Bank of New Zealand

Disclosure Statement

For the six months ended 31 March 2021

No. 95

Disclosure Statement

For the six months ended 31 March 2021

This Disclosure Statement has been issued by Bank of New Zealand for the six months ended 31 March 2021 in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order").

In this Disclosure Statement, unless the context otherwise requires:

a) "Banking Group" means Bank of New Zealand's financial reporting group, which consists of Bank of New Zealand, all of its wholly owned entities and other entities consolidated for financial reporting purposes; and

b) Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

Contents

Bank of New Zealand Corporate Information

Address for Service

The name of the Registered Bank is Bank of New Zealand (referred to either by its full name or as the "Bank"). The Bank's address for service is Level 4, 80 Queen Street, Auckland 1010, New Zealand.

Nature of Business

The Bank is a company domiciled in New Zealand. It was incorporated in New Zealand on 29 July 1861. The Banking Group provides a broad range of banking and financial products and services to retail, business, agribusiness, corporate and institutional clients.

Guarantees

Covered Bond Guarantee

Certain debt securities ("Covered Bonds") issued by the Bank, or its wholly owned controlled entity, BNZ International Funding Limited, acting through its London Branch ("BNZ-IF"), are guaranteed by CBG Trustee Company Limited, as trustee of the BNZ Covered Bond Trust (the "Covered Bond Guarantor"). The Covered Bond Guarantor has guaranteed the payment of all interest and principal under the Covered Bonds pursuant to a guarantee which is secured over a pool of assets. The Covered Bond Guarantor's address for service is Level 9, 34 Shortland Street, Auckland 1010, New Zealand.

The Covered Bond Guarantor is not a member of the Banking Group and has no credit ratings applicable to any senior unsecured obligations payable in New Zealand dollars. The Covered Bonds have been assigned a long term credit rating of Aaa and AAA from Moody's Investors Service Pty Limited and Fitch Australia Pty Limited, respectively. Refer to note 7 for further information. Further details about the above guarantee can be obtained by referring to the Bank's Disclosure Statement for the year ended 30 September 2020 which is available at www.bnz.co.nz.

Other material obligations of the Bank are not guaranteed.

Ultimate Parent Bank

Ultimate Parent Bank and Address for Service

The ultimate parent bank, and ultimate holding company, of Bank of New Zealand is National Australia Bank Limited. National Australia Bank Limited's address for service is Level 1, 800 Bourke Street, Docklands, Victoria 3008, Australia.

References in this document to "NAB" are references to National Australia Bank Limited's financial reporting group, which consists of National Australia Bank Limited, all of its wholly owned entities and other entities consolidated for financial reporting purposes.

Legally Enforceable Restrictions that may Materially Inhibit National Australia Bank Limited's Legal Ability to Provide Material Financial Support to Bank of New Zealand

Since 30 September 2020, there have been no material changes in regulations, legislation, or other restrictions of a legally enforceable nature that may materially inhibit the legal ability of National Australia Bank Limited to provide material financial support to the Bank.

Pending Proceedings or Arbitration

The Bank's Directors are of the opinion that there are no pending proceedings or arbitrations concerning any member of the Banking Group, whether in New Zealand or elsewhere, that may have a material adverse effect on the Registered Bank or the Banking Group.

Other Matters

The Bank's Directors are of the opinion that there are no other matters relating to the business or affairs of the Registered Bank or the Banking Group which would, if disclosed in this Disclosure Statement, materially affect the decision of a person to subscribe for debt securities of which the Registered Bank or any member of the Banking Group is the issuer.

Directorate

Prudence Mary Flacks resigned as a Director of the Bank, effective 30 October 2020.

Responsible Persons

Mr. Douglas Alexander McKay, ONZM, Non-Executive Director, Chairman, and Ms. Angela Mentis, Executive Director, have been authorised in writing to sign this Disclosure Statement in accordance with section 82 of the Reserve Bank of New Zealand Act 1989 ("RBNZ Act"), on behalf of the other Directors, being:

Mai Chen
Bruce Ronald Hassall
Louis Arthur Hawke
Kevin John Kenrick
Gary Andrew Lennon
Linley Ann Wood

Auditor

The auditor whose report is referred to in this Disclosure Statement is Ernst & Young. Ernst & Young's address for service is Level 9, EY Building, 2 Takutai Square, Britomart, Auckland 1010, New Zealand.

Income Statement

For the six months ended 31 March 2021

Dollars in Millions	Note	Banking Group Unaudited 6 Months 31/3/21	 Audited 12 Months 30/9/20	 Unaudited 6 Months 31/3/20
Interest income				
Effective interest income		**1,461**	3,440	1,842
Fair value through profit or loss		**44**	179	109
Interest expense		**432**	1,537	900
Net interest income		**1,073**	2,082	1,051
Gains less losses on financial instruments	2	**135**	88	76
Other operating income	3	**191**	350	181
Total operating income		**1,399**	2,520	1,308
Operating expenses		**500**	1,158	647
Total operating profit before credit impairment charge and income tax expense		**899**	1,362	661
Credit impairment charge / (write-back)	8	**(17)**	300	151
Total operating profit before income tax expense		**916**	1,062	510
Income tax expense on operating profit		**256**	300	143
Net profit attributable to the shareholder of the Bank		**660**	762	367

The accounting policies and other notes form part of, and should be read in conjunction with, these interim financial statements.

Statement of Comprehensive Income

For the six months ended 31 March 2021

Dollars in Millions	Banking Group Unaudited 6 Months 31/3/21	 Audited 12 Months 30/9/20	 Unaudited 6 Months 31/3/20
Net profit attributable to the shareholder of the Bank	**660**	762	367
Other comprehensive income/(expense):			
Items that will not be reclassified to profit or loss			
Actuarial gain/(loss) on defined benefit plan	**-**	1	-
Movement in asset revaluation reserve	**(1)**	-	-
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	**(23)**	(67)	464
Tax on items recognised in equity	**6**	19	(130)
	(18)	(47)	334
Items that may be reclassified subsequently to profit or loss			
Movement in cash flow hedge reserve	**(103)**	23	6
Movement in cost of hedging reserve	**3**	(12)	11
Tax on items recognised in equity	**28**	(3)	(5)
Revaluation of equity instruments held at fair value through other comprehensive income ("FVOCI")	**-**	1	-
	(72)	9	12
Total other comprehensive income/(expense)	**(90)**	(38)	346
Total comprehensive income attributable to the shareholder of the Bank	**570**	724	713

The accounting policies and other notes form part of, and should be read in conjunction with, these interim financial statements.

Statement of Changes in Equity

For the six months ended 31 March 2021

Dollars in Millions	Ordinary Capital	Retained Profits	Asset Revaluation Reserve	Cash Flow Hedge Reserve	Cost of Hedging Reserve	FVOCI Reserve	Total Share-holder's Equity
	Banking Group Unaudited 6 Months 31/3/21						
Balance at beginning of period	4,056	4,493	3	113	(9)	1	8,657
Comprehensive income/(expense)							
Net profit attributable to the shareholder of the Bank	-	660	-	-	-	-	660
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	-	(23)	-	-	-	-	(23)
Reserve movement through other comprehensive income	-	-	(1)	(103)	3	-	(101)
Tax effect on items directly recognised in equity	-	6	-	29	(1)	-	34
Total comprehensive income/(expense)	-	643	(1)	(74)	2	-	570
Balance at end of period	4,056	5,136	2	39	(7)	1	9,227
	Audited 12 Months 30/9/20						
Balance at beginning of year	4,056	3,778	3	96	-	-	7,933
Comprehensive income/(expense)							
Net profit attributable to the shareholder of the Bank	-	762	-	-	-	-	762
Actuarial gain/(loss) on defined benefit plan	-	1	-	-	-	-	1
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	-	(67)	-	-	-	-	(67)
Reserve movement through other comprehensive income	-	-	-	23	(12)	1	12
Tax effect on items directly recognised in equity	-	19	-	(6)	3	-	16
Total comprehensive income/(expense)	-	715	-	17	(9)	1	724
Balance at end of year	4,056	4,493	3	113	(9)	1	8,657
	Unaudited 6 Months 31/3/20						
Balance at beginning of period	4,056	3,778	3	96	-	-	7,933
Comprehensive income/(expense)							
Net profit attributable to the shareholder of the Bank	-	367	-	-	-	-	367
Credit risk adjustments on financial liabilities designated at fair value through profit or loss	-	464	-	-	-	-	464
Reserve movement through other comprehensive income	-	-	-	6	11	-	17
Tax effect on items directly recognised in equity	-	(130)	-	(2)	(3)	-	(135)
Total comprehensive income/(expense)	-	701	-	4	8	-	713
Balance at end of period	4,056	4,479	3	100	8	-	8,646

The accounting policies and other notes form part of, and should be read in conjunction with, these interim financial statements.

Balance Sheet

As at 31 March 2021

		Banking Group		
		Unaudited	Audited	Unaudited
Dollars in Millions	Note	31/3/21	30/9/20	31/3/20
Assets				
Cash and liquid assets	4	7,291	3,933	7,002
Due from central banks and other institutions	5	1,028	782	2,254
Trading securities	6	7,780	10,814	7,946
Derivative financial instruments		5,804	6,140	9,791
Loans and advances to customers	7	90,700	88,149	89,549
Amounts due from related entities	13	105	1,053	717
Other assets		628	492	392
Deferred tax		297	295	274
Property, plant and equipment		425	423	393
Goodwill and other intangible assets		255	229	182
Total assets		114,313	112,310	118,500
Liabilities				
Due to central banks and other institutions	10	4,612	2,820	2,619
Trading liabilities		224	54	21
Derivative financial instruments		4,278	4,711	7,761
Deposits and other borrowings	11	73,699	71,841	72,956
Bonds and notes		18,103	19,512	21,207
Current tax liabilities		9	39	132
Amounts due to related entities	13	1,304	1,903	2,090
Other liabilities		908	824	1,121
Subordinated debt	12	1,949	1,949	1,947
Total liabilities		105,086	103,653	109,854
Net assets		9,227	8,657	8,646
Shareholder's equity				
Contributed equity – ordinary shares		4,056	4,056	4,056
Reserves		35	108	111
Retained profits		5,136	4,493	4,479
Total shareholder's equity		9,227	8,657	8,646
Interest earning and discount bearing assets		105,161	103,063	105,631
Interest and discount bearing liabilities		88,716	89,212	93,290

The accounting policies and other notes form part of, and should be read in conjunction with, these interim financial statements.

Condensed Cash Flow Statement

For the six months ended 31 March 2021

		Banking Group		
		Unaudited 6 Months	Audited 12 Months	Unaudited 6 Months
Dollars in Millions	Note	31/3/21	30/9/20	31/3/20
Cash flows from operating activities				
Cash was provided from:				
Interest income		1,512	3,644	1,951
Other cash inflows provided from operating activities		192	381	200
Cash was applied to:				
Interest expense		(491)	(1,714)	(989)
Other cash outflows applied to operating activities		(750)	(1,409)	(871)
Net cash flows from operating activities before changes in operating assets and liabilities		463	902	291
Net change in operating assets and liabilities		2,335	461	2,426
Net cash flows from operating activities		2,798	1,363	2,717
Net cash flows from investing activities		(54)	(146)	(77)
Net cash flows from financing activities		621	(1,566)	588
Net movement in cash and cash equivalents		3,365	(349)	3,228
Cash and cash equivalents at beginning of period		1,597	1,946	1,946
Cash and cash equivalents at end of period		4,962	1,597	5,174
Cash and cash equivalents at end of period comprised:				
Cash and liquid assets	4	7,291	3,933	7,002
Due to central banks and other institutions classified as cash and cash equivalents	10	(1,641)	(1,949)	(1,452)
Amounts due from related entities classified as cash and cash equivalents	13	84	1,045	703
Amounts due to related entities classified as cash and cash equivalents	13	(772)	(1,432)	(1,079)
Total cash and cash equivalents		4,962	1,597	5,174

The accounting policies and other notes form part of, and should be read in conjunction with, these interim financial statements.

Note 1 Principal Accounting Policies

These interim financial statements are general purpose financial reports prepared in accordance with New Zealand Generally Accepted Accounting Practice as appropriate for profit oriented entities, the requirements of IAS 34 *Interim Financial Reporting*, NZ IAS 34 *Interim Financial Reporting* and the Order, and should be read in conjunction with the Disclosure Statement for the year ended 30 September 2020.

Reclassification of financial information

Certain comparative balances have been reclassified to align with the presentation used in the current reporting period. These reclassifications have no impact on the overall financial performance or financial position for the comparative periods.

Changes in accounting policies and disclosure

Accounting policies used in the preparation of these interim financial statements are consistent with the accounting policies used in the preparation of the Disclosure Statement for the year ended 30 September 2020, except for as detailed below.

Investment Management Services Presentation Change

During the 2021 financial year, the Banking Group updated the presentation of expenses related to its investment management services. 'Investment management expenses', which is made up of expenses that are direct and incremental to earning income from the provision of investment management services, are presented together with 'investment management income'. The 'Net investment management income' is now presented within 'Other operating income' in the Income Statement. Previously expenses related to investment management services were included within 'Operating Expenses' in the Income Statement.

Presenting 'investment management income' and 'investment management expenses' together in 'Other operating income' better reflects the results of the Banking Group's investment management activities.

The change has been applied retrospectively and impacted the prior period financial statements of the Banking Group as follows:

- A decrease of $9 million in 'Other income' and 'Operating expenses' for the 31 March 2020 half-year, and
- A decrease of $19 million in 'Other income' and 'Operating expenses' for the year ended 30 September 2020.

Refer to Note 3 *Other operating income* for the disclosure of 'Net investment management income'.

There were no new, or substantial amendments to existing standards or interpretations adopted during the period that had a material impact on the Banking Group.

The following issued, but not yet effective, amendments to accounting standards have not yet been adopted.

Interest Rate Benchmark Reform

The Banking Group is exposed to a range of interbank offered rates (IBORs) through various financial instruments including loans, bonds, debt issuances and derivatives. Some IBOR quotations are likely to cease being published from 1 January 2022, others from 1 July 2023 and some will continue indefinitely as published quotations.

In this regard the Banking Group is reviewing *Interest Rate Benchmark Reform – Phase 2* to consider the financial reporting implications. The amendments provide a practical expedient for modifications and derecognition of financial instruments, relief from discontinuing hedge accounting and additional disclosure about risk arising from IBOR transitioning. While the mandatory effective date of the amendments for the Banking Group is 1 October 2021, the Banking Group is assessing the impact of early adoption.

The Banking Group continues to prepare to transition impacted financial instruments in accordance with relevant industry timelines and regulatory guidelines subject to customer preferences and contractual obligations, where applicable.

Critical accounting assumptions and estimates

The preparation of these interim financial statements requires the use of critical accounting estimates, judgements and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. The Banking Group estimates the amount expected to be paid to tax authorities based on its understanding and interpretation of relevant tax laws which may require the exercise of judgement. Except as explained below, there have been no significant changes to the accounting estimates, judgements and assumptions used in preparing the interim financial statements compared to those applied in the preparation of the Disclosure Statement for the year ended 30 September 2020. The Banking Group has considered the impact of COVID-19 in determining the estimates, assumptions and judgements used to prepare the interim financial statements. Consistent with prior periods the most significant area impacted by COVID-19 is the measurement of credit losses, as set out below.

Measurement of expected credit losses

While the methodologies applied in the expected credit loss ("ECL") calculations remained unchanged from those applied in the Disclosure Statement for the year ended 30 September 2020, the Banking Group has incorporated estimates, assumptions and judgments specific to the impact of COVID-19 and the associated support packages in the measurement of ECL through forward looking economic adjustments. These are explained further in note 8.

Income Statement Notes

Note 2 Gains Less Losses on Financial Instruments

	Banking Group		
	Unaudited	Audited	Unaudited
	6 Months	12 Months	6 Months
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Trading gains less losses on financial instruments	**97**	185	9
Net gain/(loss) attributable to assets, liabilities and derivatives designated in hedge relationships	**7**	(6)	(15)
Net gain/(loss) in the fair value of derivatives used for hedging purposes not designated in hedge relationships	**5**	(21)	9
Net gain/(loss) in the fair value of financial assets designated at fair value through profit or loss and related derivatives (refer to table below)	**2**	(23)	1
Net gain/(loss) in the fair value of financial liabilities designated at fair value through profit or loss and related derivatives (refer to table below)[1]	**22**	(45)	78
Other gains less losses on financial instruments	**2**	(2)	(6)
Total gains less losses on financial instruments	**135**	88	76
Net gain/(loss) in the fair value of financial assets designated at fair value through profit or loss and related derivatives includes:			
Credit risk adjustments on financial assets designated at fair value through profit or loss	**2**	(21)	1
Gain/(loss) in the fair value of financial assets designated at fair value through profit or loss	**(15)**	(16)	(10)
Net gain/(loss) in the fair value of financial liabilities designated at fair value through profit or loss and related derivatives includes:			
Gain/(loss) attributable to derivatives used for hedging of financial liabilities designated at fair value through profit or loss	**(158)**	49	184
Gain/(loss) in the fair value of financial liabilities designated at fair value through profit or loss	**180**	(94)	(106)

[1] All foreign currency gains/(losses) are excluded from this category. Due to the Banking Group's practice of managing all foreign exchange risk centrally, all foreign currency gains/(losses) are included within 'Trading gains less losses on financial instruments' above.

Note 3 Other Operating Income

	Banking Group		
	Unaudited	Audited	Unaudited
	6 Months	12 Months	6 Months
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Other operating income			
Money transfer fees	**58**	88	48
Fees earned on financial assets and liabilities at fair value through profit or loss	**16**	36	19
Fees earned on financial assets and liabilities at amortised cost	**79**	148	76
Fees earned on trust and other fiduciary activities	**3**	10	5
Net investment management income	**7**	12	6
Other income, other fees and commissions income	**28**	56	27
Total other operating income	**191**	350	181
Net investment management income includes:			
Investment management income	**17**	31	15
Investment management expenses	**(10)**	(19)	(9)

Asset Notes

Note 4 Cash and Liquid Assets

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	31/3/21	30/9/20	31/3/20
Coins, notes and cash at bank	210	182	314
Transaction balances with central banks	5,796	2,182	4,625
Transaction balances with other institutions	335	570	1,017
Securities purchased under agreements to resell with central banks	69	-	-
Securities purchased under agreements to resell with other institutions	881	999	1,046
Total cash and liquid assets	7,291	3,933	7,002

Where the Banking Group has accepted collateral arising from secured placements and reverse repurchase agreements, the Banking Group is obliged to return equivalent securities. Securities repledged by the Banking Group are strictly for the purposes of providing collateral for the counterparty. These transactions are conducted under terms that are usual for customary standard lending, and securities borrowing and lending activities.

The Banking Group has accepted collateral with a fair value of $1,003 million as at 31 March 2021 arising from reverse repurchase agreements included in cash and liquid assets and amounts due from related entities (refer to note 13), which it is permitted to sell or repledge (30 September 2020: $2,048 million; 31 March 2020: $1,761 million).

Government securities with a fair value of $68 million were repledged as at 31 March 2021 (30 September 2020: $324 million; 31 March 2020: $234 million). The Bank's obligation to repurchase government securities is classified under due to central banks and other institutions (refer to note 10).

Note 5 Due from Central Banks and Other Institutions

Included in due from central banks and other institutions as at 31 March 2021 was $825 million of collateral posted with counterparties to meet standard derivative trading obligations (30 September 2020: $628 million; 31 March 2020: $1,516 million).

Note 6 Trading Securities

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	31/3/21	30/9/20	31/3/20
Government bonds, notes and securities	4,960	6,167	3,589
Semi-government bonds, notes and securities	1,209	2,949	2,881
Corporate and other institutions bonds, notes and securities	1,611	1,698	1,476
Total trading securities	7,780	10,814	7,946

Included in trading securities as at 31 March 2021 were $530 million encumbered through repurchase agreements (30 September 2020: $1,360 million; 31 March 2020: $713 million). These trading securities have not been derecognised by the Bank as the Bank retains substantially all the risks and rewards of ownership. Counterparties have the right to sell or repledge these encumbered securities. The Bank's obligation to repurchase trading securities is classified under due to central banks and other institutions (refer to note 10) and amounts due to related entities (refer to note 13).

Note 7 Loans and Advances to Customers

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	31/3/21	30/9/20	31/3/20
Overdrafts	2,042	2,136	2,506
Credit card outstandings	876	900	1,038
Housing loans	49,493	45,850	44,597
Other term lending	38,407	38,809	40,983
Other lending	594	1,154	978
Total gross loans and advances to customers	91,412	88,849	90,102
Deduct:			
Provision for credit impairment and credit risk adjustments on financial assets (refer to note 8)	853	910	776
Deferred and other unearned future income and expenses	(92)	(68)	(68)
Fair value hedge adjustments on housing loans	(49)	(142)	(155)
Total deductions	712	700	553
Total net loans and advances to customers	90,700	88,149	89,549

Included in loans and advances to customers as at 31 March 2021 was $65 million of collateral posted with counterparties to meet standard derivative trading obligations (30 September 2020: $631 million; 31 March 2020: $413 million).
As at 31 March 2021, included within the Banking Group's loans and advances to customers were housing loans with a carrying amount of $17,125 million that have been transferred to consolidated structured entities but not derecognised in their entirety (30 September 2020: $13,547 million; 31 March 2020: $11,163 million).

The Banking Group had issued debt securities with a face value of $4,072 million that were guaranteed by the Covered Bond Trust as at 31 March 2021 (30 September 2020: $4,292 million; 31 March 2020: $4,413 million). The underlying collateral that supports the guarantee provided by the Covered Bond Trust comprised housing loans, collections receivable and cash with a carrying amount of $4,741 million as at 31 March 2021 (30 September 2020: $4,734 million; 31 March 2020: $4,728 million).

Note 8 Allowance for Expected Credit Losses

Expected Credit Losses ("ECL") are derived from unbiased probability weighted estimates of loss. The measurement of ECL and assessment of significant increase in credit risk, considers information about current conditions, past events, as well as reasonable and supportable forecasts of future economic conditions.

The Banking Group's ECL measurement is derived from a probability weighted average of three distinct scenarios (base case, upside and downside) in addition to forward looking adjustments for emerging risk at an industry, geography or segment level. The probability of each scenario is determined by considering relevant macro-economic outlooks and their likely impact on the Banking Group's credit portfolios.

Key estimates and assumptions

- In determining ECL, management judgement is applied, using objective, reasonable and supportable information about current and forecast economic conditions.
- Macro-economic variables used in these scenarios, include (but are not limited to) the cash rate, unemployment rates, Gross Domestic Product ("GDP") growth rates and residential property price indices.
- Forward looking macro-economic information and assumptions relating to the COVID-19 pandemic have been considered in these scenarios, including potential impacts of the COVID-19 pandemic, recognising that uncertainty still exists in relation to the duration of the COVID-19 pandemic-related restrictions and the anticipated impact of the unwinding of New Zealand Government stimulus and regulatory support measures.
- When determining whether the risk of default has increased significantly since initial recognition, both quantitative and qualitative information is considered, including expert credit assessment, forward looking information and analysis based on the Group's historical loss experience.

ECLs are either measured over 12 months or the expected lifetime of the exposure, depending on credit deterioration since origination, according to the following three stage approach:

- 12 month ECL ("Stage 1"): For exposures where there has not been a significant increase in credit risk ("SICR") since initial recognition and that are not credit impaired upon origination, the portion of the lifetime ECL associated with the probability of default events occurring within the next 12 months is recognised.
- Lifetime ECL–not credit impaired ("Stage 2"): For exposures where there has been a significant increase in credit risk since initial recognition but that are not credit impaired, a lifetime ECL is recognised reflecting the remaining lifetime of the financial asset.
- Lifetime ECL–credit impaired ("Stage 3"): Financial assets are assessed as credit impaired when one or more events that have a detrimental impact on the estimated future cash flows of that asset have occurred. For financial assets that have become credit impaired, a lifetime ECL is recognised and interest revenue is calculated by applying the effective interest rate to the amortised cost (net of provision) rather than the gross carrying amount.

The tables on pages 11 and 12 reflect allowance for ECL on financial assets held at amortised cost. The table on page 15 shows credit risk adjustments on financial assets designated at fair value through profit or loss.

	Banking Group			
	Unaudited (31/3/21)			
Dollars in Millions	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Allowance for Expected Credit Losses				
12-months ECL ("Stage 1")	2	8	47	57
Lifetime ECL				
Not credit impaired ("Stage 2")	43	35	436	514
Collective assessed - credit impaired ("Stage 3 - Collective")	38	18	21	77
Individually assessed - credit impaired ("Stage 3 - Individual")	1	8	165	174
Total lifetime ECL	82	61	622	765
Total ECL	84	69	669	822

Movement in allowance for ECL

The total provision for credit impairment reduced by $57m compared to the balance at 30 September 2020, reflecting a general improvement in asset quality, partially offset by an increase in the downside probability for collective provision forward looking economic adjustments and $44m of write-offs. The downside probability was raised due to volatility in macro-economic factors, considering the point in the economic cycle, risks that remain in relation to COVID-19 and the potential for supply chain constraints.

Individually assessed provisions reduced by $37m compared to the balance at 30 September 2020, due to write offs and work-outs. Collectively assessed provisions reduced by $20m compared to the balance at 30 September 2020 with $2m reduction in Stage 1, $14m increase in Stage 2 and $32m reduction in Stage 3.

Movement in gross carrying amount

Retail facilities use the number of days past due or the relative change in probability of default at account level to determine significant increase in credit risk. The Banking Group considers that significant increase in credit risk occurs when an asset is more than 30 days past due resulting in a movement from Stage 1 to Stage 2.

For Non-retail facilities internally derived credit ratings represent a key determinant of credit risk. Credit risk is deemed to have increased significantly if the credit rating has significantly deteriorated at the reporting date, relative to the credit rating at the date of initial recognition. When determining whether the risk of default has increased significantly since initial recognition, the Banking Group considers both quantitative and qualitative information including expert credit risk assessment, forward looking information such as economic adjustment and analytics based on the Banking Group's historical experience. Consistent with the application of the forward-looking economic adjustment and the decision to increase probability to the downside scenario, underlying gross carrying amounts of the portfolio moved from Stage 1 to Stage 2.

Note 8 Allowance for Expected Credit Losses *continued*

The following tables provide a reconciliation from the opening balance to the closing balance of provision for credit impairment and show the movement in opening balance where financial assets have transferred between provision stages during the period.

	Banking Group				
	Unaudited (31/3/21)				
	Collectively assessed allowance			Individually assessed allowance	
Dollars in Millions	Stage 1	Stage 2	Stage 3	Stage 3	Total
Movement in Allowance for ECL					
Residential mortgage lending					
Balance at beginning of period	5	33	53	3	94
Changes to the opening balance due to transfer between ECL stages:					
Transferred to Stage 1	2	(2)	-	-	-
Transferred to Stage 2	-	2	(2)	-	-
Transferred to Stage 3 - Collective	-	(1)	1	-	-
Transferred to Stage 3 - Individual	-	-	-	-	-
Charge/(credit) to income statement due to new and increased provisions (net of releases)[1]	(5)	11	(14)	(1)	(9)
Amounts written off	-	-	-	(1)	(1)
Recovery of amounts written off	-	-	-	-	-
Balance at end of period - Residential mortgage lending	2	43	38	1	84
Other retail exposures					
Balance at beginning of period	8	48	15	7	78
Changes to the opening balance due to transfer between ECL stages:					
Transferred to Stage 1	4	(4)	-	-	-
Transferred to Stage 2	(1)	3	(2)	-	-
Transferred to Stage 3 - Collective	-	(2)	2	-	-
Transferred to Stage 3 - Individual	-	(1)	(4)	5	-
Charge/(credit) to income statement due to new and increased provisions (net of releases)[1]	(3)	(9)	7	4	(1)
Amounts written off	-	-	-	(12)	(12)
Recovery of amounts written off	-	-	-	4	4
Balance at end of period - Other retail exposures	8	35	18	8	69
Corporate exposures					
Balance at beginning of period	44	417	39	205	705
Changes to the opening balance due to transfer between ECL stages:					
Transferred to Stage 1	40	(38)	(2)	-	-
Transferred to Stage 2	(9)	20	(11)	-	-
Transferred to Stage 3 - Collective	-	(5)	5	-	-
Transferred to Stage 3 - Individual	-	(3)	(3)	6	-
Charge/(credit) to income statement due to new and increased provisions (net of releases)[1]	(28)	45	(7)	(17)	(7)
Amounts written off	-	-	-	(31)	(31)
Recovery of amounts written off	-	-	-	3	3
Discount unwind[2]	-	-	-	(1)	(1)
Balance at end of period - Corporate exposures	47	436	21	165	669
Total					
Balance at beginning of period	57	498	107	215	877
Changes to the opening balance due to transfer between ECL stages:					
Transferred to Stage 1	46	(44)	(2)	-	-
Transferred to Stage 2	(10)	25	(15)	-	-
Transferred to Stage 3 - Collective	-	(8)	8	-	-
Transferred to Stage 3 - Individual	-	(4)	(7)	11	-
Charge/(credit) to income statement due to new and increased provisions (net of releases)[1]	(36)	47	(14)	(14)	(17)
Amounts written off	-	-	-	(44)	(44)
Recovery of amounts written off	-	-	-	7	7
Discount unwind[2]	-	-	-	(1)	(1)
Total provision for credit impairment balance at end of period	57	514	77	174	822

[1] Classified as credit impairment charge in the income statement.

[2] The impairment loss on an impaired asset is calculated as the difference between the asset's carrying amount and the estimated future cash flows discounted to its present value using the original effective interest rate for the asset. This discount unwinds through interest income over the period the asset is held.

Note 8 Allowance for Expected Credit Losses *continued*

The following tables summarise the changes in gross carrying amounts to explain changes in the Banking Group's provision for credit impairment for the period.

	Banking Group				
	Unaudited (31/3/21)				
	Collectively assessed			Individually assessed	
Dollars in Millions	Stage 1	Stage 2	Stage 3	Stage 3	Total
Movement in gross loans and advances to customers					
Residential mortgage lending					
Gross carrying amount at beginning of period	45,039	567	236	8	45,850
Transfers					
Transferred to Stage 1	337	(309)	(27)	(1)	-
Transferred to Stage 2	(589)	608	(18)	(1)	-
Transferred to Stage 3 - Collective	(99)	(31)	130	-	-
Transferred to Stage 3 - Individual	(1)	-	(4)	5	-
Net further lending/(repayment)	(1,046)	(16)	(2)	2	(1,062)
Additions	9,539	-	-	-	9,539
Deletions	(4,680)	(95)	(53)	(5)	(4,833)
Amounts written off	-	-	-	(1)	(1)
Total gross carrying amount at end of period	48,500	724	262	7	49,493
Allowance for ECL	2	43	38	1	84
Total net carrying amount at end of period	48,498	681	224	6	49,409
Other retail exposures					
Gross carrying amount at beginning of period	2,258	176	26	8	2,468
Transfers					
Transferred to Stage 1	90	(89)	(1)	-	-
Transferred to Stage 2	(135)	137	(2)	-	-
Transferred to Stage 3 - Collective	(8)	(10)	18	-	-
Transferred to Stage 3 - Individual	(1)	(1)	(2)	4	-
Net further lending/(repayment)	(99)	(23)	(1)	13	(110)
Additions	333	-	-	-	333
Deletions	(262)	(31)	(14)	(3)	(310)
Amounts written off	-	-	-	(12)	(12)
Total gross carrying amount at end of period	2,176	159	24	10	2,369
Allowance for ECL	8	35	18	8	69
Total net carrying amount at end of period	2,168	124	6	2	2,300
Corporate exposures					
Gross carrying amount at beginning of period	19,455	18,855	234	542	39,086
Transfers					
Transferred to Stage 1	2,717	(2,714)	(3)	-	-
Transferred to Stage 2	(5,286)	5,386	(79)	(21)	-
Transferred to Stage 3 - Collective	(28)	(41)	73	(4)	-
Transferred to Stage 3 - Individual	(58)	(10)	(17)	85	-
Net further lending/(repayment)	(2,498)	887	(14)	4	(1,621)
Additions	6,493	-	-	-	6,493
Deletions	(2,466)	(2,648)	(80)	(154)	(5,348)
Amounts written off	-	-	-	(31)	(31)
Total gross carrying amount at end of period	18,329	19,715	114	421	38,579
Allowance for ECL	47	436	21	165	669
Total net carrying amount at end of period	18,282	19,279	93	256	37,910
Total					
Gross carrying amount at beginning of period	66,752	19,598	496	558	87,404
Transfers					
Transferred to Stage 1	3,144	(3,112)	(31)	(1)	-
Transferred to Stage 2	(6,010)	6,131	(99)	(22)	-
Transferred to Stage 3 - Collective	(135)	(82)	221	(4)	-
Transferred to Stage 3 - Individual	(60)	(11)	(23)	94	-
Net further lending/(repayment)	(3,643)	848	(17)	19	(2,793)
Additions	16,365	-	-	-	16,365
Deletions	(7,408)	(2,774)	(147)	(162)	(10,491)
Amounts written off	-	-	-	(44)	(44)
Total gross carrying amount at end of period	69,005	20,598	400	438	90,441
Allowance for ECL	57	514	77	174	822
Total net carrying amount at end of period	68,948	20,084	323	264	89,619

Note 8 Allowance for Expected Credit Losses *continued*

Impact of changes in gross carrying amount on ECL

Further information specific to each of the Banking Groups portfolios is included below.

Residential Mortgages

Residential Mortgage Lending gross carrying amount increased by $3,643 million in the first half of the 2021 financial year, with associated ECL falling by $10 million since 30 September 2020. Gross Lending Assets are for the majority Stage 1 and are collectively assessed.

Movements in ECL reflected house price actual returns and resulting improvements in base case economic estimates from 2020. The Banking Group retained the downside stress scenario with an increase in probability weightings reflecting volatility in macro-economic factors, considering the point in the economic cycle, risks that remain in relation to COVID-19 and the potential for supply chain constraints.

Corporate exposures

Corporate gross carrying amount reduced by $507 million in the first half of the 2021 financial year, this exposure incorporates support lending under the New Zealand Government's Business Finance Guarantee Scheme ("BFGS") which is 80% guaranteed by the New Zealand Treasury.

Movements in ECL reflected lower credit impairment charges due to a lower number of individually impaired exposures, combined with write-backs. Improvements in the underlying portfolio was offset by increased probability weighting to the downside forward looking economic scenario reflecting volatility in macro-economic factors, considering the point in the economic cycle, risks that remain in relation to COVID-19 and the potential for supply chain constraints. The impact of that percentage increase is that the economic adjustment component of provision was materially unchanged from 30 September 2020.

The following table shows the key macro-economic variables used in the base case and downside scenario at 31 March 2021.

	Base case (%)			Downside (%)		
	FY 2021	FY 2022	FY 2023	FY 2021	FY 2022	FY 2023
Macro-economic indicators						
Gross domestic product change year on year	1.2	3.8	2.7	0.4	5.8	4.1
Unemployment	4.8	4.1	4.6	10.4	9.4	8.6
House price change year on year	15.7	2.3	3.8	(18.5)	(5.0)	-

	Banking Group		
	Unaudited (31/3/21)		
Dollars in Millions	Collective Allowance	Individual Allowance	Total
Reported probability weighted ECL	648	174	822
100% base case ECL	283	174	457
100% downside ECL	1,043	174	1,217

The probability weighted ECL is a blended outcome taking into consideration the respective scenarios applied across each of the Banking Group's major loan portfolios. The following table shows the reported total provisions for ECL based on the probability weighting of scenarios, with the sensitivity range reflecting the ECL impacts assuming a 100% weighting is applied to the base case scenario or the downside scenario (with all other assumptions held constant).

Note 8 Allowance for Expected Credit Losses *continued*

Credit risk adjustment on financial assets designated at fair value through profit or loss

The changes in value of financial assets designated at fair value through profit or loss that are attributable to changes in credit risk have been calculated using a statistical-based calculation that estimates expected losses attributable to adverse movement in credit risks.

Credit risk adjustments on financial assets designated at fair value through profit or loss are analysed in the following table.

	Banking Group			
	Unaudited (31/3/21)			
Dollars in Millions	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Credit risk adjustment on individual financial assets				
Loans and advances to customers				
Balance at beginning of period	-	-	22	22
Charge/(credit) to income statement	-	-	4	4
Balance at end of period	-	-	26	26
Credit risk adjustment on groups of financial assets				
Loans and advances to customers				
Balance at beginning of period	-	-	11	11
Charge/(credit) to income statement	-	-	(6)	(6)
Balance at end of period	-	-	5	5
Total credit risk adjustments on loans and advances designated at fair value through profit or loss	-	-	31	31
Trading derivative financial instruments				
Balance at beginning of period	-	-	28	28
Charge/(credit) to income statement	-	-	(13)	(13)
Balance at end of period	-	-	15	15
Total credit risk adjustments on trading derivative financial instruments	-	-	15	15

Note 9 Asset Quality

The Banking Group provides for credit impairment as disclosed in note 8. Accordingly, when management determines that a loan is not expected to be recovered in full, the principal amount and accrued interest on the obligation are written down to estimated net realisable value.

		Banking Group			
		Unaudited (31/3/21)			
Dollars in Millions	Note	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Individually impaired assets - at fair value through profit or loss					
Balance at beginning of period		-	-	42	42
Additions		-	-	12	12
Deletions		-	-	(2)	(2)
Balance at end of period		-	-	52	52
Credit risk adjustments on individual financial assets designated at fair value through profit or loss	8	-	-	26	26
Individually impaired assets - at amortised cost					
Gross carrying amount at end of period		7	10	421	438
Allowance for ECL - Stage 3 - individual	8	1	8	165	174
Total impaired assets at end of period		7	10	473	490
Individually impaired assets - undrawn lending commitments					
At amortised cost		-	1	6	7
At fair value through profit or loss		-	-	-	-
Other assets under administration		3	1	3	7

	Banking Group			
	Unaudited (31/3/21)			
Dollars in Millions	Residential Mortgage Lending	Other Retail Exposures	Corporate Exposures	Total
Past due assets not individually impaired				
Loans and advances to customers				
1 - 7 days past due	111	34	182	327
8 - 29 days past due	91	24	45	160
1 - 29 days past due	202	58	227	487
30 - 59 days past due	68	12	43	123
60 - 89 days past due	25	5	10	40
90+ days past due	70	17	74	161
Total past due assets not individually impaired	365	92	354	811

Liability Notes

Note 10 Due to Central Banks and Other Institutions

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Transaction balances with other institutions[1]	**1,061**	1,283	787
Deposits from central banks	**99**	166	286
Deposits from other institutions[2]	**844**	664	891
Securities sold under agreements to repurchase from central banks[3]	**2,029**	142	300
Securities sold under agreements to repurchase from other institutions[1]	**579**	565	355
Total due to central banks and other institutions	**4,612**	2,820	2,619

[1]Classified as cash and cash equivalents in the cash flow statement.

[2] Included in deposits from other institutions as at 31 March 2021 was $1 million classified as cash and cash equivalents in the cash flow statement (30 September 2020: $1 million; 31 March 2020: $10 million).

[3] Included in securities sold under agreements to repurchase from central banks was nil (30 September 2020: $100 million; 31 March 2020: $300 million) classified as cash and cash equivalents in the cash flow statement, $1,029 million (30 September 2020: $42 million; 31 March 2020: nil) relating to Term Lending Facility and $1,000 million (30 September 2020: nil; 31 March 2020: nil) relating to Funding for Lending Programme.

Included in due to central banks and other institutions as at 31 March 2021 was $727 million of collateral posted by counterparties to meet standard derivative trading obligations (30 September 2020: $652 million; 31 March 2020: $962 million).

Note 11 Deposits and Other Borrowings

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Deposits not bearing interest	**11,049**	8,703	7,417
On-demand and short term deposits bearing interest	**32,804**	28,957	26,031
Term deposits	**25,165**	29,920	33,009
Total customer deposits	**69,018**	67,580	66,457
Certificates of deposit	**659**	924	2,052
Commercial paper	**4,022**	3,337	4,447
Total deposits and other borrowings	**73,699**	71,841	72,956

Included in deposits and other borrowings as at 31 March 2021 was $15 million of collateral posted by counterparties to meet standard derivative trading obligations (30 September 2020: $2 million; 31 March 2020: $13 million).

Note 12 Subordinated Debt

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	31/3/21	30/9/20	31/3/20
Subordinated notes due to related entity	500	500	500
Perpetual notes due to related entity	900	900	900
Subordinated notes due to external investors	549	549	547
Total subordinated debt	1,949	1,949	1,947

Subordinated Notes due to related entity - treated as Tier 2 capital

On 8 May 2018, the Bank issued $500 million of subordinated unsecured notes ("Subordinated Notes") to National Australia Bank Limited. The Subordinated Notes are treated as Tier 2 capital under the Bank's regulatory capital requirements. The Subordinated Notes will mature on 8 May 2028. The Subordinated Notes do not confer any right to vote in general meetings of the Bank or National Australia Bank Limited.

Redemption

Subject to certain conditions, including the approval of the RBNZ, the Bank has the option to redeem all or some of the Subordinated Notes for their face value together with accrued interest (if any) on any interest payment date on or after 8 May 2023. In addition, subject to certain conditions, including the approval of the RBNZ, the Bank may redeem at any time all (but not some only) of the Subordinated Notes if a regulatory or tax event occurs.

Interest

The interest rate for the Subordinated Notes is reset every six months based on the prevailing six month bank bill rate plus a margin of 1.95% per annum for the term of the Subordinated Notes. Interest is payable semi-annually in arrear subject to the Bank being solvent (by satisfying the solvency test in section 4 of the Companies Act 1993) on the relevant payment date and remaining solvent immediately after making the payment. If the Bank does not pay an amount on the Subordinated Notes because it has not satisfied the solvency test, the Bank must pay that amount on the first date on which it is able to make the payment and satisfy the solvency test.

Interest will accrue daily (at the interest rate then applicable to the Subordinated Notes) on any interest that is not paid when scheduled as a result of the Bank not satisfying the solvency test on the relevant payment date. If some or all of the Subordinated Notes are converted or written off, any rights to receive interest on those Subordinated Notes (including any accrued but unpaid interest) are also terminated and written off.

Conversion

If a non-viability trigger event ("NVTE") occurs, some or all of the Subordinated Notes will automatically and immediately be converted into ordinary shares in the Bank ("BNZ Shares") or written off.

Under the terms and conditions of the Subordinated Notes, an NVTE will occur if: (i) the RBNZ gives the Bank a direction under the RBNZ Act requiring the Bank to exercise its right of conversion or write off of its Tier 2 capital instruments; (ii) the Bank is made, subject to statutory management under the RBNZ Act and the New Zealand statutory manager announces his or her decision, to convert or write off the Bank's Tier 2 capital instruments.

Ranking of Subordinated Notes

In a liquidation of the Bank (if the Subordinated Notes have not been converted or written off), the claims of holders of Subordinated Notes will rank: (1) ahead of claims of holders of BNZ Shares and other subordinated securities that rank below the Subordinated Notes (such as the Perpetual Notes due to related entity); (2) equally with claims of other holders of Subordinated Notes, the holders of the Listed Subordinated Notes and holders of other subordinated securities that rank equally with the Subordinated Notes; and (3) behind all other claims (such as those of the Bank's secured creditors, depositors and holders of unsecured unsubordinated bonds issued by the Bank from time to time). If the Subordinated Notes are converted into BNZ Shares, holders will rank equally with existing shareholders of the Bank.

Perpetual Notes due to related entity - treated as Additional Tier 1 capital

On 20 October 2016, the Bank issued $900 million of mandatorily convertible subordinated perpetual unsecured notes ("Perpetual Notes") to National Australia Bank Limited. The Perpetual Notes are treated as Additional Tier 1 capital under the Bank's regulatory capital requirements. The Perpetual Notes have no fixed maturity date and will remain on issue indefinitely if not repaid, converted or written off. The Perpetual Notes do not confer any right to vote in general meetings of the Bank or National Australia Bank Limited.

Interest

The interest rate for the Perpetual Notes is fixed at 6.7539% per annum until 20 October 2021 ("Optional Exchange Date") and, thereafter, will change to a floating interest rate equal to the three month bank bill rate plus a margin of 4.410% per annum. Interest payments are non-cumulative and payable annually in arrear until the Optional Exchange Date.

Following the Optional Exchange Date, the interest payments are payable quarterly in arrear. Interest payments are subject to the Bank's discretion and certain conditions being satisfied (including RBNZ requirements). If interest is not paid, the Bank may not (except in limited circumstances) pay any dividends on BNZ Shares or undertake a share buy-back or other capital reduction until interest is next paid. Unpaid interest is cancelled and does not accumulate.

Conversion

On 20 October 2023, subject to certain mandatory conversion conditions, all of the Perpetual Notes will be converted into BNZ Shares. If the mandatory conversion conditions are not met, the mandatory conversion will be deferred for a specific period (provided that conversion is not required to take place as a result of a common equity trigger event ("CETE") or a NVTE).

The number of BNZ Shares issued on a conversion is determined by reference to the net assets of the Bank in the Bank's most recently published Disclosure Statement and such other information as the Bank considers appropriate.

On the Optional Exchange Date, or on any date if a regulatory or tax event occurs, the Bank may convert or redeem some or all of the Perpetual Notes. Any such conversion or redemption is subject to certain conditions, including in the case of redemption the approval of the RBNZ.

Note 12 Subordinated Debt *continued*

Perpetual Notes due to related entity - treated as Additional Tier 1 capital *continued*

Conversion *continued*

If a CETE or an NVTE occurs, the Bank must convert some or all of the Perpetual Notes into BNZ Shares. Under the terms and conditions of the Perpetual Notes, a CETE will occur if the Banking Group's Common Equity Tier 1 capital ratio is equal to or less than 5.125% and an NVTE will occur if the RBNZ directs the Bank to convert or write off the Perpetual Notes or the Bank is made subject to statutory management and the statutory manager decides the Bank must convert or write off the Perpetual Notes.

Ranking of Perpetual Notes

In a liquidation of the Bank (if the Perpetual Notes have not been converted or written off), the claims of holders of Perpetual Notes will rank: (1) ahead of claims of holders of BNZ Shares and other subordinated securities that rank below the Perpetual Notes; (2) equally with claims of other holders of Perpetual Notes and holders of other subordinated securities that rank equally with the Perpetual Notes; and (3) behind all other claims on the Bank (such as those of the Bank's secured creditors, depositors and holders of the Subordinated Notes and Listed Subordinated Notes, and other unsecured unsubordinated bonds issued by the Bank from time to time). If the Perpetual Notes are converted into BNZ Shares, holders will rank equally with existing shareholders of the Bank.

Subordinated Notes due to external investors - treated as Tier 2 capital

On 17 December 2015, the Bank issued $550 million of subordinated unsecured notes ("Listed Subordinated Notes"). The Listed Subordinated Notes are treated as Tier 2 capital under the Bank's and National Australia Bank Limited's regulatory capital requirements. The Listed Subordinated Notes are scheduled to mature on 17 December 2025. The Listed Subordinated Notes do not confer any right to vote in general meetings of the Bank or National Australia Bank Limited.

Redemption

Subject to certain conditions, including the approval of the RBNZ, the Bank has the option to redeem all or some of the Listed Subordinated Notes for their face value together with accrued interest (if any) on any of the remaining interest payment dates. In addition, subject to certain conditions, including the approval of the RBNZ, the Bank may redeem at any time all (but not some only) of the Listed Subordinated Notes if a regulatory or tax event occurs.

Interest

On 17 December 2020, the interest rate for the Listed Subordinated Notes was reset at 2.728% per annum. Interest is payable quarterly in arrear subject to the Bank being solvent (by satisfying the solvency test in section 4 of the Companies Act 1993) on the relevant payment date and remaining solvent immediately after making the payment. If the Bank does not pay an amount on the Listed Subordinated Notes because it has not satisfied the solvency test, the Bank must pay that amount on the first date on which it is able to make the payment and satisfy the solvency test.

Interest will accrue daily (at the interest rate then applicable to the Listed Subordinated Notes) on any interest that is not paid when scheduled as a result of the Bank not satisfying the solvency test on the relevant payment date. If some or all of the Listed Subordinated Notes are converted or written off, any rights to receive interest on those Listed Subordinated Notes (including any accrued but unpaid interest) are also terminated and written off.

Conversion

If an NVTE occurs, some or all of the Listed Subordinated Notes will automatically and immediately be converted into National Australia Bank Limited ordinary shares ("NAB Shares") or written off.

Under the terms and conditions of the Listed Subordinated Notes, an NVTE will occur if: (i) the RBNZ gives the Bank a direction under the RBNZ Act requiring the Bank to exercise its right of conversion or write off of its Tier 2 capital instruments; (ii) the Bank is made subject to statutory management under the RBNZ Act and the New Zealand statutory manager announces his or her decision to convert or write off the Bank's Tier 2 capital instruments; or (iii) APRA has provided a written determination to National Australia Bank Limited that without the conversion or write off of a class of capital instruments of National Australia Bank Limited which includes the Listed Subordinated Notes, or a public sector injection of capital into, or equivalent capital support with respect to, National Australia Bank Limited, APRA considers that National Australia Bank Limited would become non-viable.

In connection with the Listed Subordinated Notes, a Coordination Agreement dated 11 November 2015 between the Bank, National Australia Group (NZ) Limited ("NAGNZ"), National Equities Limited and National Australia Bank Limited sets out intragroup transactions that are intended to occur on conversion of the Listed Subordinated Notes. Under this agreement, the Bank is required to issue a variable number of BNZ Shares to NAGNZ for an amount equivalent to the Listed Subordinated Notes converted into NAB Shares.

Ranking of Listed Subordinated Notes

In a liquidation of the Bank (if the Listed Subordinated Notes have not been converted or written off), the claims of holders of Listed Subordinated Notes will rank: (1) ahead of claims of holders of BNZ Shares and other subordinated securities that rank below the Listed Subordinated Notes (such as the Perpetual Notes); (2) equally with claims of other holders of Listed Subordinated Notes, the holders of the Subordinated Notes and holders of other subordinated securities that rank equally with the Listed Subordinated Notes; and (3) behind all other claims (such as those of the Bank's secured creditors, depositors and holders of unsecured unsubordinated bonds issued by the Bank from time to time). If the Listed Subordinated Notes are converted into NAB Shares, holders will rank equally with existing shareholders of National Australia Bank Limited.

Recent Developments

On 31 March 2021, the RBNZ announced that the restriction on redeeming non-Common Equity Tier 1 capital instruments had been lifted completely and on 11 May 2021, the Bank announced that it would exercise its option to fully redeem the Listed Subordinated Notes on the next interest payment date of 17 June 2021.

Notes to and Forming Part of the Financial Statements

Other Notes

Note 13 Related Entity Transactions

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Total balances with related entities			
Amounts due from related entities[1]	**105**	1,053	717
Derivative financial assets with related entities	**2,216**	2,296	3,848
Amounts due to related entities[2]	**1,304**	1,903	2,090
Derivative financial liabilities with related entities	**1,703**	1,989	2,982
Subordinated debt due to related entities (refer to note 12)	**1,400**	1,400	1,400

[1] Included in amounts due from related entities as at 31 March 2021 was $84 million classified as cash and cash equivalent in the cash flow statement (30 September 2020: $1,045 million; 31 March 2020: $703 million).

[2] Included in amounts due to related entities as at 31 March 2021 was $772 million classified as cash and cash equivalent in the cash flow statement (30 September 2020: $1,432 million; 31 March 2020: $1,079 million).

Included within the amounts due from and due to related entities were the following balances:

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	**31/3/21**	30/9/20	31/3/20
Amounts due from related entities			
Securities purchased under agreements to resell to ultimate parent	**60**	1,030	697
Amounts due to related entities			
Deposit from controlled entity of ultimate parent	**664**	342	716
Collateral deposit posted by ultimate parent to meet standard derivative trading obligations	**490**	381	960
Securities sold under agreements to repurchase from ultimate parent	**23**	999	275

Other transactions with related entities

Dividends paid to the shareholder, if any, are disclosed in the statement of changes in equity.

Notes to and Forming Part of the Financial Statements

Note 14 Fair Value of Financial Assets and Financial Liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. For the purposes of this note, carrying amount refers to amounts reflected in the balance sheet.

Hierarchy for fair value measurements

The tables on pages 21 and 22 present a three-level fair value hierarchy of the Banking Group's financial assets and financial liabilities which are measured at fair value or amortised cost.

The three levels in the hierarchy are based on the valuation methods and assumptions used in determining the fair values of financial assets and financial liabilities. The levels are as follows:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).
- Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs). The Banking Group did not have any financial assets or financial liabilities measured at fair value that met the criteria of Level 3 classification.

Management uses its judgement in selecting an appropriate valuation technique for financial instruments which are not quoted in an active market.

The Banking Group considers transfers between levels of the fair value hierarchy, if any, to have occurred at the beginning of the respective reporting period. There were no transfers between any of the levels in the six months ended 31 March 2021 (year ended 30 September 2020: nil; six months ended 31 March 2020: nil).

Financial assets and liabilities at fair value

		Banking Group Unaudited (31/3/21)		
Dollars in Millions	Fair Value Total	Fair Value Level 1	Fair Value Level 2	Fair Value Level 3
Financial assets				
Trading securities	**7,780**	**4,828**	**2,952**	**-**
Derivative financial instruments	**5,804**	**-**	**5,804**	**-**
Loans and advances to customers	**940**	**-**	**940**	**-**
Financial liabilities				
Trading liabilities	**224**	**199**	**25**	**-**
Derivative financial instruments	**4,278**	**-**	**4,278**	**-**
Deposits and other borrowings	**4,681**	**-**	**4,681**	**-**
Bonds and notes	**15,504**	**-**	**15,504**	**-**
		Audited (30/9/20)		
Financial assets				
Trading securities	10,814	6,167	4,647	-
Derivative financial instruments	6,140	-	6,140	-
Loans and advances to customers	1,412	-	1,412	-
Financial liabilities				
Trading liabilities	54	31	23	-
Derivative financial instruments	4,711	-	4,711	-
Deposits and other borrowings	4,868	-	4,868	-
Bonds and notes	17,825	-	17,825	-
		Unaudited (31/3/20)		
Financial assets				
Due from central banks and other institutions	586	-	586	-
Trading securities	7,946	3,506	4,440	-
Derivative financial instruments	9,791	-	9,791	-
Loans and advances to customers	1,776	-	1,776	-
Financial liabilities				
Due to central banks and other institutions	132	-	132	-
Trading liabilities	21	8	13	-
Derivative financial instruments	7,761	-	7,761	-
Deposits and other borrowings	8,056	-	8,056	-
Bonds and notes	19,394	-	19,394	-

Note 14 Fair Value of Financial Assets and Financial Liabilities *continued*

Hierarchy for fair value measurements *continued*

Financial assets and liabilities at amortised cost[1]

	Banking Group				
	Unaudited (31/3/21)				
Dollars in Millions	Carrying Value	Fair Value Total	Fair Value Level 1	Fair Value Level 2	Fair Value Level 3
Financial assets					
Loans and advances to customers	89,760	89,662	-	2,042	87,620
Financial liabilities					
Deposits and other borrowings	69,018	69,043	-	69,043	-
Bonds and notes	2,599	2,605	-	2,605	-
Subordinated debt	1,949	1,975	552	1,423	-
	Audited (30/9/20)				
Financial assets					
Loans and advances to customers	86,737	86,808	-	2,136	84,672
Financial liabilities					
Deposits and other borrowings	66,973	67,051	-	67,051	-
Bonds and notes	1,687	1,689	-	1,689	-
Subordinated debt	1,949	1,995	555	1,440	-
	Unaudited (31/3/20)				
Financial assets					
Loans and advances to customers	87,773	87,896	-	2,506	85,390
Financial liabilities					
Deposits and other borrowings	64,900	65,013	-	65,013	-
Bonds and notes	1,813	1,686	-	1,686	-
Subordinated debt	1,947	1,936	551	1,385	-

[1] Fair values for financial assets and liabilities at amortised cost, where the carrying amount is not considered a close approximation of fair value.

The fair value estimates are based on the following methodologies and assumptions:

Due from central banks and other institutions and Due to central banks and other institutions
These assets and liabilities are primarily short term in nature or are receivable or payable on demand. In such cases the carrying amounts approximate their fair value or have been determined using discounted cash flow models based on observable market prices as appropriate.

Trading securities and Trading liabilities
Trading securities include treasury bills, bank bills and bonds, promissory notes, and government and other securities. Trading liabilities include short sales of securities. Where quoted market prices are not available, the Banking Group obtains the fair value by means of discounted cash flows and other valuation techniques based on observable market prices. These techniques have accounted for factors such as interest rates, credit risk and liquidity.

Derivative financial instruments
The fair values of trading and hedging derivatives, including foreign exchange contracts, interest rate swaps, interest rate and currency option contracts, and currency swaps, are obtained from observable market prices as at the reporting date, discounted cash flow models or option pricing models as appropriate.

Loans and advances to customers
The carrying value of loans and advances is net of provision for credit impairment, credit risk adjustments, unearned and deferred income. Floating rate loans to customers generally reprice within six months, therefore, their fair value is assumed to equate to their carrying value. For fixed rate loans, the fair value is estimated by discounting the expected future cash flows based on the maturity of the loans and advances, using current market interest rates. The fair value of loans and advances reflects the movement in observable market interest rates since origination but does not include any adjustments for deferred income.

Deposits and other borrowings
With respect to customer deposits, the fair value of non-interest-bearing, call and variable rate deposits and fixed rate deposits repricing within six months is approximated as the carrying value as at the reporting date. For other fixed rate term deposits, the fair value is estimated by discounting the cash flows based on the maturity of the deposit, using current market interest rates.

With respect to certificates of deposit and commercial paper, these liabilities are primarily short term in nature. The carrying amounts have been determined using discounted cash flow models based on observable market prices.

Bonds and notes
The fair value of bonds and notes is calculated based on a discounted cash flow model using a yield curve appropriate to the remaining maturity of the instruments. This is based on observable market prices as at the reporting date where available, otherwise alternative observable market source data is used. The fair value includes a calculation of the Banking Group's own credit risk based on observable market data.

Note 14 Fair Value of Financial Assets and Financial Liabilities *continued*

Hierarchy for fair value measurements *continued*

Subordinated debt

For Subordinated Notes and Perpetual Notes, the fair value is estimated by discounting the expected future cash flows based on the maturity of the notes, using current market interest rates of similar types of notes. The fair value of Listed Subordinated Notes is based on quoted closing market prices as at the reporting date.

Other financial assets/liabilities

These include securities sold/purchased but not yet settled and accrued interest. Securities sold/purchased but not yet settled and the fair value of accrued interest is approximately equal to the carrying amounts on the balance sheet due to their short term nature.

Note 15 Segment Analysis

Operating segments

An operating segment is a component of an entity engaging in business activities and whose operating results are regularly reviewed by the entity's chief operating decision maker. For each operating segment identified by the Banking Group, financial information is regularly reported to the Bank's Executive Team for the purposes of performance evaluation and resource allocation.

The Banking Group's business is organised into two major reportable and operating segments: Partnership Banking; and Corporate and Institutional Banking. Partnership Banking provides financial products and services to retail, business and private customers. Corporate and Institutional Banking provides financial products and services to corporate and institutional customers.

Revenues and expenses directly associated with each operating segment are included in determining their result. Transactions between operating segments are based on agreed recharges between segments. Segment revenue represents revenue directly attributable to a segment and a portion of the Banking Group's revenue that can be allocated to a segment on a reasonable basis. Segment revenue includes Net interest income and Other operating income, and includes transfer pricing adjustments to reflect inter-segment funding arrangements.

Segment profit represents operating profit before unrealised fair value gains or losses on financial instruments, fair value credit risk adjustment and income or expenses which are one-off in nature and are not part of the Banking Group's core business operations.

Included within the 'Other' category in the following table are business activities that are not separately reportable segments; other balances excluded for management reporting purposes, but included in the consolidated financial statements of the Banking Group for statutory financial reporting purposes; elimination entries on consolidation of the results and of the Banking Group's controlled entities in the preparation of the consolidated financial statements of the Banking Group; and results of an entity included for management reporting purposes, but excluded from the consolidated financial statements of the Banking Group for statutory financial reporting purposes.

	Banking Group				
	Unaudited 6 Months 31/3/21				
Dollars in Millions	Partnership Banking[2]	Corporate and Institutional Banking[2]	Total Reportable Segments	Other[2]	Total Banking Group
Net interest income	**815**	**206**	**1,021**	**52**	**1,073**
Other income[1]	**114**	**123**	**237**	**89**	**326**
Total operating income	**929**	**329**	**1,258**	**141**	**1,399**
Operating profit before income tax expense	**551**	**247**	**798**	**118**	**916**
Income tax expense	**154**	**69**	**223**	**33**	**256**
Net profit attributable to the shareholder of Bank of New Zealand	**397**	**178**	**575**	**85**	**660**
	Audited 12 Months 30/9/20[2]				
Net interest income	1,568	406	1,974	108	2,082
Other income[1]	223	246	469	(31)	438
Total operating income	1,791	652	2,443	77	2,520
Operating profit before income tax expense	945	408	1,353	(291)	1,062
Income tax expense	264	115	379	(79)	300
Net profit attributable to the shareholder of Bank of New Zealand	681	293	974	(212)	762
	Unaudited 6 Months 31/3/20[2]				
Net interest income	804	201	1,005	46	1,051
Other income[1]	124	124	248	9	257
Total operating income	928	325	1,253	55	1,308
Operating profit before income tax expense	521	222	743	(233)	510
Income tax expense	145	63	208	(65)	143
Net profit attributable to the shareholder of Bank of New Zealand	376	159	535	(168)	367

[1] Other income includes Gains less losses on financial instruments (refer to note 2) and Other operating income (refer to note 3).

[2] Comparative balances have been reclassified to align with the segment definitions as at 31 March 2021.

Note 16 Contingent Liabilities and Other Commitments

Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic benefits is not probable or cannot be reliably measured. Where some loss is probable and can be reliably measured, provisions have been made. Contingent liabilities are not recognised in the balance sheet, but are disclosed unless the likelihood of payment is remote.

From time to time, the Banking Group is exposed to contingent risks and liabilities arising from conduct of its business, including:

- actual and potential disputes, claims and legal proceedings;
- investigations into past conduct, including actual and potential regulatory breaches, carried out by regulatory authorities;
- internal investigations and reviews into past conduct, including actual and potential regulatory breaches, carried out by the Banking Group (sometimes with the assistance of external parties); and
- contracts that involve giving contingent commitments such as warranties, indemnities or guarantees.

The Banking Group has received information requests from its regulators as part of both industry and bank-specific reviews being undertaken, and the Banking Group has also initiated contact with its regulators on compliance-related matters. The scope of reviews, inquiries and investigations can be wide-ranging and can result in enforcement proceedings and customer remediation programmes.

There are contingent liabilities in respect of all such matters. Such matters are often highly complex and uncertain. Where appropriate, provisions have been made. The aggregate potential liability of the Banking Group in relation to these matters cannot be accurately assessed.

Further information on some specific contingent liabilities that may impact the Banking Group is set out below.

The Banking Group has been progressing a programme of work to strengthen its Anti-Money Laundering (“AML”) and Countering Financing of Terrorism (“CFT”) programme. The work involves significant investment in systems and personnel to ensure an effective control environment and an uplift in compliance capability. In addition to a general uplift in capability, the programme of work aims to remediate specific compliance issues and weaknesses. The Banking Group continues to keep the RBNZ informed of significant AML or CFT compliance issues and its progress in resolving these issues, and will continue to cooperate with, and respond to queries from, the RBNZ. As this work progresses, further compliance issues may be identified and reported to the RBNZ or equivalent foreign regulators, and additional strengthening may be required. The potential outcome, including enforcement proceedings, and total costs associated with specific issues identified to date, and for any issues identified in the future, remain uncertain.

The Labour Inspectorate of the Ministry of Business, Innovation and Employment (“MBIE”) has undertaken a programme of compliance audits of a number of New Zealand organisations, including the Banking Group, in respect of the Holidays Act 2003 (the “Holidays Act”). Since 2017, the Banking Group has worked with MBIE to review its compliance with the Holidays Act, including in respect of annual and public holiday payments to certain employees, and is completing remediation, as agreed with MBIE. In addition, the legislative interpretation of the definition of “discretionary payments” under the Holidays Act is not yet certain and, once it has been definitively determined, any potential implications for the Banking Group will need to be considered.

Contingent liabilities and credit related commitments at face value arising in respect of the Banking Group's operations were:

	Banking Group		
	Unaudited	Audited	Unaudited
Dollars in Millions	31/3/21	30/9/20	31/3/20
Contingent liabilities			
Bank guarantees	**64**	74	65
Standby letters of credit	**250**	254	265
Documentary letters of credit	**203**	166	162
Performance related contingencies[1]	**1,021**	1,022	1,039
Total contingent liabilities	**1,538**	1,516	1,531
Credit related commitments			
Revocable commitments to extend credit	**9,690**	9,164	9,706
Irrevocable commitments to extend credit	**12,671**	12,599	11,142
Total credit related commitments	**22,361**	21,763	20,848
Total contingent liabilities and credit related commitments	**23,899**	23,279	22,379

[1] Comparative information for the six months ended 31 March 2020 has been restated due to a data capture error.

Note 17 Concentrations of Credit Exposures to Individual Counterparties and Groups of Closely Related Counterparties

The Banking Group's disclosure of concentrations of credit exposures to individual counterparties and groups of closely related counterparties is based on actual credit exposures and excludes credit exposures to connected persons, the central government or central bank of any country with a long term credit rating of A- or A3 or above, or its equivalent, and excludes supranationals or quasi-sovereign agencies with a long term credit rating of A- or A3 or above, or its equivalent. Peak credit exposures to individual counterparties are calculated using the Banking Group's end of period Common Equity Tier 1 capital.

	Banking Group Unaudited (31/3/21) Credit Exposures to Individual Counterparties and Groups of Closely Related Counterparties Long Term Credit Rating	
Number of bank counterparties	Peak End-of-Day A-or A3 or above or its equivalent	Balance Sheet Date A-or A3 or above or its equivalent
Percentage of Common Equity Tier 1 capital		
10-14%	3	1
15 -19%	-	-
20 -24%	-	-
Number of non-bank counterparties		
Percentage of Common Equity Tier 1 capital		
10-14%	1	-
15 -19%	1	-
20 -24%	-	-

Where the Banking Group is funding large loans, it is common practice to share the risk of a customer default with other connected banks or enter into other risk lay-off arrangements. The above table has been compiled using gross exposures before risk lay-offs. No account is taken of collateral, security and/or netting agreements that do not qualify for offset in accordance with NZ IAS 32 Financial Instruments: Presentation which the Banking Group may hold in respect of the various counterparty exposures.

The Banking Group had no bank counterparties, supranationals or quasi-sovereign agencies with a long term credit rating below A- or A3, to whom their aggregate credit exposure, as at 31 March 2021, and peak end-of-day aggregate credit exposure, for the six months ended 31 March 2021, equalled or exceeded 10% of the Banking Group's Common Equity Tier 1 capital.

The Banking Group had no non-bank counterparties with a long term credit rating below A- or A3, to whom their aggregate credit exposure, as at 31 March 2021, and peak end-of-day aggregate credit exposure, for the six months ended 31 March 2021, equalled or exceeded 10% of the Banking Group's Common Equity Tier 1 Capital.

Note 18 Insurance Business

The Banking Group does not conduct any Insurance Business, as defined in the Bank's Conditions of Registration. The Bank's Conditions of Registration can be obtained by referring to the Bank's Disclosure Statement for the year ended 30 September 2020.

Note 19 Capital Adequacy

The RBNZ minimum regulatory capital requirements for banks have been established under RBNZ Capital Adequacy Framework (Internal Models Based Approach) ("BS2B") and Capital Adequacy Framework (Standardised Approach) ("BS2A") based on the international framework developed by the Bank for International Settlements, Committee on Banking Supervision, commonly known as Basel III. These requirements outline how minimum regulatory capital is to be calculated and provide methods for measuring risks incurred by the banks in New Zealand.

The Basel III framework's objective is to develop capital adequacy guidelines that are more accurately aligned with the individual risk profile of banks. Basel III consists of three pillars – Pillar One covers the capital requirements for banks for credit, operational, and market risks. Pillar Two covers all other material risks that are not already included in Pillar One. Pillar Three relates to market disclosure.

RBNZ Capital Adequacy Framework

The Banking Group has calculated its implied Risk-Weighted Exposure and minimum regulatory capital requirements based on BS2B for the majority of credit risk portfolios.

Under BS2B, accredited banks use their own models for estimating risk and minimum capital requirements. Under the Internal Ratings Based Approach for credit risk, the level of risk associated with customers' exposures is determined by way of the primary components of Probability of Default, Loss Given Default and Exposure at Default. These components and associated processes are subject to regular review. For exposures in the Specialised Lending asset category (including Project Finance, Object Finance, Commodity Finance and Income Producing Real Estate) the Banking Group uses supervisory slotting estimates provided by the RBNZ.

The exceptions to the Internal Ratings Based Approach for credit risk are portfolios of relatively low materiality which are subject to the standardised treatment as set out in BS2A.

Capital for market risk has been calculated in accordance with the approach specified in BS2B.

Capital requirement for operational risk has the same meaning as in Part 9 of BS2A, subject to a minimum value of $600 million.

Capital management policies

The Banking Group's primary objectives in relation to the management of capital adequacy are to comply with the requirements set out by the RBNZ, the Banking Group's primary prudential supervisor, to provide a sufficient capital base to cover risks faced by the Bank and to maintain a credit rating to support future business development.

Total regulatory capital is defined as the sum of Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital. Tier 1 capital is defined as the sum of Common Equity Tier 1 capital and Additional Tier 1 capital. The Banking Group's Common Equity Tier 1 capital includes paid up ordinary shares and retained profits less certain deductions, Additional Tier 1 capital includes perpetual notes and Tier 2 capital includes revaluation reserves and subordinated debt.

The Banking Group is required under its Conditions of Registration to maintain a minimum ratio of total eligible or qualifying capital to total risk-weighted assets of 8%, of which a minimum of 4.5% must be held in Common Equity Tier 1 capital and a minimum of 6% must be held in Tier 1 capital. The Banking Group must maintain a minimum Common Equity Tier 1 buffer ratio of 2.5% above these minimum ratios or it will face restrictions on the distribution of earnings and be required to prepare a capital plan that restores the Banking Group's buffer ratio and have that capital plan approved by the RBNZ.

The RBNZ has announced significant changes to the capital adequacy framework for New Zealand registered banks, which will result in a significant increase in the level of capital that the Banking Group is required to hold, as well as changes to what types of instruments constitute eligible regulatory capital. The new regime is currently expected to be implemented in stages from 1 July 2021, with a transition period of seven years before banks are required to fully comply with the new rules.

The Banking Group has an Internal Capital Adequacy Assessment Process ("ICAAP") in place which complies with the requirements set out in the RBNZ's "Guidelines on a Bank's Internal Capital Adequacy Assessment Process" ("BS12") as specified under the Bank's Conditions of Registration. The Banking Group's ICAAP outlines the approach to maintaining capital adequacy, risk appetite and stress testing. The ICAAP considers all material risks consistent with the Banking Group's risk appetite and outlines the capital requirements.

Capital requirements, as detailed in the Banking Group's ICAAP document, are managed by the Bank's Risk Return Management Committee ("RRMC") and Asset, Liability and Capital Committee under delegated authority from the Board of Directors.

For more information on the capital structure of the Banking Group, refer to page 34.

The tables on the following pages detail the capital calculation, capital ratios and capital requirements as at 31 March 2021. During the reporting period the Banking Group complied with all RBNZ's capital requirements as set out in the Bank's Conditions of Registration.

Note 19 Capital Adequacy *continued*

Regulatory capital

The following table shows the qualifying capital for the Banking Group.

Dollars in Millions	Banking Group Unaudited 31/3/21
Qualifying capital	
Common Equity Tier 1 capital	
Contributed equity - ordinary shares	4,056
Retained profits	5,136
Accumulated other comprehensive income and other disclosed reserves	33
Deductions from Common Equity Tier 1 capital:	
Goodwill and other intangible assets	255
Cash flow hedge reserve	39
Credit value adjustment on liabilities designated at fair value through profit or loss	(92)
Prepaid pension assets (net of deferred tax)	5
Deferred tax asset	297
Total expected loss less total eligible allowances for impairment	-
Credit enhancements	1
Total Common Equity Tier 1 capital	8,720
Additional Tier 1 capital	
Perpetual Notes	900
Total Additional Tier 1 capital	900
Total Tier 1 capital	9,620
Tier 2 capital	
Revaluation reserves	2
Subordinated Notes	500
Listed Subordinated Notes	550
Total eligible impairment allowance in excess of expected loss	175
Total Tier 2 capital	1,227
Total Tier 1 and Tier 2 qualifying capital	10,847

Banking Group Basel III regulatory capital ratios

The table below shows the capital adequacy ratios for the Banking Group based on BS2B, expressed as a percentage of total risk-weighted exposures.

	Banking Group			
	Regulatory Minima	Unaudited 31/3/21	Unaudited 30/9/20	Unaudited 31/3/20
Common Equity Tier 1 capital ratio	4.50%	12.86%	11.85%	11.16%
Tier 1 capital ratio	6.00%	14.19%	13.17%	12.46%
Total qualifying capital ratio	8.00%	16.00%	14.91%	14.11%
Buffer ratio	2.50%	8.00%	6.91%	6.11%

Registered Bank Basel III regulatory capital ratios

The table below shows the capital adequacy ratios for the Registered Bank based on BS2B, expressed as a percentage of total risk-weighted exposures.

	The Registered Bank		
	Unaudited 31/3/21	Unaudited 30/9/20	Unaudited 31/3/20
Common Equity Tier 1 capital ratio	12.84%	11.80%	11.12%
Tier 1 capital ratio	14.16%	13.12%	12.42%
Total qualifying capital ratio	15.97%	14.86%	14.07%

For the purpose of calculating capital adequacy ratios for the Registered Bank under BS2B, subsidiaries are consolidated within the Registered Bank if they are either funded exclusively and wholly owned by the Registered Bank, or there is a full, unconditional and irrevocable cross guarantee between the subsidiaries and the Registered Bank.

Note 19 Capital Adequacy *continued*

Total regulatory capital requirements

	Banking Group		
	Unaudited (31/3/21)		
Dollars in Millions	Total Exposure at Default after Credit Risk Mitigation	Risk-Weighted Exposure or Implied Risk-Weighted Exposure	Total Capital Requirement[1]
Credit risk			
Exposures subject to the internal ratings based approach[1]	118,323	44,665	3,573
Specialised lending subject to the slotting approach[1]	7,944	7,362	589
Exposures subject to the standardised approach[1]	2,083	943	75
Equity exposures[1]	1	5	-
Credit Value Adjustment subject to BS2B ("CVA")	N/A	1,421	114
Agribusiness supervisory adjustment[2]	N/A	2,269	181
Total credit risk	128,351	56,665	4,532
Operational risk	N/A	8,425	674
Market risk	N/A	2,713	217
Total	128,351	67,803	5,423

[1] In calculating the total capital requirement, a scalar of 1.06 has been applied to the risk-weighted assets, as required by the RBNZ in accordance with the Bank's Conditions of Registration.

[2] The agribusiness supervisory adjustment increases the risk weight of the Banking Group's rural lending portfolio to a minimum specified by the RBNZ.

Advanced Internal Ratings Based approach to credit risk management

The Banking Group's quantitative credit risk measurement is based on the Internal Ratings Based ("IRB") approach (IRB for Retail Credit portfolios and Advanced IRB for Non-retail Credit portfolios) and uses a series of models to calculate loss estimates for the credit portfolio. This includes consideration of:

- probability of default ("PD") which estimates the probability that a customer will default over the next 12 months;
- exposure at time of default ("EAD") which estimates the amount of outstanding principal, fees and interest owed at the time of default; and
- loss given default ("LGD") which estimates the expected loss in the event of default. It is the percentage of exposure which will be lost after all recovery efforts, including legal expenses, time value of money and recovery expenses.

The above three elements (PD, EAD, and LGD) are important inputs in determining the risk-weighted exposure calculations for both on and off-balance sheet exposures, including undrawn portions of credit facilities, committed and contingent exposures. These ratings are also an important input into the credit approval, risk management, internal capital allocation and corporate governance functions of the Banking Group.

Methodologies used to calculate credit risk estimates (PD, EAD and LGD) are in accordance with BS2B and the Bank's Conditions of Registration. For credit risk estimates on some portfolios, the RBNZ has set prescribed risk estimates required to be used when calculating risk-weighted assets and capital under BS2B. The RBNZ prescribed risk estimates will continue to be used until the Banking Group develops its own internal models for these portfolios.

Controls surrounding credit risk rating systems

The credit risk rating systems cover all methods, processes, controls, data collection and technology that support the assessment of credit risk, the assignment of internal credit risk ratings and the quantification of associated default and loss estimates.

The credit risk rating systems and risk estimate processes are governed by the Banking Group's RRMC and are an integral part of reporting to senior management. Management and staff of the credit risk function regularly assess the performance of the rating systems, monitor progress on changes being made to systems and identify any areas for improvement. These systems are subject to rigorous internal review and approval and regular independent review. The annual validation of models is undertaken by specialists who are responsible for overseeing the design, implementation and performance of all rating models across the Banking Group.

The risk-weighted asset amounts presented in the following tables include a scalar of 1.06 as required by the RBNZ in accordance with the Bank's Conditions of Registration, which is not in the risk weight percentages shown.

Note 19 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach

The following tables analyse credit risk exposures by asset class split into PD bandings. The lower the PD banding the less the probability of default over the next 12 months.

	Banking Group					
	Unaudited (31/3/21)					
Dollars in Millions	Weighted Average PD (%)	Exposure at Default[2]	Exposure-Weighted LGD used for the Capital Calculation (%)	Exposure-Weighted Risk Weight (%)	Risk-Weighted Assets	Minimum Capital Requirement
Corporate						
Exposure-weighted PD grade >0 ≤ 0.1%	0.05	5,403	41	14	803	64
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.31	18,446	36	40	7,733	619
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.95	15,622	33	60	9,894	792
Exposure-weighted PD grade >1.5 ≤ 5.0%	2.48	6,996	33	78	5,798	464
Exposure-weighted PD grade >5.0 ≤ 99.99%	12.73	1,172	39	160	1,990	159
Default PD grade = 100%	100.00	590	43	164	1,028	82
Total corporate exposures	2.32	48,229	35	53	27,246	2,180
Sovereign						
Exposure-weighted PD grade >0 ≤ 0.1%	0.02	13,853	4	1	77	6
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.26	27	45	39	11	1
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.64	5	45	66	4	-
Exposure-weighted PD grade >1.5 ≤ 5.0%	2.30	-	45	101	-	-
Exposure-weighted PD grade >5.0 ≤ 99.99%	5.72	-	45	139	-	-
Default PD grade = 100%	-	-	-	-	-	-
Total sovereign exposures	0.02	13,885	4	1	92	7
Bank						
Exposure-weighted PD grade >0 ≤ 0.1%	0.04	4,741	15	5	253	20
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.18	526	47	35	193	16
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.78	6	60	87	6	-
Exposure-weighted PD grade >1.5 ≤ 5.0%	2.19	1	60	131	1	-
Exposure-weighted PD grade >5.0 ≤ 99.99%	8.28	3	60	215	7	1
Default PD grade = 100%	-	-	-	-	-	-
Total bank exposures	0.06	5,277	19	8	460	37
Residential mortgage						
Exposure-weighted PD grade >0 ≤ 0.1%	0.03	-	38	5	-	-
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.40	1,928	18	13	275	22
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.88	48,453	20	25	13,015	1,041
Exposure-weighted PD grade >1.5 ≤ 5.0%	4.92	2,048	19	67	1,461	117
Exposure-weighted PD grade >5.0 ≤ 99.99%	-	-	-	-	-	-
Default PD grade = 100%	100.00	260	21	219	605	48
Total residential mortgage exposures	1.51	52,689	20	27	15,356	1,228
Other retail[1]						
Exposure-weighted PD grade >0 ≤ 0.1%	0.05	752	86	12	97	8
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.25	512	85	38	206	16
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.92	281	84	81	240	19
Exposure-weighted PD grade >1.5 ≤ 5.0%	2.70	173	83	112	205	16
Exposure-weighted PD grade >5.0 ≤ 99.99%	12.61	99	79	141	148	12
Default PD grade = 100%	100.00	13	81	243	33	3
Total other retail exposures	1.87	1,830	85	48	929	74

[1] Other retail includes credit cards, current accounts and personal overdrafts.

[2] Exposure at default is pre-credit risk mitigation.

Note 19 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach *continued*

	Banking Group					
	Unaudited (31/3/21)					
Dollars in Millions	Weighted Average PD (%)	Exposure at Default[2]	Exposure-Weighted LGD used for the Capital Calculation (%)	Exposure-Weighted Risk Weight (%)	Risk-Weighted Assets	Minimum Capital Requirement
Retail small to medium enterprises						
Exposure-weighted PD grade >0 ≤ 0.1%	0.07	176	38	7	13	1
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.30	781	32	17	138	11
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.92	503	33	31	168	14
Exposure-weighted PD grade >1.5 ≤ 5.0%	2.61	350	34	46	169	14
Exposure-weighted PD grade >5.0 ≤ 99.99%	10.89	36	44	75	29	2
Default PD grade = 100%	100.00	31	50	198	65	5
Total retail SME exposures	2.73	1,877	34	29	582	47
Total[1]						
Exposure-weighted PD grade >0 ≤ 0.1%	0.03	24,925	17	5	1,243	99
Exposure-weighted PD grade >0.1 ≤ 0.5%	0.32	22,220	36	36	8,556	685
Exposure-weighted PD grade >0.5 ≤ 1.5%	0.90	64,870	24	34	23,327	1,866
Exposure-weighted PD grade >1.5 ≤ 5.0%	3.01	9,568	31	75	7,634	611
Exposure-weighted PD grade >5.0 ≤ 99.99%	12.66	1,310	42	156	2,174	174
Default PD grade = 100%	100.00	894	37	183	1,731	138
Total exposures	1.62	123,787	25	34	44,665	3,573

[1] The CVA and the Agribusiness supervisory adjustment have not been included in the above exposures.
[2] Exposure at default is pre-credit risk mitigation

The following table analyses the value and exposure at default of on-balance sheet exposures, off-balance sheet exposures and market related contracts under the IRB approach by asset class.

	Banking Group			
	Unaudited (31/3/21)			
Dollars in Millions	Total Exposure	Exposure at Default[2]	Risk-Weighted Assets	Minimum Capital Requirement
On-balance sheet exposures				
Corporate	33,018	33,018	19,259	1,541
Sovereign	13,169	13,169	46	4
Bank	3,036	3,036	258	21
Residential mortgage	49,494	49,494	14,554	1,164
Other retail	977	977	652	52
Retail small to medium enterprises	1,404	1,404	464	37
Total on-balance sheet exposures	101,098	101,098	35,233	2,819
Off-balance sheet exposures				
Corporate	13,756	12,550	6,955	556
Sovereign	204	520	26	2
Bank	748	730	41	3
Residential mortgage	3,664	3,195	802	64
Other retail	2,662	853	277	22
Retail small to medium enterprises	525	473	118	10
Total off-balance sheet exposures	21,559	18,321	8,219	657
Market related contracts[1]				
Corporate	160,699	2,661	1,032	83
Sovereign	23,411	196	20	1
Bank	64,370	1,511	161	13
Total market related contracts	248,480	4,368	1,213	97

[1] Total exposure for market related contracts represents gross notional amounts.
[2] Exposure at default is pre-credit risk mitigation.

Note 19 Capital Adequacy *continued*

Credit risk subject to the Internal Ratings Based ("IRB") approach *continued*

Dollars in Millions	Banking Group Unaudited (31/3/21) Exposure at Default[2]	Risk-Weighted Assets	Minimum Capital Requirement
Summary[1]			
Corporate	48,229	27,246	2,180
Sovereign	13,885	92	7
Bank	5,277	460	37
Residential mortgage	52,689	15,356	1,228
Other retail	1,830	929	74
Retail small to medium enterprises	1,877	582	47
Total credit risk exposures subject to the IRB approach	123,787	44,665	3,573

[1] The CVA and the Agribusiness supervisory adjustment have not been included in the above exposures.
[2] Exposure at default is pre-credit risk mitigation.

Specialised lending subject to the slotting approach

The tables below show specialised lending exposures for which the supervisory slotting approach has been used and includes Project Finance, Object Finance, Commodity Finance and Income Producing Real Estate exposures.

Dollars in Millions	Banking Group Unaudited (31/3/21) Total Exposure at Default after Credit Risk Mitigation	Risk Weight (%)	Risk-Weighted Assets	Minimum Pillar One Capital Requirement
On-balance sheet exposures subject to the slotting approach				
Strong	2,031	70	1,507	121
Good	3,925	90	3,737	299
Satisfactory	857	115	1,044	83
Weak	55	250	145	12
Default	53	-	-	-
Total on-balance sheet exposures subject to the slotting approach	6,921	88	6,433	515

The categories of specialised lending above are associated with the risk weight shown. These categories broadly correspond to external credit assessments from S&P Global Ratings Australia Pty Limited rating scale: BBB- or better (Strong); BB+ or BB (Good); BB- or B+ (Satisfactory); B to C- (Weak).

Dollars in Millions	Banking Group Unaudited (31/3/21) Total Exposure	Exposure at Default	Average Risk Weight (%)	Risk-Weighted Assets	Minimum Pillar One Capital Requirement
Off-balance sheet exposures subject to the slotting approach					
Off-balance sheet exposures	28	14	96	14	1
Undrawn commitments	1,765	971	86	884	71
Market related contracts	701	38	77	31	2
Total off-balance sheet exposures subject to the slotting approach	2,494	1,023	86	929	74
Total exposures subject to the slotting approach		7,944	87	7,362	589

Note 19 Capital Adequacy *continued*

Credit risk exposures subject to the standardised approach

The tables below show credit risk exposures in respect of the Banking Group, for which the standardised approach has been used

	Banking Group Unaudited (31/3/21)			
Dollars in Millions	Total Exposure at Default after Credit Risk Mitigation	Average Risk Weight (%)	Risk-Weighted Assets	Minimum Pillar One Capital Requirement
On-balance sheet exposures subject to the standardised approach				
Corporate	83	100	88	7
Residential mortgage	37	83	32	2
Past due assets	-	139	-	-
Other assets[1]	1,460	45	701	56
Total on-balance sheet exposures subject to the standardised approach	1,580	49	821	65

[1] Other assets relate to all other assets (including interest receivables, account receivables, intangibles and cash accounts) that are not included in the other categories in the table.

	Banking Group Unaudited (31/3/21)					
Dollars in Millions	Total Exposure or Principal Amount	Average Credit Conversion Factor (%)	Credit Equivalent Amount	Average Risk Weight (%)	Risk-Weighted Assets	Minimum Pillar One Capital Requirement
Off-balance sheet exposures subject to the standardised approach						
Total off-balance sheet exposures subject to the standardised approach	91	27	24	101	25	2
Market related contracts subject to the standardised approach						
Foreign exchange contracts[2]	13	N/A	1	100	1	-
Interest rate contracts[2]	1,046,251	N/A	478	19	96	8
Other	6	N/A	-	1	-	-
Total market related contracts subject to the standardised approach	1,046,270	N/A	479	19	97	8
Total exposures subject to the standardised approach		N/A	2,083	43	943	75

[2] The total exposure or principal amount reflects the gross notional value of contracts.

Equity exposures

The table below shows the capital required to be held as a result of equities held.

	Banking Group Unaudited (31/3/21)			
Dollars in Millions	Exposure at Default	Risk Weight (%)	Risk-Weighted Exposures	Minimum Pillar One Capital Requirement
Equity holdings (not deducted from capital) that are publicly traded	-	300	-	-
All other equity holdings (not deducted from capital)	1	400	5	-
Total equity exposures	1	424	5	-

Credit risk mitigation

The Banking Group assesses the integrity and ability of counterparties to meet their contractual financial obligations for repayment. Collateral security in the form of property or a security interest in personal property is generally taken for business credit except for major government, bank and corporate counterparties of strong financial standing. Longer term consumer finance (e.g. housing loans) is generally secured against real estate while short term revolving consumer credit is generally unsecured.

The table below shows the total value of exposures covered by eligible financial collateral for portfolios subject to the standardised approach and total value of exposures covered by credit derivatives and guarantees for all portfolios.

	Banking Group
Dollars in Millions	Corporate (Including Specialised Lending) Unaudited 31/3/21
For portfolios subject to the standardised approach:	
Total value of exposures covered by eligible financial collateral	-
For all portfolios:	
Total value of exposures covered by credit derivatives or guarantees	-

Note 19 Capital Adequacy *continued*

Residential mortgages by loan-to-valuation ratio

The table below sets out residential mortgages (including loans to businesses) wholly or partly secured by mortgages over residential properties as used to calculate the Banking Group’s Pillar One capital requirement.

The LVRs are calculated as the greater of the customer's current loan limit or balance, divided by the Banking Group's valuation of the security at the last credit event for the customer. Where no LVR is available, the exposure is included in the over 90% category.

	Banking Group		
	Unaudited (31/3/21)		
Dollars in Millions	On-balance Sheet Exposures at Default	Off-balance Sheet Exposures at Default[1]	Total Exposures at Default
LVR Range			
0-59%	20,475	1,345	21,820
60-69%	11,142	626	11,768
70-79%	14,356	884	15,240
80-89%	2,289	32	2,321
Over 90%	1,232	308	1,540
Total exposures at default secured by residential mortgages	49,494	3,195	52,689

[1] Off-balance sheet items include unutilised limits and loans approved, but not yet drawn.

Reconciliation of exposures secured by residential mortgages to housing loans in note 7 Loans and advances to customers

	Banking Group
	On-balance Sheet Exposures at Default Unaudited
Dollars in Millions	31/3/21
Loans and advances to customers - housing loans	49,493
Add: Partial write offs excluded under the IRB approach	1
Total housing loan exposures secured by residential mortgages	49,494

Operational risk

	Banking Group	
	Unaudited (31/3/21)	
Dollars in Millions	Implied Risk-Weighted Exposure	Total Operational Risk Capital Requirement
Operational risk	8,425	674

The Banking Group calculated operational risk capital using the standardised approach set out in BS2A, subject to a minimum value of $600 million.

Market risk

The table below shows market risk end of period and peak end-of-day capital charges.

	Banking Group			
	Unaudited (31/3/21)			
	Implied Risk-Weighted Exposure		Aggregate Capital Charge	
Dollars in Millions	End of Period	Peak End-of-Day	End of Period	Peak End-of-Day
Interest rate risk	2,698	3,509	216	281
Foreign exchange risk	14	169	1	13
Equity risk	1	1	-	-
Total market risk	2,713	3,679	217	294

The aggregate market risk exposure above is derived in accordance with BS2B and the Bank's Conditions of Registration.

For each category of market risk, the Banking Group’s end of period aggregate capital charge is the charge as at the end of period reported. The peak end-of-day aggregate capital charge is the maximum over the half year accounting period at the close of each business day.

Equity risk subject to a market risk capital charge as shown above relates to equities owned by the Bank.

Note 19 Capital Adequacy *continued*

Capital for other material risks

The Banking Group actively manages and measures all material risks affecting its operations. These risks go beyond the traditional banking risks of credit, operational and market risk. The measurement and management of all material risks is determined under the Banking Group's ICAAP and includes consideration of all other material risks, additional to those included in determining the minimum regulatory capital requirements under BS2B. Other material risks assessed by the Banking Group include balance sheet and liquidity risk, regulatory risk, conduct risk, compliance risk, sustainability risk and strategic risk.

As at 31 March 2021, the Banking Group had an internal capital allocation for strategic risk of $105 million (30 September 2020: $109 million; 31 March 2020: $109 million).

Capital structure

Contributed equity – Ordinary shares

These shares do not have a par value; each share entitles the shareholder to one vote at any meeting of shareholders. All shares rank equally in dividends and proceeds available to ordinary shareholders in a winding up.

On 31 March 2021, the RBNZ eased its prohibition on payment of dividends on ordinary shares by NZ-incorporated registered banks. The RBNZ has implemented a new restriction allowing banks to pay dividends up to a maximum of 50 per cent of prior financial year earnings and has outlined its expectations that NZ banks will exercise prudence in determining dividends. This restriction will remain in place until 1 July 2022, subject to economic conditions at that time.

Subordinated debt

Refer to note 12 for further information on perpetual notes, subordinated notes and listed subordinated notes.

Reserves

Accumulated other comprehensive income and other disclosed reserves in Tier 1 Capital includes the cost of hedging reserve of $(7) million which captures changes in fair value of hedging instruments due to currency basis and the FVOCI reserve of $1 million which captures changes in the fair value of investments in equity instruments that are measured at fair value through other comprehensive income.

The asset revaluation reserve of $2 million included in Tier 2 Capital relates to increments and any subsequent decrements arising from the revaluation of property, plant and equipment.

National Australia Bank Limited capital adequacy

The table below shows the capital adequacy ratios based on APRA capital adequacy standards, expressed as a percentage of total risk-weighted assets.

	Ultimate Parent Banking Group			Ultimate Parent Bank		
	Unaudited 31/3/21	Unaudited 30/9/20	Unaudited 31/3/20	**Unaudited 31/3/21**	Unaudited 30/9/20	Unaudited 31/3/20
Common Equity Tier 1 Capital ratio	**12.37%**	11.47%	10.39%	**12.40%**	11.50%	10.41%
Tier 1 Capital ratio	**14.01%**	13.20%	11.96%	**14.20%**	13.38%	12.13%
Total Capital ratio	**17.90%**	16.62%	14.61%	**18.33%**	17.01%	14.93%

The ultimate parent banking group data is the Level 2 capital ratio (as published in the National Australia Bank Limited Pillar 3 report) and represents the consolidation of NAB and its subsidiary entities, other than the non-consolidated subsidiaries as outlined in the Pillar 3 report.

The ultimate parent bank of the Banking Group is National Australia Bank Limited which reports under the Advanced approach for credit risk (other than for several regulatory prescribed portfolios and some other small portfolios where the standardised approach to credit risk is applied), and the AMA for operational risk. The ultimate parent bank capital ratios are effectively represented by the Level 1 capital ratios, which comprises National Australia Bank Limited and its subsidiary entities approved by APRA as part of the Extended Licensed Entity.

Under prudential regulations, NAB is required to hold capital above the prudential capital ratio ("PCR") and capital conservation buffer as determined by APRA for both the Level 1 and Level 2 Groups. The PCR is prescribed on a bilateral basis, and is not publicly disclosed. National Australia Bank Limited met the minimum capital adequacy requirements set by APRA as at 31 March 2021.

National Australia Bank Limited is required to publicly disclose risk management and capital adequacy information as at the reporting date, as specified in APRA's Prudential Standard APS 330: Public Disclosure (“APS 330”). Updates are provided on a quarterly basis in accordance with the APS 330 reporting requirements.

National Australia Bank Limited’s Annual Financial Report and Pillar 3 report, incorporating the requirements of APS 330, can be accessed at www.nab.com.au.

Note 20 Risk Management

Risk management disclosure

During the reporting period, sustainability risk was added as a material risk category within the Banking Group's risk management strategy. Sustainability risk is the risk that events (which includes Environmental, Social or Governance (ESG) issues) or conditions arise that could negatively impact the sustainability, resilience, risk and return profile, value or reputation of the Banking Group or its customers and suppliers:

For example, sustainability risk arises where:

- climate change and related policy and market changes lead to increasing customer defaults and decrease the value of collateral; and/or
- the Banking Group, its customers, or its suppliers fail to comply with legal, regulatory or voluntary standards or broader community and stakeholder expectations concerning ESG risk performance.

Sustainability risk, including that relating to climate change, is managed by implementing policies, frameworks, processes and tools used for other material risk types, such as operational risk. Governance and oversight of sustainability risk resides with the Customer and Conduct Committee, a sub-committee of RRMC.

There have been no other material changes to the Banking Group's policies for managing risk, or material exposures to new categories of risk, since 30 September 2020.

Concentrations of credit exposure

The table below presents the maximum exposure to credit risk of financial assets before taking into account any collateral held or other credit enhancements. Except for derivative financial instruments, the majority of the overseas credit exposures are raised for New Zealand based assets funded in New Zealand dollars for offshore customers.

	Banking Group
Dollars in Millions	31/3/21
Maximum exposure to credit risk	
Cash and liquid assets	7,081
Due from central banks and other institutions	1,028
Trading securities	7,780
Derivative financial instruments	5,804
Gross loans and advances to customers	91,412
Amounts due from related entities	105
Total on-balance sheet credit exposures	113,210
Off-balance sheet credit exposures	14,209
Total maximum exposure to credit risk	127,419

Note 20 Risk Management *continued*

Concentrations of credit exposure *continued*

The Banking Group's concentrations of credit exposure are reported by industry sector and geographical location in the table below. The concentrations of credit exposure by industry sector is based on Australian and New Zealand Standard Industrial Classification ("ANZSIC") codes. The concentrations of credit exposure by geographical location are based on the geographical location of the counterparty's tax residency.

	Banking Group		
	On-balance sheet Unaudited	Off-balance sheet[1] Unaudited	Total exposure Unaudited
Dollars in Millions	31/3/21	31/3/21	31/3/21
Concentration by industry			
Agriculture	13,824	1,067	14,891
Forestry and fishing	953	228	1,181
Mining	350	262	612
Manufacturing	3,329	1,532	4,861
Electricity, gas and water	1,094	505	1,599
Construction	1,102	700	1,802
Wholesale and retail trade	3,164	1,492	4,656
Accommodation, restaurants, culture and recreation	1,588	443	2,031
Transport and storage	2,013	830	2,843
Communications	350	217	567
Financial, investment and insurance	14,264	1,302	15,566
Property, business and personal services	10,083	2,099	12,182
Government, education, health and community services	8,288	1,594	9,882
Real estate - mortgage	49,493	1,919	51,412
Personal lending	994	19	1,013
Related entities[2]	2,321	-	2,321
Total credit exposures by industry	113,210	14,209	127,419
Concentration by geography			
New Zealand	107,414	13,936	121,350
Overseas	5,796	273	6,069
Total credit exposures by geography	113,210	14,209	127,419

[1] Off-balance sheet credit exposures include contingent liabilities and irrevocable commitments to extend credit.

[2] Related entities include amounts due from related entities and derivative financial assets with related entities.

Note 20 Risk Management *continued*

Interest rate repricing schedule

The following table represents a breakdown of the balance sheet by repricing dates or contractual maturity, whichever is the earlier. As interest rates and yield curves change over time, the Banking Group may be exposed to a loss in earnings due to the characteristics of the assets and their corresponding liability funding. These mismatches are actively managed as part of the overall interest rate risk management process. In managing the structural interest rate risk, the primary objectives are to limit the extent to which net interest income could be impacted from an adverse movement in interest rates and to maximise shareholder's earnings.

	Banking Group Unaudited (31/3/21)						
Dollars in Millions	Total	Up to 3 Months	Over 3 Months and up to 6 Months	Over 6 Months and up to 1 Year	Over 1 Year and up to 2 Years	Over 2 Years	Non-Interest Bearing
Assets							
Cash and liquid assets	7,291	6,981	-	-	-	-	310
Due from central banks and other institutions	1,028	1,013	15	-	-	-	-
Trading securities	7,780	3,013	754	1,806	197	2,010	-
Derivative financial instruments	5,804	-	-	-	-	-	5,804
Gross loans and advances to customers	91,412	45,488	9,015	18,622	10,473	5,701	2,113
Deductions from loans and advances to customers	(712)	-	-	-	-	-	(712)
Amounts due from related entities	105	73	-	-	-	-	32
All other assets	1,605	-	-	-	-	-	1,605
Total assets	114,313	56,568	9,784	20,428	10,670	7,711	9,152
Liabilities							
Due to central banks and other institutions	4,612	3,496	16	-	33	1,067	-
Trading liabilities	224	5	-	-	-	219	-
Derivative financial instruments	4,278	-	-	-	-	-	4,278
Deposits and other borrowings	73,699	45,846	8,613	6,114	1,294	784	11,048
Bonds and notes	18,103	2,173	867	735	3,725	10,603	-
Amounts due to related entities	1,304	1,177	-	-	-	-	127
Subordinated debt	1,949	500	-	900	-	549	-
All other liabilities	917	-	-	-	-	-	917
Total liabilities	105,086	53,197	9,496	7,749	5,052	13,222	16,370
Shareholder's equity							
Total shareholder's equity	9,227	-	-	-	-	-	9,227
Total liabilities and shareholder's equity	114,313	53,197	9,496	7,749	5,052	13,222	25,597
On-balance sheet sensitivity gap	-	3,371	288	12,679	5,618	(5,511)	(16,445)
Derivative financial instruments							
Net hedging derivative notionals	-	(2,221)	815	(9,270)	248	10,428	-
Interest sensitivity gap - net	-	1,150	1,103	3,409	5,866	4,917	(16,445)

Note 20 Risk Management *continued*

Maturity profile

The table below shows cash flows by remaining contractual maturities of the Banking Group's financial liabilities and derivative financial liabilities as at the reporting date.

The gross cash flows disclosed hereafter are the contractual undiscounted cash flows and include both principal and associated future interest payments and therefore will not agree to the carrying values on the balance sheet. Actual cash flows can differ significantly from contractual cash flows as a result of future actions of the Banking Group and its counterparties. Other liabilities only include balances which have contractual future cash flows.

	Banking Group Unaudited 31/3/21					
Dollars in Millions	On Demand	3 Months or less	3 to 12 Months	1 to 5 Years	Over 5 Years	Total (Inflow)/ Outflow
Liabilities						
Due to central banks and other institutions	1,062	1,436	1,021	1,103	-	4,622
Trading liabilities	-	6	3	20	236	265
Deposits and other borrowings	43,749	12,762	15,285	2,149	-	73,945
Bonds and notes	-	1,622	2,155	13,909	616	18,302
Amounts due to related entities	749	529	27	-	-	1,305
Other liabilities	-	339	59	157	77	632
Subordinated debt	-	6	53	1,665	527	2,251
Total	45,560	16,700	18,603	19,003	1,456	101,322
Derivative financial liabilities[1]						
Derivative financial liabilities (inflow)	-	(39,986)	(10,352)	(17,712)	(4,222)	(72,272)
Derivative financial liabilities outflow	-	42,519	12,996	23,310	5,600	84,425

[1] Derivative financial liabilities include hedging and trading derivative cash flows.

Liquidity portfolio management

The table below shows financial assets held by the Banking Group for the purpose of managing liquidity risk.

Dollars in Millions	Banking Group Unaudited 31/3/21
Cash and balances immediately convertible to cash	6,341
Net securities purchased under agreements to resell	184
Government bonds, notes and securities	4,960
Semi-government bonds, notes and securities	1,209
Corporate and other institutions bonds, notes and securities	1,611
Total liquidity portfolio	14,305

As at 31 March 2021, the Banking Group also held residential mortgage-backed securities ("RMBS") of $13,000 million of which $12,240 million is available to be sold to the RBNZ under agreements to repurchase. The amount of $12,240 million is subject to a 19% reduction in value in accordance with RBNZ's Operating Rules and Guidelines. These RMBS are secured by housing loans and other assets.

For liquidity purposes there is a 4% limit on the Banking Group's total assets giving a net balance of $4,591 million. The Banking Group had not entered into any repurchase agreements for RMBS with the RBNZ for liquidity purposes as at 31 March 2021.

Additional RBNZ facilities

As part of the COVID-19 support measures, on 20 March 2020 the RBNZ announced that it would provide term funding through a Term Auction Facility ("TAF") to give banks the ability to access term funding using repurchase agreements with qualifying collateral for a term of up to twelve months. On 10 March 2021, the RBNZ announced the removal of the TAF. The Banking Group has not entered into repurchase agreements with the RBNZ as at 31 March 2021.

On 26 May 2020, the RBNZ made available a Term Lending Facility ("TLF") to offer loans for a fixed term of three years at the rate of the Official Cash Rate ("OCR") to support lending under the BFGS. On 20 August 2020, the RBNZ announced it would extend the availability of the TLF to 31 January 2021 and extend the term to five years. On 16 December 2020, the RBNZ announced the extension of the availability of the TLF to 28 July 2021. The Banking Group has entered into repurchase agreements with the RBNZ with a value of $1,029 million as at 31 March 2021.

On 11 November 2020, the RBNZ also announced details of its Funding for Lending Programme ("FLP") aimed at lowering the cost of borrowing for New Zealand businesses and households. The FLP will allow eligible participants to access three-year floating interest rate funding at the prevailing OCR within 18 months for an initial allocation of 4% of eligible loans, with a further six months for an additional allocation of 2% of eligible loans, using qualifying collateral. The Banking Group has entered into repurchase agreements with the RBNZ with a value of $1,000 million as at 31 March 2021.

The underlying collateral accepted by the RBNZ in relation to these facilities as at 31 March 2021 are RMBS to the value of $2,427 million.

Note 20 Risk Management *continued*

Regulatory liquidity ratios

The table below shows the three-month average of the respective daily ratio values in accordance with the RBNZ's Liquidity Policy (BS13/BS13A) ("BS13") and the Bank's Conditions of Registration relating to liquidity-risk management.

The one-week mismatch ratio is a measure of the Bank's one-week mismatch amount over its total funding, where the one-week mismatch amount represents the Bank's portfolio of primary liquid assets plus expected cash inflows minus expected cash outflows during a one-week period of stress. The Bank is required to maintain this ratio above a minimum level of zero percent on a daily basis. The one-week mismatch ratio = 100 x (one-week mismatch dollar amount / total funding).

The one-month mismatch ratio is a measure of the Bank's one-month mismatch amount over its total funding, where the one-month mismatch amount represents the Bank's stock of primary and secondary liquid assets plus expected cash inflows minus expected cash outflows during a one-month period of stress. The Bank must maintain this ratio above a minimum level of zero percent on a daily basis. The one-month mismatch ratio = 100 x (one-month mismatch dollar amount / total funding).

The one-year core funding ratio measures the extent to which loans and advances are funded by funding that is considered stable. The one-year core funding ratio = 100 x (one-year core funding dollar amount / BS13 total loans and advances) and must currently remain above 50 percent on a daily basis.

	Banking Group	
	Unaudited For the 3 months ended 31/3/21	Unaudited For the 3 months ended 31/12/20
One-week mismatch ratio	**4.9%**	5.1%
One-month mismatch ratio	**5.7%**	5.8%
One-year core funding ratio	**87.8%**	88.8%

Note 20 Risk Management *continued*

Concentrations of funding

The Banking Group's concentrations of funding is reported by industry sector and geographical location in the following table. The concentrations of funding by industry sector is based on ANZSIC codes. The concentrations of funding by geographical location is based on the principal market location of the funding programmes.

		Banking Group
		Unaudited
Dollars in Millions	Note	31/3/21
Concentration by industry		
Customer deposits		
Agriculture, forestry and fishing		3,025
Mining		275
Manufacturing		1,848
Electricity, gas and water		95
Construction		1,348
Wholesale and retail trade		2,643
Accommodation, restaurants, culture and recreation		1,452
Transport and storage		876
Communications		381
Financial, investment and insurance		7,691
Property, business and personal services		12,567
Government, education, health and community services		3,610
Personal deposits		33,207
Total customer deposits by industry		69,018
Concentration by geography		
Wholesale funding		
New Zealand		11,083
Overseas[1]		19,566
Total wholesale funding by geography		30,649
Total funding		99,667
Total funding comprised:		
Customer deposits	11	69,018
Wholesale funding		
Due to central banks and other institutions		4,612
Other borrowings	11	4,681
Bonds and notes		18,103
Amounts due to related entities		1,304
Subordinated debt		1,949
Total wholesale funding		30,649
Total funding		99,667

[1] This represents the wholesale active funding programmes of BNZ-IF and the Bank from offshore markets.

Building a better working world

Independent auditor’s review report to the Shareholder of Bank of New Zealand

Conclusions

We have reviewed the consolidated interim financial statements required by Clause 25 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the “Order”) and the supplementary information required by Schedules 5, 7, 11, 13, 16 and 18 of the Order of Bank of New Zealand (the “Bank”) and the entities it controlled at 31 March 2021 or from time to time during the period (collectively the “Banking Group”) as included on pages 3 to 40 of the Disclosure Statement. The interim financial statements and supplementary information comprise:

- the balance sheet of the Banking Group as at 31 March 2021;
- the income statement, statement of comprehensive income, statement of changes in equity and condensed cash flow statement for the six months then ended of the Banking Group;
- the notes to the consolidated interim financial statements including a summary statement of significant accounting policies and;
- the supplementary information required by Schedules 5, 7, 11, 13, 16 and 18 of the Order.

Based on our review nothing has come to our attention that causes us to believe that:

- the consolidated interim financial statements (excluding the supplementary information disclosed in Notes 8, 9, 17, 18, 19 and 20, and the ‘Interest earning and discount bearing assets’ and ‘Interest and discount bearing liabilities’ disclosed on page 5 (“supplementary information”)) have not been prepared, in all material respects, in accordance with New Zealand Equivalent to International Accounting Standard 34: *Interim Financial Reporting* (NZ IAS 34) and International Accounting Standard 34: *Interim Financial Reporting* (IAS 34);
- the supplementary information (excluding information relating to capital adequacy disclosed in Note 19 and the regulatory liquidity ratios disclosed in Note 20) required to be disclosed under Schedules 5, 7, 13, 16 and 18 of the Order, does not fairly state, in all material respects, the matters to which it relates in accordance with those schedules; and
- the supplementary information relating to capital adequacy (disclosed in Note 19) and regulatory liquidity requirements (being the regulatory liquidity ratios disclosed in Note 20) that is required to be disclosed under Schedule 11 of the Order, is not, in all material respects, disclosed in accordance with Schedule 11 of the Order.

This report is made solely to the Bank’s shareholder. Our review has been undertaken so that we might state to the Bank’s shareholder those matters we are required to state to them in an independent auditor’s review report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Bank and the Bank's shareholder for our review work, for this report, or for the conclusions we have formed.

Basis for conclusions

We conducted our review in accordance with NZ SRE 2410 *(Revised) Review of Financial Statements Performed by the Independent Auditor of the Entity*. Our responsibilities are further described in the *Auditor’s Responsibilities for the Review of the Financial Statements* section of our report. We are independent of the Banking Group in accordance with the relevant ethical requirements in New Zealand relating to the audit of the annual financial statements, and we have fulfilled our other ethical responsibilities in accordance with these ethical requirements.

Ernst & Young provides audit services, other assurance and agreed upon procedures services to the Banking Group. Partners and employees of our firm may deal with the Banking Group on normal terms within the ordinary course of trading activities of the business of the Banking Group. We have no other relationship with, or interest in, the Banking Group.

Building a better working world

Directors' responsibilities for the consolidated interim financial statements and supplementary information

The directors are responsible, on behalf of the Bank, for the preparation and fair presentation of the consolidated interim financial statements in accordance with Clause 25 of the Order, which requires the consolidated interim financial statements to comply with NZ IAS 34 and IAS 34, and for such internal control as the directors determine is necessary to enable the preparation and fair presentation of consolidated interim financial statements that are free from material misstatement, whether due to fraud or error.

In addition, the directors are responsible, on behalf of the Bank, for the preparation and fair presentation of the supplementary information in the Disclosure Statement which complies with Schedules 3, 5, 7, 11, 13, 16 and 18 of the Order.

Auditor's responsibilities for the review of consolidated interim financial statements and supplementary information

Our responsibility is to express a conclusion on the consolidated interim financial statements and the supplementary information based on our review.

NZ SRE 2410 (Revised) requires us to conclude whether anything has come to our attention that causes us to believe that:

- the consolidated interim financial statements (excluding the supplementary information), taken as a whole, are not prepared in all material respects, in accordance with NZ IAS 34 and IAS 34.
- the supplementary information (excluding information relating to capital adequacy in Note 19 and the regulatory liquidity ratios disclosed in Note 20), taken as a whole, does not fairly state in all material respects, the matters to which it relates in accordance with Schedules 5, 7, 13, 16 and 18.
- the supplementary information relating to capital adequacy disclosed in Note 19 and regulatory liquidity requirements (being the regulatory liquidity ratios disclosed in Note 20), is not, in all material respects, disclosed in accordance with Schedule 11 of the Order.

A review of interim financial statements in accordance with NZ SRE 2410 (Revised) is a limited assurance engagement. We perform procedures, consisting of making enquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. The procedures performed in a review are substantially less than those performed in an audit conducted in accordance with International Standards on Auditing (New Zealand) and consequently do not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion on any element of this Disclosure Statement.

The engagement partner on the review resulting in this independent auditor's review report is Emma Winsloe.

Ernst & Young

Chartered Accountants
21 May 2021
Auckland

A member firm of Ernst & Young Global Limited

Credit Ratings

As at the date on which this Disclosure Statement is signed, the Bank has the following credit ratings applicable to its long term senior unsecured obligations payable in New Zealand, in New Zealand dollars.

Rating Agency	Current Credit Rating	Qualification
S&P Global Ratings Australia Pty Limited	AA-	Outlook Negative
Moody's Investors Service Pty Limited	A1	Outlook Stable
Fitch Australia Pty Limited	A+	Outlook Stable

Conditions of Registration

Changes in Conditions of Registration

Between 30 September 2020 and 31 March 2021, the RBNZ made the following changes to the Bank's Conditions of Registration.

On 30 November 2020, the Bank's Conditions of Registration were updated to reflect (i) a revised calculation approach for the Bank's operational risk capital to be based on the standardised approach under BS2A (including a minimum value of $600m), and ii) the continued requirement for the Bank to meet the qualitative requirements of the Advanced Measurement Approach under BS2B in relation to operational risk.

On 01 March 2021, the Bank's Conditions of Registration were updated to reinstate conditions that impose restrictions on the Bank's new residential mortgage lending at high loan-to-valuation ratios (LVRs).

From 01 January 2021, the Bank's breach reporting obligations were changed to require the Bank to publicly disclose where they have been non-compliant with their Conditions of Registration in a material respect in their Disclosure Statements.

Directors' Statement

The Directors of Bank of New Zealand state that each Director of the Bank believes, after due enquiry, that:

1. as at the date on which this Disclosure Statement is signed:
   (a) the Disclosure Statement contains all the information that is required by the Order; and
   (b) the Disclosure Statement is not false or misleading; and
2. during the six months ended 31 March 2021:
   (a) the Bank has complied with its Conditions of Registration applicable during that period;
   (b) credit exposures to connected persons were not contrary to the interests of the Banking Group; and
   (c) the Bank had systems in place to monitor and control adequately the Banking Group's material risks, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

This Disclosure Statement is dated 21st May 2021 and signed by Mr. McKay and Ms. Mentis as Directors and as responsible persons on behalf of all the other Directors.

D A McKay
Chairman

A Mentis
Managing Director and Chief Executive Officer

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