

**ANZ BANK NEW ZEALAND LIMITED
ANNUAL REPORT AND REGISTERED BANK DISCLOSURE STATEMENT**

FOR THE YEAR ENDED 30 SEPTEMBER 2017
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ANNUAL REPORT AND REGISTERED BANK DISCLOSURE STATEMENT

FOR THE YEAR ENDED 30 SEPTEMBER 2017

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ANNUAL REPORT

FOR THE YEAR ENDED 30 SEPTEMBER 2017

Pursuant to section 211(3) of the Companies Act 1993, the shareholder of the Bank has agreed that the Annual Report of the Banking Group need not comply with any of the paragraphs (a), and (e) to (j) of subsection (1) and subsection (2) of section 211.

Accordingly, there is no information to be provided in this Annual Report other than the financial statements for the year ended 30 September 2017 and the audit report on those financial statements.

For and on behalf of the Board of Directors:



John Judge
Chairman
15 November 2017



David Hisco
Executive Director
15 November 2017

GLOSSARY OF TERMS

In this Registered Bank Disclosure Statement (Disclosure Statement) unless the context otherwise requires:

Bank means ANZ Bank New Zealand Limited.

Banking Group means the Bank and all its controlled entities.

Immediate Parent Company means ANZ Holdings (New Zealand) Limited.

Ultimate Parent Bank means Australia and New Zealand Banking Group Limited.

Overseas Banking Group means the worldwide operations of Australia and New Zealand Banking Group Limited including its controlled entities.

New Zealand business means all business, operations, or undertakings conducted in or from New Zealand identified and treated as if it were conducted by a company formed and registered in New Zealand.

NZ Branch means the New Zealand business of the Ultimate Parent Bank.

ANZ New Zealand means the New Zealand business of the Overseas Banking Group.

UDC means UDC Finance Limited.

Registered Office is Ground Floor, ANZ Centre, 23-29 Albert Street, Auckland, New Zealand, which is also the Banking Group's address for service.

RBNZ means the Reserve Bank of New Zealand.

APRA means the Australian Prudential Regulation Authority.

the Order means the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014.

Any term or expression which is defined in, or in the manner prescribed by, the Order shall have the meaning given in or prescribed by the Order.

INCOME STATEMENT

	Note	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Interest income	3	6,198	6,423
Interest expense	3	3,161	3,421
Net interest income		3,037	3,002
Net trading gains	4	226	12
Net funds management and insurance income	4	329	414
Other operating income	4	378	421
Share of associates' profit		5	5
Operating income		3,975	3,854
Operating expenses	5	1,468	1,599
Profit before credit impairment and income tax		2,507	2,255
Credit impairment charge	14	62	150
Profit before income tax		2,445	2,105
Income tax expense	6	680	570
Profit after income tax		1,765	1,535

STATEMENT OF COMPREHENSIVE INCOME

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Profit after income tax	1,765	1,535
<i>Items that will not be reclassified to profit or loss</i>		
Actuarial gain on defined benefit schemes	21	18
Income tax expense relating to items not reclassified	(6)	(5)
Total items that will not be reclassified to profit or loss	15	13
<i>Items that may be reclassified subsequently to profit or loss</i>		
Unrealised gains / (losses) recognised directly in equity	(32)	91
Realised losses transferred to the income statement	12	9
Income tax credit / (expense) relating to items that may be reclassified	6	(28)
Total items that may be reclassified subsequently to profit or loss	(14)	72
Total comprehensive income for the year	1,766	1,620

BALANCE SHEET

	Note	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Assets			
Cash	9	2,338	2,274
Settlement balances receivable		536	396
Collateral paid		1,415	2,310
Trading securities	10	7,663	11,979
Investments backing insurance contract liabilities		123	119
Derivative financial instruments	11	9,878	21,110
Available-for-sale assets	12	6,360	2,859
Net loans and advances	13	117,627	114,623
UDC assets held for sale	29	3,065	-
Other assets		683	701
Life insurance contract assets		636	630
Investments in associates		7	7
Premises and equipment		367	387
Goodwill and other intangible assets	24	3,275	3,424
Total assets		153,973	160,819
Interest earning and discount bearing assets		138,795	134,489
Liabilities			
Settlement balances payable		1,840	1,771
Collateral received		613	529
Deposits and other borrowings	15	101,657	99,066
Derivative financial instruments	11	9,826	21,956
Current tax liabilities		39	21
Deferred tax liabilities		187	145
UDC liabilities held for sale	29	1,088	-
Payables and other liabilities		1,151	1,119
Employee entitlements		119	126
Other provisions		66	80
Unsubordinated debt	16	21,323	20,014
Subordinated debt	17	3,283	3,282
Total liabilities		141,192	148,109
Net assets		12,781	12,710
Equity			
Share capital	25	8,888	8,888
Reserves		48	62
Retained earnings		3,845	3,760
Total equity		12,781	12,710
Interest and discount bearing liabilities		119,814	115,961

For and on behalf of the Board of Directors:



John Judge
Chairman
15 November 2017



David Hisco
Executive Director
15 November 2017

CASH FLOW STATEMENT

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Note		
Cash flows from operating activities		
Interest received	6,223	6,443
Dividends received	5	2
Net funds management and insurance income	344	332
Fees and other income received	569	642
Interest paid	(3,100)	(3,416)
Operating expenses paid	(1,374)	(1,495)
Income taxes paid	(605)	(648)
Cash flows from operating profits before changes in operating assets and liabilities	2,062	1,860
Net changes in operating assets and liabilities:		
Change in settlements receivable	(14)	(19)
Change in collateral paid	895	(381)
Change in trading securities	4,210	164
Change in derivative financial instruments	10	(2,028)
Change in available-for-sale assets	(3,476)	(1,381)
Change in insurance investment assets	(4)	32
Change in loans and advances	(6,761)	(9,435)
Proceeds from sale of loans and advances to NZ Branch	481	697
Change in settlements payable	2	(67)
Change in collateral received	84	(1,158)
Change in deposits and other borrowings	3,356	9,142
Net changes in operating assets and liabilities	(1,217)	(4,434)
Net cash flows provided by / (used in) operating activities	8	(2,574)
Cash flows from investing activities		
Proceeds from sale of premises and equipment	9	17
Proceeds from sale of insurance policies	-	23
Purchase of intangible assets	(14)	(29)
Purchase of premises and equipment	(44)	(71)
Net cash flows used in investing activities	(49)	(60)
Cash flows from financing activities		
Proceeds from issue of unsubordinated debt	4,922	7,380
Proceeds from issue of subordinated debt	-	938
Redemptions of unsubordinated debt	(3,899)	(4,477)
Dividends paid	(1,695)	(1,363)
Net cash flows provided by / (used in) financing activities	(672)	2,478
Net increase / (decrease) in cash and cash equivalents	124	(156)
Cash and cash equivalents at beginning of the year	2,315	2,471
Cash and cash equivalents at end of the year	8	2,315

STATEMENT OF CHANGES IN EQUITY

	Note	Share capital NZ\$m	Available- for-sale revaluation reserve NZ\$m	Cash flow hedging reserve NZ\$m	Retained earnings NZ\$m	Total equity NZ\$m
As at 1 October 2015		8,888	-	(10)	3,575	12,453
Profit after income tax		-	-	-	1,535	1,535
Unrealised gains / (losses) recognised directly in equity		-	(2)	93	-	91
Realised losses transferred to the income statement		-	2	7	-	9
Actuarial gain on defined benefit schemes		-	-	-	18	18
Income tax expense on items recognised directly in equity		-	-	(28)	(5)	(33)
Total comprehensive income for the year		-	-	72	1,548	1,620
Ordinary dividend paid	25	-	-	-	(1,350)	(1,350)
Preference dividend paid	25	-	-	-	(13)	(13)
As at 30 September 2016		8,888	-	62	3,760	12,710
Profit after income tax		-	-	-	1,765	1,765
Unrealised gains / (losses) recognised directly in equity		-	7	(39)	-	(32)
Realised losses transferred to the income statement		-	-	12	-	12
Actuarial gain on defined benefit schemes		-	-	-	21	21
Income tax credit / (expense) on items recognised directly in equity		-	(2)	8	(6)	-
Total comprehensive income for the year		-	5	(19)	1,780	1,766
Ordinary dividend paid	25	-	-	-	(1,684)	(1,684)
Preference dividend paid	25	-	-	-	(11)	(11)
As at 30 September 2017		8,888	5	43	3,845	12,781

NOTES TO THE FINANCIAL STATEMENTS

1. SIGNIFICANT ACCOUNTING POLICIES

(A) Basis of preparation

(i) Statement of compliance

These financial statements have been prepared in accordance with the requirements of the Financial Markets Conduct Act 2013 and the Order. The Banking Group's financial statements are for the Bank's consolidated group, which includes its subsidiaries and associates.

These financial statements comply with:

- New Zealand Generally Accepted Accounting Practice, as defined in the Financial Reporting Act 2013
- New Zealand equivalents to International Financial Reporting Standards (NZ IFRS) and other applicable Financial Reporting Standards, as appropriate for publicly accountable for-profit entities
- International Financial Reporting Standards (IFRS).

The principal accounting policies adopted in the preparation of these financial statements are set out below.

(ii) Use of estimates and assumptions

The preparation of these financial statements requires the use of management judgements, estimates and assumptions that affect reported amounts and the application of policies.

Discussion of the critical accounting estimates, which include complex or subjective decisions or assessments, are covered in note 2. Such estimates are reviewed on an ongoing basis.

(iii) Basis of measurement

The financial information has been prepared in accordance with the historical cost basis except that the following assets and liabilities are stated at their fair value:

- derivative financial instruments
- available-for-sale financial assets
- financial instruments held for trading
- financial instruments designated at fair value through profit and loss.

(iv) Rounding

The amounts in the financial statements have been rounded to the nearest million dollars, except where otherwise stated.

(v) Principles of consolidation

Subsidiaries

The consolidated financial statements of the Banking Group comprise the financial statements of the Bank and all its subsidiaries. An entity, including a structured entity, is considered a subsidiary of the Banking Group when it is determined that control over the entity exists. Control is deemed to exist when the Banking Group is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Power is assessed by examining existing rights that give the Banking Group the current ability to direct the relevant activities of the entity.

At times, the determination of control can be judgemental. Further detail on the judgements involved in assessing control has been provided in note 2.

The effect of all transactions between entities in the Banking Group is eliminated.

Associates

The Banking Group applies the equity method of accounting for associates.

(vi) Foreign currency translation

Functional and presentation currency

Items included in the financial statements of each of the Banking Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency).

The Banking Group's financial statements are presented in New Zealand dollars, which is the Banking Group's functional and presentation currency.

Foreign currency transactions

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions.

Monetary assets and liabilities resulting from foreign currency transactions are subsequently translated at the spot rate at reporting date.

Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different to those at which they were initially recognised or included in a previous financial report, are recognised in profit or loss in the period in which they arise.

NOTES TO THE FINANCIAL STATEMENTS

(B) Operating income

(i) Net Interest income

Interest income and expense

Interest income and expense is recognised in profit or loss using the effective interest method. This method uses the effective interest rate of a financial asset or financial liability to calculate its amortised cost. The effective interest rate is the rate that discounts the stream of estimated future cash receipts or payments over the expected life of the financial instrument or, when appropriate, a shorter period, to the net carrying amount of the financial asset or liability. For assets subject to prepayment, the expected life is determined on the basis of historical behaviour of the particular asset portfolio – taking into account contractual obligations and prepayment experience.

Fees and costs, which form an integral part of the financial instruments (for example loan origination fees and costs), are recognised using the effective interest method. This is presented as part of interest income or expense depending on whether the underlying financial instrument is a financial asset or liability.

(ii) Fee and commission income

Fees and commissions that relate to the execution of a significant act (for example, advisory or arrangement services, placement fees and underwriting fees) are recognised when the significant act has been completed.

Fees charged for providing ongoing services (for example, maintaining and administering existing facilities) are recognised as income over the period the service is provided.

(C) Income tax

(i) Income tax expense

Income tax expense comprises both current and deferred taxes and is based on accounting profit adjusted for differences in the accounting and tax treatments of income and expenses (that is, taxable income). Tax expense is recognised in profit or loss, except to the extent to which it relates to items recognised directly in equity or other comprehensive income respectively.

(ii) Current tax expense

Current tax is the tax payable on taxable income for the year, based on tax rates (and tax laws) which are enacted at the reporting date. It includes any adjustment for tax payable in previous periods. Current tax is recognised as a liability (or asset) to the extent that it is unpaid (or refundable).

(iii) Deferred tax

Deferred tax is accounted for using the balance sheet method. Deferred tax arises because the accounting income is not always the same as the taxable income. This creates temporary differences, which usually reverse over time. Until they reverse, a deferred tax, or liability, is recognised on the balance sheet. Deferred taxes are measured at the tax rates that we expect will apply to the period(s) when the asset is realised, or the liability settled, based on tax rates (and tax laws) that have been enacted or substantially enacted at the reporting date.

Current and deferred tax assets and liabilities are offset only to the extent that: they relate to income taxes imposed by the same taxation authority; there is a legal right and intention to settle on a net basis; and it is allowed under the tax law of the relevant jurisdiction.

(D) Assets

Financial assets

(i) Financial assets and liabilities at fair value through profit or loss

Trading securities are financial instruments acquired principally for the purpose of selling in the short-term or which are a part of a portfolio which is managed for short-term profit-taking. Purchases and sales of trading securities are recognised on trade date and are initially designated at fair value through profit and loss, and subsequently measured in the balance sheet at their fair value with any revaluation recognised in profit and loss.

(ii) Derivative financial instruments

Derivative financial instruments are contracts whose value is derived from an underlying price index (or other variable) defined in the contract – sometimes the value is derived from more than one variable: that require little or no initial net investment; and that are settled at a future date. Movements in the price of the underlying variable, which cause the value of the contract to fluctuate, are reflected in the fair value of the derivative.

Derivative financial instruments are entered into for trading purposes (including customer-related reasons) or for hedging purposes (where the derivative instruments are used to hedge the Banking Group's exposures to interest rate risk, currency risk, price risk, credit risk and other exposures relating to non-trading positions).

Derivative financial instruments include forwards, futures, swaps and options.

Derivative financial instruments are recognised initially and at each reporting date at fair value. If the fair value of a derivative is: positive, then it is carried as an asset, but if it is negative, then it is carried as a liability. Valuation adjustments are integral in determining the fair value of derivatives. This includes a derivative credit valuation adjustment (CVA) to reflect the counterparty risk and/or event of default; and a funding valuation adjustment (FVA) to account for the funding cost and benefits in the derivatives' portfolio.

NOTES TO THE FINANCIAL STATEMENTS

Where the derivative is effective as a hedging instrument and designated as such, the timing of the recognition of any resultant gain or loss in profit or loss is dependent on the hedging designation. These hedging designations and associated accounting are as follows:

Fair value hedge

Where the Banking Group hedges the fair value of a recognised asset or liability or firm commitment, changes in the fair value of the derivative designated as a fair value hedge are recognised in profit or loss. Changes in the fair value of the hedged item attributable to the hedged risk are reflected in adjustments to the carrying value of the hedged item, which are also recognised in profit or loss.

Hedge accounting is discontinued when the hedge instrument expires or is sold, terminated, exercised or no longer qualifies for hedge accounting. The resulting adjustment to the carrying amount of the hedged item arising from the hedged risk is amortised to profit or loss over the period to maturity of the hedged item.

If the hedged item is sold or repaid, the unamortised fair value adjustment is recognised immediately in profit or loss.

Cash flow hedge

The Banking Group designates derivatives as cash flow hedges where the instrument hedges the variability in cash flows of a recognised asset or liability, a foreign exchange component of a firm commitment, or a highly probable forecast transaction. For qualifying cash flow hedges, the fair value gain or loss associated with the effective portion of the cash flow hedges is recognised initially in other comprehensive income and then recycled to profit or loss in the periods when the hedged item will affect profit or loss. Any ineffective portion is recognised immediately in profit or loss. When the hedging instrument expires, is sold, terminated, exercised, or no longer qualifies for hedge accounting, the cumulative amount deferred in equity remains in the hedging reserve, and is subsequently transferred to profit or loss when the hedged item is recognised in profit or loss.

When a forecast hedged transaction is no longer expected to occur, the amount deferred in equity is recognised immediately in profit or loss.

Derecognition of assets and liabilities

Derivative assets are removed from the balance sheet when substantially all of the risks and rewards of ownership have transferred. Derivative financial liabilities are removed from the balance sheet when the Banking Group's contractual obligations are discharged, cancelled or expired.

Derivatives that do not qualify for hedge accounting

All gains and losses from changes in the fair value of derivatives that are not designated in a hedging relationship but are entered into to manage the interest rate and foreign exchange risk of the Banking Group are recognised in profit or loss. Under certain circumstances, the component of the fair value change in the derivative which relates to current period realised and accrued interest is included in net interest income. The remainder of the fair value movement is included in other income.

(iii) Available-for-sale assets

Available-for-sale assets comprise non-derivative financial assets which the Banking Group designates as available-for-sale but which are not deemed to be held principally for trading purposes, and include equity investments and debt securities.

They are initially recognised at fair value plus transaction costs. Subsequent gains or losses arising from changes in fair value are included as a separate component of equity in the available-for-sale revaluation reserve. When the asset is sold, the cumulative gain or loss from the available-for-sale reserve is recognised in profit or loss.

(iv) Net loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and advances are initially recognised at fair value plus transaction costs directly attributable to the issue of the loan or advance, which are primarily brokerage/mortgage origination fees. Subsequently, they are measured at amortised cost using the effective interest method, net of any provision for credit impairment.

The Banking Group classifies contracts to lease assets and hire purchase agreements as finance leases if they transfer substantially all the risks and rewards of ownership of the asset to the customer or an unrelated third party. All other lease contracts are classified as operating leases.

The Banking Group enters into transactions in which it transfers financial assets that are recognised on its balance sheet. When the Banking Group retains substantially all of the risks and rewards of the transferred assets, then the transferred assets remain on the Banking Group's balance sheet, however if substantially all the risks and rewards are transferred then the Banking Group derecognises the asset.

If the risks and rewards are partially retained and control over the asset is lost, then the Banking Group derecognises the asset. If control over the asset is not lost, then the Banking Group continues to recognise the asset to the extent of its continuing involvement.

The Banking Group separately recognises the rights and obligations retained, or created, in the transfer as assets and liabilities as appropriate.

NOTES TO THE FINANCIAL STATEMENTS

Impairment of loans and advances

The Banking Group recognises two types of impairment provisions for its loans and advances:

- Individual provisions for significant assets that are assessed to be impaired; and
- Collective provisions for portfolios of similar assets that are assessed collectively for impairment.

Individually

If any impaired loans and advances exceed thresholds and an impairment event has been identified, then the Banking Group assesses the need for a provision individually.

Loans and advances are assessed as impaired if the Banking Group has objective evidence that they may not recover principal or interest payments (that is, a loss event has been incurred) and the Banking Group can reliably measure the impairment.

Collectively

To allow for any small value loans and advances where losses may have been incurred but not yet identified, and individually significant loans and advances that the Banking Group does not assess as impaired, the Banking Group assesses them collectively in pools of assets with similar risk characteristics.

The Banking Group estimates the provision on the basis of historical loss experience for assets with credit risk characteristics similar to others in the respective collective pool. The Banking Group adjusts the historical loss experience based on current observable data, such as: changing economic conditions, the impact of the inherent risk of large concentrated losses within the portfolio and an assessment of the economic cycle.

Measurement

The Banking Group measures impairment loss as the difference between the asset's carrying amount and estimated future cash flows discounted to their present value at the asset's original effective interest rate. The Banking Group records the result as an expense in profit or loss in the period the Banking Group identifies the impairment and recognises a corresponding reduction in the carrying amount of loans and advances through an offsetting provision.

Uncollectible amounts

If a loan or advance is uncollectible (whether partially or in full), then the Banking Group writes off the balance (and also any related provision for credit impairment).

The Banking Group writes off unsecured retail facilities at the earlier of the facility becoming 180 days past due, or the customer's bankruptcy or similar legal release from the obligation to repay the loan or advance. For secured facilities, write offs occur net of the proceeds determined to be recoverable from the realisation of collateral.

Recoveries

If the Banking Group recovers any cash flows from loans and advances previously written off, then the recovery is recognised in profit or loss in the period the cash flows are received.

Off-balance sheet amounts

Any off-balance sheet items, such as loan commitments, are considered for impairment both on an individual and collective basis.

Non-financial assets

(v) Goodwill

Goodwill represents the excess amount the Banking Group has paid in acquiring a business over the fair value less costs of disposal of the identifiable assets and liabilities acquired. Goodwill is recognised at cost less any accumulated impairment losses. Goodwill is reviewed for impairment at least annually or when there is an indication of impairment. This involves using the discounted cash flows methodology to determine the expected future benefits of the cash generating units to which the acquisition relates. Where the assessment results in the goodwill balance exceeding the value of expected future benefits, the difference is charged to profit or loss. Any impairment of goodwill is not subsequently reversed.

(E) Liabilities

Financial liabilities

(i) Deposits and other borrowings

For deposits and borrowings that are not designated at fair value through profit or loss on initial recognition, the Banking Group measures them at amortised cost and recognises their interest expense using the effective interest rate method. When deposits and other borrowings are managed on a fair value basis, reduce or eliminate an accounting mismatch or contain an embedded derivative, the Banking Group designates them as fair value through profit or loss.

For deposits and other borrowings designated at fair value the Banking Group recognises the amount of fair value gain or loss attributable to changes in the Banking Group's own credit risk in other comprehensive income in retained earnings. Any remaining amount of fair

NOTES TO THE FINANCIAL STATEMENTS

value gain or loss is recognised directly in profit or loss. Once the Banking Group has recognised an amount in other comprehensive income, the Banking Group does not later reclassify it to profit or loss.

Securities sold under repurchase agreements represent a liability to repurchase the financial assets that remain on the Banking Group's balance sheet, since the risks and rewards of ownership remain with the Banking Group. Over the life of the repurchase agreement, the Banking Group recognises the difference between the sale price and the repurchase price and charges it to interest expense in profit or loss.

(ii) Unsubordinated debt and subordinated debt

Unsubordinated debt and subordinated debt are measured at amortised cost, except where designated at fair value through profit or loss. Where the Banking Group enters into a hedge accounting relationship, the fair value attributable to the hedged risks is reflected in adjustments to the carrying value of the debt. Interest expense is recognised using the effective interest rate method.

(F) Equity

(i) Shares

Issued shares are recognised at the amount paid per share net of directly attributable issue costs.

(ii) Reserves

Available-for-sale revaluation reserve

This reserve includes the changes in fair value and exchange differences on the Banking Group's revaluation of available-for-sale financial assets, net of deferred taxes to be realised upon disposal of the asset.

Cash flow hedging reserve

This reserve includes fair value gains and losses associated with the effective portion of designated cash flow hedging instruments, net of deferred taxes to be realised when the position is settled.

(G) Presentation

(i) Offsetting of income and expenses

Income and expenses are not offset unless required or permitted by an accounting standard. This generally arises in either of the following circumstances:

- where transaction costs form an integral part of the effective interest rate of a financial instrument which is measured at amortised cost, these are offset against the interest income generated by the financial instrument
- where gains and losses arise from a group of similar transactions, such as foreign exchange gains and losses.

(ii) Offsetting of financial assets and liabilities

Assets and liabilities are offset and the net amount reported in the balance sheet only where there is:

- a current enforceable legal right to offset the asset and liability
- an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

(iii) Segment reporting

Operating segments are distinguishable components of the Banking Group that provide products or services that are subject to risks and rewards that are different to those of other operating segments. The Banking Group operates predominantly in the banking industry within New Zealand. The Banking Group has very limited exposure to risk associated with operating in different economic environments or political conditions. On this basis no geographical segment information is provided.

(H) Other

(i) Contingent liabilities

Contingent liabilities are not recognised in the balance sheet but disclosed in note 23 unless it is considered remote that the Banking Group will be liable to settle the possible obligation.

(ii) Accounting Standards not early adopted

A number of new standards, amendments to standards and interpretations have been published but are not mandatory for the financial statements for the year ended 30 September 2017, and have not been applied by the Banking Group in preparing these financial statements.

The Banking Group has identified three standards where this applies to the Banking Group and further details are set out below.

NZ IFRS 9 Financial Instruments (NZ IFRS 9)

NZ IFRS 9 was issued in September 2014. When operative, this standard will replace NZ IAS 39 *Financial Instruments: Recognition and Measurement* (NZ IAS 39) and includes requirements for impairment, classification and measurement and general hedge accounting.

NOTES TO THE FINANCIAL STATEMENTS

Impairment

NZ IFRS 9 replaces the incurred loss model under NZ IAS 39 with a forward-looking expected loss model. This model will be applied to financial assets measured at amortised cost, debt instruments measured at fair value through other comprehensive income, lease receivables, and certain loan commitments and financial guarantees. Under NZ IFRS 9, a three stage approach is applied to measuring expected credit losses (ECL) based on credit migration between the stages as follows:

- Stage 1: At initial recognition, a provision equivalent to 12 months ECL is recognised.
- Stage 2: Where there has been a significant increase in credit risk since initial recognition, a provision equivalent to full lifetime ECL is required.
- Stage 3: Similar to the current NZ IAS 39 requirements for individual impairment provisions, lifetime ECL is recognised for loans where there is objective evidence of impairment.

ECL are probability weighted and determined by evaluating a range of possible outcomes, taking into account the time value of money, past events, current conditions and forecasts of future economic conditions.

Classification and measurement

There are three measurement classifications under NZ IFRS 9: amortised cost, fair value through profit or loss and, for financial assets, fair value through other comprehensive income. Financial assets are classified into these measurement classifications taking into account the business model within which they are managed, and their contractual cash flow characteristics.

The classification and measurement requirements for financial liabilities under NZ IFRS 9 are largely consistent with NZ IAS 39 with the exception that for financial liabilities designated as measured at fair value, gains or losses relating to changes in the entity's own credit risk are included in other comprehensive income. This part of the standard was early adopted by the Banking Group from 1 October 2013.

General hedge accounting

NZ IFRS 9 introduces general hedge accounting requirements which more closely align with risk management activities undertaken when hedging financial and non-financial risks.

Transition and impact

Other than noted above under classification and measurement, NZ IFRS 9 has a date of initial application for the Banking Group of 1 October 2018.

The classification and measurement, and impairment requirements will be applied retrospectively by adjusting the opening balance sheet at the date of initial application, with no requirements to restate comparative periods. The Banking Group does not intend to restate comparatives. NZ IFRS 9 provides an accounting policy choice to continue with NZ IAS 39 hedge accounting given the International Accounting Standards Board's ongoing project on macro hedge accounting. The Banking Group's current expectation is that it will continue to apply the hedge accounting requirements of NZ IAS 39.

The Banking Group is in the process of assessing the impact of the application of NZ IFRS 9 and is not yet able to reasonably estimate the impact on its financial statements.

NZ IFRS 15 Revenue from Contracts with Customers (NZ IFRS 15)

NZ IFRS 15 was issued in July 2014. NZ IFRS 15 contains new requirements for the recognition of revenue.

NZ IFRS 15 requires identification of distinct performance obligations within a contract and allocation of the transaction price of the contract to those performance obligations. Revenue is recognised as each performance obligation is satisfied. Variable amounts of revenue can only be recognised if it is highly probable that a significant reversal of the variable amount will not be required in future periods.

Although a significant proportion of the Banking Group's revenue is outside the scope of NZ IFRS 15, certain revenue streams are in the scope of the standard. NZ IFRS 15 is not mandatorily effective for the Banking Group until 1 October 2018. The Banking Group is in the process of assessing the impact of application of NZ IFRS 15 and is not yet able to reasonably estimate the impact on its financial statements.

NZ IFRS 15 may be applied under different transition approaches which could impact (a) revenue recognised in future periods and (b) the opening adjustment to retained earnings at the relevant date of initial application. The Banking Group has not determined which transition approach it will adopt.

NZ IFRS 16 Leases (NZ IFRS 16)

The final version of NZ IFRS 16 *Leases* was issued in February 2016 and is not effective for the Banking Group until 1 October 2019. NZ IFRS 16 requires a lessee to recognise its right to use the underlying leased asset, as a right-of-use asset, and obligation to make lease payments as a lease liability. NZ IFRS 16 substantially carries forward the lessor accounting requirements in NZ IAS 17 *Leases*.

The Banking Group is in the process of assessing the impact of the application of NZ IFRS 16 and is not yet able to reasonably estimate the impact on its financial statements.

NOTES TO THE FINANCIAL STATEMENTS

2. CRITICAL ESTIMATES AND JUDGEMENTS USED IN APPLYING ACCOUNTING POLICIES

There are a number of critical accounting treatments which include complex or subjective judgements and estimates that may affect the reported amounts of assets and liabilities in the financial statements. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

An explanation of the judgements and estimates made by the Banking Group, in the process of applying its accounting policies, that have the most significant effect on the amounts recognised in the financial statements is set out below.

Critical accounting estimates and assumptions

Credit provisioning

The accounting policy relating to measuring the impairment of loans and advances requires the Banking Group to assess impairment at least at each reporting date. The credit provisions raised (collective and individual) represent management's best estimate of the losses incurred in the loan portfolio at balance date based on their experienced judgement.

The collective provision is estimated on the basis of historical loss experience for assets with credit characteristics similar to those in the collective pool. The historical loss experience is adjusted based on current observable data and events and an assessment of the impact of model risk. The provision also takes into account the impact of large concentrated losses within the portfolio and the economic cycle.

The use of such judgements and reasonable estimates is considered by management to be an essential part of the process and does not impact on the reliability of the provision.

Individual and collective provisioning involves the use of assumptions for estimating the amounts and timing of expected future cash flows. The process of estimating the amount and timing of cash flows involves considerable management judgement. These judgements are revised regularly to reduce any differences between loss estimates and actual loss experience.

Refer to note 14 for details of credit impairment provisions.

Critical judgements in applying the Banking Group's accounting policies

Financial instruments at fair value

The Banking Group's financial instruments measured at fair value are stated in note 1(A)(iii). In estimating fair value the Banking Group uses, wherever possible, quoted market prices in an active market for the financial instrument.

In the event that there is no active market for the instrument, fair value is based on present value estimates or other market accepted valuation techniques. The valuation models incorporate the impact of bid/ask spread, counterparty credit spreads and other factors that would influence the fair value determined by a market participant. The selection of appropriate valuation techniques, methodology and inputs requires judgement. These are reviewed and updated as market practice evolves.

Derivatives and hedging

The Banking Group buys and sells derivatives as part of its trading operations and to hedge its interest rate risk, currency risk, price risk, credit risk and other exposures relating to non-trading positions.

A hedging instrument is a designated derivative whose fair value or cash flows are expected to offset changes in the fair value or cash flows of a designated hedged item. A hedged item is an asset, liability, firm commitment or highly probable forecast transaction that: (a) exposes the Banking Group to the risk of changes in fair value or future cash flows; and (b) is designated as being hedged.

Judgement is required in selecting and designating hedging relationships and assessing hedge effectiveness. NZ IAS 39 does not specify a single method for assessing hedge effectiveness prospectively or retrospectively. The Banking Group adopts the hypothetical derivative approach to determine hedge effectiveness in line with current risk management strategies. Hedge ineffectiveness can arise for a number of reasons and whilst a hedge may pass the effectiveness tests above it may not be perfectly effective, leaving some volatility in profit or loss.

The majority of outstanding derivative positions are transacted over-the-counter and therefore need to be valued using valuation techniques. Included in the determination of the fair value of derivatives is a credit valuation adjustment (CVA) to reflect the creditworthiness of the counterparty. This is influenced by the mark-to-market of the derivative trades and by the movement in the market cost of credit. Further adjustments are made to account for the funding costs inherent in the derivative. Judgement is required to determine the appropriate cost of funding and the future expected cashflows used in this funding valuation adjustment (FVA).

Structured entities

A structured entity is an entity in which voting or similar rights are not the dominant factor in deciding who controls the entity, such as when voting rights relate to administrative tasks only and the relevant activities are directed by means of contractual arrangements. Structured entities are generally created to achieve a narrow and well defined objective with restrictions around their ongoing activities and are often thinly capitalised with a reliance on debt financing for support.

The Banking Group assesses, at inception and periodically, whether a structured entity should be consolidated based on the accounting policy outlined in note 1. Such assessments are predominantly securitisation activities and involvement with managed funds. When

NOTES TO THE FINANCIAL STATEMENTS

assessing whether the Banking Group controls (and therefore consolidates) a structured entity, judgement is required about whether the Banking Group has power over the relevant activities as well as exposure to variable returns of the structured entity. All involvement, rights and exposure to returns are considered when assessing if control exists.

The Banking Group is deemed to have power over a managed fund when it performs the function of Manager of that managed fund. Whether the Banking Group controls the managed fund depends on whether it holds that power as principal, or as an agent for other investors. The Banking Group is considered the principal, and thus controls the managed fund, when it cannot be easily removed from the position of Manager by other investors and has variable returns through significant aggregate economic interest in that managed fund. In all other cases the Banking Group is considered to be acting in an agency capacity and does not control the managed fund.

Structured entities are consolidated when control exists. In other cases the Banking Group may simply have an interest in or may sponsor a structured entity but not consolidate it.

The Banking Group considers itself the sponsor of an unconsolidated structured entity where it is the primary party involved in the design and establishment of that structured entity and where any of the following apply:

- where the Banking Group is the major user of that structured entity
- the Banking Group's name appears in the name of that structured entity or on its products
- the Banking Group provides implicit or explicit guarantees of that entity's performance.

Goodwill

Refer to note 24 for details of goodwill held by the Banking Group.

The carrying value of goodwill is subject to an impairment test to ensure that the current carrying value does not exceed its recoverable value at the balance sheet date. Any excess of carrying value over recoverable amount is taken to profit or loss as an impairment write down.

Goodwill has been allocated for impairment purposes to the cash generating units at which the goodwill is monitored for internal reporting purposes. Impairment testing of purchased goodwill is performed by comparing the recoverable value of each cash generating unit with the current carrying amount of its net assets, including goodwill. Judgement is required in identifying the cash-generating units to which goodwill and other assets are allocated for the purpose of impairment testing.

The recoverable amount is based on value-in-use calculations. These calculations use cash flow projections based on a number of financial budgets within each segment approved by management covering a three year period. Cash flow projections are based on a range of readily available economic assumptions including GDP and CPI. Cash flows beyond the three year period are extrapolated using a 2% growth rate.

These cash flow projections are discounted using a capital asset pricing model. As at 28 February 2017 when the last valuation was prepared, a discount rate of 11.5% was applied to each cash generating unit. The main variables in the calculation of the discount rate used are the risk free rate, the beta rate and the market risk premium. The risk free rate is based on the 10 year Government Bond Rate. The beta rate and the market risk premium are consistent with observable and comparative market rates applied in the regional banking sector. Market observable information is not readily available at the segment level therefore management performed stress tests for key sensitivities in each segment.

Management believes any reasonable possible change in the key assumptions on which the recoverable amount is based would not cause the Banking Group's carrying amount to exceed its recoverable amount.

NOTES TO THE FINANCIAL STATEMENTS

3. NET INTEREST INCOME

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Interest income		
<i>Financial assets at fair value through profit or loss</i>		
Trading securities	351	453
<i>Financial assets not at fair value through profit or loss</i>		
Cash	41	63
Available-for-sale assets	106	64
Net loans and advances	5,675	5,814
Other	25	29
	5,847	5,970
Total interest income	6,198	6,423
Interest expense		
<i>Financial liabilities at fair value through profit or loss</i>		
Commercial paper	122	226
<i>Financial liabilities not at fair value through profit or loss</i>		
Deposits and other borrowings	2,090	2,310
Unsubordinated debt	704	681
Subordinated debt	220	170
Other	25	34
	3,039	3,195
Total interest expense	3,161	3,421
Net Interest Income	3,037	3,002

4. NON INTEREST INCOME

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Net trading gains		
Net gain on foreign exchange trading	176	203
Net gain / (loss) on trading securities	(121)	115
Net gain / (loss) on trading derivatives	171	(306)
Net trading gains	226	12
Net funds management and insurance income		
Net funds management income	199	187
Net insurance income	130	227
Total funds management and insurance income	329	414
Other operating income		
Lending and credit facility fee income	35	55
Other fee income	702	675
Total fee income	737	730
Direct fee expense	(328)	(308)
Net fee income	409	422
Net gain / (loss) on financial liabilities designated at fair value	4	(5)
Net ineffectiveness on qualifying fair value hedges	(6)	1
Net loss on derivatives not qualifying for hedge accounting	(50)	(29)
Net cash flow hedge loss transferred to income statement	(12)	(7)
Net loss on available for sale securities transferred to income statement	-	(2)
Gain / (loss) on sale of mortgages to NZ Branch	(1)	1
Other income	34	40
Total other operating income	378	421

NOTES TO THE FINANCIAL STATEMENTS

5. OPERATING EXPENSES

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Personnel		
Salaries and related costs	801	811
Superannuation costs	29	30
Share-based payments expense	15	21
Other	11	32
Total personnel expenses	856	894
Premises		
Depreciation of premises and equipment	32	32
Leasing and rental costs	80	79
Other	41	41
Total premises expenses	153	152
Technology		
Depreciation and amortisation	44	111
Licences and outsourced services	125	116
Other	49	58
Total technology expenses	218	285
Other		
Advertising and public relations	41	42
Amortisation and impairment of other intangible assets	4	5
Freight, stationery, postage and telephone	45	48
Goodwill impairment	3	-
Professional fees	43	45
Travel and entertainment expenses	26	28
Charges from Ultimate Parent Bank	46	64
Other	33	36
Total other expenses	241	268
Total operating expenses	1,468	1,599

NOTES TO THE FINANCIAL STATEMENTS

6. INCOME TAX

	Year to 30/09/2017	Year to 30/09/2016
	NZ\$m	NZ\$m
Reconciliation of the prima facie income tax payable on profit		
Profit before income tax	2,445	2,105
Prima facie income tax at 28%	685	589
Imputed and non-assessable dividends	(1)	(1)
Change in tax provisions	(5)	(5)
Non assessable income and non deductible expenditure	2	(11)
Income tax over provided in prior years	(1)	(2)
Total income tax expense	680	570
Effective tax rate (%)	27.8%	27.1%
Amounts recognised in the income statement		
Current tax	640	582
Deferred tax	40	(12)
Total income tax expense recognised in the income statement	680	570
Imputation credits available	4,196	3,566

The imputation credit balance for the Banking Group includes the imputation credit balance in relation to both the New Zealand Resident imputation group and other companies in the the Banking Group that are not in the New Zealand Resident imputation group. The imputation credit balance available includes imputation credits that will arise from the payment of the amount of provision for income tax as at the reporting date.

NOTES TO THE FINANCIAL STATEMENTS

7. SEGMENT ANALYSIS

The Banking Group is organised into three major business segments for segment reporting purposes - Retail, Commercial and Institutional. Centralised back office and corporate functions support these segments. These segments are consistent with internal reporting provided to the chief operating decision maker, being the Bank's Chief Executive Officer.

Segment reporting has been updated to reflect minor changes to the Banking Group's structure. Comparative data has been adjusted to be consistent with the current year's segment definitions.

Retail

Retail provides products and services to Retail, Private Banking, and Business Banking customers via the branch network, mortgage specialists, relationship managers, the contact centre and a variety of self service channels (internet banking, phone banking, ATMs, website and mobile phone banking). Retail and Private Banking customers have personal banking requirements and Business Banking customers consist primarily of small enterprises with annual revenues of less than NZ\$5 million. Core products and services include current and savings accounts, unsecured lending (credit cards, personal loans and overdrafts), home loans secured by mortgages over property, investment products, superannuation and insurance services.

Commercial

Commercial provides services to Commercial & Agri (CommAgri) and UDC customers. CommAgri customers consist of primarily privately owned medium to large enterprises. Commercial's relationship with these businesses ranges from simple banking requirements with revenue from deposit and transactional facilities, and cash flow lending, to more complex funding arrangements with revenue sourced from a wider range of products. UDC is principally involved in the financing and leasing of plant, vehicles and equipment, mainly for small and medium sized businesses, as well as investment products.

Institutional

Institutional provides financial services through a number of specialised units to large multi-banked corporations, often global, which require sophisticated product and risk management solutions. Those financial services include loan structuring, foreign exchange and interest rate products, wholesale money market services and transaction banking.

Other

Other includes treasury and back office support functions, none of which constitutes a separately reportable segment.

Business segment analysis¹

	Retail	Commercial	Institutional	Other	Total
30/09/2017	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
External interest income	3,430	2,070	699	(1)	6,198
External interest expense	(1,474)	(302)	(338)	(1,047)	(3,161)
Net intersegment interest	(253)	(868)	(1)	1,122	-
Net interest income	1,703	900	360	74	3,037
Other external operating income	688	21	302	(78)	933
Share of associates' profit	5	-	-	-	5
Operating income	2,396	921	662	(4)	3,975
Operating expenses	1,005	259	184	20	1,468
Profit before credit impairment and income tax	1,391	662	478	(24)	2,507
Credit impairment charge / (release)	35	51	(24)	-	62
Profit before income tax	1,356	611	502	(24)	2,445
Income tax expense	379	172	141	(12)	680
Profit after income tax	977	439	361	(12)	1,765
Other information					
Depreciation and amortisation	12	1	-	67	80
Goodwill	1,109	1,052	1,069	-	3,230
Other intangible assets	111	2	-	65	178
Investment in associates	7	-	-	-	7
Total external assets	74,505	42,186	36,259	1,023	153,973
Total external liabilities	68,415	14,176	28,968	29,633	141,192

NOTES TO THE FINANCIAL STATEMENTS

	Retail	Commercial	Institutional	Other	Total
30/09/2016	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
External interest income	3,456	2,202	760	5	6,423
External interest expense	(1,598)	(333)	(403)	(1,087)	(3,421)
Net intersegment interest	(198)	(980)	11	1,167	-
Net interest income	1,660	889	368	85	3,002
Other external operating income	680	19	104	44	847
Share of associates' profit	5	-	-	-	5
Operating income	2,345	908	472	129	3,854
Operating expenses	1,048	256	179	116	1,599
Profit before credit impairment and income tax	1,297	652	293	13	2,255
Credit impairment charge	58	72	20	-	150
Profit before income tax	1,239	580	273	13	2,105
Income tax expense	335	163	77	(5)	570
Profit after income tax	904	417	196	18	1,535
Other information					
Depreciation and amortisation	12	1	-	135	148
Goodwill	1,109	1,052	1,072	-	3,233
Other intangible assets	118	3	-	70	191
Investment in associates	7	-	-	-	7
Total external assets	69,230	41,639	47,883	2,067	160,819
Total external liabilities	63,605	13,364	40,730	30,410	148,109

¹ Intersegment transfers are accounted for and determined on an arm's length or cost recovery basis.

Other segment

The table below sets out the profit/(loss) after tax impact of items included in Other.

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Operations and support	1	3
Economic hedges	(44)	(29)
Revaluation of insurance policies from changes in interest rates	(25)	42
Other	56	2
Total	(12)	18

NOTES TO THE FINANCIAL STATEMENTS

8. NOTES TO THE CASH FLOW STATEMENT

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Reconciliation of profit after income tax to net cash flows provided by / (used in) operating activities		
Profit after income tax	1,765	1,535
Non-cash items:		
Depreciation and amortisation	80	148
Provision for credit impairment	62	150
Deferred fee revenue and expenses	(13)	(7)
Amortisation of capitalised brokerage / mortgage origination fees	164	152
Amortisation of premiums and discounts	89	70
Fair value gains and losses	(160)	31
Loss on disposal and impairment of premises and equipment and intangibles	5	4
Deferrals or accruals of past or future operating cash receipts or payments:		
Change in net operating assets less liabilities	(1,217)	(4,434)
Change in interest receivable	(14)	29
Change in interest payable	17	(43)
Change in accrued expenses	(2)	(71)
Change in provisions	(20)	15
Change in life insurance policy assets	17	(57)
Change in other receivables and payables	(3)	8
Change in net income tax assets / liabilities	75	(78)
Dividends from associates in excess of share of profits	-	(3)
Items classified as investing activities:		
Proceeds from sale of insurance policies	-	(23)
Net cash flows provided by / (used in) operating activities	845	(2,574)

	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Reconciliation of cash and cash equivalents to the balance sheet		
Cash	2,338	2,274
Amounts included in settlement balances receivable / (payable):		
Nostro accounts	170	45
Overdrawn nostro accounts	(69)	(4)
Total cash and cash equivalents	2,439	2,315

NOTES TO THE FINANCIAL STATEMENTS

9. CASH

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Coins, notes and cash at bank	202	193
Securities purchased under agreements to resell	360	229
Balances with central banks	1,776	1,852
Total cash	2,338	2,274

10. TRADING SECURITIES

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Government securities	3,299	5,953
Corporate and financial institution securities	4,364	6,026
Total trading securities	7,663	11,979

11. DERIVATIVE FINANCIAL INSTRUMENTS

The use of derivatives and their sale to customers as risk management products is an integral part of the Banking Group's trading activities. Derivatives are also used to manage the Banking Group's own exposure to fluctuations in exchange and interest rates as part of its own asset and liability management activities.

Derivatives are subject to the same types of credit and market risk as other financial instruments and the Banking Group manages these risks in a consistent manner.

Derivatives, except for those that are specifically designated as effective hedging instruments, are classified as held for trading.

Derivatives held for trading

The held for trading classification includes two categories of derivative instruments: those held as trading positions and those used for the Banking Group's balance sheet risk management.

Trading positions

Trading positions consist of both sales to customers and market making activities. Sales to customers include the structuring and marketing of derivative products to customers which enable them to take or mitigate risks. Market making activities consist of derivatives entered into principally for the purpose of generating profits from short-term fluctuations in price or margins. Positions may be traded actively or held over a period of time to benefit from expected changes in market rates.

Balance sheet risk management

The Banking Group designates certain balance sheet risk management derivatives into hedging relationships in order to minimise income statement volatility. This volatility is created by differences in the timing of recognition of gains and losses between the derivative and the hedged item. Hedge accounting is not applied to all balance sheet risk management positions as some balance sheet risk management derivatives are classified as held for trading.

NOTES TO THE FINANCIAL STATEMENTS

	30/09/2017			30/09/2016		
	Notional principal amount NZ\$m	Fair values Assets NZ\$m	Liabilities NZ\$m	Notional principal amount NZ\$m	Fair values Assets NZ\$m	Liabilities NZ\$m
Derivatives held for trading						
Foreign exchange derivatives						
Spot and forward contracts	105,717	615	696	63,895	650	785
Swap agreements	164,131	1,773	1,895	141,306	1,718	3,157
Options purchased	1,301	17	-	2,379	50	2
Options sold	1,268	2	27	2,248	7	77
	272,417	2,407	2,618	209,828	2,425	4,021
Interest rate derivatives						
Forward rate agreements	33,945	-	-	41,507	1	5
Swap agreements	1,049,894	7,062	6,335	1,178,795	17,910	17,084
Futures contracts	80,583	5	24	78,988	3	46
Options purchased	1,928	3	-	2,366	6	-
Options sold	1,239	-	1	1,603	1	2
	1,167,589	7,070	6,360	1,303,259	17,921	17,137
Commodity derivatives	320	13	14	460	33	32
Total derivatives held for trading	1,440,326	9,490	8,992	1,513,547	20,379	21,190
Derivatives in hedging relationships						
Fair value hedges						
Interest rate swap agreements	42,038	86	618	34,639	238	386
	42,038	86	618	34,639	238	386
Cash flow hedges						
Interest rate swap agreements	22,955	302	216	18,985	493	380
Total derivatives in hedging relationships	64,993	388	834	53,624	731	766
Total derivative financial instruments	1,505,319	9,878	9,826	1,567,171	21,110	21,956

Derivatives in hedging relationships

Fair value hedges

The Banking Group's fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of fixed-rate long-term financial instruments due to movements in market interest rates.

Gain / (loss) on fair value hedges attributable to the hedged risk	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Gain / (loss) arising from fair value hedges:		
- hedged item	153	(45)
- hedging instrument	(159)	46
Net ineffectiveness on qualifying fair value hedges	(6)	1

Cash flow hedges

The Banking Group's cash flow hedges comprise interest rate swaps that are used to protect against exposures to variability in future interest cash flows on non-trading assets and liabilities which bear interest at variable rates or which are expected to be refunded or reinvested in the future. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their forecast repricing profile. This forms the basis for identifying gains and losses on the effective portions of derivatives designated as cash flow hedges.

Analysis of the cash flow hedging reserve	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Deferred gain / (loss) attributable to hedges of:		
Variable rate loan assets	159	296
Short term re-issuances of fixed rate customer and wholesale deposit liabilities	(116)	(234)
Total cash flow hedging reserve	43	62

All underlying hedged cash flows are expected to be recognised in the income statement in the period in which they occur, which is anticipated to take place over the next ten years (2016: ten years).

NOTES TO THE FINANCIAL STATEMENTS

12. AVAILABLE-FOR-SALE ASSETS

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Government securities	4,238	1,195
Corporate and financial institution securities	2,121	1,663
Equity and other securities	1	1
Total available-for-sale assets	6,360	2,859

13. NET LOANS AND ADVANCES

		30/09/2017	30/09/2016
	Note	NZ\$m	NZ\$m
Overdrafts		1,040	1,133
Credit cards outstanding		1,638	1,663
Term loans - housing		72,524	67,298
Term loans - non-housing		44,227	43,651
Finance lease and hire purchase receivables		1,577	1,324
Total gross loans and advances		121,006	115,069
Less: Provision for credit impairment	14	(579)	(622)
Less: Unearned income		(222)	(211)
Add: Capitalised brokerage/mortgage origination fees		334	360
Add: Customer liability for acceptances ¹		-	27
Net loans and advances (including assets classified as held for sale)		120,539	114,623
Less: UDC net loans and advances held for sale	29	(2,912)	-
Net loans and advances		117,627	114,623

¹ Customer liability for acceptances has been recognised in Other assets from 30 September 2017.

The Bank has sold residential mortgages to the NZ Branch with a net carrying value of NZ\$4,337 million as at 30 September 2017 (2016: NZ\$6,020 million). These assets qualify for derecognition as the Bank does not retain a continuing involvement in the transferred assets.

NOTES TO THE FINANCIAL STATEMENTS

14. PROVISION FOR CREDIT IMPAIRMENT

Credit impairment charge / (release)

	30/09/2017				30/09/2016			
	Retail mortgages	Other retail exposures	Non-retail exposures	Total	Retail mortgages	Other retail exposures	Non-retail exposures	Total
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
New and increased provisions	5	94	133	232	16	110	111	237
Write-backs	(16)	(12)	(67)	(95)	(28)	(18)	(30)	(76)
Recoveries	-	(20)	(11)	(31)	-	(22)	(3)	(25)
Individual credit impairment charge / (release)	(11)	62	55	106	(12)	70	78	136
Collective credit impairment charge / (release)	(3)	(9)	(32)	(44)	1	3	10	14
Credit impairment charge / (release)	(14)	53	23	62	(11)	73	88	150

Movement in provision for credit impairment

	30/09/2017				30/09/2016			
	Retail mortgages	Other retail exposures	Non-retail exposures	Total	Retail mortgages	Other retail exposures	Non-retail exposures	Total
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Collective provision								
Balance at beginning of the year	78	130	263	471	77	127	253	457
Charge / (release) to income statement	(3)	(9)	(32)	(44)	1	3	10	14
Balance at end of the year	75	121	231	427	78	130	263	471
Individual provision								
Balance at beginning of the year	37	6	108	151	54	9	91	154
New and increased provisions net of write-backs	(11)	82	66	137	(12)	92	81	161
Bad debts written off	(1)	(82)	(50)	(133)	(2)	(95)	(55)	(152)
Discount unwind ¹	-	-	(3)	(3)	(3)	-	(9)	(12)
Balance at end of the year	25	6	121	152	37	6	108	151
Total provision for credit impairment	100	127	352	579	115	136	371	622

¹ The impairment loss on an impaired asset is calculated as the difference between the asset's carrying amount and the estimated future cash flows discounted to its present value using the original effective interest rate for the asset. This discount unwinds as interest income over the period the asset is held.

Impaired assets

	30/09/2017				30/09/2016			
	Retail mortgages	Other retail exposures	Non-retail exposures	Total	Retail mortgages	Other retail exposures	Non-retail exposures	Total
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Balance at beginning of the year	57	27	342	426	97	32	253	382
Transfers from productive	35	106	430	571	64	129	395	588
Transfers to productive	(17)	(9)	(56)	(82)	(31)	(8)	(7)	(46)
Assets realised or loans repaid	(43)	(22)	(360)	(425)	(71)	(31)	(244)	(346)
Write offs	(1)	(82)	(50)	(133)	(2)	(95)	(55)	(152)
Total impaired assets	31	20	306	357	57	27	342	426
Other assets under administration	8	2	-	10	9	2	-	11
Undrawn facilities with impaired customers	1	-	5	6	-	1	57	58

NOTES TO THE FINANCIAL STATEMENTS

15. DEPOSITS AND OTHER BORROWINGS

	Note	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Term deposits		45,457	39,665
On demand and short term deposits		41,451	42,323
Deposits not bearing interest		8,882	7,780
UDC secured investments	21	1,039	1,592
Total customer deposits		96,829	91,360
Certificates of deposit		1,916	2,237
Commercial paper		3,721	5,364
Securities sold under repurchase agreements		157	76
Deposits from Immediate Parent Company and NZ Branch	30	73	29
Deposits and other borrowings (including liabilities classified as held for sale)		102,696	99,066
Less: UDC secured investments held for sale	29	(1,039)	-
Deposits and other borrowings		101,657	99,066

Deposits from customers, except UDC secured investments, are unsecured and rank equally with other unsecured liabilities of the Banking Group. In the unlikely event that the Bank was put into liquidation or ceased to trade, secured creditors and those creditors set out in Schedule 7 of the Companies Act 1993 would rank ahead of the claims of unsecured creditors.

16. UNSUBORDINATED DEBT

	Note	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Domestic bonds		3,900	3,975
U.S. medium term notes ¹		9,004	6,883
Euro medium term notes ¹		3,173	2,792
Covered bonds ¹	21, 28	5,325	6,218
Total unsubordinated debt issued		21,402	19,868
Fair value hedge adjustment		(53)	192
Less: held by the Bank		(26)	(46)
Total unsubordinated debt		21,323	20,014

¹ This unsubordinated debt is issued by ANZ New Zealand (Int'l) Limited and is guaranteed by the Bank.

Unsubordinated debt, other than covered bonds, is unsecured and ranks equally with other unsecured liabilities of the Banking Group.

NZX Regulation has granted the Bank a waiver from NZX Debt Market Listing Rule (Rule) 7.12.1 to the extent that this Rule requires the Bank to release to the market details of any acquisition of the Bank's domestic bonds as a result of its market-making activities or trading on behalf of its clients. The Bank will notify the NZX if any such domestic bonds are subsequently cancelled. Rule 7.12.1 does not extend to the Bank's subsidiaries in this context. The Bank will continue to comply with Rule 7.12.1 in respect of any domestic bonds that are issued, redeemed or purchased by the Bank in any other capacity.

Domestic bonds includes three series of bonds quoted on the NZX Debt Market which mature on 22 March 2019, 2 September 2021 and 1 September 2023 respectively (the Bonds). NZX Regulation has granted the Bank waivers from the requirement in Rule 5.2.3 (as modified by NZX Regulation's Ruling on Rule 5.2.3 issued on 29 September 2015) for the Bonds to be held by at least 100 members of the public holding at least 25% of the Bonds issued (Spread). The effect of these waivers is that the Bonds may not be widely held and there may be reduced liquidity in the Bonds. If there is a material reduction in the Spread of the Bonds, the Bank will notify NZX as appropriate.

NOTES TO THE FINANCIAL STATEMENTS

17. SUBORDINATED DEBT

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
ANZ Capital Notes¹		
NZD 500m ANZ New Zealand Capital Notes (ANZ NZ CN) ²	497	496
NZD 1,003m ANZ New Zealand Internal Capital Notes (ANZ NZ ICN)	1,003	1,003
NZD 938m ANZ New Zealand Internal Capital Notes 2 (ANZ NZ ICN2)	938	938
Perpetual subordinated debt		
NZD 835m perpetual subordinated bond ³	835	835
AUD 10m perpetual subordinated floating rate loan	10	10
Total subordinated debt	3,283	3,282

¹ These instruments qualify as additional tier 1 capital.

² These instruments are quoted on the NZX Debt Market.

³ These instruments are quoted on the NZX Debt Market, and qualify as tier 2 capital, subject to the RBNZ's Basel III transition adjustment. Refer to note 26 for further details.

Subordinated debt is subordinated in right of payment in the event of liquidation or wind up to the claims of depositors and all creditors of the relevant issuer or drawer of the debt.

ANZ Capital Notes

- On 5 March 2015, the Bank issued 10.03 million convertible notes (ANZ NZ ICN) to the NZ Branch at NZ\$100 each, raising NZ\$1,003 million.
- On 31 March 2015, the Bank issued 500 million convertible notes (ANZ NZ CN) at NZ\$1 each, raising NZ\$500 million before issue costs.
- On 15 June 2016, the Bank issued 9.38 million convertible notes (ANZ NZ ICN2) to the NZ Branch at NZ\$100 each, raising NZ\$938 million.

ANZ Capital Notes (the notes) are fully paid convertible non-cumulative perpetual subordinated notes.

As at 30 September 2017, ANZ NZ CN carried a BB+ credit rating from Standard and Poor's.

The notes are classified as debt given there are circumstances beyond the Bank's control where the principal is converted into a variable number of shares of the Bank (ANZ NZ ICN and ANZ NZ ICN2) or the Ultimate Parent Bank (ANZ NZ CN).

Interest

Interest on the notes is non-cumulative and payable as follows:

- ANZ NZ ICN: payable semi-annually in arrears in March and September in each year. The interest rate is based on a floating rate equal to the aggregate of the New Zealand 6 month bank bill rate plus a 380 basis point margin.
- ANZ NZ CN: payable quarterly in arrears in February, May, August and November in each year. The interest rate is fixed at 7.2% per annum until 25 May 2020, and thereafter will be based on a floating rate equal to the aggregate of the New Zealand 3 month bank bill rate plus a 350 basis point margin.
- ANZ NZ ICN2: payable semi-annually in arrears in June and December in each year. The interest rate is based on a floating rate equal to the aggregate of the New Zealand 6 month bank bill rate plus a 629 basis point margin.

Interest payments are subject to the Bank's absolute discretion and certain payment conditions being satisfied (including RBNZ and APRA (ANZ NZ CN only) requirements). If interest is not paid on the notes the Bank may not, except in limited circumstances, pay dividends or undertake a share buy-back or other capital reduction on its ordinary shares until interest is next paid.

Conversion features

On 24 March 2025 (ANZ NZ ICN) or 25 May 2022 (ANZ NZ CN) or an earlier date under certain circumstances, the relevant notes will mandatorily convert into a variable number of ordinary shares of the:

- Bank based on the net assets per share in the Bank's most recently published Disclosure Statement (ANZ NZ ICN) or
- Ultimate Parent Bank based on the average market price of the Ultimate Parent Bank's ordinary shares over a specified period prior to conversion less a 1% discount (ANZ NZ CN).

The mandatory conversion will be deferred for a specified period if the conversion tests are not met.

The Bank will be required to convert some or all of the notes if a common equity capital trigger event, or an RBNZ or APRA (ANZ NZ CN only) non-viability trigger event occurs. The ANZ NZ ICN and ANZ NZ ICN2 will convert into ordinary shares of the Bank and the ANZ NZ CN will convert into ordinary shares of the Ultimate Parent Bank, subject to a maximum conversion number.

NOTES TO THE FINANCIAL STATEMENTS

A common equity capital trigger event occurs if the:

- Banking Group's common equity tier 1 capital ratio is equal to or less than 5.125% or
- Overseas Banking Group's Level 2 common equity tier 1 capital ratio is equal to or less than 5.125% (ANZ NZ CN only).

An RBNZ non-viability trigger event occurs if the RBNZ directs the Bank to convert or write off the notes or a statutory manager is appointed to the Bank and decides the Bank must convert or write off the notes. An APRA non-viability trigger event occurs if APRA notifies the Ultimate Parent Bank that, without the conversion or write-off of certain securities or a public sector injection of capital (or equivalent support), it considers that the Ultimate Parent Bank would become non-viable.

On 25 May 2020 the Bank has the right, subject to satisfying certain conditions, to redeem (subject to receiving RBNZ's and APRA's prior approval), or to convert into ordinary shares of the Ultimate Parent Bank, all or some of the ANZ NZ CN at its discretion on similar terms as mandatory conversion.

On 24 March 2023 the Bank has the right, subject to satisfying certain conditions, to redeem (subject to receiving RBNZ's prior approval), or to convert into ordinary shares of the Bank, all or some of the ANZ NZ ICN at its discretion on similar terms as mandatory conversion.

On 15 June 2026 and each 5th anniversary thereafter the Bank has the right, subject to satisfying certain conditions, to redeem (subject to receiving RBNZ's prior approval), all or some of the ANZ NZ ICN2 at its discretion.

Rights of holders in event of liquidation

The notes rank equally with each other and with the Bank's preference shares and lower than perpetual subordinated debt. Holders of the notes do not have any right to vote in general meetings of the Bank.

Perpetual subordinated debt

Perpetual subordinated debt instruments are classified as debt reflecting an assessment of the key terms and conditions of the instruments, and an assessment of the ability, and likelihood of interest payments being deferred. Certain of these instruments have interrelationships that have been considered in this assessment.

NZD 835,000,000 bond

This bond was issued by the Bank on 18 April 2008.

The Bank may elect to redeem the bond on 18 April 2018 (the Call Date) or any interest payment date subsequent to 18 April 2018. Interest is payable semi-annually in arrears on 18 April and 18 October each year, up to and including the Call Date and then quarterly thereafter. Should the bond not be called at the Call Date, the Coupon Rate from the Call Date onwards will be based on a floating rate equal to the aggregate of the 3 month bank bill rate plus a 300 basis point margin.

As at 30 September 2017, this bond carried a BBB rating by Standard and Poor's and a Baa1 rating by Moody's.

The coupon interest on the bond is 5.28% per annum until 18 April 2018.

AUD 10,000,000 loan

This loan was drawn down by the Bank on 27 March 2013 and has no fixed maturity. Interest is payable semi-annually in arrears on 15 March and 15 September each year. The Bank may repay the loan on any interest payment date after the NZD 835,000,000 bond has been repaid in full.

Coupon interest is based on a floating rate equal to the aggregate of the Australian 6 month bank bill rate plus a 240 basis point margin, increasing to the Australian 6 month bank bill rate plus a 440 basis point margin from 15 September 2018.

NOTES TO THE FINANCIAL STATEMENTS

18. FINANCIAL RISK MANAGEMENT

Strategy in using financial instruments

Financial instruments are fundamental to the Banking Group's business, constituting the core element of its operations. Accordingly, the risks associated with financial instruments are a significant component of the risks faced by the Banking Group. Financial instruments create, modify or reduce the credit, market and liquidity risks of the Banking Group's balance sheet. The Banking Group's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the financial performance of the Banking Group.

The risk management and policy control framework applicable to the entities comprising the Banking Group has been set by the Board and Risk Committee of the Bank or the Ultimate Parent Bank, as appropriate. Likewise oversight and monitoring of material risk exposures of the Banking Group is undertaken by the Risk Management functions of the Bank and also the Ultimate Parent Bank. Throughout this document, references to the Risk Management of the operations within the entities comprising the Banking Group, implicitly involves oversight by both related entities.

Credit risk

Credit risk is the risk of financial loss from counterparties being unable to fulfil their contractual obligations. The Banking Group assumes credit risk in a wide range of lending and other activities in diverse markets and many jurisdictions. Credit risks arise not only from traditional lending to customers, but also from inter-bank, treasury, international trade and capital market activities around the world.

Credit risk incorporates the risks associated with the Banking Group lending to customers who could be impacted by climate change or by changes to laws, regulations, or other policies adopted by governments or regulatory authorities, including carbon pricing and climate change adaptation or mitigation policies.

The Banking Group has an overall lending objective of sound growth for appropriate returns. The credit risk objectives of the Banking Group are set by the Board and are implemented and monitored within a tiered structure of delegated authority, designed to oversee multiple facets of credit risk, including business writing strategies, credit policies/controls, single exposures, portfolio monitoring and risk concentrations.

Credit risk management

A credit risk management framework is in place across the Banking Group with the aim of ensuring a structured and disciplined approach is maintained in achieving the objectives set by the Board. The framework focuses on policies, people, skills, controls, risk concentrations and portfolio balance. It is supported by portfolio analysis and business-writing strategies, which guide lending decisions and identify segments of the portfolio requiring attention. The effectiveness of the framework is monitored through a series of compliance and reporting processes.

An independent Risk Management function is staffed by risk specialists. In regard to credit risk management, the objective is for Risk Management to provide robust credit policies, to make independent credit decisions, and to provide strong support to front line staff in the application of sound credit practices. In addition to providing independent credit assessment on lending decisions, Risk Management also performs key roles in portfolio management by development and validation of credit risk measurement systems, loan asset quality reporting, and development of credit standards and policies.

The credit risk management framework is top down. The framework is defined by the Banking Group's credit principles and policies. The effectiveness of the credit risk management framework is validated through the compliance and monitoring processes.

Risk Management's responsibilities for credit risk policy and management are executed through dedicated departments, which support the business units. All major business unit credit decisions require approval from both business writers and independent risk personnel.

Credit risk is controlled through a combination of approvals, limits, reviews and monitoring procedures that are carried out on a regular basis, the frequency of which is dependent upon the level of risk. Credit risk policy and management is executed through the Chief Risk Officer, who is responsible for various dedicated areas within the Risk Management division. Wholesale Risk services the Banking Group's commercial, investment banking and rural lending activities through dedicated teams. Retail Risk services the Banking Group's small business and consumer customers. The Credit Reporting team within Risk Management provides an independent overview of credit risk across the Bank at a portfolio level. The Banking Group allows sole discretion for transaction approvals at the business unit level in both the retail and wholesale lending sectors, with larger transactions approved by Retail Risk and Wholesale Risk.

Credit risk review function Group Credit Assurance also provides a further independent check mechanism to ensure the quality of credit decisions. This includes providing independent periodic checks on asset quality and compliance with the agreed standards and policies across the Banking Group.

NOTES TO THE FINANCIAL STATEMENTS

Country risk management

Some customer credit risks involve country risk, whereby actions or events at a national or international level could disrupt servicing of commitments. Country risk arises when payment or discharge of an obligation will, or could, involve the flow of funds from one country to another or involve transactions in a currency other than the domestic currency of the relevant country.

Country ratings are assigned to each country where the Banking Group incurs country risk and have a direct bearing on the Banking Group's risk appetite for each country. The country rating is determined through a defined methodology based around external ratings agencies' ratings and internal specialist opinion. It is also a key risk consideration in the Banking Group's capital pricing model for cross border flows.

The recording of country limits provides the Banking Group with a means to identify and control country risk. Country limits ensure that there is a country-by-country ceiling on exposures that involve country risk. They are recorded by time to maturity and purpose of exposure, e.g., trade, markets and project finance. Country limits are managed centrally by the Ultimate Parent Bank, through a global country risk exposure management system managed by a specialist unit within Institutional Risk.

Portfolio stress testing

Stress testing is integral to strengthening the predictive approach to Risk Management and is a key component to managing risk appetite and business writing strategies. It creates greater understanding of impacts on financial performance through modelling relationships and sensitivities between geographic, industry and business unit exposures under a range of macro economic scenarios.

The Ultimate Parent Bank has a dedicated stress testing team that assists business and risk executives in the Banking Group to model and report periodically to management and the Board Risk Committee on a range of scenarios and stress tests.

Portfolio analysis and reporting

Credit portfolios are actively monitored at each layer of the risk structure to ensure credit deterioration is quickly detected and mitigated through the implementation of remediation strategies.

Businesses incurring credit risk undertake regular and comprehensive analysis of their credit portfolios. Issue identification and adherence to performance benchmarks are reported to Risk Management and business executives through a series of reports including monthly 'asset quality' reporting. This process is undertaken by or overseen by Risk Management ensuring an efficient and independent conduit exists to identify and communicate emerging credit issues to Banking Group executives and the Board.

Collateral management

Banking Group credit principles specify lending only what the counterparty has the capacity and ability to repay and the Banking Group sets limits on the acceptable level of credit risk. Acceptance of credit risk is firstly based on the counterparty's assessed capacity to meet contractual obligations (ie interest and capital repayments). Obtaining collateral is only used to mitigate credit risk. Procedures are designed to ensure collateral is managed, legally enforceable, conservatively valued and adequately insured where appropriate. Banking Group policy sets out the types of acceptable collateral, including:

- Cash
- Mortgages over property
- Charges over business assets, eg premises, stock and debtors
- Charges over financial instruments, eg debt securities and equities in support of trading facilities
- Financial guarantees.

In the event of customer default, any loan security is usually held as mortgagee in possession while action is taken to realise it. Therefore the Banking Group does not usually hold any real estate or other assets acquired through the enforcement of security.

The Banking Group uses International Swaps and Derivatives Association Master Agreements (ISDA) to document derivatives' activities to limit exposure to credit losses. The credit risk is reduced by a master agreement to the extent that, if an event of default occurs, all contracts with the counterparty are terminated and settled on a net basis. Further, it is the Banking Group's preferred practice to include all products covered by the ISDA in the Credit Support Annex (CSA) in order to achieve further credit exposure reduction. Under a CSA, collateral is passed between the parties, depending on the aggregate mark-to-market (positive or negative) of derivative trades between the two entities, to mitigate the market contingent counterparty risk inherent in the outstanding positions.

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Concentrations of credit risk

Concentrations of credit risk arise when a number of customers are engaged in similar business activities or activities within the same geographic region, or when they have similar risk characteristics that would cause their ability to meet contractual obligations to be similarly affected by changes in economic or other conditions.

The Banking Group monitors its portfolios to identify and assess risk concentrations. Concentration limits are used to guard against large single customer or correlated credit risks. Risk Management, Business Unit executives and senior management monitor large exposure concentrations through a monthly list of the Banking Group's top corporate exposures. The ANZ Credit and Market Risk Committee and Board Risk Committee regularly review a comprehensive list of single customer concentration limits and customers' adherence to these limits.

Analysis of financial assets by industry sector is based on Australian and New Zealand Standard Industrial Classification (ANZSIC) codes. The significant categories shown are the level one New Zealand Standard Industry Output Categories (NZSIOC), except that Agriculture is shown separately as required by the Order.

The presentation of these tables has changed from previous periods to align this disclosure with the classifications in the data series S34 – *Banks: Assets – Loans by industry* published by the RBNZ. This series uses ANZSIC 2006 industry classifications rather than ANZSIC 1996 that were previously used. Updated corresponding amounts as at 30 September 2016 have been provided for comparative purposes. The most significant changes to the 30 September 2016 amounts from the previous presentation are:

- 1 Industry classification is now shown separately for New Zealand residents and non-New Zealand residents
- 2 The reduction in exposures to households, previously described as personal lending, is due to the reclassification of loans secured by rental properties to the relevant customer's industry, of which the majority are now included in rental, hiring and real estate services.

30/09/2017	Cash, settlements receivable and collateral paid NZ\$m	Trading securities and available-for- sale assets NZ\$m	Derivative financial instruments NZ\$m	Net loans and advances ³ NZ\$m	Other financial assets NZ\$m	Credit related commitments ⁴ NZ\$m	Total NZ\$m
New Zealand residents							
Agriculture	-	-	25	17,686	58	1,436	19,205
Forestry and fishing, agriculture services	-	-	1	1,277	4	240	1,522
Manufacturing	-	14	146	2,729	9	1,798	4,696
Electricity, gas, water and waste services	-	15	437	1,602	5	1,522	3,581
Construction	-	-	13	1,635	5	1,119	2,772
Wholesale trade	-	-	49	1,630	5	1,357	3,041
Retail trade and accommodation	-	1	17	3,058	10	1,133	4,219
Transport, postal and warehousing	-	9	55	1,440	5	894	2,403
Finance and insurance services	2,296	1,709	925	903	338	1,259	7,430
Public administration and safety ¹	-	7,477	621	412	1	794	9,305
Rental, hiring & real estate services	-	-	114	30,697	104	3,699	34,614
Professional, scientific, technical, administrative and support services	-	1	5	1,267	4	619	1,896
Households	-	-	-	51,554	180	11,878	63,612
All other New Zealand residents ²	-	5	240	2,625	8	1,474	4,352
	2,296	9,231	2,648	118,515	736	29,222	162,648
Overseas							
Finance and insurance services	1,795	4,325	7,006	123	-	155	13,404
Households	-	-	-	1,454	5	-	1,459
All other non-NZ residents	-	467	224	914	3	-	1,608
	1,795	4,792	7,230	2,491	8	155	16,471
Less: Provision for credit impairment	-	-	-	(495)	-	(84)	(579)
Less: Unearned income	-	-	-	(222)	-	-	(222)
Add: Capitalised brokerage / mortgage origination fees	-	-	-	334	-	-	334
Total financial assets	4,091	14,023	9,878	120,623	744	29,293	178,652

NOTES TO THE FINANCIAL STATEMENTS

30/09/2016	Cash, settlements receivable and collateral paid NZ\$m	Trading securities and available-for-sale assets NZ\$m	Derivative financial instruments NZ\$m	Net loans and advances ³ NZ\$m	Other financial assets NZ\$m	Credit related commitments ⁴ NZ\$m	Total NZ\$m
New Zealand residents							
Agriculture	-	-	23	17,779	58	1,366	19,226
Forestry and fishing, agriculture services	-	-	21	1,231	4	242	1,498
Manufacturing	-	12	185	3,555	12	2,012	5,776
Electricity, gas, water and waste services	-	21	642	1,298	4	1,255	3,220
Construction	-	-	17	1,579	5	1,030	2,631
Wholesale trade	-	-	23	1,645	5	1,596	3,269
Retail trade and accommodation	-	-	63	3,059	10	1,110	4,242
Transport, postal and warehousing	-	5	91	1,380	5	924	2,405
Finance and insurance services	2,931	2,569	1,186	807	281	1,202	8,976
Public administration and safety ¹	-	7,028	1,049	352	5	750	9,184
Rental, hiring & real estate services	-	-	75	28,230	96	3,562	31,963
Professional, scientific, technical, administrative and support services	-	-	9	1,154	4	734	1,901
Households	-	-	-	47,923	172	11,486	59,581
All other New Zealand residents ²	-	46	244	2,529	8	2,305	5,132
	2,931	9,681	3,628	112,521	669	29,574	159,004
Overseas							
Finance and insurance services	1,856	4,703	17,470	95	-	183	24,307
Households	-	-	-	1,353	5	-	1,358
All other non-NZ residents	-	454	12	1,127	4	-	1,597
	1,856	5,157	17,482	2,575	9	183	27,262
Less: Provision for credit impairment	-	-	-	(518)	-	(104)	(622)
Less: Unearned income	-	-	-	(211)	-	-	(211)
Add: Capitalised brokerage / mortgage origination fees	-	-	-	360	-	-	360
Total financial assets	4,787	14,838	21,110	114,727	678	29,653	185,793

¹ Public administration and safety includes exposures to local government administration and central government administration, defence and public safety.

² Other includes exposures to mining, information media and telecommunications, education and training, health care and social assistance and arts, recreation and other services.

³ Excludes individual and collective provisions for credit impairment held in respect of credit related commitments.

⁴ Credit related commitments comprise undrawn facilities, customer contingent liabilities and letters of offer.

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Maximum exposure to credit risk

The following table presents the maximum exposure to credit risk for on and off balance sheet financial instruments before taking account of the financial effect of any collateral held or other credit enhancements, unless such collateral meets the offsetting criteria in NZ IAS 32 *Financial Instruments: Presentation*.

The table also provides a quantification of the value of the financial charges the Banking Group holds over a borrower's specific asset (or assets) where the Banking Group is able to enforce the collateral in satisfying a debt in the event of the borrower failing to meet its contractual obligations. For the purposes of this disclosure, where the collateral held is valued at more than the corresponding credit exposure, the financial effect is capped at the value of the credit exposure. In respect of derivative financial instruments, the assessed collateral is the amount of cash collateral received and does not include the effect of any netting arrangements under ISDAs.

The assignable value of credit mitigants, such as guarantees and security interests over the assets of a customer's business, is less certain and their financial effect has not been quantified for disclosure purposes. Credit exposures shown as not fully secured may benefit from such credit mitigants.

	30/09/2017			30/09/2016		
	Maximum exposure to credit risk	Financial effect of collateral	Unsecured portion of credit exposure	Maximum exposure to credit risk	Financial effect of collateral	Unsecured portion of credit exposure
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
On and off-balance sheet positions						
Cash	2,140	360	1,780	2,081	229	1,852
Settlement balances receivable	536	266	270	396	265	131
Collateral paid	1,415	-	1,415	2,310	-	2,310
Trading securities	7,663	-	7,663	11,979	-	11,979
Derivative financial instruments	9,878	613	9,265	21,110	529	20,581
Available-for-sale assets	6,360	-	6,360	2,859	-	2,859
Net loans and advances	120,623	110,914	9,709	114,727	104,399	10,328
Other financial assets	744	378	366	678	361	317
Credit related commitments	29,293	14,526	14,767	29,653	15,193	14,460
Total exposure to credit risk	178,652	127,057	51,595	185,793	120,976	64,817

Credit quality

A core component of the Banking Group's credit risk management capability is the risk grading framework used across all major business units. A set of risk grading principles and policies is supported by a complementary risk grading methodology. Pronouncements by the International Basel Committee on Banking Supervision have been encapsulated in these principles and policies, including governance, validation and modelling requirements.

The Banking Group's risk grade profile changes dynamically through new counterparty lending and existing counterparty movements in either risk or volume. All counterparty risk grades are subject to frequent review, including statistical and behavioural reviews in consumer and small business segments, and individual counterparty reviews in segments with larger single name borrowers.

Impairment and provisioning of financial assets

The Banking Group's policy relating to the recognition and measurement of impaired assets conforms to the RBNZ's guidelines.

Loans are classified as either performing or impaired. Impaired assets are credit exposures where: there is doubt as to whether the full contractual amount (including interest) will be received; a material credit obligation is 90 days past due but not well secured; they are portfolio managed and can be held for up to 180 days past due; or concessional terms have been provided due to the financial difficulties of the customer.

An exposure is classified as past due but not impaired (less than 90 days) where the value of collateral is sufficient to repay both the principal debt and all other potential interest or there is no concern as to the creditworthiness of the counterparty in question.

The past due but not impaired (over 90 days) classification applies where contractual payments are past due by 90 days or more, or where the facility remains outside of contractual arrangements for 90 or more consecutive days, but the Banking Group believes that impairment is not appropriate on the basis of the level of security/collateral available, or the facility is portfolio managed.

The provision for credit impairment represents management's best estimate of the losses incurred in the loan portfolio at balance date based on its experienced judgement.

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Distribution of gross loans and advances assets by credit quality

The credit quality of the portfolio of loans and advances is assessed by reference to the Banking Group's risk grading principles and policies supported by a complementary risk grading methodology.

	30/09/2017				30/09/2016			
	Retail mortgages	Other retail exposures	Non-retail exposures	Total	Retail mortgages	Other retail exposures	Non-retail exposures	Total
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Strong risk rating	59,574	1,330	20,922	81,826	57,203	1,263	20,248	78,714
Satisfactory risk rating	9,135	3,153	21,995	34,283	6,335	2,997	22,309	31,641
Substandard but not past due or impaired	480	435	1,643	2,558	325	539	1,928	2,792
Total neither past due nor impaired	69,189	4,918	44,560	118,667	63,863	4,799	44,485	113,147
Past due but not impaired:								
1 to 5 days	375	113	543	1,031	337	125	350	812
6 to 29 days	181	74	99	354	131	73	42	246
1 to 29 days	556	187	642	1,385	468	198	392	1,058
30 to 59 days	85	34	171	290	109	32	62	203
60 to 89 days	95	18	12	125	82	17	6	105
90 days and over	132	31	19	182	81	26	23	130
Total past due but not impaired	868	270	844	1,982	740	273	483	1,496
Total impaired assets	31	20	306	357	57	27	342	426
Gross loans and advances	70,088	5,208	45,710	121,006	64,660	5,099	45,310	115,069

Credit quality of gross loans and advances neither past due nor impaired

The credit quality of financial assets is assessed by the Banking Group using internal ratings which aim to reflect the relative ability of counterparties to fulfil, on time, their credit-related obligations, and is based on their current probability of default.

Internal ratings

Strong risk rating - Corporate customers demonstrating superior stability in their operating and financial performance over the long-term, and whose debt servicing capacity is not significantly vulnerable to foreseeable events. Retail customers with low expected loss. This rating band broadly corresponds to ratings "Aaa" to "Ba1" and "AAA" to "BB+" of Moody's Investors Service and Standard & Poor's respectively.

Satisfactory risk rating - Corporate customers consistently demonstrating sound operational and financial stability over the medium to long term, even though some may be susceptible to cyclical trends or variability in earnings. Retail customers with moderate expected loss. This rating band broadly corresponds to ratings "Ba2" to "B1" and "BB" to "B+" of Moody's Investors Service and Standard & Poor's respectively.

Substandard but not past due or impaired - Corporate customers demonstrating some operational and financial instability, with variability and uncertainty in profitability and liquidity projected to continue over the short and possibly medium term. Retail customers with higher expected loss. This rating band broadly corresponds to ratings "B2" to "Caa" and "B" to "CCC" of Moody's Investors Service and Standard & Poor's respectively.

Movements in the rating categories between balance dates are due to both changes in the underlying internal ratings applied to customers and to new loans written or loans rolling off.

Credit quality of financial assets that are past due but not impaired

Ageing analysis of past due loans is used by the Banking Group to measure and manage credit quality. Financial assets that are past due but not impaired include those:

- Assessed, approved and managed on a portfolio basis within a centralised environment (for example, credit cards and personal loans)
- Held on a productive basis until they are 180 days past due
- Managed on an individual basis.

A large portion of retail credit exposures, such as residential mortgages, are generally well secured. That is, the fair value of associated security is sufficient to ensure that the Banking Group will recover the entire amount owing over the life of the facility and there is reasonable assurance that collection efforts will result in payment of the amounts due in a timely manner.

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Market risk

Market risk is the risk to the Banking Group's earnings arising from changes in interest rates, currency exchange rates, credit spreads, or from fluctuations in bond, commodity or equity prices. Market risk is generated through both trading activities and the interest rate risk inherent in the banking book.

The Banking Group conducts trading operations in interest rates, foreign exchange, commodities and debt securities.

The Banking Group has a detailed risk management and control framework to support its trading and balance sheet management activities. The framework incorporates a risk measurement approach to quantify the magnitude of market risk within trading and balance sheet portfolios. This approach, and related analysis, identifies the range of possible outcomes that can be expected over a given period of time, establishes the relative likelihood of those outcomes and allocates an appropriate amount of capital to support these activities.

Market risk management and control responsibilities

The Board Risk Committee has delegated responsibility for the oversight of market risk to the Asset & Liability Committee (ALCO), chaired by the Chief Financial Officer of the Bank. ALCO is required to ensure that market risk exposure across Traded and Non-Traded portfolios remains within the risk appetite specified by the Board Risk Committee. ALCO receives regular reporting on a range of trading and balance sheet market risk exposures.

The Risk Management division of the Banking Group, through the Chief Risk Officer, is responsible for the day-to-day oversight of market risk. This includes the implementation of a comprehensive limit and policy framework to control the amount of risk that the Banking Group will accept. Market risk limits are allocated at various levels and are reported and monitored on a daily basis. The detailed limit framework allocates individual limits to manage and control asset classes (e.g., interest rates, foreign exchange), risk factors (e.g., interest rates, volatilities) and profit and loss limits (to monitor and manage the performance of the trading portfolios).

Additional oversight and monitoring of material risk exposures of the Banking Group is undertaken by the Risk Management functions of the Ultimate Parent Bank.

Within overall strategies and policies, the control of market risk is the joint responsibility of business units and Risk Management, with the delegation of market risk limits from the Board Risk Committee to both Risk Management and the business units.

These risks are monitored daily against a comprehensive limit framework that includes Value at Risk, aggregate market position and sensitivity, product and geographic thresholds. To facilitate the management, control, measurement and reporting of market risk, the Banking Group has grouped market risk into two broad categories:

a. *Traded market risk*

This is the risk of loss from changes in the value of financial instruments due to movements in price factors for both physical and derivative trading positions. They arise in trading transactions where the Banking Group acts as principal with clients or with the market. The primary risk categories monitored are:

- Currency risk is the potential loss arising from the decline in the value of a financial instrument due to changes in foreign exchange rates or their implied volatilities.
- Interest rate risk is the potential loss arising from the change in the value of a financial instrument due to changes in market interest rates or their implied volatilities.
- Credit spread risk is the potential loss arising from a change in value of an instrument due to a movement of its margin or spread relative to a bench mark.

b. *Non-traded market risk (or balance sheet risk)*

This comprises the management of non-traded interest rate risk, liquidity, and the risk to capital and earnings as a result of movements in market rates.

Some instruments do not fall into either category but also expose the Banking Group to market risk. These include equity securities classified as available-for-sale. Regular reviews are performed to substantiate the valuation of these types of instruments.

In all trading areas the Banking Group has implemented models that calculate Value at Risk (VaR) exposures, monitor risk exposures against defined limits on a daily basis, and "stress test" trading portfolios.

VaR measure

A key measure of market risk is VaR. VaR is a statistical estimate of the likely daily loss and is based on historical market movements.

The confidence level is such that there is a 99% probability that the loss will not exceed the VaR estimate on any given day. Conversely there is 1% probability of the decrease in market value exceeding the VaR estimate on any given day.

The Banking Group's standard VaR approach for both traded and non-traded risk is historical simulation. The Banking Group calculates VaR using historical changes in market rates and prices over the previous 500 business days. Traded and Non-Traded VaR is calculated using a one-day holding period.

NOTES TO THE FINANCIAL STATEMENTS

It should be noted that because VaR is driven by actual historical observations, it is not an estimate of the maximum loss that the Banking Group could experience from an extreme market event. As a result of this limitation, the Banking Group utilises a number of other risk measures (e.g. stress testing) and associated detailed control limits to measure and manage market risk.

Traded market risks

	30/09/2017				30/09/2016			
	Value at risk at 99% confidence				Value at risk at 99% confidence			
	Period end	High for	Low for	Average for	Period end	High for	Low for	Average for
	NZ\$m	year	year	year	NZ\$m	year	year	year
		NZ\$m	NZ\$m	NZ\$m		NZ\$m	NZ\$m	NZ\$m
Foreign exchange risk	0.1	1.2	0.1	0.4	0.2	0.9	0.1	0.4
Interest rate risk	3.0	5.8	1.3	2.5	2.1	4.9	1.3	2.6
Credit spread risk	0.6	0.8	0.4	0.6	0.5	0.7	0.3	0.5
Diversification benefit	(0.9)	n/a	n/a	(0.9)	(0.7)	n/a	n/a	(1.0)
Total VaR	2.8	5.3	1.4	2.6	2.1	4.4	1.3	2.5

Traded market risk VaR is calculated separately for foreign exchange and for interest rate/debt markets businesses as well as for the Banking Group. The diversification benefit reflects the historical correlation between foreign exchange, interest rate and debt markets.

To supplement the VaR methodology, the Banking Group applies a wide range of stress tests, both on individual portfolios and at the Banking Group level. The Banking Group's stress-testing regime provides senior management with an assessment of the financial impact of identified extreme events on market risk exposures of the Banking Group.

Non-traded market risk (or balance sheet risk)

The principal objectives of balance sheet management are to manage net interest income sensitivity while maintaining acceptable levels of interest rate and liquidity risk and to manage the market value of the Banking Group's capital. Liquidity risk is dealt with in the next section.

Interest rate risk

The objective of balance sheet interest rate risk management is to mitigate the negative impact of movements in wholesale interest rates on the earnings of the Banking Group's banking book. Non-traded interest rate risk relates to the potential adverse impact to earnings from changes in market interest rates. This risk arises from two principal sources: mismatches between the repricing dates of interest bearing assets and liabilities; and the investment of capital and other non-interest bearing liabilities in interest bearing assets.

As part of normal business activity the Banking Group has additional risks from fixed rate mortgage prepayments and basis risk:

- Prepayment risk is the potential risk to earnings or market value from when a customer prepays all or part of a fixed rate loan and where any customer fee charged is not sufficient to offset the loss in value to the Banking Group of this financial asset due to movements in interest rates and other pricing factors. As far as possible the true economic cost is passed through to customers in line with their terms and conditions and relevant legislation.
- Basis risk is the potential risk to earnings or market value from differences between customer pricing and wholesale market pricing. This is managed through active review of product margins.

Non-traded interest rate risk is managed to both value and earnings at risk limits. Interest rate risk is reported using three measures: VaR; scenario analysis (to a 1% shock); and interest rate sensitivity gap. This treatment excludes the effect of prepayment and basis risk.

a. Non-traded interest rate risk VaR

	Period end	High for	Low for	Average for
	NZ\$m	year	year	year
		NZ\$m	NZ\$m	NZ\$m
30/09/2017				
Value at risk at 99% confidence	8.3	10.2	7.3	8.2
30/09/2016				
Value at risk at 99% confidence	9.7	10.3	7.7	8.9

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b. Scenario analysis – a 1% shock on the next 12 months' net interest income

A 1% overnight parallel positive shift in the yield curve is modelled to determine the potential impact on net interest income over the succeeding 12 months. This is a standard risk quantification tool.

The figures in the table below indicate the outcome of this risk measure for the current and comparative periods – expressed as a percentage of reported net interest income. The sign indicates the nature of the rate sensitivity with a positive number signifying that a rate increase is positive for net interest income over the next 12 months. Conversely, a negative number signifies that a rate increase is negative for the next 12 months' net interest income.

	30/09/2017	30/09/2016
Impact of 1% rate shock		
Period end	0.6%	0.4%
Maximum exposure	0.9%	1.6%
Minimum exposure	-0.3%	-0.2%
Average exposure (in absolute terms)	0.4%	0.7%

The extent of mismatching between the repricing characteristics and timing of interest bearing assets and liabilities at any point has implications for future net interest income.

Interest rate sensitivity gap

The interest rate sensitivity gap analysis provides information about the Banking Group's exposure to interest rate risk.

Sensitivity to interest rates arises from mismatches in the period to repricing of assets and that of the corresponding liability funding. These mismatches are managed within policy guidelines for mismatch positions.

The following tables represent the interest rate sensitivity of the Banking Group's assets, liabilities and off balance sheet instruments by showing the periods in which these instruments may reprice (that is, when interest rates applicable to each asset or liability can be changed).

The repricing gaps are based upon contractual repricing.

30/09/2017	Total NZ\$m	Up to 3 months NZ\$m	Over 3 to 6 months NZ\$m	Over 6 to 12 months NZ\$m	Over 1 to 2 years NZ\$m	Over 2 years NZ\$m	Not bearing interest NZ\$m
Assets							
Cash	2,338	2,140	-	-	-	-	198
Settlement balances receivable	536	129	-	-	-	-	407
Collateral paid	1,415	1,415	-	-	-	-	-
Trading securities	7,663	496	268	241	2,025	4,633	-
Derivative financial instruments	9,878	-	-	-	-	-	9,878
Available-for-sale assets	6,360	713	250	603	1,465	3,328	1
Net loans and advances ¹	120,539	60,553	8,328	18,979	21,575	11,531	(427)
Other financial assets ¹	744	77	14	29	3	-	621
Total financial assets	149,473	65,523	8,860	19,852	25,068	19,492	10,678
Liabilities							
Settlement balances payable	1,840	630	-	-	-	-	1,210
Collateral received	613	613	-	-	-	-	-
Deposits and other borrowings ¹	102,696	68,718	12,925	8,051	2,855	1,265	8,882
Derivative financial instruments	9,826	-	-	-	-	-	9,826
Unsubordinated debt	21,323	3,511	1,567	125	3,420	12,700	-
Subordinated debt	3,283	938	1,013	835	-	497	-
Other financial liabilities ¹	759	151	-	-	-	-	608
Total financial liabilities	140,340	74,561	15,505	9,011	6,275	14,462	20,526
Hedging instruments	-	1,974	(1,395)	4,425	(4,008)	(996)	-
Interest sensitivity gap	9,133	(7,064)	(8,040)	15,266	14,785	4,034	(9,848)

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30/09/2016	Total NZ\$m	Up to 3 months NZ\$m	Over 3 to 6 months NZ\$m	Over 6 to 12 months NZ\$m	Over 1 to 2 years NZ\$m	Over 2 years NZ\$m	Not bearing interest NZ\$m
Assets							
Cash	2,274	2,081	-	-	-	-	193
Settlement balances receivable	396	48	-	-	-	-	348
Collateral paid	2,310	2,310	-	-	-	-	-
Trading securities	11,979	1,092	243	308	2,090	8,246	-
Derivative financial instruments	21,110	-	-	-	-	-	21,110
Available-for-sale assets	2,859	1,956	149	50	160	543	1
Net loans and advances	114,623	61,267	8,256	18,483	18,677	8,411	(471)
Other financial assets	678	65	25	17	12	-	559
Total financial assets	156,229	68,819	8,673	18,858	20,939	17,200	21,740
Liabilities							
Settlement balances payable	1,771	666	-	-	-	-	1,105
Collateral received	529	529	-	-	-	-	-
Deposits and other borrowings	99,066	65,416	11,988	10,120	2,460	1,302	7,780
Derivative financial instruments	21,956	-	-	-	-	-	21,956
Unsubordinated debt	20,014	4,342	-	1,087	2,843	11,742	-
Subordinated debt	3,282	938	1,013	-	835	496	-
Payables and other liabilities	639	51	-	-	9	124	455
Total financial liabilities	147,257	71,942	13,001	11,207	6,147	13,664	31,296
Hedging instruments	-	17,376	(13,314)	5,850	(11,914)	2,002	-
Interest sensitivity gap	8,972	14,253	(17,642)	13,501	2,878	5,538	(9,556)

¹ Includes UDC items classified as held for sale

Foreign currency related risks

This risk relates to the potential loss arising from the decline in the value of foreign currency positions due to changes in foreign exchange rates.

For non-traded instruments in foreign currencies, the risk is monitored and is hedged in accordance with policy. Risk arising from individual funding and other transactions is actively managed. The total amounts of unmatched foreign currency assets and liabilities, and consequent foreign currency exposures arising from each class of financial asset and liability, whether recognised or unrecognised, within each currency are not material.

The net open position in each foreign currency represents the net on-balance sheet assets and liabilities in that foreign currency aggregated with the net expected future cash flows from off-balance sheet purchases and sales from foreign exchange transactions in that foreign currency. The amounts are stated in New Zealand dollar equivalents translated using the spot exchange rates as at balance sheet date.

	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Net open position		
Australian dollar	24	26
Euro	-	6
Japanese yen	3	(3)
US dollar	13	(5)
Other	2	1
Total net open position	42	25

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Liquidity risk

Liquidity risk is the risk that the Banking Group is unable to meet its payment obligations as they fall due. The timing mismatch of cash flows and the related liquidity risk is inherent in all banking operations and is closely monitored by the Banking Group.

The Banking Group's liquidity and funding risks are governed by a detailed policy framework which is approved by the Risk Committees of the Bank's and Ultimate Parent Bank's Boards. The core objective of the Banking Group's framework is to manage liquidity to meet obligations as they fall due, without incurring unacceptable losses.

Central to the Banking Group's liquidity risk management approach is the establishment of a liquidity risk appetite framework to which the Banking Group must conform at all times. The risk appetite for liquidity has been set as low, and this objective is achieved by the Banking Group managing liquidity risks within the boundaries of the following requirements and principles:

- Maintaining the ability to meet all payment obligations in the immediate term.
- Ensuring the ability to meet "survival horizons" under Banking Group specific and general market liquidity stress scenarios.
- Maintaining strength in the Banking Group's balance sheet structure to ensure long term resilience in the Banking Group's liquidity and funding risk profile.
- Limiting the potential earnings at risk associated with unexpected increases in funding costs or the liquidation of assets under stress.
- Ensuring the liquidity management framework is compatible with regulatory requirements.
- Daily liquidity reporting and scenario analysis, quantifying the Banking Group's positions.
- Targeting a diversified funding base, avoiding undue concentrations by investor type, maturity, market source and currency.
- Holding a portfolio of high quality liquid assets to protect against adverse funding conditions and to support day-to-day operations.
- Establishing detailed contingency plans to cover different liquidity crisis events.

Management of liquidity and funding risks are overseen by ALCO.

Supervision and regulation

The RBNZ requires the Bank to have a comprehensive Board approved liquidity strategy defining: policy, systems and procedures for measuring, assessing, reporting and managing domestic and foreign currency liquidity. This also includes a formal contingency plan for dealing with a liquidity crisis. The Banking Group is required to meet one week and one month liquidity mismatch ratios and a one year core funding ratio each day.

Scenario modelling

A key component of the Banking Group's liquidity management framework is scenario modelling.

Potential severe name-specific liquidity crisis scenarios which model the behaviour of cash flows where there is a problem (real or perceived) may include, but are not limited to, operational issues, doubts about the solvency of the Banking Group, or adverse rating changes. Under these scenarios the Banking Group may have significant difficulty rolling over or replacing funding. Under the liquidity policy the Banking Group must have sufficient high quality liquid assets to meet its liquidity needs for the following 30 calendar days under these scenarios.

As of 30 September 2017 the Banking Group was in compliance with the above scenarios.

Structural balance sheet metrics

The Banking Group's liquidity management framework also encompasses structural balance sheet metrics such as the RBNZ core funding ratio. These metrics are designed to limit the amount of funding required to be rolled over within a 1 year timeframe and so interact with the liquidity scenarios to maintain the Banking Group's liquidity position.

Wholesale funding

The Banking Group's wholesale funding strategy is designed to deliver a sustainable portfolio of wholesale funds that balances cost efficiency while targeting diversification by markets, investors, currencies, maturities and funding structures. Short-term wholesale funding requirements, with a contractual maturity of less than one year, are managed through the Treasury and Markets operations. Long-term wholesale funding is managed and executed through Treasury operations.

The Banking Group also uses maturity concentration limits under the wholesale funding and liquidity management framework. Maturity concentration limits ensure that the Banking Group does not become reliant on issuing large volumes of new wholesale funding within a short time period. Funding instruments used to meet the wholesale borrowing requirement must be on a pre-established list of approved products.

Funding capacity and debt issuance planning

The Banking Group adopts a conservative approach to determine its funding capacity. Annually, a funding plan is approved by the Bank's Board. The plan is supplemented by regular updates and is linked to the Banking Group's three year strategic planning cycle.

NOTES TO THE FINANCIAL STATEMENTS

Funding composition

The Banking Group actively uses balance sheet disciplines to prudently manage the funding mix. The Banking Group employs funding metrics to ensure that an appropriate proportion of its assets are funded from stable sources, including customer liabilities, longer-dated wholesale debt (with remaining term exceeding one year) and equity.

Analysis of funding liabilities by industry is based on ANZSIC codes. The significant categories shown are the level one New Zealand Standard Industry Output Categories (NZSIOC). The presentation of these tables has changed from previous periods to align this disclosure with the classifications in the data series *S41 – Banks: Liabilities – Deposits by industry* published by the RBNZ.

	Note	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Funding composition			
Customer deposits	15	96,829	91,360
<i>Wholesale funding</i>			
Unsubordinated debt		21,323	20,014
Subordinated debt		3,283	3,282
Certificates of deposit		1,916	2,237
Commercial paper		3,721	5,364
Other borrowings		230	105
Total wholesale funding		30,473	31,002
Total funding		127,302	122,362
Customer deposits by industry - New Zealand residents			
Agriculture, forestry and fishing		3,487	3,334
Manufacturing		2,024	1,978
Construction		1,851	1,598
Wholesale trade		1,433	1,284
Retail trade and accommodation		1,516	1,328
Financial and insurance services		8,996	8,918
Rental, hiring and real estate services		2,596	2,321
Professional, scientific, technical, administrative and support services		5,034	4,958
Public administration and safety		1,261	1,258
Arts, recreation and other services		1,928	1,833
Households		53,222	49,492
All other New Zealand residents ¹		3,483	3,040
		86,831	81,342
Customer deposits by industry - overseas			
Households		9,461	8,948
All other non-NZ residents		537	1,070
		9,998	10,018
Total customer deposits		96,829	91,360
Wholesale funding (financial and insurance services industry)			
New Zealand		9,134	9,080
Overseas		21,339	21,922
Total wholesale funding		30,473	31,002
Total funding		127,302	122,362
Concentrations of funding by geography			
New Zealand		95,965	90,422
Australia		796	1,017
United States		13,471	12,215
Europe		9,784	11,448
Other countries		7,286	7,260
Total funding		127,302	122,362

¹ Other includes mining; electricity, gas, water and waste services; transport, postal and warehousing; information media and telecommunications; education and training; health care and social assistance.

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Liquidity portfolio management

The Banking Group holds a diversified portfolio of cash and high quality highly liquid securities to support liquidity risk management. The size of the Banking Group's liquidity portfolio is based on the amount required to meet the requirements of its internal and regulatory liquidity scenario metrics.

Total liquidity portfolio

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Cash and balances with central banks	2,102	2,068
Certificates of deposit	59	1,124
Government, local body stock and bonds	6,609	6,117
Government treasury bills	775	811
Reserve Bank bills	-	100
Other bonds	6,390	6,483
Total liquidity portfolio	15,935	16,703

Assets held for managing liquidity risk include short term cash held with the RBNZ, New Zealand Government securities, securities issued by supranational agencies, securities issued by highly rated banks and securities issued by State Owned Enterprises, Local Authorities and highly rated NZ domestic corporates. These assets would be accepted as collateral by the RBNZ in repurchase transactions. At 30 September 2017 the Banking Group would be eligible to enter into repurchase transactions with a value of NZ\$13,832 million. The Banking Group also held unencumbered internal residential mortgage backed securities (RMBS) which would entitle the Banking Group to enter into repurchase transactions with a value of NZ\$7,297 million at 30 September 2017.

Liquidity crisis contingency planning

The Banking Group maintains liquidity crisis contingency plans defining an approach for analysing and responding to a liquidity-threatening event on a group wide basis. The framework includes:

- the establishment of crisis severity/stress levels
- clearly assigned crisis roles and responsibilities
- early warning signals indicative of an approaching crisis, and mechanisms to monitor and report these signals
- outlined action plans, and courses of action for altering asset and liability behaviour
- procedures for crisis management reporting, and covering cash-flow shortfalls
- guidelines determining the priority of customer relationships in the event of liquidity problems
- assigned responsibilities for internal and external communications.

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Contractual maturity analysis of financial assets and liabilities

The following tables present the Banking Group's financial assets and liabilities within relevant contractual maturity groupings, based on the earliest date on which the Bank or the Banking Group may be required to realise an asset or settle a liability. The amounts disclosed in the tables represent undiscounted future principal and interest cash flows, except for derivatives held for trading where the full mark-to-market amount has been included in the less than three months category. As a result, the amounts in the tables below may differ to the amounts reported on the balance sheet.

The contractual maturity analysis for off-balance sheet commitments and contingent liabilities has been prepared using the earliest date at which the Banking Group or the Bank can be called upon to pay. The liquidity risk of credit related commitments and contingent liabilities may be less than the contract amount, and does not necessarily represent future cash requirements as many of these facilities are expected to be only partially used or to expire unused.

The Banking Group does not manage its liquidity risk on this basis.

30/09/2017	Total NZ\$m	At call NZ\$m	Up to 3 months NZ\$m	Over 3 to 12 months NZ\$m	Over 1 to 5 years NZ\$m	Over 5 years NZ\$m	No maturity specified NZ\$m
Financial assets							
Cash	2,338	1,974	364	-	-	-	-
Settlement balances receivable	536	185	351	-	-	-	-
Collateral paid	1,415	-	1,415	-	-	-	-
Trading securities	8,226	-	366	804	6,323	733	-
Derivative financial assets (trading)	8,682	-	8,682	-	-	-	-
Available-for-sale assets	6,746	-	545	1,013	4,452	735	1
Net loans and advances ¹	159,358	146	16,149	17,405	54,848	70,810	-
Other financial assets ¹	332	-	276	43	13	-	-
Total financial assets	187,633	2,305	28,148	19,265	65,636	72,278	1
Financial liabilities							
Settlement balances payable	1,850	1,165	685	-	-	-	-
Collateral received	613	-	613	-	-	-	-
Deposits and other borrowings ¹	111,925	58,287	24,814	24,320	4,504	-	-
Derivative financial liabilities (trading)	8,057	-	8,057	-	-	-	-
Unsubordinated debt ²	22,783	-	1,593	2,072	15,827	3,291	-
Subordinated debt ²	3,691	-	11	878	669	2,133	-
Other financial liabilities ¹	361	-	155	6	56	144	-
Total financial liabilities	149,280	59,452	35,928	27,276	21,056	5,568	-
Derivative financial instruments used for balance sheet management							
- gross inflows	15,377	-	2,082	2,300	8,128	2,867	-
- gross outflows	(15,737)	-	(2,235)	(2,433)	(8,328)	(2,741)	-
Net financial assets / (liabilities) after balance sheet management	37,993	(57,147)	(7,933)	(8,144)	44,380	66,836	1

Contractual maturity of off-balance sheet commitments and contingent liabilities

	Total NZ\$m	Less than 1 year NZ\$m	Beyond 1 year NZ\$m
Non-credit related commitments	488	88	400
Credit related commitments	26,769	26,769	-
Contingent liabilities	2,608	2,608	-
Total	29,865	29,465	400

¹ Includes UDC items classified as held for sale.

² Any callable wholesale debt instruments have been included at their next call date. Refer to note 17 for subordinated debt call dates.

NOTES TO THE FINANCIAL STATEMENTS

30/09/2016	Total NZ\$m	At call NZ\$m	Up to 3 months NZ\$m	Over 3 to 12 months NZ\$m	Over 1 to 5 years NZ\$m	Over 5 years NZ\$m	No maturity specified NZ\$m
Financial assets							
Cash	2,274	2,045	229	-	-	-	-
Settlement balances receivable	396	58	338	-	-	-	-
Collateral paid	2,310	-	2,310	-	-	-	-
Trading securities	12,804	-	171	1,136	10,859	638	-
Derivative financial assets (trading)	19,513	-	19,513	-	-	-	-
Available-for-sale assets	2,923	-	1,670	283	969	-	1
Net loans and advances	147,972	246	15,350	17,562	50,168	64,646	-
Other financial assets	281	-	228	41	12	-	-
Total financial assets	188,473	2,349	39,809	19,022	62,008	65,284	1
Financial liabilities							
Settlement balances payable	1,740	1,111	629	-	-	-	-
Collateral received	529	-	529	-	-	-	-
Deposits and other borrowings	100,429	50,413	20,790	25,095	4,131	-	-
Derivative financial liabilities (trading)	19,374	-	19,374	-	-	-	-
Unsubordinated debt ¹	20,983	-	2,363	1,882	13,466	3,272	-
Subordinated debt ¹	3,354	-	11	33	1,369	1,941	-
Other financial liabilities	264	-	33	7	93	131	-
Total financial liabilities	146,673	51,524	43,729	27,017	19,059	5,344	-
Derivative financial instruments used for balance sheet management							
- gross inflows	16,047	-	3,006	1,811	7,642	3,588	-
- gross outflows	(16,844)	-	(3,492)	(1,823)	(7,874)	(3,655)	-
Net financial assets / (liabilities) after balance sheet management	41,003	(49,175)	(4,406)	(8,007)	42,717	59,873	1

Contractual maturity of off-balance sheet commitments and contingent liabilities

	Total NZ\$m	Less than 1 year NZ\$m	Beyond 1 year NZ\$m
Non-credit related commitments	460	92	368
Credit related commitments	27,296	27,296	-
Contingent liabilities	2,461	2,461	-
Total	30,217	29,849	368

¹ Any callable wholesale debt instruments have been included at their next call date.

NOTES TO THE FINANCIAL STATEMENTS

19. CLASSIFICATION OF FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS

	At amortised cost	At fair value through profit or loss		Hedging	Available-for-sale assets	Total carrying amount	Fair value
		Designated on initial recognition	Held for trading				
30/09/2017	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Cash	2,338	-	-	-	-	2,338	2,338
Settlement balances receivable	536	-	-	-	-	536	536
Collateral paid	1,415	-	-	-	-	1,415	1,415
Trading securities	-	-	7,663	-	-	7,663	7,663
Derivative financial instruments ¹	-	-	9,490	388	-	9,878	9,878
Available-for-sale assets	-	-	-	-	6,360	6,360	6,360
Net loans and advances ^{2,3}	120,539	-	-	-	-	120,539	120,588
Other financial assets	621	123	-	-	-	744	744
Total financial assets	125,449	123	17,153	388	6,360	149,473	149,522
Settlement balances payable	1,840	-	-	-	-	1,840	1,840
Collateral received	613	-	-	-	-	613	613
Deposits and other borrowings ³	98,975	3,721	-	-	-	102,696	102,751
Derivative financial instruments ¹	-	-	8,992	834	-	9,826	9,826
Unsubordinated debt ²	21,323	-	-	-	-	21,323	21,517
Subordinated debt	3,283	-	-	-	-	3,283	3,501
Other financial liabilities	608	-	151	-	-	759	759
Total financial liabilities	126,642	3,721	9,143	834	-	140,340	140,807
30/09/2016							
Cash	2,274	-	-	-	-	2,274	2,274
Settlement balances receivable	396	-	-	-	-	396	396
Collateral paid	2,310	-	-	-	-	2,310	2,310
Trading securities	-	-	11,979	-	-	11,979	11,979
Derivative financial instruments ¹	-	-	20,379	731	-	21,110	21,110
Available-for-sale assets	-	-	-	-	2,859	2,859	2,859
Net loans and advances ²	114,623	-	-	-	-	114,623	114,891
Other financial assets	559	119	-	-	-	678	678
Total financial assets	120,162	119	32,358	731	2,859	156,229	156,497
Settlement balances payable	1,771	-	-	-	-	1,771	1,771
Collateral received	529	-	-	-	-	529	529
Deposits and other borrowings	93,702	5,364	-	-	-	99,066	99,169
Derivative financial instruments ¹	-	-	21,190	766	-	21,956	21,956
Unsubordinated debt ²	20,014	-	-	-	-	20,014	20,148
Subordinated debt	3,282	-	-	-	-	3,282	3,351
Other financial liabilities	482	-	157	-	-	639	639
Total financial liabilities	119,780	5,364	21,347	766	-	147,257	147,563

¹ Derivative financial instruments classified as held for trading include derivatives entered into as economic hedges which are not designated as accounting hedges.

² Fair value hedging is applied to certain financial assets within loans and advances and certain financial liabilities within unsubordinated debt. The resulting fair value adjustment means that the carrying value differs from the amortised cost.

³ Includes UDC items classified as held for sale.

NOTES TO THE FINANCIAL STATEMENTS

Measurement of fair value

Valuation methodologies

The Banking Group has an established control framework that ensures fair value is either determined or validated by a function independent of the party that undertakes the transaction. The control framework ensures that all models are calibrated periodically to test that outputs reflect prices from observable current market transactions in the same instrument or other available observable market data.

Where quoted market prices are used, prices are independently verified from other sources. For fair values determined using a valuation model, the control framework may include, as applicable, independent development or validation of valuation models, any inputs to those models, any adjustments required outside of the valuation model and, where possible, independent validation of model outputs. In this way, continued appropriateness of the valuations is ensured.

In instances where the Banking Group holds offsetting risk positions, the Banking Group uses the portfolio exemption in NZ IFRS 13 *Fair Value Measurement* to measure the fair value of such groups of financial assets and financial liabilities on the basis of the price that would be received to sell a net long position (that is, an asset) for a particular risk exposure or to transfer a net short position (that is, a liability) for a particular risk exposure.

The Banking Group categorises its fair value measurements on the basis of inputs used in measuring fair value using the fair value hierarchy below:

- Level 1 – Financial instruments that have been valued by reference to unadjusted quoted prices in active markets for identical financial instruments. This category includes financial instruments valued using quoted yields where available for specific debt securities.
- Level 2 – Financial instruments that have been valued through valuation techniques incorporating inputs other than quoted prices within Level 1 that are observable for a similar financial asset or liability, either directly or indirectly.
- Level 3 – Financial instruments that have been valued using valuation techniques which incorporate significant inputs that are not based on observable market data (unobservable inputs).

Valuation techniques and inputs used

In the event that there is no quoted market price for the instrument, fair value is based on valuation techniques. The valuation models incorporate the impact of bid/ask spreads, counterparty credit spreads, funding costs and other factors that would influence the fair value determined by market participants.

The majority of valuation techniques employ only observable market data. However, for certain financial instruments the valuation technique may employ some data (valuation inputs or components) which is not readily observable in the current market. In these cases valuation inputs (or components of the overall value) are derived and extrapolated from other relevant market data and tested against historic transactions and observed market trends. To the extent that valuation is based on models or inputs that are not observable in the market, the determination of fair value can be more subjective, dependent on the significance of the unobservable input to the overall valuation.

The following valuation techniques have been applied to determine the fair values of financial instruments where there is no quoted price (level1) for the instrument:

- For instruments classified as trading securities and securities short sold, derivative financial assets and liabilities, available-for-sale assets, and investments backing insurance contract liabilities, fair value measurements are derived by using modelled valuations techniques (including discounted cash flow models) that incorporate market prices / yields for securities with similar credit risk, maturity and yield characteristics; and/or current market yields for similar instruments.
- For net loans and advances, deposits and other borrowings and unsubordinated debt, discounted cash flow techniques are used where contractual future cash flows of the instrument are discounted using discount rates incorporating wholesale market rates or market borrowing rates of debt with similar maturities or a yield curve appropriate for the remaining term to maturity.

There have been no substantial changes in the valuation techniques applied to different classes of financial instruments during the year.

NOTES TO THE FINANCIAL STATEMENTS

Valuation hierarchy for financial assets and financial liabilities measured at fair value in the balance sheet

	30/09/2017				30/09/2016			
	Level 1 NZ\$m	Level 2 NZ\$m	Level 3 NZ\$m	Total NZ\$m	Level 1 NZ\$m	Level 2 NZ\$m	Level 3 NZ\$m	Total NZ\$m
Financial assets								
Trading securities	7,276	387	-	7,663	11,967	12	-	11,979
Derivative financial instruments	5	9,870	3	9,878	3	21,100	7	21,110
Available-for-sale assets	5,336	1,023	1	6,360	1,671	1,187	1	2,859
Investments backing insurance contract liabilities	-	123	-	123	5	114	-	119
Total	12,617	11,403	4	24,024	13,646	22,413	8	36,067
Financial liabilities								
Deposits and other borrowings	-	3,721	-	3,721	-	5,364	-	5,364
Derivative financial instruments	24	9,801	1	9,826	46	21,908	2	21,956
Other financial liabilities	151	-	-	151	157	-	-	157
Total	175	13,522	1	13,698	203	27,272	2	27,477

Valuation hierarchy for financial assets and financial liabilities not measured at fair value¹

	30/09/2017				30/09/2016			
	Level 1 NZ\$m	Level 2 NZ\$m	Level 3 NZ\$m	Total NZ\$m	Level 1 NZ\$m	Level 2 NZ\$m	Level 3 NZ\$m	Total NZ\$m
Financial assets								
Net loans and advances	-	117,365	3,223	120,588	-	111,513	3,378	114,891
Financial liabilities								
Deposits and other borrowings	-	99,030	-	99,030	-	93,805	-	93,805
Unsubordinated debt	1,487	20,030	-	21,517	1,629	18,519	-	20,148
Subordinated debt	1,368	2,133	-	3,501	1,361	1,990	-	3,351
Total	2,855	121,193	-	124,048	2,990	114,314	-	117,304

¹ Fair values, where the carrying amount is not considered a close approximation of fair value.

20. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The following is an analysis of asset and liability line items in the balance sheet that combine amounts expected to be realised or due to be settled within one year and after more than one year.

	30/09/2017			30/09/2016			
	within one year NZ\$m	after more than one year NZ\$m	Total NZ\$m	within one year NZ\$m	after more than one year NZ\$m	Total NZ\$m	
Assets							
Investments backing insurance contract liabilities		120	3	123	107	12	119
Available-for-sale assets	1,400	4,960	6,360	1,915	944	2,859	
Net loans and advances ¹	24,945	95,594	120,539	24,976	89,647	114,623	
Other assets ¹	665	38	703	598	103	701	
Life insurance contract assets	45	591	636	42	588	630	
Liabilities							
Deposits and other borrowings ¹	98,193	4,503	102,696	95,301	3,765	99,066	
Payables and other liabilities ¹	1,006	178	1,184	884	235	1,119	
Employee entitlements ¹	34	86	120	29	97	126	
Other provisions	66	-	66	79	1	80	
Unsubordinated debt	3,169	18,154	21,323	4,009	16,005	20,014	
Subordinated debt ²	845	2,438	3,283	-	3,282	3,282	

¹ Includes UDC items classified as held for sale.

² Any callable wholesale debt instruments have been included at their next call date.

NOTES TO THE FINANCIAL STATEMENTS

21. ASSETS CHARGED AS SECURITY FOR LIABILITIES AND COLLATERAL ACCEPTED AS SECURITY FOR ASSETS

Assets charged as security for liabilities¹

The carrying amounts of assets pledged as security are as follows:

	Carrying Amount		Related Liability	
	30/09/2017	30/09/2016	30/09/2017	30/09/2016
	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Securities sold under agreements to repurchase	157	77	157	76
Residential mortgages pledged as security for covered bonds	10,595	10,265	5,325	6,218
Assets pledged as collateral for UDC secured investments	2,985	2,665	1,039	1,592

UDC Secured Investments are secured by a security interest granted under a trust deed over all of UDC's present and future assets and undertakings, to Trustees Executors Limited, as supervisor. The assets subject to the security interest comprise mainly loans to UDC's customers and certain plant and equipment. The security interest secures all amounts payable by UDC on the UDC Secured Investments and all other monies payable by UDC under the trust deed.

Collateral accepted as security for assets¹

The Banking Group has received collateral in relation to reverse repurchase agreements. These transactions are governed by standard industry agreements.

The fair value of collateral received and sold or repledged is as follows:

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Collateral received on standard reverse repurchase agreements		
Fair value of assets which can be sold	361	231
Fair value of assets sold or repledged	218	141

¹ Excludes the amounts disclosed as collateral paid and received in the balance sheet that relate to derivative liabilities and derivative assets respectively. The terms and conditions of the collateral agreements are included in the standard CSA that forms part of the ISDA.

NOTES TO THE FINANCIAL STATEMENTS

22. OFFSETTING

The following information relates to financial assets and liabilities which have not been set off in the balance sheet but for which the Banking Group has enforceable master netting agreements in place with counterparties. No financial assets and liabilities have been set off in the balance sheet.

	Gross amounts presented in the balance sheet NZ\$m	Related amounts not offset ¹		Net amounts NZ\$m
		Financial instruments NZ\$m	Cash collateral NZ\$m	
30/09/2017				
Financial assets				
Collateral paid	409	-	(348)	61
Trading securities ²	157	(157)	-	-
Derivative financial instruments	7,945	(7,478)	(245)	222
Financial liabilities				
Collateral received	318	-	(245)	73
Securities sold under agreements to repurchase ³	157	(157)	-	-
Derivative financial instruments	8,440	(7,478)	(348)	614
30/09/2016				
Financial assets				
Collateral paid	1,405	-	(1,332)	73
Trading securities ²	77	(76)	-	1
Derivative financial instruments	7,618	(7,280)	(323)	15
Financial liabilities				
Collateral received	358	-	(323)	35
Securities sold under agreements to repurchase ³	76	(76)	-	-
Derivative financial instruments	8,768	(7,280)	(1,332)	156

¹ The Banking Group enters into derivatives and repurchase and reverse repurchase agreements with various counterparties which are governed by industry standard master netting agreements. The Banking Group holds and provides cash and securities collateral in respect of derivative transactions covered by these agreements. The right to set off balances under these master netting agreements or to set off cash and securities collateral only arises in the event of non-payment or default and, as a result, these arrangements do not qualify for offsetting under NZ IAS 32 *Financial Instruments: Presentation*.

² This is the amount of trading securities encumbered through repurchase agreements, see financial assets pledged as collateral table in note 21.

³ Included in deposits and other borrowings, see note 15.

NOTES TO THE FINANCIAL STATEMENTS

23. CREDIT RELATED COMMITMENTS, GUARANTEES AND CONTINGENT LIABILITIES

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Contract amount of:		
Credit related commitments - facilities provided		
Undrawn facilities	26,769	27,296
Guarantees and contingent liabilities		
Guarantees and letters of credit	1,010	850
Performance related contingencies	1,598	1,611
Total guarantees and contingent liabilities	2,608	2,461
Total Credit Related Commitments, Guarantees and Contingent Liabilities	29,377	29,757

These guarantees and contingent liabilities relate to transactions that the Banking Group has entered into as principal, including guarantees, standby letters of credit and documentary letters of credit.

Documentary letters of credit involve the issue of letters of credit guaranteeing payment in favour of an exporter secured against an underlying shipment of goods or backed by a confirmatory letter of credit from another bank.

Performance related contingencies are liabilities that oblige the Banking Group to make payments to a third party should the customer fail to fulfil the non-monetary terms of the contract.

To reflect the risk associated with these transactions, they are subjected to the same credit origination, portfolio management and collateral requirements as customers that apply for loans. The contract amount represents the maximum potential amount that could be lost if the counterparty fails to meet its financial obligations. As the facilities may expire without being drawn upon, the notional amounts do not necessarily reflect future cash requirements.

Other contingent liabilities

The Banking Group has other contingent liabilities in respect of actual and possible claims and court 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 made where deemed necessary.

24. GOODWILL AND OTHER INTANGIBLE ASSETS

	30/09/2017	30/09/2016
Note	NZ\$m	NZ\$m
Goodwill	3,230	3,233
Software	67	76
Other intangibles	111	115
Goodwill and other intangible assets (including assets classified as held for sale)	3,408	3,424
Less: goodwill allocated to UDC and held for sale	29	-
Goodwill and other intangible assets	3,275	3,424

NOTES TO THE FINANCIAL STATEMENTS

25. SHARE CAPITAL

	Number of issued shares		NZ\$ millions	
	30/09/2017	30/09/2016	30/09/2017	30/09/2016
Ordinary shares	3,345,755,498	3,345,755,498	8,588	8,588
Redeemable preference shares	300,000,000	300,000,000	300	300
Total share capital	3,645,755,498	3,645,755,498	8,888	8,888

Ordinary shares

650,712 of the ordinary shares are uncalled (2016: 650,712 shares uncalled).

During the year ended 30 September 2017 the Bank paid ordinary dividends of NZ\$1,684 million (2016: NZ\$1,350 million) to the Immediate Parent Company (equivalent to NZ\$0.50 per share) (2016: equivalent to NZ\$0.40 per share).

All ordinary shares share equally in dividends and any proceeds available to ordinary shareholders on winding up of the Bank. On a show of hands every member who is present at a meeting in person or by proxy or by representative is entitled to one vote, and upon a poll every member shall have one vote for each share held.

Preference shares

All preference shares were issued by the Bank to the Immediate Parent and do not carry any voting rights. The preference shares are wholly classified as equity instruments as there is no contractual obligation for the Bank to either deliver cash or another financial instrument or to exchange financial instruments on a potentially unfavourable basis. The key terms of the preference shares are as follows:

Dividends

Dividends are payable at the discretion of the directors of the Bank and are non-cumulative. The Bank must not resolve to pay any dividend or make any other distribution on its ordinary shares until the next preference dividend payment date if the dividend on the preference shares is not paid.

Should the Bank elect to pay a dividend, the dividend is based on a floating rate equal to the aggregate of the New Zealand 6 month bank bill rate plus a 325 basis point margin, multiplied by one minus the New Zealand company tax rate, with dividend payments due on 1 March and 1 September each year.

Redemption features

The preference shares are redeemable, subject to prior written approval of the RBNZ, by the Bank providing notice in writing to holders of the preference shares:

- on any date on or after a change to laws or regulations that adversely affects the regulatory capital or tax treatment of the preference shares or
- on any dividend payment date on or after 1 March 2019 or
- on any date after 1 March 2019 if the Bank has ceased to be a wholly owned subsidiary of the Ultimate Parent Bank.

The preference shares may be redeemed for nil consideration should a non-viability trigger event occur.

Rights of holders in event of liquidation

In the event of liquidation, holders of preference shares are entitled to available subscribed capital per share, pari passu with all holders of existing preference shares and ANZ capital notes but in priority to all holders of ordinary shares. They have no entitlement to participate in further distribution of profits or assets.

The preference shares qualify as "additional tier 1 capital" for capital adequacy purposes.

NOTES TO THE FINANCIAL STATEMENTS

26. CAPITAL ADEQUACY

Capital management policies

The Banking Group's core capital objectives are to:

- Protect the interests of depositors, creditors and shareholders
- Ensure the safety and soundness of the Banking Group's capital position
- Ensure that the capital base supports the Banking Group's risk appetite, and strategic business objectives, in an efficient and effective manner.

The Board holds ultimate responsibility for ensuring that capital adequacy is maintained. This includes: setting, monitoring and obtaining assurance for the Banking Group's Internal Capital Adequacy Assessment Process ("ICAAP") policy and framework; standardised risk definitions for all material risks; materiality thresholds; capital adequacy targets; internal economic risk capital principles; and risk appetite.

The Banking Group has minimum and trigger levels for common equity tier 1, tier 1 and total capital that ensure sufficient capital is maintained to:

- Meet minimum prudential requirements imposed by regulators
- Ensure consistency with the Banking Group's overall risk profile and financial positions, taking into account its strategic focus and business plan
- Support the economic risk capital requirements of the business.

The Banking Group's Asset & Liability Committee and its related Capital Management Forum are responsible for developing, implementing and maintaining the Banking Group's ICAAP framework, including ongoing monitoring, reporting and compliance. The Banking Group's ICAAP is subject to independent and periodic review conducted by Internal Audit.

The Banking Group has complied with all externally imposed capital requirements to which it is subject during the current and prior periods.

RBNZ Basel III capital ratios	RBNZ minimum ratios	Banking Group		Bank	
		30/09/2017	30/09/2016	30/09/2017	30/09/2016
Unaudited					
Common equity tier 1 capital	4.5%	10.7%	10.0%	9.5%	8.9%
Tier 1 capital	6.0%	14.1%	13.2%	13.0%	12.2%
Total capital	8.0%	14.4%	13.7%	13.3%	12.8%
Buffer ratio	2.5%	6.2%	5.5%		

NOTES TO THE FINANCIAL STATEMENTS

Capital of the Banking Group

	Note	Unaudited 30/09/2017 NZ\$m
Tier 1 capital		
<i>Common equity tier 1 capital</i>		
Paid up ordinary shares issued by the Bank	25	8,588
Retained earnings (net of appropriations)		3,845
Accumulated other comprehensive income and other disclosed reserves		48
<i>Less deductions from common equity tier 1 capital</i>		
Goodwill and intangible assets, net of associated deferred tax liabilities		(3,399)
Cash flow hedge reserve		(43)
Expected losses to the extent greater than total eligible allowances for impairment		(312)
Common equity tier 1 capital		8,727
<i>Additional tier 1 capital</i>		
Preference shares	25	300
ANZ Capital Notes	17	2,441
Capital attributable to Bonus Bonds Scheme investors		37
Additional tier 1 capital		2,778
Total tier 1 capital		11,505
Tier 2 capital		
<i>Qualifying tier 2 capital instruments subject to phase-out under RBNZ Basel III transition arrangements</i>		
NZD 835,000,000 perpetual subordinated bond	17	835
<i>Less deductions from tier 2 capital</i>		
Basel III transition adjustment ¹		(601)
Total tier 2 capital		234
Total capital		11,739

Capital requirements of the Banking Group

	Exposure at default NZ\$m	Risk weighted exposure or implied risk weighted exposure ² NZ\$m	Total capital requirement NZ\$m
Unaudited 30/09/2017			
Exposures subject to internal ratings based approach	160,456	57,268	4,581
Specialised lending exposures subject to slotting approach	11,631	10,472	838
Exposures subject to standardised approach	1,915	479	38
Equity exposures	8	32	3
Other exposures	3,553	1,674	134
Agri business supervisory adjustment	n/a	1,363	109
Total credit risk	177,563	71,288	5,703
Operational risk	n/a	5,805	464
Market risk	n/a	4,549	364
Total	177,563	81,642	6,531

¹ Certain instruments issued by the Bank qualify as tier 2 capital instruments subject to phase-out under RBNZ Basel III transition arrangements. Fixing the base at the nominal amount of such instruments outstanding at 31 December 2012, their recognition is capped at 20% of that base from 1 January 2017; and from 1 January 2018 onwards these instruments will not be included in regulatory capital.

² Total credit risk weighted exposures include a scalar of 1.06 in accordance with the Bank's Conditions of Registration.

NOTES TO THE FINANCIAL STATEMENTS

Implementation of the advanced internal ratings based approach to credit risk measurement

The Banking Group adheres to the standards of risk grading and risk quantification as set out for Internal Ratings Based (IRB) banks in the RBNZ document *Capital Adequacy Framework (Internal Models Based Approach)* (BS2B).

Under this IRB Framework banks use their own measures for calculating the level of credit risk associated with customers and exposures, by way of the primary components of:

Probability of Default (PD): An estimate of the level of risk of borrower default graded by way of rating models used both at loan origination and for ongoing monitoring.

Exposure at Default (EAD): The expected facility exposure at default. Total credit risk-weighted exposures include a scalar of 1.06 in accordance with the Bank's Conditions of Registration.

Loss Given Default (LGD): An estimate of the potential economic loss on a credit exposure, incurred as a consequence of obligor default and expressed as a percentage of the facility's EAD. For Retail Mortgage exposures the Bank is required to apply the downturn LGDs according to loan to value (LVR) bands as set out in BS2B. For farm lending exposures the Banking Group is required to adopt RBNZ prescribed downturn LVR based LGDs, along with a minimum maturity of 2.5 years and the removal of the firm-size adjustment.

For exposures classified under Specialised Lending, the Banking Group uses slotting tables approved by the RBNZ rather than internal estimates.

The exceptions to IRB treatment are three minor portfolios where, due to systems constraints, determining these IRB risk estimates is not currently feasible or appropriate. Risk weights for these exposures are calculated under a separate treatment as set out in the RBNZ document *Capital Adequacy Framework (Standardised Approach)* (BS2A).

Classification of Banking Group exposures according to rating approach

Internal ratings based approach

IRB Asset Class	Borrower Type	Rating Approach
Sovereign	Crown	IRB - Advanced
	RBNZ	IRB - Advanced
	Any other sovereign and its central bank	IRB - Advanced
Bank	Registered banks	IRB - Advanced
Corporate	Corporation, partnerships or proprietorships that do not fit any other asset classification	IRB - Advanced
	Corporate Small to Medium Enterprises ("SME") with turnover of less than NZ\$50 million	IRB - Advanced
Retail Mortgages	Individuals' borrowings against residential property	IRB - Advanced
Other Retail	Other lending to individuals (including credit cards)	IRB - Advanced
	SME business borrowers	IRB - Advanced
Corporate sub-class - Specialised lending	Project finance	IRB - Slotting
	Income producing real estate	IRB - Slotting
Equity		IRB
Other assets	All other assets not falling within any of the above classes	IRB

Standardised approach

Exposure class	Exposure Type	Reason for Standardised Approach	Future Treatment
Corporate	Merchant card prepayment exposures	System constraints	Move to IRB
	Corporate credit cards	System constraints	Move to IRB
Bank	Qualifying Central Counterparty (QCCP)	Required by Basel III	Standardised

NOTES TO THE FINANCIAL STATEMENTS

Controls surrounding credit risk rating systems

The term "Rating Systems" covers all of the methods, processes, controls, data collection and technology that support the assessment of credit risk, the assignment of internal credit risk ratings and the quantification of associated default and loss estimates.

All material aspects of the Rating Systems and risk estimate processes are governed by the Banking Group's Risk Committee. Risk grades are an integral part of reporting to senior management and executives. Management and staff of credit risk functions, in conjunction with the relevant Retail and Wholesale Risk Committees, regularly assess the performance of the rating systems, identify any areas for improvement and monitor progress on previously identified development work needed.

The Banking Group's Rating Systems are governed by a comprehensive framework of controls that operate at the business unit and support centres, and through central audit and validation processes. All policies, model designs, model reviews, methodologies, validations, responsibilities, systems and processes supporting the ratings systems are fully documented.

The Banking Group's Retail and Wholesale ratings functions work closely with the Ultimate Parent Bank's risk ratings functions, are independent of operational lending activities and are responsible for the ratings strategies and ongoing management of credit risk models within New Zealand. The annual review of models used across the Banking Group is a function undertaken by the ANZ Decision Model Validation Unit, which is also independent of credit risk operational functions and is responsible for overseeing the design, implementation and performance of all rating models in the Banking Group.

The target approach to modelling for the Banking Group is to deploy the model most suitable for the environment. At present this involves an approach to modelling that combines models developed in New Zealand and models developed by the Ultimate Parent Bank, tested and validated for use in New Zealand, as appropriate.

Capital requirements by asset class under the IRB approach

	Total exposure or principal amount NZ\$m	Exposure at default NZ\$m	Exposure- weighted LGD used for the capital calculation %	Exposure- weighted risk weight %	Risk weighted exposure NZ\$m	Total capital requirement NZ\$m
Unaudited 30/09/2017						
On-balance sheet exposures						
Corporate	35,231	35,336	34	56	20,977	1,678
Sovereign	11,309	11,030	5	1	99	8
Bank	6,507	5,804	58	19	1,177	94
Retail mortgages	70,088	70,314	19	21	15,503	1,240
Other retail	5,211	5,302	74	94	5,300	424
Total on-balance sheet exposures	128,346	127,786	26	32	43,056	3,444
Off-balance sheet exposures						
Corporate	12,471	10,025	47	47	4,999	400
Sovereign	128	97	5	1	1	-
Bank	1,410	1,146	51	17	205	16
Retail mortgages	8,066	8,468	16	14	1,258	101
Other retail	5,591	5,609	79	56	3,354	268
Total off-balance sheet exposures	27,666	25,345	44	37	9,817	785
Market related contracts						
Corporate	114,726	3,171	61	80	2,690	215
Sovereign	17,002	82	5	31	27	2
Bank	1,028,806	4,072	62	39	1,678	135
Total market related contracts	1,160,534	7,325	61	57	4,395	352
Total credit risk exposures subject to the IRB approach	1,316,546	160,456	30	34	57,268	4,581

NOTES TO THE FINANCIAL STATEMENTS

IRB exposures by customer credit rating

Unaudited 30/09/2017	Probability of default %	Exposure at default NZ\$m	Exposure-weighted LGD used for the capital calculation %	Exposure-weighted risk weight %	Risk weighted exposure NZ\$m	Total capital requirement NZ\$m
Corporate						
0 - 2	0.06	6,174	62	45	2,972	238
3 - 4	0.33	21,429	36	40	9,112	729
5	1.02	13,986	33	60	8,840	707
6	2.30	4,833	36	83	4,248	340
7 - 8	15.52	1,711	39	161	2,919	233
Default	100.00	399	46	136	575	46
Total corporate exposures	2.04	48,532	39	56	28,666	2,293
Sovereign						
0	0.01	11,075	5	1	125	10
1 - 8	0.02	134	5	2	2	-
Total sovereign exposures	0.01	11,209	5	1	127	10
Bank						
0	0.03	60	65	18	11	1
1	0.03	9,991	58	25	2,634	211
2 - 4	0.11	969	64	40	412	33
5 - 8	1.26	2	65	115	3	-
Total bank exposures	0.04	11,022	59	26	3,060	245
Retail mortgages						
0 - 3	0.20	21,487	12	5	1,228	98
4	0.46	30,842	18	15	4,835	387
5	0.92	21,044	24	32	7,061	565
6	1.98	4,811	27	62	3,178	254
7 - 8	5.02	395	28	100	421	34
Default	100.00	203	21	18	38	3
Total retail mortgages exposures	0.88	78,782	19	20	16,761	1,341
Other retail						
0 - 2	0.10	584	77	50	306	25
3 - 4	0.26	4,883	78	54	2,811	225
5	1.01	1,856	73	74	1,458	117
6	2.18	1,807	73	90	1,730	138
7 - 8	8.06	1,712	83	128	2,317	185
Default	100.00	69	78	45	32	2
Total other retail exposures	2.56	10,911	77	75	8,654	692
Total credit risk exposures subject to the IRB approach	1.23	160,456	30	34	57,268	4,581

Credit risk exposures subject to the IRB approach have been derived in accordance with BS2B and other relevant correspondence with RBNZ setting out prescribed credit risk estimates.

NOTES TO THE FINANCIAL STATEMENTS

Specialised lending subject to the slotting approach

	Exposure at default	Risk weight	Risk weighted exposure	Total capital requirement
	NZ\$m	%	NZ\$m	NZ\$m
Unaudited 30/09/2017				
On-balance sheet exposures				
Strong	3,859	70	2,864	229
Good	5,815	90	5,547	444
Satisfactory	641	115	782	63
Weak	75	250	197	15
Default	42	-	-	-
Total on-balance sheet exposures	10,432	85	9,390	751

	Exposure amount	Exposure at default	Average risk weight	Risk weighted exposure	Total capital requirement
	NZ\$m	NZ\$m	%	NZ\$m	NZ\$m
Off-balance sheet exposures					
Undrawn commitments and other off balance sheet exposures	1,148	1,101	81	945	76
Market related contracts	2,126	98	132	137	11
Total off-balance sheet exposures	3,274	1,199	85	1,082	87

Specialised lending exposures subject to the slotting approach have been calculated in accordance with BS2B.

The supervisory categories of specialised lending above are associated with specific risk-weights. These categories broadly correspond to the following external credit assessments using Standard & Poor's rating scale, Strong: BBB- or better, Good: BB+ or BB, Satisfactory: BB- or B+ and Weak: B to C-.

Credit risk exposures subject to the standardised approach

	Exposure at default	Risk weight	Risk weighted exposure	Total capital requirement
	NZ\$m	%	NZ\$m	NZ\$m
Unaudited 30/09/2017				
On-balance sheet exposures				
Corporates	105	78	86	7
Default	1	150	1	-
Total on-balance sheet exposures	106	78	87	7

	Exposure amount	Average credit conversion factor	Exposure at default	Average risk weight	Risk weighted exposure	Total capital requirement
	NZ\$m	%	NZ\$m	%	NZ\$m	NZ\$m
Off-balance sheet exposures						
Undrawn commitments and other off balance sheet exposures	563	57	323	96	328	26
Market related contracts	343,810	-	1,486	4	64	5
Total off balance sheet	344,373	n/a	1,809	20	392	31

Credit exposures subject to the Standardised Approach have been calculated in accordance with BS2A.

NOTES TO THE FINANCIAL STATEMENTS

Equity exposures

	Exposure at default NZ\$m	Risk weight %	Risk weighted exposure NZ\$m	Total capital requirement NZ\$m
Unaudited 30/09/2017				
All equity holdings not deducted from capital	8	400	32	3

Equity exposures have been calculated in accordance with BS2B.

Other exposures

	Exposure at default NZ\$m	Risk weight %	Risk weighted exposure NZ\$m	Total capital requirement NZ\$m
Unaudited 30/09/2017				
Cash	198	-	-	-
New Zealand dollar denominated claims on the Crown and the RBNZ	1,776	-	-	-
Other assets	1,579	100	1,674	134
Total other IRB credit risk exposures	3,553	44	1,674	134

Other exposures have been calculated in accordance with BS2B.

Credit risk mitigation

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

As at 30 September 2017, under the IRB approach, the Banking Group had NZ\$1,038 million of Corporate exposures covered by guarantees where the presence of the guarantees was judged to reduce the underlying credit risk of the exposures. Information on the total value of exposures covered by financial guarantees and eligible financial collateral is not disclosed, as the effect of these guarantees and collateral on the underlying credit risk exposures is not considered to be material.

Operational risk

The Banking Group uses the Advanced Measurement Approach for determining its regulatory capital requirement for operational risk calculated in accordance with BS2B. As at 30 September 2017 the Banking Group had an implied risk weighted exposure of NZ\$5,805 million for operational risk and an operational risk capital requirement of NZ\$464 million.

Operational risk capital is modelled at a New Zealand geographic level and then distributed and adjusted for the business environment and internal controls down to the business units using the Risk Scenario Methodology. This methodology ensures that there is sufficient operational risk capital held as a buffer for rare and severe unexpected operational loss events that may impact the New Zealand business. The Methodology applies a combination of expert judgement, business unit risk profiles, audit findings, and internal and external loss events to derive a series of business specific Risk Scenarios that are applied to the capital model. The Risk Scenario approach

- assesses the level of the Bank's exposure to specified risk scenarios;
- assesses the scope and quality of the Bank's internal control environment, key operational processes and risk mitigants; and
- directly links the risk scenarios to operational risk capital.

The Banking Group's operating risk capital is calculated using the Ultimate Parent Bank's methodology, but with standalone New Zealand inputs to ensure there are no diversification benefits.

The Banking Group does not incorporate any insurance mitigation impact into its capital number. Accordingly, there are no insurance related questions contained within the Risk Scenario Methodology.

NOTES TO THE FINANCIAL STATEMENTS

Market risk

The aggregate market risk exposures below have been calculated in accordance with BS2B. The peak end-of-day market risk exposures are for the six months ended 30 September 2017.

	Implied risk weighted exposure		Aggregate capital charge		Peak occurred on
	Period end NZ\$m	Peak NZ\$m	Period end NZ\$m	Peak NZ\$m	
Unaudited 30/09/2017					
Interest rate risk	4,502	7,271	360	582	6/06/2017
Foreign currency risk	46	152	4	12	20/06/2017
Equity risk	1	1	-	-	30/09/2017
	4,549		364		

Capital for other material risks

The Banking Group has an Internal Capital Adequacy Assessment Process (ICAAP) which complies with the requirements of the Bank's Conditions of Registration.

Under the Banking Group's ICAAP it identifies and measures all "other material risks", which are those material risks that are not explicitly captured in the calculation of the Banking Group's tier 1 and total capital ratios. The other material risks identified by the Banking Group include pension risk, insurance risk, strategic equity risk, fixed asset risk, deferred acquisition cost risk, value in-force risk, business retention risk and software risk.

The Banking Group's internal capital allocation for these other material risks is NZ\$421 million. (2016: NZ\$441 million).

Capital adequacy of the Ultimate Parent Bank

Basel III capital ratios

	Overseas Banking Group		Ultimate Parent Bank (Extended Licensed Entity)	
	30/09/2017	30/09/2016	30/09/2017	30/09/2016
Unaudited				
Common equity tier 1 capital	10.6%	9.6%	10.5%	9.7%
Tier 1 capital	12.6%	11.8%	12.7%	12.1%
Total capital	14.8%	14.3%	14.8%	14.7%

For calculation of minimum capital requirements under Pillar 1 (Capital Requirements) of the Basel Accord, APRA has accredited the Overseas Banking Group to use the Advanced Internal Ratings Based (AIRB) methodology for calculation of credit risk weighted assets and the Advanced Measurement Approach (AMA) for the operational risk weighted asset equivalent.

Under prudential regulations, the Overseas Banking Group is required to maintain a Prudential Capital Ratio (PCR) as determined by APRA. The Overseas Banking Group exceeded the PCR set by APRA as at 30 September 2017 and for the comparative prior periods.

The Overseas Banking Group is required to publicly disclose Pillar 3 financial information as at 30 September 2017. The Overseas Banking Group's Pillar 3 disclosure document for the quarter ended 30 September 2017, in accordance with APS 330: *Public Disclosure of Prudential Information*, discloses capital adequacy ratios and other prudential information. This document can be accessed at the website anz.com.

NOTES TO THE FINANCIAL STATEMENTS

Residential mortgages by loan-to-valuation ratio (LVR)

As required by the RBNZ, LVRs are calculated as the current exposure secured by a residential mortgage divided by the Banking Group's valuation of the security property at origination of the exposure. Off balance sheet exposures include undrawn and partially drawn residential mortgage loans as well as commitments to lend. Commitments to lend are formal offers for housing lending which have been accepted by the customer.

Unaudited	30/09/2017		Total NZ\$m
	On-balance sheet NZ\$m	Off-balance sheet NZ\$m	
LVR range			
Does not exceed 60%	33,292	5,227	38,519
Exceeds 60% and not 70%	15,974	1,346	17,320
Exceeds 70% and not 80%	16,725	1,168	17,893
Does not exceed 80%	65,991	7,741	73,732
Exceeds 80% and not 90%	2,648	137	2,785
Exceeds 90%	1,449	188	1,637
Total	70,088	8,066	78,154

Reconciliation of mortgage related amounts

Unaudited	Note	30/09/2017 NZ\$m
Term loans - housing	13	72,524
Less: fair value hedging adjustment		(44)
Less: housing loans made to corporate customers		(2,414)
Add: unsettled re-purchases of mortgages from the NZ Branch		22
On-balance sheet retail mortgage exposures subject to the IRB approach	18	70,088
Add: off-balance sheet retail mortgage exposures subject to the IRB approach		8,066
Total retail mortgage exposures subject to the IRB approach (as per LVR analysis)		78,154

27. SUBSIDIARIES

The following table lists the principal subsidiaries of the Bank. Principal subsidiaries are those that have transactions or balances with parties outside the Banking Group. All subsidiaries are 100% owned and incorporated in New Zealand.

Principal subsidiaries	Nature of business
ANZ Investment Services (New Zealand) Limited	Funds management
ANZ New Zealand (Int'l) Limited	Finance
ANZ New Zealand Investments Limited	Funds management
ANZ New Zealand Securities Limited	On-line share broker
ANZNZ Covered Bond Trust ¹	Securitisation entity
Arawata Assets Limited	Property
Karapiro Investments Limited	Asset finance
Kingfisher NZ Trust 2008-1 ¹	Securitisation entity
OnePath Life (NZ) Limited	Insurance
UDC Finance Limited	Asset finance

¹ The Banking Group does not own ANZNZ Covered Bond Trust and Kingfisher NZ Trust 2008-1. Control exists as the Banking Group retains substantially all the risks and rewards of the operations. Details of the Banking Group's interest in consolidated structured entities is included in note 28.

NOTES TO THE FINANCIAL STATEMENTS

28. STRUCTURED ENTITIES, TRANSFERRED FINANCIAL ASSETS, FIDUCIARY ACTIVITIES AND INSURANCE

Structured entities

The Banking Group's involvement with structured entities is mainly through securitisations and its funds management activities, which are outlined further below. The Banking Group has involvement with structured entities that may be established either by the Banking Group or by a third party.

Consolidated structured entities

Kingfisher NZ Trust 2008-1 (the Kingfisher Trust)

The Banking Group has established the Kingfisher Trust as an in-house residential mortgage backed securities facility that can issue securities meeting the RBNZ criteria to use as collateral in repurchase transactions with the RBNZ.

These assets do not qualify for derecognition as the Bank retains substantially all of the risks and rewards of the transferred assets.

As at 30 September 2017 and 30 September 2016 the Banking Group had not entered into any repurchase agreements with the RBNZ for residential mortgage backed securities and therefore no collateral had been accepted by the RBNZ under this facility.

ANZNZ Covered Bond Trust (the Covered Bond Trust)

Substantially all of the assets of the Covered Bond Trust are made up of certain housing loans and related securities originated by the Bank which are security for the guarantee by ANZNZ Covered Bond Trust Limited as trustee of the Covered Bond Trust of issuances of covered bonds by the Bank, or its wholly owned subsidiary ANZ New Zealand (Int'l) Limited, from time to time. The assets of the Covered Bond Trust are not available to creditors of the Bank, although the Bank (or its liquidator or statutory manager) may have a claim against the residual assets of the Covered Bond Trust (if any) after all prior ranking creditors of the Covered Bond Trust have been satisfied.

The Banking Group continues to recognise the assets of the Covered Bond Trust on its balance sheet as, although they are pledged as security for covered bonds, the Bank retains substantially all the risks and rewards of ownership.

Unconsolidated securitisations

The Banking Group also has an interest in unconsolidated securitisation entities through the provision of funding facilities or holding bonds or notes issued by such entities. The Banking Group's exposure to these entities is not material.

Transferred financial assets

In the normal course of business the Banking Group enters into transactions where it transfers financial assets directly to third parties or to structured entities. These transfers may give rise to the Banking Group fully, or partially, derecognising those financial assets - depending on the Banking Group's exposure to the risks and rewards or control over the transferred assets. If the Banking Group retains substantially all of the risk and rewards of a transferred asset, the transfer does not qualify for derecognition and the asset remains on the Banking Group's balance sheet in its entirety.

Assets transferred to the Kingfisher Trust and the Covered Bond Trust

The Bank has purchased securities issued by both the Kingfisher Trust and the Covered Bond Trust in exchange for the transfer of the rights to the cash flows associated with the identified residential mortgages. As at 30 September 2017, NZ\$20,551 million of assets were held in the Kingfisher Trust and the Covered Bond Trust (2016: NZ\$19,656 million).

Repurchase transactions

Securities sold subject to repurchase agreements are not derecognised when substantially all the risks and rewards of ownership remain with the Bank. See note 21 for details of securities sold under agreements to repurchase. The amount of trading securities encumbered through repurchase agreements is shown in note 22. The carrying amount of the associated liabilities is not materially different to the amount of trading securities subject to the repurchase agreement.

NOTES TO THE FINANCIAL STATEMENTS

Funds management and other fiduciary activities

Funds management

Certain subsidiaries of the Bank act as trustee and/or manager for a number of unit trusts and investment and superannuation funds. The Banking Group provides private banking services to a number of clients, including investment advice and portfolio management. The Banking Group is not responsible for any decline in performance of the underlying assets of the investors due to market forces.

As funds under management are not controlled by the Banking Group, they are not included in these financial statements. The Banking Group derives fee and commission income from the sale and management of investment funds and superannuation schemes, unit trusts and the provision of private banking services to customers. The Banking Group derives commission income from the sale of third party funds management products.

Some funds under management are invested in products owned or securities issued by the Banking Group and are recorded as liabilities in the balance sheet. At 30 September 2017, NZ\$3,964 million of funds under management were invested in the Banking Group's own products or securities (2016: NZ\$3,698 million).

Custodial services

The Banking Group provides custodial services to customers in respect of assets that are beneficially owned by those customers.

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Kiwisaver	11,047	9,295
Bonus Bonds Scheme	3,405	3,561
Other managed funds	1,984	1,924
ANZ PIE Fund ¹	1,381	953
Discretionary Investment Management Service (DIMS) ²	7,193	7,007
Other investment portfolios ²	3,480	3,745
Total funds under management	28,490	26,485
Funds under custodial arrangements	7,720	7,408
Other funds held or managed subject to fiduciary responsibilities	1,557	1,927
Funds management fee income from structured entities	170	156

¹ The Banking Group established, and is considered to be the sponsor of, the ANZ PIE Fund. The ANZ PIE Fund invests only in deposits with the Bank. The Banking Group does not receive a management fee from, and does not have an interest in, the ANZ PIE Fund.

² These funds are not structured entities as they are investment portfolios managed on behalf of customers.

Provision of financial services

Financial services provided by the Banking Group to entities which are involved in trust, custodial, funds management and other fiduciary activities are provided on arm's length terms and conditions and at fair value. Any assets purchased from such entities have been purchased on an arm's length basis and at fair value. The Banking Group does not have any affiliated insurance entities or affiliated insurance groups that are not members of the Banking Group.

Except for standard lending facilities provided in the normal course of business on arm's length terms, the Banking Group has not provided any funding to entities where trust, custodial, funds management or other fiduciary activities are established, marketed and/or sponsored by a member of the Banking Group (2016: nil).

Insurance business

The Banking Group conducts insurance business through its subsidiary OnePath Life (NZ) Limited (OnePath Life).

The Banking Group's aggregate amount of insurance business comprises the total consolidated assets of OnePath Life of NZ\$921 million (2016: NZ\$926 million), which is 0.6% (2016: 0.6%) of the total consolidated assets of the Banking Group.

Risk management

The Bank and subsidiaries of the Bank participating in the activities identified above have in place policies and procedures to ensure that those activities are conducted in an appropriate manner. Should adverse conditions arise, it is considered that these policies and procedures will minimise the possibility that these conditions will adversely impact the Bank or the Banking Group. The policies and procedures include comprehensive and prominent disclosure of information regarding products, and formal and regular review of operations and policies by management.

NOTES TO THE FINANCIAL STATEMENTS

29. ASSETS AND LIABILITIES HELD FOR SALE

On 11 January 2017, the Bank announced that it had entered into a conditional agreement to sell UDC to HNA Group. The sale is subject to certain conditions (including regulatory approvals) and the Banking Group is working with HNA Group towards completion of the sale.

The assets and liabilities of UDC are classified as held for sale as at 30 September 2017. The following assets and liabilities of UDC held for sale are measured at the lower of their carrying amount and fair value less costs to sell, except for assets such as deferred tax assets and financial assets which are specifically exempt from this requirement.

	30/09/2017
	NZ\$m
Net loans and advances	2,912
Goodwill	133
Other assets	20
Total UDC assets held for sale	3,065
Deposits and other borrowings	1,039
Payables and other liabilities	33
Current tax liabilities	24
Deferred tax liabilities	(9)
Employee entitlements	1
Total UDC liabilities held for sale	1,088

NOTES TO THE FINANCIAL STATEMENTS

30. RELATED PARTY DISCLOSURES

Key management personnel

Key management personnel (KMP) are defined as directors and those executives who report directly to the Bank's Chief Executive Officer with responsibility for the strategic direction and management of a major revenue generating division or who control material revenue and expenses.

Loans made to directors and other KMP are made in the ordinary course of business on normal commercial terms and conditions no more favourable than those given to other employees or customers, including the term of the loan, security required and the interest rate.

All other transactions with KMP and their related parties are made on terms equivalent to those that prevail in arm's length transactions. These transactions generally involve the provision of financial and investment services. All such transactions that have occurred with KMP and their related parties have been trivial or domestic in nature. In this context, transactions are only disclosed when they are considered of interest to the users of the financial statements in making and evaluating decisions about the allocation of scarce resources.

	Year to 30/09/2017 NZ\$000	Year to 30/09/2016 NZ\$000
Key management personnel compensation		
Salaries and short-term employee benefits	11,430	11,382
Post-employment benefits	480	280
Other long-term benefits	60	88
Share-based payments expense	3,515	4,123
Total compensation of key management personnel	15,485	15,873
Loans to, and securities held by, key management personnel and their related parties		
Loans	5,102	7,373
Unsubordinated debt	520	520
Subordinated debt	190	190

Transactions with other related parties

The Bank and Banking Group undertake transactions with the Immediate Parent Company, the Ultimate Parent Bank, other members of the Overseas Banking Group and associates.

These transactions principally consist of funding and hedging transactions, the provision of other financial and investment services, technology and process support, and compensation for share based payments made to Banking Group employees. Transactions with related parties outside of the Banking Group are conducted on an arm's length basis and on normal commercial terms.

In addition the Bank undertakes similar transactions with subsidiaries, which are eliminated in the consolidated Banking Group financial statements. Included within the Bank's transactions with subsidiaries is the provision of administrative functions to some subsidiaries for which no payments have been made.

Transactions with related parties

	Year to 30/09/2017 NZ\$m	Year to 30/09/2016 NZ\$m
Ultimate Parent Bank and subsidiaries not part of the Banking Group		
Interest income	32	49
Interest expense	146	87
Fee income	14	19
Gain/(loss) on sale of mortgages to the NZ Branch	(1)	1
Other operating income	23	19
Operating expenses	46	64
Mortgages sold to the NZ Branch	481	697
Immediate Parent Company		
Interest expense	1	1
Associates		
Direct fee expense	10	10
Dividends received	5	2
Share of associates' profit	5	5

NOTES TO THE FINANCIAL STATEMENTS

Balances with related parties

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Ultimate Parent Bank and subsidiaries not part of the Banking Group		
Cash	64	47
Settlement balances receivable	111	31
Collateral paid	-	375
Derivative financial instruments	2,623	4,361
Other assets	42	108
Immediate Parent Company		
Derivative financial instruments	4	-
Associates		
Investments in associates	7	7
Total due from related parties	2,851	4,929
Ultimate Parent Bank and subsidiaries not part of the Banking Group		
Settlement balances payable	220	323
Collateral received	198	-
Deposits and other borrowings	11	-
Derivative financial instruments	2,486	4,818
Payables and other liabilities	31	32
Subordinated debt	1,951	1,951
Immediate Parent Company		
Deposits and other borrowings	62	29
Associates		
Payables and other liabilities	1	1
Total due to related parties	4,960	7,154

Balances due from / to related parties are unsecured. The Bank has provided guarantees and commitments to related parties as follows:

	30/09/2017	30/09/2016
	NZ\$m	NZ\$m
Financial guarantees provided to the Ultimate Parent Bank	155	152
Undrawn credit commitments provided to the Immediate Parent Company	250	250

NOTES TO THE FINANCIAL STATEMENTS

31. CAPITAL EXPENDITURE AND OPERATING LEASE COMMITMENTS

	30/09/2017 NZ\$m	30/09/2016 NZ\$m
Contracts for outstanding capital expenditure		
Not later than 1 year	4	5
Future minimum lease payments under non-cancellable operating leases		
Not later than 1 year	84	87
Later than 1 year but not later than 5 years	256	217
Later than 5 years	144	151
Total operating lease commitments	484	455
Total commitments	488	460

32. COMPENSATION OF AUDITORS

	Year to 30/09/2017 NZ\$000	Year to 30/09/2016 NZ\$000
Compensation of auditors (KPMG New Zealand)		
Audit or review of financial statements ¹	2,227	2,219
Other services:		
Prudential and regulatory services ²	225	262
Offer documents assurance or review	146	100
Other assurance services ³	95	52
Total other services	466	414
Total compensation of auditors relating to the Banking Group	2,693	2,633
Fees relating to certain managed funds and not recharged ⁴	46	48
Total compensation of auditors	2,739	2,681

¹ Includes fees for both the audit of the annual financial statements and reviews of interim financial statements.

² Includes fees for reviews and controls reports required by regulations.

³ Includes fees for controls reports, comfort letters and other agreed upon procedures engagements.

⁴ Amounts relate to the ANZ PIE Fund and certain other funds, and include fees for audits of annual financial statements and audits of summary financial statements for inclusion in offer documents, comfort letters and other agreed upon procedures engagements.

It is the Banking Group's policy that, subject to the approval of the Ultimate Parent Bank's Audit Committee, KPMG can provide assurance and other audit-related services that, while outside the scope of the statutory audit, are consistent with the role of auditor. KPMG may not provide services that are perceived to be in conflict with the role of auditor. Services that are perceived to be in conflict with the role of auditor include consulting advice and subcontracting of operational activities normally undertaken by management, and engagements where the auditor may ultimately be required to express an opinion on its own work.

NOTES TO THE FINANCIAL STATEMENTS

33. CONCENTRATIONS OF CREDIT RISK TO INDIVIDUAL COUNTERPARTIES

The Banking Group measures its concentration of credit risk using actual exposures for bank counterparties and limits for non bank counterparties. No account is taken of collateral, security and/or netting agreements which the Banking Group may hold in respect of the various counterparty exposures.

For the three months ended 30 September 2017 there were no individual counterparties (excluding connected parties, governments and banks with long term credit ratings of A- or above) where the Banking Group's period end or peak end-of-day credit exposure equalled or exceeded 10% of equity (as at the end of the period).

Concentrations of credit risk to connected persons

Credit exposures to connected persons reported in the table below have been calculated partially on a bilateral net basis and partially on a gross basis. Netting has occurred (up to a limit of 125% of the Banking Group's tier 1 capital) in respect of certain transactions which are the subject of a bilateral netting agreement.

This information has been derived in accordance with the Bank's conditions of registration and the RBNZ document *Connected Exposures Policy* (BS8). The exposures are net of individual credit impairment allowances and exclude advances to connected persons of a capital nature.

	30/09/2017		30/09/2016	
	Amount NZ\$m	% of Tier 1 Capital	Amount NZ\$m	% of Tier 1 Capital
Aggregate at end of year¹				
Bank connected persons (on gross basis, before netting)	8,074	70.2%	9,349	81.3%
Less: amount netted off	5,230	45.5%	7,619	66.2%
Bank connected persons (on partial bilateral net basis)	2,844	24.7%	1,730	15.1%
Non-bank connected persons ²	-	0.0%	1	0.0%
Peak end-of-day for the year³				
Bank connected persons (on gross basis, before netting)	8,382	72.9%	9,352	81.3%
Less: amount netted off	5,336	46.4%	5,353	46.5%
Bank connected persons (on partial bilateral net basis)	3,046	26.5%	3,999	34.8%
Non-bank connected persons ²	1	0.0%	4	0.0%
Rating-contingent limit⁴				
Bank connected persons (on a gross basis, before netting)	n/a	125.0%	n/a	125.0%
Bank connected persons (on partial bilateral net basis)	n/a	60.0%	n/a	70.0%
Non-bank connected persons	n/a	15.0%	n/a	15.0%

¹ The Banking Group has amounts due from the Immediate Parent Company and the Ultimate Parent Bank and other entities within the Overseas Banking Group arising in the ordinary course of business. These balances arise primarily from unrealised gains on trading and hedging derivative financial instruments with the Ultimate Parent Bank. As at 30 September 2017, the gross exposures to the Immediate Parent Company were NZ\$7 million (2016: NZ\$3 million). As at 30 September 2017, the gross exposures to the Ultimate Parent Bank were NZ\$8,067 million (2016: NZ\$9,346 million).

² Non-bank connected persons exposures comprise loans to directors of the Bank.

³ The Banking Group has complied with the limits on aggregate credit exposure (of a non-capital nature and net of individual provisions) to connected persons and non-bank connected persons, as set out in the Conditions of Registration, at all times during the year. The peak end-of-day credit exposure ratios for the year to connected persons are measured over Tier 1 Capital as at the end of the year. Previously Tier 1 Capital as at the beginning of the month in which the peak aggregate amount of credit exposure occurred was used to calculate the peak ratios, and comparative ratios have been updated. Both methods are allowed by the Order, and the change was made to make these disclosures consistent with private regulatory reporting submitted to the RBNZ.

⁴ Represents the maximum peak end-of-day aggregate credit exposures limit (of a non-capital nature and net of individual provisions) to all connected persons. This limit is based on the ratings applicable to the Bank's long term senior unsecured obligations payable in New Zealand in New Zealand dollars. Within the overall limit a sub-limit of 15% of Tier 1 Capital applies to aggregate credit exposures (exclusive of exposures of a capital nature and net of individual provisions) to non-bank connected persons. There have been no changes to these limits for the year ended 30 September 2017.

NOTES TO THE FINANCIAL STATEMENTS

34. RISK MANAGEMENT FRAMEWORK

The Banking Group recognises the importance of effective risk management to its business success. Management is committed to achieving strong control and a distinctive risk management capability that enables the Banking Group business units to meet their performance objectives.

The Banking Group approaches risk through managing the various elements of the system as a whole rather than viewing them as independent and unrelated parts. The risk management division (Risk Management) is independent of the business, with clear delegations from the Board, and operates within a comprehensive framework comprising:

- The Board providing leadership, setting risk appetite/strategy and monitoring progress
- A strong framework for development and maintenance of Banking Group-wide risk management policies, procedures and systems, overseen by an independent team of risk professionals
- The use of sophisticated risk tools, applications and processes to execute the global risk management strategy across the Banking Group
- Business unit level accountability, as the “first line of defence”, for the management of risks in alignment with the Banking Group’s strategy
- Independent oversight to ensure business unit level compliance with policies, regulations and laws, and to provide regular risk evaluation and reporting.

The Banking Group manages risk through an approval, delegation and limits structure. Regular reviews of the policies, systems and risk reports, including the effectiveness of the risk management systems, discussions covering the Banking Group’s response to emerging risk issues and trends, and that the requisite culture and practices are in place across the Banking Group, are conducted within the Banking Group and also by the Ultimate Parent Bank. The Board has responsibility for reviewing all aspects of risk management.

The Board has ultimate responsibility for overseeing the effective deployment of risk management frameworks, policies and processes within New Zealand. The Bank’s Risk Committee assists the Board in this function. The role of the Risk Committee is to assist the Board in the effective discharge of its responsibilities for business, market, credit, operational, compliance, liquidity, product and reputational risk management, and to liaise and consult with the Ultimate Parent Bank Risk Committee as required. Risk Management, via the Chief Risk Officer, coordinates risk management activities directly between Business Unit risk functions and Ultimate Parent Bank Group Risk Management functions.

The risk management process is subject to oversight by the Risk Committee of the Ultimate Parent Bank Board. This includes the review of risk portfolios and the establishment of prudential policies and controls.

The Banking Group’s risk management policies are essentially the same as the Ultimate Parent Bank, but are tailored where required to suit the local New Zealand regulatory and business environment.

The Audit Committee has responsibility for ensuring the integrity of the Banking Group’s financial controls, reporting systems and internal audit standards. It meets at least four times a year and reports directly to the Board. All members of the Audit Committee are non-executive directors.

Financial risk management

Refer to note 18 for detailed disclosures on the Banking Group’s financial risk management policies.

Operational Risk

Operational risk is the risk arising from day to day operational activities which may result in direct or indirect loss. These losses may result from failure to comply with policies, procedures, laws and regulations, from fraud or forgery, from a breakdown in the availability or integrity of services, systems and information, or damage to the Banking Group’s reputation.

Examples include failure to comply with policy and legislation, human error, natural disasters, fraud and other malicious acts. Where appropriate, risks are mitigated by insurance.

Risk Management is responsible for establishing the Banking Group’s operational risk framework and associated Banking Group-wide policies. Business units are responsible for the identification, analysis, assessment and treatment of operational risks on a day-to-day basis.

Business units have primary responsibility for the identification and management of operational risk with executive oversight provided through business unit Risk Forums. The Bank’s Operational Risk Executive Committee (OREC) undertakes the governance function through the bi-monthly monitoring of operational risk performance across the Banking Group. The Board and Risk Management conduct effective oversight through the approval of operational risk policies and frameworks and monitoring key operational risk metrics.

Compliance

The Banking Group conducts its business in accordance with all relevant compliance requirements. In order to assist the Banking Group identify, manage, monitor and measure its compliance obligations, the Banking Group has a comprehensive compliance framework in place, which addresses both external (regulatory) and internal compliance.

Risk Management, in conjunction with business unit staff ensure the Banking Group operates within a compliance infrastructure and framework that incorporates new and changing business obligations and processes.

NOTES TO THE FINANCIAL STATEMENTS

The compliance policies and their supporting framework seek to minimise material risks to the Banking Group's reputation and value that could arise from non-compliance with laws, regulations, industry codes and internal standards and policies. Business units have primary responsibility for the identification and management of compliance. Risk Management provides policy and framework, measurement, monitoring and reporting, as well as leadership in areas such as anti-money laundering procedures and matters of prudential compliance. The Bank's OREC, the Chief Risk Officer, the Board and the Risk Committee of the Ultimate Parent Bank Board conduct board and executive oversight.

Internal Audit

Internal Audit is a function independent of management whose role is to provide the Board and management with an effective and independent appraisal of the internal controls established by management. Operating under a Board approved Charter, the reporting line for the outcomes of work conducted by Internal Audit is direct to the Chair of the Audit Committee, with a direct communication line to the Chief Executive Officer and the external auditor.

The Internal Audit Plan is developed utilising a risk based approach and is refreshed on a quarterly basis. The Audit Committee approves the plan.

All audit activities are conducted in accordance with local and international auditing standards, and the results of the activities are reported to the Audit Committee, Risk Committee and management. These results influence the performance assessment of business heads.

Furthermore, Internal Audit monitors the remediation of audit issues and reports the current status of any outstanding audits.

HISTORICAL SUMMARY OF FINANCIAL STATEMENTS

	Year to 30/09/2017	Year to 30/09/2016	Year to 30/09/2015	Year to 30/09/2014	Year to 30/09/2013
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Interest income	6,198	6,423	6,926	6,272	5,957
Interest expense	3,161	3,421	4,051	3,529	3,344
Net interest income	3,037	3,002	2,875	2,743	2,613
Non-interest income	938	852	1,175	1,085	823
Operating income	3,975	3,854	4,050	3,828	3,436
Operating expenses	1,468	1,599	1,512	1,489	1,512
Credit impairment charge / (release)	62	150	74	(16)	63
Profit before income tax	2,445	2,105	2,464	2,355	1,861
Income tax expense	680	570	681	639	490
Profit after income tax	1,765	1,535	1,783	1,716	1,371
Dividends paid	(1,695)	(1,363)	(1,760)	(2,353)	(1,065)
Share capital issued	-	-	675	970	300
	As at 30/09/2017	As at 30/09/2016	As at 30/09/2015	As at 30/09/2014	As at 30/09/2013
	NZ\$m	NZ\$m	NZ\$m	NZ\$m	NZ\$m
Total impaired assets	357	426	382	634	901
Total assets	153,973	160,819	147,527	128,915	120,444
Total liabilities	141,192	148,109	135,074	117,134	108,990
Equity	12,781	12,710	12,453	11,781	11,454

The amounts included in this summary have been taken from the audited financial statements of the Banking Group.

GENERAL DISCLOSURES

General Matters

The Disclosure Statement has been issued in accordance with the Order.

The Bank is incorporated under the Companies Act 1993. The Bank is wholly owned by its Immediate Parent Company and ultimately by the Ultimate Parent Bank. The Immediate Parent Company of the Bank is incorporated in New Zealand and owned by ANZ Funds Pty Limited and the Ultimate Parent Bank (both incorporated in Australia). The address for service for the Ultimate Parent Bank is ANZ Centre Melbourne, Level 9, 833 Collins Street, Docklands, Victoria 3008, Australia.

The Immediate Parent Company has the power under the Bank's Constitution to appoint any person as a Director of the Bank either to fill a casual vacancy or as an additional Director or to remove any person from the office of Director, from time to time by giving written notice to the Bank. No appointment of a new Director may occur unless the RBNZ confirms that it does not object to the appointment.

Financial Support

The Ultimate Parent Bank may not provide financial support in breach of the Australian Banking Act 1959 (the Act). Under the Act:

- APRA must exercise its powers and functions for the protection of a bank's depositors in Australia and
- in the event of a bank becoming unable to meet its obligations or suspending payment, the assets of the bank in Australia will be available to meet that bank's deposit liabilities in Australia in priority to all other liabilities of the bank.

Under APRA's Prudential Standards, the Ultimate Parent Bank's ability to provide financial support to the Bank is subject to certain requirements:

- The Ultimate Parent Bank should not undertake any third party dealings with the prime purpose of supporting the business of the Bank.
- The Ultimate Parent Bank should not hold unlimited exposures (should be limited as to specified time and amount) in the Bank (e.g. not provide a general guarantee covering any of the Bank's obligations).
- The Ultimate Parent Bank should not enter into cross-default clauses whereby a default by the Bank on an obligation (whether financial or otherwise) is deemed to trigger a default by the Ultimate Parent Bank on its obligations.
- The level of exposure of the Ultimate Parent Bank's Level 1 capital base to the Bank should not exceed:
 - 50% on an individual exposure basis or
 - 150% in aggregate (being exposures to all similar regulated entities related to the Ultimate Parent Bank).

In addition, APRA has reviewed the level of financial exposures that can be provided to the respective New Zealand banking subsidiaries and branches (New Zealand operations) of the four Australian parent banks, including the Ultimate Parent Bank.

APRA has confirmed that by 1 January 2021 no more than 5% of the Ultimate Parent Bank's Level 1 Tier 1 capital base can comprise non-equity exposures to its New Zealand operations during ordinary times. Exposures in excess of this limit as at 1 January 2016 must be reduced in equal percentages over the five year transition period and may not increase above the exposures as at 30 June 2015. This limit does not include holdings of capital instruments or eligible secured contingent funding support provided to the Bank during times of financial stress.

The Ultimate Parent Bank established a New Zealand branch which was registered on 5 January 2009. The Bank sells, from time-to-time, residential mortgages into the NZ Branch to provide funding for the Bank's business. As at 30 September 2017, the NZ Branch held approximately NZ\$4.3 billion of residential mortgages. To satisfy APRA's requirements described above, the Bank intends to repay this funding at approximately NZ\$1.6 billion per annum over the transition period ending 31 December 2020.

APRA has also stated that contingent funding support by the Ultimate Parent Bank to the Bank during times of financial stress must be provided on terms that are acceptable to APRA and the Ultimate Parent Bank's exposures to the Bank and its other New Zealand operations must not exceed 50% of the Ultimate Parent Bank's Level 1 Tier 1 capital base. At present, only covered bonds meet APRA's criteria for contingent funding. On this basis, the Ultimate Parent Bank believes it will be able to continue to provide financial support to the Bank.

Further, from 1 July 2017, APRA's Level 3 Conglomerates regulations became effective which limit the financial and operational assistance the Ultimate Parent Bank can provide the Bank.

In determining the acceptable level of financial and operational exposure to the Bank, the Board of the Ultimate Parent Bank should have regard to:

- the exposures that would be approved for third parties of broadly equivalent credit status
- the impact on the Ultimate Parent Bank's capital and liquidity position and
- the Ultimate Parent Bank's ability to continue operating in the event of a failure by the Bank.

These requirements are not expected to place additional restrictions on the Ultimate Parent Bank's ability to provide financial or operational support to the Bank.

Guarantors

No material obligations of the Bank are guaranteed as at 15 November 2017.

GENERAL DISCLOSURES

ANZNZ Covered Bond Trust

Certain debt securities (Covered Bonds) issued by the Bank's wholly owned subsidiary, ANZ New Zealand (Int'l) Limited, are guaranteed by ANZNZ Covered Bond Trust Limited (the Covered Bond Guarantor), solely in its capacity as trustee of ANZNZ Covered Bond Trust. The Covered Bond Guarantor has guaranteed the payment of interest and principal of Covered Bonds with a carrying value as at 30 September 2017 of NZ\$5,325 million, pursuant to a guarantee which is secured over a pool of assets. The Covered Bond Guarantor's address for service is Level 9, 34 Shortland Street, Auckland, New Zealand. The Covered Bond Guarantor is not a member of the Banking Group and has no credit ratings applicable to its long term senior unsecured obligations. The Covered Bonds have been assigned a long term rating of Aaa and AAA by Moody's Investors Service and Fitch Ratings respectively. Details of the pool of assets that secure this guarantee are provided in note 28.

Credit Rating Information

As at 15 November 2017 the Bank has three credit ratings, which are applicable to its long-term senior unsecured obligations which are payable in New Zealand in New Zealand dollars. On 19 June 2017, Moody's Investors Service downgraded the Bank's credit rating from Aa3 to A1 and changed the outlook on the Bank from Negative to Stable.

The Bank's credit ratings are:

Rating Agency	Current Credit Rating	Qualification
Standard & Poor's	AA-	Outlook Negative
Moody's Investors Service	A1	Outlook Stable
Fitch Ratings	AA-	Outlook Stable

The following table describes the credit rating grades available:

	Standard & Poor's	Moody's Investors Service	Fitch Ratings
The following grades display investment grade characteristics:			
Ability to repay principal and interest is extremely strong. This is the highest investment category.	AAA	Aaa	AAA
Very strong ability to repay principal and interest.	AA	Aa	AA
Strong ability to repay principal and interest although somewhat susceptible to adverse changes in economic, business or financial conditions.	A	A	A
Adequate ability to repay principal and interest. More vulnerable to adverse changes.	BBB	Baa	BBB
The following grades have predominantly speculative characteristics:			
Significant uncertainties exist which could affect the payment of principal and interest on a timely basis.	BB	Ba	BB
Greater vulnerability and therefore greater likelihood of default.	B	B	B
Likelihood of default now considered high. Timely repayment of principal and interest is dependent on favourable financial conditions.	CCC	Caa	CCC
Highest risk of default.	CC to C	Ca to C	CC to C
Obligations currently in default.	D	-	RD & D

Credit ratings from Standard & Poor's and Fitch Ratings may be modified by the addition of "+" or "-" to show the relative standing within the "AA" to "B" categories. Moody's Investors Service applies numerical modifiers 1, 2, and 3 to each of the "Aa" to "Caa" classifications, with 1 indicating the higher end and 3 the lower end of the rating category.

CONDITIONS OF REGISTRATION

Conditions of Registration, applicable as at 30 September 2017. These Conditions of Registration have applied from 1 October 2016.

The registration of ANZ Bank New Zealand Limited ("the bank") as a registered bank is subject to the following conditions:

1. That-
 - (a) the Total capital ratio of the banking group is not less than 8%;
 - (b) the Tier 1 capital ratio of the banking group is not less than 6%;
 - (c) the Common Equity Tier 1 capital ratio of the banking group is not less than 4.5%;
 - (d) the Total capital of the banking group is not less than \$30 million; and
 - (e) the bank must not include the amount of an Additional Tier 1 capital instrument or Tier 2 capital instrument issued after 1 January 2013 in the calculation of its capital ratios unless it has received a notice of non-objection to the instrument from the Reserve Bank; and
 - (f) the bank meets the requirements of Part 3 of the Reserve Bank of New Zealand document: "Application requirements for capital recognition or repayment and notification requirements in respect of capital" (BS16) dated November 2015 in respect of regulatory capital instruments.

For the purposes of this condition of registration,-

the scalar referred to in the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015 is 1.06.

"Total capital ratio", "Tier 1 capital ratio", "Common Equity Tier 1 capital ratio", and "Total capital" must be calculated in accordance with the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015.

an Additional Tier 1 capital instrument is an instrument that meets the requirements of subsection 2.13(a) or (c) of the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015.

a Tier 2 capital instrument is an instrument that meets the requirements of subsection 2.16(a) or (c) of the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015.

1A. That-

- (a) the bank has an internal capital adequacy assessment process ("ICAAP") that accords with the requirements set out in the document "Guidelines on a bank's internal capital adequacy assessment process ("ICAAP")" (BS12) dated December 2007;
- (b) under its ICAAP the bank identifies and measures its "other material risks" defined as all material risks of the banking group that are not explicitly captured in the calculation of the Common Equity Tier 1 capital ratio, the Tier 1 capital ratio and the Total capital ratio under the requirements set out in the document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015; and
- (c) the bank determines an internal capital allocation for each identified and measured "other material risk".

1B. That the banking group complies with all requirements set out in the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015.

1C. That, if the buffer ratio of the banking group is 2.5% or less, the bank must:

- (a) according to the following table, limit the aggregate distributions of the bank's earnings to the percentage limit to distributions that corresponds to the banking group's buffer ratio:

Banking group's buffer ratio	Percentage limit to distributions of the bank's earnings
0% - 0.625%	0%
>0.625 - 1.25%	20%
>1.25 - 1.875%	40%
>1.875% - 2.5%	60%

- (b) prepare a capital plan to restore the banking group's buffer ratio to above 2.5% within any timeframe determined by the Reserve Bank for restoring the buffer ratio; and
- (c) have the capital plan approved by the Reserve Bank.

For the purposes of this condition of registration, —

"buffer ratio", "distributions", and "earnings" have the same meaning as in Part 3 of the Reserve Bank of New Zealand document: "Capital Adequacy Framework (Internal Models Based Approach)" (BS2B) dated November 2015.

the scalar referred to in the Reserve Bank of New Zealand document "Capital adequacy framework (Internal Models Based Approach)" (BS2B) dated November 2015 is 1.06.

CONDITIONS OF REGISTRATION

2. That the banking group does not conduct any non-financial activities that in aggregate are material relative to its total activities.
In this condition of registration, the meaning of “material” is based on generally accepted accounting practice.
3. That the banking group’s insurance business is not greater than 1% of its total consolidated assets.
For the purposes of this condition of registration, the banking group’s insurance business is the sum of the following amounts for entities in the banking group:
 - (a) if the business of an entity predominantly consists of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total consolidated assets of the group headed by the entity; and
 - (b) if the entity conducts insurance business and its business does not predominantly consist of insurance business and the entity is not a subsidiary of another entity in the banking group whose business predominantly consists of insurance business, the amount of the insurance business to sum is the total liabilities relating to the entity’s insurance business plus the equity retained by the entity to meet the solvency or financial soundness needs of its insurance business.

In determining the total amount of the banking group’s insurance business-

- (a) all amounts must relate to on balance sheet items only, and must comply with generally accepted accounting practice; and
- (b) if products or assets of which an insurance business is comprised also contain a non-insurance component, the whole of such products or assets must be considered part of the insurance business.

For the purposes of this condition of registration,-

“insurance business” means the undertaking or assumption of liability as an insurer under a contract of insurance:

“insurer” and “contract of insurance” have the same meaning as provided in sections 6 and 7 of the Insurance (Prudential Supervision) Act 2010.

4. That the aggregate credit exposures (of a non-capital nature and net of any allowances for impairment) of the banking group to all connected persons do not exceed the rating-contingent limit outlined in the following matrix:

Credit Rating of the bank ¹	Connected exposure limit (% of the banking group’s Tier 1 capital)
AA/Aa2 and above	75
AA-/Aa3	70
A+/A1	60
A/A2	40
A-/A3	30
BBB+/Baa1 and below	15

¹ This table uses the rating scales of Standard & Poor’s, Fitch Ratings and Moody’s Investors Service. (Fitch Ratings’ scale is identical to Standard & Poor’s)

Within the rating-contingent limit, credit exposures (of a non-capital nature and net of any allowances for impairment) to non-bank connected persons shall not exceed 15 percent of the banking group’s Tier 1 capital.

For the purposes of this condition of registration, compliance with the rating-contingent connected exposure limit is determined in accordance with the Reserve Bank of New Zealand document entitled “Connected Exposures Policy” (BS8) dated November 2015.

5. That exposures to connected persons are not on more favourable terms (e.g. as relates to such matters as credit assessment, tenor, interest rates, amortisation schedules and requirement for collateral) than corresponding exposures to non-connected persons.
6. That the bank complies with the following corporate governance requirements:
 - (a) the board of the bank must have at least five directors;
 - (b) the majority of the board members must be non-executive directors;
 - (c) at least half of the board members must be independent directors;
 - (d) an alternate director,—
 - (i) for a non-executive director must be non-executive; and
 - (ii) for an independent director must be independent;
 - (e) at least half of the independent directors of the bank must be ordinarily resident in New Zealand;
 - (f) the chairperson of the board of the bank must be independent; and
 - (g) the bank’s constitution must not include any provision permitting a director, when exercising powers or performing duties as a director, to act other than in what he or she believes is the best interests of the company (i.e. the bank).

For the purposes of this condition of registration, “non-executive” and “independent” have the same meaning as in the Reserve Bank of New Zealand document entitled “Corporate Governance” (BS14) dated July 2014.

CONDITIONS OF REGISTRATION

7. That no appointment of any director, chief executive officer, or executive who reports or is accountable directly to the chief executive officer, is made in respect of the bank unless:
 - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
 - (b) the Reserve Bank has advised that it has no objection to that appointment.
8. That a person must not be appointed as chairperson of the board of the bank unless:
 - (a) the Reserve Bank has been supplied with a copy of the curriculum vitae of the proposed appointee; and
 - (b) the Reserve Bank has advised that it has no objection to that appointment.
9. That the bank has a board audit committee, or other separate board committee covering audit matters, that meets the following requirements:
 - (a) the mandate of the committee must include: ensuring the integrity of the bank's financial controls, reporting systems and internal audit standards;
 - (b) the committee must have at least three members;
 - (c) every member of the committee must be a non-executive director of the bank;
 - (d) the majority of the members of the committee must be independent; and
 - (e) the chairperson of the committee must be independent and must not be the chairperson of the bank.

For the purposes of this condition of registration, "non-executive" and "independent" have the same meaning as in the Reserve Bank of New Zealand document entitled "Corporate Governance" (BS14) dated July 2014.

10. That a substantial proportion of the bank's business is conducted in and from New Zealand.
11. That the bank has legal and practical ability to control and execute any business, and any functions relating to any business, of the bank that are carried on by a person other than the bank, sufficient to achieve, under normal business conditions and in the event of stress or failure of the bank or of a service provider to the bank, the following outcomes:
 - (a) that the bank's clearing and settlement obligations due on a day can be met on that day;
 - (b) that the bank's financial risk positions on a day can be identified on that day;
 - (c) that the bank's financial risk positions can be monitored and managed on the day following any failure and on subsequent days; and
 - (d) that the bank's existing customers can be given access to payments facilities on the day following any failure and on subsequent days.

For the purposes of this condition of registration, the term "legal and practical ability to control and execute" is explained in the Reserve Bank of New Zealand document entitled "Outsourcing Policy" (BS11) dated January 2006.

12. That:
 - (a) the business and affairs of the bank are managed by, or under the direction or supervision of, the board of the bank;
 - (b) the employment contract of the chief executive officer of the bank or person in an equivalent position (together "CEO") is with the bank, and the terms and conditions of the CEO's employment agreement are determined by, and any decision relating to the employment or termination of employment of the CEO are made by, the board of the bank; and
 - (c) all staff employed by the bank shall have their remuneration determined by (or under the delegated authority of) the board or the CEO of the bank and be accountable (directly or indirectly) to the CEO of the bank.
13. That the banking group complies with the following quantitative requirements for liquidity-risk management:
 - (a) the one-week mismatch ratio of the banking group is not less than zero per cent at the end of each business day;
 - (b) the one-month mismatch ratio of the banking group is not less than zero per cent at the end of each business day; and
 - (c) the one-year core funding ratio of the banking group is not less than 75 per cent at the end of each business day.

For the purposes of this condition of registration, the ratios identified must be calculated in accordance with the Reserve Bank of New Zealand documents entitled "Liquidity Policy" (BS13) dated July 2014 and "Liquidity Policy Annex: Liquid Assets" (BS13A) dated December 2011.

14. That the bank has an internal framework for liquidity risk management that is adequate in the bank's view for managing the bank's liquidity risk at a prudent level, and that, in particular:
 - (a) is clearly documented and communicated to all those in the organisation with responsibility for managing liquidity and liquidity risk;
 - (b) identifies responsibility for approval, oversight and implementation of the framework and policies for liquidity risk management;
 - (c) identifies the principal methods that the bank will use for measuring, monitoring and controlling liquidity risk; and
 - (d) considers the material sources of stress that the bank might face, and prepares the bank to manage stress through a contingency funding plan.
15. That no more than 10% of total assets may be beneficially owned by a SPV.

CONDITIONS OF REGISTRATION

For the purposes of this condition, —

“total assets” means all assets of the banking group plus any assets held by any SPV that are not included in the banking group’s assets:

“SPV” means a person—

- (a) to whom any member of the banking group has sold, assigned, or otherwise transferred any asset;
- (b) who has granted, or may grant, a security interest in its assets for the benefit of any holder of any covered bond; and
- (c) who carries on no other business except for that necessary or incidental to guarantee the obligations of any member of the banking group under a covered bond:

“covered bond” means a debt security issued by any member of the banking group, for which repayment to holders is guaranteed by a SPV, and investors retain an unsecured claim on the issuer.

16. That—

- (a) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the notification threshold, and does not meet the non-objection threshold, unless:
 - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination and at least 10 working days have passed; and
 - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011; and
- (b) no member of the banking group may give effect to a qualifying acquisition or business combination that meets the non-objection threshold unless:
 - (i) the bank has notified the Reserve Bank in writing of the intended acquisition or business combination;
 - (ii) at the time of notifying the Reserve Bank of the intended acquisition or business combination, the bank provided the Reserve Bank with the information required under the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011; and
 - (iii) the Reserve Bank has given the bank a notice of non-objection to the significant acquisition or business combination.

For the purposes of this condition of registration, “qualifying acquisition or business combination”, “notification threshold” and “non-objection threshold” have the same meaning as in the Reserve Bank of New Zealand Banking Supervision Handbook document “Significant Acquisitions Policy” (BS15) dated December 2011.

17. That the bank is pre-positioned for Open Bank Resolution and in accordance with a direction from the Reserve Bank, the bank can—

- (a) close promptly at any time of the day and on any day of the week and that effective upon the appointment of the statutory manager—
 - (i) all liabilities are frozen in full; and
 - (ii) no further access by customers and counterparties to their accounts (deposits, liabilities or other obligations) is possible;
- (b) apply a *de minimis* to relevant customer liability accounts;
- (c) apply a partial freeze to the customer liability account balances;
- (d) reopen by no later than 9am the next business day following the appointment of a statutory manager and provide customers access to their unfrozen funds;
- (e) maintain a full freeze on liabilities not pre-positioned for open bank resolution; and
- (f) reinstate customers’ access to some or all of their residual frozen funds.

For the purposes of this condition of registration, “*de minimis*”, “partial freeze”, “customer liability account”, and “frozen and unfrozen funds” have the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

18. That the bank has an Implementation Plan that—

- (a) is up-to-date; and
- (b) demonstrates that the bank’s prepositioning for Open Bank Resolution meets the requirements set out in the Reserve Bank document: “Open Bank Resolution Pre-positioning Requirements Policy” (BS17) dated September 2013.

For the purposes of this condition of registration, “Implementation Plan” has the same meaning as in the Reserve Bank of New Zealand document “Open Bank Resolution (OBR) Pre-positioning Requirements Policy” (BS17) dated September 2013.

19. That the bank has a compendium of liabilities that—

- (a) at the product-class level lists all liabilities, indicating which are—
 - (i) pre-positioned for Open Bank Resolution; and
 - (ii) not pre-positioned for Open Bank Resolution;

CONDITIONS OF REGISTRATION

- (b) is agreed to by the Reserve Bank; and
- (c) if the Reserve Bank's agreement is conditional, meets the Reserve Bank's conditions.

For the purposes of this condition of registration, "compendium of liabilities" and "pre-positioned and non pre-positioned liabilities" have the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

20. That on an annual basis the bank tests all the component parts of its Open Bank Resolution solution that demonstrates the bank's prepositioning for Open Bank Resolution as specified in the bank's Implementation Plan.

For the purposes of this condition of registration, "Implementation Plan" has the same meaning as in the Reserve Bank of New Zealand document "Open Bank Resolution (OBR) Pre-positioning Requirements Policy" (BS17) dated September 2013.

21. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of property-investment residential loans with a loan-to-valuation ratio of more than 60%, must not exceed 5% of the total of the qualifying new mortgage lending amount in respect of property-investment residential loans arising in the loan-to-valuation measurement period.
22. That, for a loan-to-valuation measurement period, the total of the bank's qualifying new mortgage lending amount in respect of non property-investment residential loans with a loan-to-valuation ratio of more than 80%, must not exceed 10% of the total of the qualifying new mortgage lending amount in respect of non property-investment residential loans arising in the loan-to-valuation measurement period.
23. That the bank must not make a residential mortgage loan unless the terms and conditions of the loan contract or the terms and conditions for an associated mortgage require that a borrower obtain the bank's agreement before the borrower can grant to another person a charge over the residential property used as security for the loan.

In these conditions of registration,—

"banking group" means ANZ Bank New Zealand Limited (as reporting entity) and all other entities included in the group as defined in section 6(1) of the Financial Markets Conduct Act 2013 for the purposes of Part 7 of that Act.

"generally accepted accounting practice" has the same meaning as in section 8 of the Financial Reporting Act 2013.

In conditions of registration 21 to 23, —

"loan-to-valuation ratio", "non property-investment residential loans", "property-investment residential loans", "qualifying new mortgage lending amount in respect of property-investment residential loans", "qualifying new mortgage lending amount in respect of non property-investment residential loans" and "residential mortgage loans" have the same meaning as in the Reserve Bank of New Zealand document entitled "Framework for Restrictions on High-LVR Residential Mortgage Lending" (BS19) dated October 2016:

"loan-to-valuation measurement period" means—

- (a) the six calendar month period ending on the last day of December 2016; and
- (b) thereafter a period of three calendar months ending on the last day of the third calendar month, the first of which ends on the last day of January 2017.

DIRECTORATE AND AUDITOR

Any document or communication may be sent to any Director at the Registered Office. The document or communication should be marked for the attention of that Director.

Directors' interests

In order to ensure that members of the Board are reminded of their disclosure obligations under the Companies Act 1993, the following procedures are adopted:

- At least once in each year, Directors are requested to complete, in terms of section 140(1) of the Companies Act 1993, a disclosure of any interests which they have with the Bank itself. Directors are reminded at this time of their obligation under the Companies Act 1993 to disclose promptly any transaction or proposed transaction with the Bank in which they have an interest.
- Directors are also requested to make a general disclosure of their interest in other entities in terms of section 140(2) of the Companies Act 1993. In addition, they are requested to initiate a review of that disclosure if there are any significant alterations which occur subsequently during the period.

In addition to the written disclosures referred to above, Directors disclose relevant interests which they have before discussion of particular business items.

The Companies Act 1993 allows a Director with an interest in a transaction to participate in discussions and to vote on all matters relating to that particular transaction. However, the Board has adopted a guideline whereby a Director with an interest in a transaction should not be present during any discussions, and should not vote, on any matter pertaining to that particular transaction.

Transactions with Directors

No Director has disclosed that he/she or any immediate relative or professional associate has any dealing with the Banking Group which has been either entered into on terms other than those which would in the ordinary course of business be given to any other person of like circumstances or means or which could otherwise be reasonably likely to influence materially the exercise of the Director's duties as a Director of the Bank.

Board Members as at 15 November 2017

Independent Non-Executive Director and Chair

John Frederick Judge

BCom, FCA
Company Director
Auckland, New Zealand

Mr Judge is a member of the Audit Committee, the Human Resources Committee and the Risk Committee.

Other directorships: Aquatx Holdings Limited, Biotelliga Limited, Biotelliga Holdings Limited, Biotelliga Nominees Limited, Endogen Limited, Janohn Limited, Sebca Limited, John Judge Limited, Cup Limited, Sails Friday Limited, The New Zealand Initiative Limited, Hydraulink Fluid Connectors Limited, Analog Digital Instruments Limited, Hydraulink Australia Pty Limited, ADInstruments Pty Limited, ADInstruments NZ Limited

Executive Director

David Duncan Hisco

BBus, MBA
Chief Executive, ANZ Bank New Zealand Limited
Auckland, New Zealand

Other directorships: ANZ Holdings (New Zealand) Limited

Non-Executive Directors

Shayne Cary Elliott

BCom
Chief Executive Officer, Australia and New Zealand Banking Group Limited
Melbourne, Australia

Mr Elliott is a member of the Human Resources Committee.

Other directorships: ANZ Holdings (New Zealand) Limited, Australia and New Zealand Banking Group Limited and the Financial Markets Foundation for Children

Michelle Nicole Jablko

LLB (Hons), B.Ec (Hons)
Chief Financial Officer, Australia and New Zealand Banking Group Limited
Melbourne, Australia

Ms Jablko is an alternate director for Mr Elliott

Nigel Henry Murray Williams

BCom
Chief Risk Officer, Australia and New Zealand Banking Group Limited
Melbourne, Australia

Other directorships: Shanghai Rural Commercial Bank Co. Limited

Mr Williams is a member of the Risk Committee and Audit Committee.

DIRECTORATE AND AUDITOR

Independent Non-Executive Directors

Antony John Carter

BE (Hons), ME, FNZIM
Company Director
Auckland, New Zealand

Mr Carter is the Chair of the Risk Committee and a member of the Audit Committee and the Human Resources Committee.

Other directorships: Air New Zealand Limited, Avonhead Mall Limited, Blues Management Limited, Fletcher Building Limited, Fisher & Paykel Healthcare Corporation Limited, Fisher & Paykel Healthcare Employee Share Purchase Trustee Limited, Fletcher Building Industries Limited, Loughborough Investments Limited, Modern Merchants Limited, Strategic Interchange Limited, Tetrad Corporation Limited

The Rt Hon. Sir John Phillip Key, GNZM, AC

BCom
Company Director
Auckland, New Zealand

Sir John is a member of the Risk Committee, Audit Committee and the Human Resources Committee.

Other directorships: Air New Zealand Limited, Thirty Eight JK Limited

Mark John Verbiest

LLB, CFInstD
Company Director
Wanaka, New Zealand

Mr Verbiest is the Chair of the Audit Committee and a member of the Human Resources Committee and the Risk Committee.

Other directorships: Bear Fund NZ Limited, Freightways Limited, Willis Bond Capital Partners Limited, Willis Bond General Partner Limited, MyCare Limited, The Treasury, Meridian Energy Limited

Joan Withers

MBA, AFInstD
Company Director
Auckland, New Zealand

Mrs Withers is the Chair of the Human Resources Committee and a member of the Risk Committee and the Audit Committee.

Other directorships: Mercury NZ Limited, The Warehouse Group Limited, On Being Bold Limited, The Warehouse Planit Trustees Limited, The Warehouse Management Trustee Company Limited, The Warehouse Management Trustee Company No.2 Limited

Auditor

KPMG

Chartered Accountants
10 Customhouse Quay
P O Box 996
Wellington, New Zealand

DIRECTORS' STATEMENT

As at the date on which this Disclosure Statement is signed, after due enquiry, each Director believes that:

- The Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014
- The Disclosure Statement is not false or misleading.

Over the year ended 30 September 2017, after due enquiry, each Director believes that:

- ANZ Bank New Zealand Limited has complied with all Conditions of Registration that applied during that period
- Credit exposures to connected persons were not contrary to the interests of the Banking Group
- ANZ Bank New Zealand Limited had systems in place to monitor and control adequately the Banking Group's material risks, including credit risk, concentration of credit risk, interest rate risk, currency risk, equity risk, liquidity risk, operational risk and other business risks, and that those systems were being properly applied.

This Disclosure Statement is dated, and has been signed by all Directors of the Bank on, 15 November 2017.

Antony Carter



Shayne Elliott



David Hisco



John Judge



The Rt Hon. Sir John Key, GNZM, AC



Mark Verbiest



Nigel Williams



Joan Withers





Independent Auditor's Report

To the shareholder of ANZ Bank New Zealand Limited

Report on the Banking Group Disclosure Statement

Opinion

In our opinion, the accompanying consolidated financial statements (excluding supplementary information) of ANZ Bank New Zealand Limited (the company) and its subsidiaries (the Banking Group) on pages 3 to 67:

- give a true and fair view of the Banking Group's financial position as at 30 September 2017 and its financial performance and cash flows for the year ended on that date
- comply with New Zealand Generally Accepted Accounting Practice, which in this instance means New Zealand Equivalents to International Financial Reporting Standards (NZ IFRS) and International Financial Reporting Standards.

In our opinion, the supplementary information that is required to be disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the Order) and is included within the Balance Sheet and notes 14, 18, 28 and 33 of the Disclosure Statement:

- has been prepared, in all material respects, in accordance with the guidelines issued pursuant to section 78(3) of the Reserve Bank of New Zealand Act 1989 and any conditions of registration
- is in accordance with the books and records of the Banking Group in all material respects
- fairly states the matters to which it relates in accordance with those Schedules

We have audited the accompanying consolidated financial statements and supplementary information which comprise:

- the consolidated balance sheet as at 30 September 2017
- the consolidated income statement, statements of comprehensive income, changes in equity and cash flows for the year then ended
- notes, including a summary of significant accounting policies and other explanatory information
- the information that is required to be disclosed in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order.



Basis for Opinion

We conducted our Audit in accordance with International Standards on Auditing (New Zealand) (ISA's (NZ)). We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

We are independent of the Banking Group in accordance with Professional and Ethical Standard 1 (Revised) Code of Ethics for Assurance Practitioners issued by the New Zealand Auditing and Assurance Standards Board and the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code), and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code.

Our responsibilities under ISA (NZ) are further described in the Auditor's Responsibilities for the Audit of the consolidated financial statements and supplementary information section of our report.

Our firm has also provided other services to the Banking Group in relation to review of regulatory returns, internal controls reports, prospectus assurance or reviews and agreed upon procedures engagements. Subject to certain restrictions, partners and employees of our firm may also deal with the Banking Group on normal terms within the ordinary course of trading activities of the business of the Banking Group. These matters have not impaired our independence as auditor of the Banking Group. The firm has no other relationship with, or interest in, the Banking Group.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements in the current period. We summarise below those matters and our key audit procedures to address those matters in order that the shareholder as a body may better understand the process by which we arrived at our audit opinion. Our procedures were undertaken in the context of and solely for the purpose of our statutory audit opinion on the consolidated financial statements as a whole and we do not express discrete opinions on separate elements of the consolidated financial statements.

The key audit matter

Provisions for Credit Impairment

The provision for credit impairment is a Key Audit Matter as the Banking Group has significant credit risk exposure to a large number of counterparties across a wide range of lending and industries. The value of loans and advances on the balance sheet is significant and there is a high degree of complexity and judgement involved for the Banking Group in estimating individual and collective credit impairment provisions against these loans. These features resulted in significant audit effort to address the risks around loan recoverability and the determination of related provisions.

How the matter was addressed in our audit

Our audit procedures for the individual and collective provision for credit impairment included:

Provisions against specific individual loans (individual provision)

- Testing the key controls over counterparty risk grading for wholesale loans (larger customer exposures that are monitored individually). We tested the approval of new lending facilities against the Banking Group's lending policies, the performance of annual loan assessments, and controls over the monitoring of counterparty credit quality. This included testing controls over the identification of exposures showing signs of stress, either due to internal factors specific to the counterparty or external macroeconomic factors, and testing the timeliness of and the accuracy of counterparty risk assessments and risk grading against the requirements of the Banking Group's lending policies



- Performing credit assessments of a sample of wholesale loans managed by the Banking Group’s specialist workout and recovery team assessed as higher risk or impaired, and a sample of other loans, focusing on larger exposures assessed by the Banking Group as showing signs of deterioration, or in areas of emerging risk (assessed against external market conditions). We challenged the Banking Group’s risk grading of the loan, their assessment of loan recoverability and the impact on the credit provision. To do this, we used the information on the Banking Group’s loan file, discussed the case with the loan officer and management, and performed our own assessment of recoverability. This involved using our understanding of relevant industries and the macroeconomic environment, and comparing assumptions of inputs used by the Banking Group in recoverability assessments to externally sourced evidence, such as commodity prices, publicly available audited financial statements, and comparable external valuations of collateral held
- For retail loans (smaller customer exposures not monitored individually), we evaluated the Banking Group’s oversight of the portfolios, with a focus on controls over delinquency statistics monitoring. We tested the level of provisions held against different loan products, on a sample basis, based on the delinquency profile and challenged assumptions made in respect of expected recoveries, primarily from collateral held.

Provisions estimated across loan portfolios (collective provision)

- Testing the Banking Group’s processes to validate the models used to calculate collective provisions, and evaluating the Banking Group’s model methodologies against established market practices and criteria in the accounting standards
- Testing the key controls within IT systems used to calculate the collective provision, specifically those relating to data management and the completeness and accuracy of data transfer from underlying source systems to the collective provision models
- Testing the accuracy of key inputs into models by checking a sample of balances to the general ledger and risk ratings to source systems
- Challenging the key assumptions in the models such as emergence periods, probability of default and loss given default for a sample of retail and wholesale portfolios. We compared modelled estimates against actual losses incurred by the Banking Group
- Re-performing, for a sample of retail and wholesale portfolios and using a KPMG-constructed calculation tool, the calculation of collective provisions to determine the accuracy of model output.

We also challenged key assumptions in the components of the Banking Group’s collective provision balance held above modelled provision estimates. This included:

- Evaluating inputs to the concentration risk and economic cycle provisions by comparing underlying portfolio characteristics to loss experience, current market conditions and specific risks inherent in the Banking Group’s loan portfolios
- Assessing the requirement for other additional provisions by considering model or data deficiencies identified by the Banking Group’s model validation processes
- Assessing the completeness of additional provisions by checking the consistency of risks identified in the portfolios to their inclusion in the Banking Group’s assessment.



The key audit matter

Valuation of Financial Instruments

Financial instruments held at fair value on the Banking Group's balance sheet include available-for-sale-assets, trading securities, derivative assets and liabilities, investments backing insurance contract liabilities, certain debt securities, and other assets and liabilities designated as measured at fair value through profit or loss.

The instruments are mainly risk management products sold to customers or used by the Banking Group to manage its own interest rate and foreign exchange risk.

The valuation of financial instruments is considered a Key Audit Matter due to:

- Financial instruments held at fair value are significant (16% of assets and 10% of liabilities)
- The significant volume and range of products transacted, increases the risk of inconsistencies in transaction management processes that could lead to inaccurate valuation
- Determining the fair value of trading securities and derivatives involves a significant level of judgement by the Banking Group, increasing the risk of error, and adding complexity to our audit. The level of judgement increases where internal models, as opposed to quoted market prices, are used to determine fair value of an instrument
- The valuation of certain derivatives held by the Banking Group is sensitive to inputs including credit risk, funding rates, probabilities of default and loss given default, and industry practice is evolving as to how the impact of both funding and credit risk is incorporated within the valuation of certain derivative instruments. This increased our audit effort in this area and necessitated the involvement of valuation specialists.

How the matter was addressed in our audit

Our audit procedures for the valuation of financial instruments held at fair value included:

- Testing access rights and change management controls for key valuation systems
- Testing interface controls, notably the completeness and accuracy of data transfers between transaction processing systems, key systems used to generate valuations and any related valuation adjustments, and the Banking Group's market risk management and finance systems to identify inconsistencies in transaction management and valuation processes across products
- Testing the governance and approval controls such as management review and approval of the valuation models and approval of new products against policies and procedures
- Testing the front office management review and approval of the daily financial instrument trading profit and loss reconciliations prepared by the Banking Group's independent product control function
- Testing the management review and approval of model construction and validation, aimed at assessing the validity and robustness of underlying valuation models
- Testing the Banking Group's data validation controls, such as those over key inputs in generating the fair value to market data where fair values were determined by front office teams.

We carried out testing over the valuation of financial instruments with both observable and unobservable inputs. Our specific testing involved valuation specialists and included:

- Re-performing the valuation of 'level 1' and 'level 2' available for sale assets and trading securities, which are primarily government, semi-government and corporate debt securities, by comparing the observable inputs, including quoted prices, to independently sourced market data



- Using independent models, re-calculating the valuation of a sample of derivative assets and liabilities where the fair value was determined using observable inputs. This included comparing a sample of observable inputs used in the Banking Group's derivative valuations to independently-sourced market data, such as interest rates, foreign exchange rates and volatilities
- Where the fair value of derivatives and other financial assets and liabilities were determined using unobservable inputs ('level 3' instruments), challenging the Banking Group's valuation model by testing the key inputs used to comparable data in the market, including the use of proxy instruments and available alternatives
- Evaluating the appropriateness of the Banking Group's valuation methodology for derivative financial instruments, having regard to current and emerging derivative valuation practices across a range of peer institutions and against the required criteria in the accounting standards. We tested adjustments made to valuations, particularly funding and credit valuation adjustments on un-collateralised derivatives. In particular, for a sample of individual counterparties, we tested key inputs to the credit valuation adjustment calculation, including the probability of default, against observable market data. Where proxies were used, we assessed the proxy against available alternatives across a number of locations.

The key audit matter

IT systems and controls

As a major New Zealand bank, the Banking Group's businesses utilise a large number of complex, interdependent Information Technology (IT) systems to process and record a high volume of transactions. Controls over access and changes to IT systems are critical to the recording of financial information and the preparation of a financial report which provides a true and fair view of the Banking Group's financial position and performance. The IT systems and controls, as they impact the financial recording and reporting of transactions, is a key audit matter and our audit approach could significantly differ depending on the effective operation of the Banking Group's IT controls. KPMG IT specialists were used throughout the engagement as a core part of our audit team.

How the matter was addressed in our audit

We tested the control environment for key IT applications (systems) used in processing significant transactions and recording balances in the general ledger. We also tested automated controls embedded within these systems. Our audit procedures included:

- Testing the governance controls used by the Banking Group's technology teams and third party suppliers to monitor system integrity, by checking matters impacting the operational integrity of core systems for escalation and action in accordance with the Banking Group's policies
- Testing the access rights given to staff by checking them to approved records, and inspecting the reports over the granting and removal of access rights. We also looked for evidence of escalation of breaches
- Testing preventative controls designed to enforce segregation of duties between users within particular systems
- Testing the operating effectiveness of automated controls, principally relating to the automated calculation of financial transactions. We tested the inputs used within automated calculations to source data and also tested the accuracy of the calculation logic for a sample of transactions within each identified control
- Testing the operating effectiveness of automated reconciliation controls, both between systems and intra-system. For a sample of identified breaks, in reconciliations, we checked that these were recorded on exception reports, and subsequently investigated and cleared by the Banking Group.



Other Supplementary Information

The Directors, on behalf of the Banking Group, are responsible for the other information included in the Banking Group's Disclosure Statement. Other information includes the information required to be included in the Disclosure Statement in accordance with Schedule 2 of the Order. Our opinion on the consolidated financial statements does not cover any other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.



Report on other legal and regulatory requirements

In accordance with the requirements of clauses 2(1)(d) and 2(1)(e) of Schedule 1 of the Order, we report that:

- we have obtained all the information and explanations we have required
- in our opinion, proper accounting records have been kept by the Banking Group, as far as appears from our examination of those records.



Responsibilities of Directors for the consolidated financial statements and supplementary information

The Directors, on behalf of the Banking Group, are responsible for:

- the preparation and fair presentation of the consolidated financial statements in accordance with Clause 24 of the Order, NZ IFRS and International Financial Reporting Standards
- the preparation and fair presentation of supplementary information, in accordance with Schedules 2, 4, 7, 13, 14, 15 and 17 of the Order
- implementing necessary internal controls to enable the preparation of consolidated financial statements that are fairly presented and free from material misstatement, whether due to fraud or error
- assessing the ability to continue as a going concern. This includes disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless they either intend to liquidate or to cease operations, or have no realistic alternative but to do so.



Auditor's Responsibilities for the Audit of the consolidated financial statements and supplementary information

Our objective is:

- to obtain reasonable assurance about whether the Disclosure Statement, including the consolidated financial statements prepared in accordance with Clause 24 of the Order, and supplementary information, in accordance with Schedules 4, 7, 13, 14, 15 and 17 of the Order as a whole is free from material misstatement, whether due to fraud or error
- to issue an Auditor's Report that includes our opinion.



Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (New Zealand) will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error. They are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of this consolidated financial statements.

A further description of our responsibilities for the Audit of these consolidated financial statements is located at the External Reporting Board (XRB) website at:

https://www.xrb.govt.nz/Site/Auditing_Assurance_Standards/Current_Standards/Page1.aspx

This description forms part of our Auditor's Report.

Review conclusion on the supplementary information relating to Capital Adequacy

Based on our review, nothing has come to our attention that causes us to believe that the information relating to Capital Adequacy, disclosed in note 26 to the Disclosure Statement, is not, in all material respects:

- prepared in accordance with the Banking Group's conditions of registration
- disclosed in accordance with Schedule 11 of the Order.

We have reviewed the information relating to Capital Adequacy, as disclosed in note 26 of the Disclosure Statement for the year ended 30 September 2017. The information relating to Capital Adequacy comprises the information that is required to be disclosed in accordance with Schedule 11 of the Order.



Basis for conclusion on the supplementary information relating to Capital Adequacy

A review of the supplementary information relating to Capital Adequacy in accordance with NZ SRE 2410 *Review of Financial Statements Performed by the Independent Auditor of the Entity* (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. Our responsibilities under that standard are further described in the Auditor's Responsibilities for the Review of the supplementary information relating to capital adequacy section of our report.

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.



Responsibilities of Directors for the supplementary information relating to capital adequacy

The Directors are responsible for the preparation of information relating to Capital Adequacy that is required to be disclosed under Schedule 11 of the Order and prepared in accordance with the Capital Adequacy Framework (Internal Models Based Approach) (BS2B) and described in note 26 to the Disclosure Statement.



Auditor's Responsibilities for the Review of the supplementary information relating to capital adequacy

Our responsibility is to express a conclusion on the Capital Adequacy information based on our review. We conducted our review in accordance with NZ SRE 2410 Review of Financial Statements Performed by the Independent Auditor of the Entity (NZ SRE 2410) issued by the XRB. As the auditor of ANZ Bank New Zealand Limited, NZ SRE 2410 requires that we comply with the ethical requirements relevant to the audit of the annual financial statements, and plan and perform the review to obtain limited assurance about whether the capital adequacy information is, in all material respects:

- prepared in accordance with the Banking Group's conditions of registration
- disclosed in accordance with Schedule 11 of the Order.

A review of the Capital Adequacy information 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). Accordingly we do not express an audit opinion on the information relating to Capital Adequacy disclosures.



Use of this Auditor's Report

This report is made solely to the shareholder as a body. Our work has been undertaken so that we might state to the shareholder those matters we are required to state to them in the Auditor's 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 shareholder as a body for our work, this report, or any of the opinions or conclusions we have formed.

The engagement partner on the audit resulting in this independent auditor's report is Graeme Edwards.

For and on behalf of

KPMG
Wellington

15 November 2017

