



Monday, 20 April 2020

ASX Announcement

NAB announces items impacting 1H20 results and change in Wealth reporting

National Australia Bank Ltd (NAB) today announced that first half 2020 (1H20) earnings will be reduced by charges as described below:

- a net increase in provisions for customer-related remediation matters of \$268 million before tax (\$188 million after tax);
- a change to the application of the software capitalisation policy which will reduce NAB's capitalised software balance as at 31 March 2020 by \$1,056 million and reduce earnings by \$742 million after tax; and
- impairment of the carrying value of NAB's investment in MLC Life of \$214 million (before and after tax).

The net increase in the provision for remediation of \$188 million after tax is expected to reduce the Group's Common Equity Tier 1 capital (CET1) ratio by approximately 6 basis points. The change to the software capitalisation policy and impairment of NAB's investment in MLC Life have no impact on the Group's CET1 ratio.

Appendix 1 provides further disclosure of the expected impact of these items on 1H20 earnings.

Further detail will be provided when NAB releases its 2020 Half Year results. This will include information about the impact of the COVID-19 pandemic on NAB's earnings and balance sheet including provisions, combined with capital and dividend implications.

From 1H20, the Wealth business will be reported as a separate segment called MLC Wealth and no longer form part of Consumer Banking. The Group's 1H20 Results Announcement will include individual Divisional Reviews for both Consumer Banking and MLC Wealth. Appendix 2 provides restated historical financial information, reflecting this change.

The matters in this announcement remain subject to finalisation of NAB's 2020 Half Year results, including review by the auditors and final Board approvals.

Customer-Related Remediation

NAB's 1H20 earnings are expected to include charges of \$188 million after tax (\$268 million before tax) for customer-related remediation. This comprises both cash earnings charges and increased earnings for discontinued operations as set out below.

Earnings impact of remediation	\$ million (before tax)	\$ million (after tax)
Continuing operations (cash earnings)	(418)	(293)
Discontinued operations	150	105
Total provisions impacting 1H20 results	(268)	(188)

Approximately 69% of the expected 1H20 cash earnings charges are for Wealth-related matters, 23% for Banking-related matters, and 8% for Bank of New Zealand.

Of the 1H20 cash earnings charges, \$184 million after tax (\$263 million before tax) relates to additional provisions required for existing matters, with the key drivers including:

- Adviser service fees charged by NAB Financial Planning (salaried advisers). Provisions have been increased primarily to reflect a higher assumed refund rate of 40% (or approximately 56% including interest costs) compared with 28% at 30 September 2019;
- Increased Wealth-related remediation program costs; and
- Progression of work on banking-related matters.

The remainder of the 1H20 cash earnings charges of \$109 million after tax (\$155 million before tax) reflects provisions raised for newly identified matters, the most significant of which were issues relating to workplace superannuation.

In addition to the 1H20 cash earnings impacts outlined above, 1H20 earnings for discontinued operations will be increased by \$105 million after tax (\$150 million before tax), reflecting a reassessment of provisions associated with the MLC Life business.

Until all customer payments have been completed, the final cost of customer-related remediation matters remains uncertain.

Change in Application of Software Capitalisation Policy

Following a further review of NAB's application of its software capitalisation policy, a change has been made to increase the minimum threshold at which software is to be capitalised from \$2 million to \$5 million. This reflects a change in approach to managing projects which is intended to uplift business accountability for projects less than \$5 million.

The change will be applied to both current and future software balances and is expected to reduce NAB's capitalised software balance at 31 March 2020 by \$1,056 million and NAB's 1H20 cash earnings by \$742 million after tax. There is no impact on Group capital given capitalised software balances are already deducted from Group CET1 capital.

The amortisation saving in 2H20 is forecast at \$154 million, but this is expected to be broadly offset by investment expenses previously capitalised.

MLC Limited (MLC Life) impairment

The challenging operating environment within the life insurance industry has resulted in a decline in the carrying value of NAB's 20% investment in MLC Life since September 2019. This has resulted in an impairment loss of \$214 million (both before and after tax) impacting 1H20 non cash earnings for continuing operations. The impairment represents a 37% reduction in the carrying value of this investment. There is no impact on Group capital given this investment is already deducted from Group CET1 capital.

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The release of this announcement was authorised by the Board of Directors.

Appendix 1

Earnings Impact

Details of the expected 1H20 earnings impacts outlined in this announcement are provided in the following table. As has been the case in prior periods, the 1H20 change in application of the capitalisation software policy and customer-related remediation costs will be identified as 'large notable items' and are excluded from FY20 expense growth guidance of 'broadly flat'.

1H20 earnings impact of customer-related remediation, change in application of capitalisation software policy and MLC Life impairment

\$m	Customer remediation	Software policy	MLC Life impairment	Total impact
Net interest income	-22			-22
Other operating income	-220			-220
Net operating income	-242			-242
Operating expenses	-176	-1,056		-1,232
Cash earnings before tax	-418	-1,056		-1,474
Income tax expense	125	314		439
Cash earnings	-293	-742		-1,035
Non cash earnings after tax			-214	-214
Net profit from continuing operations	-293	-742		-1,249
Discontinued operations after tax	105			105
Net profit attributable to owners of NAB	-188	-742	-214	-1,144

Appendix 2

Change in Wealth Reporting

The following Group disclosures of Operating Income and Operating Expenses have been updated to show MLC Wealth separately, with historical financial information restated.

Other Operating Income	Half year to	
	Sep 19	Mar 19
\$m		
Fees and commissions	1,146	1,134
Trading income	698	752
Other	105	126
Banking subtotal	1,949	2,012
MLC Wealth	423	430
Customer-related remediation	(833)	(302)
Total other operating income	1,539	2,140

Operating Expenses	Half year to	
	Sep 19	Mar 19
\$m		
Personnel expenses	1,943	1,969
Occupancy and depreciation expenses	405	402
General expenses	1,444	1,363
Banking subtotal	3,792	3,734
MLC Wealth	308	321
Customer-related remediation	244	120
Capitalised software policy change	494	-
Total operating expenses	4,838	4,175