Westpac New Zealand Limited

Disclosure Statement

For the six months ended 31 March 2018

Contents

General information

Certain information contained in this Disclosure Statement is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (‘**Order’**).

In this Disclosure Statement, reference is made to:

– Westpac New Zealand Limited (otherwise referred to as the ‘**Bank**’);
– Westpac New Zealand Limited and its controlled entities (otherwise referred to as the ‘**Banking Group**’);
– Westpac Banking Corporation (otherwise referred to as the ‘**Ultimate Parent Bank**’); and
– Ultimate Parent Bank and its controlled entities (otherwise referred to as the ‘**Ultimate Parent Bank Group**’).

Words and phrases not defined in this Disclosure Statement, but defined by the Order, have the meaning given by the Order when used in this Disclosure Statement.

Limits on material financial support by the Ultimate Parent Bank

On 19 November 2015, the Australian Prudential Regulation Authority (‘**APRA**’) informed the Ultimate Parent Bank that its Extended Licensed Entity (‘**ELE**’) non-equity exposures to New Zealand banking subsidiaries is to transition to be below a limit of 5% of the Ultimate Parent Bank’s Level 1 Tier 1 capital, as part of an initiative to reduce Australian bank non-equity exposure to their respective New Zealand banking subsidiaries and branches.

The ELE consists of the Ultimate Parent Bank and its subsidiary entities that have been approved by APRA to be included in the ELE for the purposes of measuring capital adequacy.

APRA has allowed a period of five years commencing on 1 January 2016 to transition to be less than the 5% limit. Exposures for the purposes of this limit include all committed, non-intraday, non-equity exposures including derivatives and off-balance sheet exposures. For the purposes of assessing this exposure, the 5% limit excludes equity investments and holdings of capital instruments in New Zealand banking subsidiaries. As at 31 March 2018, the ELE’s non-equity exposures to New Zealand banking subsidiaries affected by the limit were below 5% of Level 1 Tier 1 capital of the Ultimate Parent Bank.

APRA has also confirmed the terms on which the Ultimate Parent Bank ‘may provide contingent funding support to a New Zealand banking subsidiary during times of financial stress’. APRA has confirmed that, at this time, only covered bonds meet its criteria for contingent funding arrangements.

Directors

There have been no changes in the composition of the Board of Directors of the Bank (the ‘**Board**’) since 30 September 2017.

Credit ratings

The Bank has the following credit ratings with respect to its long-term senior unsecured obligations, including obligations payable in New Zealand in New Zealand dollars, as at the date the Directors signed this Disclosure Statement:

Rating Agency	Current Credit Rating	Rating Outlook
Fitch Ratings	AA-	Stable
Moody’s Investors Service	A1	Stable
S&P Global Ratings	AA-	Negative

Guarantee arrangements

No material obligations of the Bank are guaranteed as at the date the Directors signed this Disclosure Statement.

Auditor

PricewaterhouseCoopers
PricewaterhouseCoopers Tower
188 Quay Street
Auckland, New Zealand

Other matters

On 3 May 2018 the Financial Markets Authority (‘**FMA**’) and the Reserve Bank sent a letter to the chief executives of New Zealand’s registered banks (including the Bank) requesting information on what work had been undertaken in each bank to identify and address any conduct and culture issues. This was in response to the Australian Royal Commission into misconduct in banking, superannuation and other financial services. The purpose of the request was to understand how New Zealand banks had obtained assurance that misconduct of the type highlighted in Australia is not taking place in New Zealand. The Bank responded to this request on 18 May 2018. The FMA and the Reserve Bank sent a similar letter to life insurers on 24 May 2018. The outcome of these engagements may lead to further scrutiny of the financial services industry in New Zealand.

Directors’ statement

Each Director of the Bank believes, after due enquiry, that, as at the date on which this Disclosure Statement is signed, the Disclosure Statement:

(a) contains all the information that is required by the Order; and

(b) is not false or misleading.

Each Director of the Bank believes, after due enquiry, that, over the six months ended 31 March 2018:

(a) the Bank has complied with all conditions of registration imposed on it pursuant to section 74 of the Reserve Bank of New Zealand Act 1989 (‘**Reserve Bank Act**’) except as noted in Note 14 to the financial statements and page 31;

(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 has been signed by all the Directors:

Janice Dawson

David McLean

Malcolm Bailey

Peter King

Jonathan Mason

Christopher Moller

Mary Quin

Dated this 24th day of May 2018

Income statement for the six months ended 31 March 2018

		THE BANKING GROUP		
$ millions	Note	**Six Months Ended 31 Mar 18 Unaudited**	Six Months Ended 31 Mar 17 Unaudited	Year Ended 30 Sep 17 Audited
Interest income		**1,971**	1,947	3,917
Interest expense		**(1,066)**	(1,112)	(2,176)
Net interest income		**905**	835	1,741
Non-interest income	2	**195**	188	405
Net operating income before operating expenses and impairment charges		**1,100**	1,023	2,146
Operating expenses		**(460)**	(465)	(954)
Impairment (charges)/benefits	3	**(27)**	36	76
Profit before income tax		**613**	594	1,268
Income tax expense		**(171)**	(168)	(359)
Net profit for the period/year		**442**	426	909

The above income statement should be read in conjunction with the accompanying notes.

Statement of comprehensive income for the six months ended 31 March 2018

	THE BANKING GROUP		
$ millions	**Six Months Ended 31 Mar 18 Unaudited**	Six Months Ended 31 Mar 17 Unaudited	Year Ended 30 Sep 17 Audited
Net profit for the period/year	**442**	426	909
Other comprehensive income			
Items that may be reclassified subsequently to profit or loss			
Gains/(losses) on available-for-sale securities:			
Recognised in equity	**2**	9	11
Gains/(losses) on cash flow hedging instruments:			
Recognised in equity	**(10)**	(20)	(76)
Transferred to income statement	**29**	42	79
Income tax on items taken to or transferred from equity:			
Available-for-sale securities reserve	**(1)**	(3)	(3)
Cash flow hedge reserve	**(5)**	(6)	-
Items that will be not be reclassified subsequently to profit or loss			
Remeasurement of defined benefit obligation recognised in equity (net of tax)	**(2)**	10	10
Other comprehensive income for the period/year (net of tax)	**13**	32	21
Total comprehensive income for the period/year	**455**	458	930

The above statement of comprehensive income should be read in conjunction with the accompanying notes.

Balance sheet as at 31 March 2018

		THE BANKING GROUP		
$ millions	Note	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Assets				
Cash and balances with central banks		**1,974**	1,495	1,659
Receivables due from other financial institutions		**523**	753	407
Other assets		**307**	235	264
Trading securities		**1,847**	1,708	1,797
Derivative financial instruments		**432**	63	220
Available-for-sale securities		**3,555**	3,818	4,087
Loans	4, 5	**79,113**	76,542	77,261
Due from related entities		**1,616**	1,349	2,017
Property and equipment		**140**	145	146
Deferred tax assets		**167**	171	162
Intangible assets		**616**	589	607
Total assets		**90,290**	86,868	88,627
Liabilities				
Payables due to other financial institutions		**294**	410	143
Other liabilities		**493**	434	502
Deposits and other borrowings	7	**62,183**	58,429	58,998
Other financial liabilities at fair value through income statement		**20**	10	19
Derivative financial instruments		**278**	799	484
Debt issues	8	**14,970**	15,803	16,729
Current tax liabilities		**40**	16	75
Provisions		**82**	75	85
Total liabilities excluding related entities liabilities		**78,360**	75,976	77,035
Due to related entities		**2,033**	3,066	2,126
Loan capital		**2,592**	1,138	2,616
Total related entities liabilities		**4,625**	4,204	4,742
Total liabilities		**82,985**	80,180	81,777
Net assets		**7,305**	6,688	6,850
Shareholder's equity				
Share capital		**5,100**	3,750	3,750
Reserves		**(50)**	(54)	(65)
Retained profits		**2,255**	2,992	3,165
Total shareholder's equity		**7,305**	6,688	6,850
Interest earning and discount bearing assets		**88,698**	85,611	87,294
Interest and discount bearing liabilities		**75,922**	73,441	74,996

The above balance sheet should be read in conjunction with the accompanying notes.

Statement of changes in equity for the six months ended 31 March 2018

THE BANKING GROUP		Reserves			
$ millions	**Share Capital**	**Available-for-sale Securities Reserve**	**Cash Flow Hedge Reserve**	**Retained Profits**	**Total**
As at 1 October 2016 (Audited)	3,750	1	(77)	2,886	6,560
Six months ended 31 March 2017 (Unaudited)					
Net profit for the period	-	-	-	426	426
Net gains/(losses) from changes in fair value	-	9	(20)	-	(11)
Income tax effect	-	(3)	6	-	3
Transferred to income statement	-	-	42	-	42
Income tax effect	-	-	(12)	-	(12)
Remeasurement of defined benefit obligations	-	-	-	13	13
Income tax effect	-	-	-	(3)	(3)
Total comprehensive income for the six months ended 31 March 2017	-	6	16	436	458
Transactions with owners:					
Dividends paid on ordinary shares	-	-	-	(330)	(330)
As at 31 March 2017 (Unaudited)	3,750	7	(61)	2,992	6,688
As at 1 October 2016 (Audited)	3,750	1	(77)	2,886	6,560
Year ended 30 September 2017 (Audited)					
Net profit for the year	-	-	-	909	909
Net gains/(losses) from changes in fair value	-	11	(76)	-	(65)
Income tax effect	-	(3)	22	-	19
Transferred to income statement	-	-	79	-	79
Income tax effect	-	-	(22)	-	(22)
Remeasurement of defined benefit obligations	-	-	-	14	14
Income tax effect	-	-	-	(4)	(4)
Total comprehensive income for the year ended 30 September 2017	-	8	3	919	930
Transactions with owners:					
Dividends paid on ordinary shares	-	-	-	(640)	(640)
As at 30 September 2017 (Audited)	3,750	9	(74)	3,165	6,850
Six months ended 31 March 2018 (Unaudited)					
Net profit for the period	**-**	**-**	**-**	**442**	**442**
Net gains/(losses) from changes in fair value	**-**	**2**	**(10)**	**-**	**(8)**
Income tax effect	**-**	**(1)**	**3**	**-**	**2**
Transferred to income statement	**-**	**-**	**29**	**-**	**29**
Income tax effect	**-**	**-**	**(8)**	**-**	**(8)**
Remeasurement of defined benefit obligations	**-**	**-**	**-**	**(3)**	**(3)**
Income tax effect	**-**	**-**	**-**	**1**	**1**
Total comprehensive income for the six months ended 31 March 2018	**-**	**1**	**14**	**440**	**455**
Transactions with owners:					
Share capital issued (refer to Note 9)	**1,350**	**-**	**-**	**-**	**1,350**
Dividends paid on ordinary shares (refer to Note 9)	**-**	**-**	**-**	**(1,350)**	**(1,350)**
As at 31 March 2018 (Unaudited)	**5,100**	**10**	**(60)**	**2,255**	**7,305**

The above statement of changes in equity should be read in conjunction with the accompanying notes.

Statement of cash flows for the six months ended 31 March 2018

	THE BANKING GROUP		
$ millions	**Six Months Ended 31 Mar 18 Unaudited**	Six Months Ended 31 Mar 17 Unaudited	Year Ended 30 Sep 17 Audited
Cash flows from operating activities			
Interest income received	**1,965**	1,953	3,902
Interest expense paid	**(1,118)**	(1,138)	(2,158)
Non-interest income received	**181**	182	422
Operating expenses paid	**(443)**	(414)	(844)
Income tax paid	**(217)**	(216)	(334)
Cash flows from operating activities before changes in operating assets and liabilities	**368**	367	988
Net (increase)/decrease in:			
Receivables due from other financial institutions	**228**	(33)	313
Other assets	**(25)**	1	(14)
Trading securities	**(29)**	421	312
Loans	**(1,891)**	(1,409)	(2,103)
Due from related entities	**391**	572	(281)
Net increase/(decrease) in:			
Payables due to other financial institutions	**151**	395	128
Other liabilities	**10**	(6)	9
Deposits and other borrowings	**3,185**	(362)	207
Other financial liabilities at fair value through income statement	**1**	(390)	(381)
Due to related entities[1]	**109**	573	(197)
Net movement in external and related entity derivative financial instruments	**(69)**	(489)	(627)
Net cash provided by/(used in) operating activities	**2,429**	(360)	(1,646)
Cash flows from investing activities			
Purchase of available-for-sale securities	**-**	(128)	(533)
Proceeds from available-for-sale securities	**499**	30	162
Purchase of capitalised computer software	**(30)**	(25)	(61)
Purchase of property and equipment	**(16)**	(7)	(31)
Net cash provided by/(used in) investing activities	**453**	(130)	(463)
Cash flows from financing activities			
Issue of ordinary share capital	**1,350**	-	-
Net movement in due to related entities[1]	**(158)**	(97)	(287)
Proceeds from debt issues	**550**	5,644	7,490
Repayments of debt issues	**(2,615)**	(4,650)	(5,698)
Issue of loan capital (net of transaction fees)	**-**	-	1,485
Dividends paid to ordinary shareholders	**(1,350)**	(330)	(640)
Net cash provided by/(used in) financing activities	**(2,223)**	567	2,350
Net increase/(decrease) in cash and cash equivalents	**659**	77	241
Cash and cash equivalents at beginning of the period/year	**1,659**	1,418	1,418
Cash and cash equivalents at end of the period/year	**2,318**	1,495	1,659
Cash and cash equivalents at end of the period/year comprise:			
Cash on hand	**1,750**	179	179
Balances with central banks	**224**	1,316	1,480
Receivables due from other financial institutions classified as cash and cash equivalents	**344**	-	-
Cash and cash equivalents at end of the period/year	**2,318**	1,495	1,659

[1] Certain comparatives have been revised for consistency. The reclassification was made to better reflect the Banking Group's cash flows from operating and financing activities and has no effect on the balance sheet or income statement.

The above statement of cash flows should be read in conjunction with the accompanying notes.

Notes to the financial statements

Note 1 Statement of accounting policies

These condensed consolidated interim financial statements ('**financial statements**') have been prepared and presented in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 ('**Order**') and Generally Accepted Accounting Practice, as appropriate for for-profit entities, and the New Zealand equivalent to International Accounting Standard 34 *Interim Financial Reporting* and should be read in conjunction with the Disclosure Statement for the year ended 30 September 2017. These financial statements comply with International Accounting Standard 34 *Interim Financial Reporting* as issued by the International Accounting Standards Board.

Basis of preparation

These financial statements have been prepared under the historical cost convention, as modified by applying fair value accounting to available-for-sale securities and financial assets and financial liabilities (including derivative instruments) measured at fair value through income statement or in other comprehensive income. The going concern concept has been applied.

All amounts in these financial statements have been rounded to the nearest million dollars unless otherwise stated.

The same accounting policies and methods of computation have been followed in preparing these financial statements as were used in preparing the financial statements for the year ended 30 September 2017.

The areas of judgment, estimates and assumptions in these financial statements, including the key sources of estimation uncertainty, are consistent with those in the financial statements for the year ended 30 September 2017.

Comparative information has been revised where appropriate to conform to changes in presentation in the current reporting period and to enhance comparability. Where there has been a material restatement of comparative information the nature of, and the reason for, the restatement is disclosed in the relevant note.

Note 2 Non-interest income

	THE BANKING GROUP		
$ millions	**Six Months Ended 31 Mar 18 Unaudited**	Six Months Ended 31 Mar 17 Unaudited	Year Ended 30 Sep 17 Audited
Fees and commissions	**185**	189	400
Net ineffectiveness on qualifying hedges	**4**	(9)	(12)
Other non-interest income	**6**	8	17
Total non-interest income	**195**	188	405

Note 3 Impairment charges/(benefits)

	THE BANKING GROUP				
$ millions	**Residential Mortgages**	**Other Retail**	**Corporate**	**Other**	**Total**
Six months ended 31 March 2018 (Unaudited)					
Individually assessed provisions raised	**4**	**1**	**14**	**-**	**19**
Reversal of previously recognised impairment charges	**(1)**	**(1)**	**(2)**	**-**	**(4)**
Collectively assessed provisions raised/(released)	**1**	**4**	**-**	**-**	**5**
Bad debts written-off/(recovered) directly to the income statement	**(2)**	**20**	**(11)**	**-**	**7**
Total impairment charges/(benefits)	**2**	**24**	**1**	**-**	**27**
Six months ended 31 March 2017 (Unaudited)					
Individually assessed provisions raised	3	1	5	-	9
Reversal of previously recognised impairment charges	(2)	-	(46)	-	(48)
Collectively assessed provisions raised/(released)	7	(3)	(12)	-	(8)
Bad debts written-off/(recovered) directly to the income statement	(1)	13	(1)	-	11
Total impairment charges/(benefits)	7	11	(54)	-	(36)
Year ended 30 September 2017 (Audited)					
Individually assessed provisions raised	8	4	6	-	18
Reversal of previously recognised impairment charges	(4)	(1)	(62)	-	(67)
Collectively assessed provisions raised/(released)	5	(10)	(51)	-	(56)
Bad debts written-off/(recovered) directly to the income statement	-	31	(2)	-	29
Total impairment charges/(benefits)	9	24	(109)	-	(76)

Notes to the financial statements

Note 4 Loans

	THE BANKING GROUP		
$ millions	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Overdrafts	**1,236**	1,184	1,296
Credit card outstandings	**1,548**	1,492	1,518
Money market loans	**1,228**	1,362	1,250
Term loans:			
Housing	**47,909**	46,252	46,947
Non-housing	**26,778**	25,718	25,778
Other	**790**	932	822
Total gross loans	**79,489**	76,940	77,611
Provisions for impairment charges on loans	**(376)**	(398)	(350)
Total net loans	**79,113**	76,542	77,261

As at 31 March 2018, $7,539 million of housing loans, accrued interest (representing accrued interest on the outstanding housing loans) and cash (representing collections of principal and interest from the underlying housing loans), were used by the Banking Group to secure the obligations of Westpac Securities NZ Limited ('**WSNZL**') under the Bank's Global Covered Bond Programme ('**CB Programme**') (31 March 2017: $7,539 million, 30 September 2017: $7,535 million). These pledged assets were not derecognised from the Banking Group's balance sheet in accordance with the accounting policies outlined in Note 1 to the financial statements included in the Disclosure Statement for the year ended 30 September 2017. As at 31 March 2018, the New Zealand dollar equivalent of bonds issued by WSNZL under the CB Programme was $5,506 million (31 March 2017: $3,399 million, 30 September 2017: $5,246 million).

Notes to the financial statements

Note 5 Asset quality

$ millions	THE BANKING GROUP 31 Mar 18 Unaudited Residential Mortgages	Other Retail	Corporate	Other	Total
Neither past due nor impaired	46,952	3,765	26,863	403	77,983
Past due but not impaired assets					
Less than 30 days past due	724	143	110	-	977
At least 30 days but less than 60 days past due	96	31	33	-	160
At least 60 days but less than 90 days past due	47	13	11	-	71
At least 90 days past due	63	25	12	-	100
Total past due assets not impaired	930	212	166	-	1,308
Individually impaired assets[1]					
Balance at beginning of the period	32	5	136	-	173
Additions	16	3	39	-	58
Amounts written off	(1)	(1)	-	-	(2)
Returned to performing or repaid	(20)	(2)	(9)	-	(31)
Balance at end of the period	27	5	166	-	198
Total gross loans[2]	47,909	3,982	27,195	403	79,489
Individually assessed provisions					
Balance at beginning of the period	7	5	36	-	48
Impairment charges/(benefits):					
New provisions	4	1	14	-	19
Reversal of previously recognised impairment charges	(1)	(1)	(2)	-	(4)
Amounts written off	(1)	(2)	1	-	(2)
Interest adjustments	-	-	-	-	-
Balance at end of the period	9	3	49	-	61
Collectively assessed provisions					
Balance at beginning of the period	54	97	181	-	332
Impairment charges/(benefits)	1	4	-	-	5
Interest adjustments	1	7	5	-	13
Balance at end of the period	56	108	186	-	350
Total provisions for impairment charges on loans and credit commitments	65	111	235	-	411
Provision for credit commitments	-	(4)	(31)	-	(35)
Total provisions for impairment charges on loans	65	107	204	-	376
Total net loans	47,844	3,875	26,991	403	79,113

[1] The Banking Group had undrawn commitments of $5 million (31 March 2017: $8 million, 30 September 2017: $4 million) to counterparties for whom drawn balances are classified as individually impaired assets under corporate loans as at 31 March 2018.

[2] The Banking Group did not have other assets under administration as at 31 March 2018.

Notes to the financial statements

Note 6 Financial assets pledged as collateral

The Banking Group is required to provide collateral to other financial institutions, as part of standard terms, to secure liabilities. In addition to assets supporting the CB Programme disclosed in Note 4, the carrying value of these financial assets pledged as collateral is:

	THE BANKING GROUP		
$ millions	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Cash	**177**	753	407
Securities pledged under repurchase agreements:			
Available-for-sale securities[1]	**116**	603	41
Trading securities	**20**	-	-
Total amount pledged to secure liabilities (excluding CB Programme)	**313**	1,356	448

[1] As at 31 March 2018, $116 million of available-for-sale securities were pledged as collateral to the New Zealand Branch of the Ultimate Parent Bank (31 March 2017: $603 million, 30 September 2017: $22 million) which is recorded within due to related entities and nil was pledged to third parties (31 March 2017: nil, 30 September 2017: $19 million) which is recorded as other financial liabilities at fair value through income statement.

Note 7 Deposits and other borrowings

	THE BANKING GROUP		
$ millions	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Certificates of deposit	**555**	1,617	593
Non-interest bearing, repayable at call	**5,869**	5,081	5,274
Other interest bearing:			
At call	**24,164**	23,894	23,117
Term	**31,595**	27,837	30,014
Total deposits and other borrowings	**62,183**	58,429	58,998

Deposits and other borrowings have been prepared under both the historical cost convention and by applying fair value accounting to certain products. Refer to Note 10 for further details.

Note 8 Debt issues

	THE BANKING GROUP		
$ millions	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Short-term debt			
Commercial paper	**590**	2,398	1,642
Total short-term debt	**590**	2,398	1,642
Long-term debt			
Non-domestic medium-term notes	**5,835**	6,908	6,628
Covered bonds	**5,487**	3,386	5,236
Domestic medium-term notes	**3,058**	3,111	3,223
Total long-term debt	**14,380**	13,405	15,087
Total debt issues	**14,970**	15,803	16,729

Debt issues have been prepared under both the historical cost convention and by applying fair value accounting to certain products. Refer to Note 10 for further details.

Note 9 Related entities

Controlled entities of the Bank are set out in Note 24 to the financial statements included in the Disclosure Statement for the year ended 30 September 2017. There have been no changes to the controlled entities during the period.

In November 2017, the Banking Group repaid $200 million of funding owing to the New Zealand Branch of the Ultimate Parent Bank.

On 15 February 2018, the Bank declared and paid a dividend of $1,350 million to its immediate parent company, Westpac New Zealand Group Limited ('**WNZGL**'). An issue of 1,350 million ordinary shares in the Bank to WNZGL was made on the same day of payment of the dividend at a price of $1 per share and on the same terms of issue as all other ordinary shares on issue to WNZGL.

Notes to the financial statements

Note 10 Fair value of financial assets and financial liabilities

Fair Valuation Control Framework

The Banking Group uses a Fair Valuation Control Framework where the fair value is either determined or validated by a function independent of the transaction. This framework formalises the policies and procedures used to achieve compliance with relevant accounting, industry and regulatory standards. The framework includes specific controls relating to:

- the revaluation of financial instruments;
- independent price verification;
- fair value adjustments; and
- financial reporting.

A key element of the Framework is the Revaluation Committee, comprising senior valuation specialists from within the Ultimate Parent Bank Group. The Revaluation Committee reviews the application of the agreed policies and procedures to assess that a fair value measurement basis has been applied.

The method of determining fair value differs depending on the information available.

Fair value hierarchy

A financial instrument's categorisation within the valuation hierarchy is based on the lowest level input that is significant to the fair value measurement.

The Banking Group categorises all fair value instruments according to the hierarchy described below.

Valuation techniques

The Banking Group applies market accepted valuation techniques in determining the fair valuation of over-the-counter derivatives. This includes credit valuation adjustments and funding valuation adjustments, which incorporates credit risk and funding costs and benefits that arise in relation to uncollateralised derivative positions, respectively.

The specific valuation techniques, the observability of the inputs used in valuation models and the subsequent classification for each significant product category are outlined below.

Financial instruments measured at fair value

Level 1 instruments

The fair value of financial instruments traded in active markets based on recent unadjusted quoted prices. These prices are based on actual arm's length basis transactions.

The valuations of Level 1 instruments require little or no management judgment.

Instrument	Balance sheet category	Includes:	Valuation technique
Non-asset backed debt instruments	Trading securities Available-for-sale securities	New Zealand Government bonds	These instruments are traded in liquid, active markets where prices are readily observable. No modelling or assumptions are used in the valuation.

Level 2 instruments

The fair value for financial instruments that are not actively traded are determined using valuation techniques which maximise the use of observable market prices. Valuation techniques include:

- the use of market standard discounting methodologies;
- option pricing models; and
- other valuation techniques widely used and accepted by market participants.

Notes to the financial statements

Note 10 Fair value of financial assets and financial liabilities (continued)

Instrument	Balance sheet category	Includes:	Valuation technique
Interest rate products	Derivative financial instruments Due from related entities Due to related entities	Interest rate swaps, forwards and options – derivative financial instruments	Industry standard valuation models are used to calculate the expected future value of payments by product, which is discounted back to a present value. The model's interest rate inputs are benchmark interest rates and active broker quoted interest rates in the swap, bond and futures markets. Interest rate volatilities are sourced from brokers and consensus data providers.
Foreign exchange products	Derivative financial instruments Due from related entities Due to related entities	FX swaps – derivative financial instruments	Derived from market observable inputs or consensus pricing providers using industry standard models.
Non-asset backed debt instruments	Trading securities Available-for-sale securities Due from related entities Other financial liabilities at fair value through income statement Due to related entities	Local authority and NZ public securities, other bank issued certificates of deposit, commercial paper, other government securities and corporate bonds Security repurchase agreements and reverse repurchase agreements over non-asset backed debt securities with related and third parties	Valued using observable market prices which are sourced from consensus pricing services, broker quotes or inter-dealer prices.
Deposits and other borrowings at fair value	Deposits and other borrowings	Certificates of deposit	Discounted cash flow using market rates offered for deposits of similar remaining maturities.
Debt issues at fair value	Debt issues	Commercial paper	Discounted cash flows, using a discount rate which reflects the terms of the instrument and the timing of cash flows adjusted for market observable changes in the Bank's implied credit worthiness.

Level 3 instruments

Financial instruments valued where at least one input that could have a significant effect on the instrument's valuation is not based on observable market data due to illiquidity or complexity of the product. These inputs are generally derived and extrapolated from other relevant market data and calibrated against current market trends and historical transactions.

These valuations are calculated using a high degree of management judgment.

The table below summarises the attribution of financial instruments carried at fair value to the fair value hierarchy:

	THE BANKING GROUP			
	31 Mar 18 Unaudited			
$ millions	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value				
Trading securities	7	1,840	-	1,847
Derivative financial instruments	-	432	-	432
Available-for-sale securities	1,183	2,372	-	3,555
Due from related entities	-	557	-	557
Total financial assets measured at fair value	1,190	5,201	-	6,391
Financial liabilities measured at fair value				
Deposits and other borrowings at fair value	-	555	-	555
Other financial liabilities at fair value through income statement	-	20	-	20
Derivative financial instruments	-	278	-	278
Debt issues at fair value	-	590	-	590
Due to related entities	-	403	-	403
Total financial liabilities measured at fair value	-	1,846	-	1,846

Notes to the financial statements

Note 10 Fair value of financial assets and financial liabilities (continued)

	THE BANKING GROUP			
	31 Mar 17 Unaudited			
$ millions	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value				
Trading securities	593	1,115	-	1,708
Derivative financial instruments	-	63	-	63
Available-for-sale securities	1,573	2,245	-	3,818
Due from related entities	-	622	-	622
Total financial assets measured at fair value	2,166	4,045	-	6,211
Financial liabilities measured at fair value				
Deposits and other borrowings at fair value	-	1,617	-	1,617
Other financial liabilities at fair value through income statement	-	10	-	10
Derivative financial instruments	-	799	-	799
Debt issues at fair value	-	2,398	-	2,398
Due to related entities	-	917	-	917
Total financial liabilities measured at fair value	-	5,741	-	5,741

	THE BANKING GROUP			
	30 Sep 17 Audited			
$ millions	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets measured at fair value				
Trading securities	20	1,777	-	1,797
Derivative financial instruments	-	220	-	220
Available-for-sale securities	1,556	2,531	-	4,087
Due from related entities	-	587	-	587
Total financial assets measured at fair value	1,576	5,115	-	6,691
Financial liabilities measured at fair value				
Deposits and other borrowings at fair value	-	593	-	593
Other financial liabilities at fair value through income statement	-	19	-	19
Derivative financial instruments	-	484	-	484
Debt issues at fair value	-	1,642	-	1,642
Due to related entities	-	355	-	355
Total financial liabilities measured at fair value	-	3,093	-	3,093

Analysis of movements between fair value hierarchy levels

During the period, there were no material transfers between levels of the fair value hierarchy (31 March 2017: no material transfers between levels, 30 September 2017: no material transfers between levels).

Notes to the financial statements

Note 10 Fair value of financial assets and financial liabilities (continued)

Financial instruments not measured at fair value

The following table summarises the estimated fair value of the Banking Group's financial instruments not measured at fair value:

	THE BANKING GROUP					
	31 Mar 18 (Unaudited)		31 Mar 17 (Unaudited)		30 Sep 17 (Unaudited)	
$ millions	**Carrying Amount**	**Fair Value**	Carrying Amount	Fair Value	Carrying Amount	Fair Value
Financial assets not measured at fair value						
Cash and balances with central banks	**1,974**	**1,974**	1,495	1,495	1,659	1,659
Receivables due from other financial institutions	**523**	**523**	753	753	407	407
Other assets	**242**	**242**	177	177	221	221
Loans	**79,113**	**79,189**	76,542	76,558	77,261	77,292
Due from related entities	**1,059**	**1,059**	727	727	1,430	1,430
Total financial assets not measured at fair value	**82,911**	**82,987**	79,694	79,710	80,978	81,009
Financial liabilities not measured at fair value						
Payables due to other financial institutions	**294**	**294**	410	410	143	143
Other liabilities	**403**	**403**	358	358	423	423
Deposits and other borrowings	**61,628**	**61,666**	56,812	56,850	58,405	58,450
Debt issues	**14,380**	**14,522**	13,405	13,554	15,087	15,259
Due to related entities	**1,630**	**1,640**	2,149	2,167	1,771	1,786
Loan capital	**2,592**	**2,677**	1,138	1,187	2,616	2,688
Total financial liabilities not measured at fair value	**80,927**	**81,202**	74,272	74,526	78,445	78,749

A detailed description of how fair value is derived for financial instruments not measured at fair value is disclosed in Note 26 of the financial statements included in the Disclosure Statement for the year ended 30 September 2017.

Note 11 Credit related commitments, contingent assets and contingent liabilities

	THE BANKING GROUP		
$ millions	**31 Mar 18 Unaudited**	31 Mar 17 Unaudited	30 Sep 17 Audited
Letters of credit and guarantees	**795**	764	772
Commitments to extend credit	**25,049**	24,626	25,081
Other	**10**	25	10
Total undrawn credit commitments	**25,854**	25,415	25,863

Contingent assets

The credit commitments shown in the table above also constitute contingent assets. These commitments would be classified as loans on the balance sheet on the contingent event occurring.

Contingent liabilities

The Banking Group has contingent liabilities in respect of actual and potential claims and proceedings. An assessment of the Banking Group's likely loss in respect of these matters has been made on a case-by-case basis and provision has been made in these financial statements where appropriate.

Additional information relating to any provision or contingent liability has not been provided where disclosure of such information might be expected to seriously prejudice the position of the Banking Group.

Notes to the financial statements

Note 12 Segment reporting

The Banking Group operates predominantly in the consumer banking and wealth, commercial, corporate and institutional banking, and investments and insurance sectors within New Zealand. On this basis, no geographical segment reporting is provided.

The operating segment results have been presented on a management reporting basis and consequently internal charges and transfer pricing adjustments have been reflected in the performance of each operating segment. Intersegment pricing is determined on a cost recovery basis.

The Banking Group does not rely on any single major customer for its revenue base.

Comparative information for the six months ended 31 March 2017 and the year ended 30 September 2017 has been restated following changes to the allocation of certain costs and as a result of the Ultimate Parent Bank updating its capital allocation framework. Comparative information has been restated to ensure consistent presentation with the current reporting period. The revised presentation has no impact on total profit before income tax for the six months ended 31 March 2017 or the year ended 30 September 2017.

The Banking Group's operating segments are defined by the customers they serve and the services they provide. The Banking Group has identified the following main operating segments:

- Consumer Banking and Wealth provides financial services predominantly for individuals;
- Commercial, Corporate and Institutional Banking provides a broad range of financial services for commercial, corporate, property finance, agricultural, institutional and government customers; and
- Investments and Insurance provides funds management and insurance services.

Reconciling items primarily represent:

- business units that do not meet the definition of operating segments under NZ IFRS 8 *Operating Segments* ('**NZ IFRS**' refers to applicable New Zealand equivalents to International Financial Reporting Standards);
- elimination entries on consolidation of the results, assets and liabilities of the Banking Group's controlled entities in the preparation of the consolidated financial statements of the Banking Group;
- results of certain entities included for management reporting purposes, but excluded from the consolidated financial statements of the Banking Group for statutory financial reporting purposes; and
- results of certain business units excluded for management reporting purposes, but included within the consolidated financial statements of the Banking Group for statutory financial reporting purposes.

	THE BANKING GROUP				
$ millions	**Consumer Banking and Wealth**	**Commercial, Corporate and Institutional**	**Investments and Insurance**	**Reconciling Items**	**Total**
Six months ended 31 March 2018 (Unaudited)					
Net interest income	**567**	**344**	**-**	**(6)**	**905**
Non-interest income	**96**	**76**	**69**	**(46)**	**195**
Net operating income before operating expenses and impairment charges	**663**	**420**	**69**	**(52)**	**1,100**
Operating expenses	**(342)**	**(110)**	**(15)**	**7**	**(460)**
Impairment (charges)/benefits	**(28)**	**1**	**-**	**-**	**(27)**
Profit before income tax	**293**	**311**	**54**	**(45)**	**613**
Total gross loans	**45,735**	**33,737**	**-**	**17**	**79,489**
Total deposits and other borrowings	**35,259**	**26,369**	**-**	**555**	**62,183**
Six months ended 31 March 2017 (Unaudited)					
Net interest income	508	336	1	(10)	835
Non-interest income	118	77	61	(68)	188
Net operating income before operating expenses and impairment charges	626	413	62	(78)	1,023
Operating expenses	(366)	(111)	(14)	26	(465)
Impairment (charges)/benefits	(20)	56	-	-	36
Profit before income tax	240	358	48	(52)	594
Total gross loans	43,824	33,067	-	49	76,940
Total deposits and other borrowings	33,670	23,142	-	1,617	58,429
Year ended 30 September 2017 (Unaudited)					
Net interest income	1,053	683	1	4	1,741
Non-interest income	219	153	131	(98)	405
Net operating income before operating expenses and impairment charges	1,272	836	132	(94)	2,146
Operating expenses	(708)	(221)	(29)	4	(954)
Impairment (charges)/benefits	(34)	97	-	13	76
Profit before income tax	530	712	103	(77)	1,268
Total gross loans	44,707	32,870	-	34	77,611
Total deposits and other borrowings	34,044	24,361	-	593	58,998

Notes to the financial statements

Note 13 Insurance business

The Banking Group does not conduct any insurance business (as that term is defined in the Order).

Note 14 Capital adequacy

The information contained in this note has been derived in accordance with the Bank's conditions of registration which relate to capital adequacy and the Reserve Bank of New Zealand ('**Reserve Bank**') Capital Adequacy Framework (Internal Models Based Approach) ('**BS2B**'), except for the matters of non-compliance with condition of registration 1B disclosed on page 31. The Bank considers its internal credit model methodologies result in the retention of an appropriate amount of capital to reflect its credit risk and any effect of the non-compliance with its conditions of registration 1B on the information relating to capital adequacy is not considered by the Bank to be material.

The Banking Group maintains an actively managed capital base to cover risks inherent in the business. The adequacy of the Banking Group's capital is monitored using, among other measures, the rules and ratios established by the Basel Committee on Banking Supervision ('**BCBS**') and adopted by the Reserve Bank in supervising the Banking Group.

The Banking Group's capital summary (Unaudited)

	THE BANKING GROUP
$ millions	**31 Mar 18**
Tier 1 capital	
Common Equity Tier 1 capital	
Paid-up ordinary shares issued by the Bank plus related share premium	**5,100**
Retained earnings (net of appropriations)	**2,255**
Accumulated other comprehensive income and other disclosed reserves[1]	**(50)**
Less deductions from Common Equity Tier 1 capital	
Goodwill	**(477)**
Other intangible assets[2]	**(156)**
Cash flow hedge reserve	**60**
Deferred tax asset deduction	**(167)**
Expected loss excess over eligible allowance	**(222)**
Total Common Equity Tier 1 capital	**6,343**
Additional Tier 1 capital	
Additional Tier 1 capital instruments[3]	**1,500**
Total additional Tier 1 capital	**1,500**
Total Tier 1 capital	**7,843**
Tier 2 capital	
Tier 2 capital instruments[3]	**1,106**
Revaluation reserves	**-**
Eligible impairment allowance in excess of expected loss	**-**
Total Tier 2 capital	**1,106**
Total capital	**8,949**

[1] Accumulated other comprehensive income and other disclosed reserves consist of available-for-sale securities reserve and cash flow hedge reserve as disclosed as reserves on the balance sheet.
[2] Includes capitalised transaction costs on loan capital and debt issues.
[3] Excludes capitalised transaction costs.

Capital structure

Ordinary shares

In accordance with BS2B, ordinary share capital is classified as Common Equity Tier 1 capital.

The ordinary shares have no par value. Subject to the constitution of the Bank, each ordinary share of the Bank carries the right to one vote on a poll at meetings of shareholders, the right to an equal share in dividends authorised by the Board and the right to an equal share in the distribution of the surplus assets of the Bank in the event of liquidation.

Note 14 Capital adequacy (continued)

Additional Tier 1 loan capital

A summary of the key terms and features of the Additional Tier 1 loan capital ('**AT1 notes**') is provided below:

$	Issue date	Counterparty	Interest rate	Optional redemption date
NZ$1,500 million notes [1]	22 September 2017	NZ Branch	NZ 90 day bank bill rate + 3.9594% p.a.	21 September 2027 and every fifth anniversary thereafter

[1] The AT1 notes rank equally amongst themselves and are subordinated to the claims of depositors and senior or less subordinated creditors of the Bank.

Interest payable

Quarterly interest payments on the AT1 notes are at the absolute discretion of the Bank and will only be paid if the payment conditions are satisfied, including that the interest payment will not result in the Bank becoming insolvent immediately following the interest payment; not result in a breach of the Reserve Bank Prudential Standards; and the payment date not falling on the date of a capital trigger event or non-viability trigger event. Interest payments are non-cumulative. If interest is not paid in full, the Bank may not determine or pay any dividends on its ordinary shares or undertake a discretionary buy back or capital reduction of the Bank's ordinary shares (except in limited circumstances).

Redemption

The Bank may elect to redeem all or some of the AT1 notes for their face value on 21 September 2027 and every fifth anniversary thereafter, subject to the Reserve Bank's prior written approval. Early redemption of all of the AT1 notes for certain tax or regulatory reasons is permitted subject to the Reserve Bank's prior written approval.

Conversion

If a capital trigger event or non-viability trigger event occurs, the Bank must convert some or all of the AT1 notes into a variable number of ordinary shares issued by the Bank (calculated with reference to the net assets of the Bank and the total number of ordinary shares on issue at the conversion date) that is sufficient, in the case of a capital trigger event, to return the Bank's Common Equity Tier 1 capital ratio to above 5.125% as determined by the Bank in consultation with the Reserve Bank; or, in the case of a non-viability trigger event, to satisfy the direction of the Reserve Bank or the decision of the statutory manager of the Bank. A capital trigger event occurs when the Bank determines, or the Reserve Bank notifies in writing that it believes, the Bank's Common Equity Tier 1 Capital ratio is equal to or less than 5.125%. A non-viability trigger event occurs when the Reserve Bank or the statutory manager (appointed pursuant to section 117 of the Reserve Bank Act) directs the Bank to convert or write off all or some of its AT1 notes.

If conversion of the AT1 notes does not occur within five business days of a capital trigger event or a non-viability trigger event, holders' rights in relation to the AT1 notes will be immediately and irrevocably terminated.

The Bank is able to elect to convert all the AT1 notes for certain tax or regulatory reasons (or in certain other circumstances).

Tier 2 loan capital

A summary of the key terms and features of the Tier 2 loan capital ('**Tier 2 notes**') is provided below.

$	Issue date	Counterparty	Interest rate	Maturity Date	Optional redemption date
AU$1,040 million notes [1]	8 September 2015	London Branch of the Ultimate Parent Bank	Australian 90 day bank bill rate + 2.87% p.a.	22 March 2026	22 March 2021 and every interest payment date thereafter

[1] The Tier 2 notes rank equally amongst themselves and are subordinated to the claims of depositors and senior or less subordinated creditors of the Bank.

Interest payable

Interest payments on the Tier 2 notes are subject to the Bank being solvent at the time of, and immediately following the interest payment.

Early redemption

The Bank may elect to redeem all or some of the Tier 2 notes for their face value together with accrued interest (if any) on 22 March 2021 or any interest payment date thereafter, subject to the Reserve Bank's prior written approval. Early redemption of all of the Tier 2 notes for certain tax or regulatory reasons is permitted on an interest payment date subject to the Reserve Bank's prior written approval.

Conversion

If a non-viability trigger event occurs, the Bank must convert such number of the Tier 2 notes into a variable number of ordinary shares issued by the Bank (calculated with reference to the net assets of the Bank and the total number of ordinary shares on issue on the conversion date) that is sufficient to satisfy the direction of the Reserve Bank or the decision of the statutory manager. A non-viability trigger event occurs when the Reserve Bank or the statutory manager (appointed pursuant to section 117 of the Reserve Bank Act) directs the Bank to convert or write off all or some of its Tier 2 notes. If conversion of the Tier 2 notes fails to take effect within five business days, holders' rights in relation to the Tier 2 notes will be immediately and irrevocably terminated.

Note 14 Capital adequacy (continued)

Reserves

Available-for-sale securities reserve

This comprises the changes in the fair value of available-for-sale financial securities, net of tax. These changes are transferred to non-interest income in the income statement when the asset is either disposed of or impaired.

Cash flow hedge reserve

This comprises the fair value gains and losses associated with the effective portion of designated cash flow hedging instruments, net of tax.

Capital ratios (Unaudited)

The Basel banking accords (the '**Accords**') have been developed and strengthened over time by the BCBS to enhance the banking regulatory framework. The Accords are made up of the different Basel frameworks with the latest being Basel III. Basel III builds on the Basel I and Basel II frameworks, and seeks to improve the banking sector's ability to deal with financial and economic stress, improve risk management and strengthen banks' transparency. The Basel III framework is built on three mutually reinforcing pillars. Pillar 1 sets out the mechanics for minimum capital adequacy requirements for credit, market and operational risks. Pillar 2 relates to the internal assessment of capital adequacy and the supervisory review process. Pillar 3 deals with market disclosure and market discipline.

For the purposes of calculating the capital adequacy ratios for the Bank on a solo basis, wholly-owned and wholly-funded subsidiaries of the Banking Group are consolidated with the Bank. In this context, wholly-funded by the Bank means there are no liabilities (including off-balance sheet obligations) to anyone other than the Bank, the Inland Revenue or trade creditors, where aggregate exposure to trade creditors does not exceed 5% of the subsidiary's shareholders' equity. Wholly-owned by the Bank means that all equity issued by the subsidiary is held by the Bank or is ultimately owned by the Bank through a chain of ownership where each entity is 100% owned by its parent.

The table below is disclosed under the Reserve Bank's Basel III framework in accordance with Clause 15 of Schedule 11 to the Order and represents the capital adequacy calculation based on BS2B.

	THE BANKING GROUP			THE BANK	
%	Reserve Bank Minimum Ratios[1]	31 Mar 18	31 Mar 17	31 Mar 18	31 Mar 17
Common Equity Tier 1 capital ratio	6.5	**11.8**	10.7	**9.4**	8.5
Tier 1 capital ratio	8.0	**14.6**	10.7	**11.6**	8.5
Total capital ratio	10.0	**16.6**	12.8	**13.3**	10.2
Buffer ratio	2.5	**5.3**	4.7	**N/A**	N/A

[1] Changes to the Bank's conditions of registration, effective from 31 December 2017, have increased the Common Equity Tier 1 capital ratio, Tier 1 capital ratio and Total capital ratio ('**minimum capital ratios**') by 2% compared to the minimum capital ratios as at 30 September 2017. The increased minimum capital ratios will remain in place until the Bank has satisfied the Reserve Bank that all existing issues in relation to the matters of non-compliance on page 31 have been resolved.

Banking Group Pillar 1 total capital requirement (Unaudited)

	THE BANKING GROUP		
	31 Mar 18		
$ millions	Total Exposure After Credit Risk Mitigation	Risk-weighted Exposure or Implied Risk-weighted Exposure	Total Capital Requirement
Credit risk			
Exposures subject to the internal ratings based approach	**101,520**	**40,242**	**3,219**
Equity exposures	**-**	**-**	**-**
Specialised lending subject to the slotting approach	**7,758**	**7,113**	**569**
Exposures subject to the standardised approach	**2,815**	**1,045**	**84**
Total credit risk (scaled)[1]	**112,093**	**48,400**	**3,872**
Operational risk	**N/A**	**4,514**	**361**
Market risk	**N/A**	**924**	**74**
Supervisory adjustment	**N/A**	**-**	**-**
Total	**112,093**	**53,838**	**4,307**

[1] The value of the scalar used in determining the credit risk weighted exposure is 1.06 as required by the conditions of registration.

Note 14 Capital adequacy (continued)

Capital for other material risks (Unaudited)

The Banking Group's internal capital adequacy assessment process identifies, reviews and measures additional material risks that must be captured within the Banking Group's capital adequacy assessment process. The additional material risks considered are those not captured by Pillar 1 regulatory capital requirements and include compliance risk, conduct risk, liquidity risk, reputational risk, environmental, social and governance risk, business/strategic risk, other assets risk, model risk, deferred acquisition cost risk and subsidiary risk.

The Banking Group's internal capital allocation for 'other material risks' is $246 million as at 31 March 2018 (31 March 2017: $83 million).

Ultimate Parent Bank Group Basel III capital adequacy ratios (unaudited)

The table below represents the capital adequacy calculation for the Ultimate Parent Bank and the Ultimate Parent Bank Group based on Australian Prudential Regulation Authority's ('**APRA**') application of the Basel III capital adequacy framework.

%	31 Mar 18	31 Mar 17
Ultimate Parent Bank Group (excluding entities specifically excluded by APRA regulations)[1, 2]		
Common Equity Tier 1 capital ratio	**10.5**	10.0
Additional Tier 1 capital ratio	**2.3**	1.7
Tier 1 capital ratio	**12.8**	11.7
Tier 2 capital ratio	**2.0**	2.3
Total regulatory capital ratio	**14.8**	14.0
Ultimate Parent Bank (Extended Licensed Entity)[1, 3]		
Common Equity Tier 1 capital ratio	**10.4**	10.2
Additional Tier 1 capital ratio	**2.4**	1.8
Tier 1 capital ratio	**12.8**	12.0
Tier 2 capital ratio	**2.1**	2.6
Total regulatory capital ratio	**14.9**	14.6

[1] The capital ratios represent information mandated by APRA. The capital ratios of the Ultimate Parent Bank Group are publicly available in the Ultimate Parent Bank Group's Pillar 3 report. This information is made available to users via the Ultimate Parent Bank's website (www.westpac.com.au).
[2] Ultimate Parent Bank Group (excluding entities specifically excluded by APRA regulations) comprises the consolidation of the Ultimate Parent Bank and its subsidiary entities except those entities specifically excluded by APRA regulations for the purposes of measuring capital adequacy (Level 2). The head of the Level 2 group is the Ultimate Parent Bank.
[3] Ultimate Parent Bank (Extended Licensed Entity) comprises the Ultimate Parent Bank and its subsidiary entities that have been approved by APRA as being part of a single Extended Licensed Entity for the purposes of measuring capital adequacy (Level 1).

Under APRA's Prudential Standards, Australian authorised deposit-taking institutions ('**ADI**'), including the Ultimate Parent Bank Group are required to maintain minimum ratios of capital to risk weighted assets ('**RWA**'), as determined by APRA. For the calculation of RWAs, the Ultimate Parent Bank Group is accredited by APRA to apply advanced models permitted by the Basel III global capital adequacy regime. The Ultimate Parent Bank Group uses the Advanced Internal Ratings Based ('**Advanced IRB**') approach for credit risk, the Advanced Measurement Approach ('**AMA**') for operational risk and the internal model approach for interest rate risk in the banking book for calculating regulatory capital.

APRA's prudential standards are generally consistent with the International Regulatory Framework for Banks, also known as Basel III, issued by the BCBS, except where APRA has exercised certain discretions.

The Ultimate Parent Bank Group is required to disclose additional detailed information on its risk management practices and capital adequacy on a quarterly basis. This information is made available to users via the Ultimate Parent Bank's website (www.westpac.com.au).

The Ultimate Parent Bank Group (excluding entities specifically excluded by APRA regulations), and the Ultimate Parent Bank (Extended Licensed Entity as defined by APRA), exceeded the minimum capital adequacy requirements as specified by APRA as at 31 March 2018.

Notes to the financial statements

Note 15 Risk management

15.1 Credit risk

Credit risk mitigation

The Banking Group uses a variety of techniques to reduce the credit risk arising from its lending activities (refer to Note 35.2 to the financial statements included in the Disclosure Statement for the year ended 30 September 2017 for further details). This includes the Banking Group establishing that it has direct, irrevocable and unconditional recourse to collateral and other credit enhancements through obtaining legally enforceable documentation.

The Banking Group includes the effect of credit risk mitigation through eligible guarantees within the calculation applied to Loss Given Default ('**LGD**'). The value of the guarantee is not always separately recorded, and therefore, not available for disclosure, under Clause 7 of Schedule 11 to the Order.

Definitions of PD, LGD and EAD

i. **Probability of Default ('PD')**
The PD is a through-the-cycle assessment of the likelihood of a customer defaulting on its financial obligations within one year.

ii. **LGD**
The LGD represents an estimate of the expected severity of a loss to the Banking Group should a customer default occur during an economic downturn.

iii. **Exposure at Default ('EAD')**
EAD represents an estimate of the amount of committed exposure expected to be drawn by the customer at the time of default.

Credit risk exposures by asset class

The Banking Group's credit risk exposures by asset class as at 31 March 2018 (Unaudited)

Exposure-weighted PD Grade (%)	Weighted Average PD %	EAD $ millions	Exposure-weighted LGD %	Exposure-weighted Risk Weight %	Risk-weighted Assets[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Residential mortgages						
0.00 to 0.10	-	-	-	-	-	-
0.10 to 0.25	**0.18**	**2,729**	**19.10**	**7.29**	**211**	**17**
0.25 to 1.0	**0.49**	**26,603**	**20.72**	**17.00**	**4,794**	**384**
1.0 to 2.5	**1.42**	**21,883**	**20.09**	**34.12**	**7,915**	**633**
2.5 to 10.0	**4.46**	**3,796**	**22.30**	**74.31**	**2,990**	**239**
10.0 to 99.99	-	-	-	-	-	-
Default	**100.00**	**263**	**22.21**	**212.35**	**592**	**47**
Total	**1.59**	**55,274**	**20.51**	**28.17**	**16,502**	**1,320**
Other retail						
0.00 to 0.10	-	-	-	-	-	-
0.10 to 0.25	**0.14**	**559**	**40.64**	**12.83**	**76**	**6**
0.25 to 1.0	**0.36**	**1,519**	**62.94**	**37.45**	**603**	**48**
1.0 to 2.5	**2.22**	**1,353**	**68.48**	**89.74**	**1,287**	**103**
2.5 to 10.0	**5.48**	**347**	**84.47**	**126.69**	**466**	**37**
10.0 to 99.99	**20.72**	**240**	**70.60**	**147.01**	**374**	**30**
Default	**100.00**	**21**	**72.42**	**103.32**	**23**	**2**
Total	**3.12**	**4,039**	**64.06**	**66.08**	**2,829**	**226**
Small business						
0.00 to 0.10	**0.03**	**147**	**73.76**	**7.06**	**11**	**1**
0.10 to 0.25	-	-	-	-	-	-
0.25 to 1.0	**0.30**	**621**	**21.45**	**17.62**	**116**	**9**
1.0 to 2.5	**1.84**	**1,487**	**20.92**	**26.58**	**419**	**34**
2.5 to 10.0	**4.76**	**301**	**19.74**	**29.15**	**93**	**7**
10.0 to 99.99	**15.65**	**32**	**21.95**	**44.22**	**15**	**1**
Default	**100.00**	**39**	**21.72**	**229.80**	**95**	**8**
Total	**3.34**	**2,627**	**23.89**	**26.90**	**749**	**60**

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

Notes to the financial statements

Note 15 Risk management (continued)

Exposure-weighted PD Grade (%)	Weighted Average PD %	EAD $ millions	Exposure-weighted LGD %	Exposure-weighted Risk Weight %	Risk-weighted Assets[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Corporate/Business lending						
0.00 to 0.02	-	-	-	-	-	-
0.02 to 0.04	**0.03**	**2,686**	**35.04**	**11.06**	**315**	**25**
0.04 to 0.10	**0.08**	**4,121**	**53.25**	**29.62**	**1,294**	**104**
0.10 to 0.50	**0.21**	**8,455**	**43.76**	**39.67**	**3,555**	**284**
0.50 to 3.0	**1.56**	**13,349**	**35.28**	**72.79**	**10,300**	**824**
3.0 to 10.0	**3.70**	**780**	**34.74**	**100.15**	**828**	**66**
10.0 to 99.0	**24.82**	**1,414**	**39.17**	**192.68**	**2,888**	**231**
Default	**100.00**	**132**	**42.62**	**213.69**	**299**	**24**
Total	**2.40**	**30,937**	**40.17**	**59.40**	**19,479**	**1,558**
Sovereign						
0.00 to 0.02	**0.01**	**1,432**	**16.25**	**2.24**	**34**	**3**
0.02 to 0.04	**0.02**	**3,173**	**9.14**	**1.46**	**49**	**4**
0.04 to 0.10	**0.05**	**5**	**25.00**	-	-	-
0.10 to 0.50	-	-	-	-	-	-
0.50 to 3.0	-	-	-	-	-	-
3.0 to 10.0	-	-	-	-	-	-
10.0 to 99.0	-	-	-	-	-	-
Default	-	-	-	-	-	-
Total	**0.01**	**4,610**	**11.37**	**1.70**	**83**	**7**
Bank						
0.00 to 0.02	-	-	-	-	-	-
0.02 to 0.04	**0.03**	**1,717**	**15.45**	**3.96**	**72**	**6**
0.04 to 0.10	**0.05**	**2,266**	**54.83**	**21.19**	**509**	**41**
0.10 to 0.50	**0.13**	**43**	**60.00**	**28.52**	**13**	**1**
0.50 to 3.0	**1.22**	**5**	**56.90**	**94.34**	**5**	-
3.0 to 10.0	**3.70**	**2**	**10.00**	**47.17**	**1**	-
10.0 to 99.0	-	-	-	-	-	-
Default	-	-	-	-	-	-
Total	**0.05**	**4,033**	**38.10**	**14.04**	**600**	**48**
Total credit risk exposures subject to the internal ratings based approach		**101,520**			**40,242**	**3,219**

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

The following table summarises the Banking Group's credit risk exposures by asset class arising from undrawn commitments and other off-balance sheet exposures. These unaudited amounts are included in the previous tables.

	Undrawn Commitments and Other Off-balance Sheet Amounts		Market Related Contracts	
$ millions	**Value**	**EAD**	**Value**	**EAD**
Residential mortgages	**9,933**	**7,463**	-	-
Other retail	**3,222**	**1,879**	-	-
Small business	**858**	**768**	-	-
Corporate/Business lending	**9,616**	**9,700**	-	-
Sovereign	**220**	**211**	-	-
Bank	**811**	**851**	-	-
Total	**24,660**	**20,872**	-	-

Note 15 Risk management (continued)

The Banking Group's equity exposures as at 31 March 2018 (Unaudited)

Equity	Total Exposure $ millions	Risk Weight %	Risk-weighted Exposure[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Equity holdings (not deducted from capital) that are not publicly traded	-	300	-	-
All other holdings (not deducted from capital)	-	400	-	-

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

The Banking Group's specialised lending: Project and property finance credit risk exposures as at 31 March 2018 (Unaudited)

Supervisory slotting grade	Total Exposures After Credit Risk Mitigation $ millions	Risk Weight %	Risk-weighted Assets[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Strong	2,979	70.00	2,212	177
Good	3,823	90.00	3,647	292
Satisfactory	719	115.00	876	70
Weak	143	250.00	378	30
Default	94	-	-	-
Total	7,758	86.50	7,113	569

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

The following table summarises the Banking Group's specialised lending: Project and property finance credit risk exposures arising from undrawn commitments and other off-balance sheet exposures. These amounts are included in the above table.

	EAD $ millions	Average Risk Weight %	Risk-weighted Assets[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Undrawn commitments and other off-balance sheet exposures	1,200	88.13	1,121	90

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

The Banking Group's credit risk exposures subject to the standardised approach as at 31 March 2018 (Unaudited)
Calculation of on-balance sheet exposures

	Total Exposure After Credit Risk Mitigation $ millions	Average Risk Weight %	Risk-weighted Exposure[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Other assets[2]	1,846	34.60	677	54
Total on-balance sheet exposures	1,846		677	54

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.
[2] Other assets relate to property and equipment, other assets and related parties.

Notes to the financial statements

Note 15 Risk management (continued)

Calculation of off-balance sheet exposures

	Total Exposure or Principal Amount $ millions	Average Credit Conversion Factor %	Credit Equivalent Amount $ millions	Average Risk Weight %	Risk-weighted Exposure[1] $ millions	Minimum Pillar 1 Capital Requirement $ millions
Market related contracts subject to the standardised approach						
Foreign exchange contracts	15,833	N/A	903	20.00	191	16
Interest rate contracts	51,295	N/A	66	20.00	14	1
Credit value adjustment	-	N/A	-	-	163	13
Total market related contracts subject to the standardised approach	67,128		969		368	30
Standardised subtotal (on and off-balance sheet)			2,815		1,045	84

[1] The value of the scalar used in determining the risk weighted assets is 1.06 as required by the conditions of registration.

Residential mortgages by loan-to-value ratio ('LVR') as at 31 March 2018 (Unaudited)

LVRs are calculated as the current exposure divided by the Banking Group's valuation of the residential security at origination.

For loans originated from 1 January 2008, the Banking Group utilises data from its loan system. For loans originated prior to 1 January 2008, the origination valuation is not separately recorded and is therefore not available for disclosure. For these loans, the Banking Group utilises its dynamic LVR process to estimate an origination valuation.

Exposures for which no LVR is available have been included in the 'Exceeds 90%' category in accordance with the requirements of the Order.

	THE BANKING GROUP					
	31 Mar 18					
LVR range $ millions	Does not exceed 60%	Exceeds 60% and not 70%	Exceeds 70% and not 80%	Exceeds 80% and not 90%	Exceeds 90%	Total
On-balance sheet exposures	19,828	11,465	11,956	2,846	1,631	47,726
Undrawn commitments and other off-balance sheet exposures	5,039	1,223	898	119	184	7,463
Value of exposures	24,867	12,688	12,854	2,965	1,815	55,189

Reconciliation of residential mortgage-related amounts (Unaudited)

The table below provides the Banking Group's reconciliation between any amounts disclosed in this Disclosure Statement that relate to mortgages on residential property.

	THE BANKING GROUP
$ millions	31 Mar 18
Term loans - Housing (as disclosed in Note 4) and Residential mortgages - total gross loans (as disclosed in Note 5)	47,909
Reconciling items:	
Unamortised deferred fees and expenses	(166)
Fair value hedge adjustments	(17)
Value of undrawn commitments and other off-balance sheet amounts relating to residential mortgages	9,933
Undrawn at default[1]	(2,470)
Residential mortgages by LVR	55,189
Accrued interest receivable	85
Residential mortgages - EAD (as disclosed in Credit risk exposures by asset class)	55,274

[1] Estimate of the amount of committed exposure not expected to be drawn by the customer at the time of default.

Note 15 Risk management (continued)

15.2 Operational risk

Operational risk capital requirement (Unaudited)

	THE BANKING GROUP	
	31 Mar 18	
$ millions	Implied Risk-weighted Exposure	Total Operational Risk Capital Requirement
Methodology implemented Advanced Measurement Approach		
Operational risk	**4,514**	**361**

15.3 Liquidity risk

Liquid assets (Unaudited)

The table below shows the Banking Group's holding of liquid assets and represents the key liquidity information provided to management. Liquid assets include high quality assets readily convertible to cash to meet the Banking Group's liquidity requirements. In management's opinion, liquidity is sufficient to meet the Banking Group's present requirements.

	THE BANKING GROUP
$ millions	31 Mar 18
Cash and balances with central banks	**1,974**
Receivables due from other financial institutions	**344**
Receivables due from the Ultimate Parent Bank	**427**
Supranational securities	**1,458**
NZ Government securities	**1,574**
NZ public securities	**1,301**
NZ corporate securities	**1,432**
Residential mortgage-backed securities	**3,950**
Total liquid assets	**12,460**

Regulatory Liquidity Ratios (Unaudited)

The Bank calculates liquidity ratios in accordance with the Reserve Bank document entitled 'Liquidity Policy' (BS 13) ('**BS 13**'). Ratios are calculated daily and are part of the Bank's management of liquidity risk (refer to Note 35.4 to the financial statements included in the Disclosure Statement for the year ended 30 September 2017 for further details). Quarterly, average ratios are produced in line with Reserve Bank rules and guidance.

	THE BANKING GROUP	
%	31 Mar 18	31 Dec 17
Average for the three months ended		
One-week mismatch ratio	**5.72**	5.92
One-month mismatch ratio	**9.35**	9.71
Core funding ratio	**83.53**	84.27

Contractual maturity of financial liabilities (Unaudited)

The table below presents cash flows associated with financial liabilities, payable at the balance sheet date, by remaining contractual maturity. The amounts disclosed in the table are the future contractual undiscounted cash flows, whereas the Banking Group manages inherent liquidity risk based on expected cash flows.

Cash flows associated with financial liabilities include both principal payments as well as fixed or variable interest payments incorporated into the relevant coupon period. Principal payments reflect the earliest contractual maturity date. Derivative liabilities designated for hedging purposes are expected to be held for their remaining contractual lives, and reflect gross cash flows over the remaining contractual term.

Derivatives held for trading and certain liabilities classified in other financial liabilities at fair value through income statement are not managed for liquidity purposes on the basis of their contractual maturity, and accordingly these liabilities are presented in either the on demand or up to 1 month columns. Only the liabilities that the Banking Group manages based on their contractual maturity are presented on a contractual undiscounted basis in the following table.

Notes to the financial statements

Note 15 Risk management (continued)

$ millions	On Demand	Up to 1 Month	Over 1 Month and Up to 3 Months	Over 3 Months and Up to 1 Year	Over 1 Year and Up to 5 Years	Over 5 Years	Total
	THE BANKING GROUP						
Financial liabilities							
Payables due to other financial institutions	-	294	-	-	-	-	294
Other liabilities	-	88	-	-	-	-	88
Deposits and other borrowings	29,048	5,471	11,637	14,657	2,094	-	62,907
Other financial liabilities at fair value through income statement	-	20	-	-	-	-	20
Derivative financial instruments:							
Held for hedging purposes (net settled)	-	4	3	66	59	2	134
Held for hedging purposes (gross settled):							
Cash outflow	-	6	14	206	1,881	596	2,703
Cash inflow	-	-	-	(159)	(1,606)	(547)	(2,312)
Debt issues	-	10	412	1,725	12,708	995	15,850
Due to related entities:							
Non-derivative balances	616	116	243	29	769	-	1,773
Derivative financial instruments:							
Held for trading	14	-	-	-	-	-	14
Held for hedging purposes (net settled)	-	14	41	67	69	-	191
Held for hedging purposes (gross settled):							
Cash outflow	-	-	18	54	1,582	60	1,714
Cash inflow	-	-	(16)	(48)	(1,485)	(57)	(1,606)
Loan capital	-	-	14	40	229	2,779	3,062
Total undiscounted financial liabilities	29,678	6,023	12,366	16,637	16,300	3,828	84,832
Total contingent liabilities and commitments							
Letters of credit and guarantees	795	-	-	-	-	-	795
Commitments to extend credit	25,049	-	-	-	-	-	25,049
Other commitments	10	-	-	-	-	-	10
Total undiscounted contingent liabilities and commitments	25,854	-	-	-	-	-	25,854

15.4 Market risk

Market risk notional capital charges (Unaudited)

The Banking Group's aggregate market risk exposure is derived in accordance with BS2B and is calculated on a six monthly basis. The end-of-period aggregate market risk exposure is calculated from the period end balance sheet information.

For each category of market risk, the Banking Group's peak end-of-day aggregate capital charge is derived by determining the maximum over the six months ended 31 March 2018 of the aggregate capital charge for that category of market risk at the close of each business day derived in accordance with BS2B.

Notes to the financial statements

Note 15 Risk management (continued)

The following table provides a summary of the Banking Group's notional capital charges by risk type as at the reporting date and the peak end-of-day notional capital charges by risk type for the six months ended 31 March 2018:

	THE BANKING GROUP	
	31 Mar 18	
$ millions	Implied Risk-weighted Exposure	Aggregate Capital Charge
End-of-period		
Interest rate risk	**924**	**74**
Foreign currency risk	**-**	**-**
Equity risk	**-**	**-**
	924	**74**
Peak end-of-day		
Interest rate risk	**1,314**	**105**
Foreign currency risk	**-**	**-**
Equity risk	**-**	**-**

Notes to the financial statements

Note 15 Risk management (continued)

Interest rate sensitivity (Unaudited)

The following table presents a breakdown of the earlier of the contractual repricing date or maturity date of the Banking Group's net asset position as at 31 March 2018. The Banking Group uses this contractual repricing information as a base, which is then altered to take account of consumer behaviour to manage its interest rate risk.

	THE BANKING GROUP						
$ millions	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	Total
Financial assets							
Cash and balances with central banks	1,750	-	-	-	-	224	1,974
Receivables due from other financial institutions	521	-	-	-	-	2	523
Other assets	-	-	-	-	-	242	242
Trading securities	1,554	286	7	-	-	-	1,847
Derivative financial instruments	-	-	-	-	-	432	432
Available-for-sale securities	-	-	1,406	761	1,388	-	3,555
Loans	43,093	5,313	11,044	14,454	5,585	(376)	79,113
Due from related entities	1,536	-	-	-	-	80	1,616
Total financial assets	48,454	5,599	12,457	15,215	6,973	604	89,302
Non-financial assets							988
Total assets							90,290
Financial liabilities							
Payables due to other financial institutions	294	-	-	-	-	-	294
Other liabilities	-	-	-	-	-	403	403
Deposits and other borrowings	40,065	8,227	6,058	1,320	644	5,869	62,183
Other financial liabilties at fair value through income statement	20	-	-	-	-	-	20
Derivative financial instruments	-	-	-	-	-	278	278
Debt issues	4,288	1,327	-	1,617	7,738	-	14,970
Due to related entities	1,673	10	-	23	26	301	2,033
Loan capital	2,592	-	-	-	-	-	2,592
Total financial liabilities	48,932	9,564	6,058	2,960	8,408	6,851	82,773
Non-financial liabilities							212
Total liabilities							82,985
On-balance sheet interest rate repricing gap	(478)	(3,965)	6,399	12,255	(1,435)		
Net derivative notional principals							
Net interest rate contracts (notional):							
Receivable/(payable)	13,890	(1,421)	(6,409)	(9,393)	3,333		
Net interest rate repricing gap	13,412	(5,386)	(10)	2,862	1,898		

Notes to the financial statements

Note 16 Concentration of funding

$ millions	THE BANKING GROUP 31 Mar 18 Unaudited
Funding consists of	
Payables due to other financial institutions	**294**
Deposits and other borrowings	**62,183**
Other financial liabilities at fair value through income statement	**20**
Debt issues[1]	**14,970**
Due to related entities[2]	**1,732**
Loan capital	**2,592**
Total funding	**81,791**
Analysis of funding by geographical areas[1]	
New Zealand	**64,553**
Australia	**1,247**
United Kingdom	**7,979**
United States of America	**1,073**
Other	**6,939**
Total funding	**81,791**
Analysis of funding by industry sector	
Accommodation, cafes and restaurants	**366**
Agriculture	**1,370**
Construction	**1,643**
Finance and insurance	**30,465**
Forestry and fishing	**188**
Government, administration and defence	**2,000**
Manufacturing	**1,602**
Mining	**72**
Property services and business services	**5,793**
Services	**4,310**
Trade	**1,787**
Transport and storage	**848**
Utilities	**556**
Households	**25,353**
Other	**3,706**
Subtotal	**80,059**
Due to related entities[2]	**1,732**
Total funding	**81,791**

[1] The geographic region used for debt issues is based on the nature of the debt programmes. The nature of the debt programmes is used as a proxy for the location of the original purchaser. Where the nature of the debt programme does not necessarily represent an appropriate proxy, the debt issues are classified as 'Other'. These instruments may have subsequently been on-sold.

[2] Amounts due to related entities, as presented above, are in respect of deposits and borrowings and exclude amounts which relate to derivatives and other liabilities.

Australian and New Zealand Standard Industrial Classification ('**ANZSIC**') has been used as the basis for disclosing industry sectors.

Note 17 Concentration of credit exposures

$ millions	THE BANKING GROUP 31 Mar 18 Unaudited
On-balance sheet credit exposures consists of	
Cash and balances with central banks	1,974
Receivables due from other financial institutions	523
Other assets	242
Trading securities	1,847
Derivative financial instruments	432
Available-for-sale securities	3,555
Loans	79,113
Due from related entities	1,616
Total on-balance sheet credit exposures	89,302
Analysis of on-balance sheet credit exposures by industry sector	
Accommodation, cafes and restaurants	407
Agriculture	8,166
Construction	507
Finance and insurance	6,117
Forestry and fishing	410
Government, administration and defence	5,528
Manufacturing	2,191
Mining	163
Property	6,556
Property services and business services	1,261
Services	1,790
Trade	1,858
Transport and storage	1,166
Utilities	1,903
Retail lending	49,958
Subtotal	87,981
Provisions for impairment charges on loans	(376)
Due from related entities	1,616
Other assets	81
Total on-balance sheet credit exposures	89,302
Off-balance sheet credit exposures consists of	
Credit risk-related instruments	25,854
Total off-balance sheet credit exposures	25,854
Analysis of off-balance sheet credit exposures by industry sector	
Accommodation, cafes and restaurants	100
Agriculture	544
Construction	645
Finance and insurance	1,715
Forestry and fishing	138
Government, administration and defence	743
Manufacturing	1,651
Mining	168
Property	1,555
Property services and business services	541
Services	685
Trade	2,012
Transport and storage	716
Utilities	1,471
Retail lending	13,170
Total off-balance sheet credit exposures	25,854

ANZSIC has been used as the basis for disclosing industry sectors.

Note 17 Concentration of credit exposures (continued)

Concentration of credit exposures to individual counterparties (Unaudited)

The following credit exposures are based on actual credit exposures to individual counterparties and groups of closely related counterparties.

The number of individual bank and non-bank counterparties to which the Banking Group has an aggregate credit exposure or peak end-of-day aggregate credit exposure that equals or exceeds 10% of the Banking Group's Common Equity Tier 1 capital (**'CET 1'**):

	THE BANKING GROUP	
	31 Mar 18	
% of Banking Group's CET 1	Bank Counterparties[1] Long-term credit rating A- or A3 and above	Non-bank Counterparties[2] Long-term credit rating A- or A3 and above
As at 31 March 2018[3]		
Exceeds 10% and not 15%	1	1
Exceeds 15% and not 20%	-	1
Exceeds 20% and not 25%	-	-
Exceeds 25% and not 30%	-	-
Peak end-of-day aggregate credit exposure for the three months ended 31 March 2018[3]		
Exceeds 10% and not 15%	1	1
Exceeds 15% and not 20%	-	-
Exceeds 20% and not 25%	-	-
Exceeds 25% and not 30%	-	1

[1] A counterparty is a bank counterparty if it is a bank that is not a member of the group of closely related counterparties or it is a group of closely related counterparties of which a bank is the parent.
[2] A counterparty is a non-bank counterparty if it is a non-bank that is not a member of a group of closely related counterparties or it is a group of closely related counterparties of which a bank is not the parent.
[3] There were no individual non-bank counterparties with aggregate credit exposure that equals or exceeds 10% of the Banking Group's equity and with a long-term credit rating of at least BBB- or Baa3, or its equivalent, and at most BBB+ or Baa1, or its equivalent.

The peak end-of-day aggregate credit exposure to each individual counterparty (which are not members of a group of closely related counterparties) or a group of closely related counterparties has been calculated by determining the maximum end-of-day aggregate amount of actual credit exposure over the relevant three month period and then dividing that amount by the Banking Group's equity as at the end of the period.

Credit exposures to individual counterparties (not being members of a group of closely related counterparties) and to groups of closely related counterparties exclude exposures to connected persons, to the central government or central bank of any country with a long-term credit rating of A- or A3 or above, or its equivalent, or to any supranational or quasi-sovereign agency with a long-term credit rating of A- or A3 or above, or its equivalent. These calculations relate only to exposures held in the financial records of the Banking Group and were calculated net of individually assessed provisions.

Conditions of registration

Non-compliance with conditions of registration

The Bank underwent a review of compliance with certain aspects of condition of registration 1B in response to a notice issued by the Reserve Bank under section 95 of the Reserve Bank Act during the reporting period ('**Section 95 Review**'). Condition of registration 1B requires the Bank to comply with the Reserve Bank Capital Adequacy Framework (Internal Models Based Approach) ('**BS2B**').

The Section 95 Review considered the Bank's compliance with aspects of BS2B since accreditation in 2008. It found that the Bank had not complied with aspects of BS2B over that period, and in particular it used a number of capital models not approved by the RBNZ and failed to meet requirements around model governance, process and documentation.

The Bank accepts the findings of the Section 95 Review and is committed to addressing the issues raised. As disclosed in Note 14 to the financial statements, the Bank considers its current internal credit model methodologies result in the retention of an appropriate amount of capital to reflect its credit risk. Any effect of the non-compliance with condition of registration 1B on the information relating to capital adequacy disclosed in the financial statements is not considered by the Bank to be material.

During the reporting period, the Bank was non-compliant with condition of registration 1B in relation to the following matters:

- It has continued to operate versions of the following capital models which were not approved by the Reserve Bank, in some cases since December 2008:
  - Probability of Default ('**PD**') models for small business and agriculture.
  - Loss Given Default ('**LGD**') and Exposure at Default ('**EAD**') models for credit card exposures.
  - PD and LGD models for:
    - Banks;
    - Sovereigns;
    - Corporates; and
    - SME Corporates.
  - Risk Grade model utilised within expert judgement evaluation for wholesale property development and investment customers.
  - For one obligor, the slotting rule utilised, applied within the Specialised Lending Income Producing Real Estate asset class, was not approved by the Reserve Bank.
- In some instances, changes to expert judgement policies, compositional changes and an asset class segmentation rule within the Bank's loan book were not notified to the Reserve Bank as required under paragraph 1.3A(a) of BS2B.
- The Bank's Model Compendium required under 1.3B of BS2B is not accurate as it does not include all models, has unapproved models and has not been updated to include changes in models.
- It is not fully compliant with paragraph 4.246 of BS2B in that, with the exception of wholesale property development and investment customers, non-retail risk grade credit policy overrides are not captured and monitored.
- It is not fully compliant with paragraph 4.248 of BS2B in that not all historical origination data for non-retail customers is maintained in a format that allows easy accessibility to key data used to derive the original risk rating.
- It is not fully compliant with 4.256 of BS2B in that WNZL management accountabilities and authorities are not specified in the relevant framework policies published by the Ultimate Parent Bank.
- For less than one percent of its residential mortgages by loan value, its use of total committed exposure rather than EAD for calculating loan-to-value ratio ('**LVR**') for capital adequacy purposes does not meet the minimum LGD requirements of paragraph 4.150 of BS2B. Additionally, for less than 5% of accounts by number, the security value utilised within the calculation of LVR is an updated valuation and not the origination value as required by that paragraph.
- For credit risk capital purposes, off-balance sheet exposures include amounts that have been approved but not yet drawn by the customer. The Bank has identified that, for some loans to commercial and corporate customers, amounts approved but not yet drawn are not accurately included in its capital estimates. The aggregate amount is not assessed to be material.
- The Banking Group has some minor portfolios where risk weights for these exposures are assessed for capital adequacy under a standardised approach rather than under BS2B without the Reserve Bank's approval.
- For a small number of corporate customers, certain committed credit facilities have been incorrectly recorded as uncommitted. This has been corrected and capital calculations adjusted accordingly. The aggregate amount is not assessed to be material.
- It is not fully compliant with 4.205 and 4.324 of BS2B in that the Bank has not risk-weighted the residual value of operating leases at 100%. This has been corrected and the capital calculations adjusted accordingly. The aggregate amount is not assessed to be material.
- It is not fully compliant with 4.93 of BS2B in that the Bank has not applied the appropriate facility maturity for drawn amounts for the lease portfolio (less than 0.4% of total exposure). The aggregate amount is not assessed to be material.

In addition to the non-compliance described above, the Section 95 Review noted that the Bank had failed to meet the Reserve Bank's requirements in relation to:

- model documentation and associated model documentation policies;
- internal processes for changes to the Bank's rating system;
- data maintenance; and
- policies or processes to support incorporating conservatism into models and estimates.

Changes to conditions of registration

On 19 December 2017, the Reserve Bank advised the Bank on changes to its conditions of registration to give effect to the Reserve Bank's further changes to the LVR restrictions, which ease those restrictions. These changes to the conditions of registration came into effect from 1 January 2018, being::

(a) a limit of 5 per cent on new lending carried out in the relevant measurement period for residential property investment applies where the LVR is greater than 65 per cent (previously, the required LVR was 60 per cent), and

(b) a limit of 15 percent (previously, the required limit was 10 per cent) on new non-residential property investment lending carried out in the measurement period where the LVR is greater than 80 per cent.

Independent auditor's review report

To the shareholder of Westpac New Zealand Limited

Report on the financial statements

We have reviewed pages 3 to 30 of the Disclosure Statement for the six months ended 31 March 2018 (the "Disclosure Statement") of Westpac New Zealand Limited (the "Bank") and the entities it controlled at 31 March 2018 or from time to time during the period (the "Banking Group"), which includes the 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. The financial statements comprise the balance sheet as at 31 March 2018, the income statement, the statement of comprehensive income, the statement of changes in equity and the statement of cash flows for the six months then ended, and the notes to the financial statements that include a statement of accounting policies and selected explanatory notes for the Banking Group.

Directors' responsibility for the financial statements

The Directors of the Bank (the "Directors") are responsible on behalf of the Bank for the preparation and presentation of the Disclosure Statement, which includes financial statements prepared in accordance with Clause 25 of the Order and for such internal controls as the Directors determine are necessary to enable the preparation of 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 presentation of supplementary information in the Disclosure Statement which complies with Schedules 3, 5, 7, 11, 13, 16 and 18 of the Order.

Our responsibility

Our responsibility is to express the following conclusions on the financial statements and supplementary information presented by the Directors based on our review:

- in relation to the financial statements (excluding the supplementary information) whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the financial statements 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);
- in relation to the supplementary information (excluding the supplementary information relating to capital adequacy and regulatory liquidity requirements) whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information does not fairly state the matters to which it relates in accordance with Schedules 5, 7, 13, 16 and 18 of the Order; and
- in relation to the supplementary information relating to capital adequacy and regulatory liquidity requirements whether, in our opinion on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information is not, in all material respects, disclosed in accordance with Schedule 11 of the Order.

We conducted our review in accordance with the New Zealand Standard on Review Engagements 2410: *Review of Financial Statements Performed by the Independent Auditor of the Entity* (NZ SRE 2410). As the auditor of the Banking Group, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements.

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Independent auditor's review report *(continued)*

A review in accordance with NZ SRE 2410 is a limited assurance engagement. The auditor performs procedures, primarily 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 International Standards on Auditing. Accordingly, we do not express an audit opinion on the financial statements and supplementary information.

We are independent of the Banking Group. Our firm carries out other services for the Banking Group in the areas of other assurance services and agreed upon procedures. In addition, certain partners and employees of our firm may deal with the Banking Group on normal terms within the ordinary course of trading activities of the Banking Group. These matters have not impaired our independence as auditor of the Banking Group.

Conclusion

We have examined the financial statements and supplementary information and based on our review, nothing has come to our attention that causes us to believe that:

a) the financial statements on pages 3 to 30 (excluding the supplementary information) have not been prepared, in all material respects, in accordance with NZ IAS 34 and IAS 34;

b) the supplementary information prescribed by Schedules 5, 7, 13, 16 and 18 of the Order, does not fairly state the matters to which it relates in accordance with those Schedules; and

c) the supplementary information relating to capital adequacy and regulatory liquidity requirements prescribed by Schedule 11 of the Order, is not, in all material respects, disclosed in accordance with Schedule 11 of the Order

Emphasis of matter

Without modifying our conclusion, we draw attention to the disclosures in Note 14 of the financial statements and to the other information on page 31 of the Disclosure Statement, which disclose certain matters of non-compliance with condition of registration 1B by the Bank. This includes the fact that the Bank continues to operate versions of certain internal models for credit risk that have not been approved by the Reserve Bank of New Zealand. However, as disclosed in Note 14 of the financial statements and the other information on page 31 of the Disclosure Statement, the Bank considers its current internal credit model methodologies result in the retention of an appropriate amount of capital to reflect its credit risk and any effect of the non-compliance with condition of registration 1B on the information relating to capital adequacy disclosed in the financial statements is not considered to be material.

Who we report to

This report is made solely to the Bank's shareholder. Our review work has been undertaken so that we might state those matters which we are required to state to them in our 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 procedures, for this report, or for the conclusions we have formed.

For and on behalf of:

PricewaterhouseCoopers

Chartered Accountants
24 May 2018

Auckland

Westpac New Zealand Limited.

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