sector, the biggest improvement in this ratio was Deutsche Bank with a 367 bps increase, from -1.44% to 2.23%. Due to the nature of the bank, most of the bank's income comes under the non-interest category and is fairly volatile in nature between years. As this is where most of the bank's income is generated, this is also the big driver behind its increase in profit.

Looking at the major banks, three saw improvements in the ratio while two saw decreases. The largest of these movements was from BNZ, which saw a 51 bps reduction in the ratio from 0.70% in 2011 to 0.19% in 2012. This is on the back of an improvement between 2010 and 2011 of 18 bps. As was the driver of the 2010 – 2011 movement, this decrease is due to a large movement in "gains less losses on financial instruments at fair value". In 2011, BNZ saw a gain of $120 million in this category, while in 2012 there was a loss of $23 million.

The rest of the majors saw less significant movements. For example, Kiwibank's 11 bps decrease compared to CBA's 5 bps and ANZ and Westpac's 7 bps increases. Kiwibank's decrease was mainly due to flat non-interest income compared to a large growth in asset base. CBA's increase was largely driven by a net fair value gain, with the 2011 gain of $4 million increasing to $37 million in 2012, whilst ANZ and Westpac's increases were driven by small increases over a variety of other income lines.

Operating expense ratio

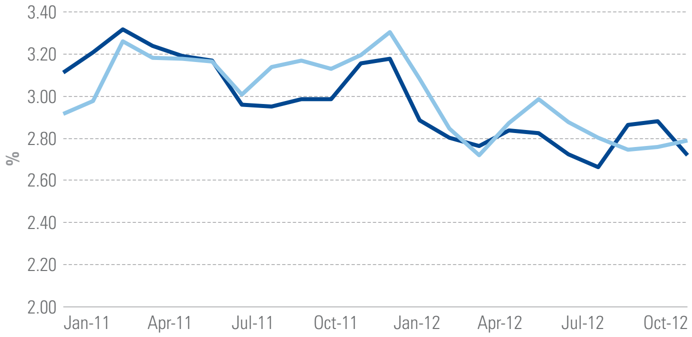
On an overall level, operating expenses as a proportion of operating income increased over the two years, from 43.76% in 2011 to 44.47%. Operating income was slightly up from $10,166 million to $10,486 million, whilst operating expenses increased at a higher rate, from $4,448 million to $4,663 million.

Amongst the majors BNZ had the largest increase in the ratio, up from 39.92% in 2011 to 46.35% in 2012. Looking into the drivers of this ratio, operating expense for BNZ increased from $754 million to $762 million. In addition operating income decreased, from $1,889 million to $1,644 million.

Kiwibank had the biggest improvement in the operating expense/operating income ratio, seeing a decrease from 64.04% in 2011 to 61.34%. The main reason was a significant increase in operating income (net interest income plus non-interest income), which rose from $353 million in 2011 to $419 million – driven by an increase in interest income, which rose from $720 million in 2011 to $773 million in 2012. This increase in operating income more than offset the increase seen in operating expenses, which increased from $226 million to $257 million.

TABLE 5: PERSONNEL COST	2012			2011		
	Employee numbers	Personnel cost $Million	Cost/ average employees $000's	Employee numbers	Personnel cost $Million	Cost/ average employees $000's
ANZ BG	9,183	942	100.6	9,551	933	98.0
Bank of New Zealand	4,611	417	89.3	4,726	421	91.4
CBA + ASB	4,695	440	93.9	4,674	432	94.5
Kiwibank	1,024	91	88.7	1,029	84	84.9
Westpac	4,856	446	91.9	4,853	436	89.1

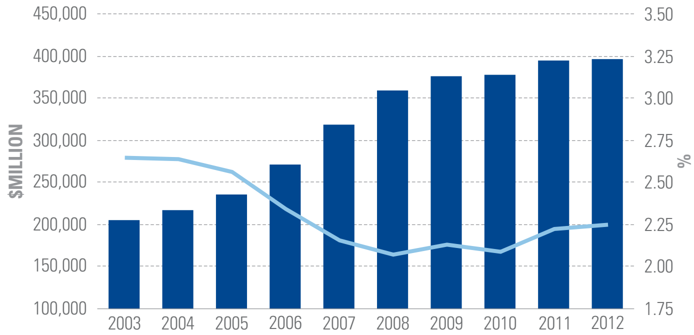
15 MOVEMENT IN RESIDENTIAL MORTGAGE MARGINS VS SWAP RATES



Bank margin over 1 year swaps
Bank margin over 2 year swaps

Source: Reserve Bank of New Zealand Statistics, Bloomberg

16 REGISTERED BANKS: TOTAL ASSETS VS INTEREST MARGIN



Total assets (LHS)
Interest margin (RHS)

CBA also performed well over the year. Its ratio dropped from 41.92% to 39.79%. This was driven largely by an increase in operating income, which rose from $1,684 million in 2011 to $1,812 million, while operating expenses were relatively flat between the years, only moving from $706 million to $721 million. The increase in operating income was mainly due to a reduction in interest expense, which is an indication of cheaper funding.

Even after the movements, Kiwibank still has the highest ratio out of the major banks, and this should slowly continue to improve as more economies of scale are gained from its continued growth. BNZ, even after its spiked increase this year, still has a ratio below that of ANZ. While Westpac has had a fairly flat movement over the year, it still reports the lowest ratio out of the major banks.

Personnel expenses continue to be a large part of operating expenses. Over the year, personnel expenses saw an increase from $2,453 million to $2,501 million, as banks continue to be one of the country's key employers.

Asset quality

Overall, reported asset quality in the registered banks continued to improve, with the impaired asset expense dropping from $879 million in 2011 to $653 million in 2012, a decrease of $226 million or 25.7%. The decrease in impaired asset expense highlights that the credit quality in the New Zealand economy has improved since the GFC, but the reduction is partly due to legacy assets already being provisioned for in previous years. Many legacy assets remain on the balance sheets of banks as a stark reminder of New Zealand's love affair with land, as banks work out the best way to exit them.

Most banks saw a drop in impaired asset expense compared to 2011. The exceptions were ANZ ($12 million increase), HSBC ($13 million increase), Kookmin Bank ($2 million increase) and SBS ($5 million increase), seeing a higher expense in 2012.

ANZ was the only major bank that saw an increase in impaired asset expense compared to 2011, albeit a fairly small one compared to the size of the expense, going from $190 million in 2011 to $202 million. BNZ had the biggest drop in its impaired asset expense, reducing year on year by more than 50 percent. This was a decrease to $61 million in 2012 from $152 million in 2011, a drop of $91 million. This decrease was due both to a decline in the amount of individual impairment charge and collective provision reversals, which netted down the overall impairment charge.

In line with the decreases seen above, this is reflected in the ratio of impaired asset expense to average gross loans and advances. Overall, this ratio has improved from 0.29% in 2011 to 0.21% in 2012.

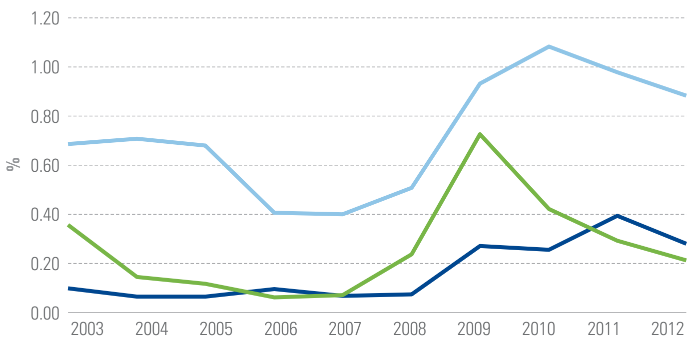
On an individual basis, Kiwibank had a dramatic drop from 2011, decreasing from 0.72% to 0.29%. This decrease has brought Kiwibank's ratio more in line with the ratios of the other major banks, and is a positive sign for a bank still in its growth stage. Part of the reason for the decrease in the ratio was the growth being seen in the loan book, but the main reason for this drop was the decrease in the level of impaired asset expense being seen this year, dropping from $79 million in 2011 to $35 million, a 55.7% decrease.

BNZ and Westpac also saw falls in their ratio. BNZ had a large fall from 0.27% in 2011 to 0.10% in 2012, and Westpac moved from 0.39% to 0.31%. As noted above, the largest driver for BNZ's dramatic drop in the impaired asset expense to average gross loans and advances ratio was the large reduction in impaired asset expense, which dropped by $91 million down to $61 million, a 59.87% decrease.

CBA saw a small decrease over the year, while ANZ's marginally increased, with the increase in impairment expense only slightly offset by growth in lending.

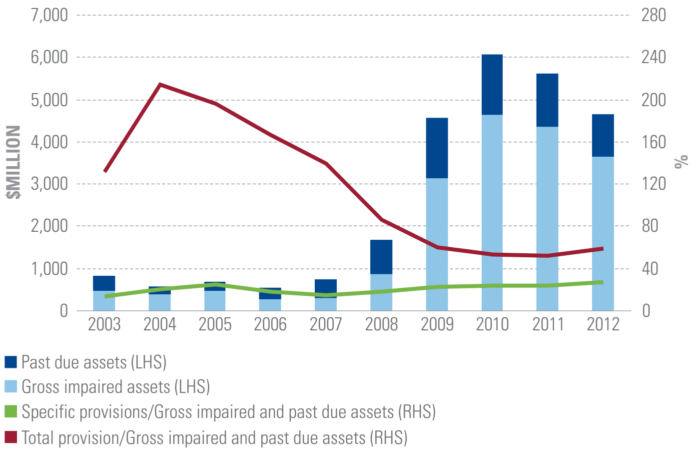
Newly registered The Co-operative Bank also had a favourable movement in its ratio, which dropped from 0.31% to 0.14%. That would be largely driven by the drop in impaired asset expense from $3.5 million in 2011

17 REGISTERED BANKS: IMPAIRED ASSET EXPENSE TO LOANS AND ADVANCES

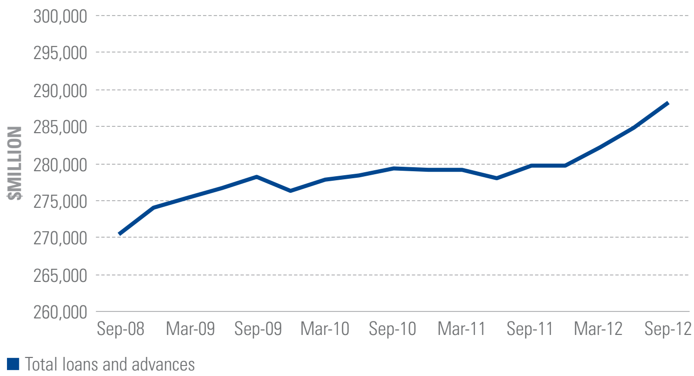


Net loan write offs/Average loans and advances
Total provisions for doubtful debt/Gross loans and advances
Impaired asset expense/Average loans and advances

18 REGISTERED BANKS: GROSS IMPAIRED AND PAST DUE ASSETS



19 MAJOR BANKS: TOTAL LOANS AND ADVANCES



to $1.6 million, a movement of 54.28%, while a slightly increased loan book would also have had a small positive impact on the bank's ratio.

Analysis of lending

Gross loans and advances for the sector have increased this period by $9,744 million to $310,143 million, an increase of 3.2%. This is a trend similar to that observed by the Reserve Bank of New Zealand (RBNZ) which reported increases in the following lending categories; agricultural lending up at 4.4%, business lending up at 4.1% and total household lending up at 2.7%. Figure 20 illustrates that all three lending categories are on an upwards trend as the economy recovers, and demand for credit increases.

Comments from bank executives indicate that while lending portfolios are increasing the growth is hard earned, with competition for good credit prominent. Searching for new lending assets is a must to maintain growth. And holding onto existing customers is very important, as asset run off is high as the deleveraging theme continues again this year.

Households and businesses are taking advantage of the low interest environment in three ways; repaying debt where they can and taking advantage of the competition amongst the banks – and negotiating more favourable pricing with the banks when they make a new borrowing.

The individual performance of the banks varied but growth in lending assets occurred across most. The Bank of Tokyo-Mitsubishi increased by 23.5% to $2,366 million, and Kiwibank continued to maintain growth at an increase of 8.24% to $12,536 million. Quarterly analysis shows that while Kiwibank has experienced good growth over the past 24 months, that growth seems to be slowing.

The big four Australian banks all experienced lending growth in 2012, with increases in gross loans and advances ranging from 1.2% to 3.3%.

Figure 22, displaying credit exposures by sector as at September 2012, shows that mortgages still dominate the lending composition at 52%, followed by other commercial lending at 17% and agriculture, forestry, fishing and mining at 16%. Year on year the sectoral composition has not changed with 3.2% growth in lending assets over the period.

Analysis of funding

The lessons learnt from the GFC by the banks and the regulators have led to banks strengthening their balance sheets and funding sources. This resulted in a change in the composition of funding for banks.

This was illustrated in the 'Reserve Bank of New Zealand: Bulletin, Vol. 75 No.2, June 2012, article *Bank funding – the change in composition and pricing*'; which noted that post the GFC banks have moved away from short-term wholesale debt instruments – such as commercial paper which are typically issued out of the European and US debt markets – to stickier types of funding such as retail deposits and long-term wholesale debt. The need to do this was born out of the effect the GFC had in tightening up global funding markets. Also contributing was new regulation introduced by the RBNZ which stipulates that banks need to hold a minimum core funding ratio of 75% (the ratio increased from 70% to 75% in January 2013). The core funding ratio is calculated as core funding divided by total loans and advances. Wholesale funding broadly needs to have residual maturities of at least 12 months to classify as core funding. Retail deposits classify as core funding even though the maturity profile is less than 12 months because they are considered to be stickier, i.e. the retail deposits will typically rollover at maturity rather than be paid out.

This change in funding composition requirement has been a contributing factor to an increase in customer deposits, which rose by 9.8% in 2012. Other factors contributing to the increase in customer deposits are the deleveraging environment, earthquake insurance payouts and the 'flight to quality'.

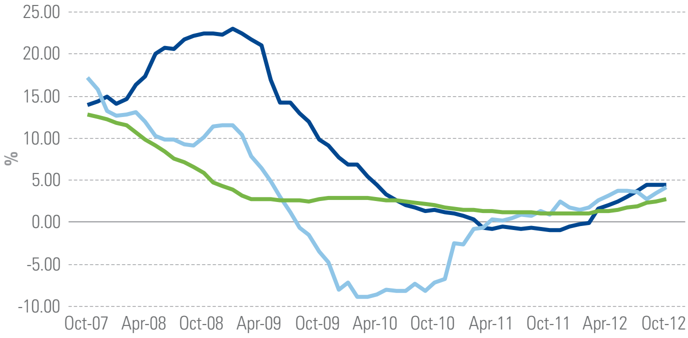
The change in the geographical mix of funding is also a by-product of the lessons learnt from the GFC as the banks look to obtain more funding domestically, and to reduce the reliance on funding which is more volatile and at risk of flight offshore. Year on year, the five major banks have reduced their reliance on offshore funding from 36% in 2011 to 32% in 2012, with the largest percentage change occurring for Westpac and BNZ (which both fell by 8%).

Capital adequacy

The locally incorporated banking sector has an average Total capital ratio of 12.9%, an increase of 50 bps from 12.4% in 2011. The Tier One capital ratio has increased by 90 bps from 10.4% to 11.3%.

All banks are well above the Basel II minimum Tier One and Total capital ratios of 4.0% and 8.0% respectively. However, the new Basel III regulatory capital reforms, applicable from 1 January 2013, have changed not only these minimum requirements but also the categorisation and composition of regulatory capital. From the beginning of 2013, banks will be required to maintain Common Equity Tier One, Tier One and Total capital ratios of 4.5%, 6.0% and 8.0% respectively. These minimum requirements

20 INCREASE IN NEW ZEALAND LENDING (YEAR ON YEAR GROWTH)



Lending – Agriculture (year on year growth)
Lending – Business (year on year growth)
Lending – Total household (year on year growth)
Source: Reserve Bank of New Zealand Statistics

21 INCREASE IN REGISTERED BANK AND NON-BANK BUSINESS LENDING

Registered bank business lending
Non-bank business lending
Source: Reserve Bank of New Zealand Statistics

are increased further at 1 January 2014 with the imposition of a 2.5% capital conservation buffer comprised of Common Equity Tier One capital. If banks encroach upon this buffer, they will be subject to restrictions on their distributions.

Separate analysis of the locally incorporated banks shows a mixture of results, but the overall trend is an increase in their capital adequacy ratios. One of the banks with the largest increase was BNZ, which increased its Total capital ratio by 150 bps from 11.8% to 13.3%. This increase was due to an increase in Tier One capital due to retention of retained profits and a capital issue of $400 million. This increase in Tier One capital was partially offset by a reduction in Tier Two capital as $367 million of subordinated debt was repaid.

Westpac New Zealand Limited also had a good increase in its capital adequacy ratios, with the total capital ratio increasing to 14.1%, an increase of 110 bps. This was driven by a share issue during the year of $1,130 million which funded the reorganisation of its New Zealand operations, transferring exposures from its Branch banking operation to its locally incorporated legal entity (driving the counter increase in the level of risk weighted exposures).

Tier Two capital as a percentage of Total capital has reduced, which was an expected outcome of the Basel III regulatory capital reforms. These have driven a renewed emphasis on higher quality capital and loss absorption capabilities. Existing Tier Two capital instruments lack the capability to absorb losses, and are now unlikely to meet the enhanced recognition and loss absorption criteria. This is leading to a withdrawal of these instruments from the market, rather than amendments to the terms and conditions to make them Basel III complaint.

Funds under management

Funds under management for the major banks have seen a reasonable increase in size over the year, and have recovered well from the fairly flat growth seen in 2011. The increase in 2012 overall is 11.7%, increasing funds under management to $31,490 million (table 6).

The increases being seen in the funds under management will be due both to more funds being placed under management (a result of the deleveraging trend being seen in the economy), and to the returns that these funds generated over the year. The additional funds being placed under management could be due partially to customers regaining some confidence in the market and looking for better returns than are generated in the cash deposit "safe havens". This is an encouraging sign for the economy.

As a note from last year, Kiwibank acquired Gareth Morgan Investments, taking it into the KiwiSaver market. This has been included in table 6, as together with the comparatives for these funds in 2011. On the 1 February 2013, BNZ announced that it would launch its own KiwiSaver product. BNZ had previously partnered with KiwiSaver provider AXA.

All of the major banks saw increases in funds under management over the year. The biggest increases as a percentage were seen by BNZ (19.8%) and Westpac (19.7%). CBA and Kiwibank also experienced fairly good percentage increases over the year, up 15.3% and 16.6% respectively.

While ANZ had the lowest percentage increase over the year, it had the largest gain over the year in absolute terms and it still has the most funds under management in the market by quite a margin, making up roughly half the market.

TABLE 6: MAJOR BANKS: FUNDS MANAGEMENT ACTIVITIES

	2012 $Million	2011 - 2012 Movement %	2011 $Million
ANZ BG	15,685	6.5	14,721
Bank of New Zealand	1,922	19.8	1,604
CBA + ASB	5,925	15.3	5,139
Kiwibank	3,076	16.6	2,638
Westpac	4,882	19.7	4,077
Total	**31,490**	**11.7**	**28,179**

22 REGISTERED BANKS: SECTORAL ANALYSIS OF CREDIT EXPOSURES AS AT 30 SEPTEMBER 2012

Mortgages 52% (2011: 52%)
Agriculture, Forestry, Fishing and Mining 16% (2011: 15%)
Manufacturing 2% (2011: 3%)
Utilities 1% (2011: 1%)
Construction 1% (2011: 1%)
Other commercial lending 17% (2011: 17%)
Finance, investment and insurance 5% (2011: 6%)
Government and public authorities 3% (2011: 2%)
Personal loans 3% (2011: 3%)

Source: RBNZ, C7 Sectoral analysis of outstanding NZD claims: Registered banks (NZ$ million) Enterprise industry divisions – ANZSIC

TABLE 7: FOREIGN EXCHANGE TRADING INCOME	2012 $Million	2011 $Million
ANZ BG	144	137
Bank of New Zealand	84	89
CBA + ASB	18	18
Westpac	85	76
Total	**331**	**320**

TABLE 8: OTHER TRADING INCOME	2012 $Million	2011 $Million
ANZ BG	-13	91
Bank of New Zealand	59	32
CBA + ASB	70	54
Westpac	31	- 22
Total	**147**	**155**

23 HISTORICAL NATIONAL TOTALS: MORTGAGEE SALES BY MONTH

Source: Terralink International Limited

Treasury and trading income

Foreign exchange trading income generated by the major four banks over the year was fairly consistent with that generated in 2011, increasing slightly from $320 million to $331 million.

Whilst foreign exchange trading income was fairly flat between years for each of the big four banks, other trading income had quite extreme fluctuations.

On an overall basis, the movement in other trading income from 2011 seems quite small, as it only fell from $155 million to $147 million. However, on an individual basis, there were large movements in all four of the banks that were offsetting each other to result in this flat overall movement.

The only decrease in other trading income was for ANZ, which saw such a large drop that it offset the other three bank's increases. The fall was $104 million, from $91 million in 2011 to a loss of $13 million. Looking into the items that make up other trading income, this drop was due to a decrease in "gain on trading securities", from $204 million in 2011 to $101 million. The other factor making up other trading income, "net loss on trading derivatives", stayed flat year on year at a loss of $114 million.

This decrease in ANZ fully offset the higher gains seen by BNZ, CBA and Westpac, whose income rose by $27 million, $16 million and $53 million respectively. What the analysis above shows is the volatility in the markets and around the pricing of the instruments used in hedging and trading, and the impact that this volatility can have on earnings.

The major banks have seen a fall in the nominal value of the derivatives they hold over the year. Most of this decrease is being seen in the interest rate contracts, with the overall nominal value of exchange rate contracts being fairly flat over the year.

Looking at the interest rate contracts on an individual bank level, the largest fall was experienced by ANZ. The nominal value of its contracts fell from $763 billion to $625 billion, a decrease of $138 billion or 18%. As ANZ has the largest proportion of derivatives held, any decrease by ANZ heavily influences the overall trend being seen. ANZ's large drop is mainly occurring in the interest rate swaps market, where there has been a decrease of $106 billion. However, we expect the banks and customers to increase their use of these instruments in the coming year, as interest rate hikes are forecast to occur late 2013 or early 2014. These instruments will be used to hedge interest rate risk, as the expectation of rate rises increases.

TABLE 9: MAJOR BANKS: DERIVATIVE CONTRACTS

	Year	Interest rate contracts					Exchange rate contracts			
		Forwards $Million	Swaps $Million	Futures $Million	Options $Million	Total $Million	Forwards $Million	Swaps $Million	Options $Million	Total $Million
ANZ BG	2012	45,071	546,039	29,818	4,070	624,998	59,825	133,033	3,449	196,307
	2011	*73,346*	*651,803*	*26,272*	*11,069*	*762,490*	*62,682*	*126,389*	*4,551*	*193,622*
Bank of New Zealand	2012	6,661	201,196	117,618	775	326,250	40,729	41,153	2,250	84,132
	2011	*4,555*	*237,039*	*23,123*	*4,081*	*268,798*	*37,300*	*42,528*	*5,751*	*85,579*
CBA + ASB	2012	5,248	79,658	2,001	190	87,097	13,205	12,048	237	25,490
	2011	*9,360*	*77,033*	*1,485*	*88*	*87,966*	*7,794*	*15,296*	*59*	*23,149*
Kiwibank	2012	200	14,840	975	-	16,015	1,013	457	11	1,481
	2011	*200*	*8,744*	*1,301*	-	*10,245*	*650*	*513*	-	*1,163*
Westpac	2012	2,354	174,595	5,827	1,895	184,671	21,232	30,015	-	51,247
	2011	*1,333*	*185,383*	*12,160*	*4,102*	*202,978*	*23,846*	*26,879*	-	*50,725*
Total	**2012**	**59,534**	**1,016,328**	**156,239**	**6,930**	**1,239,031**	**136,004**	**216,706**	**5,947**	**358,657**
	2011	***88,794***	***1,160,002***	***64,341***	***19,340***	***1,332,477***	***132,272***	***211,605***	***10,361***	***354,238***

Performance rankings

RANKING OF NEW ZEALAND INCORPORATED BANKS[a]

	Total assets	$Million	Increase in total assets	%	Capital adequacy ratio	%	Net profit after tax	$Million	Increase in net profit after tax	%	Net profit after tax/ Average equity	%	Net interest income/ Average total assets	%	Impaired asset expense/ Average gross loans & advances	%	Operating expenses/ Operating Income	%
1	ANZ Bank New Zealand Limited	118,047	Bank of Baroda (New Zealand) Limited	14.44	Bank of India (New Zealand) Limited	259.00	ANZ Bank New Zealand Limited	1,325	Kiwibank Limited	272.15	ASB Bank Limited	16.84	Bank of India (New Zealand) Limited	3.54	ASB Bank Limited	0.09	TSB Bank Limited	40.24
2	Bank of New Zealand	72,945	Westpac New Zealand Limited	13.57	Bank of Baroda (New Zealand) Limited	149.90	ASB Bank Limited	685	Bank of Baroda (New Zealand) Limited	258.25	TSB Bank Limited	12.69	Bank of Baroda (New Zealand) Limited	3.18	Bank of New Zealand	0.10	ASB Bank Limited	41.02
3	Westpac New Zealand Limited	68,345	Bank of India (New Zealand) Limited	9.77	The Co-operative Bank Limited	17.50	Westpac New Zealand Limited	613	Westpac New Zealand Limited	41.57	ANZ Bank New Zealand Limited	12.18	The Co-operative Bank Limited	2.75	TSB Bank Limited	0.13	Westpac New Zealand Limited	41.43
4	ASB Bank Limited	63,489	Rabobank New Zealand Limited	9.59	TSB Bank Limited	15.42	Bank of New Zealand	580	ASB Bank Limited	20.60	Bank of New Zealand	12.05	Rabobank New Zealand Limited	2.73	The Co-operative Bank Limited	0.14	ANZ Bank New Zealand Limited	46.01
5	Kiwibank Limited	14,745	TSB Bank Limited	6.49	Southland Building Society	14.40	Kiwibank Limited	79	ANZ Bank New Zealand Limited	20.56	Westpac New Zealand Limited	11.91	Southland Building Society	2.47	ANZ Bank New Zealand Limited	0.22	Bank of New Zealand	46.35
6	Rabobank New Zealand Limited	7,867	Kiwibank Limited	6.29	Westpac New Zealand Limited	14.10	Rabobank New Zealand Limited	54	TSB Bank Limited	20.03	Kiwibank Limited	11.66	Westpac New Zealand Limited	2.33	Kiwibank Limited	0.29	Rabobank New Zealand Limited	46.36
7	TSB Bank Limited	5,165	Southland Building Society	1.00	Bank of New Zealand	13.29	TSB Bank Limited	48	Bank of New Zealand	-13.56	Rabobank New Zealand Limited	8.09	ANZ Bank New Zealand Limited	2.27	Bank of Baroda (New Zealand) Limited	0.32	Southland Building Society	53.88
8	Southland Building Society	2,841	ASB Bank Limited	0.77	ASB Bank Limited	12.60	Southland Building Society	12	Southland Building Society	-17.44	Southland Building Society	5.64	ASB Bank Limited	2.06	Westpac New Zealand Limited	0.34	Kiwibank Limited	61.34
9	The Co-operative Bank Limited	1,451	ANZ Bank New Zealand Limited	0.03	ANZ Bank New Zealand Limited	12.48	The Co-operative Bank Limited	6	The Co-operative Bank Limited	-20.22	The Co-operative Bank Limited	4.47	TSB Bank Limited	2.06	Rabobank New Zealand Limited	0.44	Bank of Baroda (New Zealand) Limited	71.06
10	Bank of Baroda (New Zealand) Limited	61	The Co-operative Bank Limited	-0.06	Rabobank New Zealand Limited	11.13	Bank of Baroda (New Zealand) Limited	1	Rabobank New Zealand Limited	-25.20	Bank of Baroda (New Zealand) Limited	1.71	Bank of New Zealand	2.05	Bank of India (New Zealand) Limited	0.78	The Co-operative Bank Limited	85.01
11	Bank of India (New Zealand) Limited	55	Bank of New Zealand	-1.34	Kiwibank Limited	10.80	Bank of India (New Zealand) Limited	0	Bank of India (New Zealand) Limited	-89.07	Bank of India (New Zealand) Limited	0.04	Kiwibank Limited	1.80	Southland Building Society	0.87	Bank of India (New Zealand) Limited	94.88
	Incorporated total	**355,011**	**Incorporated total**	**2.78**	**Incorporated total**	**12.99**	**Incorporated total**	**3,403**	**Incorporated total**	**16.27**	**Incorporated total**	**12.58**	**Incorporated total**	**2.19**	**Incorporated total**	**0.21**	**Incorporated total**	**45.24**

RANKING OF NEW ZEALAND BRANCH BANKS[b], [c]

	Total assets	$Million	Increase in total assets	%	Capital adequacy ratio	%	Net profit after tax	$Million	Increase in net profit after tax	%	Net profit after tax/ Average equity	%	Net interest income/ Average total assets	%	Impaired asset expense/ Average gross loans & advances	%	Operating expenses/ Operating Income	%
1	Westpac Banking Corporation New Zealand Branch	17,851	JPMorgan Chase Bank, N.A. New Zealand Branch	112.81	Rabobank Nederland New Zealand Branch	17.50	Westpac Banking Corporation New Zealand Branch	196	JPMorgan Chase Bank, N.A. New Zealand Branch	182.21	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	174.89	JPMorgan Chase Bank, N.A. New Zealand Branch	2.28	Westpac Banking Corporation New Zealand Branch	-0.14	Rabobank Nederland New Zealand Branch	3.11
2	Commonwealth Bank of Australia New Zealand Branch	10,051	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	25.25	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	16.27	ANZ Banking Group New Zealand Branch	50	Rabobank Nederland New Zealand Branch	146.69	JPMorgan Chase Bank, N.A. New Zealand Branch	119.34	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	1.66	JPMorgan Chase Bank, N.A. New Zealand Branch	0.00	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	12.47
3	ANZ Banking Group New Zealand Branch	9,798	Rabobank Nederland New Zealand Branch	15.45	Citibank, N.A. New Zealand Branch	16.20	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	39	Deutsche Bank AG, New Zealand Group	141.51	Kookmin Bank Auckland Branch	66.01	Citibank, N.A. New Zealand Branch	1.61	Citibank, N.A. New Zealand Branch	0.00	Commonwealth Bank of Australia New Zealand Branch	12.50
4	Rabobank Nederland New Zealand Branch	6,534	Commonwealth Bank of Australia New Zealand Branch	1.05	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	14.60	Commonwealth Bank of Australia New Zealand Branch	36	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	28.79	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	31.08	Kookmin Bank Auckland Branch	1.54	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	0.00	JPMorgan Chase Bank, N.A. New Zealand Branch	15.56
5	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	4,921	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	-1.61	Deutsche Bank AG, New Zealand Group	14.50	Rabobank Nederland New Zealand Branch	35	Commonwealth Bank of Australia New Zealand Branch	28.57	Rabobank Nederland New Zealand Branch	26.28	Rabobank Nederland New Zealand Branch	1.45	Rabobank Nederland New Zealand Branch	0.02	Westpac Banking Corporation New Zealand Branch	16.04
6	Deutsche Bank AG, New Zealand Group	3,093	Kookmin Bank Auckland Branch	-2.72	Kookmin Bank Auckland Branch	13.55	JPMorgan Chase Bank, N.A. New Zealand Branch	27	Citibank, N.A. New Zealand Branch	15.86	Australia and New Zealand Banking Group Limited – New Zealand Branch	24.75	Australia and New Zealand Banking Group Limited – New Zealand Branch	1.22	Australia and New Zealand Banking Group Limited – New Zealand Branch	0.09	Australia and New Zealand Banking Group Limited – New Zealand Branch	25.71
7	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	2,574	Deutsche Bank AG, New Zealand Group	-5.76	JPMorgan Chase Bank, N.A. New Zealand Branch	13.04	Deutsche Bank AG, New Zealand Group	22	ANZ Banking Group New Zealand Branch	13.64	Deutsche Bank AG, New Zealand Group	22.22	Westpac Banking Corporation New Zealand Branch	0.85	Commonwealth Bank of Australia New Zealand Branch	0.70	Kookmin Bank Auckland Branch	27.55
8	Citibank, N.A. New Zealand Branch	2,148	ANZ Banking Group New Zealand Branch	-6.23	ANZ Banking Group New Zealand Branch	12.20	Citibank, N.A. New Zealand Branch	18	Westpac Banking Corporation New Zealand Branch	-26.59	Citibank, N.A. New Zealand Branch	11.67	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	0.55	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	0.74	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	43.71
9	JPMorgan Chase Bank, N.A. New Zealand Branch	1,006	Citibank, N.A. New Zealand Branch	-19.90	Westpac Banking Corporation New Zealand Branch	11.70	The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	17	The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	-29.88	Westpac Banking Corporation New Zealand Branch	7.17	Deutsche Bank AG, New Zealand Group	0.53	Kookmin Bank Auckland Branch	1.07	Citibank, N.A. New Zealand Branch	47.36
10	Kookmin Bank Auckland Branch	427	Westpac Banking Corporation New Zealand Branch	-22.38	Commonwealth Bank of Australia New Zealand Branch	11.00	Kookmin Bank Auckland Branch	4	Kookmin Bank Auckland Branch	-39.47	Commonwealth Bank of Australia New Zealand Branch	5.91	Commonwealth Bank of Australia New Zealand Branch	0.44	Deutsche Bank AG, New Zealand Group	5.00	Deutsche Bank AG, New Zealand Group	53.41
	Branch total	**58,403**	**Branch total**	**-7.27**	**Branch total**	**n/a**	**Branch total**	**444**	**Branch total**	**10.71**	**Branch total**	**10.97**	**Branch total**	**1.00**	**Branch total**	**0.27**	**Branch total**	**25.58**

Key: n/a = not available/applicable. Branch total capital adequacy ratio cannot be calculated as ratio is obtained from the overseas banking group.

Footnotes

(a) Incorporated Banks – for the purposes of aiding comparison we have separated certain banking groups to report the locally incorporated entity in the performance rankings as a New Zealand incorporated bank; ANZ Bank New Zealand Limited, ASB Bank Limited, Westpac New Zealand Limited and Rabobank New Zealand Limited.

(b) Branch Banks – for the purposes of aiding comparison we have separated certain branch banks from its locally incorporated entities for presentation in the performance rankings as a New Zealand branch bank; Australia and New Zealand Banking Group Limited New Zealand Branch, Commonwealth Bank of Australia New Zealand Branch, Westpac Banking Corporation New Zealand Branch (separate from the New Zealand Division) and Rabobank Nederland New Zealand Branch. Rabobank Nederland New Zealand Branch's head office account, which comprises current period and cumulative surpluses, has been reclassified from liability to equity for consistency with other banks. This has impacted certain ratios.

(c) The capital adequacy ratio disclosed is for the overseas banking group.

gold silver bronze

Analysis of financial statements

ANALYSIS OF ANNUAL RESULTS OF REGISTERED BANKS[a]					Size & strength measures									Growth measures		
	Location of head office	Balance date	Year	Rank by total assets	Total assets * $Million	Net assets[h] $Million	Total capital adequacy ratio[i] %	Tier 1 capital adequacy ratio[i] %	Net loans and advances $Million	Customer deposits $Million	Number of employees[j] #	Number of branches[k] #	Number of owned ATMs[l] #	Increase In net profit after tax %	Increase In underlying profit %	Increase in total assets %
Australia and New Zealand Banking Group Limited – New Zealand Banking Group[b]	Wellington	30-Sep	2012	1	127,469	5,778	12.20	10.80	96,710	64,490	9,183	312	736	16.59	7.33	-0.48
		30-Sep	*2011*		*128,089*	*5,043*	*12.10*	*10.90*	*94,248*	*60,421*	*9,551*	*314*	*770*	*25.14*	*20.53*	*3.66*
Bank of Baroda (New Zealand) Limited	Auckland	31-Mar	2012	16	61	41	149.90	149.90	19	19	16	3	3	258.25	258.25	14.44
		31-Mar	*2011*		*53*	*40*	*230.90*	*230.90*	*8*	*12*	*11*	*1*	*1*	*102.91*	*102.91*	*31.97*
Bank of India (New Zealand) Limited	Auckland	31-Mar	2012	17	55	50	259.00	259.00	5	3	8	1	0	-89.07	-70.99	9.77
		31-Mar	*2011*		*50*	*50*	*419.00*	*419.00*	*0*	*0*	*7*	*1*	*0*	*0.00*	*0.00*	*0.00*
Bank of New Zealand	Wellington	30-Sep	2012	3	72,945	5,111	13.29	11.26	59,204	37,090	4,611	178	459	-13.56	-16.48	-1.34
		30-Sep	*2011*		*73,933*	*4,197*	*11.84*	*8.99*	*57,262*	*33,218*	*4,726*	*179*	*445*	*11.46*	*50.08*	*6.18*
Citibank, N.A. New Zealand Branch[c]	Auckland	31-Dec	2011	12	2,148	165	16.20	14.70	783	1,037	38	1	0	15.86	9.10	-19.90
		31-Dec	*2010*		*2,682*	*146*	*17.06*	*15.17*	*377*	*1,281*	*37*	*1*	*0*	*-26.30*	*-24.12*	*-23.39*
Commonwealth Bank of Australia New Zealand Banking Group[d]	Auckland	30-Jun	2012	4	69,192	4,174	11.00	10.00	57,258	39,067	4,695	145	483	19.33	14.14	1.23
		30-Jun	*2011*		*68,351*	*3,859*	*11.70*	*10.00*	*56,604*	*33,713*	*4,674*	*144*	*461*	*94.81*	*15.86*	*-1.82*
Deutsche Bank AG, New Zealand Group[e]	Auckland	31-Dec	2011	9	3,093	110	14.50	12.90	291	159	34	1	0	141.51	141.67	-5.76
		31-Dec	*2010*		*3,282*	*88*	*14.10*	*12.30*	*101*	*491*	36	1	0	*-163.10*	*-161.54*	*5.91*
JPMorgan Chase Bank, N.A. New Zealand Branch[f]	Wellington	31-Dec	2011	14	1,006	36	13.04	9.44	46	148	13	1	0	182.21	220.26	112.81
		31-Dec	*2010*		*473*	*7*	*13.50*	*9.50*	*0*	*126*	*15*	*1*	*0*	*513.18*	*684.28*	*186.94*
Kiwibank Limited	Wellington	30-Jun	2012	5	14,745	747	10.80	10.40	12,495	11,551	1,024	281	286	272.15	164.86	6.29
		30-Jun	*2011*		*13,873*	*606*	*10.50*	*9.00*	*11,532*	*10,571*	*1,029*	*288*	*284*	*-53.70*	*-40.01*	*13.38*
Kookmin Bank Auckland Branch	Auckland	31-Dec	2011	15	427	4	13.55	10.30	146	124	12	1	0	-39.47	-41.12	-2.72
		31-Dec	*2010*		*439*	*7*	*13.44*	*10.89*	*143*	*108*	*12*	*1*	*0*	*-19.02*	*-20.22*	*1.69*
Rabobank Nederland New Zealand Banking Group[g]	Wellington	31-Dec	2011	6	10,495	807	17.50	17.00	9,517	4,126	288	32	0	2.44	-7.01	11.07
		31-Dec	*2010*		*9,449*	*720*	*16.30*	*15.70*	*8,839*	*4,050*	*256*	*30*	*0*	*-25.84*	*3.59*	*6.12*
Southland Building Society	Invercargill	31-Mar	2012	10	2,841	214	14.35	12.52	2,435	2,477	372	16	0	-17.44	-22.55	1.00
		31-Mar	*2011*		*2,813*	*201*	*13.60*	*11.26*	*2,594*	*2,398*	*353*	*17*	*0*	*-5.23*	*10.63*	*7.08*
The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	Auckland	31-Mar	2012	11	2,574	95	16.27	11.76	2,366	59	16	1	0	28.79	11.85	25.25
		31-Mar	*2011*		*2,055*	*12*	*15.82*	*11.42*	*1,916*	*61*	*14*	*1*	*0*	*17.32*	*27.64*	*30.69*
The Co-operative Bank Limited	Wellington	31-Mar	2012	13	1,451	130	17.50	17.20	1,209	1,213	297	31	0	-20.22	-24.43	-0.06
		31-Mar	*2011*		*1,452*	*124*	*17.30*	*16.90*	*1,167*	*1,163*	*295*	*31*	*0*	*-45.87*	*-41.48*	*4.04*
The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	Auckland	31-Dec	2011	8	4,921	-1	14.60	12.40	3,433	3,092	241	3	0	-29.88	-31.66	-1.61
		31-Dec	*2010*		*5,002*	*9*	*14.70*	*11.70*	*3,129*	*2,427*	*239*	*3*	*0*	*10.76*	*11.71*	*5.29*
TSB Bank Limited	New Plymouth	31-Mar	2012	7	5,165	396	15.42	15.42	2,757	4,715	270	24	43	20.03	11.17	6.49
		31-Mar	*2011*		*4,850*	*358*	*15.78*	*15.78*	*2,642*	*4,442*	*241*	*25*	*47*	*-22.14*	*-18.91*	*10.10*
Westpac Banking Corporation – New Zealand Division	Auckland	30-Sep	2012	2	77,329	4,990	11.70	10.30	60,222	41,967	4,856	205	529	13.96	7.39	-0.56
		30-Sep	*2011*		*77,768*	*4,236*	*11.00*	*9.70*	*58,513*	*38,019*	*4,853*	*205*	*529*	*-12.71*	*17.21*	*7.63*
Bank sector total			**2012**		**395,918**	**22,846**	**n/c**	**n/c**	**308,896**	**211,338**	**25,974**	**1,236**	**2,539**	**13.64**	**6.85**	**0.33**
			2011		***394,613***	***19,703***	***n/c***	***n/c***	***299,074***	***192,501***	***26,349***	***1,243***	***2,537***	***9.78***	***15.74***	***4.34***
ANZ Bank New Zealand Limited	Wellington	30-Sep	2012		118,047	7,530	12.48	10.80	87,278	64,490	8,500	312	736	20.56	11.19	0.03
		30-Sep	*2011*		*118,015*	*7,400*	*12.74*	*10.02*	*84,235*	*60,421*	*8,773*	*314*	*770*	*32.89*	*27.52*	*4.45*
ASB Bank Limited	Auckland	30-Jun	2012		63,489	4,139	12.60	11.70	53,142	39,297	4,675	145	483	20.60	15.27	0.77
		30-Jun	*2011*		*63,002*	*3,899*	*12.80*	*11.20*	*52,513*	*34,072*	*4,652*	*144*	*461*	*140.68*	*25.74*	*-0.80*
Australia and New Zealand Banking Group Limited – New Zealand Branch	Wellington	30-Sep	2012		9,798	227	12.20	10.80	9,412	0	3	1	0	13.64	9.52	-6.23
		30-Sep	*2011*		*10,449*	*177*	*12.10*	*10.90*	*9,941*	*0*	*3*	*1*	*0*	*-53.19*	*-53.33*	*-3.88*
Commonwealth Bank of Australia New Zealand Branch	Auckland	30-Jun	2012		10,051	638	11.00	10.00	4,037	55	20	1	0	28.57	25.00	1.05
		30-Jun	*2011*		*9,947*	*581*	*11.70*	*10.00*	*3,612*	*108*	*22*	*1*	*0*	*-53.33*	*-51.81*	*-10.37*
Rabobank Nederland New Zealand Branch	Wellington	31-Dec	2011		6,534	150	17.50	17.00	1,730	1,162	n/a	1	0	146.69	116.63	15.45
		31-Dec	*2010*		*5,660*	*115*	*16.30*	*15.70*	*1,728*	*1,372*	*n/a*	*1*	*0*	*3.25*	*-4.05*	*-11.55*
Rabobank New Zealand Limited	Wellington	31-Dec	2011		7,867	692	11.13	7.67	7,786	2,965	288	32	0	-25.20	-31.17	9.59
		31-Dec	*2010*		*7,178*	*638*	*12.11*	*8.22*	*7,053*	*2,676*	*256*	*30*	*0*	*747.43*	*747.99*	*3.49*
Westpac Banking Corporation New Zealand Branch	Auckland	30-Sep	2012		17,851	2,797	11.70	10.30	386	0	160	1	0	-26.59	-22.06	-22.38
		30-Sep	*2011*		*22,997*	*2,671*	*11.00*	*9.70*	*6,837*	*4,689*	*240*	*1*	*0*	*-27.84*	*-6.68*	*4.25*
Westpac New Zealand Limited	Auckland	30-Sep	2012		68,345	5,319	14.10	12.00	59,751	41,967	4,696	205	529	41.57	33.48	13.57
		30-Sep	*2011*		*60,179*	*4,019*	*13.00*	*10.50*	*51,599*	*33,330*	*4,613*	*205*	*529*	*51.40*	*45.77*	*10.01*

Key: *Total assets = Total assets – Goodwill and other intangible assets (excluding software).
n/c = not able to calculate sector average capital adequacy ratios as some banking group entities' ratios are obtained from the overseas banking group
n/a = not available

Footnotes

Changes in accounting policy that have not had a material impact on the financial statements have not been detailed in the following footnotes. The effect of the changes listed below has been to impact certain ratios, or lead to the omission of certain ratios.

Where comparatives are not for the equivalent period, or the entity was not operational in either period, performance details have not been provided.

(a) If in its latest published financials an entity has changed its comparative year figures we have restated the numbers accordingly.

(b) Figures are for the New Zealand Banking Group, which comprises the aggregated New Zealand operations of Australia and New Zealand Banking Group Limited, including those operations conducted through the New Zealand Branch and the ANZ Bank New Zealand Limited Group.
Consolidated accounts for ANZ Bank New Zealand Limited include the results of UDC Finance Limited, which is also shown separately within the Finance Companies section.

(c) Figures are for the New Zealand Banking Group, which comprises Citibank, N.A. New Zealand Branch and Citicorp Services Limited and its subsidiaries.

(d) Figures are for the New Zealand Banking Group, which comprises Commonwealth Bank of Australia New Zealand Branch including various controlled entities and the ASB Banking Group Operations comprising ASB Bank Limited, ASB Holdings Limited and ASB Funding Limited.

(e) Figures are for the New Zealand Banking Group, which comprises Deutsche Bank AG New Zealand Branch, Deutsche New Zealand Limited, in-substance subsidiaries and other New Zealand subsidiaries of Deutsche New Zealand Limited.

(f) Figures shown are for the New Zealand Banking Group, which comprises JPMorgan Chase Bank New Zealand and associated entities.

(g) Figures are for the New Zealand Banking Group, which comprises Rabobank Nederland New Zealand Branch, Rabobank New Zealand Limited and various subsidiaries. Rabobank Nederland New Zealand Branch's head office account, which comprises current period and cumulative surpluses, has been reclassified from liability to equity for consistency with other banks. This has impacted certain ratios.

(h) Net assets represent total equity less goodwill and other intangibles.

(i) Risk weighted assets and capital adequacy ratios are as at the applicable balance sheet date. Capital adequacy ratios for the branch banks relate to either the overseas bank or the overseas banking group, whichever is publicly available, but where both are available the overseas banking group will be presented.

(j) Employee numbers are on a full time equivalent basis (including casuals and contracting staff) as at the applicable balance sheet date.

(k) Number of branches includes all retail outlets as at the applicable balance sheet date.

(l) Number of owned ATMs as at the applicable balance sheet date.

Analysis of financial statements

ANALYSIS OF ANNUAL RESULTS OF REGISTERED BANKS[a] (CONTINUED)		Credit quality measures							Profitability measures										Efficiency measures	
	Year	Impaired asset expense $Million	Past due assets $Million	Gross impaired assets $Million	Individual provision for doubtful debts/ Gross impaired assets %	Collective provision/ Net loans and advances %	Total provision for doubtful debts/Gross loans and advances %	Impaired asset expense/ Average gross loans and advances %	Total operating income $Million	Net interest income/ Average total assets %	Interest margin %	Interest spread %	Non-interest income/ Average total assets %	Net profit after tax $Million	Net profit after tax/ Average equity %	Net profit after tax/ Average total assets %	Underlying profit $Million	Underlying profit/ Average total assets %	Operating expenses[h]/ Average total assets %	Operating expenses[h]/ Operating income %
Australia and New Zealand Banking Group Limited – New Zealand Banking Group[b]	2012	202	226	1,405	32.81	0.64	1.11	0.21	3,614	2.12	2.44	2.08	0.71	1,265	14.34	0.99	1,714	1.34	1.33	46.98
	2011	*190*	*307*	*1,792*	*28.52*	*0.71*	*1.25*	*0.20*	*3,409*	*2.07*	*2.39*	*2.08*	*0.64*	*1,085*	*13.32*	*0.86*	*1,597*	*1.27*	*1.29*	*47.58*
Bank of Baroda (New Zealand) Limited	2012	0	0	0	0.00	0.40	0.40	0.32	3	3.18	3.30	-0.83	1.31	1	1.71	1.22	1	1.22	3.19	71.06
	2011	*0*	*0*	*0*	*0.00*	*0.40*	*0.40*	*0.80*	*2*	*3.26*	*3.34*	*-0.07*	*0.57*	*0*	*0.48*	*0.42*	*0*	*0.42*	*3.34*	*87.30*
Bank of India (New Zealand) Limited	2012	0	0	0	0.00	0.39	0.39	0.78	2	3.54	3.60	2.41	0.04	0	0.04	0.04	0	0.14	3.40	94.88
	2011	*0*	*0*	*0*	*0.00*	*0.00*	*0.00*	*0.00*	*0*	*0.00*	*0.00*	*0.00*	*0.00*	*0*	*0.00*	*0.00*	*0*	*0.00*	*0.00*	*34.17*
Bank of New Zealand	2012	61	250	459	40.31	0.48	0.79	0.10	1,644	2.05	2.32	2.03	0.19	580	12.05	0.79	821	1.12	1.04	46.35
	2011	*152*	*202*	*659*	*34.45*	*0.49*	*0.88*	*0.27*	*1,889*	*1.93*	*2.19*	*1.92*	*0.70*	*671*	*16.07*	*0.93*	*983*	*1.37*	*1.05*	*39.92*
Citibank, N.A. New Zealand Branch[c]	2011	0	0	0	0.00	0.00	0.00	0.00	48	1.61	1.63	1.52	0.37	18	11.67	0.75	25	1.04	0.94	47.36
	2010	*0*	*0*	*0*	*0.00*	*0.00*	*0.00*	*0.00*	*42*	*1.28*	*1.29*	*1.23*	*0.07*	*16*	*11.33*	*0.51*	*23*	*0.75*	*0.61*	*44.80*
Commonwealth Bank of Australia New Zealand Banking Group[d]	2012	74	219	301	33.55	0.26	0.44	0.13	1,812	1.94	2.05	1.68	0.69	716	16.50	1.04	1,017	1.48	1.05	39.79
	2011	*87*	*336*	*355*	*23.66*	*0.33*	*0.47*	*0.15*	*1,684*	*1.80*	*1.88*	*1.46*	*0.64*	*600*	*15.00*	*0.87*	*891*	*1.29*	*1.02*	*41.92*
Deutsche Bank AG, New Zealand Group[e]	2011	11	0	11	100.00	0.00	3.64	5.00	88	0.53	0.58	0.51	2.23	22	22.22	0.69	30	0.94	1.47	53.41
	2010	*76*	*0*	*37*	*100.00*	*0.00*	*26.81*	*43.30*	*42*	*2.76*	*3.01*	*2.90*	*-1.44*	*-53*	*-36.55*	*-1.66*	*-72*	*-2.26*	*1.19*	*90.48*
JPMorgan Chase Bank, N.A. New Zealand Branch[f]	2011	0	0	0	0.00	0.00	0.00	0.00	51	2.28	3.15	2.67	4.67	27	119.34	3.59	43	5.88	1.08	15.56
	2010	*0*	*0*	*0*	*0.00*	*0.00*	*0.00*	*0.00*	*22*	*3.45*	*4.52*	*4.02*	*3.35*	*9*	*220.66*	*2.95*	*14*	*4.26*	*2.54*	*37.34*
Kiwibank Limited	2012	35	36	84	48.81	0.40	0.73	0.29	419	1.80	1.82	1.42	1.13	79	11.66	0.55	127	0.89	1.80	61.34
	2011	*79*	*33*	*106*	*47.35*	*0.32*	*0.75*	*0.72*	*353*	*1.47*	*1.48*	*1.16*	*1.24*	*21*	*3.55*	*0.16*	*48*	*0.37*	*1.73*	*64.04*
Kookmin Bank Auckland Branch	2011	2	0	2	0.00	0.00	0.00	1.07	9	1.54	1.54	1.52	0.54	4	66.01	0.82	5	1.15	0.57	27.55
	2010	*0*	*0*	*0*	*0.00*	*0.00*	*0.00*	*0.04*	*11*	*2.00*	*2.01*	*1.98*	*0.62*	*6*	*78.27*	*1.35*	*8*	*1.94*	*0.66*	*25.25*
Rabobank Nederland New Zealand Banking Group[g]	2011	33	65	396	27.03	0.31	1.42	0.36	255	3.01	3.08	2.69	-0.45	86	11.31	0.87	127	1.28	0.95	37.14
	2010	*34*	*76*	*391*	*29.77*	*0.22*	*1.52*	*0.39*	*242*	*3.59*	*3.69*	*3.38*	*-0.95*	*84*	*15.96*	*0.92*	*137*	*1.49*	*0.79*	*29.74*
Southland Building Society	2012	22	12	41	49.13	0.38	1.20	0.87	88	2.47	2.51	2.19	0.64	12	5.64	0.42	19	0.66	1.68	53.88
	2011	*17*	*6*	*38*	*33.07*	*0.35*	*0.83*	*0.67*	*87*	*2.34*	*2.37*	*2.04*	*0.86*	*14*	*7.51*	*0.52*	*24*	*0.88*	*1.69*	*52.77*
The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	2012	0	0	0	0.00	0.00	0.00	0.00	23	0.55	0.57	0.52	0.45	17	31.08	0.72	20	0.87	0.12	12.47
	2011	*0*	*0*	*0*	*0.00*	*0.00*	*0.00*	*0.00*	*21*	*0.67*	*0.69*	*0.67*	*0.47*	*13*	*114.36*	*0.71*	*18*	*0.99*	*0.15*	*12.99*
The Co-operative Bank Limited	2012	2	3	5	28.24	0.23	0.34	0.14	61	2.75	2.78	2.41	1.45	6	4.47	0.39	8	0.52	3.57	85.01
	2011	*4*	*1*	*5*	*21.21*	*0.28*	*0.37*	*0.31*	*62*	*3.02*	*3.07*	*2.67*	*1.34*	*7*	*5.90*	*0.50*	*10*	*0.70*	*3.42*	*78.27*
The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	2011	25	0	75	54.78	0.05	1.24	0.74	143	1.66	1.74	1.60	1.22	39	174.89	0.79	56	1.13	1.26	43.71
	2010	*11*	*0*	*72*	*25.65*	*0.06*	*0.64*	*0.34*	*150*	*1.84*	*1.91*	*1.75*	*1.24*	*56*	*205.86*	*1.15*	*82*	*1.68*	*1.16*	*37.81*
TSB Bank Limited	2012	3	7	5	37.51	0.60	0.67	0.13	118	2.06	2.07	1.60	0.30	48	12.69	0.96	67	1.34	0.95	40.24
	2011	*3*	*8*	*4*	*27.69*	*0.61*	*0.65*	*0.13*	*106*	*2.00*	*2.02*	*1.49*	*0.28*	*40*	*11.56*	*0.86*	*61*	*1.31*	*0.90*	*39.54*
Westpac Banking Corporation – New Zealand Division	2012	184	184	868	31.91	0.55	1.00	0.31	2,108	1.97	2.21	1.81	0.75	759	14.77	0.98	1,090	1.41	1.08	39.56
	2011	*226*	*256*	*919*	*28.94*	*0.68*	*1.13*	*0.39*	*2,044*	*2.04*	*2.30*	*1.91*	*0.68*	*666*	*14.98*	*0.89*	*1,015*	*1.35*	*1.07*	*39.29*
Bank sector total	**2012**	**653**	**1,002**	**3,651**	**34.17**	**0.48**	**0.88**	**0.21**	**10,486**	**2.03**	**2.25**	**1.90**	**0.62**	**3,678**	**14.30**	**0.93**	**5,170**	**1.31**	**1.18**	**44.47**
	2011	***879***	***1,225***	***4,378***	***30.26***	***0.54***	***0.98***	***0.29***	***10,166***	***2.00***	***2.22***	***1.89***	***0.63***	***3,236***	***14.10***	***0.84***	***4,839***	***1.25***	***1.15***	***43.76***
ANZ Bank New Zealand Limited	2012	193	210	1,366	32.94	0.69	1.20	0.22	3,688	2.27	2.65	2.18	0.85	1,325	12.18	1.12	1,798	1.52	1.44	46.01
	2011	*178*	*288*	*1,726*	*28.62*	*0.79*	*1.36*	*0.21*	*3,415*	*2.22*	*2.59*	*2.12*	*0.74*	*1,099*	*10.33*	*0.95*	*1,617*	*1.40*	*1.40*	*47.44*
ASB Bank Limited	2012	47	219	251	30.68	0.26	0.41	0.09	1,731	2.06	2.16	1.76	0.68	685	16.84	1.08	974	1.54	1.12	41.02
	2011	*72*	*336*	*342*	*22.81*	*0.31*	*0.46*	*0.14*	*1,613*	*1.93*	*2.01*	*1.55*	*0.62*	*568*	*15.16*	*0.90*	*845*	*1.34*	*1.10*	*43.15*
Australia and New Zealand Banking Group Limited – New Zealand Branch	2012	9	16	39	28.21	0.17	0.29	0.09	105	1.22	1.28	1.28	-0.19	50	24.75	0.49	69	0.68	0.27	25.71
	2011	*13*	*19*	*66*	*25.76*	*0.10*	*0.27*	*0.13*	*105*	*1.29*	*1.35*	*1.41*	*-0.30*	*44*	*28.39*	*0.41*	*63*	*0.59*	*0.27*	*27.62*
Commonwealth Bank of Australia New Zealand Branch	2012	27	0	50	48.00	0.22	0.81	0.70	88	0.44	0.47	0.25	0.44	36	5.91	0.36	50	0.50	0.11	12.50
	2011	*15*	*0*	*13*	*46.15*	*0.64*	*0.80*	*0.38*	*65*	*0.36*	*0.38*	*0.22*	*0.26*	*28*	*4.91*	*0.27*	*40*	*0.38*	*0.10*	*15.38*
Rabobank Nederland New Zealand Branch	2011	0	0	0	0.00	0.09	0.09	0.02	49	1.45	1.53	1.44	-0.64	35	26.28	0.57	48	0.78	0.03	3.11
	2010	*-1*	*0*	*0*	*0.00*	*0.07*	*0.07*	*-0.08*	*22*	*2.05*	*2.17*	*2.10*	*-1.68*	*14*	*13.07*	*0.23*	*22*	*0.36*	*0.02*	*6.73*
Rabobank New Zealand Limited	2011	33	65	396	27.03	0.36	1.71	0.44	201	2.73	2.75	2.22	-0.05	54	8.09	0.72	75	1.00	1.24	46.36
	2010	*35*	*76*	*391*	*29.72*	*0.26*	*1.87*	*0.50*	*212*	*2.87*	*2.90*	*2.38*	*0.14*	*72*	*15.91*	*1.02*	*109*	*1.54*	*0.97*	*32.37*
Westpac Banking Corporation New Zealand Branch	2012	-5	0	1	0.00	0.26	0.26	-0.14	318	0.85	1.51	1.28	0.71	196	7.17	0.96	272	1.33	0.25	16.04
	2011	*2*	*0*	*125*	*34.40*	*0.73*	*1.35*	*0.03*	*412*	*1.22*	*2.00*	*1.65*	*0.61*	*267*	*10.37*	*1.19*	*349*	*1.55*	*0.27*	*14.81*
Westpac New Zealand Limited	2012	190	184	867	31.83	0.55	1.01	0.34	1,856	2.33	2.35	1.76	0.56	613	11.91	0.95	897	1.40	1.20	41.43
	2011	*224*	*256*	*794*	*28.21*	*0.68*	*1.11*	*0.44*	*1,625*	*2.29*	*2.31*	*1.74*	*0.54*	*433*	*10.14*	*0.75*	*672*	*1.17*	*1.27*	*44.86*

Footnotes

Changes in accounting policy that have not had a material impact on the financial statements have not been detailed in the following footnotes. The effect of the changes listed below has been to impact certain ratios, or lead to the omission of certain ratios.

Where comparatives are not for the equivalent period, or the entity was not operational in either period, performance details have not been provided.

(a) If in its latest published financials an entity has changed its comparative year figures we have restated the numbers accordingly.

(b) Figures are for the New Zealand Banking Group, which comprises the aggregated New Zealand operations of Australia and New Zealand Banking Group Limited, including those operations conducted through the New Zealand Branch and the ANZ Bank New Zealand Limited Group.
Consolidated accounts for ANZ Bank New Zealand Limited include the results of UDC Finance Limited, which is also shown separately within the Finance Companies section.

(c) Figures are for the New Zealand Banking Group, which comprises Citibank, N.A. New Zealand Branch and Citicorp Services Limited and its subsidiaries.

(d) Figures are for the New Zealand Banking Group, which comprises Commonwealth Bank of Australia New Zealand Branch including various controlled entities and the ASB Banking Group Operations comprising ASB Bank Limited, ASB Holdings Limited and ASB Funding Limited.

(e) Figures are for the New Zealand Banking Group, which comprises Deutsche Bank AG New Zealand Branch, Deutsche New Zealand Limited, in-substance subsidiaries and other New Zealand subsidiaries of Deutsche New Zealand Limited.

(f) Figures shown are for the New Zealand Banking Group, which comprises JPMorgan Chase Bank New Zealand and associated entities.

(g) Figures are for the New Zealand Banking Group, which comprises Rabobank Nederland New Zealand Branch, Rabobank New Zealand Limited and various subsidiaries.
Rabobank Nederland New Zealand Branch's head office account, which comprises current period and cumulative surpluses, has been reclassified from liability to equity for consistency with other banks. This has impacted certain ratios.

(h) Operating expenses comprise total expenses less interest expense less loan write-offs less bad debts less abnormal expenses less impairment changes less amortisation of intangibles.

Registered banks – balance sheets

		Assets ($Million)									Liabilities ($Million)								Equity ($Million)					
Entity name	Balance date	Cash on hand, money at call and balances with other banks	Trading, investment securities, investments in subsidiaries and investment properties	Derivative financial instruments	Loans and advances (less provisions)	Balances with related parties	Fixed assets	Intangibles	Other assets	Total assets[a]	Customer deposits	Balances with other banks and money market deposits	Debt securities	Derivative financial instruments	Balances with related parties	Subordinated debt	Other liabilities	Total liabilities	Share capital – ordinary shares	Head office account	Convertible debentures/Perpetual preference shares	Other equity/Cash flow hedge reserves	Retained earnings	Total equity
2012																								
Australia and New Zealand Banking Group Limited – New Zealand Banking Group	30-Sep-2012	4,289	12,838	10,050	96,090	3,125	323	3,502	651	**130,868**	64,490	1,534	25,064	10,880	17,068	835	1,820	**121,691**	6,413	11	0	138	2,615	**9,177**
Bank of Baroda (New Zealand) Limited	31-Mar-2012	38	0	0	19	3	1	0	0	**61**	19	0	0	0	0	0	0	**20**	40	0	0	0	1	**41**
Bank of India (New Zealand) Limited	31-Mar-2012	48	0	0	5	1	1	0	1	**55**	3	0	0	0	2	0	0	**5**	50	0	0	0	0	**50**
Bank of New Zealand	30-Sep-2012	3,682	3,660	5,324	58,919	288	214	166	858	**73,111**	37,090	1,996	18,566	5,612	3,610	0	960	**67,834**	1,851	0	910	179	2,337	**5,277**
Citibank, N.A. New Zealand Branch	31-Dec-2011	448	730	0	783	183	0	0	4	**2,148**	1,037	23	0	0	908	0	15	**1,983**	29	33	0	0	103	**165**
Commonwealth Bank of Australia New Zealand Banking Group	30-Jun-2012	1,144	6,756	2,507	57,109	228	178	423	1,170	**69,515**	39,067	1,815	9,281	2,315	8,840	2,900	800	**65,018**	704	462	1,285	654	1,392	**4,497**
Deutsche Bank AG, New Zealand Group	31-Dec-2011	126	753	0	291	1,842	3	0	78	**3,093**	159	444	578	0	1,562	212	28	**2,983**	20	0	0	2	88	**110**
JPMorgan Chase Bank, N.A. New Zealand Branch	31-Dec-2011	234	465	0	46	47	0	1	213	**1,007**	148	0	463	0	140	0	219	**970**	0	0	0	0	36	**37**
Kiwibank Limited	30-Jun-2012	486	1,505	138	12,445	58	19	49	45	**14,745**	11,551	334	1,806	156	18	64	69	**13,998**	360	0	149	-19	257	**747**
Kookmin Bank Auckland Branch	31-Dec-2011	1	0	0	146	279	0	0	0	**427**	124	181	0	0	117	0	1	**423**	0	4	0	0	0	**4**
Rabobank Nederland New Zealand Banking Group	31-Dec-2011	24	0	57	9,487	844	4	0	78	**10,495**	4,126	1,980	0	17	3,501	0	64	**9,688**	341	150	0	0	316	**807**
Southland Building Society	31-Mar-2012	113	266	3	2,426	0	22	2	10	**2,842**	2,477	52	0	10	11	61	15	**2,627**	0	0	0	5	211	**215**
The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	31-Mar-2012	115	0	60	2,366	23	1	0	9	**2,574**	59	0	0	60	2,356	0	4	**2,479**	0	83	0	0	12	**95**
The Co-operative Bank Limited	31-Mar-2012	64	163	0	1,207	0	6	5	6	**1,451**	1,213	0	11	1	83	0	12	**1,322**	0	0	0	0	130	**130**
The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	31-Dec-2011	558	552	124	3,431	219	2	23	31	**4,940**	3,092	153	635	151	848	0	44	**4,923**	0	15	0	2	0	**17**
TSB Bank Limited	31-Mar-2012	98	2,299	1	2,740	0	17	0	11	**5,165**	4,715	0	0	1	0	0	53	**4,769**	10	0	0	0	386	**396**
Westpac Banking Corporation – New Zealand Division	30-Sep-2012	2,036	6,770	5,506	59,892	2,006	162	652	830	**77,854**	41,967	214	14,337	5,841	7,884	712	1,384	**72,339**	139	1,513	1,284	53	2,526	**5,515**
Bank sector total		**13,504**	**36,757**	**23,770**	**307,402**	**9,146**	**954**	**4,823**	**3,995**	**400,351**	**211,338**	**8,726**	**70,741**	**25,045**	**46,948**	**4,784**	**5,488**	**373,071**	**9,957**	**2,271**	**3,628**	**1,014**	**10,410**	**27,280**
2011																								
Australia and New Zealand Banking Group Limited – New Zealand Banking Group	30-Sep-2011	6,899	10,174	13,015	93,576	3,090	325	3,507	925	**131,511**	60,421	2,936	23,848	10,912	20,757	1,434	2,738	**123,046**	6,413	11	0	187	1,854	**8,465**
Bank of Baroda (New Zealand) Limited	31-Mar-2011	42	0	0	8	2	0	0	0	**53**	12	0	0	0	1	0	0	**13**	40	0	0	0	0	**40**
Bank of India (New Zealand) Limited	31-Mar-2011	50	0	0	0	0	0	0	0	**50**	0	0	0	0	0	0	0	**0**	50	0	0	0	0	**50**
Bank of New Zealand	30-Sep-2011	4,268	3,997	6,949	56,983	600	200	152	936	**74,085**	33,218	2,672	22,339	6,051	4,117	367	972	**69,736**	1,451	0	910	144	1,844	**4,349**
Citibank, N.A. New Zealand Branch	31-Dec-2010	1,201	1,000	0	377	100	0	0	3	**2,682**	1,281	26	0	0	1,219	0	9	**2,535**	29	33	0	0	85	**146**
Commonwealth Bank of Australia New Zealand Banking Group	30-Jun-2011	2,800	6,182	2,380	56,419	62	158	399	274	**68,674**	33,713	4,633	10,946	2,851	8,975	2,667	707	**64,492**	704	462	1,285	564	1,167	**4,182**
Deutsche Bank AG, New Zealand Group	31-Dec-2010	160	851	0	101	2,120	4	0	46	**3,282**	491	297	946	23	1,217	204	16	**3,194**	20	0	0	1	67	**88**
JPMorgan Chase Bank, N.A. New Zealand Branch	31-Dec-2010	62	206	0	0	202	0	1	2	**474**	126	0	30	0	167	0	143	**466**	0	0	0	0	8	**8**
Kiwibank Limited	30-Jun-2011	737	1,448	74	11,495	4	25	48	45	**13,874**	10,571	796	1,510	183	15	143	49	**13,267**	310	0	150	-39	187	**608**
Kookmin Bank Auckland Branch	31-Dec-2010	1	0	0	143	295	0	0	0	**439**	108	88	0	0	235	0	1	**432**	0	7	0	0	0	**7**
Rabobank Nederland New Zealand Banking Group	31-Dec-2010	72	0	36	8,820	447	7	0	68	**9,449**	4,050	1,153	0	12	3,466	0	48	**8,729**	342	115	0	0	263	**720**
Southland Building Society	31-Mar-2011	71	120	3	2,585	0	22	3	10	**2,814**	2,398	107	0	13	12	61	20	**2,612**	0	0	0	1	201	**202**
The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch	31-Mar-2011	82	0	41	1,916	10	0	0	5	**2,055**	61	0	0	41	1,937	0	4	**2,044**	0	3	0	0	9	**12**
The Co-operative Bank Limited	31-Mar-2011	89	183	0	1,164	0	7	4	4	**1,452**	1,163	0	11	2	139	0	13	**1,328**	0	0	0	0	124	**124**
The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch	31-Dec-2010	785	665	128	3,127	268	2	20	25	**5,021**	2,427	164	719	157	1,490	0	35	**4,993**	0	28	0	0	0	**28**
TSB Bank Limited	31-Mar-2011	86	2,110	1	2,626	0	18	0	8	**4,850**	4,442	0	0	1	0	0	49	**4,492**	10	0	0	1	348	**358**
Westpac Banking Corporation – New Zealand Division	30-Sep-2011	2,570	7,631	6,060	58,114	2,272	154	617	875	**78,293**	38,019	778	19,186	5,448	6,692	785	2,624	**73,532**	139	1,389	1,284	-35	1,984	**4,761**
Bank sector total		**19,976**	**34,569**	**28,686**	**297,453**	**9,472**	**925**	**4,751**	**3,226**	**399,059**	**192,501**	**13,651**	**79,535**	**25,694**	**50,439**	**5,661**	**7,429**	**374,911**	**9,508**	**2,047**	**3,629**	**823**	**8,141**	**24,148**

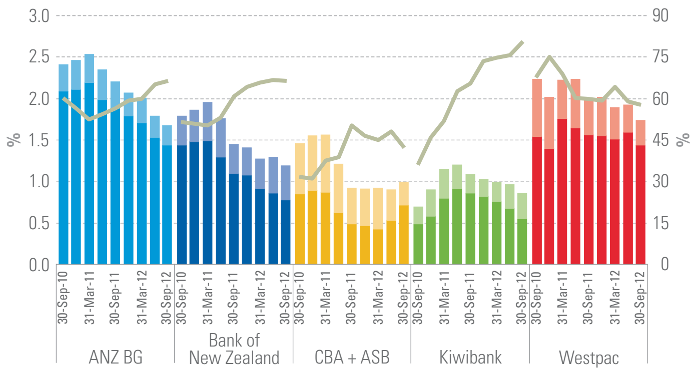
Footnote
(a) Total assets is based on audited financial statements and includes intangible assets.

Quarterly analysis

Size & strength measures	31-Dec-10	31-Mar-11	30-Jun-11	30-Sep-11	31-Dec-11	31-Mar-12	30-Jun-12	30-Sep-12
Total assets[d] ($Million)								
ANZ Banking Group – New Zealand Banking Group[a]	121,012	121,530	121,774	125,576	121,604	121,241	125,655	127,366
Bank of New Zealand	68,512	68,535	69,319	73,933	71,329	71,555	72,762	72,945
Commonwealth Bank of Australia New Zealand Banking Group[a]	69,416	68,701	68,275	68,678	70,925	69,715	69,092	68,497
Kiwibank Limited	12,921	13,796	13,827	14,684	14,374	14,604	14,696	14,930
Southland Building Society	2,823	2,811	2,836	2,847	2,837	2,839	2,785	2,875
The Co-operative Bank Limited[c]	n/d	1,448	1,454	1,449	1,454	1,446	1,469	1,475
TSB Bank Limited	4,720	4,850	4,913	4,977	5,150	5,164	5,193	5,236
Westpac Banking Corporation – New Zealand Division[a]	72,218	73,958	74,809	77,676	75,966	75,034	78,329	77,202
Total	**351,622**	**355,629**	**357,206**	**369,820**	**363,640**	**361,599**	**369,981**	**370,526**
Increase in gross loans and advances (%)								
ANZ Banking Group – New Zealand Banking Group[a]	-0.26	-0.38	-0.78	-1.05	-0.11	0.36	1.26	1.03
Bank of New Zealand	0.49	0.94	0.79	0.85	-0.01	2.11	0.69	1.16
Commonwealth Bank of Australia New Zealand Banking Group[a]	-0.78	-0.75	-1.23	0.51	-0.10	0.17	0.60	1.79
Kiwibank Limited	2.27	2.49	2.93	3.08	1.85	1.98	1.09	1.42
Southland Building Society	6.02	-0.57	-1.31	-1.06	-1.66	-1.90	-1.55	-2.43
The Co-operative Bank Limited[c]	n/d	n/d	1.07	1.14	0.84	0.55	1.28	2.42
TSB Bank Limited	1.37	2.20	1.27	1.65	0.33	1.05	0.86	-0.12
Westpac Banking Corporation – New Zealand Division[a]	0.24	-0.16	-0.76	2.80	-0.07	1.07	0.79	1.10
Average	**0.05**	**0.39**	**-0.39**	**0.62**	**0.00**	**0.88**	**0.88**	**1.20**
Capital adequacy (%)								
ANZ Banking Group – New Zealand Banking Group[a, b]	11.90	12.10	11.80	12.10	12.00	12.60	12.30	12.20
Bank of New Zealand	11.32	11.29	11.24	11.84	12.17	12.39	12.72	13.29
Commonwealth Bank of Australia New Zealand Banking Group[a, b]	11.50	11.50	11.70	11.80	11.20	11.20	11.00	11.00
Kiwibank Limited	11.40	10.50	10.50	10.50	11.50	10.50	10.80	10.80
Southland Building Society	13.97	13.60	13.89	14.25	14.58	14.35	14.77	14.89
The Co-operative Bank Limited[c]	n/d	17.30	18.10	17.50	17.50	17.50	17.50	17.10
TSB Bank Limited	16.29	15.78	16.16	16.09	15.63	15.42	15.23	15.39
Westpac Banking Corporation – New Zealand Division[a, b]	10.50	11.00	11.00	11.00	11.00	10.80	10.70	11.70
Net profit ($Million)								
ANZ Banking Group – New Zealand Banking Group[a]	260	218	257	350	415	200	350	300
Bank of New Zealand	150	105	131	285	289	63	176	52
Commonwealth Bank of Australia New Zealand Banking Group[a]	148	119	159	188	205	165	158	190
Kiwibank Limited	5	1	7	18	20	23	18	30
Southland Building Society	5	2	3	3	4	2	5	2
The Co-operative Bank Limited[c]	n/d	n/d	1	0	2	2	2	1
TSB Bank Limited	11	10	12	12	13	11	14	13
Westpac Banking Corporation – New Zealand Division[a]	144	135	167	220	206	171	196	186
Total	**723**	**590**	**737**	**1,076**	**1,154**	**637**	**919**	**774**

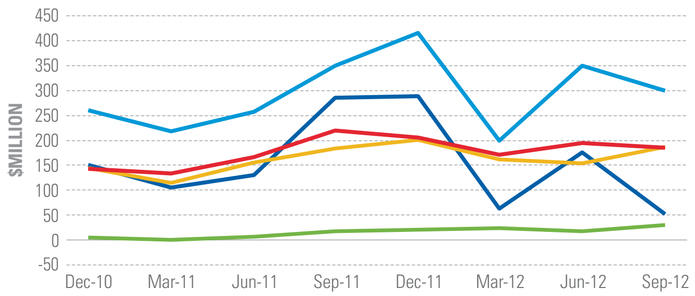
Profitability measures	31-Dec-10	31-Mar-11	30-Jun-11	30-Sep-11	31-Dec-11	31-Mar-12	30-Jun-12	30-Sep-12
Interest margin (%)								
ANZ Banking Group – New Zealand Banking Group[a]	2.39	2.36	2.41	2.46	2.53	2.54	2.45	2.43
Bank of New Zealand	2.14	2.18	2.24	2.27	2.23	2.42	2.32	2.31
Commonwealth Bank of Australia New Zealand Banking Group[a]	1.96	1.99	2.00	2.05	2.12	2.03	1.89	2.10
Kiwibank Limited	1.46	1.54	1.47	1.68	1.74	1.80	1.89	1.94
Southland Building Society	2.70	2.40	2.34	2.42	2.60	2.63	2.66	2.59
The Co-operative Bank Limited[c]	n/d	n/d	2.73	2.76	2.88	2.72	2.70	2.76
TSB Bank Limited	2.19	1.83	1.99	2.08	2.08	2.13	2.10	2.03
Westpac Banking Corporation – New Zealand Division[a]	2.14	2.10	2.43	2.55	2.15	2.22	2.24	2.22
Average	**2.17**	**2.15**	**2.25**	**2.32**	**2.27**	**2.31**	**2.24**	**2.27**
Non-interest income/Total assets (%)								
ANZ Banking Group – New Zealand Banking Group[a]	0.58	0.66	0.57	0.84	1.10	0.34	0.81	0.67
Bank of New Zealand	0.67	0.29	0.32	1.57	1.33	-0.47	0.42	-0.51
Commonwealth Bank of Australia New Zealand Banking Group[a]	0.54	0.52	0.55	0.67	0.70	0.50	0.86	0.67
Kiwibank Limited	1.32	1.15	1.25	1.12	1.13	1.13	1.09	1.16
Southland Building Society	0.74	0.75	0.62	0.65	0.65	0.62	0.64	0.72
The Co-operative Bank Limited[c]	n/d	n/d	1.46	1.16	1.52	1.68	1.70	1.66
TSB Bank Limited	0.26	0.24	0.31	0.36	0.35	0.20	0.30	0.36
Westpac Banking Corporation – New Zealand Division[a]	0.67	0.69	0.66	0.73	0.76	0.78	0.69	0.82
Average	**0.63**	**0.58**	**0.57**	**0.93**	**0.99**	**0.34**	**0.72**	**0.49**
Impaired asset expense/Average gross loans (%)								
ANZ Banking Group – New Zealand Banking Group[a]	0.14	0.21	0.19	0.24	0.19	0.24	0.20	0.21
Bank of New Zealand	0.28	0.40	0.13	0.27	0.02	0.19	0.08	0.13
Commonwealth Bank of Australia New Zealand Banking Group[a]	0.19	0.49	-0.06	0.08	0.15	0.08	0.21	0.08
Kiwibank Limited	0.77	0.93	0.78	0.27	0.33	0.29	0.26	0.03
Southland Building Society	0.47	1.23	0.46	0.78	0.84	1.41	0.49	1.02
The Co-operative Bank Limited[c]	n/d	n/d	0.15	0.19	0.01	0.20	0.11	0.25
TSB Bank Limited	0.16	0.20	0.15	0.21	0.08	0.07	0.06	0.08
Westpac Banking Corporation – New Zealand Division[a]	0.40	0.42	0.48	0.26	0.14	0.49	0.21	0.39
Average	**0.26**	**0.38**	**0.21**	**0.22**	**0.15**	**0.26**	**0.18**	**0.20**
Operating expenses/Operating income (%)								
ANZ Banking Group – New Zealand Banking Group[a]	50.73	58.85	47.87	41.47	39.49	58.73	43.97	53.37
Bank of New Zealand	43.56	47.69	48.77	30.33	32.72	62.30	43.61	73.43
Commonwealth Bank of Australia New Zealand Banking Group[a]	43.33	42.34	47.51	40.67	36.29	43.22	45.22	40.00
Kiwibank Limited	67.29	69.82	64.49	66.88	63.58	61.32	66.97	63.16
Southland Building Society	56.52	48.09	62.50	58.81	54.45	47.54	56.15	59.68
The Co-operative Bank Limited[c]	n/d	n/d	85.65	92.62	85.13	83.42	80.02	85.64
TSB Bank Limited	39.29	44.78	37.90	39.89	38.15	47.66	33.90	39.33
Westpac Banking Corporation – New Zealand Division[a]	44.02	45.88	38.42	38.11	41.05	40.99	42.99	40.48
Average	**47.17**	**51.31**	**46.74**	**39.34**	**39.04**	**52.05**	**45.14**	**50.79**

24 PAST DUE AND GROSS IMPAIRED ASSETS VS GROSS LOANS AND ADVANCES

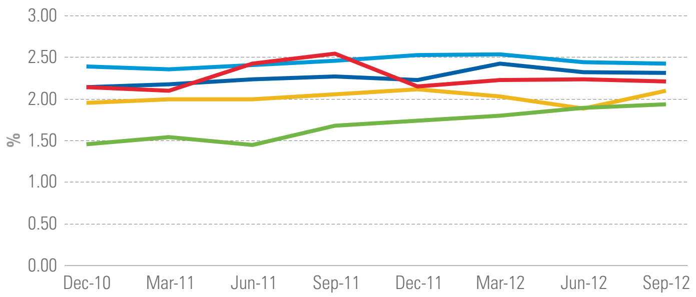


- Gross impaired/Gross loans and advances (LHS)
- Past due/Gross loans and advances (LHS)
- Total provisions/Past due and gross impaired assets (RHS)

25 NET PROFIT AFTER TAX

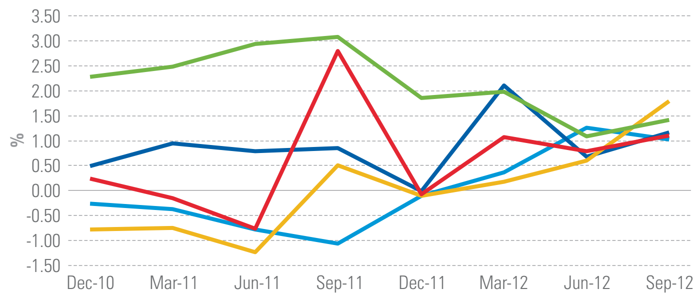


26 INTEREST MARGINS

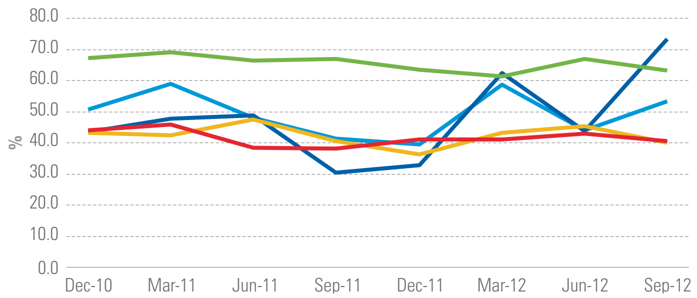


ANZ BG | Bank of New Zealand | CBA + ASB | Kiwibank | Westpac

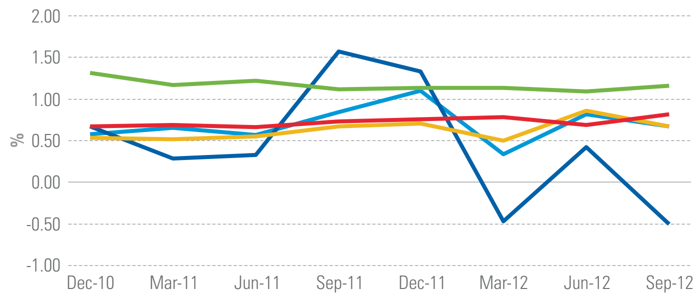
27 QUARTERLY INCREASE IN GROSS LOANS AND ADVANCES



28 OPERATING EXPENSES VS OPERATING INCOME

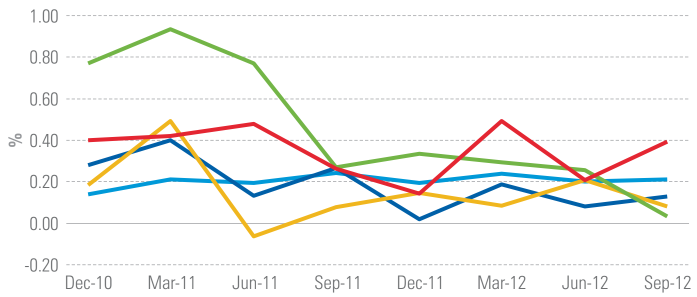


29 NON-INTEREST INCOME VS AVERAGE TOTAL ASSETS



ANZ BG | Bank of New Zealand | CBA + ASB | Kiwibank | Westpac

30 IMPAIRED ASSET EXPENSE VS AVERAGE GROSS LOANS AND ADVANCES

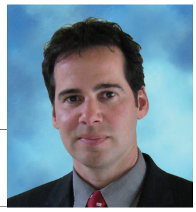


ANZ BG | Bank of New Zealand | CBA + ASB | Kiwibank | Westpac

Footnotes

(a) The results for Australia and New Zealand Banking Group, Commonwealth Bank of Australia and Westpac Banking Corporation relate to the total New Zealand operations of these entities.
(b) The capital adequacy ratio's reported are for the overseas banking group.
(c) The Co-operative Bank Limited obtained bank registration on 26 October 2011. However, for all quarters prior to the December 2011 quarter figures disclosed are in accordance with Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order (No 3) 2011.
(d) Total assets = Total assets – Goodwill and other intangibles
n/d = In this or the previous quarter the Bank did not disclose the standard disclosure statement and therefore we are unable to calculate the necessary figures.

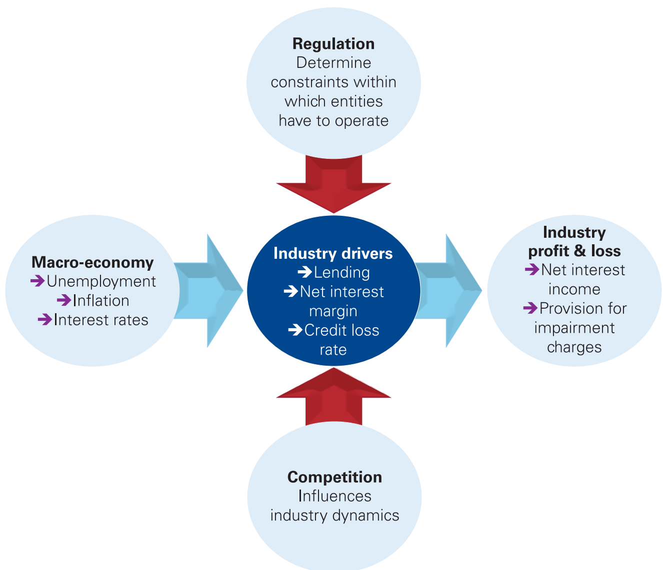
Banking industry forecasts



Christoph Schumacher | Professor for Innovation and Economics | Massey University
Additional contribution by: Sabrina Ruhnau

This section provides a forecast of the key performance drivers for the New Zealand banking industry. We use a combination of macro-economic variables and time-series analysis to provide quarterly forecasts for the next two years ending in December 2014. Our results are displayed in table 10.

31 FORECASTING APPROACH



Total industry lending is expected to continue its slow rise over the next two years, while the overall credit loss and net interest margin, as expressed as a percentage of total lending, are both showing a decline to a moderate extent. The expectation of a declining net interest margin may be driven by increased competition among banks. Based on these findings, we predict profitability to slightly decrease till the first quarter of the current year, however, expect profitability to recover from the second quarter onwards.

We use historical data of macro-economic variables, such as inflation, interest rates and unemployment rates, as well as third-party forecasts to predict the three core industry performance drivers: lending, net interest margin, and credit loss rate. This forms the structural part of our forecast. Additionally, we incorporate a time-series element of these industry drivers into our analysis to improve the quality of our predictions.

The definition of industry drivers are:

- **Lending** – 'the total volume of lending broadly defined, that is, all interest-earning assets.'
- **Net interest margin** – 'the difference between interest income and interest expense, expressed as a percentage of lending.'
- **Credit loss rate** –'provision for credit impairment, expressed as a percentage of lending.'

After forecasting the three industry drivers and by establishing reasonable assumptions regarding the impact of the remaining profit and loss items, we are able to estimate the profitability of the banking industry, expressed as profit before tax (see figure 31 Forecasting Approach).

Our regression results suggest that changes in lending volume are negatively associated with changes in unemployment and positively with changes in inflation. The November 2012 *Financial Stability Report*, issued by the Reserve Bank of New Zealand (RBNZ), asserts that labour income has grown during the past six month, interest rates remain low, lending criteria has relaxed and the housing market activity has improved recently. This, together with a relatively high level of unemployment (the unemployment rate reached 7.3% at the end of last year – a 13 year high), helps to explain the expected moderate increase in lending in our forecast. However, the RBNZ belief that the combination of a difficult external

TABLE 10: INDUSTRY DRIVER		2012 Q1 Actual	2012 Q2 Actual	2012 Q3 Actual	2012 Q4 Forecast	2013 Q1 Forecast	2013 Q2 Forecast	2013 Q3 Forecast	2013 Q4 Forecast	2014 Q1 Forecast	2014 Q2 Forecast	2014 Q3 Forecast	2014 Q4 Forecast
Lending ($bn)	Upper CI				438	459	481	506	531	557	584	615	646
	Forecast	352	355	360	378	384	391	399	407	414	421	430	439
	Lower CI				326	321	318	315	311	308	304	301	298
Net interest margin (%)	Upper CI				2.7%	2.8%	2.9%	3.0%	3.1%	3.2%	3.4%	3.5%	3.7%
	Forecast	2.3%	2.2%	2.3%	2.1%	2.1%	2.1%	2.1%	2.1%	2.1%	2.1%	2.1%	2.0%
	Lower CI				1.7%	1.6%	1.5%	1.5%	1.4%	1.3%	1.3%	1.2%	1.1%
Credit loss rate (%)	Upper CI				0.7%	0.8%	0.9%	0.9%	1.0%	1.1%	1.2%	1.3%	1.4%
	Forecast	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.2%	0.1%	0.1%	0.1%	0.1%
	Lower CI				-0.3%	-0.4%	-0.5%	-0.6%	-0.7%	-0.8%	-0.9%	-1.0%	-1.2%
Profit before tax ($bn)	Calculated	5.31	5.50	4.98	4.85	4.92	5.04	5.14	5.20	5.27	5.39	5.51	5.59

funding environment, tighter core funding regulations and a stronger emphasis on retail deposits by the banking sector, may endanger the expected upturn in credit expansion.

While we still find a positive link between net interest margin and inflation, we believe that this association might weaken in the future. Historically, banks have borrowed at shorter maturities and lent at longer maturities. However, it seems that these days, banks more actively manage maturity mismatches via changes in the funding profile, business mix, and hedging activities. This prediction is supported by the RBNZ's observation that in contrast to previous years, banks have sought to reduce their reliance on short-term wholesale funding by borrowing for longer terms since the breakout of the crisis (RBNZ FSR, November 2012).

Overall credit losses are negatively linked to short-term interest rates. We hypothesize that short-term interest rates are used as a proxy for the economic cycle. This is plausible, given the important role that short-term interest rates play as a counter-cyclical monetary policy tool.

Comparing our 2012 forecast of industry drivers and industry profit before tax (see Financial Institutions Performance Survey 2011) with actual 2012 data, we find that all our predictions are within the 95 percent confidence interval. In particular, the values for industry lending differed on average only by 1.25 percent from the actual values, as the total lending turned out to be slightly lower than expected. In contrast, net interest margins were on average 2.51 percent higher than suggested by our forecast.

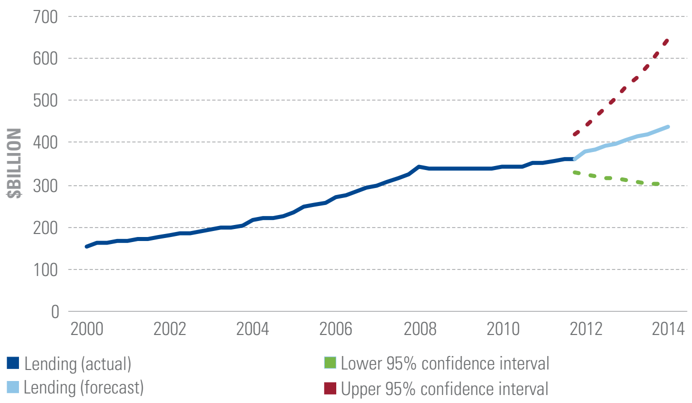
We would like to note that the forecast lacks assumptions regarding regulatory requirements and competition in the market, which clearly have an impact on lending volume, margins, and credit loss rates. However, the RBNZ states: "(...) increasing capital requirements should have little or no permanent impact on the bank's weighted average cost of capital or lending rates." (RBNZ FSR, November 2012). This somewhat surprising statement can be explained by two effects. Firstly, higher capital tends to reduce the spreads at which banks can borrow, and secondly, expectations regarding the return on equity (RoE) are likely to decline as soon as banks become less leveraged.

Regarding regulatory aspects and influential external factors, the RBNZ summarizes that all banks are comfortably meeting the new regulatory requirements for core funding, which have been in effect since the 1 January 2013.

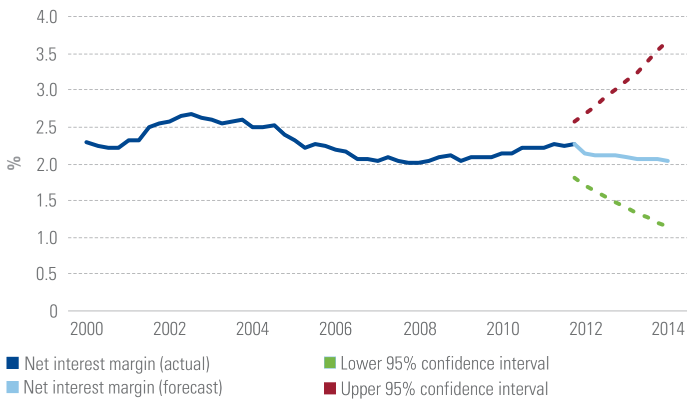
The external environment still poses some risks for the financial system in New Zealand, even if domestic banks rely less on external funding. Furthermore, the increasing net external liabilities of the public sector and the still highly leveraged agricultural sector may negatively influence the financial sector's performance.

On a positive note, as a result of unprecedented monetary and fiscal policies, particularly in the Eurozone and the United States, current financial market conditions seem to have improved slightly. Also, the Canterbury rebuild could provide an impetus for the construction sector and therefore stimulate overall demand, which would boost the whole economy (RBNZ FSR, November 2012).

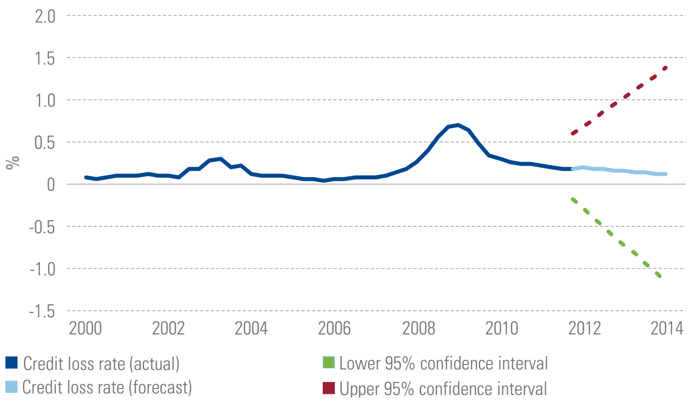
32 INDUSTRY LENDING



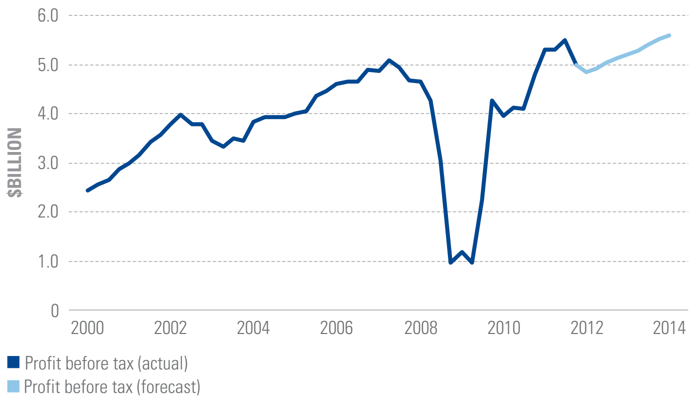
33 INDUSTRY NET INTEREST MARGIN



34 CREDIT LOSS RATE



35 INDUSTRY PROFIT BEFORE TAX



Forecast technical appendix

Data

Our data consists of the industry drivers (for which we calculate forecasts) and macro-economic data (actual and forecast) which we use in our forecasts of the industry drivers.

Industry drivers

Historical industry data were obtained from the Reserve Bank of New Zealand under the section "G3 Registered Banks: summary of selected aggregate financial data". This data is based on RBNZ surveys and is disclosed on a quarterly basis. The latest quarter disclosed as of 12 April 2012 was the September 2011 quarter. Hence, our first forecasted period is the final quarter of 2011. From the RBNZ data we calculate historical time-series of the three industry drivers we forecast.

1. Lending volume (lending)

   = Cash and balances with Central Bank + Balances with other financial institutions + Securities + Mortgage lending + Other lending

2. Net Interest Margin (nim)

   = (Interest Income - Interest Expense) / lending

3. Credit Loss Rate (clrate)

   = Provision for credit impairment / lending

Macro-economic variables

We examined several macro-economic variables in order to assess their ability to predict the three industry drivers. The macro-economic variables we considered are set out in the table at the bottom of the page. However, only three variables ended up being statistically significant in predicting the industry drivers, namely unemployment, inflation (the CPI index) and the 90 day bank bill rate.

Methodology

Our methodology comprised of the following steps:

1. Transform dependent and independent variables to achieve a stationary time-series. For our purposes, this is equivalent to ensuring that the time series does not exhibit a unit root (the lack of unit root suggests the absence of a stochastic trend, which is the usual source of non-stationarity in economic and financial time-series).

2. Use a heteroskedasticity-robust ordinary least squares regression to identify a subset of lagged economic variables ($\{x_{i,t-1}\}$) that exhibit statistically significant predictive power with regards to the industry variable (y_t) being predicted.

   $$y_t = \alpha + \beta_1 x_{1,t-1} + \cdots + \beta_n x_{n,t-n} + \varepsilon_t$$

   where

   $$x_{t-1} = \ln(X_{t-1}) - \ln(X_{t-2})$$

   is the lagged difference in logs of the economic variable X_{t-1} (if originally specified in levels). (Refer to the Statistical Issues section below regarding our rationale for using lagged differences in logs).

3. Based on the candidate economic regressors identified above, we re-estimate the previous equation as structural ARIMA equation of the form:

   $$\Delta_d y_t = \alpha + \beta_1 \Delta_d x_{1,t-1} + \cdots + \beta_n \Delta_d x_{n,t-n} + \mu_t$$

   where μ_t encompass the error term and the ARIMA(p,d,q) time-series elements of the regression

   $$\mu_t = \emptyset_1 \Delta_d \mu_{t-1} + \cdots + \emptyset_p \Delta_d \mu_{t-p} + \theta_1 \varepsilon_{t-1} + \cdots \theta_q \varepsilon_{t-q} + \varepsilon_t$$

4. We consider various ARIMA(p,d,q) models in terms of p Autoregressive (AR) lags, q moving average (MA) lags and order of integration (I) d (usually $d=1$) until we obtain a model that is statistically significant in both the ARIMA terms as well as the macro-economic regressors used.

5. Next we verify that both the industry driver (the dependent variable) and the macro-economic variables (the regressors) used in the regression are stationary by using standard statistical tests to reject the presence of unit roots (we use the Phillips & Perron and Dickey & Fuller procedures to test for the presence of unit roots).

6. We then test whether there is any evidence of residual autocorrelation in the error term ε_t by looking at the autocorrelation and partial autocorrelation graphs of ε_t.

7. We select among competing specifications using the following as a guide:

   (a) The principle of parsimony – since we have a limited number of data points

Macro variable	Description	Units	Source
gdp	Gross Domestic Product (expenditure based)	$mn, nominal index	RBNZ
bankbill90	90-day bank bills rate	%, annualised	RBNZ
govbond10y	10-year government bond yield	%, annualised	RBNZ
unemployed	Number of registered unemployed	Number	RBNZ
avgqhouseloancount	Average number of home loans approved	Number	RBNZ
estpop	Estimated population of New Zealand	Thousands	Statistics NZ
cpindx	Consumer Price Index	Index level	RBNZ
housepricendx	REINZ house price index	Index level	REINZ
weeklyearnings	Weekly earnings	$, nominal	Statistics NZ
nzstocksndx	New Zealand all stocks index	Index level	NZSE

we prefer estimating fewer coefficients. This also guards against over-fitting, which can lead to bad out-of-sample forecasting performance.

(b) Statistical significance. We prefer models where the coefficients of the regressors have higher statistical significance.

(c) Information criterion. We use the Aikake and Bayesian information criterion to assess the informational power of each specification.

8. Once we are decided on a specification, we generate point forecasts and confidence intervals for that industry variable. The final specifications used to generate our forecasts are set out in the table at the bottom of this page.

Confidence intervals

Our forecasts are accompanied by confidence intervals set at a 95% confidence level. That is, the eventual outcome should (in theory) lie between the upper and lower interval bounds 95% of the time. These confidence intervals are based on a number of statistical assumptions and should be taken with a grain of salt. We did not attempt to calculate a confidence interval for the calculated profit before tax – doing so would involve pulling on so many additional assumptions that we would not have much confidence in the resulting confidence intervals! Suffice to say that we would not place too much reliance on the more distant forecasts of industry profit before tax, given the confidence intervals of the industry drivers used in its calculation.

Statistical issues

Most of our variables are in levels with a substantial trend. This means these variables are not stationary in a time-series sense (among other things, they do not have a stable mean and variance over time). To avoid problems with spurious regressions (i.e. non-sensical results), it is necessary to transform these variables to ensure they are stationary.

We use the difference of logs transform, that is, for variable X_t in levels we calculate

$$x_{t-1} = \ln(X_{t-1}) - \ln(X_{t-2})$$

as the difference in the log-levels of X_{t-1} and X_{t-2}. This transformed variable is a close approximation to the percentage change in X_{t-1}, which has an intuitive interpretation and is often used by economists.

This also obviates the need to adjust for inflation, since a percentage change in a dollar level eliminates any inflation (or other trend) that may be inherent in those dollar values.

A second concern is endogeneity – this issue can arise whenever we are performing a time-series regression of two variables observed at the same time where the causality between those two variables could conceivably take place in both directions. If this is the case, one of the assumptions of ordinary least squares regression is violated leading to a biased estimation of regression coefficients (the so-called the simultaneous equations bias). To avoid this complication we use lagged regressors in those cases where causality could realistically go in either direction. By using lagged regressors we avoid the issue of endogeneity altogether since causality cannot go backwards in time.

Limitations and caveats

Forecasting has its limitations, as anyone who relies on weather forecasts will undoubtedly be aware. Some of these limitations are generic, while others are specific to our forecasts.

Generic limitations

Unexpected events could take place in the future, changing the outcomes of forecasted variables. As a matter of definition, an unexpected event cannot be incorporated into a forecast (it wouldn't be unexpected if one could).

Statistical forecasts generally rely on past associations perpetuating into the future. But of course the world is constantly changing and this may not be the case.

The specific model being used may not be correctly specified – it might omit important variables or it may be of the wrong form. The forecast will be accordingly handicapped.

Specific limitations

Our specifications do not take into account competition or regulatory factors, even though these factors are undoubtedly important determinants of industry performance.

Our forecasts rely in turn on third-party forecasts of macro-economic variables – in particular unemployment, inflation and short-term interest rates. Any error in those third-party forecasts will carry over into our forecasts.

Variable	Specification
Lending	$\Delta_1\ln(lending_t) = \alpha + \beta_1\Delta_1\ln(cpindx_{t-1}) + \beta_2\Delta_1\ln(unemployed_{t-1}) + \mu_t$ with $\mu_t = \emptyset_1\Delta_1\mu_{t-1} + \theta_1\varepsilon_{t-1} + \varepsilon_t$
Net interest margin	$\Delta_1\ln(nim_t) = \alpha + \beta_1\Delta_1\ln(cpindx_{t-1}) + \mu_t$ with $\mu_t = \emptyset_1\Delta_1\mu_{t-1} + \varepsilon_t$
Credit loss rate	$\Delta_1 clrate_t = \alpha + \beta_1\Delta_1\ln(bankbill90_{t-1}) + \beta_2\Delta_1 clrate_{t-1}) + \mu_t$ with $\mu_t = \emptyset_1\Delta_1\mu_{t-1} + \varepsilon_t$

IFRS 9 – Are we there yet?

Rajesh Megchiani | Senior Manager | Financial and Regulatory Risk Management | KPMG

IFRS 9 *Financial Instruments* is expected to be one of the most significant standards to impact bank financial reporting since the introduction of IFRS in New Zealand. The project to replace IAS 39 *Financial Instruments: Recognition and Measurement* with IFRS 9 has been underway since November 2008 and is still ongoing. In 2011, The International Accounting Standards Board (IASB) deferred the effective date of IFRS 9 from 1 January 2013 to annual periods beginning on or after 1 January 2015 as there were delays in completing the hedging and the impairment phases of the project. Although the IASB is not yet able to issue the final version of IFRS 9, it is possible that the IASB will be able to issue this in late 2013. A critical element in achieving this will be making sustained progress on accounting for impairment.

The accounting for financial instruments under IAS 39 is widely believed to be complex and difficult to apply. The IAS 39 replacement project is driven in part by requests from the G20 following on from the GFC to reduce the complexity of accounting for financial instruments. The G20 leaders summit called on accounting standard setters to work with supervisors and regulators to improve the standards and achieve a single set of high-quality global accounting standards on financial instruments. However, a single-set of standards is no longer likely since the Financial Accounting Standards Board (FASB) and IASB are on divergent paths with respect to certain aspects of the project, particularly accounting for impairment, and will be issuing a different set of standards.

The IASB had adopted a phased approach in order to accelerate the replacement of IAS 39 and address the consequences of the financial crisis as quickly as possible. However, considering the potential delays, it remains to be seen whether IFRS 9 will be completed in time for entities to early adopt the new standard.

In a New Zealand context, IFRS 9 is likely to be adopted by the External Reporting Board (XRB) as soon as it is issued by the IASB without any significant changes. If the final versions are issued as planned, registered banks would need to start considering an implementation plan and also the level of involvement for the board and audit committees. For banks, IFRS 9 should not only be seen to be about changes in accounting rules as it is also could have wider regulatory capital and liquidity implications.

The status of the three phases at the date of this publication, key changes compared to IAS 39 and the potential impact on banks are detailed below.

Significantly complete. However, some changes expected.

Significant work required to complete.

IFRS 9 Phase and key changes compared to IAS 39	Status	Impact on banks
CLASSIFICATION AND MEASUREMENT The classification and measurement model for financial assets and liabilities was completed by 2010. However, in November 2012, the IASB issued an exposure draft that amends this classification and measurement model. These changes have pervasive implications on the existing IFRS 9 classification and measurement principles. This phase could potentially be finalised by the second half of 2013.		→ Although the requirements are simpler, more judgement is required to be made in determining classification and measurement of financial assets. → Banks will need to review the terms of their existing portfolio of financial assets and the purpose of holding those assets to determine the appropriate classification. → There will potentially be changes in the causes of profit or loss volatility depending on how the financial assets are classified and measured under IFRS 9. → There could potentially be significant impact on the computation of banks' regulatory capital. For example, assets that an entity may previously have expected to measure at amortised cost may be required to be measured at fair value through other comprehensive income with any unrealised fair value changes adjusting its regulatory capital.

IFRS 9 Phase and key changes compared to IAS 39	Status	Impact on banks
CLASSIFICATION AND MEASUREMENT(CONTINUED) **Key changes compared to IAS 39** **Financial assets** **Debt instruments** Two key principles have been introduced in IFRS 9 to identify instruments that should be classified and measured at amortised cost. These are: (a) the contractual cash flow characteristics (i.e. are the cash flows solely payment of principal and interest?); and (b) the business models in which they are managed (i.e. is the financial asset held to collect the contractual cash flows?). **Equity instruments** With respect to equity instruments, IFRS 9's classification principles requires these to be measured at fair value with management having an irrevocable option on initial recognition to present in other comprehensive income. However, there will be no recycling of gains and losses on these instruments to profit or loss. There is also a reduction in the number of classification options from four in IAS 39 (i.e. held to maturity, loans and receivables, fair value through profit or loss and available for sale) to three in IFRS 9 (i.e. Fair value through profit or loss, Fair value through other comprehensive income and amortised cost).		→ Banks should consider if these changes have any impact on its corporate clients as they may now prefer to invest in more simple debt instruments so as to avoid having to measure them at fair value through profit or loss This could potentially have an impact on the banks' revenue and the products it offers.
Financial liabilities There is no change in the classification and measurement of financial liabilities except that for financial liabilities designated under the fair value option, changes in the fair value attributable to own credit risk should be recognised in other comprehensive income (OCI) rather than in the profit or loss (as required under IAS 39). Overall, significant improvements have been made in the principles relating to classification and measurement under IFRS 9. However, it could be argued that the IASB has not necessarily met their objective of simplifying the classification and measurement of financial instruments as now more judgement needs to be applied under IFRS 9 in the classification of financial assets.		→ Reduction in profit or loss volatility as IFRS 9 would require own credit risk adjustments on financial liabilities to be reflected in OCI.
HEDGE ACCOUNTING The hedge accounting phase has been split into (a) General hedge accounting and (b) Macro hedge accounting. **General hedge accounting** In September 2012, the IASB issued an exposure draft on general hedge accounting which proposed to align hedge accounting more closely with risk management. The objective was also to reduce the detailed rules that made hedge accounting under IAS 39 complex. Originally, the IASB had planned to finalise the standard in December 2012. However, due to certain comments received from respondents, the IASB now expects to issue the final standard later in 2013 after the comments have been addressed.		→ Opportunity to apply a number of hedging strategies which were previously not permitted under IAS 39. → More judgement is required to be applied to assess effectiveness of hedging relationships compared to using a bright-line test of 80% – 125%. → There will be additional systems implications to operationalise qualitative hedge effectiveness assessments. → Accounting for simple hedges is expected to be easier. It is also expected to offer some genuine opportunities for banks to sell products they were unable to under the previous regime.

IFRS 9 Phase and key changes compared to IAS 39	Status	Impact on banks
HEDGE ACCOUNTING (CONTINUED) **Key changes compared to IAS 39** (a) New potential hedging strategies can be adopted. For example: – Non-contractually specified inflation can be included in a hedging relationship. – Flexibility in the application of the net position approach. Currently IAS 39 only allows the gross currency approach. – More flexibility to hedge aggregated exposures (i.e. combination of a derivative and non-derivative). – Currency basis spreads, time value of purchased options and forward element of forward contracts may be deferred or amortised. (b) The increased level of judgement and relaxation of hedging requirements are complemented with more extensive disclosure requirements.		
Macro hedge accounting This project addresses dynamic risk management strategies for open portfolios (also known as "macro hedging"). This project was initially part of IFRS 9 Phase III: hedge accounting. However, it was decoupled from the IFRS 9 project into a separate project in May 2012. This separation is expected to facilitate the completion of IFRS 9 whilst allowing the IASB staff to elicit a broader range of accounting alternatives from a broader range of constituents on the accounting for macro hedging. The IASB is working towards issuing a discussion paper in the first half of 2013. **Key changes compared to IAS 39** The IASB has yet to make any decisions regarding portfolio fair value hedging of interest rate risk, which has always been seen as one of the more controversial aspects of hedge accounting for banks. In Europe, a portion of the guidance on hedge accounting was carved out to allow banks to hedge portfolios of financial assets and liabilities, consistent with their risk management strategies. The IASB is expected to consider how to address the many issues that this type of hedging presents (for example, hedging core deposits, prepayable fixed rate assets etc.) as part of this phase of the replacement project for IAS 39.		→ Banks may continue fair value hedge accounting for a portfolio hedge of interest rate risk as defined in IAS 39 until the macro hedge accounting project is finalised.
IMPAIRMENT The FASB and the IASB were working jointly on a model for accounting for impairment of financial assets based on expected credit losses which would replace the current incurred loss model in IAS 39. The IASB issued an exposure draft *Financial instruments: Amortised Cost and Impairment* in 2009. However, in July 2012, the IASB and the FASB decided to pursue different solutions to the impairment model – although both are still based on the expected losses approach. The IASB has redeliberated the issues and received feedback and plans to expose its expected loss model in the first quarter of 2013. **Key changes compared to IAS 39** At this stage the key change is the expected loss approach followed in IFRS 9 compared to the incurred loss approach in IAS 39. Although a number of models for the expected losses approach have been discussed, a tangible model acceptable to the constituents has not been finalised yet.		→ The change from incurred loss model to expected loss model will result in accelerated recognition of losses and potential earnings volatility. → Effective communication to stakeholders and market of the impact on earnings is critical. → Banks will also need to consider whether this will have any impact on pricing of its products. → The impact of changes in capital requirement will need to be assessed and planned. → The extent of overlap with expected losses under Basel framework needs to be determined. → New or changed data requirements could significantly impact processes, systems and reporting. → Potential opportunities exist to streamline processes – align regulatory and financial reporting processes.

Finance companies sector performance

Overview of results

2012 was a good year for the Finance Company sector participants as a whole. Profit levels rose due to improving margins and asset quality, and were offset only slightly by increasing compliance and regulatory costs.

As will be discussed further, these increasing margins can largely be attributed to the steady lending rates achieved by the institutions combined with a decreasing cost of funding.

The improvement in asset quality can be seen across the sector, both in the expenses being incurred and in a fall in the levels of assets being assessed as past due or impaired.

PGG Wrightson Finance was acquired by Heartland. We will analyse this as part of the Savings Institutions sector review.

TABLE 11		Total
Increase in total assets		1.6%
Increase in net profit after tax		14.4%
Reduction in impaired asset expense (% of loans and advances)	bps	76
Increase in interest margin	bps	73

Profit

Aggregate profit for the sector increased by 14.4% from $205.0 million in 2011 to $234.6 million in 2012.

This rise has been driven by several factors. There has been a large increase in net interest income, which has moved from $542 million in 2011 to $593 million in 2012 (an increase of $51 million). There is also a partially offsetting decrease in non-interest income, which has moved from $197 million in 2011 to $175 million in 2012. Impaired asset expense has fallen significantly, with an improvement in expense from $117 million in 2011 to $63 million in 2012. However, this is mostly offset by the $48 million increase in operating expenses, which rose from $335 million to $383 million.

Profit results varied with some entities showing growth and others a decline.

The highest levels of profit growth were seen by Mercedes-Benz (121%), Avanti Finance (69%) and Orix (52%), while the lowest levels of growth were seen in Toyota Finance (-24%), Motor Trade Finance (-18%) and Fisher & Paykel Finance (-14%). This demonstrates the significant variation in the performances of the companies in this sector for the year.

The profit growth at Mercedes-Benz was largely cost driven as revenue for the year was fairly flat. There was a large decrease in interest expense, from $17.3 million to $14.9 million, while falls were also seen in the operating expenses and impaired asset expenses. While the interest expense has decreased, the related party loan balance that the interest expense is derived from has increased, demonstrating the fall in the cost of funding.

For Toyota Finance, the profit movement can largely be attributed to increases in operating expenses of $9.2 million. That is mostly offset by a decrease in interest expense of $8.6 million, and also a large one-off fair value gain in 2011 that is not present in 2012 which leads to a decrease of $11.0 million. The profit result, while still lower than last year, is still a good level of profit for the company when compared to levels of profit seen in 2009 and 2010.

Overall, lower costs of funding and a continued improvement in the quality of assets, slightly offset by increased operating expenses, has led to a good level of profit growth for the sector as a whole.

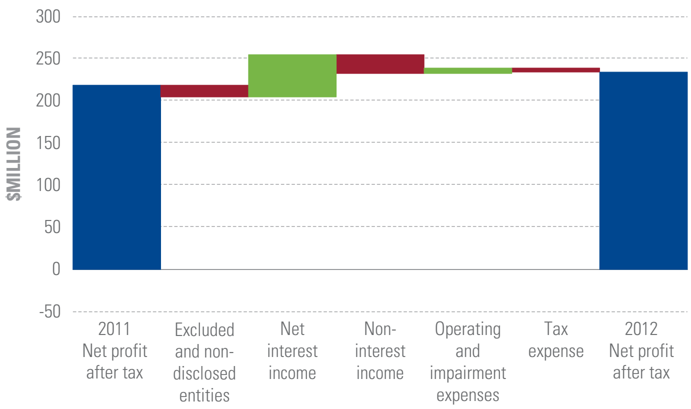
Total assets

Total assets for the sector have increased by 1.64%, growing from $8,375 million in 2011 to $8,512 million in 2012.

On an entity level basis, there has been quite a mixture of increases and decreases in the sector, with seven increasing their assets over the year and five seeing decreases.

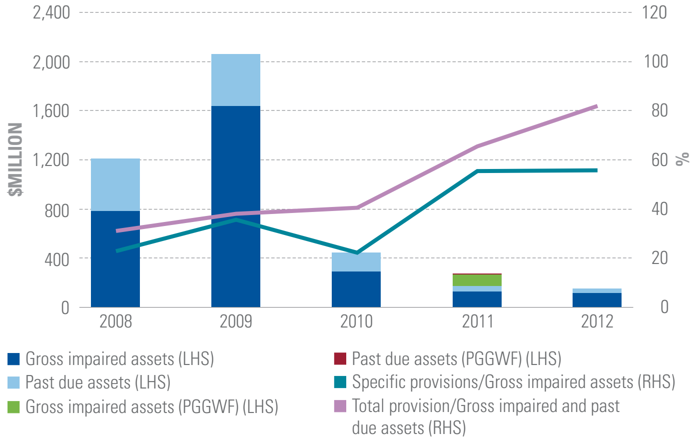
Leading the increases were Fuji Xerox Finance, with a 12.67% increase over the year, and Mercedes-Benz Financial Services, with a 12.07% rise. Fuji Xerox Finance's increase is mostly

36 FINANCE COMPANIES: MOVEMENT IN NET PROFIT AFTER TAX



Excluded and non-disclosed entities are John Deere Financial Limited, The Warehouse Financial Services Limited and PGGWF

37 FINANCE COMPANIES: GROSS IMPAIRED AND PAST DUE ASSETS



driven by a rise in net loans and advances, while Mercedes-Benz Financial Services' rise can be attributed to increases in both net loans and advances and cash on hand, coinciding with an increase in related party funding.

The biggest decreases seen by the sector were in Medical Securities, which dropped by 7.98% over the year, and Orix, which saw a 3.29% decrease. Medical Securities' decrease was due to a fall in net loans and advances, but was slightly offset by an increase in cash on hand. On the other hand, Orix actually saw a rise in net loans and advances, but a drop in leased assets caused a net decrease in assets.

GE Capital had a fairly flat year on the asset growth front. However, when looking at the entities making it up, there was a fair amount of movement. Custom Fleet had a good year for asset growth, managing a 7.98% increase, due to an increase in loans and receivables. GE Commercial Finance saw a large drop in assets, which netted off the increase seen in Custom Fleet, with the movement showing a decrease of 31.62%. This is driven by a large drop in loans and receivables. GE Finance and Insurance stayed fairly flat over the year, which, when combined with the changes in the other two entities, results in an overall flat figure. This shows the benefits of running a diversified business.

Asset quality

There has been a marked improvement in asset quality for the sector as a whole as demonstrated by a variety of measures. Impaired asset expense has decreased from $117 million in 2011 to $63 million in 2012, gross impaired assets have fallen from $128 million to $115 million, past due assets have dropped from $49 million to $35 million, and the impaired asset expense as a proportion of average gross loans and advances ratio has improved from 1.68% in 2011 to 0.92% in 2012.

Looking into the companies driving the decrease in impaired asset expense, GE Capital is by far the largest contributor, with a fall of $43 million. When compared to a total decrease in the sector of $55 million, this is clearly the driving force behind the movement. Within GE Capital, this decrease is being led by Custom Fleet, where the impaired asset expense is $25.5 million lower than in 2011, down from $25.8 million to $0.3 million. GE Finance and Insurance also contributed $14 million towards this decrease. Fisher and Paykel was the other driver behind the decrease in the sector, with its expense down from $19 million in 2011 to $11 million, a drop of $8 million.

The decrease in gross impaired assets was driven by a range of entities. UDC contributed with a drop of $8 million, Fisher & Paykel Finance a drop of $4.5 million and Motor Trade Finance a $3.5 million fall. The general trend for entities in the sector was asset quality improvement. Only two entities in the sector saw an increase in gross impaired assets; Mercedes-Benz, with an increase of $4 million, and Instant Finance with a rise of $1.4 million. It should be noted that not all entities disclose their gross impaired assets.

Past due assets' decrease was largely driven by a decrease in UDC of $8 million, and Fisher & Paykel Finance of $6 million. The rest of the sector saw fairly small movements up and down. Refer to the analysis table for more information.

The best impaired asset expense to gross loans and advances ratios were Orix (-0.46%), Medical Securities (-0.14%) and UDC (0.30%). However, the best improvements in the year were seen by GE Capital, down from 3.74% to 1.62% (a movement of 2.12%) and Fisher & Paykel Finance with a drop from 3.11% to 1.86% (down 1.25%). As these are two of the largest entities in the sector by measure of total assets, these decreases largely drive the trend for the sector. UDC, the other of the three largest entities, was fairly flat between 2011 and 2012. Looking into GE Capital, all three of the entities within this brand improved their ratio between the years, with Custom Fleet having the most dramatic improvement from 5.00% in 2011 to 0.06% in 2012. This follows the trend seen above in impaired asset expense, as this is one of the drivers of this ratio.

Overall, the industry is showing a continued improvement in asset quality, through both the assets held and the expenses incurred.

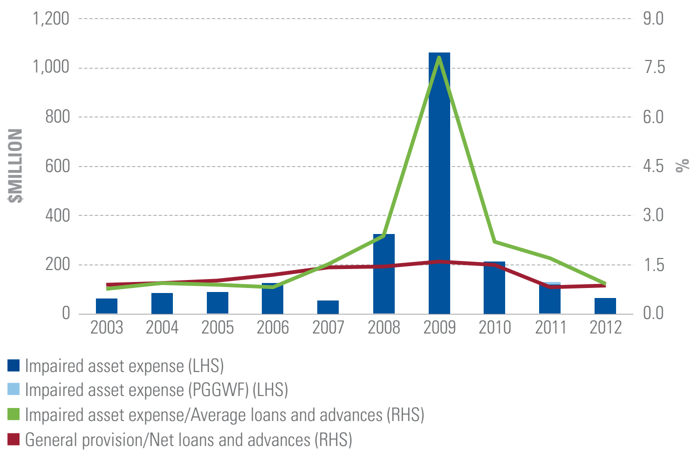
Interest margin

The finance sector has seen an increase in the interest margin overall, from 6.48% in 2011 to 7.21% in 2012, an increase of 73 bps. This is driven by an increase being seen in 10 of the 12 sector participants, with BMW Finance and Avanti Finance leading the increases with rises of 150 bps and 119 bps respectively.

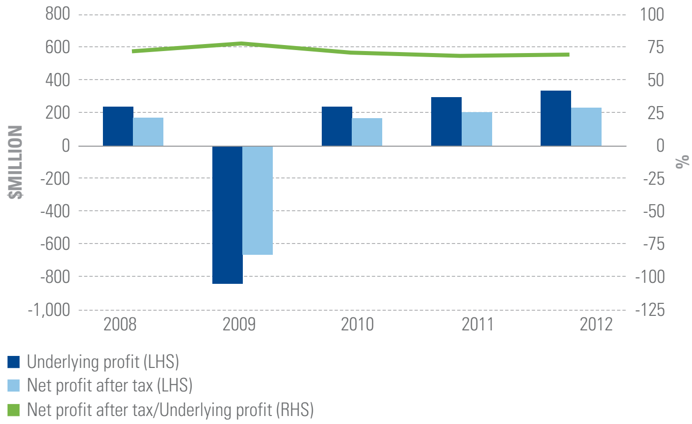
Of the largest five entities, this trend was driven by Motor Trade Finance, Toyota Finance and GE, with fairly significant increases of 114 bps, 102 bps and 80 bps respectively.

Analysis shows this trend is caused by a decrease in the cost of funding for the finance companies which is not being mirrored by pressure on the lending side. This can be shown by interest expense for the industry decreasing from $386 million to $342 million, a decrease of 11.4%, while interest bearing liabilities only decreased by 0.2%. On the flip side, lending has stayed fairly flat, as interest income has increased from $928 million to $935 million, a 0.7% increase, while interest earning assets have increased from $8,134 million to $8,305 million, an increase of 2.1%. This shows that the interest income / interest bearing assets ratio has stayed roughly the same while the interest expense / interest bearing liabilities has changed to a much more favourable ratio for the finance companies.

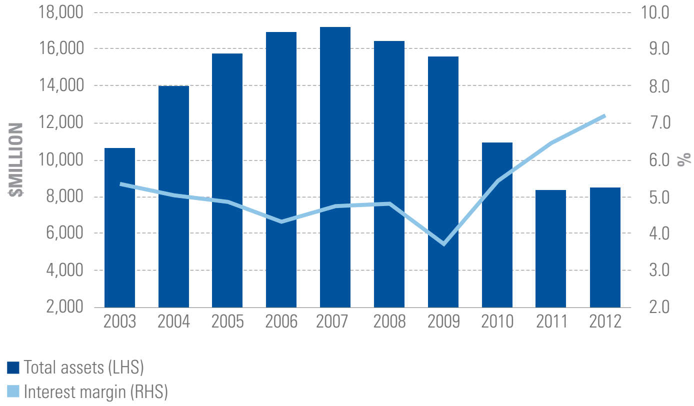
38 FINANCE COMPANIES: IMPAIRED ASSET ANALYSIS



39 FINANCE COMPANIES: UNDERLYING PROFIT AND NET PROFIT AFTER TAX



40 FINANCE COMPANIES: TOTAL ASSETS VS INTEREST MARGIN



Operating expenses

The sector saw an increase in operating expenses as a proportion of operating income, from 43.56% in 2011 to 47.85% in 2012.

Looking at individual Survey participants there was a mix of increases and decreases in this ratio, ranging from a rise of 19.59% to a 16.37% fall.

The largest increases were seen by Toyota Finance New Zealand Limited (19.59%), Fisher & Paykel Finance Group (11.87%) and BMW Financial Services New Zealand Limited (11.04%), while the biggest reductions in this ratio were seen by Mercedes-Benz Financial Services (-16.36%), Orix New Zealand Limited (-13.34%) and Avanti Finance Limited (-8.59%).

Looking at the ratios, Mercedes-Benz Financial Services currently has the best ratio, at 23.27%, while the highest ratio is currently Motor Trade Finances Limited, with 79.28%.

On an overall sector basis, operating income increased by $27.8 million, but this was offset by an even larger rise in operating expenses, which increased by $45.0 million, resulting in an adverse movement in the ratio. Participants of the Survey note that there has been additional expenditure due to IT, regulatory and compliance costs, which partially stem from new regulatory requirements such as the Anti-Money Laundering and Countering Financing of Terrorism Act. This is in line with the trend seen above, as this additional operating expenditure would not result in a proportionate increase in operating income.

Looking at Toyota Finance New Zealand Limited, this increase reverses all of the decrease seen between 2010 and 2011, and further lifts it from its 2010 ratio (46.45% in 2012, 26.86% in 2011 and 38.85% in 2010). The financial statements show a large increase in operating expenses, from $13.4 million in 2011 to $22.6 million in 2012, an increase of $9.2 million. The main drivers of this increase are $2.3 million of additional computer expenses, $1.5 million of additional advertising expenses, $1.7 million of additional dealer support expenses and an extra $1.8 million of salaries, wages and superannuation expenses.

The driver behind the improvement of the ratio for Mercedes-Benz Financial Services is fairly flat operating income combined with a decrease in operating expenses. These operating expenses comprise in part the financial statement caption "other expenses", which has decreased from $3.0 million in 2011 to $1.5 million in 2012. A limited breakdown of these are provided in the notes to the financial statements, which show that there has been a large drop in legal, professional and management fees ($443,000 in 2011 compared to $186,000 in 2012), and a drop in rent and infrastructure costs ($647,000 in 2011 compared to $465,000 in 2012). The notes provide only limited insights into the drivers of this decrease in other expenses. However, we can note that this has not led to a reduction in operating income, thus the ratio has markedly improved.

Performance rankings

	Rank by total assets	Increase in total assets %	Gearing %	Net profit after tax $000's	Interest margin %	Impaired asset expense/ Average loans & advances %	Operating expenses/ Operating income %
Avanti Finance Limited	12	4.64	37.73	6,768	13.37	1.85	42.19
BMW Financial Services New Zealand Limited	9	-1.33	9.05	5,961	6.91	0.35	51.83
Fisher & Paykel Finance Group	4	-2.55	12.09	18,653	10.33	1.86	52.86
Fuji Xerox Finance Limited	8	12.67	23.28	10,272	7.22	1.37	24.63
GE Capital	1	1.05	11.12	95,983	9.15	1.62	46.53
Instant Finance Limited	11	3.85	26.99	6,324	19.57	2.63	60.85
Medical Securities Limited	10	-7.98	20.92	2,854	4.03	-0.14	64.25
Mercedes-Benz Financial Services New Zealand Limited	6	12.07	6.94	7,542	4.52	0.75	23.27
Motor Trade Finances Limited	5	0.68	17.49	4,648	9.45	0.37	79.28
ORIX New Zealand Limited	7	-3.29	34.59	17,219	10.72	-0.46	47.67
Toyota Finance New Zealand Limited	3	-0.92	13.64	20,385	5.17	0.39	46.45
UDC Finance Limited	2	4.58	14.04	37,950	4.27	0.30	34.61
Sector total		**1.64**	**7.97**	**234,559**	**7.21**	**0.92**	**47.85**

gold silver bronze

Analysis of financial statements

ANALYSIS OF CONSOLIDATED ACCOUNTS OF FINANCE COMPANIES[(a)]				Size & strength measures					Growth measures		
	Rank by total assets	Balance date	Year	Total assets $000	Net assets $000	Gearing %	Net loans and advances[(e)] $000	Number of employees[(f)] #	Increase in net profit after tax %	Increase in underlying profit %	Increase in total assets %
Avanti Finance Limited	12	31-Mar	2012	83,860	31,637	37.73	84,428	52	68.57	59.93	4.64
			2011	80,139	28,654	35.76	81,118	44	150.31	156.15	136.43
BMW Financial Services New Zealand Limited	9	31-Dec	2011	249,489	22,585	9.05	235,574	17	49.55	46.08	-1.33
			2010	252,852	21,624	8.55	212,457	17	48.62	46.58	7.76
Fisher & Paykel Finance Group[(d)]	4	31-Mar	2012	772,646	93,393	12.09	594,531	250	-13.92	-7.15	-2.55
			2011	792,835	83,810	10.57	601,596	240	39.03	23.31	4.25
Fuji Xerox Finance Limited	8	31-Mar	2012	261,630	60,917	23.28	250,992	n/d	-6.85	-6.85	12.67
			2011	232,204	50,645	21.81	226,688	n/d	-6.06	1.05	9.17
GE Capital	1	31-Dec	2011	2,526,165	280,876	11.12	1,935,453	708	20.58	15.49	1.05
			2010	2,499,796	184,269	7.37	1,866,270	731	32.54	33.09	-9.44
Instant Finance Limited	11	31-Mar	2012	85,391	23,051	26.99	81,049	121	18.45	14.23	3.85
			2011	82,228	19,806	24.09	76,170	118	63.77	57.60	16.11
Medical Securities Limited	10	31-Mar	2012	232,457	48,631	20.92	182,088	34	-8.23	-10.19	-7.98
			2011	252,629	45,777	18.12	225,255	33	-17.99	-20.98	-2.57
Mercedes-Benz Financial Services New Zealand Limited	6	31-Dec	2011	395,380	27,427	6.94	361,578	24	120.72	104.79	12.07
			2010	352,788	24,885	7.05	333,663	27	-11.22	35.77	4.13
Motor Trade Finances Limited	5	30-Sep	2012	408,060	71,382	17.49	368,542	50	-17.78	-3.92	0.68
			2011	405,320	69,282	17.09	374,655	49	6.54	29.59	-12.35
ORIX New Zealand Limited	7	31-Mar	2012	282,576	97,755	34.59	45,042	64	52.06	41.78	-3.29
			2011	292,187	80,306	27.48	36,650	66	31.16	21.18	-7.96
Toyota Finance New Zealand Limited	3	31-Mar	2012	1,100,660	150,172	13.64	675,330	81	-24.28	-19.04	-0.92
			2011	1,110,887	156,706	14.11	633,891	83	130.71	119.68	9.13
UDC Finance Limited	2	30-Sep	2012	2,114,131	296,894	14.04	2,035,407	167	31.31	26.40	4.58
			2011	2,021,483	278,944	13.80	1,972,269	185	59.07	49.95	-4.98
Finance sector total[(c)]			**2012**	**8,512,445**	**1,204,720**	**7.97**	**6,850,014**	**1,568**	**14.44**	**12.44**	**1.64**
			2011	**8,375,348**	**1,044,708**	**6.91**	**6,640,682**	**1,593**	**225.70**	**518.23**	**-4.72**
GE Management have made a decision to go to market under one brand, GE Capital. Operationally this is occurring; however, legally they operate more than one entity. For the purposes of the above table we have amalgamated the Financial Statements of GE Finance and Insurance and Custom Fleet. For information purposes we include below the data for each entity.											
Custom Fleet NZ[(b)]		31-Dec	2011	1,100,563	n/a	n/a	643,672	n/d	361.07	333.78	7.98
			2010	1,019,213	n/a	n/a	517,314	n/d	-58.19	-61.15	-3.54
GE Finance and Insurance		31-Dec	2011	1,324,036	223,016	16.84	1,220,548	708	-26.66	-29.82	-0.60
			2010	1,332,057	175,019	13.14	1,227,829	731	129.20	140.57	-13.68
GE Commercial Finance NZ		31-Dec	2011	101,566	42,302	41.65	71,233	n/d	-55.26	-42.93	-31.62
			2010	148,526	41,766	28.12	121,127	n/d	-45.24	-44.17	-7.54
At the time the non-banking survey was released in December 2012 these companies had not released their current year financial statements.											
John Deere Financial Limited		31-Oct	2011	99,611	7,481	7.51	95,096	n/d	14.12	7.50	-2.38
The Warehouse Financial Services Limited		30-Sep	2011	91,949	16,851	18.33	73,544	n/d	27.18	27.12	2.27

Key: n/a = not available/applicable; n/d = not disclosed.

Footnotes

Changes in accounting policy that have an immaterial impact on the financial statements have not been detailed in the following footnotes. The effect of the changes listed below has been to impact certain ratios, or to lead to the omission of certain ratios.

(a) Where applicable, consolidated Group numbers have been used.
(b) As at its balance dates, Custom Fleet NZ had goodwill and other intangible assets which exceeded its equity. In accordance with the Survey definitions, total assets and net assets are adjusted to exclude goodwill. We do not believe it is appropriate to present negative net tangible assets or gearing ratios; therefore, where they arise, they have been excluded.
(c) Companies with Total Tangible Assets less than $75 million are excluded from all sector totals.
(d) Fisher & Paykel Finance Group comprises Fisher & Paykel Finance Limited and Fisher & Paykel Finance Holdings Limited (and their respective subsidiaries).
(e) Net loans and advances exclude operating lease assets.
(f) Employee numbers are on a full time equivalent basis (including casuals and contracting staff) at the annual balance date and the prior balance date.

Analysis of financial statements

ANALYSIS OF CONSOLIDATED ACCOUNTS OF FINANCE COMPANIES (CONTINUED)[a]		Credit quality measures					Profitability measures						Efficiency measures	
	Year	Impaired asset expense $000	Provision for doubtful debts/ Gross loans and advances %	Past due assets $000	Gross impaired assets $000	Impaired asset expense/Average loans and advances %	Interest margin %	Interest spread %	Non-interest income/Average total assets %	Net profit after tax $000	Net profit after tax/Average net tangible assets %	Underlying profit $000	Operating expenses/ Average total assets %	Operating expenses/ Operating income %
Avanti Finance Limited	2012	1,538	4.34	208	11,588	1.85	13.37	9.12	9.56	6,768	22.45	9,455	9.78	42.19
	2011	1,311	4.65	250	13,776	2.27	12.18	7.69	13.36	4,015	19.28	5,912	13.07	50.78
BMW Financial Services New Zealand Limited	2011	794	0.85	n/d	n/d	0.35	6.91	6.36	0.68	5,961	26.97	8,321	3.90	51.83
	2010	2,173	0.94	n/d	n/d	1.06	5.41	4.73	0.07	3,986	17.73	5,696	2.22	40.79
Fisher & Paykel Finance Group[d]	2012	11,112	0.00	26,376	29,584	1.86	10.33	9.89	3.34	18,653	21.05	34,733	6.57	52.86
	2011	19,348	0.00	32,252	34,036	3.11	10.11	9.68	3.41	21,669	26.80	37,406	5.08	40.99
Fuji Xerox Finance Limited	2012	3,280	0.00	n/d	n/d	1.37	7.22	6.52	0.10	10,272	18.41	10,122	1.77	24.63
	2011	2,056	0.00	n/d	n/d	0.95	8.17	7.42	-0.26	11,027	24.43	10,866	2.03	25.93
GE Capital	2011	31,774	2.15	n/d	n/d	1.62	9.15	8.59	3.76	95,983	41.27	136,619	5.83	46.53
	2010	74,958	3.47	n/d	n/d	3.74	8.35	8.02	4.29	79,600	55.18	118,296	4.87	39.84
Instant Finance Limited	2012	2,066	3.84	0	4,929	2.63	19.57	15.76	15.55	6,324	29.51	9,311	21.10	60.85
	2011	1,008	3.85	0	3,550	1.40	19.28	15.42	16.61	5,339	28.58	8,151	23.38	66.14
Medical Securities Limited	2012	-294	0.32	36	n/d	-0.14	4.03	3.01	0.26	2,854	6.05	3,999	2.75	64.25
	2011	946	0.44	43	n/d	0.40	4.44	3.56	0.28	3,110	7.03	4,453	2.61	55.28
Mercedes-Benz Financial Services New Zealand Limited	2011	2,605	2.35	307	8,519	0.75	4.52	3.99	0.00	7,542	28.83	10,471	1.06	23.27
	2010	3,911	2.30	269	4,194	1.18	4.32	3.72	0.00	3,417	14.44	5,113	1.71	39.63
Motor Trade Finances Limited	2012	1,396	1.09	89	1,007	0.37	9.45	8.02	2.69	4,648	6.61	8,656	9.46	79.28
	2011	980	1.26	58	4,494	0.25	8.31	6.64	2.16	5,653	8.34	9,009	7.98	77.61
ORIX New Zealand Limited	2012	-191	2.08	n/d	329	-0.46	10.72	9.99	4.90	17,219	19.34	22,886	7.19	47.67
	2011	-79	3.06	n/d	958	-0.18	10.23	9.01	3.81	11,324	15.32	16,142	8.25	61.01
Toyota Finance New Zealand Limited	2012	2,550	2.83	40	4,077	0.39	5.17	4.53	0.44	20,385	13.29	30,434	2.59	46.45
	2011	5,699	2.88	991	4,240	0.90	4.15	3.34	1.44	26,921	18.79	37,590	1.49	26.86
UDC Finance Limited	2012	6,031	1.87	7,520	55,403	0.30	4.27	3.48	0.04	37,950	13.18	52,445	1.50	34.61
	2011	4,891	2.13	15,539	63,107	0.24	3.69	2.85	0.04	28,901	10.93	41,491	1.50	40.20
Finance sector total[c]	**2012**	**62,661**	**1.78**	**34,576**	**115,436**	**0.92**	**7.21**	**6.44**	**2.07**	**234,559**	**20.85**	**337,452**	**4.35**	**47.85**
	2011	**117,202**	**2.25**	**49,402**	**128,355**	**1.68**	**6.48**	**5.85**	**2.30**	**204,962**	**24.08**	**300,125**	**3.75**	**43.56**
GE Management have made a decision to go to market under one brand, GE Capital. Operationally this is occurring; however, legally they operate more than one entity. For the purposes of the above table we have amalgamated the Financial Statements of GE Finance and Insurance and Custom Fleet. For information purposes we include below the data for each entity.														
Custom Fleet NZ[b]	2011	333	0.93	n/d	n/d	0.06	7.78	7.66	1.48	46,130	n/a	64,793	2.89	31.99
	2010	25,839	3.93	n/d	n/d	5.00	6.18	6.28	1.41	10,005	n/a	14,937	3.39	46.31
GE Finance and Insurance	2011	32,392	2.90	n/d	n/d	2.56	10.74	9.86	5.86	47,997	24.12	68,726	8.56	52.93
	2010	46,151	3.61	n/d	n/d	3.39	10.00	9.38	6.78	65,447	45.99	97,927	6.29	38.58
GE Commercial Finance NZ	2011	-951	0.00	n/d	n/d	-0.99	3.31	2.51	0.69	1,856	4.42	3,100	1.75	50.50
	2010	2,968	0.00	n/d	n/d	2.36	7.49	7.11	0.51	4,148	10.45	5,432	1.51	21.76
At the time the non-banking survey was released in December 2012 these companies had not released their current year financial statements.														
John Deere Financial Limited	2011	3	0.00	n/d	n/d	0.00	4.62	4.40	0.06	1,980	30.50	2,751	1.93	41.34
The Warehouse Financial Services Limited	2011	767	3.94	n/d	2,894	1.03	11.14	10.41	6.04	7,500	49.83	10,761	4.72	27.13

Key: n/a = not available/applicable; n/d = not disclosed.

Footnotes

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(c) Companies with Total Tangible Assets less than $75 million are excluded from all sector totals.
(d) Fisher & Paykel Finance Group comprises Fisher & Paykel Finance Limited and Fisher & Paykel Finance Holdings Limited (and their respective subsidiaries).

Savings institutions sector performance

Overview of results

The 2012 Survey of savings institutions has seen a mixed result in profitability for sector participants. Overall, profitability for the sector has increased, on the back of a decline in the level of impaired asset expenditure, as the credit quality continues to improve. The remaining Survey participants have weathered the GFC storm and are now positioning themselves to build on their standing in the market.

One way participants are positioning themselves in the market is through amalgamations and mergers, which are continuing to occur in the sector. This is illustrated by the merger of Credit Union Baywide and Manchester Unity Credit Union (although a sector participant, the latter is below the threshold for inclusion in the survey) and more recently, in December 2012, the merger of Credit Union North and First Credit Union. These mergers are likely occurring as entities try to achieve economies of scale in light of increasing costs, and to combat competition faced in the market place.

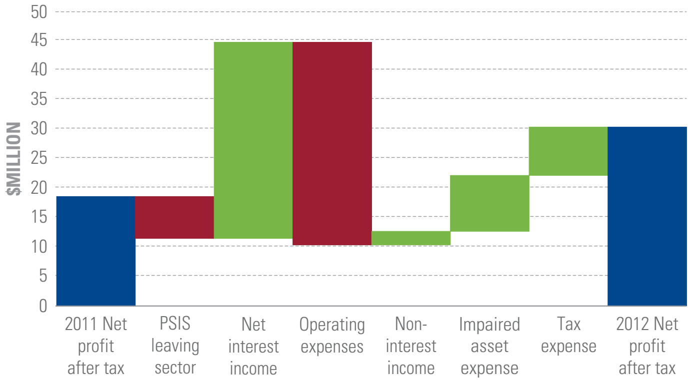
A driver behind increasing costs is new and amended regulation. As noted in our regulatory change and challenges section of this publication, there is a suite of new and amended regulation coming into force in 2013 such as the Anti-Money Laundering and Countering Financing of Terrorism Act. These new regulations are increasing IT and compliance costs.

Competition in the residential lending market, which the sector is heavily involved in, remains intense with asset growth difficult. This is driven by all registered banks offering customers competitive rates in this market, which is putting a squeeze on margins.

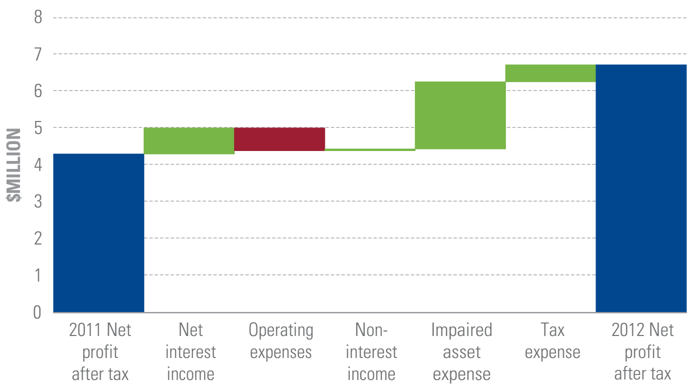
As commented in the 2011 Survey, The Co-operative Bank has moved out of the savings institutions sector and is now reported under the registered bank sector. On 17 December 2012 the RBNZ announced that Heartland Building Society, a key subsidiary of Heartland New Zealand Limited (Heartland), had been registered as a bank in New Zealand. As Heartland's most recent balance date was 30 June 2012, and it was a building society at that date, it has been included in the savings institutions sector analysis for this Survey.

As a result of prior year amalgamations, mergers, and the exit of The Co-operative Bank and SBS due to obtaining registered bank status, the sector has reduced in size to a point where Heartland makes up a significant proportion of the sector. This means Heartland's trends and performance have a significant impact on the trends of the sector. To take account of this, we will discuss the trends of the sector either as trends of the total sector, which includes Heartland, or as a total sector without Heartland, to be referred to as the sub-sector.

41 TOTAL SECTOR – MOVEMENT IN NET PROFIT AFTER TAX



42 SUB SECTOR – MOVEMENT IN NET PROFIT AFTER TAX



Profitability

Reported net profit for the total sector was $30.34 million, an increase of $18.89 million or 165% over the prior year. The sub-sector reported a net profit of $6.73 million, which equated to an increase of $2.43 million or 56%.

Driving the rise in profitability in the sub-sector was CU North and Wairarapa BS, with increases of $1.77 million (237% increase) and $1.10 million (130%) respectively over the prior year.

CU North significantly reduced its impaired asset expense in the current year, to $0.37 million compared to $1.90 million in the prior year, and employee benefit expenditure also saw a decrease of $0.88 million, both of which significantly contributed to the improved profitability. These favourable movements were partially offset by a reduction in net interest income of $0.96 million.

Wairarapa BS increased its net profit after tax to $0.25 million from a loss of $0.85 million in the prior year, an increase of 130%. Looking into the drivers for the change in profitability, the following favourable movements are noted; interest income was up $0.12 million, no asset impairment expense was reported in 2012 compared to an expense in the prior year of $0.18 million, there was a reduction in the fair value loss on investment property of $0.21 million and there was a one off deferred tax expense in the prior year of $0.35 million.

CU Baywide, First CU, CU South and Police & Families CU all had decreases in net profit after tax compared to the prior year. CU South fell by 52%. The primary reason for this was stated by the CEO in the latest Annual Report to be "principally driven by a significant fall in member demand for personal loans".

Heartland had a spectacular rise in reported net profit after tax of $16.46 million or 230%. The increase was driven by a significant fall in the impaired asset expense, which decreased by $7.66 million in 2012. Profit before impaired asset expense and income tax rose by $4.52 million on the back of an increase in net interest margin. However, this was offset by an increase in operating expenses, which would include banking license costs.

Net interest margin

The sector as a whole improved its net interest margin (NIM) by 14 bps to 4.09% in the 2012 year. However, the sub-sector actually decreased its NIM by 26 bps to 4.46%, which is an indication there is continuing downward pressure on margins for the smaller operators.

TABLE 12: MEMBERS GROSS LOANS

Entity	2012 $'000	2011 $'000	Movement $'000	Movement %
Credit Union Baywide	160,426	122,869	37,557	31%
First Credit Union	71,496	70,070	1,426	2%
Credit Union North	69,548	71,972	-2,424	-3%
Credit Union South	74,808	86,709	-11,901	-14%
Nelson Building Society	254,715	225,106	29,609	13%
Police & Families Credit Union	53,863	50,955	2,908	6%
Wairarapa Building Society	82,660	88,793	-6,133	-7%
Sub-sector total	**767,516**	**716,474**	**51,042**	**7%**
Heartland New Zealand Limited	2,105,702	1,745,608	360,094	21%
Sector total	**2,873,218**	**2,462,082**	**411,136**	**17%**

TABLE 13: MEMBERS GROSS DEPOSITS

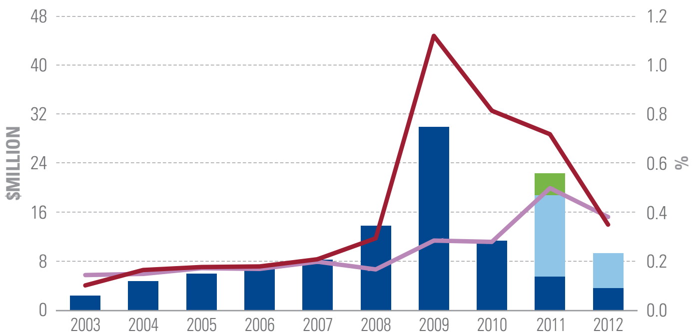
Entity	2012 $'000	2011 $'000	Movement $'000	Movement %
Credit Union Baywide	185,225	138,618	46,607	34%
First Credit Union	94,036	86,961	7,075	8%
Credit Union North	83,962	88,363	-4,401	-5%
Credit Union South	93,227	95,110	-1,883	-2%
Nelson Building Society	318,192	276,359	41,833	15%
Police & Families Credit Union	72,668	68,588	4,080	6%
Wairarapa Building Society	86,712	92,967	-6,255	-7%
Sub-sector total	**934,022**	**846,966**	**87,056**	**10%**
Heartland New Zealand Limited	1,939,489	1,787,524	151,965	9%
Sector total	**2,873,511**	**2,634,490**	**239,021**	**9%**

Out of the seven participants of the sub-sector, four increased their NIM and three saw decreases. CU Baywide had the largest reduction in NIM, of 92 bps to 5.90%.

CU Baywide's decrease in NIM appears to be due to the merger with Manchester Unity Credit Union (CU) which happened on the 29 June 2012. As this date is close to its year end date, no interest income and expense from the Manchester Unity CU was included in the income statement, but all the interest earning assets of Manchester Unity CU have been included on the balance sheet. Therefore, the denominator used in the NIM calculation has been increased without the corresponding net interest income. If Manchester Unity CU's interest earning assets were excluded as of year-end date, the adjusted NIM would have been 6.73%, a decrease of only 9 bps compared to the prior year.

Nelson BS marginally increased its NIM year on year to 2.41% up 7 bps. Nelson BS also had a

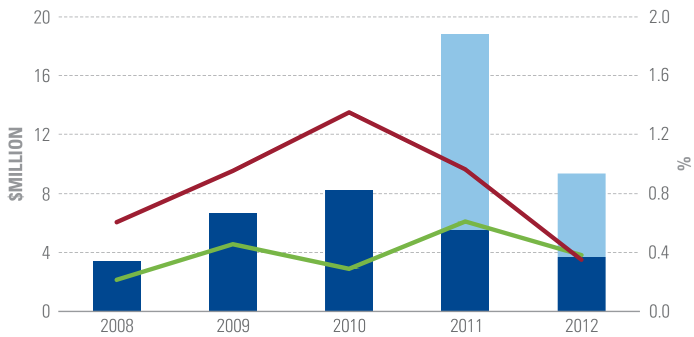
43 IMPAIRED ASSET ANALYSIS



- Impaired asset expense (LHS)
- Impaired asset expense (LHS) – Balance of the total represented by Heartland New Zealand Limited
- Impaired asset expense (LHS) – Balance of the total represented by PSIS
- Collective provision/Net loans and advances (RHS)
- Impaired asset expense/Average loans and advances (RHS)

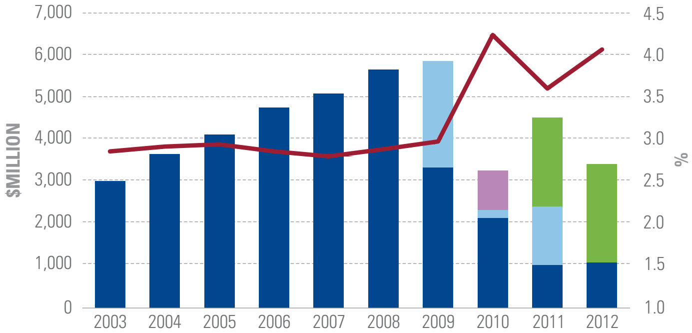
44 IMPAIRED ASSET ANALYSIS

All years have been restated to show the eight entities that are in this period



- Impaired asset expense (LHS)
- Impaired asset expense (LHS) – Balance of the total represented by Heartland New Zealand Limited
- Collective provision/Net loans and advances (RHS)
- Impaired asset expense/Average loans and advances (RHS)

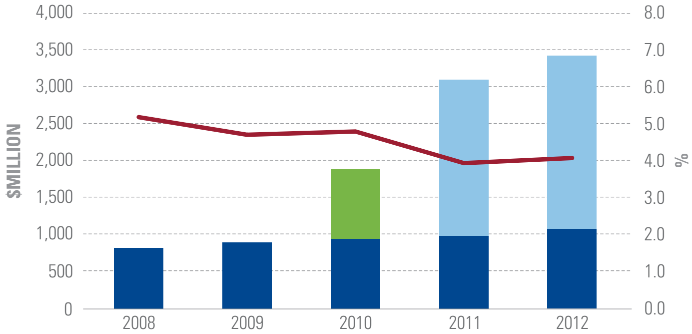
45 TOTAL ASSETS VS INTEREST MARGIN



- Total assets (LHS)
- Total assets (LHS) Companies leaving sector (2009 SBS, 2010 HBS, 2011 PSIS)
- Total assets (LHS) Quantum represented by Heartland New Zealand Limited
- Total assets (LHS) CBS/SCBS (which forms part of Heartland New Zealand Limited in 2011)
- Interest margin (RHS)

46 TOTAL ASSETS VS INTEREST MARGIN

For the eight entities included in the 2012 Survey



- Total assets (LHS)
- Total assets (Heartland New Zealand Limited) (LHS)
- Total assets (CBS/SCBS – which forms part of Heartland New Zealand Limited in 2011) (LHS)
- Interest margin (RHS)

good increase in net loans and advances, which were up 13%. During the year, cash and cash equivalent assets fell by 32% while term investments rose by 162%. This shift from cash to term investments would have had a favourable impact on net interest margin, as higher returns are earned on term investments.

Heartland increased its NIM from 2.51% to 3.74% (123 bps). Behind this increase, it was noted that net interest income increased by $22.05 million and net loans and advances increased by 21%, an increase of $367 million. These increases are driven by the acquisition of PGG Wrightson Finance Limited, which occurred on 31 August 2011. The acquisition resulted in a change in lending mix, and this, combined with a lower funding cost, have resulted in a positive impact on the overall net interest margin.

Impaired asset expense

The impaired asset expense continues to trend down since the peak in 2009 (see figure 43). Year on year, the total sector impaired asset expense has decreased by $9.48 million (50.3%).

The biggest contributor to the fall in the impaired asset expense is Heartland, which reduced its impairment expense by $7.66 million to $5.64 million (see figure 44), a decrease of 57.6%. Heartland's past due assets fell by 22.6% from $67.20 million to $52.00 million and coupled with this, their gross impaired assets reduced from $68.54 million to $56.83 million. The decreases noted across all these measures indicate an improvement in the quality of the loan book. Looking into the detail of the Heartland accounts, it can be seen that the investment property balance has increased significantly during the year. This could be explained by past due and impaired property loans' underlying securities being acquired by Heartland and the corresponding loan written off, thus reducing the gross impaired and past due loan balances.

The sub-sector also decreased its impaired asset expense year on year, with a reduction of $1.82 million (32.9%) to $3.72 million. Leading the decrease was CU North, whose impaired asset expense fell by $1.53 million, an 80.5% reduction. The largest contributor to the sub-sector impaired asset expense was CU South at $1.67 million, which reported an increase of 6.4%.

Gross impaired assets across the sub-sector also fell, by $2.29 million (15.4%). The largest reductions were reported by CU Baywide and CU South, with decreases of $1.25 million and $1.21 million respectively. CU North went against the trend, rising by $0.83 million. Overall, the sector is continuing to see a gradual improvement in the quality of loan assets, as indicated by the analysis above.

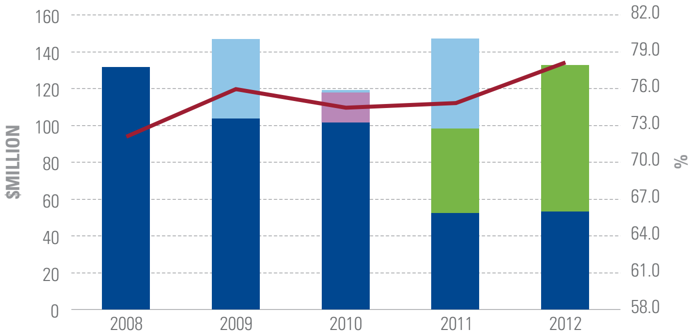
Total assets

Total assets for the sector rose from $3,105 million to $3,430 million over the year, a $325 million or 10.5% increase.

In the sub-sector, this change was an increase of $96 million to $1,085 million. This rise was predominantly driven by CU Baywide, which saw an increase of $51 million (30.4%), and Nelson BS, up $44 million (14.7%). CU Baywide's higher number was mainly due to its merger with Manchester Unity Credit Union, which contributed assets of $47.2 million. The rest of the sub-sector saw relatively little change, with results ranging between the 7% increase seen by CU Baywide and the 6% decrease at Wairarapa BS.

Driving these rises in total assets is growth in loans and advances. The sub-sector saw a $53 million increase in net loans and advances over the year. CU Baywide ($37.5 million) and Nelson BS ($29.6 million) were the drivers of the increase, which is consistent with the rises in total assets seen above. However, slightly offsetting this increase in net loans and advances was CU South, which saw a slight fall of $10.8 million over the year. CU Baywide's increase, as noted above, was predominantly due to its merger with Manchester Unity Credit Union, which boosted net loans and advances by $31.6 million.

47 OPERATING EXPENSES VS OPERATING EXPENSES/OPERATING INCOME



- Operating expenses (LHS)
- Operating expenses – Entities leaving sector (2009: SBS, 2010: HBS, 2011: The Co-operative Bank (formally known as PSIS))
- Operating expenses – Heartland NZ Limited
- Operating expenses – CBS/SCBS – which forms part of Heartland in 2011
- Operating expenses/Operating income (RHS)

Heartland's total assets rose by $229 million to a year-end figure of $2,345 million. This was driven largely by an increase in net loans and advances, which rose by $367 million. This was largely a result of the acquisition of PGG Wrightson Finance Limited. The increase was partially offset by a reduction in cash and cash equivalents.

Operating expenses

Operating expenses as a proportion of operating income for the sector saw an unfavourable increase – from 73.23% to 78.13%.

For the sub-sector, the operating expense to operating income ratio has been fairly flat, with only a 1 basis point movement over the year (from 82.67 to 82.66). However, the almost-unchanged number for the sector disguised a wide range of results from individual entities.

The largest increase was reported by Police & Families CU, up 7.15%, which brings its ratio to 65.32% for the year. The decreasers are led by Wairarapa BS, whose ratio fell by 26.78%, bringing the ratio down to 88.85%.

To put the changes into perspective; even though Police & Families CU saw the largest rise in its ratio, it still has the lowest ratio in the sector. And Wairarapa BS's decrease only sees its position within the sector change from the highest operating expense to operating income ratio to second highest. For Heartland, the operating expense to operating income ratio has increased quite dramatically from 64.72% to 75.35% and this is driving the overall sector movement. An analysis of the factors making up the ratio shows operating income has increased by $34.8 million from 2011, while operating expenses have increased by $33.7 million.

A closer look into the detail of Heartland's operating expenses shows the lift in operating expenses is largely driven by a rise in personnel expenses of $12.4 million (57%) and an increase of other operating expenses of $7.0 million (53%).

Performance rankings

	Rank by total assets	Increase in total assets %	Gearing %	Net profit after tax $'000	Interest margin %	Impaired asset expense/ Average loans & advances %	Operating expenses/ Operating income %
Credit Union Baywide	3	30.43	14.43	1,186	5.90	0.53	86.51
First Credit Union	4	7.33	18.37	877	5.03	0.92	79.56
Credit Union North	7	-3.49	16.15	1,023	5.25	0.52	89.19
Credit Union South	5	1.99	16.11	407	8.80	2.02	85.70
Heartland New Zealand Limited	1	10.81	15.86	23,606	3.74	0.27	75.35
Nelson Building Society	2	14.69	5.88	1,672	2.41	0.11	69.94
Police & Families Credit Union	8	6.59	16.43	1,318	4.35	0.05	65.32
Wairarapa Building Society	6	-5.87	14.96	251	1.87	0.00	88.85
Sector total		**10.47**	**14.87**	**30,340**	**4.09**	**0.35**	**78.13**

gold silver bronze

Analysis of financial statements

ANALYSIS OF CONSOLIDATED ACCOUNTS OF SAVINGS INSTITUTIONS				Size & strength measures					Growth measures		
	Rank by total assets	Balance date	Year	Total assets $'000	Net assets $'000	Gearing %	Net loans and advances $'000	Number of employees #	Increase in net profit after tax %	Increase in underlying profit %	Increase in total assets %
Credit Union Baywide[a]	3	30-Jun	2012	218,498	31,538	14.43	158,617	99	-1.66	-1.59	30.43
			2011	*167,518*	*27,300*	*16.30*	*121,113*	*97*	*-18.95*	*-19.56*	*12.51*
First Credit Union	4	30-Jun	2012	116,901	21,469	18.37	70,990	46	-6.70	-6.70	7.33
			2011	*108,914*	*20,592*	*18.91*	*69,815*	*44*	*-9.18*	*-9.18*	*2.74*
Credit Union North[b]	7	30-Jun	2012	103,373	16,690	16.15	68,698	103	236.95	236.95	-3.49
			2011	*107,112*	*15,667*	*14.63*	*70,816*	*106*	*-215.99*	*-215.99*	*-6.54*
Credit Union South[c]	5	30-Jun	2012	114,888	18,512	16.11	74,741	95	-43.00	-43.00	1.99
			2011	*116,207*	*18,105*	*15.58*	*85,531*	*96*	*7.04*	*7.04*	*8.09*
Nelson Building Society	2	31-Mar	2012	339,856	19,976	5.88	254,615	34	25.90	11.16	14.69
			2011	*296,321*	*18,312*	*6.18*	*225,006*	*30*	*-9.66*	*-4.16*	*8.71*
Police & Families Credit Union	8	30-Jun	2012	87,430	14,363	16.43	53,850	13	-16.53	-16.53	6.59
			2011	*82,023*	*13,111*	*15.98*	*50,933*	*12*	*12.71*	*12.71*	*8.09*
Wairarapa Building Society	6	31-Mar	2012	104,067	15,570	14.96	82,660	8	129.49	156.42	-5.87
			2011	*110,556*	*15,319*	*13.86*	*87,690*	*8*	*-1,991.11*	*-9,600.00*	*-4.23*
Sub-sector total			**2012**	**1,085,013**	**138,118**	**12.73**	**764,171**	**398**	**56.39**	**35.63**	**9.75**
			2011	***988,651***	***128,406***	***12.99***	***710,904***	***393***	***-36.65***	***-27.13***	***4.50***
Heartland New Zealand Limited	1	30-Jun	2012	2,345,379	372,088	15.86	2,086,308	353	230.48	75.23	10.81
			2011	*2,116,535*	*294,991*	*13.94*	*1,719,451*	*338*	*355.84*	*695.84*	*124.37*
Sector total			**2012**	**3,430,392**	**510,206**	**14.87**	**2,850,479**	**751**	**165.00**	**62.50**	**10.47**
			2011	***3,105,186***	***423,397***	***13.64***	***2,430,355***	***731***	***185.87***	***205.45***	***64.35***

ANALYSIS OF CONSOLIDATED ACCOUNTS OF SAVINGS INSTITUTIONS (CONTINUED)		Credit quality measures					Profitability measures						Efficiency measures	
	Year	Impaired asset expense $'000	Provision for doubtful debts/Gross loans and advances %	Past due assets $'000	Gross impaired assets $'000	Impaired asset expense/Average loans and advances %	Interest margin %	Interest spread %	Non-interest income/Average total assets %	Net profit after tax $'000	Net profit after tax/ Average total assets %	Underlying profit $'000	Operating expenses/ Average total assets %	Operating expenses/ Operating income %
Credit Union Baywide[a]	2012	751	1.20	n/d	4,434	0.53	5.90	5.39	1.81	1,186	0.61	1,234	6.60	86.51
	2011	*1,384*	*1.56*	*n/d*	*5,682*	*1.15*	*6.82*	*6.14*	*2.22*	*1,206*	*0.76*	*1,254*	*7.26*	*81.33*
First Credit Union	2012	651	1.23	177	2,002	0.92	5.03	4.28	1.71	877	0.78	877	5.27	79.56
	2011	*467*	*0.68*	*71*	*1,982*	*0.65*	*5.22*	*4.46*	*1.79*	*940*	*0.87*	*940*	*5.56*	*80.93*
Credit Union North[b]	2012	370	2.37	169	2,781	0.52	5.25	4.66	7.13	1,023	0.97	1,023	10.92	89.19
	2011	*1,896*	*2.76*	*37*	*1,948*	*2.42*	*5.89*	*5.30*	*7.08*	*-747*	*-0.67*	*-747*	*11.77*	*91.90*
Credit Union South[c]	2012	1,667	1.73	0	3,140	2.02	8.80	8.19	4.01	407	0.36	407	10.93	85.70
	2011	*1,567*	*2.80*	*0*	*4,354*	*1.78*	*9.37*	*8.70*	*4.04*	*851*	*0.76*	*851*	*11.18*	*83.80*
Nelson Building Society	2012	252	0.13	0	0	0.11	2.41	2.17	0.33	1,672	0.53	2,330	1.89	69.94
	2011	*29*	*0.10*	*8*	*161*	*0.01*	*2.34*	*2.10*	*0.29*	*1,328*	*0.47*	*2,096*	*1.84*	*71.13*
Police & Families Credit Union	2012	28	0.25	183	194	0.05	4.35	3.79	0.24	1,318	1.56	1,318	2.99	65.32
	2011	*20*	*0.24*	*0*	*420*	*0.04*	*4.32*	*3.72*	*0.52*	*1,579*	*2.00*	*1,579*	*2.82*	*58.17*
Wairarapa Building Society	2012	0	0.00	201	0	0.00	1.87	1.61	0.57	251	0.23	268	1.99	88.85
	2011	*179*	*1.24*	*157*	*295*	*0.19*	*1.63*	*1.27*	*0.20*	*-851*	*-0.75*	*-475*	*1.94*	*115.63*
Sub-sector total	**2012**	**3,719**	**0.81**	**730**	**12,551**	**0.50**	**4.46**	**3.98**	**1.86**	**6,734**	**0.65**	**7,457**	**5.14**	**82.66**
	2011	***5,542***	***1.15***	***273***	***14,842***	***0.76***	***4.72***	***4.18***	***1.99***	***4,306***	***0.45***	***5,498***	***5.44***	***82.67***
Heartland New Zealand Limited	2012	5,642	1.30	52,004	56,825	0.27	3.74	2.90	0.93	23,606	1.01	20,329	3.39	75.35
	2011	*13,298*	*2.19*	*67,198*	*68,537*	*0.76*	*2.51*	*1.74*	*0.92*	*7,143*	*0.34*	*11,601*	*2.16*	*64.72*
Sector total	**2012**	**9,361**	**1.17**	**52,734**	**69,376**	**0.35**	**4.09**	**3.37**	**1.26**	**30,340**	**0.93**	**27,786**	**4.06**	**78.13**
	2011	***18,840***	***1.89***	***67,471***	***83,379***	***0.97***	***3.95***	***3.17***	***1.55***	***11,449***	***0.46***	***17,099***	***3.94***	***73.23***

Key: n/a = not available/applicable; n/d = not disclosed.

Footnotes

(a) The trading name of Credit Union Baywide is NZCU Baywide.
(b) The trading name of Credit Union North is NZCU North.
(c) The trading name of Credit Union South is NZCU South.

Registered banks

Ownership, credit ratings and descriptions of the rating grades (as at 31 December 2012)

Registered banks	Ultimate shareholdings	%	Long-term credit rating		
			Standard & Poor's	Moody's	Fitch
ANZ Bank New Zealand Limited	Australia and New Zealand Banking Group Limited	100	AA-	Aa3	AA-
ASB Bank Limited	Commonwealth Bank of Australia Limited	100	AA-	Aa3	AA-
Australia and New Zealand Banking Group Limited – New Zealand Branch[(a)]	Australia and New Zealand Banking Group Limited	100	AA-	Aa2	AA-
Bank of Baroda (New Zealand) Limited	Bank of Baroda (India)	100	-	Baa3[(b)]	BBB-
Bank of India (New Zealand) Limited	Bank of India (India)	100	BBB-	Baa3[(c)]	-
Bank of New Zealand	National Australia Bank Limited	100	AA-	Aa3	AA-
Citibank, N.A. New Zealand Branch and Associated Banking Group[(d)]	Citigroup Inc.	100	A	A3	A
Commonwealth Bank of Australia New Zealand Branch[(e)]	Commonwealth Bank of Australia Limited	100	AA-	Aa2	AA-
Deutsche Bank AG, New Zealand Branch[(f)]	Deutsche Bank AG	100	A+	A2	A+
JPMorgan Chase Bank, N.A. New Zealand Branch[(g)]	JPMorgan Chase & Co.	100	A+	Aa3	A+
Kiwibank Limited	New Zealand Post Limited/New Zealand Government	100	A+	Aa3	AA
Kookmin Bank Auckland Branch[(h)]	KB Financial Group Inc.	100	A	A1	A
Rabobank Nederland New Zealand Banking Group[(i)]	Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.	100	AA-	Aa2	AA
Rabobank New Zealand Limited	Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.	100	AA-	-	-
Southland Building Society	Mutual	100	-	-	BBB
The Bank of Tokyo-Mitsubishi UFJ Limited, Auckland Branch[(j)]	The Bank of Tokyo-Mitsubishi UFJ Ltd.	100	A+	Aa3	A-
The Co-operative Bank Limited	Co-operative	100	BBB-	-	-
The Hongkong and Shanghai Banking Corporation Limited, New Zealand Branch[(k)]	HSBC Holdings plc	100	A+	Aa3	AA-
TSB Bank Limited	TSB Community Trust	100	BBB+	-	-
Westpac Banking Corporation – New Zealand Division[(l)]	Westpac Banking Corporation	100	AA-	Aa2	AA-
Westpac New Zealand Limited	Westpac Banking Corporation	100	AA-	Aa3	AA-

Long-term credit ratings grades assigned by Standard & Poor's	Description of the steps in the Standard & Poor's credit rating grades for the rating of the long-term senior unsecured obligations payable in New Zealand, in New Zealand dollars.
AAA	Extremely strong capacity to meet financial commitments. Highest Rating.
AA	Very strong capacity to meet financial commitments.
A	Strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances.
BBB	Adequate capacity to meet financial commitments, but more subject to adverse economic conditions.
BB	Less vulnerable in the near-term but faces major ongoing uncertainties to adverse business, financial and economic conditions.
B	More vulnerable to adverse business, financial and economic conditions but currently has the capacity to meet financial commitments.
CCC	Currently vulnerable and dependent on favourable business, financial and economic conditions to meet financial commitments.
CC	Currently highly vulnerable.
Plus (+) or Minus (-)	The ratings from AA to CCC may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.
BB, B, CCC and CC	Borrowers rated BB, B, CCC, and CC are regarded as having significant speculative characteristics. BB indicates the least degree of speculation and CC the highest. While such borrowers will likely have some quality and protective characteristics, these may be outweighed by large uncertainties or major exposures to adverse conditions.
Assigned by Moody's Investors Service	Moody's Investors Service appends numerical modifiers 1, 2 and 3 in each generic rating classification from Aa through Caa. The modifier 1 indicates the obligation ranks in the higher end of its generic category; the modifier 2 indicates a mid range ranking; and the modifier 3 indicates the lower end of that generic category.
Assigned by Fitch Ratings	Fitch Ratings applies "investment grade" rates 'AAA' to 'BBB' to indicate relatively low to moderate credit risk, while those in the "speculative" or "non-investment grade" categories which have either signalled a higher level of credit risk or that a default has already occurred, Fitch Ratings applies a 'BB' to 'D' rating. The modifiers "+" or "-" may be appended to a rating to denote relative status within major rating categories. Credit ratings express risk in relative rank order, which to say they are ordinal measures of credit risk and not predictive of a specific frequency of default or loss.

Footnotes

(a) Rating of ANZ Banking Group Limited.
(b) Rating of Bank of Baroda (India).
(c) Rating of Bank of India (India).
(d) Rating of Citibank N.A.
(e) Rating of Commonwealth Bank of Australia.
(f) Rating of Deutsche Bank AG.
(g) Rating of JPMorgan Chase Bank, N.A.
(h) Rating of Kookmin Bank (South Korea).
(i) Rating of Rabobank Nederland.
(j) Rating of The Bank of Tokyo-Mitsubishi UFJ Limited.
(k) Rating of HSBC Holdings plc.
(l) Rating of Westpac Banking Corporation (Australia).

Non-banks

Ownership and credit ratings (as at 31 December 2012)

Finance company	Ultimate shareholding	%
Avanti Finance Limited	Various investment/nominee companies	100
BMW Financial Services New Zealand Limited	BMW AG	100
Fisher & Paykel Finance Group	Haier (Singapore) Management Holding Co. Pte. Limited	100
Fuji Xerox Finance Limited	Fuji Xerox Co. Ltd (Japan)	100
GE Capital[(a)]	General Electric Company	100
Instant Finance Limited	Various Private Shareholders	100
John Deere Financial Limited	Deere & Company (USA)	100
Medical Securities Limited	Medical Assurance Society New Zealand Limited	100

Finance company	Ultimate shareholding	%
Mercedes-Benz Financial Services New Zealand Limited	Daimler AG	100
Motor Trade Finances Limited	Various Licensed Motor Vehicle Dealers	100
ORIX New Zealand Limited	ORIX Corporation	100
The Warehouse Financial Services Limited	Westpac Banking Corporation The Warehouse Group Limited	51 49
Toyota Finance New Zealand Limited	Toyota Motor Corporation (Japan)	100
UDC Finance Limited	Australia and New Zealand Banking Group Limited	100

Finance company/ Savings institutions	Credit rating agency	Rating outlook[(b)]
AA+		
GE Capital[(c)]	Standard & Poor's	Stable
AA		
Fuji Xerox Finance Limited[(d)]	Rating and Investment	Stable
AA-		
UDC Finance Limited	Standard & Poor's	Stable
Toyota Finance New Zealand Limited[(e)]	Standard & Poor's	Negative
A		
BMW Financial Services New Zealand Limited[(f)]	Standard & Poor's	Stable
A2		
John Deere Financial Limited[(g)]	Moody's	Stable
A-		
Mercedes-Benz Financial Services New Zealand Limited[(h)]	Standard & Poor's	Stable
ORIX New Zealand Limited[(i)]	Standard & Poor's	Stable
Medical Securities Limited	Standard & Poor's	Stable
BBB-		
Heartland New Zealand Limited[(j)]	Standard & Poor's	Stable

Finance company/ Savings institutions	Credit rating agency	Rating outlook[(b)]
BB+		
Nelson Building Society	Fitch Rating International	Stable
Wairarapa Building Society	Fitch Rating International	Stable
Police & Families Credit Union	Standard & Poor's	Stable
Fisher & Paykel Finance Group	Standard & Poor's	Stable
BB		
Credit Union Baywide	Standard & Poor's	Stable
Credit Union North	Standard & Poor's	Stable
First Credit Union	Standard & Poor's	Stable
Avanti Finance Limited	Standard & Poor's	Stable
BB-		
Credit Union South	Standard & Poor's	Stable
Not Rated		
Motor Trade Finances Limited	n/a	n/a
Instant Finance Limited	n/a	n/a
The Warehouse Financial Services Limited	n/a	n/a

Footnotes

(a) Comprising GE Finance & Insurance Limited, Custom Fleet Limited and GE Commercial Limited.
(b) Descriptions of the rating grades are provided on page 52.
(c) Rating of parent company GE Capital.
(d) Rating of parent company Fuji Xerox Co. Ltd.
(e) Rating of parent company Toyota Financial Services Corp.
(f) Rating of parent company BMW AG.
(g) Rating of John Deere Financial Limited Australia.
(h) Rating of parent company Daimler AG.
(i) Rating of parent company ORIX Corporation.
(j) Rating of Heartland Building Society.

Definitions and abbreviations

Terms and ratios used in this Survey	Definitions used in this Survey
Gearing	Net assets divided by total assets.
Gross impaired assets	Includes all impaired assets, restructured assets, assets acquired through the enforcement of security, but excludes past due assets.
Impaired asset expense	The charge to the Profit and Loss Account for bad debts and provisions for doubtful debts, which is net of recoveries (where identifiable).
Interest bearing liabilities	Customer deposits (including accrued interest payable where identifiable), balances with banks, debt securities, subordinated debt and balances with related parties.
Interest earning assets	Cash on hand, money on call and balances with banks, trading and investment securities, net loans and advances (including accrued interest receivable where identifiable), leased assets net of depreciation and balances with related parties.
Interest expense	Includes all forms of interest or returns paid on debt instruments.
Interest margin	Net interest income divided by average interest earning assets.
Interest spread	Difference between the average interest rate on average interest earning assets, and the average interest rate on average interest bearing liabilities.
Loans and advances	Includes loans and advances, lease receivables (net of unearned income) and accrued interest receivable (where identifiable), but excludes amounts due from banks, marketable securities, loans to related parties, sundry debtors and prepayments.
Net assets	Total assets less total liabilities.
Net interest income	Interest income (including net income from acting as a lessor) less interest expense.
Net loans and advances	Loans and advances, net of individual provisions for doubtful debts.
Net profit after tax	After minority interests, adjusting for the impact of subvention payments.
Operating expense	Includes all expenses charged to arrive at net profit before tax (excluding interest expense, impaired asset expense, subvention payments, depreciation of leased assets where a lessor and amortisation/write-off of goodwill and other intangibles).
Operating income	Net interest income and income from all other sources net of depreciation of leased assets, but excludes subvention receipts.
Past due assets	Includes any asset which has not been operated by the counterparty within its key terms for 90 days and which is not an impaired or restructured asset.
Provision for doubtful debts	Includes both collective and individual provisions for bad and doubtful debts.
Total assets	Excludes goodwill assets (unless specifically defined).
Total liabilities	Includes subordinated debt, but excludes minority interest.
Ultimate shareholding	Identifies the ultimate holding company rather than any intermediate holding companies.
Underlying profit	Operating income less operating expense and impaired asset expense. Items of a non-recurring nature, unrelated to the ongoing operations of the entity, are excluded.

Abbreviations used in this Survey	
AFA	Authorised Financial Advisers
AML/CFT	Anti-Money Laundering and Countering Funding of Terrorism
The AML/CFT Act	The Anti-Money Laundering and Countering Financing of Terrorism Act 2009
APRA	Australian Prudential Regulation Authority
bps	Basis points
CCCFA	Credit Contracts and Consumer Finance Amendments
CU	Credit Union
DIA	Department of Internal Affairs
D-SIB	Domestic – Systemically Important Banks
FASB	Financial Accounting Standards Board
FATCA	Foreign Account Tax Compliance Act
FFIs	Foreign Financial Institutions
FIPS	Financial Institutions Performance Survey
FMA	Financial Markets Authority
The FMCB	The Financial Markets Conduct Bill
GDP	Gross Domestic Product
GFC	Global Financial Crisis
GMI	Gareth Morgan Investments
G-SIB	Global – Systemically Important Banks
Heartland	Heartland New Zealand Limited
IASB	International Accounting Standards Board
IGA	Intergovernmental Agreement
IRD	New Zealand Inland Revenue Department
IRS	US Internal Revenue Service
LHS	Left-hand side
LVRs	Loan-to-value ratios
MBIE	Ministry of Business Innovation and Employment
NBDT	Non-banking deposit taking institution
NIM	Net Interest Margin
NPAT	Net Profit after Tax
NZD	New Zealand dollar
NZX	New Zealand Stock Exchange
OBR	Open Bank Resolution
OCI	Other comprehensive income
OCR	Official Cash Rate
PGGWF	PGG Wrightson Finance Limited
QFE	Qualifying Financial Entities
RBNZ	Reserve Bank of New Zealand
RHS	Right-hand side
RoA	Return on Assets
RoE	Return on Equity
US	United States of America
XRB	External Reporting Board

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