National Australia Bank

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ASX Announcement

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NAB December Quarter Trading Update

Key points

- National Australia Bank unaudited cash earnings for the first quarter were approximately $1.1 billion, an increase of more than 20% on the fourth quarter of the 2009 financial year. This included a contribution of $33 million from recent acquisitions. The earnings improvement reflected a decline in the charge for bad and doubtful debts and sound business performance.
- Total group revenue and net interest margin were broadly stable compared to the second half of 2009, with the benefit of repricing activity undertaken in 2009 offset by higher wholesale funding costs and heightened competition for deposits. Asset volume growth was subdued due to reduced customer demand and a de-leveraging of large corporate balance sheets. Markets trading income settled back towards 2008 financial year levels from the exceptional levels of 2009, as market uncertainty reduced.
- Expenses continue to be tightly managed across the Group.
- Asset quality trends are encouraging.
  - The Group charge for bad and doubtful debts (B&DD) in the December quarter was $202 million lower at $739 million compared to the September 2009 quarter.
  - The ratio of group 90+ days past due and gross impaired assets to Gross Loans and Acceptances (GLA) has been broadly flat since June and was 1.84% at 31 December 2009, compared to 1.75% at September 2009.
- For the financial year to date approximately $11 billion of term wholesale funding has been raised compared to a 2010 full year target of $20 to $25 billion. This has been achieved without the use of any government guarantees. The weighted average term to maturity of the funds raised year-to-date is just under six years. The Stable Funding Index was 81% at 31 December 2009 (78% at 30 September 2009).
- The Group continues to maintain a strong liquidity position.
- The Group capital position is also strong, with the Tier 1 ratio increasing to 9.3% from 9.0% at 30 September 2009. Any capital impact of the proposed AXA APH acquisition will only occur after the transaction has received final court approval. The capital requirement will be assessed at that time after considering the March capital position, the level of scrip acceptances by AXA minority shareholders and the business outlook.

Executive Commentary

"Our businesses delivered a sound result in the December quarter. This was achieved despite subdued credit growth, heightened competitive pressures and a continued upward trend in average funding costs," National Australia Bank Group CEO Cameron Clyne said.

"Bad and doubtful debt charges have fallen and are not expected to return to the peak experienced in the third quarter of the 2009 financial year. However, given the fragile global recovery and uncertain regulatory environment, a conservative approach to capital and liquidity management remains appropriate.

"We continued to invest in business banking and wealth management in Australia through a combination of organic and inorganic initiatives. One important part of this, the integration of Aviva, is progressing well and exceeding our expectations.

"Work to finalise our proposal to acquire the Australian and New Zealand businesses of AXA APH is on-going.

"In Australia actions taken to eliminate many customer unfriendly fees, as part of creating a sustainable long term business, have delivered a significant reduction in customer complaints. Since July we have seen a steady improvement in NAB's personal customer satisfaction levels. We are attracting new customers and also retaining more customers. In the financial year to the end of January, new transaction account openings are up by 25% while closures have fallen by 22% compared to the same time last year.

"Our United Kingdom franchise remains well positioned to benefit from any improvement in operating conditions. We will continue to monitor market developments in the UK," he said.

Business Commentary[1]

Business Banking

Business Banking revenue continued to grow. Lending volumes were held steady even though system declined due to low customer appetite for credit and de-leveraging of large corporate balance sheets. Competition for loans and deposits was strong. Business Banking maintained clear leadership over its major competitors in customer satisfaction (East & Partners, Business Banking Customer Satisfaction Monitor - December 2009).

While the business credit environment continues to show signs of improvement, the potential impact on customers of the strong Australian dollar and rising interest rates is uncertain. The ratio of 90+ days past due and gross impaired assets to GLAs increased marginally to 1.95% at 31 December 2009 from 1.89% at 30 September 2009.

Personal Banking

Personal Banking has undertaken a range of initiatives to improve customer relationships and build a more sustainable, long term business model based on fair value for customers.

Reflecting the impact of the abolition of certain fees, other operating income reduced. There also continues to be pressure on net interest income from higher wholesale funding costs and intense competition for deposits. As a result of all these factors, total revenue in Personal Banking fell.

Underlying cost growth remains well controlled, with savings from efficiency and quality initiatives continuing to fund ongoing business investment.

During the quarter the Challenger Mortgage Management business (subsequently re-branded Advantedge) was acquired including approximately $4.5 billion of mortgages. Excluding this, the mortgage book grew at approximately 0.9 times system.

[1] Business structure changes reflected in the trading update are explained in the attachment to this announcement.

Household deposits grew more than twice system largely as a result of strong growth in UBank - our new online savings bank franchise.

The ratio of 90+ days past due and gross impaired assets to GLAs fell from 1.00% at September 2009 to 0.91% at December 2009. Excluding Advantedge, the ratio of 90+ days past due and gross impaired assets to GLAs was 0.95% at 31 December 2009.

MLC & NAB Wealth

Revenue continued to strengthen during the quarter in line with the recovery in investment markets. Funds under management increased due to both market performance and positive net flows, resulting in increased market share for the investments business. Insurance net income has shown a recovery from the prior quarter with claims experience more in line with long term norms. While we continue to invest in the business, operating cost growth has been well contained.

The integration of Aviva is progressing well and exceeding our expectations. The JBWere strategic alliance is now fully operational. Adviser retention has been good and total adviser numbers have increased post acquisition.

Wholesale Banking

With reduced market uncertainty, revenues for the Markets and Treasury businesses, while strong, have declined from the exceptional levels of last year. Sales and Trading revenue has remained solid during the quarter and is broadly consistent with the average revenue performance during the second half of the 2009 financial year.

Wholesale Banking has experienced a significant fall in bad and doubtful debt charges against the prior quarter. The portfolio is stable with over 90% the equivalent of investment grade.

New Zealand

Economic conditions in New Zealand remain weak, although there are some early signs of improvement, reflected in modest GDP growth over the last two quarters. Demand for both business and consumer credit remains low.

Competition for deposits continues to be intense. However, asset repricing and favourable mix changes within the housing portfolio provided some offset in the quarter, keeping net interest margin relatively stable. Revenue was largely consistent with the 2009 second half average revenue performance.

Business lending decreased slightly during the quarter reflecting a weaker business credit environment and customers reducing debt. Market share in deposits increased, helping to strengthen BNZ's Customer Funding Index.

Costs continue to be carefully managed and remain flat against prior periods.

There are some early signs that asset quality is stabilising. The ratio of 90+ days past due and impaired assets to GLAs increased only modestly during the quarter to 1.60% at 31 December 2009 from 1.53% at 30 September 2009.

United Kingdom

The UK operating environment remains challenging despite some early signs of economic recovery. Cash earnings benefited from a lower bad and doubtful debt charge, albeit still above historical levels, and easing of funding costs.

Underlying net interest income continued to improve during the quarter as basis risk moderated and front book margins strengthened across key personal and business products. Competition for deposits remained strong. Other operating income remains under pressure.

The ratio of 90+ days past due and gross impaired assets to GLAs deteriorated in the quarter to 2.90% from 2.61% at September 2009, driven predominantly by the commercial property portfolio.

Specialised Group Assets

The Specialised Group Assets portfolio comprises non-franchise activities previously managed by nabCapital.

The UK and US economies, which remain fragile, are strong influences on the portfolio. Accordingly, further deterioration of the portfolio is expected in the 2010 financial year, with key watch areas being the leverage and property exposures. The portfolio is not currently profitable.

There was no material change in the position of the Synthetic Collateralised Debt Obligations (SCDOs) in the first quarter. During this period one of the six SCDOs breached its original attachment point. The SCDO hedge worked as expected with negligible impact on earnings.

Further details of the current and historic economics of the Specialised Group Assets portfolio will be provided during March in conjunction with the re-presentation of results under the new operating structure.

Balance Sheet Commentary

Bad and Doubtful Debt Provisions

Collective Provision balances have increased marginally to $3,573 million. Specific Provision balances have increased by $291 million since 30 September 2009.

Total provision balances (including the credit risk adjustment on assets at fair value) as at 31 December 2009 were $5,415 million compared to $5,104 million at 30 September 2009.

Both specific and collective provision coverage ratios have increased since 30 September 2009.

Capital

At 31 December 2009 the Group's Tier 1 capital ratio was 9.3%. The increase in the Tier 1 ratio over the quarter is primarily attributable to lower risk weighted assets reflecting muted balance sheet growth and some improvement in credit quality. The increase in the Tier 1 ratio is also net of a number of regulatory changes.

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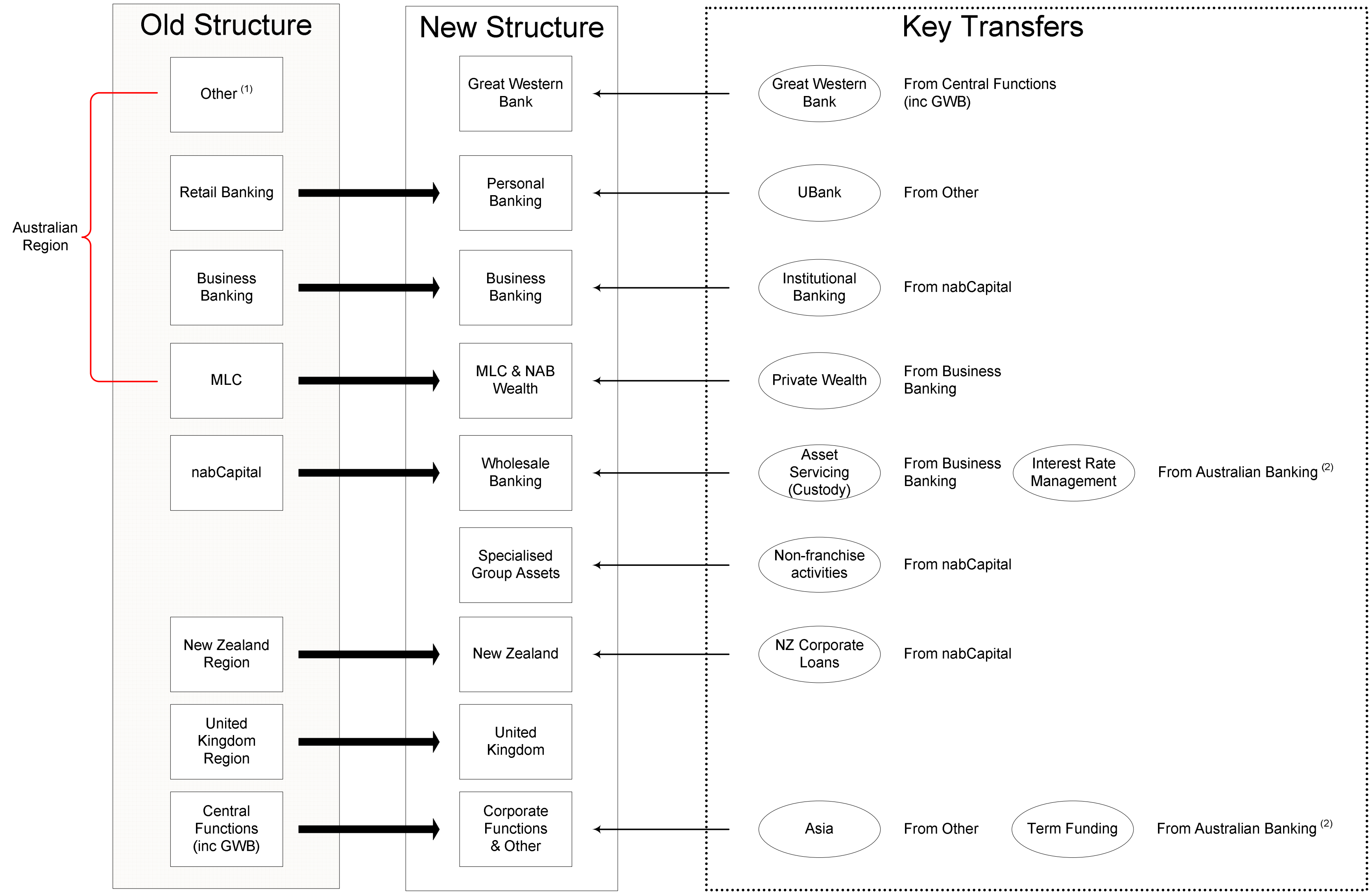
Disclaimer

This announcement is based on unaudited information. It also contains certain forward-looking statements. The words "anticipate", "believe", "expect", "project", "estimate", "likely", "intend", "should", "could", "may", "target", "plan" and other similar expressions are intended to identify forward-looking statements. Indications of, and guidance on, future earnings and financial position and performance are also forward-looking statements. Such forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors, many of which are beyond the control of the Group, which may cause actual results to differ materially from those expressed or implied in such statements. There can be no assurance that actual outcomes will not differ materially from these statements. For further information on important factors that could cause actual results to differ materially from those projected in such statements are contained in the Group's Annual Financial Report.

Attachment - New Structure & Key Transfers



(1) Old structure Other only contained UBank and Asia
(2) Australian Banking comprised old structure Retail Banking and Business Banking