Disclosure Statement.

For the six months ended 31 December 2015.

Kiwibank.

Number 58

Contents.

General matters

Details of incorporation

Kiwibank Limited (“**Kiwibank**”) is a company domiciled in New Zealand and was incorporated in New Zealand under the Companies Act 1993 on 4 May 2001. On 29 November 2001, Kiwibank was registered as a bank under the Reserve Bank of New Zealand Act 1989 (the **“RBNZ Act”**) and was required to comply with the conditions of registration as laid down by the Reserve Bank of New Zealand (**“RBNZ”**) from that date onwards.

This Disclosure Statement has been issued by Kiwibank for the six months ended 31 December 2015, in accordance with the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (the **“Order”**). Words and phrases defined by the Order have the same meanings when used in this Disclosure Statement.

In this Disclosure Statement, **“Banking Group”** means Kiwibank’s financial reporting group, which consists of Kiwibank, all of its wholly owned entities and all other entities consolidated for financial reporting purposes.

Registered office

The registered office is: Kiwibank Limited, New Zealand Post House, Level 12, 7 Waterloo Quay, Wellington 6011, New Zealand.

Address for service

The address for service is: Kiwibank Limited, Ground Floor, New Zealand Post House, 7 Waterloo Quay, Wellington 6011, New Zealand.

Other material matters

The Board of Directors of Kiwibank (the “**Board**”) are of the opinion that, other than outlined below, there are no matters relating to the business or affairs of Kiwibank or the Banking Group, which would, if disclosed in this Disclosure Statement, materially affect the decision of a person to subscribe for debt securities of which Kiwibank or any member of the Banking Group is the issuer.

Kiwibank has determined that it is appropriate to modernise its core banking system over the next 3-5 years. Therefore, there will be a higher level of investment during this period which will be actively managed to minimise the risk of unplanned costs or operational risk from a significant change programme.

Pending proceedings or arbitration

The Board are of the opinion that, other than outlined below, there are no pending legal proceedings or arbitration concerning Kiwibank or any member of the Banking Group, whether in New Zealand or elsewhere, that may have a material adverse effect on Kiwibank or the Banking Group.

In June 2013, a group called Fair Play on Fees announced plans for a representative action against banks in New Zealand in relation to certain default fees charged to New Zealand customers. In November 2013, the group issued proceedings against Kiwibank. The potential outcome of the proceedings cannot be determined with any certainty at this stage.

Credit ratings

Kiwibank has the following credit ratings applicable to its long term unsecured obligations payable in New Zealand, in New Zealand dollars:

Rating agency	Credit rating and outlook
Standard & Poor’s (Australia) Pty Limited (“S&P”)	A+ (stable outlook)
Moody’s Investors Service	Aa3 (stable outlook)
Fitch Ratings	AA+ (stable outlook)

Conditions of registration

Changes in conditions of registration

The RBNZ issued revised conditions of registration which were effective from 1 November 2015. The revised conditions:

- refer to revised versions of:
  - Capital Adequacy Framework (Standardised Approach) (BS2A);
  - Application for Capital Recognition or Repayment (BS16);
  - Framework for Restrictions on High-LVR Residential Mortgage Lending (BS19); and
  - Connected Exposures Policy (BS8);
- impose revised high-LVR speed limits, in line with the revised BS19, and remove certain conditions;
- include in the conditions that the bank must receive a notice of non-objection from the RBNZ before recognising an Additional Tier 1 or Tier 2 instrument as capital and to apply certain notification and capital repayment approval obligations on the bank; and
- remove superseded references to the Financial Reporting Act 1993.

Directorate

Catherine Maria Savage resigned as a director on 31 January 2016.

There have been no other changes in the Board since 30 June 2015.

Responsible persons

Rob Morrison and Alison Gerry have been authorised in writing to sign this disclosure statement in accordance with Section 82 of the RBNZ Act, on behalf of the directors, being:

Robert William Bentley Morrison	Hon. Sir Michael John Cullen
Alison Rosemary Gerry	Brian Joseph Roche
Lindsay Wright	Carol Anne Campbell

Auditor

The auditor whose review opinion is referred to in this disclosure statement is Chris Barber assisted by PricewaterhouseCoopers, acting as agent on behalf of the Office of the Auditor General. His address for service is PricewaterhouseCoopers, 113-119 The Terrace, Wellington, New Zealand.

Guarantees

As at the date the Board approved this Disclosure Statement, the payment obligations of Kiwibank have the benefit of a deed poll guarantee by NZP (the "**NZP Guarantee**") and (in relation to certain debt securities issued by Kiwibank) a guarantee by Kiwi Covered Bond Trustee Limited (the "**Covered Bond Guarantee**"). A summary of the details of each guarantee are set out below.

Further details on the NZP Guarantee can be obtained by referring to Kiwibank's Disclosure Statement for the year ended 30 June 2015 which is available at www.kiwibank.co.nz.

NZP Guarantee

NZP supports Kiwibank as a registered bank.

The following is a summary of the main features of the NZP Guarantee as at 31 December 2015:

i. The address for service of NZP is: Ground Floor, New Zealand Post House, 7 Waterloo Quay, Wellington 6011, New Zealand.

ii. NZP is not a member of the Banking Group (as that term is defined in the Order).

iii. The NZP Guarantee is an unsecured guarantee of all the payment obligations (excluding any payment obligations, the terms of which expressly provide in writing that they do not have the benefit of the NZP Guarantee) of Kiwibank. The NZP Guarantee can be terminated on not less than three months' notice being given to creditors (as that term is defined in the NZP Guarantee). Any such termination does not affect any existing payment obligations owed under the NZP Guarantee at the termination date. The NZP Guarantee has no expiry date.

NZP has a credit rating applicable to its long term unsecured obligations payable in New Zealand, in New Zealand dollars, from S&P of A+ (stable outlook).

Covered Bond Guarantee

Certain debt securities ("**Covered Bonds**") issued by Kiwibank are guaranteed by Kiwi Covered Bond Trustee Limited (the "**Covered Bond Guarantor**"), solely in its capacity as Trustee of Kiwibank Covered Bond Trust. The Covered Bond Guarantor has guaranteed the payment of interest and principal of Covered Bonds, pursuant to a guarantee which is secured over a pool of assets. The Covered Bond Guarantor's address for service is Level 9, 34 Shortland Street, Auckland, New Zealand. The Covered Bond Guarantor is not a member of the Banking Group. The Covered Bonds have been assigned a long term rating of Aaa and AAA by Moody's Investors Service and Fitch Ratings respectively.

Directors' statement

The directors of Kiwibank state that each director believes, after due enquiry, that:

1. As at the date on which the Disclosure Statement is signed:
   i. the Disclosure Statement contains all the information that is required by the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014; and
   ii. the Disclosure Statement is not false or misleading.
2. During the period ended 31 December 2015:
   i. Kiwibank has complied with the conditions of registration applicable during the period;
   ii. credit exposures to connected persons were not contrary to the interests of the Banking Group; and
   iii. Kiwibank 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.

Signed by Rob Morrison and Alison Gerry as directors and responsible persons on behalf of all the directors listed in the Directorate of this Disclosure Statement:

17 February 2016

Interim financial statements

Consolidated income statement
For the six months ended 31 December 2015

		The Banking Group		
Dollars in millions	Note	**Unaudited 6 months ended 31/12/15**	Unaudited 6 months ended 31/12/14	Audited year ended 30/06/15
Interest income		**470**	472	957
Interest expense		**(281)**	(293)	(596)
Net interest income		**189**	179	361
Net gains/(losses) on financial instruments at fair value	2	**7**	3	5
Gross fee and other income		**97**	101	194
Direct fee expenses		**(48)**	(43)	(87)
Net fee and other income		**49**	58	107
Total operating income		**245**	240	473
Operating expenses		**(146)**	(133)	(284)
Impairment (losses)/reversals on loans and advances	10	**(6)**	(9)	(13)
Profit before taxation		**93**	98	176
Income tax expense		**(22)**	(27)	(49)
Profit after taxation		**71**	71	127
Attributable to:				
Owners of the parent		**71**	71	127
Non-controlling interest		**-**	-	-

Consolidated statement of comprehensive income
For the six months ended 31 December 2015

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/15**	Unaudited 6 months ended 31/12/14	Audited year ended 30/06/15
Profit after taxation	**71**	71	127
Other comprehensive income			
Net gain/(loss) from changes in reserves that may subsequently be reclassified to profit or loss			
Available-for-sale reserve (net of tax)	**(3)**	4	10
Cash flow hedge reserve (net of tax)	**3**	(36)	(74)
Other comprehensive income for the period/year	**-**	(32)	(64)
Total comprehensive income for the period/year	**71**	39	63
Attributable to:			
Owners of the parent	**71**	39	63
Non-controlling interest	**-**	-	-

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated statement of changes in equity

For the six months ended 31 December 2015

					The Banking Group				
Dollars in millions	Note	Fully Paid Ordinary Shares	Retained earnings	Available-For-Sale Reserve	Cash Flow Hedge Reserve	Perpetual Capital Reserve	Total Equity Attributable to Owners of the Parent	Non-Controlling Interest	Total
Balance at 1 July 2014		400	436	(2)	20	-	854	149	1,003
Unaudited 6 months ended 31 December 2014									
Unaudited profit for the period		-	71	-	-	-	71	-	71
Other comprehensive income									
Available-for-sale financial assets (net of tax)		-	-	4	-	-	4	-	4
Cash flow hedges (net of tax)		-	-	-	(36)	-	(36)	-	(36)
Total other comprehensive income		-	-	4	(36)	-	(32)	-	(32)
Total comprehensive income		-	71	4	(36)	-	39	-	39
Transactions with owners									
Transaction with non-controlling interest		-	-	-	-	-	-	1	1
Dividends paid on ordinary shares		-	(1)	-	-	-	(1)	-	(1)
Dividends paid to non-controlling interest		-	(4)	-	-	-	(4)	-	(4)
Unaudited balance at 31 December 2014		400	502	2	(16)	-	888	150	1,038
Audited year ended 30 June 2015									
Audited profit for the year		-	127	-	-	-	127	-	127
Other comprehensive income									
Available-for-sale financial assets (net of tax)		-	-	10	-	-	10	-	10
Cash flow hedges (net of tax)		-	-	-	(74)	-	(74)	-	(74)
Total other comprehensive income		-	-	10	(74)	-	(64)	-	(64)
Total comprehensive income		-	127	10	(74)	-	63	-	63
Transactions with owners									
Repurchase of perpetual preference shares		-	-	-	-	-	-	(150)	(150)
Issue of perpetual capital		-	-	-	-	147	147	-	147
Transaction with non-controlling interest		-	-	-	-	-	-	1	1
Dividends paid on ordinary shares		-	(22)	-	-	-	(22)	-	(22)
Dividends paid to non-controlling interest		-	(9)	-	-	-	(9)	-	(9)
Audited balance at 30 June 2015		400	532	8	(54)	147	1,033	-	1,033
Unaudited 6 months ended 31 December 2015									
Unaudited profit for the period		**-**	**71**	**-**	**-**	**-**	**71**	**-**	**71**
Other comprehensive income									
Available-for-sale financial assets (net of tax)		**-**	**-**	**(3)**	**-**	**-**	**(3)**	**-**	**(3)**
Cash flow hedges (net of tax)		**-**	**-**	**-**	**3**	**-**	**3**	**-**	**3**
Total other comprehensive income		**-**	**-**	**(3)**	**3**	**-**	**-**	**-**	**-**
Total comprehensive income		**-**	**71**	**(3)**	**3**	**-**	**71**	**-**	**71**
Transactions with owners									
Dividends paid on ordinary shares	9	**-**	**(24)**	**-**	**-**	**-**	**(24)**	**-**	**(24)**
Distributions to holders of perpetual capital		**-**	**(6)**	**-**	**-**	**-**	**(6)**	**-**	**(6)**
Unaudited balance at 31 December 2015		**400**	**573**	**5**	**(51)**	**147**	**1,074**	**-**	**1,074**

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated balance sheet

As at 31 December 2015

		The Banking Group		
Dollars in millions	Note	**Unaudited 31/12/15**	Unaudited 31/12/14	Audited 30/06/15
Assets				
Cash and cash equivalents		**478**	448	492
Due from NZP related parties	3	**77**	77	77
Due from other financial institutions	4	**209**	119	194
Financial assets held for trading		**66**	48	96
Available-for-sale assets		**1,165**	1,083	1,222
Loans and advances	5	**16,349**	15,054	15,598
Derivative financial instruments		**451**	184	480
Property, plant and equipment		**20**	15	20
Intangible assets		**138**	97	116
Deferred taxation		**27**	17	32
Other assets		**16**	19	17
Total assets		**18,996**	17,161	18,344
Total interest earning and discount bearing assets		***18,326***	*16,817*	*17,642*
Liabilities				
Due to other financial institutions		**82**	118	325
Due to NZP related parties	3	**10**	8	6
Deposits and other borrowings	6	**14,430**	13,283	13,740
Derivative financial instruments		**537**	302	475
Debt securities issued	7	**2,507**	2,067	2,397
Current tax liability		**14**	17	21
Other liabilities		**86**	76	92
Subordinated debt	8	**256**	252	255
Total liabilities		**17,922**	16,123	17,311
Equity attributable to owners of the parent				
Share capital		**400**	400	400
Reserves		**674**	488	633
Total equity attributable to owners of the parent		**1,074**	888	1,033
Non-controlling interest		**-**	150	-
Total equity		**1,074**	1,038	1,033
Total liabilities and shareholders equity		**18,996**	17,161	18,344
Total interest and discount bearing liabilities		***15,843***	*14,503*	*15,434*

The notes on pages 8 to 24 form part of these interim financial statements.

Interim financial statements continued

Consolidated cash flow statement

For the six months ended 31 December 2015

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/15**	Unaudited 6 months ended 31/12/14	Audited year ended 30/06/15
Cash flows from operating activities			
Interest received	**486**	477	974
Interest paid	**(288)**	(277)	(575)
Fees and other income	**97**	101	194
Direct fee expenses	**(48)**	(43)	(87)
Operating expenses paid	**(138)**	(123)	(243)
Taxes paid	**(24)**	(17)	(38)
Net cash flows from operating activities before changes in operating assets and liabilities	**85**	118	225
Net changes in operating assets and liabilities			
Decrease/(increase) in financial assets held for trading	**30**	-	(47)
Decrease/(increase) in available-for-sale assets	**56**	16	(114)
Increase in loans and advances	**(766)**	(418)	(973)
Decrease/(increase) in net amounts due from related parties	**3**	(20)	(19)
(Increase)/decrease in balances due from other financial institutions	**(15)**	3	(72)
Increase in deposits and other borrowing	**699**	517	967
(Decrease)/increase in balances due to other financial institutions	**(243)**	(67)	139
Net cash flows provided by operating activities	**(151)**	149	106
Cash flows from investing activities			
Purchase of property, plant and equipment	**(3)**	(5)	(13)
Purchase of intangible assets	**(33)**	(21)	(51)
Net cash flows from investing activities	**(36)**	(26)	(64)
Cash flows from financing activities			
Increase/(decrease) in debt securities issued	**204**	(135)	14
Net issue of perpetual capital notes/bonds	**-**	-	147
Repurchase of perpetual preference shares	**-**	-	(150)
Dividends paid on ordinary shares	**(24)**	(1)	(22)
Distributions to holders of perpetual capital	**(6)**	-	-
Dividends paid to non-controlling interest	**-**	(4)	(9)
Net cash flows from financing activities	**174**	(140)	(20)
(Decrease)/increase in cash and cash equivalents	**(13)**	(17)	22
Cash and cash equivalents at beginning of the period/year	**492**	461	461
Effect of exchange translation adjustments	**(1)**	4	9
Cash and cash equivalents at end of the period/year	**478**	448	492

The notes on pages 8 to 24 form part of these interim financial statements.

Notes to the interim financial statements

1. Summary of significant accounting policies

1.1 Reporting entity

In these interim financial statements, the reporting entity is Kiwibank Limited ("**Kiwibank**" or the "Bank"). The "**Banking Group**" consists of Kiwibank and its subsidiaries. Kiwibank is a profit oriented entity incorporated and domiciled in New Zealand under the Companies Act 1993 and is registered as a bank under the Reserve Bank of New Zealand Act 1989.

The principal activity of the Banking Group is the provision of retail and banking products and services to individuals and small to medium-sized businesses.

Kiwibank's immediate parent company is Kiwi Group Holdings Limited ("**KGHL**"), its ultimate parent company is New Zealand Post Limited ("**NZP**") and the ultimate shareholder of Kiwibank is the New Zealand Crown (the "**Crown**").

1.2 Basis of preparation

These interim financial statements are for the Banking Group for the six months ended 31 December 2015 and have been prepared in accordance with Generally Accepted Accounting Practice in New Zealand, as appropriate for profit oriented entities. They comply with NZ IAS 34 *Interim Financial Reporting, IAS 34 Interim Financial Reporting* and the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (the "**Order**"). These interim financial statements should be read in conjunction with the Banking Group's financial statements for the year ended 30 June 2015, which comply with International Financial Reporting Standards ("**IFRS**") as issued by the International Accounting Standards Board.

Measurement base

These interim financial statements are based on the general principles of historic cost accounting, modified by the application of fair value measurements for available-for-sale financial assets, financial instruments held at fair value through profit or loss and all derivative contracts. The carrying values of recognised assets and liabilities that are hedged items in fair value hedges, and otherwise carried at amortised cost, are adjusted to record changes in fair value attributable to the risks that are being hedged.

1.3 Accounting policies

The accounting policies adopted in the preparation of the interim financial statements are consistent with those followed in the preparation of the Banking Group's annual financial statements for the year ended 30 June 2015.

1.4 Basis of consolidation

The consolidated interim financial statements of the Banking Group comprise the interim financial statements of Kiwibank and its subsidiaries for the period ended 31 December 2015, using the acquisition method. Subsidiaries are entities that are controlled by Kiwibank.

1.5 Functional and presentation currency

The functional and presentation currency of Kiwibank and the Banking Group is New Zealand dollars. All amounts are expressed in millions of New Zealand dollars, unless otherwise stated.

1.6 Comparative amounts

Certain comparative balances have been reclassified to ensure consistency with the current period's presentation.

During the year ended 30 June 2015, the Banking Group amended the presentation of the income statement in relation to the disclosure of direct fee expenses. This change was in accordance with NZ IAS 1 and was implemented to improve the presentation for users of the financial statements.

Notes to the interim financial statements continued

2. Net gains/(losses) on financial instruments at fair value

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/15**	Unaudited 6 months ended 31/12/14	Audited year ended 30/06/15
Derivative financial instruments held for trading	**1**	(2)	(6)
Financial assets held for trading	**-**	3	5
Net ineffectiveness on qualifying fair value hedges	**1**	-	(1)
Cumulative gain transferred from available-for-sale reserve	**5**	-	2
Cumulative loss transferred from cash flow hedge reserve	**-**	1	3
Net foreign exchange gains	**-**	1	2
Total gains on financial instruments	**7**	3	5

Net ineffectiveness on qualifying cash flow hedges is $0.0m (31 December 2014: $0.0m; 30 June 2015: ($0.1m)). Net ineffectiveness on qualifying fair value hedges is $1.1m (31 December 2014: ($0.1m); 30 June 2015: ($1.1m)).

3. Related parties

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Outstanding balances			
Due to NZP related parties	**10**	8	6
Included in deposits	**26**	27	28
Included in non-controlling interest	**-**	1	-
Total balances due to related parties	**36**	36	34
Receivables			
Due from NZP related parties	**77**	77	77
Included in loans and advances	**2**	2	2
Total balances due from related parties	**79**	79	79

NZP has a credit facility with the Banking Group, allowing NZP to draw down to the extent that the Banking Group does not exceed credit exposure to connected persons of 15% of Tier 1 capital, as required in its banking conditions of registration. When loans are drawn down the transaction is undertaken at market interest rates. As at 31 December 2015 the amount owed by NZP to the Banking Group was $76m (31 December 2014: $76m; 30 June 2015: $76m). This does not exceed the 15% of Tier 1 capital requirement.

The Crown has entered into a $300m uncalled capital facility with NZP where NZP can drawdown capital for contingent events around Kiwibank's conditions of registration. The annualised cost of this facility on charged to Kiwibank by NZP is $3.6m.

Notes to the interim financial statements continued

4. Due from other financial institutions

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Unsettled receivables	**-**	-	32
Short term advances due from other financial institutions	**33**	11	23
Collateralised loans	**176**	108	139
Total – current	**209**	119	194

As at 31 December 2015, included within the balance above, is $176.3m of collateral pledged by Kiwibank in respect of its credit support annex obligations to derivative counterparties (31 December 2014: $108.4m; 30 June 2015: $138.5m).

5. Loans and advances

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Residential	**14,354**	13,235	13,718
Other retail	**409**	371	381
Business	**1,639**	1,505	1,552
Gross loans and advances	**16,402**	15,111	15,651
Collective allowance for impairment losses	**(44)**	(40)	(41)
Allowance for individually impaired assets	**(9)**	(17)	(12)
Net loans and advances	**16,349**	15,054	15,598
Current	**1,155**	1,038	1,059
Non-current	**15,194**	14,016	14,539

Notes to the interim financial statements continued

6. Deposits and other borrowing

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Demand deposits non-interest bearing	**1,426**	1,213	1,255
Demand deposits bearing interest	**2,999**	2,608	2,747
Term deposits	**10,005**	9,462	9,738
Total deposits from customers	**14,430**	13,283	13,740
Current	**13,968**	12,924	13,385
Non-current	**462**	359	355

In the event of the liquidation of Kiwibank, deposit holders will rank equally with all other creditors but ahead of subordinated debt holders and shareholders. In addition, all payment obligations of Kiwibank, excluding any payment obligations, the terms of which expressly provide that they do not have the benefit of the guarantee, are guaranteed under the NZP Guarantee.

The Kiwibank PIE Unit Trust (the "**Trust**"), established in May 2008, operates three funds; the PIE Term Deposit Fund, the Notice Saver and PIE Online Call Fund. Kiwibank Investment Management Limited is the Issuer and Manager (the "**Manager**"), Trustees Executors Limited is the Trustee and Kiwibank is the Promoter of the Trust. Units in the Trust do not directly represent deposits or liabilities of Kiwibank, however the Trust is invested exclusively in term and call deposits with Kiwibank. At 31 December 2015, $3,723m of the Trust's funds were invested in Kiwibank products or securities (31 December 2014: $3,664m; 30 June 2015: $3,735m).

Kiwibank guarantees the payment obligations of the Manager and any amounts owing to Unitholders under the Trust Deed in respect of their Units and agrees to pay to Unitholders any shortfall between the amount they may receive on redeeming their Units or in the winding up of the Trust and the balance of their Unit Accounts.

7. Debt securities issued

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Short term debt			
Commercial paper at fair value through profit or loss	**600**	531	615
Certificates of deposit	**360**	339	191
Long term debt			
Medium term notes	**1,302**	989	1,328
Covered bonds	**220**	192	236
Fair value hedge adjustment	**25**	16	27
Total debt securities issued	**2,507**	2,067	2,397
Current	**1,145**	870	836
Non-current	**1,362**	1,197	1,561

In the event of the liquidation of Kiwibank, holders of these debt securities, with the exception of covered bonds, will rank equally with all other creditors but ahead of subordinated debt holders and shareholders. In addition, all payment obligations of Kiwibank, excluding any payment obligations, the terms of which expressly provide that they do not have the benefit of a deed poll guarantee (the "**NZP Guarantee**") provided by NZP, are guaranteed under the NZP Guarantee.

The guarantee arrangements and other details relating to covered bonds are disclosed in note 18.

Kiwibank has not had any defaults of principal, interest or other breaches with respect to debt securities issued during the year (period ended 31 December 2014: none; year ended 30 June 2015: none).

Notes to the interim financial statements continued

8. Subordinated debt

	The Banking Group		
Dollars in millions	**Unaudited as at 31/12/15**	Unaudited as at 31/12/14	Audited as at 30/06/15
Subordinated bonds	**150**	149	149
Capital notes	**106**	103	106
Total subordinated debt	**256**	252	255
Current	**4**	3	3
Non-current	**252**	249	252

During the period ended 31 December 2015, $nil of subordinated debt was issued or called by the Banking Group (period ended 31 December 2014: $nil issued or called; year ended 30 June 2015: $nil issued or called).

As at 31 December 2015, $208m (31 December 2014: $208m; 30 June 2015: $208m) of the subordinated debt qualified as Tier 2 capital for Capital Adequacy calculation purposes.

The contractual terms of subordinated debt instruments on issue expressly provide that they do not have the benefit of the NZP Guarantee.

The Banking Group has not had any defaults of principal, interest or other breaches with respect to these liabilities during the period (period ended 31 December 2014: none; year ended 30 June 2015: none).

The subordinated debt instruments on issue are subordinate to all other general liabilities of the Banking Group and are denominated in New Zealand dollars.

The terms and conditions of the subordinated debt instruments on issue are as follows.

Instrument	Issue date	Amount $m's	Coupon rate	Call date	Maturity date	Credit rating
Subordinated bonds	10 December 2012	150	5.80% p.a.	15 December 2017	15 December 2022	BB+
Capital notes	6 June 2014	100	6.61% p.a.	15 July 2019	15 July 2024	BB+

Capital Notes

The Capital Notes have been issued by Kiwi Capital Funding Limited ("**KCFL**"), an entity controlled by Kiwibank and which is part of the consolidated Banking Group. The entire proceeds from the issue of Capital Notes were used to purchase convertible subordinate bonds issued by Kiwibank (the "**Kiwibank Bonds**"). Interest on the Capital Notes is payable semi-annually at an initial rate of 6.61% p.a. subject to the condition that KCFL receives a corresponding payment of interest from Kiwibank on its investment in the Kiwibank Bonds.

KCFL's obligation to pay interest changes or will terminate should any of the Kiwibank Bonds be converted into ordinary shares or written off. The Capital Notes have a maturity date of 15 July 2024, however, KCFL will make early repayment of the Capital Notes should Kiwibank elect to make early repayment of the Kiwibank Bonds as outlined above. KCFL's obligation to repay the capital notes changes or will terminate should any of the Kiwibank Bonds be converted into ordinary shares or written off.

9. Dividends paid on ordinary shares

During the period ended 31 December 2015 Kiwibank paid ordinary dividends of $24.0m to the immediate parent company, KGHL (period ended 31 December 2014: $0.6m; year ended 30 June 2015: $21.7m).

Notes to the interim financial statements continued

10. Asset quality

Impairment losses per income statement

	The Banking Group		
Dollars in millions	**Unaudited 6 months ended 31/12/15**	Unaudited 6 months ended 31/12/14	Audited year ended 30/06/15
Collective impairment losses on loans and advances	**3**	3	4
Individual impairment losses on loans and advances	**3**	6	9
Total impairment losses per income statement	**6**	9	13

Summary of lending

	The Banking Group			
Unaudited as at 31 December 2015 Dollars in millions	**Residential unsecured lending**	**Residential mortgage loans**	**Business exposures**	**Total**
Neither past due nor impaired	**438**	**15,162**	**651**	**16,251**
Past due but not impaired (a)	**46**	**84**	**5**	**135**
Impaired (b)	**1**	**11**	**4**	**16**
Gross	**485**	**15,257**	**660**	**16,402**
Collective allowance for impairment (c)	**(11)**	**(24)**	**(9)**	**(44)**
Individual allowance for impairment (d)	**(1)**	**(6)**	**(2)**	**(9)**
Net loans and advances	**473**	**15,227**	**649**	**16,349**

a: Loans and advances past due but not impaired

	The Banking Group			
Unaudited as at 31 December 2015 Dollars in millions	**Residential unsecured lending**	**Residential mortgage loans**	**Business exposures**	**Total**
Past due less than 30 days	**30**	**56**	**5**	**91**
Past due 30 – 59 days	**10**	**19**	**-**	**29**
Past due 60 – 89 days	**3**	**4**	**-**	**7**
Past due 90 days or greater	**3**	**5**	**-**	**8**
Total past due but not impaired	**46**	**84**	**5**	**135**

Notes to the interim financial statements continued

10. Asset quality continued

b: Impaired assets

	The Banking Group			
Unaudited 6 months ended 31 December 2015 Dollars in millions	Residential unsecured lending	Residential mortgage loans	Business exposures	Total
Gross impaired				
Balance at beginning of the period	1	11	11	23
Transfers from performing	5	9	-	14
Transfers to performing	-	-	(6)	(6)
Asset realisations and loans repaid	-	(8)	(1)	(9)
Amounts written off	(5)	(1)	-	(6)
Balance at end of the period	1	11	4	16
Individual allowance for impairment	(1)	(6)	(2)	(9)
Total net impaired assets	-	5	2	7

c: Reconciliation of collective allowance for impairment losses by asset class

	The Banking Group			
Unaudited 6 months ended 31 December 2015 Dollars in millions	Residential unsecured lending	Residential mortgage loans	Business exposures	Total
Balance at beginning of the period	9	17	15	41
Impairment losses on loans not at fair value through profit or loss	2	7	(6)	3
Total collective allowance for impairment losses	11	24	9	44

d: Reconciliation of individual allowance for impairment losses by asset class

	The Banking Group			
Unaudited 6 months ended 31 December 2015 Dollars in millions	Residential unsecured lending	Residential mortgage loans	Business exposures	Total
Balance at beginning of the period	1	5	6	12
Impairment losses on loans and advances	5	4	1	10
Amounts written off	(5)	(1)	-	(6)
Reversals of previously recognised impaired assets	-	(2)	(5)	(7)
Total individual allowance for impairment losses	1	6	2	9

e: Asset quality of loans and advances:

Interest revenue foregone on impaired assets is calculated using actual interest written off and interest suspended during the period. There are no real estate or other assets acquired through the enforcement of security/collateral held at 31 December 2015 (31 December 2014: nil; 30 June 2015: nil). There are no assets under administration as at 31 December 2015 (31 December 2014: nil; 30 June 2015: nil).

There are no unrecognised impaired assets as at 31 December 2015 (31 December 2014: nil; 30 June 2015: nil). The aggregate amount of undrawn balances on lending commitments to counterparties for whom drawn balances are classified as individually impaired is $0.7m at 31 December 2015 (31 December 2014: $2.5m; 30 June 2015: $0.5m).

Notes to the interim financial statements continued

10. Asset quality continued

f: Credit quality of financial assets neither past due nor impaired

A large portion of the credit exposures, such as residential mortgages, are 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.

The credit quality of loans and advances to customers that were neither past due nor impaired can be assessed by reference to the Bank's credit scoring systems. At the origination of loans and advances to Customers, retail advances are credit scored based on a combination of debt servicing ability, behavioural loan characteristics and loan-to-valuation ("**LVR**") ratios. Non-retail advances are individually risk graded against similar characteristics. These credit scoring characteristics are reviewed periodically for adverse changes during the loan's life. Interest continues to be accrued on all loans. No interest has been foregone.

11. Segment analysis

For the purposes of determining reportable operating segments, the chief operating decision-maker has been identified as the Kiwibank Leadership Team ("**KBLT**"), which consists of the Chief Executive and his direct reports. The KBLT reviews the Banking Group's internal reporting pack on a regular basis to assess performance and to allocate resources. A reportable operating segment is a distinguishable part of the Banking Group, engaged in providing products and services which are subject to risks and returns that are different from those of other segments. The business segments are defined by the customers that they service and the services they provide.

The KBLT assesses the performance of the operating segments based on a measure of profit before tax. This measurement basis includes a reallocation of internal overhead expenses from non-income generating cost centres of the business. Net interest income at a segmental level includes an allocation for internal transfer pricing which eliminates to zero at a Banking Group level. Transfer pricing is allocated on a basis which reflects intersegment funding arrangements.

A summarised description of each business unit is shown below:

- Personal– Provides banking products and services to the personal banking segment via the Banking Group and NZP distribution channels and the bank's funding reserves.
- Business– Provides banking products and services to the business sector, via the Banking Group and NZP distribution channels. Included within the segment are Business and Treasury services.

	The Banking Group		
Dollars in millions	Personal markets	Business markets	Total
Unaudited 6 months ended 31 December 2015			
External revenues	**260**	**(15)**	**245**
Intersegment revenues	**(105)**	**105**	**-**
Total revenues	**155**	**90**	**245**
Profit before taxation	**42**	**51**	**93**
Unaudited 6 months ended 31 December 2014			
External revenues	249	(9)	240
Intersegment revenues	(91)	91	-
Total revenues	158	82	240
Profit before taxation	58	40	98
Year ended 30 June 2015			
External revenues	494	(21)	473
Intersegment revenues	(184)	184	-
Total revenues	310	163	473
Profit before taxation	95	81	176

Notes to the interim financial statements continued

12. Concentration of credit risk

Concentrations of credit risk arise where the Banking Group is exposed to risk in activities or industries of a similar nature. An analysis of financial assets by industry sector at the reporting date is as follows:

	The Banking Group
Dollars in millions	Unaudited as at 31/12/15
New Zealand	
Government, local authorities and services	**1,057**
Finance, investment and insurance	**1,334**
Households	**14,649**
Transport and storage	**66**
Electricity, gas and water	**4**
Construction	**215**
Property and business services	**993**
Agriculture	**30**
Health and community services	**69**
Personal and other services	**85**
Retail and wholesale trade	**77**
Food & other manufacturing	**200**
Overseas	
Finance, investment and insurance	**69**
	18,848
Less allowance for impairment losses	**(53)**
Other financial assets	**9**
Total	**18,804**

Notes to the interim financial statements continued

12. Concentration of credit risk continued

	The Banking Group		
Unaudited as at 31 December 2015 Dollars in millions	Maximum exposure	Collateral	Net exposure
Credit risk relating to balance sheet assets			
Fixed rate lending at amortised cost	12,145	(12,138)	7
Variable rate lending	3,848	(3,846)	2
Unsecured lending	409	-	409
Due from other financial institutions	209	-	209
Balances with related parties	77	-	77
Derivative financial instruments	451	(77)	374
Financial assets held for trading	66	-	66
Available-for-sale assets	1,165	-	1,165
Cash and cash equivalents	478	-	478
Other financial assets	9	-	9
	18,857	(16,061)	2,796
Less allowance for impairment	(53)	-	(53)
Total	18,804	(16,061)	2,743

The table above represents a worst case scenario of credit risk exposure to the Banking Group at 31 December 2015. The exposures set out are based on net carrying amounts as reported in the balance sheet.

Australian and New Zealand Standard Industrial Classification ("**ANZIC**") codes have been used as the basis for disclosing customer industry sectors.

The exposure of the Banking Group derived from loans and advances to retail and corporate customers is 87% of the total maximum exposure.

The table above 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 the debt in the event of the borrower failing to meet its contractual obligations. For the purposes of this disclosure, where collateral held is valued at more than the corresponding credit exposure, coverage is capped at the value of the credit exposure less amounts for which an individual impairment allowance has been recognised. The most common type of collateral is over real estate including residential, commercial, industrial and rural property.

The Banking Group is potentially exposed to credit risk for undrawn loan commitments (note 15) for an amount equal to the undrawn balance.

Notes to the interim financial statements continued

13. Concentration of funding

Concentrations of funding arise where the Banking Group and Kiwibank are funded by industries of a similar nature or in particular geographies. ANZIC codes have been used as the basis for disclosing industry sectors. An analysis of financial liabilities by industry sector and geography at the reporting date is as follows:

	The Banking Group
Dollars in millions	Unaudited as at 31/12/15
Analysis by industry sector	
New Zealand	
Transport and storage	**102**
Finance, investment and insurance	**3,646**
Electricity, gas and water	**8**
Food & other manufacturing	**65**
Construction	**68**
Communications	**27**
Government, local authorities and services	**485**
Agriculture	**30**
Health and community services	**259**
Personal and other services	**246**
Property and business services	**424**
Education	**145**
Retail and wholesale trade	**60**
Households	**10,642**
Overseas	
Finance, investment and insurance – Australia	**57**
Finance, investment and insurance – rest of world	**1,304**
Households – Australia	**36**
Households – rest of world	**208**
	17,812
Other financial liabilities	**72**
Total	**17,884**

Notes to the interim financial statements continued

14. Interest repricing

The table below summarises the Banking Group's exposure to interest rate risk. It includes financial instruments at their carrying amounts, categorised by the earlier of contractual repricing or maturity dates. The fair value adjustment on the revaluation of financial instruments is categorised in the appropriate repricing category.

	The Banking Group						
	Unaudited as at 31/12/15						
Dollars in millions	Total	Non-interest bearing	Up to 3 months	3 to 6 months	6 months to 1 year	Between 1 & 2 years	Over 2 years
Financial assets							
Cash and cash equivalents	478	46	432	-	-	-	-
Due from other financial institutions	209	-	209	-	-	-	-
Financial assets held for trading	66	-	7	-	1	4	54
Available-for-sale assets	1,165	-	319	54	28	310	454
Loans and advances	16,349	(29)	5,154	1,180	3,409	4,789	1,846
Derivative financial instruments	451	451	-	-	-	-	-
Due from NZP related parties	77	1	45	-	-	31	-
Other financial assets	9	9	-	-	-	-	-
Total financial assets	18,804	478	6,166	1,234	3,438	5,134	2,354
Financial liabilities							
Due to other financial institutions	(82)	(5)	(77)	-	-	-	-
Deposits and other borrowings	(14,430)	(1,426)	(8,807)	(1,990)	(1,745)	(244)	(218)
Derivative financial instruments	(537)	(537)	-	-	-	-	-
Debt securities issued	(2,507)	-	(1,457)	(69)	-	(206)	(775)
Term subordinated debt	(256)	-	-	-	-	(150)	(106)
Due to NZP related parties	(10)	(10)	-	-	-	-	-
Other financial liabilities	(62)	(62)	-	-	-	-	-
Total financial liabilities	(17,884)	(2,040)	(10,341)	(2,059)	(1,745)	(600)	(1,099)
On-balance sheet gap	920	(1,562)	(4,175)	(825)	1,693	4,534	1,255
Net derivative notional principals	18	-	5,730	(289)	(1,744)	(3,512)	(167)
Net effective interest rate gap	938	(1,562)	1,555	(1,114)	(51)	1,022	1,088

15. Liquidity

The table on page 20 summarises the cash flows of the Banking Group by remaining contractual maturities as at the reporting date. The amounts disclosed are the contractual undiscounted cash flows and include principal and future interest cash flows and therefore may not agree to the carrying values on the balance sheet. Actual cash flow may differ significantly from the contractual cash flows disclosed below as a result of future actions of the Banking Group and/or its counterparties, such as early repayments or refinancing of term loans.

The majority of the longer term Loans and advances are housing loans which are likely to be repaid earlier than their contractual terms. Deposits and other borrowings include substantial customer savings deposits and cheque accounts, which are at call. History demonstrates that such accounts provide a stable source of long term funding for the Bank.

The Banking Group does not manage its liquidity risk on the basis of the information provided on page 20.

Notes to the interim financial statements continued

15. Liquidity continued

	The Banking Group						
	Unaudited as at 31/12/15						
Dollars in millions	On demand	Up to 3 months	3 to 12 months	Between 1 & 5 years	More than 5 years	Gross nominal inflow/ outflow	Carrying amount
Non-derivative cash flows							
Liabilities							
Due to other financial institutions	(82)	-	-	-	-	(82)	(82)
Deposits and other borrowings	(5,254)	(4,917)	(3,887)	(525)	-	(14,583)	(14,430)
Debt securities issued	(272)	(660)	(258)	(1,464)	(37)	(2,691)	(2,507)
Subordinated debt	(3)	-	(12)	(279)	-	(294)	(256)
Due to NZP related parties	(10)	-	-	-	-	(10)	(10)
Other financial liabilities	(62)	-	-	-	-	(62)	(62)
Total financial liabilities	(5,683)	(5,577)	(4,157)	(2,268)	(37)	(17,722)	(17,347)
Assets							
Cash and cash equivalents	478	-	-	-	-	478	478
Due from other financial institutions	177	32	-	-	-	209	209
Financial assets held for trading	-	1	3	62	10	76	66
Available-for-sale assets	56	131	178	874	-	1,239	1,165
Loans and advances	161	338	1,103	3,829	28,455	33,886	16,349
Due from NZP related parties	-	30	17	30	-	77	77
Other financial assets	9	-	-	-	-	9	9
Total financial assets	881	532	1,301	4,795	28,465	35,974	18,353
Net non-derivative cash flows	(4,802)	(5,045)	(2,856)	2,527	28,428	18,252	1,006
Derivative cash flows – net							
Interest rate derivatives	(11)	(14)	(57)	(46)	(2)	(130)	
Total	(11)	(14)	(57)	(46)	(2)	(130)	
Derivative cash flows – gross							
Foreign exchange derivatives							
Inflow	472	437	170	816	37	1,932	
Outflow	(481)	(450)	(185)	(738)	(42)	(1,896)	
Total	(9)	(13)	(15)	78	(5)	36	
Off balance sheet cash flows							
Capital commitments	-	(4)	(1)	(1)	-	(6)	
Undrawn loan commitments	(2,541)	-	-	-	-	(2,541)	
Lease commitments	-	(1)	(4)	(16)	-	(21)	
Total	(2,541)	(5)	(5)	(17)	-	(2,568)	
Net cash flows	(7,363)	(5,077)	(2,933)	2,542	28,421	15,590	
Cumulative net cash flows	(7,363)	(12,440)	(15,373)	(12,831)	15,590	15,590	

Notes to the interim financial statements continued

15. Liquidity continued

The Banking Group holds a diversified portfolio of high quality liquid securities to support its liquidity risk management. The size of the Banking Group's liquidity portfolio is based on the amount required to meet its liquidity policy and includes items both classified as cash and cash equivalents and those classified as operating assets in the consolidated cash flow statement.

	The Banking Group
Dollars in millions	Unaudited as at 31/12/15
The Banking Group's liquidity portfolio is based on the amount required to meet its liquidity policy.	
Cash on hand and with central banks	412
Certificates of deposit	138
Government bonds and treasury bills	572
Local body stock and bonds	31
Other bonds	887
Total	**2,040**

15. Financial instruments

Fair value measurement

Assets and liabilities carried at fair value or for which fair values are disclosed have been classified into three levels according to the quality and reliability of information used to determine the fair values. The three levels of the fair value hierarchy are defined as follows:

Level 1 – Fair value measurements are those derived from unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 – Fair value measurements are those where quoted market prices are not available, for example where the instrument is traded in a market that is not considered to be active or valuation techniques are used to determine fair value and where these techniques use inputs that are based significantly on observable market data.

Level 3 – Fair value measurements where at least one input which could have a significant effect on the instrument's valuation is not based on observable market data.

Valuation methodology

The fair values of assets and liabilities carried at fair value were determined by application of the following methods and assumptions.

Held for trading and available-for-sale securities

Estimates of fair value for both held for trading and available-for-sale securities are based on quoted market prices or determined using market accepted valuation models as appropriate (including discounted cash flow models) with inputs including an interest rate yield curve developed from quoted rates and market observable credit spreads.

Debt securities issued

Debt securities issued that are classified at fair value through profit or loss are short term in nature. For these liabilities fair value has been determined using a discounted cash flow model with inputs including an interest rate yield curve developed from quoted rates and market observable credit spreads.

Derivative financial instruments

Where the Banking Group's derivative financial assets and liabilities are not traded on an exchange, they are valued using valuation techniques, including discounted cash flow and option pricing models, as appropriate. The types of derivatives classified as level 2 and the valuation techniques used include:

- Interest rate swaps which are valued using discounted cash flow models; the most significant inputs into those models are interest rate yield curves which are developed from quoted rates.
- Foreign exchange derivatives that do not contain options which are priced using rates available from publicly quoted sources.

Notes to the interim financial statements continued

16. Financial instruments continued

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Unaudited as at 31 December 2015				
Financial assets				
Derivative financial assets	**-**	**451**	**-**	**451**
Financial assets held for trading	**2**	**64**	**-**	**66**
Available-for-sale financial assets	**579**	**586**	**-**	**1,165**
Total financial assets at fair value	**581**	**1,101**	**-**	**1,682**
Financial liabilities				
Derivative financial liabilities	**-**	**537**	**-**	**537**
Debt securities issued	**-**	**600**	**-**	**600**
Total financial liabilities at fair value	**-**	**1,137**	**-**	**1,137**

There have been no transfers between levels 1 and 2 during the period ended 31 December 2015 (period ended 31 December 2014: no transfers; year ended 30 June 2015: no transfers). There were also no transfers into/out of level 3 during the period ended 31 December 2015 (period ended 31 December 2014: no transfers; year ended 30 June 2015: no transfers).

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Unaudited as at 31 December 2014				
Financial assets				
Derivative financial assets	-	184	-	184
Financial assets held for trading	3	45	-	48
Available-for-sale financial assets	650	433	-	1,083
Total financial assets at fair value	653	662	-	1,315
Financial liabilities				
Derivative financial liabilities	-	302	-	302
Debt securities issued	-	531	-	531
Total financial liabilities at fair value	-	833	-	833

	The Banking Group			
Dollars in millions	Level 1	Level 2	Level 3	Total
Audited as at 30 June 2015				
Financial assets				
Derivative financial assets	1	479	-	480
Financial assets held for trading	58	38	-	96
Available-for-sale financial assets	664	558	-	1,222
Total financial assets at fair value	723	1,075	-	1,798
Financial liabilities				
Derivative financial liabilities	-	475	-	475
Debt securities issued	-	615	-	615
Total financial liabilities at fair value	-	1,090	-	1,090

Notes to the interim financial statements continued

16. Financial instruments continued

	The Banking Group					
	Unaudited as at 31/12/15		Unaudited as at 31/12/14		Audited as at 30/06/15	
Dollars in millions	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value	Carrying amount	Estimated fair value
Assets						
Financial assets held for trading	**66**	**66**	48	48	96	96
Available-for-sale assets	**1,165**	**1,165**	1,083	1,083	1,222	1,222
Loans and advances	**16,349**	**16,458**	15,054	15,100	15,598	15,704
Derivative financial instruments	**451**	**451**	184	184	480	480
Due from NZP related parties	**77**	**77**	77	77	77	77
Liabilities						
Deposits and other borrowings	**(14,430)**	**(14,447)**	(13,283)	(13,285)	(13,740)	13,759
Derivative financial instruments	**(537)**	**(537)**	(302)	(302)	(475)	(475)
Debt securities issued	**(2,507)**	**(2,515)**	(2,067)	(2,076)	(2,397)	(2,405)
Subordinated debt	**(256)**	**(259)**	(252)	(258)	(255)	(262)
Due to NZP related parties	**(10)**	**(10)**	(8)	(8)	(6)	(6)

The carrying values of the following financial instruments are a reasonable approximation of fair value because, for example, they are short-term in nature or reprice to current market rates frequently: cash and cash equivalents, due from other financial institutions, other financial assets, due to other financial institutions and other financial liabilities.

17. Credit exposure concentrations

Credit exposures to individual counterparties

Credit exposure concentrations are disclosed on the basis of actual credit exposures and gross of set-offs. Peak end-of-day aggregate credit exposures have been calculated using the Banking Group's Tier 1 capital at the end of the period.

There are no individual counterparties (excluding connected parties, governments and banks with long term credit ratings of A-, A3 or its equivalent or above), where the period end and peak end-of-day aggregate actual credit exposures, net of individual credit impairment allowances (which were nil), equalled or exceeded 10% of the Banking Group's shareholder equity as at the reporting date.

18. Fiduciary activities and securitisation

Provision of financial services

Financial services provided by Kiwibank to entities which are involved in trust, custodial, funds management and other fiduciary activities, are provided at fair value, except that Kiwibank does not charge Kiwibank Investment Management Limited, the Manager of the Kiwibank PIE Unit Trust, any bank fees. Further, the Kiwibank PIE Unit Trust bank account used for tax payments does not earn interest.

Insurance business

The Banking Group does not conduct insurance business. However, certain insurance products which are marketed through the Banking Group's retail network are underwritten by Kiwi Insurance Limited, a wholly owned subsidiary of KGHL, Kiwibank's immediate parent company.

Notes to the interim financial statements continued

18. Fiduciary activities and securitisation continued

Kiwi Covered Bond Trust

On 23 January 2013, the Kiwi Covered Bond Trust (the "**Covered Bond Trust**") was established to hold Kiwibank housing loans and to provide guarantees to certain debt securities issued by the Bank. Guarantees provided by Kiwi Covered Bond Trustee Limited, as Trustee of the Covered Bond Trust, have a priority claim over the assets of the Covered Bond Trust. Since 19 February 2013, selected Kiwibank housing loans have been transferred to the Covered Bond Trust in order to facilitate the Bank's covered bond programme. These assets do not qualify for derecognition as the Banking Group retains a continuing involvement and retains substantially all the risks and rewards of ownership of the transferred assets. The Covered Bond Trust is consolidated within the Banking Group.

Substantially all of the assets of the Covered Bond Trust comprise housing loans originated by the Bank, which are security for the guarantee of issuances of covered bonds by the Bank. 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 carrying value of the Covered Bond Trust pool at 31 December 2015 is $316m (31 December 2014: $316m; 30 June 2015: $316m). These securities are ring fenced to ensure they are not used as collateral outside of agreements established in relation to the Covered Bond Trust.

Kiwibank RMBS Trust Series 2009-1

The purpose of the Kiwibank RMBS Trust Series 2009-1 (the "**RMBS Trust**") is to provide an in-house residential mortgage-backed securities facility to issue securities as collateral for borrowing from the Reserve Bank of New Zealand. As at 31 December 2015, included within Loans and advances to customers on the Banking Group's consolidated balance sheet were housing loans with a carrying value of $600m held by the RMBS Trust (31 December 2014: $600m; 30 June 2015: $600m). These housing loans do not qualify for derecognition as the Bank retains substantially all of the risks and rewards of ownership. The RMBS Trust is consolidated within the Banking Group.

19. Risk management

There have been no material changes to the Banking Group's policies for managing risk, or material exposures to new categories of risk since 30 June 2015.

20. Capital expenditure commitments

Capital expenditure commitments contracted for as at 31 December 2015, but not provided for in these interim financial statements, total $5.8m (31 December 2014: $7.9m; 30 June 2015: $6.3m) of which $0.6m (31 December 2014: $2.5m; 30 June 2015: $1.7m) are due between one and five years from the reporting date.

21. Contingent liabilities and loan commitments

In June 2013, a group called Fair Play on Fees announced plans for a representative action against banks in New Zealand in relation to certain default fees charged to New Zealand customers. In November 2013, the group issued proceedings against Kiwibank. The potential outcome of the proceedings cannot be determined with any certainty at this stage.

Other than the above, there are no material contingent liabilities as at 31 December 2015 (31 December 2014: nil; 30 June 2015: nil).

Undrawn loan commitments as at the reporting date are disclosed in note 15.

22. Events subsequent to the reporting date

On 29 January 2016, Fitch Ratings revised Kiwibank's outlook to stable from positive.

There are no other events that occurred subsequent to the reporting date, that require recognition, or additional disclosure in these interim financial statements.

Capital adequacy

The "**Banking Group**" consists of Kiwibank Limited and its subsidiaries. The Banking Group is subject to the capital adequacy requirements for registered banks as specified by the Reserve Bank of New Zealand ("**RBNZ**"). The RBNZ has set minimum acceptable regulatory capital requirements that are consistent with the internationally agreed framework developed by the Basel Committee on Banking Supervision.

The Bank must comply with RBNZ minimum capital adequacy ratios, as calculated under the Basel III framework in accordance with the RBNZ document *Capital Adequacy Framework (Standardised Approach)* (BS2A), as determined in its conditions of registration.

Ordinary shares

The ordinary shares issued by the Bank, which are fully paid, are included within CET 1 capital. The material terms and conditions of the ordinary shares are:

a) each share contains a single right to vote;

b) there are no redemption, conversion or capital repayment options/facilities;

c) there is no predetermined dividend rate;

d) there is no maturity date; and

e) there are no options to be granted pursuant to any agreement.

Perpetual bonds

The Perpetual bonds, issued by the Bank and which are fully paid, are included within AT1. The Perpetual bond issue is subordinate to other term subordinated debt issues and all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The material terms and conditions are:

a) the Perpetual bonds constitute direct, perpetual, convertible, non-cumulative, unsecured, subordinated debt securities issued by Kiwibank;

b) interest on the Perpetual bonds is payable quarterly at an initial rate of 7.25% p.a. subject to the absolute discretion of Kiwibank;

c) interest is non-cumulative;

d) the Perpetual bonds may be required to be converted into ordinary shares of Kiwibank Limited (or written off if conversion into ordinary shares is not possible) if certain events occur;

e) the Perpetual bonds do not have a maturity date, however, Kiwibank may elect to make early repayment on 15 July 2019 or any reset date thereafter (reset dates occur at 5-yearly intervals, commencing on 27 May 2020); and

f) the Perpetual bonds are not guaranteed by any member of the Banking Group, Kiwibank's parent companies (including New Zealand Post), the Crown or by any other person.

Subordinated bonds

The subordinated debt issue, issued by the Bank and which is fully paid, is included within Tier 2 capital. The issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The material terms and conditions are:

Subordinated debt issued 10 December 2012:

a) the Subordinated Bonds constitute direct, unsecured, subordinated debt obligations of Kiwibank;

b) the Subordinated Bonds pay interest at the Coupon Rate of 5.8% pa;

c) interest will be paid in arrears in equal semi-annual instalments. Payments of interest are subject to Kiwibank and the Banking Group being able to satisfy the Solvency Test immediately following payment;

d) the maturity date of the Subordinated Bonds is 15 December 2022. Kiwibank may redeem the Subordinated Bonds on the First Call Date (15 December 2017) and on any Interest Payment Date thereafter subject to Kiwibank and the Banking Group being able to satisfy the Solvency Test immediately following the payment; Kiwibank may also redeem the Subordinated Bonds at any time (including before the First Call Date) if a Regulatory Event or a Tax Event occurs; and

e) the Subordinated Bonds are not guaranteed by any member of the Banking Group, Kiwibank's parent companies (including New Zealand Post), the Crown or by any other person.

Under the RBNZ's Basel III rules the $150m subordinated debt is subject to a loss absorbency haircut.

Convertible subordinated bonds

The convertible subordinated bond issue, issued by the Bank and which is fully paid, is included within Tier 2 capital. The issue is subordinate to all other general liabilities of the Banking Group and is denominated in New Zealand dollars. The material terms and conditions are:

a) the convertible subordinated bonds constitute direct, unsecured, subordinated debt obligations of Kiwibank;

b) interest on the convertible subordinated bonds is payable semi-annually at an initial rate of 6.61% p.a. subject to the condition that Kiwibank and the Banking Group is solvent after each payment;

c) the convertible subordinated bonds may be required to be converted into ordinary shares of Kiwibank Limited (or written off if conversion into ordinary shares is not possible) if certain events occur;

d) the convertible subordinated bonds have a maturity date of 15 July 2024, however, Kiwibank may elect to make early repayment on 15 July 2019 or any semi-annual interest payment date thereafter; and

e) the convertible subordinated bonds are not guaranteed by any member of the Banking Group, Kiwibank's parent companies (including New Zealand Post), the Crown or by any other person.

Capital adequacy continued

Risk exposures

Risk weighted exposures are derived by assigning risk weight percentages to certain material risk categories of exposures. These exposures are measured or estimated from: i) selected balance sheet assets; ii) off balance-sheet exposures and market contracts; and iii) business unit net income.

The Bank's current prudential capital requirements based on assessments of its material risk classes (commonly referred to as "Pillar I" risk classes under Basel III) can be summarised as follows:

- Credit risk – The vulnerability of the Banking Group's lending and investment portfolios to systemic counterparty default. The risk based capital allocation is computed based on RBNZ Standardised Approach Credit Risk methodology (BS2A).
- Market risk – The vulnerability of earnings to movements in interest rates and currency volatility. The risk based capital allocation is computed based on RBNZ Standardised Approach to Interest Rate Risk (BS2A).
- Operational risk – The risk of loss, resulting from inadequate or failed internal processes (including legal risks), people and systems and from external events. The risk based capital allocation is computed based on RBNZ Standardised Approach to Operational Risk methodology (BS2A).

Kiwibank's Board is ultimately responsible for capital adequacy and approves capital plans and establishes minimum internal capital levels and limits. These are typically higher than the regulatory minimum.

The capital adequacy tables set out on pages 26 to 31 summarise the composition of regulatory capital and capital adequacy ratios for the period ended 31 December 2015. Throughout the period Kiwibank and the Banking Group complied with both regulatory and internal capital adequacy requirements.

Regulatory capital ratios

	The Banking Group	
Dollars in millions	**31/12/15**	31/12/14
Capital adequacy ratios		
Common Equity Tier 1 capital ratio	**9.0%**	9.4%
Tier 1 capital ratio	**10.6%**	10.8%
Total capital ratio	**12.8%**	13.3%
RBNZ minimum ratios		
Common Equity Tier 1 capital ratio	**4.5%**	4.5%
Tier 1 capital ratio	**6.0%**	6.0%
Total capital ratio	**8.0%**	8.0%
Buffer ratios		
Buffer ratio	**4.5%**	4.8%
Buffer ratio requirement	**2.5%**	2.5%

	Kiwibank Limited	
Dollars in millions	**31/12/15**	31/12/14
Capital adequacy ratios		
Common Equity Tier 1 capital ratio	**8.6%**	9.1%
Tier 1 capital ratio	**10.1%**	10.5%
Total capital ratio	**12.3%**	12.9%

Capital adequacy continued

Regulatory capital

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

	The Banking Group
Dollars in millions	**31/12/15**
Common Equity Tier 1 capital	
Issued and fully paid up share capital	**400**
Retained earnings (net of appropriations)	**573**
Accumulated other comprehensive income and other disclosed reserves [1, 2]	**(46)**
Less deductions from Common Equity Tier 1 capital	
Intangible assets	**(138)**
Cash flow hedge reserve	**51**
Deferred tax assets	**(8)**
Total Common Equity Tier 1 capital	**832**
Additional Tier 1 capital	
Perpetual bonds [3]	**147**
Total Additional Tier 1 capital	**147**
Total Tier 1 capital	**979**
Tier 2 capital	
Subordinated debt	**208**
Total Tier 2 capital	**208**
Total capital	**1,187**

1 Includes Available for Sale Reserve of $5m. The available-for-sale reserve includes the cumulative net change in the fair value of available-for-sale securities until the investment is derecognised or impaired.

2 Includes cash flow hedge reserve of ($51m). The cash flow hedging reserve comprises the effective portion of the cumulative net change in the fair value of foreign exchange and interest rate derivative contracts related to hedged forecasted transactions that have not yet occurred. The cash flow hedge reserve is not eligible for inclusion in capital under BS2A 7 (3)(c).

3 Additional Tier 1 capital consists of Perpetual bonds, which are classified as equity of the Banking Group for financial reporting purposes.

Capital adequacy continued

On-balance sheet exposures

	The Banking Group			
	31/12/15			
Dollars in millions	Total exposure	Risk weighting	Risk weighted exposure	Minimum Pillar I capital requirement
On-balance sheet exposures				
Cash and gold bullion	46	0%	-	-
Sovereigns and central banks	943	0%	-	-
Multilateral development banks and other international organisations	244	0%	-	-
Public sector entities	34	20%	7	1
	4	100%	4	-
Banks	498	20%	100	8
	141	50%	71	6
Corporate	88	50%	44	4
	640	100%	640	51
Residential mortgages not past due	12,755	35%	4,464	357
	479	40%	192	15
	1,471	50%	736	59
	28	70%	20	2
	186	75%	140	11
	7	90%	6	-
	203	100%	203	16
Impaired assets	8	100%	8	1
Past due residential mortgages > 90 days	4	100%	4	-
Other past due assets	2	150%	3	-
Non risk weighted assets	616	0%	-	-
Other assets	599	100%	599	48
Total on-balance sheet exposures	**18,996**		**7,241**	**579**

Capital adequacy continued

Off-balance sheet exposures and market related contracts

	The Banking Group					
	31/12/15					
Dollars in millions	Total exposure	Credit conversion factor	Credit equivalent amount	Average risk weighting	Risk weighted exposure	Minimum Pillar I capital requirement
Direct credit substitute	**5**	**100%**	**5**	**100%**	**5**	**-**
Asset sale with recourse	**-**	**100%**	**-**	**-**	**-**	**-**
Forward asset purchase	**-**	**100%**	**-**	**-**	**-**	**-**
Commitment with certain drawdown	**27**	**100%**	**27**	**100%**	**27**	**2**
Note issuance facility	**-**	**50%**	**-**	**-**	**-**	**-**
Revolving credit facility	**310**	**50%**	**155**	**40%**	**62**	**5**
Revolving credit facility	**1,040**	**20%**	**208**	**37%**	**77**	**6**
Revolving credit facility	**109**	**0%**	**-**	**37%**	**-**	**-**
Performance-related contingency	**1**	**50%**	**1**	**100%**	**1**	**-**
Other commitments where original maturity is greater than one year	**261**	**50%**	**131**	**49%**	**64**	**5**
Other commitments where original maturity is less than or equal to one year	**60**	**20%**	**12**	**100%**	**12**	**1**
Other commitments where original maturity is less than or equal to one year	**-**	**20%**	**-**	**20%**	**-**	**-**
Other commitments that cancel automatically when the creditworthiness of the counterparty deteriorates or that can be cancelled unconditionally at any time without prior notice	**733**	**0%**	**-**	**100%**	**-**	**-**
Market related contracts:[1]						
(a) Foreign exchange contracts	**1,864**	**n/a**	**142**	**50%**	**71**	**6**
(b) Interest rate contracts	**51,433**	**n/a**	**528**	**33%**	**174**	**14**
(c) CVA					**158**	**13**
Total off-balance sheet exposures	**55,843**		**1,209**		**651**	**52**

[1] The credit equivalent amount for market related contracts was calculated using the current exposure method.

Residential mortgages by loan-to-value ratio

	The Banking Group		
	31/12/15		
Dollars in millions	On-balance sheet	Off-balance sheet	Total
LVR 0% – 80%	**13,233**	**331**	**13,564**
LVR > 80% – 90%	**1,500**	**16**	**1,516**
LVR 90% +	**411**	**16**	**427**
Total	**15,144**	**363**	**15,507**

The LVR classification above is calculated in line with the Bank's Pillar I capital requirement, which includes capital relief for "Welcome Home" loans that are guaranteed by the New Zealand Crown. Loans with an LVR greater than 80% are presented after the mitigation of credit risk from third party lenders' mortgage insurance, where applicable.

At 31 December 2015, of the loans with an LVR greater than 80%, $463m relates to "Welcome Home" loans, whose credit risk is mitigated by the New Zealand Crown. Of the remaining loans with an LVR greater than 80%, Kiwibank uses lenders' mortgage insurance on selected loans.

Capital adequacy continued

Reconciliation of residential mortgage-related amounts

	The Banking Group
Dollars in millions	31/12/15
Residential mortgages total on-balance sheet exposures	15,144
Collective allowance for impairment	24
Deferred arrangement fees	89
Gross residential mortgage loans per asset quality (note 10)	**15,257**
Corporate lending residentially secured	(903)
Gross residential loans and advances to customers	**14,354**

Credit risk mitigation

	The Banking Group			
	31/12/15			
Dollars in millions	Total value of on- and off-balance sheet exposures covered by eligible collateral (after haircutting)	Total value of on- and off-balance sheet exposures covered by guarantees or credit derivatives	Risk weighted exposure	Minimum Pillar I capital requirement
Sovereign or central bank	-	-	-	-
Multilateral development bank	-	-	-	-
Public sector entities	-	-	-	-
Bank	(51,019)	-	(308)	(25)
Corporate	_	-	-	-
Residential mortgage	-	-	-	-
Other	-	-	-	-
	(51,019)	-	(308)	(25)

Operational risk

	The Banking Group	
	31/12/15	
Dollars in millions	Implied risk weighted exposure	Total operational risk capital requirement
Operational risk	1,101	88

Capital adequacy continued

Market risk

	The Banking Group			
	31/12/15			
	Implied risk weighted exposure		Aggregate capital charge	
Dollars in millions	End of period	Peak end-of-day	End of period	Peak end-of-day
Interest rate risk	**551**	**645**	**44**	**52**
Foreign currency risk	**1**	**1**	**-**	**-**
Equity risk	**-**	**-**	**-**	**-**

The aggregate market risk exposure above is derived in accordance with BS2A.

The peak end-of-day aggregate capital charge is the maximum over the half year accounting period at the close of each business day.

Total capital requirements

	The Banking Group		
	31/12/15		
Dollars in millions	Total exposure after credit risk mitigation	Risk weighted exposure or implied risk weighted exposure	Total capital requirement
Credit risk	**23,820**	**7,584**	**606**
Operational risk	**n/a**	**1,101**	**88**
Market risk	**n/a**	**552**	**44**
Total Pillar I risk	**n/a**	**9,237**	**738**

Other material risk (Pillar II)

The Bank has made an internal capital allocation of $44m (31 December 2014: $46m). The other material risks identified by the Bank include regulatory environment risk, reputational risk, systems risk and liquidity risk.

Independent Review Report

To the readers of Kiwibank Limited and the Banking Group's Disclosure Statement for the six months ended 31 December 2015

The Auditor-General is the auditor of Kiwibank Limited (the "Bank") and the entities it controlled as at 31 December 2015 or from time-to-time during the period (the "Banking Group"). The Auditor-General has appointed me, Chris Barber, using the staff and resources of PwC, to carry out the annual audit of the Bank and the Banking Group, on her behalf.

In our capacity as auditor, we have carried out a review of the:

- interim financial statements on pages 4 to 24 of the Disclosure Statement of the Banking Group for the six months ended 31 December 2015 which comprise the balance sheet as at 31 December 2015, the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the six month period ended 31 December 2015 and selected explanatory notes; and
- supplementary information as required by Schedules 5, 7, 9, 13, 16 and 18 of the Registered Bank Disclosure Statements (New Zealand Incorporated Registered Banks) Order 2014 (as amended) (the "Order") for the six months ended 31 December 2015.

Review conclusion

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

- the interim financial statements on pages 4 to 24 (excluding supplementary information included in notes 3, 10, 12, 13, 14, 15, 17, 18, and 19), are not prepared, in all material respects in accordance with New Zealand Equivalents to International Accounting Standard 34: *Interim Financial Reporting*;
- the supplementary information disclosed in notes 3, 10, 12, 13, 14, 15, 17, 18, and 19 prescribed by Schedules 5, 7, 13, 16 and 18 of the Order does not fairly state the matters to which it relates in accordance with those Schedules; and
- the supplementary information relating to Capital Adequacy disclosed on pages 25 to 31 is not in all material respects prepared in accordance with the Bank's Conditions of Registration and disclosed in accordance with Schedule 9 of the Order.

The review was completed on 17 February 2016, and is the date at which our review conclusion is expressed.

Responsibilities of the Board of Directors

The Directors of Kiwibank Limited (the "Directors") are responsible on behalf of the Bank, for the preparation and fair presentation of the half-year Disclosure Statement which includes interim financial statements in accordance with Clause 25 of the Order. The Directors are also responsible for such internal controls as the Directors determine are necessary to enable the preparation of the half-year Disclosure Statement that is free from material misstatement, whether due to fraud or error.

In addition, the Directors are responsible on behalf of the Bank, for including supplementary information in the half-year Disclosure Statement that complies with schedules 3, 5, 7, 9, 13, 16 and 18 of the Order.

These responsibilities are specified in the Order issued pursuant to the Reserve Bank of New Zealand Act 1989.

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Responsibilities of the Reviewer

We are responsible for reviewing the interim financial statements and supplementary information disclosed in accordance with Clause 25 and Schedules 5, 7, 9, 13, 16 and 18 of the Order, presented by the Directors.

We are responsible for reviewing the interim financial statements (excluding the supplementary information) in order to report to you whether, on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the interim financial statements have not been prepared, in all material respects, in accordance with New Zealand Equivalents to International Accounting Standard 34: *Interim Financial Reporting*.

We are responsible for reviewing the supplementary information (excluding the supplementary information relating to Capital Adequacy) in order to report to you whether, on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information does not fairly state the matters to which it relates in accordance with Schedules 5, 7, 13, 16 and 18 of the Order.

We are responsible for reviewing the supplementary information relating to capital adequacy in order to report to you whether, on the basis of the procedures performed by us, anything has come to our attention that would cause us to believe that the supplementary information is not in all material respects prepared in accordance with the Bank's Conditions of Registration and disclosed in accordance with Schedule 9 of the Order.

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

A review of interim financial statements 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 the Auditor-General's Auditing Standards and the International Standards on Auditing (New Zealand). Accordingly we do not express an audit opinion on these interim financial statements.

Independence

In completing our review we followed the independence requirements of the Auditor-General, which incorporate the independence requirements of the External Reporting Board.

We are independent of the Bank and the Banking Group. We have carried out assignments in the areas of assurance and advisory services, which are compatible with those independence requirements. In addition, certain partners and employees of our firm may deal with the Bank and the Banking Group on normal terms within the ordinary course of trading activities of the Bank and the Banking Group. These matters have not impaired our independence. Other than in our capacity as auditor acting on behalf of the Auditor-General, these assignments and any dealings within the ordinary course of trading activity, we have no relationship with or interests in the Bank or the Banking Group.

Chris Barber

PricewaterhouseCoopers

Chris Barber
On behalf of the Auditor-General
Wellington, New Zealand

PricewaterhouseCoopers